PRACTICAL APPROACH TO GENERAL INSURANCE MANAGEMENT

A HANDBOOK FOR INSURANCE PROFESSIONALS

The Institute of Chartered Accountants of India
(Set up by an Act of Parliament)
New Delhi

Practical Approach to General Insurance Management

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The basic draft of the publication was prepared by CA. R.C.Guria. The views expressed in the publication should not be construed as the views of the Council of the Institute of Chartered Accountants of India or any of its Committees or Boards.

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FOREWORD

The growth of the insurance industry in the country has been remarkable since its opening for the private players. Insurance industry worldwide has witnessed paradigm shift in term of developing innovative products and providing after sale service. Indian Insurance Industry is not an exception to this. Insurance companies in order to combat the increased competition and increase market share come out with new products almost every passing day. Insurance being a financial product is a complex subject which needs in-depth knowledge supplemented by updation on continuous basis. The instant publication is an attempt to provide comprehensive and useful information on varied facet of the industry.

I am happy to note that the Committee has worked meticulously to bring out the instant publication which covers contemporary and emerging areas of insurance sector. I am sure this being in the nature of ready recknor would be found useful by all those who have active interest in the insurance sector.

My compliment to CA. Charanjot Singh Nanda who has ably lead this Committee and I am sure that the Committee will continue to bring out more such publications so as to be of utility to the ICAI membership at large.

(CA. Amarjit Chopra)
President, ICAI

Date: 3rd December, 2010

Place: New Delhi

PREFACE

Growth in insurance industry has been stimulated by product innovation, vibrant distribution channels coupled with targeted publicity and promotional campaigns by the insurers. Innovations have come not only in the form of benefits attached to the products but also in the delivery mechanism through various marketing tie-ups both within the realm of financial services and outside. Despite the fact that the Indian general insurance industry has been growing at a compounded annual growth rate of 18.4 per cent (F.Y. 2003-07), its penetration level is just 0.60% of India's GDP against world average of 2.14%. The awareness of non life insurance products is very minimal in general public. It is imperative to spread awareness and create appreciable level of knowledge amongst the masses for the orderly and sustainable growth of the Indian insurance industry. Publication of this book is another step taken by the Committee in this direction.

The instant publication attempts to cover various types of insurance available in the Country such as Fire, Motor, Marine, Engineering, Liability and Health Insurance and gives comprehensive information on each of them in a very lucid manner. The publication has been designed in such a way that even a stakeholder without having technical knowledge of the subject can refer it without any inconvenience.

I place on record my sincere gratitude to CA. R.C. Guria, Chief Regional Manager, The New India Assurance Co. Ltd. for preparing the basic draft of the publication. I am grateful to CA. V. Ramasamy, former CMD, National Insurance Co. Ltd. for his valuable suggestions.

I am thankful to CA. Amarjit Chopra, President of ICAI, CA. G. Ramaswamy, Vice-President of ICAI for their involvement and encouragement and the members of the Committee, CA. Sanjeev K. Maheshwari, Vice-Chairman of the Committee, CA. Rajkumar S. Adukia, CA. Pankaj I. Jain, CA. Nilesh S. Vikamsey, CA. Atul C. Bheda, CA. Mahesh P. Sarda, CA. S. Santhanakrishnan, CA. J.

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I appreciate the efforts put in by the officials of the Secretariat of the Committee for bringing out this publication.

I am confident that the publication will be found useful by the members of our Institute and others concerned.

(CA. Charanjot Singh Nanda)
Chairman,
Committee on Banking, Insurance and Pension

Date: 9th November, 2010

Place: New Delhi

CONTENTS

1
INSURANCE: SCOPE, DEFINITION AND DEVELOPMENTS

Scope and Definition

Insurance is the oldest and the most common and practical method or technology for transfer of risks. The modern form of insurance is as old as four hundred years. Insurance is an integral part of the world economy, including the economy of a country. The whole gamut of the economy like trade, commerce and industry cannot grow without insurance. The scope and functions of insurance are defined and viewed differently through different disciplines including law, economics, history, actuarial science, risk-management technology and underwriting process. Since it is not possible to cover all these aspects in this manual, only legal and technical aspects are briefly discussed to explain the logic and anatomy of insurance. The first chapter of this insurance manual attempts to discuss the basic characteristics of insurance, types of insurance, requirements of insurable risks, insurance and adverse selection, insurance and gambling to explain how insurance works for trade, commerce, industry and economy of a country.

As defined by the Commission on Insurance Terminology of the American Risk and Insurance Association, *insurance is the pooling of fortuitous losses by transfer of such risks to insurers, who agree to indemnify the insureds for such losses, to provide other benefits on their occurrence, or to render services connected with risks*. Though this definition may not be acceptable to all, it is useful for analyzing the basic elements of insurance service.

Basic Characteristics of Insurance

The above-mentioned definition points out the basic characteristics of insurance. These are:

(i) Pooling of Losses;

(ii) Payment of Fortuitous Losses;

(iii) Risk Transfer; and

(iv) Indemnification.

Pooling of Losses

Pooling or sharing of losses is the foundation of insurance service. It enables spreading of losses incurred by few over a group of many and in the process actual loss is substituted by average loss. Precisely, insurance is averaging of loss through premium payment in advance based on loss forecasting of the group. Thus 'pooling' simply implies prediction of future losses with some accuracy based on the **law of large number,** and with statistical methods and actuarial application. The law of large number states that the greater the number of exposures, the more closely the actual results will reach the probable results that are expected from an infinite number of exposures. Although the loss due to fire of an individual firm cannot be identified and determined, the number and amount of total loss of a particular type of industry in a particular area from a particular peril or a cause can be predicted with some estimation based on previous experience of probability and severity of loss by fire in the industry. Thus an insurer predicts future losses for the group with greater degree of accuracy through the application of law of large number and charges to the individual insured a premium that will be adequate for paying all losses that may occur during a particular period.

Payment of Fortuitous Losses

A fortuitous loss is one that is unforeseen and uncertain and occurs as a matter of chance or probability. In other words, as the core of insurance function law of large number is based on the premise that losses are accidental, unforeseen and unintentional. An insurance policy is a contract for payment of fortuitous losses arising out of the operation of the perils covered by the policy, but not for the loss caused by the willful act or negligence of the insured.

Risk Transfer

Risk transfer is the prime objective of insurance. Through insurance risks are transferred from the insured to the insurer and through reinsurance process, risks are transferred from the insurer to a reinsurer, and through Alternative Risk Transfer (ART) mechanism including cat bond, insurance securitization, swaps, derivative and so on, reinsurers transfer catastrophic risks from reinsurance market to capital market. In a typical and traditional insurance process, only pure risks of accidental property damage, premature death, poor health and disablement are transferred to insurer and reinsurer.

Indemnification

Indemnification is the fundamental principle and ultimate objective of insurance. With indemnification the insured gets restored to his approximate financial position prior to the occurrence of loss. No policyholder is entitled to make any profit out of insurance contract unless the policy is a benefit policy. Most of the policy provides for indemnification of loss suffered by the insured, while only a few policies provide for payment of certain benefits on the occurrence of certain events or on maturity of endowment life insurance policy. This is discussed in detail below.

Types of Insurance

Insurance can be classified primarily as:

(i) Government insurance, and

(ii) Private Insurance.

Government Insurance

(a) Social Insurance and Pension such as Social Security Scheme, Unemployment Scheme, Healthcare, Environment Relief Fund, etc.

(b) Other Government Insurance such as ESI, Crop Insurance, etc.

Private Insurance

(a) Life and Health Insurance in various forms

(b) Property and Casualty Insurance in hundred of forms in commercial as well as personal lines such Fire Insurance, Marine Insurance, Engineering Insurance, Motor (Auto) Insurance, Liability Insurance, Burglary & Theft Insurance, W.C. Insurance, etc.

All these will be discussed separately to explain their underwriting and claims management procedures and techniques.

Requirements of Insurable Risks

Although Alternative Risk Transfer (ART) covers both pure risks and speculative risks conventional insurance covers only pure risks. However, all pure risks are not insurable. Insurability of pure risks depends on satisfaction of the following six requirements:

- There must be a large number of exposure units.
- The loss must be accidental and unintentional.
- The loss must be measurable.
- The probability of loss-occurrence is calculable.
- Cat Risks will be avoidable.
- Premium must be affordable and economically feasible.

Large Number of Exposure Units

Feasibility of insurance process depends on the operation of law of large number, which enables the insurer to predict loss of the large group on the basis of his past experience. Loss data are collected, compiled and analyzed by insurer to make loss forecasting for the target group and calculate fair premium to distribute the estimated future loss among the group members. Thus larger the group is the better will be the accuracy of loss forecasting. In order to avoid cross-subsidy as was experienced during tariff regime in India the exposure units under consideration of the insurer must be similar if not identical. With this process, insurer can ensure class-based rating and exposure rating in sharing or spreading the losses.

Accidental and Unintentional Loss

Insurance covers only accidental and unintentional losses. Which means, it covers only physical hazards, but not moral hazards that may result into intentional losses or fraudulent claims. All losses to be indemnified by insurance contract must be fortuitous and beyond the control of the insured. And loss forecasting based on law of large number considers only random occurrence of accidents, not deliberate incidents causing loss.

Measurable Loss

While only measurable accidental losses are insurable, future losses or risks not measurable are not insurable. This means that the loss should be determinable and measurable in consideration of perils, place, period, property or person**.** Life insurance (Term Insurance) meets this requirement in most cases without much difficulty vis-à-vis mortality rate, interest rate and expense charge where face value of the policy is payable in case of accidental death. But in certain cases it is really difficult to determine and measure probable loss. For example, for a personal accident policy with disablement benefit the insurer promises to pay a monthly benefit with or without medical expenses to the injured and disabled person if disability as defined in the policy arises out of accident. In such cases, the insurer really finds it difficult to measure probable loss or disability claims for the following reasons:

- Some dishonest claimants stage or present fake sickness or injury in connivance with unscrupulous medical practitioners or professionals.
- Insurers cannot be sure of measure of disability as defined in the policy.

- Sickness and disability are highly subjective and may affect two persons differently.

However, all future losses must be both determinable and measurable with realistic or statistical methods whatever may be the situation of risks in order to make the insurance mechanism meaningful and effective to the policyholders.

Calculable Probability or Chance of Loss

The whole edifice of insurance mechanism rests upon statistical as well actuarial measure of probable loss. The insurer must be able to calculate in advance both probability and severity of the loss. This probability should not be subjective probability based on individual perception or opinion, but should be the objective probability based on the statistical measure of the class of risk exposures. Without such calculation it is not possible for the insurer to render risk-based rating and underwriting for the class of risks. In order to make to probability or severity measure more realistic or accurate, the class of risk exposure units must be homogeneous. Without this calculation either the insured will be loser by way of paying premium in excess of cost or risks or the insurer will incur underwriting loss charging lesser premium. Finally, such underwriting loss will pass on to other groups or class of policyholders in the form of payment of higher premium.

Cat Risks Being Avoidable

As catastrophic losses are not measurable and predictable, they need to be avoided as far as possible. Only pure and particular risks, on the other hand, are measurable and thus insurable. Catastrophic risks such as losses due to flood, storm, typhoon, and earthquake, which cannot be predicted are fundamental risks and cannot be insured like probabilistic risks in traditional insurance. Such fundamental or cat risks can be managed through government assistance or private public partnership (PPP) or ART method of risk transfer from insurance market to capital market. Insurer who assumes cat risks can avoid the concentration of such risks by dispersing their coverage over a large geographical area with less retention and more reinsurance transfer through ART which has been discussed below.

Insurance of Catastrophic Risks – Cat Risks Pool and ART

As Terrorism Insurance Pool and motor TP Insurance Pool are working well, the government and the regulator may consider for the formation of another pool namely CAT Pool to manage insurance of catastrophic risks within the country. General Insurance Corporation (GIC), with the experience of smooth functioning of TP Pool and Terrorism Pool, may be entrusted with the authority of administering CAT Pool. There is no crunch of capital since the corporation has got interest to manage any pool because of capacity and experience. As mentioned earlier, catastrophic risks today does not follow the traditional method of risk transfer because of very high severity. The insurers in the advanced countries like the US, UK have developed a new technology for transfer of cat risks. Such technology is known as Alternative Risk Transfers (ART,) which is commonly used for transfer of many risks that are not insurable under traditional method of insurance and reinsurance. Following is the background and recent development of ART discussed in order to draw a distinction between traditional insurance and reinsurance covering insurable risks and the ART covering all risks:

- It is a mechanism of transfer of huge risks like cat risks, speculative risks, finite risks from small Insurance Market to huge Capital Market enabling spreading risks among unlimited investors in world capital market instead of confining them among limited number of insurers and re-insurers. ART is alternative and gradual process of transfer of local risk to international capital market. ART brings investors' money to the insurance market.

- The earthquake, hurricane and other natural catastrophic perils and their ever-increasing exposures have brought such revolution in the traditional or conventional reinsurance practices for the purpose of increasing the financial capacity unlimited catastrophic exposures.

- Japan, Mexico, (and city like California) and many European countries felt the serious need for finding out Alternative Reinsurance arrangements to match the catastrophic exposures which had gone far beyond the capacity of Insurance, Reinsurance, Retrocession and the Network Activity.

- ART Carriers being Captives, Risk Retention Groups, and Capital Market & Pools registered premium US$88bn in 2001 and thereafter it has been increasing faster than the accretion of traditional insurance and reinsurance market.

- Chicago Board of Trade **(**CBOT) was established in1973. In 1996, Morgan Stanley started **Cat Scheme** but could not succeed. In 1997, US$477mn **Cat** had deals for US. In 1998, more than US$2bn bonds were sold in the US. Thereafter a series of Act bonds were issued.

- The inadequacy capital and capacity of the so-called conventional reinsurance has brought hybrid ART products like i. Swaps, ii. Bonds, iii. Options and iv Securitisation through Special Purpose Vehicle (SPV) to deal with huge financial and speculative risks which are also not insurable in traditional insurance and reinsurance process.

- Corporate Financial Institutions, Mutual Funds, Syndicate of Investors and Banks have become important player of ART market for dealing financial and finite risks.

- Major ART Products in transfer of speculative risks, financial risks are Finite Risk Insurance, Run-off Solutions, Committed Capital, Multi-line, Multi-year Insurance Product, Multi-triggers Programmes of Risk Transfer, and Capital Market Solution for Weather Risks Transfer, etc.

- Apart from cat risks, many other non-traditional risks are being handled under ART. For example, FIFA Bond 2003 in the form of ART replaced conventional insurances. Munich Reinsurance Co. entered into partnership with German Bank HVB Group to include joint financing and reinsuring of large scale products. Today, more than 4000 captives are retaining around 25 per cent of the world's non-life premium.

Terrorism Pool and Insurance of Terrorism Risks

The Indian general insurance industry had set up its own independent terrorism pool after the 9/11 attacks on the US, while most of the developed countries are depending on individual governments to establish a separate terrorism pool to take care of probable contingencies. It is the government, regulator and insurance companies who have taken the initiatives to form the Terrorism Pool being managed by GIC.

India's terrorism insurance pool has been pricing the terrorism risk cover at 50 paise for every Rs 1,000 sum assured (that is value of the property) in case of industrial risks and 30 paisa for every Rs 1,000 sum assured in case of non-industrial risks. The terrorism pool is working well with a corpus of funds collected from all general insurers in India to offset possible future losses arising out of such violence. This became imperative for the country's trade, commerce and industry when terrorism risk cover was excluded globally by insurers and reinsurers. In 2001, the country's terrorism pool of Rs 300 crore per risk rose to Rs 500 crore in 2005, and today it has got the capacity to provide terrorism cover up to Rs 750 crores per risk.

"Right now the terror insurance pool stands at Rs 750 crore. If more members of the insurance community feel the need to expand the pool, it will grow. But it will depend on how much is purchased by the companies," informed J Hari Narayan, the Insurance Regulatory and Development Authority (IRDA).

On the premium, the IRDA chairman further added: "Terror insurance products are bound to be upgraded and the rate of premium might change depending upon the evolution of new products that the industry may come up with." The companies are coming out with products that have terror cover. The 9-year-old terrorism pool, with 12 public and private sector insurance companies contributing, provides terrorism insurance cover in standard fire insurance policy and the premium collected by them is pooled. These companies withdraw amounts in the case of claims against terror attacks. India follows the international market. In the absence of non-availability of reinsurance cover for terrorism risks many countries have set their own wheels and pools in motion to protect their assets from terrorism loss. For example, the German pool was formed in 2002, which was aimed at covering property and business interruption losses following any terrorist attack in Germany.

Affordable and Economically Feasible Premium

One of the major reasons for very poor penetration of insurance in India is the high rate of insurance premium for almost all products. Insurance premium is not economically feasible or affordable to more than 95 per cent of total population. For life insurance, penetration is less than 4 per cent and against non-life it is only 0.6 per cent. In order to make insurance contribute to the economy of the country, the first and foremost duty of the industry is to make insurance premium economically feasible and affordable to greater segment of the population. Insurer should take all possible measures to keep the premium as low as possible to make his product more attractive and affordable to a larger group of customers applying the law of large number and minimize the average frequency and average severity as far as possible.

Insurance and Adverse Selection

In underwriting process insurer must be careful of adverse selection, which increases the cost of insurance and affects insurance development. Adverse selection arises when risks with higher than average probability or severity of loss is insured with other standard risks with same rate, terms and conditions as applicable to the standard risks. For instance, adverse selection may arise in auto insurance with high-risk driving, in health insurance for persons with pre-existing diseases or serious health hazards, in fire insurance for a factory dealing with explosive chemicals. If the applicants for insurance with higher than average chance or severity of losses are granted insurance coverage, there will be adverse selection of risks resulting into higher average claim expenses for other insureds with lesser probability and severity of losses. The insurer should either avoid adverse selection or charge higher premium with more rigid terms and conditions so that underwriting could be risk-based and rating cost-based.

Insurance and Gambling

The purpose and process of insurance bring the clear-cut differences between insurance and gambling. Insurance is always socially and economically productive in view of its immense contribution to trade, commerce, industry and public savings and capital formation of the country while gambling is socially unproductive and harmful. Insurance is sharing of loss whereby neither insurer nor the insured make any gain or profit out of this process. It only spreads the losses of a few over the many making all survive socially and economically. Both the insurer and the insured have the common interests in loss distribution, loss prevention and loss reduction. Both are benefited if loss does not occur because reduction in loss makes the market soft while increase in incurred claim makes the market hard and many insurers make exits from the market due to loss of capital. Insurance covers only pure and particular existing risks while gambling creates a new speculative risk allowing one party to gain or make profit at the expense of others. But in gambling one party gains at the cost of others without occurrence any real loss.

Insurance and Hedging

Insurance is absolutely different from hedging though both the techniques are similar in process for transfer of risks by contracts. An insurance transaction involves transfer of pure and particular risks, which satisfy the requirements of insurability as discussed earlier but hedging is a technique of handling risks of uninsurable and speculative nature. Insurance works on law of large number for averaging of loss of a group of policyholders.

Evaluation of insurance in India

The Government companies including Life Insurance Corporation of India (LIC) and General Insurance Corporation of India (GIC) and its four subsidiaries till 1999-2000 controlled the insurance sector including life and non-life insurance business. As the insurance industry in India was exclusively reserved for the Government sector before 2000 the insurance penetration and its contribution to gross domestic product (GDP) was very negligible. Through amalgamation of 245 insurance companies LIC was established in 1956 for development and administration of life insurance business. Similarly, general insurance business was controlled by GIC and its four subsidiaries as per the General Insurance Business (Nationalization) Act, 1972, the shares of the then large number of Indian and foreign companies stood transferred to GIC and the following four subsidiaries of GIC:

1. The National Insurance Company Ltd.
2. The New India Assurance Company Ltd.
3. The Oriental Insurance Company Ltd.
4. The United India Insurance Company Ltd.

However in November 2000, GIC was notified as the Indian Reinsurer and through administrative instruction, its supervisory role over subsidiaries was ended under the General Insurance Business (Nationalization) Bill 2001. In the post 1991 era and especially in view of India’s commitment to liberalize the financial sector as per the World Trade Organization (WTO) Agreements, this sector was opened up following the recommendation of the Malhotra Committee. The Insurance Regulatory and Development Authority Act, 1999 was enacted. An authority called IRDA was established under Section 3 (1) of the IRDA Act, 1999 has had the duty to regulate, promote and ensure the orderly growth of the insurance and re-insurance business. The powers and functions of IRDA as provided in Section 14 of the Act are:

- To issue, renew, modify, withdraw, suspend or cancel a certificate of insurance as provided by Section 3 of the Insurance Act, 1938;
- To protect the interests of the policyholders in all respects of insurance;
- To specify requisite qualifications, code of conduct and practical training for agents or other insurance intermediaries;
- To specify the code of conduct for surveyor and loss assessors;
- To promote the efficiency in the conduct of insurance business;
- To promote and regulate professional organizations associated with the insurance and reinsurance business;
- To levy fees and other charges for carrying out the purposes of this Act;
- To call for information from and undertake or conduct inspection, enquiries, investigations or audit of the insurers, intermediaries and related organizations;
- To control and regulate rates, terms, conditions and benefits of any product or policy of general insurance;
- To specify the form and manner in which books of account are to be maintained and final statement of accounts to be prepared by insurers or intermediaries;
- To regulate and monitor investment of funds by insurance companies;
- To regulate and review solvency margin;

- To adjudicate disputes between insurers and intermediaries; and
- To specify the percentage of insurance business to be undertaken by the insurer in the rural or social sector

The IRDA may, in consultation with the Insurance Advisory Committee constituted by the Authority under Section 25 of the Act, make regulations in consistent with this Act and the rules made thereunder to carryout the purpose of this Act.

Establishment of Insurance Advisory Committee

1. Under Section 25 of the Act, IRDA may, by notification, establish with effect from such date as it may specify in such notification, a Committee to be known as the Insurance Advisory Committee with the objectives to advise it on the matters relating to making regulations as provided in Section 26.

2. The Insurance Advisory Committee shall consist of not more than 25 members excluding ex-officio members to represent the interests of commerce, industry, transport, agriculture, consumer forum, surveyors, agents, intermediaries, organizations engaged in safety and loss prevention, research bodies, and employees association in insurance sector.

3. The chairperson and the members of IRDA shall be the ex-officio chairperson and members of the Committee.

4. Without prejudice to the provisions of Sub-section (4), the Insurance Advisory Committee may advise IRDA on such matters as may be prescribed.

IRDA to Make Regulations

1. Under Section 26 of the Act, IRDA may, in consultation with the Insurance Advisory Committee, by notification, make

regulations consistent with the Insurance Act and the rules made thereunder to carry out the purpose of this Act.

2. Every rule and every regulation made under this Act shall be laid, after it is made, before each House of Parliament.

Other Important provisions of the Act

No insurer carrying on business in India on or after the commencement of the IRDA Act, 1999, shall be registered unless he has:

- A paid-up equity capital of Rs 100 crores, in case of life insurance or, general insurance business. All insurers (both life and non-life except LIC) should comply with the said provisions of the IRDA Act in regard to capital base.
- A paid-up equity capital of Rs 200 crores for reinsurance business.
- The promoter's holding in a private company should not be more than the percentage to be specified by the Government of India. As per the current provisions of the Act the cap in foreign direct investment is Rs 5 crores.

Small Capital Base in LIC

LIC, the country's largest financial institution, is still having paid-up capital of Rs 5crore only, which does not comply with the minimum capital prescription set out by the IRDA Act, 1999 as mentioned above. LIC's compliance of the IRDA prescription for minimum capital of Rs 100 crore requires changes in the LIC Act, 1956 to enhance its capital base. However increase in capital base of LIC from Rs 5crores to Rs 100crore is under the consideration of the Government. Such hike in the paid-capital for LICI will provide a level playing field with private insurers. Such new capital will come either from Government or LIC's reserves surplus being built by LIC to maintain the required solvency margin. Compared to other insurers' capital base (shareholders' funds), LIC's capital base is a mismatch with its volume of operation. As on 31 March 2007 the policyholders' fund managed by LIC is about 6 lakh crores while its shareholder's fund including paid-up capital and reserves and surplus is Rs 167 crores only. It is possible only because of Government guarantee to policy holders. But if the Government guarantee is withdrawn for the level playing field with private players, the capital base needs to be increased substantially by bringing changes in the LIC Act, 1956 for maintaining required solvency margin. The LIC has not been able to plough back its profits into capital as it has been distributing its entire valuation surplus in the life fund to the policyholders and its sole shareholder i.e. the Government India with the ratio of 95:5. But if the Government's guarantee, which is in the form of quasi capital, is withdrawn for level playing field, its capital base must be increased immediately to protect the policyholders' funds.

Need for Adequate Capital

Insurance business is always a risky business. If it runs mainly with policyholders' funds without requisite shareholders' fund, the policyholders will take the entire stake, which is totally unfair. The need for adequacy of capital of insurers in commensurate with the volume of policyholders' funds can be better appreciated with reference to the case of AIG which is now surviving with Government stimulus package for recovery from crisis. The AIG, the world's largest insurer, has been hit hard by sub-prime lending and credit crisis in the US. Due to financial crisis and bad investments, AIG posted net losses of US$7.7bn and US$5.4bn in the 1st and 2nd quarters of 2008, and only due to 2nd quarter loss of US$5.4bn, its share tumbled down by 8 per cent or a loss of US$2.06 per share. Thus insurance company whether private or public sector must have adequate and risk-based capital and must avoid trading on policyholder's funds to protect their interests. In the last one decade a large number of insurance companies went into liquidation due to inadequate capital following the factors like high guarantees, falling interest rates and miss-selling in advanced countries. Following are a few instances of insurance insolvencies in the advanced countries:

- **Korea –** Korea Life (1998-99), Kookim Life (2000), Hyundai Life, Hanil Life, Samshi, and Allstate Life (1999)

- **United States –** Guarantee Security Life Insurance – mutual (1991), Mutual Benefit Life Insurance – mutual (1991), Executive Life of California (1991)
- **Japan –** Nissan Mutual (1998), Toho Mutual (1999), Daihyaku Mutual (2000), Taisho Life (2000), Chiyoda Mutual (2000), Kyoei Life (2000), Tokyo Mutual (2001)
- **UK –** The Equitable (current), other few due to miss-selling

Risk-based Capital (RBC)

As per regulatory norms insurers are required to have a certain amount capital that is based on the risks of their investments and operations. Insurers are monitored by regulators based on their solvency margin calculated with reference to the ratio between Requirements Solvency Margin (RSM) and Available Solvency Margin (ASM). For non-life insurance business, which is generally a yearly contract, maintaining and monitoring solvency margin may be easier. But in case of insurers for life and health insurance business entering into long-term contracts and investing funds in long-term investments including debt securities, measure and monitoring solvency margins are very difficult task and process. It is monitored with reference to their risks assumed and the risks of investments the insurers have made. For example, insurers that invest in junk bond (less than investment grade bond) or insure credit risks of sub-prime lending or credit-card risks must deploy or set aside more capital than those who invest in Treasury Bonds or assume property risks with less probability and severity of loss exposures. The risk-based capital requirements in life insurance business are based on a formula or method that considers the following risks:

- **Asset Management Risks –** It is a risk of a drastic devaluation of assets because of a crash in stock prices or sharp fluctuation in the currency market, and risk of a sharp increase in irrecoverable loans due to failures of borrowing companies. Such default risks become severe when the investee or the parent company does not hold equivalent amount of risk-based capital which provides due protection against the financial downturn of affiliates. The asset risks include the risks of both equity asset and debt assets. Such risks can be reduced reasonably if the investment norms both prudential and exposures as prescribed by the regulators are duly complied with.

- **Insurance Risk –** It is underwriting risk depending upon the quality of risks assumed and the rate of premium along with the terms and conditions imposed to limit the liability of the insurers. It reflects the amount of surplus needed to pay for excess accidental/death claims because of random fluctuations and inadequate pricing for future liability or because of catastrophic claims beyond the calculated loss-forecasting based on morbidity and mortality rate. Such risks can be reduced substantially if there is prudent underwriting based on proper risk identification, risk analysis and risk quantification in underwriting process. Such risks generally arise out of massive insurance payouts following a disaster or catastrophe.

- **Interest Rate Risks** – Such risk comes when investment return falls below the assumed interest rate or below the guaranteed rate of return on policyholders' funds. In order to have a better clarity over this risk let us take the example of insolvency Nissan Mutual of Japan. Nissan Mutual life was a Japanese life insurance company with 10 lakh policyholders and asset of Japanese Yen 2bn. Nissan Mutual life sold individual annuities at guaranteed rates of 5 to 5-1/2 per cent. The Japanese economy was then booming and the interest rates were on high wave. In early 1990s, the bubble burst, a host of adverse consequences followed the Government bonds yields plunged into record low levels and a large gap occurred between the company's cost of liability to the policyholders and return on investments. On 25 April 1997, Japan's Finance Ministry ordered the company to suspend its business. It lost about Japanese Yen 300bn.

- **Minimum Guarantee Risk** – This risk is related to the minimum guarantee for benefits of variable insurance and variable annuity products.

- **Business Management Risk** – This is business risk in excess of normal expectations in which risk-based capital is closely controlled by solvency margin.

Calculation of Solvency Margin

The insurance regulator prescribes the norms and process for the calculation of solvency margins. In India, IRDA has issued a detailed regulation for the purpose, which has been discussed separately in subsequent chapter. Here let us examine how other countries calculate solvency margin to determine capital adequacy. For example, the solvency margin followed by Japan Life Insurers is based on the formula that considers above-mentioned risks.

$$\text{Solvency Margin Ratio (\%)} = \frac{\text{Total Amount of Solvency Margin}}{\text{Sum Total of Risks} \times \frac{1}{2}} \times 100$$

The “Total” Amount of Solvency Margin” (numerator) is the total of the following:

(a) Total Capital + Price Fluctuation Reserve + Contingency Reserve + General Bad Debt Reserve + 90% of Variance of the Estimate of Other Securities + 85% of Unrealized Gain or Loss on Real Estate + Debt Capital Instruments + Deductible Items, and others.

(b) The “Sum Total of Risks” (denominator) is calculated as follows:

$$= \sqrt{R_1^2} + (R_2 + R_3 + R_7)^2 + R_4$$

R1: Underwriting Risk, R2: Assumed Interest Rate Risk, R3: Asset Management Risk, R4: Business Management Risk and R7: Minimum Guarantee Risk

2
FUNDAMENTAL PRINCIPLES OF INSURANCE

Principles of Insurance

Insurance contracts that differ from other contracts governed by the Indian Contract Act, 1872 are governed by common law, legal principles of insurance apart from insurance laws including the Insurance Act, 1938, the Marine Insurance Act 1963 and many other relevant statutes depending upon the nature of insurance contracts or policies. This chapter deals with legal principles governing insurance contracts. Following are the fundamental legal principles of insurance:

- Principle of Indemnity
- Principle of Insurable Interest
- Principle of Utmost Good Faith
- Principle of Subrogation
- Principle of Contribution

The practical application of these basic principles of insurance applicable to property and liability insurance is examined with further details under the relevant class of insurance to provide clear understanding of these basic legal principles to appreciate the complexities of insurance contracts.

Principle of Indemnity

The principle of indemnity applies to almost all insurance contracts unless they are benefit policies. The principle of indemnity states that the insurer agrees to pay not more than actual amount of loss and the insured should not make any profit from an insurance claim. For example, in the event of total loss of the insured vehicles, insurers pay the market value of the vehicles (its depreciated value) at the time of loss or the sum insured, whichever is less. If the vehicle is damaged, the cost of repairs is paid, but if old parts are replaced by new, suitable deduction/depreciation is charged on the cost of new parts. The insurer reserves the right to repair or replace the vehicle or pay in cash. However, this principle is subject to following exceptions:

- Valued Policy (for antiques, arts, paintings etc)
- Valued Policy laws (as applicable to marine insurance)
- Replacement Cost Insurance

All these exceptions are based on the consideration that payment of the actual cash value can still result in a substantial loss to the insured. To avoid disputes in this regard at the time of claim settlement, all these aspects are to be well considered with appropriate, terms, conditions and amount of premium at the time of underwriting as well as at the time of issuance of policy. The life insurance endowment policy or Unit Linked Insurance Policy (ULIP) is another exception to the principle of indemnity. Life insurance contract is not generally considered as a contract of indemnity.

Principle of Insurable Interest

This principle determines the legal right of the proposer to insure his property or liability. Precisely to be legally enforceable, all insurance contracts must be supported by the principle of insurable interests for the following reasons:

- **To prevent gambling:** If an insurable interest is not required, insurance contracts would be gambling and would be opposed to public interests.
- **To reduce moral hazards:** If an insurable interest is not required, a dishonest person could purchase an insurance policy on someone's property and then cause a loss to that

property deliberately to receive the proceeds. But if the insured stands to lose financially, nothing is gained by causing the loss. In life insurance, an insurable interest requirement reduces the inducement to murder the insured for the purpose of making money through criminal activities.

- **To measure the amount of the insured's loss in property insurance:** Most property insurance contracts are contracts of indemnity. One measure of indemnity is insurable interest requiring that the loss payment cannot exceed the amount of insurable interest.

The principle of insurable interest is based on the following premise or assumptions:

- The existence of property exposed to loss, damage or potential liability.
- Such property or liability must be the subject matter of insurance.
- The insured must have ownership or legal relationship to the subject matter.
- Apart from complete ownership of property, potential legal liability and a contractual right can also support an insurable interest for purchasing an insurance policy.

Following are the important examples on application of this principle:

- In case of purchase of a vehicle under a hire purchase agreement, the finance company has an insurable interest in the vehicle until all the installments are paid. A clause called Agreed Bank Clause is included to protect the interest of the financier. This clause provides that in case of loss or damage to the vehicle, the insurance claim amount shall be payable to the owners i.e. the financiers.
- Motor traders, e.g. garage owners have insurable interest as bailees in respect of loss or damage to customers' cars,

which are in their custody for repair purpose. Motor Trader's Policy covers this liability.

- A bank that gives home loan or loan to businessmen has an insurable interest in the house building or the business property and takes insurance policy on these properties.

- A business man has insurable interest in book debts and may take credit policy.

- An employer as the insurable interest in the lives of his employees and he can take the Employers Liability Policy or Workers' Compensation (WC) Policy. The employer can also take GPA or JPA policy for his employees. But any individual or a firm cannot take any GPA or Group JPA policy for the public at large, where they do not have any insurable interest.

- A contractor or a sub-contractor who is responsible for loss arising out of accident due to faulty workmanship, faulty materials and other errors has the insurable interest in the project he is executing under contract. So principal or contractor or sub-contractor can take Contractor's All Risk (CAR) Policy.

Property and Liability Insurance

In property and liability insurance, the insurable interest must exist at the time of loss. If an insurable does not exist at the time of the loss, a financial loss would not occur for the insured. The principle of indemnity will be violated, if payment is made to anybody without his insurable interest in the property damaged by the occurrence of insured peril. For example, if X who had taken a fire insurance policy on 1 January 2008 for his house sold his house on 30 June 2008 to Y. Due to accidental fire occurred on 1 July 2008, the house was totally gutted. Here neither X nor Y can recover loss from the insurance company because X did not have insurable interest at the time of accident and Y is not named under the policy. In property insurance, the proposer may not have an insurable interest in the property when the contract is first written, but may expect to have an insurable interest in future at the time of possible loss. For example, in marine or transit insurance, it is common to insure consignment either for importer or return cargo (Sellers' Contingency Policy) for exporter by a marine insurance contract before the ship sails. Section 7 of the Marine Insurance Act, 1963 provides that (1) Subject to the provisions of this Act every person has an insurable interest who is interested in a marine adventure; (2) In particular, a person is interested in a marine adventure where he stands in any legal or equitable relation to the adventure or to any insurable property at risk therein, in consequence of which he may benefit by the safety or due arrival of insurable property, or may be prejudiced by its loss, or by damage thereto, or by the detention thereof, or may incur liability in respect thereof.

Legal Aspect of Principle of Insurable Interest In Marine Insurance

Again, Section 6 of The Marine Insurance Act, 1963 provides that (1) Every contract of marine insurance by way of wagering is void; (2) A contract of marine insurance is deemed to be a wagering contract:

- where the assured has not an insurable interest as defined by this Act, and the contract is entered into with no expectation of acquiring such an interest; or

- where the policy is made "interest or no interest", or "without further proof of interest than the policy itself", or "without benefit of salvage to the insurer" , or subject to any other like term provided that, where there is no possibility of salvage, a policy may be effected without benefit of salvage to the insurer".

Thus the Marine Insurance Act, 1963 defines insurable interest and its importance for marine insurance management both underwriting and claims.

Life Insurance & Insurable Interest

In life insurance, the insurable interest requirement must exist at the time of issuance of the policy, not necessarily at the time of death or maturity claim. As indicated above life insurance is not a contract of indemnity, but a valued policy that pays a stated sum upon the insured's death. Because the beneficiary has only a legal claim to receive the policy proceeds, the beneficiary does not have to prove that loss has been incurred by the insured's death.

Utmost Good Faith

An insurance contract is a contract *uberrima fides* or of utmost good faith imposing a legal obligation on the proposer to disclose material facts about the subject matter of insurance to the insurer. A wrong declaration or wrong answer in the proposal form makes the contact voidable by the insurer. Some examples of material facts that make the following types of insurance contracts voidable at the option of the insurer are given below:

- **Motor Insurance:** Type, make of vehicle, Engine and Chassis No, Year of Manufacture, Area of Use, Condition of Vehicle, Driver's Details, and Past Loss Experience, etc.

- **Fire Insurance**: Construction details, occupation details, process details, Event Analysis, FEA details, storage details, hazardous chemicals, P&M details, security details, and claim experience, etc.

- **Marine Insurance**: Section 19 of the Marine Insurance Act, 1963 clearly mentions that a contract of marine insurance is a contract based upon the utmost good faith, and if the utmost good faith be not observed by either party, the contract may be avoided by the other party. The insured must make correct representation or information in regard to cargo details, nature of packing and nature of packages, value of insurance, vessels details, transit/voyage details, BL/LR/RR No, and past claim experience to enter into a valid marine insurance contract.

The doctrine of utmost good faith imposes a higher degree of transparency on both the parties to insurance contract. The principle has its historical root in ocean marine insurance. In ocean marine insurance, the insurer has to place great faith in statements/ declarations made by the applicant for insurance where the property to be insured are generally not visually inspected and contract may be formed at a place very far from the ship or the warehouses, the points of loading and unloading. Like marine insurance, in liability insurance, an insurer has to place great faith in the statements of the applicant, as there is no scope for examination of evidence or prediction of future liability on past records.

The principle of utmost good faith is supported by following three legal doctrines:

(i) **Representation:** It is a statement made by the applicant for insurance. An insurance contract is voidable at the insurer's option if the representation is: i) material; ii) false; and iii) relied upon by the insurer. **Material** means that if the insurer had known the facts, he would not have issued the policy or would have issued a policy on different rates, terms or conditions. **False** means that if mediclaim policy is issued on the proposal from showing no high blood pressure or no past records of disorder in circulatory system, the insurer may deny payment of mediclaim if high blood pressure is found to be pre-existing.

(ii) **Concealment:** It is an intentional failure of the applicant to reveal a material fact to the insurer. The insurance contract becomes voidable at the option of the insurer due to concealment of material fact.

(iii) **Warranty:** The insurer in view of the specific representation of the proposer may impose certain **warranty** to be complied with by the insured. If the warranty is not complied with during currency of the policy, the insurance contract becomes voidable.

Life Insurance Contracts and Utmost Good Faith

Section 45 of the Insurance Act provides a special law with regard to life insurance policy. This Section provides that no policy of life insurance shall, after the expiry of two years from the date on which it was effected, be called in question by an insurer on the ground that a statement made in the proposal for insurance or in any report of medical officer or referee or friend of the insured or in any other document leading to the issuance of the policy, was inaccurate or false unless the insurer shows that such statement was on a material aspect or suppressed facts which was material to be disclose and that it was fraudulently made by the policyholder who knew at the time of making it that the statement was false or that it suppressed facts which it was material to disclose. But nothing in this Section shall prevent the insurer from calling for proof of age at any time if he is entitled to do so and no policy shall be deemed to be called in question merely because the terms of the policy are adjusted on the subsequent proof that the age of the life insured was incorrectly stated in the proposal.

Case Laws on Utmost Good faith

(a) **Roselodge vs. Castle (1966):** A company that had not disclosed the conviction of its sales manager for smuggling diamonds in the proposal form though there was no specific question in this regard in the proposal, could not succeed in recovering amount in the burglary claim for a diamond robbery.

(b) **Lambert vs. Co-operative Insurance Society (1975):** The insured did not disclose that her husband had been convicted of crime of dishonesty in 1971 at the time of renewal in 1972, though no question was asked about previous conviction. A claim was made for lost or stolen jewellery in 1972. The insurers repudiated the claim on the ground that the conviction had not been disclosed. It was held that the insured was under a duty to disclose the original conviction and the subsequent convictions when renewing the policy and what was material fact that which would influence the mind of a prudent insurer.

(c) **Bond vs. Commercial Union Assurance Co:** Bond completed a proposal for motor insurance. Later on, an accident happened when his young son drove his car. The claim under this policy failed when insurer pleaded that Bond had failed to disclose all material facts, and since all the questions in the proposal form had been fully answered, he should have informed that his young son who was likely to drive the vehicle, had previous convictions.

Principles of Subrogation

The principle of subrogation that supports the principle of indemnity implies substitution of the insurer in place of the insured for the purpose of claiming indemnity from a third person if considered liable for loss covered and paid under insurance policy. Under this principle, the insurer is entitled to recover from a negligent third party any loss paid to the insured. For example, in a marine cargo insurance, accidental loss, if admissible, is paid to the insured by the insurer with the subrogation right or the right of recovery of loss from the carrier if the accident is caused due to negligence of the carrier. Subrogation does not apply unless a loss is paid to the insured. The general rule is that by exercising its subrogation rights, the insurer is entitled only to the amount it has paid under the policy. When due to underinsurance the insured is not be fully indemnified by the insurer, any subsequent recovery by the insurer from the negligent person causing the loss may be shared by both the insured and the insurer. For example, X's house which was insured for Rs 2, 00,000 was gutted by fire due to short circuit. The house was worth Rs 3,00,000. The insurance company indemnified the loss only up to Rs 2,00,000. Subsequently, the insured recover Rs 15,00,00 from the errant electrician. The insured and the insurer would share the said recovery from the errant for Rs 100,000 and Rs 50,000 respectively. Importantly, if the insured waives the right to sue the negligent person, his right to recover the loss from the insurer stands waived. For example, in a motor accident if the insured admits his own faults or attempts to settle a collision loss with the negligent driver without the insurer consent, the insured's right to be indemnified by the insurer gets lost. The principle of subrogation meets three basic purposes:

1. It prevents the insured from collecting twice for the same loss-one from insurer and then from the offender if established.

2. It acts to hold the guilty or negligent person responsible for the loss.

3. It helps to bring down insurance loss and consequent premium rates.

The principle of subrogation does not apply to life insurance and individual health insurance contracts. Life Insurance is basically not a contract of indemnity and hence Subrogation Principle does not apply. Likewise most of the health insurance contract does not contain the subrogation clause.

Principles of Contribution

Contribution is a corollary of indemnity. There should be proper wording for it. General wording of Contribution in a standard fire policy is as follows:

> "If at the time of any loss, damage or liability arising under this policy there shall be any other insurance, whether effected by the insured or any other person covering the same property or liability or any part there of, the company shall not be liable for than its ratable portion of such loss or damage".

In this regard case studies like Gale vs. Motor Union Assurance Co. Ltd (1928) and Loyst vs. General and Life Assurance Corp. Ltd deserve special mention where both the insurance companies have been exonerated from liability with unique application of the doctrine of contribution and policy condition simultaneously. To apply this principle the consideration must be made on the important aspects like: (i) The same interest; (ii) The same subject matter; (iii) The same peril; and (iv) The same period of time.

3

ANALYSIS OF INSURANCE CONTRACT-CHARACTERISTICS

Legal Characteristics

Though an insurance contract is based on the law of contract it has certain special legal characteristics that make them different from other legal contracts. Besides main basic legal requirements of contracts including Offer and Acceptance, Consideration, Capacity to contract and legal purpose for enforceability of contracts, insurance contracts have following distinct legal characteristics:

- Aleatory Contract
- Unilateral Contract
- Conditional Contract
- Personal Contract
- Contract of Adhesion

In this chapter, we will discuss above-mentioned distinct legal characteristics besides applications of a few other legal requirements.

Aleatory Contract

An insurance contract is aleatory one rather than commutative. An aleatory contract is a contract where values exchanged are generally unequal depending upon a future uncertain event and its expected value. A commutative contract is one where the values exchanged by both the parties are principally equal. For example, the purchaser of any property pays the price that is viewed to be equal to the value of the property. But in case of a property insurance (say fire policy), the insured pay premium say one per cent in view of loss forecasting based on the probability and severity of loss due to fire perils. Although the essence of an aleatory contract is chance or the occurrence of some fortuitous event, an insurance contract should not be a gambling. In insurance, only pure risks are covered, not the speculative risks. More specifically, although both gambling and insurance are aleatory in nature; an insurance contract is not a gambling contract because no new risk is created thereby.

Unilateral Contract

An insurance contract is a unilateral contract because after payment of premium only one party is bound to keep a legally enforceable promise, i.e. to pay accidental claim or other benefits to the insured. After the first premium is paid, the insurance comes into effect, the insured cannot be forced to pay additional premium to comply with the policy provisions unless it is engineering project insurance where the insured is allowed to pay premium on installment basis. In that case the insured must continue to pay all installments of premium as per terms of the policy in order to keep the policy in force. In contrast, most commercial contracts are bilateral in nature. Each party makes a legally enforceable promise to the other party. If one party fails to perform, the other party can insist on performance or sue for damages for any breach.

Conditional Contract

An insurance contract is a conditional contract because the insurer's obligation to pay a claim depends on whether the insured or the beneficiary has complied with all policy conditions. For example, in a standard fire policy there are about 12 claim conditions apart from general provisions which the insured must comply as otherwise an insurer can repudiate a claim due to breach of any condition. One of such condition is that the insured must give immediate notice of a loss or damage arising out of an accident. If the insured delays in giving such notice for unreasonable period, the insurer can refuse to pay the claim on the ground that policy condition has been violated. Thus policy conditions impose certain duties on the insured to comply in order to make the insurer legally binding to pay insurance claim.

Personal Contract

Property insurance is a personal contract implying that the contract is entered into between the insured and the insurer and in case of loss or damage of the insured property caused by the operation of insured peril only the specified insured will be indemnified. Because of personal nature of insurance contract, the property owner must be also acceptable in view of moral hazards while property risks are analyzed due to its physical hazards for underwriting risks. Property insurance cannot be normally assigned to another party without the consent of the insurer. Assignment of property insurance to another person required for change in ownership, or use of property always alters the risk profile because it may increase the probability and severity of loss. So assignment is affected with the consent of the insurer and through an appropriate endorsement thereto in the policy. Conversely, a life insurance policy can be freely assigned to anyone without the insurer’s consent because the assignment usually does not change the risk factors or increase the probability of death.

Contract of Adhesion

It implies that the insured must accept the entire contract with all its terms and conditions and after issuance of policy cannot insist that certain provisions or conditions should be added or deleted or the contract be rewritten to suit the insured. Any change or alteration is always subject to insurer’s approval and endorsement in the policy. To redress the imbalances, if any in the policy, the courts have ruled that ambiguities or doubts in the insurance contracts are constructed against the insurer under the principle of reasonable expectations and the insured gets the benefit of doubt. The Principle of reasonable expectations implies that an insured is entitled to coverage under a policy that he or she reasonably expects it to provide and that to be effective, exclusions or qualifications must be conspicuous, plain and clear (The Legal Environment of Insurance–American Institute for property and liability underwriting).

Contract of Legal Purpose

Like other commercial contracts an insurance contract must be only for legal purpose. An insurance contract that encourages something illegal or immoral or contrary to the public interests cannot be legally enforceable. No insurance policy will cover transit risks of illegal drugs or heroin or risks of loss from seizure of illegal drugs or property.

Contract of Insurance and Rule of Agency Law

An insurance policy is normally sold through brokers, agents or corporate agents who represent the principal (insurers). As detailed in subsequent chapters, the insurance must have license to act as such as per the provisions of the specified regulation in order to represent the principal. If the agent acts within the code of conduct specified by the regulator, the principal (insurer) will be responsible for the acts of agents within the scope of their authority. This responsibility also includes fraudulent acts, omission and misrepresentations of agents. Furthermore, in insurance contract knowledge of the agent is presumed to be the knowledge of the principal in regard to policy matters within the scope of the agency.

Insurance Contract and Doctrine of Waiver and Estoppels

The doctrine of Waiver and Estoppel apply to the powers of insurance agents and also to the powers of insurers at the time of insurance claim. Under this doctrine if an insurer voluntarily waives a legal right conferred by the policy condition, he cannot deny later on the required payment of a claim under the pretext that such right has been violated. The doctrine of waiver can be defined as the voluntary relinquishment of a known legal right. The term estoppel derived from English Common law also apply to insurance contract when a representation of fact made by one person to another person is reasonably relied upon by that person to such an extent that it would be inequitable to allow the first person to deny the truth of the representation. The insurer sought to determine liability through arbitration and is estopped from exercising settlement on repair basis in motor of claims.

Insurance Contract - Offer, Acceptance and Binder

In order for insurance contract to be binding on the parties, i.e. the Insured and the insurer, there must be an offer and acceptance. An applicant makes offer and the insurer accepts the risks. Though offer and acceptance can be either oral or written, but for all practical purposes in insurance contracts offer and acceptance are only in written form. In property and liability insurance, the agent or broker who accepts premium along with duly completed offer from the prospect have the authority to bind his principal, i.e. insurer through the use of a binder. A **Binder** is a temporary contract (Cover Note). The binder or cover note obligates the insurer immediately prior to receipt of insurance application and issuance of policy. However, in some cases the agent is not authorized to bind the insurer and the application for insurance must be sent to the insurer for acceptance by the insurer and issuance of the policy thereafter.

In life insurance the procedures followed are different where life insurance cannot bind the insurer. The application is always in writing and insurer approves the insurance proposal before the life insurance is in force. A life insurance agent does not have any power to bind the insurer. Application for life insurance is always in writing and the application must be approved by the insurance. Generally, written application is submitted to the agent with first premium and a conditional receipt is given to the applicant. The most common conditional receipt is the ‘insurability premium receipt’. If the applicant is found insurable according to the standard underwriting practice, life insurance cover becomes effective and enforceable from the date of application. In property and life insurance the agent follows same practice in general subject to certain exceptional cases like renewal of policy with acceptance of renewal premium.

Basic Parts of Insurance Contracts

Insurance contracts can be divided into the following main parts:

- Insurance Agreement
- Description
- Coverage
- Exclusions
- Conditions
- General Provisions
- Endorsements
- Riders
- Deductibles

Although all insurance contracts may not contain all such parts, they provide convenient framework of insurance contracts in general for analysis of foregoing legal characteristics.

Insuring Agreement

The core part of insurance contract is Insuring Agreement that precisely specifies the promises of the insurer to indemnify loss or pay defined benefits on the occurrence of certain event due to insured perils. The wording or framework of insuring agreement of property insurance varies from that of liability insurance in respect of period of insurance, policy period, sum-insured, indemnity limit etc., which have been discussed in length in respective insurances. Life insurance which is an all-risks cover contains a different type of insurance agreement. It covers all causes of death either of accident or disease with exclusions of death due to certain aviation hazards and war perils in certain cases. The insuring agreement in property and liability insurances is known as Operative Clause, which has been discussed and analyzed under respective segments of insurances.

Description

The particulars or information about property, activity, liability covered by policy is clearly described in a schedule forming part of the policy. The particulars provided in the schedule are based on information and declarations contained in the proposal form or the offer for insurance. In property and liability insurance, the proposal containing information concerning the identification of the insured, property, liability, activity, period of insurance, amount of insurance (sum-insured or indemnity limit), amount of premium, size of deductible and other relevant information depending upon the nature and type of cover is the core part of insurance contract. If any information or declaration is found to be misrepresented, the contract will be treated void or voidable at the option of the insurer.

Coverage

It is the most essential part of insurance policy. Coverage is of two types: (i) **Named Perils Coverage;** or (ii) **All-Risks Coverage**. Under named-policy coverage, accidents and losses caused by the perils specifically named in the policy are covered. For example, a Standard Fire and Special Perils policy specifies 11 perils like fire, explosions, implosions, storm, typhoon, flood and inundation, riot, strike and malicious damage, etc. Any loss or damage by the perils specified will be admissible for indemnification by the insurer. Under “All-Risks” Policy all losses are covered except those losses specifically excluded. For example, Industrial All Risks Policy covers all losses or damages to property by any perils external or internal other than by a specifically excluded cause in the policy. “All-Risks” coverage is preferable to the insured, but not readily acceptable to the underwriters even though the insured is prepared to pay higher rate of premium because of higher probability and severity of losses in open policy. To deny payment for a claim in All-risks policy the insurer must prove that the loss is excluded specifically. So the burden of proof is placed on the insurer to deny claim while in a named-policy, such burden of proof lies on the insured. He is to prove that loss has occurred from any of the Insured Perils, but not from **uninsured perils** and **excluded perils** named in the policy. Life insurance is one kind of 'all-risks' policy because it generally covers all causes of death whether by accident or by disease. The major specific exclusions include suicide, war perils, etc.

Exclusions

Exclusions are another basic part of policy. These exclusions may of three types:

1. Excluded Perils
2. Excluded Losses
3. Excluded Property

Excluded Perils

All policies exclude certain perils or causes of loss. For example, general exclusions in a Standard Fire and Special Perils policy include loss, destruction, damage by caused by war, invasion, act of foreign enemy, nuclear fuel or waste, earthquake, volcanic eruption, etc.

Excluded Losses

Such fire policy excludes loss for first 5 per cent of every claim subject to a minimum of Rs 10,000 in respect of each and every loss arising out of Act of God (AOG) perils such as lightening, storm, tempest, flood, inundation (STFI), landslide, etc.

Excluded Property

Such fire policy covers only land-based property specified in the policy but not any property on seas or rivers or property in the air. It excludes losses to property insured if removed to any building or place other than in which it is stated to be insured except for repairs.

Conditions

This part of the insurance policy is also very important in a total insurance contract. Underwriting which is the core function of insurance includes selection of risks, acceptance of risks, rating of risks and deciding terms and conditions to limit the loss exposures according to risk analysis results. Conditioning risks and rating risks are dependent on each other. Conditions are provisions in the policy that qualify or place limitations on insurer' liability to indemnify or perform. For example, a standard fire policy specifies 15 conditions such as cancellation of policy or repudiation of loss in case of mis-representation or non-disclosure of any material particular, notifying the insurer if a loss occurs, protecting the property after loss, etc.

General Provisions

Insurance contracts also contain a number of general provisions for avoidance of disputes and disagreement between the insured and the insurer in future or at the time occurrence of accident and payment of loss. For example, a property or liability insurance policy contains the general provisions like Rules for Cancellation, Mid-term Cover, Mid-term Revision of sum-insured or Indemnity Limit, Basis of indemnity, Renewal of Policy, Other Insurance & Contribution, Subrogation, etc.

Endorsements

It is a written provision that adds to or deletes, or modifies the provisions of the original contract. There arises the need for various types of endorsement in property and liability insurance. Endorsements required for increase or decrease of sum-insured, change of place, property or persons originally covered, change in ownership are the common nature of endorsement in property insurance. Similarly, change of indemnity limits or jurisdiction may necessitate suitable endorsements. An endorsement subsequently attached to the original contract generally takes precedence over any conflicting terms in the contract unless the relevant law, rule or regulatory norms require that a standard policy shall be used with specified terms, conditions or wordings for coverage, exclusions, etc. An endorsement cannot be used to circumvent the purpose of legislation or regulation by modifying the specified terms or wordings of the standard policy. Endorsement cannot be contrary to any law or regulation.

Riders

The terms endorsements and riders are often used interchangeably and meaning almost same thing. In property and liability insurance, the term 'endorsement ' is used for subsequent change in written provision, while in life and health insurance, such provision is called rider. Different riders are used to provide for subsequent increase or decrease in benefits or waive a condition of coverage present in the original policy. Rider is used to amend the basic policy. For example, a waiver of premium rider can be added to a life insurance policy with a provision that if the insured becomes disabled, all future premiums are waived after expiry of a specified period, so long as the insured remains disabled on production of disablement certificate or necessary inspection.

Deductibles

A deductible is a common policy condition or provision that requires the insured to pay for a particular part of the loss occurred. It is a written provision in the policy, by which a specified amount is subtracted from the total loss payment that otherwise would be payable by the insurer. Almost all property insurance including fire, marine, motor, engineering insurances, health insurance contracts or policies are subject to deductibles specified in the policies. Deductibles are not used in life insurance contracts, the insured's death is, always a total loss. In liability insurance or personal accident insurance, deductibles are not provided for. Deductibles in property insurance generally serve the following purposes:

- Elimination of small claims
- Reduction of premium
- Reduction or prevention of moral or morale hazards

Deductibles encourage the insured to be more careful about loss prevention measures and protection of property. Deductibles in property insurance are of two types: Straight Deductibles and Aggregate Deductibles.

4

THE INSURANCE ACT 1938 & INSURANCE MANAGEMENT

Legal Provisions for Insurance

The Insurance Act, 1938 as amended by the Insurance (Amendment) Bill, 2001 in view of the requirements of the various provisions of the Insurance Regulatory and Development Authority Act (IRDA), 1999 enacted by the Parliament to protect the interests of policyholders, to regulate, promote and ensure orderly growth of the insurance industry in the country keeping in view to further amend the Insurance Act, 1938, the Life Insurance Corporation Act, 1956 and the General Insurance Business (Nationalization) Act, 1972. The legal provisions of this Act have been divided into 5 Parts containing 120 Sections and 8 Schedules. It is not possible to discuss all sections and schedules in this manual although all sections are equally important for the professional working in the industry in various capacities. Only a few common sections have been outlined below for ready reference. It would be better if the readers refer the original government publication for detailed study in case of specific purport or requirement.

Registration for Insurance Business

Certificate of Registration: As per the provisions of Section 3 of the Insurance (Amendment) Bill, 2001 no person shall, after the commencement of this Act, begin to carry on any class of insurance business in India and no insurer carrying on any class of insurance business in India shall, after the expiry of three months from the commencement of this Act, continue to carry on any such business, unless he has obtained from the Authority (IRDA) a certificate of registration for the particular class of business.

Provided that any certificate of registration, obtained immediately before the commencement of the IRDA Act, 1999 is deemed to have been obtained from the Authority as per provisions of the Act.

Provided that in case an insurer who was carrying on any class of insurance business in India at the commencement of the Act, failed to obtain a certificate of registration under the Act shall not invalidate any contract of insurance entered into by him.

Provided further that an insurer carrying on any class of insurance business in India before the commencement of the IRDA Act, 1999, for which no registration certificate was necessary earlier, could continue to do so for a period of three months from such commencement or if he had made an application for such registration, till the disposal of such application.

Application for Registration

Application for registration shall be made in such manner as specified in the regulations and shall be accompanied by the following documents/statements when the applicant is a company:

- A Certified copy of the Memorandum of Association or Articles of association
- The names, addresses and the occupations of the directors
- A statement of the class or classes of insurance business done or to be done
- A certificate from the RBI showing the amount deposited for such application
- A declaration verified by an affidavit by the principal of the insurer in regard to compliance of Section 6 or Section 97 in regard to paid-up equity capital or working capital
- A statement verified by an affidavit, in case of an insurer having its principal business or domicile outside India, by the principal officer stating the requirement if any, not applicable to the nationals of the country where it is domiciled or incorporated or constituted.

- A certified copy of the published prospectus and of the standard policy forms of insurance and statements of assured rates, advantages, terms and conditions to be offered in respect of insurance policies together with a certificate in connection with life insurance business by an actuary that such rates and terms are workable.

- The receipt showing payment of fees as may be determined by regulations which shall not exceed Rs 50,000 for each class of business

- Such other documents as may be specified by the Authority

Granting the Certificate of Insurance

If on receipt of an application for registration and after making such inquiry as deemed fit, the Authority is satisfied on the following aspects, the Authority may register the applicant as an insurer and grant him a certificate of registration:

- The financial strength and the general character of management of the applicant are sound.

- The volume of business likely to be achieved and the capital structure and the earning prospectus of the applicant will be adequate.

- The interests of the general public will be served if the certificate of registration is granted to the applicant in respect of class or classes of business.

- The applicant has complied with the provisions of this Section along with Sections 5, 31A and 32 of the Act.

Renewal of Registration

(a) An insurer who has been granted a certificate of registration under Section 3 shall have the registration renewed annually for each year after that ending on 31 March every year.

(b) An application for the renewal of a registration for any year shall be made by the insurer to the Authority before the 31 December of the preceding year and shall be accompanied by such documents as mentioned above for registration and evidence of payment of the fee as determined by the regulations made by the Authority, which may vary according to the total gross premium written, but shall not: i) exceed one-forth of 1 per cent of premium income or Rs 5 crore whichever is less; and ii) be less in any case, than Rs 50,000 for each class of insurance business. *This amount may vary as per regulations to be issued by the authority from time to time*.

(c) The fee as determined by the regulations made by the Authority for the purpose shall be paid into the RBI or where there is no branch of RBI, into the Imperial Bank of India or into any Government treasury.

(d) If the insurer fails to apply for renewal of registration before the date as mentioned above the Authority may accept an application for renewal of the registration on receipt from the insurer of the fee and the penalty unless the application has been made to the court under Section 3(5D).

(e) The Authority shall, on fulfillment by the insurer of the above requirements renew the registration and grant him a certificate of renewal of registration.

Certification of Soundness of Terms of Life Insurance Business

When considering an application for registration as mentioned above, if it appears to the Authority that the assured rates, advantages, terms, and conditions offered or to be offered in connection with life insurance business are in any respect not workable or sound, he may require that:

- a statement thereof shall be submitted to the actuary appointed by the insurer for the purposes and approved by the Authority.

- the insurer to make within such time as may be specified in the written order such modifications in the said rates, advantages, terms or conditions as the case may be as the actuary may report to be necessary to enable him to certify that the said rates, advantages, terms and conditions are workable and sound.

Such requirements are especially applicable to the life insurance business as it is based on long-term contracts unlike general insurance business, which are mostly annual contracts.

Requirements as to Capital

Under Section 6 of this Act, no insurer carrying on the business of life insurance, general insurance or re- insurance in India on or after the commencement of the IRDA Act, 1999 shall be registered unless he has:

- A paid-up equity capital of Rs 100 crores, in case of a person carrying on the business of life insurance or general insurance business or;

- A paid-up equity capital of Rs 200 crores in case of a person carrying on exclusively the business as a re-insurer.

Provided that in determining the paid-up equity capital as specified above, the compulsory deposit made with RBI under Section 7 of the Act as stated below shall be excluded.

Provided further that an insurance company carrying on business of life insurance, general insurance or reinsurance business before the IRDA Act 1999 and who is required to be registered under this Act shall have a paid-up equity capital in accordance with foregoing provisions.

Requirements as to Capital Structure

Under Section 6A of the Act no public company limited by shares having its registered office in India, shall carry on life insurance business, unless it satisfies the following conditions:

- The capital of the company consists only of ordinary shares each of which has a single face value
- The paid-up amount is the same for all shares, whether existing or new except during any period not exceeding one year allowed by the company for payment of calls on shares.
- Without prior approval of the Authority (IRDA), no individual, firm, group or body corporate under the same management jointly or severally shall transfer shares, where the nominal value of the shares exceeds 1 per cent of the paid-up capital of the insurer.

Note: on and from the commencement of the Insurance (Amendment) Act, 1968, the above provisions on capital structure also apply to the insurers carrying on general insurance business subject to certain modifications.

Shareholding by Promoters

Under Section 6A of the Act, no promoter shall at any time hold in an Indian insurance company, more than 26 per cent of the paid-up capital or such other percentage as may be prescribed by the authority or the Central Government. Provided that in case where an Indian insurance company commences the business of insurance in which promoters hold more than 26 per cent of the paid-up equity capital or such other excess percentage as may be prescribed by the Central Government, the promoters shall divest in a phased manner the share capital in excess of 26 per cent of the paid-up capital or such excess as may be prescribed, after a period of 10 years from the date of commencement of the said business by such Indian insurance company or within such period as may be prescribed by the Central Government. The manner and procedure for divesting excess share capital shall be specified by the regulations made by IRDA.

Deposit with RBI

Under Section 7 of this Act, every insurer shall in respect of the insurance business carried on by him in India, deposit and keep deposited with RBI for and on behalf of the Central Government the specified amount either in cash or in approved securities estimated at the market value of the securities on the day of deposit or partly in cash and partly in approved scurrilities so estimated, which are mentioned below:

(a) In case of life insurance business, a sum equivalent to one per cent of his total gross premium written in India in any financial year commencing from31 March 2000 not exceeding Rs 10 crores.

(b) In the case of general insurance business, a sum equivalent to 3 per cent of his total gross premium written in India, in any financial year commencing after 31 March 2000.

(c) In case of reinsurance business, a sum of Rs 10 crores.

Provided that where the business done or to be done is marine insurance only and relates exclusively to country craft or its cargo or both, the amount to be deposited shall be Rs 100,000. An insurer shall not be registered for any class of business in addition to the class or classes for which is already registered until the full deposit required has been made. If any part of a deposit made under this section is used in the discharge of any liability of the insurer, the insurer shall deposit such additional sum in cash or approved securities estimated at the market value of the securities on the day of deposit or partly in cash and partly in such securities, as will make up the amount so used. The insurer shall be deemed to have failed to comply with the requirements, unless the deficiency is supplied within a period of two months from the date when the deposit or any part thereof is so used for discharge of liabilities. Under Section 8 any deposit made under the provisions of Section 7 or deposits made under Section 98 by Mutual Insurance Companies and Co-operative Life Insurance Societies shall be deemed to be part of the assets of the insurer and shall not be susceptible to any assignment or charge, nor shall it be available for the discharge of any liability of the insurer other than liabilities arising out of policies of insurance issued by the insurer so long as any such liabilities remain un-discharged; nor shall it be liable to attachment in execution of any decree except a decree obtained by a policyholder in respect of a debt due upon a policy which debt the policyholder has failed to realize in any way.

Accounts and Funds

Separate Accounts and Funds for Each Class of Business

All insurers are required keep accounts for the insurance business written by them in the manners as outlined below:

- Where the insure carries on business of more than one class of business he shall keep a separate account of all receipts and payments in respect of each of such classes namely, Life insurance, Fire insurance, marine insurance, miscellaneous insurance, etc., and also a separate account of all receipts and payments in respects and payments in each of such sub-classes of miscellaneous insurance business as may be prescribed in this regard unless the Authority waives the requirement.

- Where the insurer carries on the business of life insurance all receipts due in respect of such business, shall be carried to and shall form a separate fund to be called life insurance fund the assets of which shall be kept distinct and separate from all other assets of the insurer and the deposit made by the insurer in respect of life insurance business shall be deemed to be part of the assets of such fund, within the time-limit as mentioned in Section 15(1), furnish to the Authority a statement showing in detail such assets at the end of every calendar year duly certified by an auditor.

- No insurer carrying on life insurance business shall be entitled to be registered for any class of insurance business in addition to the class or classes for which he has been registered, unless the authority is satisfied that the assets of the life fund are adequate to meet all his liabilities on policies of life insurance maturing for payment.

- The life insurance fund shall be absolutely the security of the policyholders, as though it belongs to an insurer carrying on no other business than the life insurance business and shall not be applied directly or indirectly for any purposes other than those of the life insurance business of the insurer.

Accounts and Balance Sheet and Audit

Under Section 11 of the Act, every insurer in respect of insurance business transacted by him and in respect of his shareholders' funds shall at the expiration of each financial year, prepare with reference to that year:

- Balance Sheet,
- Profit and Loss Account
- Separate account of Receipts and Payments
- Revenue account in accordance with the specific regulations by the Authority

The insurer shall keep separate accounts relating to the funds of shareholders and policyholders. The salient features of the specific regulation called IRDA (Preparation of Financial Statements and Auditor's Report of Insurance Companies) Regulations have been discussed hereafter in chapter.7

Under Section 12 of the Act, the Balance-sheet, Profit and Loss Account and Profit and Loss Appropriation Account of every insurer are subject to audit under the provisions of the Company Act, 1956 (as amended), the Accounting Standards and Auditing Standards issued by the Institute of Chartered Accountants of India (ICAI) and the IRDA (Accounts & Auditor's Report) Regulations 2000. The report of the auditors on the financial statements of every insurer shall deal with the matters specified in the Schedule C of Regulation 3 of the IRDA (Preparation of Financial statements and Auditor's Report of Insurance Companies) Regulations, 2000. The Authority, from time to time, issues separate guidelines in the matter of appointment, continuance or removal of auditors of an insurer or reinsurer, as the case may and such guidelines may include prescriptions regarding qualifications and experience of auditors, their rotation, and period of appointment.

Actuarial Report and Abstract for Life Insurance Business

Under Section 13 of the Act, every insurer carrying on life insurance business shall, in respect of the life insurance business transacted by him in India and in the case of an insurance company incorporated under the law of any country other than India, in respect of all life insurance business transacted by him, every year cause an investigation to be made by an actuary into the financial condition of the life insurance business carried on by him, including a valuation of his liabilities in respect thereto and shall cause an abstract of the report of such actuary to be made in accordance with regulations contained in Part 1 of the Fourth Schedule and in conformity with the requirements of Part 11 of the Schedule.

However after commencement of the IRDA Act 1999, it shall cause an abstract of the report of the actuary in the manner specified by the regulations called the IRDA (Actuarial Report and Abstract) Regulations, 2000. As per Regulation 4 of the said Regulations, Abstracts and statements shall be prepared separately in respect of: (a) Linked Business; (b) Non-linked Business; and (c) Health Insurance. The abstracts shall be supported by the statements to be prepared by the insurer in the specified forms and the summary statements to be prepared in: (i) Form K; and, (ii) Form IRDA-AA, as specified by IRDA (Solvency Margin of Insurers) Regulations 2000.

Investments of Assets

Under Section 27 of the Act, every insurer shall invest and all times keep invested assets equivalent to not less than the sum of:

(a) the amount of his liabilities to the holders of life insurance policies in India on account of matured claims; and

(b) the amount required to meet the liability on policies of life insurance maturing for payment in India

Less-

(i) The amount of premium which have fallen due to the insurer on such policies but have not been paid and the days of grace for payment of which have not expired; and

(ii) Any amount due to the insurer for loans granted on and within the surrendered values of policies of life insurance maturing for payment in India issued by him.

Requirements for Approved Investments

Under Section 27A of the Act, no insurer shall invest or keep invested any part of his controlled fund otherwise than in any of the following approved investments:

(a) Approved Securities

(b) Securities of or guaranteed as to principal and interest by the Government

(c) Debentures or other securities for money issued by any municipality with the permission of State Government

(d) Debentures or other securities issued by any authority constituted by any central Act or state Act or any housing scheme approved by Central or State Government

(e) First mortgage on immovable property situated in India under any housing scheme of the insurer approved by the Authority or a State Government

(f) Debentures secured by a first charge on any immovable property, plant or equipment of any company which has paid interest in full for 5 years immediately preceding or for at least 5 out of 6-7 years immediately before issue of debentures

(g) Debentures secured by a first charge on any immovable property, plant or equipment of any company where either its book value or its market value, whichever is less, is more than three times the value of such debentures

(h) First debentures secured by a first floating charge on all in its assets of a company which paid dividends on equity shares for last 5 years or for at least 5 out of 6-7 years

(i) Preference shares of a company which has paid dividends on equity shares for last 5 years or for at least 5 out of 6-7 years.

(j) Preference shares of a company on which dividends has been paid for last 5 years or for at least 5 out of 6-7 years

(k) Shares of any company, which have been guaranteed by another company, such other company having paid dividends on its ordinary shares for last 5 years or for at least 5 out of 6-7 yrs immediately preceding

(l) Shares of any company on which dividends of not less than 4 per cent including bonus have been paid for last 7 years immediately preceding or 7 out of 8-9 years immediately preceding

(m) First mortgage on immovable property situated in India or in any country where the insurer is carrying on insurance business subject to certain conditions

(n) Immovable property situated in India or in any country where the insurer is carrying on insurance business subject to certain conditions

(o) Loans on life interests or on policies of life insurance within their surrender he has acquired values issued by him or any insurer whose business

(p) Life interests

(q) Fixed Deposits with Scheduled Banks

(r) Debentures or shares in a cooperative society registered under Indian Cooperative Societies Act, 1912

(s) Such other investments as the Authority declare by notification as approved

No insurer shall directly or indirectly invest outside India the funds of the policyholders (S.27C).

Manners and Conditions of Investments

Section 27D of the Act provides that without prejudice to anything contained in Sections 27, 27A & 27B, the Authority (IRDA) may, in the interests of the policyholders, specify, by the regulations made by it, the time, manner and other conditions of investments of assets to be held by an insurer for the purpose of the Act. The authority may give specific directions for the time, manner and conditions subject to which the funds of the policyholders shall be invested in the infrastructure and social sector as may be specified by regulations made by the Authority and such regulations shall apply uniformly to all the insurers carrying on the business of life insurance, general insurance or reinsurance in India on or after the commencement of the Insurance Regulatory and Development Act, 1999.

The Authority may, after taking into account the nature of business and to protect the interests of the policyholder, issue to an insurer the directions relating to the time, manner and other conditions of investment of assets to be held by him. The Authority has already issued a regulation called the Insurance Regulatory and Development Authority (Investment) Regulations, 2000 which has been modified in 2004. The said regulation has been discussed in brief in Chapter 7.

Assignment and Transfer of Insurance Policy

Section 38 of this Act provides that a transfer or assignment of a policy of life insurance, whether with or without consideration, may be made only by an endorsement upon the policy itself or by a separate instrument, signed in either case by the transferor or by the assignor or his duly authorized agent and attested by at least one witness, specifically setting forth the fact of assignment or transfer subject to following conditions:

- The transfer or assignment shall be complete or effective upon the execution of such endorsement. Except where the transfer or assignment is in favour of the insurer it shall not be operative or shall not confer upon the transferee or assignee or his legal representative any right to sue for the amount of such policy or the moneys secured thereby until a notice in writing of the transfer or assignment and either the said endorsement or instrument itself or a certified copy thereof have been delivered to insurer.

- Upon the receipt of above notice the insurer shall record the fact of such assignment together the date thereof and the name of the transferee or assignee. On the request of the transferee or assignee and on the payment of a fee not exceeding one rupee the insurer shall grant a written acknowledgement of the receipt of such notice.

Salient Aspects of Assignment Clause in a Life Insurance Policy

Life insurance policy is freely assignable to another party. There are two types of assignments: Absolute Assignment and Collateral Assignment. Under an absolute assignment all ownership rights in the policy are transferred to a new owner. For example, the policy owner may wish to donate a life insurance to church, charity or educational institute, which can be fulfilled through an **absolute assignment**. The new owner can then exercise the ownership rights. Under the collateral assignment the policy owner assigns a life insurance policy for a loan. In collateral assignment, only certain rights are transferred to the creditor while the remaining rights remain with the policy owner. The creditor to whom the policy is assigned can claim and receive the policy proceeds up to the extent of loan or credit. The purpose of the assignment clause is to protect the insurer from paying the proceeds twice if assignment is not duly recorded before the maturity or the benefits becomes payable. The above assignment regulations protect the insurer from such situations.

Nomination of Policyholder

Section 39 of the Act provides that while effecting the policy or at any time before the policy matures for payment, nominate the person or persons to whom the money secured by the policy shall be paid in the event of his death; Where any nominee is a minor, the policyholder shall appoint in the prescribed manner any person to receive the money of the policy at the event of death during the minority of the nominee. Policy nomination will be subject to compliance of the following requirements:

- Nomination, in order to be effective, shall be communicated to the insurer and made by an endorsement on the policy and registered by him in the records.

- Any such nomination may, at any time before the policy matures for payment, be cancelled or changed by an endorsement or a further endorsement or a will. But unless notice in writing of any such cancellation or change has been delivered to the insurer, the insurer shall not be liable for any payment under the policy, to be made bona fide by him to a nominee mentioned in the text of the policy or registered in the records of the insurer.

- The insurer shall furnish to the policy-holder a written acknowledgement of having registered a nomination or a cancellation or change thereof, and may charge a fee not exceeding one rupee for registering such cancellation or change.

- Any assignment or transfer of a policy in accordance with Section 38 of the Act, shall cancel such nomination.

- Any assignment of a policy to the insurer in consideration of a loan granted by him on the security of the policy within surrender value, or reassignment of the policy for payment of such loan shall not see cancellation.

Payment of Commission

Payment of commissions or remunerations to agents, brokers and corporate agents are subject to requirements of the Insurance Act, 1938 and the regulative directives issued by IRDA in respect of Life Insurance business and General Insurance business separately from time to time.

Life Insurance Business

Under Section 40A of the Act, no person shall pay or contract to pay an insurance agent and no insurance agent shall receive by way of commission or remuneration in any form in respect of commission or remuneration in any form in respect of **any policy of life insurance** issued in India by an insurer and effected through an insurance agent, an amount exceeding:

(a) Where the policy grants an immediate annuity or a deferred annuity in consideration of a single premium or where one premium is payable on policy, i.e. **2 per cent** of that premium.

(b) Where the policy grants a deferred annuity in consideration of more than one premium, premium, i.e. $7^1/_2$ per cent of the first premium and 2 per cent of renewal premium.

(c) In any other case 35 per cent of the first year premium and $7^1/_2$ per cent of the second and thereafter 5 per cent of each renewal premium, payable.

General Insurance Business

Under Section 40A (3) of the Act, no person shall pay or contract to pay an insurance agent and no insurance agent shall receive by way of commission or remuneration in any form in respect of commission or remuneration in any form in respect of **any policy of general insurance** issued in India by an insurer and effected through an insurance agent, an amount exceeding 15 per cent of the premium payable on the policy where the policy relates to fire or marine or miscellaneous business. However, IRDA may specify the amount or percentage of commission or remuneration for agents on premium payable on policy within the limits mentioned above. Under the new circular that IRDA has rationalized sets various scales of insurance commission with the following major changes becoming effective from 1 October, 2008:

- The overall ceiling on commission continues to be 15 per cent for agents and 17.5 per cent for brokers.
- For fire, industrial risks, and engineering covers, the cap is 10 per cent for agents and 12.5 per cent for brokers.
- For motor comprehensive cover, cap on commission is 10 per cent for both agents and brokers.
- For mega risks with large sum-insured, the commission has been capped at 6.5 per cent. Earlier, the cap was applicable to companies (insured) with a paid-up capital over Rs 20 crores if the sum-insured is small.
- To prevent insurance companies from paying more commission to agents and brokers than what the regulations permit, the regulator has banned payment of any charges to the intermediaries who bring business.

Importantly, in the highly competitive market following removal of old tariff in 2007, the private companies have cut down commission on large business, because their margins have been reduced to the minimum. The state-owned companies however have continued to pay commission on large business. It is expected that as the industry settles down in the competitive market, the brokers and the insured will start quote net rates to the insured.

Limitation of Expenses of Management

Every insurer is required limit the expenses of management within permissible limits as applicable to the life insurance business as per the provisions of the Insurance Act, 1938 discussed below.

Limitation of Expenses of Management in Life Insurance Business

Under Section 40B, every insurer transacting life insurance business in India, shall furnish to IRDA within such time as may be prescribed, statements in the prescribed from certified by an actuary on the basis of premiums currently used by him in regard to new business in respect of mortality, rate of interest, expenses and bonus loading. No insurer shall, in respect of life insurance business transacted by him in India, spend as expenses of management in any calendar year, an amount in excess of the prescribed limits and in prescribing any such limits regard shall be had to the size and age of the insurer and the provisions generally made for expenses of management in the premium rates of insurers. Where an insurer spends expenses of management in any year an amount in excess of the permissible amount, he shall not be deemed to have contravened the said statutory provisions, if the excess amount so spent, is within such limits as may be fixed in respect of the year by IRDA in consultation with the Executive Committee of the Life Insurance Council constituted under Section 64F of the Act, by which the actual expenses incurred, may exceed the expenses permissible under the statutory provision.

Limitation of Expenses of Management in General Insurance Business

Under Section 40C no insurer shall, in respect any class of general insurance business transacted by him in India, spend in any calendar year as expenses of management including commission, or remuneration for procuring business, an amount in excess of the prescribed limits and in prescribing any such limits regard shall be had to the size and age of the insurer. Where an insurer spends expenses of management in any year an amount in excess of the permissible amount, he shall not be deemed to have contravened the said statutory provisions, if the excess amount so spent, is within such limits as may be fixed in respect of the year by IRDA in consultation with the Executive Committee of the Life Insurance Council constituted under Section 64F of the Act, by which the actual expenses incurred, may exceed the expenses permissible under the statutory provision.

Every insurer as aforesaid shall incorporate in the Revenue Account a certificate signed by the chairman and two directors and by the principal officer of the insurer and by an auditor certifying that all expenses of management wherever incurred, whether directly or indirectly, in respect of the business referred to the purpose, have been fully debited in the revenue account as expenses. Expenses of management mean and include all charges, wherever incurred, whether directly or indirectly, including commission payments of all kinds and in case of the insurer having his principal place of business outside India, a proper share of head office expenses, which shall not be less than such percentage as may be prescribed, of his gross premium income written direct in India during the year without taking into account premium on reinsurance ceded or accepted.

Prohibition of Rebate

As per the provisions of Section 41 of the Act, no person shall allow or offer to allow either directly or indirectly as an inducement to any person to take out or renew or continue an insurance in respect of any kind of risk relating to lives or property in India, any rebate of the premium shown on the policy, nor any person taking out or renewing or continuing a policy, shall accept any rebate, except as may be allowed in accordance with the published prospectus or tables of the insurer.

Licensing of Insurance Agents

Section 42 of the Act provides that on payment of the fee specified by the regulations, which shall not exceed Rs 250, the authority or designated officer authorized by it in this behalf, shall, in the manner determined by the regulations, issue to any person making an application in the manner determined by the regulations, a license to act as an insurance agent for the purpose of soliciting or procuring insurance business, provided: i) in the case of individual, the applicant does not suffer from any of the disqualifications specified in Section 42(4); and ii) in case of a company or firm, any of its director or partners does not suffer from any of the aforesaid disqualifications. A license issued under the provisions of the Act shall remain force for three years from the date of issue and shall be renewed by the Authority for a period of three years on the receipt of application for renewal along with prescribed fees at least 30 days before the date the license shall cease to remain in force provided the applicant does not suffer from any of the disqualifications specified in sub-section 4 of Section 42. If the renewal application received before the date of expiry of the license but not before 30 days as mentioned above, the Authority renew the license on the compliance of the aforesaid requirement with the payment of penalty not exceeding Rs 100.

Solvency Margin

As per provisions of Section 64VB of the Act, an shall, at all times, maintain an excess of the value of his assets over the amount of liabilities of not less than the amount arrived at in accordance with provisions of this Section. On or after the commencement of the IRDA Act, 1999, every insurer shall, at all times, maintain an excess of the value of his assets over the amount of liabilities of not less than the amount arrived at as follows (hereinafter referred to in this section referred to as the **"required solvency margin"**), namely:

(i) in the case of an insurer carrying on life insurance business, the required solvency margin shall be the higher of the following amounts:

  (a) Rs 500 000 000 (while Rs 100 000 0000 in case of reinsurance) or

  (b) The aggregate of the results arrived at in calculations in item (I) and item (II) as explained in the **Note ***

(ii) In the case of an insurer carrying on general insurance business, the required solvency margin, shall be the highest of the following amounts;

(a) Rs 500 000 000 (while Rs 100 0000 000 in case of reinsurance), or

(b) A sum equivalent to 20 per cent of net premium income, or

(c) A sum equivalent to 20 per cent of net incurred claim subject to credit for reinsurance in computing net premiums and net incurred claims being actual, but a percentage, determined by the regulations, not exceeding 50 per cent.

***Note:** Aggregate of the results arrived at in calculations in item (1) and calculations in item (II) for Required Solvency Margins as stated below; (quoted from the Act)

(I) Aggregate of the results arrived at by applying the calculation described in item (A)— Step 1 and the calculation described in items (B)—Step 2;

Item (A)— Step 1

A.1) There shall be taken, a sum equal to a percentage determined by the regulations not exceeding 5 per cent of the mathematical reserves for direct business and reinsurance acceptances without any deduction for reinsurance cessions

A.2) The amount of mathematical reserves at the end of the preceding financial year after the deduction of reinsurance cessions shall be expressed as a percentage of the amount of those mathematical reserves before any such deduction; and

A.3) The sum mentioned in item (A.1) above shall be multiplied.

A.3-1) Where the percentage arrived at under item (A.1) is higher than 85 per cent (50 per cent in case of reinsurance business), by that greater percentage; and

A.3-2) in any other case, by 85 per cent or 50 per cent in case of reinsurance business)

Item (A)— Step 1;

B.1) There shall be taken, a sum equal to a percentage determined by the regulations not exceeding 1 per cent the sum at risk for the policies on which the sum at risk is not a negative figure; and

B.2) The amount of sum at risk at the end of the preceding financial year for which the sum at risks is not negative after deduction of reinsurance cessions shall be expressed as a percentage of the amount of that sum at risk before any such deduction

B.3) The sum mentioned in item (A.1) above shall be multiplied—

B.3-1) Where the percentage arrived at under item (B.1) is higher than 50 per cent by that greater percentage; and

B.3-2) in any other case, by 50 per cent

(II) A percentage determined by the regulations made by the Authority of the value of assets determined in accordance with provisions of Section 64V;

Note: There is a specific regulation detailing the method for calculation of Solvency Margins for life insurance business and non-life insurance business, which have been discussed separately in Chapter 7.

5

MARINE INSURANCE MANUAL– LEGAL & TECHNICAL ASPECTS

Marine Insurance: An Overview

Marine insurance is the oldest of all the classes of insurance in existence in the world and it has occupied a very important place in the domestic and international trade of every country. History says marine insurance was practiced in Italy in the 12th Century. The Lloyd's Foundation of London adopted the practice in England in the 17th century. Major international insurance markets exist in the UK, US, Italy, Japan and Germany. The UK marine insurance market has had its center in London and the London Market includes Lloyds, Major British insurance companies, agencies and branches of foreign companies, underwriting agency companies on behalf of member companies and many mutual associations. Most of the countries have developed marine insurance markets according to their needs, facility, and capacities following the practices and guidelines adopted by Lloyds Underwriters. Marine insurance policy is very important considerations for the bankers involved in financing for international trade. As the marine insurance is international in practice, complex in character and subject to country's regulatory norms, underwriters, surveyors and insurance intermediaries must have adequate knowledge about marine insurance principles, practice, laws, rules and regulations. In India today marine insurance that includes marine cargo insurance and marine hull insurance contributes about 20 per cent of gross non-life insurance premium income. Marine cargo insurance was de-tariffed in 1994. At present, both marine cargo insurance and marine hull insurance are free from tariff.

Marine Insurance and Legal Aspects

Marine insurance business is mostly international and therefore subject to international laws and regulations though it is fundamentally governed by the oldest insurance law called the Marine Insurance Act, 1906 subsequently amended as the Marine Insurance Act, 1963 in India. It is guided by the various clauses formulated by the Institute of London Underwriters (ILU) and the International Commercial Terms now known as Incoterm 2000 developed by International Chamber of Commerce (ICC). Precisely in India marine insurance is subject to the following statutes and international regulations for import and export insurance and hulls insurance:

Statutes Governing Marine Insurance

- The Insurance Act 1938 with Insurance Rules 1939
- The Marine Insurance Act, 1963
- The Stamp Act 1899
- The Foreign Exchange Management Act
- Rules and laws relating to carriage or recovery.
- The Multimodal Transportation of Goods Act 1993 with UNCTAD/ICC Rules for Multimodal Transportation Documents
- The Indian Carriage of Goods by Sea Act, 1925 (as amended)
- The Indian Railways Act 1989
- The Carriers Act, 1865
- Indian Carriage of Goods by Air Act, 1943 and Warsaw Convention of 1929
- Indian Post office Act, 1898
- Major Port Trust Act, 1963

- Indian Port Trust Act, 1908
- Customs Act, 1962

International Rules and Regulations Governing Marine Insurance

- ICC Regulation Incoterm 2000
- The Hague Rules 1924
- The Hague –Visby Rules 1968
- The Hamburge Rules
- Institute Clauses of ILU for import /export insurance
- Institute Cargo Clauses (A), (B), and (C)
- Institute War Clauses (CARGO)
- Institute Strikes Clauses (CARGO)
- Institute Cargo Clauses (AIR)
- Institute War Clauses (AIR CARGO)
- Institute Strike Clauses (AIR CARGO)
- Institute Clauses for Hull Insurance
- Institute Time Clauses (ITC)- Hulls (1.10.83)
- Institute Voyage Clauses–Hulls (1.10.83)
- Institute Fishing Vessel Clauses

Fundamentals of Marine Insurance Contract

A contract of marine insurance is an agreement whereby the insurer undertakes to indemnify the assured, in the manner and to the extent thereby agreed, against marine losses, i.e. the losses incidental to marine adventure. Under Section 4 of the Marine Insurance Act, 1963 a contract of marine insurance protects the assured against transit losses on inland waters or on any land risk, which may be incidental to any sea voyage. Where a ship in course of building, or the launch of a ship, or any adventure analogous to a marine adventure, is covered by a policy in the form of a marine policy, marine adventure shall mean also such subject matter except as by this section provided, nothing in this Act shall alter or affect any rule of law applicable to any contract of insurance other than a contract of marine insurance as by this Act defined. A marine adventure includes an adventure where any ship, goods or other movables are exposed to perils incidental to local or inland transit. Under Section 5 of the Act every lawful marine adventure may be the subject of a contract of marine insurance subject to the provisions of this Act. As per Section 6 marine insurance contract by way of wagering is unlawful and void *ab initio*. The fundamental aspects of marine insurance contract are discussed below with certain examples.

Contract of Indemnity

The contract of marine insurance is a *contract of indemnity, which* protects against physical and other losses to moveable property and associated interests, as well as against liabilities occurring or arising during the course of a sea voyage. A contract of marine insurance is a contract whereby the insurer undertakes to *indemnify* the assured, in a manner and to the extent thereby agreed, against losses from incident to marine adventure. *Contract of indemnity* is a basic principle of the law of insurance. Common law and civil law definitions are similar in this regard. Section 3 of the Marine Insurance Act provides that a contract of marine insurance is an agreement whereby the insurer undertakes to indemnify the assured, in the manner and to the extent thereby agreed, against marine losses, that is to say, the losses incidental to marine adventure.

Contract on Utmost Good Faith

As per Section 19 a contract of marine insurance is a contract based upon the utmost good faith and if the utmost good faith, and if the utmost good faith be not observed by either party, the contract may be avoided by the other party. Under Section 20 the assured must disclose to the insurer, before the contract is concluded, every material circumstance which, is known to the assured, and the assured is deemed to know every circumstance. Under Section 21 the agent must disclose to the insurer every material circumstance which is known to himself, and an agent to insure is deemed to know every circumstance where an insurance is affected for the assured by an agent. Very importantly the duty of disclosure continues to apply even after the conclusion of the contract as decided in the case *Shipping Co. Ltd. vs. Uni-Polaris Insurance Co. Ltd. and La Réunion Européene (The Star Sea)2001.*

Contract for Insurable Interest

Section 6 of the Marine Act provides that every contract of marine insurance by way of wagering is void. A contract of marine insurance is deemed to be a wagering contract, where the assured has not an insurable interest as defined by this Act, and the contract is entered into with no expectation of acquiring such an interest. As per Section 7, which provides insurable interest, every person who is interested in a marine adventure has an insurable interest. It further provides that a person is interested in a marine adventure where he stands in any legal or equitable relation to the adventure or to any insurable property at risk therein, in consequence of which he may benefit by the safety or due arrival of the property, or may be prejudiced by its loss, or by damage thereto, or by the detention thereof, or may incur liability in respect thereof. Under Section 11 of this Act the insurer under a contract of marine insurance has an insurable interest in the risk underwritten and accepted by him, and may reinsure it with that insurable interest. Unless the policy otherwise provides, the original assured has no right or interest in respect of such reinsurance. Following are a few examples of application of insurable interests in marine insurance management:

- Where the buyer of goods has insured them, he has an insurable interest, notwithstanding that he might, at his election, have rejected the goods, or have treated them as at the seller's risk, by reason of the latter's delay in making delivery or otherwise (Section 9)

- The lender of money on bottomry has insurable interest in respect of loan (Section 12)

- The master or a crewmember of a ship has an insurable interest for his wages (Section 13)

- In the case of advance freight, the person advancing the freight has an insurable interest, in so far as such freight is not repayable in case of loss (Section 14)

- The assured has an insurable interest in insurance premium (Section 15)

The principal features of insurable interests in marine insurance are explained in sections 6 to 17 of the Marine Insurance Act, 1963.

Quantum of Insurable Interest

Section 16 describing quantum of insurable interests and Section 17 describing assignment of insurable interests need to be elaborated.

Section 16 of the Marine Insurance Act provides for determination of quantum of insurable interests in the following manner:

- Where the subject-matter insured is mortgaged, the mortgagor has an insurable interest in the full value thereof, and the mortgagee has an insurable interest in respect of any sum due or to become due under the mortgage.

- A mortgagee, consignee, or other person having an interest in the subject-matter insured may insure on behalf and for the benefit of other persons interested as well as for his own benefit.

- The owner of insurable property has an insurable interest in respect of the full value thereof, notwithstanding that some third person may have agreed, or be liable to indemnify him in case of loss.

Thus the quantum of the insurable interests is determined for various cases in various manners as provided in this Act.

Assignment of Insurable Interest

Assignment is the act of transferring the beneficial interest in a policy to another party. A marine policy is freely assignable unless assignment is expressly prohibited. A marine cargo policy may be assigned either before or after loss. The assignment may be effected either by endorsement or by other customary manner, but not by mere delivery. Section 17 of the Marine Insurance Act, 1963 provides that where the assured assigns or otherwise parts with his interest in the subject matter insured, he does not thereby transfer to the assignee his rights under the contract of insurance, unless there be an express or implied agreement with the assignee to that effect. A policy of marine insurance is not an incident of sale. Therefore for assignment of a marine policy, there must be an agreement to this effect, either written or understood before the interests pass. If this agreement exists, the policy can be assigned either before or after the assured has parted with his interest in the subject matter insured.

Section 53 provides that assured who has no insurable interest cannot assign. It further describes that where the assured has parted with or lost his interest in the subject-matter insured, and has not, before or at the time of so doing expressly or impliedly agreed to assign the policy, any subsequent assignment of the policy will be inoperative; provided that nothing in this section affects the assignment of a policy after loss. For the following marine insurance policies assignment is expressly prohibited:

- Duty Insurance Policy
- Increased Value Insurance Policy
- Special Declaration policies
- Annual Policies
- Sellers' Interests Contingency Policy
- Special Storage Risks Insurance policy

Measure of Insurable Value

One of the major problems an insurer or a surveyor generally faces is determination of insurable value of the subject matter of marine insurance. To sort out the problem he is required to refer the provisions of the Marine Insurance Act over and above technical aspects contained in the marine policy. Section 18 provides that "*Subject to any express provision or valuation in the policy, the insurable value of the subject-matter insured must be ascertained as follows:*

(1) In insurance on **ship**, the insurable value is the value, at the commencement of the risk, of the ship, including her outfit, provisions, and stores for the officers and crew, money advanced for seamen's wages, and other disbursements (if any) incurred to make the ship fit for the voyage or adventure contemplated by the policy, plus the charges of insurance upon the whole:

    The insurable value, in the case of a **steamship**, includes also the machinery, boilers, and coals and engine stores if owned by the assured; in the case of a ship driven by power other than steam includes also the machinery and fuels and engine stores, if owned by the assured; and in the case of a ship engaged in a special trade, includes also the ordinary fittings requisite for that trade"

(2) In insurance on **freight**, whether paid in advance or otherwise,

the insurable value is the gross amount of the freight at the risk of the assured, plus the charges of insurance:

(3) In insurance on **goods or merchandise**, the insurable value is the prime cost of the property insured, plus the expenses of and incidental to shipping and the charges of insurance upon the whole:

(4) In insurance on **any other subject-matter,** the insurable value is the amount at the risk of the assured when the policy attaches, plus the charges of insurance".

The Marine Insurance Act provides clearly the detailed legal provisions in regard to measure of insurable value of all kinds of subject matter of insurance, which the insurer, intermediary or surveyor may refer to for the purpose of underwriting at the time of acceptance of risks or at the time of settlement of claims as the case may be.

Technical Aspects of Marine Insurance: Policy Terms & Conditions

Standard Form of Marine Cargo Insurance Policy

The standard form of cargo policy is known as MAR Policy form containing the name of the insurer, a clause binding the insurer to the performance of the contract and the schedule specifying the certain details mentioned below. As per Section 24 of the Marine Insurance Act, 1963 a contract of marine insurance shall not be admitted in evidence unless it is embodied in a marine policy in accordance with this Act. The policy may be executed and issued either at the time when contract is concluded or afterwards. The standard form of marine policy contains a schedule specifying the following details:

- Name or names of the insurer
- Policy Number, place and date of issue
- Name of the assured with address

- Place, period and mode of transit and the commencement of transit
- Where a bank finances the transaction, the name of the bank will also appear
- Subject-matter insured and the risk insured against
- Types of Insurance Covers/ Clauses (A, B or C)
- Voyage, or period of time, or both, as the case may be, covered by the insurance
- The sum-insured
- Name of the vessel carrying cargo.(subject to Institute Classification Clause)
- Description of marks/ numbers appearing on packages, BL/ RR/Consignment note
- A policy must be signed by or on behalf of the insurer
- The subject matter must be designated in the policy with reasonable certainty
- The nature and extent of the interest of the assured in the subject-matter insured
- Designation of the subject matter insured in general terms; and interest covered
- Clause attached with a policy; ICC (A), ICC (B) or ICC(C) for sea voyage or
- Clause Inland Transit Clauses (I T C)-A, B & C for inland transits
- Shipments from named starting point to named destination

Valued vs. Unvalued Policies

Marine policy may be either valued or unvalued. Under Section 29 of the Marine Insurance Act, a valued policy is a policy, which specifies the agreed value of the subject-matter insured. Subject to the provisions of this Act, and in the absence of fraud, the value fixed by the policy is, as between the insurer and assured, conclusive of the insurable value of the subject-matter insured, whether the loss is total or partial. Unless the policy otherwise provides, the value fixed by the policy is not conclusive for the purpose of determining whether there has been a constructive total loss. Under Section 30 of the Marine Insurance Act, an unvalued policy is a policy, which does not specify the value of the subject-matter insured, but subject to the limit of the sum insured, leaves the insurable value to be subsequently ascertained.

Open Covers

Large trading concerns rendering consignments especially import and export on regular basis may not find it convenient to cover their all consignments by separate specific policies for each and every shipment. For large number of shipments/consignments specific and separate policies for every consignment is not only costly but also time-consuming and inconvenient both to the insurer and the insured from administrative point. To avoid such inconvenience and unnecessary administrative costs, open covers are arranged for such type of insurance. The open cover provides automatic and continuous protection to a regular exporter/importer engaged in international trade on submission of declaration for each and every shipment. An open cover actually is not a policy but an agreement binding on both insurer and insured to cover all shipments to be declared by the insured as per the specific terms and conditions. Premium is payable on each declaration against which specific stamp certificate is issued covering each consignment declared. There is no sum insured in open cover. There are basically two limits, i.e. (a) per bottom limit; and (b) per location limit. Generally, open covers are issued for a period of 12 months for shipments in a mechanically self-propelled vessel of steel construction as per Institute Classification Clause subject to compliance of the following requirements:

- **Sum-insured and Basis of valuation**: CIF plus 10 per cent

- **Declaration**: The assured is bound to declare each and every shipment individually or in batches and obtain a certificate of insurance for individual or group of shipments as per arrangement.

- **Certificate of Insurance:** The Certificate issued against declarations will bear stamp duty and show premium, both of which will be collected from the assured or be adjusted against the cash deposit.

- **Loss Prior to Declaration**: In the event of loss prior to declaration and/or shipment on board the vessel, the basis of valuation shall be the prime cost of the goods.

- **Limit per Bottom**: Limit of aggregate value of shipments/ consignments per vessel or other conveyance at any one time.

- **Limit per Location**: The location clause seeks to limit the value of pre-shipment accumulation, which may take place due to some unexpected causes such as strikes, labour disturbances in the port. Such accumulation of cargo in a particular location may create a catastrophic exposures in the event of occurrence of some perils like storm, riot, etc.

- **Inspection of Records**: The insurer has the privilege at any time during business hours to inspect the records of the assured in respect of the shipments coming within the terms of the open cover.

- **Under Deck**: Subject o warranty as to under-deck or on-deck shipment. Generally arrangement is made for shipment under deck while on deck shipment on special rats and terms to be separately agreed upon.

- **Cancellation**: Either party giving 30 days notice in writing may cancel open cover, provided the risk has not already attached. However War & SR & CC risks for shipments other than to or from US are subject to cancellation by 7 days' notice and War & SR & CC risks for shipments to US are subject to cancellation by 48 hours notice.

- **Insuring Clauses**: Subject to Institute Cargo clauses (A), Institute War Clauses (Cargo) and Institute Strikes Clauses (cargo) attached with open cover.

Open Policies

An open policy is a kind of floating policy, which is defined in Section 31 of the Marine Insurance Act. Consignors or clients having substantial turnover and good number of dispatches may obtain continuous insurance cover under open policy. This type of policy is generally issued for insurance of goods dispatched within the country by rail/road/air freight or registered post with Inland Transit Clause-ITC.A/B/C. The cover under open policy issued for a period of 12 months ceases on exhaustion of the sun-insured if the SI is not increased before expiry of 12 months by extra endorsement with payment of additional premium. Open Policy is issued on standard form with specific conditions of the similar nature, as discussed in the open cover. Premium is worked out and charged on the total sum insured of the open policy and paid in advance unlike open cover. Declaration must be submitted as per condition of the policy. Section 31 of the Marine Insurance Act provides that the declarations must be made in order of dispatch. They must cover all consignments to be covered under the terms of the open policy and the value of the goods must be fully stated.

Certificate of Insurance

Certificates of insurance are issued against open covers or open policies, as applicable and are subject to the terms and conditions of such open cover or open policies. Details contained in the certificates are same as those contained in the policy documents. They are:

(a) Certificate number, place and date of issue

(b) Open cover/Open policy number

(c) Name and address of the insured

(d) Description of goods, number of packages & nature of packing

(e) Voyage/ transit details along with the transshipments, if any

(f) Consignment Value

(g) Remaining value of sum-insured in case of open policy

(h) Premium and stamp duty

- Certificates issued against open cover are to be stamped

- Certificate issued against open policy is not to be stamped

(i) Terms and conditions of insurance as per the open cover or policy

(j) Sum-insured

In case of certificates issued against open policies, it will mention the remaining balance of the sum insured under the policy so that the client can take the timely action to have the sum insured increased suitably with the payment of additional premium during the currency of the open policy.

Special Declaration Policy

A special Declaration Policy (SDP) is a form of floating policy issued to clients who have a large turnover with many and different dispatches of goods anywhere within the country by rail or road or inland waterways. Special features of this policy are:

- Annual Estimated Dispatches including inter-depot movement must be substantial. Presently insurers mostly fix it for Rs 2 crore minimum.

- SDP is not issued to transport contractors/operators, cleaning or forwarding and commission agents or freight forwarders, either in their own name or jointly with the cargo-owners.

- This policy will not be issued in joint names; even not in the joint names of the companies under same management or with relation as holding/subsidiary company.

- The SDP is not assignable though the claim, if arises may be settled in favour of the consignee at the request of the assured.

- The duly completed proposal forms the basis and part of policy.

- The sum insured shall be on the basis of the previous years' turnover. In case of fresh proposal SI shall be the fair estimate of annual dispatches. If the estimated annual turnover found to be inadequate due to increase in the insured's turnover, SI may be increased once to any extent during currency of the policy on payment of additional premium. The SI of next renewal must be not less than the increased SI.

- If SI of SDP is exhausted before completion of 12 months, the insurers may issue an Open Policy, which will not carry any discount.

- For next renewal SI will be not less than the total of SI of last SDP.

- Basis of valuation shall be maximum CIF plus 10 per cent.

- Annual turnover means total value of all incoming and outgoing dispatches of raw materials, finished/ semi-finished goods, stores, capital goods or inter-depot transfers.

- Discounts on SDP are generally: (a) Turnover Discount; and (b) Good-feature Discount. According to their claim experiences different insurance underwriters allow such discounts at different rates. Generally total discounts do not exceed 60 per cent of guide rate.

- Again if Claim Ratio exceeds 60 per cent for last 3 years, rate may be enhanced in order to keep the loss ratio 60 per cent. For example, if the average claim ratio is 72 per cent, rate may be increased by 20 per cent as calculated here 72/60*100 =120 per cent. Current Rate will be 120 per cent of the earlier rate with increases 20 per cent.

Marine Cargo Clauses

The scope, cover, extent, exclusions, duration and conditions are mentioned in the applicable clauses attached to the policies. Clauses used are basically of two types: a) Institute Clauses for Overseas (Import & export) Insurance; and b) Inland Clauses. The Technical and Clauses committee of The Institute of London Underwriters (ILU) makes, revises and amends the Institute clauses. They are accepted for use in the overseas marine insurance policies by all insurers world over to maintain the uniformity and standards in the international character of marine insurance business. At present the number of Institute Clauses is many. The ILU has come out with standard sets of clauses for various types of insurance contract. Here we will examine the salient features of the principal Institute Cargo Clauses (A), (B) & (C) also called ICC 'A', ICC 'B' & ICC 'C'.

Provisions in ICC 'A', 'B' & 'C'

The cargo clauses are grouped under following 19 sub-clauses:

1. Risk Clause
2. General Average Clause
3. Both to Blame collision" Clause
4. General Exclusions Clause
5. Un-seaworthiness and Unfitness Exclusion Clause

6. War Exclusion Clause
7. Strikes Exclusion Clause
8. Duration
9. Termination of Contract of Carriage Clause
10. Change of Voyage Clause
11. Insurable Interest Clause
12. Forwarding Charges Clause
13. Constructive Total Loss Clause
14. Increased Value Clause
15. Not to Inure Clause
16. Minimizing losses (Duty of the Assured Clause)
17. Waiver Clause
18. Avoidance of delay (Reasonable Dispatch Clause)
19. English Law and practice Clause

The risk clause is different in each of the three clauses. There is some difference in general exclusion clause also.

Risks Covered in ICC (A)

ICC-A covers all risks subject to specified exclusions. It is the widest cover provided loss/damage occurred fortuitously. Onus of proof that loss caused by an excluded peril lies on the insurer.

Risks Covered in ICC (B)

ICC (B) covers the following risks:

- Fire & Explosion

- Vessel being stranded, grounded, sunk or capsized
- Overturning or derailment of land vehicle
- Collision of vessel, craft, conveyance with external object
- Discharge of cargo at a port of distress
- Earthquake, Lightening
- General average sacrifice
- Jettison
- Washing over board
- Entry of sea, lake or river water
- Total loss of any package lost over board or dropped while loading or unloading

Extension in ICC (B)

By charging extra premium, covers under ICC 'B' and 'C' can be extended to cover:

- Malicious damage
- TPND
- Fresh /Rain water damage
- Damage by hooks, oil, mud other extraneous substance
- Heating/sweating
- Leakage/contamination
- Breakage

Risks Covered in ICC (C)

It covers risks 1 to 8, out of 11 risks that are covered by ICC (B).

Extension in ICC(C)

Basic cover can be extended to cover all additional perils as mentioned in 5.14.3 for extension in ICC (B).

Exclusions in ICC (A), (B) & (C)

Total exclusions in the policy have been shown separately under the following four sub-clauses in all three-cargo clauses:

- General Exclusions Clause 4
- Un-seaworthiness and Unfitness Exclusion Clause 5
- War Exclusions Clause 6
- Strike Exclusions Clause 7

General Exclusions Clause 4

- Willful misconduct
- Ordinary leakage or breakage
- Insufficiency or unsuitability of packing.
- Loss due to inherent vice
- Loss or damage by Delay (even delay by insured peril)
- Loss due to insolvency or financial default of ship owner
- Loss due to use of any weapon of atomic war

Table-1 Comparison of ICC (A), (B), & (C) At a Glance

Type of Risks				
Covered (C); Not Covered (×)		**ICC-A**	**ICC-B**	**ICC-C**
	Loss / damage caused by / attributable to:			
1	Fire or Explosion	C	C	C
2	Vessel/Craft being stranded, grounded sunk/capsized	C	C	C
3	Overturning / derailment of land conveyance	C	C	C
4	Collision or contract of vessel, craft or conveyance with any external object other than water	C	C	C
5	Discharge of cargo at a port of distress	C	C	C
6	Earthquake, Volcanic eruption, Lightning	C	C	×
7	General average and salvage charges incurred to avoid loss from any cause except those excluded	C	C	C
8	General average sacrifice	C	C	C
9	Jettison	C	C	C
10	Washing overboard	C	C	×
11	Entry of sea, lake or river water into vessel, craft, hold, conveyance, container, lift van or place of storage.	C	C	×
12	Rainwater damage (FWD)	C	×	×
13	Total loss of any package lost over-board or dropped whilst loading or unloading from vessel or craft.	C	C	×
14	Piracy	C	×	×

15	Deliberate damage or destruction by wrongful act of any person or persons, (i.e. by malicious acts)	C	×	×
16	In the event of frustration of the voyage resulting from a risk covered, extra charges incurred in unloading, storing and forwarding to destination	C	C	C
17	Reasonable charges for averting or minimizing loss recoverable under this insurance and also those incurred with recovery rights against carriers, bailees.	C	C	C
18	Other or extraneous perils all involving a fortuity and from external causes, for example:	C	×	×
	Improper Storage	C	×	×
	Damage as a result of shifting in heavy weather	C	×	×
	Rough handling	C	×	×
	Breakage, leakage, denting, scratching, crushing, etc	C	×	×
	Heating, sweating	C	×	×
	Infestation, mould, mildew, rust, country damage	C	×	×
	Hook and sling damage	C	×	×
	Contact with mud, oil,& acids, damage by other cargo	C	×	×
	Shortage, theft, pilferage, non–delivery	C	×	×
	Other loss /damage, caused fortuitously and externally	C	×	×
19	Liability under “Both to blame collision” clause	C	C	C

Additional Cover for War, & Strike Perils

Marine All Risks Insurance as per ICC (A) does not cover war and strike risks as per the following provisions of the said clause. The War Exclusion Clause in ICC (A) provides that in no case this insurance cover loss, damage or expenses caused by:

- War, civil war, revolution, rebellion, insurrection or civil strife arising therefrom or any hostile act by or against a belligerent power;

- Capture, seizure, arrest restraint or detainment (piracy excepted) and the consequences thereof or any attempt thereat; and

- Derelict mines torpedoes bombs or other derelict weapons of war

The Strike Exclusion Clause in ICC (A) provides that in no case, this insurance will cover loss, damage, or expenses:

1. Caused by strikes, locked-out workmen, or persons taking part in labour disturbances, riots or civil commotion;

2. Resulting from strikes, lock-outs, labour disturbance, riots or civil commotions; and

3. Caused by any terrorist or any person acting from a political motive.

Thus cover granted under Institute Cargo Clauses (A), (B) & (C) specifically excludes loss, damage, or expense caused by war and strike risks. However War and strike risks can be covered upon payment of additional premium and attaching the relevant clauses to the policy. On payment of additional premium and after risks analysis underwriters may agree for inclusion of these risks in the policy to protect the assured's interests against political and social disturbances with two separate clauses named a) Institute War Clauses (Cargo) and b) Institute Strikes Clauses (Cargo).

Institute War Clauses (Cargo)

The War Risks Rating Committee, Institute London Underwriters, (ILU) issues and reviews this clause. This insurance covers loss or damages to the subject matter insured caused by:

- War, Civil War, revolution, rebellion, insurrection or civil strife arising therefrom or any hostile act by or against a belligerent power ;
- Capture, seizure, arrest restraint or detainment (piracy excepted) and the consequences thereof or any attempt thereat;
- Derelict mines torpedoes bombs or other derelict weapons of war'
- It also covers the following loss;
- General Average and Salvage Charges incurred to avoid a loss from a risk covered; and
- Charges reasonably and property incurred to avert or minimize an insured loss and to preserve and pursue recovery rights.

Institute Strike Clauses (Cargo)

This insurance covers loss or damages to the subject matter insured caused by:

- Strikes, locked-out workmen, or persons taking part in labor disturbances, riots or civil commotion; and
- Any terrorist or any person acting from a political motive.

It also covers the following loss:

- General Average & Salvage Charges incurred to avoid a loss from a risk covered; and

- Charges reasonably and property incurred to avert or minimize an insured loss and to preserve and pursue recovery rights.

This cover does not cover:

- Loss, damage or expense caused by war, civil war, revolution or strike arising; and

- Loss, damage, or expense proximately caused by delay, inherent vice or nature of the subject matter insured.

Exclusions to War and Strike Cover under with above Clauses

The exclusions are the same as under ICC (A), (B) & (C) clauses with following additional exclusions:

- Any claim based on loss from frustration of voyage or adventure (example; when the goods are prevented from reaching their destination by reason of operation of war risks, a constructive total loss may occur, although the goods are not lost or damaged in any way); and

- Loss, damage or expenses arising from absence, shortage or withholding of labour resulting from strike, lock-out, labour disturbances, riot or civil commotion (under Strike Clause).

Both to Blame Collision Clause

This is the third sub-clause in the ICC (A), (B), and (C) to indemnify the assured against such proportion of liability under the under contract of affrightment relating to '**Both to Blame Collision' Clause** in respect of a loss recoverable under the policy. Cargo owners are liable as per bills of lading to indemnify the ship owner for any amount, which the carrying vessel has to pay to the other vessel involved in collision.

Duration of Cover in – ICC- A, B & C

Duration of cover is determined by Duration …**Clause 8** (For ICC-A, B & C) as quoted below from the clause itself:

1. This insurance attaches from the time the goods leave the warehouse or place of storage at the place named herein for the commencement of the transit, continues during the ordinary course of transit and terminates either.

- on delivery to the Consignees' or other final warehouse or place of storage at the destination named herein;

- on delivery to any other warehouse or place of storage, whether prior to or at the destination name herein, which the Assured elect to use either;

  o for storage other than in the ordinary course of transit or

  o for allocation or distribution, or

- on the expiry of 60 days after completion of discharge over side of the goods hereby insured from the overseas vessel at the final port of discharge, whichever shall occur first;

2. If, after discharge over side from vessel at the final port of discharge, but prior to termination of ins. the goods are to be forwarded to a destination other than that to which they are insured, the insurance, remaining subject to termination as provided above, shall not extend beyond commencement of transit to such other destination.

Loss recoverable under ICC (A), (B) & (C)

- Particular Average – Partial loss to the cargo by insured peril

- General Average sacrifice

- Actual total loss

- Constructive total loss
- Experts incurred by the assured
  - Extra charges
  - Sue and labour charge
  - Forwarding expenses
  - General average / Salvage contribution
  - Liability BTBC

Losses mentioned above are clearly defined by the Marine Insurance Act, 1963 as explained earlier. Precisely Marine cargo claims cover both Marine Losses and Charges.

Marine Losses are broadly divided into two types: Total Loss and Partial Losses. Total Losses are of basically two types: Actual Total Loss and Constructive Total Loss, which have been defined and described by Section 57, 58 and 60 of the Marine Insurance Act. Similarly, Partial Losses are divided into broad groups: Particular Average and General Average. Particular Average comprises loss due to Short Delivery, Shortage, Partial total, Loss of Packages, Damages being Depreciation, Repair Sympathetic and Sentimental. **Charges** admissible in marine claims over and above the loss and damage to the ship or cargo are: i) Loss Prevention Charges and ii) Extra Charges. Loss prevention charges include Particular Charges, Sue & Labour Charges and Salvage Charges. The Extra Charges include Survey Fees, Auction Charges, Sale Charges, and Warehousing Charges, Loading/unloading charges or port expenses

Partial Loss and Total Loss

Section 56 provides that a loss may be either total or partial. Total loss may be either an actual total loss or a constructive total loss. Section 57 provides that where the subject-matter insured is destroyed, or so damaged as to cease to be a thing of the kind insured, or where the assured is irretrievably deprived thereof, there is an actual total loss and in the case of an actual total loss no notice of abandonment need be given.

Constructive Total Loss (Section 60)

There is a constructive total loss: a) where the subject-matter insured is reasonably abandoned on account of its actual total loss appearing to be unavoidable; or b) because it could not be preserved from actual total loss without an expenditure which would exceed its value when the expenditure had been incurred.

Constructive Total Loss Arises

Where the assured is deprived of the possession of his ship or goods by a peril insured against: (a) it is unlikely that he can recover the ship or goods, as the case may be; or (b) the cost of recovering the ship or goods, as the case may be, would exceed their value when recovered. In the case of damage to a ship, where she is so damaged by a peril insured against that the cost of repairing would exceed the value of the ship when repaired. In estimating the cost of repairs, no deduction is to be made against general average contributions to those repairs payable by other interests, but account is to be taken of the expense of future salvage operations and of any future general average contributions to which the ship would be liable if repaired. In the case of damage to goods, the cost of repairing the damage and forwarding the goods to their destination would exceed their value on arrival. Where there is a constructive total loss the assured may either treat the loss as a partial loss or abandon the subject matter to the insurer and treat the loss as if it were an actual total loss (Section 61).

General Average (Section 66)

As per Section 66 (1) *a General Average (GA) loss is a loss that arises from a general average act, general average expenditure or GA sacrifice*. It further provides that:

"…2) There is a general average act where any extraordinary sacrifice or expenditure is voluntarily and reasonably made or

incurred in time of peril for the purpose of preserving the property imperiled in the common adventure.

(3) Where there is a general average loss, the party on whom it falls is entitled, subject to the conditions imposed by maritime law, to a ratable contribution from the other parties interested, and such contribution is called a general average contribution.

(4) Subject to any express provision in the policy, where the assured has incurred a general average of expenditure, he may recover from the insurer in respect of the proportion of the loss which falls upon him; and in the case of a general average sacrifice, he may recover from the insurer in respect of the whole loss without having enforced his right of contribution from the other parties liable to contribute.

(5) Subject to any express provision in the policy, where the assured has paid, or is liable to pay, a general average contribution in respect of the interest insured, he may recover therefore from the insurer.

(6) In the absence of express stipulation, the insurer is not liable for any general average loss or contribution where the loss was not incurred for the purpose of avoiding, or in connection with the avoidance of a peril insured against.

(7) Where ship, freight, and cargo, or any two of those interests, are owned by the same assured, the liability of the insurer in respect of general average losses or contributions to be determined as if those interests were owned by different persons."

Trade Clauses & Warranties

Institute cargo clauses (A) (B) & (C) take care of the requirement of General Cargo. There are a number of commodities and foodstuffs which require special clauses provide special treatment for particular hazards of the subject matter and the uses of the trade concerned. Accordingly, ILU has devised (in consultation with trade association) standard clauses to cater to the specific needs of such interest.

Institute Commodity Trade Clauses

- Applicable to:
  - Cocoa, coffee, cotton, fats and oil not in bulk, hides and skins, leather, metals, oilseeds, sugar and tea
- The sets of clauses are:
  - Institute Commodity Trades Clauses (A), (B), (C)
  - Institute War Clauses (Commodity Trades)
  - Institute Strikes Clauses (Commodity Trades)

Institute Commodity Trade Clauses

Same as ICC A, B, and C except:

- Exclusion relating to insolvency of ship owner modified to operate only if assured was aware or should be aware
- Exclusion relating to unfitness of vessel, craft etc. modified to operate only if loading done prior to attachment of this insurance. Also privity of servant to unfitness/un-seaworthiness removed

Other Commodity Clauses

These clauses are used for special types of commodities according to their nature, composition, risk-profile, duration etc. Following are a few important clauses in this regard:

- Institute Jute Clauses
- Institute Natural Rubber Clauses
- Institute Bulk Oil Clauses
- Institute Coal Clauses

- Institute Timber Trade Federation Clauses
- Institute FOFSA Trade Clauses
- Institute Frozen Food Clauses
- Institute Frozen Meat Clauses

The special features of a few of the above clauses are briefly mentioned below.

Institute Jute Clauses

This clause is similar to Institute Commodity. Trades Clauses (B) with following main differences:

- Earthquake, volcanic eruption and lightning are not covered.
- The cover attaches only when jute is loaded on board the vessel. The time limit of 60 days after discharge at the destination port is reduced to 30 days in Jute Clauses.
- In the Termination of Contract of Carriage Clause, the time limit is reduced from 60 days to 15 days only.

Institute Coal Clauses

These clauses cover named perils similar to ICC (B) with an important difference such as the coal clauses extend the fire and explosion cover to include heating even when caused by spontaneous combustion and inherent vice of the subject matter of insurance.

Institute Bulk Oil Clauses

With most of the major risks that are covered under ICC (B), the Bulk Oil Clauses also cover leakage of oil from connecting pipelines in loading, transshipment or discharge and also loss or contamination of oil caused by negligence of master, officer and crew in pumping cargo, ballast of fuel. Loss due to contamination due to pressure of weather is also covered.

Sailing Vessels Clause for Cargo Carried in Selling Vessels

This clause governs the insurance provision for all cargo carried by sailing vessels which include country crafts both mechanized and non-mechanized. Three types of covers or clauses are available as Clause 'A', Clause 'B' and Clause 'C.

Clause 'A'

It covers total loss or constructive total loss of cargo due to Total loss or CTL of the vessel only.

Clause 'B'

It covers loss/damage to cargo due to:

- vessel being burnt / sunk
- jettison because of bad weather

Clause 'C'

It covers loss/damage to cargo due to:

- Risks covered by Clause 'B'
- Loss due to vessel being stranded
- Loss due to jettison due to stranding, sinking, burning, collision at sea

Coverage and Duration

The insurance cover starts from the time the cargo is loaded, continues during the course of voyage and ceases on landing of the cargo at the final port of discharge or 8 days after arrival of the vessel at destination, whichever occurs first. In the event of termination of adventures at an intermediate port short of destination following accident, mishap or stress of weather, the insurance ceases from the time the cargo is discharged at such port of refuge or directly into another vessel. If the voyage is not abandoned and the cargo remains in the vessel, cover continues up to 30 days from the time the vessel takes refuge.

Exclusions in Above Clauses

- All exclusions as applicable to ICC (A), (B) & (C)
- General Average Contribution
- Loss/damage willfully caused by negligence/ unlawful conduct of crew or owner
- Loss/damage due to detention / seizure by Government Authorities
- Loss/damage due to delay
- Un-seaworthiness/unfitness exclusion

Inland Vessel Clauses

This clause governs insurance cover of cargo carried in river or other smooth water including incidental land transit.

- **Coverage:**
    - Fire/explosion
    - Stranding, grounding, sinking, etc. of the vessel
    - Overturning, collision, derailment of land conveyance (warehouse to warehouse clause)
    - Collision of the vessel with external object
    - Discharge of Cargo at port of distress

- **Exclusion:**
  - General exclusion
  - Un-seaworthiness
  - WAR & SRCC

Losses and abandonment

Sections 55 to 66 of the Marine Insurance Act provide for the various loss for which the underwriters are liable in various situations in various subject matter of insurance.

Section 55 of the Act provides for included and excluded losses in the following terms:

"(1) Subject to the provisions of this Act, and unless the policy otherwise provides, the insurer is liable for any loss proximately caused by a peril insured against, but, subject as aforesaid, he is not liable for any loss which is not proximately caused by a peril insured against.

(2) In particular-

*(a) the insurer is not liable for any loss attributable to **the willful misconduct of the assured,** but, unless the policy otherwise provides, he is liable for any loss proximately caused by a peril insured against, even though the loss would not have happened but for the misconduct or negligence of the master or crew;*

(b) unless the policy otherwise provides, the insurer on ship or goods is not liable for any loss proximately caused by although the delay be caused by a peril insured against;

*(c) unless the policy otherwise provides, the insurer is not liable for ordinary wear and tear, ordinary leakage and breakage, **inherent vice or nature of the subject-matter insured,** or*

for any loss proximately caused by rats or vermin, or for any injury to machinery not proximately caused by maritime perils".

Thus Section 55(1) speaks about included loss and Section 55(2) specifies about excluded loss.

Measure of Indemnity in Case of Marine Losses

The provisions contained in Sections 67 to 78 provide for measure of indemnity for the marine losses to the subject matter of insurance under an unvalued or a valued policy.

Insurer's Liability under Valued and Unvalued Policy

Under Section 67 "the sum which the assured can recover in respect of a loss on a policy by which he is insured, in the case of an unvalued policy to the full extent of the insurable value, or, in the case of a valued policy to the full extent of the value fixed by the policy, is called the measure of indemnity. Where there is a loss recoverable under the policy, the insurer, or each insurer if there be more than one, is liable for such proportion of the measure of indemnity as the amount of his subscription bears to the value fixed by the policy in the case of a valued policy, or to the insurable value in the case of an unvalued policy".

Indemnity for Total Loss

Section 68 describes the measure of indemnity for total loss under a valued policy and an unvalued policy with the provisions that *"where there is a total loss of the subject-matter insured,(i) the measure of indemnity is the sum fixed by the policy if the policy be a valued policy and (ii) the measures of indemnity is the insurable value of the subject-matter insured if the policy be an unvalued policy".*

Indemnity for Partial Loss

Section 69, 70 & 71 of the Act describes the basis of measure of indemnity for partial losses of ship, freight and goods. Let us see how we can apply insurance law on assessment of partial loss of freight as provided by Section 70 which states that "subject to any express provision in the policy, where there is a partial loss of freight, the measure of indemnity is such proportion of the sum fixed by the policy in the case of a valued policy or of the insurable value in the case of an unvalued policy, as the proportion of freight lost by the assured bears to the whole freight at the risk of the assured under the policy."

Insurer's Rights *vis-à-vis* Claim Settlement

Insurers do have certain rights as per the following provisions contained in Section 79 to 81 of the Marine Insurance described below. Importantly, the following legal aspects are similar to the fundamental principles of insurance discussed earlier.

Right of Subrogation (Section 79)

Sometimes underwriters find it difficult to exercise the subrogation rights due to lack of clarity of legal perspectives thereof. The Marine Insurance Act is very clear in this regard providing specifically that:

"(1) *Where the insurer pays for **a total loss**, either of the whole, or in the case of goods of any apportionable part, of the subject-matter insured, he thereupon becomes entitled to take over the interest of the assured in whatever may remain of the subject-matter so paid for, and he is thereby subrogated to all the rights and remedies of the assured in and in respect of that subject-matter as from the time of the casualty causing the loss.*

*(2) Subject to the foregoing provisions, where the insurer pays for **a partial loss**, he acquires no title to the subject-matter insured, or such part of it as may remain, but he is thereupon subrogated to all rights and remedies of the assured in and in respect of the subject-matter insured as from the time of the casualty causing the loss, in so far as the assured has been indemnified, according to this Act, by such payment for the loss."*

Right of Contribution (Section 80)

We all know about insurer's right of contribution, but what is more important is the insurer's right to maintain suit against other insurers for contribution as per the provisions of the Act providing that:

"(1) Where the assured is over-insured by double insurance each insurer is bound, as between himself and the other insurers, to contribute ratably to the loss in proportion to the amount for which he is liable under his contract.

*(2) If any insurer pays more than his proportion of the loss, he is entitled to maintain a **suit for contribution against the other insurers**, and is entitled to the like remedies as a surety who has paid more than his proportion of the debt."*

Deduction for Under-insurance (Section 81)

Traditionally it is said that marine insurance is an agreed value policy where under insurance is not applicable. But the Marine Insurance Act 1963 provides something more that traditional concept with the provision that:

"Where the assured is insured for an amount less than the insurable value, or, in the case of a valued policy, for an amount less than the policy valuation, he is deemed to be his own insurer in respect of the uninsured balance".

So underinsurance will apply to marine insurance as per the Marine Insurance Act. To clarify the provisions let us consider the following example where the surveyor recommended for under insurance.

Example: A power generation company imported secondhand machinery of 1969 model from Argentina with ICC(A) Marine policy of Rs 2 crores. A professional firm of New York did the valuation of Rs 2 crores for the same, required for sanction of foreign exchange from RBI and custom duty. During voyage from Argentina to Bombay and then to Hyderabad a loss of equipment took place by non-delivery. Since second hand parts of make 1969 were outdated, the insured replaced the short-landed parts with compatible part for Rs 20 lacs. The insured submitted a claim for Rs 20 lacs with non-delivery certificate endorsed by customs. The Marine Insurance Act, 1963 helps determine the correct claim amount. After applying indices the valuation came to Rs 5 crores. The claim is originally assessed for Rs 20 lacs but if the provisions of Section 81 are applied, the loss will be admissible for Rs 8 lacs only.

Marine Cargo Insurance and Contract of Sales

Like domestic trade, in international trade, the exporter and the importers both have certain obligations to fulfill in order to make contact complete and get the due considerations. But unlike in contracts under Sale of Goods Act, in contracts of international sale, the transfer of risks and transfer of property are separated. Marine insurance management including underwriting and claims need to determine the terms of sales in various contracts of sales. In considering a proposal for cargo insurance underwriters begin with examination of the contract of sales, that specifies duties and responsibilities of the buyer and the seller and divide the transaction costs between them. A contract of sales basically provides the following two fundamental items, which are very essential for drafting and issuing marine insurance policy:

1. Terms of Sales

2. The price to be paid

These terms are varied from contract to contract, from consignment to consignment, country to country, from cargo to cargo, from market to market and so on. These terms have had wide impact over duties and responsibilities of the buyers and sellers and transfer of ownership and risks. In some cases, buyer have the major duties commencing from carrying the goods from sellers' warehouses to the buyers' premises involving all sorts of transits, customs clearance, insurance, etc. where sellers' responsibilities are the minimum. Again in some cases sellers' responsibilities are more and buyers' responsibilities are less. Furthermore, in international sales, transfer of property in goods (ownership) is different from the transfer of risks. The terms of contract dictate duties, responsibilities of the parties to the contracts of sales and also provide where and how the risks are being transferred from sellers to the buyers.

Marine Cargo Insurance and Incoterms 2000

Incoterms are international rules that are accepted by governments, legal authorities, businessmen and parishioners worldwide for the interpretation of the most commonly used terms in international trade. These terms prescribe responsibilities and obligations of the buyers and the sellers to make the transaction complete and effective. They also specify the point of transfer of risks. These terms describing the duties and responsibilities of the parties are listed numerically in a book published by International Chamber of Commerce (ICC). Businessmen from various countries have developed international commercial terms called INCOTERMS or International Commercial Terms to make the international sales easier and quicker. The latest version of Incoterms is called Incoterms 2000, which has been developed by the businessmen of various countries at the Brussels Conference under the guidance of ICC. Marine cargo underwriters are required to understand INCOTERMS while considering the contract of sales for international transactions related to import and export of goods. As per Incoterm 2000 there are 13 terms, out of which FOB, C&F, and CIF are the common ones, which we know. But others are also very important for underwriters for effective underwriting. Very precisely every term has 10 points of conditions that are covered or complied with by the seller or the buyer. The first term is **EWX**, i.e. Ex-works has the least number of obligations for the seller and consequently the largest number for the buyer. Conversely the last term **DDP** or 'Delivered Duty Paid' has the largest number of obligations for the seller and the least number for the buyer. Following few terms are discussed below:

- **FOB (Free on Board):** Under FOB contracts, the seller undertakes to deliver the goods over the ships' rail, at which point the risks pass from the seller to the buyer. The seller's responsibility is to pay all expenses until this point. He is to arrange for insurance up to the point. The buyer is also responsible for insurance from the time he assumes the risks, that is, once the goods pass the ship's rail. Sellers are responsible to clear customs dues, quality inspection charges and other export related dues. It is important that the shipment term in the bill of lading must carry the wording "Shipped on Board", it must bear the signature of the transporter or the carrier or his authorized representative with the date on which the goods are boarded. FOB price is inclusive of Ex-Works price, packing charges, transportation charges up to the place of shipment.

- **C&F/CFR (Cost and Freight):** Under this term the exporter bears the cost of carriage (freight). Risk passes from the exporter to the buyer at the port of shipment. The seller gives the notice of shipment to the buyer to enable him arrange insurance. Until shipment, the risks and however the and property in the goods remain with the shipper. The buyer is responsible for insurance from the time he assumes the risks, that is, from the point of shipment. The transfer of risks is the same as in FOB. The seller needs to protect his interests by insuring the risks in goods from his warehouse till the goods are loaded in the overseas vessel. C&F price is inclusive of Ex-Works price, packing charges, transportation charges up to shipment & freight.

- **CIF (Cost, Insurance and Freight):** The seller is responsible for insurance from own warehouse to that of the buyer at the destination point. This policy is called "warehouse to warehouse" marine policy. The policy is taken in the sellers' name and the claim is negotiated by the buyer, generally through a claims settling agent at the destination place in his own country. The seller is responsible to arrange insurance on warehouse-to-warehouse basis protecting the interests of both the seller and the buyer. Title and risks pass to the buyer when goods have been delivered abroad the ship at the loading point. Buyer supports the entire risk of transportation. CIF includes Cost, Freight and Insurance as the term provides.

- **EXW (Ex Works):** Title and risks pass to the buyer including payment of all transaction and insurance costs from the seller's door irrespective of mode of transportation. The buyer (importer) arranges insurance for consignment. The buyer has to bear all costs and risks involved in shipment transaction. Seller provides the goods for collection by the buyer on the seller's promise. Seller's responsibility is to put the goods in a good package, which is acceptable and disposable by the transport. (However if the parties wish the seller to be responsible for the loading of the goods on departure and to bear the risks and costs of loading, it needs specific wording to the effect in the contract of sales.

- **FCA (Free Carrier Point)**: The seller's responsibility is to deliver the goods into the custody of the transporter at the named points or load the goods on the buyer's vehicle. It is the buyer's responsibility to receive the seller's arriving vehicle unloaded. Thus title and risk pass to the buyer including transportation and insurance. The buyer decides the means of transport and insurance cover. The seller and the buyer agree upon the point of delivery of goods.

- **FAS (Free Alongside Ship)**: Title and risks including payment of transportation costs and insurance pass to the buyer once the goods delivered alongside ship by the seller whether used for sea or inland waterways transport. However export clearance obligation rests with the seller. Seller's responsibility ends as soon as the goods are placed cleared alongside the ship. The buyer's responsibility for all expenses and insurance start with the arrival of goods alongside ship.

- **CPT (Carriage Paid to)**: This term is used for transport by rail, road, and inland waterways. The seller and exporter are responsible for the carriage of goods to the nominated destination and to pay freight for the first carrier. He is responsible to do custom clearance and arrange and pay carrier up to the agreed destination. The buyer is responsible to pay for import customs; unloading costs and bear the risks of loss/damage after the goods are given by the first carrier. Thus the buyer needs to take insurance when he takes the risk on delivery by the first carrier.

- **CIP (Carriage & Insurance Paid)**: This term is almost similar to CPT except that the seller has to arrange and pay for the insurance against the risks of loss or damage of the goods during shipment. The seller has to take the insurance and pay the freight. The buyer has to pay customs and unloading charges. He supports the risks of loss or damage when the goods are given to the first carrier.

- **DAF (Delivered at Frontier)**; Title, risk of damage/loss and liability for import custom clearance pass to the buyer when cargo delivered to the named border point by the seller using any mode of transportation. The term is used mainly for delivery of goods by rail or road. When the buyer takes the delivery of the goods at the agreed border point, he is responsible for all custom formalities and insurance to mitigate the risks of loss or damage to the cargo. The seller is responsible to make the goods available to the buyer by the carrier up to the customs border as defined in the contract of sales.

- **DES (Delivered Ex-ship)**: Title, risks of loss/ damage or responsibility for discharge from vessel and import customs clearance pass to the buyer when the seller delivers goods on board the ship to destination port either for sea or inland waterways transportation. The seller is responsible to make the goods available to the buyer up to the named port or after crossing the customs border. The buyer is responsible to pay for unloading and insurance for risks arising after taking delivery at destination port.

- **DEQ (Delivered Ex-Quay)**: Title and risks pass to the buyer when delivered on board the ship at the destination point by the seller who delivers goods on dock at destination point cleared for import.

- **DDU (Delivered Duty Unpaid):** Seller is responsible to make the goods available at the named place in the country of importation. The seller is responsible for all transportation cost and accepts the custom duty and taxes as per custom procedure. The buyer is responsible for compliance of import customs formalities.

- **DDP (Delivered Duty Paid)** Title and risks pass to buyer when seller delivers goods to the named destination point cleared for import. The seller is responsible to make the goods to the buyer at his risk and cost as promised by the buyer. The buyer is responsible to take delivery at a nominated point and pays the expenses for loading and insurance.

Modes of Transport and Appropriateness of Incoterm 2000

Suitability of use of incoterms also depends on mode of transports. All terms are not equally suitable for all sorts of transports. A different set of incoterms have been found suitable in different mode of transports, that too also the underwriters need to know to decide the terms, conditions and warranties in the policies. Incoterms are classified based on suitability to the modes of transport.

(i) Suitable for Any Transport:

(a) **EXW** - Ex Works

(b) **FCA -** Free Carrier

(c) **CPT -** Carriage Paid To

(d) **CIP -** Carriage and Insurance Paid To

(e) **DAF -** Delivered At Frontier

(f) **DDU** - Delivered Duty Unpaid

(g) **DDP -** Delivered Duty Paid

(ii) Suitable for Air Transport:

(a) **EXW -** Ex Works

(b) **FCA -** Free Carrier

(c) **CPT -** Carriage Paid To

(d) **CIP -** Carriage and Insurance Paid To

(e) **DDU** - Delivered Duty Unpaid

(f) **DDP -** Delivered Duty Paid

(iii) Suitable for Rail Transport:

FCA - Free Carrier

(iv) Suitable for Sea and Inland Waterway Transport only:

(a) **FAS** - Free Alongside Ship

(b) **FOB** - Free On Board

(c) **CFR** - Cost and Freight

(d) **CIF** - Cost, Insurance and Freight

(e) **DES** - Delivered Ex Ship

(f) **DEQ** - Delivered Ex Quay

Marine Underwriting; Fundamental Consideration

Marine insurance underwriting is a specialized function in view of the fact that every consignment is unique in exposure because of the various factors such as cargo, ship, vehicles, roadways, sea roots, port details, packing materials, duration of transit, moral/ moral hazards of the consigners, and political risks.

Judgment Rating

In Marine Cargo, underwriting Judgment/exposure rating is preferable to standard and experience rating based on probability and severity analysis of past losses of the same or similar clients. Based on the exposures the underwriters and the assured take decisions on selection of appropriate policy from the set of open policy, open cover, annual policy, special declaration policy, and specific policy. The underwriters decide incoterms such as FOB, CIF, etc., depending upon terms of sale and decide on mode of transit-ship, roadways, airways, post office, couriers, own transport, etc.

Certain Documents in Marine Insurance

(a) Marine Declaration

There is no standard proposal form for marine cargo insurance except in case of special declaration policy, annual policy, duty and increased value insurance. However, full details of the proposed insurance are obtained as the proposal in a form called the declaration form. When the full details of a shipment are not initially available, sometimes a temporary cover note may be issued pending the ultimate issue of a formal policy. An alternative arrangement for insurance may be there under an open cover or open policy whereby the underwriter is to accept all the shipments coming within the scope and definition of the arrangement. With a understanding that the assured would declare all his shipments to be covered under the open cover or the open policy.

(b) Marine Cover Note

The risk assessed by the underwriter on the basis of information given in the declaration form duly completed and signed by the proposer. Generally a declaration form contents the following details. Over and above the specification of types of insurance covered require, i.e. ICC A or B or C as the case may be.

- Name, address and business of the proposer along with the name and address of the bank having interest in the transaction if any;

- Description of the goods to be insured along with nature of packing and marks and numbers appearing on the packages;
- Value of insurance that is sum insured with C.I.F. value+10 per cent;
- Duty and increased value components being indicated separately;
- Name of the carrying vessel along with age and other details;
- Duration and description of voyage or transit along with transshipment' and
- Bill of lading number/ air bill or air consignment number/RR or LR Number/Postal registration receipt number etc.

In case of different commodities are declared for coverage, individual values should be given for each commodity with basic shared value shown separately. On the basis of the details contained in the declaration form the underwriter is able to identify assess and evaluate the risks to be covered and rate the risk right for the cover to be granted.

Inland Transit Insurance: Underwriting Features (by Road /Rail)

For Inland Transit by Road/Rail three clauses are used. They are ITC (A), ITC (B) and ITC (C)

Inland Rail/Road Transit Clause

- **Basic Cover (ITC B)**:
  - Fire, lightning
  - Breakage of bridges
  - Collision, Overturning, derailment of carrying vehicle

- **ITC (C)**:
  - Fire & lightning only
- **ITC (A)**
  - All Risks: All risks except those specifically excluded
- **Extension of ITC (B)**
  - to include TPND, Rainwater/Fresh water damage etc
- **SRCC Risks**;
  - Such Risks may be covered as ADD ON.
  - War risk can never be covered

Exclusions to ITC (A), (B) & (C):

- Loss due to willful misconduct of the insured.
- General Ordinary leakage, wear and tear, etc.
- Loss/damage due to insufficient packing
- Inherent vice
- Delay

Duration ITC (A&B):

- Attachment: Goods leave the warehouse
- Continuance: Ordinary course of transit
- Termination:
  - On delivery to final warehouse, or
  - Expiry of 7 days after arrival of railway wagon, if transit by rail & road

  - Expiry of 7 days after arrival of vehicle at destination, in case of road transport

- Which ever shall first occur
- Extension of storage period up to 8 weeks

Duration ITC(C):

- Attachment: Loading of each package into wagon/truck
- Continuance: Ordinary course of transit
- Termination:
  - At the destination railway station, in case of rail transit
  - At the destination point, in case of road transit

Common Sub-clauses in ITC A/B/C

- Insurable Interest Clause: The insured must have insurable interest at the time the loss took place.
- Not to Inure clause: Benefit of insurance can be given or taken by the carrier
- Duty of Assured-Waiver clause: Reasonable care for averting/ minimizing loss, preserving rights against carrier, etc.
- Reasonable Dispatch Clause: To act with promptness in all circumstances

Riot & Civil Commotion Cover

SRCC Clause covering SRCC risks for inland transit insurance of goods by rail/road (not in conjunction with an overseas voyage)

SRCC Risks in Inland Transits

Risks of loss, damage or expenses are deleted under Strike, exclusion clause no.4 of ITC-A, ITC-B and ITC-C. However the same may be covered by charging additional premium and attaching the **"Strike, Riots and Civil Commotions Clause."**

Strike, Riots and Civil Commotions Clause

Risks covered: Loss or damage caused to the subject matter insured caused by

- Strikers, Locked-out workmen or persons taking part in labour disturbances, riot or civil commotions.
- *Any terrorists* or any persons acting from a political motive
- Persons acting maliciously.

Exclusions

In no case this insurance shall cover:

- Loss, damage, or expense proximately caused by delay, inherent vice or nature of the subject matter insured
- Loss, damage or expense proximately caused by the absence, shortage, or withholding of labour during any strike, lock-out, labour-disturbances, riot or civil commotion
- Any claim for expenses arising from delay or other consequential or indirect loss or damage of any kind.
- Loss, damage, or expense caused by war, civil war, revolution or strike arising therefrom or any hostile act by or against a belligerent power.

Certain Marine Insurance with Special Clauses or Covers

Duty & Increased Value Insurance

Duty Insurance and Increased Value Insurance policies are issued with above two clauses. Duty Insurance policies are taken by importers to cover payment of actual duty to government on the imported goods. Increase value of the goods by reason of the market price at destination on the date of landing is greater than CIF+duty. Such covers can be granted provided there exists insurance on CIF value of cargo and provided the carrying vessel has not arrived at destination. The scope of the cover shall be identical to that of original cargo policy. Such policies are not assignable and claims are payable only when liability is admitted under CIF policy.

Increased Value Insurance

The Increased Value Insurance is granted on the basis of this clause. This insurance is on increased value by reason of market value of the goods at destination on the date of landing of cargo being higher than the CIF and duty value of the cargo:

- The insurance is not for an agreed value;
- It is for an amount not exceeding the difference between the market value at destination on the date of lading and the total of CIF + duty;
- The policy is generally granted up to the maximum of 100 per cent of CIF value of cargo;
- Rate applicable is 100 per cent of normal CIF policy rate;
- The assured is required to bear 25 per cent of the claim amount payable under this component of this policy;
- This clause is in two parts, the former to apply when the insurance is primary and the later when the insurance is on increased value. The assured is expected to provide the various underwriters with evidence of the amounts insured under all other insurances. The effect of the clause is that all underwriters contribute and receive ratably to the values insured;

- Aneta Insurance Company vs. United Fruit Company: The US Supreme court held that the insurers' rights of recovery rested upon subrogation unaffected by valuation clause; and

- It provides the principle of application of subrogation in case of primary insurance and increased value insurance in different underwriters or markets.

Duty cover

- SI for duty to be adjusted on the basis of actual assessed duty;

- Pure indemnity policy;

- Rate of premium – 75 per cent of the rate charged for CIF value; and

- Total loss or part of cargo prior to duty becoming payable is not admissible.

Sellers' Contingency Insurance

Some countries do not allow insurance of import to be placed with foreign companies. That means goods have to be sold on FOB or C& F. If sale proceed are to be realized by means other that LC, there may be problem when buyer neither retire the document nor take delivery of goods. To protect the interest of Indian Exporters in such situations RBI has allowed the Indian insurer to grant such covers. It can be explained that when goods are sold on FOB or C&F terms, insurance on the goods is affected by the buyer to cover the buyer's interests only. The buyer's such policy does not cover the interests of the seller if there is any rejection of goods by the foreign buyer. If the rejection of the shipping documents or rejection of cargo is valid, the risk and ownership of the cargo consigned, but rejected revert to the seller and he has to make alternative arrangements for disposing of the goods. If however, such goods are lost or damaged, the situation is much worse for the seller- unless he makes some provisions for such contingency. We know some risks are covered by ECGC, but such risks covered by ECGC are credit or financial risks, but not property risks i.e. accidental physical loss or damage to the cargo.

Such risks arising from operation of insured perils after rejection of goods by the buyer are covered by Sellers' Interests Contingency Insurance. Such Insurance policy can be issued under cargo clause (A), (B) and (C) and will be subject to "Sellers Contingency Clause" The important features of the policy are:

- To protect the interest of seller only
- Policy not assignable except interest of Indian Bank
- Terms of the Sale Contract not to be altered.

The policy prohibits disclosure of its existence to other party—the buyer in particular. An important underwriting consideration of this insurance is very high moral hazard inherent in this type of coverage in view of some potential collusion between the seller and the buyer for their mutual gain. This potential moral hazard demands a careful analysis of any proposal for such type of cover.

Rejection Insurance

- Government of many countries exercise control over the quality of imported edible foods for which random sample check is made.
- Should the sample fail, the entire consignment is rejected/ destroyed without right of appeal.
- Rejection Insurance Clause is employed to cover this risk.
- There is no Institute Clause to cater to this need.
- Insurance is subject to pre-shipment survey.
- Domestic regulation of both the countries to be complied.

Stamp Duty

Marine Cargo Policy is subject to carrying stamp duty as per the Indian Stamp Act, 1899 as amended from time to time. The stamp duty is recoverable from the insured. The scale of stamp duty applicable to such policies for: i) Sea Voyage & transit country craft; ii) Other Than other Sea Voyage; and iii) Postal Sendings.

1. **Sea Voyage & Transit Country Craft:** 10 paise for every Rs 1500 (SI) or part thereof subject to the following;

   (a) Where the rate charged is 1/8 per cent or less, the stamp duty is Rs10 only irrespective of the sum-insured

   (b) Where inland transit (Rail or Road) covered in conjunction with sea voyage, the policy will be stamped according to scale applicable to sea voyage

2. **Other Than other Sea Voyage (Transit by rail, road or air)**

   (a) 50 paise when sum insured is Rs 5000 or less

   (b) Rs. 1 when sum insured is over Rs 5000

3. **Postal Sendings**

   (a) Scale as per (1) above, if it involves sea voyage

   (b) Scale as per (2) above for transit by road, rail or air

6

INSURANCE ARBITRATION AND ARBITRATION AND CONCILIATION ACT, 1996

Arbitration Clause in an Insurance Policy

Almost all insurance policies contain Arbitration Clause along with other clauses. Such agreement clause is worded as under:

"If any dispute or difference arises as to the quantum to be paid under this policy (liability being otherwise admitted) such difference shall independently of all other questions be referred to the decision of a sole arbitrator to be appointed in writing by the parties to or if they cannot agree upon a single arbitrator within 30 days of any party invoking arbitration, the same shall be referred to a panel of three arbitrators, comprising of two arbitrators, one to be appointed by each of the parties to the dispute/difference and the third arbitrator to be appointed by such two arbitrators and arbitration shall be conducted under and in accordance with the provisions of the Arbitration and Conciliation Act, 1996. It is clearly agreed and understood that no difference or dispute shall be referable to arbitration, if the Company has disputed or not accepted liability under or in respect of this policy. It is hereby expressly stipulated and declared that it shall be a condition precedent to any right of action or suit upon this policy arising out of the above that the award by such arbitrator/ arbitrators of the amount of the loss or damage shall be first obtained."

Such agreement may also provide that "— The parties shall share the expenses of the arbitrator or the arbitral tribunal equally and such expenses along with the reasonable costs of the parties in the arbitration, shall be awarded by the arbitrator or arbitral tribunal in favour of the successful party in the arbitration or where no party can be said to be have been wholly successful, to the party who has substantially succeeded. ..” “….In the event that these arbitration provisions shall be held to be invalid, then all such disputes shall be referred to the exclusive jurisdiction of the Indian Courts.”

Precisely, only disputes or differences in regard to quantum of loss between the insured and the insurer can be referred to arbitration. Arbitration clause is very vital for settlement of disputes in regard to quantum of loss. Let us examine the nature and scope of arbitration proceedings from the following example which is based on a case study on a dispute between the insured and an insurer in regard to quantum of loss where the admissibility of claim has been established the surveyor and admitted by the insurer.

Example:

- **Insurance Policy**; Standard Fire and Special Perils Policy
- **Policy Period**; 01-04-05 to 31-03-06
- **Insured;** M/s SD Vegetables Ltd and **Insurer**; India Insurance Co. Ltd.
- **Sum-insured**; Rs 250,00,000 (P&M Rs 1,35,00,000 and Stock Rs 1,15,00,000)
- **Accident**; fire occurred on 23.12.05
- **Amount Claimed**: Rs.110,00,000 (P&M Rs.40,00,000 and Stock Rs.70,00,000)
- **Preliminary S/Report**; Establishing the admissibility of claim and indicating estimated loss Rs 100,00,000
- **Detailed examination**; by the insurer along with the surveyor with reference and asked for details of closing stock with evidence and excise register and input-output register, process register, Public Weighbridge Register and extract

along with usual stock register and *challan* and bills for raw-material purchase

- **Final Report Assessment** reduced to Rs 21,31,561 for both plant and stock though surveyor recommended two Assessments (all inclusive); One for Rs 45,20,818 (both for Plant & Stock) and other for Rs 21,31,561 (plant & stock) leaving it to the final decision of the insurer.

- **Loss Voucher** issued by the insurer along with **Claim Cheque** for Rs 2131561 well explaining as to why they could not accept.

- **The insured refused** to accept the claim *cheque* disputing assessment as the surveyor had given three assessment-Preliminary Report Rs 100,000,00 and Final Survey Report gave two different assessments.

- They **referred the dispute to Arbitration** as per arbitration clause as the dispute was pertaining to quantum of loss, but not on the admissibility of claims.

- As per **Arbitration clause** the insurer agreed with such reference to arbitration.

Now let us examine the following aspects with reference to above reference to arbitration:

- **What is the basis of Arbitration and Conciliation?**
- **What is the Arbitration Agreement?**
- **How are parties required to refer to arbitration?**
- **What could be the composition of Arbitral Tribunal?**
- **How will be constituted?**
- **Can an arbitrator challenged? If yes, how?**
- **What are the Arbitral Proceedings?**

- **What could be the statement of claim and defence?**
- **Whether arbitral tribunal appoints an expert?**

Basis of Arbitration and Conciliation

Arbitration and conciliation means the settlement of a dispute by referring the dispute to a third party and abiding by his decision. Like any other commercial contract, the insurance contract creates and defines the obligations and duties between the parties to the insurance contract. In case of any dispute or grievance between the parties i.e. the insured and the insurer in regard to performance of contractual obligations, the aggrieved party may refer the disputes to the arbitrator who may decide and settle the dispute between the insured and the insurer as per the provisions of The Arbitration and Conciliation Act, 1996 which extends to whole of India and apply to all domestic as well as the international commercial arbitration or as the case may be, international commercial conciliation. Settlement of disputes in insurance contracts through reference to Arbitration is as important as settlement through Insurance Ombudsman, District Consumer Forum/State Commission/National Commission, the High Court or the Supreme Court. Arbitration is a very vital mechanism of grievance redressal in Insurance sector.

Arbitration Agreement

As per Section 7 of the Arbitration and Conciliation Act, 1996, arbitration agreement is an agreement by the parties to submit to arbitration all or certain disputes which have arisen or which may arise between them in respect of a defined legal relationship, whether contractual or not. Arbitration agreement may be in the form of an arbitration clause in a contract or a separate agreement. An arbitration agreement shall be in writing. The insurance contract containing an arbitration clause constitutes an agreement and the reference is such as to make that arbitration clause part of the insurance contract.

Power to Refer Parties to Arbitration

Under Section 8 of the Act specifies the power to refer parties to arbitration in the following manner where there is an arbitration agreement:

- A judicial authority before which an action is brought in a matter, which is the subject of an arbitration agreement, shall, if a party so applies not later than when submitting his first statement on the substance of the dispute, refer the parties to arbitration;

- The said application shall not be entertained unless it is accompanied by the original arbitration agreement or a duly certified copy thereof; and

- Notwithstanding that an application as mentioned above has been made and issue is pending before the judicial authority, an arbitration can be commenced, continued and an arbitrate award made.

Composition & Appointment of Arbitral Tribunal

Under Section 10 of the Act the number of arbitrators will be decided as follow:

- Parties are free to determine the number of arbitrators, provided that such number shall not be an even number.

- Failing above determination arbitral tribunal shall be a sole arbitrator

Section 11 provides for appointment of arbitrators in the following terms:

- A person of any nationality may be an arbitrator unless otherwise agreed by parties

- Parties are free to decide procedure of appointment of arbitrator(s).

- Failing any agreement as per procedure, each party shall appoint one.

- Two appointed arbitrators appoint the third arbitrator who shall act as the presiding arbitrator.

- The Chief Justice or any person or institution designated by him may appoint arbitrator if a party fails to appoint an arbitrator within 30 days from the receipt of request to do so or two appointed arbitrators fail to appoint the third one.

- Failing an agreement in arbitration with a sole arbitrator, the parties fail to agree on the arbitrator within 30 days from the receipt of a request by one party from the other, the appointment shall be made upon the request of a party, by the Chief Justice or any person or institution designated by him.

- Where under an agreement procedure agreed upon by the parties: (i) a party fails to act as required under the procedure; or (ii) the parties/two appointed arbitrators, fail to reach an agreement expected of them under that procedure; or iii) a person including institution fails to perform any function, a party may request or any person or institution designated by him to take necessary measure.

- The Chief Justice or the person or institution designated by him in appointing arbitrator, shall have due regard to:

    - Qualifications required of the arbitrator

    - Other considerations as likely to secure the appointment of an independent and impartial arbitrator

- In the case of appointment of sole or third arbitrator in an international commercial arbitration, the Chief Justice of India or the person or institution designated by him may appoint an arbitrator of a nationality other than the nationalities of the parties where the parties belong to different nationalities.

(In the given case the insured and the insurer one arbitrator each and the two appointed arbitrators appointed the third one as presiding arbitrator in the arbitration proceedings)

Grounds to Challenge an Arbitrator

Under Section 12 of the Act an arbitrator may be challenged if:

- Circumstances exist that give rise to justifiable doubts as to his independence or impartiality of the arbitrator;
- The arbitrator does not possess the qualifications agreed to by the parties; and
- A party may challenge an arbitrator appointed by him, or in whose appointment he has participated, only for reasons of which he becomes aware after appointment has been made.

Challenge Procedure

Under Section 13 of the Act, the parties shall adhere to following procedure to challenge arbitrator:

- A party who intends to challenge an arbitrator shall, within fifteen days after becoming aware of the constitution of the arbitral tribunal or after becoming aware of any circumstances referred to in sub-section (3) of Section 12, send a written statement of the reasons for the challenge to the arbitral tribunal.
- Unless the arbitrator challenged under sub-section (2) withdraws from his office or the other party agrees to the challenge, the arbitral tribunal shall decide on the challenge.
- If a challenge under any procedure agreed upon by the parties or under above procedure is not successful, the arbitral

tribunal shall continue the arbitral proceedings and make an arbitral award.

- Where an arbitral award is made, the party challenging the arbitrator may make an application for setting aside such an arbitral award in accordance with Section 34.

- Where an arbitral award is set aside on an application as mentioned, the court may decide as to whether the arbitrator who is challenged is entitled to any fees.

Termination of the Mandate

(a) The mandate of an agreement shall terminate if the arbitrator:

- becomes, *de-jure* or *de-facto* unable to perform his functions or for other reasons fails to act without undue delay; or

- withdraws from his office or the parties agree to the termination of his mandate.

(b) If a controversy remains concerning any of the grounds referred to above, one party may, unless otherwise agreed by the parties, apply to the court to decide on the termination of the mandate.

Conduct of Arbitral Proceedings

- **Equal treatment of parties:** The parties shall be treated with equality and each party shall be given a full opportunity to present the case (Section 18)

- Section 19 provides for determination of rules of procedure, which is given as under:

  o The Arbitral tribunal shall not be bound by the Code of Civil Procedure, 1908 or the Indian Evidence Act, 1872.

  o The parties are free to agree on the procedure to be followed by the arbitral tribunal in conducting the proceedings.

- o Failing any agreement as mentioned above, the arbitral may conduct the proceedings in the manner it considers appropriate.
- o The arbitral tribunal will decide, under the above circumstances, the admissibility, relevance, materiality and weight of any evidence.

- **Place of arbitration:** The parties are free to agree on the place of arbitration.
- **Commencement of arbitral proceedings:** Section 21 provides that unless otherwise agreed by the parties, the arbitral proceedings in respect of a particular dispute commence on the date on which a request for reference of dispute to arbitration is received.
- **Language:** Section 22 provides that parties are free to agree on the language or language to be used in arbitral proceedings.

Statements of Claim and Defence (Section 23)

The claimant shall state the facts supporting his claim, the points at issue and the relief or remedy sought, and the respondent shall state his defence in respect of these particulars, unless the parties have otherwise agreed as to the required elements thereof. The parties may submit with their statements all documents they consider relevant or may add a reference to the documents or other evidence they will submit. Unless otherwise agreed by the parties, either party may amend or supplement his claim or defence during the course of the arbitral proceedings, unless the arbitral tribunal considers it inappropriate to allow the amendment or supplement having regard to the delay in making it.

Hearings & Proceedings (Section 24)

- Unless otherwise agreed by the parties Arbitral Tribunal shall decide whether to hold:
  - Oral Hearings for presentation of evidence or
  - Argument
  - Proceeding on the basis of documents and materials

Provided Arbitral Tribunal will hold Oral Hearings for presentation of evidence on a request of a party unless the parties have agreed that no oral hearing will be there.

- The parties shall be given in sufficient advance notice of hearings and of the meeting of the tribunal.
- All statements, documents and other information supplied or application made to the arbitrator to be communicated to other part.

Recourse against Arbitral Award

Application for Setting Aside Arbitral Award: Under Section 34 of the Act recourse to a court against an arbitral award may be made only by an application for setting aside such award in accordance with sub-section (2) and subsection (3). The court may set an arbitral award aside in any of the following two situations: a) the party making the application; or b) the Court finds it proper.

(a) The party making the application shall furnish proof that:

- A party was under some incapacity;
- The arbitration agreement is not valid under the law to which the parties have subjected it or, failing any indication thereon, under the law for the time being in force;

- The party making the application was not given proper notice of the appointment of an arbitrator or of the arbitral proceedings or was otherwise unable to present his case;

- The arbitral award deals with a dispute not contemplated by or not falling within the terms of the submission to arbitration, or it contains decisions on matters beyond the scope of the submission to arbitration, Provided that, if the decisions on matters submitted to arbitration can be separated from those not so submitted, only that part of the arbitral award which contains decisions on matters not submitted to arbitration may be set aside; or

- The composition of the arbitral tribunal or the arbitral procedure was not in accordance with the agreement of the parties, unless such agreement was in conflict with a provision of this Part from which the parties cannot derogate, or, failing such agreement, was not in accordance with this Part.

(b) The court finds that:

- The subject-matter of the dispute is not capable of settlement by arbitration under the law for the time being in force; or

- The arbitral award is in conflict with the public policy of India.

7

REGULATIONS UNDER IRDA ACT, 1999[1]

IRDA (INVESTMENT) REGULATIONS 2008

Every insurer carrying on insurance or reinsurance business in India shall invest and at all times keep invested his total assets as per provisions of Sec 27 or Sec 27A of the Insurance Act, 1938 and in the same manner as set out in specific regulations framed by the IRDA. Importantly this unit only deals with regulatory aspects, while investment accounting methods and process are discussed in the following unit XVI. Though unit XVI is basically based on AS 13, which is not relevant for insurance business, the accounting procedures are almost same for both insurance business and non-insurance business. For general accounting of investment, the students must have clear and complete understanding of accounting methods for investment as discussed in unit XVI.

In exercise of the powers conferred by sections 27A, 27B, 27D and 114A of the Insurance Act, 1938, the Authority (IRDA) in consultation with Insurance Advisory Committee, makes these regulations on Investments of insurance companies. The Regulations originally framed by the IRDA is called the IRDA (Investment) Regulations 2000, which has been amended now into IRDA (Investment) (Fourth Amendment) Regulations 2008. Here we will discuss only those regulatory aspects applicable to general insurance business. Pertinently the said regulation is meant for both life insurance business and non-life insurance business. The said regulations provide the following rules and norms which all insurance companies carrying on insurance business are required to comply.

[1] This chapter is based on IRDA's publication on Regulation.

Manner of Investments by General Insurance Companies

1. Investment assets mean all investments made out of shareholders' funds representing solvency margin and policyholders' funds at their carrying value as shown in its balance sheet drawn as per the IRDA (Preparation of Financial Statements and Auditors' Report of Insurance Companies) Regulations 2002. means

2. As per Regulation 4 (1) of the said regulation every insurer carrying on general insurance business shall invest and keep invested his investment assets in the following manner;

No	Type of Investments	Percentage
i)	Government Securities	Not less than 20% of investment assets
ii)	Govt. Securities& other approved securities incl. i) above	Not less than 30% of investment assets
iii)	Investments as specified in sec27B of the Insurance Act 1938 and Schedule II subject to Exposure / Prudential Norms specified in Regulations 5;	
	a. Approved Investments and Other Investments (out of '(iii)a' 'Other investments specified under 27B(3) of the Act, shall not exceed 25% of the Investment Assets)	Not exceeding 55%
	b. Housing and Loans to State Govt for Housing and Fire Fighting equipment by way of subscription or purchase of;	Not exceeding 5%
	1. Bonds/debentures of HUDCO and National Housing Bank	

	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) Reg,1999 3. Asset Backed Securities with underlying housing loans, satisfying the norms specified in the guidelines issued under these regulations c. **Investment in Infrastructure;** (Subscription or purchase of Bonds / Debentures, Equity and Asset Backed Securities with underlying infrastructure assets would qualify for the purpose of this requirement Infrastructure facility shall have the same meaning as given in IRDA (Registration of Indian Insurance Companies) Amendment Regulations 2008)	 Not less than 10%

Reinsurance Business

Every insurer carrying on reinsurance business shall invest and at all times keep invested his investment assets in the same manner as set out in 4(1) mentioned in 2 above, until such time, separate regulations in this behalf are formed by the Authority.

Regulatory Directives for Investments by Insurance Companies:

1. All investments in assets or instruments, which are capable of being rated as per market practice, shall be made on the basis of credit rating of such assets or instruments. No investments shall be made in instruments, if such instruments are capable of being rated, but not rated.

2. The rating should be done by a credit rating Agency registered under SEBI (Credit Rating Agencies) Regulations1999.

3. Corporation bonds or debentures rated not less than AA or its equivalent and PI or equivalent ratings for short term bonds, debentures, certificate of deposits and commercial paper, by a credit rating agency, registered under SEBI (Credit Rating Agencies) Reg,1999 would be considered as 'Approved Investments'

4. The rating of a debt instrument issued by All India Financial Instruments recognized as such by RBI shall be of 'AA' or equivalent rating.

5. Approved Investments which are downgraded below the minimum rating prescribed should be automatically re-classified under "Other Investments"

6. Investments in equity shares listed on a registered stock exchange should be made in actively traded and liquid instruments viz. equity shares other than those defined as thinly traded as per SEBI regulations and guidelines governing mutual funds issued by SEBI from time to time.

7. Not less than 75% of debt instruments excluding Government and Other Approved Securities and Investment Assets shall have a rating of 'AAA' or equivalent rating for long-term and PI+ or equivalent for short term investments.

8. It is emphasized that rating should not replace appropriate risk analysis and management on the part of the insurer. The insurer should conduct risk analysis commensurate with complexity of the products and the materiality of their holding or could also refrain from such investments.

Exposure / Prudential Norms

Without prejudice to anything contained in Sec.27A and 27B of the Insurance Act, 1938 every insurer shall limit his investments based on the following exposure norms:

Exposure norms for life (including Unit linked business), General insurance (including reinsurance) business for both Approved

Investments as per the Insurance Act, 1938, Schedule I &II of these Regulations and other Investments as permitted under 27A(2) and 27A(3) of the Insurance Act, 1938.

The following Exposure Norms in respect of both Approved Investments as per the Insurance Act, 1938 and the Regulations are required to be followed by both life insurance business and general insurance business;

<table>
<tr><th>Type of Investment</th><th>Limit for Investee Company</th><th>Limit for entire group of Investee Company</th><th>Limit for industry</th></tr>
<tr><td>a. Investment in equity, Preference Shares, Convrtibl Debenture</td><td>10% of out-standing equity share (face value) or investment asset, whichever is less in gen. insurance</td><td rowspan="2">Not more than 10% of investment of assets (including reinsurer)</td><td rowspan="2">Investment by the insurer in any industrial sector shall not exceed 10% of its total exposure to the industry sector</td></tr>
<tr><td>b. Investments in Debts, Loans, & Other investment permitted by Act or Regulation</td><td>10% of the paid share capital, free reserves, debenture, bonds of investee company or 10% of investment asset in Gen. Insurance which ever is less</td></tr>
</table>

Special Notes on Exposure Norms

1. Investment in equity including preference shares and convertible part of debentures shall not exceed 50% of the above exposure norms as mentioned in the above table

2. Investment in immovable property covered under Sec 27A(1)(n) of the Insurance Act 1938 shall not exceed, at the time of investment, 5% of the investment asset

3. An insurer shall not have investments of more than 5% in aggregate of its total investments in companies belonging to the promoters' group

4. 10% of group and industry sector exposure shall be raised upto 15% with the prior approval of the Investment Committee, which will exercise due care keeping in view the possible concentration and other related risks

5. The exposure limit for financial and banking sector shall stand at 25% investment assets for all insurers.

6. Investment in fixed deposits, term deposits and certificate of deposits of a scheduled bank shall be made in terms of the provisions of Sec. 27A(9) and Sec. 27B(10) of the Insurance Act 1938. Such investments would not be deemed as exposure to banking sector.

Investment Returns to be submitted by insurers

Reg. 6 of the Investment Regulation provides that the Quarterly Investment Returns to be submitted by every insurer to the Regulator Such Qtly investment returns shall be duly verified/ certified by CEO/ Chief of Investment

1. Statement of Investment and Income on Investment in Form 1

2. Statement of Downgraded Investments in Form 2

3. Statement of Investments (General Insurer)—Compliance Report in Form 3B

4. Exposures and other norms-Compliance Certificate in Form 4

5. Statement of Investment subject to Exposure Norms-investee company in Form 4A

6. Statement of Investment Reconciliation in Form 5

7. Statement of Mutual Fund Investment in Form 5A

8. Certificate U/S 28(2A), 28(2B), 28B of the Insurance Act, 1938 in Form 6

9. Confirmation of Investment Portfolio Details in Form 7

10. Statement of Non-performing Assets in Form 7A

Constitution of Investment Committee and its Roles

Reg.7 provides for Constitution of Investment Committee and its Roles, which are briefly discussed below;

1. Every insurer shall constitute an Investment Committee which shall consist of a minimum of two non-executive directors, the CEO, Chief of Finance, Chief of Investment Decision and the Appointed Actuary

2. Every Insurer shall draw up, annually an Investment Policy and place the same before Board of Directors for Approval. While framing such policy, the Board shall ensure compliance with the following;

   - Issues relating to liquidity, prudential norms, exposure limits, stop loss limits, security trading, management of investment risks, management of assets liabilities, scope of concurrent and internal audit of investments and investment statistics and all other internal control of investment operations, the provisions of the insurance Act 1938 and IRDA (Investments) Regulation 2000, guidelines and circulars in this regard

   - Ensuring adequate return on policyholders' funds and shareholders' funds consistent with the protection, safety and liquidity of such funds

   - The funds of the insurer shall be invested and continued to be invested in equity shares, equity related instruments and debt instruments keeping in view the requirements of the Insurance Act 1938 and IRDA (Investments) Regulation 2008

3. The investment policy as approved by the Board shall be implemented by the Investment Committee, which shall keep the Board informed about its activities and fund performance

4. The Board shall review the Investment Policy and its implementation on a half yearly basis or at such short interval as it may decide and make such modification to the investment policy as is necessary to bring it in line with investment provisions laid down in the Insurance Act and in Investment Regulations.

5. The details of IP or its review as periodically decided by the Board shall be made available to the concurrent or internal auditor. The Auditor shall comment on such review and its impact on investment operations

6. In order to ensure proper internal control of investment functions and operations the insurer shall segregate the functions and operations of front office, mid office and back office.

7. The Authority may call for further such information from time to time as it deems necessary and in the interest of the policyholders.

List of Approved Investments –Schedule II to IRDA (Investment) Regulations

Schedule II of the IRDA (Investment) Regulation provides the following list of Approved Investments for general insurance business for the purpose of Sec. 27B of the Act;

a) All investments specified in Sec. 27B of the Act except

   i) Securities of or guaranteed as to the principle and interest by the Government of the UK in another country as stated in Sec. 27B (1)(b).

   ii) Immovable property situated in another country as mentioned in 27A(1)(n)

   iii) First mortgage on immovable property situated in another country as stated in 27A(1)(i)

b) In addition to above, the following investments shall be deemed as approved investments by the Authority (IRDA) under the powers vested in it under Sec. 27B(1)(j);

i) All loans secured as per Insurance Act, secured-debentures, secured bonds and debt instruments rated as per note appended to Reg.3 & 4. Equity shares, preference shares and debt instruments issued by All India Financial Institutions recognized by RBI provided investments shall be made in terms of investment policy guidelines, benchmarks and exposure norms, limits by Board of Directors of the insurer.

ii) Bonds or debentures issued by companies rated not less than AA or its equivalent and PI or Equivalent ratings for short term bonds, debentures, certificate of deposits and commercial papers by a credit rating agency registered under SEBI.

iii) Collateralized Borrowing & Leading Obligations (CBLO) created by the Clearing Corporation of India Ltd and recognized by the RBI and exposure to Gilt, G-Sec. and Liquid mutual fund forming part of Approved Investment as per Mutual Fund Guidelines

iv) Asset Backed Securities with underlying Housing Loans or having infrastructures assets as defined under infrastructures facility in reg.2 of IRDA (Registration of Indian Insurance Companies) Amendment Regulations 2008.

v) Commercial Papers issued by a company or All India Financial Institution recognized as such by RBI having Credit rating

vi) Money market instrument as defined in Regulation 29cc) of this Regulation.

In exercise of the powers conferred by sections 27A, 27B, 27D and 114A of the Insurance Act, 1938, the Authority (IRDA) in consultation with Insurance Advisory Committee, makes these regulations on Investments of insurance companies

Every insurer carrying on insurance or reinsurance business in India shall invest and at all times keep invested his total assets as per provisions of Sec 27 or Sec 27A of the Insurance Act, 1938 and in the same manner as set out in specific regulations framed by the IRDA. All investments shall be made in graded securities and grading shall not be less than of 'Very young' rating by a reputed and independent rating agency (e.g. AA of Stand and Poor). The insurer shall invest assets in securities, which are actively traded in any Stock Exchanges in India. The insurers must make these investments in the manners set out in the said regulations without prejudice to the specific provisions of the Act.

Regulations of Investments applicable to Life Business:

Every insurer carrying on life insurance business shall invest and keep invested his controlled fund in the following manner:

No	Type of Investments	Percentage
i)	Government Securities	25%
ii)	Govt. Securities or other approved securities incl. i) above	Not less than 50%
iii)	Approved investments: a) Infrastructure & Social sector *1 b) Others under prudential norms as specified in Reg. 5	 Not less than 15% Nor exceeding 20%
iv)	Other than in Approved Investments under prudential norms as specified in Reg.5	Not exceeding 15%

Approved investments as provided by Sec 27B:

a. The investments specified in clauses (a) to (e), (n), (q), and (r) of Sec.27A (1)

b. Debentures secured by a first charge on any immovable property, plant or equipment of any company which has paid interest in full for 3 years immediately preceding or for at least 3 out of 4/5 years immediately before issue of debentures.

c. Debentures secured by a first charge on any immovable property, plant or equipment of any company where either its book value or its market value, whichever is less, is more than two times the value of such debentures.

d. First debentures secured by a first floating charge on all in its assets of a company which paid dividends on equity shares for last 3 yrs or for at least 3 out of 4/5 yrs.

e. Preference shares of a company which has paid dividends on equity shares for last 3 yrs or for at least 3 out of 4/5 yrs.

f. Preference shares of a company on which dividends has been paid for last 3 yrs or for at least 3 out of 4/5 yrs.

g. Shares of any company, which have been guaranteed by another company, such other company having paid dividends on its ordinary shares for last 3 yrs or for at least 3 out of 4/5 yrs immediately preceding.

h. Shares of any company on which dividends of not less than 4% including bonus have been paid for last 3 yrs immediately preceding or 3 yrs out of 4/5 yrs immediately preceding

IRDA (Preparation of Financial Statements and Auditor's Report of Insurance Companies) Regulations, 2002]

Indian GAAP on Insurance Accounting

Indian GAAP on Insurance Accounts comprises specific Regulation, the relevant provisions of the Insurance Act 1938 and The Companies Act, 1956 and relevant Accounting Standards issued by the Institute of Chartered Accountants of India. In this regard IRDA has issued a detailed accounting and audit regulation called The Insurance Regulatory and Development Authority (Preparation of Financial Statements and Auditor's Report of Insurance Companies) Regulations, 2002. The following financial statements of insurance company are required to be prepared as per specified formats and in accordance with Accounting Principles and General Instructions for preparations of financial statements specified in the said regulations over and above compliance of the requirements of the Companies Act,1956 and the Insurance Act,1938 and applicable Accounting Standards (AS).

- Balance Sheet
- Revenue Accounts
- Profits and Loss Account
- Receipts and Payments Account.

Regulations for Insurance Accounting

In exercise of the powers conferred by section 114A of the Insurance Act, 1938 and in suppression of The Insurance Regulatory And Development Authority (Preparation Of Financial Statements And Auditor's Report Of Insurance Companies) Regulations, 2000, the Insurance Regulatory and Development Authority in consultation with the Insurance Advisory Committee, has framed the Regulations called "IRDA (Preparation of Financial Statements and Auditor's Report of Insurance Companies) Regulations, 2002" for the purpose of accounting of insurance business. The said Regulations provide that

(1) An insurer carrying on life insurance business, after the commencement of these Regulations, 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:

(3) The report of the auditors on the financial statements of every insurer and reinsurer shall be in conformity with the requirements of Schedule C, or as near thereto as the circumstances permit.

(4) The Authority may, from time to time, issue separate directions/ guidelines in the matter of appointment, continuance or removal of auditors of an insurer or reinsurer, as the case may be, and such directions/ guidelines may include prescriptions regarding qualifications and experience of auditors, their rotation, period of appointment, etc as may be deemed necessary by the Authority.

This Unit provides the relevant extract of the Schedule B to Regulations for Preparation of financial statements, management report and auditor's report in respect of general insurance business. Schedule B deals with accounting regulations on the following heads;

Part I-Accounting Principles for Preparation of Financial Statements

Part II- Disclosures forming part of Financial Statements

Part III- General Instruction for preparation of Financial Statements

Part IV- Contents of Management Report

Part V- Preparation of Financial Statements

PART I—Accounting principles for preparation of financial statements

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:

1. Accounting Standard 3 (AS 3) – Cash Flow Statements – Cash Flow Statement shall be prepared only under the Direct Method.

2. Accounting Standard 13 (AS 13) – Accounting for Investments, shall not be applicable.

3. Accounting Standard 17 (AS 17)- Segment Reporting– shall apply to all insurers irrespective of the requirements regarding listing and turnover mentioned therein.

Premium Recognition

Premium shall be recognised as income over the contract period or the period of risk, whichever is appropriate. Premium received in advance, which represents premium income not relating to the current accounting period, shall be disclosed separately in the financial statements.

A reserve for unexpired risks shall be created as the amount representing that part of the premium written which is attributable to, and to be allocated to the succeeding accounting periods and shall not be less than as required under Section 64 V(1) (ii) (b) of the Act.

Premium Received in Advance, which represents premium received prior to the commencement of the risk, shall be shown separately under the head '*Current Liabilities'* in the financial statements.

Premium Deficiency

Premium deficiency shall be recognised if the sum of expected claim costs, related expenses and maintenance costs exceeds related reserve for unexpired risks.

Acquisition Costs

Acquisition costs, if any, shall be expensed in the period in which they are incurred.

Acquisition costs are those costs that vary with, and are primarily related to, the acquisition of new and renewal insurance contracts. The most essential test is the obligatory relationship between costs and the execution of insurance contracts (i.e. commencement of risk).

Claims

The components of the ultimate cost of claims to an insurer comprise the claims under policies and specific claims settlement costs. Claims under policies comprise the claims made for losses incurred, and those estimated or anticipated under the policies following a loss occurrence.

A liability for outstanding claims shall be brought to account in respect of both direct business and inward reinsurance business. The liability shall include: -

(a) Future payments in relation to unpaid reported claims;

(b) Claims Incurred But Not Reported (IBNR) including inadequate reserves [sometimes referred to as Claims Incurred But Not Enough Reported (IBNER)],

which will result in future cash/asset outgo for settling liabilities against those claims. Change in estimated liability represents the difference between the estimated liability for outstanding claims at the beginning and at the end of the financial period.

The accounting estimate shall also include claims cost adjusted for estimated salvage value if there is sufficient degree of certainty of its realisation.

Actuarial Valuation of claim liability – in some cases

Claims made in respect of contracts where the claims payment period exceeds four years shall be recognised on an actuarial basis, subject to regulations that may be prescribed by the Authority. In such cases, certificate from a recognised actuary as to the fairness of liability assessment must be obtained. Actuarial assumptions shall be suitably disclosed by way of notes to the account.

Procedure to determine the value of investments

An insurer shall determine the values of investments in the following manner:-

(a) Real Estate – Investment Property— Investment Property shall be measured at historical cost less accumulated depreciation and impairment loss, residual value being considered zero and no revaluation being permissible.

The Insurer shall assess at each balance sheet date whether any impairment of the investment property has occurred.

An impairment loss shall be recognised as an expense in the Revenue/Profit and Loss Account immediately.

Fair value as at the balance sheet date and the basis of its determination shall be disclosed in the financial statements as additional information.

(b) Debt Securities—Debt securities including government securities and redeemable preference shares shall be considered as "held to maturity" securities and shall be measured at historical cost subject to amortisation.

(c) Equity Securities and Derivative Instruments that are traded in active markets—Listed equity securities and derivative instruments that are traded in active markets shall be measured at fair value as at the balance sheet date. For the purpose of calculation of fair value, the lowest of the last quoted closing price of the stock exchanges where the securities are listed shall be taken.

The insurer shall assess on each balance sheet date whether any impairment of listed equity security(ies)/ derivative(s) instruments has occurred.

An active market shall mean a market, where the securities traded are homogenous, availability of willing buyers and willing sellers is normal and the prices are publicly available.

Unrealised gains/losses arising due to changes in the fair value of listed equity shares and derivative instruments shall be taken to equity under the head 'Fair Value Change Account'. The 'Profit on sale of investments' or 'Loss on sale of investments', as the case may be, shall include accumulated changes in the fair value previously recognised in equity under the heading Fair Value Change Account in respect of a particular security and being recycled to Profit and Loss Account on actual sale of that listed security.

For the removal of doubt, it is clarified that balance or any part thereof shall not be available for distribution as dividends. Also, any debit balance in the said Fair Value Change Account shall be reduced from the profits/free reserves while declaring dividends.

The insurer shall assess, at each balance sheet date, whether any impairment has occurred. An impairment loss shall be recognised as an expense in Revenue/Profit and Loss Account to the extent of the difference between the remeasured fair value of the security/ investment and its acquisition cost as reduced by any previous impairment loss recognised as expense in Revenue/Profit and Loss Account. Any reversal of impairment loss, earlier recognised in Revenue/Profit and Loss Account shall be recognised in Revenue/Profit and Loss Account.

(d) Unlisted and other than actively traded Equity Securities and Derivative Instruments—Unlisted equity securities and derivative instruments and listed equity securities and derivative instruments that are not regularly traded in active market will be measured at historical costs. Provision shall be made for diminution in value of such investments. The provision so made shall be reversed in subsequent periods if estimates based on external evidence show an increase in the value of the investment over its carrying amount. The increased carrying amount of the investment due to the reversal of the provision shall not exceed the historical cost.

For the purposes of this regulation, a security shall be considered as being not actively traded, if as per guidelines governing mutual funds laid down from time to time by SEBI, such a security is classified as “thinly traded”.

Loans

Loans shall be measured at historical cost subject to impairment provisions.

The insurer shall assess the quality of its loan assets and shall provide for impairment. The impairment provision shall not be lower than the amounts derived on the basis of guidelines prescribed from time to time by the Reserve Bank of India, that apply to companies and financial institutions.

Catastrophe Reserve

Catastrophe reserve shall be created in accordance with norms, if any, prescribed by the Authority. Investment of funds out of catastrophe reserve shall be made in accordance with prescription of the Authority.

PART II- Disclosures forming part of Financial Statements

The following shall be disclosed by way of notes to the Balance Sheet:

1. Contingent Liabilities:

   (a) Partly-paid up investments

   (b) Underwriting commitments outstanding

   (c) Claims, other than those under policies, not acknowledged as debts

   (d) Guarantees given by or on behalf of the company

(e) Statutory demands/liabilities in dispute, not provided for

(f) Reinsurance obligations to the extent not provided for in accounts

(g) Others (to be specified)

2. Encumbrances to assets of the company in and outside India.

3. Commitments made and outstanding for Loans, Investments and Fixed Assets.

4. Claims, less reinsurance, paid to claimants in/outside India.

5. Actuarial assumptions for determination of claim liabilities in the case of claims where the claims payment period exceed four years.

6. Ageing of claims – distinguishing between claims outstanding for more than six months and other claims.

7. Premiums, less reinsurance, written from business in/outside India.

8. Extent of premium income recognised, based on varying risk pattern, category wise, with basis and justification therefor, including whether reliance has been placed on external evidence.

9. Value of contracts in relation to investments, for:

   (a) Purchases where deliveries are pending;

   (b) Sales where payments are overdue.

10. Operating expenses relating to insurance business: basis of allocation of expenditure to various classes of business.

11. Historical costs of those investments valued on fair value basis.

12. Computation of managerial remuneration.

13. Basis of amortisation of debt securities.

14. (a) Unrealised gain/losses arising due to changes in the fair value of listed equity shares and derivative instruments are to be taken to equity under the head 'Fair Value Change Account' and on realisation reported in profit and loss Account.

    (b) Pending realisation, the credit balance in the 'Fair Value Change Account' is not available for distribution.

15. Fair value of investment property and the basis therefor.

16. Claims settled and remaining unpaid for a period of more than six months as on the balance sheet date.

The following accounting policies shall form an integral part of the financial statements:

1. All significant accounting policies in terms of the accounting standards issued by the ICAI, and significant principles and policies given in Part I of Accounting Principles. Any other accounting policies followed by the insurer shall be stated in the manner required under Accounting Standard AS 1 issued by the ICAI.

2. Any departure from the accounting policies as aforesaid shall be separately disclosed with reasons for such departure.

The following information shall also be disclosed:

1. Investments made in accordance with any statutory requirement should be disclosed separately together with its amount, nature, security and any special rights in and outside India.

2. Segregation into performing/ non performing investments for purpose of income recognition as per the directions, if any, issued by the Authority.

3. Percentage of business sector-wise.

4. A summary of financial statements for the last five years, in the manner as may be prescribed by the Authority.

5. Accounting Ratios as may be prescribed by the Authority.

6. Basis of allocation of Interest, Dividends and Rent between Revenue Account and Profit and Loss Account.

PART III- General Instruction for Preparation of Financial Statements

1) The corresponding amounts for the immediately preceding financial year for all items shown in the Balance Sheet, Revenue Account and Profit and Loss Account should be given.

2) The figures in the financial statements may be rounded off to the nearest thousands.

3) Interest, dividends and rentals receivable in connection with an investment should be stated as gross value, the amount of income tax deducted at source being included under 'advance taxes paid'.

4) Income from rent shall not include any notional rent.

5) (I) For the purposes of financial statements, unless the context otherwise requires -

    (a) the expression 'provision' shall, subject to note II below mean any amount written off or retained by way of providing for depreciation, renewals or diminution in value of assets, or retained by way of providing for any known liability or loss of which the amount cannot be determined with substantial accuracy;

    (b) the expression "reserve" shall not, subject to as aforesaid, include any amount written off or retained by way of providing for depreciation, renewals or diminution in value of assets or retained by way of providing for any known liability;

(c) the expression capital reserve shall not include any amount regarded as free for distribution through the profit and loss account; and the expression "revenue reserve" shall mean any reserve other than a capital reserve;

(d) The expression "liability" shall include all liabilities in respect of expenditure contracted for and all disputed or contingent liabilities.

(II) Where:

(a) any amount written off or retained by way of providing for depreciation, renewals or diminution in value of assets, or

(b) any amount retained by way of providing for any known liability is in excess of the amount which in the opinion of the directors is reasonably necessary for the purpose, the excess shall be treated for the purposes of these accounts as a reserve and not as a provision.

6) The company should make provisions for damages under lawsuits where the management is of the opinion that the award may go against the insurer.

7) Extent of risk retained and reinsured shall be separately disclosed.

8) Any debit balance of Profit and Loss Account shall be shown as deduction from uncommitted reserves and the balance if any, shall be shown separately.

PART IV- Contents of Management Report:

There shall be attached to the financial statements, a management report containing, inter alia, the following duly authenticated by the management:

1. Confirmation regarding the continued validity of the registration granted by the Authority;

2. Certification that all the dues payable to the statutory authorities have been duly paid;

3. Confirmation to the effect that the shareholding pattern and any transfer of shares during the year are in accordance with the statutory or regulatory requirements;

4. Declaration that the management has not directly or indirectly invested outside India the funds of the holders of policies issued in India;

5. Confirmation that the required solvency margins have been maintained;

6. Certification to the effect that the values of all the assets have been reviewed on the date of the Balance Sheet and that in his (insurer's) belief the assets set forth in the Balance-sheets are shown in the aggregate at amounts not exceeding their realisable or market value under the several headings – " Loans", " Investments", "Agents balances", "Outstanding Premiums", "Interest, Dividends and Rents outstanding", "Interest, Dividends and Rents accruing but not due", "Amounts due from other persons or Bodies carrying on insurance business", " Sundry Debtors", " Bills Receivable", " Cash" and the several items specified under "Other Accounts";

7. Disclosure with regard to the overall risk exposure and strategy adopted to mitigate the same;

8. Operations in other countries, if any, with a separate statement giving the management's estimate of country risk and exposure risk and the hedging strategy adopted;

9. Ageing of claims indicating the trends in average claim settlement time during the preceding five years;

10. Certification to the effect as to how the values, as shown in the balance sheet, of the investments and stocks and shares have been arrived at, and how the market value thereof has been ascertained for the purpose of comparison with the values so shown;

11. Review of asset quality and performance of investment in terms of portfolios, i.e., separately in terms of real estate, loans, investments, etc.

12. A responsibility statement indicating therein that:

    (i) in the preparation of financial statements, the applicable accounting standards, principles and policies have been followed along with proper explanations relating to material departures, if any;

    (ii) the management has adopted accounting policies and applied them consistently and made judgements and estimates that are reasonable and prudent so as to give a true and fair view of the state of affairs of the company at the end of the financial year and of the operating profit or loss and of the profit or loss of the company for the year;

    (iii) the management has taken proper and sufficient care for the maintenance of adequate accounting records in accordance with the applicable provisions of the Insurance Act 1938 (4 of 1938) / Companies Act, 1956 (1 of 1956), for safeguarding the assets of the company and for preventing and detecting fraud and other irregularities;

    (iv) the management has prepared the financial statements on a going concern basis;

(v) the management has ensured that an internal audit system commensurate with the size and nature of the business exists and is operating effectively.

13. A schedule of payments, which have been made to individuals, firms, companies and organisations in which Directors of the insurer are interested.

PART V- 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 Accounts separately for fire, marine, and miscellaneous insurance business and separate schedules shall be prepared for Marine Cargo, Marine – Other than Marine Cargo and the following classes of miscellaneous insurance business under miscellaneous insurance and accordingly application of AS 17 – Segment Reporting - shall stand modified. 1. Motor 2. Workmen's Compensation/ Employers' Liability, 3. Public/Product Liability, 4. Engineering 5. Aviation, 6. Personal Accident, 7. Health Insurance, 8. Others

(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............

	Particulars	Schedule	Current Year	Previous Year
			(Rs.'000)	(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 Reserve			
	Transfer to Other Reserves (to be specified)			
	TOTAL (C)			

Note: See Notes appended at the end of Form B-PL

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	Previous Year
		(Rs.'000)	(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			

Notes: to Form B-RA and B- PL

(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, specific claims 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 B-BS

Name of the Insurer: Registration No. and Date of Registration with the IRDA

BALANCE SHEET AS AT 31ST MARCH, 20___.

	Schedule	Current Year	Previous Year
		(Rs.'000)	(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**	**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 EARNED [NET]

Particulars	Current Year	Previous Year
	(Rs.'000)	(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)		

Note: Reinsurance premiums whether on business ceded or accepted are to be brought into account, before deducting commission, under the head reinsurance premiums.

SCHEDULE – 2: CLAIMS INCURRED [NET]

Particulars	Current Year	Previous Year
	(Rs.'000)	(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	Previous Year
	(Rs.'000)	(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	Previous Year
	(Rs.'000)	(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		

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 – 5: SHARE CAPITAL

	Particulars	**Current Year**	**Previous Year**
		(Rs.'000)	(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		
	Less : Calls unpaid		
	Add : Equity 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:
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 o Indian o Foreign				
Others				
TOTAL				

SCHEDULE – 6: RESERVES AND SURPLUS

	Particulars	Current Year	Previous Year
		(Rs.'000)	(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	Previous Year
		(Rs.'000)	(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	Previous Year
	(Rs.'000)	(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. 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. 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 Infrastructure and Social Sector		
5. Other than Approved Investments		
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 control of those policies. Significant influence may be exercised in several ways, for example, by representation on the board of directors, participation in the policymaking 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 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	Previous Year
		(Rs.'000)	(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 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

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, building and property above exclude Investment Properties as defined in note (e) to Schedule 8.

SCHEDULE-11 : CASH AND BANK BALANCES

	Particulars	Current Year	Previous Year
		(Rs.'000)	(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		

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	Previous Year
		(Rs.'000)	(Rs.'000)
	ADVANCES		
1.	Reserve deposits with ceding companies		
2.	Application money for investments		

3.	Prepayments		
4.	Advances to Directors/Officers		
5.	Advance tax paid and taxes deducted at source (Net of provision for taxation)		
6.	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 (including reinsurers)		
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 that term as given under the Companies Act, 1956.

c. Sundry Debtors will be shown under item 9 (others)

SCHEDULE – 13: CURRENT LIABILITIES

Particulars	Current Year	Previous Year
	(Rs.'000)	(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	Previous Year
	(Rs.'000)	(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	Previous Year
		(Rs.'000)	(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
(See Regulation 3)
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 the 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 Authority 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.

Accounting Regulations and Principles for Life Insurance Business

Part V of Schedule A in IRDA Accounting & Audit Regulation provides following guidelines along with the formats of Financial Statements.

1. Revenue Account called as Policyholders' Account, Profit & Loss Account called as Shareholders' Account and the Balance Sheet are to be prepared in the specified formats Form A-RA, Form A-PL and Form A-BS

2. The insurer shall prepare Revenue Account and Balance Sheet for the under-mentioned business separately and to that extent, the application of AS17 stands modified

   (a) Participating policies and Non-participating policies

   (b) Linked Business and Non-linked Business

   (c) Business within India and Business outside India

3. The insurer shall prepare separate Receipts and Payments Account in accordance with the direct method prescribed in Accounting Standard 3 "Cash Flow Statement" issued by the ICAI.

Accounting Principles in Life Insurance Business

Recognition of Income: Premium shall be recognized as income when due. For linked business the due date for payment may be taken as the date when the associated units created. In the Revenue Account (Policyholders' Account) Premium is shown as 'Premium Earned –Net' including Premium collected less Reinsurance Ceded plus Reinsurance Accepted. It requires no adjustment for Premium Reserving on account of un-expired risks, unlike premium accounting in general insurance business. 'Premium collected' comprises a) First Premium, b) Renewal Premium and c) Single Premium

Premium Deficiency: Premium deficiency is to be recognized if the sum of expected claim costs, related expenses and maintenance costs exceeds related unearned premium reserve (UPR). It depends on actuarial valuation. Future value of UPR is to be compared with the sum of expected claim costs, related expenses etc.

Acquisition Costs: Such costs shall be expensed in the period in which they are incurred. In other words if there is any premium received in advance at the end of financial year, the same will be taken as Current Liabilities and Commission or Acquisition Costs thereupon will not be considered as expenses for the said financial year and will be shown as Prepayments or Prepaid Expenditure under the head 'Advances and Other Assets'. Acquisition costs are those costs that vary with and primarily related with acquisition of new and renewal insurance business.

Claim Costs: The ultimate costs of claims shall comprise the Policy benefit amounts and Claim-settlement costs. In Revenue Account for a financial year Policy Benefit Paid (Net) means Insurance Claims comprising the following:

(a) Death Claims

(b) Maturity Claims

(c) Annuities/ Pensions in Payment

(d) Other Benefits including Surrenders and Bonuses in cash

(e) Other Claims Costs

The insurance claims as specified above will be reduced by Amount ceded in Reinsurance and increased by Amounts accepted in Reinsurance to arrive at Benefits Paid to Claimants (Net) for Revenue A/C

Actuarial valuation- Liability For Life policy: The liability of the life policies in force shall be estimated by the Appointed Actuary of the life insurer on the basis of his annual review/ investigation of the life insurance business with certain actuarial assumption. Actuarial assumptions will be disclosed by way of notes to the accounts. The liability shall be so calculated that the said amount together with future premium payments and investment income, the insurer can meet all future claims (including bonus entitlements to policyholders) and expenses. Generally policy liability assessment is based on following assumptions:

Actuarial Assumptions for Policy Liability Assessment

- Actuarial liability of both Participating and Non-participating policies in force at the end of financial year is calculated using Gross Premium Method of valuation.

- The liability calculation is based on the assumption of no change in interest, mortality, morbidity, expenses and inflation rates.

- In case of participating policies, the future bonuses are also taken into account

- An allowance for taxation and allocation of surplus to shareholders is also made.

- All assumptions are made on prudent assessment of future experience at the date of valuation with due consideration for adverse deviation.

- The interest rates used for valuation vary according to the type of plans and the mortality rates used are based on the Published Indian Assured Lives Mortality with due adjustment for expected experience and margin for adverse deviation. Morbidity rates used are based on rates used by international companies with suitable modification therein for their use in India.

- The expenses are considered either as a percentage of premium or sum-assured or per policy or a combination of these

- The unit liability in respect of linked business is taken as the NAV of the units to the credits of policyholders as on the date of valuation.

- The non-unit liability is assessed on Discounted Cash Flow on sample model points. A valuation assumption includes interest rate 5%pa and mortality rate upto 10% duly modified.

Valuation of Investment in life insurance business:

An insurer in life insurance business shall determine the values of investments in the following manner:

Real Estate—Investment Property

- The value of investment property shall be determined at historical cost, subject to revaluation at least once in every 3 years. The change in the carrying amount of the investment property shall be taken to Valuation Reserve Account. The insurer shall assess at each balance sheet date whether any impairment of the investment property has occurred.

- In case of sale of investment property, the profit or loss on sale, as the case may be, shall include accumulated changes in the carrying amount previously recognized under Revaluation Reserve A/C in respect of particular property and being recycled to the relevant Revenue A/C or Profit and Loss Account as the case may be, on sale.

- The bases for valuation shall be disclosed in the notes to the accounts. The IRDA may issue directions on release of any amount from Revaluation Reserve A/C for declaring bonus to policyholders. But except for above as per the Authority's direction, no other amount shall be distributed to shareholders out of Revaluation Reserve Account.

- An impairment loss shall be recognized as an expense in the Revenue or Profit & Loss Account, as the case may be, immediately unless the asset is carried at revaluated amount. Any impairment loss of a revaluated asset shall be treated as a revaluation decrease of that asset and if the impairment loss exceeds the corresponding revaluation reserve, such excess shall be recognized as an expense in Revenue A/c or Profit & Loss Account as the case may be.

Debt Securities

Such securities including Government securities and redeemable preference shares shall be considered as held to maturity securities and shall be measured at historical cost subject to amortization in the following manner for life insurance business;

- Debt Securities including Government Securities, where the book value is more than face value, the premium will be amortized on straight line basis over the balance period of holding /maturity in all cases of business except Unit Linked Plan where all debt security will be shown at market value

- Redeemable Cumulative Preference Shares, where book value is more than face value, the premium will be amortized on straight line basis over the balance period of holding / maturity in all classes of business for ALM

Equity Securities and Derivative Instruments traded in Active Markets:

- Listed Equity Securities and Derivative Instruments that are traded in active markets shall be measured at fair value on the balance sheet date. For the purpose of calculation of fair value, the lowest of the last quoted closing price at the stock exchanges where the securities are listed shall be taken.

- Unrealized gains/ losses arising in the fair value of listed equity shares and derivative instruments shall be taken to equity under the head 'Fair Value Change Account'.

- The 'Profit on Sale of investments' or 'Loss on Sale of investments' as the case may be, shall include accumulated changes in the fair value previously recognized in equity under the head 'Fair Value Change Account' in respect of a particular security and being recycled to the relevant Revenue Account or Profit and Loss Account on actual sale of that listed security.

- The IRDA may issue directions specifying the amount to be released from the 'Fair Value Change Account' for declaring bonus to the policyholders. Except for the above, no other amount shall be distributed to shareholders out of Fair Value Change Account. Also, any debit balance in Fair Value Change Account shall be reduced from profit / free reserves while declaring dividends

- The insurer shall assess on each balance sheet date whether any impairment of listed equity security or derivative instrument has occurred

- An impairment loss shall be recognized as an expense in Revenue/ Profit and Loss Account to the extent of the difference between the re-measured fair value of the security / investment and its acquisition cost as reduced by any previous impairment loss recognized as expense in Revenue/ Profit and Loss Account.

- Any reversal of impairment loss earlier recognized in Revenue/Profit& Loss Account shall be recognized in Revenue /Profit& Loss Account.

- Fair Value Change Account (Credit) is shown in Balance Sheet as Sources of Funds under sub-heads of Shareholders Funds and Policyholders' Funds to the their respective portions.

Unlisted & Not actively traded Equity Securities & Derivatives Instruments

Such securities or instruments unlisted or listed but not traded regularly in active markets shall be measured at historical cost. For diminution in value of such instruments, proper provision shall be made. If estimated based on external evidence show an increase in the value, the provision so made may be reversed. The increased carrying amount of investment due to the reversal of provision shall not exceed the historical cost.

Loans

Loans shall be measured at historical cost subject to impairment provision on prudential norms. After assessment of quality of loans, the impairment provisions shall not be less than the aggregate amount of such loans, which are subject to defaults of following nature

(i) Interest remaining unpaid over a period of six months

(ii) Installments falling due and remaining unpaid over a period of last six months

Investment for Linked Business

The Accounting principles used for valuation of investments are to be consistent with the principles discussed above. A separate set of financial statements for each segregated fund of the linked businesses, shall be annexed.

- Segregated funds represent funds maintained in accounts to meet specific investment objectives of the policyholders who bear the investment risk.

- Investment income/ gains and losses accrue to the specific policyholders.

- The assets of each account are not subject to claims that may arise out of any other business of such insurer.

IRDA (Assets, Liabilities and Solvency Margin of Insurers) Regulation 2000

Solvency Analysis: Its Need

Solvency margin is the excess of assets over liabilities that an insurer is required to maintain at the prudential measure and with statutory limits for the interests of the shareholders. It is akin to the capital adequacy ratio for banks. The insurers are under pressure of maintaining solvency margin at 1.5 per cent being the statutory requirement. Solvency is the ability of an insurer to pay its claims. This section deals with these regulations in brief. Solvency analysis of insurance company is one of the primary functions of insurance regulator in the open. The solvency margin measures have been structured by the IRDA in specific regulations for life insurance business and non-life insurance business separately. All companies carrying on insurance business are always required to maintain required solvency margin laid down by the regulator in the country. The solvency margin is analyzed by the regulator and other financial analysts concerned by comparing the available solvency margin (ASM) of the company with the required solvency margin (RSM) to be determined as per norms set by the Regulator according to nature and volume of business.

Available Solvency Margin (ASM)

Available solvency margin means the excess of value of assets (to be determined as per norms set by the regulator in specified form) over the value of liabilities. In India, life insurance companies are to apply IRDA Form AA for valuation of assets and IRDA Form H for valuation of liabilities in case of life business and IRDA form HG subject to adjustments as shown in Table 111 of Form KG for general insurance business.

Required Solvency Margin (RSM)

Computation of RSM varies with nature and volume of insurance business. Life insurer is required to determine the required solvency margin according to nature and volume of business in the process and Form K as specified under IRDA (Actuarial Report and abstract) Regulations 2000. General insurer is required to determine the required solvency margin in view of the nature and volume of business and the respective incurred claim as RSM-1 and RSM-2 for final RSM being higher of the two.

IRDA Guidelines on Solvency Margin Calculation & Analysis

Statement of Value of Assets

Every insurer shall prepare a statement of the value of assets in Form IRDA-Assets-AA in accordance with Schedule 1 of the said Regulation.

Determination of Amount of Liabilities

Every insurer shall prepare a statement of the amount of liabilities in accordance with Schedule IIA, in respect of life insurance business, and in Form HG in accordance with Schedule II-B, in respect of general insurance business, as the case may be.

Determination of Solvency Margin

Every insurer shall prepare a statement of solvency margin in accordance with Schedule III-A, in respect of life insurance business, and in Form KG in accordance with Schedule III-B, in respect of general insurance business, as the case may be.

Health Insurance Business Determination of Liabilities

Where the insurer transacts health insurance business, providing health covers, the amount of liabilities shall be determined in accordance with the principles specified under these Regulations.

Business outside India

Where the insurer transacts insurance business in a country outside India, and submits statements or returns or any such particulars to a public authority of that country, he shall enclose the same along with Forms specified in accordance with these Regulations and the IRDA (Actuarial Reports and Abstracts) Regulations, 2000.

Furnishing Forms

The forms namely Form AA (Assets), Form HG, Form KG shall be furnished separately to IRDA for business within India and total business transacted by the insurer (see Table-5).

Valuation of Assets

As per IRDA regulations, the assets will be valued as per the instruction content in schedule I to the related regulations.

Following assets should be placed with the value 0:

- Agent balances and o/s premium if not realized within 30 days
- Sundry debts not realizable
- Advances not realizable
- Furniture, Fixtures, dead stock and stationery
- Differed expenses
- Profit & Loss Account balance & Fictitious assets
- Reinsurance balances outstanding or more than three months
- Preliminary expenses for the formation of company

Valuation of computer equipment including software shall be computed as under:

- 75 per cent of its cost in the year of purchase
- 50 per cent office cost in the second year
- 25 per cent office cost in the third year
- 0 per cent thereafter

All other assets of an insurer have to be valued in accordance with the IRDA Regulations 2000 on preparation of financial statements and auditor's report.

Table-5 Statement of Assets–AA

Item No.	Category of Asset	Policyholders' Fund (Rs. In Lac)	Shareholders' fund (Rs. In Lac)
1	Approved Securities		
2	Approved Investments		
3	Deposits		
4	Non Mandated Investments		
5	Other Assets		
6	Total		
7	Fair Value Change Account		
8	Adjusted Value of Assets		

Valuation of Liabilities

The form and procedure for valuation of liabilities are different in life and non-life insurance companies. Liabilities in a life insurance company is valued for solvency analysis purpose as per Schedule 11-A and liabilities in a non-life insurance company is valued as per Schedule 11-B.

Valuation of Liabilities in Life Insurance Companies—Certain important aspects

- Mathematical results shall be determined separately for each contract by a prospective method of valuation.
- The valuation method shall take into account all prospective contingencies under which any premium (by the policyholder) or benefits to the policyholder may be payable under the policy.

- It also takes into account the cost of any options available to the policyholder.
- Determination of liability under each policy shall be based on prudent assumption and insurer expected experience which will improve appropriate margin of adverse deviation.
- The amount of mathematical result in respect of a policy determined in accordance with the above rule may be negative or less than the guaranteed surrender value (to be called as guaranteed surrender value deficiency reserve).
- The valuation shall be called Gross Premium Method (GPM) and may result in the increase in the amount of mathematical results.

Valuation of Liabilities in Non-Life Insurance Companies

A non-life insurer shall place a proper value in respect of the following items:

- Provision for bad and doubtful debts,
- Reserve for dividends declared/recommended, and outstanding dividends in full,
- Amount due to insurance companies carrying on insurance business, in full,
- Amount due to sundry creditors, in full,
- Provision for taxation, in full, and
- Foreign exchange reserve.

He shall determine the amount of following reserves, in manner specified herein below for each reserve:

- **Reserve for unexpired risks**, shall be, in respect of,
  - o Fire business, 50 per cent,
  - o Miscellaneous business, 50 per cent,
  - o Marine business other than marine hull business, 50 per cent; and
  - o Marine hull business, 100 per cent, of the premium, net of reinsurances, received or receivable during the preceding twelve months;
- **Reserve for O/S claims shall be determined in the following manner**:
  - o where the amounts of outstanding claims of the insurers are known, the amount is to be provided in full,
  - o where the amount of outstanding claims can be reasonably estimated according to the insurer, he may follow the 'case by case' method after taking into account the explicit allowance for changes in the settlement pattern or average claim amounts, expenses and inflation.
- **Reserves For Claims Incurred but not Reported (IBNR)**
  - o IBNR shall be determined using actuarial principles.
  - o For such determination the appointed Actuary shall follow the Guidance Notes issued by Actuarial Society of India with concurrence of the IRDA.

Calculation of Required Solvency Margins in Life Insurance Companies

Table-6: Computation of RSM Based on Mathematical Reserve

Item	Mathm. Reserve before Reinsurance	Mathm. Reserve after Reinsurance	Sum at Risk before Reinsurance	K1	Sum at Risk before Reinsurance	Sum at Risk after Reinsurance	K2	First Factor	2nd Factor	RSM
1	2	3	4	5	6	7	8	9	10	11
Non-Linked Business:										
Individual Business:										
01: Life Business								4%	0.3%	
02: General Annuity								4%	0%	
03: Pension								4%	0%	
04: Health								4%	0%	
Group Business:										
Life: Prem. guaranteed for										
05: not more than one year								1%	0.2%	
06: more than one year								3%	0.3%	
07: General Annuity								4%	0%	
08: Pension								4%	0%	
Linked Business:										
Individual Business:										
Life Business -										
11: With guarantees								2%	0.2%	
12: Without Guarantees								1%	0.3%	
General Annuity										
13: With guarantees								2%	0%	
14: Without guarantees								1%	0%	

Pension:										
15: With guarantees								2%	0%	
14: Without guarantees								1%	0%	
Group Business:										
Life Business -										
15: With guarantees								2%	0.3%	
16: Without Guarantees								1%	0.2%	
General Annuity										
17: With guarantees								2%	0%	
18: Without Guarantees								1%	0%	
Pension:										
19: With guarantees								2%	0%	
20: Without guarantees								1%	0%	
Health Insurance										
Individual Business:										
Linked Business										
21: With Guarantees								2%	0%	
22: Without guarantees								1%	0%	
23: Non-Linked Business								4%	0%	
Group Business										
Linked										
24: With Guarantee								2%	0%	
25: Without guarantee								1%	0%	
Non-Linked										
26: Premiums guarantees for not more than year								1%	0%	
27: Premium guarantees for more than one year								3%	0%	

(i) K-1= 0.85 0r (Math Reserve after Reins. or Math Reserve before Reins.) whichever is higher.
(ii) K-2 = 0.5 or (Sum at Risk after Reins./ Sum at risk before Reins) whichever is more.
(iii) RSM or Col.11 == [Col.2 x Col.4 x Col.8 + Col.5 x Col.7 x Col.9]

Table-7: Computation of RSM Based on Assets of Policyholders Funds

Category of assets	Notes	Amt. in balance sheet	3rd factor %	RSM
1	2	3	4	5
Non Mandated Investments				
Corporate Bonds 01. AAA or Equivalent 02. AA or Equivalent 03. A or Equivalent 04. BBB or Equivalent 05. BB or Equivalent 06. B or Equivalent 07. Lower than B 08. Unrated				
Mortgages 09. Residential 10. Commercial				
Real Estate 11. Residential 12. Commercial				
Preference Shares 13. Listed Preference Shares 14. Unlisted Preference Share				
Equity 15. Listed Ordinary Shares 16. Unlisted Ordinary Shares				
TOTAL				

Col. 5 = Col.3 x Col.4, Col.4 = Factor intimated by IRDA

Table-8: ASM and RSM Ratio in Life Insurance Company

	Description	Note	Adjusted Value
1	Available Assets in the Policy holders' Funds (Form AA)		
	Deduct:		
2	Mathematical Reserves (As per Form H)		
3	Other Liabilities (As per Balance Sheet)		
4	Excess in Policyholder's Funds (1-2-3)		
5	Available Assets in Shareholders' Funds		
	Deduct:		
6	Other Liabilities of Shareholders' Funds		
	(As per B/S)		
7	Excess in Shareholders' Funds (5-6)		
8	Total ASM (4+7)		
9	Total RSM		
10	Solvency Ratio (ASM/ RSM)		

Solvency Analysis in Non-life Insurance Company

Solvency Analysis in non-life insurance company is a comparative study between Available solvency Margin and Required Solvency Margin as discussed earlier. Let us now see how ASM and RSM will be determined. RSM is higher of: a) RSM-1; and b) RSM-2, ii) RSM-1 is based on Premium Collection and RSM-2 is based incurred Claims. All these aspects are specified in following briefs:

- Solvency Margin = ASM/RSM
- RSM = Higher of RSM-1 and RSM-2
- RSM-1 = Based on Net Premium

- RSM-2 = Based on Incurred Claims

A. **ASM =** Excess of Policyholders' Fund + Excess of Shareholders' Fund

B. Computation of RSM-1 & RSM-2

Table-9 RSM Based on Net Premium & Net Incurred Claim

	Class of Business	Gross Prem.	Net Prem.	Gross I/Claim	Net I/Claim	RSM-1	RSM-2	RSM
1	Fire							
2	Marine Cargo							
3	Marine Hull							
4	Motor							
5	Engineering							
6	Aviation							
7	Liability							
8	Rural Ins.							
9	Others							
10	Health Ins.							
	Total							

RSM-1 in Table-9 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. Precisely 20 per cent of amount, which is higher of gross premium multiplied by specified factor and Net Premium.

RSM-2 in Table-9 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 Net Incurred Claims. Precisely 30 per cent of amount which is higher of Gross Incurred Claim multiplied by specified factor and Net Incurred Claim.

Table-10 Factor A & Factor B

	Class of Business	Factor A	Factor B
1	Fire	0.5	0.5
2	Marine Cargo	0.7	0.7
3	Marine Hull	0.5	0.5
4	Motor	0.85	0.85
5	Engineering	0.5	0.5
6	Aviation	0.9	0.9
7	Liability	0.85	0.85
8	Rural Ins.	0.5	0.5
9	Others	0.7	0.7
10	Health Ins.	0.85	0.85

Table-11: ASM and RSM Ratio

Item	Description	Amount
1	Available Assets in Policyholders' Fund	
2	Less: Liabilities	
3	Other Liabilities	
4	Excess in Policyholders' Funds (1-2-3)	....
5	Available Assets in Shareholders' Funds	
6	Less: Other Liabilities	
7	Excess in Shareholders' Funds (5-6)	....
8	Total ASM (4+7)	....
9	Total RSM	....
10	Solvency Ratio = ASM: RSM	

Insurance Surveyors and Loss Assessors (License, Professional Requirements and Code of Conduct) Regulations, 2000

In exercise of the powers conferred by Sections 42D, 64UM and 114A of the Insurance Act, 1938 and Section 26 of the Insurance Regulatory and Development Authority Act, 1999, the Authority (IRDA), in consultation with the Insurance Advisory Committee, has made the regulation.

Licensing Procedure

An individual who intends to act as a surveyor and loss assessor in respect of General insurance business shall apply in the specified form to the IRDA for grant of license. The Authority shall satisfy itself that the applicant is a fit and proper person to be granted a license taking into consideration the following aspects in view of the duties, responsibilities and functions of surveyor and loss assessor:

- The applicant shall satisfy all the applicable requirements of section 64UM read with section 42D of the Act and rule 56A of the Insurance Rules, 1939

- The applicant shall have to possess such technical qualifications as may be specified by the Authority from time to time.

- He shall furnish evidence of payment of fees for grant of license, depending upon the categorization

- He has undergone a period of practical training, not exceeding 12 months, as contained in the regulations.

The Authority on being satisfied with the above-noted aspects shall grant the license together with an identity card mentioning the particular class or category of general insurance business namely, fire, marine cargo, marine hull, engineering, motor, miscellaneous and loss of profit insurances and the license shall remain valid for a period of 5 years from the date of issue thereof, unless cancelled earlier.

Duties and Responsibilities of a Surveyor

A surveyor and loss assessor shall investigate, manage, quantify, validate and deal with losses arising from any contingency, and report thereon, and carry out the work with competence, objectivity and professional integrity by strictly adhering to the code of conduct expected of such surveyor and loss assessor. To perform such duties and responsibilities, he shall:

- survey and assess the loss on behalf of insurer or insured and declaring whether he has any interest in the subject-matter in question or whether it pertains to any of his relatives, business partners;

- maintain confidentiality and neutrality without jeopardizing the liability of the insurer and claim of the insured;

- conducting inspection and re-inspection of the property suffering a loss;

- examine, inquire, investigate, verify and check the causes and the circumstances of the loss in question including extent of loss, nature of ownership and insurable interest;

- conduct spot and final surveys and comment upon admissibility of claim;

- estimate, measure and determine the quantum of the subject under loss;

- advise the insurer and the insured about loss-minimization, loss control, loss prevention, and safety measures, wherever appropriate, to avoid further losses;

- comment on the admissibility of the loss with reference to terms, warranty, conditions of the policy and assessing liability under the contract of insurance;

- recommend applicability of depreciation and the quantum of depreciation;
- point out discrepancy, if any, in the policy wordings;
- satisfy queries of the insured/insurer and of persons connected thereto in respect of the claim;
- give reasons for repudiation of claim, in case the claim is not covered by policy terms and conditions;
- take expert opinion, wherever required;
- comment on salvage and its disposal wherever necessary; and
- submit his report to the insurer as expeditiously as possible, but not later than 30 days of his appointment; Provided that in exceptional cases, the afore-mentioned period can be extended with the consent of the insured and the insurer.

Categorization of Surveyors

The insurers appoint surveyors for survey and loss assessment for various kinds and quantum of accidental losses on the basis of the category of survey as granted by the IRDA to the surveyors on the basis of specified criteria. Every surveyor and loss assessor whether a company or firm or an individual, shall be eligible to carry on the work as a surveyor or loss assessor, as per the categorization specified in the license. The categorization shall consist of allocation of one or more specified departments of insurance business, based on the following factors and shall include categorization of the surveyors and loss assessors into three categories, viz., Category A, Category B and Category C. The following are the criteria in this regard:

- Professional qualifications;
- Training undergone;

- Experience as surveyor and any other relevant professional experience; and
- Any other criteria, as may be specified by the Authority from time to time.

The categorization is done and reviewed by the authority from time to time on the basis of a point system developed by the Authority for the purpose.

Code of Conduct

Every surveyor and loss assessor shall:

- behave ethically and with integrity in the professional pursuits. Integrity implies not merely honesty but fair dealings and truthfulness;
- strive for objectivity in professional and business judgment;
- act impartially, when acting on instructions from an insurer in relation to a claim
- conduct himself with courtesy and consideration to all concerned for his work;
- not accept or perform survey works in areas for which he does not hold a license;
- not to accept or perform work which he is not competent to undertake.
- carry out his professional work with due diligence, care and skill and with proper regard to technical and professional standards expected of him;
- keep himself updated with all developments relevant to his professional practice;
- maintain proper record for work done by him and comply with all relevant laws;

- assist and encourage his colleagues to obtain professional qualifications, and, in this behalf, provide free article-ship / practical training for a period of twelve months;
- maintain a register of survey work for relevant information, in FORM-IRDA-11
- keep important records of the survey reports, photographs and other important documents for a period three years and furnish the same and such other specified returns, as and when called for by the Authority or the insurer;
- disclose to all parties concerned his appointment, where the acceptance or continuance of such an engagement may materially prejudice or materially affect the interests of any interested party.
- notify all interested parties immediately and seek instructions for his continuance if a conflict of interest is foreseen,
- not to disclose any information, pertaining to a client or employer or policy holder acquired in the course of his professional work, to any third party, except, where consent has been obtained from the interested party, or where there is a legal right or duty enjoined upon him to disclose; and
- not use any confidential information acquired or received by him in the course of his professional work, to his personal advantage or the advantage of a third party.

IRDA (Licensing of Insurance Agents) Regulations 2000

Insurance License

An insurance agent must hold valid license issued by the Authority under these regulations to act as an insurance agent. The insurance agent may be either insurance agent for life/non-life sector or Composite Agent. In order to obtain or renew license a person is to make an application in the prescribed form to the designated person in the insurer, who is normally in-charge of marketing operations as specified by an insurer and authorized by the Authority to issue or renew license under regulations. The application form applicable to an individual is different from that applicable for a corporate agent including firm or a company. To act as a Composite Agent (for life and general insurers) the applicant shall make two separate applications.

Issue or Renewal of License

The designated person on the receipt of the application in the specified form along with the evidence of payment of fees to the Authority and on satisfied that the applicant has complied with the following requirements may grant or renew license in the prescribed form along with the Identity card in the specified form. The requirements to be complied with by the applicant:

- Possessing the qualifications as specified in Regulation 4 (12^{th} Standard or 10^{th} Standard depending on the place with population);

- Completing the practical training as specified under Regulation under Regulation 5 for 100 hours in general and 50 hours in a case of a CA, ICWA or CS;

- Passing the examination as specified under Regulation 6;

- Possessing the requisite knowledge to solicit and procure insurance business; and

- Providing necessary service to policyholders.

Code of Conduct

An insurance agent must adhere to the code of conduct as specified in Regulation 8 and shall:

(a) Identify himself and the insurance company of whom he is an agent;

(b) Disclose his license to the prospect on demand;

(c) Gather requisite information on insurance products offered and consider the same for recommending a specific insurance plan in view of needs of the prospect;

(d) Disclose the scale of commission on the insurance product offered for sale;

(e) Indicate the premium to be charged by insurer for the insurance product to be sold;

(f) Explain to the prospect the nature and importance of information required;

(g) Bring to the notice of the insurer any adverse habits or income inconsistency of the prospect in a report called Agent's Confidential Report along with proposal;

(h) Inform the prospect promptly about the acceptance or rejection of the proposal;

(i) Obtain requisite documents required by for filling proposal with insurer;

(j) Render necessary assistance to the insured/ claimants in settlement of claims; and

(k) Advise policyholder to effect nomination, assignment, change of address etc.

No Insurance Agent shall:

(a) Solicit or procure business without holding valid license;

(b) Induce the prospect to omit any material information;

(c) Induce the prospect to submit wrong information in the proposal form;

(d) Interfere with any proposal introduced by any other insurance agent;

(e) Offer different rates and terms other than those offered by insurer; and

(f) Force the policyholders to terminate the existing policy and get a new one.

IRDA (General Insurance–Reinsurance) Regulations 2000 with Reinsurance Accounting Norms

Reinsurance is insurance for insurance companies. It is a transfer of part of the risks that a direct insurer assumes by way of primary insurance contract, to a second insurance carrier called Reinsurer. For such transfer, the reinsured and the reinsurer as per treaty or facultative arrangements share premium and claims. The reinsured also earns commission from reinsurers for his ceding premium with reinsurers at various rates and terms. The reinsured and reinsurers settle balances as per statement of accounts recording all incomes and expenditures being shared by them as per treaty or facultative contracts. The Insurance Act makes it obligatory on the part of the Indian reinsurers to enter into reinsurance contracts with Indian reinsurer. Section 101A of the Act lays down that every insurer shall reinsure with Indian reinsurers such percentage of the sum-insured on each policy as may be specified by IRDA.

Outward Reinsurance & Reinsurance Programme

1. Every company must have a reinsurance policy or programme for which the following procedures need to be followed as per regulatory guidelines;

2. Reinsurance programme of a reinsurer shall be guided by the following objectives;

    - To maximize retention within the country

- To develop adequate capacity
- To secure the best possible protection for the reinsurance costs incurred
- To simplify the administration of business

3. The insurers shall maintain the maximum possible retention commensurate with its financial strength (capital and reserve) and volume of business. They have to justify their retention policy to the IRDA and ensure that they are not fronting for a foreign reinsurer.

4. The insurer shall cede such percentage of the sum-insured on each policy for different classes of business written in India to the Indian Reinsurer as may be prescribed by IRDA;

5. The reinsurance programme shall commence from the beginning of every financial year and the insurers shall submit to the IRDA their reinsurance programmes 45 days before the commencement of the financial year;

6. The insurer shall file with the IRDA within 30 days of the commencement of the financial year a philosophy of every reinsurance treaty slip and XL Cover note in respect of that financial year and the list of reinsurers with their shares in the arrangement.

7. The insurer is to submit such information or explanations as may be required by the IRDA, which may issue necessary directions thereon;.

8. Insurers shall place their reinsurance business outside India with only those reinsurers, who have over a period of past five years, enjoyed a rating of at least BBB (as per S&P or equivalent international rating agency.

9. Reinsurers shall organize domestic pool of reinsurance for reinsurance surpluses in fire, marine and other classes in consultation with all insurers on the basis of limits and terms

being fair to all insurers and assist in maintaining retention in India. Such arrangement is to be approved by the Authority;

10. Surplus over the domestic reinsurance arrangement in the form of pool as mentioned above can be placed by the insurer independently with any reinsurer outside India complying with the requirements stated in point-7 above and subject to a limit of 10% of the total reinsurance premium ceded outside India;

11. Every insurer shall offer an opportunity to Indian insurers and Indian reinsurer to participate in its facultative and treaty surpluses before placement of such business outside India;

12. The Indian Reinsurer shall retrocede at least 50 per cent of the obligatory cessions received by it to the ceding insurers after protecting the portfolio by suitable XL cover. Such retrocession shall be at original terms plus an overriding commission of 2.5 per cent. The retrocession to each company ceding company shall be in proportion of its cessions to the Indian reinsurer; and

13. Insurers shall submit to the IRDA statistics of reinsurance transactions in the prescribed format together its annual accounts.

Inward Reinsurance

Every insurer desiring to write inward reinsurance business shall have well-defined underwriting policy for writing inward reinsurance transactions. The insurer shall ensure that such decision on acceptance of reinsurance business is taken by persons with necessary knowledge and experience. The insurer shall file with the Authority a note on its underwriting policy stating the classes of business, geographical area, underwriting limits and profit objective. He shall also file changes if any made to the note or the underwriting policy.

Outstanding Loss Provisioning

Every insurer shall provide for every reinsurance arrangement accepted on the basis of loss information advices received from brokers or cedants and where such advices are not received, on an actuarial estimation basis. In addition, the insurer shall make an appropriate provision for incurred, but not reported (IBNR) claims on its reinsurance accepted portfolio on actuarial estimation basis.

IRDA (Life Insurance - Reinsurance) Regulations 2000

Reinsurance Programme and Regulator's Prescriptions:

- Every life insurer shall draw up a programme of reinsurance in respect of lives covered by him.

- The profile of such programme duly certified by the Appointed Actuary, which shall include the names (s) of the proposed reinsurers (s), shall be filled by the insurer with the IRDA, at least 45days before commencement of each financial year.

- The insurer shall furnish the additional information as the IRDA may call for from time to time for the scrutiny of the programme and necessary changes.

- The Authority shall scrutinize such a programme of reinsurance as referred to above and may suggest changes, if it considers necessary and the insurer shall incorporate such changes forthwith in his programme.

- Every insurer shall retain the maximum premium earned in India commensurate with his financial strength and volume of business.

- The reinsurer selected by the insurer, shall enjoy a credit-rating of minimum 'BBB' of S&P or equivalent rating of any international rating agency.

- The placement of business by the insurer with any other reinsurer shall be with prior approval of the Authority.

- No reinsurance programme shall be on original premium basis unless the Authority approves such programme.

- No life insurer shall have reinsurance arrangement with the promoter company or its associate or group company, except on terms which are commercially competitive in the market and with the prior approval of the Authority.

- Every insurer shall submit to the authority statistics relating to reinsurance transactions in prescribed format together with the annual accounts.

IRDA (Third Party Administrator — Health Services) Regulations 2001

TPA Licensing – Its Conditions

A Third Party Administrator (TPA) being licensed by the Authority is engaged for a fee or remuneration for provisions of health services as per agreement with an insurer. Licensing of TPA is subject to following conditions and procedures:

- Only a company with share capital and registered under the Companies Act, 1956 can function as TPA;

- The primary object of the company shall be to carry on business in India as a TPA in health services after being licensed by the Authority;

- The minimum paid-up capital in equity shares of the company shall be Rs 1 crore;

- The company shall maintain the minimum working capital up to Rs 1 crore always;

- At least one of the directors shall be a qualified medical doctor registered under medical council of India;

- The aggregate holding of equity shares by a foreign company shall not exceed 26 per cent of the paid-up capital; and

- Any transfer of shares exceeding 5 per cent of the paid-up capital shall be intimated to IRDA.

TPA Licensing – Its Procedures

- The TPA shall make an application in the specified form together with non-refundable fee of Rs 20,000 to obtain from the IRDA a license to function as a TPA for rendering health services;

- The applicant shall furnish such information or such documents as may be called for by the Authority in course of examination of the application;

- The Authority after being satisfied on examination of the application and documents may issue a license to the applicant to function as a TPA;

- The TPA approved by the Authority shall pay a further sum of Rs 30,000 as license fee;

- A copy of the agreement entered between the TPA and an insurer any modification therein shall be filed with the Authority within 15 days of execution or modification;

- An insurer can engage by agreements more than one TPA for health services; and

- Every agreement shall describe the scope of services, facilities to be provided and about remuneration to be paid.

Administration of TPA Services

- Every TPA shall appoint with due intimation to the Authority, from among its directors or senior employees, a Chief Administrative Officer (CAO) or Chief Executive Officer (CEO), who shall be responsible for the proper day to day administration of the activities of the TPA;

- Such CAO or CEO shall posses such educational qualifications and undergo a training with such institute as specified in the regulations;
- Educational qualifications include a degree in Arts, Science, Commerce, Management, Health or Hospital Management or Medicine and pass Associateship Examination of the Insurance Institute of India'
- Every license granted by the TPA or any renewal thereof shall remain in force for three years unless the Authority revokes or cancels it earlier; and
- A license granted by TPA may be renewed for a further period of three years on submission of renewal application along with a renewal fee of Rs 30,000.

IRDA (Protection of Policyholders' Interests) Regulations, 2002

Sale of Insurance Policy

In the process of sale of insurance policy, the insurer or its agent or any intermediary shall act according to the code of conduct prescribed by: i) the IRDA; ii) the Councils that have been established under Section 64C of the Insurance Act, 1938; and iii) the recognized professional body or association of which the agent or intermediary or insurance intermediary is a member. Section 64C provides that there will be two Councils of the Insurance Association of India: i) The Life Insurance Council; and ii) The General Insurance Council. Such councils shall consist of all members and associate members who carry on insurance business in India. Sale of insurance policy shall be subject to compliance of the requirements are discussed below.

Proposal for Insurance

As per Regulation 2 proposal means a form to be filled in by the proposer for insurance, for furnishing all material information required by the insurer in respect of risk, in order to enable the insurer to decide whether to accept or decline, to undertake the risk and in the acceptance of risk, to determine the rates, terms, and conditions of cover to be granted. Thus the proposal for insurance is the foundation of formation of an insurance contract. A proposal for grant of an insurance cover whether in life insurance or general insurance must be evidenced by a written document. It is the duty of an insurer to furnish a copy of the proposal to the insured free of charge, within 30 days of the acceptance of a proposal. However in marine insurance contracts there is no practice for a written proposal form. Forms and contents of proposal forms depend on the circumstances of each case. As the insurance contract is based on utmost good faith as explained in the first chapter, the proposer is required to disclose all material facts that impact the judgment of the insurer to accept the risks and decide the rates, terms and conditions of the cover granted.

Requirements at the Point of Sale

- **A Prospectus:** There must be a prospectus i.e. a document issued by the insurer to the prospective buyers of insurance and should contain such particulars as are mentioned in Rule 11 of the Insurance Rules, 1939 and includes a brochure or leaflet serving the purpose. Such document shall specify the type and character of riders on the main product state clearly the nature of benefits, the extent of cover and explain the warranties, exceptions and conditions of the insurance cover. The allowable riders on the product shall be clearly spelt out with regard to their scope of their benefits.

- **Material Information:** An insurer or its agent or other intermediary shall provide all material information in respect of a proposed cover to the prospect to enable the prospect to decide on the best cover that would be in his/her interest.

- **Dispassionate Advice:** Where the prospect depends upon the advice of the insurer or his agent or an insurance intermediary, such a person must advise the prospect dispassionately.

- **Filling Proposal for Insurance:** Where for any reason, the proposal and other connected papers are not filled by the prospect, a certificate may be incorporated at the end of proposal form from the prospect that the contents of the form and documents have been fully explained to him and that he has fully understood the significance of the proposed contract.

- **Code of Conduct:** In the process of sale, the insurer or agent or any intermediary shall act according to the code of conduct prescribed by:

  - the IRDA

  - the Councils established under Sec.64C of the Insurance Act, 1938

  - A recognized professional body or association of which the agent or intermediary is a member

Matters to be Stated in Life Insurance Policy

1. A life insurance policy shall clearly state:

   - The name of the plan governing the policy (its terms and conditions)';Whether it is participating in profits or not;

   - Basis of participation in profits such as cash bonus, deferred bonus, simple or compound reversionary bonus;

   - The benefits payable and contingencies upon which these are payable and other terms and conditions of the insurance contract;

   - Details of the riders attaching to the main policy;

   - Date of commencement of the risk and the date of maturity or the date(s) on which the benefits are payable;

   - Premiums payable, periodicity of payment, grace period allowed for payment of the premium, the date of the last installment of premium, the implication of discontinuing the payment of an installment(s) of premium and also the provisions of a guaranteed surrendered value;

- The age at entry and whether the same has been admitted;
- The policy requirements for (a) conversion of policy into paid up policy, (b) surrender, (c) Non-forfeiture and (d) revival of lapsed policy;
- Contingencies excluded from the scope of the cover, both in respect of the main policy and the riders;
- The provisions for nomination, assignment, loans on security of the policy and a statement that the rate of interest payable on such loan amount shall be as prescribed by the insurer at the time of taking the loan;
- Any special causes or conditions such as first pregnancy clause, suicide clause etc;
- The address of the insurer to which all communications in respect of the policy shall be sent; and
- The documents that are normally required to be submitted by a claimant in support of a claim under the policy.

2. The insurer shall inform by the letter forwarding the policy that he has a period of 15 days from the date of receipt of the policy document to review the terms and conditions of the policy and where the insured disagrees to any of those terms or conditions he has the options to return the policy stating the reasons for his objection, when he shall be entitled to a refund of the premium paid, subject only to a deduction of a proportionate risk premium for the period on cover and the expenses incurred by the insurer on medical examination of the proposer and stamp duty charges.

3. In respect of a unit-linked policy, in addition to the deduction as mentioned above, the insurer shall also be entitled to

repurchase the unit at the price of the units at the date of cancellation.

4. In respect of a cover, where premium charge is dependent on age, the insurer shall insure that the age is admitted as far as possible before issuance of the policy document, in case where age has not been admitted by the time the policy is issued, the insurer shall make efforts to obtain proof of age and admit the same as soon as possible.

Matters to be Stated in General Insurance Policy

1. A general insurance policy shall clearly state:

    - The names and addresses of the insured and of any bank or any other person having financial interest in the subject matter of insurance
    - Full description of the property or the interest insured
    - Location(s) of the property or the interest insured with respective values
    - Period of insurance
    - Sum-insured
    - Perils covered or not covered
    - Any franchise or deductible applicable
    - Premium payable and where the premium is provisional subject to adjustment, the basis of adjustment of premium be stated
    - Policy terms, conditions and warranties
    - Actions to be taken by the insured upon the occurrence of a contingency likely to give rise to a claim under the policy

- Obligations of the insured in relation to the subject matter of insurance upon occurrence of a contingency likely to give rise to a claim under the policy
- Any special conditions attaching to the policy
- Provisions for cancellation of the policy on grounds of misrepresentation, fraud, non-disclosure of material facts or non-cooperation of the insured;
- The address of the insurer to which all communications in respect of the insurance contract should be sent.
- The details of the perils attaching to the main policy
- Proforma of any communication the insurer may seek from the policyholders to service the policy

2. Every insurer shall inform and keep informed periodically the insured on the requirements to be fulfilled by the insured regarding lodging of a claim arising in terms of the policy and the procedures to be followed by him to enable the insurer to settle a claim early.

Claims Procedure in Respect of a Life Insurance Policy

- An insurance policy shall state the documents which are normally required to be submitted by a claimant in support of a claim.
- An insurer, on receiving a claim, shall process the claim without delay. Any queries or requirement of additional documents, to the extent possible, shall be raised all at once and not in a piece-meal manner, within a period of 15 days of the receipt of the claim.
- A claim under a life policy shall be paid or to be disputed giving all the relevant reasons, within 30 days from the date of receipt of all relevant papers and clarifications. However, where in the opinion of the insurance company, the

circumstances of a claim warrant an investigation, it shall initiate and complete such investigation at the earliest, in any case not later than 6 months from the time of lodging claim.

- Subject to the provisions of Section 47 of the Act, where a claim is ready for payment, but the payment cannot be made due to any reasons of a proper identification of the payee, the insurer shall hold the payment for the benefit of the payee and such an amount shall earn interest at the rate applicable to a savings bank account.

- Where there is a delay on the part of the insurer in processing a claim for a reason other than that mentioned above, the insurance company shall pay interest on the claim amount at a rate which is 2 per cent above the bank rate prevalent at the beginning of the financial year in which the claim is reviewed.

Claims Procedure in Respect of a General Insurance Policy

An insured or the claimant shall give notice to the insurer of any loss arising under a contract of insurance at the earliest or within such extended time as may be allowed by the insurer. On receipt of such notice, the insurer shall respond immediately and give clear indication to the insured on the proceedings that he should follow. In cases, where any surveyor has to be appointed for assessing a loss/claim, it shall be so done within 72 hours of the receipt of intimation from the insured.

IRDA (Manner of Receipt of Premium) Regulations, 2002

Manner of Premium Payments

The payment of premium by any person (proposer) proposing to take an insurance policy or by the policyholder to an insurer may be made in any one or more of the following manner(s):

(a) Cash;

(b) Any recognized banking negotiable instrument such as cheques, including demand drafts, pay orders, banker's cheques drawn on any scheduled bank in India;

(c) Postal money orders;

(d) Credit or Debit Cards held in his name;

(e) Bank Guarantee or Cash Deposit;

(f) Internet;

(g) E-transfer;

(h) Direct credits via standing instruction of policyholder through bank transfers; and

(i) Any other method of payment as may be approved by the IRDA from time to time.

Commencement of Risk

In all cases of risks covered by the policies issued by an insurer, the attachment of risk to an insurer will be in consonance with the terms of Section 64VB of the Act and except in the cases where the premium has been paid in cash, in all other cases the insurer shall be on risk only after the receipt of the premium by the insurer, provided that in the case of a policy of general insurance that where the remittance made by the proposer or the policyholder is not realized by the insurer, the policy shall be treated as *void ab-initio*.

Provided further that in the case of a policy of life insurance, the continuance of the risk or otherwise shall depend on the terms and conditions of the policy already entered into.

Recovery of Collection Charges

The insurer may at its option recover collection charges of the instrument from the proposer.

IRDA (Obligation of Insurers to Rural or Social Sector) Regulations 2002

In exercise of the powers conferred by section 32C read with section 32B of the Insurance Act, 1938, the Authority, in consultation with the Insurance Advisory Committee, has made the regulations called the Insurance Regulatory and Development Authority (Obligations of Insurers to Rural Social Sectors) Regulations, 2000.

1. As per Regulation 3 every insurer who begins to carry on insurance business after the commencement of the Insurance Regulatory and Development Authority Act, 1999, shall, for the purposes of sections 32B and 32C of the Act, ensure that he undertakes the following obligations, during the first five financial years, pertaining to the persons in:

(a) Rural sector,

(i) For *a life insurer* —

- 7 per cent in the first financial year;
- 9 per cent in the second financial year;
- 12 per cent in the third financial year;
- 14 per cent in the fourth financial year;
- 16 per cent in the fifth year;

of total policies written direct in that year;

(ii) For a *general insurer*—

- 2 per cent in the first financial year;
- 3 per cent in the second financial year;
- 5 per cent thereafter,

of total gross premium income written direct in that year.

(b) Social sector, for all insurers —

- 5000 lives in the first financial year;
- 7500 lives in the second financial year;
- 10,000 lives in the third financial year;
- 15,000 lives in the fourth financial year;
- 20,000 lives in the fifth year;

In the first financial year, where the period of operation is less than twelve months, proportionate percentage or number of lives, as the case may be, shall be undertaken. In case of a general insurer, the obligations specified shall include insurance for crops. The Authority may once in every five years revise the obligations.

The obligations of existing insurers as on the date of commencement of IRDA Act as decided by the Authority after consultation with them and the quantum of insurance business to be done should not be less than what has been recorded by them for the accounting year ended 31st March 2002. The Authority reviews such quantum of insurance business periodically and gives directions to the insurers for achieving the specified targets.

IRDA (Licensing of Corporate Agents) Regulations, 2002

Scope and Definition

Any of the following persons who hold certificate of licence may act as an insurance agent:

1. A firm
2. A company formed under the Companies Act, 1956
3. A banking company as defined by Section 2 of the Act

4. A corresponding new bank defined by Section 5 of the Banking Companies Act, 1949

5. A regional rural bank established under Section 3 of the Regional Rural Bank Act, 1976

6. A co-operative society or a co-operative bank, registered under the Co-operative Societies Act, 1912

7. A *panchayat* or a local authority

8. A NGO or a micro finance organisation registered under Co-operative Societies Act, 1912 or registered with the Reserve Bank of India as the case may be

9. Any other institution or organisation specifically approved by the Authority.

A person desiring to obtain or renew a licence to act as a corporate agent or a composite corporate agent shall proceed in the following ways:

- To make an application to a designated person in the specified IRDA Form

- To 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.

- To ensure that the corporate insurance executive of the applicant:-

    o possesses the qualifications as specified under Regulation 4;

    o possesses the practical training as specified under Regulation 5;

- o has passed the examination as specified under Regulation 6;
- o has furnished an application complete in all respects;
- o has the requisite knowledge to solicit and procure insurance business; and
- o is capable of providing the necessary service to the policyholders;

- To ensure that a corporate insurance executive of such an applicant shall have completed from an approved institution, at least, one hundred hours' practical training which may be spread over three to four weeks, in either life or general insurance business, as the case may be.

However such practical training period will be reduced to 50 hours where the corporate insurance executive of the applicant, referred to under sub-regulation (1) is:

- Associate/Fellow of the Insurance Institute of India, Mumbai;
- Associate/Fellow of the Institute of Chartered Accountants of India, New Delhi;
- Associate/Fellow of the Institute of Costs and Works Accountants of India, Calcutta;
- Associate/Fellow of the Institute of Company Secretaries of India, New Delhi;
- Associate/Fellow of the Actuarial Society of India, Mumbai;
- Master of Business Administration of any Institution/ University recognised by any State Government or the Central Government; or
- possessing Certified Associateship of Indian Institute of Bankers (CAIIB); or

- possessing any professional qualification in marketing from any Institution/University recognised by any State Government or the Central Government—

In case of training in both life and general insurance, the duration of practical training shall be not less than 150 hours. However, if he falls within one of the above categories, he shall have to complete 50 hours from an approved institution.

Duties and Responsibilities

1. Every corporate agent shall:

   (a) be responsible for all acts, omission and commission of its corporate insurance executive and every specified person;

   (b) ensure that the corporate insurance executive and all specified persons are properly trained, skilled and knowledgeable in the insurance products

   (c) ensure that the corporate insurance executive and the specified person do not make to the prospect any misrepresentation on benefits and returns available under the policy;

   (d) ensure that no prospect is forced to buy an insurance product;

   (e) give adequate pre-sales and post-sales advice to the insured in respect of the insurance product;

   (f) extend all possible help and cooperation to an insured in completion of all formalities and documentation in the event of a claim;

   (g) give due publicity to the fact that the corporate agent does not underwrite the risk or act as an insurer; and

   (h) enter into service level agreements with the insurer in which the duties and responsibilities of both are defined.

Code of Conduct

(i) Every corporate agent or a corporate insurance executive or a specified person shall also follow the code of conduct specified below:

(a) identify himself and the insurance company of whom he is a representative;

(b) disclose his licence/ certificate to the prospect on demand;

(c) disseminate the requisite information in respect of insurance products offered for sale by his insurer and take into account the needs of the prospect while recommending a specific insurance plan;

(d) disclose the scales of commission in respect of the insurance product offered for sale, if asked by the prospect;

(e) indicate the premium to be charged by the insurer for the insurance product offered for sale;

(f) explain to the prospect the nature of information required in the proposal form by the insurer, and also the importance of disclosure of material information;

(g) bring to the notice of the insurer any adverse habits or income inconsistency of the prospect, in the form of a report (called "Insurance Agent's Confidential Report") along with every proposal submitted to the insurer, and any material fact that may adversely affect the underwriting decision of the insurer;

(h) inform promptly the prospect about the acceptance or rejection of the proposal by the insurer;

(i) obtain the requisite documents at the time of filing the proposal form with the insurer; and other documents subsequently asked for by the insurer for completion of the proposal;

(j) render necessary assistance to the policyholders or claimants or beneficiaries in complying with the requirements for settlement of claims by the insurer;

(k) advise every individual policyholder to effect nomination or assignment or change of address or exercise of options, as the case may be, and offer necessary assistance in this behalf, wherever necessary.

(ii) No corporate agent/ corporate insurance executive/ specified person shall:

(a) solicit or procure insurance business without holding a valid licence/ certificate;

(b) induce the prospect to omit any material information in the proposal form;

(c) induce the prospect to submit wrong information in the proposal form or documents submitted to the insurer for acceptance of the proposal;

(d) behave in a discourteous manner with the prospect;

(e) interfere with any proposal introduced by any other specified person or any insurance intermediary;

(f) offer different rates, advantages, terms and conditions other than those offered by his insurer;

(g) demand or receive a share of proceeds from the beneficiary under an insurance contract;

(h) force a policyholder to terminate the existing policy and to effect a new proposal from him within three years from the date of such termination;

(i) No corporate agent shall have a portfolio of insurance business from one person or one organization or one group of organizations under which the premium is in excess of fifty percent of total premium procured in any year;

(j) apply for fresh licence to act as an insurance agent, if his licence was earlier cancelled by the designated person, and a period of five years has not elapsed from the date of such cancellation; and

(k) become or remain a director of any insurance company.

IRDA (Insurance Broker) Regulations 2002

Insurance Brokers and Insurance Business Development

Insurance brokers are one of the most important classes of insurance intermediaries. Their roles and functions have become very vital in the new tariff-free regime of non-life insurance business. Today the major portion of corporate insurance business is controlled and marketed through insurance brokers. The IRDA has issued the regulations called Insurance Regulatory and Development Authority (Insurance Brokers) Regulations, 2002 to develop and regulate the roles of insurance brokers for furtherance of insurance service in India through this very important marketing intermediary in the open market. Insurance agents act for insurers, while brokers work on behalf of clients. Brokers have had duties and responsibilities and Code of conduct in carrying out their professions as per this IRDA regulation. The following persons can be insurance brokers:

- An individual
- A Firm
- A Company
- A Cooperative Society
- Any other person licensed by IRDA

Brokers' Eligibility Criteria

Following are eligibility criteria for being insurance brokers as per regulation:

- **Infrastructure:** Adequate Office Space, equipment, trained manpower
- **Qualification:** At least two persons possess any of the following qualification:
  - Bachelors/Masters degree in Arts, Science or Social Science or Science or its equivalent
  - Bachelors/ Masters degree in engineering or its equivalent
  - Bachelors/ Masters degree in law or its equivalent
  - MBA or its equivalent
  - AIII/ FIII
  - ACA/ FCA
  - AICWA/ FICWA
  - AASI/ FASI
  - AIIB
  - Any other qualification as may be specified by the IRDA from time to time
- **Training:** The principal officer of the applicant received 100 hours theoretical and practical training from an institution recognized by IRDA.
- **Examination**; The principal Officer has passed an examination conducted by the National Insurance Academy, Pune at the end of the above training.

- **Capital:** Minimum Capital for
  - Direct Broker ………..Rs 50,00,000
  - Reinsurance Broker….Rs 2,00,00,000
  - Composite Broker…...Rs 2,50,00,000
- **Professional Liability Insurance:** Compulsory in respect of liability for
  - any error or omission or negligence on his part or the part of his employees and directors
  - any loss of money or other property for which the broker is legally liable
  - any loss of documents and costs or expenses
  - fraudulent activities by broker's employees.
- **Limitation of Business from Single Source:** Business of broker shall not emanate from a single client not more than
  - 50 per cent of the premium in the first year of his business
  - 40 per cent of the premium in the second of his business
  - 30 per cent of the premium from the third year and onwards
- **Maintenance of Records:** Every insurance broker shall prepare the following financial statements:
  - Balance Sheet/Statement of Affairs
  - Profit and Loss Account
  - Cash Flow/Fund Flow
  - Additional Statements

- **Submission of Financial Statements:**

  - Every insurance broker shall submit to the Authority, a copy of the audited financial statements as stated above and the accounts shall be maintained on accrual basis.

  - Every insurance broker shall before 31st October and 30th April each year furnish to the Authority a half yearly un-audited financial statement containing details of performance and financial position.

- **Disclosure**; An insurance broker shall disclose to the Authority as and when required by it within 30 days of requisition the following information;

  - His responsibilities in regard to placement of an insurance contract

  - Any change in the information furnished earlier

  - The names of clients he manages

  - Any other requirement specified by the Authority

Brokers' (Direct) Duties & Responsibilities

- Obtaining detailed information of the client's business and risk management philosophy;

- Familiarizing himself with the client's business and underwriting information;

- Providing services related to insurance consultancy and risk management;

- Rendering advice on appropriate insurance cover and terms;

- Maintaining detailed knowledge of available insurance markets;

- Providing requisite underwriting information;
- Submitting quotation received from insurer/s;
- Acting promptly on instructions from a client and providing him written acknowledgements and progress reports;
- Assisting clients in paying premium under Section 64VB of Insurance Act, 1938;
- Assisting in the negotiation of the claims;
- Maintaining proper records of claims;
- Familiarizing himself with the client's business and risk retention philosophy;
- Rendering advice based on technical data on the reinsurance covers available in the international insurance and the reinsurance markets;
- Maintaining a database of available reinsurance markets, including solvency ratings of individual re-insurers;
- Rendering consultancy and risk management services for reinsurance;
- Exercising due care and diligence at the time of selection of re-insurers and international insurance brokers having regard to their respective security rating and establishing respective responsibilities at the time of engaging their services.
- Selecting and recommending a reinsurer or a group of reinsurers;
- Negotiating with a reinsurer on the client's behalf;
- Acting promptly on instructions from a client and providing it written acknowledgements and progress reports;
- Maintaining clear records of the insurer's business;

- Collecting and remitting premiums and claims within such time as agreed upon;
- Assisting in the negotiation and settlement of claims;
- Maintaining proper records of claims; and
- Assisting in case of commutation of reinsurance contracts placed with them.

Brokers' Code of Conduct

Brokers shall adhere to the recognized professional standards as set out by the Authority in matters relating to:

- Clients relationship
- Sales practices
- Furnishing information
- Exploration of insurance contract
- Renewal of policies
- Claims by client
- Receipt of complaints
- Documentation
- Advertisement
- Receipt of remuneration
- Training
- Rebating
- Adherence to provisions of the Act, Regulations

Guidelines on Insurance and Reinsurance Broking

- A broker shall not block capacity with one or more insurers in anticipation of being invited to quote terms for insurance requirements of a client, where the client has not yet decided as to which brokers should be invited to quote terms.
- Once the client selected the broker to quote terms of insurance requirements, all other brokers should withdraw from the particular business proposal of the client. They should also immediately inform the insurers with whom they are in touch for the purpose, about their not being invited to quote terms.
- Every broker who is invited to quote terms shall obtain a written appointment letter to develop terms. Where the client has given oral instructions to quote, the broker should record the fact in a letter to the client.
- Every broker invited to quote terms should fully comply with Para 4 of the code of conduct. The broker should clearly distinguish between the information provided by the client and information provided by the broker based on his own study risk.
- Where the client has specified the terms of insurance cover required by him, the broker shall develop terms on the basis specified by the client, but not on any other basis. However the broker may discuss with the client and agree with him to develop terms on any other basis.
- The broker may ask more than insurer to quote terms. The broker shall furnish full information on a common basis to all the insurers. This does not prevent the broker from providing.

IRDA Guidelines on "File and Use" Requirements 2006

The **IRDA Guidelines on File and Use** of General Insurance Products effective from October 2006 are briefly discussed below:

General

- Design and rating of products must be on sound and prudent underwriting basis and should provide clear and transparent cover i.e. of value to the insured.

- All literature relating to the product should be in simple language for easy understanding by the public and all technical terms should be sufficiently clarified for understanding by laymen.

- The product should be genuinely an insurance of an insurable risk with a real risk transfer. ART or financial guarantee business in any form will not be accepted.

- The insurance products should comply with the requirements of the IRDA (Protection of Policyholders' Interests) Regulations, 2002.

- The insurers should use similar wordings for same cover or the same requirement across all their products, such as clauses on Basis of Insurance, Renewal of policy, Cancellation of policy, Due diligence clause, Arbitration clause etc.

- The pricing of products should be based on support of the appropriate data and technical justification.

- The terms and conditions of the cover shall be fair between the insurer and the insured.

- Margins built into rates shall be consistent with the experience of the insurer in respect of commission, expenses of management, contingencies and profits.

- Insurer should confirm that it has taken necessary steps to ensure that the competition will not lead unprincipled rate cutting and other improper underwriting practices.

- Insurer shall not vary the scope of coverage or the terms and conditions of the cover or the wordings in respect of cover that are filled and used after approval from authority.

Filing of Products

- Once an insurance product has been filled and IRDA has not raised any query to comply, the insurer is expected to work with that product without making frequent changes to the same. IRDA will not agree to frequent changes without sufficient support and justification.

- Cancellation of cover by the insurer should provide for at least 15 days notice. Policies that are long-term in nature and annual policies that are regularly being renewed every year or where there is a reasonable expectation the annual renewal should not be refused or be cancelled without providing sufficient justification.

- Where any product is governed by rates, terms and conditions that are required by agreement to be followed by all insurers such as terrorism cover, the insurers shall be collectively responsible to ensure compliance with the requirements and guidelines of the file and use of products.

- Products, for which rates and terms and conditions were filled under the earlier file and use guidelines, need not be refined under these guidelines unless the insurers make any change in rate, terms, or conditions of cover of such products.

- When a new product is created which is merely a package of products that have been filled individually and where IRDA has no subsisting query, it is sufficient to file a short statement in this regard.

- Any non-tariff insurances issued in the past on the basis of individually rated risks based on individual experience and risk evaluation without reference to a class product design or rate and which were not filled with IRDA earlier under the earlier file and use" requirement, shall now be filled with IRDA under these guidelines

File and Use Requirements

- No general insurance product shall be sold to any person unless the requirements of the IRDA guidelines have been complied with in respect of that product.

- Where individual particulars of the product are required to be filled with IRDA, such product shall not be sold unless the required particulars have been filled and the IRDA has raised no query in respect of its rates, terms and conditions within a period of 30 days.

- Where the Authority raises query within 30 days of filling, the insurer shall not offer that product for sale, until all queries are satisfactorily complied with and the Authority confirms in writing that it has no further query regarding that product.

- It should be the joint effort of both the insurer and the IRDA to ensure that the entire procedure in regard to requirements of File and Use of products are completed within 60 days.

- If at any time it appears to IRDA that a product being sold by an insurer is not appropriate for any reason or does not carry rates, terms and conditions that are fair between the parties or the documents used with products are, in any way unsatisfactory, notwithstanding the fact that IRDA may had no subsisting queries in respect of that product when it was filed, it may express its concern and call for clarifications to remove its concerns.

- If the insurer fails to satisfy the Authority, the IRDA may require the insurer to suspend the sale of that product until it is modified in a manner acceptable to IRDA or withdraw the product from the market.

- Where the product is drawn from the market under the above circumstances, the insurer shall not bring in a new product with the same trade name.

- IRDA may require an insurer to justify the rates, terms, and conditions of insurance offered to a particular client or to a class of clients or for a particular product, within the time specified by IRDA. A mere statement that the risk is rated “on merits” will not be acceptable unless the quantification of the merits can be objectively demonstrated satisfactorily.

Board Approval of Underwriting Policy

All product design, rating, terms and conditions of the cover and underwriting activity shall be consistent with the underwriting policy approved by the full Board of Directors. A copy of the underwriting policy as approved by the Board shall be filed with the IRDA without delay and any changes made therein from time to time with the approval of the Board shall also be filled with the IRDA without delay. The underwriting policy placed before the Board shall cover the following aspects, among others:

- The underwriting philosophy of the company in the matter of the underwriting profit expectation.
- Whether each product should stand on its own costs or cross-subsidy among the products sold to one client will be acceptable. It is important for the Board to note that even though a client’s total portfolio may be profitable on gross basis, it may be a loss on net of reinsurance basis because of different percentage of retention for different classes.
- Whether the insurer will underwrite any business on a planned underwriting loss basis and if so, how the board will control its impact on its solvency margins.
- The margins that will be built into the rates to cover acquisition costs, promotional expenses, expense of management, catastrophic reserve and profit margin and to consider investment income as credit adjustment in design of rates, terms and conditions of cover.
- The list of products will fall into 5 categories as specified below. It is recognized that whenever there is any introduction

of a new product in a category or transferred to a different category, such modification should be reported to the Board and the Board's decision being filled with the IRDA

- The delegation of authority to various level of management for quoting rates, terms and conditions.

- The role and involvement of the appointed Actuary in determination of rates, terms and condition of the cover.

- The internal audit machinery to ensure the quality of underwriting.

- The procedure for reporting to the Board on the performance of the management in underwriting business and the frequency of reporting.

Responsibility for Compliance of the Guidelines

- The documents to be filled under these provisions and guidelines shall be filled under the signature of the principal officer of the insurer or a senior level officer designated by him.

- Where an insurer delegates the authority to the subordinate officer, the principal officer will remain responsible to comply with the requirements.

- Each insurer shall appoint a senior officer as 'Compliance Officer" to ensure compliance with the requirements of "file and Use".

- Where a risk is co-insured, the primary responsibility to comply with the requirements will rest with the leading co-insurer and the following insurers will remain responsible to satisfy themselves by enquiry that the guidelines have been complied with.

Classifications of Products

For the purpose of the said guidelines on "File and Use" the general insurance products are classified into following 5 categories:

(i) **Internal Tariff Rated Products** — These are standard products that can be sold by any one of the offices of the insurer with the rates, terms and conditions of the cover including choice of deductible if necessary, being standardized and listed in an Internal Guide Tariff. The said Internal Guide Tariff also provides a set of rules and procedures to be followed by line underwriters for rating if he visualizes any variation of risk evaluation of a particular risk based on the features of physical hazards, safety and loss-prevention measures, sum-insured in order to ensure risk-cost-based rating and meet competition. Precisely these are "Rule Based" underwriting products or Class-Rated products.

(ii) **Individual Experience Rated Products —** These are products where the rates, terms and conditions of cover are determined by reference to the requirements of the actual claims experience of the insured concerned. This applies to the insurance cover with low frequency and high severity of loss-forecasting.

(iii) **Exposure Rated Products** — These are the products where rates, terms and conditions are determined by the underwriters on the basis of the detailed risk identification and appropriate risk-evaluation of a particular risk exposure in stead of following class-rates. These are also known as individual-rated products. These apply to typical risks where the earlier risks data are not sufficient or not matching with any particular class of property or liability risks such as Ocean-going Transit Risks, D&O Liability Risks or E&O Liability Risks.

(iv) **Packaged or Customized Products** — These are products specially designed for an individual client or class of clients, in terms of scope of particular cover, basis of insurance, combination of different risks and perils, voluntary deductible, rates, terms, conditions of cover. Such products are also known as special contingency policies.

(v) **Large Risks or Critical Risks** — Such risks for the purpose of "File and Use" guidelines include Property risks with sum-insured of Rs 100,000 crores or more and Liability Risks of Rs 100 crores or more per event (AOA). These are typical risks, where rates, terms, conditions and deductibles are to be determined with reference to the international reinsurance markets and with facultative reinsurance arrangement with international reinsurers. The risk-exposures of such products are beyond the financial capacity of Indian insurers and reinsurers. Therefore the rates, terms, conditions of such large and critical risks are to be decided following the quotation from the international reinsurers. If the insurer varies the terms, conditions, rates and retention from those quoted by the international reinsurers, such variation must be in consistent with the underwriting policy and reinsurance policy duly approved by the Board and submitted to the Authority. Such rates and retention should have concurrence of the Appointed Actuary. Full particulars of such risks along with the quotation of Reinsurer shall be filed with the IRDA, which may raise question on their examination of rates, terms, condition, reinsurance percentage, retention limits with reference to total risk exposures and financial capacity of the insurer.

Role of Appointed Actuary

- The Appointed Actuary, in consultation with the nominated underwriters of the insurer, shall determine the requirements for collection, compilation and analysis of premium and claim data at the stage of product design. He shall ensure that such data get captured at the stage of effecting insurance and also claims intimation and all claims payments.

- He should compile various first loss rating data, schedules alongwith schedules of discounts for higher deductibles or franchise in consultation with the nominated underwriter for deciding higher deductible or franchise. Such schedules shall form the basis of rating risks on first loss insurance or without condition of average and for allowing higher discount, deductible or franchise.

- The said analysis of the Actuary should enable periodical review of rates, loadings, discounts etc for rating the risks properly.

8

GENERAL INSURANCE UNDERWRITING-PRINCIPLES AND PROCESS

Underwriting – Scope and Definition

Underwriting is the core function of general insurance business. Other functions such as claims Management, Accounts and Investment, Marketing can be outsourced, but underwriting function cannot be outsourced. Underwriting is process of writing business by insurer, i.e. Risk Identification, Risk Analysis, Risk Evaluation, Risk Acceptance, Risk Rating, Risk Improvement (Imposing Conditions and Exclusions), Risk Retention, Risk Transfer (Reinsurance). This chapter covers the following fundamental aspects related with general insurance underwriting:

- Underwriting – Scope and definition
- IRDA Directives on Underwriting
- Underwriting and Risk Inspection
- Underwriting Policy — Formulation, Implementation and Control
- Rating the Risks Right — Perspective, Principle and Process
- Underwriting & Product Development

Underwriting is a logical process of accepting risks. It is process by which an insurance company decides as to whether they can accept proposed risks and if yes, at what price, and on what terms and conditions. Underwriting follows an underwriter's judgment on acceptance of risks, based on his careful analysis of several factors including physical hazards, morale hazards, morale hazards, past loss data, future-loss forecasting, projected law of large number, government regulations and so on. Underwriting undergoes several stages. The first stage of “Underwriting” is ‘Selection and Classification of risks’. Selection signifies the underwriter’s decision to accept or reject proposed risks, while ‘Classification’ is specifying the class to which the accepted risks belong. Classification is needed for determination of rate, terms and conditions for the risks accepted. Underwriting are of two types: i) Staff Underwriting/ Corporate Underwriting; and ii) Line Underwriting.

Staff Underwriting

This is primarily involved in the process of formulating underwriting policy and underrating of large and complicated risks. The Major Functions of staff underwriting are:

- Formulation of Underwriting policy, Reinsurance Policy, Product Development Policy;
- Preparation of internal guide rates or rating plan for class-rated products;
- Reviewing and revising Rating Plans according to underwriting results in terms of growth, profitability and market conditions;
- Carrying out industry-wise risk analysis for underwriting new risks;
- Issuing Underwriting Reports and Guidelines;
- Adding/deleting particular line/segment of business based on underwriting results;
- Expansion with development of new product or existing product into new territory;
- Determining appropriate product mix;
- Determining potential volume & target; and
- Providing exhaustive list of declined risks for every class of risks.

Line Underwriting

This is a process of implementation of underwriting policy in assuming risks and rating risks as per laid down underwriting policy of the company. Line underwriters accept risks on the basis of internal guide rates and rating plan prepared by nominated/ corporate underwriters**.** Following are the major functions of line underwriters in operating offices:

- Selection of risks and the insured
- Risk Identification, Classification & Analysis
- Determination of appropriate cover
- Determination of appropriate rate, terms & Conditions as per guide
- Reference of large risks to staff underwriter with risk analysis for deciding rates, terms and conditions.
- Service to policyholders

IRDA Directives on Underwriting

While de-tariffing, IRDA has issued the following directives specifying the requirements of underwriting such as Rating Support, Policy Terms & conditions, Underwriting Function, Corporate Governance etc.

***"...**The function of underwriting and rating of insurance business should be independent of the business development function and not be made subservient to the business development function. For operating convenience, every insurer will require to have an internal guide tariff for smaller valued risks and the simple risks. Staff with authority to accept business will be trained to evaluate proposal and underwrite and rate risks as per the guide tariff. Risks not covered by guide tariff must be referred to Nominated underwriters stationed at higher offices of the insurer. These underwriters will be specially trained in evaluating risks, securing* *required reports of inspection or risk evaluation reports and underwriting and rating the risks and determining the terms and conditions of cover. The nominated underwriters with authority to accept or decline risks and to quote rates and terms will not report to any officer with business development responsibility but will only report to a senior level officer whose work and performance will be assessed on the basis of the results of the business underwritten… An insurer must have a risk inspection team within the organization or may use outsider experts for risk inspection and evaluation for underwriting…"*

All the underwriters in general insurance business are required to follow the above directives for the purpose of effective underwriting.

Underwriting and Risk Inspection

Risk Analysis involving risk identification, risk analysis, risk evaluation is the basic foundation on which the whole process of underwriting rests upon. Various management professions in various ways define risks. In insurance, risk is defined as the combination of the probability of an event and its consequences. Underwriters shall determine the insurability of risks before they accept risks. For determination of insurability depends on classification of risks, their objective probability and other considerations.

Classification of Risks and Insurability Thereof

1. **Pure Risks:** It may occur with loss but no gain. There is only chance of loss, but not of any gain. For example fire, storm, strike, flood, machinery breakdown etc are pure risks and insurable.

2. **Speculative Risk:** It may occur either with loss or gain such as Hedging, Options, and Futures etc, which are not insurable under traditional insurance.

3. **Dynamic Risks:** Those risks that change with the change of economic, social and political changes are not insurable under traditional insurance.

4. **Static Risks:** These are those risks that exist without any changes. Risks to be insurable must be static during the period of insurance. For changes, if arise, the insurers must be informed for their acceptance and necessary endorsements.

5. **Fundamental Risks:** These are those risks that affect the whole society and may arise from catastrophic, political, economic causes. Fundamental risks are more taken care of by the Government than by insurance.

6. **Particular Risk:** This risk is related to a particular individual, firm or situation is always insurable if not speculative.

   In traditional insurance underwriting only pure, particular and static risks are insurable, speculative, dynamic and fundamental risks are not insurable. Certain risks such as **Financial Risks** (Interest Risks, Liquidity Risks, Exchange Risks), **Political Risks** (Change in Govt. Policy), **Market Risks** (Failure to sell at target price, advent of better substitute, Change in customers taste, change in general economic conditions), **Technology Risks** (obsolesce of existing products) are not insurable under traditional insurance, but all these risks are insurable ART (Alternative Risk Transfer) method.

Under ART almost all risks are insurable. We will discuss here only about traditional underwriting process.

Probability of Risks and Insurability

There are two types of probability – Subjective Probability and Objective probability. The probability considered in insurance underwriting is objective probability, but not subjective probability as discussed below.

Objective Probability

In insurance, risk is mainly analyzed and considered as the chance of loss and variation of degree of loss for a particular property or situation from expected average loss in a particular class of property or occurrences. For example, it is surveyed that out 100,000 houses in a particular area 1000 houses may be lost or damaged due to fire over a particular period of one year. This 1 per cent probability is Objective Probability. In some places or periods or situations, loss may be 900 while in other years or situations it may be 1100 houses. Thus variation may come 10 per cent (+) or (-) and so on depending upon the physical hazards associated with property, place, person, period, product or plant. Loss per cent varies with all such Ps. This relative variation of actual loss from the average expected loss is objective probability statistically calculated/ determined by measure of dispersion- such as standard deviation or co-efficient of variation for class of risks.

Subjective Probability

Subjective Risk is based on individual perception or state of mind regarding the probability of occurrence of accident and the extent of loss due to accident instead of outcome of group analysis of occurrence of loss. With such individual perception of loss different persons in the same society may take mediclaim policy for different sum increased and even some people don't take any mediclaim policy according to their perception of risks. If an individual experiences occurrence of major loss due to health risk, he will take a mediclaim policy for large amount. But an individual who does not view this health risk seriously or does not experience major health expenses he may take medicalim policy for a small amount. Such individual perception about the frequency and severity of accident and loss is known as subjective risk or probability is important for an individual to take decision on amount of insurance cover, it is not considered by insurer for underwriting risks. The underwriters always take objective risk probability into consideration for their underwriting decisions.

Other Considerations for Insurability of Risks

Following are the major considerations of the underwriters for underwriting decisions:

- There must be a large number of exposure units
- The loss must be accidental
- Frequency and Severity of loss must be calculable
- Special financial instrument for transfer of catastrophic risks
- Premium must be economically feasible

Large Number of Exposure Units

Insurance is the pooling or transfer of fortuitous losses. Pooling is the spreading of losses incurred by a few over the entire group of many. This requirement stems from the law of large number on which entire insurance mechanism is based. The law of large number requires a large number of exposures to provide fairly prediction of loss and affordable price for risk transfer. The law of large number states that the greater the number of exposure, the more closely will the actual results will approach towards the probable results that were estimated from the expected group of exposures both for pricing and underwriting policy. Most of the estimates are based on the previous loss experience supported by future projection, which comes from nothing but expected large number of exposures. So if a particular risk belongs to a class of large number of exposure units, the actual loss experience of the past may be a fair approximation of future loss.

The exposure units in large number must be similar, but not necessarily identical. The exposure units may belong to the similar or same group of perils. Besides having a large number of exposure units, it is necessary that these units are independent and homogenous. The exposure units may be said to be homogenous when the frequency and severity faced by these units should be relatively same. An insurer can select homogenous units by adopting proper classification system and improving upon such system periodically based upon the past experience.

Risks for Accidental Loss

Insurance covers risk of loss or damage, which is accidental in nature. It covers a risk, which is a fortuity but not a certainty. It is for some loss or damage that happens due to fortuitous external causes but not natural behavior or inherent vice of the subject matter. It shall not come from morale or moral hazard of the insured. It is why a ICC (A) Marine Insurance Cover, an 'All Risks' transit insurance does not cover any loss or damage arising from inherent vice or nature of the subject matter. The requirement of accidental and unintentional loss comes from the following reasons:

- Moral hazards that cannot be insured will be eliminated. If the losses are not accidental some unscrupulous insured will manage to get deliberate or fraudulent claims, premium will increase for the entire group and the rest of the group will pay the price for bad moral hazards of the few.

- If the price is high for the reasons mentioned above, many will cease to be members of the group and there will not be large number of exposure units and law of large number will not operate. Thus entire device and purpose of insurance will fail.

- The law of large number is based on the random occurrence of accidental events. A deliberate loss is not a random event because it is caused deliberately. The prediction of future loss may be highly inaccurate and underwriting will be costly for insurer.

Frequency & Severity of Loss must be Measurable

Insurance pricing principle and process are based on loss exposures, i.e. estimation of expected loss. Loss exposure is analyzed by taking into consideration both the frequency and severity of loss. Loss frequency refers to the number of loss and loss severity means the amount of damage resulting from each loss in a particular group of exposures. The consideration of both the factors helps the underwriters to take proper decisions in respect of: i) Acceptance or rejection of risk; ii) Risk Retention Limit; iii)

Rates; iv) Terms, condition and deductible; and v) Risk Retention or Transfer. The underwriters apply statistical methods and measures on past loss data collection, compilation and analysis estimation of frequency and severity of loss for the expected large number of exposures.

Catastrophic Risks Underwriting

Probabilistic Risks should be separated from Catastrophic Risks in traditional insurance unless there is special arrangement of risk transfer. Recalling the 9/11 terrorist attack bringing about financial loss more than US$ 60bn and insolvencies of many insurance and reinsurance companies in the world, the underwriters should not go for insuring catastrophic risks without adequate reinsurance cover. However with introduction and use of ART products including insurance-linked securities or catastrophic bonds that transfer insurance risks from insurance markets, catastrophic risks are being insured easily though with separate consideration of rates, terms and conditions. Ideally, insurers should avoid all catastrophic risks if they do not have proper reinsurance support with ART back-up. The concentration of loss exposures in a geographical area exposed to catastrophes like flood, earthquake, hurricanes or storm may result into periodic catastrophic losses and bring consequent financial distress for the insurers or reinsurers. If such risk exposures are geographically dispersed, the possibility of catastrophic loss is reduced to the minimum. Reinsurance or ART enables cat risks geographically dispersed.

In view of rising catastrophic losses during last 4-5 years the Munich Re has guided the Indian Insurers with following prescriptions for management of Cat Risks:

1. Adequate Pricing
2. Substantial Deductibles
3. Loss Prevention
4. More Reinsurance

5. Capital Base

6. Accumulation Control

7. Prompt and Proper Claim Settlement

8. Limiting Insurer's Liability

9. Exclusion of Certain Hazards

10. Exclusion of Particularly Exposed Areas

Premium must be Economically Feasible

Premium for the risk assumed should be economically feasible. The insured should be able to pay the premium. Premium, i.e. price for insurance cover should be affordable to him. Premium to be affordable, abnormal costs of adverse selection, moral hazard, shall be eliminated in underwriting process, exposures should be considered on law of large number, with greater geographical spread, profit should be minimum and investment income should be adjusted from the total risk costs and time value of premium should be considered.

Risk Management Policy as a Part of Underwriting Policy

Every insurance company must have a clearly laid down risk management policy as a part of underwriting policy. This risk management policy is to be adopted in consideration of corporate underrating philosophy, objectives and policy. RM Policy is reviewed periodically on the basis of underwriting results.

Fundamentals of RM Policy in Insurance Underwriting

Following are the important considerations for RM policy formulation in a general insurance company:

1. Consideration of Corporate philosophy and objectives

2. Clear definition of Risk Classes to be underwritten

3. Estimation of Risk appetite in view of the financial capacity of the organization.

4. Risk governance structure with a clear-cut authority & accountability relationship

5. Decision on acceptance based loss experience but not individual risk perception

6. Underwriting function being independent of marketing function

7. Appropriate acceptance limits at every operating level based on experience

8. Underwriting experience supported by underwriter's expertise, skill & knowledge

9. A clear-cut distinction between the corporate underwriting and line underwriting

10. Review of RM policy based on emerging market condition and U/W results

11. Consideration of directions, guidelines and experience of re-insurers

12. Consideration of Regulatory Norms

Objectives of Risk Management Policy and Underwriting

RM policy of an insurer must be designed to achieve the following objectives:

1. To improve the quality of corporate underwriting and line underwriting

2. To encourage a progressive and professional corporate management practice.

3. To ensure prudent underwriting for growth with profitability

4. To manage all threats to cost, catastrophes, competition with clear vision

5. To create awareness of risk perception &analysis in all concerned in underwriting

6. To embed the mission, needs, process and direction of corporate governance.

7. To establish a culture of transparency and uniformity in risk handling activities

8. To enable wide range data mining and bring greater accuracy loss forecasting

9. To prepare for major eventualities, with adequate contingency plans.

10. To improve understanding of relationship between risks, cost and rating

11. To greater accuracy in estimation of Probable Maximum Loss (PML)

12. To ensure proper mix of retention and transfer of risk and avoid insolvency

Risk Management Process and Its Application in Underwriting

In insurance underwriting risk management involves risk identification, risk analysis, risk evaluation, Risk Acceptance, Risk Rating and Risk Financing, which are briefly discussed below.

Risk Identification

As we know, risk is defined or considered as chance of loss due to occurrence of certain perils. Risk identification process centers on defining and identifying all actual, perceived or anticipated risks associated with property or liability to be covered by intended insurance policy. It is thus exploring and specifying all kinds of hazards leading to perils that result into risks. Risk identification is the first step towards risk analysis and risk acceptance for insurance underwriting. It is the basic foundation of underwriting, as underwriter's failure to properly identify all hazards being financial, operating, legal, market, technological and environment will increase the actual loss exposure and make the underwriter insure many sure loss in place of pure loss and finally making the insurance product very costly and non-viable for the majority of the people who really need insurance. Generally risk identification is carried out through various process and methods some of which are COPE (Construction, Occupation, Protective Measures, and External exposure) Analysis, Event Analysis, Hazop Analysis, Flow/Process Chart & Organizational Chart analysis, Accounting statements, records and reports analysis, Specific Inspection, analysis of Past records and so on depending upon the place, product, process and plant exposed to risks to be covered by insurance. risk identification is generally like Engineer, Financial Professionals or by Legal Professionals in case of liability insurance.

Risk Quantification

The quantification process determines the financial impact both probability and severity, that a risk can bring on the firm. Risk quantification is typically done through application of various quantitative methods and statistical analysis including measure of central tendency, probability distribution or law of inference and analysis of past records. This requires collection of appropriate data and data mining and analysis. Selection of specific technique or method for measuring financial impact of risks varies the nature of property or liability to be insured, which is discussed more elaborately in subsequent chapters.

Risk Treatment

Loss Control, Risk Retention and Reinsurance

After risks have been identified and quantified, RM decision is to be taken for Risk Treatment including Loss Control, Retention and Reinsurance of risks. After risk analysis and quantification, when it is decided that risk will be accepted, the underwriter is to then decide rate, terms and conditions. Once the decision has been underwriter must decide how best the risks can be managed. To take such decision, the underwriter shall first classify the risks to be accepted according to the standard norms or guidelines in Underwriting Policy and then rate the risks. Finally he has to take decision on retention limit and reinsurance arrangement. The insurers generally go through following process for taking decisions on retention and reinsurance:

- Determination of Probable Maximum Limit (PML)/Estimated Maximum Loss (EML)
- Determination of retention limit as per co's financial capacity & Reinsurance Programme
- Determination of Reinsurance Methods and Treaty
- Selection of Re-insurers

The decision for retention limits and reinsurance programme is outlined in Table-12 below.

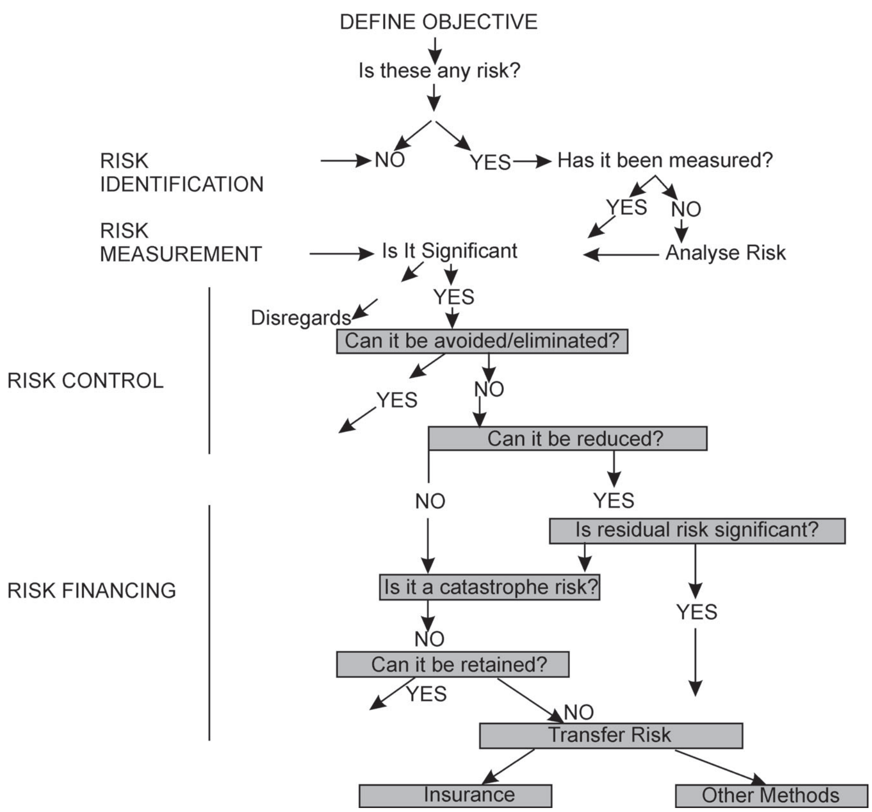
Table-12. Loss Control, Risk Retention and Reinsurance

Loss Frequency	**Loss Severity**	**Guidelines**
Low	Low	Retention
Low	High	Less retention; More Reinsurance
High	Low	Retention with deductibles
High	High	Rejection or Less retention &More Reinsurance

Rating Risks Right

One of most important RM decision in insurance underwriting is Rating Risks, which has been discussed more elaborately below.

Graphical Presentation of Risk Management Process in Underwriting



Rating Risks

Rating is the core part of underwriting. Insurance product pricing, i.e. rating is based on certain perspectives, principles and process. Major weakness of India's non-life insurance industry is its long-standing tariff regime.

Rating in Tariff Regime and De-tariff Regime

The century long tariff regime, the insurers engaged themselves in non-price forms of competition such as product differentiation, branding, rate-cutting, cross subsidy etc., which could not both benefit the customers and the insurance industry as a whole in the country. In the tariff regime, Motor TP risks were heavily underpriced and so also in case of Mediclaim insurance, which were swallowing the surplus generated by Fire & Engineering Portfolios resulting into cross-subsidization across business lines. Motor TPL cover was maintained by insurers with more than 250 per cent loss ratio and Group Mediclaim Insurance was managed with loss ratio of more than 150 per cent. This was happening only because of cross subsidy, which was the strongest inefficiency of insurance management in the tariff regime in India. Now it is de-tariffed. The Indian underwriters have got the full freedom for rating the risks in fire policy w.e.f. 1 January 2008. Detariffing of Fire, Engineering and Motor insurances in India is a historical event after continuing with tariff for more four than five decades. Today almost all products are without tariff. With this de-tariffing, the insurers are free to decide the premium rates based on their in-house guidelines and underwriting policy.

The success and survival of an insurer rests upon his skill and capability to rate the risks right. Freedom to fix price for the risk gives the real strength and autonomy to the industry. In free market all underwriters have developed mechanism to identify, analyze, evaluate risks and rate the risks according to cost of risks determined mathematically and statistically with the principle of law of large number and process of loss forecasting based on analysis of probability and severity of loss from operation of a peril.

The US, European Union (EU), Japan, Hong Kong, Taiwan, Egypt, and Philippines have been enjoying benefits of deregulation and de-tariffing since long in the form of: i) Price Mechanism; ii) alignment of price with cost of risks; iii) reduction in cost and price in the competitive environment; iv) improvement in quality of services; v) improvement in productivity; vi) innovation in products and services according to the needs of the customers; vii) elimination of cross-subsidy; and viii) practicing merit rating or experienced rating. All these have resulted into solid base of price mechanism, greater market thrust and deeper penetration. Because of earlier deregulation, China's insurance industry is much more developed with higher asset quality and better performance of companies.

Objectives of Pricing

Insurance rating is to meet three objectives: i) Regulatory Objectives; ii) Business Objectives; and iii) Social Objectives.

Regulatory Objectives

a. Rating Adequately

The regulatory requirement of pricing arises from the purpose of insurance regulation, which is to protect the interests of the policyholders and the shareholders. This means that the rates must be adequate enough to meet all future losses and expenses in time and to pay a fair return on the capital employed by the shareholders for this risk taking business. If the rates are inadequate, an insurer may become insolvent causing total loss to the policyholders' fund as well as the shareholders' fund and cause total loss of public faith and confidence in insurance industry. However, in insurance business rate adequacy measurement is really complicated because of the simple reason that insurer does not know the actual costs at the time of selling the policy. Price is estimated on loss forecasting process based on statistical methods. The premium is collected in advance in view of law of large number (projected) and expected claim costs and other expenses. If the insurers fail to achieve the targeted number or volume of business and if the actual claim costs are more than the statistically projected or forecasted loss, price collected may not be sufficient to pay all claims and expenses during the policy period. As a result, policyholders, shareholders, third-party claimants and other stakeholders may be financially harmed. Thus the Regulator shall see that rates are adequate.

b. No Excessive Rate

Again the Regulatory Authority is also to ensure that the rates are not excessive. The rates should not be more than actual value of protection or cost of risk assumed in order to ensure affordability of the insurance product for the larger section of the society. Exorbitant rates are opposed to the public interests. If it is more than expected cost of risks (arrived after application of law of large number) plus minimum profit, insurance products will go beyond the reach of the majority of the society, which will be also opposed to the objectives of the IRDA. Needless to mention, even after the expiry of a decade since constitution of IRDA, general insurance market penetration is only about 0.6 per cent, which is also a major concern of the authority. To increase insurance penetration, insurance rates should as low as possible reducing the combined ratio substantially.

c. No Discriminatory Rate

The Authority is also to ensure that similar risks with reference to probability and severity loss are not rated differently for different customers without any sufficient grounds. For example two persons of the same age, same profession, and same area should not be rated differently for same sum insured for a Personal Accident Policy. Similarly two buildings of the same age, same construction, same location, and same occupation shall not be rated differently.

Business Objectives

In today's open and global market, insurance business must meet the following objectives to ensure its survival and success:

- **Simplicity:** The rating system should be simple enough to understand and apply in a particular class of business. With an exhaustive Internal Guide by Nominated Underwriters, rating system can be made simple for the line underwriters for small and simple risks. For large and new line of business the company must have sound Risk Management and Risk Inspection Policy so that line manager can estimate/quote premium for immediate feedback to the prospective customer on his specific query without waiting long for the advice of the reinsurer.

- **Stability:** Insurers always try to make the rates stable over the short periods so that customers get confidence in the operations of the insurance company. Frequent changes in rates, terms and conditions may lead to customers' dissatisfaction and irritation resulting into loss of credibility of the insurance company. To ensure stability of rates and customers' confidence the insurers must comply with the **IRDA Guidelines on File and Use**" requirements for general insurance industry**.**

- **Responsiveness:** The rates should be responsive to changing loss exposures, current economic conditions and also to solvency margins. There should not be any rate-cutting at the cost of shareholders' fund or other policyholders' fund. For example, if inflation causes increase in medical expenses reimbursement or payment in more automobile repair claim, Mediclaim insurance premium or Motor OD premium need to be enhanced.

- **Encouragement of Loss Control Measures:** The insurer's rating policy should encourage loss-control activities that may reduce both loss-frequency and severity. With proper risk inspection and risk analysis, the insurer may find out the weakness of loss prevention measures and guide the insured accordingly to improve the arrangements so that frequency and severity can be reduced and accordingly fire rates can be also reduced. In this regard Hazop Study, Fault Tree Analysis or Dow Index Analysis and from regular risk identification and analysis deserve special mention.

Social Objectives

Availability of Insurance to the larger section of the society: Because of the unreasonable prices certain sections of the society find it difficult obtain coverage easily at a reasonable price. As we know the capacity of insurers is limited and their endeavor will be to see that their capacity is being utilized on some profitable accounts for maximization of the shareholders' wealth and income. With this objective of maximization of shareholders' wealth with only profitable accounts of insurance, insurance penetration will be affected and the social responsibility of the industry will not be served. Availability of insurance is also affected by insurance cycle.

When operating surplus is generated, the market becomes soft immediately. Again when insurers suffer heavy losses especially catastrophic ones, prices are hiked and many products go beyond the reach of the common people. So to ensure availability of insurance products for larger section of the society as per their affordability, the insurers must have ability for proper loss forecasting and stable, simple and transparent pricing system. Insurance business cannot be run in today's global market only with business objectives regardless of social objectives and regulatory objectives.

Basic Principles of Pricing

From the above discussion we can derive the following basic principles of pricing risks by the insurers in a regulated and competitive market:

- **Alignment** of price with cost of risks **(**discussed hereinafter in Fair Rating).

- **Classification** of risks based on homogeneity to apply class rate.

- **Law of Large Number** for Greater the number of risks covered, greater will be the accuracy of loss forecasting and lesser will be as per the unit of fair premium.

- **Forward looking** into expected claim costs, administrative & procurement costs and expected invest income.

- **Regulatory directives** for compliance of "File & Use" or "Use & File" requirements

These principles are being discussed hereinafter along with the methods.

Methods of Rating

The common methods of determination of basic rate or pure premium, which constitute the major part fair premium, are:

- Judgment Rating/Individual Rating
- Class Rating
- Merit Rating

The underwriting policy of the company must specify the principles and methods of rating – Basic Rates and Fair Premium for each type of business to be underwritten as per the company's underwriting philosophy, policy and objectives as well as Regulatory objectives. Precisely fair premium is the pure premium as calculated by any of the following method plus Overhead of estimated Administrative Costs and Acquisition costs reduced by expected return on investment.

(a) Judgment Rating

Judgment Rating implies that each exposure is individually analyzed, evaluated and rated on the basis of the underwriter's judgment. This method is generally used by the underwriters when the loss exposures are so diverse and do not correspond with any class data available for class rate or credible loss statistics are not available. Judgment Rating is widely used in Marine Insurance especially for import/export consignments of different clients from different places in ocean-going vessels of different capacities, class and managements, covering ports of different countries in different weather conditions with cargoes of different nature being shipped to different countries under different terms and conditions. So due to the widely varied factors of rating having no specific past loss experience statistical data, the insurers mostly used judgment rating for import/ export marine insurance.

(b) Class Rating

The most of the rates today used are class rates determined either on Pure Premium Method or Loss Ratio Method. Class Rating means that risks with similar characteristics of exposure are placed on the same underwriting class and charged the same rate. The rate that implies the average loss experience for the entire class is based on the assumption that future accidental loss will arise with same set of probability and severity. Tariff Rate or company's Internal Guide Rate are Class Rating. Generally, following aspects are taken into consideration for application of Class Rating:

- Risk grouping/classification
- Homogeneous Group in respect of the following aspects
  - o Nature of occupancy (Mfg, Trading, etc)
  - o Properties of materials (flammability, reactivity, toxicity, flash point etc)
  - o Properties of products
  - o Nature & height of constructions
  - o Process hazard (reaction, operation, boiling point, flash point, ignition point)
  - o Plant/process-(types, maintenance etc) & protection system & appliances
- Credible Data Bank for proper Statistical Analysis and technical justification.
- Probability Distribution of Loss for the particular class of risk
- Law of Large number
- Reinsurance rate

(c) Merit Rating

It depends on the retroactive claim experience of the specific business applicant. As we have discussed above, class rates and underwriting standards are based not only on class data but also on the individual characteristics of the particular business applicant. The line underwriters need to modify the class rate and even schedule rating for the particular buyer to consider the underwriter's analysis and evaluation of further additional characteristics for merit rating. There are different types of merit rating:

- Schedule Rating
- Experience Rating
- Retrospective Rating.

(d) Schedule Rating

It depends on underwriter's judicious decision to modify the class rate in view of his evaluation of additional characteristics of the business proposal of a particular nature. The additional characteristics include physical hazards, moral hazards, and existence of safety programme, improved technology, management control, and compliance of corporate governance and Government regulations etc., of the particular business in a specified class. Under this Rating Method, each exposure is individually rated or class rate is modified in view of desirable or undesirable physical features such as: i) Construction; ii) Occupation; iii) Operation Method; iv) Protection or safety measures; v) Exposures; vi) Housekeeping & Maintenance; vii) Loss Prevention or control Measures; and viii) Management outlook and attitude for loss prevention/control measures. Class Rate and associated underwriting standard may vary across the underwriters according to their claim experience and objective probability of risk (operation of law of large number).

(e) Experience Rating

It is another type of merit rating where class rate or scheduled rate is further adjusted upward or downward based on the past loss experience of the particular client for reasonable period (generally 3 years). If the insured's loss experience is better than average for the particular class of clients, the class rate is further reduced. If the loss experience is worse than the class average, the rate is increased. In determining the quantum of the rate change, the actual loss experience is modified by a credibility factor. Experience Rating is generally restricted to large customers paying large amount of premium for different classes of business for reasonable long period. This type of rating may be applied to WC Insurance, Liability Insurance or Group Mediclaim Insurance safely as it is being followed in other countries, which have been in deregulation for a pretty long time.

(f) Retrospective Rating

Under this method, the insured's loss experience during the current period is taken into account for determination of actual premium to be charged for that period. Here, a provisional premium is paid at the beginning of the policy period and the end of the period a final premium is computed actual loss experience during the period. Retrospective Rating is widely used in US for WC Policy, General Liability Policy, Auto Liability Policy, Property damage and Burglary policy for large firms.

Essential Considerations of Class Rating

(a) Homogeneity of Group

Homogeneity of buyers is one of the fundamental considerations of the classification of risks. To make the law of large number to be effective and ensure cost-based pricing, the homogeneity of the class must be established with respect to nature of property, frequency and severity of loss faced by the homogeneous group. The main purpose of an insurance classification system is to categorize risks that possess similar features and probability of loss in the same class. Suppose that in a large group of scooter insurance, each policyholder has the probability of 0.20 for suffering loss of Rs 5000 and probability of 0.80 for no loss. Since the policyholders in a homogeneous group are supposed to have same Loss distribution, the underwriters adopt fair Rating Method with the probability analysis supported by law of large number theory for a homogeneous group. The actual claim cost may vary from the expected claim cost. But with the operation of law of large number, the actual (Incurred Claim Ratio (ICR) for particular segment equals with the total amount of loss forecasting on which fair premium rate is decided for the group.

(b) Statistical Analysis for Estimated Claim Costs

Estimation of fair premium for a class of depends on Statistical Analysis comprising Measure of Central Tendency, Dispersion, Probability Distribution Analysis and Variance Analysis. Measure of Central value being either Mean or Median or Mode gives an idea of the mass. Mean is the best of all these methods of measure of Central Tendency. It is also not sufficient to get an absolute idea about the expected claim cost for the risks to be accepted. Mean gives simply an average. It cannot establish whether the observations are close to each other or far apart. A measure of dispersion/variability amongst observations in a set of loss events is therefore essential to measure the reliability or effectiveness of loss data and for necessary adjustment in the value of central tendency to arrive at fair expected value or amount of expected claim costs. Probability Distribution is characterized by two important measures: Central Tendency and Dispersion. Probability Distribution Analysis is the fundamental basis for estimating loss frequency and severity of the target group of risks to be assumed.

A Probability Distribution identifies all the possible outcomes for a random variable and the probability of all outcomes. The expected value (claim) is derived by multiplying each outcome by the probability occurrence and summing the product results. To illustrate the use probability distribution, let us examine Table-13 & 14 showing Motor OD Claims for a line underwriter for 10 years for 100 policies with Motor OD premium of Rs 100,000 per annum.

Table-13 (Premium & ICR)

Year	Policy No.	Premium Amt	Claim Amt.	Claim No	ICR %
95-96	100	100000	30000	30	30
96-97	100	100000	40000	35	40
97-98	100	100000	45000	43	45
98-99	100	100000	50000	45	50
99-00	100	100000	45000	44	45
00-01	100	100000	40000	42	40
01-02	100	100000	45000	46	45
02-03	100	100000	45000	45	45
03-04	100	100000	50000	50	50
04-05	100	100000	55000	55	55

Table-14 Expected Value

Loss Amt	Occ. Yrs	Probability	Expected Value
30000	1	0.1	30000*0.1=3000
40000	1	0.1	40000*0.1=4000
45000	5	0.5	45000*0.5=22500
50000	2	0.2	50000*0.2=10000
55000	1	0.1	55000*0.1=5500
Total	10	1.0	=45000

Expected Value = $x_1p_1 + x_2p_2 + \ldots x_np_n = \Sigma x_ip_i$. Here Rs. 45000. The Expected Value of probability distribution indicates the value where the outcomes tend to occur generally.

Probability distribution analysis lists all possible outcomes & probabilities of random variables, i.e. uncertain outcomes. Expected value of Probability Distribution is Expected Loss with maximum probability. The Incurred Claim of Rs 45,000 (45 per cent) occurred in 5 years out of 10 years. The expected Value of Motor OD Claim is 45 per cent. A distribution with a higher expected value will tend to have a higher outcome or average of estimated loss.

Probability Distribution & Variance

Variance of a Probability Distribution provides information about likelihood and magnitude by which a particular outcome will differ from the Expected Value. Variance analysis measures the probable variation in outcomes around the expected value. If a distribution of loss bears a low variance, the actual outcome is likely to be close to the Expected Value. The distribution with high variance indicates that actual outcome will be far from the Distribution. It also indicates that outcomes are difficult to be predicted for risk analysis and underwriting. Conveniently Variance Analysis is worked out with square root of variances known as Standard Deviation.

Pricing & Deductible

A deductible, which is voluntarily accepted by an insured to bear the first part of the amount of any claim at figure higher than the standard excess impacts the rating of the product sold to the particular client. In a package or Mega policy, as we know, deductibles are arranged separately for material damage insurance or at a combined figure with the associated business interruption insurance in each case with or without an aggregate limit. The use of deductibles is on the rise nowadays because of two main factors: i) capacity of the insured to bear loss (self insurance); and ii) saving of insurance cost. So if the price of product that the insured can afford to pay is not commensurate with the nature of risk and the expected risk cost, insurer may opt for higher deductible and increase his amount of self-insurance. While deciding discount on guide rates or class rates, the insurer must consider the size of the deductible and the insured's past loss experience apart from physical hazards inspected.

Pricing and Warranties

As price of a tangible product depends on its quality and specification, the price of an insurance product (a promise to indemnify accidental loss) depends on the nature and number of conditions/ warranties and exclusions. For example, in the existing Fire Policy there are 13 exclusions and 15 conditions. If any of these conditions or exclusions is removed, price may get hiked provided the insurer has got some past loss experience and fair idea of loss forecasting for such type of product. Now a question arises as to whether an insurer can charge premium nine times of the normal premium for cover for a particular class risk eliminating nine of the exclusions in a standard fire policy. Answer should be no for the reason that it is nether prudent nor permissible under regulatory norms because such type of pricing of a specially customized product for a particular client on his offer may not be supported by technical analysis of appropriate statistical data of past loss and loss forecasting for a specially designed product different from the standard product based on past experience and filled with IRDA under the requirements of “File and Use”.

Pricing and IRDA Requirements

- Designing and rating of products must be based on prudent underwriting policy;
- All literature relating to the product should be in simple language for easy understanding of the public;
- The insurance product shall comply with the requirements of the IRDA (Protection of Policyholders’ Interests) Regulations 2002;
- Insurers should use uniform wordings for describing the same and similar cover;
- Pricing should be based on support of appropriate data and technical justification;
- Margins built into rates shall be consistent with the experience of the insurer in respect of commission, expenses of management, contingencies and profit; and
- Insurer shall ensure that competitive rating will not lead to unprincipled rate cutting.

Fair Premium and Risk Cost

Rating does not mean only claim cost or risk cost. Rating means Fair Premium, which considers and cover four expected costs and one expected income element: i) Expected claim costs; ii) Administrative costs; iii) Procurement costs; iv) Cost of capital (dividend); and v) adjustment of Investment income. A fundamental principle of insurance pricing is that premium on risks assumed is adequate enough to meet: i) Expected claim cost; ii) Administrative Costs; and iii) Acquisition Costs, and to provide an expected return on capital obtained to carry out the risk taking business. Precisely, total costs as above are subject to adjustment of return on investment of policyholders' fund. Thus fair premium is based on net costs, i.e. total costs minus expected return on investment. Provision for future catastrophic losses is also one of the fundamental considerations of rating and underwriting. Rating the risks aims at building up adequate fund to provide a long-term security to the policyholders for the risks transferred by them along with protection of the shareholders' fund with due return (ROI). In the perfect competition market, price is governed by price mechanism of demand and supply of insurance services. If premium charged is more than fair premium based on above risks costs reduced by investment income, an insurance company will not be able to retain the existing market share. Expected claim costs need to be discounted in consideration of expected investment income in rating the risks right. Efficiency of rating rests not only on reducing the costs, but also on the insurer's ability to earn maximum investment income. Efficiency and efficacy of Insurance Rating depend not only on quantitative factors but also qualitative factors. To ensure proper rate making the underwriters must give due emphasis to both quantitative aspects (growth, i.e. law of large number) and qualitative aspects such as quality underwriting with appropriate terms and conditions, quality of risk management, appropriate risk transfer policy, professionalism in brokers' service, proper and prompt claim settlement proper data management and MIS system, avoidance of cross-subsidy.

Underwriting & Product Development

Product development and product differentiation according to needs, taste, and affordability of customers both present and prospective is one of the important functions of corporate underwriters. While developing or designing product with addition to new line of business or rejecting existing loss-making line of business the corporate underwriters generally consider the following aspects:

- Designing and rating of products must always be on sound and prudent underwriting basis providing clear and transparent cover or value to the target group.
- All literature relating to the product should be in simple language and should follow a similar sequence of presentation as far as possible, for easy understanding by the target segment of customers.
- All technical terms should be sufficiently clarified for understanding by laymen;
- The product should be genuinely an insurance of an insurable risk with a real risk transfer, without Alternate Risk Transfer.
- The insurance product should comply with the requirements of the IRDA (Protection of Policyholders' Interests) Regulations 2002.
- Insurers should use similar wordings for describing the same cover or the same requirement across all their products, such as clauses on renewal of insurance, basis of insurance, due diligence clause, cancellation clause, arbitration clause etc.
- The pricing of products should be based on support of appropriate data and technical justification.
- The terms and conditions of cover shall be fair between the insurer and the insured.
- Margins built into rates shall be consistent with the experience of the insurer in respect of commission, expenses of management, contingencies, profit, and the investment income.

9

FUNDAMENTALS OF FIRE INSURANCE UNDERITING

History of Fire Insurance

Fire Insurance is the oldest form of property insurance. It has started more than 350 years ago in UK, US and other western countries. The Lloyds are the pioneer in such property insurance in the world. The history says the Lloyds started such property insurance in the middle of the 18th century in a small city in the UK and then extended according to their experience and capacity to the other cities in the country and other parts of the world. Since inception they applied risk-based underwriting in fire insurance. Here property includes all movable and immovable properties located at a particular premises, such as buildings, plant and machinery, furniture, fixtures, fittings, and other contents, stocks and stock in progress along with goods held in trust or in commission including stocks at suppliers' or customers' premises. In India fire insurance was under tariff till de-tariffing since 1 January 2007. Now it is de-tariffed. With this de-tariffing, the insurers are free to decide the premium rates based on their in-house guidelines and underwriting policy.

Standard Fire Policy: General Guidelines

a. A standard fire policy is applicable to only land-based properties, unless otherwise specifically provided for.

b. "Dwellings" belonging to individuals are insured under the Home Insurance Policy or House Holders' Insurance.

c. The standard fire Policy covering buildings and other contents in the building is to show separately the amounts of sum-insured on: (i) Building; (ii) Machinery and Accessories; (iii) Stock and Stock-in-Process; and (iv) Furniture, Fixtures and

Fittings; (v) Stock in open; and (vi) other contents in the schedule forming the part of the policy.

Valued Policy

In fire insurance the underwriters generally don't issue Valued Policy except for properties such as Curios, Works of Art, Manuscripts, Obsolete machinery and the like in which Market Value cannot be ascertained. The valued policy if issued for any of the above-stated properties will be subject to valuation certificates given by the professional valuer in this regard.

Long Term Policies

Policies for a period exceeding 12 months are not issued except for dwellings in House Holders' Policy for fire risks.

Payment of Premium

Premium shall be paid in full in advance of commencement of risks and shall not be accepted in installments or by deferred payments in any form. It is not permissible to split sum insured of the same property under various policies for different periods of insurance to derive the advantage of installment payment of premium. However two different policies may be issued for stocks and other properties separately where circumstances necessitate issuance of such different policies.

Partial Insurance

An underwriter cannot issue a fire policy for partial insurance of any property. Partial insurance may arise in any of the following circumstances, which is not permissible.

(a) To issue a policy covering only certain portions of a building. However, the plinth and foundations or only the foundation of a building may be excluded.

(b) To issue a policy covering only specified machinery (except Boilers), parts of machines or accessories thereof housed in the same block or building. However, where portions of a building and/or machinery therein are under different ownership, it is permissible for each owner to get insurance cover separately but to the full extent of his interest on the building and/or machinery therein. In such cases, the Insured's interest shall be clearly defined in the policy.

Sum Insured

The policy in so far as it relates to Buildings, Machinery, Furniture, Fixtures, and Fittings & Electrical Installations shall be on Market Value basis, unless specifically covered on Reinstatement value basis. Stocks shall be on Market Value basis only. Sum Insured must represent full value of the property to avoid under-insurance and co-sharing in case of accidental loss or damage to the property insured. The Underlying principle of property insurance is that in exchange for a premium payment the insurer undertakes to indemnify the insured against any financial loss as and when he directly sustains as a result of the happening of an insured event to the subject matter of the insurance. The premium is the price charged by the insurer for the risk he undertakes and this is calculated by applying a rate to the sum insured. It is, therefore, essential that the sum for which the subject matter is insured represents its full value at the time of affecting the insurance and is maintained at the full value throughout the period of insurance cover, for which the insurer is to receive a premium commensurate with the risk.

Adequacy of Sum Insured throughout the Policy Period

If sum insured is less than the full value of the property, there will be under-insurance, implying that he is paying less than 100 per cent of the full premium. Under-insurance on a large scale must inevitably lead to increases in rates of premium for the segment of policyholders concerned, since only by this means the insurer can earn premium income he requires to maintain and build up the funds necessary to meet the claim liability from legitimate claimants during the policy period. Thus the policyholders whose sums insured are adequate and represent full value may be penalized by the actions of those who don't insure the property for the full value and make their proper contribution by way of payment of correct premium to the common fund of the policyholders.

As property insurances are annual contracts, the insured is required to reassess the sum insured at every renewal of the policy. Every insured person should be careful about the adequacy of the sum-insured. The effect of Government budget changes, replacement of older equipment of all kinds by newer or more expensive equipment, the impact of inflation and market price increases, VAT etc., are a few examples of such cases that affect maintaining the adequacy of Sum-insured of the subject of insurance through the policy period, which the insured must keep into mind while he proposes for insurance or renewal thereof.

Reinstatement of Sum Insured

When a loss occurs under a fire insurance policy, the sum is reduced by the amount paid for settlement of a claim, from the time of the loss until the next renewal date. To that extent the contract is deemed to have been completed by the insurers. If the amount insured is required to be restored to the original figure, the policy must be endorsed on payment of an appropriate additional premium on pro rata basis as reinstatement of sum-insured from the date of reinstatement to the next renewal date. But this is not applicable for the fire declaration policy. In this instance the policy wording provides that, following a loss, the sum insured is automatically restored.

Escalation

In consideration of an additional premium to be paid in advance Fire Insurance policy is issued with "Escalation Clause" which allows automatic cover for regular increase in the Sum Insured up to the selected percentage of the sum-insured throughout the period of the policy. Such escalation is generally subject to following terms and conditions:

- The selected percentage for automatic cover for increase shall not exceed 25 per cent of the Sum Insured.
- The Sum Insured at any time would be assessed after application of the Escalation Clause.
- Escalation Clause will apply to policies covering Building, Machinery and Accessories only and but not to any policy covering stock.
- Escalation Clause will apply to all policies and is not restricted to policies issued on reinstatement value basis.
- Pro-rata condition of Average will continue to apply as usual.
- The automatic increase operates from the date of inception up to the date of operation of any of the Insured Perils.

Mid-Term Cover

Generally, it was not permissible to grant mid-term cover for any catastrophic perils like storm, typhoon, flood or inundation (STFI) and Riot, Strike, Malicious Damage (RSMD). Mid-term cover is generally subject to following terms and conditions:

- Insurers must receive specific written advice accompanied by additional premium from the insured for such cover.
- Mid-term cover shall be granted for entire property at any compound or location under one or more policies without any option for selection of property.
- Mid-term Cover shall commence 15 days after the receipt of additional premium.
- Additional premium shall be charged on short period scale on full sum insured for the balance period.

Policy on Reinstatement Basis

Reinstatement, in its widest sense, means the restoration of the property insured to the condition or state in which it was existed immediately before the loss due occurred due to insured perils. In the literal meaning at the event of total loss it may be made by rebuilding the premises damaged or by replacing the goods by similar goods; where there is a partial loss, reinstatement is made by executing the necessary repairs. But the insurance policy is a contract to pay money, and money only for settlement of a claim for any accidental loss. Normally, the insured cannot demand that the insurers reinstate the property in the literal meaning. The insurers also cannot compel the insured to expend on reinstatement moneys, which they have, to pay on settlement of a claim. However reinstatement may arise in the following circumstances:

- by the insurers under the terms of the policy;
- by the insurers under statute; and
- by the insured under statute or contract.

Reinstatement by the Insurers under the Terms of the Policy

If the insurance company elects or agrees to reinstate any property damaged or lost, the insured shall at his own expense produce and furnish to the insurer all such plans, documents, books, and information as the insurer may reasonably require for reinstatement purpose. The insurer shall not be bound to reinstate exactly to the same state as it was before the loss but only up to such extent as circumstances will permit and in reasonably sufficient manner and shall not in any case be compelled to expend more than the sum insured thereon. The operative clause of the policy gives the insurers the option to reinstate, and this condition establishes the rights they will have if they exercise that option. Unless and until the insurers do decide to reinstate, the policy remains only as a contract to pay money in the event of loss. The insured cannot refuse to accept payment of money and demand reinstatement for indemnification of loss. Again, he cannot refuse to accept reinstatement if the insurers elect to reinstate by rebuilding or replacing the goods lost or damaged.

Reinstatement by the Insurers under Statute

Though any policy condition does not provide any time limit within which the insurers must elect to exercise their option of reinstating the property, the option must be exercised within a reasonable time. The insurers are to expressly notify their intention in this regard. Such option can be expressed by the insurers by conduct also making the insured think that they intend to reinstate. In such circumstances, the insured may insist on reinstatement. It would be unreasonable however to expect the insurers to reinstate until they had investigated the extent of the loss or the cost of reinstatement, and their such investigation or examination cannot be taken as an election or option therefore under which they would be bound to reinstate. Once the insurers elect to reinstate, they cannot substitute a different method of discharging their obligations under the policy, and the contract then becomes one to reinstate the property damaged or lost instead of paying a sum of money, and they must make the reinstatement adequately.

Floater Policy

Floater Policy can be issued for stocks at various locations under one Sum Insured (SI) with standard floater clause. It is subject to Standard Declaration clause. Such policy is generally issued subject to following terms and conditions:

- The minimum sum-insured should be such as specified by the company. Generally it is Rs 1 crore in one and more locations and the sun-insured should not be less than Rs 25 lakhs or the amount as specified by the company in at least one of the locations covered.
- Unspecified locations should not be allowed.
- Reduction in SI is not allowed in any circumstances.

- The rate of premium shall be the highest rate in company's guide rate to the insured's stock at any location with a loading of 10 per cent.

- In case, Stocks in process block are covered under floater policy and the rate for the process block is higher than the storage risk, the process rate plus 10 per cent loading shall apply on the whole sum-insured.

- If the stocks situated within go-downs/ process blocks in the same compound are covered under floater policy, no floater extra may be chargeable.

- Other terms, conditions and general regulations of fire insurance shall remain unchanged.

- Thus all discounts including Technical and Discretionary are allowed as per risk inspection and risk analysis.

- If it is a floater Declaration, the rules for Declaration policy will apply over and above rules of floater policy.

- The clause attached to a floater policy is "In *consideration of Floater Extra charged over and above the policy rate the Sum Insured in aggregate under the policy is available for any one, more, or all locations as specified in respect of Stocks. At all times during the currency of this policy The Insured should have a good internal audit and accounting procedure under which the total amount at risk and the locations can be established at any particular time if required. The changes in the address of locations specifically declared at inception should be communicated forthwith".*

Declaration Policy

To take care of frequent fluctuations of in stocks/stock values, Declaration Policy can be issued with standard Declaration Clause subject to following conditions for a fire insurance policy covering stock:

1. The minimum sun-insured must be substantial (Minimum SI is Rs 1 crore in general).

2. Monthly Declaration on: i) average of values at risk on each day of month; or ii) the highest value at risk during the month shall be submitted by the insured by the succeeding month.

3. The basis of valuation for declaration of stock shall be market value.

4. It is not permissible to issue Declaration Policy in respect of:

   - A short period insurance cover

   - Stocks undergoing process

   - Stock in railway sidings

5. Reduction in SI is not permitted during the policy period.

6. Refund of premium on adjustment based on the declarations shall not exceed 50 per cent of the total premium.

7. Declaration policy can be issued on Floater basis subject to following conditions:

   - It is issued for a higher Sum insured (generally Rs 2 crore minimum) with Standard Floater Declaration Clause for stock in different locations under single Sum-insured.

   - If after occurrence of any loss it is found that the amount of last declaration policies previous to the loss is less than the amount that ought to have been declared, then the amount which would be recoverable by the insured on account of loss shall be reduced in such proportion as the amount of said declaration bears to the amount that ought to have been declared.

Floater Declaration Policy

- It can be issued for higher Sum insured (presently Rs 2 crore minimum) with Standard Floater Declaration Clause for stock in different locations under single SI.
- Minimum Retention will be more than 50 per cent (presently 80 per cent)
- Other conditions applicable to Floater Policy and Declaration policy will apply here.

Cancellation of Policy

Following are the two situations when a fire policy may be cancelled:

(a) **At the option of the insured:**

- Retention of premium shall be at Short Period Scale.
- If an existing policy is replaced by a new annual policy covering the identical property, refund of premium may be allowed on pro-rata basis at the original rate for the sum insured replaced.
- If policy is canceled on Government order or for building being demolished, pro-rata refund of premium may be made.
- In case of short period policies, premium will be retained on short period scale.

(b) **At the option of the insurer**:

Refund of premium on cancellation shall be on pro-rata basis.

Standard Fire and Special Perils Policy

Major Parts of Policy

Standard Fire and Special Perils Policy is issued with the coverage of standard fire perils with the agreed or permitted add-on covers for specific properties described in the schedule forming the part of the policy. Policy should be read with proposal form, schedule, specification, endorsements, warranties and clauses as one contract. Policy covering buildings and contents shall show block-wise separate amounts on: i) Building; ii) Machinery; iii) Stocks & WIP; and iv) Furniture & other contents as mentioned earlier.

The policy is generally drafted covering the following aspects distinctly:

- Operating Clause
- Perils Covered
- General Exclusions
- General Provisions
- General Conditions
- Claim Conditions

Operating Clause

The operative clause in a fire policy may be read as: "The Insurer agrees (subject to terms, definitions, exclusions, provisions and conditions of this policy) that if after payment of first premium any of the property insured described in the schedule be lost destroyed or damaged by any of the perils specified in the schedule during the period of insurance or any subsequent period for which the insurer accepts a renewal premium, the Insurer will pay to the Insured the value of the property at the time of its loss or destruction or the amount of damage or at the Insurer's option reinstate or replace such property or any part of it provided that liability under the policy shall not exceed."

Thus, in the whole the total sum-insured or in respect of any item, it is the sum-insured at the time of loss/destruction/damage. The sum-insured remaining after deduction for any other loss or damage occurring during the same period of insurance unless the insurer shall have agreed to reinstate any such SI as mentioned earlier. The operative clause of a fire policy comprises following important aspects:

- There must be consideration, payment of premium by the insured to the insurer in advance.
- The terms, definition, exclusions, provisions and conditions are equally important and indemnity in subject to all of them.
- All the properties to be insured are clearly identified in the schedule to the policy.
- Generally policy is issued on an annual basis and it specified the date and time and commence of risk.
- All perils must be specified in the policy.
- Although the sum insured is shown in the schedule the insurer's liability needs to be further clarified in the policy. Once a claim has been paid, part of the sum insured is used up. The insurer may agree to reinstate the sum insured and this is generally arranged on payment of an additional premium based on the amount of the claim payment from the date of loss for the period up to the next renewal date.
- Insurers have the option to reinstate. This is rarely exercised due to practical difficulties. Generally, cash payment is made for replacements or reinstatement. Occasionally the option may be used if there is a suspicious of fraud or the insured command insists upper insurers' effecting the reinstatement.

Perils Covered

A Standard Fire Policy Covers the following perils:

- Fire
- Lightning

- Explosion/ implosion
- Aircraft Damage
- Riot, Strike & Malicious Damage
- Storm Cyclone, typhoon, Tempest, Hurricane, Tornado, Flood & Inundation
- Impact Damage
- Subsistence and Landslide including Rockslide
- Bursting and/ or overflowing of water tanks and pipes
- Missile Testing Operations
- Leakage from Automatic Sprinkler Installations
- Bush Fire

Add-on Covers

Standard Fire & Special Perils policy can be extended to include the following 'Add on' covers, i.e. Additional Covers on payment of additional premium and with specific endorsements thereof.

- **Architects, Surveyors and Consulting Engineers Fees** may be covered in excess of 3 per cent of claim amount up to a specified sum insured not exceeding 7.5% of claim amount generally at policy rate. Such fees up to 3 per cent of claim amount are admissible in Standard Fire policy if specifically mentioned therein.

- **Removal of Debris** may be covered in excess of 1 per cent claim amount up to a specified sum insured not exceeding 10 per cent of sum insured at policy rate.

- **Deterioration of Stocks in Cold Storage** premises due to accidental power failure consequent to damage at the premises of power station due to an insured peril may be covered for sum insured of stocks generally at 25 per cent of policy rate.

- **Forest Fire** may be covered at policy rate or more up to the policy sum insured.

- **Impact Damage due to the Insured's own Rail/Road Vehicles** may be fork lifts, cranes, tackers and articles dropped there from may be covered generally at 5 per cent of policy rate up to policy sum-insured.

- **Spontaneous Combustion for goods under specified Categories** may be covered at a very minimum rate say, Rs 0.25 to 1 per cent for sum insured of relative items or property. Examples of Spontaneous Combustible items are discussed separately.

- **Omission to Insure Additions, Alteration or Extensions** may be covered at policy rate up 5 per cent of sum insured.

- **Earthquake** may be covered at various rates from Rs 0.10 to Rs 1.00 per cent depending upon location of risks in earthquake zones. In India, the earthquake zones are divided into I to IV for the policy sum insured. Dwellings, offices, hotels, shops are rated at a very lower rate 0.10 per mille regardless of their location zones. Pipelines and its contents located outside the compound or industrial complex passing through different Earthquake zones are covered at flat rate Rs 0.35 per cent or such other rate as the company decides in the underwriting policy.

- **Leakage and/ or Contamination** from tanks are covered at a very high rate from Rs 2 to Rs 10 per mille depending on the nature of cover up to the specified sum insured.

- **Temporary Removal of Stocks clause, Loss of Rent clause, Start up expenses, Molten Material Spoilage etc.,** may be covered after proper risk analysis at different rate of premium with specific endorsements applicable to the specific endorsements.

N.B. *Rates and Percentage of sum-insured mentioned above are guiding ones but are always subject to underwriting policy of individual insurance company and the underwriting policy of the company in the tariff-free regime.*

Minimum Basic Covers in Standard Fire Policy

As per Regulators' guidelines Standard Fire Policy may cover the following minimum perils:

1. Fire (Excl. Spontaneous Combustion, Burning by Order of PA, Forest Fire, Subterranean Fire)
2. Lightning
3. Explosion/ implosion (Excluding damage to boiler, economizer, machinery resulting from own explosion implosion)
4. Aircraft Damage (Ariel/space devices or articles dropped there from
5. Impact Damage (By Rail/Road Vehicle or animal but not owned by the insured or occupier or employees)
6. Riot, Strike, Malicious Damage
7. Leakage from Automatic Sprinkler Installations (Excluding damage caused by repair or alteration to building or repair/ extension of sprinkler)
8. Storm, Cyclone, Typhoon, Tempest, Hurricane, Flood & Inundation
9. Subsidence and Landslide
10. Bursting and/or overflowing of water tanks, apparatus and pipes
11. Missile Testing Operations
12. Bush Fire

Initially the fire policy used to cover only fire peril. All other perils were available as extensions and it was up to the insured to decide his extensions according to his capacity and needs. These extensions were then granted as an endorsement. In 1987, a single fire policy was devised covering a set of perils without any cover for riot or malicious damage. In view of 1984 riots in India where it was found that a large number of fire policyholders had not extended their policy to cover against riot and strike damage perils. So the standard fire policy has been modified to cover perils including fire, explosion/implosion, aircraft, impact damage and riot and strike. Natural or atmospheric perils like storm, cyclone, typhoon, tempest and hurricane, tornado, flood and have been included as basic perils with basic rate. Subsequently, when terrorist activities started in various places of the country, demands came from the insuring public at large for cover against the terrorism risks and then tariff policy was extended to include terrorism perils in the riot and strike cover. Again after 9/11 attack at World Trade Centre the reinsurers stopped issuing cover for terrorism and then Indian insurer treated the cover for terrorism perils as extension with addition premium.

In many advanced countries like UK, Germany, etc., the minimum basic covers are only three and for every additional cover the insured is to pay extra. Similarly, if the insurers in India also reduce the basic minimum covers in Standard Fire policy as per their file & use and Underwriting Policy the insured will pay extra for every additional cover to be granted by insurers with specific terms and conditions contained in the endorsement.

Interpretations of Various Perils in Standard Fire Policy

Some of the perils covered by standard fire policy have been discussed below briefly.

(i) Fire: In order to constitute fire within the meaning of the policy three conditions must be fulfilled:

(a) There must be actual ignition

(b) There must be something on fire which ought not to be on fire

(c) The fire must be accidental or fortuitous in its origin.

Any damage to the insured property proximately caused by fire will be damage by fire whether by the fire itself or the heat and smoke generated from fire. Example of some Fire damages is given below:

- Smoke damage caused by fire
- Water damage in extinguishing the fire
- Property demolished by the Fire Brigade to prevent fire
- Damage done by firemen in executing their duties
- Losses incurred by the insured in attempting to check fire

It has been decided in *Stanley vs. Western Insurance Company* that any loss resulting from an apparently necessary and bona fide effort to put out a fire, whether it would be spoiling the goods by watering or throwing the articles out of the window or even the destroying of a neighbour's house… for the purpose of checking the progress of flames. Fire should be the proximate cause of the loss. Now question may come what is Proximate Cause? Proximate cause means the active and efficient cause that sets in motion a chain of events, which bring about a result without the intervention of any force started and working actively from a new and dependent source.

Exclusion:

Fire in the standard policy exclude damage caused to the Property Insured by

(a) Its own fermentation, natural heating or spontaneous combustion or its undergoing any heating or drying process.

(b) Burning of Property Insured by order of any Public Authority.

(c) Forest Fire

(d) Subterranean Fire

All these exclusions may be covered with additional premium as Add-on cover.

(ii) Lightning: Damage or loss caused to the property insured by lightning is always admissible in Standard Fire Policy almost in every country.

(iii) Explosion/Implosion: Fire due to explosions or implosion are covered by Standard fire policy excluding loss/damage to the following properties (from their own explosion /implosion):

- Boilers, economizers or other vessels (Other than domestic boilers)
- Other Machinery or Apparatus (in which steam is generated)
- Other contents resulting from their own explosion/ implosion caused by centrifugal forces

However damage to the insured property due to a fire caused by an explosion other property insured in the policy is covered provided the explosion is not due to an excluded peril.

(iv) Riot, Strike & Malicious Damage: It includes loss, physical damage or destruction caused to the property insured directly by any external violent means including:

- The act of any person taking part together with others in any disturbance of the public peace (whether in connection with a strike or lockout or not)
- The action of any lawfully constituted authority in suppressing or attempting to suppress any such

disturbance or in minimizing the consequences of any such disturbances.

- The willful act of any striker or locked-out worker done in furtherance of strike or in resistance to a lockout resulting in visible physical damage by external violent means.
- The action of any lawfully constituted authority in preventing or attempting to prevent any such act or in minimizing the consequences of any such act.

But excluding those caused by:

- Total or partial cessation of work or retardation or interruption of any process.
- Permanent or temporary dispossession resulting from confiscation or requisition or destruction by Government Order or Other Lawful Authority.
- Permanent or temporary dispossession of any building or plant or unit or machinery resulting from the unlawful occupation by the insured of such building or plant or unit.
- Burglary, housebreaking, theft, larceny or any such attempt in any malicious act.
- Loss of or damage to the *Property Insured* by explosion or otherwise caused by an act of terrorism committed by a person(s) acting on behalf of any organization.
- The action of any lawfully constituted authority in suppressing or attempting to suppress any such act.

If the insurer alleges that the loss or damage is not caused by an malicious act, the burden of proving the contrary shall lie upon the insured.

(v) Storm, Cyclone, typhoon, tempest, hurricane, tornado, flood and inundation: Loss or damage directly caused by Storm, Cyclone, Typhoon, Tempest, Hurricane, Tornado, Flood or Inundation excluding those resulting from earthquake, Volcanic eruption or other convulsions of nature.

(a) Seventy Two Hours Clause for Storm Peril

The Insurer are liable for any loss or damage occurring for a period up to maximum 72 hours after the expiration of this policy, provided that the first storm damage occurs prior to the date and time of the expiration of this policy. Each loss by windstorm shall constitute a single claim hereunder provided, if more than one windstorm shall occur within any period of 72 hours during the of the policy period and such windstorm shall be deemed to be a single windstorm within the meaning thereof.

(b) Seventy two hours Clause for Flood

Insurers shall not be liable for any loss caused by flood occurring before the effective date and time of this policy nor for any loss commencing after the expiration date and time of this policy. But the Insurer shall be liable for any loss or damage occurring for a period of up to maximum 72 hours after the expiration of the policy, provided that the first flood damage occurs prior to the date and time of the expiration of the policy. Each loss caused by flood and all losses caused by flood within a 72 hours period shall be deemed to constitute a single loss.

(vi) Impact Damage: Such damages include:

- Loss or damage caused to property by any rail/road vehicle
- Loss or damage by animal

Provided the said vehicles or animals do not belong to the insured.

(vii) Subsidence and Landslide: Loss or damage by Subsidence and Landslide perils are covered by standard fire policy, but the following are excluded from standard cover:

- Normal cracking or bedding down of new structure
- Coastal or river erosion
- Defective design or workmanship of any structure or plant & machinery
- Demolition, construction or repair of construction

General Conditions in Standard Fire Policy

Every Standard Fire Policy contains the following conditions the breach of which by the insured makes the contract voidable at the option of the insurer. Please note that the conditions mentioned hereinafter are quoted from the Standard Fire Policy to avoid any distortions or misunderstanding.

1. This policy shall be voidable in the event of misrepresentation, mis-description or non-disclosure of any material particular.

2. All insurances under this policy shall cease on expiry of seven days from the date of fall or displacement of any building or part thereof or of the whole or any part of any range of buildings or of any structure of which such building forms part. Provided such a fall or displacement is not caused by insured perils, loss or damage which is covered by this policy or would be covered if such building, range of buildings or structure were insured under this policy. Not withstanding the above, the Company subject to an express notice being given as soon as possible but not later than seven days of any such fall or displacement may agree to continue the insurance subject to revised rates, terms and conditions as may be decided by it and confirmed in writing to this effect.

3. Under any of the following circumstances the insurance ceases to attach as regards the property affected unless the insured, before the occurrence of any loss or damage, obtains the sanction of the company signified by endorsement upon the policy by or on behalf of the company:

- If the trade or manufacture carried on be altered, or if the nature of the occupation of or other circumstances affecting the building insured or containing the insured property be changed in such a way as to increase the risk of loss or damage by insured perils.

- If the building insured or containing the insured property becomes unoccupied and so remains for a period of more than 30 days.

- If the interest in the property passes from the insured otherwise than by will or operation of law.

4. This insurance does not cover any loss or damage to property which, at the time of the happening of such loss or damage, is insured by or would, but for the existence of this policy, be insured by any marine policy or policies except in respect of any excess beyond the amount which would have been payable under the marine policy or policies had this insurance not been affected.

5. This insurance may be terminated at any time at the request of the insured, in which case the company will retain the premium at customary short period orate for the time the policy has been in force. This insurance may also at any time be terminated at the option of the company, on15 days notice to that effect being given to the insured, in which case the company shall be liable to repay on demand a retable proportion of the premium for the unexpired term from the date of the cancellation.

6. On the happening of any loss or damage the insured shall forthwith give notice thereof to the company and shall within 15 days after the loss or damage, or such further time as the company may in writing allow in that behalf, deliver to the company:

   - A claim in writing for the loss or damage containing as particular an account as may be reasonably practicable of all the several articles or items or property damaged or destroyed, and of the amount of the loss or damage thereto respectively, having regard to their value at the time of the loss or damage not including profit of any kind.

- The Insured shall at his own expense, produce, procure and give to the company all such further particulars, plans, specification, books, vouchers, invoices, duplicates or copies thereof, documents, investigation reports (internal/external), proofs and information with respect to the claim and the origin and cause of the loss and the circumstances under which the loss or damage occurred, and any matter touching the liability or the amount of the liability of the company as may be reasonably required by or on behalf of the company together with a declaration on oath or in other legal form 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.

- In no case whatsoever, the insurer shall be liable for any loss or damage after the expiry of 12 months from the happening of the loss or damage unless the claim is the subject of pending action or arbitration.

- If the insurer disclaims liability for any claim hereunder and such claim shall not have been made the subject matter of a suit in a court of law within 12 calendar months from the date of the disclaimer then the claim shall for all purposes be deemed to have been abandoned and shall not thereafter be recoverable hereunder.

7. On the happening of loss or damage to the property insured, the company may:

   - Enter, take and keep possession of the building or premises where the loss has happened.

- Keep possession of any such property and examine, sort, arrange, remove or otherwise deal with the same, sell any such property or dispose of the same for account of whom it may concern.

The powers conferred by this condition shall be exercisable by the insurer at any time until notice in writing is given by the insured that he makes no claim under the policy, or if any claim is made, until such claim is finally determined or withdrawn.

If the insured shall not comply with the requirements of the insurer or shall hinder or obstruct the insurer, in the exercise of its powers hereunder, all benefits under this policy shall be forfeited. The insured shall not in any case be entitled to abandon any property to the company whether taken possession of by the company or not.

8. If the claim be in any respect fraudulent, or if any false declaration be made or used in support thereof or if any fraudulent means or devices are used by the insured or any one acting on his behalf to obtain any benefit under the policy or if the loss or damage be occasioned by the willful act, or with the connivance of the insured, all benefits under this policy shall be forfeited.

9. If the company at its option, reinstate or replace the property damaged or destroyed, or any part thereof, instead of paying the amount of the loss or damage, or join with any other company or insurer(s) in so doing, the company shall not be bound to reinstate exactly or completely but only as circumstances permit and in reasonably sufficient manner, and in no case shall the company be bound to expend more in reinstatement than it would have cost to reinstate such property as it was a the time of the occurrence of such loss or damage nor more than the sum insured by the company thereon. If the company so elect to reinstate or replace any property the insured shall at his own expense furnish the company with such plans, specifications, measurements, quantities and such other particulars as the company may

require, and no acts done, or caused to be done, by the company with a view to reinstatement or replacement shall be deemed an election by the company to reinstate or replace. If in any case the company is unable to reinstate or repair the property hereby insured, because of any municipal or other regulations in force affecting the alignment of streets or the construction of buildings or otherwise the company shall, in every such case, only be liable to pay such sum as would be requisite to reinstate or repair such property if the same could lawfully be reinstated to its former condition.

10. If the property insured shall, at the breaking out of any fire or at the commencement of any damage to the property by any other insured peril be collectively of greater value than the sum insured thereon, then the insured shall be considered as being his own insurer for the difference and shall bear a ratable proportion of the loss. Every item, if more than, covered by the policy shall be separately subject to this condition.

11. If at the time of any loss or damage happening to any property insured there be any other subsisting insurance whether effected by the insured or any other person covering the same property, this company shall not be liable to contribute more than its ratable proportion.

12. The insured shall at the expense of the company do and concur in doing, all such acts and things as may be necessary or required by the company for the purpose of enforcing any rights and remedies or of obtaining relief or indemnity from other parties to which the company shall be or would become entitled or subrogated, upon its paying for or making good any loss or damage under this policy, whether such acts and things shall be required before or after indemnification by the company.

13. If any dispute arises as to the quantum to be paid under this policy (when liability is otherwise admitted) such difference shall independently of all other questions be referred to the decision of a sole arbitrator to be appointed in writing by the

parties to or if they cannot agree upon a single arbitrator within 30 days of any party invoking arbitration, the same shall be referred to a panel of three arbitrators, comprising of two arbitrators, one to be appointed by each of the parties to the dispute/difference and the third arbitrator to be appointed by such two arbitrators and arbitration shall be conducted in accordance with the provisions of the Arbitration and Conciliation Act, 1996.

14. Every notice and other communication to the company required by these conditions must be written or printed.

15. At all times during the period of insurance the insurance cover will be maintained to the full extent of the respective sum insured in consideration of which, upon the settlement of any loss under the policy, pro-rata premium for the unexpired period from the date of such loss to the expiry of period of insurance for the amount of such loss shall be payable by the insured to the company. The additional premium referred above shall be deducted from the net claim amount payable under the policy. This continuous cover to the full extent will be available notwithstanding any previous loss for which the company may have paid hereunder and irrespective of the fact whether the additional premium as mentioned above has been actually paid or not following such loss.

Rule for Deletion of STFI & RSMD and Reduction in Premium Rate

It is permissible to exclude Storm, Tempest, Flood, and Inundation (STFI) and Riot, Strike, Malicious Damage (RSMD) for reduction in premium rates at inception only but not in the middle of currency of policy. The deletion applies to entire property but not to any part of the interest of the policy. In the tariff regime, the reduction of premium rate was Rs 0.25 per mile and 0.10 per mile for deletion of STFI and RSMD respectively. However with the full freedom in pricing, the individual underwriters may decide covers, exclusions, terms, conditions etc., according to their own corporate experience, underwriting policy and reinsurance programme, but obviously subject to compliance of IRDA requirements on “File and Use”.

Fire Risk Inspection for Fire Underwriting

In earlier chapter we have elaborately discussed the role and process of risk management in general insurance underwriting. Now we will discuss the specifically a few aspects of risk inspection for risk analysis, risk evaluation for insurance underwriting. For fire insurance underwriting, a construction, occupancy, protection, and external exposures (COPE) study is very essential for identifying and assessing physical hazards as discussed earlier also.

Construction

Out of the four COPE elements, construction always remains as a key factor in underwriting of fire insurance for its major role in loss prevention. Construction is a tangible property characteristic that underwriters should analyze and evaluate at the very first stage of risk inspection. The nature and quality of construction of a property are less likely to be changed frequently than are the nature and quality of occupancy, protection, and external exposures. The construction of a building has a direct impact on the extent of possible damage that a fire peril can cause. Furthermore, the quality construction always provides capacity to resist damage from other perils like AOG perils also. For better analysis of construction quality for risk inspection, the following aspects are being discussed below:

(a) Structural Features

Underwriters should be concerned with how various structural features will resist the fury of a fire and how the structural features contribute to the spread or containment of fire. Additionally, structural features are important in analyzing the effects of other perils on the structure.

(b) Fire Resistance and Flame Spread

In determining the appropriate classification for a particular structure, underwriters often analyze the fire resistance materials used in construction. In the interior of buildings, the flame spread of the interior construction materials is an important consideration. Interior materials or finish consist of material used for interior surfaces of walls and ceilings. Interior finish includes items like carpets, ceiling tiles, wallboard, insulating materials, and decorative materials.

(c) Fire Resistance

Fire resistance refers to the ability of a structure or material to withstand and contain the fury and rage of a large-scale or severe fire. Fire resistance is evaluated by exposing structural elements to fire in a controlled setting. Materials are classified by their fire-resistance capabilities, according to the Standard Methods of Tests of Fire Endurance of Building Construction and Materials. The rating largely depends on structural integrity, not to the degree of damage that may arise if fire occurs. During risk inspection the engineer must carry out an exhaustive test to evaluate the likelihood that an actual structure made of such materials that would survive a fire under certain conditions and to the certain extent.

(d) Flame Spread

The flame spread of materials is assessed by using a test tunnel. In this test a standard gas fire is applied at one end of the tunnel, and the rate of flame spread is measured. As a baseline of the evaluation of materials and to determine whether the test tunnel is set to the uniform conditions, a relative scale has been created using a piece of red oak and a piece of asbestos cement board. It is a very elaborate process which fairly helps an risk Engineer to assess the rate of flame spread in a construction.

(e) Layout of Building

It is important consideration for determination of physical hazards associated with the property insured. Following are the major factors in this regard:

- Spacing between Process block, storages and Administrative Blocks to assess PML

- o Spacing between compound wall and Process and storages blocks
- o Location of incinerator
- o Height, Length and Nature of communicating
- o How many stories are there?
- o If storied, whether staircase is segregated?
- o RCC roof/RCC intermediate floor/RCC support (50mm concrete)?
- o Any combustible false ceiling/wall lining used?
- o Whether ducting connecting various compartments?
- o Whether floor to floor communication?
- o Whether window/door opening provided for every 100 M?
- o Whether wooden intermediate floor?
- o Whether Roof and intermediate floors made of RCC construction?

(f) General Classifications of Construction for Earthquake Risks Underwriting

Class A Construction:

- RCC framed structures with RCC walls
- RCC and/or Steel framed structure
- Metal /glass/wooden cladding

Class B Construction:

- RCC and/or Steel framed structures with panel walls of

- Brick/ stone/ concrete blocks wooden framed structures
- Metal/glass/wooden cladding

Class C Construction:

- Pre-fabricated structures, structures having load bearing walls
- Wooden framed structures
- With panel walls of brick/stone/concrete blocks

(g) Other Considerations in Respect of Construction for Fire Underwriting

- Segregation between hazardous and non hazardous areas
- Segregation of internal staircases/external staircases
- Communication through passage/gangway/duct etc and their segregation
- Perfect party walls
- Segregation of other openings
- Air conditioning/ventilation
- Electrical services
- Materials handling
- Separation of floors
- Materials and Thickness
- Separating distance from compound wall by 4 m
- Separating distance from surrounding process plants/ storage area/tanks by 10 m

- Provision of two gates of size 6 m & 4 m and roads of width 4 m
- Provision of hand appliances and hydrant system with a stand by pump

Occupancy

Occupancy, i.e. the use of the building is a prime consideration in property underwriting like other prime considerations including construction, protection and external exposures. The underwriter shall consider the combustibility of contents and the amount of heat that contents will release. Occupancy hazards analysis is an important consideration for prudent underwriting not only for rating, but also conditioning the risks with appropriate warranties.

(a) Major Areas for Occupancy Hazard Analysis;

- Nature of occupancy
- Manufacturing activity
- Incidental operation in manufacturing location
- Utility activity in manufacturing location
- Auxiliary function in manufacturing location
- Office area in manufacturing. location
- Storage in manufacturing complex
- Nature and use of Storage complexes (go-downs & tank farms)
- Independent utilities and their purposes and provisions
- Commercial centers and activities (shops, hotels etc.)
- Dwellings, amusement parks and the like

(b) Properties and Compositions of Materials (Raw Materials, Finished Stock etc)

- Flammability
- Spread of fire
- Reactivity
- Toxicity
- Reaction with water
- Flash point

Protective Measures

In hazards and risks analysis for fire underwriting, the inspection of Fire Extinguishing Arrangements (FEA) and risk improvement measures is very vital. For this purpose the following aspects need to be considered:

(a) Fire Protection Systems

- Hand appliances
- Trailer pumps/fire engines
- Hydrant Systems
- Sprinkler systems
- Fixed water spray systems
- Fixed Foam Installations
- Clean Agent Fire Extinguishing Systems

(b) Hand Appliances — Basic Requirements

- Types and capacity of fire extinguishers,
- Coverage of Area
- Selection of locations
- Spares
- Adequacy

(c) Hydrant System — Main Components

- Pumps, Water reservoirs, Pipe lines, Isolation valves
- Hydrant landing valves (single/double hydrants)
- Number of hydrants/monitors required
- Pumping capacity/location of pump house
- Water reservoir capacity, Spacing of hydrants/monitors
- Pipe sizes and layout of pipes, Isolation valves (number and locations)
- Adequacy

(d) Trailer Pumps/Fire Engines — Certain Considerations

- Suitability in view of LH and OH occupancies
- Requirement of trailer pumps/fire engines
- Requirement of spares
- Adequacy

- Water source (static tanks, capacity)
- Limitations (a height of coverage)

(e) Sprinkler System

- Occupancy (light/ordinary/high) of the building
- Density of occupancy
- Pressure and flow water
- Spacing of sprinklers and pipe sizes
- Selection of sprinkler installation valve
- Various types of Automatic Sprinklers
- Water Spray or fog system
- Air Foam System
- Carbon Dioxide System
- In-rack Sprinkler System
- Early Suppression fast response (ESFR) Sprinkler

Matters to be Covered in Risk Inspection Report

After every risk inspection a detailed report is to be prepared. This report is to be thoroughly examined by the underwriters for deciding terms, conditions, warranties and rates according to risk exposures for the policy to be issued. This report must contain the following information:

(a) Basic Information & observations

- COPE analysis as discussed in point

- Process details
- Storage details
- Claims experience details

Such report shall provide facts, figures, information and observations on each and every aspect with reference to probability and severity of loss by fire perils.

(b) General Loss Prevention & Risk Improvement Measures

- Whether operators are qualified for their jobs and are aware of hazards?
- Whether management has provided adequate facilities to prevent/reduce hazards?
- Whether there are written operating instructions for safe running of the plant and for emergencies?

(c) Maintenance

- What types of maintenance are provided by Management, predictive, preventive or Breakdown, history of breakdown and time taken for repairs, maintenance of records?
- Details of maintenance contracts for specific equipment/ machines.
- Management's perception and policy on protection and maintenance of critical machines.
- A list of critical machines, its overhauling and maintenance schedule.

(d) Electrical Installations

- Whether Electrical Installations meet with relevant electrical installations regulation with specific reference to the Flame Proof Areas?

- Whether Electrical Installation needs to be improved.
- Whether it is under supervision of professionals.

(e) Safety

- Whether the company has a Safety Policy?
- Organization & supervision of Safety Department.
- Safety Awareness, Records, Training.
- Safety Drills (including Evacuation process).
- Accident Investigation Procedures.
- Details of disaster management plan, policy and programme and its effectiveness.
- Implementation of recommendations of the Safety Committees.

(f) Fire Protection Measures

- Management's policy for identification of Fire Hazards and Protection therefrom.
- Comments on adequacy and maintenance of Fire Protection Installations.
- Records of mock drills.

(g) Security

- Security organization, system and control of vehicle entry.
- Engineer's comments on adequacy of security.

- Whether area/ risk is sensitive to terrorist elements?

(h) Housekeeping

Checklist duly filled in together with the Engineer's observations.

(i) Probable Maximum Loss

Estimates of Probable Maximum Loss & Basis

(j) Other Details

- Age of plant and general observations on the condition of the plant.
- Details of claims experience for all covers / perils.
- History of cat hazards/ events at the locations viz. Earthquakes, STFI, subsidence etc.
- Machinery Loss of Profit detailed inspection
- Overall recommendations of the Engineer.

Rating Method for Fire Risks

Today there is no tariff. Insurers are free to decide or fix the price for the products (insurance policies) they are selling. There is no binding on the insurers for following the tariff. They determine price for the products according to their own cost structure based on their underwriting philosophy, policy and process, reinsurance policy and programme and risk management policy and programme as mentioned earlier. Therefore, rating method of the underwriters has been changed fundamentally in the free market. Generally, the underwriters follow an elaborate process in this regard. The method common followed by the insurers for Fire Department is briefly discussed below. Please note that the method discussed below is an example individual underwriters devise and develop their own method according to their convenience and policy.

Categorization of Products

The first two products are classified into following two groups on the basis of sum-insured:

- **Class-Rated Products** — Up to a specified limit of Sum-insured (say Rs. 5 crs) of material damage

- **Individual-Rated Products** — Beyond specified limit of Sum-insured on material damage

The other two products are underwritten only as Individual Rated Products provided the minimum sum insured is substantially large say Rs 100 crores for Industrial All Risks Insurance (IAR) and say, Rs 50 crores for Petrochemical Risk. The limits may vary from company to company as per their underwriting policy and File and Use requirements.

Underwriting Procedure of Class-Rated Products

1. The Corporate Underwriters prepare Internal Guide Rates Manual to be used by the line- underwrites in the Operating Office.

2. Line Underwriters analyze and evaluate the risks before acceptance.

3. Based on analysis the line underwriters consider discounts and decides terms, conditions and rates.

4. Discount for class-rated products are of two types: Technical and Discretionary Discounts.

5. Technical discounts are based on two factors: Construction and Claims Experience.

6. Discount for Standard construction is generally allowed up to 10 per cent.

7. Claims Experience Discount is generally allowed on various slabs, i.e. Claims Experience up to 40 per cent. Discount

allowed may be 10 per cent and Claims Experience up to 60 per cent. Discount allowed may be 5 per cent. The said claims experience is based on incurred claims ratio for preceding 36 months. For this purpose, total experience of all the policies in the name of the insured at any one complex/ compound shall be taken into account. However the loss due to storm, typhoon, flood or inundation (AOG) perils shall not be taken into account for the purpose of calculation of claims experience.

8. Discretionary Discount may be allowed by the line underwriters up to say another 10 per cent depending upon the situation to retain the renewal business of the particular client considering his less morale hazards based on professional approach and functioning, Internal Control Environment, very good accounting and administrative control etc.

9. Terrorism Risks are not subject to above Technical or Discretionary discounts.

10. Rating Method

    - Rate as per Guide Rate
    - Less: Rate for rate for deletion of STFI or RSMD (Riot, Strike and Malicious damage
    - Add: Rate for Add on Perils like Earthquake, Spontaneous Combustion etc. as discussed earlier
    - Technical Discount up to the limits specified
    - Discretionary Discount up to the limits specified
    - To Arrive at Net Rate
    - Add: Premium for Add-on Covers, if opted
    - Add: Premium on Terrorism Risks at the prescribed rate

- To Arrive Total Premium
- Add: Service Tax at the prevailing Rate

11. Rates are on Gross basis, i.e. including commission, brokerage as the case may be. In case business comes directly without intermediary, the guide rates can be reduced to the extent of commission/brokerage payable on it.

12. Short period Cover is rated as pro-rata premium + 10 per cent (if issued or renewed for less than 12 months or canceled at the request of the insured)

Underwriting Procedure of Individual-Rated Products

1. Nominated underwriters in Regional Office and Head Office underwrite individual-rated products: Individual-rated products include large and critical risks. Even the small risks within the acceptance limits of line underwriters (i.e. in branches) may be referred to nominated underwriters for approval for higher discount treating the same as Individual Rated Product underwriting. The following is the procedure followed for rating large or critical risks.

2. The Nominated Underwriter will examine the proposal form duly filled up by the insured.

3. He will also examine the risk inspection report by the risk engineer who will carry out the risk-inspection in the manner prescribed in the corporate risk inspection manual or guidelines.

4. Rating will follow the base-rate as the starting point, while discounts to be allowed will be of higher rates based on detailed risks analysis as mentioned below.

5. Technical Discount is calculated on the basis of marks allotted for physical features and claims experience and Fire Extinguishing Arrangement (FEA).

6. Marks for calculation of Technical Discounts are split into: i) Physical features; and ii) Claims Experience in certain ratios as per corporate underwriting policy

7. Physical Features Marks for Technical Discount are generally decided on the following aspects:

   - Age of the plant
   - Security Arrangement
   - Proneness to flood due to location of nearby rivers
   - Construction of blocks
   - Spacing of utilities like boiler, furnaces from the storage or process or manufacturing areas
   - General conditions of electrical installations including lightning arrestor system, plant earthing
   - No open storage of combustible materials
   - Process/ storage blocks at higher elevation compared to ground level
   - Nearness of Public Fire Brigade (Response time up to 15 minutes)
   - Safety Management System (Safety Depot, System and procedures for fire safety, Tragedy of employees and emergency management

8. Claim Experience marks are decided on the average incurred claim ratio for preceding 3 years.

9. FEA Arrangement Marks depend on the following aspects:

   - Hand Appliances & Trailer Pump Engines
   - Hand Appliances & Hydrant Systems

- Hand Appliances & Independent Sprinkler/ Fixed Water Spray SystemHand Appliances, Hydrant System and Fixed Water Spray System

10. Technical Discounts are finally decided by the nominated underwriter on Total Marks in a particular scheme as per underwriting policy of the company.

11. Scheme of Marks may be devised in a manner like: i) For total marks not exceeding 10, Discount will be say Nil; ii) Total Marks between 11 & 20, Discount will be 3 per cent; iii) Total Marks between 21 & 30, Discount will be 6 per cent; iv) Total Marks between 31 & 40, Discount will be 9 per cent; v) Total Marks between 41 and 50, Discount may be 10 per cent and so on.

12. Total Discounts, which may be sometimes more than 50 per cent depending upon the merits of the risks for Merit Rating. Merit Rating requires exhaustive analysis of both physical hazards and morale hazards while no element of moral hazards are insured.

A Case Study on Underwriting of Individual-rated Products

Let us study the following hypothetical case for better understanding of the method and process of underwriting of individual-rated products by a general insurance company:

Description of the Insured and Risks in a Data Sheet

1. Name of the Insurer; Diamond Insurance Co Ltd.

2. Name of the insured; M/s Bengal Bottlers Ltd.

3. Location of Risk; Near the bank of Hoogly River, West Bengal; in E.Q Zone III

4. A proposal for renewal of renewal of a fire policy for total sum-insured of Rs 14 crores

5. The risk with SI of Rs 14 crores is within the acceptance limit of branch manager

6. Occupation of the proposer; Bottling Plant for soft-drink

7. The proposer has been in the books of the insurer (India Insurance General) since 1990 for all types of required insurances covers being Fire, Machinery Break down, Marine, Burglary, Group Personal Accident Insurance, Group Mediclaim, Employers' Liability Insurance, Public Liability Insurance and Product Liability Insurance.

8. Total premium potentiality for all covers of the client ; Rs 20 lacs including dails of the premium and claim experience for last 3 years; (For Fire Policy only) given in Table-15 below.

Table-15: Details of Premium Claims

Year	Dept	Premium in Rs	Claims	Ratio
2006-07	Fire	2.20 lacs	Nil	Nil
2007-08	Fire	1.15 lacs	Nil	Nil
2006-09	Fire	0.75 lacs	Nil	Nil

9. Cover required in renewal; Fire excluding STFI and RSMD

10. Basic Rate Rs 1.05 per cent.

11. Net Rate with exclusion for STFI and RSMD; (1.05-0.10-0.25) : 0.70

12. Guide rate of Premium @ Re 0.70 per cent

13. Branch Manager is authorized to allow 26 per cent Discount (Tech @16 per cent+ Discretionary 10 per cent)

14. After allowance of 26 per cent Discount premium comes to say Rs 72,520. It is within acceptance limit of Rs 75 crores for Branch Manager.

15. But M/S India Insure Ltd, one competitor has quoted premium for the business for Rs 62,000, which the Insurer came to know from some reliable source.

16. The existing insurer, the branch manager of Diamond Insurance Co Ltd wants to give more discount to retain the profitable business and total premium potentiality of Rs 20 lacs for all policies with the insured. As the branch manager does not have the authority to allow discount more than 26 per cent, it will be referred to the nominated underwriter for underwriting of this class-rated product as individual-rated product.

17. Branch Manager referred the proposal for renewal with his recommendation for premium rating @0.43 per cent with existing terms and conditions.

18. After thorough examinations of business proposal and being satisfied the risk analysis with reference to the under-mentioned documents the nominated underwriter agree for 57 per cent discount as recommended by the branch manager (line-underwriter)

19. While scrutinizing the following documents for granting higher discount he is required to be sure that the estimated risk costs is less than the premium amount to be charged for risks being accepted.

Major Documents Required for Underwriting of Individual Rated Products

- Previous Policy Copy
- Proposal for renewal
- Data Sheet giving all particulars required for analysis of physical and morale hazards
- Risk Inspection Report by Company engineer or other professional engineer
- Merit Rating Sheet showing total marks allotted for the risks
- Claim Experience for last 4/ 5 years
- Other Policy details along with claim experience

- Special Loss Prevention Measures
- Recommendation with reasons for 53% discount
- Premium Calculation sheet

Classification of Materials for Spontaneous Combustion Cover

For extension of standard fire policy with Add-on cover for Spontaneous Combustion the combustible materials are classified according to severity of Spontaneous Combustion properties. Examples of a few Spontaneous Combustible items arranged in the degree of combustibility are shown in Box-1 to Box-4.

Box-1: Category I (Low or Non-existent)
• Acetone
• Acids (Except stearic acids)
• Bamboo Stock
• Betel nuts, Beedi Leaves
• Bitumen
• Castor Oil, Olive Oil, Palm Oil
• Caustic Soda
• Celluloid Tubes
• Petrol,
• Plastic Goods
• Groundnut Oil
• Many others (about 70 items)

Box-2: Category II (Moderate)
• Cotton Seed Oil
• Fertilizer
• Foam Rubber goods

- Hay & Grass
- Hydrogen Peroxide
- Rice bran and Rice Husk
- Rice Straw
- Solvent extraction
- Soya bean Oil
- Oil Cake –loose or in bags
- Pine Oil, Tarpaulin, Olive Oil
- Red Oil Urea, Whale Oil

Box-3 Category III (Variable)

- Chemicals (not specified otherwise
- Coal tar, Colours, Dyes, Chemicals
- Fire Wood, Filter Cloth
- Gunnies, Oily cotton,
- Paints and Varnish, Sodium Nitrate
- Super Phosphate, Synthetic Resins
- Yellow phosphorus, Stearic Acids

Box-4 Category IV (High)

- Alfalfa Meal, Cod Liver Oil
- Corn Meal Feeds, Empire cloth
- Fish Meal, Fish Oil, Fish Manure
- Linseed Oil, Lard Oil/ animal oil
- Nitro Cellulose Lacquers
- Oiled Fabrics, Oiled Silk
- Oiled Rags, Synthetic Enamels
- Waste of all kinds, Sponge Iron

General Exclusions in Fire Insurance Policy

Fire Policy excludes any loss, damage, cost or expense of whatsoever nature directly or indirectly caused by, resulting from or in connection with any of the following perils regardless of any other cause or event contributing concurrently or in any other sequence to the loss:

i. Political Risks Exclusion

(a) War (whether declared or not), invasion, acts of foreign enemies, hostilities or warlike operations, civil war, rebellion, revolution, insurrection, mutiny, conspiracy, military or usurped power, confiscation, nationalization, commandeering, requisition or destruction or damage by or under the order of any government *de jure* or *de-facto* or by any public or local authority.

(b) Any act of terrorism if terrorism is not covered additionally. For the purpose of this clause an act of terrorism means an act, including but not limited to the use of force or violence and/or the threat thereof, of any person or group(s) of persons, whether acting alone or on behalf of or in connection with any organization(s) or government(s), committed for political, religious, ideological, or ethnic purposes or reasons including the intention to influence any government and/or to put the public, or any Section of the public, in fear.

ii. Radioactive Contamination

Nuclear reaction or nuclear radiation or radioactive contaminations whether controlled or uncontrolled, and whether such loss be direct or indirect, proximate or remote, or be in whole or in part caused by, contributed aggravated by the peril(s) mentioned hereunder:

(a) Ionizing radiations from or contamination by radioactivity from any nuclear fuel or from any nuclear waste or from combustion of nuclear fuel;

(b) The radioactive, toxic, explosive or other hazardous or contaminating properties of any nuclear installation, reactor or other nuclear assembly or nuclear component thereof;

(c) Any weapon of war, missile or like employing atomic or nuclear fission and/or fusion or other like reaction or radioactive force or matter; and

(d) Nuclear reaction, nuclear radiation or radioactive contamination.

iii. Act of default

Any act of default committed by the insured or its representatives.

iv. Deductibles

The amounts mentioned in the schedule as being the deductibles, time excess or otherwise.

v. Pollution and Contamination

Damage caused to the insured property by pollution or contamination excluding

(a) Pollution or contamination which itself results from a peril hereby insured against.

(b) Any peril hereby insured against which itself results from pollution or contamination.

Rules and Methods for Endorsements to Standard Fire Policy for Add-On Covers

As mentioned in Para 9.18 certain Add-on covers are provided on payment of additional premium up to the limits specified in the schedule but subject to the terms and endorsements outlined below. Here endorsements for certain more extensions are briefed.

Add-on Cover for Fees of Architects, Engineers and Others

Indemnity shall include fees of Architects, Engineers, Surveyors, Engineers, Legal and other Consultants reasonably and necessarily incurred for the purpose of replacement/reinstatement and/or any other insured undertaking consequent upon an occurrence hereby insured but not for preparing claims. The amount payable for such fees shall not exceed the limit specified in the schedule.

Add-on Cover for Cost of Demolition and/or Removal of Debris

The insurance by specific endorsement for such Add-on cover extends to indemnify costs and expenses necessarily incurred by the insured with the consent of the Insurer in:

(a) Removing debris

(b) Dismantling and/or demolishing

(c) Shoring up or propping of any portions of the *Property Insured* by the said items which have sustained Damage. The liability of the insurer shall not exceed the Inner Limit of Liability stated in the Specification. The Insurer will not pay for any costs or expenses:

 (a) Incurred in removing debris except from the site of such property which has sustained damage and the area immediately adjacent to such site.

 (b) Arising from pollution or contamination of property not insured by this Section.

Terrorism

As per specific endorsement such Add-on cover does not indemnify loss of or damage caused by:

- Total or partial cessation of work or the retardation or interruption or cessation of any process or operations or omissions of any kind.
- Permanent or temporary dispossession resulting from confiscation, commandeering, requisition or destruction by order of the Government or any lawfully constituted Authority.
- Permanent or temporary dispossession of any building or plant or unit of machinery resulting from the unlawful occupation by any person of such building or plant or unit or machinery or prevention of access to the same.
- Burglary, housebreaking, theft, larceny or any such attempt or any omission of any kind of any person (whether or not such act is committed in the course of a disturbance of public peace) in any action taken in respect of an act of terrorism.
- Loss or damage, cost or expenses of whatsoever nature directly or indirectly caused by or resulting from or in connection with any action taken in controlling, preventing , suppressing or in any way relating to action taken in respect of any act of terrorism.

Inadvertent Omissions

The Add-on cover for Inadvertent Omissions is subject to a specific endorsement as follows. The Insured having notified the Company of his intention to insure all property in which they are interested and it being their belief that all such property is insured, if any such property are found to have been inadvertently omitted, the Company will deem it to be insured within the terms of this Policy on payment of additional premium on all such property as from the inception of this Policy, provided that as soon as the Insured is aware of such error or omission, full details are declared to the Company immediately.

Capital Additions

Policy may be extended to include the following cover in so far as the same are not otherwise insured:

- Any newly acquired machinery and plant or newly constructed buildings, and alterations additions and improvements to buildings subsequent to a certificate of completion; and

- Alterations, additions and improvements to machinery & plant, at the Insured Locations, but not in respect of any appreciation in value during the current Period of Insurance, provided that the Insured undertakes to give particulars within 15 days of commencement of the Insurer's liability and to effect specific insurance before the expiry of the Period of Insurance and to pay an additional premium on demand.

Expenses for Loss Minimization

The policy may be extended to indemnify the expenses incurred by the Insured for loss minimization necessarily or to prevent any aggravation of an insured loss following a loss or damage at the insured's premises including moving/shifting of property if this contributes to loss minimization, subject to a limit per loss as per schedule, but obviously on payment of additional premium.

Start-up/Shut-down Cost

This extension covers actual loss sustained due to specified start-up / shut-down costs for power and utilities such as electricity, water, steam, gas as well as feedstock, fuels or combustibles to reestablish the plant in the operational state it was at the time of the damage in a normal start-up procedure and subject to the sub-limit in the Schedule.

Rules for Interpretation of Policy Terms and Conditions

i. Identification

As mentioned earlier Policy of fire insurance along with the Schedule (which forms an integral part of this Policy) shall form the entire agreement between the Insurer and the Insuring Party including the claimant shall be read together as one contract and words and expressions to which specific meanings are attached in any part of this Policy or the Schedule thereto shall bear such specific meanings wherever they shall appear. The Policy of Insurance supersedes and replaces all prior communications, representations, warranties, undertakings and agreements between the parties whether oral or written.

ii. Assignment

Assignment or transfer of this Policy shall not be valid without the written consent of the Insurer.

iii. Designation of Property Clause

For the purpose of determining, wherever necessary, the item under which any property is insured, the Insurer agrees to accept the designation under which the property has been entered in the Insured’s books and register.

iv. To Obtain Information- the Right of the Insurer

The Insurer shall have the authority but not an obligation to inspect the insured’s property and operations at any reasonable time, and the insured shall provide the Insurer with all relevant details and information. Neither the right to make inspections nor the making thereof nor any advice or report resulting shall constitute an undertaking on behalf or for the benefit of the insured or others to determine or warrant that such property or operations are safe or are in compliance with a law, rule or regulation.

vi. Reasonable Precautions and Maintenance

The insured shall take at his own expense including all reasonable precautions, and maintain the property in a proper state of repair and comply with all reasonable recommendations made by the insurer to prevent loss of or damage to the property insured or any liability arising under this Policy and comply with all relevant statutory requirements.

vii. Preventive Maintenance

The insured takes all reasonable steps to inspect and maintain the property insured. Any plant, machinery or equipment forming the Property Insured shall be inspected and maintained in accordance with the recommendations of the suppliers or manufacturers of such plant, machinery or equipment. Such inspection and maintenance shall include safety checks, preventive inspection and maintenance, rectification of loss or damage or faults arising from normal operation or wear and tear as well as from ageing, and shall also include the repair or preventive replacement of components modules or parts. The insured shall fully observe the government and all other binding regulations in force concerning the working of the Property Insured and shall see to it that the machinery is under the supervision of competent personnel.

viii. Clarification Agreement

Property damage covered under this Agreement shall mean physical damage to the substance of property. Physical damage to the substance of property shall not include damage to data or software, in particular any detrimental change in data, software or computer programs that is caused by a deletion, a corruption or a deformation of the original structure. Consequently, the following are excluded from this Agreement i.e. policy coverage:

(1) Loss of or damage to data or software, in particular any detrimental change in data, software or computer programs that is caused by a deletion, a corruption or a deformation of the original structure, and any business interruption losses resulting from such loss or damage. Notwithstanding this

exclusion, loss or damage to data or software, which is the direct consequence of insured physical damage to the substance of property, shall be covered.

(2) Loss or damage resulting from an impairment in the function, availability, range of use or accessibility of data, software or computer programs, and any business interruption losses resulting from such loss or damage.

Property All Risks Policy: General Guidelines

Policy

Property All Risks Policy also known Industrial All Risks (IAR) Policy is written under fire department and applicable to land-based properties, unless otherwise specifically provided for in standard fire and special perils policy." Following are the important features of an IAR policy:

- Dwellings" belonging to individuals and/or establishments are to be insured under the Dwelling Insurance Policy.
- Property All Risks Policy covering Buildings and/or contents is to show block-wise separate amounts on: (i) Building; (ii) Machinery and Accessories; (iii) Stock and Stock-in-Process; and (iv) Furniture, Fixtures and Fittings; and (v) other contents. Policy consists of coverage summarized in t*he schedule.*
- Policy is generally divided into three Sections.
- Section I – All Risks (Non-Marine) Property.
- Section II – All Risks Machinery Insurance.
- Section III – All Risks Operational Business Interruption and subject to General Conditions, General Exclusions, Specific Conditions and Specific Exclusions, which form the Policy.

Policy coverage

Section – I

All Risks of Physical Loss or Damage to all permanent and temporary property of the Insured and/or for which they have an insurable interest and/or may otherwise be interested in case of fortuitous and accidental physical loss or damage covered under this Policy, whilst contained in the Premises as specified in the Schedule. Here the property means Non–Marine Property. This does include Machinery Insurance.

Section – II

All Risks of Physical Loss or Damage/Machinery Insurance for all machinery and equipment including electrical or electronic machinery of the insured's plants including spare parts with no specification being the property of the insured and all machinery and equipment in which the insured has an insurable interest in case of loss or damage covered under this Policy.

Section – III

Loss due to Business Interruption: Indemnification to the insured in respect of Loss of Gross Profits the loss actually sustained during the indemnity period resulting from a reduction in turnover including any increased cost of working due to an interruption of the insured's business following loss or damage to any property/ assets insured and recoverable under Section I. However, Business Interruption risks due perils covered under Section II are optional.

10

FIRE LOSS OF PROFIT INSURANCE POLICY

Scope

Standard Fire Policy indemnifies the insured for the material damage to the insured property caused by a fire or other allied perils specified in the policy. Fire policy is intended to put the insured in the pre-loss position after material damage to the insured property including building, plant and machinery, furniture and fixtures, stocks etc., but does not indemnify consequential loss arising out of business interruption due to accidental fire. The Fire Consequential Loss Policy also known as Business Interruption Policy or Fire Loss of Profit (FLOP) Policy indemnifies such consequential loss or loss of profit to the insured from business interruption due to operation of insured perils covered under Fire Policy. The sum insured under Consequential Loss Policy represents the amount of gross profit to be earned by the insured during the indemnity period selected. All terms and conditions applicable to Standard Fire Policy are applicable to this policy apart from certain additional terms, conditions and memos which are discussed hereinafter. To put it simply, Fire Insurance covers Capital Loss, i.e. Property damage from the operation of insured perils while Consequential Loss Insurance policy covers loss of Earning, i.e. Gross Profits including Net Profits and Standing Charges provided both the policies are issued. To explain more distinctly the covers provided by Fire Policy and FLOP Policy, the scope of the policies is outlined in Table-16.

Table-16: Covers Provided by Fire Policy and FLOP Policy

Nature of Loss	Items or Particulars of Loss or Damage	Policy to Cover
Capital or Property Loss	Building, Machinery, Stocks	Fire Insurance Policy
Variable Expenses	Raw-materials labour & other variable Exp.	Diminish with stoppage in production; **No Cover**
Fixed Expenses	Fixed Overhead/ Standing Charges such as Salaries, Interest, Rent	Consequential Loss Policy
Earnings	Net Profit	Consequential Loss Policy

Example: Let us examine how a Fire Loss of profit Policy operates.

	Position Before Fire	**Position After Fire**
Turnover/Sales	5,00,00,000	2,50,00,000
Variable Expenses	(70%) 3,50,00,000	(70%) 1,75,00,000
Standing Charges	(20%) 1,00,00,000	
Fixed Amount	(40%) 1,00,00,000	
Net Profit	(10%) 50,00,000	
Net Loss	25,00,000 (10%)	

Here, Standing Charges and Net Profit amounts 30 per cent of turnover. Loss of Profit Policy is to cover the total of Net Profit and fixed Standing Charges, which comes to Rs 150,00,000 while turnover is Rs 500,00,000 before loss. Thus Net Profit and Standing Charges constitute 30 per cent of the turnover. Due to fire and consequent business interruption, turnover has been reduced to Rs 250,00,000 i.e. Shortage in turnover is Rs 250,00,000 causing a loss for Rs 75,00,000 (profit plus standing charges) which is exactly 30 per cent of turnover shortage being Rs 250,00,000. Thus amount payable by FLOP policy is Rs 75,00,000, provided that following conditions are complied with:

(a) FLOP Policy was issued for Full Sum Insured of Rs 1,50,00,000;

(b) Claim under Fire Policy is admissible irrespective of the amount paid for material damage;

(c) Indemnity period in the policy was for the full period of business interruption; and

(d) There is no time excess.

General Guidelines

Following are the general guidelines followed for underwriting and settlement of claim:

Insuring Agreement

As per this agreement an insurer shall indemnify the insured subject to the terms, definitions, warranties, exclusions, limits provisions and conditions of this Section and of the Policy of insurance as a whole for a loss of profit or loss of interest consequent upon interruption of business due to accidental fire at any time during the Period of Insurance provided the material damage or loss is indemnifiable under the operational material damage policy (fire policy). The loss of interest insured shall be in respect of Gross Profit, the loss actually sustained during the indemnity period resulting from reduction in turnover including any Increased Cost of Working.

Indemnification

The indemnity for the loss of *Interest Insured* shall be in respect of:

(a) **Gross Profit (GP)***:* the loss actually sustained during the indemnity period resulting from a reduction in t*urnover* including any *Increased Cost of Working; or*

(b) **Specified Standing Charges**: the amount actually not earned during the indemnity period resulting from a reduction in *Turnover* including any *Increased Cost of Working*. The indemnity shall not exceed the *Sum Insured* for the *Maximum indemnity period*.

Sum Insured

The Sum Insured shall be the annual Gross Profit specified in the schedule. Gross profit means projected net profit plus the annual specified standing charges. Up to an indemnity period of one year, the annual gross profit should be selected as sum insured. Should the maximum indemnity period exceed 12 months, the gross profit or the specified standing charges shall be the pro rata amount for that period. Thus GP should be in proportion to the indemnity period selected, i.e. for 18 months 1½ times the annual gross profit; if it is for 24 months, 2 times the annual gross profit if it is for 36 months, 3 times the annual gross profit.

Period of Insurance

The Period of Insurance shall be the period specified in the schedule. If at any time after the commencement of this Policy of Insurance: a) the business is wound up or carried on by a liquidator or receiver or administrator or be permanently discontinued; or b) the Insured's interest cease otherwise than by death, then the cover under this Section shall cease on the respective date unless specifically agreed by The Insurer in writing.

Indemnity Period

The indemnity period shall be the period during which the Interest Insured is affected by an interruption of or interference with the Business Insured beginning on the date of the occurrence of loss or damage and not exceeding the maximum indemnity period specified in the schedule.

Premium

Premium shall be paid at the inception of the Policy and shall be calculated by multiplying the Sum Insured by the premium rate. If The Insured declares within twelve months after the expiry of any Period of Insurance that the GP earned during the accounting period of 12 months most closely 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 50 per cent of the Premium paid on such Sum Insured for such Period of Insurance shall be made in respect of the difference. If any loss or damage has occurred giving rise to any payment under this Section then the amount of such payment shall be added to the GP as certified by the insured's auditor and return of premium shall be based on the difference between such sum and the sum insured.

Time Excess and Deductible

In any one occurrence of loss or damage The Insurer shall not be liable for the amount obtained by multiplying the average daily value of the Interest Insured by the number of days specified in The Schedule as the time excess plus any additional amount of any Monetary Deductible specified in The Schedule.

Definitions

Annual Turnover

This means the *Turnover,* which had the interruption of or interference with the *Business Insured* not occurred, would have been achieved during the 12 months preceding either the date when the *Business Insured* is no longer affected or when the indemnity period ends, whichever is the earlier.

Turnover

The money paid or payable to the insured for goods sold and delivered and for services rendered in course of the business at the premises.

Standard Turnover

The turnover during that period in the 12 months immediately before the date of the damage, which corresponds with the indemnity period.

Gross Profit

The sum produced by adding to the net profit the amount of the insured standing charges, or if there is 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 standing charges of the business.

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.

Indemnity Period

The period beginning with the occurrence of the damage and ending not later than 12 months thereafter during which the results of the business be affected in consequence of the damage.

Rate of Gross Profit

The rate of gross profit earned on the turnover during the financial year immediately before the date of damage.

Shortage in Turnover

This is the amount by which the turnover during a period shall in consequence of the damage fall short of the part of the standard turnover, which relates to that period.

Adjustment Clause

This is the clause to which such adjustments shall be made as may be necessary to provide for the trend of the business and for variations in or special circumstances affecting the business either before or after the damage or which would have affected the business had the damage not occurred. So that the figures thus adjusted shall represent as nearly as may be reasonably practicable and the results which but for the damage would have been obtained during the relative period after the damage.

Certain Memos or Clauses

Memo 1

If during the Indemnity Period goods shall be sold or services shall be rendered elsewhere than at the premises for the benefit of the business either by the Insured or by others on his behalf the money paid or payable in respect of such sales or services shall be brought into account in arriving at the Turnover during the Indemnity Period.

Meme 2

If any Standing Charges of the business be not insured by this policy then in computing the amount recoverable hereunder as increase in Cost of Working that proportion only of the additional expenditure shall be brought into account which the sum of the Net Profit and the Insured Standing Charges bears to the sum of the Net Profit and all the Standing Charges.

Memo 3: Return of Premium Clause

"If the Insured declares, at the latest nine months after the expiry of any period of Insurance, that the GP earned (or a proportionately increased multiple thereof where the maximum Indemnity Period exceeds 12 months) during the accounting period of Insurance, as certified by the Insured's Auditors, was less than the sum insured thereon, proportionate return of premium not exceeding 50 per cent of the premium paid on such sum insured for such period of

Insurance shall be made in respect of the difference. If any damage has occurred giving rise to a claim under this policy, such return shall be made in respect only of said difference as is not due to such damage."

Memo 4: Accumulated Stock Clause

In adjusting any loss, account shall be taken and an equitable allowance to be made if any shortage in turnover due to damage is postponed by reason of the turnover being temporarily maintained from accumulated stocks of finished goods in the Insured's warehouse.

Standing Charges

Standing charges, which are many in number, are fixed expenses incurred irrespective of level of production carried out or capacity utilization. Following are only illustrative:

- Officers' salaries and benefits
- Depreciation
- Rents, rates and taxes
- Insurance
- Electricity and water charges
- Furniture equipments repairs
- Office repairs & decorations
- Motorcar expenses
- Share Registrar's fees etc
- Postage, telegram & telephones, bank charges and interest
- Advertising expenditure

- Canteen expenses
- Gratuity
- Printing and stationery
- Computer charges
- License and fees
- Legal & professional charges
- Traveling expenses
- Miscellaneous expenses, etc.

Conditions

The business interruption policy is generally subject to following conditions in addition to the conditions applicable to standard fire policy:

1. The insurance under this policy shall cease if:

    o The business be wound up or carried on by a Liquidator/ Receiver or permanently discontinued;

    o the insured's interest ceases otherwise than by death; or

    o any alteration be made either in the business or in the premises or property therein whereby the risk of Damage is increased, at any time after the commencement of this insurance, unless its continuance be admitted by memorandum signed by or on behalf of the Company.

2. Notice shall be given to the company of alteration in existing blocks, addition of new blocks and/or premises and/or deletion of existing blocks and/or premises during the currency of the Policy to enable the company to determine and to effect necessary adjustments in the premium under this Policy.

Exclusions

This policy shall not cover any loss resulting from interruption of or interference with the Business directly or indirectly attributable to any of the following causes if specified in the policy:

- loss or damage covered under the operational Fire Policy covering material damage by way of endorsement, unless expressly specified as covered in the schedule;
- any restrictions imposed by public authority, including restrictions imposed on reconstruction or operation;
- Consequential Loss due to causes such as suspension, lapse or cancellation of a lease, license or order, etc., which occurs after the date when the items lost, destroyed or damaged are in operating condition again and the Business insured could have been resumed if said lease, license or order, etc. had not lapsed or had not been suspended or cancelled;
- shortage of raw materials, semi-finished or finished products or other materials required for proper operation, not caused by loss or damage to such property by an insured peril under Fire Policy;
- loss, distortion or corruption of information in computer systems or other records or software programs unless resulting from an occurrence of loss or damage indemnifiable under the operational material damage section;
- loss or damage for which the manufacturer or supplier of the property is responsible either by law or under contract;
- The insured not having at his disposal in good time sufficient capital for repairing or replacing destroyed or damaged machinery; and
- The Insurer shall not be liable for the amount of any fines or damages for breach of contract, for late or non-completion of orders, or for penalties of whatever nature.

Types of Business Interruption Policy

Business interruption policy or Fire Consequential Policy may be any of the following three types or basis:

- Specification A – Insurance on Gross Profit on Turnover Basis
- Specification – Insurance on Gross Profit on Output Basis
- Specification C - "Difference" Basis

Specification A – Insurance on Gross Profit on Turnover Basis

The insurance under this basis is limited to loss of GP due to: (a) Reduction in Turnover; and (b) increase in Cost of Working. The amount payable as indemnity there under shall be:

(a) In Respect of Reduction in Turnover

The sum produced by applying the Rate of GP to the amount by which the Turnover during the Indemnity Period shall, fall short of the Standard Turnover in consequence of the Damage.

(b) In Respect of Increase in Cost of Working

The additional expenditure (subject to the provisions of Memo attached with the policy) necessarily and reasonably incurred for the sole purpose of avoiding or diminishing the reduction in turnover, which but for that expenditure would have taken place during the Indemnity period in consequence of the damage but not exceeding the sum produced by applying the Rate of GP to the amount of the reduction thereby avoided.

- o Less any sum saved during the Indemnity Period in respect of such of the Insured Standing Charges as may cease or be reduced in consequence of the Damage:

Provided that if the Sum Insured by this Item be less than the sum produced by applying the Rate of Gross Profit to the Annual Turnover, the amount payable shall be proportionately reduced.

Insurance on Gross Profit on Turnover Basis is subject to following **Departmental Clause:**

"*If the business be conducted in departments, the independent trading results of which are ascertainable, the provision of Clauses (a) and (b) above shall apply separately to each department affected by the damage except 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 for each department of the business (whether affected by the damage or not) to the relative Annual Turnover thereof, the amount payable shall be proportionately reduced*."

Specification – Insurance on GP on Output Basis

Insurance under this basis is limited to loss of GP due to: (a) Reduction in Output; and (b) increase in Cost of Working and the amount payable as indemnity there under shall be:

(a) In Respect of Reduction in Output

The sum produced by applying the Rate of GP to the amount by which the Output during the Indemnity Period shall fall short of the Standard Output in consequence of the Damage.

(b) In Respect of Increase in Cost of Working

The additional expenditure (subject to the provisions of Memo 2 attached with the policy) necessarily and reasonably incurred for the sole purpose of avoiding or diminishing the reduction in Output which, but for that expenditure, would have taken place during the indemnity period in consequence of the damage but not exceeding the sum produced by applying the Rate of GP to the amount of the reduction thereby avoided.

- Less any sum saved during the Indemnity Period in respect of such of the Insured Standing Charges as may cease or be reduced in consequence of the Damage; Provided that if the Sum Insured by this Item be less than the sum produced by applying the Rate of GP* to the Annual Output, the amount payable shall be proportionately reduced.

***** Appropriate multiple if the indemnity period exceeds 12 months.

Insurance on Output Basis is subject to following **Departmental Clause**:

If the business be conducted in departments, the independent trading results of which are ascertainable, the provision of Clauses (a) and (b) above shall apply separately to each department affected by the damage except 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 for each department of the business (whether affected by the damage or not) to the relative Annual Output thereof, the amount payable shall be proportionately reduced.

Specification C - “Difference” Basis

The insurance under this basis is limited to loss of GP due to: (a) Reduction in Turnover and (b) increase in Cost of Working and the amount payable as indemnity there under shall be:

(a) In Respect of Reduction in Rurnover

The sum produced by applying the Rate of GP to the amount by which the Turnover during the Indemnity Period shall, in consequence of the Damage, fall short of the Standard Turnover.

(b) In respect of increase in cost of working

The additional expenditure necessarily and reasonably incurred for the sole purpose of avoiding or diminishing the reduction in Turnover which but for that expenditure would have taken place during the Indemnity period in consequence of the Damage but not exceeding the sum produced by applying the Rate of GP to the amount of the reduction thereby avoided. Less any sum saved during the Indemnity Period in respect of such of the charges and expenses of the business payable out of the GP as may cease or be reduced in consequence of the Damage; Provided that if the Sum Insured by this Item be less than the sum produced by applying the Rate of GP* to the Annual Turnover, the amount payable shall be proportionately reduced.

* Appropriate multiple if the Indemnity Period exceeds 12 months.

Insurance on Output Basis is subject to following **Departmental Clause**;

If the business be conducted in departments, the independent trading results of which are ascertainable, the provision of Clauses (a) and (b) above shall apply separately to each department affected by the damage except 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 for each department of the business (whether affected by the damage or not) to the relative Annual Turnover thereof, the amount payable shall be proportionately reduced.

Definitions

Certain items for cover under Specification C - "Difference" Basis are subject to specific definitions or interpretations, which are provided below;

(a) **Gross Profit** – The amount by which the sum of the Turnover and the amount of the Closing Stock shall exceed the sum of the amount of the Opening Stock and the amount of the Specified Working Expenses

Note: The amount of the Opening and Closing Stocks shall be arrived at in accordance with Insured's normal accountancy methods, due provisions being made for depreciation.

(b) **Specified Workings Expenses** shall mean and include:

1. All Purchases (less Discounts Received)

2. Per cent Of the Annual Wage Roll (including Holiday and Insurance contributions)
3. Power
4. Consumable Stores
5. Carriage
6. Packing Materials
7. Bad Debts
8. Discounts Allowed
9. Any other expenses to be specified

Note: The words and expressions used in this Definition shall have the meaning usually attached to them in the books and accounts of the Insured.

(c) **Turnover:** The money paid or payable to the insured for goods sold and delivered and for services rendered in course of the business at the premises.

(d) **Indemnity Period:** The period beginning with the occurrence of the damage and ending not later than specified months thereafter during which the results of the business shall be affected in consequence of the damage.

(e) **Rate of Gross Profit:** The rate of Gross Profit earned on the turnover during the financial year immediately before the date of the damage.

(f) **Annual Turnover:** The Turnover during the twelve months immediately before the date of the damage.

(g) **Standard Turnover:** The Turnover during that Period in the twelve months immediately before the date of the damage which corresponds with the Indemnity Period.

(h) **Adjustments to Rate of Gross Profit, Annual Turnover and Standard Turnover**: Such adjustments shall be made as may be necessary to provide for the trend of the business and for variations in or special circumstances affecting the business either before or after the damage or which would have affected the business had the damage not occurred so that the figures thus adjusted shall represent as nearly as may be reasonably practicable the results which, but for the damage, would have been obtained during the relative period after the damage.

Memos

Specification C -"Difference" Basis Cover are subject to following two specific memos:

Memo 1

If during the Indemnity Period goods shall be sold or services shall be rendered elsewhere than at the premises for the benefit of the business either by the Insured or by others on his behalf the money paid or payable in respect of such sales or services shall be brought into account in arriving at the Turnover during the Indemnity Period.

Memo 2

If the Insured declares, at the latest 12 months after the expiry of any Period of Insurance, that the GP earned (or a proportionately increased multiple thereof where the maximum Indemnity Period exceeds 12 months) during the accounting period of 12 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 50 per cent of the premium paid on such Sum Insured for such period of Insurance shall be made in respect of the difference. Where, however, the declaration is not received by the Company within 12 months after the expiry of the period of insurance, no refund shall be admissible. If any damage has occurred giving rise to a claim under this policy, such return shall be made in respect only of said difference as is not due to the damage.

11

MOTOR INSURANCE – OWN DAMAGE

Application of Principles of Insurance

Motor Own Damage Insurance is subject to basic principles of insurance as applicable to other Property Insurance. Practical application of some of these principles is briefly discussed here with certain examples for better analysis and clarity in this regard.

Principle of Utmost Good Faith

As we know, this principle imposes a legal obligation on the proposer to disclose all material facts in the proposal form. The material facts such as the vehicular details-types, years of manufacture, make, engine No and capacity, chassis No, theft proneness of vehicle, geographical area of use, the driving history like drivers age, qualification, physical conditions, traffic conviction, past loss experience are required to be discussed correctly. The disclosure of above material aspects and mandatory declaration to the correctness thereof by the prospect (applicant of insurance) in the proposal form converts the duty of good faith as required in other commercial contracts into duty of utmost good faith for the party purchasing insurance in the insurance contract or policy. The answers in the proposal form become the warranties and the non-compliance of which makes the contract voidable at the option of the insurers.

Principle of Insurable Interest

Insurable Interest is the legal right of the owner to insure his vehicle. The essential requirements of insurable interest in motor insurance are: i) the existence of the ownership of the property exposed to loss or damage; ii) the insured stands to benefit by the safety of the property, right, and interest; and iii) he stands to lose by any loss, damage or injury or occurrence of any liability. Thus the insured has the insurable interest, to insure the vehicle against property damage. If a vehicle is purchased under a Hire Purchase Agreement the finance company has an insurable interest until all the installments are repaid, so a clause is included in the policy to protect the financial interest for recovery of compensation under any insurance claim arising out of damage to the vehicle. Similarly, Motor traders e.g. Garage proprietors have insurable interest as bailee's in respect of loss or damage to the customer's vehicle which are in their custody for the purpose of repair. So they can also take the policy called Motor Traders Policy covering such liability. The owner of a vehicle is also exposed to a legal liability towards third parties in respect of bodily injuries or property damage caused by the negligent use of the vehicle in view of Section 146 of the Motor Vehicles Act (M.V.Act), 1988 which provides that no person shall use or allow any other person to use a vehicle in a public place unless the vehicle is insured. This liability risks bring an insurable interest for the owner of vehicle to take insurance cover for third party liability, which has been separately discussed in the next chapter.

Principle of Indemnity

Like any other insurance contract Motor Insurance is also based on the principle of indemnity, which implies that the insured will be placed after a loss in the same position as he was immediately before the loss. He cannot make any profit out of his insurance. In the event of total loss of the vehicle, insurers may pay the market value of the vehicle (after depreciation) at the time of the loss or the sum insured whichever is less. If the vehicle is damaged, cost of repairs is paid but if old parts are replaced by new, depreciation is charged on the cost of new spare parts. Insurer reserves the option to repair or replace the vehicle or pay in cash excepting for Vintage car with the agreed value policies.

Principle of Subrogation

Subrogation is the transfer of rights from the insured to the insurer when the loss or damage to the vehicle is caused by negligence of another person. Because of this principle, insurers exercise these rights to recover the loss for the persons responsible for such damage. As per policy condition principle of subrogation may even before the payment of claim by the insurer.

Principle of Contribution

Contribution arises when there is a double insurance, i.e. when the same vehicle is found insured by two policies. According to this principle loss is shared by two insurers.

Classification of Motor Vehicles and Motor Underwriting

Vehicles under Motor insurance include Private cars, Motorized two wheelers, and commercial vehicles excluding vehicles running on rails. Vehicles are classified into various types so as to ensure that risk identification, risk analysis, risk evolution, and class rating. Vehicles are broadly classified into three categories viz. private cars, motorcycles and commercial vehicles. They are again put into various sub-classifications according nature of use, cubic capacity etc. However following classification is done for the purpose of effective underwriting of motor insurance and class rating.

Private Cars

- Vehicles used solely for social, domestic and pleasure purposes.
- Vehicles used for the business and professional purposes of the insured but not for hire, reward, racing, pace making, reliability trial or speed testing.
- Three-wheel cars used for only private purpose.

Motor Cycles

- Motor cycles with or without side cars.
- Auto cycles or mechanically assisted paddle cycles.
- Motor Scooters with or without side cars.

Commercial Vehicles

- Goods Carrying Vehicles
- Goods Carrying Vehicles (general carriage).
- Trailers – Track, Cart, Carriage or vehicles without means of self-propulsion being drawn by any self propelled vehicle.
- Passenger carrying vehicles/buses including tourist, hotel, school buses or airline buses.
- Passenger carrying vehicle for hire – (a) taxi/ cars plying for public hire (b) private taxi let out on hire and driven by owner or employee of the owner. (c) Private type taxi let out on hire and driven by the hirer with permission of owner (d) private car owned by hotels.
- Passenger carrying vehicles, motorized rickshaw.

Miscellaneous and Special Type of Vehicles

- Agricultural tractors
- Trailer fitted as cinema film recording and publicity vans
- Delivery truck
- Trailers (dustcarts, water cars)/ trailer including fire brigade and salvage cars.
- Trailer fitted as mobile shop and canteen
- Trailer – Tar spraying / trailers cleaning and leveling plant
- Cranes – trailers and tractors (i) tractors agricultural and forestry spraying plant

Other Miscellaneous Vehicles

(a) Ambulances (b) breakdown vehicles (c) dispensaries

(d) dumpers (e) dust cars (f) tractors (g) footpath rollers (i) forklift tracks, (j) road rollers, (k) road sprinklers (l) levelers etc.

Types of Policies (GR 3)

Motor Insurance Policies are classified into two basic categories:

- Own damage insurance (property insurance)
- Liability insurance (Third Party liability under Motor Vehicles Act as mentioned earlier)

So following two types of policies are issued for above types of motor insurance cover:

- **Liability Only Policy** – For only third party liability under Motor Vehicles Act 1988.
- **Package Policy –** covering third party liability under M.V Act & Own Damage to vehicle.

General Regulations for Motor Own Damage Insurance Underwriting

Motor Insurance in India is carried on within the purview of the Motor Tariff. Any alteration or extension of any of the Covers, Terms, Conditions, Exclusions, etc. of any of the policies or endorsements laid down in the tariff is permitted without prior approval of the TAC. In view of changes in technical aspects or legal requirements the TAC issues circulars from time to time for necessary modification in general regulations of motor insurance. For example, i) TAC Circular No. IMT/08/2005 dated 04.08.05 specifies for Discount on OD Premium for approved Anti-theft Devices; ii) TAC Circular No. IMT/09/2005 datd 04.10.05 specifies for Endorsement IMT-16 on PA Cover to unnamed passengers other than insured and the paid driver and cleaner; iii)TAC Circular No. IMT/10/2005 dated 10.10.05 specifies General Regulations (GR) 42 on Use of CNG/LPG fuel; iv) TAC Circular No. IMT/02/2006 dated 17.4.06 specifies GR 36A on Compulsory Personal

Accident cover under Indian Motor Tariff; v) TAC Circular No. IMT/03/2006 dated 17.04.06 specifies modification on rating of trailers under Commercial Vehicles Tariff of Indian Motor Tariff; and vi) TAC Circular No. IMT/01/2008 dated 15.09.08 specifies modification in Endorsement IMT-16 for PA Cover to unnamed passengers other than insured and the paid driver and cleaner (for vehicles rated as private cars and motorized two wheelers (not for hire or reward) etc. Thus GR provides the directives and guidelines in respect of motor insurance transaction. Important general regulations are briefly discussed hereinafter.

Proposal Form

This is the fundamental document for underwriting. The proposal form is required to be submitted by the insured to the insurer before the acceptance of the risk and at renewal in case of any material change or in case of break insurance. The insured is required to fill in and reply all questions in the proposal form for furnishing required information for the purpose of underwriting. If an insured fails to furnish the required information in the proposal form, appropriate policy may not be issued with all details required for certificate of insurance required for the use of vehicle in the public place. Proposal form as specified in Section 5 of the Indian Motor Tariff is required to be submitted by the insured before the commencement of cover and at renewal in case of material change or alteration of risks. However for change of IDV at each renewal, a fresh proposal form may not be required; such changes may be communicated by a letter signed by the insured. In case of change of insurer, a fresh proposal form is required to be submitted along with renewal notice of the previous insurer (GR 2). A specimen of Motor proposal form has been given at the end of this chapter in Annexure A for ready reference and better understanding of motor risk analysis for underwriting purpose.

Rating

The insurers are required to follow the rates provided in the tariff. The rates provided in the tariff are minimum rates. Loading on tariff premium rates by even 100 per cent may be applied for adverse claims experience of the vehicles based on the insurer's individual risk perception. If the experience continues to be adverse, a further loading of 100 per cent on the existing premium may be imposed, but no further loading shall apply (GR 3).

Extension of Geographical Area

Insurer may extend the geographical area of motor policies to include Nepal, Bhutan, Bangladesh, Pakistan, Sri Lanka, and Maldives as the case may be charging additional premium under the present tariff condition. However, to extend the geographical area of the motor policy to include Bangladesh insurers is required to charge additional premium. For such extension Endorsement IMT 1 is to be used. 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 vehicles to the extended geographical area **(GR 4).**

Vintage Car

Any car manufactured prior to 31 December 1940 and duly certified by the Vintage and Classic Car Club of India can be considered a Vintage Car for the purpose of this tariff **(GR 5).**

Classic Cars

Any car manufactured after 31 December 1940, but before 31 December 1970 and duly certified by the Vintage and Classic Car Club of India can be considered a Classic Car for the purpose of this tariff. However there is no provision for special rating for classic cars **(GR 6).**

Valued Policies

It is not permissible to issue “agreed value policy” except for Vintage Car. An agreed value policy is a policy which undertakes in case of total loss to pay a specified sum as the value of the vehicle insured and which does not take into account the current market value of such vehicle without any deduction for depreciation **(GR 7**).

Insured's Declared Value (GR 8)

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 manufacturers' 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). The IDV of the side car(s) and/or accessories, if any, fitted to the vehicle but not included in the manufacturer's listed selling price of the vehicle is also likewise to be fixed. The schedule of age-wise depreciation as shown in Table-17 is applicable for the purpose of Total Loss/Constructive Total Loss (TL/CTL) claims only. A vehicle will be considered to be a CTL, as referred to above, where the aggregate cost of retrieval and/or repair of the vehicle subject to terms and conditions of the policy exceed 75 per cent of the IDV. The depreciation for replacement of parts in partial loss claims will be as per a separate schedule specified under GR 9.

Table-17: Schedule of Depreciation for Arriving at IDV

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.

IDV shall be treated as the 'Market Value' throughout the policy period without any further depreciation for the purpose of TL/CTL claims. For the purpose of TL/CTL claim settlement this IDV will not change during the currency of the policy period in question. It is clearly understood that the liability of the insurer shall in no case exceed the IDV as specified in the policy schedule less the value of the wreck, in 'as is where is' condition **(GR 8).**

Depreciation on Parts on Partial Loss

Indemnification for partial loss shall be made subject to a deduction for depreciation at the rates mentioned below in respect of parts replaced in respect of all categories of vehicles:

	Items	Depreciation Rate
•	All rubber/nylon/plastic parts, tyres and tubes, batteries and air bags	50%
•	Fibre glass components	30%
•	All parts made of glass	Nil

Rate of depreciation for all other parts including wooden parts will be as per following schedule:

	Age of Vehicle	% of Depreciation
•	Not exceeding 6 months	Nil
•	Exceeding 6 months but not exceeding 1 year	5%
•	Exceeding 1 year but not exceeding 2 years	10%
•	Exceeding 2 years but not exceeding 3 years	15%
•	Exceeding 3 years but not exceeding 4 years	25%
•	Exceeding 4 years but not exceeding 5 years	35%
•	Exceeding 5 year but not exceeding 10 years	40%
•	Exceeding 10 years	50%

(GR.9)

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 to be insured:

(i) Private Car/Motorized Two Wheeler/Commercial Vehicle Rateable Under Section 4.C.I & C.4

Zone A: Ahmedabad, Bangalore, Chennai, Hyderbad, Kolkata, Mumbai, New Delhi & Pune

Zone B: Rest of India

(ii) For Commercial Vehicles Excluding Vehicles Rateable Under Section 4.C.I & C.4

Zone A: Chennai, Kolkata, Mumbai, New Delhi & Delhi

Zone B: Other State Capitals

Zone C; Rest of India **(GR.10)**

Period of Insurance

No policy for a period beyond 12 months may be issued or renewed unless specifically provided for. However, it is permissible to extend the policy period for a further period less than one year to suit the convenience of the insured in regard to renewal date and in such case additional premium payable by the insured may be calculated on a pro-rata basis provided such policies are renewed with the same insurer immediately after the expiry of such extension. All such extensions require attachment of warranty to the policy **(GR 11).**

Short Period Cover and Rates

Policies issued or renewed for shorter periods than 12 months must be charged for on the following scale which must be also applied in calculating the premium when policies are cancelled during the currency at the request of the insured:

Table-18: Short Period Policy Cover and Rates

PERIOD (Not exceeding)	RATE
1 month	20% of the Annual Rate
2 months	30% of the Annual Rate
3 months	40% of the Annual Rate
4 months	50% of the Annual Rate
5 months	60% of the Annual Rate
6 months	70% of the Annual Rate
7 months	80% of the Annual Rate
8 months	90% of the Annual Rate
Exceeding 8 months	Full Annual Premium

Policy issued or renewed for a short period basis may not be extended upon payment of difference of premium for the short period and for the extended period. Short period cover/ short period renewals are not permissible **(GR 12).**

Display of Premium

In case of a Package (Comprehensive) policy, the own damage and liability components of premium are to be displayed separately in the Policy Schedule. Similarly, all loadings imposed or discounts allowed on tariff rates are required to be displayed separately in the policy schedule. The own damage and liability components of premium are to be rounded off to the nearest rupee separately **(GR 13).**

Payment of Premium

The full premium is required to be collected before commencement of cover. It is not permissible to collect premium in installments **(GR 15).**

Minimum Premium

The minimum premium applicable for vehicles specially designed for use of the blind, physically handicapped or mentally retarded persons will be Rs 25 while for all other vehicles the same will be Rs 100 per vehicle **(GR 16).**

Transfer

On a transfer of ownership of the vehicle the **liability cover** only either under a Liability Only Policy or under a Package Policy in force shall automatically accrue to the new owner with the effect from the date of transfer. The transferee shall apply within 14 days from the date of transfer in writing under recorded delivery to the insurer who has insured the vehicle, with the details of registration of the vehicles, the date of transfer of the vehicle, the previous owner of the vehicle, the number and date of the insurance policy so that the insurer may make necessary changes in his records and issue a fresh Certificate of Insurance. In case of **Package policy**, transfer of the 'Own Damage' cover of the policy to the transferee shall be made by the insurer only on the receipt of a specific request from the transferee along with the consent of the transferor. If the transferee is not entitled to the benefit of "No Claim Bonus" (NCB), shown on the policy, or is entitled to lesser NCB than that shown in the policy, recovery shall be made for the difference of the two.

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 in and signed by the transferee along with the deposit of transfer fees of Rs 50 for issuance of a fresh certificate. To issue a fresh certificate in favour of the transferee, old certificate is to be surrendered. If old certificate cannot be surrendered, a proper declaration to that effect is to be taken from the transferee before a new certificate is issued in his favour. Endorsement IMT 3 is to be used **(GR 17).**

Change of Vehicles

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 the insurance on the substituted vehicle is required to be submitted to the insurer before such substitution can be carried out. Endorsement IMT-4 is to be used **(GR 18).**

Vehicles on Hire Purchase Agreement

It is not permissible to issue policy in the joint names of the hirer and the owner. Policies must be issued in the hirer. Owner's interest shall be protected by appropriate endorsement IMT- 5 **(GR19).**

Vehicles on Lease Agreement

It is not permissible to issue policies in the joint names of Lessee and Lesser. The policy must be issued in the name of the Lessee and the Lesser's interest shall be protected by the use of endorsement IMT-6 **(GR 20).**

Vehicles Subject to Hypothecation Agreement

Policy and certificate are to be issued in the name of Registered Owner only and issuance of policy or certificate in the joint names of the Registered Owner and the pledgee is prohibited. The pledgee's interest can be protected with the Endorsement IMT-7 **(GR.21).**

Cover Note

Cover note insuring Motor vehicles are to be issued only in Form No. 52 in terms of the Rule 142 of the Central Motor Vehicles Rules, 1989. In terms of Rule 142(2) of the Central Motor Vehicles Rules1989, a cover note shall be valid for a period of 60 days from the date of its issuance and the insurer shall issue a policy of insurance before the date of the expiry of the cover note **(GR 22).**

Certificate of Insurance

A certificate of insurance for a motor Vehicle is to be issued only in Form No. 51 in terms of Rule 141 of the Central Motor Vehicles Rules1989 **(GR 23).**

Format is given below.

CERTIFICATE OF INSURANCE

Policy No. ____________ Certificate No. __________

Particulars of vehicle insured :

Reg. No. & Place of Registr-ation	Engine No. & Chassis No	Make	Year of Manuf-acture	Type of Body	C.C	Seating capacity	Net Prem-ium Rs.

- Name of Registration Authority :
- Name & Address of Insured :
- Geographical Area :INDIA
- Business or Profession :
- Effective date of commencement of Insurance ; From _____O’ Clock on ______ .
- Date of expiry of the insurance. Midnight on ________
- Persons or Class of Persons entitled to drive ; Any person including the insured

Provided that a person driving holds an effective Driving license at the time of the accident and is not disqualified from holding or obtaining such a license. Provided also that the person holding an effective Learner’s License may also drive the vehicle and that such a person satisfies the requirements of Rule 3 of the Central Motor Vehicles Rules, 1989.

Limitations as to Use: The Policy covers use for any purpose other than:

(a) Hire or Reward

(b) Carriage of goods (other than samples or personal luggage)

(c) Organized racing,

(d) Pace Making

(e) Speed testing

(f) Reliability Trials

(g) Any purpose in connection with Motor Trade

I/We hereby certify that the Policy to which this Certificate relates as well as this Certificate of Insurance are issued in accordance with the provisions of Chapter X and Chapter XI of M.V. Act, 1988.

Full address of Issuing Office:

Date of issue Duly Constituted Attorney(s)

Cancellation of Insurance

A policy can be cancelled by the insurer by sending to the insured a seven days notice of cancellation by recorded delivery to the insured's last known address and the insurer will refund the pro rata premium for the balance period of the policy. Refund of premium will be subject to situation that there being no claim under the policy and the retention of minimum premium as per the tariff. A policy can be cancelled only after ensuring that vehicle is insured elsewhere at least for Liability Only Cover and after surrender of the original certificate of insurance for cancellation. Insurer should inform the RTA concerned by recorded delivery about such cancellation of insurance **(GR 24 A).**

Double Insurance

When two policies are in existence for the same vehicle with identical cover, one of the policies may be cancelled. Where one of the policies commences at a at date later than that of the other policy, the policy commencing later is to be cancelled by the insurer concerned. Refund should be granted on pro rata basis and not on short period basis on cancellation one of the policies by the insurer concerned. If a vehicle is insured at any time with two different offices of the same insurer 100 per cent 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 the pro rata refund of premium thereupon is to be allowed.

If however, due to requirements of banker or financial institution, intimated to the insurer in writing, the earlier dated policy is required to be cancelled, then refund is to be allowed after retaining premium at a short period scale for the policy was in force prior to cancellation. In all such eventualities, the minimum premium as specified in the tariff shall be retained. In either case no refund of premium shall be made for such cancellation if any claim has occurred on either of the policies during the period when both the policies were in operation, but prior to cancellation of one of the policies **(GR 24 B).**

No Claim Bonus (NCB)

No claim bonus can be earned only in the own damage section of the policy covering all classes of vehicles but not on Motor Trade Policies. (Road Transit Risk/Road Risk/Internal Risk) and policies, which cover only Fire and/or Theft Risk. For policies covering Liability with Fire and Theft Risk NCB will be applicable on the Fire or Theft components of the premium. An insured becomes entitled to NCB only at the renewal of the policy after the expiry of the full duration of 12 months. Presently “No Claim Bonus” is admissible as shown in the Table given below:

Table-19: Admissible 'No Claim Bonus'

All Types of Vehicles	Discount % on Premium
No Claim made or pending during preceding full year of insurance	20%
No Claim made or pending during preceding 2 consecutive yrs.	25%
No Claim made or pending during preceding 3 consecutive yrs.	35%
No Claim made or pending during preceding 4 consecutive yrs.	45%
No Claim made or pending during preceding 5 consecutive yrs.	50%

Sunset Clause: An insurer is entitled to NCB to an NCB of 55 per cent or 65 per cent in terms of the tariff prevailing up to July 2002 and such entitlement will remain protected for all subsequent renewals till a claim arises in the policy. In the event of insured transferring his insurance from insurer to another insurer, the transferring the insurer may allow the same rate of NCB, which the insured would have received, from the previous insurer. Evidence of the insured's NCB entitlement either in the form of renewal notice or a letter confirming NCB entitlement from the previous insurer shall be required for this purpose.

1. If an insured vehicle is sold and not replaced immediately or laid up and policy is not renewed immediately after expiry, NCB, if any, may be granted on a subsequent insurance provided such fresh insurance is affected within three years from the expiry of the previous insurance. The rate of NCB applicable to the fresh insurance shall be that on at the expiry of last 12 months period of insurance.

2. On production of evidence of having earned NCB abroad, an insured may be granted NCB on a new policy taken out

in India as per the entitlement earned abroad. Provided the policy is taken out in India within three years of expiry of the Overseas Insurance Policy subject to relevant provisions of NCB under these rules **(GR 27).**

Personal Accident Cover for Owner-Driver

The Company undertakes to pay compensation as per the following scale for bodily injury/death sustained by the owner-driver of the vehicle, in direct connection with the vehicle insured or whilst driving or mounting into/dismounting from the vehicle insured or whilst traveling in it as a co-driver, caused by violent accidental external and visible means which independent of any other cause shall within six calendar months of such injury result in:

Table-20: Personal Accident Cover for Owner-Driver

Nature of injury	Scale of Compensation
(i) Death	100 per cent
(ii) Loss of two limbs or sight of two eyes or one limb and sight of one eye.	100 per cent
(iii) Loss of one limb or sight of one eye	50 per cent
(iv) Permanent total disablement from injuries other than named above.	100 per cent

Provided always that :

- Compensation shall be payable under only one of the items (i) to (iv) above in respect of the owner-driver arising out of any one occurrence and the total liability of the insurer shall not be in the aggregate exceed the sum of Rs. 2 lakhs during any one period of insurance.

- No compensation shall be payable in respect of death or bodily injury directly or indirectly wholly or in part arising or resulting from or traceable to (1) intentional self injury suicide or attempted suicide physical defect or infirmity or (2) an accident happening whilst such person is under the influence of intoxicating liquor or drugs.

- Such compensation shall be payable directly to the insured or to his/her legal representatives whose receipt shall be the full discharge in respect of the injury to the insured.

This cover is subject to:

(a) the owner-driver is the registered owner of the vehicle insured herein;

(b) the owner-driver is the insured named in this policy;

(c) the owner-driver holds an effective driving license, in accordance with the provisions of Rule 3 of the Central Motor Vehicles Rules, 1989, at the time of the accident.

Note: It is subject to Endorsements IMT-15, IMT-16, IMT-17 & IMT-18 to be used **(GR 36).**

General Conditions

This Policy and the Schedule shall be read together and any word or expression to which a specific meaning has been attached in any part of this Policy or of the Schedule shall bear the same meaning wherever it may appear. General Conditions applicable to all types of policies are briefly discussed bellow. The insurance will cease to operate if any of the following conditions is violated.

Notice to the Company

Notice shall be given in writing to the Company immediately upon the occurrence of any accidental loss or damage in the event of any claim and thereafter the insured shall give all such information and assistance as the Company shall require. Every later claim writ summons and/or process or copy thereof shall be forwarded to the Company immediately on receipt by the insured. Notice shall also be given in writing to the Company immediately the insured shall have knowledge of any impending prosecution, inquest or fatal inquiry in respect of any occurrence which may give rise to a claim under this Policy. In case of theft or criminal act which may be the subject of a claim under this Policy the insured shall give immediate notice to the police and co-operate with the Company in securing the conviction of the offender.

No Promise Payment

No offer of promise payment or indemnity shall be made or given by or on behalf of the insured without the written consent of the Company which shall be entitled if it so desires to take over and conduct in the name of the insured the defence or settlement of any claim or to prosecute in the name of the insured for its own benefit any claim for indemnity or otherwise and shall have full discretion in the conduct of any proceedings or in the settlement of any claim and the insured shall give all such information and assistance as the Company may require.

Liability of the Company

The Company may at its own option repair, reinstate or replace the vehicle or part thereof and/or its accessories or may pay in cash the amount of the loss or damage and the liability of the Company shall not exceed:

- for total loss/constructive total loss of the vehicle - the Insured's Declared Value (IDV) of the vehicle (including accessories thereon) as specified in the Schedule less the value of the wreck.

- for partial losses, i.e. losses other than TL/CTL of the vehicle - actual and reasonable costs of repair and/or replacement of parts lost/damaged subject to depreciation as per limits specified.

Reasonable Steps to Safeguard Vehicle

The insured shall take all reasonable steps to safeguard the vehicle from loss or damage and to maintain it in efficient condition and the Company shall have at all times free and full access to examine the vehicle or any part thereof or any driver or employee of the insured. In the event of any accident or breakdown, the vehicle shall not be left unattended without proper precautions being taken to prevent further damage or loss and if the vehicle be driven before the necessary repairs are effected any extension of the damage or any further damage to the vehicle shall be entirely at the insured's own risk.

Cancellation of Policy

The Company may cancel the policy by sending 7 days notice by recorded delivery to the insured at insured's last known address and in such event will return to the insured the premium paid less the pro rata portion thereof for the period the Policy has been in force or the policy may be cancelled at any time by the insured on 7 days' notice by recorded delivery and provided no claim has arisen during the currency of the policy, the insured shall be entitled to a return of premium less premium at the Company's Short Period rates for the period the Policy has been in force. Return of the premium by the company will be subject to retention of the minimum premium of Rs 100 (or Rs 25 in respect of vehicles specifically designed/modified for use by blind/handicapped/mentally challenged persons). Where the ownership of the vehicle is transferred, the policy cannot be cancelled unless evidence that the vehicle is insured elsewhere is produced.

Any Other Insurance Claim

If at the time of occurrence of an event that gives rise to any claim under this policy there is in existence any other insurance covering the same liability, the Company shall not be liable to pay or contribute more than its ratable proportion of any compensation, cost or expense.

Arbitration to the Dispute

If any dispute or difference shall arise as to the quantum to be paid under this policy (liability being otherwise admitted), such difference shall be independent of all other questions be referred to the decision of a sole arbitrator to be appointed in writing by the parties to the dispute or if they cannot agree upon a single arbitrator within 30 days of any party invoking Arbitration, the same shall be referred to a panel of three arbitrators comprising two arbitrators one to be appointed by each of the parties to the dispute/ difference, and a third arbitrator to be appointed by such two arbitrators who shall act as the presiding arbitrator and Arbitration shall be conducted under and in accordance with the provisions of the Arbitration and Conciliation Act, 1996. It is clearly agreed and understood that no difference or dispute shall be referable to Arbitration as hereinbefore provided, if the Company has disputed or not accepted liability under or in respect of this policy.

It is hereby expressly stipulated and declared that it shall be condition precedent to any right of action or suit upon this policy that the award by such arbitrator/ arbitrators of the amount of the loss or damage shall be first obtained. It is also hereby further expressly agreed and declared that if the Company shall disclaim liability to the insured for any claim hereunder and such claim shall not, within twelve calendar months from the date of such 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.

Observance of Terms & Conditions

The due observance and fulfillment of the terms, conditions and endorsements of this Policy in so far as they relate to anything to be done or complied with by the insured and the truth of the statements and answers in the said proposal shall be conditions precedent to any liability of the Company to make any payment under this Policy.

In the Event of Death

In the event of the death of the sole insured, this policy will not immediately lapse but will remain valid for a period of three months from the date of the death of insured or until the expiry of this policy (whichever is earlier). During the said period, legal heir(s) of the insured to whom the custody and use of the Motor Vehicle passes may apply to have this Policy transferred to the name(s) of the heir(s) or obtain a new insurance policy for the Motor Vehicle.

General Exclusions

The general exclusions are applicable to all types of Motor Policies. However, the Company shall not be liable under this Policy in respect of:

- Any accidental loss or damage and/or liability caused sustained or incurred outside the geographical area;
- Any claim arising out of any contractual liability;
- Any accidental loss damage and/or liability caused sustained or incurred whilst the vehicle insured herein is:
    - being used otherwise than in accordance with the 'Limitations as to Use' or
    - being driven by or is for the purpose of being driven by him/her in the charge of any person other than a Driver as stated in the Driver's Clause.
- Any accidental loss or damage to any property whatsoever or any loss or expense whatsoever resulting or arising there from or any consequential loss;
- Any liability of whatsoever nature directly or indirectly caused by or contributed to by or arising from ionizing radiations or contamination by radioactivity from any nuclear fuel or from any nuclear waste from the combustion of nuclear fuel. For the purpose of this exception combustion shall include any self-sustaining process of nuclear fission;
- Any accidental loss or damage or liability directly or indirectly caused by or contributed to by or arising from nuclear weapons material;

- Any accidental loss or damage and/or liability directly or indirectly or proximately or remotely occasioned by contributed to by or traceable to or arising out of or in connection with war, invasion, the act of foreign enemies, hostilities or warlike operations (whether before or after declaration of war) civil war, mutiny rebellion, military or usurped power or by any direct or indirect consequence of any of the said occurrences and in the event of any claim hereunder the insured shall prove that the accidental loss damage and/or liability arose independently of and was in no way connected with or occasioned by or contributed to or traceable to any of the said occurrences or any consequences thereof and in default of such proof, the Company shall not be liable to make any payment in respect of such a claim; and

- The Company shall not be liable for each and every claim under Section I (loss of or damage to the vehicle insured) of this Policy in respect of the deductible stated in the schedule.

Insurance of Private Cars/Three/Two Wheelers

This insurance covers accidental loss or damage to the vehicle and/or liability arising out of the use of vehicle as described in the policy occurring during the period of insurance, subject to the terms, conditions, endorsements, clauses or warranties forming part of the policy. Following are the important aspects to be considered for issuance of Motor OD policy covering private car or two-wheeler.

Types of Vehicles

Following types vehicles are considered here:

(a) Private Car Type Vehicles used for social, domestic and pleasure purposes and also for professional purposes (excluding the carriage of goods other than samples) of the insured or used by the insured's employees for such purposes but excluding use for hire or reward, racing, pace making, reliability trial, speed testing and use for any purpose in connection with the Motor Trade.

(b) Motorized three wheeled vehicles (including motorized rickshaws/cabin body scooters used for private purposes only).

(c) Motorized three wheeled vehicles (including motorized rickshaws/cabin body scooters used for private purposes only), with engine cubic capacity exceeding 750 cc but not exceeding 1000 cc, are to be rated on the basis of minimum cubic capacity of 1000 cc. Motorized three wheeled vehicles with engine cubic capacity not exceeding 750 cc. is also to be rated as Private Cars with 50 per cent discount on Own Damage premium only.

Rating Factors

The premium rating is based on the following factors:

- Insured's Declared Value (IDV) of the vehicle
- Cubic Capacity
- Geographical Zones
- Age of the vehicle
- Additional premium for electrical / electronic items
- Additional premium for electrical / electronic items
- Additional premium for compulsory PA cover to owner-driver

Risks Covered

This policy covers the indemnification of the accidental loss or damage to the vehicle or the accessories thereon due to the following perils:

- Accidental external means

- Fire, explosions, self-ignition or lightning
- Burglary, housebreaking or theft
- Riot and Strike
- Earthquake
- Flood, typhoon, hurricane, storm, tempest, cyclone hailstorm
- Malicious act
- Terrorist Activity
- While in transit
- Landslide and Rock side

Protections, Removal and Re-delivery

In case of the vehicle being disabled due to loss or damage from the insured peril, the insurer will indemnify the reasonable cost of protection and removal to the nearest repairer and redelivery to the insured up to the limits specified in the policy.

Limitation as to Use

The policy covers the use of the vehicle for any purpose other than those specified below:

- Hire or Reward
- Carriage of goods (other than samples of personal luggage)
- Organized racing
- Pace making
- Speed testing

- Reliability Trials
- Any purpose in connection with Motor Trade

Condition as to Driver

Any person including the insured may drive the policy, provided that:

- A person driving holds an effective driving license at the time of accident and is not disqualified from holding or obtaining such a license
- The person holding an effective learner's license may drive the vehicle but must satisfy the requirements of Rule 3 of the Central Motor Vehicles Rule of 1989

Note: General Regulations, General Conditions, General Exclusions will apply to this policy

Motor Policy - Commercial Vehicles (Certain Special Considerations)

It is subject to all General Regulations, General Conditions, General Exclusions discussed earlier.

General

The scope, coverage conditions etc., of motor policy are almost same as are mentioned above in respect of Motor Insurance policy in respect of private cars, two wheelers etc., used for private purpose discussed earlier except the following aspects specially applicable for Motor Policy applicable for Motor Policy in respect of Commercial vehicles.

Specific Exclusions

The insurer will not be liable to pay in respect of the following:

- Consequential loss, depreciation, wear and tear, mechanical or electrical breakdown, failures or breakages;

- Damage or loss caused by overloading or strain of the insured vehicle;
- Damage to accessories caused by burglary or housebreaking or theft unless such insured vehicle is stolen at the same time;
- Damage to tires or tubes unless the vehicle is damaged at the same time; and
- Deductible for the amount specified in the policy.

Limitation to use

As per Motor Vehicles Rules 1989

Conditions as to Drivers

Table-21 shows the classes of persons entitled to drive the commercial vehicles.

Table-21: Classes of Persons Entitled to Drive Commercial Vehicles

Stage Carriage/ contract Carriage/ Private Service Vehicle	Any person including insured: ▪ Provided that a person driving holds an effective driving license at the time of the accident and is not disqualified from holding or obtaining such a license ▪ Provided also that the person holding an effective learner's license may also drive the vehicle when not used for the transport of passengers at the time of accident and that such a person satisfies the requirements of the Rule 3 of the Central Motor Vehicles Rules 1989.

Goods Carriage	Any person including insured: ▪ Provided that a person driving holds an effective driving license at the time of the accident and is not disqualified from holding or obtaining such a license ▪ Provided also that the person holding an effective learner's license may also drive the vehicle when not used for the transport of goods at the time of accident and that such a person satisfies the requirements of the Rule 3 of the Central Motor Vehicles Rules 1989
Non Transport Vehicles	Any person including insured ▪ Provided that a person driving holds an effective driving license at the time of the accident and is not disqualified from holding or obtaining such a license ▪ Provided also that the person holding an effective learner's license may also drive the vehicle and that such a person satisfies the requirements of the Rule 3 of the Central Motor Vehicles Rules 1989

Rules Applicable to Tankers Carrying Hazardous Chemicals

Rule 129 - Spark Arrester

Every goods carriage carrying goods of dangerous or hazardous nature to human life, shall be fitted with a spark arrester as per Rule 129 of The Central Motor Vehicles Rules 1993.

Rule 131 - Responsibility of Consignor for Safe Transport of Dangerous/Hazardous Goods

i. It shall be the responsibility of the consignor intending to transport any dangerous or hazardous goods listed in the Table II, to ensure the following, namely:

a. The goods carriage has a valid registration to carry the said goods

b. The vehicle is equipped with necessary first aid, safety equipments and antidotes as may be necessary to contain any accident.

c. The transporter or the owner of the goods carriage has full and adequate information about the dangerous or hazardous goods being transported

d. The driver of the goods carriage is trained in handling the dangers posed during transport of such goods

ii. Every consignor shall supply to the owner of the goods carriage full and adequate information about the dangerous and hazardous goods being transported as to enable the owner and the driver to

a. Comply with the requirements of Rules 129 to 137

b. Be aware of the risks created by such goods to health or safety or any person

iii. It shall be the duty of the consignor to ensure that the information is accurate and sufficient for the purpose of the complying with the provisions of Rules 129 to 137.

Rule 132 - Responsibility of the Transporter or Owner of Goods Carriage

i. It shall be the responsibility of the owner of the goods carriage transporting any dangerous or hazardous goods to ensure the following, namely:

a. The goods carriage has a valid registration to carry the said goods and the said carriage is safe for the transport of the said goods

b. The vehicle is equipped with necessary first aid, safety equipments, tools box and antidotes as may be necessary to contain any accident.

ii. Every owner of a goods carriage shall, before undertaking the transportation of dangerous or hazardous goods in his goods carriage, satisfy himself that the information given by the consignor is full and accurate in all respects and correspond to the classification of such goods specified in Rule 137.

iii. The owner of the goods carriage shall ensure that the driver of such carriage is given all the relevant information in writing as given in goods entrusted to him for transport and satisfy himself that such driver has sufficient understanding of the nature of such goods and the nature of the risks involved in the transport of such goods and is capable of taking appropriate actions in case of any emergency.

iv. The owner of the goods carriage for the dangerous or hazardous goods and the consignor of such goods shall lay down the route for each trip which the driver shall be bound to take unless directed or permitted otherwise by the police authorities. They shall also fix a timetable for each trip to the destination and the back with reference to the route so laid down.

v. It shall be the duty of the owner to ensure that the driver of the goods carriage carrying dangerous or hazardous goods holds a driving license as per provisions of Rule 9.

vi. Notwithstanding anything contained in Rules 131 and 132, it shall be sufficient compliance of the provisions of these rules if the consignor transporting dangerous or hazardous goods and the owner of the goods carriage or the transporter abide by these conditions.

Motor Trade Road Risks Policy

It is subject to all general regulation, general conditions and general exclusions discussed earlier. This policy is issued on a Named Driver or Trade Certificate Basis. Where a firm deals in with both registered and un-registered vehicles, then policies may be issued on both Named Driver and Trade Certificate basis.

Perils Covered and Indemnification

1. An insurer will indemnify the insured against loss or damage to the vehicle insured hereunder and/or its accessories whilst thereon:

    - by fire explosion self ignition or lightning ;
    - by burglary housebreaking or theft ;
    - by riot and strike;
    - by earthquake (fire and shock damage)
    - by flood typhoon hurricane storm tempest inundation, cyclone hailstorm frost
    - by accidental external means
    - by malicious act
    - by terrorist activity
    - whilst in transit by road rail inland waterway lift elevator or air
    - by landslide/rockslide

Exclusions

- Consequential loss, depreciation, wear and tear, mechanical or electrical breakdown, failures or breakage’s nor for damage caused by overloading or strain nor for loss or damage to accessories by burglary, housebreaking or theft unless the vehicle insured is stolen at the same time.

- Damage to tyres and tubes unless the vehicle insured is damaged at the same time in which case the liability of the Company is limited to 50 per cent of the cost of the replacement.
- Any accidental loss or damage suffered whilst the insured or any person driving the vehicle with the knowledge and consent of the insured is under the influence of intoxicating liquor or drugs.
- In the event of the vehicle insured being disabled by reason of loss or damage covered under this Policy the Company will bear the cost of protection and removal to the nearest repairer and redelivery to the insured but not exceeding Rs 150 in respect of any one accident.

Rating

(a) For Road Risks

Table-22: Limit of OD Loss/Damage say up to Rs 25000

Named Drivers/ Trade Certificate	**OD Premium**	**TP Liability Premium**
1st Named Driver / Certificate Additional Drivers	Fixed Amount + % of IDV	Amount fixed by pool
Say 2nd to 5th	Certain Additional Amount per head	Additional Amount as per pool
6th to 10th	Less Additional Amount per head	Additional Amount as per pool
11th to 15th	Further less Additional Amount per head	Additional Amount as per pool
16th and above	Further less Additional Amount per head	Additional Amount as per pool
1.If OD indemnity limit exceeds Rs 25000 OD premium will increase as per U/W policy		
TP Liability for property damage may be increase with additional premium.TP Liability for bodily injury like other is unlimited		

(b) No Claim Discount

No claim discount may be allowed provided that no own damage claim is pending and no payment has been made in connection with any vehicle covered by this policy. Generally following type of No Claim Discount was followed by insurers for motor trade and and industrial risk.

Table-23: No Claim Discount

Claim Status	**No Claim Discount (old)**
No Claim made or pending for preceding 1. year of ins.	15 per cent
No Claim made or pending for preceding 2 cons. year of ins	25 per cent
No Claim made or pending for preceding 3 year or more	30 per cent

Motor Trade Internal Risk Policy: Specific Considerations

It is subject to all general regulation, general conditions and general exclusions discussed earlier. This policy covers risks of Motor Manufacturers and Motor Trade Assembly factories. Generally two types of Policies are issued for this purpose; “A” Policy and “B” Policy “A” Policy covers only Liability to Public Risks and “B” Policy covers Property Damage and Liability to Public Risks.

Indemnity

Table-24: Indemnity Cover

Cover	**Indemnity**	
	Policy A	**Policy B**
Bodily Injury	Unlimited	Unlimited
Property Damage excluding damage to vehicles	Rs. 150000 AOA	Rs 150000 AOA
Damage to vehicles property	Not Applicable	Rs 150000 AOA
Damage to own vehicle	Not Applicable	Rs 30000 AOA

Basis of Rating

- Superficial area of premises (Whole of land & Building)
- % of Wages paid to the employees.

Motor Proposal Form

A specimen of Motor proposal form has been given hereinafter for ready reference and for better understanding of motor risk analysis for motor underwriting. Every insurance company shall draft or design the proposal form according to their underwriting policy. However the following type of proposal form is generally used for private car or motorized two wheelers.

PROPOSAL FORM

(The queries made/details stated below are the minimum requirements to be furnished by a proposer. The Insurer may seek any other information as desired for underwriting purpose.)

Proposer's (Owner's) Full Name:
Address (Address where vehicle is normally kept and used):
Pin Code: Tel. No: Fax No: E-Mail Address:
Occupation / Business: Type of Cover required : Liability Only Policy / Package Policy / Others (specify)
Period of Insurance: From .... To ....

1. Registration No. and Date of Registration of the Vehicle:
2. Registering Authority & Location:
3. Year of Manufacture:
4. Engine No:
5. Chassis No.:
6. Make of Vehicle:

7. Type of Body/Model:

8. Cubic Capacity:

9. Seating capacity including Driver:

10. Whether the vehicle is driven by non-conventional source of power If yes, please give details. Yes/No

11. Whether the vehicle is used for driving tuitions. Yes/No

12. Whether extension of geographical area to the following countries required ? Yes/No
    Bangladesh, Bhutan, Maldives, Nepal.
    Pakistan and Sri Lanka

    If 'Yes' state the name of the countries.

    1)

    2)

    3)

13. Whether use of vehicle is limited to own premises? Yes/No

14. Whether vehicle is used for Commercial purposes? Yes/No

15. Whether vehicle belongs to foreign embassy / consulate? Yes/No

16. Whether the car is certified as Vintage car by Vintage and Classic Car Club of India? Yes/No

17. Whether vehicle is designed for use of Blind/ Handicapped/mentally challenged persons and duly endorsed as such by RTA? Yes/No

18. Whether the vehicle is fitted with fibre glass tank? Yes/No

19. Do you wish to opt for higher deductible over and above the compulsory deductible (Rs 50 for Two Wheelers and Rs.500/Rs.1000/- for Private Cars) Yes/No

If yes, please specify the amount
(for two wheelers) Rs 500/750/1000/1500/3000

(for private cars) Rs 2500/5000/7500/15000

20. Are you a member of Automobile Association of India? Yes/No

If yes, please state

a. Name of Association ____________________

b. Membership No. ________________________

c. Date of expiry _________________________

21. Are you entitled to No Claim Bonus? Yes/No

If yes, please submit proof thereof.

22. Is the vehicle fitted with the any Anti-theft device approved by the AARI.? Yes/No

If Yes, attach Certificate of Installation in the vehicle issued by Automobile Association of India.

23. Liability to Third Parties.
The policy provides Third Party Property Damage (TPPD) of Rs.1 lakh/-(Two wheelers) and Rs.7.5 lakhs (Private Cars).

Do you wish to to restrict the above limits to the statutory TPPD Liability limit of Rs.6000/- only? Yes/No

24. Do you wish to cover Legal Liability to?

A) Driver (No. of persons _____________) Yes/No

B) Other employees (No. of persons_________) Yes/No

C) Unnamed Passengers (No. of Persons______) Yes/No

25. Do you wish to include Personal Accident (P.A.) Cover for Named persons? Yes/No

    If yes, give name and Capital Sum Insured (CSI) opted for. The maximum CSI available per person is Rs 2 lakhs in the case of Private cars and Rs. 1 Lakh in the case of Motorised two wheelers.

    Name **CSI Opted (Rs)**

    1.

    2.

    3.

26. Do you wish to include P.A. Cover for unnamed

    persons /hirer/pillion passengers (two wheelers)? Yes/No

    If yes, give the number of persons and Capital Sum Insured (CSI) opted. The maximum CSI available per person is Rs. 2 lakhs in the case of Private cars and Rs. 1 lakh in the case of Motorised two wheelers.

    Number of persons **CSI Opted (Rs)**

27. Insured's Declared Value (Please fill up Ttable-25)

Table-25: Insured's Declared Value

Insured's Declared Value of vehicle	Non - electrical accessor-ies fitted to the vehicle	Electrical & electronic accessor-ies fitted to the vehicle	Side Car (two wheeler) Trailer (Pvt. cars)	Value of CNG / LPG Kit	Total Value
Rs.	Rs.	Rs.	Rs.	Rs.	Rs.

28. Previous History

    a. Date of Purchase of the vehicle by the proposer _______________

b. Whether the vehicle was New or Second Hand at the time of Purchase _______________

c. Will the vehicle be used exclusively for

A. private, social, domestic, pleasure & professional purposes (Yes/No)

B. carriage of goods other than samples orpersonal luggaged. (Yes/No)

d Is the vehicle in good condition ? (Yes/No)

If "No" please give full details ______________________________

e. Name and address of the previous insurer ___________________

f. Previous Policy Number ____________________ Period of Insurance from ________/_________/________ to ______/ ________/_____

g. Type of cover: Liability Only Cover / Package Cover /Others (specify)

h. Claims lodged during the preceding 3 years — Year — Number — Amount (Rs.)

i. Has any insurance company ever :

(a) declined the proposal (Yes/No)

(b) cancelled & refused to renew (Yes/No)
(if yes, reasons there for)...........................

(c) imposed special condition or excess (Yes/No)
(if yes, reasons and details thereof).............

29. Details of Hire Purchase / Hypothecation / Lease

(a) Is the vehicle proposed for insurance :

Under Hire Purchase (Yes/No)
Under Lease Agreement (Yes/No)
Under Hypothecation Agreement (Yes/No)

(b) If yes, give name and address of concerned parties ____________

30. Details of Driver:

(a) Age Owner Driver

Others

(b) Does the driver suffer from defective vision or hearing or any physical infirmity. (Yes/No)

If "Yes" please give details.

(c) Has the driver ever been involved/convicted for causing any accident or loss ? If yes, please give details as under including the pending prosecution, if any:

Driver's Name	Date of Accident	Circumstances of Accident/ Claim	Loss/Cost Rs.

31. Any other relevant information:

Declaration by Insured

I / We hereby declare that the statements made by me / us in this Proposal Form are true to the best of my / our knowledge and belief and I / We hereby agree that this declaration shall form the basis of the contract between me / us and the "______________________________ Co. Ltd."

I/We also declare that any additions or alterations are carried out after the submission of this proposal form then the same would be conveyed to the insurers immediately.

Place

Date Signature of Proposer

12

MOTOR THIRD PARTY INSURANCE

Motor Third Party Insurance – Background and Present Scenario

Motor Third Party business constitutes a major portfolio in non-life insurance. In 200-05 it has come to Rs 2,114 crores being 11 per cent of total business. It is the highest loss incurring business with Incurred Claim Ratio-250 per cent being the major concern for all insurers because of huge outstanding claims being 20 lakhs in number and for Rs 15,000 crores (Approximately) in volume. This volume of outstanding claims constitutes 75 per cent of total outstanding claims in the industry creating a major concern for all market players. Most of the underwriters are not interested in underwriting this loss portfolio for the following problems. In view of social objectives as well as the individual insurers' reluctance or resistance to transact such loss-incurring business because of above inherent problems, the regulator has shifted the responsibility of management of Motor Third Party insurance business to Motor Third Party pool as it is being followed in many other countries.

Problems in Motor Third Party Insurance

Major concerns of insurers in respect of Motor Third Party Insurance are:

- Escalating TP Claims and Incurred Claim Ratio
- Delay in Disposal of Claims
- Rampant Malpractices in TP Claims
- Low Rate of premium –total mismatch with I/claim

- No Co-operation from the insured & police
- No Cap on the upper limit of Compensation
- No time limit to file petition
- Wide Jurisdiction- Multiplicity of Claims
- Absolute Liability
- Limited Defences
- Liberal interpretation of the Act in favour of petitioner and insured
- Computation of final liability – a major problem in view of ever changing trend and inconsistency on the basis of computation.
- Multiplier method (Lord Wright) - The choice of multiplier to be decided by the Court out of the experience with consideration for pecuniary loss caused to dependents and annual dependency of the dependents for systematic & realistic basis.
- Although the maximum multiplier should not exceed 18 there are many reported case where the multiplier 13 has been used for a person aged 37 & 15 for a person aged 52
- Notional income has been increased from Rs 2000 to Rs 3000 pm over the last 2 years while about 50 per cent of the population lives below poverty line.
- Assessment of injury claims should be on the realistic basis especially in case of evaluation of disability depending on rating of permanent disability established, functional evaluation of medical expert, loss of earning affected by disability.

Legal Aspects

The Third Party Liability covered by the Act Only Policy includes the legal liability arising under Common Law (Law of Torts) and under the specific statute, i.e. the Motor Vehicles Act 1988 (M.V. Act 1988). The law of torts implies the civil wrong including negligence or breach of duty of care or breach of duty to take care of the third party. The motor insurance is influenced and necessitated by the Motor Vehicles Act, 1988 (The original Motor Vehicles Act 1939). This act makes it mandatory for the owner or user of the vehicles in the public place to insure the vehicles against the third party risk along with the licensing of drivers, registration of motor vehicles, construction equipments and maintenance of vehicles, controller of traffic. The chapter X, XI and XII of the Motor Vehicles Act 1988 deal exclusively with compulsory third party insurance or motor vehicles. The provisions in the chapters are the fundamental legal aspects for management of motor insurance both underwriting and claims especially in respect of third party liability.

No Use of Motor Vehicle without Insurance

Section 146 of the M.V. Act 1988 provides that 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 complying with the requirements of the Act.

Insurance Policy to be Issued by an Authorized Insurer

Sec.147 of the Motor Vehicles Act provides that the policy of insurance must provide the following cover:

- Against any liability which may be incurred by the insured in respect of death or bodily injury to any person
- Damage to any property of third party
- Against death or bodily injury to any passenger of a public service vehicle caused by the use of his vehicle in the public place.

But this policy shall not cover the following:

- Any contractual liability
- Any liability in respect of death or disablement or bodily injury arising out of and in the course of employment of the employee of the insured. However this policy shall cover liability arising under Workmen Compensation Act 1923 in respect of death or bodily injury to such employee – if engaged in driving the vehicle or if engaged as conductor, ticket examiner in public service vehicle or if it is a goods carriage, being carried in the vehicle.

Motor Vehicles Act 1988 & Third Party Insurance

The Motor Vehicles Act 1988 governs and administers the compulsory Motor Third Party Insurance, i.e. Act only Policy. The provisions of Section 140 to 144 deal with "Liability without Fault". The provisions of Section 145 to 164 of the Act deal with Insurance of Motor Vehicles against Third Party Risks. The provisions of Section 165 to 176 of the Act deal with third part claims under Claims Tribunal.

No-fault liability or Liability without Fault under Section 140

- It provides for payment of compensation on fault basis for Rs 50,000 in case of death and Rs 25,000 in case of disablement.
- It provides for payment of minimum statutory relief to the victim of the road accident or his legal representative.
- The claimant in this case is not required to prove wrongful act, default or negligence on the part of the owner of the vehicle or any other person.
- It is defeated neither by quantum of compensation nor the legal defence of contributory negligence to the motorist or the insurer.

- The motor accident claims tribunal has also to adjudicate on the case on no fault basis.

Under Section 141(3) if the compensation on the principle of fault is less than the no-fault liability, then the insurance companies are not entitled to recover the payment made under no-fault liability, but if it be more, then the difference between the two compensation amounts will be required to be paid by the insurance companies.

Unlimited Liability

All limitations of liability for death or bodily injury to third parties based upon the class of vehicle are abolished. In effect, the liability of insurance companies for all classes of vehicles for third party death or bodily injury will be deemed as UNLIMITED and would cast upon the insurance companies the duty to satisfy the entire judgment passed by the MACT, and no portion thereof can be shared by the insured unless the liability of the insurer is exonerated in terms of the statutory defences contained in Section 149(2) of the new Act. In respect of damage to the property of third party, the limit continues at Rs 6000.

Notice to the Insurance Company

Under Section 149 if before commencement of proceedings, in which judgement/award is given, no notice is given to the insurance companies, then no such award or judgement is binding upon the insurer. Under 1939 Act, even the notice at the time of execution or appeal was considered as sufficient. Thus, under the Act 1988, no sum shall be payable by the insurer in respect of any judgement unless, before the commencement of the proceedings, the insurer had notice through the Court concerned of the bringing of the proceedings.

Transfer of Certificate of Registration

Under Section 157 of the new Act lays down that when the Certificate of Registration is transferred from one person to another, then the Policy of insurance in respect of that vehicle shall also be deemed to have been transferred to that other person from the date on which the owner-ship of the motor vehicle stands transferred.

Production of Certificates

Section 158 provides that a person driving a motor vehicle involved in an accident in any public place should produce:

- the Certificate of Insurance
- the Certificate of Registration

Structured Compensation

Section 163 provides structured and final determination of compensation which cannot be altered or affected by taking recourse to any other section in the Act unlike Section 140 where the compensation awarded can be set off against a higher compensation receivable under Section 166. It is final but not an interim compensation. A claim application under Section 163-A is not tenable in general if income of the victim exceeds Rs 40,000 per Annum, but if the person with higher income notionally brings down his income Rs 40,000 in order to present the case under Section 163-A it is permitted.

Salient aspects of U/s 163 (A) & 163(B)

The compensation as per structure formula depending upon the age and the multiplier:

- Minimum compensation Rs 50,000.
- Besides compensation General damages for funeral expenses, loss of consortium, loss of estate, municipal taxes in case of death.
- General damages for pain and sufferings and medical expenses.

- The compensation mentioned in the schedule shall be payable on the basis of no fault however, the scheme is optional and if the claimant feels that, the amount prescribed in the schedule is not acceptable a claim can be filed under the existing provision of the Motor Vehicles Act 1988.

Withdrawal of Period of Limitation

Section 166 of Motor Vehicles Act has withdrawn the period of limitation. Insurers may move to reintroduce it as per recommendation of the committee. As the recent amendment of Section 166 a claimant may file a claim petition at any place like place of accident, place of residence of victim or place of residence of claimant giving rise to multiplicity of claims and the real problem in effective use of police report available under Section 158(6) for proper settlement of claim. All above legal provision have had major impact on the decision of the underwriter about selection, classification, acceptance and rating of motor TP risks today.

Compensation for "Hit and Run Accident"

Section 161 provides for payment of compensation (solatium) as follows:

(a) in respect of the death of any person resulting from a hit and run motor accident, a fixed sum of Rs 8500.

(b) in respect of grievous hurt to any person resulting from a hit and run motor accident, a fixed sum of Rs 2000.

"Grievous hurt" shall have the same meaning as in the provisions of Section 320 of the Indian Penal Code.

Legal Definitions of Certain Terms Used for Motor TP Insurance

Following terms are to be used as per definitions given by the Motor Vehicles Act.1988 both for the purpose of underwriting and settlement of claim as per court orders.

Contract Carriage

This means a motor vehicle which carries passengers for hire or reward and is engaged under a contract whether expressed or implied, for the use of such vehicle as a whole for the carriage of passengers mentioned therein and enter into by a person holding a permit in relation to such vehicle or any such person authorized by him in this behalf on a fixed or agreed rate or sum on a time basis or from one point to another without stopping to pick up or set down passengers not included in the contract anywhere during the journey and including a maxi cab or a motor cab.

Stage Carriage

This means a motor vehicle constructed or adopted to carry more than 6 passengers excluding the driver for hire or reward at separate fares either for the whole journey or stages of the journey.

Driving License

This means the license issued by competent authority under chapter II of the Motor Vehicles Act 1988.

Public Place

This means a road, street, way or other place whether a thorough fare or not to which the public have right of access and includes any place or stand at which passengers are picked up or set down by a stage carriage.

Hit and Run Accident

Sections 161, 162 & 163 of Motor Vehicles Act, 1988 incorporates special provisions regarding compensation in respect of “hit and run motor accidents. Section 161 defines ‘hit and run motor accident’ as 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.

Motor TP Underwriting

Following are the major aspects considered by insurer for underwriting of motor TP insurance:

- Separate proposal form
- Risk-based rating.
- Proposal form to be filled up by the proposer with his signature and date
- Scrutinized and signature of the underwriter in support of acceptance
- Proposal to be preserved for review at the time of processing of claim
- Break Insurance is subject to following procedure
    - Inspection by responsible officer with time & proof.
    - Fresh Proposal,
- T P Liability premium is collected by insurer on behalf of the Indian Motor Third Party Insurance Pool (IMTPIP)
- No Agency Commission or Brokerage on Motor Third Party Insurance business
- Documents to be collected with proposal
    - Copy of RC Book
    - Invoice copy
    - Previous insurance policy
    - copies of permit, fitness, route permit and proof of residence of owner (commercial vehicle)

- Motor TP Premium is determined by pool and TACC in consideration of the followings factors:
    - o Class of vehicle
    - o Cubic capacity
    - o Use of vehicle
    - o Gross vehicle weight (GVW)
    - o Special types of vehicles
    - o Passenger Carrying Vehicles
    - o Goods Carrying Vehicles
    - o Motor Trade (Road Transit) Risks

Indian Motor Third Party Insurance Pool (IMTPIP)

At Present Motor Third Party Insurance is administered by Motor Pool known as Indian Motor Third Party Insurance Pool (IMTPIP). As per the new arrangement, all third party motor insurance premiums and claims are managed by IMTPIP being controlled by the General Insurance Corporation of India. Motor TP Pool is an arrangement among members being insurers to share the motor TP risk insurance. India Motor Insurance Pool is a risk sharing pool formed by 13 participating non-life insurers for taking over the motor third party risks. Under this pool arrangement, the participating insurers on the basis of their respective market share the motor third party claims. Pooling is achieved through a multi-lateral reinsurance arrangement. In this mechanism, underwriting insurer-collecting premium is responsible for collecting and remitting the service tax. Again, claim servicing insurer is responsible to deduct and remit tax on payments as and when required.

Need of Motor TP Pool

In the Tariff regime Vehicle owners many times faced difficulty in securing motor vehicle insurance for their vehicles because of high claim ratio for motor third party insurance. In detariff regime, with Freedom for individual underwriters to underwrite motor risks at rates and terms appropriate for insurers, the difficulty of the vehicles owners might have got aggravated especially w.r.t. commercial vehicles because the underwriters are always reluctant to avoid Motor TP insurance in view of the fact that Motor TP claim ratios are more than 200 per cent. Motor TP premium rates unable to cover Claim. The major share of TP insurance was cross-subsidized by the profits from Fire and Engineering business in the tariff regime. But in the de-tariff regime such cross-subsidization has become quite impossible, as premium in fire and engineering department has been slashed by 70 to 80 per cent from the rates provided by erstwhile tariff. As TP insurance is mandatory in terms of Motor Vehicles Act 1988, the Government felt the need of formation of Indian Motor Third Party Insurance Pool for the benefit of the society at large ensuring easy insurance of motor third party liability risks. Consequently IRDA intervened and directed formation of Indian Motor Third Party Insurance Pool effective from Ist January 2007.

Operation of Motor TP Pool

For the financial year 2007-08, the first year of operation, Motor TP Pool collected premium of Rs 2800 crores. In 2008-09, this premium has been increased by another 20 per cent. With claim payouts, the pool is set to create a database of claims settlement, which may enable the pool to increase or decrease the technical reserves. With this process, the pool will be treated as a profit center and corporatization will be done after the pool becomes a profitable entity. Currently, most of the insurance companies resort to over provisioning as a prudential norm. Under this new arrangement, no vehicle owner shall be denied for TP insurance cover for the vehicle with valid permit for use on public roads except on grounds of attempted fraud. IMTPIP call centre has been set up to receive intimation regarding accident to the insured vehicles. The call centre will collect information on a standard template. If the vehicle is registered under the Pool, then the call center will intimate underwriting and claims office about the accident (with TOLL FREE NO. 1800 224080; Tolled Dial: 32648888).

IMTPIP-Members

Every insurer who is registered for carrying on general insurance business (including motor insurance business) under the Insurance Act, including GIC of India shall be member of the Pool. Specialist insurers like ECGC, Agriculture Insurance Corporation and stand-alone health insurers are exempted.

IMTPIP Administrator

General Insurance Corporation of India is the Pool Administrator in conformity with the IRDA regulations.It will act under the guidance of the General Insurance Council is to establish various committees who advise GIC on various aspects of IMTPIP –Administrator. Following are the important committees formed by General Insurance Council to extend support and advices to GIC for the administration of motor TP pool.

- Underwriting Committee
- Claims Committee
- Administration Committee
- Investment Committee
- Accounts Committee
- Statistical Committee
- IT Committee

IMTPIP - Shares of Members

GIC rupee share is same as the percentage share of statutory cessions to GIC, while other members' share are in the same proportion as the total GDPI of the insurer in respect of all classes of general insurance business for a financial year bears to the total market GDPI in India in respect of all classes of general insurance business of all member insurers for the financial year.

Motor TP Pool Premium Rates

Coverage is only for TP insurance cover without any element of motor OD cover. It is strictly in compliance with the procedures, terms and conditions as laid down by the Underwriting Committee of the Pool in the Manual. Rates notified by IRDA are binding for the pool. Following is the summary of Motor TP premium:

1. TP Premium—Private Car & Two-Wheeler

Private Car	Premium
– Not exceeding 1000 cc	670
– Not exceeding 1500 cc	800
– Exceeding 1500 cc	2500
Two Wheeler	
– Not exceeding 75 cc	300
– Not exceeding 150 cc	300
– Not exceeding 350 cc	300
– Exceeding 350 cc	620

2. TP Premium— Goods carrying vehicle Public carrier & Private carrier

i. Goods carrying vehicle	**Public carrier**	**Private carrier**
– Not exceeding 7500 Kg.GVW	5580	5000
– Not exceeding 12000 Kg.	5920	5300
– Not exceeding 20000 Kg.	6090	5440
– Not exceeding 40000 Kg.	6260	5610
– Exceeding 40000 Kg.	6770	6050
ii. Three wheelers (motorized)	1530	1450

3. Passenger carrying vehicle

i. Four wheelers with capacity not exceeding 6 persons

– Cubic capacity	Basic Premium
– Not exceeding 1000 cc	1650
– Not exceeding 1500 cc	2330
– Exceeding 1500 cc	2840

Basic premium will be loaded by prem. per passenger @ Rs 350 (license capacity)

ii **Four wheelers capacity exceeding 6 persons** basic premium with loading @ Rs 235 per person. Rs 3160

iii. **Three- wheelers with capacity up to 6 persons'** basic premium with loading @ Rs.315 per person Rs 510

iv. Motorised two wheelers (hire or reward)

Cubic capacity	Premium
• Not exceeding 75 cc	300
• Not exceeding 150 cc	300
• Not exceeding 350 cc	300
• Exceeding 350 cc	680

IMTPIP - Claim processing

Third party death or injury/physical damage claims shall be settled in a speedy and efficient manner in accordance with the instructions of the General Insurance Council. The Council adopted a pro-active claims settlement policy with most efficient claims processing practices possible. Claims processing for pooled business always follow procedures and limits of authority as laid down by the Claims Committee.

IMTPIP - Remuneration

Motor TP pool business is not subject to any agency commission or brokerage. The underwriting insurer will be paid a reinsurance commission of 10 per cent 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 per cent of the total premium on motor third party insurance business in respect of the business underwritten for the pooled account.

IMTPIP - Accounts

The accounting year for the Pool will be from 1st April to 31st March. The Pool system is designed to develop the accounts of the pooled business on real-time basis. The Pool Administrator will render the accounts for all Members at such frequency and within such time as the appropriate Committee may decide from time to time. The appropriate Committee will decide on the frequency of settlement of pooled premiums and claims paid.

IMTPIP - Termination

The appropriate committee may terminate the membership of an insurer by giving notice in writing, if member at any time:

- lose the whole or any part of its paid up capital, or
- go into liquidation or receiver be appointed, or
- be acquired or controlled by any other Company, or
- Commit any breach of the conditions of Pool Agreement.

Notwithstanding cancellation of participation of a Member in the Pool, the member shall remain fully responsible for its share in the Pool in respect of all business underwritten for the account of the Pool by all Members up to the date of effect of cancellation.

Certain Terms in Motor Third Party Insurance Policy

(Applicable to all classes of vehicles with suitable amendments in 'Limitations as to Use')

Liability to Third Parties

Subject to the Limit of liability as laid down in the schedule hereto, the Company will indemnify the insured in the event of accident caused by or arising out of the use of the Motor Vehicle anywhere in India against all sums including claimant's costs and expenses which the insured shall become legally liable to pay in respect of:

- death of or bodily injury to any person so far as it is necessary to meet the requirements of the Motor Vehicles Act.
- damage to property other than property belonging to the insured or held in trust or in the custody or control of the insured up to the limit specified in the schedule.

Reimbursement of Legal Costs

The Company will also pay all costs and expenses incurred with its written consent.

Limitations of the Indemnity

In terms of and subject to the limitations of the indemnity which is granted by this policy to the insured, the Company will indemnify any driver who is driving the Motor Vehicle on the insured's order or with insured's permission provided that such driver shall as though he/she were the insured observe fulfill and be subject to the terms exceptions and conditions of this policy in so far as they apply.

Entitlements of Indemnity

In the event of the death of any person entitled to indemnity under this policy the Company will in respect of the liability incurred by such person indemnify his/her personal representative in terms of and subject to the limitations of this Policy provided that such personal representative shall as though such representative was the insured observe fulfill and be subject to the terms exceptions and conditions of this Policy in so far as they apply.

Fatal Inquiry or Alleged Offence

The Company may at its own option

(A) arrange for representation at any Inquest or Fatal Inquiry in respect of any death which may be the subject of indemnity under this Policy; and

(B) undertake the defence of proceedings in any Court of Law in respect of any act or alleged offence causing or relating to any event which may be the subject of indemnity under this Policy.

Avoidance of Certain Terms and Right of Recovery

Nothing in this Policy or any endorsement hereon shall affect the right of any person indemnified by this Policy or any other person to recover an amount under or by virtue of the provisions of the Motor Vehicles Act. But the insured shall repay to the Company all sums paid by the Company which the Company would not have been liable to pay but for the said provisions.

General Exceptions

- The Company shall not be liable in respect of any claim arising whilst the vehicle insured herein
  - o being used otherwise than in accordance with the 'Limitations as to Use'; or
  - o being driven by or is for the purpose of being driven by him/her in the charge of any person other than a Driver as stated in the Driver's Clause.
- The Company shall not be liable in respect of any claim arising out of any contractual liability.
- Except so far as is necessary to meet the requirements of the Motor Vehicles Act, the Company shall not be liable in respect of death arising out of and in the course of employment of a person in the employment of the insured or in the employment of any person who is indemnified under this policy or bodily injury sustained by such person arising out of and in the course of such employment.
- Except so far as is necessary to meet the requirements of the Motor Vehicles Act, the Company shall not be liable in respect of death or bodily injury to any person (other than a passenger carried by reason of or in pursuance of a contract of employment) being carried in or upon or entering or mounting or alighting from the Motor Vehicle at the time of the occurrence of the event out of which any claim arises.

- The Company shall not be liable in respect of any liability directly or indirectly or proximately or remotely occasioned by contributed by or traceable to or arising out of or in connection with War, Invasion, the Act of foreign enemies, hostilities or warlike operations (whether before or after declaration of war), Civil War, Mutiny, Rebellion Military or usurped power or by any direct or indirect consequences of any of the said occurrences and in the event of any claim hereunder, the Insured shall prove that the accident, loss, damage and/or liability, arose independently of and was in no way connected with or occasioned by or contributed to by or traceable to any of the said occurrences or any consequences thereof and in default of such proof, the Company shall not be liable to make any payment in respect of such a claim.

- The Company shall not be liable in respect of any liability directly or indirectly caused by or contributed to by or arising from nuclear weapons material.

Legal Decisions on Motor Third Party Insurance

Public Place

Sec. 146 of M.V. Act requires that no person shall use a motor vehicle in a public place unless there is in force a policy of insurance complying with the requirements of the Motor Vehicles Act.1988:

- In **G. Bhuvanewari vs. Sornakumar (2000),** it was held that public place would cover all places including those places of private ownership where the members of the public could have an access whether free or controlled in any manner whatsoever.

- In **UII vs. Lakshmi (1997),** a wide expanse of the paddy field where an accident took place was held to be a public place.

- In **The New India Assurance Co. Ltd. vs. Urmiladevi (1998**), a person looking after his contract work in a factory was hit by a truck at the factory gate and he sustains fatal injuries. He is entitled to compensation for motor accident under the Motor Vehicles Act 1988.

Use of Vehicle

As per Section 165 death or personal injury must have resulted out of an accident by the use of motor vehicle:

- In **The Oriental Fire & General Insurance Co. Ltd. vs. Sripat (1998**), the death of a cleaner working underneath of his stationery vehicle was said to have met with an accident out of use of vehicle in public place.

- **In UIIC vs. Pushpalaya Printers (2004**), a road roller moving close by to a house that caused damage to the building by tremor caused to the ground and the wall said to have caused an impact and hence actionable.

- **In UIIC vs. Forest Department,** the truck of the forest department met with an accident due to wrongful act of the occupants of the pickup van who throw logs in the public road with a view to obstruct a chase of the patrolling party.

- **Ritadevi vs. The New India Assurance Co. Ltd. (2000),** a passenger who was last seen in the auto rickshaw has been found murdered later. It was held by the Supreme Court that the death must be constructed as having been caused by an accident involving the use of motor vehicle.

Admissibility of TP Claim for a Passenger in a Goods Carrying Vehicle

- **Mallawa vs. The Oriental Insurance Co. Ltd. (1999),** no claim was admissible for a passenger in a good carrying vehicle.

- **The New India Assurance Co. Ltd. vs. Satpalsingh (2000),** the above judgement was considered not applicable for the amended Motor Vehicles Act, 1988 as Insurance policy covering third party risk without any exclusion for gratuitous passenger.

- **The New India Assurance Co. Ltd. vs. Asarani Devi (2002),** the Supreme Court upheld the decision in Satpalsingh Case. Supreme Court also decided that, as per amended provisions of the Motor Vehicles Act effective from 14 November 1994 the policy of insurance shall cover against any liability which may be incurred by the insured for death or bodily injury to any person including owner of the goods or his authorized representative carried in the vehicle.

- **Kaniapa Nadar vs. Jayapandi Madras (1997),** held that persons travelling in the goods vehicle along with their paddy bags were entitled to get compensation in case of injuries and for legal representative in case of death.

The above court judgments are indicative of increasing trend of Motor TP claims resulting into high claim costs. Hence Motor TP underwriting should be very cautious and systematic so that false claims and high awards of courts can be reduced and portfolio cannot bleed heavily affecting other portfolio.

13
HEALTH INSURANCE UNDERWRITING MANUAL

Health Insurance - World's Fastest Growing Insurance Products

Health insurance is one of the world's fastest growing insurance products since it has the highest growth potential in India with a population of 1.3 billion. But the growth potential of health insurance has always remained untapped in India for many reasons. As per industry report, for the year ended 31 March 2008 insurers registered health insurance premium of Rs 5000 crores (approximately) covering about 25 million people or about 2 per cent of the total population of India. There are many reasons for such poor penetration of health insurance in the country. If we discuss evaluation of medical insurance in we will understand that health insurance Underwriting depends on a host of micro and macro factors such as:

Macro Factors

1. Government Healthcare policy—Health Financing, Provisioning etc
2. Government Health Expenditure-Budget Allocation
3. Private Expenditure and paying capacity for healthcare.

Micro Factors

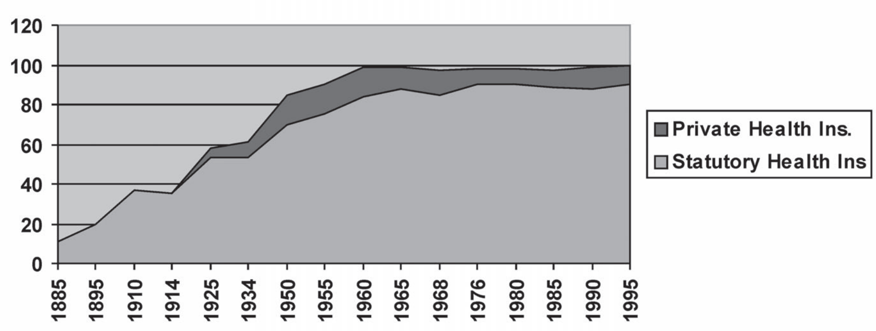
1. Individual Underwriting Policy following Underwriting Philosophy of Insurer
2. Product Development customizing the needs of customers' segments

3. Databank for treatment costs –Disease-wise, Community-wise, Class-wise etc.

Health Insurance and Its Evaluation

Most societies have had able mechanism to social health risks since long. This was originally in the form of mutual-aid societies or organizations like Tontines in West Africa. These associations collected money and supported patients who needed expensive healthcare. It was based on the principle of solidarity and reciprocity. But this mechanism could not thrive much because of two limitations: i) Arbitrary arrangement; and ii) Limited funds. Health insurance as we see it today started in the 17th century with solidarity-based relief funds in Germany. Bismarck passed the first insurance law in 1883, bringing all voluntary funds for the purpose into a single health insurance scheme. Gradually, social health insurance scheme has been developed to the present practice of health insurance mechanism covering 90 per cent of total population in Germany today as it appears from the Figure-1 and similar developments have taken place in many other European countries today.

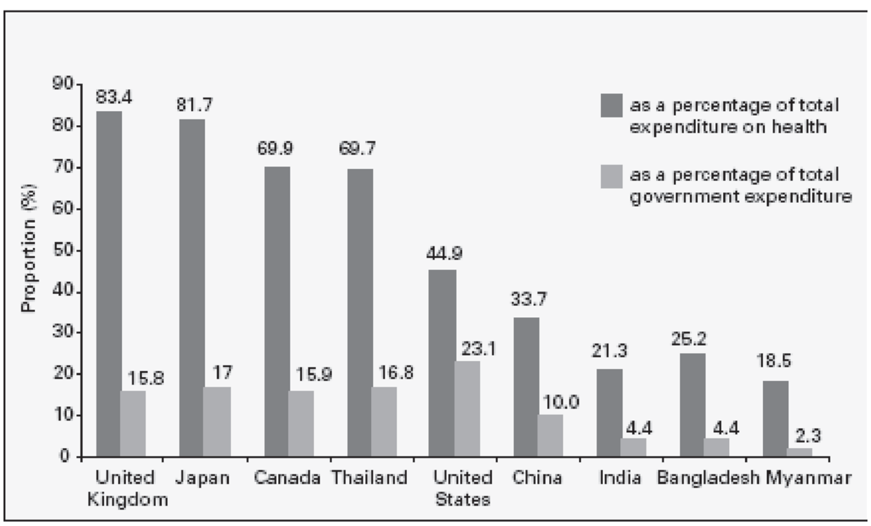
Figure-1. Coverage in Percentage of Total German Population by Health Insurance (1885-1995)



Impact of Govt. Expenditure in India Public Health on Health Insurance

The Indian Constitution lays the prime responsibility for public health for state governments. The Central Government provides about 15 per cent of the funds required mainly spent on national health programmes. Public health expenditure currently for the huge population of 1.3 billion is far below the requirement. Out of the total health expenditure in the country, the share of government expenditure is only about 21 per cent while in U.K. and Japan it is more than 80 per cent, in Canada and Thailand it is about 70 per cent and in the US it is about 45 per cent. Again the share of government health expenditure was calculated as about 4.4 per cent of total expenditure for the 2001-02 as per studies conducted by the Ministry of Health and Welfare, Government of India, though the National Health Policy 2002 provides for the Government's commitment for better health and access to healthcare.

Figure-2. Government expenditure on public health



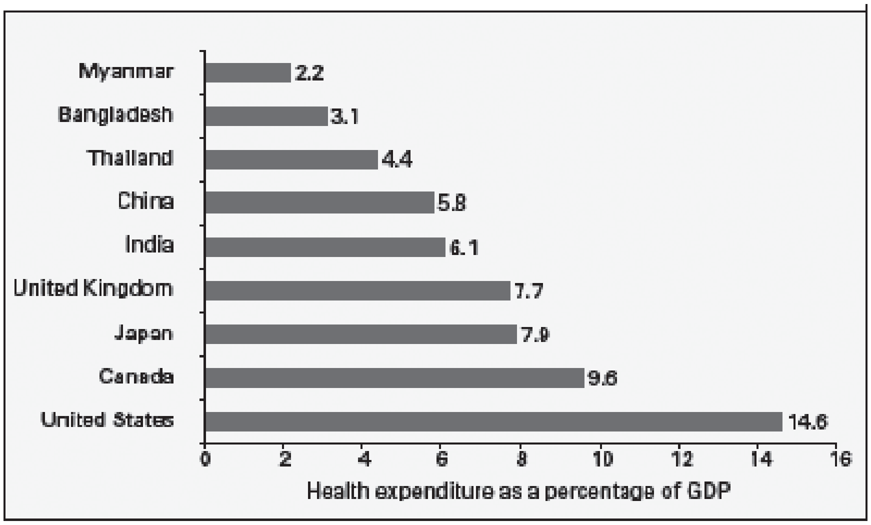
Source: World Health Organisation (2002)

Figure-2. shows on Government Health Expenditure clearly indicates high growth potentials of health insurance for public health where Government contribution is minimal.

Impact of Private Expenditure on Healthcare & Health Insurance

Although India's public spending is low, overall health spending has been increasing due to higher private spending. In 2002, total spending on health was estimated to be 4.8 per cent of GDP, over three times public spending. As a result, India's overall expenditure on health in 2002 was 6.1 per cent of GDP and, as Figure-3 shows, compares well with other developing countries. Currently, less than 10 per cent of the Indian population has some kind of health insurance cover. This includes those covered under the Central Government Health Scheme (4 million beneficiaries), the Railways Health Scheme (1.2 million) and the Employees' State Insurance Scheme (0.3 million). The robust growth of the Indian economy at more than 6 per cent every year, together with a rapid rise in personal incomes, has led to this gap in healthcare spending being increasingly met by private health expenditure. On average, every family spends up to 10 per cent of annual household consumption towards healthcare needs.

Figure-3. Comparison of health expenditure



Source: World Health Organisation (2002)

Health Insurance Evaluation in India

In India health insurance has been in existence for a number of years even prior to nationalization of insurance sector. Formal system of health insurance in India started with the introduction of the **Employees State Insurance Scheme** under the **Employees State Insurance Act, 1948** which provides for both cash and medical benefits to employees in the organizations that comply with certain requirements for registration. The said scheme provides OPD and IPD services and a large variety of cash benefits to insured employees in case of various eventualities and loss of pay. This scheme covers about 33 million people. In 1954 the Government introduced another insurance scheme called the **Central Government Health Scheme (CGHS)** for Central Government employees. This scheme covers about 4.4 million beneficiaries including all categories of current and retired Central Government employees, members of parliament, Supreme Court and High court judges and certain other categories of beneficiaries. The said scheme is financed mainly by the central government and nominal contribution by the Government employees for the comprehensive healthcare including both outpatient care and hospitalization in Government as well as private hospital.

Non-life insurers started **formal health insurance** before nationalization in a very small way. Even after nationalization PSU insurers continued to issue tailor-made group health insurance policies to large corporate clients purely on accommodation basis and as such claim ratio was very unsatisfactory. Then there was no scheme for individuals and families. In 1981, a limited cover was devised for individuals and families. This was structured only in 1986 after 15 years from nationalization, when PSU non-life insurers standardized the terms and conditions of health insurance and launched **Standard Mediclaim Policy** both for individuals and groups under a market agreement. The said standard product for Maximum Sum-insured of Rs 83,000 has been revised after 10 years in 1996 to increase the SI up to Rs 100,000. Subsequently the sum-insured was increased to Rs 3 lakh and presently modified to Rs 5 lakh (maximum SI) in the light of experience of the insurers and suggestions from insuring public and various interested groups.

A mini version of health scheme called *'Jana Arogya Bima'* was also introduced in 1996 for the weaker sections of the society. Since then mediclaim insurance has started growing both on individual and group schemes, though its penetration is far from the world standard for the reasons being critically examined here to bring required reforms. The said mediclaim insurance is a voluntary health insurance covering hospitalization and domiciliary hospitalization benefits (specified days) with certain exclusions like pre-existing diseases, pregnancy and childbirth, HIV/AIDS etc. (maternity is covered in group policy). It is an indemnity either on reimbursement basis or Cash-less settlement through TPA (recent episode). There has been also a major revision in regard to maximum age, which stands up to 80 years (subject to necessary medical examinations) in some versions though underwriting practices and rating vary widely at higher age groups.

Reasons for Poor Penetration of Health Insurance:

1. Socio-economic factors such as mal-distribution of income and wealth.

2. 80 per cent population consider healthcare as tertiary needs due to lack of affordability

3. Consequent Low private spending on healthcare and insurance

4. Protection of insurance sector till end of 20th century.

5. No insurance regulation up to the end of 20th century

6. Lack of public awareness of various health insurance policies.

7. Lack of transparency in underwriting and claims settlement practices

8. Consequent lack of public faith in insurance services

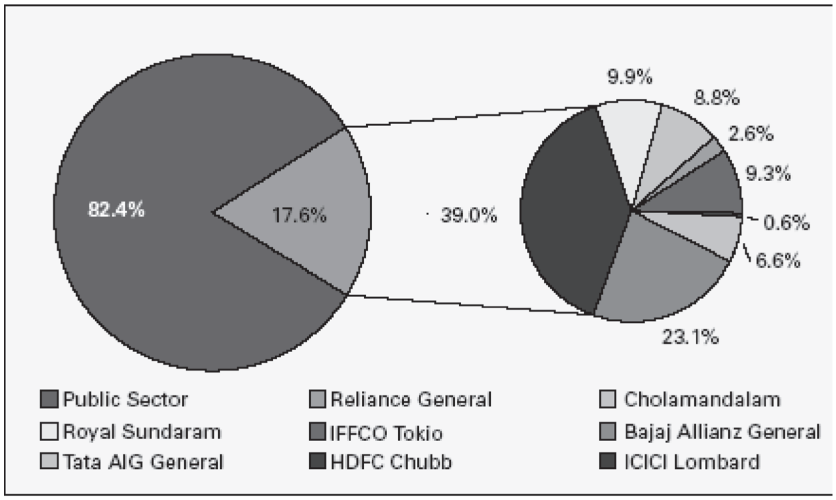
9. Lack of customized products based on needs of various segments of customers.

10. Lack of appropriate databank of medical treatment costs – segment/community-wise and disease-wise to ensure risk-based rating

Current Perspective of Health insurance In India

Though the need for rationalization of Health insurance has been immensely felt by all since long, the growth potential rising with growing population has always remained vastly untapped mainly due to protection of insurance service and want of regulation for cost-based pricing and need-based product-development. Most of the insurers have been following the age-old traditional practice of underwriting and rating with arbitrary decision on discounts without any statistical analysis and loss forecasting for rating the health risks. The insurers did not even hesitate to allow 50 per cent discount (over and above 10 per cent agency commission) to some unauthorized TPA collecting premium from public). As of 31 March, 2007 approximately 35 million persons are covered by various Health Insurance covers. Out of 35 million, 25 million are covered by ESI and roughly 11 million by various insurance companies. The regulations only permit general insurance companies to offer stand-alone health insurance products, while life insurers are allowed to offer riders such as critical illness cover attached to basic life policies – although subject to certain restrictions. Health cover premiums, however, account for less than 1 per cent for life insurers and 10 per cent for general insurers of total premiums. The insuresr have also launched a few new products or riders like Jan Arogya, Bhavishya Arogya, Universal Health Insurance, Senior Citizen Unit Plan, LIC Asha Deep, Asha and Nav Prabhat, etc.

Figure-4. Market share of public and private sector companies in the health segment (2004/2005 financial year)



Source: IRDA Journal

The aggregate health premiums of four public sector companies accounted for 82 per cent and 18 per cent by all private sector non-life insurers in 2004-05. The state owned companies have had earlier little focus on growth of this line of business on a professional and profitable basis. They have mainly attempted to market health insurance cover on a discounted basis to employer groups as an accommodation, primarily to gain access to the profitable lines of the employers' insurance portfolio of property insurance, which are subject to regulated tariffs resulting into significant profit margins. But for higher penetration of this essential insurance product to tap the huge potential rising with growing populations it needs a lot of reforms in underwriting and marketing functions discussed hereinafter. Both PSU and Private players need to develop new products according to the needs and capacity of customers to tap the fastest growing market for health insurance. Health Insurance sector grows 30 per cent in 2008-09 with premium collection of Rs 6625 crores.

Current Scenario of Indian Health Insurance

Health Insurance is now the second largest segment after motor insurance in non-life insurance sector. This segment contributes 20.31 per cent of the total premium. In 2008-09, Health Insurance premium came to Rs 6625.46 crores while the total premium earned by non-life insurance industry was Rs 32629.45 crores. This was in addition to Rs 6625 crores health insurance premium earned by general insurance sector, wile hlife insurance sector earned health insurance premium for Rs 339.20 crores in 2008-09. It is now emerging as a very vital line of business for non-life insurance sector. Number of policies has been increased to 3790838 in 2007-08 from 2265451 in 2003-04 and number of members has been increased to 24121625 in 2007-08 from 8361629 in 2003-04. Number of claims have been increased to 1436998 in 2007-08 from 360088 in 2003-04. Incurred claim ratio has been increased to 105 per cent in 2007-08 from 80 per cent in 2006-07. It has further increased to 117 per cent in 2008-09. Group Health Insurance ICR is different for different companies, ranging from 117 per cent to 183 per cent.

Economics of Health Insurance and its Better Penetration

This segment has had tremendous prospect in India. Health Expenditure is a major outgo from the Government revenue or individual's income. Individual's income or financial capacity may not be sufficient in the event of even minor hospitalizations. Thus health insurance is the most ideal mechanism for transfer of individual health risks to the large community. It protects an individual's earnings by transferring the health risks. Health insurance always provides a better access to healthcare. It is used as the most effective tool for obtaining cost-effective healthcare in almost all developed and developing economics. Then, why India will be exception to that unique mechanism for transfer of health risks with the poorest of the poor penetration of health insurance despite its fastest growing potentials. It is true, presently the health portfolio is showing very high claim ratio about 120 per cent rendering price high and the portfolio non-viable. The possible reasons for such high ICR of health insurance are: i) Premium not commensurate to the risks costs ii) Mis-use of health care services and supply by other stakeholders; iii) Increasing Medical and Hospitalization expenses due to general inflation hike; iv) poor Underwriting; and v) Pricing without consideration of risk cost.

But if underwriters at the initiatives of the regulator adopt the following strategic actions, health insurance will be equally viable and vibrant like other portfolios and help to achieve the objectives of National Health Policy.

1. **To apply the law of large number:** Insurance is basically based on law of large number. Greater the number, lesser will be the average cost. No product can be sold less than average cost (AC). In competitive price, equilibrium is achieved when Price (P) = AR=AC=MR=MC (where AR=Average Revenue, MR=Marginal Revenue and MC =Marginal Cost). In insurance business, AC, MC, MR, AR & P – all will be lower with the gradual increase in number of particular. It is not denying that with continuous escalation of medical costs, incurred claim ratio is increasing. But the needs for health insurance are also increasing very fast. Underwriter can exploit the growing markets with the following cycle of underwriting and rating:

    - Designing Proper Products with mix of Indemnity and Benefit.
    - Using Alternatives as drivers for reduction of loss and moral hazards.
    - Using alternatives to increase the use of insurance by public for healthcare.
    - Increase in number of risks will reduce average cost and finally premium.
    - Reduction in price will make it affordable to larger number of population.

2. **To Emphasize on Marketing Strategy:** Another major cause for poor penetration of health insurance is poor marketing strategy of PSU insurers. Health insurance has been mainly marketed as group policy on accommodation basis to the corporate clients and then to city-dweller. The major population in our country lives in villages where city-based

agents did not go much for marketing. Statistical analysis shows that claim experience in rural areas is far better than that in city-area. So, all insurers must give special emphasis on rural marketing for better penetration and reducing average claim costs. There must be a strategic marketing of health insurance, which need the following measures to be adopted:

- Designing product according to needs of the target group.
- Devising Basic cover with minimum price as per the affordability of the target group. Universal Health Insurance is an example here.
- Emphasizing on publicity and advertisement for product like UHI.
- Effective training for marketing force on policy coverage, exclusions, terms and conditions and avoiding dummy agency or agency attrition.
- Structuring agency commission- flat commission and profit commission to bring more professionalism in marketing management.

3. **To Apply Cost-based Pricing:** Health Insurance can be made viable only by having properly designed products, cost-based pricing and sound-underwriting as we know all. Underwriting must be independent of marketing to avoid miss selling adopted for commission-earning. Risk price must follow the risk-costs being the aggregate of expected claim costs, acquisition costs, management costs, cost of capital. The said aggregate of expected costs must be adjusted by the expected investment income of the fund collected for this portfolio. To follow this approach uniformly, the corporate underwriter must fix a base price or guide rate for the line underwriters who will adjust the same with appropriate loading or discount based on risk-management technology. In health insurance following Rating Methods are followed in general:

- **Risk Rating** based on objective probability and severity of individual risk

- **Community/ Class Rating** based on a system of determining uniform for all individuals in a community or group.

- **Income Rating** based on the system of determining premium on the basis of income or wages of the individuals. (ESI scheme)

- **Experience Rating** based on the insured's past loss. (Group policy)

For this purpose collection and build up of database is essential. Insurance companies are neither have proper database nor they are sharing their data, with each other whatever they have. Therefore product pricing in India is still in the nature of management decision. IRDA has initiated efforts to complete data from various companies in specified format. TAC has already started has collected data on health insurance. Once this process is complete and database becomes accessible to all insurers, it will be easier to make actuarial calculation and adopt risk-based pricing.

4. **To Apply Risk Management Technology:** Health insurance underwriting must be risks-based as otherwise it will creep in cross-subsidy and become non-viable as usual. Underwriting practice must reflect the underlying risks-posed by each individual and allow premium accurately follow the risks costs. Unlike before underwriting or acceptance should not be on any accommodation ground for any other insurance products generating underwriting surplus. For no product in the de-tariff regime will generate more than minimum required surplus. For this purpose appropriate analysis of health risks by following methods is a must:

   - Avoid Adverse Selection or moral hazards.

   - Devise an effective risk management programme to avoid moral hazards, adverse selection, frauds and cost escalation.

5. **To Cover Senior Citizens with Proper Underwriting**: For effective underwriting of health insurance for senior citizens following measures are of special importance:

   - IRDA's mandate for insurers carrying on health insurance to cover all senior citizens irrespective of age, health conditions after proper medical test at the entry level except for pre-exiting disease, terminal or incurable diseases found in test.

   - Affordability is the major problem for senior citizen group. It requires a lot of price adjustments in consideration of individual health status, sex, occupation, life-style etc., while rating particular risks.

6. **To Apply Risk Based Capital Norms:** Every product must stand on its own cost for its perpetual succession and viability. Every health insurance product should be managed in the strict principle of financial management-sources of funds and application of funds for the product or policy. With this process insurers can easily maintain solvency as well as liquidity for business growth. IRDA may come out for RSM and ASM separately for this department to ensure RBC norms compliance.

7. **To Devise Separate Regulation or Government Notification:** As per recent estimates, the insurable population for health in India is about 35 crores out of which hardly 10 per cent are actually covered by various schemes/policies presently. According to the WHO, India ranks 118 out of 191 countries, below even Pakistan and Bangladesh in respect of healthcare. In view of above scenario and National Health policy "health for all" the regulatory should mandate the insurance companies to carry on health insurance business to the specified percentage of their total business so that the majority of population do have access to healthcare as per national health policy.

8. **To Intensify PR and Publicity to Popularize Health Insurance:** There must be proper training and adequate number of seminar on Health Insurance so that all personnel both administrative and marketing are equipped with requisite skill, knowledge and ability to underwrite and manage health insurance with growth and profitability.

9. **To Standardize Policy Wordings — Coverage, Exclusions, Terms, Conditions etc:** In order to maintain the homogeneity of products and bring transparency in marketing in competitive market the IRDA may stress upon standardization and uniformity of terms, conditions and definitions of all health insurance products being marketed by insurers to bring the confidence of the customers and protect them from being misled by service providers. This will ensure healthy growth in the market.

10. **To Address the Issue of Regulations for Service Providers:** Health insurance development depends largely on professional approach, attitude and activates of all service providers including TPAs, Brokers, Agents etc apart from professionalism in underwriters. Health sector is not properly regulated in India despite the fact Indian health insurance market has had great potentials. There is no strict control over service provider. The service providers are free to charge any amount to different category of patients causing the tremendous increase in incurred Claim ratio for this segment for more than 100 per cent. All hospitals need to be graded and services are to be standardized to provide quality medical services at the affordable cost to help the insurance sector to tap the high potentials of growth of this segment. Insurance market has been detariffed, but policy wordings have remained the same causing the barrier for the efficient insurer to increase efficiency and productivity in servicing this growing segment.

Mediclaim Policy

Types of Policies

There are various types of health or mediclaim insurance products and plans issued by various non-life insurance companies. Life insurance companies have also started issuing health insurance products of late. Health insurance products used by the non-life insurance companies are generally come under following categories:

- Standard Mediclaim Policy (individual)
- Standard Mediclaim Policy (group)
- Health Plus Medical Expenses Policy
- Group Health Plus Medical Expenses Policy
- Jan Arogya Bima Policy
- Overseas Mediclaim Policy
- Universal Health Policy

General Practices

The number and nature of medical policy are increasing rapidly today to satisfy the needs of the different segment of customers with different products and plans and to exploit the market potentials. Recent developments in the market are:

- Free Look Period with plan for three years term policy or less than three-year-term;
- Renewable in general except on grounds of fraud, Moral hazards and misrepresentation;
- Rejection generally Not allowed on arbitrary ground;
- 15 days time to renew, but No cover during this period;

- Renewal Notice to specify quantum of premium with note explaining the reason for increase in premium;

- Denial of insurance to senior citizens only with written and recorded reasons;

- Insurers to reimburse at least 50 per cent of cost of pre-insurance medical examinations in Empanel Govt. Medical institutions and provide the copies of medical examinations, if requested;

- Health Insurance Policies are required to include;

  - o Entry Age till 65years

  - o Annexure showing coverage and key terms in simple language

  - o Proper disclosure and policy documents all product specifications and exclusions

Standard Mediclaim Policy

As the number of mediclaim policies is many, it is not possible to discuss all mediclaim policies in this manual. However the salient features of standard mediclaim policy has been discussed below.

Who can Take This Policy?

This insurance is available to persons between the age of 18 to 60 years. Children between the ages of 3 months to 18 years can be covered provided parents are covered simultaneously. The persons beyond 60 years can continue their insurance provided they are insured under Mediclaim policy with the Company without any break.

What does This Policy Cover?

- The policy covers hospitalization expenses for the treatment of illness/injury provided hospitalization is more than 24 hours.

Pre-hospitalization expenses for 30 days and post hospitalization expenses for 60 days are also payable.

- Day-care treatment: The Medical expense towards specific technologically advanced day-care treatments / surgeries where 24 hour hospitalization is not required.

- Ambulance Charges for shifting the insured from residence to hospital are covered up to the limits specified in the policy.

- Ayurvedic /Homeopathic and Unani system of medicine are covered to the extent of 25 per cent of Sum Insured provided the treatment is taken in the Government Hospital.

- Pre-existing diseases are covered only after 4 continuous and claim free renewals with our Company.

- Pre-existing conditions like Hypertension, Diabetes, and their complications are covered after two years of continuous insurance on payment of additional premium.

General Exclusions

- Diseases contracted within 30 days of insurance

- Dental treatment except arising out of accident

- Debility and General Run Down Conditions

- Sexually transmitted diseases and HIV/AIDS

- Circumcision, Cosmetic surgery, Plastic surgery unless required to treat injury or illness

- Vaccination and Inoculation

- Pregnancy and child birth

- War, Act of foreign enemy, ionizing, radiation and nuclear weapon.

- Treatment outside India
- Naturopathy
- Domiciliary Treatment
- Experimental or unproven treatment
- All external equipments such as contact lenses, cochlear implants etc

Premium

- Premium is based on age of the proposer and geographical area of treatment. Individual company has its own guide-rates

Special Features of Mediclaim Policy

- Discount in premium for family cover
- Loyalty Discount
- Good Health Discount
- Cumulative Bonus
- Cost of Health Check up
- Income Tax Benefit under Section 80D of IT Act

How to Avail Claim?

Claims are administered through Third Party Administrators (TPA) whose contact particulars appear on the policy document. Insured can opt for cashless or reimbursement facility for their claims. The proposer has the option to avail TPA services, which is cashless or direct service by Policy issuing Office, which is on reimbursement basis. Accounting and Administrative control of TPA Health Services have been discussed hereinafter separately, which the auditor may specially consider for the planning and performance of independent audit of operational units of general insurance companies.

Accounting and Internal Control of Claims Settled by TPA

The IRDA had formed a panel with members from all segments of stakeholders to look into the scope of the functions, best practices and turnaround time and financial aspects of TPA for health services in view of a lot of complaints against TPA. Some of the major complaints against TPA are as under:

1. Many TPAs are not prompt in responding to calls made by customers.

2. Time taken by TPAs in settling claim is more than expected or standard.

3. Delay in delivery of claims cheques despite regular release of float fund by insurers.

4. Float funds released by insurers are sometimes higher that total claims settled by TPA

5. Hospital bills settled by TPA are overcharging.

6. Pre-authorization and claim settlement process are not simple, standardized and uniform.

7. No common software platform to cut down the delay in processing claims.

8. Claim intimations and analysis of claims are not sent by TPA to insurers in time.

9. Stale or un-presented cheques are not properly accounted for before replenishment.

10. Claims are settled on arbitrary basis without strict adherence to policy terms and limits

All such anomalies and deficiency of services on the part of TPA require proper accounting and administrative control by insurer for TPA transactions. Following is a few guidelines for such control, which may be one of the important considerations for statutory branch auditors in this regard for their expression of opinion on the true and fair view of the state of affairs or profit or loss of the insurance company.

TPA Float Reconciliation and Internal Control on TPA Claim Settlement

(I) Particulars/Documents to be Referred

Service Level Agreements (SLA); SLA entered with all TPA Services by the insurers in accordance with the guidelines provided by IRDA. The SLA will provide for terms for Float Funds to be released to the TPA Service provider to serve the purpose of an Imprest Account with further Replenishment from time to time depending on the frequency/amount of payment of claims to the Insureds:

- Float Payment Register with All TPAs
- Cash Book of all TPAs ,
- Cheque Payment Register of all TPAs ,
- Bank Statements of all TPAs
- Details of all Replenishments with Identifications i.e. Lot Number etc

(II) Accounting of TPA Claims

TPA claims are accounted for and controlled by insurers at three stages:-i) On receipt of list of Claims intimated to TPA; ii) on settlement of claims by TPA; and iii) Release of Float Accounts for replenishment of funds used by TPA for settlement of a claim.

(III) Reconciliation of Float Accounts

For exercise of proper accounting and administrative control there must be reconciliation between the float payments by insurers to TPA and amount paid by TPA to customers with reference to SLA as mentioned above. Prior to such reconciliation of Float Accounts by Accounts Sept, Technical Department shall ensure that all floats amounts have been have approved by them in compliance with the terms of SLA and after verification of every individual claims payments with policy terms, conditions and limits.

(IV) Float Account Reconciliation Process

1. To verify details of all Replenishments with Identifications i.e. Lot Number etc.

2. To verify that all Cheques have been issued by TPA with consecutive serial Number/sequence of number and date. To ascertain that all cheques issued for settlement of claims have been immediately delivered and debited in the Float Bank Account within reasonable time.

3. To verify the statement of claims paid (payment register) followed by our replenishments of the imprest/float ensuring that; a) Cheques were prepared serially and issued immediately and Total amount of Cheques prepared for a particular period were within the Float/ Imprest limit.

4. To verify that all TPA Service providers have utilized the Float Funds and then made requisitions for replenishments only after physical delivery of claim cheques that fall in line with SLA and subject imprest limits.

5. To further verify that there was no case of delayed preparation of cheques coupled with further delay in delivery of the same resulting into huge accumulation of fund arising from unpresented cheques.

6. To verify that in no case, replenishments have been found to be more than the amounts of cheques issued and entered in payment Register over a particular period.

7. To verify that Total Amount Cleared from Float Account is tallied with the amount of cheques issued out of Float Bank Account.

8. To verify validity of insurance, Adequacy of sum-assured, Admissibility of claims as per policy terms and conditions for all claims settled by TPA.

9. To verify that no duplicate payment has been made by TPA.

10. To verify adjustment of Stale cheques and proper accounting thereof.

(V) Analysis of Claims Handling

As a process of exercising proper administrative and accounting control, there must be proper analysis of claims for the Year ending in the following manner as required by IRDA Regulation on TPA:

1. Total number of claims received during the year

2. No. of claims settled;

   - within 1 month from date of receipt of claim
   - 1 to 3 months …………….
   - 3 to 6 months …………….
   - more than 6 months ………………

3. No. of claims outstanding at the end of the year

   - Outstanding up to 1 month
   - ... DO ... 1 to 3 months

- ... DO ... 3 to 6 months
- ... DO ... more than 6 months

4. Information on individual claims outstanding for more than 6 months.

Health Insurance Market in India — Present, Potentials and Penetration

Present Scenario

Health Insurance market has increased substantially during last two years as evident from the Table-26 that shows general health insurance premium figures (Rs in crores):

Table-26: General Health Insurance Premium

Particulars/Parameters	2008-09	2007-08	2006-07
Health Insurance Premium Collected	6625.46	5124..95	3208.73
Total General Insurance Premium	32629.45	29808.90	26517.20
% of Health Ins. Premium to Total Premium	20.31%	17.19%	12.1%
Accretion of Health Insurance	30%	60%	60%

Health insurance premium of Rs 6625.46 crores collected by general insurance companies and Rs 330.20 crores collected by life insurance companies in 2008-09 shown compound average growth of 37 per cent from 2002-03 when mediclaim insurance premium collection was only for Rs 761 crores. Apart from health insurance products or policies being issued by Public sector and private sector insurance companies, there are large number of health insurance schemes and projects run by the Central Governments and State Governments. Government Health insurance Schemes or plans like ESI, CGHS, various, Universal Health Insurance Schemes launched by the Central Government, *Rastriya Swatha Bima* plans contributed by the Central Government, State Government and beneficiaries and managed by mostly insurance companies deserve special mention in this regard.

Potentials and Penetration

Health Insurance has had great potentials in India though the present market penetration is very poor. Out of 1.2 billion population roughly 3.5 crore people are covered under variously health insurance schemes of Governments and mediclaim insurance policies or plans by insurance companies. If the present trend of growth over 39 per cent continues mediclaim insurance premium collection may cross Rs 15,000 crores and Rs 25,000 crores in 2015-16.

Rashtriya Swasthaya Bima Yojna

Rashtriya Swasthaya Bima Yojna - A New Era of Health' for the Poor

The Central Government has launched a new health insurance scheme for the Below Poverty Line (BPL) families in the unorganized sector Scheme called *Rashtriya Swasthaya Bima Yojna* (RSBY) which was announced by the Prime Minister Manmohan Singh in 2007 on the Independence Day, i.e. August 15, 2007. The objective of RSBY is to provide the insurance cover to BPL households from major health shocks that involve hospitalization. It is under implementation by various states all over the country under a 5-year plan for rolling out the RSBY, which allows each participating state to cover 20 per cent of their respective districts each year. The National Sample Survey Organization (NSSO) 2004 had reported that 65 per cent of India's poor get into debt and 1 per cent fall under BPL because of sickness. Health insurance is the answer to the health woes of the poor. The RSBY scheme implemented by the Government of India with effect from 1 April, 2008 heralded the '**dawn of a new era of health' for the poor** and is the 'apt and best' gift for the poor amidst all the gloom and doom in the marketplace. By 1 April, 2008, almost every large State Government has expressed its intention of joining the scheme and 15 states like Delhi, Rajasthan, Gujarat, Haryana, Bihar, Uttrakhand, Kerala, Punjab, Chhatisgarh, Karnataka, Maharashtra, Tamil Nadu, Uttar Pradesh, West Bengal and Jharkhand have already taken appropriate measures in this regard, while many states like Delhi, Haryana, AP, UP, and Rajasthan have begun enrollment. As of now, no time frame has been fixed but it would be done in due course.

Financing of the Scheme

The majority of the financing, about 75 per cent, is provided by the Government of India while the remainder is paid by the State Government. The State Governments engage in a competitive bidding process and select a public or private insurance company licensed to provide health insurance by IRDA. The technical bids submitted must include a number of elements as per the Government of India requirements. The insurer must agree to cover the benefit package prescribed by the Government of India through a cashless facility that in turn requires the use of smart cards which must be issued to all members. This requires that a sub-contract be arranged with a qualified smart card provider. The insurer must also agree to engage intermediaries with local presence such as NGOs etc., in order to provide grassroots outreach and assist members in utilizing the services after enrollment. The insurer must also provide a list of empanelled hospitals that will participate in the cashless arrangement. These hospitals must meet certain basic minimum requirements (e.g., size and registration) and must agree to set up a special RSBY desk with smart card reader and trained staff. The list should include public and private hospitals. The financial bid is essentially an annual premium per enrolled household. The insurer is compensated on the basis of the number of Smart Cards issued, i.e. households covered. Each contract is specified on the basis of an individual district in a state and the insurer agrees to set up an office in each district where it operates. While more than one insurer can operate in a particular state, only one insurer can operate in a single district at any given point in time. The hardware and software specifications laid down by the Government of India imply inter-operability across districts and states.

Major Features of RSYB

- The RSYB is termed as a ‘visionary national health insurance scheme for protection of BPL households from major health shocks requiring hospitalization. The RSBY is the brainchild of an IAS officer named Anil Swarup.

- It is designed to provide financial protection from healthcare expenses to the poor segment of the society and improve the public health care services with competition, incentives and improved technology.

- It provides a cover for Rs 30,000 in patient’ Health Insurance Package (Hospitalization) benefits per family per annum on a family floater basis at a premium of Rs 600, that will be borne by both the Central (75 per cent) and State Governments (25 per cent).

- The package includes about 727 pre-defined surgical package including Maternity & Networking care.

- All Pre-existing Diseases covered from day one.

- Pre/post hospitalization expenses and limited transportation expenses are covered.

- The State governments through insurance companies are implementing the scheme.

- A ‘poor’ patient has a wide and varied choice, from among 1000 Government and private hospitals. The poor also have a choice to exit from a bad hospital, for something that only the rich can afford to do today.

- The State governments can choose from 18 public or private insurance companies.

- There is now money in catering to the poor, which naturally boosts the competition between insurers, and hospitals.

- Hospitals will not shun the poor because they don't want to lose the potential revenue of Rs 30,000. Hospitals would also ultimately improve the quality of healthcare and new hospitals will come up.

- Since the Insurers earn premiums they also have the added advantage of receiving incentives to recruit the poor.

- The magical smart cards carried by the 'insured' have a cutting edge technology and are designed to prevent fraud because of 11 unique types of embedded software. It has the photo, fingerprints of the family, and an official's 'key' who is accountable.

- Cashless and paperless transactions for the 725 pre-agreed medical procedures can be done without any hassles with the card.

- The smart card facilitates medical expenses to the tune of Rs 30,000 and it tracks day-to-day expenses in the hospital where the money is deducted automatically after each procedure.

- There is no need for pre-approval or reimbursement. The smart card empowers a poor Bengali to use a hospital in Mumbai as the poor migrate wherever they have opportunities to earn.

- Smart cards can dramatically slash corruption in all our social programmes. It exposes corruption quickly as it can also carry data on payments for rations (PDS) or earnings from employment schemes like National Rural Employment Guarantee Scheme (NREGS).

- The smart card is the absolute way for the real poor to receive the money directly without interference of the rich or the middle class people.

- An electronic list of eligible BPL households is provided to the insurer according to a prescribed format.

- The smart card will be issued by the insurance company through the instrumentality of the smart card service providers. However, the ownership, of the card will remain with the Central government. The smart card would be delivered on the spot after printing on the location itself. The cost, if any, would be borne by the insurance company as a part of the overall bill.

- The smart card cannot be issued in the absence of head of the family as his photograph has to appear on the face of the card. However, it can be issued in case the head of the family is present but the members of the family are missing. Their details can be added subsequently at the district kiosk to be maintained by the insurance companies.

- Coverage under the scheme is provided for BPL families (up to a unit of five). A family would comprise the household head, spouse and up to three dependents.

- The dependents would include such children and/or parents of the head of the family as are listed as part of the family in the BPL database. If the family size is more than five, the head of the family would decide as to who all should be left out. However, in case the name of the spouse is listed as part of the family in the database, the second member would necessarily be the spouse and the selection would be for the remaining three slots.

- The smart card entitles its bearer to a list of pre-specified in-patient services in the second month following enrollment. Provisions exist for pro-rata premium payments to the insurance company in the event of partial year enrolment subject to a minimum of six months.

- The transaction process begins when the member visits the participating hospital and his or her card is swiped.

- The registration fee of Rs 30 would be collected from the beneficiary by the insurance company and adjusted against the payment of premium to be made to the insurance company by the State Government.

Current Status of RSBY Implementation

- It has been implemented by 22 states across the country with the participation of about eleven insurance companies. In some states such insurance facility has been also extended to non-BPL families.

- Approximately 8.9 smart cards have been issued covering nearly 35 milion people.

14

ENGINEERING INSURANCE

Fundamentals of Engineering Insurance

Rapid industrialization and modernization of life have led to increasing use of machines and erection of more plants and projects all over the world. All such machines and projects are exposed to various types of risks such as accidental breakdown or accidental damage to the project at various stages from erection and commissioning to running of plant, that require repairs or replacements of part or whole of a machinery or a plant. There is also risk of loss of production due to break down of machinery or delay in construction of project due to its accidental damages. For all such purposes the Engineering insurance is of great use to industry everywhere. The origin of Engineering Insurance dates back to the early part of Industrial Revolution and in 1858 the Steam Boiler Assurance Company combined inspection service with indemnity for accidental loss by external cause. In India the origin of engineering Insurance is traced back to 1950s when New India Assurance Company Ltd set up an Engineering Department followed by The Oriental Insurance to transact this class of insurance.

Scope of Engineering Insurance

Engineering Insurance is basically of two types: Operational Engineering Insurance and Project Engineering Insurance. Again for these two Engineering Insurances following types of policy are issued.

Operational Engineering Insurance

- Machinery Insurance also known as Machinery Breakdown Insurance (MB)
- Boiler and Pressure Plant (BPP) Insurance

- Machinery Loss of Profit (MLOP) Insurance
- Contractors' Plant and Machinery Insurance
- Civil Engineering completed Risks (CECR)
- Electronic Equipment Insurance (EEI)
- Deterioration of Stocks (DOS) Insurance

Operational Engineering Insurance Policies are annual and renewable at expiry. It is very important to note that IAR (Industrial All Risks) Policies covering MB and MLOP along with Fire, Burglary and Loss of profits are underwritten by Fire Department.

Project Engineering Insurance

- Contractors' All Risks Insurance (CAR)
- Erection All Risks Insurance (EAR) also known as Storage-Cum Erection (SCE)
- Marine-Cum-Erection (MCE) Insurance
- Contract Works Insurance
- Advance Loss of Profit (ALOP)
- Delay in Start-Up Insurance (DSU)

Risk covered loss, damage and/or liability caused by or arising from or in consequence, directly or indirectly of fire including extinguishment of a fire or clearance of debris and dismantling necessitated thereby smoke, soot, aggressive substance, lightning, explosion of any kind (other than bursting or disruption of turbines, compressors, cylinders of steam engines, hydraulic cylinders or fly wheels of other apparatus subject to centrifugal force, internal pressure) theft, collapse of buildings, subsidence, landslide, rockslide, water which escapes from water containing apparatus, flood, inundation, storm, tempest, earthquake, volcanic eruption nor other Acts of God, impact of land borne or waterborne or airborne craft or other aerial devices and/or articles dropped there from.

Risk Inspection and Underwriting

Engineering Insurance is highly specialized and requires technical knowledge and expertise in respect of risk identification, risk analysis and risk evaluation for prudent underwriting, i.e. selection of risks, classification of risks and rating of risks and accepting with appropriate terms and conditions. For this purpose, the services of engineers in various disciplines are utilized. For proper underwriting a pre-inspection is conducted by an experience engineer who is to submit risk inspection report covering the following aspects:

- Detail Risk Inspection Report
- Housekeeping arrangements
- Fire protection and prevention measures and features
- Potential for flooding at site
- Potential changes in working condition
- Change in working condition
- Preventive maintenance,
- Corrective Maintenance
- Productive Maintenance

Machinery Breakdown Insurance

Scope and Cover

Machinery Insurance policy is also known Machinery Break down (MB) policy. MB Policy covers all stationary, mechanical and electrical equipments used in industries against any unforeseen loss, sudden loss or damage by any clause internal or external not specifically excluded in the policy whether during work, rest, dismantling or shifting within the premises. For example, explosion by bursting or disruption of turbines, compressors, cylinders of steam, engines, hydraulic cylinders, or fly wheels, or other apparatus from centrifugal force or internal pressure will be covered by the policy. Any loss or damage by fire within the electrical appliances and installation insured by this policy arising from or occasioned by overrunning, excessive, excessive pressure, short circuiting, arcing, self-heating or leakage of electricity from any cause is covered; provided that this extension shall apply only to the specified electrical machine, apparatus, fixture, fitting, electrical installation.

General Exclusions

MB policy does not cover any loss or damage from any of the causes mentioned below:

- Fire, Smoke, lightning
- Explosions in Chemical Recovery Boilers.
- War, Civil War and war like operations
- Rebellion, Revolution, Insurrection, Mutiny, Riot, Strike, Lock-out & MD
- Requisition or Destruction or Damage by the order of any Government
- Atomic, ionic and nuclear perils, radioactive contamination
- Overload experiments
- Normal wears & tears
- Willful act/neglect or gross negligence
- Flood, inundation, storm, tempest, earthquake or other AOG perils

- Previous defect known to insured
- Consequential loss of any kind
- Foreseeable events such as consequences of normal operation and continual mechanical, thermal, chemical or electrical effect, wear & tear, corrosion, erosion, undue deposit, etc
- Breakdown caused by testing or experiments
- Damage for which manufacturer/ others are liable by law or under contractual obligation

Special Exclusions

- Excess or deductible specified in the schedule is to be first borne by the insured
- Loss or damage of belts, ropes, chains, rubber tyres, dies, moulds, blades, items made of glass, porcelain, ceramics, operating media such as lubricating oil, fuel, catalyst etc unless the machines are damaged are indemnifiable under the terms of policy
- Loss or damage for which manufacturer or supplier or retailer of the property is responsible by law of contract

Sum Insured

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. The policy requires that in case of any loss or damage to any insured machinery or equipment, the company shall pay all 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 repair shop, custom duty, if any, and to the extent, such expenses have been included in the sum insured; 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.

Extensions or Add-On Cover

The standard MB policy shall not indemnify the following loss or damages due to mechanical or electrical break down of any machinery. But these perils can be covered as Add-on Covers with proper endorsement:

- Express freight, holiday and overtime rates of wages
- Additional rate for airfreight only
- Surrounding property damage
- Third party liability
- Customs duty

Important Considerations for Underwriting

- Sum insured to be taken is the current replacement value all machinery.
- Replacement value includes freight, customs and erection cost also if included.
- Sum-insured can be increased or decreased during the policy period.
- Short period policy can be issued.
- Discount for standby and seasonal equipments may be granted.
- Strong recommendation to accept risk after satisfactory inspection.

- Machines are to be insured after successful commissioning only. Not at the stage of erection, testing & commissioning in any case.

- Before rating, it is necessary to collect full nameplate details of the machine – Year, Make, Span of life, years of use, market value, experience of loss, maintenance, nature of use, availability of spare parts and other details as mentioned in the following Para. All such details must be enquired and mentioned in the detailed inspection report and shall be the basis of acceptance of risks and rating thereof.

Risk Inspection

Risk inspection, risk analysis and risk evaluations are the preconditions to engineering insurance like any other insurance. But risk inspection in engineering insurance is a specialized function requiring proper knowledge, skill and expertise in mechanical and technical aspects of machines concerned apart from the financial aspects including value, cost, repair cost or expenses, past loss experience etc. However following aspects deserve a special mention in respect of risk inspection in engineering insurance:

- Physical condition of machine & equipment

- Loss -related problems with other machines

- Unconventional features.

- Plant configurations.

- Loss history

- Maintenance

- Diagnostic checks

Diagnostic and Technical Checks

- Infrared imaging for determining local hot spot in transformer & furnace

- Oil spectrograph for analyzing the presence of metal particle in oil
- X-ray inspection of weld
- Ultrasonic inspection for detecting flows and cracks in shaft and machine casing.
- Vibration monitoring

Premium Rating

Previously MB rates were under tariff which has been withdrawn from 1.1.2007. As per tariff the rates vary from R 0.20 per cent to Rs 2 per cent according the nature and type of machinery or accessories. But these rates have been drastically reduced by the individual insurers according to their respective loss ratio. Insurers have reduced rates by 70-80 per cent of the erstwhile Tariff. Insurers generally adopt merit rating for they prepare a detailed Merit Rating Sheet. A specimen of Merit Rating sheet is given below:

Specimen of Merit Rating Sheet

Risk inspection, Analysis and Merit Rating Sheet

1. Name of the Proposer:
2. Location of the premises:
3. Date of Inspection:
4. Name of Person Inspected the Risk:
5. Proposed Period of Insurance:
6. Voluntary Higher Excess, if any:
7. List of Additional Covers opted:
8. Analysis of Physical Hazards and points earned on good features (see Annex-A)

9. Incurred claim figures for last 3 years:
(Example in Annex B; Claim Experience, Excess Recommended & Points)

10. Calculation of Rate to be charged; (see Annex-C)

Annex A: Physical Features and Points Earned

S. No.	Features of the Risk	Yes/ No	Points Earned
1	**Maintenance Procedures**		
a)	Whether all types of maintenance (predictive, preventive, etc.) procedures are followed as per the manufacturers' instructions		10
b)	Whether all types of maintenance (predictive, preventive, etc.) procedures as per the manufacturers' instructions are partly followed		5
c)	Maintenance procedures not followed satisfactorily		0
2	**AMC**		
a)	Whether the AMC in force		10
b)	Whether the AMC not in force		0
3	**Operation and maintenance staff**		
a)	Whether operated and maintained by trained and experienced staff		10
b)	Operated and maintained by trained or experienced staff but there is bypassing of safety & control systems sometimes with the written permission from the maintenance in-charge		5
c)	Not operated and maintained by trained or experienced staff and / or no requirement of written permission from		

	the maintenance in-charge for bypassing of safety & control systems		0
4	**Spread of Risk**		
a)	All the Insurable machines covered		5
b)	Only selected categories of equipments covered		0
5	**Frequency of Breakdowns**		
a)	No Breakdowns during the previous year.		10
b)	Number of Breakdowns during the previous year is one only		5
c)	Number of Breakdowns during the previous year is more than one		0
6	**Security System**		
a)	24 hrs. Watch & ward facility AND access to the location is restricted		10
b)	Either 24 hrs. Watch & ward facility OR access to the location is restricted		5
c)	Neither 24 hrs. Watch & ward facility NOR access to the location is restricted		0
7	**No. of shifts**		
a)	Only one shift		10
b)	Two shifts		5
c)	Three shifts		0
8	**Repairs of sub-assemblies/part.**		
a)	The manufacturers' facility or any facility authorized by the manufacturers available locally		10
b)	The manufacturers' facility or any facility authorized by the manufacturers available within India		5

b)	Outside India		0
9	**Type of Machinery /Equipment**		
a)	Indigenous		5
b)	Imported		0
10	**ISO Certification (ISO 9000/9001)**		
a)	Certified		5
b)	Not Certified		0
11	**Age of Plants and Machineries**		
a)	0-5 years		10
b)	5-10 years		5
c)	More than 10 years		0
	Total Earned Points		

Annex-B: Claim Experience and Determination of Excess and Points Earned

	Incurred Claim Ratio of Machineries for Last 3 Years	**Excess**	**Points**
a)	Up to 20%	Normal	
b)	More than 20 % to up to 40%	Normal	
c)	More than 40 % to up to 60%	Normal	
d)	More than 60% to up to 70%	Normal	
e)	More than 70% and up to 100%	150% of normal	
f)	More than 100%	200% of normal	

Annex-C: Effective Points Earned and Rate to be Charged

SN	Total Points Earned	Rate to be Charged
1.	Above 50	21
2.	Above 40	18
3.	Above 30	15
4.	Above 20	5
5	Above 10	3
6	Less than 10	0

Basis of Indemnity – (As per Tariff Condition)

(a) In cases where damage to an insured item can be repaired, the Company will pay expense 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 hereinabove 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 affected 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'.

Electronic Equipment Policy

It is virtually an all risk cover for any unforeseen and sudden physical loss or damage from any cause (other than specially excluded) and in a manner necessitating repair or replacement of electronic equipments. Now-a-days electronic equipments are commonly used in both in business and domestic purposes. Thus electronic equipment policy is very important engineering policy. Indemnity provided in the form of Cash, Replacement and Repairs. Policy is issued with basic warranty of: i) Maintenance agreement; ii) Safety Checks; and iii) Preventive Maintenance.

Types of Electronic Equipments (few examples)

- Analytical instruments such as, chromatograph
- Communication & broadcasting equip: multiplex equipment. Audio-visual System
- Consumer electronics: microwave ovens.
- Control instrument & industrial electronic: timers & gauges.
- Data processing system: scanners, computer, software system, UPS etc
- Defence equipments: radars
- Electronic components: TV rectifiers, chokes
- Electro magnetic components: relay switch.
- Medical equip:- x-ray machine Medical, Biomedical, Micro-Processor Power electronics:-ups and thyristors.

Scope of Cover

The policy is generally divided into following three sections for determining scope of cover, exclusions, special terms and conditions and rating:

1. Equipments (Section I)
2. External data media (optional) (Section II)
3. Increased cost of working (optional) (Section III)

Equipments (Section I)

(i) Scope of Cover

The Insurer agrees with the insured (subject to the exclusions and conditions contained in the policy or endorsed hereon) that if at any time during the period of Insurance stated in the schedule or during any subsequent period for which the insured pays and the company may accept the premium for the renewal of this policy, the items or any part thereof entered in the schedule shall suffer any unforeseen and sudden physical loss or damage from any cause, other than those specifically excluded, in a manner necessitating repair or replacement, the insurer will indemnify the insured in respect of such loss or damage as hereinafter provided by payment in cash, replacement or repair (at their own option) up to an amount not exceeding in any one year of insurance in respect of each of the items specified in the schedule the sum set opposite thereto and not exceeding in all the total sum expressed in the schedule as insured hereby.

(ii) Special Exclusion to Section-I

The insurer shall not, however, be liable for:

(a) The excess stated in the schedule to be borne by the Insured in any occurrence;

(b) Loss or damage caused by any faults or defects existing at the time of commencement of the present insurance within the knowledge of the insured, or his representatives;

(c) Loss or damage as a direct consequence of the continual influence of operation (e.g. wear and tear, cavitations, erosion, corrosion, incrustation);

(d) Any costs incurred in connection with the elimination of functional failures unless such failures were caused by an indemnifiable loss or damage to the insured items;

(e) Any cost incurred in connection with the maintenance of the insured items, such exclusion also applying to parts exchanged in the course of such maintenance operations;

(f) Loss or damage for which the manufacturer or supplier of the insured items is responsible either by law or under contract;

(g) Loss or damage to rented or hired equipment for which the owner is responsible either by law or under a lease and/ or maintenance agreement;

(h) Consequential loss or liability of any kind or description;

(i) Loss of or damage to bulbs, valves, tubes, ribbons, fuses, seals, belts, wires, chains, rubber tyres, exchangeable tools, engraved cylinders, objects made of glass, porcelain or ceramics sieves or fabrics, or any operating media (e,g, lubricating oil, fuel, chemicals); and

(j) Aesthetic defects such as scratches on painted polished or enameled surfaces.

In respect of parts mentioned under i) and j) above the company shall be liable to provide compensation in the event that such parts are affected by an identifiable loss or damage to the insured items.

(iii) Sum Insured

It is a 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, dues and customs duties, if any and erection costs. The sum insured of the equipment insured under this section shall include the value of ‘system software’.

(iv) Rating

Before 1.1.2007 this insurance was under tariff. In the de-tariff regime every company will apply their individual guide rates and arrive at the final rates on the basis of proper risk analysis on Merit Rating Sheet Show below:

Risk Analysis/Risk Inspection and Merit Rating

ELECTRONIC EQUIPMENT INSURANCE POLICY

Name of the proposer:

Location of the premises where equipments kept:
(for more than one location list be attached.)

Date of inspection:

Name of Person Inspected the Risk:

Proposed Period of Insurance:

Voluntary Higher Excess, if any:

List of Additional Covers opted

Physical features Analysis (see Annex-D)

ICR for last 3 years including the expiring policy (see Annex E)

Rating (see Annex F)

Annex-D: Physical Features Analysis

S.N.	Features of the Risk	Yes/ No	Points Earned
1.	**AMC**		
a)	Whether the AMC in force		10
b)	Whether the AMC not in force		0
2.	**Operation and maintenance staff**		
a)	Whether operated and maintained by trained and experienced persons		10
b)	Operated and maintained by trained or experienced persons but there is by-passing of safety & control systems sometimes.		5
c)	Not operated and maintained by trained or experienced persons.		0
3.	**Repair facility**		
a)	In-house repair facility is available		10
b)	No in-house repair facility available but repair can be carried out within India.		5
c)	Repairs cannot be carried out within India.		0
4.	**Power Supply**		
a)	Adequate and Reliable with backup UPS System/Voltage stabiliser		10
b)	Adequate and Reliable without backup UPS System/Voltage stabiliser		5
c)	Frequent Power Tripping with Current/ Voltage Fluctuations		0
5.	**Spread of Risk**		
a)	All the Insurable equipments/categories of equipments covered		10
b)	Only selected equipments/categories of equipments covered		0

6.	**Frequency of Breakdowns**		
a)	No Breakdowns during the previous year.		10
b)	Number of Breakdowns during the previous year is one only		5
c)	Number of Breakdowns during the previous year is more than one		0
7.	**Security System**		
a)	24 hours Watch & ward facility and access to the premises is restricted with access control system		10
b)	Either 24 hours Watch & ward facility OR access to the premises is restricted with access control system		5
c)	Neither 24 hours Watch & ward facility NOR access to the premises is restricted with access control system		0
8.	**Fire Fighting Facility****		
a)	Whether Hand Appliances, Fire Alarm System and Hydrant System are available		10
b)	Whether Hand Appliances and Fire Alarm System are available		5
c)	Whether only Hand Appliances available		0
**Applicable only when Fire & Special Perils are not deleted			
9.	**Protection Against Flood & Inundation**		
a)	Entire Risk located on First floor and above		10
b)	Part of Risk or entire Risk located on Ground floor		5
c)	Part of Risk or entire Risk located in basement		0

10.	**House Keeping and Working Environment**		
a)	Working in controlled atmosphere (dust, humidity, air conditioning etc.)		10
b)	Not working in controlled atmosphere (dust, humidity, air conditioning etc.) but excellent house keeping		5
c)	Not working in controlled atmosphere (dust, humidity, air conditioning etc.) and housekeeping is not excellent		0
11.	**ISO certification (ISO 9000/9001)**		
a)	Certified		5
b)	Not Certified		0
12	**Location (for Earthquake Zone)**		
a)	Zone I		0
b)	Zone II		5
c)	Zone III and IV		10
	Total Earned Points		

Annex-E: ICR for Last 3 Years, Excess and Points Earned

	Incurred Claim Ratio for Last 3 Years	Excess	Points
a)	Up to 20%	Normal	
b)	More than 20 % to up to 40%	Normal	
c)	More than 40 % to up to 60%	Normal	
d)	More than 60% to up to 70%	Normal	
e)	More than 70% and up to 100%	150% of normal	
f)	More than 100%	200% of normal	

*In case of bio-medical equipments, if the claim ratio is more than 100 per cent the loading may be 50 per cent

Annex-F: Rates on Total Points Earned

SN	Effective Points Earned	Rate to be charged
1.	Above 50	21
2.	Above 40	18
3.	Above 30	15
4.	Above 20	5
5	Above 10	3
6	Less than 10	0

Loading for Waiver Warranty Relating to Maintenance Agreement

The warranty relating to 'Maintenance Agreement' under the policy can be waived by charging the following loadings:

(a) Equipments* with sum Insured up to Rs. 1 lakh……………50 per cent loading on Tariff Rates

(b) Equipments* with sum Insured above Rs. 1 lakh…………..100 per cent loading on Tariff Rates

* In case of computers, the term equipment shall include the entire computer system comprising or CPU, key boards, monitors, printers, stabilizers, UPS, etc.

- The maintenance agreement warranty with regards to 'personal computers' with a sum insures up to Rs 1 lakh can be waived.

- Wherever, the component 'In- House' maintenance facility is available, the warranty relating to 'Maintenance Agreement' with the manufacturers of the equipments can be deleted for all electronic equipments except 'Medical Equipment' covered under 'Electronic Equipment Insurance'.

Section II – External Data Media

(i) Scope of Cover

The insurer agrees with the Insured that if the external data media mentioned in the Schedule inclusive of the information stored thereon, which can be directly processed in EDP systems, shall suffer any material damage caused by peril covered under Section 1 of this Policy, the insurer will indemnify the Insured provided in respect of such loss or damage up to an amount not exceeding in any one year of insurance in respect of each of the data media specified in the Schedule the sum set opposite thereto and not exceeding in all the total sum insured hereby, provided always that such loss or damage occurs during the period of Insurance stated in the Schedule or during any subsequent period for which the Insured pays and the Company may accept the premium for the renewal of this Policy. This cover applies while the insured data media are kept on the Premises. Coverage against restoration of data under Section II is only to be granted if backup system is available. Thus cover applies if the external data media, specified in the schedule (type and quality) inclusive of the information stored, which can be directly processed in EDP system suffers material damage by perils covered under Section 1 of the policy. In case the external data media specified in the schedule, inclusive of the information stored therein, which can be directly processed in EDP systems, shall suffer any material damage caused by a peril covered under Section 1 of the policy, the company will indemnify the insured in respect of loss or damage up to an amount not exceeding in any one year of insurance in respect of each of the data media specified in the schedule the sum set opposite thereto and not exceeding in all the sum insured hereby:

Provided always that such loss or damage will occur during the period of insurance or during subsequent period for which the insured pays and company may accept the premium for renewal of the policy. The pre-condition to such cover is that insured data media are kept in the premises.

(ii) Special Exclusions Applicable to Section II

The Company shall, not be liable for:

- the excess stated in the Schedule to be borne by the Insured in any one occurrence;
- any costs arising from false programming, punching, labeling or inserting, inadvertent canceling of information or discarding of data media, and from loss of information caused by magnetic fields; and
- Consequential loss of any kind or description whatsoever.

(iii) Special Provisions Applicable to Section II

- Sum insured shall be the amount required for restoring the insured external data media by replacing lost or damaged data media by new material and reproducing lost information.
- Indemnification will be made by the insurer for the expenses that can be proved to have been incurred by the insured within a period of 12 months from the date of the occurrence strictly for the purpose of restoring the insured external data media to a condition equivalent to that that existing prior to the occurrence and necessary for permitting data processing operations to be continued in the normal manner.
- It is not necessary to reproduce lost data or information, or if such reproduction is not effected within 12 months after the occurrence, the insurer, the insurer shall be liable to indemnify the expenses incurred for replacing the lost or damaged data media themselves by new material.
- From the date of occurrence of damage indemnifiable, the sum insured shall get reduced for the remaining period of insurance.

Section-III – Cover for Increased Cost of Working

(i) Cover

Notwithstanding special Exclusion under Section 1 of this policy the insurer hereby agrees to indemnify the insured not exceeding the limits of indemnity stated in the schedule for all additional costs which the Insured shall incur to ensure continued data processing on substitute equipment if such costs arise as an unavoidable consequence of an admissible loss or damage during the period of insurance to property insured under the Material Damage Section of this policy.

(ii) Section Exclusions to Section 111

The company shall not be liable for:

- Costs incurred for use of substitute equipment during the Time Excess stated in the schedule.
- ‘Costs for replacement of data media, data and regeneration of data.
- Costs arising out of circumstances, which are not connected with the insured material damage. The company shall not be liable for additional costs arising out of:
    - o bodily injuries,
    - o orders or measures imposed by any public authority,
    - o expansion and improvements of the equipments,
    - o lack of funds causing delay in repairs or replacement of damaged equipments,
- Any other consequential loss such as loss of market or interest.

(iii) Special Conditions Applicable to Section III

Memo 1: Indemnity Period

- The Indemnity period shall commence with putting into use the substitute equipments.

- The Insured shall bear that proportion of each claim, which corresponds to the Time excess agreed.

Memo 2: Sum Insured

- The 'indemnity limit per hour' and 'total sum insured' stated in the schedule shall be declared by the insured. The total sum insured shall represent the aggregate limit of indemnity payable for all events occurring during the period of insurance. The company will also reimburse the insured for personnel expenses and costs for transportation of materials following an event giving rise to a claim under this section of the policy provided separate sums therefore have been entered in the schedule.

- As from the date of an indemnifiable occurrence the sum insured shall be reduced for the remaining period of insurance by an amount of indemnity aid unless- reinstated by payment of an additional premium prescribed by the company.

Memo 3: Indemnity

- The company shall indemnify those costs and expenses, which can be proved to have been incurred during the indemnity, the period to maintain data processing operations to their previous extent, that are additional to those which would have been incurred during the same period if no insured event had occurred.

- The total indemnity per event shall not exceed an amount equal to the agreed 'indemnity limit per hour' or the 'actual hourly rate payable for the use of substitute equipments', whichever is less multiplied by the number of working hours stated as 'Indemnity Period' in the schedule or by the actual number of working hours for which the substitute equipment is put into use, whichever shall be less.

- However, if it is found, following an interruption, that the limit selected 'per hour' is less than the amount actually incurred per hour for use of substitute equipment, the company shall be liable to indemnify the insured in the same proportion as the limit selected 'per hour' bears to the amount actually incurred per hour.

  Provided always that:

  o the interruptions shorter than the Time Excess stated in the schedule shall be excluded from the scope of this policy; and

  o in respect of interruptions longer than the Time Excess the insured shall bear that proportion of each claim which corresponds to the Time Excess.

Risk Analysis for EEI Policy — (applicable to all Sections)

The Engineer responsible for risk inspection need to special attention to the following hazards and risks during his pre-acceptance risk inspection and risk analysis:

a. Identification of Hazards in Software Industry

- Heat, smoke & water
- Fire and other hazards
- Hazards due to construction elements
- Hazards due to exposure from adjoining risks
- Hazards due to electrical defects

b. Hazards due to Construction Elements

- Storage of raw material and finished goods
- Location and exposure
- Electrical installation
- Natural and health hazards

c. Other Hazards

- A fire in vicinity of electronic equipment may damage by heat, flame, soot & gas
- Lightning may cause electronic equipment to fail
- High discharge of electricity can damage entire system
- Careless handling, operational error

Electronic All Risks (Ear)/Store-cum-Erection (SCE)

It is project insurance. This type of policy is commonly issued for insurance coverage of various projects under erection.

Scope and Cover

Erection All Risks Policy (EAR) also known as Store-cum-Erection (SCE) policy provides all-risks insurance cover for erection of electrical plant and machinery and equipment and structures involving no or very little civil engineering work. Following rapid industrialization this form of insurance has gained a lot of importance and has become indispensable for protecting the financial interests of entrepreneurs in projects in this country. Any kind of large project involves a number of hazards both for the contractor and for the owners of the works (principal), and financial institutions lending against large erection projects require protection under the EAR policy to safeguard their financial outlay. In most contracts for erection jobs EAR Insurance is specified as one of the prerequisite conditions.

The policy may be required by any firm that assumes a risk for the erection of a project e.g. manufacturers or suppliers of machinery if they carry out the erection, or firms of contractors deputed for specific erection jobs or purchasers of machinery to be erected. Each of the firms concerned may insure their interests under an EAR Policy. It is also possible to issue a joint policy in the names of one or more parties such as principals, principals and/or contractors and/or subcontractors in respect of an entire project.

Insurable Property

Some contracts involve both civil engineering works and erection of machinery and equipment and require both covers i.e. CAR and EAR. The insurance package, which combines the two covers, is known as **Contract Works Insurance.**

Risk covered

Following risks are covered by such policy:

- All AOG (Act of God) perils – Natural calamities like earthquake, landslide, flood, storm, cyclone etc
- Fire, lightening, riot, and strike and sabotage
- Theft & Burglary
- Faults during erection, lack of skill/carelessness of workers and handling risks
- Short circuit, explosions tearing apart on account of Centrifugal forces
- Electrical & Mechanical failure during trial & testing.

Exclusions (Risks not covered)

Such policy does not cover following loss or damages occurred due to willful acts, negligence of the insured or war & war like perils:

- War and similar other risks including nuclear reaction
- Damage failing under manufacturer's guarantee
- Cost of rectification of any error during erection unless results into physical loss
- Willful act or gross negligence of the insured
- Consequential loss of any kind and contractor liability
- Normal wear and tear, gradual deterioration due to atmosphere condition resulting into rust, scratching of painted and polished surface, breakage of glass etc.
- Manufacturing guarantee
- Inventory loss
- Rectification
- Consequential loss, penalty
- Excess

Sum Insured

The sum insured shall be the completely erected value of the property inclusive of freight etc., and the costs of erection. Separate sum insured is specified for Section 1 and Section 11. Following aspects are considered for determination of sum-insured under this policy

a. Section I for Material Damage Cover

Plant and equipment to be erected (brief details) need to be analyzed with reference to landed cost of imported machinery at factory site, invoice cost, freight, insurance, handling, clearing and transport, customs duty, machinery fabricated or manufactured in India, invoice cost including insurance, handling, clearing and transport upto factory site, freight, erection cost, civil engineering works (permanent and temporary), clearance and removal of debris, construction plant and machinery and surrounding property.

b. Marine/Transit Risks

Where marine or transit insurance connected with Erection All Risks Insurance of any project either simultaneously or later on in one combined policy, the amount of transit value is to be included in the sum-insured.

c. Sub-contracts

In case of sub-contracts forming part of a project, it is to be insured that irrespective of weather the project value has been broken into various sections , order or contracts placed with different suppliers/ contractors/ sub-contractors or the work carried out by the insureds themselves, all are included in the sum insured.

Precisely the **sum-insured** in Marine-Cum-Storage-Cum Erection insured shall include the following components:

- Marine (Imports) –landed costs at site
- Marine (Indigenous)-landed cost at site
- Cost of Erection (Exclusive of prospective expenses, but inclusive of costs of visits of specialists and supervision charges
- Permanent Civil Engineering Works
- Escalation amount only up to 50 per cent
- Duty in case of overseas consignment over and above CIF value. It will include Custom duty paid or to be paid on clearance and clearing & forwarding charges to the agents concerned.

- The amount of storage risks at the Fabricators' Premises or Workshops can be covered as an extension to the EAR/ SCE policies. Importantly such storage, the premium rate and excess may be separate.

Period of Insurance

i. Erection Period

- Pre Storage (Transit)
- Actual Erection
- Pre-Commissioning

ii. Testing Period

- Of Individual Machine
- Of Complete Plant

iii. Maintenance Period

- Visit
- Extended

Period of insurance needs consideration of following aspects:

(a) Basic Period/Erection Period

The insurance shall commence, (not withstanding any date to the contrary specified in the Schedule) only from the time after the unloading of the property specified in the schedule from any conveyance at the site specified in the schedule and shall continue until immediately after the first test operation or test loading is concluded (whichever is earlier) but in no case beyond four weeks from the day on which, after completion of erection a trial running is made and/or readiness for work is declared by the erectors/ contractors, whichever is earlier. If however, a part of a plant or one or several machines is/are tested and put into operation the cover for the particular part of the plant or machine cease whereas it continues for the remaining parts which are not yet ready.

In case after the expiry of four weeks of trial running, approval of the plant or any part thereof is not given by the concerned authorities the cover for the extended period of further trial running can be converted at extra premium to be arranged beforehand. In the case of second-hand/used property, the insurance hereunder shall, however, cease immediately on the commencement of the test. 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.

(b) Testing Period

The testing period is normally the most hazardous period for plant and machinery. Not only are the various items subjected to operating conditions and load for the first time but also for many types of plant the introduction of feedstock increases both the fire and explosion hazards (e.g. Petroleum Refineries, Petrochemical Plants, etc.). Testing operations can be divided into two categories viz. Cold Testing and Hot Testing. In order to determine the "Testing, period for purpose of the EAR policy", following aspects require special mention:

(i) Cold Testing: The Cold Testing (functional testing) is the checking of parts and elements of insured property by mechanical, electrical, hydrostatic, or other forms of testing under 'no load' conditions. Cold testing excludes the operation of furnaces or the application of any direct or indirect heat, the use of feedstock or other materials for processing. In electrical power stations, cold testing excludes connections to a grid or other load circuits of electrical generating, transforming, converting or rectifying equipment.

(ii) Hot Testing (operational & commissioning tests): The checking of parts, elements and/or production lines of insured property under full or partial load and normal or simulated operating conditions including the use of feedstock or other material for normal processing or other media for load simulation. In electrical power stations "hot testing" means checking after connection to a grid or other load circuit of electrical generating, transforming, converting or rectifying equipment. Commissioning tests/Acceptance tests shall mean operation of insured property under production conditions for the purpose of attaining (quantity, quality) specification requirements.

Cold testing period is generally treated as a part of the normal or Erection Period and does not worry the insurers. However, "Hot Testing" period is very relevant for the insurers. The Works Contract may use the terms 'hot test', 'operational test', 'commissioning test' or 'acceptance test' to indicate the period during which the plant is exposed to full load conditions for the first time, with the plant personnel lacking extensive training. Since the insurer is confronted with a period of considerably increased risk, a higher rate & Excess is applied for the testing period. Maintenance extensions are also granted. The storage and erection period, testing period and the maintenance period are shown separately.

Basis of Indemnity

In case of loss or damage the insurer provides the indemnity to the insured on the following basis:

i. Partial Loss

- Repairs or Replacements of parts
- Reimbursement of freight, duty, insurance and taxes paid for parts
- Cost of erection

ii. Total Loss

- Up to the limit of sum-insured

iii. Constructive Total Loss

- Repair Charges or replacement based on market value

Again the indemnity mentioned above is subject to following deductions:

- Specified Excess/Deductibles
- Salvage
- Average or underinsurance
- Modifications
- Wear & tear of parts of used/second hand equipment

Rating

In Erection All Risks/Storage-cum Erection Insurance class rate is used. For this purposes, risks are classified into hundreds of groups according the respective probability and severity of claims experience. Following aspects need to be specially considered for rating under this policy:

a. Rating for Material Damage

i. **Class rates:** According to industry experience erection work is classed into many group for rating purpose such as Air Compressors, Asbestos Plant, Aluminum Plant. Bakeries, Blast Furnace, Breweries, Cable Work, Cable Laying, Cattle Feed plants, Cellular Telephones, Cement Manufacturing, Chemical Plants, Confectionary work, Dal Mills, Diesel Engines, Edible Oil Plant, Engineering Workshop, Flour Mills, Fertilizer Plant, Gas Work, Glass Work, Hydro Power Units, Ice Cream Plant, LPG Building Plant and so on. Basic rates vary from Rs 1 per mill to Rs 5 per mill.

ii. **Periodical Rate:** Final rate of premium depends on the period of construction and testing period such as:

- Rate for the 1st month + 1 month testing period …Basic Rate per mille
- Monthly Rate for

b. Example: Rating in Tariff Regime

- Work/Plant/Project wise Rate (For example, Asbestos plant (2.5 per cent), Ash Handling Plant(2.5 per cent), Air Compressors (2.25 per cent), Baby Food plant (2 per cent), Bakeries (2 per cent), Cable Works (2.25 per cnet), Cable Laying (2.75 per cent), Flour Mills (2 per cent) etc.

- The basic rate as exemplified is meant for first two months (1st month + 1 month testing)

- The rate will be enhanced at certain per cent per month for subsequent 10 months and certain per cent per month for period exceeding 12 months.

The EAR/SCE period has to commence from the date of arrival of first consignment at the site. Additional premium is to be charged for Dismantling Cover and Earthquake perils in the following basis:

- Additional Rate for Dismantling Cover – 60 per cent of SCE rate

- Additional Rate for Earthquake Cover (As per Zone)- It may be on First Loss basis – 50-40 per cent of rate for 20-10 per cent SI

The rates and methods mentioned above are illustrative and were followed in the tariff regime.

c. Rating Method in De-Tariff Regime

Now in the de-tariff regime every company has got the full freedom in underwriting and pricing. They are to now rate every risk on the basis of the risk analysis of individual project risk, their own underwriting policy and reinsurance programme. Merit Rating is followed in the project insurance. For merit rating underwriters calculate the merit points earned by the project to decide the rates to be charged. For merit rating risks are to be identified and analyzed. In the following annexures it has been discussed more clearly.

Risk Analysis and Risk Inspection for Merit Rating – Erection All Risk Insurance

1.	Name of the Proposer /	:
2.	Contractor/Financers	
3.	Location of Project site (city, district & state)	:
4.	Nature of risk (with risk code)	:
5.	Proposed Project Period (Including testing)	:
6.	Total Testing period included in the	:
7.	Policy period	:
8.	List of additional/Add on covers Opted (If yes Annexure-G to be enclosed)	:
9.	Voluntary higher excess, if opted	:
10.	Whether new or second-hand equipment involved	:
11.	Analysis of physical features (see Annexure G)	:
12.	Rate to be Charged; (see Annexure H)	:

Annex-G: Physical Features

S.N.	Features of the Risk	Yes/ No	Points Earned
1.	**Type of Project**		
a)	Whether Greenfield project		10
b)	Whether New separate unit within existing Plant/ Project		5
2	**Location (For Flood And Inundation Features/ Low Lying Area)**		
a)	Low Risk (the risk is not located in low lying area and is far away from sea/ river and there is no past history of flood and inundation during the last five years)		10
b)	Moderate Risk (either the risk is located in low lying area and near sea/ river or there is past history of flood and inundation during the last five years)		5
c)	High Risk (the risk is located in low lying area and near sea/ river as well as there is past history of flood and inundation during the last five years)		0
3.	**Project Location (for Cyclone feature)**		
a)	Whether Located in Low Wind/ Low cyclone prone area		10
b)	Whether Located in Moderate Wind/ Moderate cyclone prone area		5
c)	Whether Located in High Wind/ High cyclone prone area		0
4.	**Project Location (for riots/civil disturbance feature)**		
a)	Whether Located in Low risk prone area based on history		10

b)	Whether Located in Moderate risk prone area based on history		5
c)	Whether Located in High risk prone area based on history		0
5.	**Earthquake Zone**		
a)	Whether Project Located in Zone III or IV or Earthquake Protection Design is as per the standards for the risk located in Zone-I or Zone-II respectively		10
b)	Whether Project Located in Zone II but Earthquake Protection Design is not as per the standards for that Zone		5
c)	Whether Project Located in Zone I or Zone-II with no Earthquake Protection Design		0
6.	**Fire Fighting Facility**		
a)	Whether Hand Appliances, Fire tender or Trailor Pumps and Hydrant System available		10
b)	Whether Hand Appliances and Fire Tender or Trailor Pumps or Hydrant System available		5
c)	Whether only Hand Appliances available		0
7.	**Fire brigade**		
a)	Own Fire brigade or public fire brigade is available within 5 KM without railway level crossing *en route*		10
b)	No own fire brigade but the public fire brigade is available within 10 KM with or without railway level crossing *en route*		5
c)	Neither own fire brigade nor the public fire brigade within 10 KM		0

8.	**Security Arrangement**		
a)	Whether 24 hrs. watch & ward facility and Compound Wall around the site available		10
b)	Whether 24 hrs. watch & ward facility without Compound Wall around the site is available		5
c)	Whether 24 hrs. watch & ward facility and Compound Wall around the site is not available		0
9.	**Repair Facility**		
a)	Whether repair facility available within India		5
b)	Whether repair facility not available within India		0
10.	**Reputation of Contractor(s)**		
a)	Highly reputed and experienced contractor		10
b)	Moderately reputed and experienced contractor		5
c)	Low reputed and experienced contractor		0
11.	**Number of add on covers opted requiring extra premium opted**		
a)	More than six		10
b)	Three to six		5
c)	Less than three		0
	TOTAL POINTS EARNED		

Annex-h: Points Earned & Rate to be Charged

S.No.	Effective Points Earned	Rate to be Charged
1.	ABOVE 50	
2.	ABOVE 40	
3.	ABOVE 30	
4.	ABOVE 20	
5.	ABOVE 10	
6.	BELOW 10	

Premium Adjustment Clause

This is the same as in CAR policy, except the reference in this clause is made to prime cost of Plant and Equipment. Basis of loss settlement and reinstatement of sum insured clauses are the same as in CAR policy. Construction plant, surrounding property and third party liability etc., are optional covered and the comments made earlier apply.

Deductibles

Excess is applied separately for:

- Storage and erection claims
- Testing Claims
- Maintenance Claims
- Fire and Act of God perils.
- Third Party Liability for property damage

Deductible is an important tool of risk improvement, loss reduction and consequent premium reduction.

Civil Engineering Works as an Extension

Subject to the exceptions contained herein, or endorsed hereon, this Policy is extended to cover the risks of loss or damage to property brought on to the Site of Erection for the Performance of the erection contract, details of which are stated as under:

All Permanent Civil Engineering Works such as buildings, foundations, earthwork, including materials for the construction thereon. All temporary works such as buildings, sheds are covered, provided that the following exclusions shall apply:

- Loss or damage directly caused by defective workmanship, material, or design or wear and tear, mechanical breakdown or derangement, deterioration due to lack of use or obsolescence.
- Any loss of property either by disappearance or by shortage if such disappearance or shortage alone in revealed during and after an inventory is made.
- Cessation of work whether total or partial,
- Loss, destruction of damage of accounts, bills, currency, stamps, deeds, evidence of debt, money notes or securities.
- The exclusions of loss or damage caused by (i) above shall be limited to the machine structure or work immediately affected and shall not extend to other work or property lost or damaged in consequence of the defect, wear, breakdown or deterioration.

Refund of Premium for Early Completion of the Project:

Refund of premium for completion of the project earlier than the period mentioned in the policy schedule for any project (including the testing period) may be allowed subject to the under-mentioned conditions being complied with:

- The period of insurance is 18 months and above.

- Notice for early completion being given in advance to the insurer, i.e. before commencement of testing or in any case not later than 7 days after commencement of testing.

- Claims Experience under the policy being less than 60 per cent.

- The minimum period for which refund can be claimed shall be 3 months.

- The refund of premium would be allowed only after re-working of the premium on reduced policy period.

Maintenance Visits and Extended Maintenance Cover – (TAC Guidelines)

a) Limited Maintenance Visits Cover Endorsement As per TAC Directives)

In consideration of the payment of an additional premium by the insured (which is included in the Total Premium set forth in the schedule), it is hereby declared and agreed that the indemnity provided by this policy is extended to include maintenance cover for the period of ____ months to be reckoned from the date of completion of Testing, provided the policy period has been extended till completion of Testing. However, during the Maintenance Period this Insurance shall cover solely loss of or damage to the contract works caused by the insured contractor(s) in the course of the operations carried out for the purpose of complying with the obligations under the maintenance provisions of the contract.

b) Extended Maintenance Cover (Endorsement As per TAC Directives)

In consideration of the payment of an additional premium by the Insured (which is included in the total premium set forth in the schedule) it is hereby declared and agreed that the indemnity provided by this policy is extended to include Maintenance Cover for the period of _____ months to be reckoned from the date of completion of Testing, provided the policy period has been extended till completion of Testing. However, during the Maintenance period this insurance shall cover loss or damage to the contract works:

- Caused by the Insured contractor(s) in the course of the operations carried out for the purpose of complying with the obligations under the maintenance provisions of the contract.

- Occurring during the maintenance period provided such loss or damage was caused on the site during the erection period.

(c) Warranty on Extended Maintenance Cover (Endorsement as per TAC Directives)

It is agreed and understood that otherwise subject to the terms, exclusions, provisions and conditions contained in the policy or endorsed thereon and subject to the Insured having paid the agreed extra premium, this insurance shall be extended for the maintenance period specified hereunder to cover loss or damage to the contract works:

Caused by the insured contractor(s) in the course of the operations carried out for the purpose of complying with the obligations under the maintenance provisions of the contract.

- Occurring during the maintenance period provided such loss or damage was caused on the site during the erection period before the certificate of completion for the loss or damaged section was issued.

  Maintenance cover from __________ to ___________

  Extra premium _____________

General Conditions (As per Tariff)

1. The due observance and fulfillment of the terms of this Policy in so far as they relate to anything to be done or complied with by the Insured and the truth of the statements and answers in the questionnaire and proposal made by the

Insured shall be a condition precedent to any liability of the company.

2. The Schedule and the Section(s) shall be deemed to be incorporated in and form part of this policy and the expression 'this Policy' wherever used in this contract shall be read as including the Schedule and the Section(s). Any word or expression to which a specific meaning has been attached in any part of this Policy or of the Schedule or of the Section(s) shall bear such meaning wherever it may appear.

3. The Insured shall at his own expense take all reasonable precautions and comply with all reasonable recommendations of the Company to prevent loss, damage or liability and comply with statutory requirements and manufacturers' recommendations.

4. Representatives of the Company shall at any reasonable time have the right to inspect and examine the risk and the Insured shall provide the representatives of the company with all details and information necessary for the assessment of the risk.

5. The Insured shall immediately notify the Company by telegram and in writing of any material change in the risk and cause at his own expense such additional precautions to be taken as circumstances may require and the scope of cover and/or premium shall, if necessary be adjusted accordingly.

6. No material alteration shall be made or admitted by the Insured whereby the risk is increased unless the continuance of the Insurance be confirmed in writing by the Company.

7. In the event of any occurrence, which might give rise to a claim under this Policy, the Insured shall:

   o 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.

- o take all steps within his power to minimize the extent of the loss or damage.
- o preserve the parts affected and make them available for inspection by a representative of the company or surveyor deputed by the Company.
- o furnish all such information and documentary evidence as the company may require.
- o inform the police authorities in case of loss or damage due to theft or burglary.

8. The Company shall not in any case be liable for loss, damage or liability of which no notice has been received by the company within 14 days of its detection.

9. 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. In all other cases, a representative of the Company shall have the opportunity of inspecting the loss or damage before any repairs or alterations are affected. If a representative of the Company does not carry out the inspection within a period of time which could be considered as adequate under the circumstances the Insured is entitled to proceed with the repairs or replacement.

10. The liability of the Company under this Policy in respect of any item sustaining damage shall cease if said item is not repaired properly without delay.

11. The Insured shall at the expense of the Company do and concur in doing and permit to be done all such acts and things as may be necessary or required by the Company in the interest of any rights or remedies, or of obtaining relief or indemnity from parties (other than those insured under this Policy) to which the company shall be or would become entitled or subrogated upon their paying for or making good any loss or damage under this Policy, whether such acts

and things shall be or become necessary or required before or after the Insured's indemnification by the company.

12. If any dispute or difference shall arise as to the quantum to be paid under this Policy (liability being otherwise admitted) such difference shall independently of all other questions be referred to the decision of a sole arbitrator, to be appointed in writing by the parties to or, if they cannot agree upon a single arbitrator within 30 days of any party invoking Arbitration, the same shall be referred to a panel of three Arbitrators comprising of two Arbitrators - one to be appointed by each of the parties to the dispute/difference, and the third Arbitrator to be appointed by such two Arbitrators and arbitration shall be conducted under and in accordance with the provisions of the Arbitration and Conciliation Act 1996.

13. It is clearly agreed and understood that no difference or dispute shall be referable to arbitration as hereinbefore provided, if the Company has disputed or not accepted liability under or in respect of this Policy.

14. It is hereby expressly stipulated and declared that it shall be a condition precedent to any right of action or suit upon this Policy that the award by such Arbitrator/Arbitrators of the amount of the loss or damage shall be first obtained.

15. If a claim is in any respect fraudulent, or if any false declaration is made or used in support thereof, or if any fraudulent means or devices are used by the Insured or anyone acting on his behalf to obtain any benefit under this Policy, or if a claim is made and rejected and no action or suit is commenced within three months after such rejection or, in case of arbitration taking place as provided therein, within three months after the Arbitrator or Arbitrators or Umpire have made their award, all benefit under this Policy shall be forfeited.

16. If at the time any claim arises under this Policy there be any other insurance covering the same loss, damage or liability

the company shall not be liable to pay or contribute more than their rateable proportion of any claim for such loss, damage or liability.

17. 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.

18. Claims experience under the policy as on date of cancellation should be less than 60 per cent of reworked premium.

19. The unexpired period is not less than 3 months or 25 per cent of the policy period, whichever is less, testing period should not have commenced.

20. This insurance may also at any time be terminated at the option of the Insurer by 15 days notice to that effect being given to the Insured in which case the Insurers shall be liable to repay on demand a rateable proportion of the premium for the unexpired term from the date of cancellation.

Contractors All Risk Policy

Scope

Contractors All Risk Policy is concerned with contracts involving civil engineering works such as construction of buildings, bridges etc. This applies to all risks located in India for which the value of civil work involved is more than 50 per cent of the total contract value. Principal or Contractor/sub- contractor can take this Policy. If Marine Insurance associated with CAR for any project is placed in India simultaneously or differently, CAR cover may include transit risks also. Storage Risk at Fabricators Premises/Workshop with additional premium and additional Excess may also be covered under CAR policy. Add on cover like Earthquake Perils may be covered with additional premium as per earthquake zone rate of premium.

Any loss or damage to the contract works during the course of the construction due to any cause will result in heavy financial loss to the contractor. The principal/owner normally makes the contractor responsible for accidents due to faculty workmanship, faulty material and other errors of the contractor in the contract condition. The contractors' margin of profit may not be adequate to reconstruct after damage if any. This is why the contractor needs this sort of insurance protection to be indemnified of any accidental loss or damages of any perils unless specifically excluded.

The plant insurable under this policy could be broadly into boilers, transformers, switchgear, compressors and plant for manufacturing purposes etc. Other equipments include structural steelwork, tanks, oil refinery plant, blast furnaces etc. The policy may cover an individual machine e.g. turbine, generator, etc., or an overall composite project, e.g. power generating station, steel mill, oil refinery, industrial premises, etc.

Sum Insured

The following items are taken into account for determination of the sum insured.

(a) Marine (imports) – Landed Cost at site,

(b) Marine (Indigenous) -at cost

(c) Cost of Construction,

(d) Permanent Civil Engineering Works

(e) Half the escalated value, if escalations opted for

(f) Preoperative expenses

Marine/Transit Risks: Where Marine/Transit Insurance connected with Contractor's All Risks Insurance of any project is placed in India simultaneously or later on in one combined policy or under separate policies, in one department or in different departments, the matter relating to Contractors All Risk Cover is required to be underwritten, subject to these General Regulations.

Premium Rating

Premium shall be computed for the total period commencing from the commencement of work or date of arrival of the first consignment at the site of erection whichever is earlier. For the purpose of rating following aspects are taken into considerations:

- Rate as per Nature of Work, Plant, Height of Construction, etc
- Minimum Rate for 3 months
- Additional Rate beyond 3 months
- Rate for sum insured up to Rs 100 crores
- Rate for SI beyond that
- Storage Risk at the fabricators premises is admissible at additional premium
- Earthquake Cover with additional premium as per earthquake zone rate. is admissible with separate excess for such cover
- Separate premium for Third Party Liability according to indemnity limit selected

Premium Rate up to Rs. 100 crores – Few Examples

Rate given in Table-27 is as per earlier tariff that has been reduced substantially in the current detariff regime according to their loss experience or underwriting policy.

Table-27: Premium Rates

Risk	Nature	Rate %	Rate %
Building-office, Hotels Residential, Commercial	No RCC, Not more than 2 storeys	1.00	0.02pm
—do—	DO beyond 2 and upto 5 storeys	1.75	0.025pm
Factory Sheds, Ware-house, Cold Storage etc	RCC Frame Not more than 5 storeys	1.5	0.025pm
—do—	DO Beyond 5 but upto10 storeys	2.00	0.03pm
Factory Sheds Ware-house, Cold Storage etc	No RCC Construction	2.25	0.02pm
—do—	RCC	2.00	0.02pm
Roads	In Township	2.00	0.025pm
—do—	In Plain Areas	2.50	0.03pm
—do—	In Hilly Areas	3.00	0.04pm

The rates mentioned above are only illustrative**.** Now individual underwriter will follow their own underwriting policy, rate structure after proper risk analysis for each and individual risks.

Storage Risks Rates for Fabrication Workshop

This is an extension to CAR policy and genially rated at the following rates:

Rate…Rs 0.30 per mile per annum or part thereof

Excess …….Rs 1500 per claim

Additional Rates for Earthquake (Fire and Shock)

Irrespective of sum-insured for CAR, the following additional rates are to be charged over the CAR Rate for risks located in the Earthquake Zone which is divided into four Zones I to IV. Generally, Zones I and II, no premium rates are charged as per earlier tariff. For Zone 1, rate is Rs 1 per mile and Zone II it is Rs 0.50 per mile in general. In this regard the following regulations are followed by individual underwriters:

- The above additional rates are to be charged on pro-rata basis for period shorter than one year.
- All Acts of God perils other than earthquake are covered in the standard policy without additional premium for them.
- The rates mentioned above for earthquake cover are charged for the total CAR policy period including all extensions.
- Earthquake cover in Zone 1 and Zone 11 is optional as mentioned above, but cannot be granted in the mid-term or for part of the policy period.
- Excess for all AOG perils including Earthquake, Landslide, Rock-slide, Flood-inundation, Storm etc., is generally Rs 25,000 for Zone 1 and Rs 10,000 for Zone II.

Mid-Term Increase in Sum-insured

In case any need arises for increase in sum-insured of CAR during the policy period, the premium should be collected on the additional sum insured at applicable rate for entire period of policy without applying pro-rata premium on such increased sum-insured.

Discount for Higher Excess

All rates for CAR insurance are subject to minimum Excess per claim and separately for a) Normal; and b) AOG covers.

c) Discounts for Oopting Higher Excess (both Normal and AOG claims) as per earlier tariff which may be used as guideline.

Table-28: Discount for Higher Excess

Excess	Discount in Premium
2 times the Minimum Excess	5%
5 times the Minimum Excess	10%
10 times the Minimum Excess	20%
20 times the Minimum Excess	30%

Table-29: Discounts for Opting Higher Excess in Earthquake Risks

Earthquake Excess Increased to	Discount in Earthquake Premium
2 times the Minimum Excess	5%
5 times the Minimum Excess	10%
10 times the Minimum Excess	20%
20 times the Minimum Excess	30%

Notes:

- Above rates are given as guidelines subject corporate underwriting policy
- These discounts are separately considered irrespective of the other excess

Third Party Liability

Third Party Liability Insurance cover is granted with the following terms and conditions in general:

- Sum-insured is decided with two indemnity limits being AOA and AOY

- Sum- insured may be up to a certain limit (say AOA- Rs 10 crores and Sum-insured beyond that, but to certain per cent of erected value

- Sum-insured beyond a specified limits to be decided by the underwriters after careful risk analysis i.e. CASE study (discussed earlier)
- Policy excess both normal and AOG claims will apply to TP property liability damage claims
- Excess applicable to AOG Claims will apply to TP liability arising from AOG perils

Surrounding Property Damage Cover

CAR may be extended to cover the surrounding property of the insured subject to a separate sum-insured with the payment of additional premium at 50 per cent of the CAR rate.

Escalation Provisions

A CAR policy generally provides Escalation benefit which may be limited to 50 per cent of the sum-insured of the CAR depending upon the situation. The escalation amount may be specified in the policy either in terms of per cent or in amount. For the purpose of calculation of escalation certain procedure is followed in general.

15

MISCELLANEOUS INSURANCE

Miscellaneous Insurances Large in Number

In non-life insurance the products of Miscellaneous Insurance are large in number and variety in characters. The following are the important and most common products in miscellaneous insurance:

- Personal Accident Insurance
- Group Personal Accident (GPA) insurance
- Janata Personal Accident (JPA) Insurance
- House Holder Insurance
- Shopkeeper Insurance
- Money in Transit Insurance
- Baggage Insurance
- All Risks Insurance
- Pedal Cycle Insurance
- Burglary Insurance
- Fidelity Guarantee Insurance
- Banker indemnity Insurance
- Jewllers Block Insurance
- Many more others

Personal Accident Insurance

Coverage

This policy covers death, bodily injury including permanent total disablement, permanent partial disablement, and temporary total disablement solely and directly from accident caused by violent and visible means, for which the insurer shall pay to the insured person or his legal personal representative, as the case may be, the sums subject to the terms, conditions and exclusions specified in the policy. This policy can be issued to both individual and a defined group of individuals. Precisely, this policy contains the following features:

- Worldwide Cover on 24 hours basis
- Claim is admissible in case of bodily injury solely/directly resulting from accident by violent visible external means
- Accident resulting in death/ permanent disablement (impairment of limbs, loss of hearing, sight, etc)
- Payment to insured/nominee in case of eventuality due to accidental death from
- Solely and directly from Accident causing
  - (i) Permanent total diablement;
  - (ii) Permanent partial diablement ; and
  - (iii) Temporary total disablement.

Definitions of Various Terms

- **Bodily Injury:** The use of this term excludes disease from natural causes, but disease proximately caused by accident, is bodily injury (unless specifically excluded by the Policy). Mental shock, fright of grief, unless causing some physical injury or disease does not come within the scope of bodily injury, but the modern tendency is towards the inclusion of any disablement caused by shock.

- **Solely and Directly:** The effect of this phrase is to require that the bodily injury shall have been caused solely and directly by an accident; in turn, the bodily injury must directly and independently of any other cause result in death or disablement; hence if any other cause contributes to the result, the insured event has not occurred.

- **Accident:** An accident is an event, which is wholly unexpected, not intended or designed. It does not include the cumulative result of a series of small incidents. Thus, a bent hand, the result of using a pneumatic drill, is not caused by accident.

- **Permanent Total Disablement:** Here, disablement is of permanent and irrecoverable nature and is absolutely total, in the sense that the insured person is prevented from engaging in gainful employment of any kind. (Example: Paralysis). The return is specified that for loss of little finger, compensation is 4 per cent of capital sum insured, loss of four fingers 35 per cent, loss of hearing both ears 75 per cent and so on.

- **Temporary Total Disablement:** As the name implies, this is a disablement which is total (i.e. the insured person is prevented from engaging in any occupation or business) but for a temporary period only. This temporary period may be days, weeks, months or even years.

Benefits Available

- DEATH

- PTD (Permanent total disablement)

- PPD (Permanent partial disablement) and

- TTD (Temporary total disablement)

- Cumulative bonus
- Add on cover – medical reimbursement benefit

Table of Benefits

1. Death only (100 per cent CSI)
2. Loss of two limbs, 2 eyes or 1 limb and 1 eye (100 per cent CSI)
3. Loss of one limb or one eye (50 per cent CSI)
4. Permanent Total Disablement from injury other than those named above (100 per cent)
5. Permanent Partial Disablement (percentage details as given in PA policy bond)
6. Temporary Total Disablement (TTD).1 per cent, of CSI, up to 100 weeks. (Maximum Weekly Benefit not exceeding the specified amount generally Rs 5,000/- or some other)

Note: CSI means Capital Sum Insured

Additional Benefits

(Without additional premium in general)

- Transportation of dead body including funeral charges – Rs 1000/- or 2 per cent of CSI
- Education Grants– in event of death/PTD – compensation up to 2 dependent children – up to 25 years
- If one dependent child, it is 10 per cent of CSI subject to maximum of Rs 5000
- If more than one dependent child, it is 10 per cent of CSI subject to maximum of Rs 10000

Premium Rating Method and Basis

Generally, following rate (Rs per Mile) is charged on the basis of nature of risks and number of benefits. Following rates are only illustrative. Individual insurers are free to rate the products according to their claim experience and risk perception.

Table-30: Premium Rating Method and Basis

Number of Benefits	Normal Risk	Medium Risk	Heavy Risk
As per (1) Above	0.40	0.60	0.90
As per (1) to (4) Above	0.45	0.65	1.05
As per (1) to (5) Above	0.90	1.25	1.90
As per (1) to (6) Above	1.50	2.00	3.00

Nature of risks as mentioned in Table-30 depends on the occupation of the individuals or group of individuals covered by policy. Following is the illustrative explanation of the nature of occupation for the purpose of rating:

- **Normal Risk:** Bureaucrats, Lawyer, Accountants, Architects, Bankers, Consulting Engineers, Teachers, Persons engaged in administrative Functions and persons primarily engaged in occupations of similar hazards.

- **Medium Risk:** Builders, Contractors, Engineers engaged in superintending functions only, veterinary doctors, Paid drivers, Persons engaged in occupations of similar hazards and not engaged in manual labour.

- **High Risk:** Workers in mines, Explosives, electrical installation with high tension supply, Jockeys, Circus personnel, persons engaged in racing wheels, horse back, gaming, hunting, mountaineering, winter sports, skiing, ice skating, hand gliding, river rafting and persons engaged in similar occupations/hazards.

PA-Family Package & Extension

(Suggested guidelines as per present practice)

Family package can be granted on the following pattern:

- Insured (earning member) and Spouse (if earning) CSI for each person as per norms
- Spouse (If not earning) 50 per cent of SI or Rs 1 lakh (or some other specified amount)
- Children (age..5-25 years) 25 per cent of CSI or Rs 50,000 or some other specified amount
- Children ….for death and permanent disablement only in general.
- Family Discount…10 per cent

Extension

This policy can be extended to include reimbursement up to a specified limit and with additional premium as guided below or some other specified amount:

- Medical Reimbursement…40 per cent of claim or 10 per cent of CSI
- Additional Premium ….20 per cent of basic prem.

Provisos on Determination of Sum Insured

- CSI – to be fixed at the commencement, no change
- Risk Analysis — Occupation
- SI of Table III — 2 years income
- Total SI (All Table) — 6 years Income

- Table III cover – up to Rs 5 lakh as std. Risk, Special Risk analysis beyond that
- Cumulative Limits. More than one policy with insurers is allowed.

Exclusions

The exclusions commonly found for Payment of compensation in respect of death, injury or disablement of the insured are as follows:

- From intentional self-injury, suicide or attempted suicide
- Whilst under the influence of intoxicating liquor or drugs
- Whilst engaging in aviation or Ballooning whilst mounting into, dismounting from or traveling in any balloon or aircraft other than as passenger (fare paying or otherwise) in any duly licensed standard type of aircraft anywhere in the world
- Directly or indirectly caused by venereal diseases or insanity
- Arising or resulting from the insured committing a breach of law with criminal intent
- From service in the armed forces
- Resulting directly or indirectly from child birth or pregnancy
- War and kindred peril and nuclear risks
- Suicide is not an accident. Besides it is an offence under the Indian Penal Code and the insured is not allowed to benefit from his own criminal act. But when the circumstances are such that the evidence is equally consistent with either suicide or accident, then the presumption of law against suicide applies and accident will be presumed
- Claims arising out of liquor or drugs, venereal diseases, breach of law with criminal intent are not payable on grounds of public policy. The word ‘criminal intent’ is important

Notes on the Exclusions

- Suicide is not an accident. Besides it is an offence under the Indian Penal Code and the insured is not allowed to benefit from his own criminal act. But when the circumstances are such that the evidence is equally consistent with either suicide or accident, then the presumption of law against suicide applies and accident will be presumed.

- Claims arising out of liquor or drugs, venereal diseases, breach of law with criminal intent are not payable on grounds of public policy.

- Aviation or ballooning present abnormal risks. (Cover may be arranged at extra premium on merits of each case).

Policy Conditions

A policy should be issued with the following conditions:

1. Notice and proof of claims

    o Written notice of claims with full particulars must be give to the Company immediately.

    o In case of death written notice must, unless reasonable cause is shown, be so given before internment or cremation, and in any case, within one calendar month after the death.

    o In the event of loss of sight or amputation of limbs, written notice thereof must be given within one calendar month after such loss of sight or amputation.

2. Proof of claim satisfactory to the Company shall be furnished.

3. Any medical or other agent of the company shall be allowed to examine the person of the Insured on the occasion of any alleged injury or disablement

4. In the event of death, to make a post mortem examination of the body of the insured.

5. A post mortem examination report, if necessary, should be furnished within the space of fourteen days after demand in writing.

6. In the event of loss of sight the Insured shall undergo at the Insured's expense such operation or treatment, as the company may reasonably deem desirable.

7. In the case of claim by death or permanent total or partial disablement, all sums payable shall be only on the delivery of this policy for cancellation.

8. No sum payable under this policy shall carry interest.

9. No claims is payable if the claim is fraudulent or supported by fraudulent statement.

Group Personal Accident (GPA)

PA policy issued to a group of persons is called GPA which is similar to Individual PA policy in terms of coverage, general conditions, and exclusions. Special conditions for such policy are:

- It will be issued to the employees of a firm, company / association/ club with employer-employee relationship.

- It may also cover members of an institution, Society, or association with named persons or unnamed persons basis and with no employer-employee relationship.

- Group Discount is allowed on the basis of group size which is generally as shown in Table-31.

Table-31: Pattern of Group Discount (illustrative)

No. of Persons	Discount (%)
101 –1000	5
1001 – 10000	7.5
10001 – 50000	10
50001 – 100000	12.5
100001 – 200000	15
200001 – 500000	20
500001 – 1000000	25
Above 10 lakhs	30

Jewellers Block Insurance

Scope

This is a special package policy devised to meet the various insurance needs of jewellers carrying on their business. However, moral hazard in this policy is considerably high. Acceptance of risks in this business demands careful analysis of the proposal forms containing the detailed particulars on security, nature of property, and situation of property. A careful scrutiny of the proposal form is also necessary in order to know the claim history since earlier history has bearing on underwriting a proposal of jeweller operating for the 1st year is a bad risk. Since the business relates to valuable items like gold and jewellry, the security factors of the risk assume considerable importance. The questions on particulars of safe, occupancy at night, night watchman, burglar alarm system, etc., need to be answered and analyzed. Separate limits (sum insured) are provided for risks on the premises, outdoor risk when the property is in the custody of gold smiths, brokers, agents, cutters, partners and employee, including transit risks. There is separate item for furniture fixtures and fittings at the premises. The proposer has to complete question No. 8 very clearly, giving full values of insurance. The basis of valuation shall be the insured cost plus 10 per cent thereof. Cover granted is generally divided into 4 Sections as under:

Section-I: Loss of or damage to property whilst contained in the premises insured by fire, explosion, lightning, burglary, house breaking, theft, hold up, robbery, riot, strikes and malicious damage and terrorism.

Section-II: Cover as in Section 1 whilst the property insured is in the custody of the insured, his/her partners, his employees, duly constituted attorneys, directors, sorters of diamonds or whilst such property (excluding cash or currency notes) is in the custody of persons not in regular employment of the insured such as brokers, agents, cutters and goldsmiths.

Section-III: All risks cover whilst such property is in transit by Registered Parcel Post, Air Freight and through *Angadia* subject to exclusions.

Section-IV: Loss of or damage to property due to fire, explosion, lightning, burglary, house breaking, theft, hold up, robbery, riot, strikes and malicious damage.

Explanation to Scope of Cover

Section-I

This section covers loss of or damage to property, whilst contained in the premises where the insured's business is carried on or at other premises where the insured's property is deposited as specified in the schedule by Fire, Explosion, Lightning, Burglary, House- breaking, Theft, Hold-up, Robbery and Riot and strike damage only. Terrorism also becomes part of cover at an additional premium of Rs 0.03 per mile. Limits of indemnity (i.e. sum insured) are shown separately for:

(A) Properly insured on the premises:

1) properly in display windows

2) properly in locked safe on the premises

3) elsewhere in the premises

(B) Cash and currency notes:

1) bank lockers

2) private lockers (Address of all lockers required) subject to insured maintaining separate register to record all deposits , withdrawal in such lockers

The property insured is defined as stock in trade consisting of jewelry, gold and silver ornaments, pearls, precious stones, cash, currency notes, etc. usual to the conduct of the insured's business, belonging to him or held in trust or on commission for which he is responsible. The cover is subject to the warranty that all stocks whilst at the premises specified in the schedule shall be secured in locked burglar proof safe at night and at all times out of business hours.

Section- II

Loss of or damage to property insured and specified in the schedule is covered excluding cash and currency notes whilst in the custody of brokers, agents or cutters or goldsmith or sorters of diamond not in regular employment of the insured whether directly entrusted by the insured or otherwise. The following aspects should be considered for the purpose of underwriting and acceptance of risk under this section:

- Complete list of brokers, agents or cutters or goldsmith or sorters of diamond
- Verification of appropriate documentary evidence
- Issuance of cover subject to the condition on availability of documentary evidence
- Defining/specifying the limit of value of jewellry to be held in the custody of brokers agent etc.
- Analysis of various control system including administrative control, accounting control etc.

- Verification of earlier deals or transaction of this sort with brokers, agents or cutters or goldsmith or sorters of diamond.

Section III

This section covers the insured property excluding cash and currency notes while in transit within India in any of the nature.

- Register insured post up to a certain limit (say Rs 500,00,000) or up to certain per cent of total sum insured.

Rating Method

Rating depends on the class of risks as mentioned below and the nature of covers mentioned in the sections and the sum-insured opted.

Class of Risks**:** Based on the security factors

- Class I: Watchmen employed on 24 hours basis (round the clock) exclusively for all the premises declared for insurance.

- Class II: Common watchmen for the premises for 24 hours for the entire building.

- Class III: All types of other risks.

- Rate generally varies from 0.25 per cent to 0.50 per cent. Higher the class the, greater is the rate. Higher the sum insured, lower is the rate in Section 1.

- Special discount may be allowed if some special protective device or special security measures like built in vaults, strong room, closed circuit, TV system, and armed guard are adopted.

Money Insurance

Cover

This policy provides cover against loss of money in transit by the insured or insured' authorized employee caused by robbery, theft, or any other fortuitous perils. This policy also covers the loss by burglary, housebreaking whilst money is retained at insured's premises in safe or strong room. They money meant for the this policy will include cash, bank drafts, currency notes, cheques and postal orders in the following situations:

(a) Wages in transit from bank to insured premises:

(b) Cash in transit from the insured's premises to post office for purchase of postal orders, money orders, postage or revenue stamps;

(c) Postal orders, etc, in transit from the post office to insured's premises;

(d) Wages in transit from the insured's main premises to insured's branch premises;

(e) Cash, other than wages, in transit from bank to insured's premises, from insured's premises to bank and between insured's main premises and the insured's branch premises;

(f) Cheques, bills of exchange, money orders and postal orders in transit from the insured's premises to bank;

(g) Cash collected by employees from the time of collection and until delivered at the insured's premises or bank on the day of collection; and

(h) Unpaid wages, etc., retained at the insured's premises in burglar-resisting safe, or strong room.

Sum Insured – Money in Transit

- Two amounts are specified in the policy:
    - o limit of the insurer's liability for any one loss
    - o Estimated amount in transit during the year

  Limit of the insurers' liability for any one loss is in fact the sum insured in so far as it determines what the insurer has to pay against a claim.

Money Insurance Exclusions

(a) Shortage due to error or omission

(b) Loss of cash entrusted to any person other than the insured or an employee of the insured

(c) Losses due to the fraud/dishonesty of an employee of the insured (insurers cover such losses provided they are discovered within 48 hours of their occurrence)

(d) Losses which are covered by other policies

(e) Losses arising from war and allied risks

(f) Losses arising from riot, strikes and civil commotion and acts of terrorism

(g) Losses occurring by the use of keys to the safe unless such keys were obtained by force or threat

(h) Money carried under contract of affreightment and theft of money from unattended vehicle.

Rating

Generally following pattern is followed:

- Rate for transit within radius of 2 km (minimum rate say 0.30 per cent)

- Rate for transit within radius of 25 km (moderate rate say 0.40 per cent)
- Rate for transit beyond radius of 25 km (maximum rate say 0.50 per cent)
- Extra premium for riot & strike cover

House Holder Insurance

This policy is a package policy providing cover for building, furniture, fixtures, contents in the building along with the covers for All Risks insurance, plate glass insurance, domestic appliances including TV, refrigerator, VCR, computer or other electronic items and also public liability for bodily injury or property damage caused to third party due to act of negligence of the homeowner or any member of the family. It also provides WC liability cover for bodily injury caused to the servants, cooks, gardeners or drivers. It is a very important miscellaneous insurance product in non-life insurance. But due to lack of appropriate drive for marketing, this insurance could not develop much in the tariff regime though it has had its huge potentiality. The following is the structure of cover of House Holder Insurance along with the rate Structure in the Tariff Regime. This rate structure is now valid in tariff regime and the insurers are free to decide the rate, terms and conditions of the policy according to their underwriting policy though they are required to follow the specific policy wordings suggested or accepted by the regulators.

Rating Structure (applicable to tariff regime)

This is for reference only and it is to be revised by every insurer according to their underwriting policy and claim experience in the past for this department. Again the sections of cover mentioned hereinafter can be suitable changed and improved for the purpose of product development and better marketing.

Table-32: Rating Structure

Sections	Fire &Allied Perils (Building. & Contents) (Note; damage to documents, jewellery, Cash not covered)	Guide Rate 0.50%
II	Burglary & House-breaking	2.40%
III	All Risks Insurance	10%
IV	Plate Glass—Fixed & Interior, show room (10% SI. I)	10.00
V	Domestic Appliances	2.50%
VI	TV, VCR, VCP	10%
VII	Pedal Cycle	20%
VIII	Baggage	7.5%
IX	Personal Accident	0.45, 0.60 etc
X	Public Liability @0.5%o & WC As per guide rate	

Suggested Recommendations or Underwriting Considerations

- Minimum three sections are to be covered
- Cover for Sec I(B) i.e. fire insurance cover for contents is Compulsory
- Group Discount is generally is allowed when cover for minimum 4 sections are opted and higher discount is allowed when greater number of sections are opted. Discounts generally vary from 10 per cent to 30 per cent depending upon the number of sections of cover opted.
- For Personal Computer:, cover is issued like EEI policy cover
- Though Fire perils are covered in the fire lines of business, Excess on Fire cover is not applicable in general

- Terrorism Cover (optional); Rs 0.30 per cent
- **TV,VCR, VCP:** covers include perils including Fire, Mechanical & electrical breakdown & Theft cover
- Acceptance of All Risks cover needs careful risk analysis i.e. analysis of physical hazards and moral hazards. Risks associated with handing of the property are very important.
- Domestic Appliances cover include the perils like: Fire, Mechanical & electrical breakdown

Shopkeepers Insurance Policy

Scope

It provides insurance cover to cater the requirements of small shopkeepers by covering several risks arising from a variety of perils under a single cover in different sections as briefly outlined in Table-33:

Table-33: Insurance Cover against Various Perils

Section I	Fire & Allied Perils as pr fire policy (Buildings & Contents
II	Burglary & House-breaking
III	Money Insurance.(Transit, Safe, Counter sep SI)
IV	Pedal Cycle with PLI of Rs10000 (10% SI of Section I)
V	Plate Glass—Fixed & Interior, show room (10% SI. I)
VI	Neon & Glow signs (Fire & allied, RSMD)2%SI
VII	Baggage Insurance (2% of SI)
VIII	PA (As per PA Cover Table D, C, B& A)
IX	Fidelity Guarantee (10% of SI of Sec I)
X	Public Liability 5% SI& (XI) Business Interruption

Major Underrating Considerations

- Minimum Cover is 4
- Cover under Section I(B) & II being fire cover for contents and Burglary cover are Compulsory
- Group. Discount is admissible as per HHI Policy
- For LOP cover; covers under Section I & II are compulsory
- Excess: AOG 5 per cent Minimum Rs 10,000 & Maximum Rs 25,000 others Rs 10,000 for every loss of other perils may be imposed
- Discount: 15 per cent to 20 per cent depending on no of sections
- Terrorism Cover (optional); Rs 0.30 per cent
- W C Cover: As per old tariff for guidance

Burglary Insurance

Scope

The Policy covers against loss or damage by burglary house breaking (i.e. theft following upon actual, forcible and violent entry of and/or exit from the premises incl. Holdup risk, in respect of contents of offices, warehouses, shops, etc., and cash in safe or strong room & also damage caused to the premises. Property covered by this policy is illustrated below:

- Stock In Trade
- Goods held in trust
- Furniture & Fixtures
- Tools of Trade

- Any Contents
- Cash In safe

Conditions & Causes

- Key clause (obtaining key by violence, threats, force)
- Complete list of amount of cash (in some other place)
- Liability limited to amount shown by records.

Underwriting Considerations

- **Proposal Form:** Details of proposer, business or profession, situation and construction of premises, schedule of items, SI, past experience, present policy.
- **COPE Analysis/Survey:** Class of construction, nature and period of occupation, Protective/ Safety Measures, Survey in case of large or complicated risks.
- Moral hazards, system of stock taking and maintenance of books of accounts. Separate sum-insured for goods owned, goods held in-trust.
- Furniture, cash in safe, details of safe size, make etc., highest value of single item, PML, points of entry and exits.. how safeguarded.
- Cash In Safe Cover needs careful analysis of Cash Secured in a safe, Burglarproof
- Approved Make and Design
- Key Clause
  - o Cannot be deleted by payment of extra premium.
  - o Cash-in-safe to be kept secure in some other place, other than safe – as per records

Rating

Rating can be as per COPE analysis or survey report. Rate varies from 0.10 per cent to 0.50 per cent depending upon risk analysis, Business cash and valuables in safe is subject to greater rate. Business cash and valuables in strong room is subject to lower rate. Additional premium is charged on RSMD.

Types of Burglary Policies

- Full Value – Non Declaration Policy
- Declaration Policy
- First Loss Policy/Partial Value Policy
- Valued Policy - Policy based on inventory & Valuation
  - based on inventory & valuation clause
- Original cost price + overheads (profits to be excluded)
- Non-Declaration Policy - Value to be specified at inception. SI likely to be stable during the period of cover.
- Declaration Policy – SI not fixed, varies according to value & quality of stock (e.g. grains, cereals, cotton, raw materials) – Provisional premium adjusted against actual premium.

First Loss Burglary Insurance

In the event of lesser probability of total loss, a proposer may request Insurance for a per cent of total stocks so declared. Such insurances are called “partial Value” of “First Loss” insurance. Here insurers are willing to accept deliberate under insurance with a sum insured based on the insured’s own estimate of the maximum possible loss.

The Declared Value clause in the First loss Policies introduces a declared value into the wording, but this declared value is not the sum insured. The sum insured is the insured’s estimate of the maximum loss likely to occur (which is selected per cent of full value) and this sum insured is the limit of insurer's liability. The declared value should be the total value of the insured property and it is on this figure that the premium is calculated. However premium is charged as per cent of total stocks so declared based on selected per cent.

Condition of partial average, as under, will apply:

"It is hereby declared and agreed that this policy is issued as the First Loss Insurance up to —— per cent of the insured's total stocks (100 per cent) as limits in the schedule attached to and forming part of the policy. It is generally further declared and agreed that in the event of the total value of stocks at risk at the time of loss be greater than the total value declared for purposes of this insurance and incorporated in the schedule, the insured shall be considered as being his own insurer, for the difference, and shall bear a rateable share of the loss accordingly."

Rate generally charged as a percentage of Full Premiums (guidelines)

Selected % of Full Value Cover	**% of premium on Full Value**
75%	90%
65%	85%
50%	70%
25%	50%

Exclusions

- Gold/silver articles, precious stones, curios, manuscripts etc., unless specifically insured.
- Loss or damage where an inmate or a member of the

Insured's household is involved/business staff is concerned as principal or accessory.

- Loss or damage recoverable under fire or plate glass or motor insurance policy.
- Riot, Strike, Civil Commotion, Terrorist Activities, EQ, Flood Storm & Cyclone
- Loss or damage where business staff is associated.
- Loss resulting from any act committed by any other person lawfully on the premises.
- Which could be insured against by a fire, plate glass or motor insurance policy.
- Loss to deeds, bonds, BR, Promissory Notes, cash, treasury notes, bank notes, cheques, securities, stamps, books of accounts, manuscripts.
- Riot & Strike, Consequential loss, wear and tear.
- War & war like Operations.
- Nuclear perils.
- Cash or other property abstracted from safes (linked with key clause – not covered unless key/duplicate belonging to insured has been obtained by violence, threat, use of force against person/property.

Definitions of Various Terms in the Policy

- The act of breaking and entering a dwelling at night to commit a felony (as theft); broadly the entering of a building with the intent to commit a crime;
- The crime of entering a building illegally and stealing things from it;

- Felonious entry of insured premises by violent forcible means; Theft by person in premises who subsequently breaks out by violent forcible means – leaving visible marks;

- Cover is for theft of property after actual forcible and violent entry into the premises or theft followed by actual forcible and violent exit. It also covers risk of hold-up;

- **Housebreaking** (IPC..S.445): Committing house trespass by one who enters into a house and quits after committing offence;

- **Theft** (IPC..S.378); Taking away any movable property dishonestly out of the possession of any person without his consent;

- **Robbery** (S.390); Causing or attempting to cause to any person death, hurt, restraint, fear for theft or carrying away property. Aggravated theft;

- **Dacoity** (S.391): Robbery by five or more persons;

Burglary in policy includes theft upon felonious entry by violent and forcible means. Visible marks of entry or exit.

Bankers' Blanket Indemnity Insurance

Scope

The policy provides indemnity for any direct loss of money or security sustained by the bank (insured) and discovered during policy period.

- Money

- Bank notes

- Bullions, coin, currency

- Jewellery, precious stones, ornaments

- Revenue stamp etc

Indemnity

- On Premises
- In Transit
- Forgery or Alteration
- Dishonesty
- Hypothecated goods
- Registered postal sendings
- Appraisers

Bankers' Indemnity Insurance- Security

- Bank money orders
- Bill of exchange
- Bill of lading
- Bonds
- Certificate of Deposits
- Certificate of Shares
- Cheques, coupons, debentures, DDs
- Postal Order, FD, etc.
- Insurance deposited by insured

Bankers' Indemnity Insurance Employee

- All existing employees (Officers, clerks and sub staff)

- Permanent/temporary
- Full time/part time
- Contract/otherwise
- Apprentice
- All on salary roll but not director or partner of the bank

Definitions of Risks Covered

A. **On Premises** – Money or securities on own premises of the banker being lost or destroyed by fire, riot, strike, burglary, housebreaking, theft, robbery or holdup even by the employees.

B. **In Transit** – Money/security being lost, stolen, misled, misappropriated while in transit in the hands of the employees (also negligence or fraud of the employees).

C. **Forgery/Alteration** – Payment of bogus fictitious forged or raised cheques or drafts, payment of genuine cheques, drafts or FD bearing forged endorsement. The cover is operative irrespective of weather, set instruments, a receipt over the counter or through clearing house or by mail.

D. **Dishonesty —** The criminal act of an employee of the insured with respect to the loss of money/securities wherever committed and whether singly or jointly with others

E. **Hypothecated Goods** – Fraud or dishonesty of the insured employees in respect of gods/ commodities placed or hypothecated to the bank.

F. **Registered Postal Sendings** – Loss by robbery or theft dispatched by registered insured post from the bank to the consignee (10 per cent of the SI or 50000 whichever is less).

G. **Appraisers** – Loss due to inferiority or criminal act of the appraisers who are on the approved list.

H. **Janata Agents** – Loss due to inferiority or criminal act of Janata Agents/Pygmy collectors who are regular part time agents of bank appointed after full scrutiny.

Excess and Exclusions

- Compulsory excess - 25 per cent of loss or 2 per cent of basic SI whichever is higher but not exceeding Rs 5000, Rs 50,000. Rs 25,000 for small, nationalized and other banks.

- Excess will not apply to loss or damage by fire, riot, strike, burglary and housebreaking.

- Excess 25 per cent for each and every claim for next three covers.

- Loss of money or securities due to wrongful act of directors or partners.

- Loss of any property or securities confined to the care of bank but the value and description not ascertained by the bank before loss.

- Trading losses – Whether or not within the knowledge of bank.

- Loss caused by war and allied risk.

- Loss attributable to computer software or EDP.

- Loss caused by earthquake, typhoon, cyclone, flood

- Loss caused by nuclear weapon, material, fuel etc.

- Loss due to acts committed by the concerned employee after discovery of the loss in which the same employee had been involved.

Underwriting Considerations

- Sum-Insured —Insured to select basic SI applicable to first five covers of the policy and SI of last three covers as the percentage of basic SI.

- Rating —Basic SI and number of employees and others including appraisers, janata agents etc., at the beginning of FY.

Rating

(a) Guide Rates for Basic Cover on Basic Sum-insured:

o Small Banks….	4 per cent of Basic SI
o Nationalized Banks…	8 per cent of Basic SI
o Co-operative Banks and Foreign banks	6 per cent of Basic SI

(b) Staff Loading; 5 per cent (maximum) for normal increase;

(c) Rating varies with the size of banks (small and large) Nationalized banks and others etc;

(d) When claim experience is above 70 per cent, the risk will be reviewed for rating at the time of renewal;

(e) It is permissible to increase limits under items A & B in Standard Policy Form by payment of appropriate additional premium;

(f) Additional Premium for additional cover for Flood inundation and earthquake;

(g) Admissible Discounts on Lesser Number of Branches covered:

No of Branches	Discount
Up to 50	20 per cent

51 to 100	15 per cent
101 to 250	10 per cent
251 to 500	5 per cent
Above 500	Nil

As number of branches increases, the control and supervision become less effective. So generally no discount is allowed for banks having branches exceeding 500.

Conditions

Generally this policy is issued with the following conditions:

- Investigation and assessment by chartered accountant in case of accident;
- Loss not discovered within the period of the insurance will not be admissible;
- In the event of non-renewal or cancellation of the policy for losses not discovered within 6 calendar months next following the date of expiry or the date of cancellation is not admissible;
- Loss not sustained within retroactive period not exceeding 2 years from the date of discovery is not admissible;
- Indemnity is provided on discovery basis not on concurrence basis;
- Cancellation with 15 days notice either side is provided as clause;
- Refund of premium on pro rata basis on cancellation by insurer;
- Refund of premium on short period basis on cancellation by the insured is available;

- Reasonable steps taken by bank to safeguard the property insured and secure all doors, windows;
- Audit of accounts; and
- Adjustment of money due to employees while settling the claim on the policy.

16

LIABILITY INSURANCE UNDERWRITING

Liability Insurance – A Specialized Underwriting

One of the emerging risks is the Liability Risk. Liability insurance covers the legal liability of the insured for their act of negligence or breach of duty either under common law or under specific enactment. Liability insurance covers only civil liability, but not criminal liability. Unlike property insurance, liability insurance is very critical in nature in view of the various factors like its intangibility, liability from the third party, difficulty in determination of sum-insured, depending on legal jurisdiction, difficulty in determination of indemnity limit, absence of statistical or technical data required for rating or deciding the terms, conditions or warranties of the policy and so on. The nature and amount of liability depend on the judgment of court, which cannot be predicted or forecasted for assessing the loss forecasting. The increasing public awareness about their legal rights against the act of negligence or nuisance of others is giving rise to the larger amount of court awards unlike before. The product liability and, D&O liability and professional liability are some of the major areas that individuals and organizations are encountering with larger amount of court awards for their act of negligence or nuisance.

The courts in various parts of countries are pronouncing verdicts for different amounts of awards against the same or similar nature of negligence or breach of duty. Neither the insured nor the insurer can predetermine the frequency or severity of loss like the property insurance in view of the past losses data. The evolving civilization and the modernization of life have been increasing the tendency for higher frequency and severity of liability losses or award as it appears from recent court judgments.

Liability Insurance vs. Property Insurance

Liability policy also covers the insured's strict liability or vicarious liability arising from negligence or breach of duty of his employees and others under his care and supervision it is very difficult for the insured and the insurer to properly predict the sources of the liability and the gravity of negligence impacting the amount of liability awards and claims. Thus liability insurance underwriting is a specialized underwriting based sound knowledge and skill of the underwriters' about legal, technical, social and financial aspects, which will be discussed in general as well as in particular for the product concerned hereinafter. Property Insurance Underwriting is based on basically on COPE study while Liability Insurance requires CASE Study. COPE implies Construction. Occupation, Protective Measures and External Exposures, which have been discussed in property insurance, CASE implies Circumstances, Activity, Security and Event, which will be discussed in detail hereinafter.

Sources or Origin of Legal Liability

Liability arising from the following sources may be covered by various insurance policies to provide protection to civil wrong doers either individual or enterprise:

i. **Common Law/Law of Tort** gives a person the right to claim damages against injury or loss sustained by him from negligence, nuisance or trespass from the wrong doer. Tort also includes libels and slanders, but they are not covered by all liability policies.

ii. **Statutory Law** brings liabilities to insure. For example, Public Liability Insurance Act 1991, The Motor Vehicles Act 1988, The WC Act 1923, etc., are some of the important enactments that necessitate purchase of Insurance policies to meet our legal liabilities to third parties and employees.

iii. Breach of Contract (not willful) giving rising to violation of right created by an agreement enforceable at law.

Tort is a civil wrong for which the remedy is a common law of action for un-liquidated damage. The law of tort is a part of common law implying some breach of duty usually – the general duty that lies on all sections of society to take care that no injury or damage is caused to other people. A breach of contract is normally less frequent cause of claims than the tort. The breach of duty under common law is common for all liability insurance while the liability from the breach of contract is considered only in professional indemnity insurance policy or errors and omission insurance policy. The underwriter must understand the breach of contract and tort properly before he underwrites liability risks through any policy. Law of tort is basically a law of negligence being the foundation of legal liability in most of the cases.

What is Negligence?

As mentioned above, negligence is the most common form of tort, which is found to be covered by all liability insurance policies. Now question comes: what is negligence for which action can be initiated against the negligent person? Negligence is failure to exercise due care in a case where a duty of care exists. Negligence may arise from any of the following breaches of duty:

Negligence under Common Law

Every citizen under any common law has the duty to take reasonable care or exercise reasonable skill so that his action does not harm others. In **Blyth vs. Birmingham Waterowrks Co.** (1856) negligence has been defined as the omission to do something which a reasonable man guided by those considerations which ordinarily regulate the conduct of human affairs would do, so or doing something which a prudent reasonable man could not do. Lord Atkin in a leading case namely **Donoghue vs. Stevenson** (1932) observed that "… the rule that you are to love your neighbour …who, then in law is my neighbour? The answer seems to be persons who are so closely and directly affected by my act that I ought reasonably to have them in contemplation as being so affected when I am directing my mind to the acts or omissions, which are called in question"

Later on he in another case further emphasized "Every person…is under Common law obligation to some persons in some circumstances to conduct himself with reasonable care so as not to injure those persons likely to be affected by his want of care" The above legal decisions have precisely described the nature and extent of our liability arising from negligence and breach of duty under common law. We all owe to others for our every activity in the society and thus liability insurance policy to transfer our liability risks to others.

Negligence under Contract

A breach of duty arising from the express or implied terms contract to take reasonable care and skill in the performance of the contract constitutes a negligence giving rise to a right to the other party to bring action against the negligent party.

Negligence under Statute

A beach of common duty of care imposed by PLI Act 1991, Sales of Goods Act, WC Act 1923, Companies Act or any other specific enactments in vogue in India, SEBI Regulations or any other regulations imposing specific duty of care for others. Negligence or breach of duty as explained above does not automatically involve liability unless there is an action for damages and the following conditions are proved by the plaintiff in his action:

- The defendant was under a duty to exercise care towards the plaintiff
- There was a breach of that duty
- The plaintiff sustained damages from such breach.
- The breach of duty is the proximate cause of the damages.

When a plaintiff in an action for negligence suffers no damage to his person or property, the common law does not permit him to recover notional loss except under the cases of economic loss or financial loss in certain cases. In **SCM vs. WJ Whittall and Sons (1970) —** a contractor cut an electric cable running alongside road and supplying electricity to the plaintiff's factory. The plaintiff's action for damages included:

(a) £368 for loss of metal in the course of processing,

(b) £400 loss of profit which would have been made on the metal and

(c) £1767 the estimated profit that could be made on further lots of metal, which would have been processed in the time, it took for restoring the electricity supply.

It was held that only £368 for loss of metal and £400 loss of profit thereupon were recoverable, but not £1767 being remote and indirect economic loss.

Imputed Negligence

Under certain circumstances, the negligence of one person may be attributed to another. For example the negligent act of an employee may be imputed to the employer. Due to negligent act of a nurse causing injury to the patient the doctor or surgeon is held liable legally. This is also called Vicarious Liability law by which a motorist's negligence is imputed to the vehicle owner. Imputed negligence may arise in partnership business or joint venture business. Liability arising from imputed negligence is also covered in liability insurance.

What is Nuisance?

It is a wrong done to another person by unlawfully disturbing him in the enjoyment of his property or in the exercise of common right. Nuisances are divided into two groups: Public and Private.

Public Nuisances

This generally do not fall within the purview of law of torts except in particular case constituting some form of tort under common law. Keeping a house disorderly, throwing fireworks in the street, selling food unfit for human consumption. A member of public who suffers damages over and above the inconveniences suffered by public at large may sue the wrong doer under public nuisance, which is criminal offence.

Private Nuisance

This is interference for a substantial length of time by owner or occupier of property with the use or enjoyment of neighboring property. Interferences with rights that are actionable may be exemplified as wrongful disturbance of rights to land, lights, air, water, rivers etc. Wrongful act of causing noxious things such as smoke, smell, noise etc

A nuisance to be sustainable in an action must have two features namely **Injuria** and **Damnum.** The former refers to a wrongful act that constitutes or causes damage, while the later implies that damage or loss actually suffered by the plaintiff. No action for nuisance will sustain unless actual damage is caused and suffered. Mere discomfort or inconvenience is not actionable unless it is substantial. **Trespass** is a wrongful act committed with force or violence on the person, property or relative right of another. Thus if a person collides with another, it will be a trespass to the person who may suffer damage as a result of collision by the defendant. However trespass to be fit for action and to be covered by liability policy must be negligent act.

Scope of Liability Insurance

All individuals and organizations exposed to liability from third party may obtain protection under various types of liability insurance policies. Liability insurance policies provide indemnity to the insured for his **legal liability**, which may arise under common law, under statute, or under contract to other persons including customers, employees and the public at large being affected various activities of the insured. There are different types of liability insurance policy. One particular type of risk may be covered by a specific policy like public liability policy and product liability policy, etc., or a combined policy like commercial general liability policy may be issued against several eventualities. The following are the major liability insurances available in India:

- Public Liability Insurance
- Product Liability Insurance
- Professional Liability Insurance
- Aviation Liability Insurance
- Motor Third Party Liability Insurance
- Commercial General Liability Insurance
- Employers' Liability Insurance
- Directors & Officers' Liability Insurance
- Errors & Omission Liability Insurance
- Clinical Trial Liability Insurance
- Stock Brokers Liability Insurance
- Insurance Brokers' Liability Insurance
- All these insurances have been discussed in details in subsequent chapters

Fundamental Principles of Liability Insurance

Fundamental principles of insurance- Utmost good faith, Indemnity, insurable interest, subrogation and contribution will apply to liability insurance with same basis as in property insurance.

Utmost Good Faith

Under the principle of utmost good faith, every proposer for insurance must disclose to the insurer all material facts about the risks offered that he knows or ought to know. Every circumstance, information or particular which would influence the judgment of a prudent underwriter in deciding on acceptance of risk, determining premium and fixing terms and conditions is considered to be material fact. For underwriting liability insurance insurers require duly completed proposal form with a lot of questionnaires, which help the underwriters to identify, analyze and evaluate risks for taking decisions on acceptance of the risks with appropriate terms and conditions and right amount of premium. The proposal form normally incorporates a declaration to the effect that the particulars therein are true and correct and the proposal and declaration shall be the basis of the contract. The insurers may treat the contract void able and repudiate the claim if the due to non-disclosure or misrepresentation of some material facts. Liability policy is normally issued for a period of one year. This means that each time a policy is renewed is a new contract and the insured is under duty to disclose all material facts every time (Stokell vs. Heywood.1897). So renewal notice should contain a warning about the duty of disclosure including the necessity to advise changes affecting the policy which have occurred from policy inception or last renewal date whatever applicable.

Insurable Interest

A person seeking liability policy must have in any liability that he may incur, for his payment of compensation for damages caused to others expose him to financial loss. Therefore, if a policy purports to cover liabilities by persons other than the insured, it is to be examined whether the insured was acting as an agent for the other person or whether the insured has the insurable interest in the performance of other person. For example, a D&O Liability Insurance Policy is taken by a company for its directors and officers while E&O liability insurance policy is taken by a hospital or medical establishment.

Essentials of Insurable Interests

- There must be some potential liability, which may devolve on proposer;
- This liability or interest will be the subject matter of insurance; and
- The insured must stand to benefit by the absence of liability or to suffer financial loss from the occurrence of liability.

Indemnity

The principle of indemnity is also a fundamental principle in liability insurance as in property insurance. The insured may recover his actual loss subject to the indemnity limit specified in the policy. All liability insurances are contracts of indemnity and the amount payable on the happening of an event insured against is limited to the extent of the insured's financial loss or indemnity limit whichever is less. Very importantly liability insurance covers only legal liability, but not any moral liability.

Subrogation

The principle of subrogation which is a corollary of indemnity applies in liability insurance. For example, an insured may be liable for the negligent act of his employee. If the insurers pay the loss, the insured's right against the employee will be transferred to the insurers. The insured cannot recover both under insurance policy and from the negligent performer and make profit out of his loss. During underwriting and issuance of policy, the underwriter must be careful about the insertion of the express subrogation condition in the policy apart from implied condition in empowering insurers to exercise subrogation right even before settlement of claim by way of requiring the insured to give all assistance and stating that the insurer may act in the name of the insured.

Contribution

Contribution is a corollary of indemnity. It is inserted as one of condition in every liability policy with wording like “If at the time of any loss, damage or liability arising under this policy, there shall be any other insurance covering such loss, damage or liability or any part thereof, the company shall not be liable more than its rateable proportion thereof.” To apply this principle, consideration must have the following aspects:

- The same interest
- The same subject matter
- The same peril
- The same period of time

Types of Cover in Liability Policy

Liability policy can be classified into a) Claim-Made Liability Insurance and b) Occurrence Liability Insurance in view of the nature and extent of liability of the insurer to the insured in terms of a liability policy

Occurrence Based/Trigger Liability Insurance - Basic Features

The bodily injury or property damage must occur during the policy period. This policy applies to a legal liability of the insured for a particular claim even if made until many years after the policy ends but that particular injury or property damage must occur during policy period. So, only condition to be complied for determining the liability of the insurer to the insured is occurrence of accident from insured perils during policy period. Claims may come in any number of years after occurrence.

Example: M/s A& Co had been purchasing from Insurer ‘X’ with an inception date of 1st January 2000 which was the retroactive date. On 1st January 2004 the policy was purchased from Insurer ‘Y’ and on 1st January 2005 from insurer ‘Z’. On 1st July 2005 a claim was made by a customer against A & Co for an injury occurred on

1st October 2004 for the use of his product manufactured in December 2003. A & Co has been insured continuously under product policy. Now it is with insurer Z.

Question: Which insurer X, Y or Z is to pay the claimant's damage?

Answer: The events are depicted on a line below:

Product Mfd.	Injury occurred	Claim Made
2003	2004	2005

As the injury occurred in 2004 while insurer Y's policy was in effect, Y would respond the claim. The occurrence coverage trigger is easy to understand and apply to claims resulting from accidents that occur at a definite time, such as motor vehicle accident, fire explosion etc. But applying the occurrence trigger cover can be sometimes very costly and difficult to be managed like claims for disease resulting from prolonged exposures to asbestos after 40 years from occurrence.

Claim-made Liability Policy

To address the problems of Occurrence Based/Trigger Liability Insurance insurers have developed Claim-made policy to pay claims that are first made during period of insurance. Under this policy the insurer will not be liable to the insured for any legal liability incurred by him unless the third party makes claim within the period of insurance. In almost all countries Claim-made version of liability policy is widely used for limiting their liability and ensuring prudent underwriting in view of loss forecasting.

A major problem posed for insurers by these long-tail claims is that their ultimate cost cannot be accurately predicted when they calculate or develop the premium for such policy. The insurer may not realize that the product or the accident from business activity of the insured can cause latent injury and the unanticipated claims for many years in future may be subject to liberalized law or monetary inflation. Consequently premium charged by the insurer is inadequate to pay covered claims. Now the most of liability policies (public, product professional Indemnity) are issued on claim-made basis instead of occurrence basis all most everywhere unless it is specifically required and agreed by insurer on special considerations.

Retroactive date & Claim-made Policy

A retroactive date is very vital in a liability policy and is more vital in a Claims-made policy. There may be a situation where a claim made policy may contain:

- No retroactive date,
- A retroactive date (same as the policy inception date) or
- A retroactive date that precedes policy inception date.

The above three situation will imply different nature of liability of the insurer to the insured in respect of his legal liability as explained below briefly.

If it has no retroactive date, the policy will cover claims first made during the policy period regardless of when the injury occurred. If it has a retroactive date, the policy will cover claims first made during the policy period only if the injury occurred on/after retroactive date.

Once a retroactive date has been established, insurer may not advance the retroactive date without the consent of the insured, and may do so if any of the following has occurred:

- The insured has changed insurers.
- The insured's operations have changed substantially.
- The insured failed to provide the insurer with material information.
- The insured has requested the change.

If a retroactive date is advanced in a new or renewal policy, the new policy will not cover claims made during the new policy period if the injury occurred before the retroactive date shown in the new policy. However, the claim may be covered under the extended reporting period provisions of an earlier claims-made policy.

Public Liability Insurance

It covers the Legal Liability of the Insured towards the damages to the third party for death/injury/diseases and property damage due to accidents up to the limits specified in the policy. There are three types of public liability Insurance: i) Public Liability Insurance Act Policy; ii) Public Liability Industrial Risk Insurance; and iii) Public Liability Non-industrial Risks Insurance.

Public Liability Act Policy (PLI Act, 1991)

It is a compulsory insurance for the firms and individuals owning or handling hazardous materials. The Preamble of the Act states: “An Act to provide for public liability insurance for the purpose of providing immediate relief to the persons affected by accident occurring while handling any hazardous substances and for matters connected therewith”. As per Section 3 the owner shall be liable to give relief as specified in the Act for death or injury to any person (other than workman) or damage to property arising out of an accident. It is on No-fault basis. Claimant is not required to prove that accident was due to fault of any person. Examples of certain hazardous materials are: i) Toxic Chemicals like Amition, Benzedrine, Benzedrine salts, Crimidine, Fluroacetic acid, salts, Chloromethyl, Ammonia, Chlorine etc; ii) Highly Reactive Substances like Acetylene, Hydrogen, Propylene oxide, Methyl ethyl, Liquid oxygen etc; and iii) Explosive Chemicals like Cellulose nitrate, Barium aside, Mercury fulminate, Nitroglycerine. Like these there are more than 400 chemicals for which the individuals or firms require Public Liability policy under PLI Act 1991 if they handle these chemicals for production, processing, treating, and transporting etc.

Scope and Cover

All firms/individuals owing/dealing with hazardous goods are required to take this policy satisfying the limits specified in the Act. The policy covers Legal liability of the insured towards damages of the third party in respect of death/injury/diseases and property damages due to accident the specified insurance Limits called AOA (Any One Accident) and AOY (Any One Year). AOA will be equal to Paid up Cap (Maximum Rs 5crores) and AOY is 3 times of AOA and Max Rs 50 crores. Rule 10 provides maximum aggregate liability of the insurer to pay relief to several claimants shall not exceed Rs 5crores for AOA and Rs 15 crores for AOY.

Compensation Per Person

Fatal Accidents: Rs 25,000 + Medical Expense up to Rs 12,500

Injury: Per cent of Disability + Medical Expenses as above

Loss of Earning: Rs 1000 per month if hospitalized for more than 3 days

Property Damage: Rs 6000

Exclusions

- Liabilities from willful non-compliance of any statutory provision
- Fines, Penalties, punitive/exemplary damages awarded by Court
- Liability arising from any other legislation
- Damages to the property owned/ leased by the insured
- Damages caused directly or indirectly by war, invasion, act of foreign enemy, civil war, rebellion, revolution insurrection or military power, etc.
- Loss or damages caused or contributed by ionizing, radiation or contamination by radioactivity from any nuclear fuel or west

Premium Computation

It has two components: a) Indemnity Premium based Indemnity Limit (AOA) and b) Turnover Loading based turnover amount. Indemnity Premium is calculated as follows:

Indemnity Premium Indemnity Limit (Rs)	Rate per % (Rs)	Indemnity Limit	Rate per % (Rs)
Up to 1.0 lakh	0.70	Up to 2.5 lakh	0.75
Up to 5.0 lakh	0.80	Up to 10 lakh	0.85
Up to 50 lakh	0.95	Up to 100 lakh	1.00
Up to 250 lakh	1.05	Up to 500 lakh	1.10

Table-34: Turnover Loading for Premium

Turnover

Up to Rs 1crore	Rs 0.12 p.m. Minmum Rs 12
Beyond Rs 1 cr up to Rs 5 cr	Rs 1200+0.084%
Beyond Rs 5 cr up to Rs 10 cr	Rs 4560+0.072%
Beyond Rs 10 cr up to Rs 50 cr	Rs 8160+0.060%
Beyond Rs 50 cr up to Rs 100 cr	Rs 32160+0.048%
Beyond Rs 100 cr up to Rs 250 cr	Rs 56160+0.036%
Beyond Rs 250 cr up to Rs 500 cr	Rs 1101600+0.010%
Beyond Rs 500 cr up to Rs 1000 cr	Rs 135160+0.0075%
Beyond Rs 100 0cr up to Rs 2000 cr	Rs 172660+0.0050%
Beyond Rs 2000 cr	Rs 222660+0.0025%

Thus total premium is the aggregate of indemnity premium and turnover loading.

For manufacturing units, turnover means Annual Gross Sales of all goods including all levies and taxes including Godown Warehouse owners-Total annual rental receipts, and for Transport operators, it is the total annual freight receipts and others and total annual gross receipts.

Major Industrial Accidents in India

Apart from Bhopal Gas Tragedy in 1984 where thousands of people injured/died there are many chemical explosions and accidents which deserve special mention for appreciating the importance of this vital liability policy in India. Table-35 shows a few examples of such accidents

Table-35: Major Industrial Accidents in India

Year	Industry and Place	People Affected	Nature of Accident
December 1985	Sree Ram food & Firtilizers, Delhi	502	Oleum Gas Leak
July 1987	Bhorari Industrial Area, Pune	420	Sulphur Trioxide leak
June 1987	Industry in Bhubaneswar, Orissa	4	Amonia Gas leak
November 1987	Industry in Ahmedabad, Gujrat	5000	Oleum Gas Leak
May 1988	Industry in Ahmedabad, Gujrat	72	Acid tanker overturned
October 1989	Industry in Ganjam in Orissa	106	Chlorium gas
November 1990	Indian Petro Chemical Ltd Maharst	85	Explosion in gas plant
November 1991	Gwalior Rayon& Silk M.P	109	Chemical Explosion

November 1991	Dhanu Maharastra	119	Chemical Explosion
April 1992	Nayabazr, Delhi	12	Chemical Explosion
September 1992	National Fertilizer	22	Ammonia gas leak
May 1993	Century Rayon, Maharastra	134	Sulphuric Acid Leak
October 1994	Jhansi, UP	85	Chemical Explosion

Recently there are any other chemical explosions for which business houses have been exposed to public liability risks.

Public Liability Insurance (Industrial Risks)

Scope and Cover

(a) **Legal liability** of the insured towards damages to the third party in respect of death/injury. Property Damage arising out of accident occurred in the policy period in the manufacturing units or storage place such as go downs, depots, tank farms, etc., for the claims made by the third party against the insured in the period of insurance. Such policy may cover more than one manufacturing or storage units.

(b) **Legal costs** and expenses incurred with the prior consent of the insurer are also covered by such policy.

Above liability is subject to limits of indemnity being AOA and AOY and other terms and conditions of the policy. Such policy is not issued with unlimited liability.

(c) **Ratios** of AOA and AOY may be any of 1:1, 1:2, 1:3, and 1:4

(d) **Pollution Risks**

A standard policy does not cover pollution risks. It can be covered with additional premium and specified endorsement. Such cover is subject to following conditions;

- Submission of additional information as per questionnaire to the proposal form.
- Submission of certificate from Pollution Control Board grating permission to carry on such business.

(e) **Transportation Risks** The policy does not cover TP liability arising out of transportation of hazardous and dangerous substances unless specifically declared and covered by endorsement with payment of additional premium.

(f) **Retroactive Date:** As mentioned earlier the policy must specify the retroactive date which is generally the date when risk is first incepted under a claims-made policy and there from renewed without break in the total period of insurance. There will not be any liability before the retroactive date mentioned in the schedule of the policy.

Classification of Risks

For the purpose of rating the risks properly, manufacturing risks are broadly classified into following groups. It can be further sub-classified according to the underwriting policy of the insurer for the convenience of rating the public liability risks of industrial sector. Table-36 provides an example of such classification.

Table-36: Classification of Risks

Group	Industry
Group 1	Biscuit, Coir, Glass& Ceramic, Silk etc.
Group 2	Breweries, Cigarette, Shoe, Sugar, Textiles, Woolen etc
Group 3	Distilleries, Manmade yarn/fiber making, Paper & cardboard mills, jute mills
Group 4	Celluloid, Fertilizer, Match, Petroleum Refinery, petrochemicals, rubber

Rating Risks

Rating is based on the following five factors:

- Risks Group
- Basic Indemnity Limit
- Ratio of Indemnity Limits (AOA: AOY)
- Annual Turnover
- Number of units

We have to examine now how the above factors will be applied here.

(a) Indemnity Premium

Table-37: Basic Rate Percentage for the Risk Group and (AOA: AOY)

Risk Group	1 : 1	1 : 2	1 : 3	1 : 4
1	0.15	0.22	0.27	0.30
2	0.18	0.26	0.32	0.36
3	0.21	0.30	0.37	0.42
4	0.24	0.34	0.42	0.48

We understand greater the ratio and higher the Group, higher is the Rate. The above rate is basic rate, which will be adjusted with specified multiplier for required indemnity limit, number of units in order to arrive at the indemnity premium.

Table-38: AOA Limit & Multiplier

AOA Limit (Rs in lakh)	Multiple	AOA Limi (-Rs in lakh)	Multiplier
Up to 10	28	Between 301 and 350	17
Between 10 and 25	26	Between 351 and 400	18
Between 25 and 50	25	Between 401 and 450	15
Between 51 and 75	24	Between 451 and 500	14
Between 76 and 100	23	Between 501 and 600	13.5
Between 101 and 150	21	Between 601 and 700	13
Between 151 and 200	20	Between 701 and 800	12
Between 201 and 250	19	....	
Between 251 and 300	18	Between 5000 and 10750	7.50

To arrive at the applicable indemnity rate we are to multiply the basic rate in Table-37 with above multiplier. Again the applicable indemnity rate will be adjusted according to multiplier for the units applicable as shown in Table 39.

Table-39: Multiplier for Multiple Units

AOA: AOY / Units	1:1	1:2	1:3	1:4
1	1.00	1.00	1.00	1.00
2	1.35	1.50	1.60	1.75
3	1.50	1.70	2.00	2.20
4	1.65	1.90	2.25	2.80
5	1.80	2.05	2.50	2.80
10	2.00	2.50	3.00	3.50
15	2.00	2.50	3.15	3.75

After applying the above multiplier we will arrive at the final rate of indemnity premium.

(b) Turnover Loading

Turnover loading will be calculated as shown in Table-40 to be applied on the projected turnover of the insured.

Table-40: Turnover Loading

First Rs 1 crore	**Rs 1000 (min)**
Above 4 cr to 5 cr	Rs 1000+0.07%o on balance
“ Rs 5 cr to Rs10 cr	Rs 3800+0.06%o on balance
“ Rs 10 cr to Rs50 cr	Rs 6800+0.05%o on balance
“ Rs 50 cr to Rs100 cr	Rs 26800+0.04%o on balance
“ Rs 100 cr to Rs250 cr	Rs 46800+0.03%o on balance
“ Rs 250 cr to Rs500 cr	Rs 91800+0.02%o on balance
“ Rs 500 cr	Rs 141800+0.01%o on balance.
# This Table is For Gr.1	#For Gr.3—120%of Gr.1prm
#For Gr.2–110%of Gr. 1	#For Gr.4—140%of Gr.1 pm

(c) Method of Calculation of Premium

Table-41: Method of Calculation of Premium

A	Basic Rate (Table-1—Risk Group &AOA:AOY	*
B	Apply multiplier (Table-2)for AOA limit on (a)	*
C	Apply multiplier (Table-3)for multi units on (b)	*
D	Add: Turn Over Loading	*
E	Add: Pollution Extra	*
F	Add: Pollution Extra	
G	Basic Premium	**
H	Turnover Loading	*
I	Pollution Extra @50% of (1+2)	*
J	Net Premium	****

Example: Application of above underwriting aspects of Public Liability insurance (Industrial Risks Following particulars are obtained from the proposal from of ABC Ltd for underrating:

- Fertilizer Manufacturing Company
  - o Number of Units-5
  - o Projected Turnover Rs 250 crore
  - o AOA—Rs 40 lacs
  - o AOA:AOY=1:4
  - o Extension required; Pollution Risks

Premium Calculation

As per earlier tables and discussion, the Fertilizer Manufacturing Company will come under risk group 4 where Basic Rate is 0.48 per cent. Now AOA Limit of Rs 40 lakhs will be broken into following for appropriate multiplier:

(a) Multiplier:

AOA Limit	Multiplier
Up to Limit Rs 25 lakhs-	26
For Balance Rs 15 lakhs-	-25

(b) Adjustment of Basic Rate

(a) Rate up to Indemnity Limit Rs 25 lakhs — 0.48*26 per cent =X

(b) Balance Indemnity Limit Rs 15lakhs — 0.48*15 per cent =Y

Indemnity Premium (single Unit) = X+Y

Application 2

(i) Insured ………………….Jute Mill, ABC Ltd.

(ii) Number of Units-………..4

(iii) Turnover ……………….Rs 300 crores

(iv) AOA …………………...Rs 30 lakhs

(v) AOA:AOY…………….I:3

(vi) Extension- Pollution Risks

Premium Calculation

i) Risk Group- 3, ii) Basic Rate-0.37 per cent iii) Multiplier for AOA Limit Rs 30 lakh):

Up to Limit Rs 25 lakhs- — 26; For Balance Rs.5 lakhs - —— 25

a) Rate up to limit Rs 25 lakhs —0.37*26 per cent =9.62

b) Balance Limit Rs 5 lakhs — 0.37*25 per cent =9.25

a) Indemnity Premium

Rs 25 lakhs X 9.62	= 24050	
Rs 5 lakhs X 9.25	= 4625	Rs.28675
Indemnity Premium for 4 units (Rs 28675X 2.25)	= Rs 64,519 (A)	
Turnover Premium (Rs 91800+10000)	=101800	
Turnover Premium for Risk Group 3 (101800X120 per cent)	= Rs 12,21,60 (B)	
Pollution Extra 30 per cent of (64519+122160)	= Rs 56004(C)	
Total Premium (A+B+C)	Rs 2,42,683	

Public Liability (non-industrial risk)

Scope and cover

This policy cover legal liability of the insured to third party on account of accidental bodily injury/death/disease and/or loss or damage to their property arising out of claim made for any accident occurred during the policy period up to maximum liability being limits indemnity i.e. AOA and AOY specified in the policy. No policy can be issued with unlimited liability. The ratio of indemnity limits of AOA and AOY may be 1:1, 1:2, 1:3 or 1:4. The risks to be covered under this policy shall be non-industrial organizations including such as Hotels/Motels/Club Houses/Restaurant/Boarding and Lodging Houses/Guest Houses/Cinema Halls /Auditorium/ Theatre/Theatre/Public Halls/Office/Residential Premises/ Administrative Premises/Medical Establishments/Research Institutions/Laboratories/Airport Premises/School/Educational Institutions/Public Libraries/Exhibitions/Fairs and Fetes/Stadiums and Pandals/Permanent Amusement Parks/Film Studios (Indoor and Outdoor)/Circus/Zoo/Depots/Warehouse Godown/Shop/Tank Farm.

Extensions: Pollution, Transport Risks and AOG perils can be covered with additional premium and specific endorsement as standard policy does not cover these risks.

Premium – Rating Factors

- Type of Construction
- Occupancy/Storage
- Ratios of AOA:AOY
- Height of Building—if exceeding 22 metres, loading 10 per cent
- Risk Group
- Risk Group
- Turnover

- Addl. Premium: Height (beyond 22 metres); 10 per cent For Lifts and10 per cent of basic

Basic Rates (Guide Rates) per Mille

Table-41: Basic Rates for Various Gropus

Risk Group	Ratio of Indemnity AOA &AOY			
	1:1	**1:2**	**1:3**	**1:4**
1	0.15pm	0.22pm	0.27pm	0.30pm
2	0.18pm	0.26pm	0.32pm	0.36pm
3	0.21pm	0.30pm	0.37pm	0.42pm
4	0.24pm	0.34pm	0.42pm	0.48pm

The above guide rates will be decided by every company according to their own experience and underwriting policy.

Limit of Indemnity and Multiplier

Table-42: Limit of Indemnity and Multiplier

AOA Limit (Rs in lakh)	Multiple	AOA Limit (Rs in lakh)	Multiplier
Up to 10	28	Between 301and 350	17
Between 10 and 25	26	Between 351 and 400	18
Between 25 and 50	25	Between 401 and 450	15
Between 51 and 75	24	Between 451 and 500	14
Between 76 and 100	23	Between 501 and 600	13.5
Between 101 and 150	21	Between 601 and 700	13
Between 151 and 200	20	Between 701 and 800	12
Between 201 and 250	19	....	
Between 251 and 300	18	Between 5000 and 10750	7.50

To arrive at the applicable indemnity rate we are to multiply the basic rate in Table-37 with above multiplier. Again, the applicable indemnity rate will be adjusted according to the following multiplier for the units applicable.

Rate for the Multiple Limits

If more than one unit is covered by one policy, the above applicable indemnity premium rate will be multiplied by different multipliers as decided in the underwriting policy. Generally, the multiplier shown for industrial risks is followed for non-industrial risks for this purpose (see Table-42).

Turnover Loading

Turnover loading is added to the Indemnity Premium. The turnover loading is decided according to the rates decided by the individual company. However, it is calculated in the same method as is discussed under industry risks. Again such turnover loading is adjusted for risks group in the same method as provided in Table-43 below.

Table-43: Turnover Loading

Risk Group	Premium
2	110% of Group 1 premium
3	120% of Group 1 premium
4	140% of Group 1 premium

If more than one unit either in same location or different location are covered under single Indemnity Limit in a policy, either separate loading on turnover shall be applied as above each unit depending upon the risk group or on the total turnover treating all risks under the highest Risk Group.

Excess

Compulsory Excess: For all policies compulsory excess should imposed to reduce moral hazards. Generally, ¼ per cent of AOA limit subject to maximum of Rs 100,000 is decided for compulsory excess. The same also applies to both bodily injury and property damage claims inclusive of defense or legal costs arising out of any one accident.

Voluntary Excess varies from 1 per cent to 10 per cent for discount from 2.5 per cent to 15 per cent.

Short Scale

Policy for short period is granted with Short Scale.

Transportation Extension

On payment of additional premium it is extended like extension of pollution risks and AOG perils. If transportation limit is less than the Indemnity Limit of the policy, 50 per cent of the premium calculated for the premises indemnity will be applied.

Exclusions (Industrial & Non-Industrial Risks)

The public liability insurance both industrial and non-industrial risks do not cover the loss or damages arising out of accidents due to following perils:

- Contractual Liability
- Act of God Perils (can be covered as extension)
- Deliberate/willful non-compliance of statutory requirements
- Loss of pure financial loss, i.e. goodwill/market etc.
- Personal injuries like libel, slander etc.
- Infringement of plans, copy rights etc.
- Fines, penalties, punitive and exemplary damages
- War and nuclear perils
- Loss Prior to Retroactive Date

- Liability from Transportation of hazardous items (can be covered as extension)
- Use of aircraft, watercraft or hovercraft
- Damage to property owned/hired or in custody of insured
- Injury or Damage prior to Retroactive Date
- Deliberate disregard of reasonable steps to prevent claims
- Liability insurable under Workmen Compensation Act
- Liability which may be specifically covered elsewhere

Principal Clauses (Applicable to both industrial and non-industrial risks)

i. **Indemnity Clause:** The indemnity only applies to claims arising out of accidents occurring in the Insured premises during the period of insurance first made in writing against the Insured during the policy period and the insured is indemnified in accordance with Operative Clause for and/or arising out of injury/damage but only against the claims arising out of or in connection with the business specified in the schedule and not against claims arising out of or in connection with: a) Pollution howsoever caused unless specifically covered; and b) any product. Here injury means death, bodily injury, illness or disease of or to any person. Policy Period means the period the period commencing from effective date and hour and terminating on the expiry date as shown in policy schedule. Period of Insurance means the period commencing from the retroactive date and terminating on the expiry date. Retroactive Date means the date when the risk is first incepted and thereafter renewed without break Premises includes pipelines running outside up to 1 km from it.

ii. **Notification Extension Clause:** If the company accepts any notification of the insured during the policy period about any specific event or circumstances which may give rise to a claim which form the subject matter of indemnity by the policy, the company will deal with such claim as if they had been first made against the insured during the policy period up to the maximum time limit laid down in the Indian Limitation Act.

iii. **Extended Claim Reporting Clause:** In case of non-renewal or cancellation of policy, the company will allow a time limit not exceeding 90 days from the date of expiry or cancellation of the policy, provided no insurance is in force during the extended reporting period for same interest, for notification of claims for accidents which had taken place during period of insurance.

iv. **Indemnity Limits:** Company's total liability to pay compensation, defense costs, fees and expenses shall not exceed the Indemnity limit stated in the schedule. Indemnity Limit applies to any one claim or series of claim arising from one originating cause and to total liability of the company during policy period.

v. **Claim Series Clause:** All claims arising out of the same cause or error are to be aggregated & treated as one claim and no coverage for claims made arising from one specific cause which are made later than 3 years after the first claim of the series.

vi. **Compulsory Excess:** The insured shall bear as Compulsory excess the amount or percentage of the limit of indemnity per any one accident so stipulated. Such excess shall be applicable to both: a) death/bodily injury; and b) property damage inclusive of costs.

Product Liability Insurance

Product Liability Insurance is one of the very important liability insurances. Its importance is all the more rise in the process of global market and MNC operations.

Product Liability - International Perspectives

In the UK the product liability of the businessmen are generally decided in considerations of the following statutes over and above the common law which is the foundation of this legal liability:

- The Sale of Goods Act 1979 (consolidating earlier Act 1893 & Act 1973)
- The Supply of Goods (Implied terms) Act 1967
- The Misrepresentation Acts 1967
- Hire Purchase Act 1965
- The Consumer Credit Act 1974
- Unfair Contract Terms Act 1977
- Consumers Protection Act 1978

Similar enactments are there in other countries to make manufactures and dealers will be legally liable to customers and others for damage and injury arising out of product. In the US, Japan and other countries also similar enactments govern the product liability over and above the common law.

Product Liability - Statutes in India

The Consumer Protection Act 1986 and the Sale of Goods Act 1938 are important statutory enactments conferring on the buyer to claim damages for breach of duty. The Consumer can go to The District Forum, The State Commissions or The National Commission for compensation for damages in case deficiency of services under The Consumer Protection Act. Under the Sale of Goods Act, a seller has responsibility to ensure that the goods sold correspond with the description or the sample, if sale made by sample (Section 15). He has the responsibility to ensure that the goods sold are fit for the purpose (Section 6). He has the duty to ensure that in case of contract of sale by sample the goods shall correspond with sample and free from defects (Section 17). Section 59 gives right to the buyer to claim for damages for breach of contract.

Legal Aspects

All sellers of goods whether manufacturers or retailers, requirements, expectation, or suppliants of suppliers of credit, may incur legal liability. Public liability Insurance covers the legal liability for accidental injury to third party or damages to their property due to any act or negligence of the insured or his employees while Product liability Insurance covers Legal Liability for Injury (Death/ Disease) /damage to property caused by any goods manufactured/ supplied/treated/sold/repaired/altered/serviced in the country or abroad and accident occurred outside the insured's place or premises. General public Liability Policy excludes the liability for bodily injury or property damage arising out of the use of product at the customers' place. Product liability covers mainly:

(i) Liability in tort in Negligence or breach of duty for care

(ii) Statutory Liability (Imposed by law) but not contractual liability

Two case studies being Donohue vs. Stevenson (1932) and Fisher vs. Harrods Ltd deserve special mention to explain the operation of common law or law of tort for ascertaining the legal liability from negligence for manufactures along with the distributors or local dealers who sell goods to the ultimate customers.

Product Liability Risk Analysis and Underwriting

(i) Product Liability Risk Analysis

- The possibility; of a defective product causing injury, illness, loss or damage;
- The extent of possible injury, illness, loss or damage.
- The nature of the goods manufactured

All these will indicate to the underwriter the possibility of defective products causing injury, illness, loss or damage, while the uses of the products will enable him to assess the possible extent of any damage. It is essential that an underwriter know exactly what products are supplied and for what purpose they will be used. Sometimes engineering /electronic pharmaceutical products will not enable the underwriter to easily appreciate the extent of the risk or to apply a correct rating. It may be that the manufacturer or producer has no standard product and may manufacture a wide range of products to specific order. In this connection their brochures or advertising literature will be of considerable help. Where goods are produced to individual requirement the underwriter will require details of production for the preceding twelve months to see if any regular pattern can be established.

(ii) Risks Associated with Products not Manufactured

Where goods are supplied, rather than manufactured by the insured a confirmation that no contractual liability is involved, which may preclude the recovery from manufacturer is required to be examined by the underwriter. Many claims that fall to be dealt with by this type of policy arise from a breach of the conditions of fitness or merchantability implied under the Sale of Goods Act and it is important to know the part played by the proposer in the chain of supply. Claims made by the retailer under this heading will usually be recoverable from the wholesaler and by the wholesaler from the manufacturer. The latter may in turn have recourse to the supplier of components or perhaps somebody who has treated the raw material.

(iii) Design Risks

The standard cover provided for products liability insurance often excludes errors in design or formula. There is considerable demand for this cover and practice varies between insurers as to the extent to which they will provide it. Insurers are normally prepared to provide this form of indemnity in approved cases for a premium consideration, which will reflect the nature of the product, the degree of exposure and the experience and qualifications of those employees concerned with design, formula or specification. The following considerations are important for an underwriter to decide whether he would provide for these risks and if yes, on what terms:

- The length of the time the product has been on the market in the form currently used.
- Whether any change in the design is in the offing.
- The qualifications & experience of those entrusted with product design or formula.
- R&D policy, process and implementation.
- Quality Control system on product efficacy, side effects.

(iv) Classification of Risks

- Risks for Manufacturing Goods
- Risks for supply of raw-materials & imported goods
- Risks for Wholesale & Distribution trades
- Risks for retailers.

(v) Categorization of Risk in View of Relative Hazards

All products to be classified or categorized for risks classification and application of class rates in rating and deciding terms and conditions; Following are the common type of categorization of product risks:

- Paper, cardboard goods, soft furnishing
- Food drinks for human consumption with packaging quality
- Engineering products
- Electrical products

- Motor vehicles
- Plant & Machinery
- Electronic goods
- Animal Feeding staff
- Pharmaceuticals
- Aircraft products etc

Traditionally category 1 is relatively low hazard and category 10 has high claim hazard.

(vi) Other Underwriting Considerations

- **Cover:** Legal liability arising out of defective products manufactured in India up to the specified maximum limit of indemnity for liability arising within India. Exports from the US/Canada may be covered with Domestic Cover but with higher rates. This cover is granted subject to declaration of the insured as regards compliance of relevant statutory requirements such as ISI/ISO standards, Sale of Goods Act, PCB regulations etc.

- **Rating:** This is based on Annual Turnover, Indemnity Limits & Selected ratio of AOA: AOY.

- **Liability:** This is restricted to accidental bodily injury/death or property damage from use of product to third party.

- **Extensions:** Exports Vendors' liability for named ones and additional premium 5 per cent on limit of indemnity + loading on exports turnover. Unnamed ones with additional premium 10 per cent + loading.

- **Loading:** These are for three categories in case of exports or use of products in: i) US/Canada; ii) Organizations under economic co-operation development; and iii) Others

- **RBI Permission:** Policy is issued with pre condition that claim will be settled in Indian currency. In case settlement in foreign exchange is required, RBI permission is required.

- **Compulsory Excess**: ¼ per cent per accident and maximum per policy restricted to Rs 100,000.

- **Voluntary Excess:** 1 per cent to 10 per cent discount on premium varying from 2.5 to 15 per cent.

- **Retroactive Date:** As mentioned in the policy being renewed without break.

- **Cross Liabilities:** Each person/ party will be separately entitled for indemnity in respect of any claim made against them. This would however be restricted to limits of indemnity specified in the policy.

Exclusions

Following are the exclusions in a standard Product Liability Insurance. A standard product liability Policy does not cover or indemnify the following items:

- Repairs, replacements, modification of defective products

- Non-compliance of statutory orders/regulations, fines, penalty

- Loss of goodwill/market

- Loss due to War 7 allied perils

- Damage to property owned by or held by the insured

- Loss prior to Retroactive Date

- Loss from willful disregard of technical/administrative norms

- Loss due to contractual Liability

- Failure of the product for the purpose intended
- Product Guarantee

Conditions

Product Liability insurance is subject to following conditions:

- The insured is to serve a written Notice of loss or liability occurred to the underwriter immediately after accident followed by copy of writ summon.
- There will no admission of liability by the insured without prior consent of the insurer.
- The insurer has right but no obligation to defend. Defense cost is admissible under indemnity limit.
- Insured shall provide all assistance to the underwriter in conducting legal proceedings.
- Any change material to the risk is to be intimated to the insurer immediately.
- Policy and schedule are to be read and considered together for terms and conditions.
- Proper maintenance of records of the turnover for inspection by the underwriters.
- In case of double insurance Contribution Clause will apply like any other insurance.
- Cancellation clause with 30 days notice with the minimum retention being 25 per cent of the annual premium, but no refund if claim is intimated.
- In the event of claim there will be no reinstatement but reduction in indemnity limit.

- Benefits of the policy stand forfeited if claim is fraudulent.
- Cause of action could be within India except for export goods covered.
- For settlement of dispute interpretation will be as per Indian Law.

Manufacturers' and Vendors' Liability

All sellers or repairers of goods, whether they be manufacturers, wholesalers, or retailers, may incur liability to their customers and others for injury, illness, loss or damage arising from the supply of goods. In many cases, the goods pass through several hands, for example, manufacturer, wholesaler, retailer, before they finally reach the consumer and it is not possible to give any general rule as to where liability will ultimately rest; it depends on the circumstances in each case. While liability rests with the ultimate seller, a negligent manufacturer should not escape the results of his negligence. A purchaser might, therefore, claim from a retailer and the retailer in turn may succeed in passing the claim back to the manufacturer (assuming he is not precluded from so doing by a contractual agreement). Here the judgment of **Donoghue vs. Stevenson (1932**) is very important to decide the extent of legal liabilities of the related parties including manufacturer, wholesaler, retailer etc.

Territorial Limits

It is usual to offer cover for injury or damage occurring anywhere in the world. In view of the amount of export business involved it is essential for an insured to have a policy with as few restrictions as possible. It is, however, usually a requirement that the goods involved are supplied from the insured's premises, details of which have been given to the insurers. For a policy issued in this country this will mean premises in Great Britain, Ireland, the Isle of Man or the Channel Islands. An insured may manufacture abroad and distribute from overseas premises on a world-wide basis. He may export from this country to an overseas subsidiary – there are many possible variations. Where overseas premises are involved it is preferable for products liability insurance to be arranged locally.

Jurisdiction for Operation of Policy Operation

Some policies apply a clause which states that actions for damages must be brought in the courts of this country, that is, not overseas. Other insurers will provide full world-wide cover subject to the payment of appropriate premium. There can, however, be problems about jurisdiction, and these presently causing insurers much concern, especially in connection with claims from North America. If, for example, a claimant is domiciled in North America he can usually bring a claim there irrespective of where the accident or injury occurred. In underwriting product liability insurances, therefore, it is necessary to consider the amount of export business involved and the countries concerned. Considerably higher rates apply to North American exports because of the higher rates of damages awarded in America and the stricter liability which applies there to manufacturers and distributors.

Replacement of Defective Goods

The cost of repairing, renovating, replacing, or recalling unsuitable or defective goods are not covered. Some risks may be covered under a products guarantee policy.

Goods for Use in Aircraft, Hovercraft or Watercraft

This exception is not common to all insurers but there is a catastrophe risk involved in aircraft and ships. A small defective part might cause a plane to crash, and if a manufacturer is engaged in producing parts for aircraft and ships it is an important factor, which the underwriter must take into account.

Faulty Design/Formula

An exclusion of any claim arising through faulty or defective design or formula or the unsuitability of the goods for the purpose for which they were designed, is common. Cover against unsuitability is a matter for a products guarantee policy but depending on the type of product involved, cover is often given for the faulty or defective design risk. A professional risk should be insured under a professional indemnity policy.

Liability Assumed under Contract

It is normal to insure legal liability and not contractual liability with this class of business. If the exception is to be deleted it is essential to know exactly what contractual liabilities have been assumed. An insurer's liability is reduced if the insured is legally able to contract out of liability. Conversely, the risks are materially increased if, for example, a retailer is unable, because of a contractual agreement, to pass liability back to a manufacturer. It is better if each party accepts responsibility for their own acts of negligence.

Goods in Custody or Control of the Insured

It is customary to exclude liability arising while the goods are still in the insured's possession. If the goods cause an accident to a third party within the insured's premises, the liability would be insured's vehicles, and liability for injury or damage caused by the goods would in those circumstances be a matter of the motor policy.

Professional Liability Insurance

A Professional Indemnity Policy is a contract between the insured professional and the insurer and the insurer agrees to indemnify the insured (professional) against claim made by the his clients or persons affected by the negligent acts, errors or omissions in the professional's activity or business. Here the clients of a professional and persons affected by the professional's activity are collectively called Third Party while the insured and the insurer are the First and Second Parties.

Legal Aspects

Professional Indemnity Insurance is relatively of recent origin and has been introduced in the Lloyd's of London in the 20th century after the landmark decisions in **Hedley Byrne & Co. Ltd (1963)** which acted as prime movers for the development of market for this cover in London though insurance companies have been operating there since the 17th century offering mainly Marine Insurance, Life Insurance, Fire and accident Insurance. The Institute of London Underwriters issued clauses for Builders' Risks Insurance in 1899. Third Part Liability Insurance has been recognized in the London Market by law in the Marine Insurance Act 1906, The Road Traffic Act 1930 and the Third Parties (Rights against Insurers) Act 1930. Even though the cases on professional liability have been found fairly early as per law reports, the fear of moral hazards has caused delay in arrival of Professional indemnity insurance in the insurance market there. However the decisions in court cases have not only widened the market for this policy but also made this insurance compulsory for certain professionals thereat. The lawyers' indemnity insurance is compulsory in the countries like England and Wales, Denmark, Australia, Belgium, Finland, Germany, Ireland, Liechtenstein, Luxemburg, Netherlands, Norway, New Guinea, Scotland, Singapore, South Africa, Sweden, Canada, and US.

Policy Scope & Cover

The purpose of the policy is to protect a professional person against his legal liability to pay damages to persons who have sustained loss or damages arising out of his own professional negligence or that of his employees in the conduct of the profession. The policy offers indemnity strictly on legal liability but not on moral liability. The basis of this legal liability is a breach of contract or duty by the professional to take reasonable care and skill and standard of competence in the performance of his duty to the third party. The implied conditions for Professional Legal Liability are as under:

- Existence of a Contractual Relationship for duty and care
- Breach of duty to exercise care, competence and skill
- Breach of duty or negligence has caused loss/damage to the client

Such Insurance policies are available to almost all professionals such as Doctors and Medical Practitioners, Chartered Accountants, Financial or Management Consultants, Barristers and Advocates, Engineers and Architects, Builders, IT Professionals, Estate Agents, Surveyors, Valuers, Stockbrokers, and Insurance brokers etc (see Table-44).

Table-44: Policy Cover to Professionals

Professionals	Doctors & Medical Practitioners	Engineers Architects, Builders	Accountants, Management Consultants etc.	Lawyers Barristers, Advocates etc
Legal Liability & defense Costs for	Death & Bodily injury of patients	Death, injury & Construction Damage	Loss & Damage of Clients& Third Party	Loss& Damage of Clients& Third party
Negligence, Errors & Omissions of	Insured, qualified Nurse Technicians	Individual, employees& predecessors	Individual, firm, employees & predecessors	Individual, employees predecessors

Elements of Risks

A professional Indemnity policy may define the risks to be covered or the subject matter of insurance using any or all of the following elements:

- In relation to the Professional activity or service;
- In relation to the **causes of action** against professionals by the third party; and
- In relation to a **claim made** by the third party against the professionals.

Generally a professional indemnity policy defines the risks elements using each of these elements in various ways, forms and clauses. The policy cover also makes the use of the words like “Loss”, “Liability” or “Claim” to define the risk elements.

Professional Activity/Service

This basic element of risks is defined or dealt with in number of ways like:

- Activity of a named profession.
- Activity in the conduct of business/profession
- Advice in the professional capacity
- Drafting of documents in the professional capacity.
- Agency or representation in the professional capacity (auctioneers /estate agents)

Causes of Action

The insurer's promise to indemnify is limited to the defined causes of action by the third party against the insured. The policy provides that the cause of action must be for the breach of duty of the professional due to his negligent act, error or omission.

Policy Wording and Clauses

i. Operative Clause

The basis of this policy is the written proposal form, declaration and the premium paid as consideration for or on account of such indemnity for the insured named in the schedule of the policy.

"Now this policy witnesses that subject to the terms, exceptions and conditions contained herein or endorsed hereon, the company will indemnify the insured against legal liability for damages and claimant's costs fees and expenses anywhere in India in accordance with Indian Law in respect of any claim for breach of professional duty against the insured and notified to the company during the period of insurance by reason of neglect, error and omission committed in good faith in connection with the profession on the part of the insured or the predecessor in the profession or any employee of the insured or the predecessors in the profession".

ii. Indemnity Clause

It provides that indemnity applies only to claims arising out of damages during the period of insurance first made in writing against the insured during policy period. The insured is indemnified in accordance with the operative clause for the breach of professional duty by reason of any negligent act, error or omission committed during the period of insurance by the following:

- The insured as stated in the policy;
- The predecessors in the business of the firm; and
- An employee of the insured or the predecessors.

This clause also provides that there shall be no liability for any act committed prior to the retroactive date stated in the policy schedule.

iii. Limit of Indemnity Clause

This clause provides that irrespective of the number of persons mentioned as insured in the schedule the total liability of the company for damages inclusive of defense costs in respect of all claims made against the insured shall not exceed the limit of indemnity for the policy period stated in the schedule. In other words the total of all claims against the insured, qualified and unqualified staff, nurses covered in the policy will not exceed the overall limit of indemnity with a proviso that per accident (AOA) indemnity is limited to 25 per cent of the AOY limit.

iv. Claim Series Clause

This clause provides that where a series of losses/injuries/deaths are attributable directly to the same cause/error or omission in the discharge of the professional service or act all such claims are added together and treated as one claim and such claim shall be deemed to have been made at the point of time when the first of the claims was made in writing. Any claim from the same cause made 3 years after the first claim of the series will not be covered.

Policy Excess

Generally, policy excess is considered as shown in Table-45. But such excess may differ with underwriters as per their underwriting policy.

(i) Compulsory Excess

Table-45: Compulsory Access

	Professionals	Compulsory. Excess
1	Doctors/Medical Practitioners	NIL
2	Medical Establishments	0.25% of AOY Limit & Min.Rs.1000/-
3	Architect, Engineers, Interior Decorators	0.50% of AOY Limit & Min.Rs.5000/-
4.	Chartered Accountants	-DO-
5	Lawyers, Barristers etc	-DO-

(ii) Voluntary Excess

The insured may opt for voluntary Excess which shall be applicable to each and every claim, in addition to the compulsory excess to enjoy certain discounts premium.

General Exclusions

Professional Liability Insurance does not cover or indemnify the following loss or liability incurred by the insured:

- Contractual liability
- Liability for any act in violation of any law
- Services rendered under influence of intoxicants
- Pure financial loss i.e. loss of market or goodwill
- Personal Injuries like Libel, Slander etc.
- Fines, penalties etc.

- War and nuclear perils
- Employer's Liability
- Injury/damage occurred before retroactive date
- Deliberate disregard of insured's staff to duty & care
- Third Party Public Liability
- Criminal act or act in violation of law/ordinance
- Services rendered under influence of intoxicating liquor or drugs

Guide Rates for Professional Indemnity Policy

Following is the guide rates, which are generally used by insurers today. However they may refer to the reinsurers' prescriptions/ guidelines for major such risks:

Table-46: Guide Rates for Professional Indemnity Policy

1	**Doctors:**	
	a) Physician without dispensing/other facilities	0.30%
	b) Specialist/Consulting physicians (non-surgical)	0.60%
	c) Surgeon (Excl. specialist in plastic surgery, lithotripsy, dentist & similar extra corporal treatment	1.20%
	d) Surgeon (plastic surgery), Anaesthetics	1.80%
	Note: Additional Premium of 7.5% Indemnity premium for staff. Rate is reduced if AOA:AOY is reduced	
2	**Medical Establishments:**	
	Basic	1.80%
	Plus Loading on Inpatients (per capita) As per register	5/%

	“ “ on outpatients (per capita) “	1/%
	“ “ for radioactive treatment (Excluding X-Ray)on total premium	15%
	“ “ Unqualified nurses/technical or para-medical staff	7.5%
3	**Engineers, Architects & Interior Decorators**	7.5%
	Plus Loading on Annual Fees (3yrs’ Average projected)	1%
4	**Chartered Accountant, Financial/ Management Consultants**.	
	Loading on qualified persons (per head)	4%
	“ on Apprentices –Rs 50 per hour & other staff –Rs 25 per hour	Rs 100
5	**Lawyers, Advocates, Solicitors & Counsels**	
	Loading on Qualified Staff @Rs150 per hour & other Rs.50 per hour	5%

Commercial General Liability Insurance

Though all individuals and organizations both commercial and non-commercial face liability exposures for their activities, commercial organizations are exposed more to liability losses than others. A liability loss is an amount that a person is required to pay as a result of legal claim against him for his wrongful acts causing injury or damage to others. Wrongful acts causing legal liability or claim may arise from any of the bases, namely: i) Torts or Common Law; ii) Statutes; and iii) Contracts. Each of the above general legal liabilities being the foundation of commercial general liability has been also discussed earlier. However certain more aspects are being examined here along with the specific requirements and elements of CGL policy.

Legal Liability Exposure on Torts or Common Law

A tort is a wrongful act or omission-causing harm to others (negligence) or invading other's protected rights (nuisance). If someone's acts of negligence or nuisance cause harms to others, the law provides for remedy to the victim through an action for damages or compensation. This is the legal liability exposure. Each and everyone in the society do have such legal liability exposure and the degree of exposures varies with the nature and volume of social or economic activity of the individual. An individual or organization can transfer such liability exposure (only civil) to an insurance company through an appropriate liability policy. The legal liability exposures may be grouped under the following major categories:

- Public Liability or Premises and Operation Liability
- Products liability or products and Completed Operations Liability
- Motor or Automobile Liability
- Marine or Watercraft Liability
- Workmen Compensation and Employers' Liability
- Professional Liability
- Commercial general Liability
- Clinical Trial Liability
- Directors' and Officers' Liability

In all the above liability exposures torts are fundamental origins of legal liability. Torts are many, but commonly classified into: i) Negligence; ii) Intentional Torts; and iii) Strict Liability.

Negligence or Unintentional Torts

Negligence is a tort or a civil wrong determined under common law. Negligence is an unintentional tort involving the failure of a person to exercise the degree of care that a reasonable person would have exercised under similar circumstances to avoid doing harm to others. If a person does something that a reasonably prudent person would not have done or if a person fails to do something that a reasonably prudent person would have done, such *act of commission* or *omission* is considered **negligence** under common law. As decided by **Blyth V Birmingham Waterworks co. (1856**), "negligence is an omission to do something, which a reasonable person, guided by those considerations, which ordinarily regulate the conduct of human affairs, would do, or doing something, which a prudent and reasonable person would not do."

"Each has a duty to his fellows so to regulate his actions the condition of his property and the activities, as not to cause injury or damage to others ..." **Donoghue V. Stevenson**. 1932

In order to succeed in an action against negligence the plaintive, i.e. the victim must prove the following three aspects:

(a) The defended owed a duty of care to the victim (the plaintiff);

(b) There has been a breach of duty, and

(c) He has sustained an injury or damage as a result of the breach.

Negligence is the most common base for legal liability insurable under liability policy. The onus of proof for negligence generally rests on the plaintiff. As mentioned earlier existence of legal duty of care may arise from common law, statutes or contract. Here our discussion is confined to negligence under common law only. The third part of the action for negligence is damages, which are again two types: **Compensatory Damages and Punitive Damages.** Again Compensatory damages are divided into two categories: Special damages and General damages.

Defenses to Negligence Actions

In a negligence action for compensation, the plaintiff has to prove all the three basic aspects or elements of Negligence. The defendant again may take following defenses to avoid his legal liability for negligence:

- **Inevitable Accident** (Hidden defect in machinery)
- **Act of God** (Storm, earthquake, lightening)
- **Emergency** (out of eminent danger but not negligence)
- **Contributory Negligence /Comparative Negligence** (Blame to each other/Atkins' Law)
- **Assumption of Risk (**other than PLI Act Policy or Motor TP Policy providing no-fault liability)
- **Contracting Out** (Disclaimer Notices)
- **Limitation** (Barred by law of limitation)

Intentional Torts

In contrast to negligence there could be many torts, which may be intentional. Some of the intentional torts are exemplified below:

- Tort against Property: Nuisance, Trespass,
- Tort against person: Libel, slander, defamation, battery, assault, false arrest etc.
- Invasion of right of privacy
- Misuse of Legal Process

Nuisance

It is also a tort implying a wrong done by one to a person by unlawfully disturbing him in the enjoyment of his property or in some cases in the exercise of the common right. Nuisance is one area of law where the liability can arise even though one has taken all reasonable care. As decided in **Greenwood vs. Portwood**, encroachment/enlargement of tree roots in two neighbouring property would cause liability of nuisance and once damage was proved by the plaintive, the defended would automatically incur liability. Similarly escape of dust, fumes, and smells may bring legal liability nuisance of the offender. Importantly if this activity does not give rise to physical harm to the plaintive or to his property there will be no indemnity under the policy even though the defended may suffer financial loss by complying with injunction if any.

Commercial General Liability — Coverage

CGL policy covers a wide range of liability loss exposures of commercial organizations. The loss exposures come under following broad categories:

1. Premises and Operation Liability Risks
2. Products and completed operations Liability Risks
3. Limited Contractual liability
4. Personal and Advertising injury liability
5. Medical payments
6. Supplementary Payments

The origins of liability in CGL Policy are: i) Common Law; ii) Contract; and iii) Statute. Common forms of Torts that are covered in CGL Policy are as usual Negligence, Nuisance Trespass, Strict Liability, Libel and Slander, Liability for occupier's premises. CGL policy first introduced in US in 1941 has become the most trusted liability policy all over the world because of its well-tested definitions, wordings, clauses etc. The first CGL policy **introduced in 1941** by the casualty insurers in US was comprehensive in nature and known as comprehensive general liability policy. In 1986, the comprehensive general liability policy was replaced by the simplified CGL policy. In 1996, The American Association of Insurance filed revised version of CGL policy on behalf of its member insurers with two distinct versions of the CGL forms: **“Occurrence Version”** and “**Claim-made Version”**. They differ from each other with respect to the coverage of claim only in the following lines:

1. The occurrence version covers all bodily injuries or property damages that occur during the policy period.

2. The claim-made version covers all bodily injuries or property damages that occur during the policy period provided claims are made against the insured during the policy period.

Except above difference in respect of coverage of claims, the two versions of CGL policy are the same containing following main **6 sections** in the policy.

Section I — Coverages

1. Coverage A-Bodily Injury and Property Damage Liability

2. Coverage B-Personal and Advertising Injury Liability

3. Coverage C-Medical payments

4. Supplementary Payments

Section II —Who is an insured

1. Individual—Named Insured and his spouse

2. Partnership—Partners and their spouses (only to the conduct of business)

3. Limited Liability Co. —Members of the company

Section III — Limits of Insurance

Section IV — Conditions

Section V — Extended Reporting Period

Section VI — Definitions

Insuring Agreement for Coverage A — Bodily Injury and Property Damage

The provisions for coverage consist of an insuring agreement and several exclusions. If a claim made against the insured meets the entire criterion in the said insuring agreement and does not come within purview of the specified exclusions, it is admissible subject to policy terms and conditions. Again the Insuring Agreement has distinct parts:

(i) An agreement to pay damages on behalf of the insured; and

(ii) An agreement to defend the insured against claims for damages under policy.

(i) Duty to Pay Damages

Insurer's duty to pay damages for the liability claims made against the insured depends on the satisfaction of the following conditions:

- Insured must be legally liable to pay damages;
- The damages must result from bodily injury or property damage;
- The bodily injury or damages must result from an occurrence of accident;
- The accident must occur during policy period and in coverage territory;
- The claim must be made against the insured during policy period (Claim-made version);
- Damages must be with in the terms and conditions; and
- Liability as per limits of insurance.

The CGL policy contains an exclusion of bodily injury or Property damages intended by the insured. For example, if a building is set on fire on purpose by the insured, CGL policy will not over any claim against him. It is very important to note the difference between intentional acts and unintentional torts.

(ii) Duty to Defend

Coverage A Insuring Agreement also expresses the insurer's right and duty to defend the insured against any suit seeking damages for bodily injury or property damage. In determining whether the insurer has a duty to defend, consideration would be based on the findings from the allegations expressed in the complaint or petition of the plaintiff. The insurer shall not have any duty to defend if the allegations against the insured are not covered by the policy. In US, CGL form revised in 1996 contains the amended insuring agreement to State that the insurer has no duty to defend the insured against any suit seeking compensation for injury or damage to which the insurance does not applies.

Premises and Operations Liability (Public Liability) — Coverage A

It is the basic and common component of general liability. Before introduction of CGL cover Public liability policy has been popular covering premises and operation liability. CGL cover is still divided into two broad consideration for risk analysis and rating purposes: i) Premises and Operation Liability; and ii) Products and Completed Operation Liability. Generally, a separate rate is considered for each category. As we know, underwriting of underwriting of premises liability insurance is much more critical than property insurance. For underwriting this liability insurance an exhaustive CASE (Circumstances, Activity, Security and Events) study is required to be done to assess the liability exposures. The critical aspect of premises liability can be appreciated from the following comparative study between property insurance and premises liability insurance:

1. In property insurance liability of insurer is determined by terms and conditions of policy while in liability insurance the

amount payable by the insurer is determined primarily by the liability of the policy holder to compensate the third party suffering loss, injury, or damages due to his wrongful act and then by the terms and conditions of the policy covering the legal liability of the insured.

2. In property insurance maximum liability of the insurer is determined on the basis of sum insured along with the operation of the principal of contribution and subrogation while in a liability policy provides an indemnity in respect of insured legal liability to the third party.

3. The legal liability may arise from the three principle causes namely,

   (a) The common law as decided by the courts over many years in view of the socio-economic culture, conditions, and development;

   (b) Statutory liability as rate down by the Acts of Parliament; and

   (c) The contractual obligation between the two parties (the insured and third party).

   But the contractual liabilities as mentioned above in © are specifically excluded from the covered afforded by most of the liability policy.

4. The public liability policy covers the only civil wrong either under common (law of torts) or under statutes due to breach of duty by the policyholders, which may arise in the forms of Negligence, Nuisance, trespass, stick liability causing bodily injury or damage to the property of third party. The above basic elements of liability policy are being discussed hereinafter. A commercial general liability also covers libel, slander or false imprisonment over and above forms of liabilities.

Pollution Exclusions in Premises/Public Liability

CGL policy provides for **Absolute Pollution Exclusions**. Bodily injuries or property damages resulting from the release of pollutants are not admissible. But in many cases it is very difficult to exclude all pollution incidents from the CGL cover under this clause. This Exclusion contains some explicit exceptions as mentioned below:

- Bodily Injury or property damage by heat, smoke fumes emanating from a fire at the premises where insured or contractor is working. Thus smoke and fumes from a hostile fire at the insured's premises infiltrated a neighboring warehouse and caused damage to the goods in the warehouse. The Insured's CGL policy would cover claim for such damages.

- Another express exception to such pollution exclusions is coverage for bodily injury or property damage resulting from the escape of lubricants or fuel needed for normal function of mobile equipment.

- Third express exception to such absolute exclusion may be bodily injury caused by smoke, fumes, vapour, or soot from equipment used to heat a building provided such bodily injury must be sustained within building.

- Another exception to such exclusion may be relating to bodily injury or property damage resulting from the release of pollutants at any place away from the named insured's premises where the named insured or his contractor is performing.

Products and Completed Operations Coverage

It is a component of Coverage A. It can be also purchased as stand alone coverage. This cover responds to claims for bodily injury or property damage arising out of the named insured's products or completed operations. Product Liability and Completed Operations Liability are so similar that they are treated as components of one exposure. It is the legal responsibility of the manufacturers, distributors, and retailer to ensure that the use of product will not harm customers or users of the products. Product Liability lawsuits are based on negligence or strict liability in tort or both. Under strict liability in tort, the conduct of the manufacture, distributor or retailer is irrelevant and the focus is on the product itself and whether it was unsafe. They could have used utmost care in making, designing the product. However, the plaintiff must prove the following elements to succeed in against the defendants:

Products

1. The product was defective when it left the manufacturer's or supplier's place.

2. The defective condition made the product dangerous.

3. The defective product caused the plaintiff's injury.

Completed Operations

1. Injury or damage from work

2. Injury/damage must occur away from premises

3. Work causing injury completed or abandoned

Exclusions

1. Work not yet completed or abandoned

2. Products still in possession of the insured

Personal and Advertising Injury

This is under coverage B. This is considered to be a basic coverage under CGL. Those who do not need this cover can get it excluded by endorsement. Under this cover the insurer agrees to pay the sums that the insured becomes loyally liable to pay as damages. The insurer also agrees to defend the insured against any suit. This cover will not respond to any claim for bodily injury or property damage. This cover applies to personal injury if the injury is caused by an offense arising out of the named insured's business excluding advertising, publishing, broadcasting or telecasting done by the named insured. Coverage B applies to advertising injury only if the injury is caused by an offense committed in the course of advertising the named insured's goods, products and services. This cover is not appropriate for insuring the advertising injury liability exposure of an advertising agency or other firm involved in providing advertising services.

Examples of Personal Injury

- False arrest, detention or imprisonment
- Malicious prosecution
- The wrongful eviction or wrongful entry
- Defamation libel or Slander/ Product Disparagement
- Oral/written publication damaging person's privacy

Examples of Advertising Injury

- Use of another's advertising idea in advertisement
- Infringing on other's copyright, trade mark or slogan
- Oral/written publication of material that violates a person 's right of privacy

Medical Expenses Cover – CGL

This coverage is not liability insurance in true sense because the insured pays regardless of whether the insured is legally liable for that. This coverage is included in CGL Policy to give relief to the insured by providing a small amount of compensation for settling minor injury cases without having regard to his actual liability of the insured. This is viewed as a means of making prompt settlement to the potential liability claimant in order to avoid possibly larger liability in future. It is inbuilt cover and can be deleted by endorsement. The insurer agrees to pay medical expenses for bodily injury caused by an accident occurring in or on the ways to premises that the insured owns or rents. The accident must take place in the CGL coverage territory and during policy period and medical expenses must be incurred and reported to the insurer within one year up to the date of accident. The bodily injury caused by an accident that occurs away from the insured's premises (example of job site, where the insured's contractor is working) is covered if the accident results from the named insured' operations.

- Payments made regardless of fault.
- Payments within applicable limit of insurance.
- Reasonable expenses paid for:
    - o First aid administered during accident.
    - o Necessary medical, surgical, x-ray, dental services etc.
    - o Necessary ambulance, hospital, nursing professional and funeral services.
- **Medical Expenses Payable for Bodily Injury Caused by an Accident**
    - o On premises owned or rented;
    - o On ways next to premises owned or rented; and
    - o Because of operations.

Provided that –

(a) The accident in the coverage territory and during the policy period.

(b) The expenses incurred and reported within 30 days of the date of accident.

(c) Submission for examination by physician as often as reasonably required.

Supplementary Payments

The supplementary Payment Section provides for the details of the cost that insurer will pay with respect to (1) any claim to be investigated or settled by the insurer or any suit the insurer defends the insured under either coverage 'A' or Coverage 'B'. The supplementary payments may consist of the following:

- All legal expenses such defense cancel fees
- Cost of bail bond related with bodily injury liability coverage
- All reasonable expenses incurred by the insured at the request of insurer for investigation or defense
- All court expenses, imposed against the insured
- Prejudgment interest awarded against the insured relating to the judgment the insurer satisfies

Common Exclusions to CGL Cover

A standard CGL Policy is subject to following common exclusions. Again, there may be other express exceptions to such common exclusions:

- Expected or Intended Injury
- Contractual Liability
- Liquor Liability
- Workmen Compensation and similar laws
- Employers' Liability
- Pollution Liability
- Aircraft, Auto or Watercraft

- Mobile Equipment
- War Warlike action or Insurrection, Rebellion
- Damage to owned/ rented/ occupied property
- Damaged own product
- Damage to own work
- Damage to Impaired Property or Property not physically Injured
- Recall of Products, Work or Impaired Property
- Electronic Data

Claims Made vs. Occurrence Based Policy

There are two versions of CGL policy- Claims Made policy and Occurrence Based Policy. The most commonly accepted form of CGL policy is written on “Claim-Made Basis” as compared to “Occurrence Based Policy” as discussed earlier. With a claim-made policy, a claim is covered under the policy in effect at the time the claim is made provided the injury has occurred during policy period and after retroactive date. In the Claims-made coverage form, both Coverage A and Coverage B are subject to a claims-made coverage trigger. The basic requirement of the claim made trigger is that the claim for bodily injury or property damage (or personal injury or advertising injury) must be first made against any insured during either the policy period or an extended reporting period provided that the injury or damage must have occurred before the end of the policy period and after the retroactive date provided in the policy. In Occurrence based policy, event giving rise to the claim must occur during policy period and the insurer would respond whenever the claim is thereafter made on the insured. The occurrence-based policy covers injury that occurs during policy period regardless of when claims are made. A claim made today for injury that occurred 30 years ago could be covered under occurrence-based policy that was in effect in 30 years before. As this occurrence version of CGL policy is long-tail claims oriented, determination of cost and management of claims are the major problems for the insurers. The insurers cannot predict the cost for pricing risks for such liability exposures. Occurrence trigger cover has become very costly and difficult for Lloyds' underwriters for their liability cover for industry of asbestos and other harmful substances in 1980s and onwards. To address such problems, insurers developed claim-made policy.

Claims-Made Wording

It mandates that:

- The event giving rise to the claim should have occurred during the period of insurance and
- Claim should be made during policy period
- Period of insurance is determined as period between the date of inception of the First Claims Made policy (continued without a break) and expiry of the current policy Claims-made policy may be issued with:
  - (i) No retroactive date; or
  - (ii) A retroactive date same as the policy inception date; or
  - (iii) A retroactive date preceding the policy inception date. This aspect has been discussed earlier.

CGL Policy Conditions (Section IV)

This section addresses various matters, such as the insured's duties in the event of occurrence, claim, or suit, the insured's right to sue the insurer, principle of contribution, subrogation etc.

(a) **Duties of the Insured after occurrence, Offense, Claim or Suit:**

- Immediate Notice,
- Contents in notice—time, place and cause of occurrence, names and address of insured persons and witnesses, nature and location of injury or damage etc.
- Others

(b) **Legal Actions against the insurers;** providing for procedure and on agreed settlement

(c) **Other Insurance** mentioning about Primary Insurance, Excess Insurance and method of sharing

(d) **Premium Audit:** Provision for computation of final premium after audit for adjustment against advance premium and for due return of excess premium if paid in advance and for recovery of the shortage, if any.

(e) **Representations:** Statements in the policy issued are based on the insured's representations.

(f) **Separation of Insured:** Application of insurance to each insured separately against whom claim is made

(g) **Renewal of Policy:** Providing rule and procedure for non-renewal of policy (by notice before 30days)

(h) **Transfer of Recovery Rights:** The insured will bring suit or transfer those rights to insurer

(I) **Bankruptcy:** Insolvency of insured will relieve insurer of their obligation

Extended Reporting Periods (Section V)

A claim-made CGL policy provides for two extended reporting period: i) Basic Extended Reporting Period and ii) Supplemental Reporting Period.

a. **Basic Extended Period** is provided automatically without any additional premium if the policy is cancelled or not renewed or the insurer renews the policy with later retrospective date or with occurrence base. With such extension policy will cover claims made against the insured within 5 years for the occurrence within policy period and reported within 60 days from expiry. It does not increase Limits of Insurance or apply to claims to be covered by subsequent policy.

b. **Supplemental Extended Reporting** is granted under the same circumstances as above provided the named insured requests in writing within 60 days from the expiry of policy and pays an additional Premium specified by the insurer. The supplemental tails begins when basic tails ends and it continues indefinitely for the occurrence reported to the insured within 60 days, but did not result into claims even after 5 years.

Directors' and Officers' Liability Insurance

In recent years, corporate issues and attention have focused on corporate governance centering round managerial ethics and regulations on finance, markets, environment, legislations, and employment practices. The spate of corporate collapses all over the world, the emergence of market-oriented management practices combined with liberalization on flow of cross-border movement of huge funds in the forms of FDI, ADA, GDR and ECB and vulnerability of capital market have given real fillip to devise good corporate governance framework and find the ways and means of ensuring effective corporate governance practices to diverse stakeholders. Corporate governance practices and procedures differ widely across the world depending on nature, volume, spread and jurisdiction of corporate activities. On a widely scattered and spread of shareholding, it is the board of directors who are in charge of foundation and compliance of corporate governance requirements.

The corporate governance compliance was brought into sharp focus by the extensive study report submitted by the Cadbury

Committee to the London stock exchange in 1992. The Cadbury Committee Report has laid down "Code of Best Practices" spelling out the methods of governance to strike the balance between the powers and the accountability of the directors for the best performance of the corporation. But the question arises as to how to mitigate or manage the liability for the financial losses arising out of negligence or other wrongful acts comprising breach of trust, duty or loyalty of the directors or shirking their corporate responsibility or disregarding the code best practices of corporate governance. The answer can be found in a duly defined Directors and Officers Liability Policy, which will indemnify the stakeholder for the financial losses, caused to them due to wrongful acts of officers and directors of the company.

The Companies Act and directors' & Officers' Liability

The companies Act 1956 (Amendment) provides a general prohibition on reimbursement or indemnification of legal liability against the directors and officers for their wrongful acts. The Act also provides for unlimited liability of the directors in the limited company. By this, the directors and officers will themselves be liable for compensation for the financial losses caused to various stakeholders for their wrongful acts even without indemnification from company. Sometimes if in the court it is established that the wrongful acts of directors causing financial losses to the company or its stakeholders are the consequences of the decisions taken by them for only the interests of the company, the company is required to indemnify the liability of the directors and officers of the company. But question arises as to how the directors and officers will mitigate the unlimited liability or the company will reimburse the liability of the directors or officers if they have done only for the interests of the company. The answer lies in the Directors and Officers Liability Policy. The salient provisions of the companies (Amendment Act) Act 2002 are quoted below for ready reference.

Section 201: Avoidance of Provisions Relieving Liability of Officers and Auditors

Save as provided in this section, any provision, whether contained in the article of a company or in an agreement with a company or in any other instrument, for exempting any officer of the company or any person employed by the company as auditor from, or indemnifying him against, any liability which, by virtue of any rule of law, would otherwise attach to him in respect of any negligence, default, misfeasance, breach of duty or breach of trust of which he may be guilty in relation to the company, shall be void: Provided that a company may, in pursuance of any such provision as aforesaid, indemnify any such officer or auditor against any liability incurred by him in defending any proceedings, whether civil or criminal, in which judgment is given in his favour or in which he is acquitted or discharged or in connection with any application under Section 633 in which relief is granted.

Section 322: Directors with Unlimited Liability

In a limited company, the liability of the directors or of any director or manager may, if so provided by the memorandum, be unlimited. In a limited company in which the liability of a director or manager is unlimited, the directors and the manager of the company, and the member who proposes a person for appointment to the office of director or manager, shall add to that proposal a statement that the liability of the person holding that office will be unlimited; and before the person accepts the office or acts therein, notice in writing that his liability will be unlimited, shall be given to him by the following or one of the following persons, namely, the promoters of the company, its directors, or manager, if any, and its officers. If any director, manager or proposer makes default in adding such a statement, or if any promoter, director, manager or officer of the company makes default in giving such a notice, he shall be punishable with fine which may extend to Rs 10,000 and shall also be liable for any damage which the person so appointed may sustain from the default; but the liability of the person appointed shall not be affected by the default.

Section 323: Special Resolutions for Unlimited Liability of Directors

A limited company may, if so authorized by its articles, by special resolution, alter its memorandum so as to render unlimited the liability of its director or of any director or manager. Upon the passing of any such special resolution, the provisions thereof shall be as valid as if they had been originally contained in the memorandum: Provided that no alteration of the memorandum making the liability of any of the officers referred to in sub-section (1) unlimited shall apply to such officer if he was holding the office from before the date of the alteration, until the expiry of his then term, unless he has accorded his consent to his liability becoming unlimited.

Underwriting Practice and Perspectives

D&O Liability insurance is of various coverages with a variety of terms, conditions and exclusions. Insurance in any form or cover may not help them to get indemnification in their legal liability payments in real actions. Directors and officers, therefore, need to know what is covered and what is not. Policy terms and conditions, insuring agreements before they take proper insurance cover against their potential liability risks in their managerial profession. Similarly, insurers also need to identify, analyze and evaluate the liability risks exposures of directors and officers before they issue an appropriate cover of D&O Liability insurance. This article is aimed at helping both the groups being the insured and the insurers in understanding and assessing their respective roles, activities and manages their risks in a proper way. This article provides a comprehensive information with a lot of international case studies of this liability insurance, which will be of great use to the insurers, the insured being corporations, directors and officers, brokers and other professionals like accountants and advocates to use appropriate D&O liability policy to manage the unlimited legal liability risks of directors and officers. This article is also intended to provide the legal perspective of good corporate governance and create the awareness about the effectiveness of D&O Liability Insurance for the purpose among the directors, officers and auditors of the company.

Directors & Officers Liability Insurance—International Perspectives

D&O Liability insurance protects directors and officers from liability arising from their actions connected to corporate position and managerial activities. About 95 per cent of Fortune 500 companies are having D&O Liability Insurance policy today to cover defined corporate risks of legal from various stakeholders of the body corporate for wrongful actions or breach of duty or negligence under common law or under statute like companies Act or other statutes. Studies indicate that the average settlement of securities fraud litigation in 1999 was more than US$8mn with average defense costs more than US$1mn. D&O Liability Insurance plays a major role in managing these ever increasing corporate management risks in today's evolving litigation and liberalized environment. From its modest beginning in 1930s by Lloyd's of London, D&O Liability Insurance has become a prime corporate insurance cover being issued by almost all leading insurers in the today's business world. The non-life insurance industry has matured itself to devise required D&O Liability products with a large number of new and novel covers from the historic focus on personal financial protection to officers and directors. Other liability insurance policies mostly cover third party liability for bodily injury or property damages but not financial loss due wrongful acts or breach of duty of directors or officers, for which actions are taken by stakeholders either on common law or various statutes.

D&O Liability Insurance is coupled with coverages designed to protect the corporation in additions personal protections to its directors and officers. According to the 1997 Wyatt Report, companies with assets more than US$10bn had 63 per cent D&O claims. 42 per cent of large banks had at least one claim against their directors and officers. Insurance cannot prevent insolvencies, rectify wrong actions, reduce the financial losses, improve the working of director and bring transparency, but only indemnify financial loss of the above stakeholders in case of sudden collapse or insolvency of the corporations due to negligence, breach of duty or civil wrong under legislation, regulations or common law.

Major Coverage in D&O Liability Insurance

At its most basic level, D&O Liability Insurance covers the legal liability of directors and officers for their wrongful actions under common law or corporate law due to their corporate positions. Due to general expansion of the industry, tremendous growth in capital market with more and more liberalization and globalizations and consequent market pressure D&O insurance has expanded beyond its original and basic cover "A".

Major Coverages:

Agreement 'A'… Coverage directly to Directors

Agreement 'B'… Coverage for Corporate Reimbursement to Directors and Officers

Agreement 'C'… Coverage for Entity Securities

Agreement 'D'… Coverage for Employment Practices Liability

A single policy may provide multiple and varied covers either with different insuring agreements by standard forms and clauses or with different endorsements for different covers.

Insuring Agreement A

It is also known as "A-Side Coverage" providing coverage directly to the directors and officers for loss and defense expenses resulting from legal liability from wrongful actions or decisions. A-Side Cover applies where the corporation does not indemnify its directors and officers. Reference can be made Section 201 of the Companies Act 1956.

Insuring Agreement 'B'

It is a corporate reimbursement coverage. Under this cover the insurer reimburses the company for loss resulting from the company's obligations to reimburse the directors and officers to the extent required or permitted by law under the proviso of the

Section 201 of the Companies Act for suits alleging wrongful acts committed by directors and officers.

Insuring Agreement 'C'

It is coverage for Securities Wrongful Acts like:

1. Any violation of Securities Laws; SEBI Laws or

2. Act, error, omission, misstatement, misleading statement or breach of duty by an Insured in connection with the purchase or sale, or offer to purchase or sell, securities issued at any time by the Insured Entitlement.

Insuring Agreement 'D'

It is coverage against legal liability from Employment Practices Wrongful Acts like:

(1) Wrongful discharge or termination of employment, including constructive discharge;

(2) Employment-related misrepresentation;

(3) Sexual or other workplace harassment;

(4) Wrongful failure to employ or promote;

(5) Wrongful deprivation of career opportunity, employment or promotion;

(6) Wrongful discipline or evaluation;

(7) Failure to adopt or provide adequate employment or workplace policies and procedures;

(8) Wrongful retaliation;

(9) Violation of any law concerning discrimination in employment, promotion; and

(10) Violation of corporate policy on transfer, promotion and mobility, etc.

All individual coverages are subject to distinct terms, conditions, definitions, limits and exclusions. Coverage is limited to claims first made during the policy period. It is on claim-made basis, but not occurrence basis. Here the insurer does not have duty to defend generally, but right to defend and required to cover the insured defense costs. Even though the insurer has right to defend, he cannot impose his decision in regard to appointment of legal counsel and the points of defenses on the insured.

F&Qs in D& O Liability Insurance Underwriting

- **Who can be covered by the policy?**
  - o Directors and Officers of the company
  - o Former, Present and Future Directors and officers
  - o Outside Directors and Nominee Directors
  - o Officers /employees occupying Management or Supervisory capacity.
  - o Directors and officers of the Holding Company.
  - o Parent Company and the Existing Subsidiaries
  - o Directors representing the group in an associate company
- **Does D&O Liability Policy cover Shadow directors?**

  Shadow directors are not covered by policy. Underwriters try to find out the role of shadow Director in the managerial
- **Who is shadow director?**

  Shadow Director is someone who holds the majority of equity, owns the company and retains the control over functioning over the company, but places others on the board as directors and officers to make the people think that others are liable for any wrong done, but not he. Sometimes it is found that spouse or a company secretary has been made director by one who controls the company instead of being personally listed as directors in company's paper. But under common law such shadow directors will be held liable under principle of strict liability.

- **What does D& O Liability Insurance Policy cover?**

D&O Policy covers "Wrongful Acts" of Individual Directors/Officers of Company. Wrongful acts mean any error, misstatement, misleading statement, act, omission, neglect, breach of duty, breach of trust or breach of warranty by director /officers in the discharge of their duties. There are two types of coverage: i) Corporate Indemnification; and ii) Indemnification to Directors and Officers directly.

- **What are the typical "Wrongful Acts admissible in D& O Policy?**

Following are the wrongful acts covered by D&O Liability Insurance policy:

o Inaccurate statements of financial conditions

o Errors in annual accounts

o Conflict of interest

o Lack of application of diligence or good faith

o Mismanagement of funds

o Misstatements in prospectus

o Allotment of shares

- o Unauthorized or imprudent loans or investments
- o Failure to obtain competitive bids
- o Imprudent expansion resulting in a loss
- o Unwarranted dividend payment, salaries or compensation.
- o Improper loans made to directors
- o Violation of Loan covenant
- o Misleading statements filed with the Stock Exchange
- o Misrepresentation in acquisition agreement for the purchase of another company
- o Wrongful dismissal of an employee.
- o Employee discrimination or unfair employment practices

How do the underwriters identify potential risks from above wrongful acts?

With proper Circumstances, Actions, Security and Events (CASE) study the underwriter identify, analyze and evaluate all possible risks factors before they issue such policy to any company or directors. With risk management expertise, the insurers also help the corporations and their directors to make a systematic approach and strategy for financial risk analysis and ensure better corporate governance.

Who can Sue Directors and officers for Negligence & Wrongful Acts?

The common conception wrongfully held by directors is that only shareholders can bring actions against them for their wrongful acts. But it is not a fact. Any of the following stakeholders can bring successful actions against directors and officers for their wrongful acts as illustrated above:

- Shareholders, bondholders or other security holders
- Govt. departments, Tax &Security authorities and Regulatory Authorities
- Customers and Depositors,
- Creditors
- Competitors
- Employees –present and past
- Receivers, Liquidators and administrators

Underwriters always make a due diligence analysis about the role, dominance and possible liability risks from each of the above potential claimants before issuance of any policy. Let us discuss the nature of some successful actions that arise from following stakeholders.

a. Shareholders

Shareholders are the most-interested group depending upon the directors managing their fund and running the company on their behalf. The return on their investment and the security thereof depend absolutely on the health of the organizations being managed by directors and officers only. So they owe jointly and severally a great duty of care, trust and loyalty to the shareholders i.e. the owners of the company. The right for action against the directors extends to legal representatives of deceased shareholders. A few examples of actions of shareholders against directors are:

1. Shareholders have succeeded in actions directors when profit forecasts made by directors at the beginning of the year went in vain at the end of the year.
2. Shareholders have brought actions against directors for misleading statements of the directors who led the shareholders to sell their shares prematurely at the price less than that they could have sold for later.

3. Where capital comes from other sources like venture capital, private individuals (business angles) and merchant banks, the lenders in such situations are similar to that of shareholders and can bring actions against directors for misrepresentation causing financial loss of capital providers.

b. Creditors

In case of insolvency, creditors are worst affected if they are unsecured. Secured creditors can lose out if the assets charged are not realizable much. Loans or credits received are utilized for book debts, property and buildings, plant and machinery, investments and advances. Building may be overvalued; property may not exist or exist for lower value, plant and machinery may be unusable, investment may be of less realizable value. For all these reasons, secured creditors or lenders may face severe consequences from corporate financial crisis and directors and officers will be liable to them for such consequences due to their wrongful acts or breach of duty by as mentioned above.

c. Customers

Customers may bring action directly against the directors and officers of the company for defects or deficiency in the products sold under statements of directors or responsible officers of the company. Product liability insurance may respond to such action, if it is brought against the company. But if it is taken personally against any director or officer giving statement or representation for marketing of products, then D&O Liability Insurance policy is to respond such action and claim.

d. Government Departments & Agencies and Regulators

The Government departments including Taxation Department, Import & Export Department, Excise Department Money Market Regulator (RBI), Capital Market Regulator (SEBI), Department for Protection of Environment (Pollution Control Board) are responsible for protection of national resources and pursue actions directors or the company.

e. Receivers Liquidators and Administrators

When a company gets into financial crisis and insolvency, official receiver, liquidator and administrator (generally accountants and advocates) can initiate actions against directors and officers of the company for the financial loss arising out of wrongful acts or breach of duty of officers and directors.

What are the types of D&O cover over the world?

Generally, policy is granted on annual basis. In very a few cases, cover is granted over a longer period say 3 years. For every renewal a new proposal is obtained to do the risk analysis prior to renewal. In some cases, insurers renew policy on the basis of declaration of insurance. Cover is granted on Blanket Basis providing that the range of individuals who can be regarded as past or present or future directors or officers of the company or its subsidiary. Associated companies may also need protection depending upon the level of control from the parent company generally holding more than 50 per cent voting rights. Thus all directors and officers existing, future and former including shadow and constructive of both executive and non-executive may be included on an unnamed Blanket Basis.

What are the major factors in Risk Evaluation?

Underwriting Considerations of D&O liability insurance are based liability risk identification, analysis and evaluation. Such type of risk identification involves the following major aspects:

- Financial history of the organization
- Its asset size
- Its organizational structure
- Geographical spread
- Recent profile or events
- The size of the sum insured

- The deductible selected
- Past claims history

Basis of Risk Evaluations for Underwriting Risks Proposal Form

A detailed Proposal Form is essential for this class of business involving wide and varied risk exposures of the directors and officers to all stakeholders including shareholders, creditors, employees, customers, public and regulators. Apart from usual or standard questions asked about the name, address, date of establishment and commencement, business activities, previous insures, specific questions are asked about shares, shareholders, holding pattern, strategic events, etc., as additional information for next one year. A specimen of Proposal Form is appended for ready reference. Some of the additional information are outlined below:

- **A list of all persons** who are directors or officers of the company or its subsidiaries is required to given. Information about their age, position, qualification, experience etc., are also sought here.
- **Number of shareholders** and what percentage of shares is owned by the directors.
- **Details of shareholdings mean** whether greater than 5 per cent in any class of the company's issued shares? If yes, their status, influence over the management or strategic decision, on fund-management, investment and borrowings, merger and acquisition, expansion, internal and external reconstruction etc.
- Are the **shares listed** on a recognized stock exchange? If yes, give details.
- What **new businesses or projects** have been acquired or completed currently during last twelve months and potential risk exposures therein?

- Are any **acquisitions or mergers** or strategic alliance under considerations currently?

- Is there **any existing D&O Liability** in effect? If yes, what is its periodicity? Nature of cover? Side A or side B and others? Amount of SI? Basis of deciding SI? Would any claim which has been made or which is now pending against any person who proposed for insurance have fallen within scope of such policy?

- Is the company or any person proposed for insurance aware, after enquiry, of **any circumstances or incident** which it or he reason to suppose might afford grounds for any future claim such as would fall within the scope of the proposed insurance.

- Insurers need to know and identify the **likelihood or possibility of claims arising out of past events**, which may surface in the policy period though it will be claim-made policy.

- Insurers need to be more analytical about **future events of the company or directors** that may give rise to claims for legal liability against directors and officers of a company for their wrongful decisions about future events. So appropriate enquiries must be made by the underwriters for past as well as future events and consider full and truthful answers to such questions before they accept the risks.

Common Exclusions in D&O Insurance Policy

i. No coverage will be available under this Policy for Loss, other than Defense Expenses, from Claims:

   a. Against any Insured brought about or contributed to in fact by any dishonest or fraudulent act or omission or any willful violation of any statute, rule or law by any Insured;

   b. Against any Insured brought about or contributed to in fact by the gaining by any Insured of any profit, remuneration or advantage to which such Insured is not legally entitled; or

c. Based on, arising out of, directly or indirectly resulting from, or in any way involving any actual or proposed payment by the Insured Entity of allegedly inadequate consideration in connection with the purchase or sale of securities.

ii. No coverage will be available under this Policy for Loss, including Defense Expenses, from Claims based on, arising out of, directly or indirectly resulting from, or in any way involving any:

1. Actual or alleged bodily injury, sickness, mental anguish, emotional distress, disease or death of any person, libel, slander, oral or written publication of defamatory or disparaging material, or damage to or destruction of any tangible property including loss of use thereof;

2. Actual, alleged or threatened exposure to, or generation, storage, manifestation, transportation, discharge, emission, release, dispersal, seepage, migration, escape, appearance, presence, reproduction, growth, treatment, removal or disposal of any Pollutant;

3. Cost, expense or charge to test, monitor, clean up, remediate, mitigate, remove, contain, treat, detoxify, neutralize, rehabilitate, or in any other way respond to or assess the effect(s) of any Pollutant; or

4. Policy does not cover any loss or liability occurred from operation of regulation, order, direction or request to test for, monitor, clean up, remove, contain, treat, detoxify or neutralize any Pollutant.

iii. No Coverage for claims in the actions in Insured vs. Insured that is Directors Vs Directors.

Clinical Trial Liability Insurance Policy

Before a new drug is introduced in the market, the pharmaceutical company and the authorities need to make sure it will work as anticipated on human beings and that there would be no unacceptable side-effects to using it. Prior to this stage, the drug would already have been tried out in the laboratory and on animals, but we still need to be sure how it works on human beings. Hence, after animal testing has indicated prior positive results, the drug is tried out on human beings in a carefully controlled environment. The various stages of testing it out on human beings are collectively refereed to as clinical trials.

Stages of Clinical Trials

There are three stages or phases of clinical trials prior to marketing.

Phase I trials are done on relatively small groups of people (20-80) to evaluate the safety of the drug, determine a safe dosage range and identify it side-effects.

In Phase II trails, the coverage is expanded to about 100-300 people and the focus here is on studying the effectiveness of the drug and further evaluating its safety.

Phase III trials typically involve groups of 1,000-3,000 people.

The idea is to confirm the effectiveness of the drug over a larger sample, monitor side effects, compare the drug with existing treatments and collect information on how the drug can be used most safely. There is another phase, Phase IV, which is after marketing of the drug begins. Unlike other three phases, which are in the nature of controlled experiments, Phase IV essentially consists of collecting feedback on the drug once it is in use.

F&Qs for Underwriting Decision

i. Who decides on whom the trials are conducted?

The decision to participate in a clinical trial is entirely voluntary.

Typically, patients suffering from a disease and hopeful of a new drug that could help cure it would be the ones most likely to volunteer. However, it is the duty of the organization conducting the trials to ensure that the patients who do so are giving their "informed consent". This concept means that the patients have to be fully briefed about the expected benefits, side-effect and potential risk involved in testing of the new drug before they volunteer to participate. Volunteers can opt out of the trials at any stage.

ii. Can anybody conduct a clinical trial?

No. Before a clinical trial can be conducted, permission must be sought from the relevant authorities. In the US for instance, it is Food and Drug Administration that is responsible for sanctioning clinical trials. In India, it is the Drug Controller. A drug company seeking to conduct a clinical trial must approach these authorities and seek permission to do so.

Underwriting Considerations/Clauses

The policy is issued on claims-made basis and business is underwritten on annual basis such as:

- The policy wordings are to be based on the wordings of product liability insurance subject to the following exclusions and conditions.
- No coverage for injuries to health and health and deterioration of health for already existing injuries to health that would also have occurred or continued to exist, if the volunteer would not have participated in the clinical test.
- No coverage for genetic injuries, for any claim resulting from an HIV/AIDS.
- No coverage for injuries to health, if they are due to the fact that the participants of the clinical tests acted knowingly against the orders of the personnel that was in charge of the test and its execution.
- No coverage for the inefficacy of the tested product.

- No coverage for medical malpractice.
- An injury to health is deemed to have occurred as soon as the injured has consulted a medical doctor because of symptoms that are then or later identified as symptoms of an injury to health caused by the test.
- No insurance cover for ex-gratia payments.
- An injury to health is deemed to have occurred as soon as the injured has consulted a medical doctor because of symptoms that are then or later identified as symptoms of an injury to health caused by the test.
- It is presumed that the risks and benefits as well as the experimental character of the tests are explained in such a way to the participants that no liability because of lacking or insufficient information may arise.
- All necessary approvals of the competent regulatory authority, viz. Drugs Controller General of India (DCGI)/Ministry of Health, etc., for the trials is issued prior to the commencement of the trials.
- The clinical trials of new products are to be specifically excluded if cover is required for Bio-equivalence and Bioavailability tests of products available in the market.
- Liability arising due to findings of the preceding phase of study to be excluded.
- Claims reporting period is limited up to 60 days from the date of completion of trial.

Underwriting Requirements

- Proposal Form duly filed, signed and stamped (as per annexure ‘A’)
- Indemnity Limits (AOA/AOY)

- Protocol (Summary)
- Whether Drug Controller's/Ethics Committee and Government Department permission
- Volunteer Consent Form
- Copy of Agreement and Contract with other parties
- In what phase the trial is in and number
- Phase I – if the trial is done on small groups of people e.g. 20-80 persons
- Phase II – if the trial is on a group of 100 to 300 people
- Phase III- if the number of persons involved is 1000 to 3000.
- Phase IV – the trial is after marketing of drug begins
- Information & Experience of earlier trials, if done
- Balance Sheet of last 2 years

Insuring Agreement

The company will indemnify the insured against those sums, subject to terms of this policy that the insured becomes legally obliged to pay as compensation for bodily injury to a research subject and or any other such person (the company is also liable to pay claimants costs, fees, and expenses), which result from an occurrence and/ or a series of occurrences during the period of insurance (policy period). Research subject shall mean any person participating in a trial including their dependents, heirs, executors, administrators, and legal representatives.

17

CREDIT INSURANCE

Background of Credit Insurance

Credit Insurance provides a protection against failure of its customers to pay their debts. Like any form of insurance, Credit Insurance is purchased to protect a business from a large loss that could impair its performance. Credit Insurance protects receivables from debtors over protracted default or insolvencies of buyers. Exporters structure their Receivables through the letter of credit or Trade Credit. LC is a letter from a bank guaranteeing a payment to a seller on time. If the buyer is unable to make payment on purchase, the bank will have to make the payment. Today with several foreign banks going to difficult times and companies filing for bankruptcies have resulted in Indian companies rushing for insurance cover. There is now increasing demand for cover from number of exporters to obtain cover from Export Credit Guarantee Corporation (ECGC) and other insurance companies like The New India Assurance Company Ltd, ICICI Lombard, Bajaj Allianz etc. The ECGC is the country's largest and the world's 5^{th} largest credit insurer. In view of present credit crisis in the world, many offers and enquiries for credit insurance from business houses in India are being rejected especially when the importers are US-based. In these stressed financial times, geographical location is the most important consideration for underwriting risks for insurance companies. In the changed environment underwriting credit risks and rating thereof have become very stringent factoring in Rating Level, Credit Policy, and Credit Management. Let us now discuss the general guidelines of Credit Insurance followed by insurance players:

What is credit risk?

Thus Credit Risks mean risks of financial loss from bad debts and credit losses.

Major Types of Credit Risks

- Export Credit Risks
- Domestic Credit Risks
- Commercial Risks
- Political Risks

Major Sources of Credit Risks

- Trade Receivables (Book Debts)
- Loans
- Bonds
- Securitization

Commercial Risk

- Non payment by the buyer – protracted default
- Insolvency of the buyer
- Risk of non-payment of dues due to death, default, delay, insolvency etc.
  - o by retailers/wholesalers and manufactures.
  - o by consumer and retailer
  - o by borrowers of Loans
  - o by importers (Export Credit)

Political Risk

- Military or civil war, revolution, riot or insurrection
- General moratorium on payment by the government of buyer's country

- Cancellation of import license
- Government decision preventing performance
- Political events, economic difficulties, legislative or administrative measures preventing payment

What is Credit Insurance?

Credit insurance is transfer of above-noted credit risks. Credit insurance, also called accounts receivable insurance, provides your business with protection against the failure of your customer to pay its trade debts. This situation arises because customer becomes insolvent or because customer does not pay within the set timeframe. These risks are usually described as commercial risks. Companies that export can also protect themselves against a range of political risks that may prevent or delay payment. This happens when payment is not received as a direct result of a war in the buyer's country, cancellation of a contract by the government of the buyer's country, or when a government implements regulations which either prevent the export or import of the goods – or prevent or restrict the transfer of hard currency – from the buyer's country. Credit Insurance provides two types of covers: Domestic Cover and Export Cover.

Domestic Cover:

- Insolvency of buyers
- Protracted Default

Export Cover

- Insolvency of Buyers
- Protracted Default
- Political Risks

Why Credit Insurance?

On average, 40 per cent of a company's assets are in the form of trade debts. Sometimes the figure is higher. It is very difficult for a company to predict which client will default on payment. Close to 50 per cent of all payment defaults arise from vendors with whom stable and long-term trade relationships have been established. The cost of non-payment to a business is quite substantial. For example, if a company's profit margin is 5 per cent and one of its customer defaults on a debt of Rs 100,000, the company will have to achieve additional sales of Rs 2,000,000 to make up for the lost profits. It is more costly and difficult than to take credit insurance at a very low cost of insurance. More importantly, the lost cash flow could be devastating. Non-payment weakens a company and lowers its investment capacity. A credit insurance policy helps in the management of fire's accounts receivables and compensates you in the event of non-payment. So customers ranging in size from small businesses to large, multi-national companies (MNCs) in most sectors including trading, manufacturing, services use credit insurance to manage their various types of credit risks over and above their internal credit-monitoring and credit management process. Following are the major benefits of Credit Insurance:

- Protection from bad-debt losses;
- Better credit control and protection against catastrophic bad-debt losses;
- Better risk management through an early warning system-bolstered by the Insurer through their Data Bank;
- Better business planning through the elimination of unknown risks;
- Improved working capital Management because of enhancing the quality of accounts receivable with credit insurance;
- Better sales targeting through proprietary information that can be used to target new customers and markets and monitor existing customers;

- The benefit of Data Bank and debt collection capabilities and network;
- Improved cash flow, as Insured receive payment for unpaid invoices that are insured;
- Safe expansion of sales Secure better borrowing terms;
- Saves costly & time consuming litigation in buyers own country;
- Enables Export without Letter of Credit – most buyers refrain from opening LCs; and
- Enables Post shipment credit at cheaper rates.

Given that the average level of bad debt experienced by companies is approximately 0.7 per cent of sales, the majority of businesses find credit insurance to be highly cost-effective. The Credit Insurance is also a credit risk management tool that can provide concrete solutions for the trade expansion and business growth strategy and panning. It is an insurance product with an ongoing process of partnership between you and the Insurer. The insurer vets a debtor's credit-worthiness and monitors his financial position to identify possible problems.

Indemnity

The level of indemnity typically ranges from 80-100 per cent; however, the level varies depending on the policy, an insured selects on the basis of his credit management process, experience, accounts receivable portfolio and premium payment decision. If he incurs a loss, how soon a claim will be paid. Generally, the claim is paid within 180 days on a domestic loss. Export losses may take a bit longer time. However, if the export loss is due to insolvency of foreign customers, it is paid within 180 days of the date of loss.

Cost of Credit Insurance

For the most popular policy, the premium is calculated on a percentage of the insured's sales. This rate is generally less than 1 per cent, depending on the trading history, nature and volume of credit, credit monitoring, experience of debt loss, trade sector, customer base etc. When political risk coverage is included, the premium may be higher.

Underwriting Aspects

Credit Limits

- Assigned for each buyer
- Represent peak outstanding of that buyer
- Approval for a specific credit limit on each buyer
- Credit limit parameters:
    - Credit worthiness of the buyer
    - Maximum outstanding balance
    - Credit period

Credit Period

(Maximum period not to exceed 180 days)

- Maximum credit period to be specified in the policy
- Extension of due date
- No extra charge or prior approval required if within the maximum credit period
- Prior approval required if due date exceeds maximum period as per policy

Credit Risk Assessment

- Customers' ability to pay

- Their willingness to pay
- Debtors' Turnover Ratio - a high ratio naturally means vulnerability

Customers' Ability to Pay

(It is analyzed in view of following aspects)

- Customers' Annual Report
- Credit Rating of Customers
- Market Knowledge
- Visits

Annual Report to be Analyzed

- Balance Sheet showing financial resources and their use
- P/ L A/C shows profitability
- Creditors/Turnover Ratio & Debtors/ Turnover Ratio

Credit Rating of Customers

- Using available company data
- Rating varies with availability and quality report

Market Knowledge

- Industry Performance
- Company performance compared with industry

General Exclusions in Credit Insurance Cover

Following losses are not covered by Credit Insurance:

- Loss from trade disputes

- Sale to subsidiary & associates
- Sales made against irrevocable letter of credit
- Pre-shipment Loan
- Nuclear explosions & contamination
- Devaluation & depreciation of currency
- Interest on late payment
- Loss of credit from War between France/UK/US/China/Russia

International Perspectives of Credit Insurance

To understand the credit risks, we may simply refer the US$1.5tn subprime credit causing greatest financial crisis in the world. The US Government has made largest financial bailout of US$700bn to buy troubled financial assets. The US rescue measures plan in this credit crisis this year may run up to US$1.8tn, which is equivalent to about US$6000 per American and about US$15000 per US household. The Goldman Sachs and Morgan Stanley – the two formidable names in finance have eaten up their pride and expertise to convert into ordinary banks today because of their poor financial risks management. In India, 9 largest commercial banks including SBI, ICICI Bank, HDFC bank have hade exposure of bad credit risks of about US$420mn in US financial giants that have collapsed today. The Indian Bank have already lost about Rs 400 crores due to their because of their bad investments in the financial instruments of troubled US financial giants like Lehman Brothers and AIG. The dangerous bubble of derivatives amounting to US$677tn has burst today putting the whole world in the jitters. We observe the following aspects from International perspective:

- Over the last 5 years there has been increasing interest by regulators and other market bodies in US, UK, Canada, Japan and Bermuda in the subject of credit risk transfer between insurers, reinsurers, banks, and other financial institutions.

- Credit insurance in the form of Credit derivative, securitization, and insurance of credit risks has grown rapidly for last 5 years and finally resulted to global financial meltdown today.

- The regulators are concerned with two major issues in Credit Risks transfer.

Certain Problems Perceived In Credit Risk Transfer

- Considering above International Association of Insurance Supervisors (IAIS) observed that:

  - o Most Existing data on Credit Risk Transfer relate to overall market statistics and do not provide deeper insight into underwriting of Credit Insurance exclusively.

  - o There is no definitional boundary between Credit Risk Transfer (underwriting Activities) and Investment activities.

- AS per British Bankers Association (BBA) Report, 2002 Insurance industry globally accepted around US$667bn credit derivative.

- However US$667bn represented less than 5 per cent of total assets of insurance industry. In 5 major economies (Europe, US, Africa, Asia and Canada) indicating that credit derivative is relatively small in comparison of the total assets of insurers' investments.

- In the absence of traditional boundaries, it is very difficult to collect specific data on Credit Risk Transfer Activities considered underwriting and investment activities, which provide the foundation of Credit Risk Insurance.

- Global Credit Derivative market has been growing at brisk pace since 2000.

- Insurers have been actively selling credit protection structured as Insurance products or credit derivatives but difficulties arise to identify investment activities where insurers take on Credit risks in other forms such as Collaterized Default Options (CDOs).

- As per BBA report of 2002 Credit Derivative would reach US$5tn which would also raise market share of Credit Risk transfer to insurers and re-insurers.

- Besides structured insurance products on Credit Risk, insurers have been taking on Credit Risks in Credit Default Obligation (CDO) and Credit Linked Note (CLN).

- Sometimes Credit Risk Transfers are effected within group particularly conglomerates as a means of minimizing regulatory capital which is not a driver of Credit Risk Transfer growth.

- But whichever mechanism is adopted for Credit Risk Transfer insurers are experiencing large losses almost everywhere. Today's AIG collapse is due to huge loss from Credit Insurance on Financial Derivatives.

- Capital adequacy supported by strong risk management system is the key to Credit Risk Transfer business for insurers and re-insurers, which AIG has failed to do.

- Supervisors have been always placing greater reliance on Risk-management and sound investment policy of insurers.

- Credit Derivative a common product for transfer of Credit Risks. It's a contract providing for payment by the insurer (protection seller) to the insured (protection buyer) occurrence of a credit event. A Credit event means a failure to pay or insolvency. Credit Derivative serves similar purpose as credit insurance does.

- The International Swaps and Derivative Association (ISDA) have taken initiatives for collection of data from borrower for assessing creditworthiness of borrowers for risk assessment purpose. Banks and financial institutions including insurers and re-insurers use these data for risk assessment for accepting risks.

- In 2003, CDS rose to US$3.6tn, but long-running bankruptcy proceedings of Enron Corporation had cast shade over the entire market.

- After Enron bankruptcy major questions have come whether buyers of US$2.4bn CLNs tied to Enron Credit worthiness and underwritten by Citigroup will get paid and if so, how much they will receive and from whom?

- Procedure in brief: Protection buyer pays premium for the cover until credit events occur. Following a credit event the particular buyer will receive compensation for the loss on asset. The contract is drafted with confirmation document & legal agreement.

Credit Default Swap (CDS) and Credit Insurance

- Only Vanila credit Derivative and CDO are commonly used as Credit Transfer instruments.

- Because of increased complexities and blurring the boundaries of investment and Credit Transfer with variation in the terminology being used here and there it is very difficult to distinguish them.

- CDS is a contract that enables one party (Protection of buyer, insured) to buy protection against the risk of default of specified reference asset issued by a specified reference party from another party, i.e. protection of seller or insurer.

- But this sort of Trade Credit Insurance created a lot of dispute after the Enron bankruptcy. It is also evident that Banks use Credit Default Swaps due to inefficiency weakness in market.

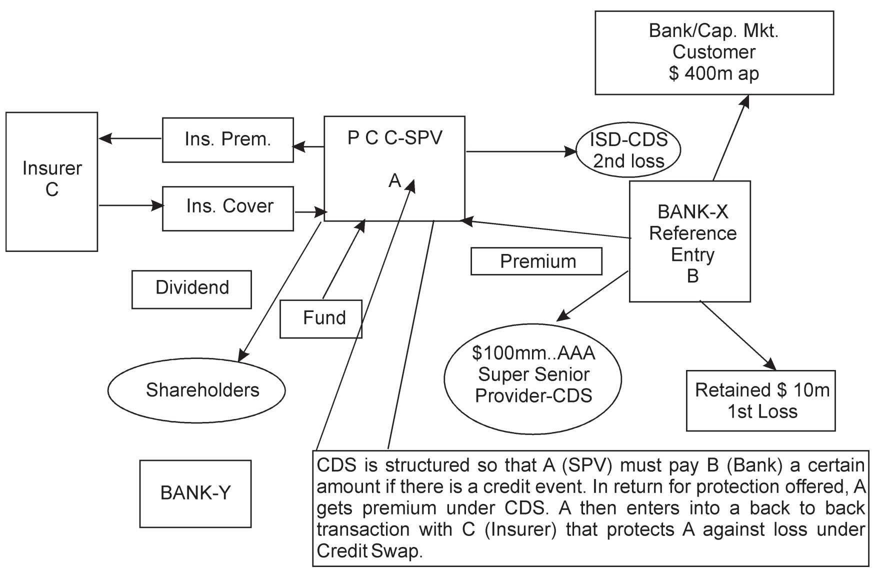
- When the borrowers involved fail to make payment of interest and principal, the buyer of the protection can exchange the debt it holds for cash from the sellers of Swap.

Hybrid Credit Risk Insurance Mechanism/ Model

The Graph-2 presents the Hybrid Credit Risk Insurance Mechanism.

Graph-2: Synthetic Securitization – Credit Insurance

Synthetic Securitization –Credit Insurance



Other Credit Derivatives: Basic Features

CLN

- A bilateral security containing an embedded credit derivative which cannot be separated from fixed income instrument.

- Note is linked to both credit-worthiness of issuer and underlying obligation of issuer to pay excess amount over par value of note.

- The Protection seller/ investors receive excess on regular coupon and par value of note at maturity if no credit event occurs.

- If reference asset defaults, net amt received by protection seller is deducted at maturity. It is deemed funded credit derivative.

CDO- Collateralized Obligation

- A CDO is a security whose payoff is derived from credit performance of a portfolio of a debt obligation-a variation of an asset-backed security.

- A bank may sponsor CDO to which it the transfer Credit Risks.

- Objectives of the sponsor of a CDO are to: i) obtain protection against credit risks; and ii) to earn profit from managing a portfolio of Credit-risk business.

- Motivation of this transfer is to exploit the bank's funding cost advantages.

- CDO – a funded vehicle in which investment is made by beneficiaries of C.

- It offers risk-return mechanism for CDO investors.

18
MARINE HULL INSURANCE

Scope of Cover

Hull insurance is a specialized insurance and needs underwriter's proper knowledge, skill understanding on various aspects such as types of hulls, value age construction, and capacity (tonnage) nature of cargo carried registry classification trading warranties etc. Hull insurance deals in the insurance of hull and machinery of ocean-going and other vessels like barges, trawlers, fishing and sailing vessels. It also covers the ship-owners' other insurable interests, known as subsidiary interests, like freight and disbursements. Hull insurances also deal in Insurance of "construction risks" or "builder's risks" for vessels when they are under construction. Apart from these, there are certain special types of hull covers such as Chatterers' Liability risks, Ship Repairers' Liability risks, Third Party Liability risks, etc., which are underwritten on a very selective basis where they are specially needed by valued clients. Insurance of offshore oil/gas exploration and production units as well as associated construction risks are also covered by hull insurance.

Precisely, Hull Policy covers any loss or damage to ships, vessels, tankers, bulk carriers, and selling vessels including Hull and Machinery, Freight, Disbursements and various liabilities. Hull policies are issued to ship-owners, ship-builders, charters, bankers or financiers of ships or vessels with Insurable interests. Thus the subject matter of Hull Insurance may include various properties. Ship-owners take marine insurance for their ships, freight, disbursements, and other interests against the under-mentioned marine perils. Hull insurance for vessels when they are under construction are called "construction/Builders' Risks" Insurance. Insurance of Oil Drilling Rigs and Offshore Oil platforms as well as allied construction risks is a recent, but a major development in marine.

Categorization of Vessels

The vessels are broadly classified into following two groups:

a. **Mechanically Self–propelled Vessels of Steel Construction –** Classed with Lloyd's register of shipping or any other internationally recognized Classification Society such as Indian Register of shipping (IRS), these vessels may be any of the types like liners, or tramps carrying cargo or passengers either for domestic trade or international trade.

b. **Smaller Crafts of Local Origin, Built of Steel** — Wood or fibre glass which is not subject to any classification is under this category. Generally, such crafts are used in inland waters, postal areas or within port areas or harbors. During tariff reason a scheme introduced by GIC in consultation with TAC for classification of postal crafts like barges, trawlers, tugs used for rating purpose.

Underwriting Aspects

In Marine Hull Insurance, underwriting considerations are many in number, of which only a few of them are briefly discussed below:

General Considerations

- Type of the vessels
- Construction (Steel, wood, composite or fibre glass)
- Name of builders and place of building the same
- Age and tonnage of vessel
- Dimensions (Length, breadth, draught etc.)
- Whether vessel is equipped with twin screws, Double bottom, Collision bulkhead
- Method of propulsions and particulars of engines (Makers,

type of engine, fuel used, number of propellers, number of cylinders

- Particulars of FEA
- Classification Society
- Whether registered under Merchant Shipping Act
- Date of last survey
- Port of registry and Registration Certificate No
- FOC country
- Trade in which vessel is engaged
- Trading Warranties and navigational limits
- Nature of cargo usually carried
- Singleton or fleet
- Claim experience for last 5years
- Ownership and Management details
- Conditions to be imposed or the amount of deductible
- Period of insurance for Time policy or details of voyage in case of voyage policy
- Number of crew and officers and qualification of masters
- Place and period of being laid-up
- Usual repair costs
- Whether covered against P&I risks
- Probability and severity of loss in similar risks

Valuation of Vessel

It should be neither too low nor too high. Too low indicates high moral hazards while too high value will be adverse underwriting for CTL. It is important to mention that Section 77(1) of Marine Insurance Act provides that unless the policy otherwise provides, the insurers is liable for successive loss even though the total amount of such losses may exceed the sum insured. So unless there is TL or CTL, under insurance is very costly for insurer. Some of the above aspects are discussed more elaborately below for better analysis.

Types, Age and Designs of Ships or Vessels

There are many types and designs of ships or vessels, which need to be examined for identification, selection and classification of risks before the risks are accepted and rated. Most of them are constructed of steel and welded and they are capable of sailing on the seas in ballast or with cargo. After construction of a vessel, it has to be registered and a certificate of registration is obtained as per Merchant Shipping Act and other Government regulations in this regard. For risk analysis, following aspects are considered as discussed below.

Volume in Cubic Capacity of the Ship

Gross Register Tonnage (GRT) is calculated by dividing the volume in cubic feet of the ship's hull below the tonnage deck, plus all spaces above the deck by 100.

Net Register Tonnage (NRT) is the gross tonnage less certain spaces (viz. machinery, crew accommodation, ballast spaces) and is intended to encompass only those spaces used for carriage of cargo.

Deadweight Tonnage (DWT) means the capacity in tons of the cargo required to load a ship to her load line level.

Classification Certificate

The Classification Certificate issued by IRS would confirm that a ship registered under it has been built according to its rules and that it has both structural and mechanical fitness for the intended service. This is an important document for underwriter.

Management or Ownership of Ship

It is very important consideration for determining the moral and morale hazards associated with risks to reduce the scope of maritime frauds which are very common in marine insurance.

Route of Voyage or Ports Covered

This aspect is an important analysis in consideration of safety, security and maintenance of the ship, resulting into both physical and moral hazards.

Nature of Cargo or Carriage

There are many types of vessels, namely, General cargo vessels, Dry bulk carriers, Liquid bulk carriers, and Passenger vessels as discussed below more elaborately to identify and analyze the risks associated with the line of carriage and nature of cargo. Nature of carriage and cargo has had important bearing on risk element and rating factor.

Risk Analysis and Risks Conditioning

If above risk analysis shows adverse results, following actions are taken:

- Imposition of proper warranties
- Limiting the scope of the cover
- Imposing the adequate excess or deductible; Deductible applies to all partial loss claims including particular average repair costs, dry-docking, Sue and Labour charges, salvage charges, Contribution to general average claims under collisions
- Loading of premium

Deciding Declined Risks

Each insurance company maintains a list of Declined Hull Risks according to its underwriting policy and reinsurer's prescriptions. However following is the list of declined risks in general:

- Older Country crafts
- Vessels over 20 years old
- Towage Risks of wooden vessels
- Ship-breaking risks
- Small boats
- Yatches
- Vessels with very high claim ratio
- Risks declined by other insurers

Types of Ocean-going Vessels

There are basically four main types of sea going vessels, namely: General Cargo Vessels, Dry Bulk Carriers, Liquid Bulk Carriers, and Passenger Vessels. These can be further divided into ocean-going and coastal tonnage. The ocean-going general cargo vessel is usually in the 5,000 to 15,000 GRT range. This category also includes specialized vessels, such as container ships, barge carriers (LASH-lighter Abroad Ship), RO-RO (Roll on, Roll off) vessels, Reefers (Refrigerated Vessels) etc. Many general cargo vessels are built for specific purposes, e.g. car carriers, livestock carriers, log carriers, heavy lift vessels, etc. We have discussed below the types of vessels and the risks associated with them for the purpose of risk identification and risks analysis and underwriting of marine hull insurance.

Liners and Tramps

General cargo vessels may also be sub-divided into liners and tramps. Liners are better managed and better maintained because they must keep to a time schedule. Liner services require a huge capital investment. It therefore obviously follows that owners wish to protect this by employing quality management. The strict requirements of liner services mean that the vessels must be fit and well maintained at all times. So, the average age of liner vessels is less than that of tramps. Liner services attract a better standard of officers and men. In boom times, when there is heavy demand on tonnage, even older tramps, which may have been laid up for years, are brought into service. These constitute an inferior risk and would call for special underwriting attention. All these aspects indicate that lines are better risks than tramps, which the underwriters have to take into account while deciding acceptance of risks.

Coastal Tonnage

Many of the considerations that apply to oceangoing vessels also apply to coastal tonnage and the distinctions between liners and tramps apply in the same way. Coasters are generally smaller in size and many are engaged in the carriage of bulk cargoes. So, coastal voyages are often of considerable length. Moreover, weather conditions during monsoons over the entire coast like of India call for special underwriting attention. However, coastal tonnage does not have to withstand the same strains as ocean-going vessels. Coastal vessels enter and leave ports more frequently than ocean-going vessels and they often operate in congested waters. Therefore the risk of collision and damage from contract with quays and piers is greater for coastal tonnage.

Dry Bulk Carriers

These are specially constructed vessels in the size range of a few thousand GRT used for coasters to over 70,000 GRT for ocean-going tonnage. The main bulk cargoes carried are iron and other ores, coal, grain, bauxite and phosphates. The main features of these vessels are the single weather deck and large holds with wide hatches to facilitate loading and discharge by mechanical means. For underwriting of such type of hull an underwriter will have to consider important aspects like: i) Nature of cargo carried; ii) Routes; iii) Whether vessel is converted to carry bulk cargo: iv) The extent of such conversion; and v)Whether vessel is a safe vessel from the point of stability.

Liquid Bulk Carriers (Tankers)

Tankers are strongly constructed and are fitted out to carry bulk liquids (e.g. crude oil). The effect of liquid cargo on the stability of the vessel is considerable. Therefore, tankers have wing tanks on either side of the centre tanks and no double bottom. Other aspects from the underwriting point of view are:

- Collision damage is more costly to repair, as tankers have longitudinal framing rather than the conventional transverse framing of general cargo vessels.

- Due to the "live" nature of the liquid cargo, tankers ordinarily sustain heavier damage than other cargo ships, if they go around.

- A tanker has a shorter life than a general cargo carrier, as many liquids have corrosive effect upon steel, spirit being worse than crude oil in this respect and molasses being more corrosive than either.

- There is considerable danger of fire and explosion, particularly during and after discharge operations, since dangerous inflammable gases form within the tanks.

- The risk of pollution following a casualty makes salvage operations more difficult and expensive. In some cases of serious damage, governments may deny entry to ports and may require the tanker to be taken to distant waters and sunk.

Super Tankers

The terms super tanker, very large crude carrier (VLCC) and ultra large crude carrier (ULCC) are used for huge tankers of 75,000 to 150,000 DWT tons, 150,000 to 300,000 DWT tons and 300,000

DWT tons and more. These tankers are subject to following extra hazards:

- Tankers of 100,000 DWT tons fully loaded may draw 47 feet and would encounter limitations in approaches to harbors. It therefore becomes necessary in serving certain ports to lighten part of the cargo before the vessel proceeds to her discharge point. This may be done in unprotected waters and uncertain weather.

- VLCCs are unable to pass through the Suez Canal when fully laden. Therefore they have to take the longer sea passage via the Cape of Good Hope and return in ballast via Suez.

- These giants cannot maneuver easily, nor can they steer below a minimum speed. Consequently, very careful navigation is required.

- Structural weakness may arise during the voyage. As repair facilities are available only in select docks, repairs are generally costly.

- There have been a number of violent explosions on these vessels when in ballast and when undergoing tank-cleaning operations.

Combination Carriers

They are specially designed so that they can carry bulk dry cargoes as well as oil and thus provide greater flexibility in operation. These vessels may be of two types: ore/bulk/oil (OBCs) in 70,000 to 150,000 DWT range and Oil/ore vessels in 150,000 to 250,000 DWT range. Some bulk trades are seasonal. Oil shipments are more frequent in winter than in summer. In such circumstances, the combination carriers switch from one trade to anther according to the respective trade requirements and the state of the freight market. A combination carrier has large hatches, so that bulk cargoes can be loaded and discharged. The hatches do have special covers with sealing devices so that the tanks can contain the oil cargo without spillage. The central section is used for the carriage of ore while the tanks are used for oil.

Containers Vessels

These vessels are meant for carriage of fully laden container cargo and are normally engaged on a fast liner service between specific ports. Container vessels require special shore and discharge facilities. The carrying capacity is normally very high in the number of containers being carried, namely: i) 20-foot equivalent units (TEUs), i.e. up to 20 tons capacity; or ii) 40 foot equivalent units (FEUs), i.e. 40 tons capacity. Important underwriting considerations are loss of containers overboard and the exposure to very high values for hull and cargo combined.

Lighter Abroad Ship (LASH)

LASH and Sea Bee vessels are mother ships, which carry “floating containers” in the form of barges up to 1,000 tons displacement. Barges are transported to an overseas port area when they are lowered into the water and towed to their ultimate destination.

Roll on – Roll off (RO-RO) Vessels

A RO-RO vessel provides the facility for shipping lorries, and trailers, etc., without use cranes. A huge amount of cargo is carried on trucks and trailers which travel direct from the shippers’ premises in the country of origin on RO-RO vessels via stern, bow or side doors, and delivered to the consignees’ premises at the final destination point in the same vehicle. This of operation is used for ferries of trucks and trailers etc. carrying cars and buses. Use of RO-RO vessels is of particular value in serving ports with inadequate handling facilities. When the RO-RO facility is used, the cargo remains on the same vehicle right from the time it leaves the premises of the consigner till it reaches the final destination point. Handling at ports is dispensed with.

Passenger Vessels

These are cruise vessels or passenger liners which sail on voyages to distant areas of beautiful but rocky or shallow coasts or near the icy waters of the Arctic and Antarctic. Most of these vessels posses' modern navigational systems, for example, satellite navigation. Risk of fire perhaps remains the greatest hazard in such type of vessels.

Fishing Vessels

Fishing Vessels are generally built of wood, steel or fibre. Types of craft differ according to the sort of fishing process pursued, the waters in which the fishing takes place, Geographical or physical features of the area of operations. Class/Un-classed vessels however, require to be surveyed out of water and all machinery should be thoroughly examined. Insurance of fishing vessels in India was governed by a special Tariff which has prescribed a special proposal form designed to extract all relevant information with regard to the owner and the craft, experience of the skipper, type of fishing, geographical limits, past insurance and claims history, etc. In the detariff regime, we should take special care also because of its high probability of loss. The amount of deductible will depend upon the age and size of the vessel together with the owner's past claims record. All such physical and moral hazards are considered for underwriting of such type of vessels.

Offshore Oil/Gas Exploration & Production Units

These units are constructed in connection with either exploration or for commercial production of oil or gas from the ocean beds. They are made like artificial islands where the risks are very high in various forms and ways indicated hereinafter. A comprehensive cover is generally given to cover plant& machinery, various operations, and transport of P&M, products and stores and PA of employees in the units. The probability and severity of risks depend on the structure, construction, size and location of units. They are located hundreds of kilometers away in the mid-sea as is Bombay High Offshore. Broadly, there are four main types of off shore units for oil/gas exploratory drilling:

1. The jack-up units are self-elevating platforms, which can float freely with legs retracted by a jacking system for

movements in tow. Prime considerations are the design and efficiency of the jacking system and its proper operation, the nature of the sea bed and methods of coping with the penetration of the legs in soft or uneven bottom areas. Casualties have occurred mainly during tows or whilst jacking up or down.

2. The semi-submersible or column stabilized drilling platforms can be bottom supported and/or free floating. These units are larger and more expensive than the jack-up type. They can operate in deeper water and usually have a multi-anchoring system employing up to 10 separate lines.

3. The ship-shape unit is basically a modified conventional ship, with a slot for drilling through, located in the centre.

4. The fixed structure is usually a platform constructed on four or more piled legs. These platforms are put together at sea usually with the aid of special heavy lift crane barges. As the platforms are stationary, they are naturally constructed on known oil or gas fields. When exploratory drilling is completed, these units can be used as production platforms or stations. All such factors are considered for underwriting of offshore oil/Gas Exploration & Production Units.

Specific Underwriting Considerations for Offshore Oil/Gas Exploration Units

Following are the underwriting considerations for offshore oil/ gas production unit:

- **Professional Approach, Analysis of Risks:** Underwriters engage professional engineers and obtain professional advice. Technical appraisal is obtained from Classification Societies and specialist surveyors regarding structural strength and seaworthiness of the units.

- **Quality of Professional Management (Technical and Financial):** Factors like safe operating procedures, a good recruitment and training programme, good staff relations, all lead to increased efficiency, increased production and fewer casualties and claims and risk improvement.

- **Development of Corrosion Damage:** As these platforms are fixed in sea water in most cases, there is the problem of marine growth and corrosion and consequent high physical hazards.

- **Size of Structure and Local Weather Conditions:** There is considerable risk involved in towage of large structures and these risks have to be weighed carefully as also local weather conditions.

- **Preventive Measures Collision Risks:** It is always a risk for structures floating or fixed at sea. Its probability and severity are of important considerations.

- **Fire Fighting Arrangement:** This peril is always a major hazard associated with the possibility of a "blowout". Bombay High fire on 23 April 2007 is the worst accident in the history of ONGC in terms of property loss in ONGC history.

- **Past Records of Earthquake & Tsunami:** Effect of an earthquake on equipment concentrated over an oil field could be major catastrophic.

Types of Polices

Following types of policies are available in Marine Hull department to cover ship owners various insurable interests:

Hull and Machinery Insurance

This policy covers the hull, machinery, equipment and stores etc. on boat but not cargo. The policy indemnifies the ship owner against partial loss, total loss either actual or constructive, general awareness, salvage charges, sue and labors expenses and ship owners liability towards other vessels due to collisions. Normally, three fourth of the collision liability is covered under this policy and remaining one fourth may be covered with Protection and Indemnity

(P&I) Clubs. Under certain circumstances the Hull and Machinery policy is extended to cover ship owner's liabilities towards port authorities for removal or wreck of the vessel and damage done to docks, jetties, wharfs etc.

Freight Policy

The earnings of a vessel described as Freight for Time can be insured up to 25 per cent of the Hull value provided no additional insurances on disbursements are granted. This is subjected to ITC freight clause of 1 October 1983 which provides an indemnity for loss of freight. Any claim on loss of time whether arising from a peril of sea or otherwise is specifically excluded. This insurance also does not cover partial loss of freight other than general average loss under 3 per cent excess unless caused by fire, sinking, standing. The contribution of freight towards general averages, salvage charges and sue & labors expenses are also covered. The salient aspects of this policy have been discussed separately.

Disbursements and Increased Value Insurance

These are ship owner's own expense incurred in fitting out and provisioning the vessel and other items not included in the hull valuation. An amount up to 25 per cent of the hull value may be insured provided no freight insurances are placed. The conditions are against Total and/or Constructive Total loss of vessel, Plus Excess Liability for collision, general average, and salvage and salvage charges and sue and labors charges arising where there is a shortfall between the insured value of the vessel and contributing value of the vessel for claims purposes.

Premium of Insurance

Sometimes policy is issued to ensure the premiums as the cost of all insurance are quite substantial on a reducing basis implying that amount of indemnity gets reduced by one twelfth every month. This policy covers premium of hull and machinery, freight and disbursements interests including premium on.

Return of Premium

There may be a policy to insure the prospective return of premium on Total Loss Only condition return of premium for lay up or under repair are recoverable only at the expiry of the policy period as such returns are payable only with condition that vessel has not been a total loss within the policy period.

Loss of Hire Insurance

This policy covers loss of higher charges suffered by a ship owner when the ship given on a charter is laid up for repairs following an accident from the perils covered under Hull and Machinery policy. The condition applicable to this policy is those covered by the ITC-Hulls but excluding total loss. This policy is issued with a stipulation that repairs must be commenced within 12 months of the expiry of the policy. The important underwriting considerations for such a policy are age, size, trade of the vessel, ownership record, management and past experience.

Loss of Profits Insurance

This policy covers the loss of profits of a Charter over the period of the Charter if the vessel is time chartered or loss of profit during the voyage following a total loss of a vessel if the vessel is chartered for a voyage.

Institute Times Clauses – Hulls – Salient Features

Various ITC Clauses

The Institute Time Clauses-Hulls (1.10.83) (ITC-Hulls) from the basis of the Marine Hull Policies. There are certain variations in this clause according to the specific purposes of cover, but in general all policies find their basic condition set out in ITC Hulls. Following are the few variations provided by the various clauses:

1. Institute Time Clauses- Hulls-Total Loss-General Average and ¾ Collisions Liability (1.10.1983)

2. Institute Time Clauses- Hulls- Total Loss Only (Including salvage, Salvage Charges and Sue and Labor 1983)

3. Institute Time Clauses- Hulls- Disbursements and Increased Value (Total Loss Only including Excess Liabilities) 1983

4. Institute Time Clauses- Hulls- Excess Liabilities

An underwriter must have a proper understanding of all- Institute Time Clauses- Hulls, as mentioned above as they are foundation of all Marine Hull Policies.

Cover Provided By ITC Hulls

The ITC Hull provides the following covers:

(a) Total loss of the insured vessel of both actual and CTL.

(b) Cost of repairs for damage to the insured ship by insured perils. This includes particular average damage and general average sacrifice.

(c) Unpaired damage: A reasonable allowance for depreciation in the value of the insured ship by reason of damage remaining un-repaired at the expiry of the policy provided the ship has not become a total loss during the period of policy.

(d) Sue and Labor expense incurred in connection with an insured peril.

(e) Salvage Charges.

(f) General Average contribution paid or payable contribution for general average act required by an insured peril.

(g) Collision Liability i.e., legal liability that the assured may incur by way of damages to the owners of any other vessel or cargo therein, going to a collision caused by the negligence of the insured vessel.

Deductible: a specified amount is deductible from claims arising from each separate accidents or occurrence other than Total Loss or Constructive Total Loss of the vessel.

Termination (Clause 4)

This insurance shall terminate automatically if any of the following situations arise unless the underwriters agree to the contrary in writing:

(a) Change of classification of society.

(b) Change, Suspension, Discontinuation, withdrawal or expiry of the class of vessel. It is pertinent to mention that if the vessel is at sea, such automatic termination as above shall be deferred until arrival at the next port of call. The cover however continues uninterrupted during any suspension of class, which is due to an insured casualty situation, unless the vessel leaves her next port without the approval of the classification society.

Change, Voluntary or Otherwise

- Ownership or flag;
- Transfer to new management;
- Charter on a bareboat basis; or
- Requisition for title or use of the vessel.

If the vessel has cargo on board and has already sailed from her loading port or is at sea in ballast, such automatic termination shall be deferred until arrival at final port of discharge if with cargo or at port of destination if in ballast. In the event of requisition for title or use without the prior execution of a written agreement by the assured, the clause gives the owners 15 days cover during which to regularize their affairs with the requisitioning authorities. When the Termination Clause operates a pro rata daily net premium is admissible.

Assignment (Clause 5)

For the purpose of assignment of policy, the following requirements are to be complied:

- Notice of assignment duly signed by the assured or the assignor in case of subsequent assignment must be served to he underwriter.
- Endorsement to be passed on the notice.

No claim will be admissible unless endorsement is passed.

Perils/Risks (Clause 6)

The policy coves the following perils causing loss or damage to the property or the liabilities mentioned above. ITC-Hulls (1.10.83), which consist of 26 clauses, provide the widest cover for hull and machinery interests. The perils covered by hull policy are classified under group 6.1 and 6.2 under Clause No.6.

Perils Under 6.1

- Perils of the seas, rivers, lakes or other navigable waters
- Fire, explosion
- Stranding, sinking etc
- Overturning, derailment (of land conveyance)
- Violent theft by persons outside the vessel
- Collision
- General Average Sacrifice, Sacrifice, salvage charges
- Jettisons
- Piracy

- Breakdown of or accident to nuclear installation or reactors.
- Contact with aircraft or similar objects, dock/harbour equipment or installation
- Earthquake volcanic eruption or lightning

Perils Under 6.2

- Negligence of Master, Officers, Crew or pilots
- Negligence of repairers, or chatterers,
- Accidents in loading, discharging or shifting cargo or vessels
- Bursting of boilers, breakage of shafts or any latent defect in the machinery/hull.
- Battery of Master, Officers or crew

Provided such loss or damage arising from the perils of under 6.2 has not resulted from want of due diligence by the assured, owners or managers as the assured has some control over the perils specified under this group, while he does not have any control over the perils under 6.1. However the onus of proof for want of due diligence is upon the insurers if they wish to avoid a claim on that ground i.e. “want of due diligence”.

Pollution Hazards Clause (No.7)

As per this clause cover is granted if the vessel is damaged or destroyed by a government authority in order to avoid pollution hazards, for example when a badly damaged tanker is deliberately set on fire. The act of the government authority must directly come from the casualty covered by the insured perils and the assured must have done his best endeavours to prevent pollution.

$3/4^{th}$ Collision Liability (Clause No. 8)

It provides the indemnity to the assured for $3/4^{th}$ of any sum paid by the assured to any other person by reason of the assured's legal liability to pay for damages for any of the following situations:

- Loss or damage to any other vessel or property on any other vessel;
- Delay to or loss of use of any such other vessel or property thereon; and
- General average or salvage of, salvage under contract of any such other vessel.

The indemnity provided by this Collision Liability Clause is in addition to the indemnity provided by the other scope of the policy. Only the following types of losses are admissible under $3/4^{th}$ collision liability clause. The assured is to bear $1/4^{th}$ of the amounts paid in respect of the following items covered by this clause:

- Total loss of the other ship or property
- Cost of repairing other ship
- Financial Loss arising from the use of other ship or property thereon.
- Financial loss arising from delay of the other ship (also known as demurrage)
- Compensation for the loss suffered by damage to property on the other ship
- General Average Sacrifice
- General Average Contribution paid by the other ship or property thereon.
- Contributions to Salvage awards incurred by the other ship or property thereon
- Payment incurred by the other ship or property thereon for salvage services.

- Legal expenses incurred by the assured with the consent of the underwrites

Such additional indemnity will be subject to the following conditions:

- Where the insured vessel is in collision with another vessel and both the vessels are to blame, then unless the liability is decided by law, the indemnity shall be calculated on the principle of cross liability as if the respective vessels owners had been compelled to pay to each other such proportion of each others' damages as may have been properly admissible in ascertaining the balance payable by or to the assured in consequence of the collision.

- The underwriters will also pay 3/4th of the legal costs incurred by the assured with the prior written consent of the underwriters.

Exclusions

There is no liability of the underwriters under this clause in respect of:

- Removal or disposal of obstructions, wrecks or any other thing

- Any real or personal property except other vessel or property thereon

- The cargo or other property on, or the engagements of the insured vessel

- Loss of life, personal injury or illness

- Pollution or contamination of any real or personal property

Hull Rating

Generally following are the important factors generally considered for rating hull:

- Vessel type, age, tonnage, trade-hazards & limits,
- Management & Ownership
- Past Claims Ratio
- Valuation of the vessel
- Classification Society and maintaining the class
- Type of insurance
- Underwriting experience of similar risks

For the purpose of calculating the rate of premium to be charged for various hulls, the hull risks are divided basically into following two parts:

1. Total Loss Element of the risk
2. Average Loss Element (other than total loss element known as "ex T.L.")

Customarily separate rates are decided for the above to elements so as to arrive at the overall rate for the policy, which is called the "slip rate". The Total Loss Rate is generally taken as the current market rate for the Total Loss. It is applied on the insured value of the hull after adjustment by value factor of the ship.

The "ex. T.L." rate is mainly determined by the size of the ship. Generally it is a fixed amount multiplied by DWT of the vessel or GRT. DWT is the capacity in tons of the cargo required to load a ship to her 'load line level'. The use of DWT of the vessel is justified in view of the fact that the deadweight tonnage represents a vessel's carrying capacity. It also signifies the size and earning capacity of a vessel. GRT means the volume of the interior of the vessel including all spaces, which are permanently closed and expressed in tons of hundred cubic feet. In case of passenger vessels the GRT is generally used for calculation. LPG/LNG carriers are generally rated on their carrying capacity measured in cubic meters. The tankers and bulk carriers are rated on the DWT. The tonnages are generally ascertained by reference to the Lloyd's Register.

Total Loss Rate of the vessel will be fixed of the various factors as mentioned earlier. The "ex. T.L." premium rate is decided in consideration of some additional factors over and above the factors used for Total Loss Rate. The additional factors are the condition of the vessel, availability of the repaired facilities, degree of its sophistication, trading limits, etc. As mentioned earlier, the above two rates constitute finally the slip rate which is ported to the client.

Example: From the following particulars we may calculate the premium and slip rate for the ship named MV Ashok:

- The vessel .... M..V. Ashok
- Line International Shipping Line
- Year Built 1990
- GRT 15,000
- Insured Value .... Rs. 20,000,0000
- Cargo Carried .... General
- Trading Limit .... World wide
- Total Loss Rate 0.50%
- "ex. T.L. Rate" .... Rs. 50 per GRT
- Deductible .... 10 lakh

Calculation of Premium

(a) Total Loss Premium:
@ 0.50% on Rs. 20,000,0000 10,00000

(b) Ex. T.L. Premium
@ Rs.50 per GRT= 50 x 15000= 7,50,000

Total premium (a + b) 17.50.000

(c) Slip Rate…17,50,000/ 20,0000000x 100 .... 0 .875%

Freight Insurance – Salient Aspects

Freight for specific voyages or anticipated freight may be insured in the following cases:

- Partial Loss
- Total Loss

Freight-A real and substantial property of the ship-owner at risk in marine adventure as is the ship and the cargo in it.

Insurability of Freight

- Prepaid Freight: Freight pre-paid or payable in advance is at the risk of the owner of the cargo and is included in the cargo value in cargo policy.
- Freight Payable "ship or cargo lost or not lost": Freight payable irrespective of delivery or non-delivery of cargo. It is at the risk of cargo-owner, but not ship owner.
- Freight payable on delivery: Carrier is not entitled to freight if cargo is not delivered. If delivered in damaged conditions, the carrier is not deprived of right to freight.
- Lump sum Freight: In some special contract of carriage which entitle the carrier to receive the lump sum freight even before the whole delivery of cargo.
- Time Charter Freight: Freight payable to ship-owner for the use of his ship for carriage of goods for a specific period of time. It is generally payable in advance monthly with a term that if the vessel fails to operate due to some certain events

for more than 24 hrs, the payment of hire will cease until it is operational. It is a risk of ship-owner.

Risks of Loss of Freight to Carrier (Ship-owner/ Charterer) arise either from Loss of Ship or Loss of Cargo. But there is no risk when freight is prepaid/ paid in advance and is not refundable (mentioned above)

Insurance of Freight Risks with Standard Clauses

- Institute Time Clauses –Freight (1.10.83)
- Institute Voyage Clauses—Voyage (1.10.83)

Policy is generally on Time basis of 12 months. There may be additional policies on voyage basis if any particular voyage exceeds the SI for time. Freight Insurance Policy may be either Valued Policy i.e. Agreed Insured Value of Freight insured or Unvalued Policy, i.e. Insurable Value laid down by S18(2) of MI Act 1963. Gross amount of freight at the risk plus of the assured plus charges of insurance and earning freight.

19

CLAIMS – SURVEY AND SETTLEMENT

Prime Functions

Insurance has got three prime functions: Underwriting, Claims-settlement, Investment and Accounting. Thus claims-settlement is one of the prime functions of insurance company. The success, survival and growth largely depend on the insurer's ability to settle claim properly and promptly. The techniques and procedures of claims-settlement depend on the nature and types of insurance. The procedures followed for settlement of property claims are absolutely different from those followed in the liability claims. In this chapter procedures for major property claims like Fire, Marine and Motor claims and for liability claims under Motor Third Party insurance are briefly discussed. Other Liability claims have been discussed separately in Chapter-16 for Liability Insurance. Before we discuss on the procedural aspects of claim-settlement we need to discuss duties and responsibilities of the surveyor in respect of insurance survey, which is the first step towards settlement of claims under all property insurances.

Duties and Responsibilities of a Surveyor

As per IRDA regulation called Insurance Surveyors Regulations 2000, a surveyor and loss assessors shall, investigate, manage, quantify, validate, and deal with losses arising from an accident or contingency and report thereupon and carry out the work with competence, objectivity, and professional integrity and with strict adherence to the code of conduct specified in the said regulation. In order to discharge the specified duties and responsibilities, the surveyor and loss assessor shall:

- Declare whether he has any interest in the subject matter in survey or whether it pertains to any of his relatives or business partners.

- Maintain confidentiality and neutrality in all respects.
- Conduct inspection and re-inspection of the property under survey.
- Examine, inquire, investigate, verify, check the causes and the circumstances of the loss in question, the nature of ownership, and insurable interest.
- Comment upon franchise, excess/under insurance and other related matters.
- Estimate, measure, and determine the quantum and description of the subject loss.
- Advise the insured and the insurer about the loss-minimization, loss control, security and safety measures wherever appropriate to avoid further losses.
- Comment on the admissibility of the loss and the observance of warranty and conditions of policy.
- Survey and assess the loss.
- Assess the liability of the insurer under the contract of insurance.
- Point out the discrepancy, if any, in the policy wordings.
- Satisfy the queries of the insured and the insurer in respect of loss or claims.
- Recommend applicability of depreciation and percentage/ quantum of depreciation.
- Give reasons for repudiation of claims.
- Comment on salvage and disposal of salvage.

- Submit report to the insurer as expeditiously as possible, but not than 30 days of his appointment. In exceptional cases, this period can be extended with the consent of the insurer and the insured.

Claims under Fire Insurance

Fire Claims — Procedures and Formalities

Appointment of Surveyor

On receiving claim intimation an appropriate surveyor with requisite qualification, IRDA gradation, experience, exposure has to be deputed forthwith by the insurer.

Survey Report

Final Survey Report is to be submitted by the surveyor within shortest possible time. Where due to circumstances beyond the control of the surveyor, the final report is like to be delayed, the surveyor shall submit a preliminary report within 5 days and the interim status report within 30 days indicating the stage at which the survey work rests, the difficulties encountered in finalizing the survey report and when the final survey report could be expected. If there is any doubt as to the cause of fire, the same has to be informed by the surveyor at the preliminary stage itself to the insurer so that help of an expert/consultant /investigator can be taken. It is to be also indicated in his written communications with the claimant. Survey and assessment of fire claims are preferably done by Chartered Accountants holding IRDA License and adequate exposure and experience. During survey and reporting loss with his recommendation for settlement the surveyor shall take into account all-above mentioned terms, conditions and exclusions of policy.

Special Investigation on Admissibility or Assessment of Loss

The insurer in consideration of preliminary survey report may depute a competent investigator for special investigation on such aspects as specified in the survey report. The investigator will investigate the whole occurrence and submit investigation report with all evidences. On submission of report by the investigator, the insurer will hold a joint meeting of surveyor and investigator and the client to sort out all confusions and establish admissibility of claims or determine proper quantum of loss as per terms of policy.

Documents Necessary for Settlement of Claims

Policy Copy, Survey Report, Duly Completed Claim Form, Police Report, Photographs, and Fire Brigade Report, etc., are fundamental documents required for processing claims. For settlement of claims arising out of Act of God perils like flood, landslide, earthquake, storm etc., newspaper cuttings, metrological report are required in addition to above documents.

Settlement of Claim (Payment/Repudiation)

The insurer is to settle claim within 30 days from submission of final survey report. While settling the claim the insurer shall consider the coverage, terms, conditions and exclusions as mentioned above. Let us see in the following example, how policy condition on contribution will apply in settlement of a fire claim.

Application of Contribution Clause for Assessment of Loss under a Fire Policy

X has taken two fire policies from two insurers being A and B with SI Rs 100,000 and Rs 200,000 for same subject matter of insurance, which has been damaged by an accident fire during the policy period. The loss has been assessed for Rs 60,000. Let us examine how the liability under Policy A and Policy B will be determined when: a) Value at Risk is Rs 300,000; b) Rs 400,000; or c) Rs 200,000. The liability is calculated as under:

Case (a); Value at Risk is Rs 300,000

1. Liability under Pol. A…60000 X 1 /3 = Rs 20,000

2. Liability under Pol. B…60000 X 2/3 = Rs 40,000

Rs 60,000

Case (b); Value at Risk is Rs 400,000

1. Liability under Pol. A…60000 X 1 /4 = Rs 15,000

2. Liability under Pol. B…60000 X 2/4 = Rs 30,000

Rs 45,000

Case (c); Value at Risk is Rs 200,000

1. Liability under Pol. A…60000 X 1 /2 = Rs 30,000

2. Liability under Pol. B…60000 X 2/2 = Rs 60,000

Adjustment of actual loss i.e. Rs 60,000 in above ratio:

1. Liability under Pol. A…60000 X 3/9 = Rs 20,000

2. Liability under Pol. B…60000 X 6/9 = Rs 40,000

Rs 60,000

Duties of the Insured at the Event of Claim

In the event of loss and/or damage, claim or suit, which may reasonably give rise to a claim under this Policy of insurance, the Insured shall give to the Insurer as soon as practicable, but not later than 15 days after the occurrence of the event a written notice containing particulars sufficient to identify the loss and/or damage, claim or suit and also reasonably obtainable information with respect to the time, place and circumstances thereof as well as nature and extent of the loss or damage, and the names and addresses of available witnesses. The insured will do the following:

- Take such measures as may be reasonable for the purpose of averting or minimizing such loss or damage

- Ensure that all rights against carriers, bailees or other third parties are properly preserved and exercised; if claim is made or suit is brought against The Insured, The Insured shall at the earliest practicable advise the Insurer of every demand, notice, summons or other process received by him or his representative.

- Co-operate with the insurer and upon the Insurer's request, assist in making settlements, in the conduct of suits and in enforcing any right of contribution or indemnity against any person or organization who may be liable to The Insured because of property damage with respect to which insurance is afforded under this Policy, and The Insured shall attend hearings, and trials and assist in securing and giving evidence and obtaining the attendance of witnesses.

- Do and concur in doing and permit to be done all such things as may be practicable to establish the cause and extent of the loss or damage.

- Preserve all parts affected and make them available for inspection by the Insurer as long as the insurer may require

- Furnish any information and documentary evidence that The Insurer may require together with, if required, a statutory declaration of the truth of the claim

- Inform the police of loss or damage due to major fire, theft or house breaking or actions by any malicious person and render all assistance to the police.

Insurer's Duties in Case of a Loss Reported on a Policy

On the happening of any loss or damage to any of the property insured and reported under a insurance policy, the insurer will take the following actions for prompt settlement of claims:

- Appoint Surveyor within 72 hours;

- Arrange to obtain Survey Report within 30 days;

- Obtain clarifications for query, dispute or ambiguity if any on Survey Report within15 days from the date of receipt of report;
- Ask the surveyor to submit additional report or observation on the clarification-received from the claimant;
- Decide settlement within 30 days from submission of Survey report;
- Make payment within 7days after the claimant's acceptance of settlement amount to avoid delay of settlement and consequent penal interest 2 per cent above bank rate.
- In case of repudiation of claim, the insurer shall communicate through registered post specifying the breach of policy condition and

For the purpose of loss minimization and prompt settlement of claim in terms of specified policy condition the insurer may also:

- take possession of any property of the Insured in the buildings or on the Premises at the time of the loss or damage;
- keep possession of any such property and examine, sort, arrange, remove or otherwise deal with the same; and
- sell any such property or dispose of the same for account of whom it may concern.

The powers conferred by the policy condition in this regard can be exercised by the Insurer at any time until notice in writing is given by the Insured that he is not making any claim for the accident intimated under the policy or if any claim is made, until such claim is finally determined or withdrawn. If the insured or any person acting on his behalf does not comply with the requirements of the insurer, or hinders or obstructs the insurer, all benefits under this policy shall be forfeited. The insured shall not in any case be entitled to abandon any property to insurer whether taken possession of by the insurer or not.

Rights of Insurer in Case of a Loss

On the happening of any loss or damage to any of the property insured under this Policy the Insurer may enter and take and keep the possession of the building or premises where the loss or damage has occurred. The insurer may sell any such property or dispose of the same for account of whom the claim is concerned for loss minimization. The powers conferred by this policy condition can be exercised by the insurer at any time until notice in writing is given by the Insured that he makes no claim under this Policy or, if any claim is made, until such claim is finally determined or withdrawn as mentioned earlier. However in the exercise or purported exercise of the said powers the Insurer shall not incur any liability to the insured or diminish its rights to rely upon any of the conditions of the policy as regards claim.

Consideration of Certain Conditions or Provisions in regard to Claims Salvage

The salvage of any insured property damaged on the occurrence of accident shall accrue to the insurer (subject to indemnification in full). Insurer shall have the right to take possession of such salvage. It is the duty of the surveyor to quantify and value the salvage for adjustment, if salvage is taken by the insured or for sale or disposal with the consent and advice of the insurer. For this purpose, the surveyors make physical verification and examination apart from the reconciliation with the schedule forming the part of the policy, books and accounts maintained by the claimant, other evidences and reports and stock statements if any submitted to the financier or the Government Department as the case may be.

Underinsurance

If the property insured is, at the commencement of any damage, be collectively of greater value than the Sum Insured thereon, then the insured shall be considered as being his own insurer for the difference, and shall bear the rateable proportion of the loss accordingly. Salvage is to be considered in the same proportion.

Every item specified in the policy or in the schedule forming the part of the policy shall be separately subject to this condition. For the purpose of the purpose of determination of underinsurance, the surveyor may consider Audited Accounts, Inventory Register, purchase bills, invoices, and challans. Asset Register duly verified by the management from time to time, market value of the assets, slow-moving or obsolete items in stock register, stock-turnover ratio, and excise register etc., depending upon the nature and location of asset.

Contribution

If at the time of any loss occurred to any property insured, there be any other subsisting insurance or insurances whether effected by the insured or by any other person taking cover for the same property, the insurer shall not be liable to pay or contribute more than its ratable proportion of such loss or damage. To put it into more simple words, if at the time of loss, there are more than one insurance for the same property or part thereof, the admissible loss will be borne by the all the insurers concerned will contribute to the loss in the same proportion as the their policy sum insured bear to the total loss.

Deductibles

Deductibles including franchise or excess either compulsory or voluntary in consideration for reduction in premium are deducted from the assessed loss as per policy terms and conditions. A policy does not cover the amounts of the deductibles stated in the schedule in respect of every loss occurred during the policy period Deductibles are considered after the application of all other terms and conditions of the policy including underinsurance, if any.

Disclaimer of Liability

In no case the insurer shall be liable for any loss or damage after the expiry of 12months from the happening of the loss or damage unless the claim is the subject of pending action or arbitration; The condition no. 6 of Fire Policy provides inter-alia " *..in no case whatsoever shall the company be liable for any loss or damage* *after expiry of 12 months from the happening of the loss or damage unless the claim is the subject of 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 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 hereafter be recoverable hereunder..."*

Subrogation

Insurer shall, upon indemnification to the insured of any loss, damage, be subrogated to all the insured's rights of recovery against any other person, firm or corporation who may be legally or contractually liable for such loss, damage subject to following terms:

- If there is a partial reimbursement, subrogation is restricted to the amount settled.
- The insurers shall pass on to the insured such money or monies recovered by them that is in excess of the loss, damage or expenses so received by the insured.

The Insurers may make a claim upon and institute legal proceedings against any parties believed responsible for loss, damage or expense reimbursed in the name of the Insured, and the insured shall provide full co-operation to the insurer in pursuing such claim or legal proceedings. The insured shall, at the insurer's expense, do and concur in doing and permit to be done all such actions as may be necessary or required by the insurer in the exercise of any rights or remedies or for the purpose of obtaining relief or indemnity to which the Insurer is or would become entitled or which is or would be subrogated to him upon indemnification of any loss or damage under the policy, regardless of whether such action is or becomes necessary or required before or after the indemnification made by the insurer to the insured.

Arbitration

If any dispute or difference arises in regard to the quantum to be paid under the policy (liability being otherwise admitted) such difference shall independently of all other questions, be referred to the decision of a sole arbitrator to be appointed in writing by the parties to the insurance contract, i.e. the insured and the insurer, but if they cannot agree upon a single arbitrator within 30 days of any party invoking arbitration, the same shall be referred to a panel of three arbitrators, comprising of two arbitrators, one to be appointed by each of the parties to the dispute/difference and the third arbitrator to be appointed by such two arbitrators and arbitration shall be conducted under and in accordance with the provisions of the Arbitration and Conciliation Act, 1996.

Reinstatement of Policy Limit after Indemnification of a Loss

At all times during the period of insurance the insurance cover will be maintained to the full extent of the respective sum insured in consideration of which upon the settlement of any loss under a policy, pro rata premium for the amount of such loss shall be payable by the Insured to the insurer for the unexpired period from the date of such loss to the expiry of period of insurance. Such pro-rata premium shall be deducted from the net claim amount payable under this Policy. The purpose of this condition is to ensure continuity of the cover to for the insured property to the full value of insurance, but only subject to the right of the Insurer for continuing cover for full amount after occurrences of loss and settlement of claim after deduction of pro rata premium from the claim amount, Such pro rata premium is to be calculated from the date of loss till expiry of this Policy. However in case the insured immediately on occurrence of loss does not exercise his option to reinstate the sum insured as above sum insured shall stand reduced by the amount of loss.

Loss Indemnified under Policy on Reinstatement Basis

Fire policy may be issued either on Market Value basis or Reinstatement Basis at the option of the insured with the insurer agreeing with the option of the insured. Reinstatement may be applied to goods as well as to buildings. The duty of reinstating may be literally fulfilled in respect of goods, but for a building the insurers' duty will be fulfilled if the restored building is substantially the same as it was before accident. It would be unreasonable to demand a literal performance for buildings, since it is impracticable to restore every minute detail of a building. But once the insurers have elected to reinstate, they must perform their contract and cannot withdraw if they find that their choice is more onerous or costly than they expected. It was held in **Brown vs. Royal Insurance Co.** compelling the insurers to carry out reinstatement of the property damaged, that the insurer had elected to make under a condition of the policy. In this case when the work of reinstatement was in progress the Commissioners of the Sewers condemned the premises as dangerous and had them demolished. The insurers then pleaded that the dangerous condition of the buildings had been caused by the fire, and that by their demolition performance of reinstatement was rendered impossible; also, that if the buildings had not been demolished they would have restored them to the condition that they were in before the fire.

The court held that the defendants had failed to prove that reinstatement was impossible, and that although they might have shown that performance had become more expensive than one they had expected, still, having elected to reinstate, they were bound by their election and must either perform according to the terms of the *contract or pay damages for not doing so. Lord Campbell, in the course of judgment; said: "....The case stands as if the policy had been simply to reinstate the premise in case of fire, because, where a contract provides for an election, the party making the election is in the same position as if he had originally contracted to do the act which he has elected to do….*". Where the insurers do not fulfill their duty they are liable for damages for their failure. Where a better building is given to the insured, the insurers cannot compel him to bear a part of the cost, unless there was previous agreement to this effect. Average cannot be applied to reduce the liability of the insurer if there is underinsurance and the insurer opts to reinstate. The damage may be partial and the cost of reinstatement may be within the inadequate sum insured, but average is not applicable to reinstatement by he insurer.

Thus if the policy is issued with **Reinstatement Basis** supported by specific reinstatement clause, in the event of loss or damage to the insured property, the insurance benefits in shall be determined on the basis of the cost of replacing or reinstating the insured property. The liability of the insurer shall not exceed the cost of replacing or reinstating the property with property of a substantially similar kind and type not superior to or more extensive than the insured property. Assessment of loss under a fire policy is made with reference to the Reinstatement clause in the policy which may provide that:

- The work of replacement or reinstatement (which may be carried out upon another site and in any manner suitable to the requirements of the insured subject to the liability of the Company not being thereby increased) must be commenced and carried out with reasonable dispatch and in any case must be completed within 12 months after the destruction or damage or within such further time as the Company may in writing allow.

- Where for any reason, it is not possible or if the insured elects not to rebuild or replace, the insurer will pay to the insured the Actual Cash Value of the property at the time of loss. If insured property, at the time of reinstatement/ replacement/repair following a loss or damage indemnifiable under the policy is of greater value than the sum insured under the policy, then the insured shall be considered as his own insurer for the difference and shall bear a ratable proportion of loss.

- Each item in the schedule of the subject matter of insurance, to which this condition applies, shall be separately subject to the foregoing provision. Claims for loss of stock including raw materials, finished goods, feedstock, chemicals, stores and spares and other insured stock and work in progress are to be settled on Actual Cash Value only.

- With respect to catalysts lost or damaged, the basis of indemnity if cover is endorsed to this Policy of Insurance is the Actual Cash Value at the time of the loss as per endorsement.

- Where the Assets damaged or lost are those for which The Insured is only contractually liable for maintenance, the basis of indemnity shall still remain the same as above, irrespective of any contract to the contrary.

Insurer's Liability with 72 hours Clause for Claims from Act of God Perils

Storm (Windstorm) Loss

Insurers shall not be liable for any loss occurring before the effective date and time of the Policy nor for any loss commencing after the expiry date and time of the Policy. However, the insurer will be liable for any loss occurring for a period of up to 72 hours after the expiry of the Policy, provided that the first windstorm damage occurs prior to the date and time of the expiry of the Policy. Each loss by windstorm shall constitute a single claim provided, if more than one windstorm shall occur within any period of 72 hours during the Policy period and such windstorm shall be deemed to be a single windstorm within the meaning thereof.

Earthquake Loss

Insurers shall not be liable for any loss caused by an earthquake occurring before the effective date and time of this policy nor for any loss commencing after the expiry date and time of the policy. However, the insurer will be liable for any losses occurring for a period of up to 72 hours after the expiration of this Policy, provided that the earthquake occurs prior to the date and time of the expiry of the Policy. All losses caused by earthquake shall constitute a single loss if more than one earthquake shock occurs within 72 hours period.

Flood Loss

Insurers shall not be liable for any loss caused by flood occurring before the effective date and time of this policy nor for any loss commencing after the expiry date and time of this policy. But the insurer will be liable for any losses due to flood occurring for a period up to 72 hours after the expiry of the policy, provided that the first flood damage occurs prior to the date and time of the expiry of the policy. All losses caused by flood within a 72 hours period shall be deemed to constitute a single loss.

Loss not Admissible under a Standard Fire Policy

Loss from Excluded Perils

A Standard Fire Policy does not cover loss or damage to any property Insured caused directly or indirectly by or in connection with or arising from:

- inherent vice, latent defect, wear and tear or gradual deterioration, leakage, seepage, pollution, contamination, overflowing of tank, smog or extremes or changes of temperature or humidity;

- non-functional or inadequate heating, air-conditioning or cooling equipment including operating error, condensation, excessive moisture, dampness of atmosphere, seepage;

- disease, deterioration, decay, mildew, mould, fungus, wet or dry rot, insect larvae or vermin of any kind;

- infestation loss or damage by normal settling, shrinkage or expansion in buildings or foundations, other loss or damage of gradual nature, such as corrosion, erosion, cavitation, rust and scale, scratching of painted or polished surfaces, unless fortuitous accidental loss or damage covered under this Policy of Insurance;

- infidelity or any dishonesty on the part of The Insured or any of his employees or others to whom the property may be delivered or entrusted, inventory shortage or unexplained disappearance; processing, renovating, repairing or faulty workmanship thereon unless fortuitous accidental loss o covered under this Policy

- go-slow, total or partial cessation of work;

- loss of use, delay or loss of markets or Consequential Loss of any nature;
- shrinkage, evaporation, loss of weight, leakage, breakage of glass or other fragile articles, marring, scratching, exposure of light, or change in colour, texture or flavour unless fortuitous accidental loss or damage covered under this Policy of Insurance;
- theft where Property Insured is left in the open and not contained in buildings on permanent foundations, unless storage of such item is normally in the open;
- release, discharge, or dispersal of toxic or hazardous substances, contaminants or pollutant, proximate or remote; and
- loss or damage for which cover is available under Section II of this Policy of Insurance.

Loss from Excluded Property

- Aircraft, watercraft including floating equipment, ships and vessels, spacecraft and satellites, railway locomotives, rolling stock;
- Vehicles, construction plant and equipment other than those used within the Insured Premises and expressly defined in the schedule;
- Money, stamps, cash, credit cards, cheques, securities or obligations of all kind, deeds or documents, evidence of debt or title, patterns, plans, designs, rare books, jewellery, precious stones, gems or metals, unless specifically covered;
- Furs and garments trimmed with fur;
- Works of art, unless expressly specified in The Schedule;

- Standing timber, growing crops, livestock and animals, and landscaping;
- Land including topsoil, backfill or land values, water, roads, runways, railway lines, transmission and distribution lines outside plant Premises, drainage and culverts, canals, dams, reservoirs, wells, pipelines outside plant Premises, tunnels
- Explosives, refractory linings whilst in process, materials in process damaged by operational error and as a result of its undergoing any process, maintenance, repair or testing or any emergency shutdowns;
- Goods or property in transit other than within the Premise;
- Property of the Insured, which has been, transferred into the possession of others, under leasing or rental agreements, hire, purchase, credit sale agreements; and
- Loss or damage to Property Insured if removed to any building or place other than in which it is herein stated to be insured, except machinery and equipment temporarily removed for repairs, cleaning, renovation or other similar purposes for a period not exceeding 60 days.

Claims under Business Interruption or FLOP Policy

Scope and Basis of Loss of Gross Profit

In respect of loss of Gross Profit covered by a Consequential Loss policy or Fire Loss of Profit policy (FLOP) or Business Interruption Policy, the insurer shall assess and indemnify the loss equivalent to the amount obtained by multiplying the rate of gross profit with the amount by which the actual turnover during the indemnity period falls short of the standard turnover, which would have been achieved, had the loss or damage not occurred. If the annual Sum insured as per policy issued is less than the amount obtained by multiplying the Rate of Gross Profit by the Annual turnover or, if the indemnity period exceeds twelve months, the Turnover or the loss of profit thus calculated for the equivalent period, the amount payable shall get reduced proportionately. Thus loss of profit indemnifiable under Business Interruption Policy or FLOP means Gross Profit including Net Profit, Specified Standing Charges and Increased Cost of Working. The admissibility of claim under FLOP or Business Interruption Policy is established with admissibility of loss under standard fire policy for material damage.

Specified Standing Charges

In respect of Specified standing charges, the Insurer shall pay the amount obtained by multiplying the percentage by which the actual turnover during the indemnity period falls short of the turnover which would have been achieved had the interruption of or interference with the Business Insured not occurred by the amount of Specified standing charges incurred during the interruption or interference. If the Sum Insured hereunder is less than the amount obtained by multiplying the Rate of Gross Profit by the Annual turnover or, if the indemnity period exceeds twelve months, the pro rata turnover for that period, the amount payable shall be reduced proportionately.

Increased Cost of Working

In respect of indemnification of Increased Cost of Working, the Insurer shall pay the additional expenditure necessarily and reasonably incurred for the sole purpose of avoiding or diminishing the reduction in period of interruption and consequent loss of turnover, it is established that such process in reduction in the period of insurance was not possible without such additional cost/ expenditure of working. The indemnity shall not exceed the amount of loss of Interest Insured thereby avoided.

Calculation of Rate of Gross Profit and Annual Turnover

In calculating the Rate of Gross Profit and Annual turnover, the following aspects shall be taken into account:

- the trend of the Business Insured;
- the results of the Business Insured during the financial year preceding the date of the loss or damage or, in the event of the loss or damage occurring during the first year of commercial operation, the Turnover during the following financial year;
- any circumstances affecting the Business Insured either before or after loss or damage or which would have affected the Business Insured had the loss or damage not occurred;
- any benefits from deferred sales as a consequence of an interruption of or interference with the Business Insured which The Insured may receive during a period of six months immediately following the re-commissioning of insured plant and/or machinery after a loss or damage;
- allowance for the time spent on any overhauls, inspections or modifications carried out during the period the Business Insured was affected by any interruption or interference;
- any money paid or payable in respect of goods which are sold or services which are rendered elsewhere than at the Premises for the benefit of the Business Insured either by The Insured or by another party acting on his behalf;
- any amount saved during the indemnity period in respect of any charges and expenses of the business payable out of the Gross Profit that may cease or be reduced in consequence of loss or damage; and
- The final figures shall represent as closely as may be deemed reasonable the results, which the Business Insured would have achieved, had the loss/damage not occurred.

Payment of Indemnity

The Insurer is entitled to postpone payment if: (a) there are doubts as to the insured's right to receive payment, in which case payment shall not be made till such time as the necessary proof is furnished by the Insured or the Insurer accepts liability thereupon; or (b) as a result of any loss or damage or any interference with or interruption of the Business insured, police or criminal investigations have been initiated against the Insured in which case payment will not become due until the completion of such investigations, provided always that if the Insured is convicted of any offence in respect of business interruption, the insurance cover under the policy shall be void.

Policy Clauses Considered for Settlement of Claim under FLOP

Alternative Trading Clause

If during the Indemnity Period goods are sold or services are rendered elsewhere than at the business premises for the benefit of the business either by the insured or by others on his behalf, the money received or receivable in respect of such sales or services shall be brought into account in arriving at the amount pf turnover during the Indemnity Period.

Uninsured Standing Charges Clause

If any standing charges of the Business are not insured by the Policy of Insurance (having been deducted in arriving at the Gross Profit insured) then in computing the amount recoverable hereunder as Increase in Cost of Working, that proportion only of any additional expenditure shall be brought into account which the Gross Profit bears to the sum of the Gross Profit and the uninsured standing charges.

Uninsured Standing Charges

Where the Specified Working Charges or Standing Charges are recognized as variable charge or left uninsured specifically, such Uninsured Standing Charges shall be deleted in arriving at the quantum of loss of profit with reference to such Clause.

Professional Accountants Clause

Any particulars or details contained in the books of account or other business books or documents of the insured, which may be required by the insurer for the purpose of investigating or verifying any claim hereunder may be produced by professional accountants and their report shall be prima facie evidence of the particulars and details to which such report relates. The Insurer will pay to the insured the reasonable charges payable by the insured to their professional accountants for producing such particulars or details or any other proofs, information or evidence as may be required by the insurer and reporting that such particulars or details are in accordance with the Insured's books of account or other business books or documents provided that the sum of the amount payable under this clause shall not exceed the limit stated in the schedule and the amount otherwise payable under the Policy shall not exceed the liability of the insurer as stated.

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.

The Insured's Special Obligations Following Business Interruption

- The insured shall be under obligation to keep for the Period of Insurance complete records of the Business Insured, including balance sheets, the records of inventories, production and sales for the three preceding years. All records shall be held in safekeeping and, as precautionary measures the Insured shall also keep separate sets of such records.

- In the event of any occurrence of loss or damage which might cause an interruption of Business Insured the insured shall immediately notify the insurer and send it written confirmation thereof within forty-eight hours of the occurrence.

- The Insurer or his representatives shall have unlimited access to the premises to establish the possible cause and extent of the loss or damage, its effect on the interest insured, to examine the possibilities for minimizing the interruption of the Business Insured, and if necessary, to make reasonable recommendations for the avoidance or minimization of such interruption or interference.

- The Insurer and his representatives shall have the right to enter any building where the loss has happened and may take possession of or require that any of the damaged property insured be rendered to them and may keep possession of and deal with such damaged property for all reasonable purposes and in any reasonable manner. This condition shall be evidence of the leave and license of the insured to the insurer.

- If the insured or anyone acting on his behalf hinders or obstructs the insurer in any way or does not comply with any recommendations, all benefits under this Section shall be forfeited.

- In the event of a claim being made under this policy, the insured shall at his own expense deliver to the insurer not later than 30 days after the interruption of the Business insured or within such further periods as the insurer may allow in writing a written statement setting forth particulars of the claim.

- The Insured shall at his own expense produce and furnish to the insurer such books of account and records or other evidence as may reasonably be required by the insurer for the purpose of investigating or verifying the claim together with, a statutory declaration of the truth of the claim and of any matters connected therewith.

Exclusions for Business Interruption

This policy does not cover any loss resulting from interruption of the Business directly or indirectly attributable to any of the following causes:

- loss or damage covered under Fire Policy;
- any restrictions imposed by public authority, including restrictions imposed on reconstruction or operation causing business interruption;
- consequential Loss due to causes such as suspension, lapse or cancellation of a lease, licence or order, etc., which occurs after the date when the items lost, destroyed or damaged are in operating condition again and the business could have been resumed if said lease, licence or order, etc. had not lapsed or had not been suspended or cancelled;
- shortage of raw materials, semi-finished or finished products or other materials required for proper operation, not caused by loss or damage to such property by an insured peril covered under Standard Fire policy;
- loss, distortion or corruption of information on computer systems or other records or software programs unless resulting from an occurrence of loss or damage indemnifiable under the operational material damage Section;
- loss or damage for which the manufacturer or supplier of the property is responsible either by law or under contract;
- The insured not having at his disposal in good time sufficient capital for repairing or replacing destroyed or damaged machinery; and
- the amount of any fines or damages for breach of contract for late or non-completion of orders or for penalties of whatever nature.

Application — Assessment of Loss under FLOP Insurance Policy

Let us now examine how loss under FLOP policy will be assessed with application of the above noted process and provisions for assessment of Loss under the said policy.

XYZ Ltd, Manufacture of Pharmaceutical products took a FLOP for **Sum Insured** of Rs 11,150,000 (Gross Profits). A fire occurred on7 March 2005 and caused material damage of Rs 20.50 lakhs admissible under standard fire policy. The surveyors have collected the following details for determination of loss under FLOP.

Business Trend: Increase12%

Period of Insurance: 01.01.2008 to 31.12.2008

Indemnity Limit:: 6 Months Time Excess; 3 Days

Occurrence of accident: 07.03.2008 at 17:50 hrs

Completion of repairs: 15.04.2008 at 17:00 hrs.

Interruption Period: 24.25 days in March and 14.75 days in April, Total 39 days

Other Information collected in this regard:

- Net Turnover(2007) Rs 3,13,29,000
- Turnover (March & April'07) Rs 2674500 and 2705900
- Expenses for Loss Minimization Rs 20500
- Reduction in Insured Costs. Rs 6060
- Actual Turnover during Interruption: Rs 39,93,100
- Opening Stock Rs 25,80,000
- Raw-materials Rs 2,11,62,000
- Other Expenses Rs 2,18,000
- Closing Stock Rs 26,83,000

Solution: Calculation of Loss of Profit (M/S. X YZ Ltd.)

Box-2: Trading Account for the Year Ended on 31 December 2007

Opening Stock	25,80,000	Turnover	3,13,29,000
Raw-materials	2,11,62,000	Closing Stock	26,83,000
Other Expenses	2,18,000		
Gross Profit (A)	1,00,52,000		
	3,40,12,000		**3,40,12,000**

Now we are required to: i) calculate GP Ratio; ii) determine loss of profit due to reduction of turnover; and iii) adjust the Turnover with the trend.

1. Gross Profit Ratio: 10052000/31329000 x 100 = 32.1 per cent
2. Turnover for March+April' 07 (Rs2674500 + 2705900) = Rs 53,80,400
3. Adjusted Turnover (with Increase Trend @12 per cent) = Rs 60,26,048
4. Actual Turnover (March & April' 08) = Rs 39,93,100
5. Reduction in Turnover (3-4) = Rs 20,32,948
6. Loss of Gross Profit (2032948 x 32.1) = Rs 65,2576
7. Actual Loss suffered (Rs 652576+20500-6060) = Rs 66,701

Loss as calculated above is to be adjusted with Turnover Trend, time excess, under-insurance as explained below:

Time Excess = 3 days

Gross Profit Loss (24.25+14.75) = 39 days

Loss for 3 days (667016/39 X 3) = Rs 51,309

Indemnity for 36 days = (Rs 667016-51309)	= Rs 6,15,707
Annual Turnover (As per last A/c):	= Rs 3,13,29,000
Adjusted Turnover with Increase Trend 12 per cent:	= Rs 350, 88,480
Gross Profit @ 32.1 per cent on Rs 350,88,480	= Rs 11,263,402
It is underinsurance as Rs 11263402 is more than SI of Rs 1, 11, 50,000	
Admissible Claim Rs 615707 X 11150000/ 11263402	Rs 609508

Claim Settlement Procedure.

a. A chartered Accountant conversant with Loss of profit insurance is generally deputed for survey and assessment of such claims;

b. Claim under Loss of Profit policy is admissible only when the claim under Std Fire Policy is admissible for material damage. Thus admissibility is conditional;

c. The surveyor shall study all conditions and warranties of the policy and comment upon them in his report to support his assessment as exemplified in above application;

d. Additional Documents required for assessment of claim under this policy are earlier year Audited Annual Accounts, Purchase &Sales Record, Turnover Records etc;

e. Adjustment of GP Ratio as per trend, Adjustment of Turnover as per trend etc; and

f. Assessment of claim after adjustment of Time Excess and Under Insurance.

Motor OD Claims Settlement

Basis of Settlement of Motor OD Claims

Motor OD loss is settled under any of three bases depending upon the nature, extent of damage:

- Total Loss Basis
- Repair Basis
- Cash Loss Basis

Methods followed for Total Loss Settlement

Following methods are followed for Total Loss Settlement:

- When a surveyor finds that damaged vehicle is beyond repair or repairs are not economic proposition, he recommends for settlement of claim on Total Loss Basis after negotiation with the insured.
- Total Loss settlement is negotiated and recommended for reasonable sum representing the market value of the vehicle immediately prior to the loss.
- In Total Loss, if market value is more than the insured value, the settlement is brought down to the insured value.
- In Total Loss the insured is paid in cash and the insurer takes over the salvage of the damaged vehicle which is disposed off then on their own.
- In total loss before actual payment is made, the insurer will collect RC Book, Tax Token, Ignition Keys, blank TO & TTO duly signed by the insured.
- If the vehicle is beyond repair, it requires to be scrapped, RC Book and Keys are to be returned to RTA.

- Total Loss by theft is to be supported by a copy of FIR and SDE in claim intimation or Claim Form.

- Police Certificate for the case as True but Undetected is essential for total loss theft claim.

- All documents as mentioned separately along with RC book and Taxation Certificate must be collected. If they are stolen with the vehicle, it is necessary for the insured to obtain duplicate ones from RTO and submit the same to insurer.

- The insured shall submit an undertaking that he would refund the claim amount, if subsequently the vehicle is traced and delivered back to him.

- The Insurer shall inform the Registering Authority by Registered AD letter that the total loss claim is being processed for payment in respect stolen vehicle No. and request them not to effect transfer the ownership of the vehicle to anyone. This will prevent theft from disposing off the stolen vehicle. The Registering Authority may also inform that the vehicle has not been registered by them or it is plying in someone's name.

- Market value for untraced or old type vehicle — Opinions of two or three motor surveyors based their information such as Make, Manufacturing year, Past Claim, Improvement carried out, is to be obtained for deciding the amount of settlement. Average of above 2/3 valuations given independent surveyors becomes the basis for settlement of claim.

Settlement of Motor OD Claims on Repair Basis

Following methods are followed for "Settlement on Repair Basis":

- On receipt of notice of loss, the insurer shall verify that the policy is in force.

- He will register the claim and issue an claim form, and obtain a detailed estimate of repairs.

- He may require the insured to obtain estimate from another repairer if efficiency and integrity of first repairer are in question.

- He will depute a surveyor preferably with automobile engineering background. For major repair or repair for commercial repairer three types of survey are carried out, which are Spot Survey, Final Survey and Re-inspection after Repair.

- The surveyor will investigate, enquire, survey the accidental damage, and assess the loss preferably at garage. He will inspect the damaged vehicle, discuss about the cost of repair or replacement and submit his survey report at the soonest possible time.

- In case of commercial vehicle or major damage to private vehicle, in addition to Final Survey as mentioned above a spot survey is carried out by separate surveyor at the spot of accident before the vehicle is shifted to garage for repair.

- Major damage, insurer may visit to place of accident or garage for inspection.

- For minor damage for which estimated repair cost will not exceed Rs 20,000, the insurer may settle claim on the basis of his in-house survey report without deputing independent surveyor.

- Insurer settles claim within 30 days after submission of final report and of bills, voucher and cash memo duly verified by the survey for re-inspection.

- The repairer is instructed to keep aside the savage of damaged parts, if any, for being collected by the salvage buyer at the value indicated in his report.

- Or else, the repairer may retain the salvage and deduct the salvage value from the assessed claim amount.

- On receipt of the final bill of repairs and a satisfaction note from the insured that the vehicle has been repaired to his satisfaction, the repairer is paid or reimbursement is made to the claimant.

- For settlement of claims for commercial vehicle, verification of DL with RTO extract is made compulsory.

- Claims on repair basis for vehicles stolen and recovered subsequently, the procedure briefed above is to be followed in addition to a spot survey at the police station immediately after the notice of recovery.

Settlement of Motor OD Claims on Cash Loss Basis

Following methods are followed for “Settlement on Cash Loss Basis”:

- Claims settled on Total Loss Basis make the insurer owner of salvage and Claims settled on Repair Basis allow payment on completion of repair and on production of bills and receipts thereof.

- But under certain circumstances the insurers are compelled to: i) settle total loss claim without claiming the salvage; or ii) reimburse the insured the repair costs without submission of repair bill or even without verifying whether vehicle is or will be repaired or not.

- This sort of settlement is a Compromise settlement also known “Cash Loss Settlement” generally resorted to commercial vehicles.

- Sometimes repairs to a commercial vehicle require huge expenditure and the owner is not in a position to wait for reimbursement until repair is complete and survey is carried out.

- In such situation the insurer and the insured come to an arrangement for such compromise settlement with reimbursement 25 per cent to 30 per cent less than the amount assessed where the insurer does not insist on the repair of the vehicle.

- Reduction by 25 per cent to 30 per cent takes care of Sales Tax, Excise Duty which the insured may avoid by repairing with second-hand spare parts.

- Cash Loss settlement is also adopted for total loss settlement without salvage, when difficulties arise in disposing of the salvage at reasonable value. In such cases, the value of salvage is mutually agreed upon as recommended by surveyor and deducted from the amount of total loss as assessed. The insured is reimbursed the "Net Total Loss".

Documentation Requirements

Claim Intimation letter, Claim Form duly completed and signed by the Insured along with following documents:

- a. Policy Copy, b. Sport Survey Report, c. Repairer Estimate, d. RC Book Copy, e. DL copy with RTO extract, f. Final Repair bill and Receipt, g. Final Survey Report, h. Re-inspection Survey Report, i. Final Police Report (in case of theft claim), j. Transfer Form from RTO.

Motor Third Party Claims Settlement

Major Aspects to be Considered for Settlement of Motor TP Claims

The Motor Third Party Claims Settlement is made as per provisions of the Motor Vehicle Act, 1988 for payment of compensation to the third party (other than the insured) for death or injuries to third party due to accident. The amount of compensation is decided either as per the provisions and structured basis specified in Section 163A of the Act or as per the provisions of Section 166 of the Act following the common law basis. For settlement of Motor Third

Party Claims, the provisions of Section 140, Section 146, Section 147, Section 148, Section 149, Section 150, Section 160, Section 163, Section 165, Section 166 and Section 170, along with various court decisions are specially referred to and applied for defending the case in the court of law and finally to determine the admissibility and assessment of claims. However the following issues need to be considered:

- Use of motor vehicle at public place
- Categories of vehicle
- Person entitled to make claim
- Defendant in petition
- Effect of non-impleadment of necessary party
- Claims tribunal
- Jurisdiction of the court
- Conciliation and the *Lok Adalat*
- Determinant of the compensation

Some of the above aspects are examined with reference to the provisions of the **Motor Vehicle Act, 1988 (**as amended) for deciding the admissibility, assessment and finally settlement of Motor Third Party Claims.

Applicability of the Motor Vehicle Act, 1988

For injuries or death caused in the motor accident depending on following factors, which are to compiled with or satisfied as per the provisions of the Motor Vehicle Act,1988:

- Accident in public place
- Accident out of the use of motor vehicle

- Persons competent to approach the tribunals for claim
- A person against whom the claim could be made
- Application of relevant sections of Motor Vehicle Act,1988

Accident in Public Place

Section 146 of Motor Vehicle Act requires that no person shall use a motor vehicle in a public place unless there is in force a policy of insurance complying with the requirements of the Motor Vehicle Act, 1988. Following are a few cases in this regard, which need to be considered by the insurer for defending the case in the court of law:

- **G Bhuvanewari vs. Sornakumar (2000**) decides that public place would cover all places including those places of private ownership where the members of the public could have an access whether free or controlled in any manner whatsoever.
- **UII vs. Lakshmi (1997**) a wide expanse of the paddy field where an accident took place was held to be a public place.
- **The New India Assurance Co. Ltd. vs. Urmiladevi (1998**) a person looking after his contract work in a factory was hit by a truck at the factory gate and he sustains fatal injuries.

Use of Motor Vehicle

As per Section 165 of the Act, death or personal injury of third party must have resulted out of an accident by the use of motor vehicle for payment of the motor third party claims in satisfaction of the court award under the Motor Vehicle Act, 1988. The following case studies clarify the provisions:

- **The Oriental Fire & General Insurance Co. Ltd. vs. Sripat (1998):** The death of a cleaner working underneath of his stationery vehicle was said to have met with an accident out of use of vehicle in public place.

- **UIIC vs. Pushpalaya Printers (2004):** A road roller moving close by to a house that caused damage to the building by tremor caused to the ground and the wall said to have caused an impact and hence actionable for loss or damage suffered by third party.

- **UIIC vs. Forest Department:** The truck of the forest department met with an accident due to wrongful act of the occupants of the pickup van who was throwing logs in the public road with a view to obstruct a chase of the patrolling party. The damages or loss caused to third party are subject to actions under **the Motor Vehicle Act, 1988.**

- **Ritadevi vs. The New India Assurance Co. Ltd. (2000):** A passenger who was last seen in the auto rickshaw has been found murdered later. It was held by the Supreme Court that the death must be constructed as having been caused by an accident involving the use of motor vehicle.

Documents Required for TP Claim

a) Court Award from MACT (Motor Accident Claim Tribunal) court satisfying the relevant provisions of the Act, b) RC Book, c) Insurance Policy, d) Driving License, e) Police Report, f) Income Statement, g) Road Permit, h) Post Mortem Report for payment of death claim, i) Disablement Certificate for settlement of claim for disablement j) Medical and Hospital bills supported by relevant medical Bills with receipts certified by hospital and the attending doctor for payment.

Motor Vehicles Act & determination of Compensation to Third party

- **Hit and Run Case:** Section 161 provides for payment of compensation from solatium fund, Rs 25,000 for death and Rs 12,500 for grievous hurt.

- **Liability without Fault:** Section 140 provides for payment of compensation on fault basis for Rs 50,000 in case of death and Rs 25,000 in case of disablement.

- **Payment of Compensation on Structural Formula:** Under Section 163 (A) & 163(B), compensation as per structure formula is provided depending upon the age, income and the multiplier with Minimum compensation Rs 50,000.

Marine Insurance Cargo Claims

Marine Cargo Claims — Scope and Nature

Marine Cargo Claims is very complex as one single risk insured may involve multiplicity of type of transits, modes of conveyance, nature of cargo, moral hazards of consignor or consignee, nature or cause of accidents etc., which have had direct impact over the admissibility and assessment of claim. In order to ensure prompt and proper settlement of claims, the insurer shall look into the following aspects of claim management:

1. **Appointment of Appropriate Surveyor** who can establish the insurer's liability in consideration of admissibility and assessment of claims. The surveyor must be through about the policy coverage, exclusions, terms, conditions, warranties, the terms of relevant ICC or ITC clause, the provisions of the Marine Insurance Act, as applicable to the particular policy and claims in order to establish the admissibility of claim and make proper assessment thereof.

2. **Nature and Types of Losses** (Discussed Separately)

3. **Documentation to Support Claims** (Discussed separately)

4. **Recovery Action against Carrier** (Discussed Separately)

5. **Loss Minimization Aspects** (Discussed Separately)

6. **Claim Processing and Settlement** promptly and properly

Types of Cargo Loss

i. Total Loss — Actual or Constructive

ii.	Partial Loss	— a) Particular Average
		b) General Average
iii.	Expenses	— a) Sue and Labour Charges
		b) Particular Charges
		c) Salvage Charges
iv.	Extra Charges	— a) Survey Fees
		b) Sale fees

Losses under above category are to be established and assessed in terms of policy conditions and the provisions of the Marine Insurance Act 196.3

a. Partial and Total Loss

As described under Section 56 of The Marine Insurance Act, namely:

- A loss may be either total or partial. Any loss other than a total loss is a partial loss.
- A total loss may be either an actual total loss, or a constructive total loss.
- Unless a different intention appears form the terms of the policy, an insurance against total loss includes a constructive, as well as an actual, total loss.
- Where the assured brings a suit for a total loss and the evidence proves only a partial loss, he may, unless the policy otherwise provides, recover damage for a partial loss.
- Where goods reach their destination in species, but by reason of obliteration of marks, or otherwise, they are incapable of identification, the loss, if any, is partial and not total.

b. Actual Total Loss

Subject matter is totally destroyed or so damaged as to cease to be thing of the kind insured or the assured is irretrievably deprived thereof as per Section 57(1) of the Marine Insurance Act, 1963. If no news received after the lapse of a reasonable period, it is presumed to be actual total loss by marine peril. Cargo also deemed to be actual total loss as per Section 58. Total loss as mentioned in Section 68 will be determined and decided with reference to the provisions of this Act, and to any express provision in the policy, where there is a total loss of the subject-matter insured. The measure of total loss will be decided with reference to following two situations:

(i) if the policy be a valued policy, the measure of indemnity is the sum fixed by the policy; and

(ii) If the policy be an unvalued policy, the measure of indemnity is the insurable value of the subject-matter insured.

c. Constructive Total Loss

This arises when the subject matter is reasonably abandoned either because: a) actual total loss appears unavoidable; or b) to prevent actual total loss requires expenditure exceeding the saved value as per Section 60, which also provides that:

1. Subject to any express provision in the policy, there is a constructive total loss where the subject-matter insured is reasonably abandoned on account of its actual total loss appearing to be unavoidable, or because it could not be preserved from actual total loss without an expenditure which would exceed its value when the expenditure had been incurred.

2. In particular, there is a constructive total loss:

   - where the assured is deprived of the possession of his ship or goods by a peril insured against;

- it is unlikely that he can recover the ship or goods, as the case may be;
- the cost of recovering the ship or goods, as the case may be, would exceed their value when recovered;
- in the case of damage to a ship, where she is so damaged by a peril insured against that the cost of repairing the damage would exceed the value of the ship when repaired;
- In estimating the cost of repairs, no deduction is to be made in respect of general average contributions to those repairs payable by other interests, but account is to be taken of the expense of future salvage operations and of any future general average contributions to which the ship would be liable if repaired; or
- In case of damage to goods, where the cost of repairing the damage and forwarding the goods to their destination would exceed their value on arrival.

Examples of Assessment in Total Loss (Assuming admissibility of claim is established)

Example 1: 2000 bags of sugar are insured for and valued at Rs 4,00,000. Out of which, 10 bags are totally damaged by insured peril. What would be claim Amount?

Assessment

Bags being of equal value, the insured value of 10 bags are Rs 2000 would be the amount of assessment of claim.

Example 2: Insurance of 125 computers under ICC (A) for Rs. 30,50,000

100 Computers… Model A @ Rs 20,000 each (Invoice Price)	20,00,000

25 typewriters Model B @ Rs 40,000 each (Invoice Price)	10,00,000
Total Invoice Value	30,00,000

When consignment arrived at destination, one Computer Model A and the other computer Model B were found missing. What would be claim Amount?

Assessment

Invoice Price of Model A	Rs 20,000
Invoice Price of Model B	Rs 40,000
Invoice value of the missing machines	Rs 60,000

Total invoice value of Rs 30,00,000 insured for Rs 30,50,000

Hence Invoice value of Rs.60,000 is insured for Rs 61000

Claim payable for Rs 61,000

Partial Loss — Particular Average and Particular Charges

Particular average: As provided in Section 64 of the Marine Insurance Act, 1963 particular average loss is a partial loss of the subject-matter insured, caused by a peril insured against, and which is not a general average loss.

Particular Charges: Expenses incurred by or on behalf of the assured for the safety or preservation of the subject-matter insured, other than general average and salvage charges, are called particular charges. Particular charges are not included in particular average.

Salvage charges: As provided in Section 65 of the Marine Insurance Act, subject to any express provision in the policy, salvage charges incurred in preventing a loss by perils insured against may be recovered as a loss by those perils. “Salvage charges” means the charges recoverable under maritime law by a salver independently of contract. They do not include the expenses of services in the nature of salvage rendered by the assured or his agents, or any person employed for hire by them, for the purpose of averting a peril insured against. Such expenses, where properly incurred, may be recovered as particular charges or as a general average loss, according to the circumstances under which they were incurred.

Examples of Partial Loss

Example 3: A consignment of jute insured for Rs 22,00,000 found partially damaged at destination. As per Survey report, Gross Arrived Damaged Value at destination was Rs 800,000 and Gross Sound value determined was Rs 20,00,000

Assessment:

Partial Loss worked out is as under:

G.A.S.V.	Rs 20,00,000
G.A.D.V.	Rs 8,00,000
Loss	Rs 12,00,000

Per cent Damage to Cargo =

$$= \frac{12,00,000 \text{ x } 100}{20,00,000} = 60 \text{ per cent}$$

Thus Assessed loss is 60 per cent of insured value of Rs 22,00,000 = Rs 1,32,000.

Claim is payable for Rs 1,32,000

Example 4: 4000 T-shirts insured for Rs 400,000, so value, were shipped to Australia from Mumbai. On the voyage heavy weather was experienced and damage to cargo occurred, consequent to leakage in the hold. Subsequently, a fire broke out, seriously damaging the ship and cargo. On arrival, following losses were ascertained:

(a) 1200 T-shirts damaged by fire – depreciation 30 per cent

(b) 400 T-shirts damaged by sea water – depreciation 50 per cent

(c) 120 T-shirts were found missing.

(d) 100 T-shirts were lost overboard during discharge

(e) 2180 T-shirts arrived sound

Survey fees were Rs 10,000. Each box was invoiced at the same price and therefore each case was of equal value. What will be the assessment of loss to cargo damaged under three policy coverages namely ICC (A), ICC (B) and ICC(C)?

Assessment:

Particulars	**Insured Value**	**Depreciation**	**Claim**
1200 pieces fire damage	Rs 120,000	30%	36,000
400 pieces seawater damage	40,000	50%	20,000
100 piecess lost overboard	10,000		10,000
120 pieces missing	12,000		12,000
			Rs 78,000

Coverage Amount Assessed under three Coverage ICC (A/B/C)

(a) **Claim under ICC (A)**

All 4 items	….	78,000	
Plus survey fees	….	10,000	**Rs 88,000**

(b) Claim under ICC (B

First Three Items	….	66000	
Survey Fees	…	10000	**Rs 76,000**

(c) Claim under ICC(C)

1200 piecss fire damage	36,000	
Survey fees	10,000	**Rs 46,000**

Thus assessment will differ with the nature of coverage.

Partial Loss of Ship

As provided under Section 69 where a ship is damaged, but is not totally lost, the measure of indemnity subject to any express provision in the policy, is decided in the following situations:

1. where the ship has been repaired, the assured is entitled to the reasonable cost of the repairs, less the customary deductions, but not exceeding the sum insured in respect of any one casualty;

2. where the ship has been only partially repaired, the assured is entitled to the reasonable cost of such repairs, computed as above, and also to be indemnified for the reasonable depreciation, if any, arising from the un-repaired damage, provided that the aggregate amount shall not exceed the cost of repairing the whole damage, computed as above;

3. where the ship has not been repaired, and has not been sold in her damaged state during the risk, the assured is entitled to be indemnified for the reasonable depreciation arising from the un-repaired damage, but not exceeding the reasonable cost of repairing such damage, computed as above; and

4. where the ship has not been repaired, and has been sold in her damaged state during the risk, the assured is entitled to be indemnified for the reasonable cost of repairing the damage, computed as above, but not exceeding the depreciation in value as ascertained by the sale.

Documents to be Verified

Documents required for settlement of marine cargo claims are many and vary according to nature and type of losses. However following are the fundamental documents:

- Original policy/Certificate/Declaration under open policy
- Shipping Invoice with price, description, sale terms, packing list
- Bill of Lading (as a receipt for the goods and evidence of shipment, which also indicates the condition of the goods on loading, Clean BL)
- Railway Receipt/lorry Receipt/Air Consignment Note/Postal Receipt
- Certificate of Origin showing the origin of goods, if required
- Bill of Entry (Details of shipment, Customs duty assessed/ paid)
- Pre-shipment Survey/inspection Report
- Master's Protest or Extract from vessel's log book giving details of the way the vessel sustained casualty/loss/damage/ heavy weather
- Lost Overboard Certificate if loss occurred during loading/ discharge
- Delivery ex ship Receipt given to ship-owners by cargo superintendent if employed. Also details of landing remarks on damage

Other Particulars to be Verified

For transit ex-ship to final destination, following documents are mandatory:

- Identification of Carrier (whether authorized or not)
- Nature of receipt given by carrier on collection of goods
- Nature of receipt given to the carrier upon delivery
- Open Assessment Report by Carrier
- Survey Report showing cause, nature and extent (sound and unsound)
- Account of sales-date, place, unit price with details of sound value
- Accounts of reconditioning costs, if any
- Condemnation Certificate, if damaged goods are destroyed on orders of health authorities or other Government authority

Engineering Insurance Claims

Scope and Nature of Insurance Claims

Engineering Claims arise from various types of Engineering policies, namely: a) project policies for erection insurance like, Marine Cum-Erection, Storage Cum-Erection, Erection All Risks Insurance, and Contractors' All Risks Insurance, and Contractors' Plant and Machinery Insurance; b) Consequential Loss Insurance like Advance Loss of Profit Insurance; or c) Operational Policies of Machinery Breakdown Insurance, Boiler Explosion Insurance and Electronic Equipment Insurance.

Claims under Erecting All Risks Insurance

All accidental physical loss/damage due to any cause except those specifically excluded

is admissible under this payable. Thus claims that may arise from any of the following risks/incidents occurred during the period of project covered by the policy are payable under policy after deduction for policy excess or voluntary excess:

- Act of God Risks — Earthquake, Landslide, Flood, Storm etc.
- Fire, Lightening, Riot & Strike, Sabotage
- Theft & Burglary
- Faults during erection, lack of skill/carelessness of workers
- Short Circuit, explosions tearing apart for centrifugal forces
- Electrical and Mechanical Failure during trial & testing

But the claims arising from the following perils are not admissible under this policy:

- War Risks including nuclear reaction
- Damages falling under manufacturer's guarantee
- Cost of rectification or correction of any error unless results into physical loss
- Willful act or gross negligence of the insured
- Consequential loss of any kind and contractor liability
- Normal Wear & tear, gradual deterioration due to atmospheric condition resulting into rust, scratching etc.

Importantly loss occurred during transit of project materials are also covered under the policy. Erection All Risks insurance is a combined cover for marine/transit cum EAR provided cover for risks starts right from the moment the machinery leaves the Indian/ foreign manufacturers' warehouse and remained in force during voyage till the erection is over and tested.

Limit of indemnity is decided in consideration of sum-insured which may include the amounts of the following items:

- Imports (Landed Costs) at site
- Indigenous Materials (Landed costs) at site
- Costs of Erection (Exclusive of preoperative Exp but including costs of visits of specialists and supervision charges
- Permanent Civil Eng. Works
- Half the escalated value, if escalation opted for

If following items are additionally covered with specific endorsement on payment of additional premium, the claim for the following items is also payable along the amounts of loss or damage to the above noted items:

(a) Custom duty paid on clearance

(b) Clearing & Forwarding charges to the agents.

(c) Storage loss or damage at fabricator's premises/workshop

Claims under Machinery Breakdown Insurance

Scope and Nature of Claims

Claims that may arise from any of the following risks/incidents occurred during the period of insurance are admissible and payable after deduction of specified excess:

Electrical Breakdown due to:

- under voltage
- excess current
- loose connection

- arcing
- sparking
- ageing insulation
- open circuit
- short circuit

Mechanical Breakdown due to:

- Mechanical breakdown due to
- falling object
- entry of foreign object
- failure of safety devices
- failure of parts - rotating/reciprocating
- faulty operations
- over heating
- vibration
- fouling - abuse
- dust - humidity

Loss not Covered under the Policy

Any loss or damaged to the insured machinery due to following causes are not payable under this policy:

- Risks covered by Fire policy
- War - nuclear

- Overload Test
- Wear & Tear
- Wilful act
- Gross negligence
- Existing defect
- Consequential loss
- Effect - continuous usage
- Excess
- Manufacturing defects

Basis of Indemnity

Present day replacement value of new machine is the basis of indemnity. The replacement value may include: i) Basic cost; ii) Incidental/erection cost or reinstatement value provided the sum-insured is adequate. Indemnity may be required for partial loss or total loss depending upon the nature or extent of loss. Claim for Partial loss that may include the costs of Repairs and Replacement of parts without deduction for depreciation. Total loss comprising present day replacement value is settled up to the sum-insured after deduction for salvage and specified excess, but without deduction for depreciation.

Basis for Settlement of Claim

Claims are settled on the basis of final survey report. The surveyor shall investigate, inquire the cause of loss, establish the admissibility of claims and finally determine the liability of the insurer in respect of accidental damage or loss to the insured property keeping in view of the foregoing aspects in this regard. However the surveyor must confirm the following aspects establishing the admissibility of claim for damage or loss to a TG set:

- In case of claim for breakdown of turbo generator (TG set), the surveyor shall investigate and confirm that all mechanical and electrical parts have been inspected and overhauled thoroughly under the supervision of maker's representatives in a completely opened up state at least at least every 2 years and overall shall take place after 32000 hours of operation or every 4 years. Such inspection report has been furnished to the insurer immediately after the work was done and claim does not include any element of said overhauling expenses.

- The insured has rendered the aforesaid regular inspections in such a way as to enable the insurer's representative to be present at the inspection. The insurer shall be informed at least 7 days in advance of the commencement of any overhauling necessary as per expert opinion. If the insured fails to comply with the requirements of this condition, the insurer shall be free from all liability for loss or damage whatsoever.

- The claim has not arisen from excluded perils viz., willful act or gross negligence of insured or their responsible representatives.

- The surveyor has to also enquire and confirm that loss is not inflated by wear and tear of any machine or parts thereof and accident, Loss, Damage or Liability has not been caused by or arising from or in consequences of overload experiments or tests requiring the imposition.

20

INSURANCE CLAIMS–LIABILITY INSURANCE

Liability Insurance Claims Vs. Property Insurance Claims

The procedures followed for settlement of claims under liability insurance are different from those followed for claims under property insurance as discussed in the previous chapter. In the property insurance for settlement of claims, only the liability of the underwriters to the insured is decided as per policy terms and conditions, while in liability insurance claims, the insurers are to consider two types of liabilities- one liability of the insured to the third party and other is the liability of the insurer to the insured. The liability of the insured to the third party is decided by the Court of Law either under relevant statutes or under common law, while the liability of the insurer to the insured is decided as per terms and conditions of the liability policy covering the specific liability risk. Unless and until the liability of the insured is established in the court of law, there could be no liability of the insurer to the insured. The Insured and the insurer are to take all possible defenses as per merit of the cases in the legal actions brought by the third party against the insured person either to reduce or avoid the liability. After the insured's liability is determined by the court, the next consideration comes as to whether the said liability comes within the purview of the policy issued to the insured.

If the liability is admissible under relevant liability policy, then the indemnity will be decided according to the term and conditions of the policy applicable. For claims under property policy the surveyors investigate, examine and establish the admissibility of the loss with reference to the proximate cause of loss as covered by the insured perils and other terms and conditions of the policy and then make the assessment with reference to his physical verification of damage and examinations of books and accounts, evidences, reports etc. But in liability claims the professional surveyors are replaced by the efficient lawyers and investigators for defending the legal case and action brought by the third party. In liability claims, apart from technical knowledge, the insurers must have fair knowledge on various laws, legal aspects and regulations to defend the case on behalf of the insured to justify the liability under action brought by the third party. The Liability policies are of two types: Claims Made Liability Policy and Occurrence Based Liability Policy.

Claims Made Policy Vs. Occurrence Based Policy

In almost all countries Claim-made version of liability policy is widely used by insurers for limiting their liability and ensuring prudent underwriting in view of huge loss asbestos claims being paid by Lloyds many years after issuance of occurrence based Employers' Liability policy. In Chapter 16, the requirements of Claim Made Policy have been discussed. Here we will discuss the application of those requirements with practical examples. The liability claim made for bodily injury or property damage that occurred due to negligence of the insured must be first made by third party against the insured during either policy period or extended reporting period provided. Claims Made Policy wording mandates that the event-giving rise to the claim should have occurred during the period of insurance and claim should be made during period of insurance. Period of insurance is determined as period between the date of inception of the First Claims Made policy (continued without a break) and expiry of the current policy. Occurrence based wording simply imply that event giving rise to the claim must occur during policy period and the insurer would respond to claims whenever the claim is thereafter made on him.

Example: Mr "X" purchased 1-year claim made product policy from RI Insurance with an inception date of 1 January, 2007 which was the retroactive date. On 1 January 2008 the policy was purchased from PI Insurance Co. for 1-year with the retroactive date of 1 January 2008. Now, on 1 July 2008 claim was made against Mr "X" for an injury occurred on 1 October 2008 for the use of his product manufactured in December 2006.

Q. 1. Would 2008 policy of PI Insurance cover the claim first made in 2005?

Q. 2. Would 2007 policy of RI Insurance cover the claim first made in 2005?

Answers

Product Manufactured	Injury Occurred	Claim Made
2006	2007	2008

1. No, 2008 policy of PI will not respond even though the claim occurred during policy period as it has occurred before retroactive date.

2. No, 2007 policy of RI will not respond even though the injury occurred within the retroactive date for the product manufactured in 2006.

Product Liability Claims

Legal Aspects of Product Liability Claims

According to merits of the case producers, distributors and retailers are severally or jointly liable for bodily injury (death or disease) caused to the consumers (user) due to defect in the goods. But in many cases only manufactures are held liable. In this regard the judgment pronounced by Lord Atkin in Donoghue vs. Stevenson (1932) deserves special mention. When a manufacturer sells his products in such a form or manner that he intends them to reach the ultimate consumers in the same form in which the products left him with no reasonable possibility of intermediate examination and with the knowledge that the absence of reasonable care in the preparation or putting up of the products will result in an injury to the consumer's life or property, then the manufacturer owes the duty to the consumers to take that reasonable care in stead of a retailer or distributor.

The circumstances of the aforesaid case were that a bottle of ginger-beer manufactured by the defendant was purchased from a retailer by a friend of the plaintiff. The bottle was opaque. After consuming some of the ginger-beer the plaintiff found in the bottle some remains of a snail. She also suffered injury from consumption of ginger. The plaintiff brought a legal action and succeeded in her claim against the defendant for damages in respect of the shock and illness which she suffered. The direct liability of the manufacturer to the consumer arises when goods are sold in the manner as described above especially in case of foodstuffs or beverages. The Lord Atkin principle has also operated in connection with a wide variety of products, like cosmetics, perfumes, underwear, hair dye, and motor cars. Furthermore, it has been held to apply not only to manufacturers but also to repairers (Herschtal vs. Steward and Arden Ltd., 1940). This kind of liability claims for negligence probably extend only to injury to persons or damage to property belonging to third party and not to any financial losses incurred by third party due to fact that goods are merely defective. Actions brought on a breach of condition or warranty implied or expressive by Sale of Goods Act is different from actions based on negligence of the manufacturer or traders as the case may be.

Claim on Product Guarantee Vs. Product Liability Claim

The object of product guarantee insurance is to indemnify the insured against some of the risks, which are not covered under a standard product liability policy. In particular claims under product guarantee relate to the failure of the product to fulfill its intended propose, which is totally different from claims under product liability insurance which covers the legal liability of the producers or traders for the damages including third party bodily injury or property party damages caused due to defects in the products manufactured or sale. A product liability policy does not cover replacement of goods supplied or financial loss. Following cases are the financial loss which will be considered claims under product guarantee, but not claims under product liabilities.

For loss of trade sustained by the retailer, for example, a café proprietor may lose trade as a result of publicity following a prosecution against him for supplying a meat pie with a foreign body in it. Financial loss incurred by the user when goods fall to fulfill the purpose for which they were supplied, without there being any injury or damage. For example, new machinery in a factory may develop a fault causing a shut-down of the factory until it can be corrected. Wages may have to be paid during the period and trade may be lost. Compensation may be claimed from the supplier of the machinery. After being put on to the market it may be discovered that the product has a dangerous fault. It may be necessary to withdraw the product completely and replace it, or to recall it to have the fault corrected. A limited market exists to offer cover against some of these risks although co-insurance will usually apply and the insured will be responsible for a percentage of each claim. All these are the financial risks may be covered by Product Guarantee Insurance, but not by the Product Liability Insurance which covers only claim for bodily injury including third party death and injury arising out of products insured.

Claims under Public Liability Policy

Origin of Public Liability Claims

Claims under Public Liability policy may come from individuals and businesses connected with the handling of hazardous substances or process exposing themselves into accidental bodily injuries or property dames to outsiders. Thus all dealing hazardous goods are required to take PLI under the Act. The indemnity only applies to claims arising out of accidents occurring in the Insured premises during the period of insurance first made in writing against the Insured during the policy period and the insured is indemnified in accordance with Operative clause of the policy for and/or arising out of injury/damage but only against the claims arising out of or in connection with the business specified in the schedule.

Types of Liability Claims

This insurance policy indemnifies the insured for the payment of liability towards the people affected by the accident due to death, injury or property damage. The admissibility and assessment of Claims under Public Liability Policy according to the nature of liability policies which are grouped under following three classes:

1. Public Liability Insurance Act Policy (PLI Act'91)
2. Public Liability Insurance(Industrial Risk)
3. Public Liability Insurance (Non-industrial Risks)

Fundamental considerations for claims under Public Liability policy are:

- Legal Liability of the Insured
- Towards the damages to the third party
- Death/injury/diseases/Property Damage
- Due to Accidents
- Up to Indemnity Limit specified in policy

Claim Settlement Factors under Public Liability Act Policy

- No necessity to prove the insured's fault/ negligence causing accidental damage.
- Accident in insured's trade/establishment
- Injury or Damage to Property due to accident.
- Investigation under the advice of the Collector
- Order by the Court in jurisdiction

Compensation Limits Per Person under Public Liability Act Policy

The limits for compensation per person as provided by Sec.3 and the Schedule in the PLI Act are as under:

- **Fatal Accident:** Rs 25,000
- **Permanent Total Disablement:** Rs 25,000
- **Permanent Partial Disablement:** Relief is based on per cent of Disability certified by an authorized physician/ Registered. Medical practitioner
- **Loss of Earning:** Rs 1000 per month if victim is hospitalized for more than 3 days and above 16 yrs of age
- **Medical Expense:** up to Rs 12,500 (maximum) in each case.
- **Property Damage:** Rs 6000

But the total indemnity to be made by the insurers to the insured depends on AOA and AOY limits specified in the policy.

Claims under Public Liability Insurance for Industrial Risk

The amounts of compensation are decided by the court as per the common law. There are no limits for compensation. But there are always limits of liability for indemnifications. Total claim amount or indemnity under Public Liability Insurance for Industrial Risk and Non-Industrial Risks are decided as per the Indemnity clause in the policy.

Indemnity Clause

Like the provisions of the Act Policy the indemnity only applies to claims arising out of accidents occurring in the Insured premises during the **period of insurance** first made in writing against the Insured during the **policy period** and the insured is indemnified in accordance with Operative clause for and/or arising out of **injury/ damage** but only against the claims arising out of or in connection with the business specified in the schedule and not against claims arising out of or in connection with: a) pollution howsoever caused unless specifically covered; b) any product. Here **Injury** means death, bodily injury, illness or disease of or to any person. **Policy Period** means the period commencing from effective date and hour and terminating on the expiry date as shown in policy schedule. **Period of Insurance** means the period commencing from the retroactive date and terminating on the expiry date. **Retroactive Date** means the date when the risk is first incepted and thereafter renewed without break. **Premises** include pipelines running outside up to 1 km from the place of origin.

Reporting of Claims and Admissibility under Public Liability Insurance for Industrial Risk

In order to be admissible claims must be reported as per two important clauses of the policy: i) Notification Extension Clause; and ii) Extended Claim reporting Clause.

(i) Notification Extension Clause

If the company accepts any notification of the insured during the policy period about any specific event or circumstances which may give rise to a claim which form the subject matter of indemnity by the policy, the company will deal with such claim as if they had been first made against the insured during the policy period up to the maximum time limit laid down in the Indian Limitation Act.

(ii) Extended Claim reporting Clause

In case of non-renewal or cancellation of policy, the company will allow a time limit not exceeding 90 days from the date of expiry or cancellation of the policy, provided no insurance is in force during the extended reporting period for same interest, for notification of claims for accidents which had taken place during period of insurance.

Indemnity Limits and Other Relevant Considerations for Deciding Claims

- **Indemnity Limits:** Insurer's total liability to pay compensation, defense costs, fees and expenses shall not exceed the Indemnity limit stated in the schedule. Indemnity Limit applies to any one claim or series of claim arising from one originating cause and to total liability of the company during policy period.

- **Claim Series Clause:** All claims arising out of the same cause or error are to be aggregated and treated as one claim and no coverage foe claims made arising from one specific cause which is made later than 3 years after the first claim of the series.

- **Compulsory Excess:** The insured shall bear as Compulsory excess the amount or percentage of the limit of indemnity per any one accident so stipulated. Such excess shall be applicable to both: a) death/bodily injury; and b) property damage inclusive of costs.

Professional Liability Claims

The technical and administrative aspects of all liability claims are same. Only legal aspects which are the origin of liability claims are different in different liability claims. To make the legal aspects of professional liability clear we need to first discuss a few case studies on the legal liability of various professionals.

Case Studies on Professionals' Legal liability

The origin of professional liability insurance claims lies in the legal decisions in the court of law. Following are the few case studies thereupon:

1. **Candler vs. Crane Christmas & Co (1932):** On the request of the MD of a company, a Chartered Accountant (CA) prepared accounts of the company. The plaintiff used the said accounts for his investment decision in the company. The plaintiff invested in equities of the company relying on CA's accounts, but the company went into liquidation very shortly thereafter and the plaintiff suffered financial loss. It was held that there was no contractual relation between the plaintiff and the defendant and therefore the defendant was not liable to the plaintiff.

2. **Hydley Byrne & Co Ltd. vs. Heller & Partners (1963):** It is a leading case on the legal liability of a merchant bank to the third party. The judgment in this case was a landmark one making a breakthrough in the perspective of the legal liability of the professionals. It was held in this case that professional are liable to third party for financial loss or other loss incurred by him due to negligence or breach of duty irrespective of the existence of any contract with the persons or contractual relationship between the professional and others concerned. They are liable to the users of his professional opinions for the financial loss incurred by the users even without his contractual relationship with the plaintiff. The decision of Candler case was just reversed. After this landmark judgment on the nature and extent of legal liability of professionals who owe legal liability to third party for their professional knowledge, ethics, skill and standard that the third party rely upon. It was decided by the House of Lords in the case that though Merchant Bank gave the report of credit rating of a potential customer of the plaintive on request of the plaintiff's Bank, it was liable to the plaintiff i.e. bank's customer, who suffered financial for granting credit to his customers having relied upon the report of the merchant bank.

3. **Dodds & Dodds Vs. Millmann (1964):** Similar decision was taken in this case fixing the liability of builder's agent for his misstatement for the loss suffered by the plaintiff who relied upon the agent's statement for his purchase.

4. **Yianniv Edwin Evands & Sons Case (1981):** The Court decided the liability of a professional valuer to the third party who suffered financial loss, having relied upon the professional's report for his mortgage deals with others as the report was a negligent misstatement.

5. In **Clay Vs. A.J. Crump and Sons (1963),** an architect was held responsible (together with the contractors) for personal injuries caused by collapsing of walls. The architect, instead of going to look at the wall himself, spoke to the demolition

contractor who in turn took the opinion of a foreman. The architect was held to be negligent for failing to exercise adequate supervision, skill and knowledge as he delegated his duties for work of supervision to others, what he was under an obligation to perform himself.

6. In **Cherry Ltd. Vs. Allied Insurance Brokers, Ltd., (1978**), the brokers failed to tell their clients that an insurance policy was no longer in force and they were held liable to the clients for property damage following a serious fire.

7. In **Bell Hotels Ltd. Vs. Motion & Anr (1952**), a firm of valuers said that the value of premises was approximately £16,000 and that brewery companies would not be interested. Plaintiffs sold for £25,000 to a brewery company. It was held that the defendant had not exercised reasonable skill and care, and damages were assessed at £5000.

These few case studies indicate how professionals owe legal liabilities to third party. There may be admissible claims if the professionals are adequately covered by appropriate Professional Insurance Liability Policies. Professional liability policies may be written either on Occurrence Basis or on Claim-Made Basis. The technical aspects and the indemnity amount of professional liability claims depend upon the nature of Professional Liability Insurance Policy.

Professional Liability Claims on Claim–Made Professional Liability

This policy provides indemnity not on occurrence basis, but on Claim made basis. The insurer will indemnify the insured for any legal liability / claim made by the third party (Clients/others) against the insured within the duration of the policy. A Claim made policy involves the following three elements:

- Third Party's claim against the Insured must be within the duration of the policy.

- The Insured event is a legal claim made by the third party against the insured.

- Third Party's claim against the insured is under the jurisdiction of Indian Courts.

Example: Mr "X", a CA took a professional indemnity policy from Fortune Insurance Co. Ltd. under a claim made clause in the year 1996. In 1998, he changed his insurer for Goodluck Co. Ltd. replacing Fortune Insurance Company Ltd. with occurrence basis with retroactive on 1st January 1998 and thereafter, he renewed the policy with Goodluck Co. Ltd. for subsequent years also. Five years after the expiry of the first policy with Fortune Insurance Co. Ltd., he came to know about a claim lodged against him by his client, "ABC Co. Ltd." for the mistakes he committed in the year 1996.

Questions:

1. Would Mr X's expired claim made policy in Fortune Co. cover this claim?

2. Would Mr X's new occurrence policy from Goodluck Co. cover?

Answers:

1. No, for basic extended reporting period (60 days after the expiry of the policy) was over. Secondly, the claim has been lodged against Mr X 5 years after the expiry of the policy.

2. No, the claim occurred before the commencement of the policy.

Liability Claims under Commercial General Liability Policy

Indemnity Limits

Claims under CGL Policy depend on limits of insurance in the

Policy. This may consist of the following limits to be considered for deciding the quantum of claims according the nature thereof:

(i) **General Aggregate Limit** for damages payable: i) for bodily injury or property damage in premises and operation liability, but not damages for 'Products and Completed Operations' under Coverage A; ii) for personal and advertising injury liability under Coverage B; and iii) Medical expenses under Coverage C.

(ii) **Product and Completed Operation Aggregate Limit** for damages payable for 'Products and Completed Operations' under Coverage A.

(iii) **Each Occurrence Limit** specifies the maximum amount of damages payable under Coverage A and Coverage C for any one occurrence.

(iv) **Personal and advertising injury Limit** specifies the maximum amount of damages payable for personal and advertising injury sustained by any one person or organization under Coverage B for any one occurrence.

(v) **Fire Damage Limit** specifies the maximum amount payable by the insurer for damages resulting from any one fire covered by Fire Legal Liability Coverage.

(vi) **Medical Expenses Limit** specifies the maximum amount payable by the insurer under Coverage to any one person.

Example: A CGL Policy issued to X Ltd provides the following insurance limits:

a.	General Aggregate	Rs 10,00,000
b.	Product Comp. Aggregate	Rs 10,00,000
c.	Each Occurrence	Rs 5,00,000
d.	Personal &Adv. Injury	Rs 5,00,000

During the policy period from 1st January 2006 to 31st December 2006 X Ltd faced and paid following liability claims for damages for seven different occurrences:

	Damages paid by X Ltd	Occurrence/Accident Type
1.	Rs 3,50,000	Accidents in Premises
2.	Rs 5,00,000	Accidents/ injury out of use of Products
3.	Rs 6,00,000	Personal and Advertising injury Liability
4.	Rs 3,00,000	Personal and Advertising injury Liability
5.	Rs 2,00,000	Products and Completed Operations'
6.	Rs 4,00,000	Products and Completed Operations'
7.	Rs.3,000	Medical Payments

Decide the liability of the insurer for each of the above occurrences

Answer: Liability of Insurer will be determined as below:

1. Rs 3,50,000 payable from **General Aggregate Limit**
2. Rs 5,00,000 payable from **Product and Completed Operation Aggregate Limit**
3. Rs 5,00,000 out of Rs 6,00,000 payable from **General Aggregate Limit** (Balance Rs 1,50,000)
4. Rs 1,50,000 out of Rs 3,00,000 payable from **General Aggregate Limit** (Balance Rs 1,50,000)
5. Rs 2,00,000 payable from **Product and Completed Operation Aggregate Limit**.
6. Rs 3,00,000 out of Rs 4,00,000 payable from **Product &Completed Operation Aggregate**

7. Rs 3,000 not payable as there is no bal **in General Aggregate Limit**

The above example has made the application of insurance limits very clear and will help the underwriters to decide the limits for determination of exposures and determine rates, terms therefore accordingly.

CGL Claims and Coverage Territory

The overage territory depends on the policy definition. If it is worldwide, then international waterways and international air space are also included in the coverage territory. In this regard following three aspects deserve a special mention in respect of products and completed operations:

1. Products made and sold by the insured in the basic coverage territory.

2. Activities of a person having home in the basic coverage territory are away from that on his named business.

3. Extension of the coverage territory for the goods or products sometimes refers to as worldwide product coverage.

Application: Mr X had brought some medicine made by a company in India before he left for Australia on business tour. After arriving at Australia Mr X took medicine and fell ill. After completing the tour and returning to India he sued the pharmaceutical Co. Y Ltd. for damage causing bodily injuries because of the use of medicine.

Q: Will the CGL policy of Y Ltd. cover the claim of Mr X?

A: Yes, since Y Ltd. sold the medicine in India provided it has taken extension for world wide product coverage.

Claims under Premises Liability or Product Liability

Sometimes confusions arise as to the scope of liability in some cases and application of limits insurance. To deal with the case and establish the admissibility and assessment of claims, the underwriter needs to analyze the relevant situation very carefully.

Applications: In a furniture shop, a customer, Mr X sat on a chair to discuss his requirement. Due to certain defect in the chair, the back of the chair went out and Mr X fell down and got injury. Now **Questions** come: Is the injury of Mr X due to Product Hazards? Does a CGL policy cover the damages/compensation to X? If yes, under which limit?

Answer: Even if the chair was a product of the Furniture Shop, the injury was not within the products hazard as defined in CGL Policy in consideration of the following two reasons:

- The chair was in the physical possession of the insured.
- The accident occurred at the named insured's premises.
- So Mr X's bodily injury will be covered under Premises and Operation of Coverage A. The amount payable by insurer for such damages will reduce the General Aggregate limit, but not the Products-Completed Operations aggregate Limit.

Fire Legal Liability Coverage and CGL Claims

Fire Legal Liability Coverage is mentioned at the end of exclusions for **Damage to Property** under Coverage A, which states that "…Paragraphs of this exclusion do not apply to damage by fire to premises while rented to you or temporarily occupied by you with permission of the owner…" It is subject to separate limit of insurance as specified in limits of insurance. This limit is generally lower than per occurrence limit. Thus salient aspects of this cover are;

- Part of Premises and Operation Coverage, but a distinct coverage
- Rented to or temporarily occupied by the named insured with the owner's permission

- Subject to Separate limits to be specified in limits of insurance
- Subject to exclusions for expected or intended injury or contractual

Application: X Ltd. leased one room in a big building in Delhi for his shop of motor spare parts. Due to negligence of an employee the rented premises caught fire and damage occurred for Rs 200,000 for the rented one and Rs 400,000 for other parts. Workers in other shops got injury and claimed for Rs 100,000. If Fire Damage Limit is Rs 500,000, each occurrence limit Rs 500,000 and aggregate Rs 20 lakh what would be the insurer's liability?

	Nature of Loss	Loss Claimed	Loss Payable
1.	Damage to rented premises	200,000	50,000
2.	Damage to rest of building	400,000	400,000
3.	Bodily Injury	100,000	50,000
	Total		**Rs 500,000**

Extended Reporting Periods and Claims Thereon

The implication of this clause has been discussed in Chapter 16. Here we will discuss the application of this clause.

Application: X was insured by a Claim-made CGL policy issued by P Insurance Co. During renewal X Ltd purchased an Occurrence CGL Policy from R Ins. Co. 40 days after the claim-made policy expired, the insured (X) came to know about an injury that occurred one week before the expiry of claim-made policy. X immediately reported the occurrence to P Insurance Co. and R Insurance Co. 1 year later the insured person finally made claim against X. Now question comes; which insurance cover will respond to the claim?

Answer: As the basic extended reporting period was in effect, because claim-made period was not renewed and *claim was for bodily injury caused by an occurrence reported to P Ins. Co within*

60 days of the expiry of the policy, P's policy will respond to the claim.

Directors' and Officers' Liability Insurance Claims

Background of Directors' and Officers' Liability Insurance Claims

Directors' and Officers' Liability Insurance is a claim made policy, which applies only to claims first made during the policy period. The limit of liability available to pay damages or settlements will be reduced by the payment of defense expenses. The insurer has no duty to defend any insured. Background of Directors' and Officers' Liability Insurance Claims can be analyzed with reference to the Wyatt Survey Report 1997 on payment of liability claims in the US. Similar is the position in the other western countries, namely:

- 31 per cent of all companies were having D&O Liability Claims.
- Public Companies were having D&O Liability Claims 3 times more than private Companies.
- Companies with more than 500 shareholders were susceptible to high frequency.
- Companies with less than US$100mn assets were having 12 per cent susceptibility to claims.
- Companies with more than US$10bn assets were having more than 63 per cent susceptibility to claims.
- The main areas of claims were wrongful termination, marketing discrimination, dishonesty and frauds, and financial reporting.

As per the 1993 Wyatt Survey, the increasing trend of corporate losses in 1990s has triggered actions and suits against directors.

The major claimants are stockholders or shareholders primarily followed by employees, customers and government agencies. One third of all corporate bodies reporting losses have faced least one claim against directors and officers. Again one-third of corporate having D&O Liability Insurance is having at least one D&O Claim. The common claims are relating to misleading statement, misrepresentation, breach of employment contract, breach of duty of care or loyalty to minority shareholders, breach of duty of fiduciary or breach of duty of disclosures to shareholders and also frauds and dishonesty. In banks and other financial institution, the common allegation is that of imprudent investment or loans and advances. Such type of liability risks worst affects the directors and officers in financial institutions. However with improved system of credit rating analysis and wide use of IT and communications worldwide, the probability as well as severity of bad investments has been reduced substantially. In late 1990s, the new high tech companies having often relied upon few experts or few products for their success have experienced attack of D&O suits from their stakeholders for the sudden corporate collapses arising from fall or failure of limited products or experts. However, the developments in both products and methods have reduced the liability exposures of directors and officers from the failure of products, process and persons in tech industries. So the underwriters need to weigh Credit Rating for the company and IT network in the whole system of policy, functions and internal control and finally corporate governance compliance.

D&O Liability Exposures in the UK and Other countries

As mentioned earlier D&O Liability claims in the UK are very common in nature and severe in quantum from various stakeholders of the corporate as experienced following case studies:

Wallersteiner vs. Moir (1975)

A minority shareholder who pursued a derivative action in his own name on behalf of the company against a director was awarded indemnity from the company for his costs. This created a precedent by which companies can be ordered to indemnify shareholders for the costs of an action before it commences.

British Airways Board vs. Parish (1979)

A director who signed a company cheque, which was subsequently dishonoured, but omitted the word 'Limited' was held personally liable for £34000 following liquidation of the company.

Dorchester Finance Co. Ltd and another vs. Stebbing and others (1980)

Two directors, both accountants signed blank cheques allowing a third, Stebbing to make loans amounting to £400000 without adequate security in breach of the Moneylenders Act. All three defendants were held liable for damages.

Prudential vs. Newman Industries (1981)

Prudential, a minority shareholder, succeeded in a derivative action against the chairman and vice chairman due to breach of duty and conspiracy over the recommendation to purchase another company. The action decided for £1mn, half of which was paid personally by the directors without being reimbursed by the company.

Estmanco (Kilner House) Ltd. vs. The Greater London Council (1982)

A shareholder without voting right was allowed to bring a derivative action against the board. The decision in this case has had very significant implications for companies having shares with restricted voting rights. Since then, the two tier structure of shares has fallen out of favour in the UK.

Evans and Sons vs. Spritebrand Ltd. and Another (1985)

A director was held personally liable for an alleged tort on the ground that he personally authorized the company to infringe copyright law by manufacturing certain components.

Caparo Industries vs. Dickman and Others (1989)

An investor succeeded in an action for damages against the auditors of a company.

Hanson (1989)

A multinational group sold a controlling interest in a subsidiary, Smith Corona, by floating it on the US Stock Exchange at a price of US$22 a share. Soon afterwards, the company cut the dividend, reduced profits, and laid of staff and share price dropped to under US$5. A shareholder class was settled for around US$24mn including legal costs. This case showed how a fancy financial strategy carried out by a group in order to reduce its losses on a subsidiary back-fired the decision makers where shareholders were expected to carry out the burden. So the shareholders can now expect better ethical standard and corporate governance from the directors in the past.

Action by Legislation on Insolvency

The liquidator of the company took action on behalf of creditors because the directors continued trading when they knew that company was insolvent. Two directors had paid the liquidator £75000.

Some D&O Liability Exposure Cases in India

1. The Supreme Court decision in M C Mehta vs. Union of India case relating to Oleum gas leak of M/S Shriram Industries. "The Management of Shriram will obtain an undertaking from the Chairman and Managing Director of the Delhi Cloth Mills Ltd., which is the owner of the various units of Shriram, as also from the Officer or Officers who are in actual management of the caustic chlorine plant, that in case there is any escape of chlorine gas resulting in death or injury to the workmen or to the people living in the vicinity, they will be personally responsible for payment of compensation for such death or injury and such undertaking shall be filed in court within 1 week from today."

2. In another case namely **Anil Hada vs. India Acrylic Ltd** – the Supreme Court held that Directors of a Company are personally responsible for the debts of the Company.

Common Types of Breaches of Duty Leading to Claims

In order to make the proper risk analysis, underwriters shall appreciate the risk profile of directors with reference to the wide range of their duties. Again to appreciate the risk profile of the directors, the underwriters need to know the strategies, planning, programmes, budgeting, operations, events in respect of production, marketing, financial and investment activities of the prospect company. As per Corporate law duties of directors are about hundreds in number. The complex character and huge number of duties that lead to claims under this policy may be brought under following brief description for the purpose of risk analysis. The breach of any of the following duties can give rise to personal liabilities either in nature of civil or criminal wrongs. Needless to mention, D&O Liability Insurance covers civil liability, but not criminal liability.

- **Duty of Care:** Directors must act with due diligence and care. This signifies that in managing the company affairs they should take as much as care as a prudent director will take in the similar situation. All decisions must be taken and all actions must be performed in good faith and in a manner, which serves the best interest of the company and does not lead to any conflict of interests.

  Martine vs. Harline (1992) US: An individual director was held liable for losses incurred by an Employee Plan Benefit. The director appointed an unqualified person to run the plan. Even though the director was one of the several executives who had approved the appointment and as he argued, others could have outvoted him in any case, the Court rejected the defense.

  Smith vs. Van Gorkom (1985) US**:** This case established that for takeover situation the directors must make a thorough, well-documented investigation and analysis before any decision.

- **Duty of Compliance:** Directors must act within the legal and regulatory framework. They must comply with various statutes, common and international law, taxation law and rules, security regulations and regulatory norms. They must also act as per corporate objectives laid down by the Memorandum of Association and within the limits of authority laid down by the Articles of Association of the company. Failure to abide by statutes affecting capital issues, taxation laws, corporate laws, common laws, environment laws etc., may bring actions against the directors by various interested groups as mentioned earlier.

- **Duty of Loyalty:** It is the duty of the directors to be loyal to the shareholders (owners of the company) who have appointed or selected them for managing the company affairs on their behalf. Accordingly, they must act and take decisions with total integrity and in the best interests of the company keeping their personal interests as secondary ones.

  First Maryland Savings and Loan US: The bank failed and formers directors were sued on the basis of that, instead of making profits for the bank, directors had been helping themselves and their friends to get rich. The jury awarded US$350mn as the result of an action brought by Maryland Deposit Insurance Fund.

- **Duty of Disclosure:** Directors are required to disclose all material facts and figures correctly in annual report or other statements signed and submitted to various authorities, regulators, stakeholders, financiers or interested groups and interested members of public. or agencies.

  Shapiro vs. American Home (1984) US: Shapiro, a company president misrepresented gross income in the proposal form and was convicted of securities fraud. This case raised a debate on the severability of the proposal form and policy. Finally one director held it that material representation or officer can relieve the insurer of the liability towards any other individual.

Credit Lyonnais Bank vs. Pathe Communication Corp (1991) US: In this case, the company board's duty to creditors and employees was recognized in preference to shareholders. When a firm was going to be insolvent, the board of directors attempted for high risks of expansion and strategies. The shareholders were aware of the risks, so the primary duty moved away from them to the creditors when the strategy failed and the firm went under insolvency.

21

LEGAL AND TECHNICAL ASPECTS OF LIFE INSURANCE

Application for Insurance and Acceptance

Prospects

A dully completed proposal or application of insurance is the basis of any insurance contract. It is required for life insurance contract as well. The duly filled in proposal form is thoroughly examined, considered and accepted by the insurer to issue an insurance policy to the insurance applicant. The application of insurance is required to be filled in by the proposer on the basis of prospectus giving details about the insurer, plans of insurance, general terms and conditions. The prospectus for insurance cover shall state details of the various insurance plans on offer, the benefits, available riders, their basis other terms and conditions, whether policy is participating or non-participating. Prospectus and proposal forms are available from agents and also in internet. The general terms, conditions, warranties, benefits, duties, and rights etc., mentioned in the prospectus forming an integral part of insurance contract are binding upon both the insured and the insurer after acceptance of business and issuance of insurance policy. The provisions of IRDA Regulation called **'Protection of Policyholders Interests Regulations' 2002** may be referred for further details in this regard.

Proposal Form

The duly completed proposal form is normally supported by the personal statement of health and habits of the person to be insured and the confidential report of the agent. Sometimes the person to be insured could be different from the proposer, as in the case of parents proposing for insurance cover for their children. In case medical examination for the prospect is required as per the prospectus, the personal statement is referred to a medical examiner. As per laid-down norms regulations, a copy of the proposal form is enclosed with the policy issued to the policyholder. If the proposal form needs to be filled up in a language, which is not familiar to the proposer or if the proposer is illiterate and where he can affix his thumb impression only, some one (agent) filling in the proposal form is to declare in the relevant proposal form that he has explained the contents to the proposer and the proposer has understood the same.

Principle of Utmost Good-faith

In a proposal form, the proposer makes a declaration to the effect that all statements in the proposal form are true in every respect. In case of any misstatement, misrepresentation or concealment of fact, the insurance contract is liable to be cancelled on the ground of breach of the fundamental principle of utmost good-faith. However the insurer's right to cancel the contract is governed by the provisions of Section 45 of the Insurance Act 1938. The said provisions precisely stipulate that a policy cannot be called in question after 2 years or on the grounds of false statement or non-disclosure of fact, unless it is proved to be material and made with fraudulent intent.

The duty of disclosure rests on both the parties: the insured and the insurer. The breach of duty on the part of the proposer comes to light easily. But there could be cases of breach of duty of disclosure on the part of the insurer or the agent making representation on behalf of the insurer. Following are the two situations, where a breach of duty of disclosure, i.e. principle of utmost good-faith on the part of the insurer may arise:

- Making untrue statement in the prospectus during sale; and
- Not intimating the proposer certain benefits such as loans, fixed rate of return or bonus, which are not available in certain policies.

Principle of Insurable Interest

As mentioned earlier, an insurance contract is based on the fundamental principle of insurable interest. In consideration of this principle all risks are not insurable and all applications of insurance or proposals are not acceptable unless the proposers do have the insurable interest in the life being insured by him. It has been decided in the court of law that a person has unlimited insurable interest in his own life. Following are the few situations where the proposers might have insurable interests in others' life and apply for insurance cover for them:

- A husband has insurable interest in the life of his wife and vice-versa;
- An employer has insurable interest in the life of his employees;
- An employee has insurable interest in the life of his employer;
- A creditor has insurable interest in the life of the debtor;
- Partners have insurable interest in the life of other partners;
- A surety has insurable interest in the life of his co-surety; and
- Parents have insurable interest in the life of a child.

Above category of persons can be applicants for life insurance covers for others.

Medical Examination

- The person proposed to be insured is normally subject to medical examination to determine the state of health and the terms of insurance to be agreed upon and premium to be decided. High age of the person to be insured and high proposed sum-insured may require rigorous/detailed medical examination with more medical tests like Radiology, Sonography, ECG, and Stress test etc. However insurers sometimes may waive the requirement of medical examination or liberalize the process of medical examination in certain cases or for certain type of policies on the basis of their specialized knowledge and experience.

- Non-medical insurance schemes offered by insurers are generally meant for persons with maximum age at the entry up to 45years or with maximum sum-assured for Rs 1 lakh or Rs 2 lakh.

- Sometimes non-medical group insurance schemes are offered to Government departments, Quasi-Government offices, State corporations, government industrial undertaking, even non-government commercial or industrial undertakings in view of their compliance of requirement of medical examination at the time of recruitment and report thereof. However many insurers offer non-medical scheme for persons with SSC/ Matric passed with the maximum sum-assured of Rs 8 lakhs or Commissioned officers in armed forces with the maximum sum-assured of Rs 10 lakhs provided the insured person does not exceed 45 years of age.

Age Proof

Death risks increase as the age advances. Age proof is a vital document for risk analysis and risk evaluation for life insurance policies for determination the cost of risks. Municipal Birth Certificate, Certificate from school or college records, Certificate from the service register in case of Government employees or semi Government employees, Passport, etc., are considered standard age-proof.

Special Reports

Apart from proposal form, personal statement, agent's report, medical examiner's report, age-proof as mentioned above, special medical reports may be required in any of the following situations of life insurance underwriting:

a. Very high sum assured, say, above Rs 5 lakhs;

b. Higher age at the entry-level;

c. Proposal for insurance cover under a high-risk plan; and

d. Some adverse features, symptoms disclosed by standard medical reports.

Such special reports are called for a fair assessment of risk. These special reports may relate to medical/ health condition, income, habits, and life-style, etc. Such report is also needed to establish that the sum assured proposed for a key person represents fairly the value of that person to the enterprise.

Acceptance of Risks

After careful examination of the proposal for insurance cover and above-noted particulars or reports, the underwriter decides to accept the risks at the standard rate of premium or modified rate of premium for the proposed sum-insured or for lesser amount, Depending upon the risk-analysis report an underwriter may go for following types of modifications from the proposed cover:

a. accepting risks for a Sum assured lesser than that proposed;

b. accepting for a shorter term than proposed;

c. accepting for a different plan than proposed;

d. imposing higher premium than the standard rate in the table;

e. excluding certain risks from than standard cover; and

f. imposing a lien that reduces the insurer's liability under certain conditions or for certain period.

The terms under which the proposal is finally accepted by the underwriter, are communicated to the proposer. If the acceptance is on the proposed terms and on ordinary rates, the deposit premium, if adequate, is considered First Premium and the risk will commence from that date. If the acceptance is on the modified terms and the proposer agrees with modified terms, the risks commence only after payment of the additional premium. The

First Premium Receipt is the evidence of the commencement of risk, till the policy is issued.

Premium above Rs 50,000 Not to be received in Cash

As per IRDA directives all insurance companies are required to strictly adhere to Anti-money Laundering (AML) guidelines and not to accept premiums worth more than Rs 50,000 in cash. Premium amount more than Rs 50,000 must only be accepted by insurers through banking channels such as cheque, credit card or demand draft or e-payments. As per IRDA directives on AML guidelines, if premium amount from a policyholder exceeds Rs 50,000 in a month, insurance companies are required to examine such receipts from all angles or aspects of AML norms. Such AML guidelines are to adhere to by all insurers for making payment to policyholders' IRDA Circular dated 31 March 2006. In the following recent circular IRDA has allowed payments through electronic payment methods also. As per Circular No.018/ AML-CIR/IRDA/ E-Payments dated 9 July 2009 all payments should be made after due verification of the bona fide beneficiary through Account Payee Cheques in order to ensure audit trail and a control mechanism on all payments in the light of the vulnerability of fund transfers for money laundering purposes. In this circular, IRDA has permitted to make payments to policyholders and beneficiaries through electronic payment methods such as Electronic Clearing Service (ECS), and National Electronic Funds Transfer (NEFT).

No Policy From Future Date

The Supreme Court has ruled that an insurance company cannot issue a policy from a future date without the consent of the insured. The ruling came after an appellant was awarded a compensation of Rs 7.96 lakh for her husband death in an accident under a policy that came into force a day after his death. The Supreme Court passed the ruling setting aside a Delhi High Court judgment.

IRDA Norms for Payment to Policyholders

With a circular to the life insurance companies IRDA has tightened the norms for payment of premium for the protection of policyholders' interest. As per the norms premium paid in the second year should not be less than 75 per cent of the premium paid in the first year. IRDA has mentioned in the circular that where products had provided for more than 25 per cent reduction in subsequent premium, the difference of premium should be treated as a single premium and the commission clawed back and invested in the policyholders' account. IRDA has also decided to penalize if the life insurance policies are not renewed in order to reduce mis-selling of life insurance.

Life Insurance Contractual Provisions and Clauses

Universally life insurance policies or plans are based on certain contractual provisions that are binding on both the parties. Few such provisions are discussed below.

Ownership

The insured, the beneficiary, a trust or another party having insurable interest in other's life can be the owner of a life insurance policy. Under this clause or provisions, the policy-owner possesses all contractual rights in the policy. These rights include changing the beneficiary, surrendering the policy for cash value, taking loans against amount paid for the policy, receiving bonus, electing settlement options. The policy also provides for a change of ownership. The policy owner can also designate a new owner by filling an appropriate form for which insurance company pass necessary endorsement to effect the change in ownership.

Whole Contract

A policy and the attached application constitute the contract as a whole between the parties being the assured and the insurer. All statements in the application are considered to be representations forming part of the insurance application. The policy or the insurance contract will be considered void in case of a misrepresentation provided such misrepresentation is material for the underwriter's decision on acceptance of risk, deciding rate of premium or terms of policy. The insurer cannot change the policy terms unless the policy owner agrees for the change. A policy may provide an entire-contract clause, which prevents the insurer from amending the policy without the consent of the policy owner.

Riders

Riders mean additional benefits. Insurers allow additional benefits by way of riders to the main policy on payment of additional premium. The benefits under the riders are not the same among the insurers. Different underwriters offer different types of riders at different amount of additional premium. Rider of Accident benefit may provide for the payment of the amount more than (say, double) the basic sum assured under the policy on the insured's death by accident. But all riders are subject to payment of additional premium for additional benefit. The rider may be subject to certain specified conditions. For example, Accident benefit is payable only if death occurs within 120 days from injuries caused in the accident. The bodily injury should have resulted directly from the accident.

Suicide Clause

Most of the life insurance policies contain a suicide clause. The suicide clause provides that if the insured commits suicide within certain period of time from the date of issuance of policy, the sum-assured will not be paid and there may be refund of premium or some other term. In certain countries or in certain policies, suicide is excluded for only one year. If the assured commits suicide after expiry of one year, the policy proceeds may be paid just like any other claim provided the clause will provide to that effect. The prospect or the insurance applicant should look into it especially in case of ULIP policy especially, which is nothing, but an investment plan. Generally, burden of proving suicide rests on the insurer. The purpose of suicide clause is to reduce adverse selection of risks as the insurer gets some protection against the individual who wishes to purchase life insurance with an intention of committing suicide and make money for others.

Grace Period

Life insurance policies provide grace period by which the policyholder gets a period of 31 days more to pay premium overdue. In certain types of policies and in certain countries, the grace period may be of longer time, say, 61 days. The policy remains in force during stipulated grace period. If the insured person dies within the stipulated grace period, the overdue premium is deducted from the policy proceeds and the balance is paid to legal heirs. The purpose of the grace period is to prevent the policy from lapsing by giving the policyholder additional time to pay an overdue premium. Thus it provides considerable financial flexibility to him when he is temporarily in short of funds or he forgets to pay premium in time.

Reinstatement Clause

A policy may lapse if premium is not paid within grace period. Sometimes Reinstatement Provision permits the policyholder to reinstate a lapsed policy subject to compliance of certain requirements as under:

- Interest along with overdue premium is repaid or reinstated from the respective due dates;
- The policy must not have been surrendered for its cash value;
- It is reinstated within stipulated time;
- It is beneficial for a policyholder to reinstate a lapsed policy rather than purchase a new policy in view of the following reasons;
- Premium is lower, because the reinstated policy was purchased at lower age;
- Acquisition costs may be incurred for a new policy, which will be finally borne by the policyholders. This can be avoided in case of reinstatement of policy;

- Cash values and dividends are usually higher under reinstated policy; and

- A new policy may not fetch any cash values until the expiry of a specified time.

Suicide clause period may not be applicable to reinstated policy. Statements contained in the application cannot be contested or challenged in case of reinstated policy.

Incontestable Clause

This clause may provide that the insurer cannot challenge the policy or any of the statements in the application after it has been in force for a certain period of time during the insured's lifetime. For example, an insurer cannot repudiate a death claim on the ground of a material misstatement/misrepresentation or concealment in the application for insurance. The purpose of this clause in the policy is to protect the beneficiary if the insurer tries to deny payment on the ground of misrepresentation or concealment in the policy after expiry of certain period. This clause again enables the insurer to avoid policy if he detects fraud in the policy within that period. However, in the following situations an insurer can deny payment of claim even after the contestable period runs out:

- The insurable interest does not exist at any time;

- The applicant for insurance has been replaced by someone else for medical examination; and

- The beneficiary takes out the policy with a motive to murder the insured.

Policy Assignment

A life insurance policy is freely assignable to another party. A life insurance policy is a contract between the assured and the insurer that confers the right to money on the policyholders. It represents rights or an actionable claim as described in the Transfer of Property Act, 1982. A life insurance policy forms part of the estate owned by the policyholder. Like any other property, it can be sold, mortgaged, charged, or gifted under the Transfer of Property Act. When an assignment is made, the rights and the interests of the policyholder or assignor are transferred to the assignee. The transfer of property can be done only by a person who owns the property and is competent to contract. Thus the assignor must be major and must not suffer from any disqualification legally like being convicted of any criminal offence. Assignment of life insurance policy is governed by Section 38 of the Insurance Act, 1938 in the following manners:

- Assignment may be made with or without consideration
- Assignment can be made by an endorsement on the policy itself or by a separate instrument
- Signature of assignor is attested by at least one witness
- Assignment is complete on execution of endorsement or separate instrument
- The insurer has to record the fact of assignment
- Assignment by endorsement does not require stamp duty but assignment by separate instrument has to be done on stamped document.

Assignment is of two types: absolute and conditional. In an absolute assignment, the assignor loses all his rights and title in the policy and the assignee can deal with policy in any manner he likes. He needs not to take the consent from the assignor. In a conditional assignment, the rights, the title and the interests in the policy automatically get reverted to the assignor on the occurrence of the specified conditions without consent of the assignee, such as the assignor survives the date of maturity or that the loan is repaid. In case a policy is assigned in favour of two or more persons, the assignees acquire the interests in the policy, as tenants in common. In other words each assignee acquires an undivided and specific interest. On the death of one tenant, his interest passes to his legal heirs, but not to his co-tenant. In case a policy is taken by a person on the life of another, all rights, title and interests in the policy vest in the proposer.

Nomination

A notice of nomination is served on the insurer to protect the interests of the nominee in case of death of the assured during currency of the policy. Precisely, a nomination gives the nominee only the right to receive the policy money in the event of the death of the life assured. Section 39 of the Insurance Act, 1938 provides rules of nomination, according to which the owner of a policy on his own life at any time during the term of the policy before maturity, nominate the person or persons, to whom the money payable under the policy shall be paid in the event of his death. A person holding policy on the life of another, cannot effect a nomination. An assignee who is not the life assured cannot effect a nomination. The nominee's name is incorporated in the policy document. A prosper for insurance cover for his own life can mention the name, age and the relationship of the person whom he would like to nominate. If nomination is made after the commencement of the policy, a notice of such nomination is required to be served on the insurer so that the insurer can register the same.

If the nomination is done at the time of taking policy, it cannot be made subsequently by endorsement on the policy. An earlier nomination can also be cancelled and a new nomination be done at the will of the policy owner by way of subsequent endorsement. The nominee can give a valid discharge but has to hold the claim on behalf of those entitled to it. When the nominee is a minor and there is no appointee, the claim amount under the policy cannot be paid to the guardian either appointed or natural. It can be paid only to the legal heirs of the deceased life assured. An assignment cancels a nomination. But an assignment made in favour of the insurer, inconsideration for loan granted against the security of the policy, does not cancel the policy. If the nominee dies after the death of the life assured, but before the payment of the death claim, the policy money will become a part of the estate of the life assured and would be paid to his representatives. In case of policies where the maturity amount is payable in installments after the maturity as in case of educational annuity policies and the life assured dies after maturity, the remaining installments will be paid to the nominee, but he does not have the right to continue future installments payable.

Alterations

The policy document provides the specified terms of contract. These terms continue to operate throughout the currency of the policy. However in certain situations, certain terms can be modified by the parties to the contract with their mutual consent. For example, situations may arise where the policyholder may want alterations in the terms of the contract to suit changed circumstances. He may want to reduce the Sum Assured finding it difficult to continue the payment of premium for the original sum-assured. There could be various types of alterations to meet the requirements to the parties to the contract, such as:

- Alteration in plan or term
- Change in the mode of payment of premium
- Alteration in name
- Change of nominee
- Change from the without profit plan to with profit plan or vice versa
- Splinting of policy into more than one, etc.

Alterations are considered if the policy is in force for the full sum assured. Alterations are not allowed in the first year of policy unless it is a case of correction or changes which do not affect the basic insurance contract. While agreeing for alterations, the insurer is to ensure that there is no adverse selection and there is no increase in risk element with same amount of premium. Increase in sum assured, Increase in term, etc., are the cases where risk elements increase. Such type of alterations is not allowed.

Alterations are made by suitable endorsements on the policy itself. Endorsements are passed on payment of requisite fees. A fresh policy is issued if the alterations are of a substantial nature.

Duplicate Policy

In case a policy document is misplaced, lost, damaged or torn, there may be a need of duplicate policy. Such damage, loss or misplacement of policy shall not make the insurer free from liability to pay off policy amount to the policyholders. The insurer can issue duplicate policies on the request of the policyholders in any of the above situations. Before issuing duplicate policy the insurers take all possible precautions to avoid any sort of fraud or mischief, which may be attempted with the duplicate policy. In case the policy is lost by theft, the policy owner needs to file a FIR with the police station and obtain the Final investigation report of the police. The insurer may issue a duplicate policy on obtaining FIR report and an indemnity bond after making proper advertisement. In case the policy document is partially burnt, mutilated or damaged, the remains may be examined for identification and surrender to the insurer for issuance of a duplicate policy without advertisement and indemnity bond. The costs of issuing a duplicate policy including advertisement cost, and stamp duty are borne by the policyholder. The duplicate policy must show “Duplicate” by a rubber stamp or otherwise, though it is as good as original for all practical purposes.

Surrenders

A life insurance policy can be surrendered at any time before it becomes a maturity claim. The amount payable on surrender is called the surrender value or Cash Value. The surrender values may be published in the prospectus or in the policy as conditions. Sometimes surrender value is announced as a matter of legal requirement. The surrender value is announced usually as percentage of the premium paid or a percentage of the paid up value. Such percentage increases as the duration of the policy increases. Again such percentage decreases as the original term of the policy increases. For example, between two policies for the terms of 20 and 30 years, the surrender value on the former will be more than the latter on expiry of a certain period of time.

Surrender values are kept low by insurers, particularly in the early years of a policy due to various reasons such as: i) initial deposits of premium are not fully credited to policyholders' accounts because a large share of the same is spent for acquisition costs; ii) a large share also goes to meet the death claims; iii) to discourage surrender; and iv) to encourage anti-money laundering process.

Loans

Generally, loans are granted up to certain percentage of the surrender value for the policies in force and are subject to payment of interest payable on the loan sanctioned. Such loans may be repaid in full or in part, during the currency of the policy leaving the balance to be adjusted against the amount payable on maturity claims as when arise. The interest on loan is payable generally at half-yearly basis in order to coincide with the due dates of premium and interest for broken period is charged separately. Broken period is the period between the date of loan and the policy anniversary following the date of loan sanctioned. Only the persons having absolute right, title and interest on the policies can avail of the loan facilities. The assured has to assign the policy absolutely to the insurer for getting loan under policy.

Foreclosure

When a loan is granted against a policy, the life assured has a choice to pay off the interest becoming due or allow it to be accumulated and to be adjusted from the maturity moneys payable when the claim arises. This may be possible only when premiums are paid regularly and the policy remains in full force. If there is a default in the payment of premium, the policy status would have to be checked to make sure that the surrender values are adequate to meet the arrears of loans and interest. If the principal loan and the accumulated interest is likely to become more than the surrender value, a case of foreclosure arises. When it is decided to effect foreclosure, the policyholder is advised accordingly and requested to pay the arrears of loan interests. If there is continued default, the policy is foreclosed and surrendered to loans. The balance surrender value, if any, after adjustment of the principal loan and interest due thereupon will be paid to the policyholder. However a foreclosed policy may be reinstated, if desired by the policyholder on compliance of the following conditions:

- Outstanding loan interest with accumulated interest thereon is paid up to date.
- There is satisfactory evidence of continued good health.
- The reinstatement of a foreclosed policy is not allowed if the balance surrender value has been paid to the policyholder to avoid moral hazards.

The foreclosure action is considered complete when the insurer takes decision in this regard. The nomination, if any upon the policy ceases to exist. If the life assured dies before payment of the balance surrender value, the amount is not payable to the nominee, but only to the legal heirs of the deceased assured.

Distribution of Surplus

Distribution of surplus in the form of bonus to the policyholders has to be decided very logically, equitably and simple manner so that the same is understood by the policyholders. The sum asured is increased by the extent of bonus. The equitable principle demands that the policyholders would get bonus equivalent to the contributions made by them to the surplus. There are many critical considerations that influence the decisions of equity distribution of bonus from surplus. Some of the considerations are indicated below:

- The variations in the rates of interests
- Future trends in the rates of interests
- Policies that were subject to lower rates of bonus earlier.
- Higher rates of interest and longer terms contribute more and thus provide the base for higher bonus

Under Simple Reversionary Bonus system, bonus is decided as a uniform percentage addition to the basic sum assured and is payable along with the sum assured on maturity or death claim. Some insurers allow policyholders to take the cash value of the bonus additions. Some allow the bonus to be used to reduce the future premiums.

Under Compound Reversionary Bonus system, the percentage addition applies to the basic sum assured plus the earlier vested bonus additions. For example, basic sum assured is Rs 100,000 and the bonus already declared on it is Rs 2000. This means bonus declared is Rs 50 per thousand. Under Simple Reversionary Bonus system, the bonus payable is Rs 5000. Under Compound Reversionary Bonus system, the bonus payable will be Rs 6000.

Life Insurance Policies and Claims

Policy Claims – Scope

Policy claim means a demand of the insured or the beneficiary of the policy on the insurer for a certain sum of money on the happening of specified events. When such events happen, the insurer has to pay to the policyholder or the beneficiary or the nominee as the case may be, the specified sum of money as per the terms and conditions of the policy. Sale of policy is nothing but making promise. When a claim is settled as per policy condition, the real service is rendered. So the prompt and proper settlement of policy claims is one of the most important functions of an insurance company. The volume or value of yearly policy claims is quite substantial for any insurance company. For example, in 2005-06, LIC disbursed the following amount of policy claims:

Maturity Claims

Number	:	116 Lakhs
Amount	:	Rs 24,737 crores, which is about 40 per cent of renewal premium for the year

Death Claims

Number	:	5 Lakhs
Amount	:	Rs 3,303 crores, which is about 3 per cent of total premium for the year

Above data clearly indicates the volume and significance of financial transactions arising out of insurance claims payments in life insurance business.

Claims may be of the following types:

- **Maturity Claims:** Claims becoming payable on survival up to the end of the policy term, which is the date of maturity.
- **Death Claims:** Claims becoming payable at the event of death of the life assured during the policy term.
- **Survival Benefits:** Benefits becoming payable on survival up to a specified period during the policy term.

Maturity Claims

Such claim includes the Sum Assured and other guaranteed additions, if any, plus accrued bonus payable as per the terms of the policy, if the life assured lives up to the end of the policy term. Any debt or charge on the policy like outstanding loan or premium is deducted from the gross maturity amount payable. Settlement of maturity claims is comparatively easier and free from complications or hazards compared to other claims as such claims are paid to the policyholders only. Insurer sends discharge form well in advance and initiates action for settlement of maturity claim so that the policyholder receives the claim cheque on the date of maturity. The policyholders return the discharge voucher duly stamped, signed and witnessed along with the following documents:

- policy document for cancellation
- proof of age, if required

- document of assignment, if assignment is executed on a separate paper

The discharge voucher will mention both gross amount, necessary deductions and net amount payable clearly. The gross amount normally consists of the basic sum assured or paid up value, the vested bonus, interim bonus payable, any deposit lying in the policy account and return of excess premium, if any. The deductions to be made from maturity claims, generally include loan amount, outstanding interest thereon, unpaid premium, if any, and other charges.

However difficulties arise if the policyholder dies after the date of the maturity and before the payment of the maturity proceeds. In such case the maturity claim amount is included with the estate of the deceased policyholder. The claim amount is then payable to the legal heirs of the policyholder. The settlement is made on the basis of indemnity bond or a declaration of title from an appropriate judicial authority.

- The nomination aspect is not taken into account. But the assignment aspect is considered for settlement of maturity claims. In case the policy is absolutely assigned, then the settlement is made in favour of the absolute assignee.

- If at the time of claim, the original policy document is not found, the insurer may settle the maturity claims on the basis of an indemnity bond without following the procedures of issuance of duplicate policy unless the circumstances warrant the same.

Death Claims

Death Claims are comparatively less in number and amount. Death claims are of two types: i) Early or Premature Claims; and ii) Non-Early Claims. Claims arising within two years from the date of commencement or revival of or reinstatement of insurance are called early claims and claims arising more than two years from the date of commencement or revival of or reinstatement are called

Non-early claims. The death of the life assured has to be intimated in writing to the insurer by the nominee, assignee, a relative, the employer, the agent along with the policy particulars, name of the life assured, the date of death and its cause, relationship of the informant with the deceased life assured. The insurer shall be satisfied with the genialness of the claim intimation and call for the following documents normally:

- Policy document along with the assignment deed
- Declaration from the claimant giving the details of cause of death, nature of last illness, treatment, and creation along with necessary document
- Death certificate issued by the municipality or any other competent authority
- Proof of title of claim

When the policy exists for more than 3 years and the proof of claim is clear, the discharge voucher is issued along with request for compliance of certain requirements. In case of valid nomination or assignment, the settlement of death claim becomes easier because in such situation further proof is required. In case there is no valid nomination or assignment, the claimant will have to produce satisfactory evidence of the title to the estate of the deceased life-assured. Such evidences may be succession of certificate, probate of a Will. However the insurer may waive evidence of title in the following cases and settle the claim on the strength of an indemnity bond in order to enable the claimant to overcome his financial crisis:

- No dispute among the heirs or relatives of the deceased as regards policy moneys
- No situation requiring an evidence of title on any will, estate or insurance policy
- The amount payable under all polices is not very large

Depending upon the common law, local custom or the religion of the deceased and the amount payable, a claim may be settled to natural heirs on the basis of a joint discharge. For example, as far as Hindus, Sikhs or Jains are concerned the widow, mother, sons and daughters and sons and daughters of predeceased daughters constitute the natural heirs. If any of the aforesaid heirs is a minor, the natural guardian (father or mother) will have to sign the indemnity bond and discharge voucher on behalf of the minor. However in case of very small amount payable, the indemnity bond may be waived. In case of early Claims, the insurer becomes extra-cautious so that fraudulent payment is avoided and the interests of the particular community of policyholders are well protected. In such case generally the following requirements are adopted:

- Statement from the medical professional attending the last illness with details on previous history and treatment thereof.
- Statement from the hospital in case of hospital treatment extended to the deceased life-assured.
- If the death was caused by some unnatural causes, certified copies of post-mortem report, the police inquest report, panchnama report, and magistrate report.
- Details or certificate of cremation-time, place, witness etc.
- Statement from the employer, if any about leave, cause of sickness etc.

However the insurer can repudiate or deny the claim on the ground of misrepresentation or concealment of material facts irrespective their importance on underwriting. In certain countries the court of law does not allow the insurers to repudiate deny insurance claim unless it is established that such misrepresentation was intentional to secure some undue advantage.

22

LIFE INSURANCE PRODUCT MANUAL

Genesis of Life Insurance Introduction

Life insurance products are usually considered as “plans” of insurance. These plans have two basic elements of cover: “Death Cover” or “Risk Cover”. Death Cover provides for “specified benefit” payable on the death of the insured person within specified period, while Risk Cover provides for “Survival Benefit” being the amount paid on his survival of a specified. There are several life insurance products or plans. These plans are broadly classified into following groups: i) Term Insurance; ii) Whole Life Policy; iii) Endowment Policy; iv) Money Back Policy; v) Joint Life Policy; vi) Group Insurance Policy; vii) ULIP/Unit-Linked Insurance Plan/Policy; viii) Pensions Plans or Annuities; ix) Children Policies; and x) Women Policies.

Term Insurance

Insurance Plans providing only death cover are called Term Insurance. If the insured does not die within the specified period, no payment is made under term insurance. Term insurance provides protection for a specified period of time. This period could be as short as one year only or as long as 5, 10, and 20 years or for a specified age, which could be as high as 80 depending upon the profile of the life assured. Policies are issued with various guarantees of payments. The longer the guarantee, the higher is the initial premium. If the insured person dies during the policy term/period, the company will pay the face value of the policy to his beneficiary. If he lives beyond the policy term he had selected, no benefit is payable to him. As a rule, term policies offer a death benefit with no savings element or cash value. Precisely, a term insurance is a life insurance that provides coverage at a fixed rate of payments for a fixed period of time being the relevant term. If the insured dies during the term, the death benefit will be paid to the beneficiary. Term life insurance is the original form of life insurance. Following are the following special features for term insurance:

1. Premiums are locked in for the specified period of time under the policy terms. Premiums payable for term insurance are lower at the earlier ages as compared with the premiums payable on whole-life or permanent insurance.

2. Term rates of premium rise as the insured persons grow older.

3. Term plans may be "convertible" to a permanent plan of insurance.

4. The coverage may be of 'fixed level' providing the same benefit until the policy expires.

5. The insured person may have "decreasing" coverage during the term period with the premiums remaining the same.

6. Traditionally, insurers do not have right to change premiums after the policy is sold. Since such policies may continue for many years, insurers must use conservative mortality, interest and expense rate estimates in the premium calculation.

7. Adjustable premium insurance, however, allows insurers to offer insurance at lower "current" premiums based upon less conservative assumptions with the right to change these premiums in the future. The premium, however, can never be more than the maximum guaranteed premiums stated in the policy.

If the insured person does not pay the premium for his term insurance policy, such will generally lapse without cash value, as compared to a permanent type of policy that has a cash value component. Currently, term insurance rates are very competitive. Term insurance is the least expensive pure life insurance coverage available. This is purely risk protection. Term insurance functions in a manner similar to non-life insurance plans life Motor Insurance or Householder Insurance that satisfies and pays for claims against what is insured if the premiums are up to date and the contract has not expired, but there is no return of Premium paid.

Common form of term insurance is Annual Renewable Term. In this form, the premium is paid initially for one year of coverage, and then the policy is continued for a given period of years on the same terms. This period varies from 10 to 30 years, or occasionally until the age of 95. As the insured ages, the premiums increase with each renewal period. In this form the premium is slightly higher than for a single year's coverage, but the chances of the benefit being paid are much higher. Another form of annual renewable term insurance is guaranteed Level Premium Term Life Insurance, where the premium is guaranteed to be the same for a given period of years. The most common terms are 10, 15, 20, and 30 years as the case may be. In this form, the premium paid for each year remains the same for the duration of the contract. This cost is based on the summed cost of each year's annual renewable term rates, with a time value of money adjustment made by the insurer. Thus, the longer the term, the higher is the annual premium, because, more expensive risks being older to insure years are averaged into the premium. Most level term forms of insurance include a renewal option and allow the insured to renew for a maximum guaranteed rate if the insured period needs to be extended.

Types of Term Insurance

There are various types of Term Insurance such as Pure Term Insurance, Renewable Term, and Convertible Term, Level or Decreasing Term.

Pure Term Insurance: Only one risk i.e. death is covered under this plan. As explained earlier, term insurance provides temporary protection for a specified number of years. It is usually renewable and convertible. Under this plan, the sum-insured is payable on the death of the insured during the specified period.

Renewable Term Plans: It gives the insured the right to renew for another period when a term ends, regardless of the state of his health. With every renewal premium is generally increased on the basis of actuarial analysis. Policy is renewed by one for suitable term and options so as to meet one's specific needs and circumstances including one's health, age and financial capacity as otherwise renewal may be costly or leave one's beneficiary without coverage at the real need or contingency.

Convertible Term Policies: This often permits the life assured to exchange the policy for a permanent plan. One exercises this option during the conversion period. The length of the conversion period may vary depending on the type of term policy originally purchased. If the insured converts within the prescribed period, he is not required to give any information about his health, age or other particulars. The premium rate he pays on conversion is usually based on his 'current attained age, on the conversion date. This type of policy often provides the maximum protection with the smallest amount of cash outlay.

Level or Decreasing Term: Under a level term policy the face value or the sum assured of the policy remains the same for the entire period. With decreasing term the face amount reduces over the period and the premium remains the same each year. Generally, such type of term policies are purchased as mortgage protection with the amount of insurance cover decreasing as the balance of the mortgage decreases. If the insured dies the proceeds of the policy can be used to pay off the mortgage.

Term Policy - An Example

- **Policy Name:** A Simple Term Policy from Fortune Insurance Company
- **Policy Term:** 3 years
- **Sum Assured:** Rs 10,000
- **Premium:** Rs 100 per year to be paid for three years

- **Benefit:** The insured's beneficiary will get Rs 10,000 at the event of death of the insured during the period of 3 years. Nothing is payable at the maturity on survival.

- **Entry:** Minimum age at entry is 18 years while Maximum Age- is 44 years.

- **Lapsation:** If premium is not paid within the grace period of 30 days, the policy will lapse.

- **Exclusion:** No claim will be paid on death, if the life insured person commits suicide within 12 months from the date of issue of this policy or the date of any reinstatement of the policy.

- **15 Day Lock Period:** The policyholder may cancel this policy by returning it to the insurer within 15 days of receiving it together with a letter requesting for cancellation of the policy. The company will refund the premium paid by the policyholder less a deduction of: i) proportionate premium for the time cover provided up to cancellation; and ii) expenses incurred by the company for medical examination of the insured person and stamp charges etc.

Limitations of Pure Term Insurance and Whole Life insurance

Term Insurance both Pure Term Insurance Plans and Whole Life Insurance Plans as discussed below are subject to certain inherent limitations. In view of such limitations of pure term policies or whole life policies, it is always prudent for all to buy term insurance and invest the difference in the dividend earning stocks in stead of purchasing one Pure Term Insurance or Whole Life Policy or Permanent Life Insurance policy with minimum return for the beneficiaries. If one is prudent with the money one has today and wants to get rid of his home loan, car loan and credit card debt and to put money into retirement plans, one need not go for permanent insurance or whole life or for 30 years Term Insurance plans from now for whole amount to protect one's family when one will die.

Pure Term Insurance plans and Permanent Life insurance Plans can be further analyzed comparatively in terms of purpose and price of the respective plans. Term life insurance is a pure death benefit; its primary use is to provide his dependents financial coverage for financial responsibilities of the insured for repayment of his debt for durables/housing loan, children higher education and even for funeral cost where it is very substantial. Term life insurance is generally chosen in favor of permanent life insurance because it is usually less expensive (depending on the length of the term). Many financial experts generally recommend for pure term life insurance in place of permanent life insurance, as a means to cover potential expenses until such time that there are sufficient funds available from savings to protect those whom the insurance coverage is intended to protect. For example, an individual may choose to obtain a policy for the term that will expire at the point of his retirement age based on his prudential analysis that on his retirement, he would have amassed sufficient funds with retirement benefits and savings to protect his dependents and discharge his financial liabilities.

Whole Life Insurance

Basics of Whole Life Policy

While term insurance is designed to provide protection for a specified time period, permanent insurance is designed to provide coverage for entire lifetime of the insured. To keep the premium rate level, the premium at the younger ages exceeds the actual cost of protection. This extra premium builds up a reserve element (cash value) which helps pay for the policy in later years as the cost of protection increases beyond the premium amount. Whole life policies spread the cost of insurance cover over a longer period of time in order to level out the increasing cost of insurance in the older stage of life. In some form of policies, premiums are required to be paid for a set number of years while in others, premiums are paid throughout the lifetime of the insured. The insurance company invests the excess premium in securities and adjusts the investment income against the increasing cost of insurance in the older stage of life.

There is a whole life policy called cash value life insurance. This type of whole life policy generates return of savings element. Cash values are typical to a permanent life insurance policy. The size of cash value build-up in such whole life policy differs from company to company according to their fund management ability. Sometimes correlation between the size of the cash value and the premiums paid cannot be even statistically established. It is the cash value of the policy that can be accessed while the policyholder is alive. Common features of Whole-life Policy are:

- Premium is payable each year.
- Death benefits are payable to the beneficiary.
- Policyholder would receive Cash surrender value if policy is surrendered prior to death.
- Policyholder may take a loan against the cash value of the policy at a specified rate of interest.
- Such outstanding loans, if not repaid, will be adjusted against the death benefit.
- Many permanent policies will contain provisions, which specify these tax requirements.
- There are two basic forms of Whole life insurance — Traditional Whole Life and Interest-sensitive Whole Life.
- Traditional Whole Life policies are based upon long-term estimates of mortality, cost of protection, expense, interest.
- The premiums, death benefits and cash values are stated in the policy.

- There are different versions of traditional permanent insurance such as Non-Participating Whole Life, Participating Whole Life, Econometric Whole Life, Limited Payment Whole Life, Single Premium Whole Life etc.

- Interest Sensitive Whole Life Insurances which allocate investment earnings differently from traditional whole life reflect current fluctuations in interest rates periodically.

- There may be different forms of Interest Sensitive Whole Life Insurances such as Universal Life, Excess Interest Whole Life, Current Assumption Whole Life, Single Premium Whole Life etc.

Non-Participating Whole Life

All values related to the policy (death benefits, cash surrender values, premiums) are usually determined at time of policy issue, for the life of the contract, and usually are altered after issue. During underwriting of risk the insurance company considers all risk of future performance versus the actuaries' estimates. If future claims are underestimated, the insurance company makes up the difference with underwriting loss. On the other hand, if the actuaries' estimates on future death claims are high, the insurance company will retain the difference as underwriting profit. The disadvantage is that it pays no dividends.

Participating Whole Life

In a participating policy also known as a with-profits policy in the insurance company shares the excess profits also called dividends or bonus with the policyholder. Typically these dividends or bonus are not taxable because they are considered an overcharge of premium due to wrong underwriting of loss. The dividends represent the favorable mortality, good claim experience and sound investment income of the company. Dividends can be paid in cash or used to reduce premiums or left to accumulate at interest or used to purchase paid-up additional insurance. But dividends are not guaranteed.

Indeterminate Premium Plan Whole Life

It is similar to non-participating, except that the premium may vary year to year. It provides for adjustable premiums. However, the premium will never exceed the maximum premium guaranteed in the policy. The company will charge a “current” premium based on its current estimate of investment earnings, mortality, and expense costs. If these estimates change in later years, the company will adjust the premium accordingly but never beyond the maximum guaranteed premium stated in the policy.

Economic Plan Whole Life

It is a blending of participating whole life and term insurance, wherein a part of the dividends is used to purchase additional term insurance to provide a higher death benefit, at a cost to long term cash value. If in some policy years the dividends are below projected investment earnings, the death benefits get reduced in those years. Eventually, the dividend additions should, at least equal the original amount of supplemental coverage as otherwise it is possible that at some future time there could be a substantial decrease in the amount of supplemental insurance coverage if dividends are not sufficient to purchase enough paid up additions at a future date. Thus an economic whole life policy provides for a basic amount of participating whole life insurance with an additional supplemental coverage provided through the use of dividends.

Limited Pay Whole Life

If the insured wants to pay premiums for a limited time cover the limited payment whole life policy gives him lifetime protection. It requires only a limited number of premium payments. Because the premiums are paid over a shorter span of time, premium payments will be higher than that under other whole life plans. It is similar to a participating policy, but instead of paying annual premiums for life, they are paid for a certain number of years. The policy may also be set up to be fully paid up at a certain age, such as 65 or 70. The policy itself continues for the life of the insured. With this plan the insurance company builds up sufficient cash value within the policy during the payment years to fund the policy for the remaining part of the insured's life.

Single Premium Whole Life

Single premium whole life is one kind of limited pay whole life plan where only one large premium payment is made. The policy is fully paid up and no further premiums are required to be made. Such policies generally provide substantial surrender charges if you want to cash in the policy during the first few years. Since a substantial payment is involved, it should be viewed as an investment-oriented product. Interest in single premium life insurance generally arises from the tax-deferred treatment of its cash-values build-up. Taxes will be incurred on the gain, however, when the insured surrenders this policy. He may borrow on the cash value of the policy, but he may incur a substantial tax bill when he surrenders, even if he has borrowed out all the cash value.

Interest Sensitive Whole Life Policy

On traditional whole life plans Insurers guarantee stated future benefits based on long-term estimation of future earnings and overall company experience, but on interest sensitive whole life, they allocate investment earnings differently in view of current fluctuations in interest rates. The advantage is that improvements in interest rates will be reflected more quickly in interest sensitive insurance than in traditional; the disadvantage, of course, is that decreases in interest rates will also be considered effectively in the interest sensitive whole life plans. There are four basic interest sensitive whole life policies: Universal Life, Excess Interest Whole Life, Current Assumption Whole Life, and Single Premium Whole Life.

The Universal Life Policy

The universal life policy is designed to reflect the insurer's current mortality and expense as well as interest earnings rather than past rates. Universal life Insurance consists of three basic elements of the policy: premium, death benefit and cash value. The insurance company credits premium collections to the Cash Value Account of the policyholder. Periodically the company deducts its expenses and the cost of insurance protection from the Cash Value Account. Cost of insurance is usually determined and described as the mortality deduction charge. The balance of the cash value account accumulates with the interest credited. The company guarantees a minimum interest rate and considers a maximum mortality charge. Some universal life policies also specify a maximum basis/amount for the expense charge. When interest rates are high, benefit projections (such as cash value) are also high. Some universal life plans allows the policyholders to change or skip premium payments or change the death benefit more easily than with any other policy. The policy usually gives the policyholders an option to select one or two types of death benefits. Under one option, beneficiaries receive only the face amount of the policy. Under the other, they receive both the face amount and the cash value account. If a universal life policy is surrendered, policyholder may receive less than the cash value account because of deduction of surrender charges.

Excess Interest Whole Life

All of the flexible features of Universal Life are not available in this policy called excess interest whole life. The key feature is that premium payments are required when due just like traditional whole life. Premiums are paid when due not to make the policy lapse. With the premium level fixed, any additional or excess interest credited, or better life insurance experience, will improve the cash value of the policy. The premium level will probably be comparable to traditional whole life policies. Cash value may be also used to pay future premium payments. This type of product maximizes the deferred tax growth of your cash value.

Current Assumption Whole Life

Current assumption whole life is similar to a universal life policy only with exception that insurance company determines the amount of premium to be paid. The company sets the initial premium based upon its current estimate of future investment incomes and mortality experience and retains the right to review its original estimates with reference to actual performance or experience to increase or decrease the amount of premium payments later. In some cases to avoid subsequent increase in premium payments, the face value of coverage may be reduced so that you can continue to pay the original premium. Current mortality and experience and investment earnings can be credited to the insurance policy either through the cash value account and/or the premium or dividend structure. This type of policy has the following features:

- The premiums are subject to change based on the experience (mortality, expenses, investment) of the company.
- The policyholder does not exercise control over the changes.
- The policyholder can use the cash value to make loans just as he/she would with any traditional ordinary life insurance policy.
- A minimum amount of cash value is guaranteed.
- The death benefit does not fluctuate.

Endowment Policy

Unlike whole life, an endowment life insurance policy is designed primarily to provide a living benefit and secondarily to provide life insurance protection. Therefore, it is more of an investment than a whole life or traditional term insurance. Endowment life insurance pays the face value of the policy either at the insured's death or at a certain age after a number of years of premium payment. Endowment life insurance is a method of accumulating savings and capital for a specific purpose and for protecting a particular savings program against the saver's premature death. Many investors use endowment life insurance to fund anticipated financial needs, such as children's higher education or retirement. Premium for an endowment life policy is much higher than those for a whole life policy. Endowment policies cover the risk for a specified period at the end of which the sum assured is paid back to the policyholder along with all bonus/ dividends accumulated during the term of the policy. This is the major benefit of an endowment policy over a whole life one. An endowment policy is thus a life insurance contract designed to pay a lump sum amount after a specified term either on its maturity or on earlier death of the insured person. Terms are generally for 10, 20, or 30 years or up to a certain age limit of the insured persons. Some policies also pay out in the case of critical illness depending upon the policy conditions. These policies are typically traditional with profits or unit-linked funds. Endowment policies can be surrendered for the surrender value which is determined by the insurance company depending on how long the policy has been continued and how much has been paid into it.

A Term Insurance plan with a pure endowment plan of the double the value is called a Double Endowment Policy under which the amount payable on survival is double the amount payable on death. Another Endowment Policy also known as Money Back Policy or Anticipated Endowment Policy under which is 20 per cent of sum assured is paid on survival of 5 years and 40 per cent on survival of 20 years and full sum insured on death any time within 20 years. There are various types of endowment plans such as: i) Endowment plans with Fixed Guaranteed Returns; ii) Traditional Endowment with profits; iii) Unit-linked Endowment; iv) Full endowment; v) Traded Endowment; and vi) Modified Endowment.

Endowment Plans with Fixed Guaranteed Returns

It offers fixed returns that vary from insurers to insurers considering factors including interest rate movements, asset allocation and reinvestment risks. The insurers also consider lot many factors depending upon economic scenarios for arriving at the exact returns ensuring their viability. These endowments plans largely invest in debentures, corporate bonds.

Traditional With Profits Endowments

Under such Endowment Plans the sum assured guaranteed to be paid is increased on the basis of investment performance through the addition annual bonuses. Regular bonuses are guaranteed at maturity and a further non-guaranteed bonus may be paid at the end known as a terminal bonus. During adverse capital market or money market conditions, the encashment value, i.e. surrender value may get reduced.

Unit-linked Endowment Plans

Unit-linked endowments are investments where the premium is invested in units of an insurance fund. Units are encashed to cover the cost of the life assurance. Policyholders can often choose which funds their premiums are invested in and in what proportion. Unit prices are published on a regular basis and the encashment value of the policy is the current value of the units. This is the simplest definition.

Full Endowment Plans

A full endowment is a with-profits endowment where the basic sum assured is equal to the death benefit at start of policy and, assuming growth the final payout would be much higher than the sum assured.

Low Cost Endowment

A low cost endowment is a combination of an endowment where an estimated future growth rate will meet a target amount and a decreasing life insurance element to ensure that the target amount will be paid out as a minimum if death occurs. The cost endowment is designed to pay off interest only mortgage at maturity or earlier death in favour of full endowment with the required premium would be much higher.

Pure Endowment

Life insurance policy under which its face value is payable only if the insured survives to the end of the stated endowment period; no benefit is paid if the insured dies during the endowment period. It is an assurance policy that promises to pay an agreed amount if the policyholder is alive on a specified future date. If the policyholder dies before the specified date no payment is made and the premium payments cease.

Group Insurance

Group insurance is an insurance plan that covers a group of people, who may be the members of societies, employees of an organization or professionals in a common group. Group insurance provided to members of a formal group such as employees of a firm or members of an association is distinguished from individual insurance in which single policies are sold to one person at a time. The concept of group insurance probably originated in ancient Rome with the Roman burial societies. Group (term) Insurance Scheme is meant to provide life insurance protection to groups of people. Administration of the scheme is on group basis and cost is low. Under Group (Term) Insurance Scheme, life insurance cover is allowed to all the members of a group subject to some simple insurability conditions without insisting upon any medical evidence. Scheme offers covers only on death and there is no maturity value at the end of the term. Group (Term) Insurance Scheme is usually offered under One Year Renewable Group term assurance plan.

Every year on Annual Renewal date the insurer charges the premium depending upon the changes in size and age distribution of the age group. Group Term Insurance has a number of varieties or schemes. The Scheme may provide for a uniform cover to all members of the group or graded covers for different categories of members, cover for all amounts of outstanding housing loans or vehicle advances, or some other benefits (e.g., life cover to supplement pension or PF benefits in case of death). The schemes may have add-ons or rider like Double Accident Benefit, Critical Illness Benefit, Disability benefit etc.

Gratuity Insurance Plan

Gratuity is a statutory benefit governed by Payments of Gratuity Act, 1972. Under the Act, it is employer's statutory liability to pay 15 days salary (15/26 of a month's wages, taking the last drawn salary as the basis) for every completed year service to each of his employees on their exit, for any reason after 5 years of continuous service, subject to the specified maximum limit. The employee is eligible for 15 days of pay for each completed year of service on any of the following situations:

- Retirement
- Permanent Total Disablement during service
- Death During Service
- Resignation from service

The employer may also devise a gratuity benefit being higher than what is stipulated in the statutory requirements. Gratuity Liability tends to increase with time as the salary and the tenure of the employees increase. An employer can pay out the gratuity proceeds from his current revenue income (on PAYGO basis) but this can cause financial strain for him sometimes. Thus, a prudent and tax-saving way of meeting Gratuity Liability is to ascertain such liability, set up by a Gratuity Fund and meet liability from the fund as and when required.

Life insurance companies offer Gratuity Insurance Plan to the employers as a Deposit Administration type of Gratuity liability. The contribution made by the employer will continue to accumulate and at the end of the financial year the income or interest earned on his contribution will be credited to his gratuity plan account. The rate of interest will have two components: a guaranteed part and a non-guaranteed part. The non-guaranteed part would apply only to withdrawals taking place in that year and is not guaranteed for the subsequent years. The guaranteed part once allotted is guaranteed. With this insurance plan the employer builds a Gratuity Fund systematically, benefiting from investments returns, which are safe and stable and thus provide the benefits in a cost effective manner. The contributions made towards the Gratuity Liability will depend on "actuarial valuation." The Gratuity Liability and contribution can be estimated on an actuarial valuation provided by a qualified actuary based on Accounting Standard (AS) 15.

ULIP and Its Basics

Unit Linked Insurance Plans (ULIPs) are insurance plans similar to mutual funds and have been sold by life insurance companies over a decade in India. ULIP is a genetic term used to describe insurance plans, where the choice for financial asset lies with the investors. The structure is similar to that of a mutual fund. ULIP premium is allocated to any of the funds being Equity, Income, or Balanced Funds depending on the choices of customers and the gains in the value of these assets are reflected in the Net Asset Value (NAV) of the units. Charges towards insurance and asset management are recovered from policyholders. At present, most of the life insurance companies focus on sale of ULIP.

Life Insurance Companies and ULIP

At present, most of the life insurance companies collect on an average 70 per cent new premium from ULIPs. Again 60 to 80 per cent of amount collected from sale of ULIPs are deployed in the stock market depending upon the risk profile of plans. For example, LIC had 85 per cent of its first year premium collection from ULIPs in 2007-08. Going by industry estimates, over 190 ULIPs have been launched in the market to attract retail investors. About 70 per cent of the schemes which are old schemes being carried fore more than 10 years have been redesigned in 2009-10 to meet the prescribed requirements of IRDA. Up to 2008-09, the ULIP products were being sold in the market as long-term investment products.

Salient Features of ULIP Schemes

1. ULIPs are issued for various 5 years to 20 years, with options or flexibility in payment of premium for various periods 3 years, 5 years, 10 years, or 20 years, etc.

2. Every scheme provides maximum sum assured, minimum premium, maximum policy term, premium paying term, minimum and maximum maturity age etc.

3. The ULIP schemes enhance the value of savings over a period of time and offer options to the customers to choose the investment plans according to their Risks appetite and investment horizons at various points during the life of the policy.

4. There are different modes available for payment of premium: Single Premium, Yearly premium, Half-yearly or Monthly Premium as per terms of the scheme.

5. Investors may choose investment option from a wide range of funds or options ranging from pure debt fund to various combinations of debt and equity funds depending upon the investors' risks appetite.

6. There are various Funds Investment Options such as Secured Funds, Balanced Funds, and Growth Funds. According to options exercised by the investors, the insurance companies make the asset allocations to Equity, Debt and Cash Securities. In the Secured Fund option, the maximum allocated to Debt Security and no investment in Equity. While in Balanced funds options, assets are allocated to Equity and Debt almost equally, in option for Growth Funds, maximum is allocated to Equity.

7. Sometimes, the policyholders are allowed to make switch over from one fund to another fund during the policy period with or without fees depending upon the policy term.

8. Plans provide investors to take advantage of market volatilities through systematic investment plans in equity.

9. Some plans allow partial withdrawal to provide liquidity to the investors within the fixed tenure of investment.

10. With wide array of funds, riders and options, most of the ULIPs provide the policyholders with the freedom to fulfill both investment needs and insurance needs. ULIPs provide twin benefits market linked returns and insurance cover.

11. Every ULIP scheme is subject to various fund options, which the policyholders choose based on their risk appetite. Accordingly the investible, premium is invested in the market through the fund options exercised.

12. Benefits under ULIPs are generally Maturity Benefits, Death Benefits, and Rider Benefits. Maturity Benefit arises when fund value is paid on completion of policy term. Death Benefit is generally higher of the fund value or sum assured (net of partial withdrawals).

13. Rider Benefits depend on the terms of the plans. Critical Illness Care Rider, Accidental Death Benefit Rider, Premium Payer Waiver Benefit Rider, Income Sustainer Rider, etc.

14. Critical Illness Care Rider may provide for payment of lump sum amount to take care of certain specified critical diseases.

15. Accidental Death benefit Rider provides for payment of accidental death benefit if the death occurs as a result of an accident.

16. Under Premium Payer Waiver Benefit Rider, in the event of death of the proposer, the cover for the Life Assured under the base policy continues and the future premiums under the base policy, payable during rider term will be paid by the insurer.

17. Income Sustainer Rider provides for additional benefit in the case of total and permanent disability due to Accident or Sickness, on a certain scale or percentage of income for certain period or till the end of the base policy with or without cap of maximum period as specified in the plan.

18. After deducting the applicable charges the premium collected as per the terms of the policy is allocated to the unit account. The unit value is subject to various changes and value of units may increase or decrease depending the on the NAV. Periodically, the insurance company notifies the policyholder about his unit account summary.

19. Method of Calculation of Net Asset Value: The following methods are commonly followed for the purpose:

- The unit price of a fund is determined by dividing the value of assets in the funds at the time of valuation (at the end of the day) by the number of units.

- For new business, units will be allocated depending on the price of the units using the closing NAV on the day of cheque realization or policy issuance date, whichever is later.

- NAV of each of the funds is computed at the end of the day (daily basis).

- NAV is calculated on 'appropriation basis' or 'expropriation basis' depending on whether the company is purchasing or selling the assets in order to meet the day to day transactions of Unit allocations.

- NAV on Appropriation basis is equivalent to Market/Fair value of the funds' investments + Expenses Incurred in the purchase of the assets + Value of any Current Assets + Any Accrued Income – the value of any current assets divided by number of existing units at the valuation date (before any new units are allocated).

- NAV on Expropriation basis is equivalent to Market/Fair value of the funds' investments — Expenses Incurred in the sale of the assets + Value of any Current Assets + Any Accrued Income –- the value of any current assets divided by number of existing units at the valuation date (before any units are redeemed).

20. Charges for ULIPs and Regulatory Directives: As per IRDA circular dated 22nd July 2009, the charges for ULIPs as filed under "File and Use Guidelines" shall not be modified or changed without obtaining the approval of the IRDA. ULIPs prescribe certain charges which are deducted either from the contributions or from the fund. In 2005, the IRDA had, in its circular dated 21st December 2005 defined various charges which could be levied on the management of the funds under ULIPs.

21. As per IRDA Circular No. 20/IRDA/Act/ ULIP/09-10 dated 22nd July 2009 at the time of maturity, the insurer must issue the policyholders a certificate showing year-wise contributions, charges deducted, fund value and final payment made to the policyholder taking into account partial withdrawals, if any. This certificate shall also show the actual gross yield and net yield taking into account actual charges deducted.

22. A few ULIP schemes are referred here as matter of illustrations:

    - **Canara HSBC Unit Linked Whole Life Plan –** An investment linked plan which gives investment return as well as life cover up to 99 years

    - **Sahara Ankur Plan –** A Flexible Unit Linked Investment according to investors' needs and risk profile

    - **Max New York Life Unit Builder Plus –** A limited pay ULIP which gives guaranteed returns and also an annual income plan (after certain period)

    - **LIC Jeevan Astha Scheme**

    - **LIC Wealth Plus** – an ULIP that guarantees returns equal to the highest NAV

    - **LIC Profit Plus Plan** – A unit linked endowment plan

ULIPs and Life Insurance Cover

Life Insurance business is booming up as per the latest data published by IRDA. The total first-year premium collected by the life insurance sector has shown a 15 per cent growth for the period from February 2009 to January 2010 as against a meager growth of 3.5 per cent for the corresponding period in 2008-09. The said robust growth apparent indicates that more and more people are purchasing insurance products in the country to protect their safety and security in future and this sector has not been affected by the global financial crisis. But an in-depth analysis may suggest something otherwise, which can be outlined following points:

- Though the first premium is on the substantial rise, the life cover sum-assured per policy has been extremely reduced.
- People have reduced purchase of life cover, but are buying more and more ULIPs.
- As per IRDA data published (the Economics Times 9 April 2010), the first premium collected on ULIPs stood at Rs 15,838 crore through about 41 lakh policies, while the term insurance plans brought premium collection of Rs 2,063 crore through the sale of about 6 lakh policies for a particular period.
- ULIPs are being sold in much higher scales aggravating the problem of under-insurance and financial security of the common mass in the society and purpose of purpose of insurance.
- For the Quarter ended December 2009 the total amount of life cover by about of 38 lakh ULIPs sold, was just Rs 22.5 crore resulting into average life cover of Rs 59 per policy. With life insurance cover like these, we should think whether ULIPs are really proper insurance cover or just a cover up aggravating the problem of under insurance.
- ULIP sales depend on stock market scenario. Keeping in view of the volatility of Stock Market the investors should decide for purchase of ULIP because the investment risks in this policy are borne by the policyholders.
- LIC planned for mopping up Rs 18,000 crores from new ULIP plan, Wealth Plus cashing on the demand for Tax-savings options ahead.

ULIPS vs. Mutual Fund Investments

The ULIPS are as good as Mutual Fund Investments with the features or differences among the two investment plans being MFs and ULIPs as shown in Table-47.

Table-47: ULIPs and Mutual Fund Investments

Features	Mutual Fundss	ULIPS
Asset Class	Equity MFs have high Exposure in the stock market	ULIPs give moderate Exposure in the stock market
Investment Decision	Very aggressive with focus on high return	Aggressive with focus on stability of returns
Maturity	Tax savers come with a 3 year lock-in period. Others don't have lock-in period	ULIPs come with 5-20 year maturity Money locked in till maturity
Tax Benefit	Only present in tax-saves scheme	80C benefits for all ULIP investments
Returns	Returns are tax-free	Returns are tax-free
Charges	No entry load, Commission as decided by investors	ULIPs have high entry load. Commission 30-40 per cent.

Turf War between IRDA and SEBI over the Regulation of ULIPS

Though investments in ULIPs are largely similar to investments in mutual funds, ULIP issue is not subject to approval of the SEBI, the capital market watchdog. The insurance watchdog, IRDA, which regulates ULIPs has been telling investors that their investments in ULIPs offered by various insurance companies are safe and secure. But now the insurance companies have been hit hard by a turf or territory war between SEBI and IRDA over the regulation and administration of ULIPs, one of the hottest products in today's bull run, when SEBI first issued a Show-Cause Notice to 14 insurance companies in January 2010 to explain why they have not taken SEBI's approval before selling ULIPs and then issued order on 9 April 2010 banning 14 life insurance companies from selling ULIPs. These 14 life insurance companies include Ageon Religare Life, Aviva Life, Bajaj Allianz Life, Bharati AXA Life, Birla Sun Life, HDFC Standard Life, ICICI Prudential Life, ING Vyasa Life, Kotak Mahindra, Old Mutual Life, Max New York Life Metlife India, Reliance Life, SBI Life and Tata AIG Life.

The regulator's order has had implications not only for the life insurance companies, but also for their promoters who have sunk in over Rs 26,000 crore (the Economics Times 11 April 2010). Rejecting the arguments by insurance companies that ULIP Schemes are insurance products, a view also endorsed by IRDA, SEBI issued the order to the life insurance companies. The traditional policies are oriented towards protection and eligibility for bonus. ULIPs, on the other hand are seen as long-term savings instruments sold at the risks of policyholders. TULIPS (Traditional plus ULIP) offer flexibility to the policyholder in terms of investment returns and also life cover. Today most of the ULIPs are TULIPS. A part from the premium is invested in equities or Government bonds depending upon the choice of the policyholders at their risks only and other part of the premium is taken for life risks.

The investments are similar to mutual fund investments and returns are reflected in the increase in the value of the units mirrored by NAV declared by the insurance company. Internationally, regulators give flexibility to insurers to sell any policy. There is no stipulation on the business portfolio mix between traditional policies and TULIPS. But in India in consideration of composition and perceptions about life risks and investment risks of policyholders especially in rural and semi rural areas, where lots of mis-selling are reported, the regulators shall come out with proper stipulation as to minimum share of life risks cover in the overall portfolio of TULIPS so to avoid under insurance and protection of the policyholders' interests properly, whether they are regulated by IRDA or SEBI.

23

ACCOUNTING MANUAL – LIFE INSURANCE BUSINESS

We have already discussed Accounting Regulations and Principles for Life Insurance Business in Chapter-7**.** Here we discuss certain additional aspects with a few formats of financial statements and the regulatory requirements thereof.

Management Report Forming Part of Financial Statements

A management report generally containing the following particulars duly authenticated by the management shall be attached to the financial statements as per regulatory requirements:

1. Confirmation regarding the continued validity of the registration granted by the Authority;

2. Certification that all the dues payable to the statutory authorities have been duly paid;

3. Confirmation to the effect that the shareholding pattern and any transfer of shares during the year are in accordance with the statutory or regulatory requirements;

4. Declaration that the management has not directly or indirectly invested outside India the funds of the holders of policies issued in India;

5. Confirmation that the required solvency margins have been maintained;

6. Certification to the effect that the values of all the assets have been reviewed on the date of the Balance Sheet and that in his (insurer's) belief the assets set forth in the Balance-

sheets are shown in the aggregate at amounts not exceeding their realisable or market value under the several headings – “Loans”, “ Investments”, “Agents balances”, “Outstanding Premiums”, “Interest, Dividends and Rents outstanding”, “Interest, Dividends and Rents accruing but not due”, “Amounts due from other persons or Bodies carrying on insurance business”, “Sundry Debtors”, “Bills Receivable”, “Cash” and the several items specified under “Other Accounts”;

7. Certification to the effect that no part of the life insurance fund has been directly or indirectly applied in contravention of the provisions of the Insurance Act, 1938 (4 of 1938) relating to the application and investment of the life insurance funds;

8. Disclosure with regard to overall risk exposure and strategy adopted to mitigate same;

9. Operations in other countries, if any, with a separate statement giving management’s estimate of country risk, exposure risk and the hedging strategy adopted;

10. Ageing of claims indicating the trends in average claim settlement time during the preceding five years;

11. Certification to the effect as to how the values, as shown in the balance sheet, of the investments and stocks and shares have been arrived at, and how the market value thereof has been ascertained for the purpose of comparison with the values so shown;

12. Review of asset quality and performance of investment in terms of portfolios, i.e., separately in terms of real estate, loans, investments, etc.

13. A responsibility statement indicating therein that:

    - in the preparation of financial statements, the applicable accounting standards, principles and policies have been followed along with proper explanations relating to material departures, if any:

- the management has adopted accounting policies and applied them consistently and made judgements and estimates that are reasonable and prudent so as to give a true and fair view of the state of affairs of the company at the end of the financial year and of the operating profit or loss and of the profit or loss of the company for the year;

- the management has taken proper and sufficient care for the maintenance of adequate accounting records in accordance with the applicable provisions of the Insurance Act 1938 (4 of 1938)/Companies Act, 1956 (1 of 1956), for safeguarding the assets of the company and for preventing and detecting fraud and other irregularities;

- the management has prepared the financial statements on a going concern basis;

- the management has ensured that an internal audit system commensurate with the size and nature of the business exists and is operating effectively; and

14. A schedule of payments, which have been made to individuals, firms, companies and organisations in which Directors of the insurer are interested.

Allocation of Operating Expenses to Various Business Segments

Operating Expenses relating to insurance business are to be allocated to Non-linked participating, Non-linked Participating, General Annuities, Pensions, and Group Business etc., on the following basis:

(a) Expenses which are directly identifiable are allocated on actual basis;

(b) Other expenses which are not directly identifiable are allocated out of the common pool on any of the following basis or a combination of these;

- Number of policies
- Total Premium collected
- Sum insured

(c) The method of allocation has to be decided based on the nature of expenses (New business/renewal, Fixed/variable and identifiable parameters based on expenses classes are applied to each line of business); and

(d) Allocation of common expenses between various business segments and allocation of expenses between Participating, Non-Participating and annual policies are to be certified by the Appointed Actuary.

Financial Statement Formats as per Regulations

Life Insurers shall prepare Financial Statements including Revenue Account, Profit and Loss Account and Balance Sheet in the following manner:

- Revenue Account also called as Policyholders' Account, Profit & Loss Account called as Shareholders' Account and the Balance Sheet are to be prepared in the specified formats Form A-RA, Form A-PL and Form A-BS respectively.
- The insurer shall prepare Revenue Account for the under-mentioned business separately and to that extent the application of AS17 stands modified:
    - o Participating policies and Non-participating policies
    - o Linked Business and Non-linked Business
    - o Business within India and Business outside India
- The insurer shall prepare separate Receipts and Payments Account in accordance with the direct method prescribed in

Accounting Standard 3 “Cash Flow Statement” issued by the ICAI.

Format of Balance Sheet — Form A-BS

Table-48: Balance Sheet of Life Insurance Company

Particulars	Scheme	Current Year	P/Year
SOURCES F FUNDS			
Shareholders’ Funds:			
Share Capital			
Reserves and surplus			
Credit / (debit) fair value change account			
Sub-total			
Borrowings			
Policyholders’ funds:			
Credit / (debit) fair value change account			
Policy Liabilities			
Insurance Reserves			
Provision for linked liabilities			
Sub-total			
Funds for future appropriations			
Total (Sources of Funds)			

APPLICATION OF FUNDS			
Investments			
Shareholders'			
Policyholders'			
Assets held to cover linked liabilities			
Loans			
Fixed assets			
Current assets			
Cash & Bank Balances			
Advances and Other Assets			
Sub total (A)			
Current Liabilities			
Provisions			
Sub total (B)			
Net Current Assets (C) = (A-B)			
Miscellaneous expenditure (not written off)			
Debit balance in profit & loss account (Shareholders' Account)			
Total Application of Funds			

Format of Revenue Account — Form A-RA

Table -49: Revenue Account of Life Insurance Company

Particulars	**Scheme**	**C/ Year**	**P/ Year**
Premiums earned – net			
Premium Reinsurance ceded Reinsurance accepted–			
Income from Investments			
Interest, Dividends & Rent – Gross Profit on sale/ redemption of investments (Loss on sale/ redemption of investments) (d) Transfer/Gain on revaluation/ change in fair value*			
Other Income (to be specified)			
TOTAL (A)			
Commission			
Operating Expenses related to Insurance Business Provision for doubtful debts			
Bad debts written off			
Provision for Tax			
Provisions (other than taxation)			
(a) For diminution in the value of investments (Net) (b) Others (to be specified)			
TOTAL (B)			

Benefits Paid (Net)			
Interim Bonuses Paid			
Change in valuation of liability in respect of life policies Gross Amount ceded in Reinsurance 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)			

* Represents the deemed realised gain as per norms specified by IRDA

Format of Revenue Account — Form A-PL

Table-50: Profit & Loss Account for the Year Ended 31 March 200…

Particulars	**Scheme**	**Current Year Rs.'000**	**Previous Year Rs.'000**
Amounts Transferred from Policyholders A/C			
Income From Investments a) Interest, Dividend & rent—Gross			

b) Profit on sale/redemption of investments c) Loss on Sale/redemption of investments			
Other Income (To be specified)			
Total (A)			
Expenses other than those directly related to insurance business			
Bad Debts Written off			
Provisions (Other than taxation) a) 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) Balance at the beginning of the year b) Interim Dividend paid during the year c) Proposed Dividend d) Dividend Distribution Tax e) Transfer to Reserves/other accounts (specified)			
Profit Carried ……………to the Balance Sheet			

Notes:

(a) **Others shall include items like foreign exchange gains or losses and other items*

(b) *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 the head "Advance Taxes Paid and Taxes Deducted at Source"*

(c) *Income from rent includes only the realized rent. It shall not include notional one.*

Requirements for Balance Sheet Items

(a) Share Capital: Balance shall be supported by a schedule containing the following information;

(i) Authorized Capital – No. of shares and value

(ii) Issued capital – No of shares and value

(iii) Subscribed Capital – No of shares and value

(iv) Called-up Capital – No of shares and value

Less: Calls Unpaid

Add: Shares Forfeited (Amount originally paid up)

Less: Par Value of Equity Shares bought back

Less: Preliminary Expenses on Underwriting of Shares

In the notes following aspects are to be disclosed:

- o Particulars of different classes of capital
- o Amount capitalized on account of bonus share
- o Part of capital held by a holding company.

- o Pattern of holding (Promoters – Indian and Foreign) being number of shares and per cent

(b) **Reserves and Surplus:** Such Balance shall be classified into following heads:

(i) Capital reserve

(ii) Capital Redemption Reserve

(iii) Share Premium

(iv) Revaluation Reserve

(v) General Reserves less: Dr. Bal. in profit and loss A/C and Amount Utilized in Buy Back

(vi) Catastrophe Reserve

(vii) Other Reserves (To be specified)

(viii) Balance of Profit and Loss Account

(c) **Borrowings:** These will include the amounts under distinct heads like:

(i) Debentures

(ii) Fixed Deposits

(iii) Banks

(iv) Financial Institutions; and

(v) Other entities carrying on insurance business and others. The extent to which the borrowings are secured shall be separately disclosed stating the nature of the security under each of the above heads.

(d) **Investments:** (i) Investments in the balance sheet must be supported by two separate schedules showing investments of shareholders' fund and those policyholders' fund separately. Each Schedule will show the details of long-term and short-term investments under the following heads:

- Govt. Securities and Government Guaranteed bonds including Treasury bills
- Other Approved Securities
- Other Investments
    - Shares –Equity and Preference
    - Mutual Funds
    - Derivative Instruments
    - Debentures/ Bonds
    - Other Securities
    - Subsidiaries
    - Investment Properties—Real Estate

ii. Total investment in will be segregated into Investments in India and outside India.

iii. Investments made out of Catastrophe Reserve will be shown separately.

iv. Debt Securities will be considered as "held to maturity" securities and will be measured at historical costs subject to amortization.

v. Investment Property means a property including land, building or part of a building or both held to earn rental income or for capital appreciation or for both, rather than use in services or for administrative purposes.

(e) **Loans:** Loan Amount in Balance Sheet will be supported by complete schedule showing the following details therein

Security-wise Classification

— Secured….a) On Mortgage of property, b) On shares and Bonds c) Others

— Unsecured…a) Loans against Policies b) Others

Borrower-wise Classification

(a) Central and State Government

(b) Banks and Financial Institutions

(c) Subsidiaries

(d) Companies

(e) Loans against policies

(f) Others

Performance-wise Classification

Standard: i) In India; and ii) Outside India

Non-standard: i) In India; and ii) Outside India

Maturity-wise Classification: a) Short term; and b) Long Term

Note: Short-term loans shall include those, which are repayable within 12 months.

(f) **Fixed Assets:** Amount of Fixed Assets in Balance sheet will be supported by complete schedule containing following information as per IRDA regulation:

(i) Gross Block less Depreciation resulting into net block for every fixed asset.

(ii) Fixed Assets shall include Goodwill, Land-Freehold, Leasehold property, Buildings, Furniture & Fixtures, Information & Technology equipment, Vehicles, and Office equipments.

(**g**) **Cash and Bank Balances:** Cash and Bank Balances shall include the following items to be specified in the schedule:

- Cash including cheques, drafts & stamps
- Bank Balances showing separately under Current A/Cs, Deposit A/Cs & Others
- Money at call and Short Notice
- Others (To be specified)

Note: Total Cash and Bank balances to be disclosed separately in India and Outside. India

Requirements for Revenue Account

(A) Income

- Premium Earned net showing separately: a) Premium; b) Reinsurance Ceded; and c) Reinsurance Accepted;
- Income from Investments showing separately; a) Interest, dividend and Rent (gross); b) Profit on sale/redemption of investments; c) loss on sale/redemption of investments; and d) Transfer/Gain on revaluation/change in Fair value that represents the deemed realized gain as per norms specified by the authority; and
- Other Income to be specified.

(B) Commission

- Commission

- Operating Expenses related to Business (Management Expenses)
- Provision for Doubtful debts, Bad Debt, Provision for Tax, and Provision for Diminution in the value of asset

(C) Benefits

- Benefits Paid...Net
- Interim Bonus Paid
- Change in Valuation of liability in respect of life policies: a) Gross*; b) Amount ceded in Reinsurance; and c) Amount Accepted in reinsurance

Note: Here Gross represents Mathematical Reserves after allocation of bonus.

(D) Surplus: Surplus /Deficit = A-B-C

Items under A, B, and C have been specified above

(E) Appropriation of Surplus

Appropriation of Surplus will be shown in the following manners:

- Transfer to Shareholders' A/C
- Transfer to Other Reserve
- Balance being Funds for Future Appropriation

(F) Additional Aspects of Revenue Account

- Premium Incomes received from business concluded in and outside India are to be shown separately;
- Reinsurance Premiums on business both ceded and accepted are to be brought into Gross Amount, i.e. before deducting commission;

- Claims incurred shall comprise claims paid, specific claims settlement costs and change in the outstanding provisions for claims at the year end;

- Items of expenses and income in excess of 1 per cent of total premium (less reinsurance) or Rs 500,000, whichever is higher, shall be shown as a separate item; and

- Fees and expenses connected with claims shall be included in claims.

Regulatory Requirements and Format for Cash Flow Statement

Insurance company is to prepare Cash Flow Statements in direct method as per regulatory requirement. Following is the format of Cash flow statement for life insurance business. Cash flow statement examines liquidity of a business enterprise. Cash Flow Statement in direct method enables the regulator to examine cash inflow and Cash Outflow from each of the activities of the firm separately. Table-51 shows the format of Cash Flow Statement (Receipt and Payment Account) for life insurance business.

Table-51: Cash Flow Statement Format

A i	**Inflow From Operating Activities**	**Current Year**	**Previous Year**
1.	Premium Income Net		
2.	Other Income, Increase in premium deposit		
3	Fund Contributed by Govt. of India		
	Total Inflow		
A ii	**Outflow for Operating Activities**		
4.	Operating Expenses & Commission		

5.	Claims Paid to Policyholders		
6.	Decrease in Unit Capital		
7.	Increase in Advance Deposits		
	Total Outflow (b)		
A iii	**Cash General From Operation (a-b)**		
8.	Less: Income Tax paid		
9.	Less: Bonus Paid to Policyholders		
10.	Less: Dividend Paid to Shareholders		
A.	Net Cash Generated from Operations		
B.	Cash Flows From Investing Activities:		
11.	Interest & Dividend Income		
12.	Total Fund Available (A+B)		
13.	Fixed Assets Purchase		
14.	Investments Purchase (net of sales)		
15.	Increase in Cash &Cash Equivalent (12-13-14)		
16.	Cash & Cash Equivalent at the beginning of Yr.		
17.	Cash &Cash Equivalent at the end of Yr (15+16)		

24

ACCOUNTING MANUAL – GENERAL INSURANCE BUSINESS

Formats of Financial Statements

Financial Statements are to be prepared and audit reports will be made in compliance with following requirements of IRDA (Preparation of Financial Statements and Auditors Report of Insurance Companies) Regulations, 2000:

- **Part I**- Accounting Principles for Preparation of Financial Statements
- **Part II**- Disclosures forming part of Financial Statements
- **Part III**- General Instruction for preparation of Financial Statements
- **Part IV**- Contents of Management Report
- **Part V-** Preparation of Financial Statements

In this chapter, additional aspects, along with a few formats of financial statements and the regulatory requirements thereof, are discussed. Non-Life Insurers shall prepare Financial Statements as per specified Forms such as Revenue Account in Form B- RA, Profit and Loss Account in Form B-PL and Balance Sheet in Form B-BS as specified in Part V in Schedule B of Regulation 3. The said Financial Statements will be prepared in accordance with General Instructions for preparations as per Part III. The said Financial Statements shall be supported by Disclosures Forming

Part of Financial Statements and the comments of Management report as per Part II and Part IV of the Schedule B respectively. The Specified Forms of financial statements are given hereinafter as ready reference. Thus following financial statements are to be prepared in the prescribed formats:

- Balance Sheet
- Revenue Accounts
- Profit and Loss Account
- Receipts and Payments Account

Accounting Principles

Accounting Principles as prescribed by IRDA regulations for recognition of income and expenditure have been discussed in Chapter 7. In this chapter, INBR Provisions which is one of the important major elements of the claim cost is discussed. Claims Cost in general insurance business needs to be specially appreciated as it accounts more than 70 per cent of the business costs. It's determination and estimation requires considerations of some crucial factors, including: all regulatory requirements discussed in Chapter 7 are to be considered by the management for the preparation of financial statements in compliance with regulatory requirements. In addition to the above-mentioned regulatory requirement, the provision for IBNR and IBNER deserves special mention, which the management will consider for preparation of financial statements and the auditor will consider for expression of opinion on the 'true and fair view' aspect of the financial statements as required by Standard on Auditing (SA) 200:

- Provisions for Liability for Outstanding Claims include: a) Claims reported but not paid; b) Claims Incurred but not Reported (IBNR); c) Claims Incurred but not Enough Reported (IBNER). Provisions for all such outstanding claims must be properly estimated, evaluated and accounted for as they will determine and impact future cash outgo and value of asset of the insurer when such liabilities for Outstanding claims will be settled shortly.

- The management shall review provisions for all such outstanding claims periodically and give effect to changes if any on review, in respect of estimated O/s claim liability, as such represents the difference between the estimated liability for outstanding claims at the beginning of the year and at the end of the particular period in order to enable the financial statements exhibit the true and value of profit or loss or the state of affairs of the insurer.

- The accounting estimate shall also include claims costs adjusted for estimated salvage value, if there is sufficient degree of certainty of its realization.

- As per IRDA (Appointed Actuary) Regulations, the duties and obligations of an appointed actuary of an insurer shall include in the case of the insurer carrying on general insurance business to ensure that… the actuarial principles in the determination of liabilities, have been used in the calculation of reserves for IBNR and other reserves where actuarial advice is sought for by the Authority (IRDA).

As per IRDA (Preparation of financial statements and auditor's Report of insurance companies) regulations, 2002 estimation of O/s Claim liability needs to be Actuarial Valuation in some cases. Estimate of claims made in respect of contracts exceeding four years shall be recognized on an actuarial basis as per prescribed regulatory norms. In such cases certificate from a recognized Actuary as to the fairness of liability assessment must be obtained. Actuarial assumptions shall be suitably disclosed by way of notes to the accounts.

Principles on Valuation of Investment

An insurer in life insurance business shall determine the values of investments in the manner, as discussed below.

Real Estate — Investment Property

- The value of investment property shall be determined at historical cost, subject to revaluation at least once in every 3 years. The change in the carrying amount of the investment property shall be taken to Valuation Reserve Account. The insurer shall assess at each balance sheet date whether any impairment of the investment property has occurred.

- In case of sale of investment property, the profit or loss on sale, as the case may be, shall include accumulated changes in the carrying amount previously recognized under Revaluation Reserve A/C in respect of particular property and being recycled to the relevant Revenue A/C or Profit and Loss Account as the case may be, on sale.

- The bases for valuation shall be disclosed in the notes to the accounts. IRDA may issue directions on release of any amount from Revaluation Reserve A/C for declaring bonus to policyholders. But except for the above as per the Authority's direction, no other amount shall be distributed to shareholders out of Revaluation Reserve Account.

- An impairment loss shall be recognized as an expense in the Revenue or Profit and Loss Account, as the case may be, immediately unless the asset is carried at revaluated amount. Any impairment loss of a revaluated asset shall be treated as a revaluation decrease of that asset and if the impairment loss exceeds the corresponding revaluation reserve, such excess shall be recognized as an expense in Revenue A/C or Profit and Loss Account as the case may be.

Debt Securities

Such securities including Government securities and redeemable preference shares shall be considered as held to maturity securities and shall be measured at historical cost subject to amortization in the following manner for life insurance business:

- Debt Securities including Government Securities, where the book value is more than face value, the premium will be amortized on straight line basis over the balance period of holding /maturity in all cases of business except Unit Linked Plan where all debt security will be shown at market value.

- Redeemable Cumulative Preference Shares, where book value is more than face value, the premium will be amortized on straight line basis over the balance period of holding / maturity in all classes of business for ALM.

Equity Securities and Derivative Instruments Traded in Active Markets

- Listed Equity Securities and Derivative Instruments that are traded in active markets shall be measured at fair value on the balance sheet date. For the purpose of calculation of fair value, the lowest of the last quoted closing price at the stock exchanges where the securities are listed shall be taken.

- Unrealized gains/losses arising out of fair value of listed equity shares and derivative instruments shall be taken to equity under the head ‘Fair Value Change Account’.

- The appreciation in the value of investments, being in the nature of unrealized gain is not taken into account for determining profit or loss of non-life business. It is also mentioned in the Union Budget 2010-11 that the unrealized gains due to appreciation in the value of investments will not be included in the total income. This amendment is proposed to take effect from 1st April 2011 and accordingly apply in relation to the Assessment Year 2011-12 and onwards.

- The 'Profit on Sale of investments' or 'Loss on Sale of investments' as the case may be, shall include accumulated changes in the fair value previously recognized in equity under the head 'Fair Value Change Account' in respect of a particular security and being recycled to the relevant Revenue Account or Profit and Loss Account on actual sale of that listed security.

- The IRDA may issue directions specifying the amount to be released from the 'Fair Value Change Account' for declaring bonus to the policyholders. Except for the above, no other amount shall be distributed to shareholders out of Fair Value Change Account. Also, any debit balance in Fair Value Change Account shall be reduced from profit/free reserves while declaring dividends.

- The insurer shall assess on each balance sheet date whether any impairment of listed equity security or derivative instrument has occurred.

- An impairment loss shall be recognized as an expense in Revenue/Profit and Loss Account to the extent of the difference between the re-measured fair value of the security/ investment and its acquisition cost as reduced by any previous impairment loss recognized as expense in Revenue/Profit and Loss Account.

- Any reversal of impairment loss earlier recognized in Revenue /Profit& Loss Account shall be recognized in Revenue /Profit and Loss Account.

- Fair Value Change Account (Credit) is shown in Balance Sheet as Sources of Funds under sub-heads of Shareholders Funds and Policyholders' Funds to the their respective portions.

Unlisted & Not Actively Traded Equity Securities & Derivatives Instruments

Such securities or instruments unlisted or listed but not traded regularly in active markets shall be measured at historical cost. For diminution in value of such instruments, proper provision shall be made. If estimated based on external evidence show an increase in the value, the provision so made may be reversed. The increased carrying amount of investment due to the reversal of provision shall not exceed the historical cost.

Loans

Loans shall be measured at historical cost subject to impairment provision on prudential norms. After assessment of quality of loans, the impairment provisions shall not be less than the aggregate amount of such loans, which are subject to defaults of following nature:

- Interest remaining unpaid over a period of six months
- Installments falling due and remaining unpaid over a period of last six months

Balance Sheet of a Non-life Insurance Company

The Balance Sheet of a Non-life Insurance Company shall have the following items of assets and liabilities with comparative figures for the current year and previous year with detailed schedules for the respective items of assets and liabilities:

Table-52: Balance Sheet Form B- BS

	Scheme	Current Year	Previous Year
SOURCES OF FUNDS			
Share capital			
Reserves and surplus			
Fair value change account			
Borrowings			
TOTAL			
Application of Funds			
Investments			
Loans			
Fixed assets			
Current Assets			
Cash and Bank Balances			
Advances and Other Assets			
Sub-Total (A)			
Current liabilities			
Provisions			
Sub-Total (B)			
Net Current Assets (C) = (A - B)			
Miscellaneous expenditure (Not written off)			
Debit Balance in P& L Account			
Total			

Example: A balance sheet for a General Insurance Company has been prepared below with a few assumed figures to clarify certain aspects on Sources of Funds and Application of Funds.

ABC General Insurance CO. Ltd.
Balance Sheet as on 31st March 2008

Particulars	**Schedule**	**Current year**	**Previous year**
A. Sources of Funds		(Rs. in million)	
1. Share Capital		200.00	150.00
2. Reserves and Surplus		4608.03	4166.41
3. Fair Value Change Account -		12211.27	6846.97
4. Borrowings		Nil	Nil
Total (A)		17019.30	11163.38
B. Application of Funds			
1. Investments		20665.26	14575.23
2. Loans		786.52	874.13
3. Fixed Assets		121.06	114.41
4. Deferred Tax Assets -		61.75	84.07
5. Current Assets			
a. Cash and Bank Balances		3059.71	2286.09
b Advances and Other Assets		2230.12	1738.56
Total Current assets (a+b):		5289.83	4024.65
c. Current Liabilities*		7134.74	6085.25

	d. Provisions **	2871.54	2578.57
	Total Current Liabilities (c+d)	10006.28	8663.82
	Net Current Assets (a+b-c-d)	-4716.45	-4639.17
6.	Miscellaneous Expenditure (to the extent not, written off or adjusted)	101.16	154.72
7.	Debit Balance in Profit and Loss A/C	Nil	Nil
	Total (B)	17019.30	11163.38

* Current Liabilities include Outstanding Claims for Rs 5505.40mn along with other items in the schedule of current liabilities

** Provisions include Unexpired Reserves Rs 2253.51mn along with other items in the schedule of provisions

Analysis of Funds

As mentioned earlier insurance business is run with two funds – Policyholders funds and Shareholders funds which constitute of the following items specifically. For better clarification, figures given hereinafter are taken from the balance sheet shown in the example:

Shareholders' Fund (Rs in million)

• Share Capital...	200.00	
• Capital Reserve	—	
• General Reserve	4608.03	
• Misc. Reserve	—	
		4808.03

Policyholders' Fund:

• Unexpired Reserves	2253.51	
• Outstanding Claims	5505.40	**7758.91**
Total Funds		**12566.94**

(Ratio between two funds: 38: 62)

Revenue Account Format

Income and Expenditure will be recognized as per principles specified in Chapter 7 (see Table-53).

Table-53: Revenue Account Form B – RA

Particulars	Schedule	Current Yr.	Prv. Yr.
Premium earned (Net)	1		
Profit/loss on sale/redemption of investments			
Others (to be specified)			
Interest, Dividend & Rent—Gross			
Total (A)			
Claims Incurred (Net)	2		
Commission	3		
Operating Expenses related to Insurance business	4		
Total (B)			
Operating profit/loss from Fire/Marine/ Misc. Business C=(A—B)			
Appropriations			
Transfer to Shareholders' Account			
Transfer to Catastrophe Reserve			
Transfer to other Reserves (to be specified)			
Total (C)			

Example: Let us examine how a Revenue Account is prepared for a Non-life Insurance Company called **Diamond General Insurance Co Ltd** (see Table-54 55, 56 and 57)

Table-54: Fire Insurance Revenue Account for the Year Ended 31st March 2006 (Rs in crore)

Particulars	Scheme	2005-06	2004-05
1. Premium earned (Net)	1	79000	
2. Profit/loss on sale/ redemption of investments		4000	
3. Others (to be specified)			
4. Interest, Dividend & Rent—Gross		9000	
Total (A)		**92000**	
5. Claims Incurred (Net)	2	26000	
6. Commission	3	4000	
7. Operating Expenses		33000	
Total (B)		**63000**	
Operating profit/loss Business C=(A—B)		29000	
APPROPRIATIONS			
Transfer to Shareholders' A/C (P&L Account)		29000	
Transfer to Catastrophic Reserve		—	
Transfer to other Reserves (to be specified)		—	
Total (C)		**29000**	

Schedules to Fire Insurance Revenue Account For the year ended 31st March 2006

Table-55: Schedule 1 — Premium Earned (Net)

Particulars	2005-06	04-05
Premium From Direct Business	107000	
Add; Premium on Reinsurance Accepted	16000	
Less: Premium on Reinsurance Ceded	46000	
Net Premium	77000	
Adj. For Change in Reserve in Unexpired Risks (38500-37500)	2000	
Net Premium Earned (Net)	79000	

Table-56: Schedule 2 — Claim Paid (Net)

Particulars	2005-06	04-05
Claim Paid Direct	37000	
Add; Claims on Reinsurance Ceded	6000	
Less: Claims on Reinsurance Accepted	12000	
Net Claims Paid	31000	
Add: Outstanding Claims at the end (net)	47000	
Less: Outstanding Claims at the Beginning (net)	52000	
Incurred Claims Net	26000	

Table-57: Schedule 3 — Commission (Net)

Particulars	2005-06	04-05
Commission Paid Direct	9000	
Add; Commission on Reinsurance Accepted	4000	
Less: Commission on Reinsurance Ceded	9000	
Net Commission	4000	

Profit and Loss A/C Format — Form B-PL

Table-58: Profit and Loss A/C Format — Form B-PL

Particulars	Schedule	Current Yr.	Prv. Yr.
OPERATING PROFITS/LOSS			
Fire Insurance			
Marine Insurance			
Miscellaneous Insurance			
INCOME FROM INVESTMENTS			
Interest, Dividends & \Rents—Gross			
Profit on Sale of Investments			
OTHER INCOME (To be specified)			
Total (A)			
PROVISIONS (Other than taxation)			
For diminution in value of investment			
For doubtful debts			
Others (to be specified)			
OTHER EXPENSES			
Expenses other than those related to Ins. Business			
Bad Debts written off			
Others (To be specified)			

Total (B)			
Profit Before Tax			
Provisions for Taxation			
APPROPRIATIONS			
Interim Dividend Paid during the year			
Proposed Final Dividend			
Dividend distribution tax			
Transfer to any Reserve or Other Account			
Balance of profit / loss brought forward from last yr.			
Balance carried forward to Balance Sheet			

Cash Flow Statement

Cash Flow Statement is useful in providing users of financial statements with a basis to assess the ability of the firm to generate cash and cash equivalent and the needs of the firm to utilize those cash flows. The financial decisions that are taken by users require an evaluation of the ability of the firm to generate cash and cash equivalent and the timing and certainty of their generation. In insurance industry the cash flow statement is of prime importance to the users of the financial statements as the insurance carries risk taking business dealing with intangible product, i.e. promise to indemnify loss in future as and when accident will occur in consideration of premium collected currently. The insurers need to have both solvency and liquidity sufficiently to pay off its liability for claims at the time of accident, i.e. occurrence of perils. Thus an insurer should always prepare a cash flow statement and should present it for each period for which financial statements are presented as per regulatory norms and forms. As per IRDA regulations Cash Flow statement in an insurance company is to be prepared in a Direct Method where AS 3 will not be applicable (see Table-59). A cash flow statement if used in conjunction with other financial statements provides information that enables the user to evaluate the charges in the net assets of the insurance company, its financial structure (including its liquidity and solvency). For the purpose of preparing cash flow statement in an insurance company, following terms need to be defined for proper interpretation and use.

Cash: It comprises on hand and demand deposits with banks of the corporate office and its all operational units including overseas ones, on the other.

Cash Equivalents: These are short term, highly liquid investments that are readily convertible into known amounts of cash and which are subject to an insignificant risk of changes in value.

Cash Flows: These are inflows and outflows of cash and cash equivalents.

Operating Activities: These are the principal revenue-producing activities of a firm (insurer) and other activities that are not investing or financing activities. In insurance company cash flow from operating activates (insurance activities) is a key indicator of the extent of the extent to which the operations of the enterprise have generated sufficient cash flows to maintain to maintain the operating capability of the insurers, pay claims, commission, management expenses and pay dividends and repay loans and borrowings.

Investing Activities: These are the acquisitions and disposals of long term assets and other investments not included in cash equivalent.

Financing Activates: These are activities that result in changes in the size and composition of the shareholders funds and policyholders funds (in case of insurance company) and borrowings of the firm.

Preparation of Cash Flow Statement: The cash flow statements should be prepared and presented classified and segregating Operating, Investing and Financing activities.

Table-59: Direct Method Cash Flow Statement (Applicable to Insurance Company)

Cash flows from operating activities		
Cash receipts from customers		
Cash paid to suppliers and employees		
Cash generated from operations		
Income taxes paid		
Cash flow before extraordinary item		
Proceeds from earthquake disaster settlement		
Net Cash from operating activities		
Cash flows from investing activities		
Purchase of fixed assets		
Proceeds from sale of equipment		
Interest received		
Dividends received		
Net cash from investing activities		
Cash flows from financing activities		
Proceeds from issuance of share capital		
Proceeds from long-term borrowings		
Repayment of long-term borrowings		
Interest paid		
Dividends paid		
Net cash used in financing activities		
Net increase in cash and cash equivalents		
Cash and cash equivalents at beginning of period		
Cash and cash equivalents at end of period		

Table-60 shows the format of Cash Flow Statement given for comparative study:

Table-60: Indirect Method Cash Flow Statement

Cash flows from operating activities		
Net Profit before taxation, and extraordinary item		
Adjustments for:		
- Depreciation		
- Foreign exchange loss		
- Interest income		
- Dividend income		
- Interest expense		
- Operating profit before working capital changes		
- Increase in sundry debtors		
- Decrease in inventories		
- Decrease in sundry creditors		
Cash generated from operations		
Income tax paid		
Cash flow before extraordinary item		
Proceeds from earthquake disaster settlement		
Net Cash from operating activities		
Cash flows from investing activities		
Purchase of fixed assets		
Proceeds from sale of equipment		
Interest received		
Dividend received		
Net Cash flows from financing activities		
Cash flows from financing activities		
Proceeds from issuance of share capital		

Proceeds from long term borrowings		
Repayment of long-term borrowings		
Interest paid		
Dividend paid		
Net cash used in financing activities		
Net increases in cash and cash equivalents		
Cash and cash equivalents at beginning		
of period		
Cash and cash equivalents at end of period		

Following is an extract of the Cash Flow Statement prepared by a non-life insurance company in 2008-09.

Receipt & Payment Account/Cash Flow Statement for the period 01.04.2008 to 31.03.2009

Description	Amount in Rs.(000) **Current Year**	Amount in Rs.(000) **Previous Year**
Operating Activities		
Profit Appropriate to General Reserve	1265475	10700322
Adjustment for Non- Cash Items		
Deferred Expenses	0	476070
Unexpired Risks Reserves	2510091	1028499
Special Contingency Reserves for URR	449500	0
Additional Provisions for Outstanding Claims	6785764	3806514
Depreciation	481854	356358
Provision for Dividend and Dividend Tax	526478	3310959
Provision for Tax - India	410100	955668

Provision for Tax - Foreign	345666	0
Deferred Tax	-131491	304037
Reserve for Doubtful Debts	108320	-11027
Foreign Currency Translation Reserve	1778508	-784146
General Reserve Adjustment for AS 15	0	-389700
Other Provisions	802682	-196797
Prepaid Expenses	-116966	0
Profit on sale of Assets	-4970	-2674
Balance Written Back	-564923	210201
	14646088	**19764284**
Items Considered Separately		
Investment Items - Interest, Dividend, Rent & Provisions	-12307648	-23460453
Investment Items - Profit on sale of Investments	-4560616	0
	-2222176	**-3696169**
Net Increase in Current Assets	-7961987	-5086648
Net Cash Flow from Operating Activities Before Tax	-10184163	-8782817
Net Tax Expenses – Indian	-1699977	-9529798
Net Cash Flow from Operating Activities After Tax		
A	**-11884140**	-18312615
Investing Activities		
Interest, Dividend & Rent	12362688	11849662
Net Increase / Decrease in Investments	7728648	6138560
Net Increase / Decrease in Loans	639023	876886
Net Addition to Assets	-906159	-179649

Net Cash Flow from Investing Activities **B**	**19824200**	**18685459**
Financing Activities		
Dividend Paid		
C	**-3310959**	-3416300
Increase/Decrease in Cash & Bank Balances during the year (A+B+C)=D	**4629101**	-3043456
Cash & Bank Balances as per Schedule **at the end of period** (D+E)= **F**	33208377	28579276
Cash & Bank Balances as per Schedule **at the beginning of period E**	28579676	31622732

Disclosures for Financial Statements (As per Regulatory Norms)

Disclosure By Notes

The following shall be disclosed by way of notes to the Balance Sheet:

1. Contingent Liabilities

   a. Partly-paid up investments

   b. Underwriting commitments outstanding

   c. Claims, other than those under policies, not acknowledged as debts

   d. Guarantees given by or on behalf of the company

   e. Statutory demands/liabilities in dispute, not provided for

   f. Reinsurance obligations to the extent not provided for in accounts

   g. Others (to be specified)

2. Encumbrances to assets of the company in and outside India;

3. Commitments made and outstanding for Loans, Investments and Fixed Assets;

4. Claims, less reinsurance, paid to claimants in/outside India;

5. Actuarial assumptions for determination of claim liabilities in the case of claims where the claims payment period exceed four years;

6. Ageing of claims–distinguishing between claims outstanding for more than six months and other claims;

7. Premiums, less reinsurance, written from business in/outside India;

8. Extent of premium income recognised, based on varying risk pattern, category wise, with basis and justification therefore;

9. Value of contracts in relation to investments, for:

   o Purchases where deliveries are pending;

   o Sales where payments are overdue;

   o Operating expenses relating to insurance business: basis of allocation of expenditure to various classes of business;

   o Historical costs of those investments valued on fair value basis;

   o Computation of managerial remuneration;

   o Basis of amortisation of debt securities;

10. Unrealised gain/losses arising due to changes in the fair value of listed equity shares and derivative instruments are

to be taken to equity under the head 'Fair Value Change Account' and on realisation reported in profit and loss Account. Pending realization, the credit balance in the 'Fair Value Change Account' is not available for distribution;

11. Fair value of investment property and the basis therefore; and

12. Claims settled and remaining unpaid for a period of more than six months as on the balance sheet date.

Disclosure on Accounting Ratios

Following Accounting Ratios are furnished in the Annual Report for analysis of Financial Statements:

- Gross Premium& Growth Rate
- Gross Premium to Shareholders Funds Ratio
- Growth Rate of Shareholders Funds
- Net Retention Ratio
- Net Commission Ratio
- Management Expenses to Gross Premium
- Combined (Claim & Mgmt. Exp.) Ratio
- Technical (Unexpired) Reserves to Net Premium Ratio
- Underwriting Balance Ratio
- Operating Profit Ratio
- Liquid Assets to Liabilities Ratio
- Net Earnings Ratio
- Return on Net Worth

- Reinsurance Ratio

Some of the accounting Ratios are discussed separately under 24.9 heading.

Disclosures on Investments, Business Segments

- Investments made in accordance with any statutory requirement should be disclosed separately together with its amount, nature, security and any special rights in and outside India.
- Segregation into performing/ non performing investments for purpose of income recognition as per the directions, if any, issued by the Authority.
- Percentage of business sector-wise.
- A summary of financial statements for the last five years, in the manner as may be prescribed by the Authority.
- Allocation of Interest, Dividends etc between Revenue Account and Profit& Loss Account.

Accounting Policies Forming Part of Financial Statements

All significant accounting policies in terms of the accounting standards issued by the ICAI, and significant principles and policies given in regulation and other accounting policies followed by the insurer shall be disclosed. Any departure from the accounting policies as aforesaid shall be separately disclosed with reasons for such departure.

Management Report – Its Contents

There shall be attached to the financial statements, a management report containing the following confirmation, certificates and particulars duly authenticated by the management as per regulatory norms:

- Confirmation regarding the continued validity of the registration;
- Certification that all the dues payable to the statutory authorities have been duly paid;
- Confirmation to the effect that the shareholding pattern and any transfer of shares during the year are in accordance with the statutory or regulatory requirements;
- Declaration that the management has not directly or indirectly invested outside India the funds of the holders of policies issued in India;
- Confirmation that the required solvency margins have been maintained;
- Certification to the effect that the values of all the assets have been reviewed on the date of the Balance Sheet and that in his belief the assets set forth in the Balance-sheets are shown in the aggregate at amounts not exceeding their realisable or market value under the several headings – “Loans”, “Investments”, “Agents balances”, “Outstanding Premiums”, “Interest, Dividends and Rents outstanding”, “Interest, Dividends and Rents accruing but not due etc;
- Operations in other countries, if any, with a separate statement giving the management’s estimate of country risk, exposure risk and hedging strategy adopted;
- Ageing of claims indicating the trends in average claim settlement time during the preceding five years;
- Certification to the effect as to how the values, as shown in the balance sheet, of the investments and stocks and shares have been arrived at, and how the market value thereof has been ascertained for the purpose of comparison;
- Review of asset quality and performance of investment in terms of portfolios, i.e., separately in terms of real estate, loans, investments, etc;

- A responsibility statement indicating therein that:
    - o in the preparation of financial statements, the applicable accounting standards, principles and policies have been followed along with proper explanations relating to material departures, if any;
    - o the management has adopted accounting policies and applied them consistently and made judgements and estimates that are reasonable and prudent so as to give a true and fair view of the state of affairs of the company at the end of the financial year and of the operating profit or loss and of the profit or loss of the company for the year;
    - o the management has taken proper and sufficient care for the maintenance of adequate accounting records in accordance with the applicable provisions of the Insurance Act 1938/ Companies Act, 1956;
    - o the management has prepared financial statements on a going concern basis;
    - o the management has ensured that an internal audit system commensurate with the size and nature of the business exists and is operating effectively; and
    - o A schedule of payments, which have been made to individuals, firms, companies and organisations in which Directors of the insurer are interested.

Financial Statement Analysis

The users of financial statements cannot form any opinion on any of the trends for their economic decisions with the company only on the basis of financial statements unless they use various ratio analysis, trend analysis with comparative and classified Accounting or Financial Statement. In using the Financial Statement including Balance Sheet, Income Statements along with required disclosure and management report and computing percentage change, trend change, component percentages, and ratios as exemplified in annexure, the finance manager and analyst constantly search for some standard of comparison to establish whether the information and relationship they have found are favourable or adverse for their future economic decisions. Generally, two standards of comparison used by financial analysts are: (i) the Past Performance of the company; and ii) the position of the company with respect to industry performance in the country and overseas. The insurance business is carried on with international process, principle and perspective because of its very nature of international character. So its trend analysis or trend percentage need be compared with industry data and international standard to judge the company's position in respect of growth, profitability, liquidity and solvency etc. From Balance Sheet, Revenue Account and Profit and Loss Account many Accounting Ratios as mentioned under section **24.6.2** can be obtained for Financial Management and analysis of financial health of an insurance company.

Accounting Policies Followed by General Insurance Company

To discuss the accounting policy let us refer the Balance Sheet as on 31st March 2009 published in the Annual Reports of the New India Assurance Company Ltd. for the year 2008-09.

Table-61: The New India Assurance Co. Ltd
Balance Sheet as on 31st March 2009

Particulars Schedule	**Current year (Rs'000)**	**Previous year** (Rs'000)
A. Sources of Funds		
1. Share Capital	**2,000,000**	2,000,000
2. Reserves and Surplus	**71,221,519**	67,728,035
3. Fair Value Change Account -	**74,172,943**	139,592,747
4. Borrowings	**-**	-
Total A	**147,394,462**	209,320,782

B. Application of Funds		
1. Investments	**177,675,725**	246,328,697
2. Loans	**5,938,624**	6,577,647
3. Fixed Assets	**1,581,706**	1,152,431
4. Deferred Tax Assets -	**233,054**	101,563
5. Current Assets		
a. Cash and Bank Balances	**33,208,377**	28,579,276
b. Advances and Other Assets	**50,670,163**	**36,701,783**
Sub Total (a+b)	**83,878,540**	65,281,059
c. Current Liabilities	**89,761,083**	77,620,843
d. Provisions	**32,152,104**	**32,499,772**
Sub Total (c+d)	**121,913,187**	110,120,615
Net Current Assets (a+b-c-d)	**-38,034,647**	-44,839,556
6. Miscellaneous Expenditure (To the extent not, written off or adjusted)	-	
7. Debit Balance in Profit and Loss Account		
Total B	**147,394,462**	**209,320,782**

Significant Accounting Policies and Notes to Accounts form integral part of the Balance Sheet as on 31st March 2009.

Accounting Convention

The Financial Statements are drawn up in accordance with the provisions of Section 11 (1) of the Insurance Act, 1938, regulations framed under Insurance Regulatory Development Act, 1999, read with the provisions of Sub-sections (1), (2) and (5) of Section 211, sub-section (5) of Section 227 of the Companies Act, 1956. The said statements prepared on the historical cost convention and on accrual basis, comply with accounting standards referred in Section 211 (3C) of the Companies Act, 1956 and IRDA (Preparation of Financial Statements and Auditors' Report of Insurance Companies) Regulations to the extent applicable, and conform to practices prevailing in the general insurance industry except as otherwise stated.

25

AUDITS IN GENERAL INSURANCE BUSINESS

Scope of Various Insurance Audits

Insurance Business is subject to various audits such as Internal Audit, Statutory Audit, Operational Audit, Underwriting Audit, Investment Audit etc. Every audit has some import role to improve the quality of insurance accounting and to exercise the better financial control over the fund management and financial management of the insurance company. In insurance business, audits carried out are basically of two type;-Management Audit and Statutory Audit. In PSU organizations, another important audit called CAG audit is also carried out in addition to above two audits. The management audits include Internal Audit, Underwriting, Claims Audit, and Special Audit. The Statutory Auditors are to report to the members of the company in the specified manner. The auditor's report should describe the scope of the audit by stating that the audit was conducted in accordance with requirements of the Companies Act'1956, The Insurance Act 1938 and IRDA Regulations and relevant Auditing and Assurance Standards.

Insurance Act, 1938 and Audit

As per Section 12 of the Insurance Act, 1938 the Balance Sheet, Profit and Loss Account, Revenue Account and Profit and Loss Appropriation Account of every insurer, in the case of an insurer specified in sub-clause (a)(ii) or sub-clause (b) of clause (9) of Section 2 in respect of all insurance business transacted by him, and in the case of any other insurer in respect of the insurance business transacted by him in India, shall, unless they are subject to audit under the Indian Companies Act,1913, be audited annually by an auditor, and the auditor shall, in the audit of all such accounts have the powers of, exercise the functions vested in, and discharge the duties and be subject to the liabilities and penalties imposed on, auditors of companies by Sec 145 of the Indian Companies Act, !913. Now the provisions of the Companies Act, 1956 as amended from time to time are to be followed in place of the provisions of the Indian Companies Act, 1913.

The Companies Act 1956 and Insurance Audit

Insurance Audit is performed basically as per provisions of the Companies Act, 1956, the IRDA (Preparation of Financial Statements and Audit Report) Regulations 2000 and the Accounting Standards and Auditing Assurance Standards passed by the Institute of Chartered Accountants of India. Statutory Audit, which ensures that accounting, has been rendered as per the requirements of various statutes and standards applicable to insurance business. The statutory auditor is to verify that the insurance accounting has been completed as per the provisions of the above statutes and regulations. Statutory audit has had an important bearing upon the quality as well as the financial control of insurance accounts. As insurance accounting is a special type of accounting the Regulatory Authority laid down a set of requirements in respect of Statutory Audit Report on insurance accounting. The insurance audit is also subject to the provisions of Section 227 of the Companies Act, 1956, which provides the powers and duties of auditors. Under the provisions of Section 227 every auditor shall inquire the areas and aspects as specified by Sub-section (IA) and shall report to the members of the company on the accounts examined by him and on every balance sheet and profit and loss account and on every other document declared by this Act to be part of or annexed to the balance sheet or profit and loss account, which are laid before the company.

IRDA Regulations & Insurance Audit

The statutory audit is to ensure that his report provides those information and particulars as per regulatory norms. Following are the regulatory requirements for Audit Report as per schedule C of the Regulation called IRDA (Preparation of Financial Statements and Auditor's Report of Insurance Companies) Regulations 2000.

Information in Auditor's Report

As per IRDA Regulations, the auditors shall report that: a) all information and explanations necessary for their audit have been obtained by them and found satisfactory; b) proper books of account have been maintained by the insurer; c) proper returns from branches audited or unaudited have been received and were adequate; d) financial statements are in agreement with books of accounts; and e) the actuarial valuation of liabilities is duly certified by the appointed actuary to the effect that such valuation are in agreement with the guidelines and norms issued by IRDA.

Opinion of Auditor

Auditors shall express opinions on: a) True and Fair View of the financial position, i) whether the balance sheet gives a true and fair view of the affairs of the insurer at the end of the financial year, ii) whether revenue account gives a true and fair view of the surplus or the deficit for the financial year, iii) whether the profit and loss account gives a true and fair view of the profit or loss for the financial year and iv) whether the receipts and payments account gives a true and fair view of the receipts and payments for the financial year; b) Financial Statements stated in a above are prepared in accordance with the requirements of the Insurance Act, the IRDA Act, the Companies Act; c) Investments are valued in accordance with the provisions of the Act and IRDA Regulations thereupon; and d) the Accounting Policies selected by the insurer are appropriate and in accordance with the applicable accounting standard.

Certification by Auditor

Auditors shall further certify that: a) the management report has been reviewed by them and there is no apparent mistake or material inconsistencies with the financial statements; b) the terms and conditions of registration have been complied with by the insurer; c) cash balances and securities have been verified by them; d) investment and transactions relating to trust undertaken by insurer as trustee have been verified by them; and e) 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.

Audit Report

The above-noted the matters for auditors' report as specified in the regulations have been described in the following paragraph keeping in view of the provisions of Section 227 of the Companies Act, 1956.

Statutory Auditors Their Opinion

Statutory Auditors audit and express their opinion on the financial statements including Balance Sheet, Revenue Accounts, Profit and Loss Account and the Receipts and Payments Account of the insurance company for the year ended, which includes: a) Returns and Records of Regional or Zonal Offices; b) Divisional Offices c) Branch Offices; and d) Foreign Branches as the case may be, audited by the other auditors appointed by the competent authority. The preparation of financial statements audited by them is the responsibility of the company's management. Auditors' responsibility is to express an opinion on the financial statements based on their audit. The auditors shall express their opinion specifically on the following aspects as required by the IRDA in the specified regulations and by the provisions of the Section 227 of the Companies Act, 1956:

- Whether 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 found them satisfactory;

- Whether the insurer has maintained proper books of account so far as appears from an examination of those books;

- The Balance Sheet, Revenue Accounts, Profit and Loss Account and Receipts and Payments Account are in agreement with the books of account and returns;

- Whether proper returns, audited or un-audited, from branches and other offices have been received and whether they were adequate for the purpose of audit;

- Whether the balance sheet gives a true and fair view of the insurer's affairs as at the end of the financial year/ period; Whether the revenue account gives a true and fair view of the surplus or the deficit for the financial year/ period; Whether the profit and loss account gives a true and fair view of the profit and loss or the financial year/ period; Whether the receipts and payments account gives a true and fair view of the receipts and payments for the financial year/ period;

- Whether the financial statements are prepared in accordance with the requirements of the Insurance Act, 1938, the Insurance Regulatory and development Act, 1999 and the Companies Act, 1956, to the extent applicable and in the manner so required;

- Whether investments have been valued in accordance with the provisions of the Act and the specified Regulations;

- Whether 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 the regulations or any order or direction issued by the IRDA in this regard;

- The auditors shall further certify that they have reviewed the management report and there is no apparent mistake or material inconsistencies with the financial statements; the insurer has complied with the terms and conditions of the registration stipulated by the authority;

- The auditors are to specifically certify that: 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;

- They have verified the investments and transactions relating to any trusts undertaken by the insurer as trustee; and 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 relating to the application and investments of the policyholders' funds. Some aspects are specified in their report after verification of assets and liabilities and vouching of revenue and expenditure of the insurance company; and

- In their opinion, the accounting policies selected by the company are appropriate and are in compliance with the applicable accounting standards and with the accounting principles, as prescribed in the IRDA regulations.

Statutory Auditors' Comment

- Reconciliation of inter-office balances and availability of balance confirmations for their necessary comments on certain balances on the financial statements;

- Availability or verification of the historical/weighted average cost of listed and unlisted equity/equity related instruments/ preference shares, the value of which were impaired on or before 31st March 2000 and the consequent impact of impairment losses recognized in Profit and Loss/Revenue account;

- Availability or verification/ reconciliation of reinsurers' balances and balance confirmations and its consequent impact on the financial statements;

- The accounting of Tax Liability in Foreign Countries are proper and in accordance with the Accounting Standard;

- Adequacy of Internal Audit and Control System and corporate governance; and

- Procedure followed for Amortization of expenses on account of Pension, Gratuity and Leave Encashment under Voluntary and whether in accordance with Accounting Standard 15.

Audit of Accounts of Branch Office or Divisional Office

As per the provisions of the Section 228 of the Companies Act 1956 (As amended) the accounts of branch office or divisional office shall be audited by the company's auditor appointed under Section 224 or by a person qualified for appointment as auditor of a company under Section 226, or where the branch office is situated in a country outside India, and the same shall be audited either by the company's auditor or a person qualified as aforesaid or by an accountant duly qualified to act as an auditor of the accounts of the branch in accordance with the laws of the country. Some important aspects, which the branch auditor must consider in devising audit programme for statutory audit of Branch/Divisional, are discussed below.

Examination of Premium Income

The Branch or Divisional Office (DO) auditor is to check the following aspects in respect of premium income booked by the Operating Office (OO):

- Whether premium has been recognized by OO as income over the contract period of risk or the period of risks, whichever is appropriate?
- Whether unearned premium received in advance, which represents premium income not relating to the current accounting period, has been disclosed separately in the financial statements?
- Whether a reserve for unexpired risks has been created as the amount representing that part of the premium written which is attributable to, and to be allocated to the succeeding accounting periods?
- Whether premium Received in Advance, which represents premium received prior to the commencement of the risk, has been separately shown under the head 'Current Liabilities' in the financial statements?

- Whether unearned premium has been shown separately as Current Liabilities. Importantly premium received in advance shall not be included in the unearned premium?

- Whether Premium Deficiency has been recognized when the sum of expected claim costs, related expenses and maintenance costs exceeds related unearned premiums?

- Whether necessary changes based on actuarial/technical evaluation has been made to the liability for contracts exceeding four years?

Examination of Claim Expenses

- Whether the components of the ultimate cost of claims to an insurer comprise the claims under policies and specific claims settlement costs?

- Whether the claims under policies comprise the claims made for losses incurred, and those estimated or anticipated under the policies following a loss occurrence?

- Whether the liability for outstanding claims in respect of both direct business and inward reinsurance business, has been brought to account?

- Whether the accounting estimate includes claims cost adjusted for estimated salvage value if there is sufficient degree of certainty of its realization?

- Whether all the claims have been recorded in books of accounts and not kept outside the books for any reason whatsoever?

- Whether reserves have been made for IBNR and IBNER?

- Whether estimate of claims made in respect of contracts exceeding four years have recognized on an actuarial basis?

- Whether all the claims relating to Health/Mediclaim are transferred from Float account and brooked in claims ledger account? Does the Float account show only the Deposit amount? Steps to be taken to reconcile the same at the year end?

- Whether the TPA claims provisions have been made as per the statements received from the TPA?

Examination of Management Expenses

- Whether the competent authority has approved all management expenses?

- Whether items of Management expenses in excess of one per cent of net premium or Rs 500,000, whichever is higher have been shown separately?

- Whether any expenses of revenue nature have been treated as capital expenditure?

- Whether all expenses incurred, but not paid have duly accounted for under the relevant head and shown separately as current liabilities?

Investments Audit at Corporate Level

- Are the certificates or other documents evidencing the ownership of securities produced?

- Is the method of accounting (e.g. cost or market value) appropriate, having regard to the requirements of the company?

  - o Has the method been consistently applied?

  - o Do the financial statements disclose the method of accounting followed?

Valuation of Investments

Real Estate- Investment Property

- Whether the Investment Property has been measured at historical cost less accumulated depreciation and impairment loss (residual value being considered zero and no revaluation being permissible.)
- Whether the Insurer has assessed at each balance sheet date any impairment of the investment property occurred?
- Whether an impairment loss has been recognized as an expense in the Revenue / Profit and Loss Account immediately?
- Whether the Fair value as at the balance sheet date and the basis of its determination has been disclosed in the basis of its determination has been disclosed in the financial statements as additional information?

Debt Securities

Whether the debt securities including government securities and redeemable preference shares have been considered as “held to maturity” securities and have been measured at historical cost subject to amortization?

Equity Securities and Derivative Instruments

- Whether the listed equity securities and derivative instruments that are traded in active markets have been measured at fair value as at the balance sheet date?
- Whether the insurer has assessed on each balance sheet date whether any impairment of listed equity security, i.e. derivative(s) instruments has occurred? (an active market shall mean a market, where the securities traded are homogenous, availability of willing buyers and willing sellers is normal and the prices are publicly available).

- Whether the unrealized gains/losses arising due to changes in the fair value of listed equity shares and derivative instruments have been taken to equity under the head ' Fair Value Change Account'?
- Whether the profit on sale of investments' or loss on sale of investments', as the case may be, includes accumulated changes in the fair value previously recognized in equity under the heading Fair Value Change Account in respect of a particular security and being recycled to Profit and Loss Account on actual sale of that listed security?
- Whether debit balance in the said Fair Value Change Account has been reduced from the profits/ free reserves while declaring dividends?
- Whether the insurer has assessed, at each balance sheet date, whether any impairment has occurred?
- Whether the impairment loss has been recognized as an expense in Revenue/Profit and Loss Account to the extent of the difference between the remeasured fair value of the security/ investment and its acquisition cost as reduced by any previous impairment loss recognized as expense in Revenue/Profit and Loss Account to the extent of the difference between the remeasured fair value of the security/ investment and its acquisition cost as reduced by any previous impairment loss recognized as expense Revenue/Profit and Loss Account?
- Whether any reversal of impairment loss, earlier recognized in Revenue/Profit and Loss Account has been recognized in Revenue/Profit and Loss Account?
- Whether unlisted and other than actively traded Equity Securities and Derivative Instruments are measured?
- Whether the unlisted equity securities and derivative instruments and listed equity securities and derivative instruments that are not regularly traded in active market have been measured at historical costs?

Common Audit Queries in General Insurance Business

Common Audit Queries at Operating Office Level

Most of the cases may pertain to System and Procedural Lapses in stead of gross financial irregularity or embezzlement and frauds. But the procedural lapses should not be taken lightly. The system lapses should be also viewed by the auditor like financial irregularity and frauds as the said lapses generally in serious consequences such as high operating loss or deficit, high management expenses or acquisition costs and finally erosion of policyholders' funds who do not have any control over the management of insurance business. So the auditor must take serious view of System and Procedural lapses and report upon them. A few examples of system lapses are given below for general understanding:

- Abnormal delay in satisfying Court Award on MACT cases resulting into payment of additional interests;
- Lapses and delay in processing and settlement of claims resulting into improper settlement and affecting customers' service;
- Delay in satisfaction of MACT Awards resulting into extra interest payment;
- Lack of proper follow-up for 34 MACT Recovery Right Cases results into loss of corporate interest and funds;
- Improper Distribution of Survey Jobs resulting into delayed and improper settlement of claims;
- Non-maintenance of Surveyors' Deputation Register results into improper distribution of survey job, lack of claim-monitoring, delayed and improper settlement of claims;
- Short collection of premium

- Settlement of Motor OD Claim Net of Salvage Basis with wrong assessment Salvage

- **Improper Disposal of Salvage:** Instead of disposing the salvage on the Highest bidder for Salvage of Motor OD claim on total loss basis, the salvage remained lying with the repairer who insisted for payment of rent;

- **No Review and Reconciliation of claims file settled by TPA:** Insurers need to make proper reconciliation and verification of claims settled by TPA on regular basis to protect the financial interest of the company;

- **Non-maintenance of Discount Allowed or Business Approval Register**: It is now required to maintain business approval register showing the amount of technical discount allowed and the basis thereof. Please clarify whether you have taken proper action in this regard to ensure prudent underwriting of business as per corporate guide-tariff or underwriting manual.

Common Audit Queries at Corporate Level

- **Deficiency or Inadequacy of Underwriting Plans:** Policy and Guidelines in consideration of underwriting results in terms of growth, profitability and solvency.

- **Deficiency in Reinsurance Policy and Programmes:** This is in consideration of reinsurance results in terms of total cessions, acceptance and capital adequacy.

- **Deficiency in Investing and Financing Activities:** This is in consideration of investment income and Return on investment and dividends payouts.

26

REINSURANCE ACCOUNTING MANUAL-PROCESS & PRACTICE

Reinsurance Accounting - Scope & Objectives

Reinsurance is insurance for insurance companies. It is a transfer of part of the risks that a direct insurer assumes by way of primary insurance contract, to a second insurance carrier called Reinsurer. For such transfer, the reinsured and the reinsurer as per treaty or facultative arrangements share premium and claims. The reinsured also earns commission from reinsurers for his ceding premium with reinsurers at various rates and terms. The reinsured and reinsurers settle balances as per statement of accounts recording all incomes and expenditures being shared by them as per treaty or facultative contracts. Reinsurance accounting is a process of identifying, analyzing and reporting such financial data and results for the various groups of people interested in reinsurance transactions for their various decisions. It is worth-mentioning that reinsurance accounting deals with not only financial aspects but also technical and legal aspects of reinsurance. Reinsurance Accounting process and methods are based on class of business, types and methods of reinsurance, types of arrangements or treaties. We would therefore need to explain fundamental aspects of various treaties like Quota Share, Surplus Treaties and excess of Loss treaties and their impacts on reinsurance accounts.

It is also very important to mention that reinsurance accounting is kept by purchaser of product (the reinsured) for the use of sellers (reinsurers) and other users such as shareholders, Management, Employees, Regulatory Authorities and Taxation Authorities, Brokers, Financial analysts, etc. Reinsurance Accounts are maintained mainly to provide important statistical analysis of financial as well as technical data such as premium, incurred claims, commission, premium reserves, Claims Reserves, Cash calls, various commissions (normal, profit or overriding commission), Taxes and management expenses. With reinsurance accounts the reinsured and reinsurer determine profitability for each and every reinsurance treaty or facultative transactions so that they can decide future reinsurance cover with the best possible rates and terms. Reinsurance accounts also facilitate all periodical reconciliations and settlement of quarterly or periodical balances to avoid undue gains or losses due to fluctuations of exchange rates. It also provides proper mechanism for age-wise analysis of recoverable. Appreciation and analysis Reinsurance Accounting gives rise to following queries, which we need to consider before, we form any opinion thereupon or take any decision therefrom.

- Is profit earned on insurance business is really profit?
- Is Profit on Reinsurance Accounts not a reserve against some future cat liability?
- If one major cat loss in 30 years wipes out entire profits, what should be treatment of taxes?

Reinsurance Accounting — Purpose

Reinsurance benefits the direct insurer in many ways – stabilizing the direct insurer's balance sheet by transferring major part of risks, reducing the probability of his insolvency by assuming catastrophic risks, enlarging his underwriting capacity by accepting a proportional share of risks and enhancing his efficiency with reinsurer's services such as compiling and presenting underwriting data, from sources around the world, evaluating and assessing special risks, and providing loss adjustment support.. All such services of reinsurance are made available with reinsurance accounting records of financial and technical data identified, analyzed and reviewed for reinsurance treaty formation, renewal and settlement. So without proper reinsurance accounts, reinsurance service that is international in character, practice and perspectives in risk transfer technology cannot be properly utilized.

Reinsurance Accounting — Principles & Prerequisites

There is neither any accounting principle, nor any accounting standards that are internationally accepted for reinsurance. Principally reinsurance accounting and its procedures follow the foundation of reinsurance treaty. This article is aimed at dealing with following fundamental areas of reinsurance accounts:

1. Prerequisites for preparation of correct statements of reinsurance accounts;
2. Procedures of recognition of revenue, determination of reserves;
3. Accounting Entries with reference general accounts and final statement of accounts; and
4. Statement of Profit Commission.

Prerequisites

We need to consider following basic requirements of reinsurance accounts:

- Accounting Formats & System
- Reinsurance Portfolio
- Underlying Reinsurance Treaties

All these items are generally specified in reinsurance treaties to avoid confusions or controversies.

Reinsurance Accounting — Formats and Systems

Reinsurance Accounting Formats

There is no standard format of reinsurance accounts that has been globally accepted. Over the years a number of attempts have been made to standardize the Reinsurance Accounts to a global acceptance, but limited success has been achieved so far. Certain examples of accounts are shown hereinafter vis-à-vis various Accounts formats commonly followed for reinsurance accounting all over the world. The reinsurance accounts formats include various treaty accounts, Profit and Loss Statement or Profit Commission Statement.

Reinsurance Accounting Systems

Before one proceeds to prepare accounts and statistics, one must consider which accounting system is to be used as a basis in a specific case. Generally, this is specified in the reinsurance treaty concerned. If it is not specified, an accounting system, which is common in the relevant class of business, will have to be selected. But once an accounting system is chosen, it should not be changed in order to maintain uniformity and consistency. Treaty is blind because everything decided on the results revealed by Accounts. Accounting System is one of the fundamental aspects that help to analyze and interpret the reinsurance results through reinsurance accounts. There are three major accounting systems: a) Accounting Year System; b) Occurrence Year System; and c) Underwriting Year System. Accounting systems determine what premiums or losses should go into accounts and according to which treaty criteria and how. While preparing accounting statements such as Reinsurance Treaty Account, Profit Commission Statement etc., Accounting system determines as to how premium reserves, loss reserves, profit commissions to be determined.

Reinsurance Accounting Year System

In this system, the premiums and losses are entered into the accounts according to the treaty criteria for the relevant accounting year without any break up of income (premium) and expenditure (claims/commission) by year of occurrence or underwriting year. Premium is booked as per due date or premium paid and claims as per date of payment. While preparing Profit Commission Statement and Reinsurance Treaty Accounts on accounting year basis, all transactions are accounted for same treaty period with following debits and credits without reference to underwriting year:

Debit Items	Credit Items
Claims	Premium Reserve
Commissions	Loss Reserve B/F
Miscellaneous Charges	Premiums etc.
Loss Reserve Carried Forward	
Premium Reserve Carried Forward	
Allowance for Re-insurer's Exp Brought Forward	

The reserves mentioned here are not cash reserves, but technical reserves that the ceding insurer may retain from the reinsurer although the same may be replaced by portfolio transfers. Losses payable to the reinsured company are divided between losses already paid by the ceding company and loss reported but unpaid by ceding company. Unearned premium reserves held by the reinsured are similar to loss recoverable from the reinsurer, if reinsurer cancels treaty or becomes insolvent, the unearned premium reserves must be adjusted by ceding company against loss.

Reinsurance Accounting — Occurrence System

In this system premiums and losses are recorded in the accounts according to treaty terms for the relevant year of occurrence with breakdown of losses by year of occurrence. Here premium is booked as per due date or premium paid, but losses are booked according to date of occurrence which is clearly defined for each class of business in the treaty.

Reinsurance Accounting — Underwriting Year System

Under this system, the premiums, losses are entered in the accounts according to the treaty terms for the relevant underwriting years (breakdown of premium and losses by underwriting years).

For calculation of profit for profit commission of the underwriting year and determination of closing balances for periodical settlement, all transactions of an underwriting year are accounted for in the same underwriting year without reference to accounting year. Premium and paid losses are accounted according to the policy period. Generally the preparation of the first statement is deferred until at least one year after the end of the underwriting year. Readjustment statements are then rendered in accordance with treaty terms until all liabilities have expired and been accounted for. Sometimes treaty may provide for closing of accounts after a specified period in order to account for liability and transfer of any outstanding liability to the next open underwriting year. Thus all subsequent transactions for claims or liabilities relating to preceding underwriting years are then included in the profit commission statement and for settlement of periodical balances under Underwriting Year System. Pertinently, no premium reserve or no loss reserve will be brought forward or carried forward unlike calculation of profit commission under accounting year basis to determine the profit commission.

Reinsurance Portfolio

The basis of all reinsurance treaty accounts (with exception of facultative reinsurance) is the reinsurance portfolio as per the terms, definitions and conditions of the reinsurance treaty. Insurance portfolio based on reinsurance treaty includes huge individual risks of distinct classes covered by the treaty. Different portfolios are constructed for different classes of business such as motor, fire, marine, engineering etc. The said portfolio that provides the data on premium, risk, risk date, loss, date of loss, date of payments, is the basic foundation of reinsurance accounting. Insurance portfolio is constructed in many ways. It may be Balanced or Unbalanced portfolio. Balanced Portfolio is one based on many similar and equivalent risks balancing of portfolio losses collectively and distributing proportionately as per terms of treaty. There could be also unbalanced portfolios. Examples of such unbalanced portfolios are those of nuclear power or aviation insurance risks. Here huge risk exposures arise from a relatively small number of objects insured through accumulation of sums insured under property, hull, liability and accident coverage. Such risks cannot be possibly borne by a single insurance or reinsurance company. It necessitates setting up national pools, which retain part of risk exposures for national insurance companies collectively enabling the balance to be reinsured. Table-62 gives some basic ideas and concepts how reinsurance portfolio serves as basis for reinsurance accounts.

Table-62: Reinsurance Portfolio (Marine)

Vessels	SI	Period Date	Due Date	Prem-ium	Loss Date	Loss	Payment Date
Asoke	2,00,000	1.1.05– 31-12-05	1.01.05 1.10.05	5000 5000	—	NIL	—
Victor	4,00,000	1.2.05– 31-01-06	1.02.05	20000	07.4.05	5000	02.08.05
Calcutta	7,50,000	1.4.05– 31-03-06	1.04.05	37500	6.12.05	7500	01.02.06
Bombay	10,00,000	1.7.05– 31-12-05	1.07.05 1.10.05	25000 25000	8.10.05	20000	20.10.05
Madrid	14,00,000	1.9.05– 31-08-06	1.09.05	28000			
Madras	18,00,000	1.01.06– 30-06-06	1.01.06	36000	07.4.06	150000	03.03.07
Singapore	20,00,000	1.01.06– 31.12-06	1.01.06 1.07.06	40000 10000			
Hong Kong	20,00,000	1.01.06– 31.12.06	1.01.06 1.07.06	10000 40000	4.03.06	40000	7.04.06
Total				**281500**		**222500**	

***Note:* This table has been used in examples 4 to 10 hereinafter.**

Underlying Reinsurance Treaties

Accounting entries vary with Methods and Types of reinsurance. Methods are two: Facultative and Obligatory. Types are also two: Proportional and Non-proportional. Table-63 gives the standard accounting entries to be passed for reinsurance accounts.

Table-63: C1 Accounting Entries for Reinsurance Transactions

Transaction	Accepted / Ceded	Debit A/C	Credit A/C
Premium for Current Year	Accepted	Cedant	Premium
Premium for Current Year	Ceded	Premium	Reinsurer
Commission	Accepted	Commission	Cedant
Commission	Ceded	Reinsurer	Commission
Brokerage	Accepted	Brokerage	Broker
Brokerage	Ceded	Brokerage	Broker
Claims Paid	Accepted	Claims	Cedant
Claims Paid	Ceded	Reinsurer	Claims
Portfolio Premium Entry	Accepted	Cedant	Premium
Portfolio Premium Entry	Ceded	Premium	Reinsurer
Portfolio Loss Entry	Accepted	Cedant	Outstanding Claims
Portfolio Loss Entry	Ceded	Outstanding Claims	Reinsurer
Portfolio Premium Withdrawal	Accepted	Premium	Cedant
Portfolio Premium Withdrawal	Ceded	Reinsurer	Premium
Portfolio Loss Withdrawal	Accepted	Outstanding Claims	Cedant
Portfolio Loss Withdrawal	Ceded	Reinsurer	Outstanding Claims
Profit Commission	Accepted	Commission	Cedant
Profit Commission	Ceded	Reinsurer	Commission

Methods and Types of Reinsurance — Facultative Reinsurance and Accounting

Under this method risks are reinsured on individual basis, where the insurer has no obligation to cede a risk in a primary insurance contract and the reinsurer has also the option to of accepting or declining each proposal. When reinsuring facultatively, the insurer may obtain reinsurance coverage before accepting risks of the insured. Facultative reinsurance may be either proportional or non-proportional. Accounting entries are same irrespective of methods and types of reinsurance. What is to be specially considered here is distribution of premium and claims as per arrangement. Generally premium is booked under this method on net of commission basis. However some Facultative Obligatory treaty may provide for some commission, which is substantially less than the quota share and surplus treaty because of the simple fact that premium paid under this treaty is very less compared to loss exposure.

What is Facultative Obligatory?

It is a contract of reinsurance whereby the ceding company may cede risks of any agreed class of insurance, which the reinsurer must accept if ceded. This form is thus a combination of facultative and treaty norms.

What is Treaty or Obligatory Reinsurance?

In treaty or obligatory reinsurance, the direct insurer is obliged to cede to the reinsurer an agreed share of the risks defined in the treaty. The reinsurer is obliged to accept that share. He cannot refuse to accept the risks falling within the scope of the treaty. As a rule obligatory reinsurance treaties are terminable on an annual basis in view of treaty results or other factors. Treaty reinsurances may be proportional or non-proportional. Proportional reinsurance treaties are Surplus treaty and Quota share. Non-proportional reinsurance treaties are Excess of Loss (XOL) and Excess of Loss Ratio (Stop Loss).

Quota Share Treaty and Reinsurance Accounting

The quota share treaty is an automatic reinsurance whereby the ceding company is bound to part with a fixed percentage of every risk written by it. The same percentage is applied to each and every risk to determine cession in the class of insurance as reinsured. It is immaterial how large or small is the sum insured or how good or bad the risk is. This is different from surplus method where the percentage reinsured varies with each risk according to the underwriter's decision in determining the surplus for reinsurance.

Example: 1 *Insurer X entered into an 80 per cent Quota Share Treaty of all fire business written in India. Distribute premium between X and RI for the following fire businesses written by India @ Rs 1 per cent with SI of Rs 500,000, Rs 100,0000, Rs 200,0000 and Rs 400,0000 under Fire Policy 01/07. 02/07, 03/07 & 04/07 (see Table-64)*.

Table-64: Statement Showing Distribution of SI & Premium Business

	A	B	C	D	
Sum-insured	100%	500000	1000000	2000000	4000000
Premium Total	100%	500	1000	2000	4000
Ceding Company	20%	100	200	400	800
Reinsurer	80%	400	800	1600	3200

Let us now examine how Claims will be distributed in a quota Share treaty:

Example: 2 *From the following particulars calculate retention and reinsurance cessions in a 20% quota share treaty entered into by insurer XY with reinsurer RI for 2006 with maximum cession Rs 90,00,000:*

(a) Premium rate 1 per cent

(b) Sum insured of Rs 50,00,000 with claim of Rs 44,00,000

(c) Sum insured of Rs 110,00,000 with claim Rs 1,000 only

(d) Sum insured of Rs 600,00,000 with claim Rs 6,00,000

Answer: Accounting Statement showing distribution of SI, Premium and Claims

1. SI Distribution

	SI	**Retention**	**Quota Cession**	**Fac SI**
a.	50,00,000	40,00,000-80%	10,00,000-20%	NIL
b.	110,00,000	88,00,000-80%	22,00,000-20%	NIL
c.	600,00,000	480,00,000-80%	90,00,000-15%	30,00,000-5%

2. Premium Distribution

	Total Premium	**Retention**	**Cession**	**Fac Share**
a.	50,000	40,000- 80%	10,000-20%	NIL
b.	1,10,000	88,000-80%	22,000-20%	NI
c.	6,00,000	4,80,000-80%	90,000 – 15%	30,000

3. Claim Distribution

	Total Claim	**Retention**	**Cession**	**Fac Share**
a.	4000000	3200000-80%	8,00,000-20%	NIL
b.	1,000	800 – 80%	200 – 20%	NIL
c.	600000	480000-80%	90,000-15%	30,000-5%

Example: 3 Quota Share Reinsurance Accounting

Let us now prepare Quota Share Reinsurance Accounting of XYZ Insurer Ltd. Mumbai, for the accounting transactions as reflected in Reinsurance Portfolio specified in Table 1 shown earlier using following Quota Share Treaty with Bharat Reinsurer Ltd, Mumbai.

Table-65: Marine Quota Share Treaty

Portfolio	As per Insurance Portfolio specified in Table-63
Treaty Inception	01.01.2005
Reinsurance share	40 per cent with Bharat Reinsurer, 40 per cent others; 20 per cent retention by XYZ
Proportional Cover	Sum-insured 2000000; Bharat Reinsurer max. liability 800000
Management Exp.	5 per cent
Commission	22.5 per cent
Profit Commission	Sliding Scale Profit Commission 30 per cent Profit Commission on profit up to 10 of premium booked 40 per cent Profit Commission on profit 10-20 per cent of premium booked 50 per cent Profit Commission on rest of profit Losses carried forward to extinction
Accounts	Underwriting Year Basis; Half-yearly A/Cs Statement Closing of books on 31 December Deadlines-60 days; Confirmation – 30 days Settlement; 30 days by both parties; Accounting Currency and Payment Currency-INR Set-off permitted with all balances
Loss Reserves	100 per cent

Example: 4 Statement of Account for 1st half year 2005 may be prepared in the following format taking premium and claims specified in earlier Table-64.

XYZ Ins. Co. Ltd
Mumbai

Bharat Reinsurer Ltd
Mumbai

Reinsurance Treaty	Marine Quota Share
Accounting Period	1st Half Year, 2005
Accounting System	Underwriting Year
Accounting Currency	INR

100 per cent figures accounted for

Table-66: Statement of Account

Particulars	**Treaty Year**	**Debit Amt.**	**Credit Amt.**
Premiums (5000+20000+37500)	2005	–	62500.00
Commission 22.5 per cent	DO	14062.50	
Paid Claims		–	
		48437.50	–
		62500.00	62500.00
Bharat's 40 per cent reinsurance Share	40 per cent		19375.00

Example: 5 Statement of Account for 2nd half year 2005 may be prepared in the following format taking premium and claims specified in Table-63.

XYZ Ins. Co. Ltd.
Mumbai

Bharat Reinsurer Ltd
Mumbai

Reinsurance Treaty	Marine Quota Share
Accounting Period	2nd Half Year, 2005

Accounting System Underwriting Year

Accounting Currency INR

100 per cent figures accounted for

Table-67: Statement of Account

Particulars	Treaty Year	Debit Amt.	Credit Amt.
Premiums (5000+ 25000+25000+28000)	2005	–	83000.00
Commission 22.5 per cent	DO	18675.00	
Paid Claims (Payment—2.8.05 & 11.10.05)	DO	25000.00	
Balance		39325.00	—
		83000.00	83000.00
Bharat's 40 per cent reinsurance share	40 per cent		15730.00

Example: 6 Statement of Account for 1st half year 2006 may be prepared in the following format taking premium and claims specified in Table-63.

XYZ Ins. Co. Ltd. **Bharat Reinsurer Ltd**
Mumbai **Mumbai**

Reinsurance Treaty Marine Quota Share

Accounting Period 1st Half Year, 2006

Accounting System Underwriting Year

Accounting Currency INR

100 per cent figures accounted for

Table-68: Statement of Account

Particulars	Treaty Year	Debit Amt.	Credit Amt.
Premiums	2006	-	86000.00
Commission 22.5 per cent	DO	19350.00	
Paid Claims (Payment—1.2.06)	2005	7500.00	
Balance		59150.00	—
		86000.00	86000.00
Bharat's 40 per cent reinsurance Share	40 per cent		23660.00

Example: 8 Statement of Account for 2nd half year 2006 may be prepared in the following format taking premium and claims specified in Table-68.

XYZ Ins. Co. Ltd	**Bharat Reinsurer Ltd**
Mumbai	**Mumbai**
Reinsurance Treaty	Marine Quota Share
Accounting Period	2nd Half Year, 2006
Accounting System	Underwriting Year
Accounting Currency	INR

100 per cent figures accounted for

Table-69: Statement of Account

Particulars	Treaty Year	Debit Amt.	Credit Amt.
Premiums	2006	-	50000.00
Commission 22.5 per cent	DO	11250.00	
Paid Claims	DO	40000.00	
Balance			1250.00
		51250.00	51250.00
Bharat's 40 per cent reinsurance Share			23660.00

Example: 9 Now let us now prepare Profit and Loss statement as on 31st December 2005 on the basis of reinsurance Accounts transactions recorded in the above noted Half-yearly Accounts following data specified in Table-63 and Quota Share Treaty shown in Table-69.

Profit and Loss statement as on 31.12.2005

XYZ Ins. Co. Ltd	**Bharat Reinsurer Ltd**
Mumbai	**Mumbai**
Reinsurance Treaty	Marine Quota Share
Accounting Period	2005
Accounting System	Underwriting Year
Accounting Currency	INR
100 per cent figures	

Table-70: Statement of Account

Premiums	**Debit Amt.**	**Credit Amt.**	145500.00
Commission		32 737.50	
Paid Claims		25000.00	
Loss Reserves 100 per cent		7500.00	
Mgmt. Expenses 5 per cent		7275.00	
Profit		72987.50	
		145500.00	**145500.00**
Calculation of Profit Commission	**Profit**	**Debit**	**Credit**
30 per cent profit commission up to 10 per cent of Premium	14550	4365.00	
40 per centprofit commission for another 10 per cent of premium	14550	5820.00	
50 per cent profit commission for the balance profit	43887.50	21944.00	
Profit Commission			32129.00
		32129.00	**32129.00**

Example: 10 Now let us now prepare Profit and Loss statement as on 31st December 2006 on the basis of reinsurance Accounts transactions recorded in the above noted Half-yearly Accounts following data specified in Table-63 and Quota Share Treaty shown in Table-70.

Profit and Loss statement as on 31.12.2006

XYZ Ins. Co. Ltd Mumbai	**Bharat Reinsurer Ltd Mumbai**
Reinsurance Treaty	Marine Quota Share
Accounting Period	2006
Accounting System	Underwriting Year
Accounting Currency	INR
100 per cent figures	

Table-71: Statement of Account

Premiums	**Debit Amt.**	**Credit Amt.**	**145500.00**
Commission		32737.50	
Paid Claims		40000.00	
Loss Reserves 100 per cent			
Mgmt. Expenses 5 per cent		7275.00	
Profit		*65487.50*	
		145500.00	**145500.00**
Calculation of Profit Commission	**Profit**	**Debit**	**Credit**
30% profit commission up to 10 per cent of Premium	14550	4365.00	
40%profit commission for another 10 per cent of premium	14550	5820.00	
50 per cent profit commission for the balance profit	36387.50	18194.00	
Profit Commission			28379.00
		28379.00	**28379.00**

Note: *As in 2006 transactions, there is no change other than paid claims which correspond with the aggregate of paid claims and Loss reserves (25000+7500).*

Example-11 Accounting treatment in General Accounts vis-à-vis Reinsurance Accounts

Reinsurer—M/s Universal Reinsurance Co Ltd
Half Yearly **Profit & Loss Statement** As on 30th June 2003
Reinsurance Treaty: Quota Share; **Treaty Year**: 1st Half '03

Table-72: Accounting System — Underwriting Year Class of Business (Marine)

Particulars	%		Debit Amt	Credit Amt.	Remarks
Portfolio Premium Entry	35	Ceded		8000000	Debit-Premium A/c
Portfolio Loss Entry		*O/s claim*		5000000	Debit-O/s Claim
Premium for Current year*				40000000	Debit-Premium A/c
Commission	40	Premium	16000000		Credit-Com A/c
Claims Paid			6000000		Credit-Claim A/c
			—		Credit -Bank
Expenses of Management	2.5	Premium	1000000		Credit- M/Exp
Portfolio Premium Withdrawal	35	Premium	14000000		Credit-Premium A/c
Portfolio Loss Withdrawal		*O/s claim*	7000000		Credit-O/s Claim
Balance being profit			9000000		
			53000000	**53000000**	
Profit b/d				8000000	
Profit Commission	20		1600000		

*Premium: Refer Table-63 for Portfolio. Total of first four items

Surplus Reinsurance

Under the surplus treaty the ceding insurer (direct insurer) decides the limit of liability which he wants to retain on any one risk or class of risk. This limit is called as retention limit but may also actually retain lesser amount as commensurate to his risk exposure. The surplus over and above this retention is allotted to one or more insurer, e.g. a ceding insurer's maximum retention limit may be Rs 2,00,000 on fire insurance covering all cotton mills, jute mills and flour mills. Distribution of sum insured between direct insurer and re-insurer is shown in Table-73.

Table-73: Share of Insurance and Reinsurance

Risk	Total SI	Insurance share		Reinsurance share	
ABC	100000	100%	100000	0%	Nil
BCD	200000	100%	200000	0%	Nil
CDE	300000	66.67%	200000	33.33%	100000
DEF	400000	50%	200000	50%	200000
EFG	500000	40%	200000	60%	300000
FGH	600000	33.33%	200000	67.67%	400000
GHI	1000000	20%	200000	80%	800000
HIJ	2000000	10%	200000	90%	1800000

Surplus Treaty

Generally, the amount ceded to a surplus treaty is expressed in the number of lines. For example, a line is equal to the ceding company's retention, e.g. if a ceding insurer has a 5 lines surplus treaty on the basis of a maximum retention limit of Rs 1,00,000 the capacity of the treaty to accept the liability over and above the retention would be Rs 5,00,000 (5 x Rs 1,00,000) and the ceding insurer would have the treaty protection for policy having sum insured up to Rs 6,00,000 where the ceding insurer issued policies for the sum insured exceeding the limits of treaty, i.e. Rs 6,00,000, he has the option either to bear the balance in his own account (in addition to his existing retention) or he may effect further reinsurance. Such excess balance may be reinsured either facultatively or by any other surplus treaty automatically. Such further surplus treaty is called Second Surplus treaty. Surplus Treaty accounting incorporating above example is done in the following manner under the accounting year system:

Example: 12 Any Insurance Co., 9, Nowhere Street,

No city in India

Portfolio	Marine as mentioned above
Treaty inception	1st January 2004
Reinsurance share	5 lines surplus treaty
Proportional cover	500,000 and 100,000 = 1 line
Commission	30 per cent + 0.5 per cent if loss ratio < 42.5 per cent + up to 7.5 per cent if loss ratio < 28.5 per cent Difference: 0.5 per cent commission for 1 per cent loss ratio Provisional commission during the year: 32.5 per cent
Profit commission	Management expenses 3 per cent Profit commission 20 per cent
Rendering of accounts	Closing of books at 31st December Deadlines: rendering of accounts 60 days, Accounting currency INR Payment currency INR
Unearned premium reserve	40 per cent
Loss reserves	Are entered at 100 per cent

Example: 13 A Specimen of Surplus Treaty

Ceding Company:	X Insurance Co. Ltd
Reinsure:	Y Reinsurance Co. Ltd

Treaty: First Surplus Fire Treaty # Period 1st Qtr.2003

Reinsurance Share: 40%

Table-74: Surplus Treaty

	Debit	Credit
Portfolio Premium Entry (1-1-2003)		7000000
Portfolio Loss Entry (1-1-2003)		6000000
Premium (1st Qtr)		6000000
Commission 40%	2600000	
Taxes & Charges	200000	
Claims Paid	5000000	
Premium Reserve retained 40%	2400000	
Credit For Cash Loss		200000
Portfolio Loss Entry	7000000	
Balance due to Reinsurer	2000000	
	19200000	19200000

Notes on Accounts

Reinsurance Premium: What is premium is determined as per local practice, terms of contract, and class of business. In some market, premium means gross premium and expenses, fees taxes are accounted separately (see Example 12) while in other cases marine and aviation business it is accounted on net basis (see Example 13). Consequently commission amount becomes relatively less in the second case.

Reinsurance Commission: Reinsurance Commission is paid by the re-insurer to the ceding (direct) insurer and is decided as per cent of premium for reimbursement of acquisition cost (agency commission) and management expenses. Reinsurance Commission is calculated by applying the agreed per cent of commission to the premium ceded less returns and cancellation. Different rates are decided for different class of business. Again this rate may be either fixed or sliding scale. Under sliding scale rate of commission is based on the loss ratio of treaty during a treaty year or during any one accounting year as per uniform practice. As we know, loss ratio is usually calculated as per cent of incurred claim on premium. For example, if incurred claim is Rs 50,000 and premium is Rs 100,000, then loss ratio is 50 per cent. A treaty may provide following type of sliding scale commission (example):

Rate of	commission	30%	if Loss	ratio	is 65% or more
"	"	35%	"	"	is below 65%
"	"	36%	"	"	is below 64%
"	"	37%	"	"	is below 63%
"	"	38%	"	"	is below 62%
"	"	39%	"	"	is below 61%
"	"	40%	"	"	is below 60%
"	"	41%	"	"	is below 59% and so on.

Profit Commission: Profit commission is an additional commission percentage payable to a ceding insurer on profitable treaties in accordance with an agreed formula. It is therefore an incentive for ceding insurers to produce profitable business. There are two types of profit commission statements: Statements on accounting year basis and Statement on Underwriting Year basis. Fire and Accidental proportional treaties are usually on an accounting year basis while Marine and aviation on underwriting year basis. Generally only proportional treaties provide for profit commission and non-proportional treaties rarely contains profit commission clause. When a treaty provides for profit commission, the ceding insurer must prepare profit commission statement to see whether the treaty is showing profit or loss.

Profit Commission on Accounting Year Basis: A profit commission on Accounting Year Basis requires all transactions for the same treaty period without reference to underwriting year, to be accounted for in the same profit commission statement. A typical example would include the Debit Items like Claims, Commissions, Miscellaneous Charges, Premium Reserve Carried Forward, Loss Reserve Carried Forward, allowance for Re-insurer's Exp and Credit Items like Premium Reserve Brought Forward, Loss Reserve Brought Forward, and Premiums etc. An example (E.3) of Profit Commission statement on accounting year basis is provided hereinafter.

Profit Commission on Underwriting Year Basis: All transactions of an underwriting year, without having regard for Accounting Year, are accounted for determining profit for that underwriting year for commission computation. When this sort of commission statement is considered, the preparation of the first statement is deferred until one year after the end of the underwriting year. Readjustment statements are then rendered in accordance with treaty terms for various liabilities occurred. Every treaty contains a detailed provisions in regard to close of an accounting year ‘s accounts after a specified period, transfer of any outstanding liability to the next open underwriting year so as to cover all subsequent transactions relating to all preceding underwriting years for determining profit commission.

Aggregate Annual Profit: Where a treaty covers more than one currency or class of business, it is a normal practice to combine the results of each section of the treaty or the results of more than one treaty to determine the aggregate annual profit for calculation of profit commission.

Example: 14. Profit Commission Statement on Accounting Year Basis from 1st January 2003 to 31st December 2003

Table-75: First Surplus Fire Treaty with Y Re-insurer

Particulars	Dr. Amount	Cr. Amount
Premium Reserve B/f (Portfolio entry) as on 1.1.03		8000000
Loss Reserve B/F (Portfolio entry) as on 1.1.03		7000000
Premium		20000000
Commission 45%	9000000	

Claims Paid	6000000	
Taxes & Charges	500000	
Management exp. 2.5%	500000	
Premium Portfolio Withdrawal 35% as on 31.12.03	7000000	
Loss Portfolio Withdrawal 35% as on 31.12.03	8000000	
Profit for the year 2003	4000000	
	35000000	35000000
Average Profit		
Profit for 2003 4000000		
Profit for 2002 6000000		
Profit for 2001 1000000		
Average Profit 3000000		
Profit Commission say 20% (as per treaty)		600000

Example: 15. Profit Commission Statement on Underwriting Year Basis Profit Commission Statement for the period from 1st January 2004 to 31st December 2004 of X Insurance Company Ltd.

Table-76: Marine Quota Share Treaty with Y Re-insurer

Particulars	**Dr. amount**	**Cr. Amount**
Premium Reserve B/f (Portfolio entry) as on 1.1.04		7000.00
Loss Reserve B/F (Portfolio entry) as on 1.1.04		1000.00
Premium		15000.00
Commission 45%	6750.00	

Claims Paid	2500.00	
Taxes & Charges	500.00	
Management exp. 5%	750.00	
Premium Portfolio Withdrawal 50% as on 31.12.04	7500.00	
Loss Portfolio Withdrawal as on 31.12.04	3000.00	
Profit for the year 2004	2000.00	
	23000.00	23000.00
Calculation of profit commission - 100%		
30% profit commission - up to 10% of premium - 1500.00	450.00	
40% profit commission - balance 10% of premium 200.00	80.00	
	2000.00	
Total Profit Commission	530.00	

Example-16: Excess of Loss Treaty and Reinsurance Accounting

Table-77: Excess of Loss Treaty for Rs 9,50,000
Excess Rs 50,000

Year	Premium (Rs)	Claims to be Accounted for
2000	8,00,000→	1 claim of Rs. 60,000/- paid. Rs. 10,000/- loss to treaty
2001	9,00,000→	1 of 2000 of which Rs. 30,000/- paid and Rs. 90,000/- outstanding. i.e. Rs. 70,000/- to treaty.
	→	1 of 2000 Rs. 40,000/- paid and Rs. 20,000/- outstanding i.e. Rs.10,000/- to treaty.

	→	1 of 2001 Rs. 70,000/- paid i.e. 2000 to treaty.
2002	10,00,000→	1 of 2000 estimated Rs. 2,40,000/- i.e. Rs. 1,90,000/- to treaty
	→	3 of 2001 estimated to Rs. 80000/- Rs.1,25,000/- & Rs.180000/- i.e. Rs. 30,000/-, Rs. 75,000/- & Rs. 1,30,000/- to treaty
2003	12,00,000→	1 of 2000 estimated loss Rs.1,00,000/- i.e. Rs. 50,000/- to treaty
	→	2 of 2001 estimated loss Rs.2,90,000/- & Rs.1,25,000/- i.e. Rs.2,40,000/- & Rs.75,000/- to treaty.
	→	1 of 2002 estimated loss Rs.180000/- i.e. Rs.130000/- to treaty
2004	15,00,000→	1 of 2001 estimated loss Rs.170000/- i.e. Rs.120000/- to treaty
	→	2 of 2002 estimated loss Rs.310000/- & Rs.180000/- i.e. Rs.260000/- & Rs. 130000/- to treaty
	→	1 of 2003 estimated loss Rs.190000/- i.e. Rs.140000/- to treaty.

The percentage shown in Table-77 gives the cost of claims to be debited to the reinsurance account during these years. These percentages are referred to as the burning cost. Sometimes, an average is taken of the above percentages and the loading was added to cover to reinsurance expenses and profit. Sometimes reinsurance accounts based on the above percentage may not consider certain aspects such as: i) claims still outstanding; ii) IBNR Claims increasing court awards and inflationary effect. So, while computing the burning cost, all these aspects should be considered with due adjustments to the accounting results.

Statutory Accounting Provisions for Certain Reinsurance Recoverable

- Unsecured Recoverable from unauthorized reinsurers,
- Unsecured Recoverable from slow-paying (authorized) reinsurers,
- Overdue Recoverable from both authorized and unauthorized reinsurers, and
- Recoverable Others in dispute from unauthorized reinsurers and from non-slow-paying authorized reinsurers.

On the statutory balance sheet, **Reinsurance Recoverable on paid losses** and loss adjustment plus expenses are shown as an asset. **Reinsurance Recoverable on unpaid losses** and loss adjustment expenses are shown as a contra-liability to gross unpaid losses and loss adjustment expenses. Ceded unearned premium *reserves* are shown as a contra-liability to gross unearned premium reserves. The provision for reinsurance is a liability that relates to all of these items.

27

Role and Opportunities for Chartered Accountants in Insurance Industry

Scope and Opportunities for CAs

Indian Insurance sector which has been in a robust growth track since opening up of the industry to the private and global, this sector offers enormous scope and opportunities for chartered accountants in various roles or capacities. Currently, industry growth is much ahead of GDP growth of the country. In 2009-10, life insurance business grew by 25 per cent and general insurance business by 14 per cent. Life insurance companies collected record premium of Rs 1,09,290 crore in fresh business while non-life insurance collected premium of Rs 34,627crores. With this sort of high growth track, the sector is set to create enormous opportunities of both employment and professional services for all types of professionally qualified people today and tomorrow. Precisely, the liberalization of insurance industry has not only enabled stiff growth in the sector with the entry of multinational giants, but also widened the scope and opportunities of professionals like engineers, chartered accountants, lawyers and MBAs in the industry. In this chapter, we discuss how to identify the scopes and opportunities for CAs along with their roles and responsibilities in the respective capacities in the insurance industry.

Chartered Accountants as Insurance Managers

Now almost all insurance companies are recruiting hundreds of professionally qualified people like Engineers, CAs, and MBAs for managing their business expansion and rapid growth. In consideration of critical and technical aspects in business operations, the prospects and scope of professional services are more in general insurance business compared to life insurance business. The growth of general insurance industry is directly linked with the economy both national and international. If economy grows by 9 per cent, the insurance business is bound to grow substantially. For example, motor insurance grew more than 12 per cent and health insurance by 30 per cent in the last financial year. Unlike in fiscal in 2009-10, there was upswing in Fire and Engineering Insurance also. Such growth of business in all companies is not only enhancing the scope of audits in size and number, but also increasing audit fees substantially. Growth of Fire and Engineering Insurance demands more professional services.

Most of the non-life companies are looking into 13-15 per cent business growth in consideration of growing Indian Economy. For example, New India, the largest non-life insurance company in India is projecting for Rs 10,000 crores in 2012-13 with 15 per cent annual growth. Some of the PSU general insurance companies are having surplus capacity, i.e. over-capitalization. To manage rapid business growth as well as to utilize surplus capacity, the insurance companies are required to recruit more and more insurance managers with professional knowledge and qualifications where Chartered Accountancy is considered very important professional qualification is a financial sector.

Responsibilities of a CA as an Insurance Manager

As insurance manager, CA is to manage risk inspection, risk analysis, business underwriting, marketing management claims management, customer service management, management information system, personnel management, accounts and financial management, internal control, audit and management audit, investment portfolio management, IT service management, etc. Now technology is in a constant state of transition. In insurance management the pace of technology change is very fast – both in business management and risk management. Today most of the insurance companies have adopted web-based core insurance system solution. For example, in New India core insurance known as Customer Web-based Insurance System Solution (CWISS) for underwriting and marketing of almost all products is in place. To that end they need to go further extra miles and stay ahead to achieve further business growth and greater penetration, which is must for the insurance sector to be really effective and useful to the larger segment of the society.

Today insurance penetration of general sector is only 0.6 per cent, the vast market has remained untapped due to want of professional insurance management and lack of real competitive environment. To ensure greater insurance penetration and make the sector really known for the service with its customized products and service with affordable price, greater competition and more employment professionals like CAs, MBAs, and engineers are indispensable. As insurance is financial institution, the scope of employment of CAs is really huge in various capacities, as the services of this sector are still beyond the reach or knowledge of the common mass of the society, insurance has not become so attractive to many professionals including CAs. This sector has huge potential for all professionals.

Today the major challenges faced by most of the insurance companies are proper product development, appropriate investment portfolio management, speedy claims management and loss prevention in line with insurance cycle movement and stringent regulatory framework. CAs , as the experience goes, are best-suited to offer their service with specialized knowledge of accounts, finance and commercial laws and professional skills to meet the challenges of the insurance management. It is not out of place to mention that during the period from 2005 to 2009 all four PSU general insurance giants in India were headed by CAs as CEOs, who could bring the industry to the new heights of growth with profitability.

Chartered Accountant as Statutory Auditor

A large number of CAs are engaged in and associated with the insurance industry as statutory auditors. With rapid expansion of insurance business, the scope of CAs as statutory auditors is also increasing substantially. Here let us analyze in brief as to how the roles and responsibilities of CAs (discussed in Chapter-25) are becoming complex in the growing complexities of the industries in the regulated and highly sophisticated IT environment. The issuance of new regulations with frequent amendments in earlier regulations aiming at protection of policyholders' interests and the use of more and more sophisticated information technology have widened both opportunities and responsibilities of chartered accountants in the industry. To play their roles as statutory auditors, the chartered accountants must have following attributes:

- Proper understanding of complexities of insurance operations;
- Knowledge of insurance core functions being underwriting, claim processing, investment and accounts;
- Knowledge of industry regulations, legal and other external factors;
- Application of accounting policies, accounting standards; and
- Understanding of internal control systems and its major components.

Chartered Accountants as Internal Auditors

Internal audits or management audits in insurance companies are at present mostly carried out by their employees of the internal audit department. The internal audit department of an insurance company carries out such audit covering mainly business underwriting, claims settlement, management expenses payment, etc., in accordance with corporate manual without having much regard for the best practices of internal audit keeping in view of significant developments occurring in Indian insurance sector functioning with internal standard. In the post liberalization period, Indian insurance sector is going global in all respects including business operations, cross-border capital raising, overseas investments, etc. They have had little care and exposure to the impact of transition to IFRS implementation or convergence. Though they are required to bring the issues and impact to the corporate management on top priority for the thoughtful consideration of the audit committee and the board of directors.

Though the determination of the ways and impact of transition or convergence to IFRS and the responsibilities of making accounting treatment and necessary disclosures come within the purview of the Accounts, Finance and Taxation departments in the company, the entire process of providing guidelines do come under the roles and responsibilities of the internal auditor. But the internal auditors may not be able to meet such new challenge, unless they are professionally qualified accountants or auditors. Thus in the changed environment the role and opportunities the CAs as internal auditors are really immense and such opportunities will get wider as the sector is growing very today. If the Development Committee of the Institute takes up the matter with the IRDA or Authorities of the insurance sector, the internal audit may be assigned by the individual insurance companies to the professional CAs.

Responsibilities of CAs as Internal Auditors

If internal audits are conducted by CA Firms they may look into the following important aspects and report to the management of various discrepancies and deviations from the standards set by the management:

- **Underwriting Audit** covering Risk Analysis, Risk Acceptance, Rating, Risk Conditioning, Risk Transfer and Review of Underwriting Policy;

- **Revenue Audit** covering collection of premium as per company's manual and guidelines, deposit of premium before acceptance of premium, recognition of premium and treatment of advance premium;

- **Management Expenses audit & budgetary control** vouching and examining management expenses as per corporate norms and guidelines, budgetary limits and sanction and as per financial power and limits laid down in the Financial Order approved by the Board of directors;

- **Claim Audits** asking for verification of claims payment with reference to companies' manual, policy terms and conditions, legal provisions of the applicable statutes or enactments. During claim payment audit auditors shall pay special attention to admissibility of claim with reference to perils covered, perils excluded, perils uninsured, compliance of policy conditions and warranties, relevant legal aspects such as provisions of Marine Insurance Act in case of Marine Claims, Provisions of the Public Liability Act in case of liability claims under the Act, provisions of the Workmen Compensation Act in case WC Claim or employer's liability claim, the provisions of Motor Vehicles Act and the relevant court awards in case of Motor Third Part claims etc. The internal auditor shall thoroughly examine the assessment of claims with reference to the sum-insured, actual loss incurred either on market value or reinstatement value as per terms of the policy, salvage recovered, policy excess, documentary evidence &books of accounts, audit reports if any, other evidences according to the merits of the case. The auditors also see that all claims are being promptly settled for the purpose of loss prevention and avoidance of exaggeration of loss. He also verifies that claims have been registered immediately and have not remained pending for settlement for unreasonable period due to non-submission of survey reports or ambiguity in survey reports. They also verify the claims referred to consumer forums, State Commission or National Commissions or courts. They are to examine thoroughly examine all such legal claims with reference to complaints or demand of the petitioners, policy terms and conditions, defense taken in the court, opinion of the advocate, auditor's opinion on handling the court matter;

- **Cash Management** is for anking of cash premium collection, fund transfer, balance in current accounts-whether more than optimal, whether there is any old cases of cheques deposited, but not collected/credited;

- **Capital Expenditure & Fixed Assets Audit** intends that the auditors verify that all fixed assets are acquired or capital expenditure has been incurred only on approval of the competent authority as per corporate norms and procedures. Fixed assets have been maintained with all required details indicating existence at specified location, year of purchase, value of the property, control no, date of physical verification by the management etc;

- **Reinsurance Audit** is the verification of reinsurance treaty results and faculty arrangements with reference to capacity retention, actual retention, review of reinsurance programme and reinsurance treaty and review of Reinsurance Policy.

As Indian insurance sector is today operating in more complex and competitive situations internal audit in insurance companies is gaining a steadily higher profile and it is expected to assure the management always that the key risks within an organization are being well managed through the principles and process of enterprise risk management. The role of the internal auditor in insurance company is to provide assurance to management that all key risks are being managed effectively. To do this, the internal auditor will evaluate the quality of risk assumption processes (business acceptance), systems of internal control and corporate governance processes, across all parts of an organization and report this directly and independently to the most senior level of management. Internal auditors need to assist the top management to identify key performance areas (KPA) of the organization, department, and identify the relevant risk factors and assess their significance. Changing trends and business/economic conditions impact the way the internal auditor assesses risk and report the same to the management for corrective measures assuring reduction of probability of operating loss. The techniques of internal auditing need to be changed from a reactive and control based approach to a more proactive and risk based approach. This enables the internal auditor to anticipate possible future concerns and opportunities as well as identifying current issues.

All these demand that like statutory auditors, internal auditors also must have professional qualifications, knowledge, skills and technical standards and codes of conduct, which the company's own department personnel might not have to the fullest extent. So both the insurance companies, the regulator and our institute may give due consideration for full-fledged implementation of practice of internal audit by the firm of chartered accountants to make the internal audit transform into proactive and risk based approach from reactive form. Internal auditors typically issue reports at the end of each audit with their findings, recommendations, and any responses or action plans from management to earlier findings and recommendations. Recently, the insurance regulator has taken a step forward in this regard by introducing concurrent audit in insurance sector. The regulator has mandated the insurance companies (both life and general business) to get their investment transactions audited by chartered accountants. As per recent amendment in Investment Regulation of IRDA, insurance firms will have to get their investment transactions and related systems audited at least once in three years in certain situations as elaborated below.

CAs as Concurrent Auditor for Investment Functions

The IRDA vide its circular dated 22nd August 2009, has mandated the insurance companies (both life and general business) to appoint a firm of CAs as concurrent auditor to get their investment transactions and related systems audited at least once in three years where Assets Under Management (AUM) comprising shareholders' funds and policyholders' funds exceed Rs 1000 crore. Other insurers have an option to get their investment transactions and related system audited either through internal resources (internal auditor) or by a firm of chartered accountants on a quarterly basis.

As we know, concurrent audit is a systematic and timely examination of financial transactions on a regular basis to ensure accuracy and compliance with procedure and guidelines. Concurrent audit is carried out concurrently with the occurrence of financial transactions. Concurrent Audit is an examination, which is contemporaneous with the occurrence of transactions. It attempts to shorten the time-lag between a transaction and its examination by an independent person not involved in the occurrence of the transaction and its documentation. It puts an emphasis on substantive checking in key areas rather than on test checking in almost all functions of the entity.

There is a difference between internal audit and concurrent audit. The scope and coverage of internal audit are much more comprehensive and of wide range as discussed above compared to concurrent audit which is very specific in nature, periodicity and process being discussed herein after for concurrent audit for investment transactions of insurance companies. The proposed concurrent audit system, which is exhaustive in operation, looks into investments transactions and risk analysis and risk evaluation of investment functions keeping in view of corporate policy of investment and protection of the policyholders' funds. It will also ensure that the companies comply with IRDA's investment guidelines.

Responsibilities of Concurrent Investment Audit

- The main objective of concurrent audit is to provide safety mechanism to policyholders' funds which are considerably huge in size and complex in nature for management of funds ensuring solvency, i.e. the ability to pay claims both maturity and accidental.

- The concurrent auditor is to verify that all investment functions of the investment department are as per corporate investment policy approved by the Board and the corporate policy is in accordance with the prescribed provisions of the specified regulations.

- If the auditor finds any deviation in the operation of the investment department from the Board approved policies, such deviations with their observation shall be brought to the notice of the Audit Committee of the Company. The auditor shall also report the serious observations instantly to the management to take immediate steps to prevent the recurrence of the incidents.

- As per IRDA a concurrent auditor will "ensure the availability of all risk management principles. Hence from risk management view point, this is an important step". One firm cannot be a concurrent auditor of more than two companies.

- The investment departments of Insurance companies manage huge investments comprising of both Shareholders' and Policyholders' funds of the companies according to laid down investment policy and guidelines. Such fund management involves critical financial risk management exposed to severe financial loss especially when the financial market is very volatile like now. It is essential that a periodic review of such investment is carried out through Internal Audit (or) Concurrent Audit in a professional manner and standard in order to ensure the safety of the funds and a good quality Investment portfolio that could support the solvency requirements and protect the policyholders' interests.

CAs in the Role for Risk Inspection & Risk Evaluation

Though insurance sector has been in excellent growth zone, non-life insurance companies have been operating with very low or negative underwriting surplus since long all over the world. In the current global economic recessions it has become more depressing. The global recession has hit hardest the financial sectors in the developed countries. Insurance companies also therefore could not escape from its impact. The five biggest investment banks including Lehman Brothers have collapsed; top 20 banks in the US have been under stress test. Simultaneously, the biggest insurance company of the world, the AIG which was about to be collapsed has been bailed out by US Government by US$180bn package to protect the 74 million policyholders' funds in 130 countries. This has happened mainly due to bad financial risk management in banks and insurance sector of the developed countries. Thus insurers all over the world have been suffering underwriting losses due to lack of prudent underwriting which is based on the application of risk management process and technology. Here like engineers, CAs are also equally effective provided they acquire knowledge and qualification on risk management.

CAs can complete Risk Management course to avail this opportunity in the insurance industry. The entire edifice of underwriting process in general insurance business rests upon risk analysis and risk evaluation for both financial risks and technical risks where chartered accountants have had immense role to play. Though such services are professionally provided by engineers in most cases, in my opinion CAs can also provide such services in a big way when they are already associated with insurance sector as surveyor and loss adjusters. In India, scope of professional services for risk inspection and risk evaluation for insurance underwriting in general insurance business is being immensely felt in consideration of increasing underwriting losses. The CAs can prove their worth in this field or capacity by reducing underwriting losses with the application of principles and process of risk management.

Almost all PSU general insurers are suffering from huge underwriting losses today. Even in the private non-life insurance sector which closely monitors its incurred claims, the underwriting losses have been doubled to Rs 815 crore in FY09 from Rs 415 crore in FY 2008. The general insurance companies are offsetting underwriting losses against sizeable invest income and especially against profit from sale of investments. But such comfortable adjustment will not go for long time; the insurance firms will have to reduce underwriting losses at any cost. The only way to avoid or reduce underwriting losses is to pursue prudent underwriting i.e. risk based underwriting based on proper risk inspection and risk evaluation. In such business environment, chartered accountants with added qualification or training on risk management may avail the opportunities in the sector. For ready reference the responsibilities of CAs in the role of risk inspection are briefly discussed hereinafter.

Responsibilities of CAs as Risk Analyst and Risk Manager

Risk management involves risk identification, risk analysis, risk evaluation, risk acceptance, risk rating and risk financing, which are being discussed below briefly. The risk management process and techniques have been discussed in Chapters-8, 9 & 11 for property insurance and in chapter under liability insurance.

Risk Identification

It also implies specification of hazards leading to perils that result in risks, i.e. the chance of loss due to occurrence of perils. The hazards are physical, moral and morale. This stage is very vital as failure to properly identify all financial, operating, legal, market, technological and environment risks may lead to unexpected loss. Generally, following methods, analysis and documents are used for identification of all possible risks:

i. Analysis, Charts and Records: Under this, event Analysis, Hazop Analysis, Flow/Process Chart and Organizational Chart, Accounting Records, Specific Inspection, Past records, COPE Study, and CASE Study are covered.

ii. Selection of Risks: All risks are not insurable. The auditors are to examine whether there is any acceptance of risks that are not insurable. To establish the inseparability of risks, the following segregation must be there:

- Pure Risks Vs. Speculative Risks
- Static Risks Vs. Dynamic Risks
- Probabilistic Risks Vs. Catastrophic Risks
- Particular Risks Vs. Fundamental Risks

Under traditional insurance only pure, static, probabilistic and particular risks are insurable. Catastrophic risks are insurable with a very limited retention by direct insurer, but with major transfer through reinsurance**.** Elements of market risks, interest risks, speculative risks, financial risks or technology risks are not insurable at all in traditional insurance though they are insurable in Alternative Risk Transfer (ART) technology.

iii. Classification and evaluation of Risks: After establishing the insurability, the next step in underwriting is to identify the potential exposure of the property to various perils according to the hazards content. The hazards contained in the property or liability determines the degree of probability and severity of loss. To classify the risks, the underwriter carries out Risk Identification, Risk Analysis and Risks Evaluation. Risk identification is the first stage of classification of risks. As we know, the probability of loss varies from 0 to 1. As per the probability measure, risks are classified and evaluation for loss forecasting and risk rating.

iv. Risk Quantification: The quantification process determines the financial impact that risk can impact the insured. This is typically done through various quantitative tools or statistical analysis and qualitative analysis. Statistical analysis includes measure of central tendency, probability distribution or law of inference. This is based on collection of proper data and its appropriate analysis intended for loss forecasting, i.e. measuring the probable risk costs. Selections of specific techniques for measuring the financial impact of risks vary widely and depend largely on the nature of the underwriting exposures.

Major Considerations of Risks Analysis and Risks Evaluation

- What types of property are subject to damage?
- What perils can lead to loss/ damage to property?
- What is the value exposed to loss?
- Will the property be replaced or repaired?
- Will the firm have to raise funds to replace uninsured property?
- Will the firm suspend operations following a direct loss?
- What is the potential loss of profit from business interruptions?

- What operating expenses would continue despite the suspension?
- Will losses continue if normal production is resumed?
- If Yes, what actions might reduce these losses and at what cost?
- What is the risk Transfer Costs
- Is Risk Transfer costs preferable to self-insurance?
- How to evaluate risks, SI, PML?
- How to decide Insurance Cover?
- How to decide terms of indemnification?

Major Considerations of Risk Identification for Property Risks

- COPE study (Construction, Occupation, Protective Measures & Exposures)
- Risk Profile
- Relationship
- Structure
- Developments/ Change in structure
- Operational aspects
- Contingency plans for dealing events
- Risk Management Identification System

Risk Identification System

- Identification of all intended users
- Organizational Chart

- Flow chart
- Event Analysis
- Hazop Study
- Financial Statement Analysis
- Review of report by the expert groups
- Users- internal & external to be interviewed

Chartered Accountant as Insurance Surveyor

Next to Statutory audit, Insurance survey provides second most important avenue for CAs. A large number of CAs are associated with the insurance industry in the capacity of insurance surveyor and loss assessor. To carry out insurance survey profession effectively and efficiently, a chartered accountant must have proper experience and sound knowledge on the following regulations, statutes and technical aspects.

Regulatory Aspects

CAs must be thorough about two regulations namely: a) IRDA (Protection of Policyholders' Interests) Regulations, 2002; and b) Insurance Surveyors and Loss Assessors (Licensing, Professional Requirements and code of conduct) Regulations, 2000. The following two regulations are significant:

(a) IRDA (Protection of Policyholders' Interests) Regulations, 2002: Following are the important requirements in regard to survey of insurance claims which are to be complied with for insurance survey:

- An insured or the claimant shall give notice to the insurer of any loss arising under contract of insurance at the earliest or within such extended time as may be allowed by the insurer.

- On receipt of such a communication, the insurer shall respond immediately and give clear indication to the insured on the procedures that he should follow.

- In cases where a surveyor has to be appointed for assessing a loss/claim, it shall be so done within 72 hours of the receipt of intimation.

- Where the insured is unable to furnish all the particulars required by the surveyor or where the surveyor does not receive the full cooperation of the insured, the insurer or the surveyor as the case may be, shall inform in writing the insured about the delay that may result in the assessment of the claim.

- The surveyor shall be subjected to the code of conduct laid down by the Authority while assessing the loss, and shall communicate his findings to the insurer within 30 days of his appointment with a copy of the report being furnished to the insured, if he so desires.

- Where, in special circumstances of the case, either due to its special and complicated nature, the surveyor shall under intimation to the insured, seek an extension from the insurer for submission of his report. In no case shall a surveyor take more than six months from the date of his appointment to furnish his report.

- If a survey report is found to be incomplete in any respect, the insurer shall require the surveyor under intimation to the insured, to furnish an additional report on certain specific issues as may be required by the insurer. Such a request may be made by the insurer within 15 days of the receipt of the original survey report.

- The facility of calling for an additional report by the insurer shall not be resorted to more than once in the case of a claim.

- On receipt of said advice the surveyor shall furnish an additional report within three weeks of the date of receipt of communication from the insurer.

- On receipt of the survey report or the additional survey report, as the case may be, an insurer shall within a period of 30 days offer a settlement of the claim to the insured.

- If the insurer, for any reasons (e.g. breach of policy conditions) to be recorded in writing and communicated to the insured, decides to reject a claim under the policy, it shall done within a period of 30 days from the receipt of the survey report or the additional survey report, as the case may be.

- Upon acceptance of an offer of settlement by the insured, the claim shall be made within 7 days from the date of acceptance of the offer by the insured. In the cases of delay in the payment, the insurer shall be liable to pay interest at a rate which is 2 per cent above the bank rate.

(b) IRDA Insurance Surveyors & Loss Assessors (Licensing, Professional Requirements and Code of Conduct) Regulations, 2000: This regulation provides rules and regulations on: a) Licensing procedure and legal requirements; b) Requisite qualifications for being surveyors; c) payment of fees to IRDA; d) Categorization of surveyors; e) Code of conduct; and f) Duties and responsibilities of a surveyor. All such aspects have been discussed in Chapter-7. However, the duties and responsibilities of the surveyor are outlined below for ready reference for responsibilities of CAs as surveyor:

- A surveyor and loss assessor shall investigate, manage, quantify, validate and deal with losses arising from any contingency, and report thereon, and carry out the work with competence, objectivity and professional integrity by strictly adhering to the code of conduct expected of such surveyor and loss assessor.

- He will survey and assess the loss on behalf of insurer or insured and declaring whether he has any interest in the subject-matter in question or whether it pertains to any of his relatives, business partners.

- He will maintain confidentiality and neutrality without jeopardizing the liability of the insurer.
- He will examine, inquire, investigate, verify and check the causes and the circumstances of the loss in question including extent of loss, nature of ownership and insurable interest.
- He will estimate, measure and determine the quantum of the subject under loss.
- He will advise the insurer and the insured about loss-minimization, loss control, Loss prevention, and safety measures, wherever appropriate, to avoid further losses.
- He will comment on the admissibility of the loss with reference to terms, warranty, conditions of the policy and assessing liability under the contract of insurance.
- He will recommend for applicability of depreciation and quantum thereof.
- He will point out discrepancy, if any, in the policy wordings.
- He will satisfy queries of the insured /insurer in respect of admissibility and assessment of a claim.
- He will give reasons for repudiation of claim, specifying the policy condition breached.
- He may take expert opinion, wherever required.
- He will comment on salvage and its disposal as per laid down norms of insurer.
- He will submit his report to the insurer as expeditiously as possible, but not later than 30 days of his appointment. In exceptional cases, the afore-mentioned period can be extended with the consent of the insured and the insurer.

Legal Aspects

The surveyor must have sound knowledge on the Insurance Act 1938 and the Indian Contract Act 1872, The Consumer Forum Act 1976 in general. In case of marine survey, the surveyor must have through knowledge about the Marine Insurance Act. For motor survey, the knowledge on the Motor Vehicles Act (relevant portion) is essential. Apart from above statutory aspect, the surveyor must have knowledge of common law in respect of Waiver and Estoppel. Waiver is a Voluntary relinquishment of a known right accrued to a person. For example if the insurer fails to take advantage of the breach of any policy condition within reasonable time, he will be said to have waived his right to reject the claim.

Evans vs. Employers Mutual (1936)**:** A breach of policy condition discovered by insurer while investigating claim, but he arranged for disposal of salvage without taking action against breach of condition and dealt with claim. It is a waiver of the breach. Estoppel is a legal bar created by a person's own action. If insurer sought to determine liability through arbitration, he is estopped from exercising settlement on repair basis.

Technical Aspects

The technical aspects fundamentally arise from policy terms and conditions. To appreciate and apply technical aspects in insurance claims, insurance surveyor shall find answers for following queries:

- What is the Proximate Cause of Loss?
- Is the ascertained proximate cause is Insured Peril?
- What is the amount of Loss payable in terms of policy?
- Are all Clauses and conditions complied with?

Proximate Cause

Let us discuss about proximate cause for its proper understanding and application for establishing the admissibility of claim. Proximate cause means the active efficient cause that sets in motion a chain of events which brings about a result, without the intervention of any force started and working actively from a new and independent source.

Pawsey vs. Scottish Union & National Insurance Co. (1908): Proximate cause need not be the last cause immediately before the event. The last cause may merely a link in the chain connecting the event with the proximate cause. The event is the natural consequence of the cause, and the event is connected with the cause by a chain of circumstances leading naturally and in the ordinary course from the one to the other. Then the cause is to be regarded as proximate cause, however the long, the chain may be.

Chartered Accountants as Insurance Brokers

Insurance brokers are playing today very important roles as insurance intermediaries. Their roles and functions have become very vital today in the new tariff-free regime of non-life insurance business. Today a large portion of corporate insurance business is being procured and managed through insurance brokers. The IRDA has issued the regulations called Insurance Regulatory and Development Authority (Insurance Brokers) Regulations, 2002 to develop and regulate the roles of insurance brokers for furtherance of insurance service in India through this very important marketing intermediary in the open market. Insurance agents act for insurers, while brokers work on behalf of clients. Brokers have had duties and responsibilities and code of conduct in carrying out their professions as per this IRDA regulation. The following persons can be insurance brokers:

i) An individual,

ii) A Firm,

iii) A Company,

iv) A Cooperative Society

Brokers' Eligibility Criteria

Following are eligibility criteria for being insurance brokers as per regulation:

- **Infrastructure**; Adequate Office Space, equipment, trained manpower
- **Qualification**; At least two persons possess any of the following qualification;
  - Bachelors/Masters degree in Arts, Science or Social Science or Science
  - Bachelors/Masters degree in engineering or its equivalent
  - Bachelors/Masters degree in law or its equivalent
  - MBA or its equivalent
  - AIII/ FIII
  - ACA/ FCA
  - AICWA/ FICWA
  - AIIB

Considering above eligibility criteria, the roles and opportunities of CAs can be easily assessed. The CAs with his professional knowledge, skill, experience and business development acumen, can easily make career planning as insurance broker and intermediary. For further details and determining the duties and responsibilities, see Chapter-7.

Chartered Accountants as Corporate Agents

CAs also render professional services as corporate insurance executive for corporate agents. As per regulation called IRDA (Licensing of Corporate Agents) Regulations, 2002 any of the following persons who hold certificate of licence may act as a corporate agent:

i) A firm, ii) A company formed under the Companies Act, 1956, iii) A banking company, iv) A regional rural bank established under the Regional Rural Bank Act, iv) A co-operative society or a co-operative bank, and v) A registered NGO.

A CA can manage professionally and very efficiently the portfolio of a corporate agent as corporate insurance executive.

Eligibility Criteria for a Corporate Insurance Executive

- The corporate insurance executive must have qualifications as specified under Regulation and practical training as specified under Regulation, passed the examination as specified under Regulation 6.
- He must hve the requisite knowledge to solicit and procure insurance business; and is capable of providing the necessary service to the policyholders.
- He must complete, at least, one hundred hours' practical training from an approved institution, which may be spread over three to four weeks, in either life or general insurance business, as the case may be.
- However such practical training period will be reduced to 50 hours where the corporate insurance executive of the applicant, is:
    - o Associate/Fellow of the Insurance Institute of India, Mumbai;
    - o Associate/Fellow of the Institute of Chartered Accountants of India
    - o Associate/Fellow of the Institute of Costs and Works Accountants of India,

- o Associate/Fellow of the Institute of Company Secretaries of India, New Delhi;
- o Associate/Fellow of the Actuarial Society of India, Mumbai;
- o Master of Business Administration of any recognized Institution/ University