INTRODUCTION TO INSURANCE

Chapter Introduction

This chapter aims to introduce the basics of insurance, trace its evolution and how it works. You will also learn how insurance provides protection against economic losses arising as a result of unforeseen events and serves as an instrument of risk transfer.

Learning Outcomes

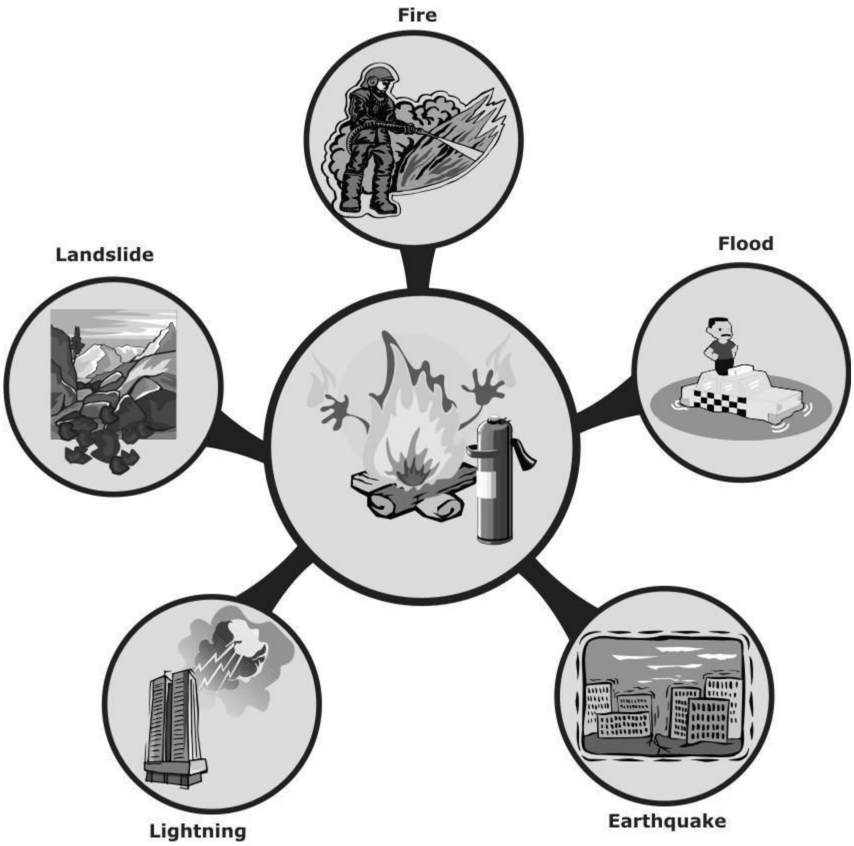
A. Life insurance - History and evolution
B. How insurance works
C. Risk management techniques
D. Insurance as a tool for managing risk
E. Role of insurance in society

A. Life insurance - History and evolution

We live in a world of uncertainty. We hear about:

- trains colliding;
- floods destroying entire communities;
- earthquakes that bring grief;
- young people dying suddenly pre-maturely

Diagram 1: Events happening around us



Why do these events make us anxious and afraid? The reason is simple.

i. Firstly these events are unpredictable. If we can anticipate and predict an event, we can prepare for it.

ii. Secondly, such unpredictable and untoward events are often a cause of economic loss and grief.

A community can come to the aid of individuals who are affected by such events, by having a system of sharing and mutual support.

The idea of insurance took birth thousands of years ago. Yet, the business of insurance, as we know it today, goes back to just two or three centuries.

1. History of insurance

Insurance has been known to exist in some form or other since 3000 BC. Various civilisations, over the years, have practiced the concept of pooling and sharing among themselves, all the losses suffered by some members of the community. Let us take a look at some of the ways in which this concept was applied.

2. Insurance through the ages

Babylonian Traders	The Babylonian traders had agreements where they would pay additional sums to lenders, as a price for writing off of their loans, in case a shipment was lost or stolen. These were called 'bottomry loans'. Under these agreements, the loan taken against the security of the ship or its goods had to be repaid only if and when the ship arrived safely, after the voyage, at its destination.
Traders from Bharuch and Surat	Practices similar to Babylonian traders were prevalent among traders from Bharuch and Surat, sailing in Indian ships to Sri Lanka, Egypt and Greece.
Greeks	The Greeks had started benevolent societies in the late 7th century AD, to take care of the funeral - and families of members who died. The Friendly Societies of England were similarly constituted.
Inhabitants of Rhodes	The inhabitants of Rhodes adopted a practice whereby, if some goods were lost due to jettisoning[1] during distress, the owners of goods (even those who lost nothing) would bear the losses in some proportion.
Chinese Traders	Chinese traders in ancient days would keep their goods in different boats or ships sailing over the treacherous rivers. They assumed that even if any of the boats suffered such a fate, the loss of goods would be only partial and not total. The loss could be distributed and thereby reduced.

3. Modern concepts of insurance

In India the principle of life insurance was reflected in the institution of the joint-family system in India, which was one of the best forms of life insurance down the ages. Sorrows and losses were shared by various family members in the event of the unfortunate demise of a member, as a result of which each member of the family continued to feel secure.

The break-up of the joint family system and emergence of the nuclear family in the modern era, coupled with the stress of daily life has made it necessary to evolve alternative systems for security. This highlights the importance of life insurance to an individual.

i. Lloyds: The origins of modern commercial insurance business as practiced today can be traced to Lloyd's Coffee House in London. Traders, who used to gather there, would agree to share the losses, to their goods being carried by ships, due to perils of the sea. Such losses used to occur because of maritime perils, such as pirates robbing on the high seas, or bad sea weather spoiling the goods or sinking of the ship due to perils of the sea.

ii. Amicable Society for a Perpetual Assurance founded in 1706 in London is considered to be the first life insurance company in the world

4. History of insurance in India

a) India: Modern insurance in India began in early 1800 or thereabouts, with agencies of foreign insurers starting marine insurance business.

The Oriental Life Insurance Co. Ltd	The first life insurance company to be set up in India was an English company
Triton Insurance Co. Ltd.	The first non-life insurer to be established in India
Bombay Mutual Assurance Society Ltd.	The first Indian insurance company. It was formed in 1870 in Mumbai
National Insurance Company Ltd.	The oldest insurance company in India. It was founded in 1906 and it is still in business.

Many other Indian companies were set up subsequently as a result of the Swadeshi movement at the turn of the century.

Important

The Insurance Act 1938 was the first legislation enacted to regulate the conduct of insurance companies in India. This Act, as amended from time to time continues to be in force. The Controller of Insurance was appointed by the Government under the provisions of the Insurance Act.

b) Nationalisation of life insurance: Life insurance business was nationalised on 1st September 1956 and the Life Insurance Corporation of India (LIC) was formed. There were 170 companies and 75 provident fund societies doing life insurance business in India at that time. From 1956 to 1999, the LIC held exclusive rights to do life insurance business in India.

c) Nationalisation of non-life insurance: With the enactment of General Insurance Business Nationalisation Act (GIBNA) in 1972, the non-life insurance business was also nationalised and the General Insurance Corporation of India (GIC) and its four subsidiaries were set up. At that point of time, 106 insurers in India doing non-life insurance business were amalgamated with the formation of four subsidiaries of the GIC of India.

d) Malhotra Committee and IRDAI: In 1993, the Malhotra Committee was setup to explore and recommend changes for development of the industry including the reintroduction of an element of competition. The Committee submitted its report in 1994.In 1997 the Insurance Regulatory Authority (IRA) was established. The passing of the Insurance Regulatory& Development Act, 1999(IRDAI) led to the formation of Insurance Regulatory and Development Authority of India (IRDAI) in April 2000 as a statutory regulatory body both for life, non-life and health insurance industry. IRDA has been subsequently renamed as IRDAI in 2014.

Amending the Insurance Act in 2015, certain stipulations have been added governing the definition and formation of insurance companies in India.

An Indian Insurance company includes a company 'in which the aggregate holdings of equity shares by foreign investors, including portfolio investors, do not exceed forty-nine percent of the paid up equity capital of such Indian insurance company, which is Indian owned and controlled, in such manner as may be prescribed'.

Amendment to the Insurance Act also stipulates about foreign companies in India, A foreign insurance company can engage in reinsurance through a branch established in India. The term "re insurance" means the 'insurance of part of one insurer's risk by another insurer who accepts the risk for a mutually acceptable premium'

5. Life insurance industry today

Currently, there are 24 life insurance companies operating in India as detailed hereunder:

a) Life Insurance Corporation (LIC) of India is a public sector company
b) There are 23 life insurance companies in the private sector

c) The postal department, under the Government of India, also transacts life insurance business via Postal Life Insurance, but is exempt from the purview of the regulator

B. How insurance works

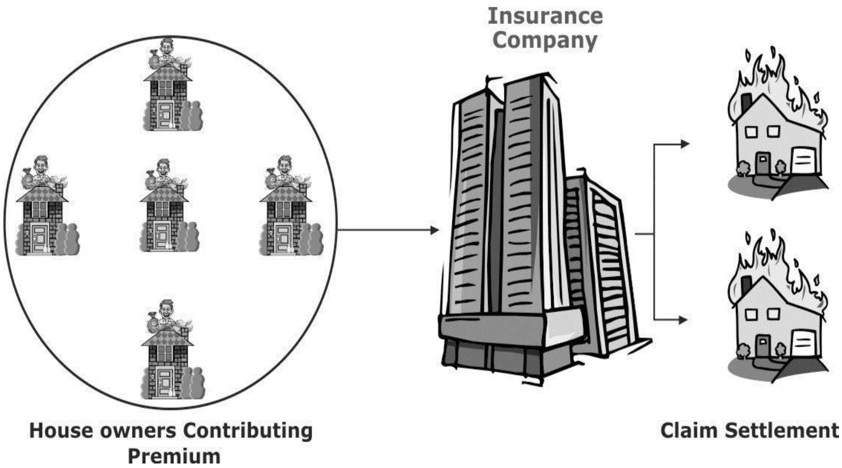
Modern commerce was founded on the principle of ownership of property. When an asset loses value (by loss or destruction) due to a certain event, the owner of the asset suffers an economic loss. However if a common fund is created, which is made up of small contributions from many such owners of similar assets, this amount could be used to compensate the loss suffered by the unfortunate few.

In simple words, the chance of suffering a certain economic loss and its consequence could be transferred from one individual to many through the mechanism of insurance.

Definition

Insurance may thus be considered as a process by which the losses of a few, who are unfortunate to suffer such losses, are shared amongst those exposed to similar uncertain events / situations.

Diagram 2: How insurance works



There is however a catch here.

i) Would people agree to part with their hard earned money, to create such a common fund?
ii) How could they trust that their contributions are actually being used for the desired purpose?

iii) How would they know if they are paying too much or too little?

Obviously someone has to initiate and organise the process and bring members of the community together for this purpose. That 'someone' is known as an 'Insurer' who determines the contribution that each individual must make to the pool and arranges to pay to those who suffer the loss.

The insurer must also win the trust of the individuals and the community.

1. How insurance works

a) Firstly, these must be an asset which has an economic value. The **ASSET**:
   i May be **physical** (like a car or a building) or
   ii May be **non-physical** (like name and goodwill) or
   iii. May be **personal** (like one's eyes, limbs and other aspects of one's body)

b) The asset may lose its value if a certain event happens. This chance of loss is called as **risk.** The cause of the risk event is known as **peril**.

c) There is a principle known as **pooling**. This consists of collecting numerous individual contributions (known as premiums) from various persons. These persons have similar assets which are exposed to similar risks.

d) This pool of funds is used to compensate the few who might suffer the losses as caused by a **peril.**

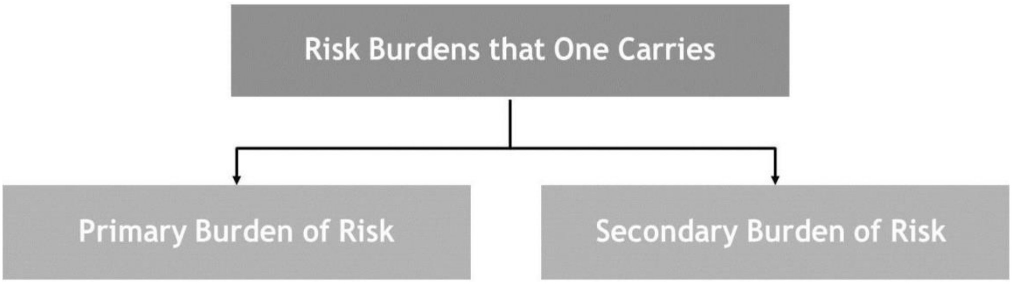
e) This process of pooling funds and compensating the unlucky few is carried out through an institution known as the **insurer.**

f) The insurer enters into an insurance **contract** with each person who seeks to participate in the scheme. Such a participant is known as **insured.**

2. Insurance reduces burdens

Burden of risk refers to the costs, losses and disabilities one has to bear as a result of being exposed to a given loss situation/event.

Diagram 3: Risk burdens that one carries



There are two types of risk burdens that one carries - **primary and secondary**.

a) Primary burden of risk

The **primary burden of risk** consists of losses that are actually suffered by households (and business units), as a result of pure risk events. These losses are often direct and measurable and can be easily compensated for by insurance.

b) Secondary burden of risk

Suppose no such event occurs and there is no loss. Does it mean that those who are exposed to the peril carry no burden? The answer is that apart from the primary burden, one also carries a secondary burden of risk.

The **secondary burden of risk** consists of costs and strains that one has to bear merely from the fact that one is exposed to a loss situation. Even if the said event does not occur, these burdens have still to be borne.

Let us understand some of these burdens:

i. Firstly there is **physical and mental strain caused by fear and anxiety**. The anxiety may vary from person to person but it is present and can cause stress and affect a person's wellbeing.
ii. Secondly when one is **uncertain about whether a loss would occur or not**, the prudent thing to do would be to set aside a reserve fund to meet such an eventuality. There is a cost involved in keeping such a fund. For instance, such funds may be held in a liquid form and yield low returns. By transferring the risk to an insurer, it becomes possible to enjoy peace of mind, invest funds that would otherwise have been set aside as a reserve, and plan one's business more effectively. It is precisely for these reasons that insurance is needed.

C. Risk management techniques

Another question one may ask is whether insurance is the right solution to all kinds of risk situations. The answer is 'No'.

Insurance is only one of the methods by which individuals may seek to manage their risks. Here they transfer the risks they face to an insurance company. However there are some other methods of dealing with risks, which are explained below:

1. Risk avoidance

Controlling risk by avoiding a loss situation is known as risk avoidance. Thus one may try to avoid any property, person or activity with which an exposure may be associated.

2. Risk retention

One tries to manage the impact of risk and decides to bear the risk and its effects by oneself. This is known as self-insurance.

3. Risk reduction and control

This is a more practical and relevant approach than risk avoidance. It means taking steps to lower the chance of occurrence of a loss and/or to reduce severity of its impact if such loss should occur.

Important

The measures to reduce chance of occurrence are known as '**Loss Prevention**'. The measures to reduce degree of loss are called '**Loss Reduction**'.

Risk reduction involves reducing the frequency and/or sizes of losses through one or more of:

a) **Education and training**, such as holding regular “fire drills” for employees, or ensuring adequate training of drivers, forklift operators, wearing of helmets and seat belts and so on.

One example of this can be educating school going children to avoid junk food.

b) **Making Environmental changes**, such as improving “physical” conditions, e.g. better locks on doors, bars or shutters on windows, installing burglar or fire alarms or extinguishers. The State can take measures to curb pollution and noise levels to improve the health status of its people. Regular spraying of Malaria medicine helps in prevention of outbreak of the disease.

c) **Changes made in dangerous or hazardous operations,** while using machinery and equipment or in the performance of other tasks.

For example leading a healthy lifestyle and eating properly at the right time helps in reducing the incidence of falling ill.

d) **Separation**, spreading out various items of property into varied locations rather than concentrating them at one location, is a method to control risks. The idea is, if a mishap were to occur in one location, its impact could be reduced by not keeping everything at that one place.

For instance one could reduce the loss of inventory by storing it in different warehouses. Even if one of these were to be destroyed, the impact would be reduced considerably

4. **Risk financing**

This refers to the provision of funds to meet losses that may occur.

a) **Risk retention through self-financing** involves self-payment for any losses as they occur. In this process the firm assumes and finances its own risk,either through its own or borrowed funds, this is known as **self-insurance**.The firm may also engage in various risk reduction methods to make the loss impact small enough to be retained by the firm.

b) **Risk transfer** is an alternative to risk retention. Risk transfer involves transferring the responsibility for losses to another party. Here the losses that may arise as a result of a fortuitous event (or peril) are transferred to another entity.

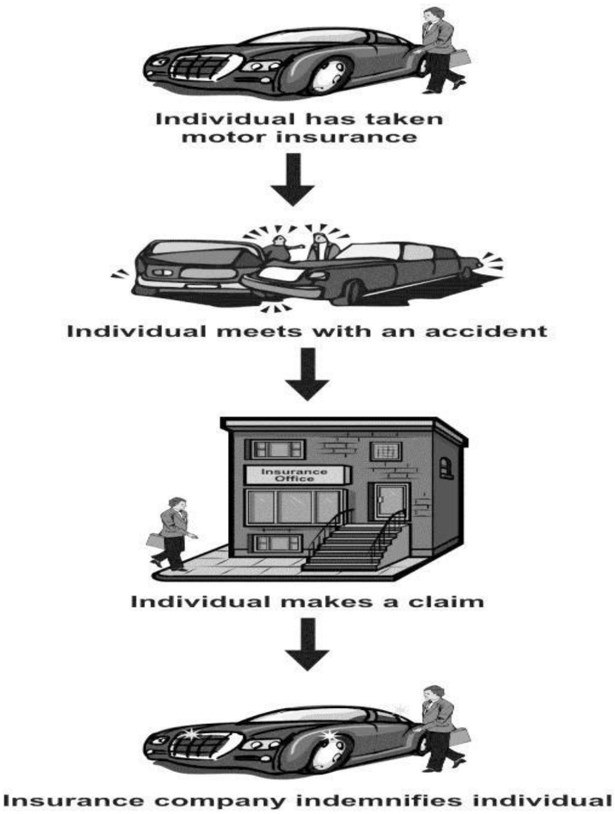
Insurance is one of the major forms of risk transfer, and it permits uncertainty to be replaced by certainty through insurance indemnity.

Insurance vs Assurance

Both insurance and assurance are financial products offered by companies operating commercially. Of late the distinction between the two has increasingly become blurred and the two are taken as somewhat similar. However there are subtle differences between the two as discussed hereunder.

Insurance refers to protection against an event that **might** happen whereas assurance refers to protection against an event that **will** happen. Insurance provides cover against a risk while assurance covers an event that is definite e.g. death, which is certain, only the time of occurrence is uncertain. Assurance policies are associated with life cover.

Diagram 4: How insurance indemnifies the insured.



There are other ways to transfer risk. For example when a firm is part of a group, the risk may be transferred to the parent group which would then finance the losses.

Thus, insurance is only one of the methods of risk transfer.

D. Insurance as a tool for managing risk

When we speak about a risk, we are not referring to a loss that has actually been suffered but a loss that is likely to occur. It is thus an expected loss. The cost of this expected loss (which is the same as the cost of the risk) is the product of two factors:

i. The **probability** that the peril being insured against may happen, leading to the loss
ii. The **impact** or the amount of loss that may be suffered as a result

The cost of risk would increase in direct proportion with both probability and amount of loss. However, if the amount of loss is very high, and the probability of its occurrence is small, the cost of the risk would be low.

Diagram 5: Considerations before opting for insurance.

1. **Considerations before opting for Insurance**

   When deciding whether to insure or not, one needs to weigh the cost of transferring the risk against the cost of bearing the loss, that may arise, oneself. The cost of transferring the risk is the insurance premium - it is given by two factors mentioned in the previous paragraph. The best situations for insurance would be where the probability is very low but the loss impact could be very high. In such instances, the cost of transferring the risk through its insurance (the premium) would be much lower while the cost of bearing it on oneself would be very high.

a) **Don't risk a lot for a little**: A reasonable relationship must be there between the cost of transferring the risk and the value derived

b) **Don't risk more than you can afford to lose**: If the loss that can arise as a result of an event is so large that it can lead to a situation that is near bankruptcy, retention of the risk would not appear to be realistic and appropriate

c) **Consider the likely outcomes of the risk carefully**: It is best to insure those assets for which the probability of occurrence (frequency) of a loss is low but the possible severity (impact), is high.

E. Role of insurance in society

Insurance companies play an important role in a country's economic development. They are contributing in a significant sense to ensuring that the wealth of the country is protected and preserved. Some of their contributions are given below.

a) Their investments benefit the society at large. An insurance company's strength lies in the fact that huge amounts are collected and pooled together in the form of premiums.

b) These funds are collected and held for the benefit of the policyholders. Insurance companies are required to keep this aspect in mind and make all their decisions in dealing with these funds so as to be in ways that benefit the community. This applies also to its investments. That is why successful insurance companies would not be found investing in speculative ventures i.e. stocks and shares.

c) The system of insurance provides numerous direct and indirect benefits to the individual, his family, to industry and commerce and to the community and the nation as a whole. The insured - both individuals and enterprises - are directly benefitted because they are protected from the consequences of the loss that may be caused by an accident or fortuitous event. Insurance, thus, in a sense protects the capital in industry and releases the capital for further expansion and development of business and industry.

d) Insurance removes the fear, worry and anxiety associated with one's future and thus encourages free investment of capital in business enterprises and promotes efficient use of existing resources. Thus insurance encourages commercial and industrial development along with generation of employment opportunities, thereby contributing to a healthy economy and increased national productivity.

e) A bank or financial institution may not advance loans on property unless it is insured against loss or damage by insurable perils. Most of them insist on assigning the policy as collateral security.

f) Before acceptance of a risk, insurers arrange survey and inspection of the property to be insured, by qualified engineers and other experts. They not only assesses the risk for rating purposes but also suggest and recommend to the insured, various improvements in the risk, which will attract lower rates of premium.

g) Insurance ranks with export trade, shipping and banking services as an earner of foreign exchange to the country. Indian insurers operate in more than 30 countries. These operations earn foreign exchange and represent invisible exports.

h) Insurers are closely associated with several agencies and institutions engaged in fire loss prevention, cargo loss prevention, industrial safety and road safety.

Information

Insurance and Social Security

a) It is now recognised that provision of social security is an obligation of the State. Various laws, passed by the State for this purpose involve use of insurance, compulsory or voluntary, as a tool of social security. Central and State Governments contribute premiums under certain social security schemes thus fulfilling their social commitments. The Employees State Insurance Act, 1948 provides for **Employees State Insurance Corporation** to pay for the expenses of sickness, disablement, maternity and death for the benefit of industrial employees and their families, who are insured persons. The scheme operates in certain industrial areas as notified by the Government.

b) Insurers play an important role in social security schemes sponsored by theGovernment such as

1. RKBY - Rashtriya Krishi Bima Yojana
2. RSBY - Rashtriya Swasthya Bima Yojana
3. PMJBY - Pradhan Mantri Jeevan Jyoti Bima Yojana
4. PMSBY - Pradhan Mantri Suraksha Bima Yojana

All these benefit the community in general.

d) All the **rural insurance schemes**, operated on a commercial basis, aredesigned ultimately to provide social security to the rural families.

d) Apart from this support to Government schemes, the insurance industry itself offers on a commercial basis, insurance covers which have the ultimate objective of social security. Examples are: **Janata Personal Accident, Jan Arogya** etc.

CUSTOMER SERVICE

Chapter Introduction

In this chapter you will learn the importance of customer service. You will learn the role of agents in providing service to customers. You will learn different grievances redressal mechanisms available for Insurance policyholders. You will also learn how to communicate and relate with customer.

Learning Outcomes

A. Customer service - General concepts
B. Insurance agent's role in providing great customer service
C. Grievance redressal
D. Communication process
E. Non-verbal communication
F. Ethical behaviour

After studying this chapter, you should be able to:

1. Illustrate the importance of customer services
2. Describe quality of service
3. Examine importance of service in the insurance industry
4. Discuss the role of an insurance agent in providing good service
5. Review grievance redressal mechanism in insurance
6. Explain the process of communication
7. Demonstrate the importance of non-verbal communication
8. Recommend ethical behaviour

A. Customer service - General concepts

1. Why Customer Service?

Customers provide the bread and butter of a business and no enterprise can afford to treat them indifferently. The role of customer service and relationships is far more critical in the case of insurance than in other products.

This is because insurance is a service and very different from real goods. Let us

examine how buying insurance differs from purchasing a car.

A Car	Insurance of the car
It is a tangible good, that can be seen, test driven and experienced.	It is a contract to compensate against loss or damage to the car due to an unforeseen accident in future. One cannot see or touch or experience the insurance benefit till the unfortunate event occurs.
The buyer of the car has an expectation of some pleasure at the time of purchase. The experience is real and easy to understand.	The purchase of insurance is not based on expectation of immediate pleasure, but fear/anxiety about a possible tragedy. It is unlikely that any insurance customer would look forward to a situation where the benefit becomes payable.

A car is produced in a factory assembly line, sold in a showroom and used on the road. The three processes of making, selling and using take place at three different times and places.	In case of insurance it can be seen that production and consumption happen Simultaneously. This simultaneity of *production and consumption* is a distinctive feature of all services.

What the customer really derives is a service experience. If this is less than satisfactory, it causes dissatisfaction. If the service exceeds expectations, the customer would be delighted. The goal of every enterprise should thus be to delight its customers.

2. Quality of service

It is necessary for insurance companies and their personnel, which includes their agents, to render high quality service and delight the customer.

But what is high quality service? What are its attributes?

A well-known model on service quality [named "**SERVQUAL**'] would give us some insights. It highlights five major indicators of service quality:

a) **Reliability**: the ability to perform the promised service dependably and accurately. Most customers regard reliability as being the most important of the five dimensions of service quality. It is the foundation on which trust is built.

b) **Responsiveness**: refers to the willingness and ability of service personnel to help customers and provide prompt response to the customer's needs. It may be measured by indicators like speed, accuracy, and attitude while giving the service.

c) **Assurance**: refers to the knowledge, competence and courtesy of service providers and their ability to convey trust and confidence. It is given by the customer's evaluation of how well the service employee has understood needs and is capable of meeting them.

d) **Empathy**: is described as the human touch. It is reflected in the caring attitude and individualised attention provided to customers.

e) **Tangibles**: represent the physical environmental factors that the customer can see, hear and touch. For instance the location, the layout and cleanliness and the sense of order and professionalism that one gets when visiting an insurance company's office can make a great impression on the customer. The physical ambience becomes especially important because it creates first and lasting impressions, before and after the actual service is experienced.

2. Customer service and insurance

Ask any leading sales producers in the insurance industry about how they managed to reach the top and stay there. You are likely to get a common answer, that it was the patronage and support of their existing clients that helped them build their business.

You would also learn that a large part of their income comes from the commissions for renewal of the contracts. Their clients are also the source for acquiring new customers.

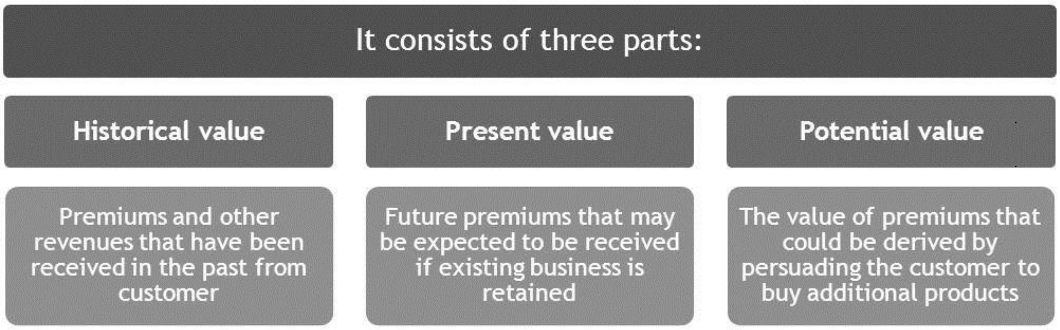
What is the secret of their success?

The answer, most likely is, **commitment to serving their customers**.

How does keeping a customer happy benefit the agent and the company?

To answer this question, it would be useful to look at customer's lifetime value.

Customer lifetime value may be defined as the sum of economic benefits that can be derived from building a sound relationship with a customer over a long period of time.
Diagram 1: Customer Lifetime Value



An agent who renders service and builds close relationships with her customers, builds goodwill and brand value, which helps in expanding the business.

B. Insurance agent's role in providing great customer service

Let us now consider how an agent can render great service to the customer. The role begins at the stage of sale and continues through the duration of the contract, and includes the following steps. Let us look at some of the milestones in a contract and the role played at each step.

1. The Point of Sale - Best advice

The first point for service is the point of sale. One of the critical issues involved in purchase of non-life Insurance is to determine the **amount of coverage [Sum Insured] to be bought**.

Here it is important to keep a basic percept in mind - Do not recommend insuring where the risk can be managed otherwise. The insured needs to make sure that the expected loss involved is greater than the cost of insurance. If the premium payments are high compared to the loss involved, it may be advisable to just bear the risk.

On the other hand, if the occurrence of any contingency would lead to financial burden, it is wise to insure against such contingency.

Whether insurance is needed or not, depends on the circumstances. If the probability of loss or damage to an asset due to a peril is negligible, one may retain the risk rather than insure it. Similarly if an item has insignificant value, one may not insure it.

Example

To a homeowner living in a flood prone area, purchasing cover against floods would prove to be helpful.

On the other hand, if the home owner owns a home at a place where the risk of floods is negligible it may not be necessary to obtain cover.

In India, motor insurance against third party is compulsory under the law. In that case, the debate about whether one needs insurance or not is irrelevant.

One must purchase third party insurance if he owns a vehicle because it is mandatory if one wants to drive on a public road. At the same time it would be prudent to cover the possibility of loss of own damage to the car which is not mandatory.

In case a portion of the possible loss can be borne by oneself, it would be economical for the insured to opt for a **deductible**. A corporate customer may have varied needs, right from the coverage of factory, people, cars, liability exposures etc. She needs the right advice for the coverage and policies to be taken.
Most non-life insurance policies broadly fall in two categories:

Named peril policies
All risk policies

The latter are costlier as they cover all losses which are specifically not excluded under the policy. Hence opting for 'named peril' policies where the most probable causes of loss are covered by the perils named in the policy may be more beneficial, as such a step could save premiums and provide need based cover to the insured.

The agent really begins to earn her commission when she renders best advice on the matter. It would be worthwhile for the agent to remember that while one may view insurance as the standard approach for dealing with the risk, there are other techniques like risk retention or loss prevention that are available as options for reducing the cost of insurance.

From the standpoint of an insured the relevant questions for instance may be:

- How much premium will be saved by considering deductibles?
- How much would a loss prevention activity result in reduction in premiums?

When approaching the customer as a non-life insurance sales person the question an agent needs to ask herself is about her role vis-à-vis the customer. Is she going there just to get a sale or to relate to the customer as a coach and partner who would help him to manage his risks more effectively?

The customer's angle is different. He is not so much concerned with getting maximum insurance per rupee spent, but rather in **reducing the cost of handling risk**. The concern would be thus on identifying those risks which customer cannot retain and hence must be insured.

In other words the role of an insurance agent is more than that of a mere sales person. She also **needs to be a risk assessor, underwriter, risk management counsellor, designer of customised solutions and a relationship builder who thrives on building trust and long-term relationships**, all rolled into one.

2. The proposal stage

The agent has to support the customer in filling out the proposal for insurance. The insured is required to take responsibility for the statements made therein. The salient aspects of a proposal form have been discussed in chapter 5.

It is very important that the agent should explain and clarify to proposer the details to be filled as answer to each of questions in the proposal form. In the event of a claim, a failure to give proper and complete information can jeopardise the customer's claim.
Sometimes there may be additional information that may be required to complete the policy. In such cases the company may inform the customer directly or through the agent / advisor. In either case, it becomes necessary to help the customer complete all the required formalities and even explain to him or her why these are necessary.

3. Acceptance stage

a) Cover note

The cover note has been discussed in chapter '5'.It is the agent's responsibility to ensure that the cover note is issued by the company, where applicable, to the insured. Promptness in this regard communicates to the client that his interests are safe in the hands of the agent and the company.

b) Delivery of the policy document

Delivery of the policy is another major opportunity that an agent gets to make contact with the customer. If company rules permit a policy document being delivered in person, it may be a good idea to collect it and present the document to the customer.

If the policy is being sent directly by mail, one must contact the customer, once it is known that the policy document has been sent. This is an opportunity to visit the customer and explain anything that is unclear in the document received. This is also an occasion to clarify various kinds of policy provisions, and the policy holder's rights and privileges that the customer can avail of. This act demonstrates a willingness to provide a level of service beyond the sale.

This meeting is also an occasion to pledge the agent's commitment to serving the customer and communicating full support.

The next logical step would be to ask for the names and particulars of other individuals he knows who can possibly benefit from the agent's services. If the client can himself contact these people and introduce the agent to them, it would mean a great breakthrough in business.

c) Policy renewal

Non-life insurance policies have to be renewed each year and the customer has a choice at the time of each renewal, to continue insuring with the same company or switch to another company. This is a critical point where the goodwill and trust created by the agent and the company gets tested.

Although there is no legal obligation on the part of insurers to advise the insured that his policy is due to expire on a particular date, yet as a matter of courtesy and decidedly a healthy business practice, insurers issue a **"Renewal Notice"** one month in advance of the date of expiry, inviting renewal of the policy. The agent needs to be in touch with the customer well before the renewal due date to remind the latter about renewal so that he can make provision for the same.

The relationship gets strengthened by keeping in touch with the client from time to time, by greeting him on some occasion like a festival or a family event. Similarly when there is a moment of difficulty or sorrow by to offering assistance.

4. The claim stage

The agent has a crucial role to play at the time of claim settlement. It is her task to ensure that the incident giving rise to the claim is immediately informed to the insurer and that the customer carefully follows all the formalities and assists in all the investigations that may need to be done to assess the loss.

C. Grievance redressal

1. Overview

The time for high priority action is when the customer has a complaint. Remember that in the case of a complaint, the issue of service failure [it can range from delay in correcting the records of the insurer to a lack of promptness in settling a claim] which has aggrieved the customer is only a part of the story.

Customers get upset and infuriated a lot more because of their interpretations about such failure. There are two types of feelings and related emotions that arise with each service failure:

- Firstly there is a sense of unfairness, a feeling of being cheated
- The second feeling is one of hurt ego - of being made to look and feel small

A complaint is a crucial "**moment of truth**" in the customer relationship; if the company gets it right there is potential to actually improve customer loyalty. The human touch is critical in this; customers want to feel valued.

If you are a professional insurance advisor, you would not allow such a situation to happen in the first place. You would take the matter up with the appropriate officer of the company. **Remember, no one else in the company has ownership of the client's problems as much as you do**.

Complaints / grievances provide us the opportunity to demonstrate how much we care for the customer's interests. They are in fact the solid pillars on which an insurance agent's goodwill and business is built. At the end of every policy document, the insurance companies have detailed the procedure of grievance redressal, which should be brought to the notice of the customers at the time of explaining the document provisions.

Word of mouth publicity (Good/Bad) has significant role in selling and servicing. Remember good service gets rewarded by 5 people being informed, where as bad service is passed on to 20 people.

2. Integrated Grievance Management System (IGMS)

IRDA has launched an Integrated Grievance Management System (IGMS) which acts as a central repository of insurance grievance data and as a tool for monitoring grievance redress in the industry.

Policyholders can register on this system with their policy details and lodge their complaints. Complaints are then forwarded to respective insurance company. IGMS tracks complaints and the time taken for redressal. The complaints can be registered at:
http://www.policyholder.gov.in/Integrated_Grievance_Management.aspx

3. The Consumer Protection Act, 1986

This Act was passed "*to provide for better protection of the interest of consumers and to make provision for the establishment of consumer councils and other authorities for the settlement of consumer's disputes.*" The Act has been amended by the Consumer Protection (Amendment) Act, 2002.

a) Definitions under the Act

Some definitions provided in the Act are as follows:

Definition

"Service" means service of any description which is made available to potential users and includes the provision of facilities in connection with banking, financing, insurance, transport, processing, supply of electrical or other energy, board or lodging or both, housing construction, entertainment, amusement or the purveying of news or other information. But it does not include the rendering of any service free of charge or under a contract of personal service.

Insurance is included as a service

"**Consumer**" means any person who:

i. Buys any goods for a consideration and includes any user of such goods. But does not include a person who obtains such goods for resale or for any commercial purpose or
ii. Hires or avails of any services for a consideration and includes beneficiary of such services.

'**Defect**' means any fault, imperfection, shortcoming inadequacy in the quality, nature and manner of performance which is required to be maintained by or under any law or has been undertaken to be performed by a person in pursuance of a contract or otherwise in relation to any service.

'**Complaint**' means any allegation in writing made by a complainant that:

i. An unfair trade practice or restrictive trade practice has been adopted
ii. The goods bought by him suffer from one or more defects
iii. The services hired or availed of by him suffer from deficiency in any respect
iv. Price charged is in excess of that fixed by law or displayed on package Goods which will be hazardous to life and safety when used are being offered for sale to the public in contravention of the provisions of any law requiring trader to display information in regard to the contents, manner and effect of use of such goods

b) Consumer disputes redressal agencies

Consumer disputes redressal agencies are established in each district and state and at national level.

i. District Forum: The forum has jurisdiction to entertain complaints, where value of the goods or services and the compensation claimed is up to Rs. 20 lakhs The District Forum is empowered to send its order/decree for execution to appropriate Civil Court.

ii. State Commission: This redressal authority has original, appellate and supervisory jurisdiction. It entertains appeals from the District Forum. It also has original jurisdiction to entertain complaints where the value of goods/service and compensation, if any claimed exceeds Rs. 20 lakhs but does not exceed Rs. 100 lakhs. Other powers and authority are similar to those of the District Forum.

iii. National Commission: The final authority established under the Act is the National Commission. It has original; appellate as well as supervisory jurisdiction. It can hear the appeals from the order passed by the State Commission and in its original jurisdiction it will entertain disputes, where goods/services and the compensation claimed exceeds Rs.100 lakhs. It has supervisory jurisdiction over State Commission.

All the three agencies have powers of a Civil Court.

c) Procedure for filing a complaint

The procedure for filing a complaint for the three redressal agencies mentioned above is very simple. There is no fee for filing a complaint or filing an appeal whether before the State Commission or National Commission.

The complaint can be filed by the complainant himself or by his authorised agent. It can be filed personally or can even be sent by post. It may be noted that no advocate is necessary for the purpose of filing a complaint.

d) Consumer Forum orders

If the forum is satisfied that the goods complained against suffer from any of the defects specified in the complaint or that any of the allegations contained in the complaint about the services are proved, the forum can issue an order directing the opposite party to do one or more of the following namely,

i. To **return** to the complainant **the price**, [or premium in case of insurance], the charges paid by the complainant
ii. To award such amount as **compensation** to the consumers for any loss or injury suffered by the consumer due to negligence of the opposite party iii. To **remove** the defects or **deficiencies** in the services in question
iv. To **discontinue the unfair trade practice** or the restrictive trade practice or not to repeat them
v. To provide for **adequate costs** to parties

e) Consumer disputes categories

The majority of consumer disputes with the three forums fall in the following main categories, as far as the insurance business is concerned:

i. Delay in settlement of claims
ii. Non-settlement of claims
iii. Repudiation of claims iv. Quantum of loss
v. Policy terms, conditions etc

4. The Insurance Ombudsman

The Central Government under the powers of the Insurance Act, 1938 made **Redressal of Public Grievances Rules, 1998** by a notification published in the official gazette on November 11, 1998. These rules apply to life and non-life insurance, for all personal lines of insurances, that is, insurances taken in an individual capacity.

The objective of these rules is to resolve all complaints relating to settlement of claim on the part of the insurance companies in a cost effective, efficient and impartial manner.

The Ombudsman, by mutual agreement of the insured and the insurer can act as a mediator and counsellor within the terms of reference.

The decision of the Ombudsman, whether to accept or reject the complaint, is final.

a) Complaint to the Ombudsman

Any complaint made to the Ombudsman should be in writing, signed by the insured or his legal heirs, addressed to an Ombudsman within whose jurisdiction, the insurer has a branch / office, supported by documents, if any, along with an estimate of the nature and extent of loss to the complainant and the relief sought.

Complaints can be made to the Ombudsman if:

i. The complainant had made a previous written representation to the insurance company and the insurance company had:

- Rejected the complaint or
- The complainant had not received any reply within one month after receipt of the complaint by the insurer
- The complainant is not satisfied with the reply given by the insurer.

ii. The complaint is made within one year from the date of rejection by the insurance company.

iii. The complaint is not pending in any Court or Consumer Forum or in arbitration.

b) Recommendations by the Ombudsman

There are certain duties/protocols that the Ombudsman is expected to follow:

i. Recommendations should be made within one month of the receipt of such a complaint
ii. The copies should be sent to both the complainant and the insurance company
iii. Recommendations have to be accepted in writing by the complainant within 15 days of receipt of such recommendation
iv. A copy of acceptance letter by the insured should be sent to the insurer and his written confirmation sought within 15 days of his receiving such acceptance letter

If the dispute is not settled by intermediation, the Ombudsman will pass award to the insured which he thinks is fair, and is not more than what is necessary to cover the loss of the insured.

c) Awards by Ombudsman

The awards by Ombudsman are governed by the following rules:

i. The award should not be more than Rs. 20 lakh (inclusive of ex-gratia payment and other expenses)
ii. The award should be made within a period of 3 months from the date of eceipt of such a complaint, and the insured should acknowledge the receipt of the award in full as a final settlement within one month of the receipt of such award
iii. The insurer shall comply with the award and send a written intimation to the Ombudsman within 15 days of the receipt of such acceptance letter
iv. If the insured does not intimate in writing the acceptance of such award, the insurer may not implement the award

GRIEVANCE REDRESSAL MECHANISM

Insurance industry is essentially a service industry where, in the present context, customer expectations are constantly rising and dissatisfaction with the standard of services rendered is ever present. Despite there being continuous product innovation and significant improvement in the level of customer service aided by use of modern technology, the industry suffers badly in terms of customer dissatisfaction and poor image. Alive to this situation the Government and the regulator have taken a number of initiatives.

IRDAI's regulations stipulate the turnaround times (TAT) for various services that an insurance company has to render the consumer. These are part of the IRDAI (Protection of Policyholders' Interests Regulations), 2002.Insurance companies are also required to have an effective grievance redressal mechanism and IRDAI has created the guidelines for that too.

Grievance redressal mechanism - Consumer courts, Ombudsman

1. Integrated Grievance Management System (IGMS)

IRDAI has launched an Integrated Grievance Management System (IGMS) which acts as a central repository of insurance grievance data and as a tool for monitoring grievance redress in the industry.

Policyholders can register on this system with their policy details and lodge their complaints. Complaints are then forwarded to the respective insurance companies.

Grievance redressal mechanism

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2 The Consumer Protection Act, 1986

This Act was passed "to provide for better protection of the interest of consumers and to make provision for the establishment of consumer councils and other authorities for the settlement of consumer's disputes". The Act has been amended by the Consumer Protection (Amendment) Act, 2002.

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

a) Consumer disputes redressal agencies

"Consumer disputes redressal agencies" are established in each district and state and at national level.

i. District Forum

- The forum has jurisdiction to entertain complaints, where value of the goods or services and the compensation claimed is up to Rs.20 lakhs.
- The District Forum is empowered to send its order/decree for execution to appropriate civil court.

ii. State Commission

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- It entertains appeals from the District Forum.
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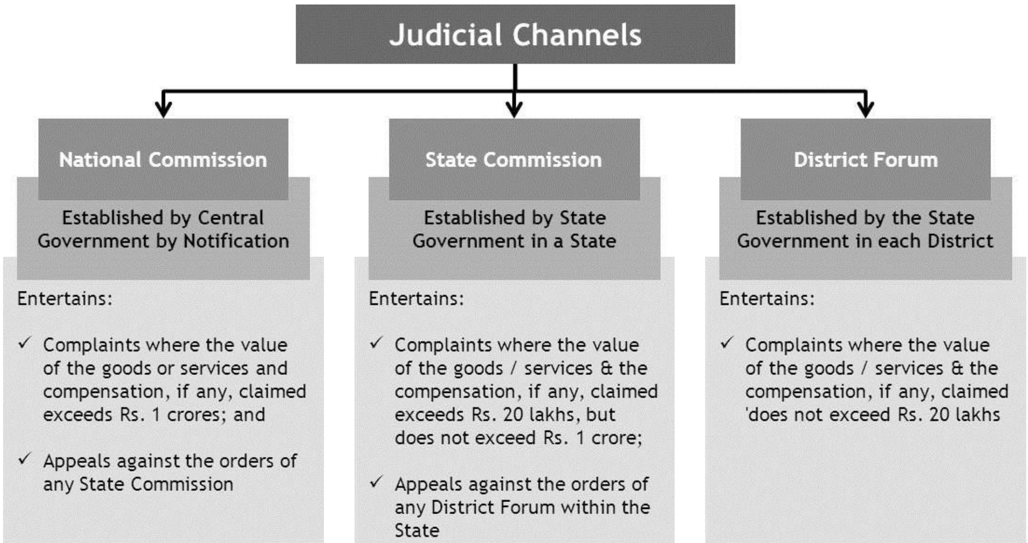
Diagram 1: Channels for grievance redressal



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The decision of the Ombudsman, whether to accept or reject the complaint, is final.

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iii. The complaint is made within one year from the date of rejection by the insurance company
iv. The complaint is not pending in any court or consumer forum or in arbitration

Award

If the dispute is not settled by intermediation, the Ombudsman will pass an award to the insured which he thinks is fair, and is not more than what is necessary to cover the loss of the insured.

The awards by Ombudsman are governed by the following rules:

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iii. The insurer shall comply with the award and send a written intimation to the Ombudsman within 15 days of the receipt of such acceptance letter
iv. If the insured does not intimate in writing the acceptance of such award,the insurer may not implement the award

1. Insurance contracts - Legal aspects

a) The insurance contract

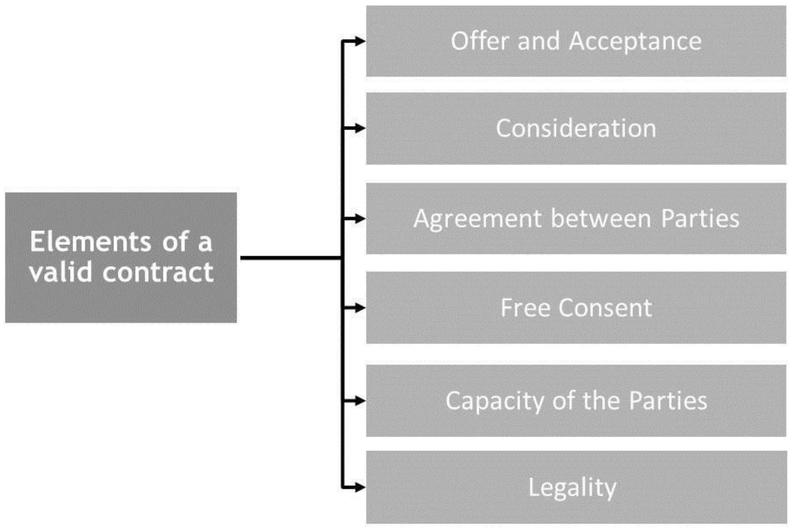
Insurance involves a contractual agreement in which the insurer agrees to provide financial protection against certain specified risks for a price or consideration known as the premium. The contractual agreement takes the form of an insurance policy.

b) Legal aspects of an insurance contract

We will now look at some features of an insurance contract and then consider the legal principles that govern insurance contracts in general.

An insurance policy is a contract entered into between two parties, viz., the company, called the **insurer**, and the policy holder, called the **insured** and fulfils the requirements enshrined in the Indian Contract Act, 1872.

Diagram 1: Insurance contract



Elements of a valid contract

Diagram 2: Elements of a valid contract

The elements of a valid contract are:

2. Insurance contracts - Special features

a) Uberrima Fides or Utmost Good Faith

This is one of the fundamental principles of an insurance contract. Also called uberrima fides, it means that every party to the contract must disclose all material facts relating to the subject matter of insurance.

A distinction may be made between Good Faith and Utmost Good Faith. All commercial contracts in general require that good faith shall be observed in their transaction and there shall be no fraud or deceit when giving information. Apart from this legal duty to observe good faith, the seller is not bound to disclose any information about the subject matter of the contract to the buyer.

The rule observed here is that of **"Caveat Emptor" which means Buyer Beware**. The parties to the contract are expected to examine the subject matter of the contract and so long as one party does not mislead the other and the answers are given truthfully, there is no question of the other party avoiding the contract

Utmost Good Faith: Insurance contracts stand on a different footing. Firstly, the subject matter of the contract is intangible and cannot be easily known through direct observation or experience by the insurer. Again there are many facts, which by their very nature, may be known only to the proposer. The insurer has to often rely entirely on the latter for information.

Hence the proposer has a legal duty to disclose all material information about the subject matter of insurance to the insurers who do not have this information.

If utmost good faith is not observed by either party, the contract may be avoided by the other. This essentially means that no one should be allowed to take advantage of his own wrong especially while entering into a contract of insurance.

It is expected that the insured should not make any misrepresentation regarding any fact that is material for the insurance contract. The insured must disclose all relevant facts. If this obligation did not exist, a person taking insurance might suppress certain facts impacting the risk on the subject matter and receive an undue benefit.

The policyholder is expected to disclose the status of his health, family history, income, occupation etc. truthfully without concealing any material fact so as to enable the underwriter to assess the risk properly. In case of non-disclosure or misrepresentation in the proposal form which may have impacted the underwriting decision of the underwriter, the insurer has a right to cancel the contract

b) Material facts

Material fact has been defined as a fact that would affect the judgment of an insurance underwriter in deciding whether to accept the risk and if so, the rate of premium and the terms and conditions.

Whether an undisclosed fact was material or not would depend on the circumstances of the individual case and could be decided ultimately only in a court of law. The insured **has to disclose** facts that affect the risk.

Let us take a look at some of the types of material facts in insurance that one needs to disclose:

Breach of Utmost Good Faith

We shall now consider situations which would involve a Breach of Utmost Good Faith. Such breach can arise either through Non-Disclosure or Misrepresentation.

Non-Disclosure: may arise when the insured is silent in general about material facts because the insurer has not raised any specific enquiry. It may also arise through evasive answers to queries raised by the insurer. Often disclosure may be inadvertent (meaning it may be made without one's knowledge or intention) or because the proposer thought that a fact was not material.

In such a case it is innocent. When a fact is intentionally suppressed it is treated as concealment. In the latter case there is intent to deceive.

Misrepresentation: Any statement made during negotiation of a contract of insurance is called representation. A representation may be a definite statement of fact or a statement of belief, intention or expectation. With regard to a fact it is expected that the statement must be substantially correct. When it comes to Representations that concern matters of belief or expectation, it is held that these must be made in good faith.

Fraud

A policy of insurance may be called in question at any time within three years from the date of issuance of the policy or the date of commencement of risk or the date of revival, of the policy or the date of the rider to the policy, whichever is later, on the ground of fraud:

The insurer shall have to communicate in writing to the insured or the legal representatives or nominees or assignees of the insured the grounds and materials on which such decision is based.

The term "Fraud" has been defined and specified as follows:

The expression "fraud" means any of the following acts committed by the insured or by his agent, with the intent to deceive the insurer or to induce the insurer to issue a insurance policy:

(a) the suggestion, as a fact of that which is not true and which the insured does not believe to be true;
(b) the active concealment of a fact by the insured having knowledge or belief of the fact;
(c) any other act fitted to deceive; and
(d) any such act or omission as the law specially declares to be fraudulent.

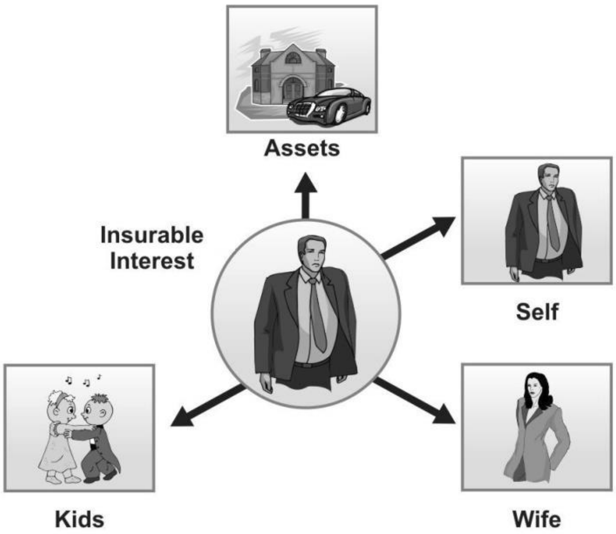
c) Insurable interest

The existence of 'insurable interest' is an essential ingredient of every insurance contract and is considered as the legal pre-requisite for insurance. Let us see how insurance differs from a gambling or wager agreement.

1. **Gambling and insurance**

   Consider a game of cards, where one either loses or wins. The loss or gain happens only because the person enters the bet. The person who plays the game has no further interest or relationship with the game other than that he might win the game. Betting or, wagering is not legally enforceable in a court of law and thus any contract in pursuance of it will be held to be illegal. In case someone pledges his house if he happens to lose a game of cards, the other party cannot approach the court to ensure its fulfillment.

Diagram 3: Insurable interest according to common law



2 **Time when insurable interest should be present**

In insurance, insurable interest should be present at the time of taking the policy. In general insurance, insurable interest should be present both at the time of taking the policy and at the time of claim with some exceptions like marine policies.

d) Proximate Cause

The last of the legal principles is the principle of proximate cause.
Proximate cause is a key principle of insurance and is concerned with how the loss or damage actually occurred and whether it is indeed as a result of an insured peril. If the loss has been caused by the insured peril, the insurer is liable. If the immediate cause is an insured peril, the insurer is bound to make good the loss, otherwise not.

Under this rule, the insurer looks for the predominant cause which sets into motion the chain of events producing the loss. This may not necessarily be the last event that immediately preceded the loss i.e. it is not necessarily an event which is closest to, or immediately responsible for causing the loss.

Definition

Proximate cause is defined as the active and 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.

e) Indemnity

The principle of indemnity is applicable to Non-life insurance policies. **It means that the policyholder, who suffers a loss, is compensated so as to put him or her in the same financial position as he or she was before the occurrence of the loss event.** The insurance contract (evidenced through insurance policy) guarantees that the insured would be indemnified or compensated up to the amount of loss and no more.

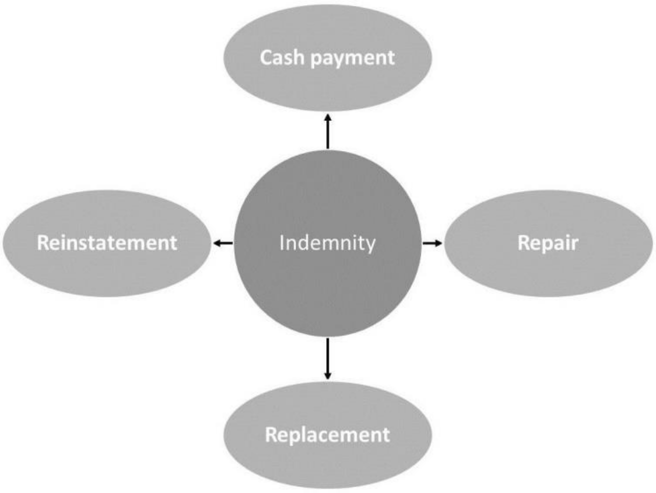
The philosophy is that one should not make a profit through insuring one's assets and recovering more than the loss. The insurer would assess the economic value of the loss suffered and compensate accordingly.

In most types of non-life insurance policies, which deal with insurance of property and liability, the insured is compensated to the extent of actual amount of loss i.e. the amount of money needed to replace lost or damaged property at current market prices less depreciation.

Indemnity might take one or more of the following modes of settlement:

- Cash payment
- Repair of a damaged item
- Replacement of the lost or damaged item
- Restoration, (Reinstatement) for example, rebuilding a house destroyed by fire

Diagram 1: Indemnity



But, there is some subject matter whose value cannot be easily estimated or ascertained at the time of loss. For instance, it may be difficult to put a price in the case of family heirlooms or rare artefacts. Similarly in marine insurance policies it may be difficult to estimate the extent of loss suffered in a ship accident half way around the world.
In such instances, a principle known as the Agreed Value is adopted. The insurer and insured agree on the value of the property to be insured, at the beginning of the insurance contract. In the event of total loss, the insurer agrees to pay the agreed amount of the policy. This type of policy is known as "**Agreed Value Policy**"

f) Subrogation

Subrogation follows from the principle of indemnity.

Subrogation means the transfer of all rights and remedies, with respect to the subject matter of insurance, from the insured to the insurer.