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Driven by distinction

DIP101: Unit-1

NATURE OF INSURANCE

UNIT ONE: OUTLINE

1;Concept of risk:

- The variety of ways the word risk is used.
- Definition of Risk.
- Components of Risk.

2; General classification of risks

- Characteristics of Insurable Risks

3;Methods of handling risks

Concept of Risk

- Insurance is a financial mechanism that responds to the challenges posed by risk to society.
- In fact, risk is the basic problem which insurance responds to.
- A discussion of the meaning of risks and the challenges it posed to society is therefore critical to an understanding of the role that insurance plays in mitigating the consequences of risks.

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The word is used in a variety of ways.

1. Risk as a Cause of Loss

- This refers to risk as something which may cause an unfavorable outcome. Hence we talk of risk of theft, accident, death, plane clash, fire etc

2. Risk as a Probability or Likelihood

- refers to the likelihood of something negative happening which means **the probability of occurring**
- e.g.- a house built near a river has a higher probability of flooding

  - a fast driver has a high likelihood of being involved in an accident.
- It is clear from this that there are different levels of risk or degree of likelihood because probability of occurrence could vary from very high to very low.

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3. Risk as the Object of Loss

- Here the object which can suffer a loss is referred to as the risk.
- eg ;cars, houses, planes, ships etc .
- It is therefore common for a surveyor who has been given instructions to surveyor a certain property by an insurer to be heard saying that they are going to see the risk.

4. Taking a Risk

- placing oneself in a situation where a loss can occur.
- Eg ;therefore buying shares, starting a new business or even crossing a busy street .

5. Chance

- We talk of risks when our minds are focused on an **unfavorable** outcome.
- When we focus our minds on a favorable or desired outcome, we talk of chance.
- Eg; talk of **the risk** of death, but **the chance** of passing an examination; **risk of being** involved in a accident, but **the chance** of crossing a swollen river.

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6. Risk signifies uncertainty in many situations in life.

- In broadest context the term risk describe situations in which there is an exposure to adversity
- Eg; one's house may catch fire or be broken into, one's car may be stolen or be involved in accidents, and one may be involved in an accident or die prematurely.

DEFINITION OF RISK

- The chance of loss;
- The possibility of loss;
- The uncertainty of loss;
- The dispersion of actual from expected results;
- The probability of any outcome being different from the one expected;
- A combination of hazards; or
- A condition in which a loss of losses are possible.

B. COMPONENTS OF RISK

Three vital components.

1. Uncertainty;
2. Levels of risk;
3. Risk as the cause of loss.

1. Uncertainty

- Uncertainty implies some **doubt about the future based on either lack of knowledge or imperfection of knowledge.**
- Exists even when the person exposed to risk does not know of its existence.
- For example, even though a drunken person crossing a road may not know of the risk one is facing, uncertainty still exists.

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2. Levels of Risk

2.1 Frequency and Severity

1. Frequency

- Risk is a combination of the **likelihood** of an event
- **Likelihood** refers to the probability of occurring.
- The higher the probability of frequency, the easier it becomes to predict the likely frequency and hence the lower the uncertainty.
- Eg; A good example of such high frequency risks is found in self service stores
- This requires Budgeting.

2. Severity

- **The impact** of an event is looked into in the right of its severity.
- People can accommodate the consequences of minor losses which occur all the time without any serious problems.
- However, they would be reluctant to shoulder high potential losses from events that occur rarely.
- This requires insurance

High frequency - low severity risks

- Occur often but with very minimal impact e.g.:

i. minor injuries while playing football
ii. Shoplifting

Low frequency - high severity risks

- Occur rarely but their impact is severe e.g.:

i. plane crashes
ii. marine accidents

Low Frequency/High Severity Risks

- loses occur very rarely but when they do, severity tends to be high.
- eg; in aviation and marine accidents. Only a few accidents are minor.
- In this category we also put death, theft of a car, burning of a factory and burning of one's house.
- these types of losses are the subject of insurance.

3. Risk as the Cause of Loss

- **Peril - prime cause of loss** e.g.

i. Fire

ii. theft

iii. hail

iv. earthquake.

- **Hazard- a condition that may increase or decrease the effect of a peril** e.g.

i. The nature of construction in fire insurance

ii. The state of health in life assurance.

3.1 Classification of Hazards

May be **physical** or **moral.**

1. Physical Hazards

- **The tangible characteristics that may increase or decrease the likelihood of an event**.

Examples in **fire** insurance are:

i. type of construction;

ii. location of the building; and

iii. the occupancy of the building.

In motor insurance:

i. the age

ii. the value of a vehicle.

2. Moral Hazards

- Arise from the nature and behavior of human beings connected with the subject matter of insurance.

Examples: On the part of the insured,

i. lodging fraudulent claims

ii. exaggerating losses,

iii. withholding material facts

iv. carelessness.

3. Morale Hazard

- Some scholars have a third classification of hazard called morale hazard.
- This refers to situations where losses increase because there is insurance cover in place.

Example of this are:

- When some people have purchased insurance, they may tend to be more careless in their dealing with the insured property;
- doctors, pharmacists, lawyers, and investigators have been known to charge more when they know that the cost will be met by insurers;
- courts also tend to give higher awards when they know that there is insurance in place.

C.GENERAL CLASSIFICATION OF RISK

- Financial versus non-financial risks;
- Pure versus speculative risks;
- Fundamental versus particular risks.
- Dynamic versus static risks

C.1 Financial versus Non-Financial Risks

- **Financial risks** - outcomes can be measured in monetary terms. Examples:

i. material damage to property after fire
ii. theft of goods.

- **Non-Financial risks** – outcomes may not be quantified in monetary terms. Examples:

i. choices of wrong careers
ii. loss of items with sentimental attachment, e.g. a locket given by a loved one.

C.2 Pure versus Speculative Risks

- **Pure risks - involve loss or break-even situations.** Examples:

i. Fire

ii. burglary risks.

- **Speculative risks - involve loss, break-even and the possibility of gain.**

Examples:

i. buying shares

ii. pricing of new products.

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C.3 Fundamental versus Particular Risks

Fundamental risks

- cause is beyond the control of human beings
- indiscriminate in their effects.
- impersonal in origin and consequences. Examples:

i. Hurricanes

ii. Earthquakes

Particular risks

- personal in origin and consequences. Examples:

i. Fire

ii. Theft

iii. motor accidents

Dynamic risks

- **are risks resulting from changes in the state of the economy.**

Examples:

i. changes in price levels,

ii. consumer tastes,

iii. income and technology.

- These changes may cause financial loss to some members of the society e.g. some factories may close down as a result of competition and changes in technology resulting in loss of jobs. Such changes generally benefit the society in the long run.
- However, they may make some segments of the society incur losses in the long run. Dynamic risks are unpredictable, as they do not occur with any degree of regularity. As a rule dynamic risks are not insurable.

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Static risks

- involve losses that would occur even if there were no changes in the economy.
- involve either the destruction of assets or changes in their possession.
- are generally natural perils and risks arising from dishonesty of individuals.

Examples include;

- theft, accidents, fire, flood and storms
- Society gains nothing from these risks either in the short or long run.
- Static risks are generally the subject of insurance.

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CHARACTERISTICS OF INSURABLE RISKS

- **Theory** - it is possible to insure any risk provided the insured is willing to pay the required premium and the insurer is willing to give cover.

- **In practice** – all insurable risks must possess the following characteristics:

Cont'd

- Fortuitous Nature
- Monetary value
- Insurable interest
- Homogenous exposures
- Pure risks
- Particular risks
- Public policy

a. Fortuitous Nature

- The happening of the event must be entirely fortuitous or accidental, as far as the person seeking insurance is concerned.
- it is not possible to insure against an event which will definitely occur because in such case, there is no uncertainty of loss and therefore there is no risk.
- Transfer of risk relates to the exposure which will suffer loss. This exposure is not known. Hence fortuitous

- This condition also rules out insuring inevitable losses such as;
  - wear,
  - tear and
  - depreciation as these are not accidental. It is known that they will occur.
- The best approach of handling such losses is to budget for them as it is known that they will occur.

- Any loss deliberately inflicted by the insured on the subject matter of insurance would also not attract any compensation because it is not accidental.
- One would have no moral right to complain about a loss that one visited upon oneself.
- Note, deliberate acts by other people are accidental in as far as the insured is concerned.
- Therefore for the risk to be insurable, its frequency and severity must be beyond the control of the insured and its occurrence must be accidental or fortuitous.

- In life assurance, it is known that death is a certainty ,However, what is insured in life assurance is the timing of death, which is unknown.
- The uncertainty of when death will occur- and the risk of pre-mature death, is the subject of life assurance.

b. Financial Value

- The purpose of insurance is to provide a financial compensation when an insured event takes place.
- The insurance is merely a financial system of providing compensation against losses. This is so for all classes of insurance.
- All risks insured against must result in a loss capable of being measured in financial terms.

- This concept is easy to understand in the cases of loss, **destruction or damage to physical property** as their loss can easily be quantified in money terms and compensation given within the terms and conditions of the policy.
- In liability insurances, **courts decide the level of compensation** due to the injured persons by taking into account such factors as the medical bills, their age and what they could have earned during the period they were disabled by the injury.

- In life and personal accident assurances, the amount payable is agreed on at the inception date of a contract.
- Ones death or accident resulting in disablement, the agreed amount is paid and the contract is deemed executed.
- The amount paid is not compensation; but a financial benefit payable as agreed, when the contract comes into force,
- The contract therefore, meets the requirement of the risk the loss being capable of being measurable in financial terms.

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- It will also be appreciated that there are some losses which may be difficult to quantify in financial terms because the items concerned have some sentimental value.
- Examples are items like
  - jewellery,
  - photographs,
  - manuscripts and
  - documents such as identification cards and passports, among others.
- Such are not normally insurable unless there is a contrary agreement.

c. Insurable Interest

- The practice of insurance is guided by a number of legal principles. One of the most important of these principles is that of insurable interest.

- This principle states that there must be a legally recognised relationship between the insured and the subject matter of insurance such that if the subject matter of insurance is damaged, lost or - in the case of a person- injured, the insured will suffer a financial loss.
- On the other hand, if it is the subject matter is not damaged, lost or injured, the insured will be able to derive a benefit from its continued existence in its current state.

- Without the application of this principle in insurance, it is easy to anticipate situations where a person could insure the property of someone else so that when the property is lost or damaged one receives a "compensation".

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d. Homogeneous Exposures

- Homogeneous means a sufficient number of exposures to similar risks, With these the insurer can be able to forecast or predict the expected loss with precision.
- In the absence of a large number of similar homogeneous exposures, it becomes difficult to predict the expected outcomes.
- Without being able to make this prediction, the law of large numbers cannot be applied and calculation of premiums would be difficulty.
- It is therefore a condition that for a risk to be insured there must be a large number of similar or homogenous exposures.

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e. Pure Risks

- **Pure risks** have two outcomes :
  - loss or
  - no loss.

  Examples

i. The risk of a house catching fire is a pure risk because the house either catches fire or does not catch fire.

ii. So is the theft of a car – either the car is stolen or is not stolen.

- **Speculative risks**, on the other hand, have three outcomes - loss, no-loss, or break-even.

Examples

i. Buying share in the stock exchange is a speculative risk because one can gain if the share price appreciates or loses if the price goes down. On the other hand, one breaks even if the price of shares remains the same.

ii. Staring a new business

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- All business ventures amount to speculative risks because they have a possibility of gain, break-even or loss.
- One cannot insure for making a loss in their business even if we have already said that insurance compensates someone for the loss that they make.
- The losses that one makes must be pure risks in order to be able to get compensation from insurance.

- If it were possible to insure the profit that a person hoped to make from business efforts, then there would be little incentive for one to do everything possible in order to generate profits.
- Lack of efforts to secure profits would still result in profit, because the policy would pay in the event of no profit being made.

f. Particular Risks

- Risks may be classified into
  - particular and
  - fundamental risks
- Particular risks are personal in origin and consequences. They affect individuals and companies or only a small segment of the population. They are normally the responsibility of those affected.
- They include the risk of
  - theft,
  - fire,
  - accident,
  - riot,
  - malicious damage.
- It is this category of risks that insurance normally deals with.

- Fundamental risks, on the other hand, makes them uninsurable in most cases.
- It is not, however, fully accurate to say that no fundamental risks can be insured, but it is true to say that, insurers are generally very selective in the choice of fundamental risks that they can insure.

- Fundamental risks which arise from the nature of society are not usually insurable.

Examples of these are

- war,
- changing fashions and
- inflation.

- Limited insurance is available for fundamental risks arising out of natural occurrences such as
  - typhoons,
  - earthquake,
  - tornadoes,
  - hail,
  - hurricane
- **As a rule, fundamental risks are looked upon as the responsibility of society and not simply the responsibility of those who opt for insurance.**

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g. Public Policy

- Public policy is what society considers being right and morally sound. Hence, all contract that deals with illegal goods such as narcotic drugs are illegal.
- Insuring another person goods and then deliberately causing loss or damage to them in order to benefit from insurance is also against public policy because the person who suffered the loss was not the one who was compensated.
- However, there are still other risks, which generally should not be insured.

- It is also not acceptable to insure against the risk of a criminal venture going wrong.
- For example
  - society cannot accept to have thieves effecting policies, which would pay them the expected "loss" if the police caught up with them and deprived them of the stolen goods.

- Neither can one insure against a fine imposed by a court of law if one is for breaking a law such driving while drunk. The risk they run is that a large fine could be imposed.

- There is a financial relationship with the loss, and it could be argued that the loss is fortuitous as far as the person is concerned.
- But society will, however, not accept that a person could be able to avoid a just punishment by simply entering into a contract of insurance; as this would defeat the purpose of a just punishment.

- **Every contract of insurance must therefore be in accordance with what the society considers to be just, fair and legal. In other words, it must be consistent with public policy.**

E. COST OF RISK

1. Frequency of risk

- Risks of a catastrophic nature have tended to occur more often than in the past. Examples : the Kenya Airways plane crash on the West African Coast, the Asian tsunami of 2004, earthquakes in Asia, Hurricane Katrina in the USA and Flooding in Mozambique.

2. Monetary cost or financial severity

- The recent world disasters have cost the insurance industry billions of shillings.
- Less visible costs such as loss of experience, quality, reputation, cost of retraining.

3. Human cost in terms of pain and suffering

- Insurers have tried to meet this cost by offering financial compensation.

F. Methods of handling risk

- Risk is a threat which is widespread, and, therefore, society must find proper ways of dealing with it;
- In developed countries governments handle some fundamental risks;
- In developing countries the governments' role in handling fundamental risks is passive or absent;
- Particular risks are handled by individuals;

The main methods of handling risks

1. Avoidance;
2. Retention;
3. Reduction; and
4. Risk transfer.

1:Avoidance

- Avoidance involves not engaging in a venture which one considers risky;
- For example, if one fears the risk of theft, they can avoid it by not venturing into businesses such as supermarket;
- It is a negative approach to handling risk as economic development cannot occur if people keep away from some economic activities.

2: Retention

An individual or organization handles the consequence of risk on their own.

- **Intentional or voluntary**
  - individual or organisation recognises the existence of risk but decides to retain it by creating a fund from which losses would be paid;
  - This is common if there are no attractive alternatives, e.g. when premiums are very high;
  - Guiding factor - the frequency and severity of risk;
  - Large, unpredictable risk requires insurance.
- **Involuntary retention**
  - Risk is retained simply because an individual or organisation does not recognise the existence of the risk.

Reduction

- Reduction takes place when steps are taken to **minimize** the frequency of a loss occurring or its severity should it occur;
- Before a loss occurs, measures may be taken to ensure that the frequency and or the severity of the loss are reduced to the minimum.

Examples:

- ➢ Police escort of money in money insurance;
- ➢ Employment of a watchman and burglar proofing in theft insurance.

- Again after a loss has occurred, steps can be taken **to reduce** its impact : **Examples:**

- ➢ sprinklers in fire insurance;
- ➢ Economic disposal of salvage in motor insurance.

Risk transfer

- Risk transfer occurs when the financial consequences of an event are shifted from one party to another. Examples:
  - a landlord may shift the risk of the house catching fire to the tenant;
  - The owner of goods can shift the risk of loss of or damage of goods to a transporter
- This is normally done through suitably worded contracts;
- The most commonly used method of risk transfer is insurance;

Insurance

- Insurance involves transferring of risk to some other party more competent to handle the risk;
- A person transfers the risk to the insurer that, in turn, spreads the risk to the **whole body of policyholders**.
- The insurance company in turn facilitates the spread of risk. To another insurance company- **Co- insurance**
- The company transfers the risks it feels it cannot handle on its own to other insurance companies through the process of **reinsurance.**
- Reinsurance companies can also transfer the risks they have assumed to still other re- insurance companies.
- This is called **retrocession**

Why insurance is a superior method of handling risks???

1. It anticipate losses and their chance or probability of occurring and plans for them;
2. It creates a fund out of which the few who suffer losses are paid;
3. It employs trained personnel to deal with insurance matters in tall the fields of operation;
4. It spreads risks nationally, regionally, and internationally through reinsurance (reinsurance is discussed in the subject: **Principles and Practice of Insurance**)
5. Premium payable is/are significantly less than the risk one is exposed to;
6. Once the contract of insurance is entered into, the insurer will pay for the loss provided premiums were paid and the insured observed the terms and conditions of the contract;
7. A contract of insurance is formal and is legally enforceable; and

- A contract of insurance is protected under the Insurance Act.

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THE END

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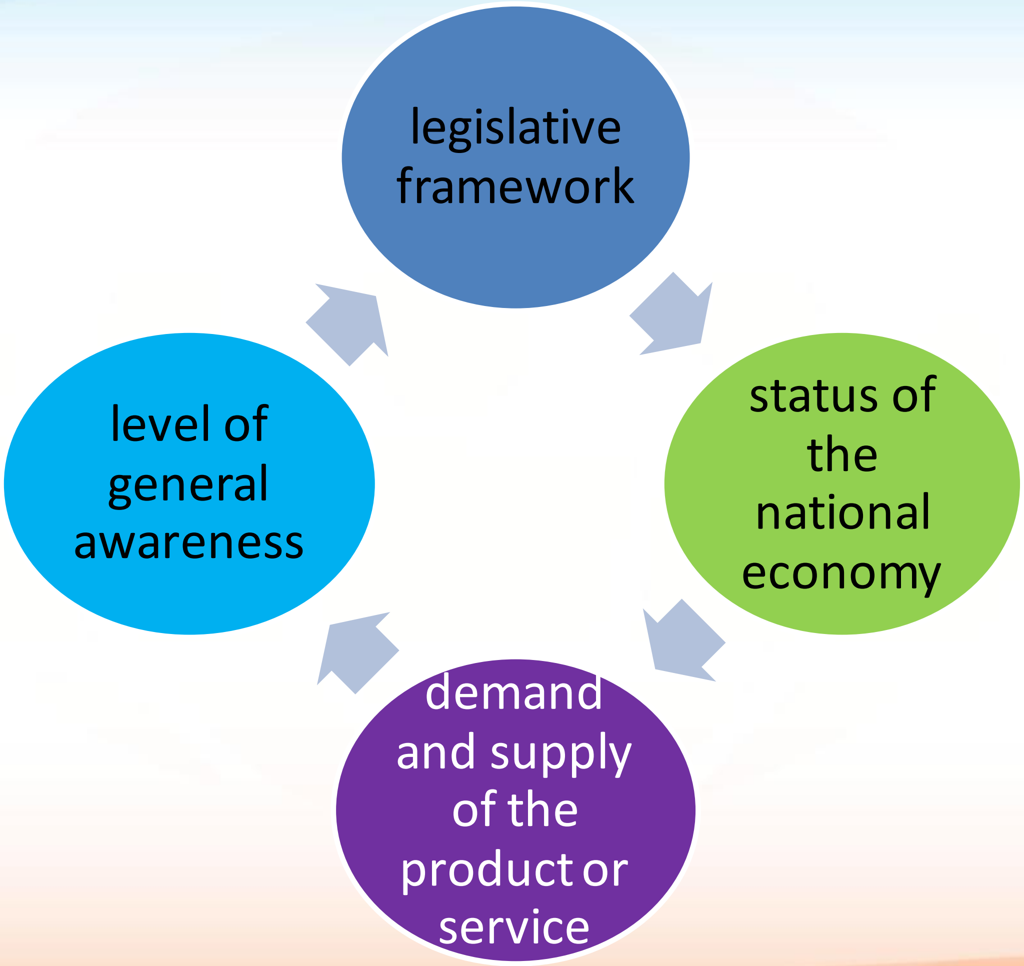
HISTORICAL DEVELOPMENT OF INSURANCE

DIP 101

UNIT-2

Development of any economic activity depends on:



A. Traditional Forms of Insurance

- Modern insurance is a relatively new idea in Africa as the concept was introduced by the colonial powers.
- However, African societies had some traditional methods of handling risks and uncertainties-the challenges with which insurance deals.
- Some examples of such traditional practices include:

i. Extended family system;
ii. Harambee;
iii. The Edir system;
iv. Age groups
v. Herd shifting.

1. Extended Family System

- This involves members of an extended family, clan or tribe sharing certain responsibilities such as meeting the costs of bringing up orphaned children.
- It was generally understood that an individual belonged to the extended family or clan and therefore, if one house caught fire, members of the extended family, clan or tribe would come together and assist in putting up another house.

2. Harambee

- This involves people coming together to contribute money for personal or community challenges such as a high medical bill or school fees in college.
- It is a relic of the extended family system and is still in existence today though it is fast fading due to misuse by a wide cross section of political leaders and others.

3. The Edir system

- The Edir system originated in Ethiopia.
- It was more refined and is still being practiced today.
- Under the arrangement, a group of people, usually with a common interest or background, agree to pay a certain sum of money to a fund used for helping out members of the group when faced with emergency needs such as the provision of funeral expenses.

4. Age Groups

- Members of the same age group i.e. those who went through rites of passage such as circumcision together would always come together to assist one of their own in the event of a bad incidence such as sickness or death in the family.

5. Herd Shifting

- Herd shifting was a system where a part of one's domestic animals – mostly cows, sheep and goats- were kept at a distance relative's place.
- This ensured that in the event of an outbreak of a disease in one area, a part of the herd would be saved.
- The relative would take care of the animals.
- His "premium" would be the enjoyment of the animal's milk or labor.

Short comings

- No underwriting was undertaken and no actuarial tables were used.
- The pool concept and modern investment methods were unknown.
- Neither was there reinsurance.
- They only made arrangements to cater for a loss after it had occurred.

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- On the other hand, modern insurance scientifically predicts losses and create a fund up front to cater for them.
- With the introduction of modern economic systems, the traditional methods of insurance have gradually given way to the modern insurance practices.

B. HISTORY OF THE MODERN CLASSES OF INSURANCE

Marine Insurance

- Origin of the present day insurance can be traced to early maritime trade.
- Merchants, whose goods were being carried on the same ship, shared in the losses of fellow merchants.
- As much as this practice reduced the risk of loss, each merchant could not know in advance of the voyage what the individual share of loss would be.

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- Marine insurance evolved to address this need.
- Lloyds of London was among the early providers of modern marine insurance.
- The largest market of marine insurance in the world today.

Fire Insurance

- Great Fire of London 1666.
- Lasted five days.
- Virtually wiped out the entire town structures then built of wood.
- Largely responsible for the beginning of fire insurance.
- Following the fire, several companies came up which provided fire insurance as reconstruction work was undertaken.

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Personal Accident Insurance

- Product of the Locomotive Engine.
- Early trains were prone to accidents and risk of fire by flying sparks.
- Policies were issued to compensate **train passengers** against **rail accidents**.

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Motor Insurance

- First motor vehicle appeared on the United Kingdom's roads in the 1890s.
- Its use as a means of transport grew considerably during and after the First World War.

- Motor vehicle accidents led to an agitation for compensation.
- Culminated in the passing of the Road Traffic Act, 1930 - compulsory compensation for injuries.
- Kenya - The Insurance (Motor Vehicles Third Party Risks) Act in 1946 - compulsory third party motor insurance.

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Life Assurance

- Established by a group of people bearing the same risk.
- Each contributed an equal amount of money monthly.
- When one of the members died, the accumulated amount would be shared at the end of the year amongst the dependants.
- No fixed amount was payable - sum assured depended on the total contributions and the number of deaths during the year.

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- 1756 - statistics had been collected to make it possible to establish a minimum fixed amount payable on death.
- Beginning of the use of ***mortality tables*** in life assurance.

- First half of the 19th century, only term assurances were being offered.
- Any one could take a policy in the life of another.
- There was a possibility of that person dying and they gain.

- Resulted in gambling which led to the introduction of the **Life Assurance Act of 1774.**
- Popularly known as the Gambling Act.
- Prohibited people from taking out any life policy on the life of another without having an insurable interest in the life assured.

Development of the Insurance Industry in Kenya

- Modern insurance introduced in Africa about 100 years ago by colonial powers.
- African societies managed risks through the extended family, clan or tribe.
- National spirit of Harambee is an offshoot of this system.
- Stumbling block for the development of modern insurance.

Evolution of insurance in Kenya

Period before the Insurance Companies Ordinance Cap 486 which became effective on 2nd May 1961.

Period after the Insurance Companies Ordinance.

Period after the Insurance Act Cap. 487, 1984.

Period Before 2nd May 1961

British settlers introduced insurance to Kenya.

Initially operations were carried out by agencies of the home companies.

Full companies developed running branch offices.

Submitted regular returns to the parent companies in their countries of origin.

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#1 First Companies to operate:

1. **1904** - London and Lancashire Insurance Company appointed agents to cover Nairobi only.

2. **1922** - Royal Exchange Assurance was the first to open a full branch office.

3. **1929** - Commercial Union opened branch office.

No local insurance industry because:

Branch offices were operating as extensions of their parent companies abroad.

There was no local retention.

They were not controlled by any specific local legislation.

Local proprietors started setting up insurance companies.

1. **1930** - Pioneer General Assurance Society Limited
2. **1937** - Jubilee Insurance Company Limited
3. **1948** - Pan African Insurance Company Limited.

- **1961 - 14** insurance companies operating in Kenya and transacting all classes of insurance business.

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The industry was subject to the British laws.

Industry was developed along the British practices.

The insurances being transacted were mostly **fire, marine cargo** and a little **motor** insurance.

Period from 2nd May 1961

- The Insurance Companies Ordinance – Cap.486.
- Legislation of an insurer required:

1. **local incorporation** in Kenya or East Africa
2. **licensing** by the Registrar of Companies.

Paid up Capital

- Not less than £50,000.
- Mutual associations:

i. £20,000 in case of Life Assurance

ii. £20,000 for each of the other classes of non-life business transacted.

- The amounts were to be **deposited with the Registrar of Companies.**

- For the first time, local insurers were required to maintain a certain **level of solvency**.
- Required to conduct their **business on sound insurance practice**.

- The major developments in the insurance industry started during the post-independence period.
- Kenya National Assurance Company Limited – **1964**
- Kenya Reinsurance Company Limited – **1970**

Turning point

- **1978** - Minister for Finance directed that all imports and exports in the country be insured with locally incorporated insurance firms.

This was insurance for **marine cargo**.

The Insurance Act Cap 487 (1984)

- Enacted in 1984 and came into effect on 1st January 1987.
- Geared towards:

1. **supervising** and **regulating** the Insurance industry
2. protecting members of the insuring public.

IRA

Requirements for the Insurance companies under the Act include:

- a third of the board members must be Kenyan;
- minimum capital requirements;
- reinsurance arrangement to be approved by the Commissioner of Insurance
- solvency margins;

- accounting records to be submitted to the Commissioner in a prescribed format;
- top management to be approved by the Commissioner;
- limitation of management expenses;
- control of commission payable to intermediaries;
- investment guidelines.

Classes of insurance were classified as follows:

- fire Insurance
- theft Insurance
- liability Insurance
- motor Insurance
- personal Accident
- engineering including contractor's all risks
- workmen's compensation/employer's liability
- marine and aviation
- long term insurance, which includes life assurance

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C: Common Features in the Development of Insurance

1.most of the general insurance classes **developed after the industrial revolution.**

2.insurance companies and Lloyds of London have **perfected the methods of practicing insurance** over the years and a large part of present day practices originates from them.

3.most classes of insurance have **developed in response to a demand for protection** by the society.

4.Insurance companies started off as **specialist companies**.

5.Companies have **gathered considerable experience in many forms of insurance**.

6.The **growth of reinsurance** gives insurers financial protection.

7. Growth of certain classes of insurances was given a major boost by **the passage of legislation** eg Employees compensation and motor vehicle 3rd party risks

- Measure of government control of Companies legislation by way of for example **Life assurance Act 1774 and the Marine Assurance act 1906** have influenced insurance practice up to this day.

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Challenges to the development of the insurance industry

1.poor economic growth - lack of purchasing power.

2.cultural practices and norms-discourage the growth of the industry as individuals still tend to rely on the support of the extended family.

3.lack of product development by insurers to enable them offer products that satisfy the changing needs of the public.

4.Inadequate selling skills and unethical practices – led to negative image.

5.Competition - in the 1990s the Insurance industry experienced a wave of emerging new products e.g. Health Management Organisations (HMOs) and Banks (Bancassurance).

6.Lack of general awareness

THE END

COLLEGE OF INSURANCE

Driven by distinction

UNIT -3

INSURANCE

AND

THE ECONOMY

INTRODUCTION

Meaning of Insurance

- The business of insurance involves transferring the risk of loss from individuals and organisations to insurance companies;
- The risk is transferred when the person who desire insurance enters into a contract with an insurance company;
- Some of the terms commonly used in the business of insurance are now discussed here below:

Terms used in insurance

Insurance contract

- Is an undertaking or agreement in which one party, the insurer, agrees for a return of a small consideration, called premium, to pay another party, the insured/policyholder, a sum of money, or its equivalent, if a specified event occurs within a stated period.

Insurer

- The insurer is the party that agrees to pay a sum of money to another party on the occurrence of a stated loss;
- This is therefore the insurance company whose main duties are:
  - Procuring business from prospective clients;
  - Scrutinizing and making decision on the various types of proposal and deciding on whether to accept to give insurance cover or not;
  - Paying claims.

Insured

- The assured is the policy owner and is the person entitled to receive money under an insurance contract on the happening of a stated event within the stated period of time.

Premium

•This is the amount of money or price paid by the insured to secure the payment of the sum insured on the happening of the loss insured against;

•The premium is paid to the insurance company for the assumption of the risk insured against.

Insurance policy

•This is the document which evidences the existence of an assurance contact.

Sum assured

•This is the amount of money payable on the happening of the event assured against.

Policyholder

•The policyholder is the person who is the legal owner of the policy and has secured the contract with the insurer;

A. Functions of insurance

- There are three main functions of insurance.
- They are:

I. Transfer of risk

II. Creation of common pool; and

III. Working out equitable premium.

1.Risk Transfer

- The first and primary function of insurance is to act as risk transfer mechanism.
- Insurance does not prevent losses from occurring.
- Even when one insures one's property, the risk of loss is not removed.
- Transfer of risk, and insurance only assists in transferring the financial consequences of the insured peril to an insurer.
- In return, the insured pays a premium.

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Cont'd

- Even when a property is insured, the risk of loss is not removed;
- Transfer of risk the insurer only assists in shifting the financial consequences of the insured peril to an insurer;
- In return, the insured pays a premium as the price of buying insurance.

2.Creation of a common pool

- Second function of insurance is to create a common pool.
- An insurance company gathers people who want insurance protection.
- It takes contributions in the form of premiums (price of insurance) from many people exposed to similar risks.
- It creates and sets itself to operate a common pool the pool.

- From the pool, it pays the few who incur losses.
- Pool mechanism is based on the premise that the unfortunate few will be compensated by the fortunate many.
- Insurers use past experience to determine losses that are likely to occur in a year.

- For example, if past experience shows that five out of 500 houses valued at Kshs.2,000,000 each are likely to be damaged by fire within the year, the loss expected would be:

Kshs.2,000,000 x 5 = Kshs.10,000,000

$$\text{Premium} = \frac{\text{Amount of loss}}{\text{No. of policyholders}}$$

$$= \text{Kshs.}\frac{10{,}000{,}000}{500} = \text{Kshs.}20{,}000$$

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3.Equitable premium

- The third function of insurance is to collect equitable premiums from members of the common pool., i.e., those who choose to insure;
- An equitable premium is a fair premium;
- Insurance makes it possible to pay a premium that reflects the risk insurance companies has insured;
- This is arrived at after taking into account such factors are value, history of loss, age, and frequency and severity of exposure to risk of the subject matter of insurance.

- Example:
    - ➢A person proposing to insure a wooden house would be charged a higher premium than that of a person proposing to insure a stone house.
    - ➢Similarly, a person who proposes to insure a house valued at Kshs.4,000,000 would have to pay a higher premium than a person who proposes to insure a house valued at Kshs.2,000,000.

Other examples

- A house constructed of timber and roofed with corrugated iron sheet represents a higher risk of catching fire than one constructed of stones and roofed with tiles;
- A mobile phone shop represents a higher risk of theft than a bookshop because mobile phones are more attractive to thieves than books. Other businesses with high level risk are shops dealing with cell-phones, tobacco, and wines and spirits;
- An inexperienced and young male driver has a higher chance of causing an accident when compared to an middle aged and experienced driver; and
- A person who drives a lot has a higher chance of being involved in a road accident when compared to one who hardly drives.

- Risks also vary from one subject matter of insurance to another. Hence, one insuring big a factory cannot be expected to pay the same premium as one insuring a motor cycle as factory value is be much higher than that of a motor cycle.

In summary we may note that each risk will vary from others depending on:

- The perception of the expected:
- Frequency; and
- Severity.

- It is the duty of the insurer to assess the risk in each case and fix a premium that is consistent with the magnitude of the risk introduced to the pool in terms of frequency and severity.

- The process of assessing the amount of the risk introduced into the pool by each unit of exposure and deciding on the terms of insurance is called **underwriting.**

COLLEGE OF INSURANCE
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B. The importance/Benefits of insurance

- Insurance has evolved to safeguard the interests of people from uncertainty by providing certainty of payment when unforeseen events occur causing losses.
- The role and importance of insurance can been discussed in three phases:
  - uses to individual;
  - uses to a special group of individuals i.e. business or industry; and
  - uses to the society.

COLLEGE OF INSURANCE
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Economic Benefits

i. Peace of mind
ii. Protection
iii. Savings
iv. Investments
v. Reduction and control
vi. Invisible earnings

Peace of mind

- Security wish is the prime motivating factor for arranging insurance;
- Lack of security creates uncertainty and may discourage investment;
- Secondly, factors which cause loss such as fire, vehicle accidents and death are almost always beyond the control of the person who suffers from them;
- By means of insurance the uncertainty that centres about the wish for security and its attainment may be eliminated.

Protection on mortgaged property

- At the death of the owner of the mortgaged property, the property is taken over by the lender of money and the family will be deprived of the use of the property;
- A life policy provides adequate amounts to clear the loan balance;
- The lender may wish to get the property insured because in the event of its damage or destruction the borrower may be unable to continue paying the loan.

Protection

- This is all the more important in life assurance where a policyholder is assured that in the event of pre mature death, one's dependants will be paid a lump sum or an income to mitigate the financial consequences of the death.
- In businesses the security from losses which insurance provide means that losses which would be devastating to the firm will now be passed on to the insurance company.
- This way, management will be able to concentrate in running the business without fear of losses.

Life insurance encourages saving

- The elements of saving and investment are present only in the life insurance;
- In most life policies the element of saving predominates;
- Many policies combine savings and protection;
- The saving with insurance has certain extra advantages such as;
  - ➢ systematic saving is possible because regular premiums are required to be compulsorily paid;
  - ➢ An estate is created immediately the policy comes into force;
  - ➢ Money saved with the insurance company can earn interest in the form of bonuses;
  - ➢ The interest earned through bonus is tax free;
  - ➢ Premiums contributed enjoy tax relief

Investments

- Life insurance provides profitable investment Individuals unwilling or unable to handle their own funds have been pleased to find an outlet for their investment in life insurance policies;
- Endowment policies, multipurpose policies, deferred annuities can provide a better form of investment;
- The elements of investment like regular saving, capital formation, and return of the capital along with certain additional returns like bonus or interest are perfectly observed in life insurance;
- In Kenya, the insurance policies carry a special exemption from income-tax;
- Life assurance policies thus provide individuals with a mechanism for investing regularly.

Loss control and reduction

- Insurers are actively involved in the reduction and control of losses;
- Through the efforts of the insurers, and reinsurers public education in insurance takes place.

Pre-loss control

Pre-loss Control

- the effect of the loss is anticipated and steps taken to ensure that the frequency and (or) the severity of the loss are reduced to the minimum.
- In most cases before an insurer can agree to give cover, they will employ the services of an insurance surveyor who will visit the risk, surveyor it and make suggestions on how the risk can be improved.
- Insurers pay the surveyor's fee. Surveyors are commonly used in fire, theft and liabilities risks. loss preventive

Examples:

i. Police escort in money insurance

ii. employment of a watchman and burglar proofing in theft insurance.

- Insurers and insurance brokers are also involved in educating their insured and their employees, in particular, and members of the public in general on loss minimization measures.

e.g.- by sponsoring programs on loss minimization on the television or radio stations

- by sponsoring articles in the print and electronic media.

For example in the 1970s the defunct Kenya National Assurance Company Ltd used to sponsor a radio program dedicated to educating the public on loss minimization measures.

- The National Hospital Insurance Fund also has such a program going on currently in the Kenya Broadcasting Corporation (KBC) Radio Station.

Post-Loss Control

- Whenever a major loss occurs the insurer concerned appoints a loss adjuster.
- The main brief of the loss adjuster is to quantify the extent of the loss and advice on whether the claim is payable or not under the policy.
- However, a loss adjuster is also expected to investigate the cause(s) of the loss and make recommendations on the measures that could be put in place so as to avoid similar future losses.
- A loss adjuster is also expected to advice the insured and the insurer on the most economical methods of disposing the salvage, if any.
- Any money realized on disposal of the salvage mitigates the loss.

6. Invisible Earnings

- The insurance industry can be a contributor to the balance of invisible trade for a country.
- This can be through either direct insurance or reinsurance.
- When individuals and companies from neighboring countries insure in Kenya, the country becomes an exporter of insurance services.
- The same happens when a local insurer accept reinsurance business from, say Tanzania.
- Of course, claims will have to be paid and therefore sometimes the invisible account can register a deficit

SOCIAL BENEFITS

Insurance also avails social benefits to the community. Among these are:

- Job creation;
- Job retention;
- Prevention of economic disruption;
- Provision for old age; and
- Provision for Education.

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a. Job Creation

- As we have already noted investors have the confidence to put money in commerce and industry because insurers give assurance of compensation in the event of a loss.
- These investments create job opportunities in the society.
- At the same time, the various players in the insurance industry employ people to undertake the various tasks that they perform.
- Such includes, but are not limited to selling, claims handling, underwriting and reinsurance.
- It will be appreciated that in a developing county such as Kenya, unemployment is always a challenge. Any system therefore that alleviates it is desirable pay a positive role in the wellbeing of the society.

b. Job Retention

- In the event of an occurrence of an unfavorable event, such destruction by fire, an organization does not have to close down and render employees jobless.
- This is because the insurer concerned will pay a compensation for the loss.
- The victim of the loss will therefore be able to go on with the business. This ensures that jobs are retained.

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c. Provision for old age

- Life assurance provides a mechanism through which people can save for old age.
- This can be done for example through the purchase of endowment assurance policies which mature at the time of retirement or of annuities which are payable from the age of retirement until death.

d. Provision for education

- It is possible for parents to use life assurance to create a fund to be available at the time that the child is expected to enter school or university by arranging for an appropriate endowment policy.
- through a term policy, a parent can ensure that a lump sum is payable in the event of their pre mature death and the same is used to pay school fees of the child.

e) Avoiding Disruption of a Community

- When insurers provide funds for reconstruction of a property destroyed by perils, it means that the economic activity can be able to go on, that is, goods and services can continue to be produced and therefore available to the citizens.
- The social disruption of the other businesses linked to the insured business, which has suffered a loss, either as suppliers, employees or buyers is likewise avoided.

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THE END

REVISION QUESTIONS

1. Highlight/Explain three common features of development of insurance.
2. Highlight four benefits an individual gets from purchasing insurance.
3. List three examples of pre-loss /post loss measures
4. Outline six reasons why insurance is considered the most superior method of handling risks.
5. State three ways insurance provides protection.
6. State/Explain three components of risks
7. State/Explain three functions of insurance.
8. State/Explain four cultural practices that are similar to insurance.
9. State four advantages and disadvantages of self- insurance
10. State two ways a risk may be retained.
11. What do you understand by the term public policy.

Revision Questions

1. State four methods of handling risks.
2. Outline three ways in which insurable risks may be classified.
3. State five economic benefits of Insurance.
4. Explain the two levels of insurable risks.
5. List four circumstances under which moral hazard may arise.
6. Distinguish between fundamental and particular risks.

REVISION QUESTIONS (Eassy)

1. Explain six characteristics of insurable risks.
2. Explain three functions of Insurance.
3. Explain six ways insurance aids investment in the nation.
4. Explain five benefits a company derives from voluntarily retaining risks.
5. Explain four social benefits of insurance.
6. Outline five factors that have hindered the growth of insurance in Kenya.
7. Outline four traditional methods similar to insurance.
8. Outline four ways insurance effectively spreads insured risks.
9. Explain speculative risks, and give three such risks that are insurable.sAZX

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THE STRUCTURE OF THE INSURANCE MARKET

DIP 101

UNIT-4

INTRODUCTION

- Traditional market place is a physical location/place where buyers and sellers meet to transact business.
- This is possible for tangible commodities.
- For insurance industry, there is no single place where the buyer, sellers and middlemen meet to transact insurance except Lloyds in London

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Cont.

The insurance market place refers to a mechanism by which buyers and sellers come together.

Buying and selling of insurance takes place any time whenever it is required and convenient to the parties e.g. through phone, fax, e-mail, physical contact with each other or an intermediary.

Players in the Insurance Market Place

The insurance market comprises:

- **Sellers**
- **Buyers**
- **Intermediaries/Middlemen**
- **Service providers**

A. SELLERS OF INSURANCE

Insurance companies, captives and reinsurance companies.

There is also self-insurance.

Insurance and reinsurance companies are limited liability companies with shareholders as the owners.

A. 1 Insurance Companies

- In order to transact business in Kenya an insurance company must among other requirements be:
  - Incorporated under Companies' Act.
  - Licensed under the Insurance Act.

Currently there are 43-49 licensed insurance companies in Kenya.

Classification of Insurance Companies

A.1.1 Type of business

A.1.1.1 Life Insurance companies:

- Underwriting only long-term business (life, pension and annuities) e.g. Old Mutual, CFC life, Trinity and Metropolitan.

A.1.1.2 General insurance companies:

- Underwrite short-tem insurance only (property, liability, heath and pecuniary) e.g. Lion of Kenya, Real, Fidelity.

Cont'

A.1.1.3 Composite:

- Underwrite both long-term and short-term business e.g. Britak, ICEA, Kenindia, Jubilee.

A.1.1.4 Specialist:

- Underwrite only one class of insurance either in long-term or short-tem business only e.g. Direct Line Insurance Co. (Motor class)

A.1.2 Classification by form of ownership

A.1.2.1 Proprietary companies:

- Owned by shareholders who appoint board of directors to run the firm.

A.1.2.2 State- owned companies:

- Owned by government who appoint the directors to run the firms.

A.1.2.3 Captive companies:

- Subsidiaries formed by a parent company to underwrite some of their insurable risks.

A. 1.2.3 Reinsurance Companies

- Companies formed to give insurance protection to insurance companies.
- Insurers transfer to reinsurers whole or part of the risks they have assumed from policyholders.
- An insurer may find the risk too big for its own account and, therefore, seeks cover for the excess amount of risk.
- If an insurer insures part of the risk it has assumed, this is called reinsurance.

Cont’

- In Kenya there are **2** locally incorporated reinsurance companies,

  which are Kenya Reinsurance Corporation and East Africa Reinsurance Company and **2** regional reinsurance companies, Zep Re and Africa Re
- Reinsurance Companies formed to give insurance protection to insurers.
- Insurers transfer to reinsurers whole or part of the risks they have assumed from policyholders.

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Kenya Reinsurance Corporation

- In a bid to save foreign exchange, an Act of Parliament set up the Kenya Reinsurance Corporation in 1970 with the main purpose of creating local reinsurance capacity by offering compulsory reinsurance in the Kenyan market.
- It is a government parastatal which initially used to receive mandatory cessions of business from direct underwriting companies.

Cont'

- The cessions were mandatory in that direct insurers had no option but to cede at least a given amount ob business to the Corporation.
- Mandatory cessions have been phased out after which the corporation have to compete for business like any other reinsurance company.
- At the moment, Kenya - Reinsurance still enjoy 18% mandatory treaty cessions.

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A.1.2.4 Self-insurance

- Funds set aside to meet certain losses.
- An alternative or in addition to insurance.
- Mostly used by some big organisations who feel that:
    - They strong enough financially;
    - Self-insurance is cheaper than commercial insurance; or
    - Market does not cater for their special needs.

COLLEGE OF INSURANCE
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Characteristics operational programme:

- Organization must be big enough to make the losses predictable;
- Plan must be financially dependable;
- Exposure units should be widely distributed geographically so as to prevent a catastrophe wiping out the fund.

Advantages of self-insurance

- No business acquisition costs, commissions or administrative costs and profit margins hence premiums are lower.
- Interest return on investment and profits belong to the insured.
- Claims are settled without dispute.
- Insured has an incentive to reduce and control the risk of loss.
- Adverse claims experience of other organizations does not increase premiums.

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Disadvantages

- In times of difficulty there may be temptation to borrow from the fund.
- Catastrophe may occur and wipe out the whole scheme.
- Funds are kept in short-term easily convertible form, which earns little interest.
- There may be criticism by shareholders because the creation of the fund appears to reduces their profits.
- There is no spreading of risk rinciple of insurance

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B. BUYERS OF INSURANCE

- Individuals
  - Private individuals
- Organisations
  - Government organisations
  - Parastatals
  - Counties
  - Industrial organisations
  - Commerce organisations

Organization of Insurance Companies

There is no uniformity is practice or of titles between companies but the following functions are performed in all the companies:

- Board of Directors
- Chief Executive Officer/Managing Director
- Company Secretary
- Management Services
- Personnel
- Accounts
- Investment
- Information technology

NOTE : Diagram on pg141

COLLEGE OF INSURANCE
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Board of Directors

- They formulate the overall plan of operation of the company in the best interests of the owners taking into account the interests of policyholders, staff, the public and the effect of market competition.
- They comprise both executive (working) and non-executive (non-working) directors.
- Executive directors are often persons of status who add prestige and experience to the company.

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CHIEF EXECUTIVE OFFICER/MANAGING DIRECTOR

- He is a member of the board of directors and carries the duty of implementing decisions at the organization level.
- He is the executive director.

COMPANY SECRETARY

- The role of the company secretary is the administration of the organizations and ensuring that the company complies with company and insurance company law.

MANAGEMENT SERVICES

- These are specialists employed to ensure that the company keeps up with changes in the market e.g. statisticians and economists, organization and methods staff.

PERSONNEL

- This department ensures that employees are well trained, remunerated and motivated. They also recruit staff.

ACCOUNTS

- The accounts function is very important in insurance.
- There are stringent regulations for the reporting of insurance accounts.
- The accountant works closely with the company secretary.

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INVESTMENT

- The reserves of funds held by insurance companies must be invested for security and income.
- If long-term business is transacted an actuary must be consulted and there may be an investment manager or the life manager.

INFORMATION TECHNOLOGY

- is central in financial services to enable them control their exposure to risk and define the process by which they deliver their service to their customers.

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Geographical organisation of Insurance of Insurance Companies

- Most Kenyan companies are only based in Kenya but with the establishment of the East Cooperation several insurance companies and brokers have opened offices in Tanzania and Uganda.
- Within the country most insurers and brokers have a head office usually in Nairobi and branches in other towns.
- Life companies have more branches than general insurance companies.
- There are a few foreign companies operating in Kenya with their head offices in other countries for instance Old Mutual and Pan Africa Life and AIG.

An insurance company may have:

Executive Head Office

- These may be located in a capital city.

Administrative Head Office

- This carries out the main management and underwriting functions.

Main branches

- These are responsible for initial underwriting within their area and that of their sub-branches. They are also responsible for claims handling and mainly for sales promotion.

Sub-branches

- The main purpose of a sub-branch is sales promotion in its area.

See Diagram –pg142

Decentralisation of authority

- The organization of an insurance company can range from complete centralization of all decision making at head office to complete decentralization with branches having wide ranging powers within broad guidelines.
- The regional system lies between these two extremes.

Centralisation

- In this system, all underwriting, claims, policy drafting, renewals and accounts work is handled from head office with the branches merely being sales outlets.

Centralization

Advantages

- Uniformity of policy, practice and routine
- Most economic use of mechanized methods
- Fewer experts required with resultant saving in salaries.
- Branches relieved of routine work and can then concentrate on selling.

Disadvantages

- The system is often run from an area of high salary, building and rating costs e.g. Nairobi.
- Poor service can result from the administration being remote from the customer.
- Excessive power in a few hands. Dictatorial attitudes can develop in underwriting to the detriment of the company.
- Lack of promotion prospects for most staff.

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Decentralization

Advantages

- Local officials will best understand local conditions
- Good local service is possible
- Branch staff become more knowledgeable by having to make decisions
- Brings democracy to the underwriting policy of the company,
- Creates better staff morale by providing more chances of promotion to the higher grades of post required at the branches.

Disadvantages

- Many experts will be required, with a higher salary bill as a result.
- Branches inundated with routine work, instead of concentrating on selling which is their main function.
- Wasted effort in trying to make each branch expert in everything.
- Divergence of practice is likely to develop between branches and this can be embarrassing if it becomes known to the public. It could also lead to misleading statistics.

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Importance of management

- Selects good business;
- Charges appropriate rates- i.e. rates which are competitive, within the law and any market agreements that the company may have entered into;
- Crafts suitable policies;
- Carefully selecting service providers;
- Engages in prudent investments decisions;
- Continuously developing new products to meet the changing needs of customers;
- Seeks to continuously expand it premium income, return on capital, market share and profitability;
- Adopting a positive altitude towards it obligations to policyholders and claimants.
- etc

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C. INTERMEDIARIES

- Insurance may be bought directly or through intermediaries.
- The main intermediaries operating in the Kenyan market are:
  - Insurance Agents and
  - Insurance brokers

C.1 Agents

- An agent is a person who acts for or on behalf of another.
- Insurance agents represent insurance companies.
- They represent as many companies as they wish in the Kenyan market.
- For one to be an agent, one has to possess a Certificate of Proficiency (COP), be appointed as an agent by a principal and be licensed under the Insurance Act

C.2 Insurance Brokers

- Are specialists in the field of insurance and their full time occupation is the placing of insurance.
- As specialists, they are required to uphold high standards of expertise and are required to place the interest of their client before all others.

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Cont'

- Some specialise in one field of insurance e.g., motor, medical or reinsurance .
- Free to represent all licensed insurance companies.
- There are currently 137 licensed insurance brokers in Kenya.

NOTE- functions- Pg-135

C.3 Health Management Organizations (HMOs)

- HMOs provide an array of medical services on a pre-arranged basis.
- Provide healthcare services by giving in-patient and outpatient cover, road and air evacuation, funeral expenses, personal accident insurance, etc.
- Some of them own their own health clinics, diagnostic laboratories and ambulance services.

Cont'

- Until December 2004, HMOs were giving unfair competition to insurers as they were offering insurance services without being regulated.
- From January 2005 they were

  brought under Insurance Act through the Insurance (Amendment) Act 2003.

Provisions of amendment in respect to HMOs

- Now referred to as Medical Insurance Providers (MIPs);
- Are categorized as insurance intermediaries as they do not carry risks;
- If an MIP wants to carry risks then they must fulfill the same licensing requirements as insurance companies.

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Current MIPs classification depending on mode of operation

- MIPs now classified into three categories depending on their mode of operations.
  - Broker selling medical insurance covers provided or underwritten by insurance companies;
  - Those managing funds on behalf of clients to pay for medical claims incurred and receive a fee from clients for the service;
  - Those giving cover to their clients and reinsure with insurers/reinsurers.
  - Also undertake health management of their clients by operating their own clinics. Ensures that claims are properly controlled.

D. SERVICE PROVIDERS

- Are persons who provide various types of services to the insurance industry.
- Main ones are the:
  - Surveyor
  - Risk Manager
  - Loss Adjuster
  - Motor Assessor
  - Loss Assessor
  - Investigator
  - Claims Settling Agent

D.1 The Surveyor

- Assesses the extent of the risk to which the insurance company is exposed.
- Gives advice on the extent of the risk exposure and risk improvement measures.
- Advises on rates, terms and policy conditions.
- It advisable that a surveyor be consulted at the planning stage of a project to give advice before the commencement of insurance cover.

Cont'

- A surveyor may be needed in almost all classes of insurance but is mostly used in fire, burglary

  and marine insurance.

- In marine insurance business they survey or assess losses on behalf of the insurer or the insured.

Currently in Kenya there are 26 licensed

surveyors.

D.2 The Risk Manager

- Risk managers deal with identification, analysis (measurement) and control of risks. Risk control may take the form of, avoidance , reduction, retention, insurance and transfer to a third party.
- They set up and advice on programmes of loss minimization

Currently in Kenya there are **5**

licensed Risk managers.

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D.3 The Loss Adjuster

- Are professionals qualified to investigate and assess magnitude and cause of loss.
- Also advise on loss minimisation and negotiate with policyholders and insurers on claim settlement.
- May also settle losses of big magnitude on behalf of the insurer.
- Though commissioned insurers they operate independent of them.

COLLEGE OF INSURANCE
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Functions of loss adjusters

- Investigate the cause of the loss;
- Assess the magnitude of the loss;
- Advise on policy interpretation;
- Negotiate on the quantum payable;
- Check on breach of warranties and policy conditions and advice the insurance company accordingly;
- Advice whether the loss falls within the policy terms;
- Advice on how similar future losses can be avoided;
- Advise on the most economical method of disposable of salvage if there is any.

COLLEGE OF INSURANCE
Driven by distinction

D.4 The Loss Assessor

- Like loss adjusters, insurers appoint loss assessors after a loss has taken place to quantify the magnitude of loss and advise on the method of compensation.
- Are used mostly in general classes of insurance to asses losses of small magnitude.

COLLEGE OF INSURANCE
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D.5 The Motor Assessor

- Are registered to do motor vehicle assessment only as this is their area of competence.
- Insurers normally appoint them to come up with independent reports on extent of losses and the best methods of granting indemnity.
- Some insurers also have internal motor assessors.

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Motor Assessors advise on:

- Extent of loss;
- Best method of providing indemnity;
- Causes of the accident;
- Where to get spare parts;
- Whether the vehicle can be repaired;
- Best repairers/garages.

D.6 The Investigator

- Appointed after a loss has taken place when insurers want to get facts leading to the loss.
- Used mostly in general classes of insurance.
- Useful when foul play is suspected.
- Also be used in life assurance if a claim arouses suspicion

In Kenya currently there are 106 licensed investigators.

COLLEGE OF INSURANCE
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D.7 Claims Settling Agents

- Negotiate and settle insurance claims on behalf of insurance companies.
- They may do this for policies issued by insurers inside or outside the country.

In Kenya currently there are **2** licensed claims settling agents.

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An Actuary

- Is a financial engineer who uses mathematical skills and past experience can predict the likely outcome of future events.
- Calculates the applicable premium for a risk.
- Is also involved in valuing assets and liabilities of life assurance companies after a period specified in the Insurance Act
- in order to determine whether the assets will be sufficient to pay off the liabilities of a company.
- In pension schemes an actuary determines the benefits payable to individual pensioners and the cost of joint pension schemes.

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E. COMPETITION WITHIN THE INSURANCE INDUSTRY

- We shall restrict ourselves to competition among insurers though clearly, there is also competition among the other financial service providers like banks.
- Competition among insurers may take any of the following forms:

Prices

- Insurers compete on the basis of price by offering lower priced products than other companies dealing in the same line of insurance.
- An insurer can reduce premiums by cutting down on the cost of operations. If a company succeeds in reducing the costs that are common to all insurance companies, the price of its insurance will go down.
- The costs include payment of claims, loss adjustment expenses, cost of marketing, administrative expenses, and taxes.

Quality

- Insurance companies compete by offering different forms of policies, or offering policies with additional benefits to the insured.
- One aspect of this competition has been the broadening of coverage under various policies and offering additional services.
- For instance, motor insurance policies now also include vehicle recovery services following carjacking.

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Service

- Insurance is a promise of future performance. A buyer rarely knows if the service purchased will materialise until a loss occurs.
- A major feature that some insurers are good at is the service or the advice their agents give to clients.
- Insurers who give good advice or service will enjoy competitive advantages over those that give none or give inadequate service.

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Gifts

- Insurers may give free gifts in addition to the service they give. Examples of such gifts are umbrellas, T- shirts, pens and caps.

Location and Hours of Business

- Insurers use location and hours of business for competitive purposes. Some insurers
- have established branch offices in different parts of the country thus taking services
- closer to the people. Others open during lunch hours and/or on Saturdays, thereby
- using hours of work as a means of competing with other insurers.

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Commissions

- Commissions may be used for competition. Insurers who give maximum commissions or who treat their intermediaries in a special way have a competitive edge over those who give low commissions or who do not give intermediaries special treatment.
- In Kenya, the maximum commission rates are prescribed under the Insurance Act , and, therefore, this form of competition is seldom used.

CO-OPERATION IN THE INSURANCE INDUSTRY

- Although there is intense competition in the insurance market, there are also many areas in which the players co-operate. In most cases co-operation arises out of economic necessity.
- In other cases it is designed to spread risk among insurers, while at other times co-operation is aimed at improving public relations and insurance education in the country.

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The most important co-operative bodies are;

- The Association of Kenya Insurers ,
- The Association of Kenya Reinsurers ,
- The Association of Insurance Brokers of Kenya,
- The Association of Kenya Independent Insurance Agents , and
- The Insurance Institute of Kenya

1. The Association of Kenya Insurers (AKI)

- The Association of Kenya Insurers is a voluntary, independent and non-profit making body that acts in consultative and advisory capacity for direct insurance companies transacting business in Kenya.

The objectives of this body are to:

– bring together insurers transacting insurance business in Kenya;
– promote the advancement of, and put on a sound basis, the business of insurance in Kenya;
– deal with general matters affecting the insurance industry;
– create a better understanding of insurance among all sections of the community;
– avail opportunities for consultation and co-operation on any matter affecting the common interests of its members;
– provide technical services through its technical committees;

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- act as a medium of consultation and communication with the government, or any party, on matters affecting the insurance industry;
- gather and collate market-wide statistics from its members; and
- administer the provision of motor insurance certificates;

- **All the insurance companies transacting direct insurance business in Kenya are members of AKI .**

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2. The Association of Kenya Reinsurers

- This is an independent non-profit-making body representing the interest of the reinsurance companies transacting business in Kenya.
- The four reinsurance companies currently operating in Kenya are members. Their objectives are similar to those of the Association of Kenya Insurers .

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3. The Association of Insurance Brokers of Kenya (AIBK)

- The Association of Insurance Brokers of Kenya is a lobby group and a voluntary body for insurance brokers who have met the legal requirements of carrying on the business of a broker in Kenya.
- The objectives of the Association are:
  - ensures that its members adopt sound insurance practices;
  - takes action wherever interests of its members are threatened by way of legislation or otherwise;

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- arbitrates or settles disputes between its members and insurers or third parties;
- supports its members legally;
- contributes to worthy causes; and
- co-operates with other bodies having similar objectives;

- Currently all licensed brokers are members of the Association of Insurance Brokers of Kenya.

4. The Insurance Institute of Kenya (IIK)

- The Insurance Institute of Kenya is an organisation for professionals working in the insurance industry.
- The main role of the institute is to:
  - promote insurance education by way of conferences, seminars, meetings, and research;
  - ensure that high standards are maintained in the insurance sector; and
  - collaborate with institutes and bodies having similar objectives.

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5. The Institute of Loss Adjusters and Risk Surveyors (IARS)

- This is an association of loss adjusters and risk surveyors that acts as a lobby group for the interest of its members.
- It acts as a medium of consultation and communication on behalf of the members with the government, the insurance industry and any other party that affects them

6. Motor Assessors Association of Kenya (MAAK)

- This is an association of the motor assessors of Kenya which avails its members opportunities for consultation and cooperation on any matters affecting their common interest.

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7. Association of Kenya Independent Insurance Agents

The Association of Kenya Independent Insurance Agents is a voluntary association of agents transacting insurance business in Kenya. Its objectives are:

- to be a collective bargaining platform;
- to be a self-regulatory body;
- to be an empowerment vehicle through training and education;
- to create unity of purpose;
- to promote economic and social welfare through a co-operative society which will offer savings and loan facilities to members.

8. National Association of Kenya Investigators

- It coordinates the professional conduct of those practitioners engaged in rendering all manner and categories of investigative services.
- The Association aims at promoting professional development, education, ethical guidelines, standards, protection of clients' interests and enforcing professional discipline on its members.
- Another objective of NAKI is to create public awareness of the importance of investigation services by providing professional services.

9. The Insurance Trainin g and Education Trust

- This is a trust charged with the responsibility of providing high standards of insurance education and examinations in Kenya.
- It is run by a board of trustees representing all players in the insurance industry.

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It has two arms to it:

- The College Management Board manages the College of Insurance, which offers insurance training while;
- Kenya National Insurance Examinations Board (Interim) manages insurance examinations.

10. Other Co-operative Bodies

- There are other co-operative bodies, such as, the Aviation Underwriters of Kenya and the Engineering Group, who deal with issues unique to their class

of insurance.

- These co-operative bodies facilitate the meeting of members to exchange views of mutual interest.
- Commitee for Liaison between Underwriters and Brokers
- This acts as a medium of consultation between the Association of Kenya Insurers and the Association of Insurance Brokers of Kenya (AIBK), with the aim of creating better working relations between members of the two bodies.

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Fundamentals of Insurance

- The aim of the CLUB is to bring better understanding between the Underwriters and
- Brokers on matters of common interest, like levels of commission, policy wording,
- scope of cover providers pensions and claims handling etc.

COMPETITION FROM OTHER FINANCIAL SERVICES PROVIDERS

- In the recent past, the Kenyan insurance industry has been affected by the activities of banks and other financial institutions

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1. Banks

- There is a wave of convergence of banking and insurance services known as
- bancassurance . Bancassurance is a French term referring to the distribution and delivery of insurance cover by banks to their clients and account holders.
- The banks act as intermediaries and to some extent offer unfair competition to traditional intermediaries like insurance brokers because they have a wide customer base and branch network which they use to capture a large portion of the insurance customers.

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- Further, they have a client database from which they are able to identify prospects likely to require insurance.
- For example, they offer life policies and personal accident insurance to their clients who maintain a certain level of cash balance in their bank accounts.
- They have an opportunity for cross selling of banking and insurance services.
- In fact, bancassurance is a package of financial services that can fulfill both banking and insurance needs at the same time.

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- In addition, the enactment of the Retirement Benefits Act (1997) has also enabled banks in Kenya to take a more active role in the running of retirement benefit schemes. Insurance companies have traditionally carried out these roles.
- However, bancassurance is also an opportunity for growth of the insurance industry in the country in that banks will facilitate more insurance penetration at the grassroots as they have more branches than any one insurance company or broker.

2. Supermarkets

- Some supermarkets are successfully entering the financial services market by offering insurance products as a marketing strategy to draw customers to shop at their outlets.
- As intermediaries just like banks , they are taking advantages of their brand name to bring together a large number of potential customers for their services.
- Customers tend to trust a popular brand name rather than individual agents and brokers. This might end up taking business away from agents and insurance brokers

3;Micro- Finance Organizations

- Micro- finance organizations are able to attract small irregular savings from the informal sector.
- They offer loans under a system where savers are organized in groups in which members guarantee each other.
- This presents competition to investment products offered by life assurance companies.

4;Saving and Credit Cooperatives

- They are formed by employees , now a main feature in many places of work.
- They offer lower interest rates than commercial banks and pay dividends to their members unlike life assurance offices which only pay bonuses to their with-profit policies.
- Are managed by the employees themselves through their elected representatives and this sense of control plus the fact that they are able to deduct both loan repayment and monthly savings installments at source makes them a strong competitor to long term business.

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5; Shares

- When a person buys shares of a certain company, one becomes one of the many owners of that company and is entitled to the dividends declared.
- Buying of shares is, therefore, a form of investment.

Shares can also be used as a:

- Security for loans;
- A form of saving;
- An easy and quick asset to buy and sell.

Shares, therefore, provide an option which can compete with life assurance.

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6;Unit Trusts

- It is becoming increasingly common for life assurance companies to form trusts purely dedicated to investment.
- These investments yield higher returns than interest rates ordinarily paid by banks on deposits.
- Investors can withdraw their money at any time without any major penalty
- Unit trusts are not a life assurance cover as there is no underwriting required for one to put in their money.
- Investors can, therefore, freely put in their money.
- As such investments have no life cover; some investors may prefer them to life assurance-thus constituting a form of competition to life assurance.

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Bonds

- A bond is a type of loan where the borrower promises to pay the lender some interest quarterly or semi-annually at some date in the future.
- Bonds may be issued by companies and by government.
- The borrower also promises to repay the initial money invested by the lender.
- The profit from a bond is gained in the form of an interest.

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THE END

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CLASSES OF INSURANCE

Unit -5

Categories of Insurances

There are two main categories of insurance namely

1. Life Assurance/Long Term business
2. General Insurances/ Short term Insurance Business

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LONG TERM BUSINESS

INTRODUCTION

- Life policies are generally based **on the life** of a particular person called the **life assured** and becomes payable on **maturity** of the policy or prior the **death of that person**.

- At the commencement of negotiations, the **person on whose life a policy** is to be based must be named and the risk of death during the term of the policy assessed.
- **The assured** is the name given to the person who effects a life policy and is **the original owner** of the policy.
- The assured is therefore **the owner of the policy**.

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CATEGORIES OF LIFE POLICIES

1. **Own Life Policy**

- This is a life policy effected by individuals on their own lives.
- The assured and the life assured are the same.

2. **Life of Another Policy**

- This is a policy taken out on the life of another named person.
- The person effecting the policy must have insurable interest on the life assured.
- For example a dependant may take out a policy on the life of the person upon whom they are financially dependent.

3. Joint Life Policy

- This is a policy effected jointly by two persons e.g. husband and wife on their joint lives.

There are two basic types of joint life policy:

i. first death policy;

ii. second death policy.

- **The first death** policy will pay out the sum assured on death of the first life while the second death policy will pay the sum assured on the death of the second life assured.
- **Joint life**, second death policies are sometimes called *joint **last survivor policy***.

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- Joint first death policies are often used to provide protection for dependants where there is a joint mortgage so that the survivor is not burdened with unserviceable debt.
- A joint life first death policy is more expensive than a joint life second death policy because the claim is usually payable at an earlier date.

LIFE ASSURANCE PRODUCTS

Life policies fall broadly into three basic types:

- Ordinary Life assurance
- Industrial life assurance
- Group life and retirement Schemes(Supper-annuation)

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1. Ordinary life assurance Products

I. Term assurance;
II. Whole life assurance;
III. Endowment assurance;

I. TERM ASSURANCE

- Oldest form of life assurance practice.
- Payment of sum assured is only made if the life assured dies within the time specified in the policy.
- If death does not occur during that period:

i. no payment is made

ii. the assured does not usually receive a return of premiums.

- Premiums are kept at modest level since they are paid solely to provide the life cover.
- Do not contain any investment element.

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Types of Term Assurance

- Level term assurance
- Renewable term assurance
- Convertible term assurance
- Decreasing term assurance
- Increasing term assurance
- Family income policy.

1.Level Term Assurance

- Simplest form of term assurance.
- The sum assured is chosen at the outset and the amount remains constant throughout the term of the policy.
- Once it has expired, it has no further value
- It only pays if the life assured dies during the term of the policy

2. Renewable Term Assurance

- On the expiry date, the assured has an option to take out a further term assurance:

✓at ordinary rates,

✓without further evidence of health,

✓as long as the expiry date is not beyond a certain age.

- Each subsequent policy will have an option of renewing.
- At renewal, the premium will increase based on the current age of the life assured.
- Premiums are slightly higher than for similar level term assurance.

3. Convertible Term Assurance

- Has an option that enables the assured to convert it at any time during its existence to a whole life policy or endowment policy.
- The premium for the new policy will be that applicable to whole life or endowment policies for a person of the life assured's age at the time of conversion.
- Premiums are slightly higher than for similar level term assurance.

4 .Decreasing Term Assurance

- The sum assured reduces steadily throughout the term.
- Used to cover decreasing debt e.g. outstanding loan on a house purchase mortgage.
- Another example - credit life policies.
- The premium remains constant through out the period.
- Premiums are sometime paid for a shorter period than the policy term mainly to avoid the temptation of the assured to lapse the policy in the final policy years.
- Premiums are slightly cheaper than for level term assurance or the same but payable for a shorter period.

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5.Increasing Term Assurance

- Allows for the sum assured to be increased by the policyholder without any medical evidence.
- Limit of increase may be up to 50% of the original sum assured.
- Designed to counter the effects of inflation as it reduces the real value of the cover.

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- Initial premiums will be relatively high.
- Subsequent premiums are increased in line with:

i. the sum assured

ii. the age of the life assured.

6.The Family Income Policy

- A type of a term assurance plan.
- Pays out an income rather than a lump sum on the death of the life assured.
- Its main intention is to replace the income, which the life assured, would produce for their family if they were still alive.

II. WHOLE LIFE ASSURANCE

- A whole assurance is a permanent policy.
- It lasts for the whole of the life assureds' lifespan.
- Pays out the sum assured whenever the life assured dies.

- Pays out a lump sum rather than income on death.
- Premiums can be paid throughout life or cease on attainment of a certain age, usually 65 years, although the contract continues until death.

TYPES OF WHOLE LIFE ASSURANCE POLICIES

- Traditional Whole Life Policies
- Unit Linked Whole Life

1 .Traditional Whole Life Policies

1. ***Fixed Death Benefit***
- Pay the same fixed sum whenever death occurs.
- Called a non-profit or non-participating policy.

2. ***Increasable Death Benefit***
- Pay the sum assured plus profits realized and allocated at the discretion of the life office up to the time of death.
- Called with- profit or participating policy.

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Unit-linked Whole Life Assurance

- The death benefit payable is equal to the rate of return realized on premium invested in an authorized unit trust investment fund.
- Death benefit is guaranteed and cannot fall below a stated minimum.

- Where the investment returns exceed the minimum life cover, the larger amount will be paid on death.
- The amount to be paid is, therefore, either: -
  - The guaranteed sum assured or
  - The value of the investments: - whichever is larger.

III.ENDOWMENT POLICIES

- A life cover for a fixed period and the sum assured is payable on death within the period or, if no death occurs, the sum assured is paid at the end of the policy duration, that is, maturity.
- A savings type of cover under which the sum assured is payable at maturity – after a certain number of fixed years.

- **Main purpose**:

to provide financial benefit for the policyholder after an agreed period has elapsed.

- **Secondary purpose:**

to provide a financial protection if the policyholder dies while the policy is still in force.

- May be cancelled by the policyholder who may receive cash or surrender value from the life office.
- Possible because there is an investment element in the premium.
- As an alternative to cancelling or surrendering the policy, an endowment may be made “paid-up”.

TYPES OF ENDOWMENT ASSURANCE

1. Non-profit Endowment

- Most basic form of endowment
- Level premiums
- Payout of only a fixed guaranteed sum assured on maturity, or earlier death.

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2. With-Profits Endowment

Most common features

- Amount payable on maturity or earlier death will be the guaranteed sum assured, plus any accrued annual bonuses.
- If the policy continues to maturity or death, these bonuses will be increased by payment of a one-off terminal bonus.
- Eventual amount payable cannot be guaranteed because bonuses declared vary from year to year.
- However, they have a guaranteed minimum payout upon death.

3.Flexidowment

- Overcomes the drawbacks of fixed maturity date and low surrender value of the traditional endowment.
- May be cashed in without the normal surrender penalty at any time after ten years.
- The surrender value is usually guaranteed, or part guaranteed, rather like an early maturity value.

4.Unit-linked Endowment

- Premiums are invested in the internal fund of a life office (run on the lines of a unit trust) buying units on a regular basis.
- The value of the policy goes up and down with the value of the units.
- There is always a minimum value of life cover.

5.Pure Endowment

- Not truly a life policy since it provides no life cover.
- A simple contract that pays out the maturity value at the date specified if the life assured is alive.
- If the life assured dies before the maturity date, there is no pay out, although some offices will return the premium if this occurs.

CHILDREN ASSURANCE POLICIES

1. Child's advanced policy

-It is effected on the life of the parent with an option date coinciding with a child's 18^{th} 0r 21 birthday

- At that age the child takes over the policy without any requirement of evidence of good health
- The child can continue policy as a whole life or endowment policy or can opt to surrender it or convert it to a paid up policy

2.School fees policies

- The parent effects an endowment policy on his life
- The sum assured is payable in installments spread over the period of the child's college years.
- Or a term assurance policy is effected on the life of the parent.
- The sum assured payable on premature death of the parent is utilized to pay the chids school fees.

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- **If parent dies before the option date**

- premium payment will cease but policy will continue to be enforce until the option date

- **If the child dies**

- arrangements can be made for a return of premium or transferring the policy to another child

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ANNUITIES

- Not a life assurance contract.
- A contract to pay periodical income to the annuitant(the person on whose life the contact depends).
- The income is usually payable for life or a guaranteed period.
- The income is bought by an individual with a single premium or a series of premiums.

- **Single premium annuity**, the annuity can be immediate, starting straight away after the payment.
- **Series of premium annuity**, the annuity is deferred, starting after a certain period has elapsed.
- Can be arranged on a **joint basis** for a couple. In this case, income continues for the rest of both lives.
- Annuities are the basis of pension schemes.

Immediate Annuity

- Simplest form of contract.
- The annuitant pays a single premium in return for periodical payments for the rest of the annuitant's life.
- Mainly purchased by retired people who want an income that is guaranteed to last for the rest of their lives, no matter how long that may be.

Deferred Annuity

- Provides for payment of periodical and regular income, commencing at a future date.
- **Deferred Period** -The duration between the date of the contract and the date on which the annuity is payable.
- Often, regular premiums are payable throughout the deferred period.
- If the annuitant dies during the deferred period, the life office will usually return the premiums paid.

The main types of annuities

- Temporary annuity
- Annuity certain
- Guaranteed annuity
- Joint life and last survivor annuity

Temporary Annuity

- Pays a periodical income for a fixed period of time or until the death of the annuitant, whichever is earlier.
- Has a fixed date at which time the annuity payments will cease unless death has already occurred.

Annuity Certain

- A contract to pay an annuity for a specified period regardless of whether the annuitant survives.
- Does not depend on the age or life of the annuitant as payment is guaranteed.

- If the annuitant dies during the period of payment, the installments would continue to be paid to the deceased’s estate or named beneficiary until the end of the term.

Guaranteed Annuity

- An immediate annuity.
- Guaranteed for a minimum period regardless of when the annuitant dies. For example, an annuity guaranteed for 15 years will be paid for 15 years or for life whichever is the longer.

- If the annuitant dies during the guaranteed period the balance of the guaranteed installments will be payable to their estate, although a commuted cash sum may be available instead.

Joint Life and Last Survivor Annuity

- Have been developed to ensure that the annuity payments continue to the surviving partner after the death of their spouse.
- Pay an annuity for the joint lifetimes of the two annuitants.

- Payments usually continue in full after the first death but sometimes may be reduced.
- Can be in advance or arrears, with or without proportion and with or without guarantee, as for single life annuities.

INVESTMENT POLICIES

With-profit Policies

- Life offices carry out annual valuations of assets and liabilities of their life funds.
- This normally reveals a surplus, which is usually apportioned between:
- shareholders
- policyholders of with-profit policies.

This addition is known as *bonus* or *profit.*

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Types of Bonus

There are two types of bonus:

- Reversionary
- Terminal

1.Reversionary Bonus

- A reversionary bonus is declared annually and increases the value of the policy year by year.
- Its usually expressed as a percentage of the sum assured,
- the higher the sum assured the greater the bonus.

The bonus can be either *simple* or *compound.*

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- **simple bonus** is based purely on the original sum assured
- **compound bonus** is based on the sum assured plus previous bonuses.
- Once allocated, a reversionary bonus cannot be removed.
- Its only payable at the same time as the sum assured, i.e. on death or maturity.

2.Terminal Bonuses

- only added when a policy becomes a claim
- not payable on surrender.
- It is expressed as a percentage of the total bonuses earned.
- Under a with-profit policy, the policyholder benefits in some measures from investment performance of life fund
- but the link is not direct and depends on
- the annual valuation of the fund's assets and liabilities and
- the decision of the directors as to how to allocate any surplus.

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UNIT TRUSTS

- A trust is a legal entity that provides for ownership of property by one person for the benefit of another.
- It is an equitable arrangement involving three parties i.e.

I. The founder who decides to set up the trust
II. The trustee/s appointed to manage the trust and its property
III. The beneficiaries for whose benefits the trust is set up

-

- A unit trust is a pooled investment vehicle for small private investors to obtain professional management and a wide spread investment portfolio.
- The investor buys a certain number of units in the trust, which is managed by the unit trust manager in order to achieve (hopefully) a high income or capital growth.

Examples of Unit Trusts

1. Money Market Fund

- The portfolio objective is to outperform the income yield available on money market call account by investing in interest bearing securities and other short-term money market instruments with a maturity of less than 12 months,
- such as bank deposits and
- treasury bills.

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2. Income Fund

- This is a low risk fund that aims to achieve a reasonable level of current income and maximum stability for the capital invested.
- It is recommended for short to medium investment period i.e. two to three years.

3.Balanced Fund

- This is a medium risk fund that aims at achieving a reasonable level of current income and offer an investor a long-term capital growth.
- achieved by investing in **a diversified spread** of equities and fixed income securities.
- **A balanced portfolio** can help lessen the volatility of each investment category as prices of equities and fixed income investment often move in opposite direction.
- investment term is over two years.
-

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- The fund may from time to time be invested in money market instruments:
- money market
- cash funds
- cash deposits,
- Depending on the opinion of the fund manager,
- the prevailing market and
- economic conditions

UNIT PRICING STRUCTURE

- The units have two prices, **selling (offer price) and buying back (Bid price).**

- The offer price_is the price which the life office uses to allocate units to a policy when premiums are paid, for example, if the offer price is KShs. 100 and a premium amount of KShs. 1,000 is applied to buy units, it will buy 10 units.

- The bid price_is the price, which the life office will give for the units if the policyholder wishes to claim under the policy.
- If the bid price, for example, is KShs. 95, the units can be cashed in for Kshs. 950.

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- The units are priced periodically and the purchase and sale of the unit is always done on the price of the next valuation following the receipt of premium or request for encashment.

- Insurance companies doing unit-linking business usually send to their clients statements of unit holdings and current values of the units held to show them how their investment is performing.

UNIT-LINKED POLICIES

- A unit-linked policy is one in which a specific proportion of the premium is used to purchase life cover while the balance i.e. the larger proportion is invested in units in a special unitized fund set up by the life office or alternatively in an authorized unit trust.

- Some companies offer policyholders a choice of funds to invest the premium in.
- This type of policy is an alternative to a conventional with-profit policy.
- A minimum guaranteed life cover is normally maintained throughout the policy's life
- the value of the investment is mirrored in the price of the units
- Thus the policy's value moves up or down reflecting changes in the performance of the chosen fund.
- At maturity the policyholder receives the net value of all the units purchased with his premium or the units themselves.

MEDICAL INSURANCE

- Are contracts of indemnity
- they enable the insured to claim not more than the cost of treatment.

Expenses covered:

- Private medical treatment
- Hospitalization
- Nursing services
- Theatre services

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- Drugs and dressing
- Doctors and consultant’s services
- Diagnostic services such as x-ray and laboratory

Riders- Extensions

benefit such as:

- Rescue and evacuation costs
- Funeral and body repatriation costs
- Maternity and child birth charges
- Ante natal care
- Dental charges
- Optical costs, etc.

Exclusions are:

- Cosmetic treatment
- Convalescence
- Childbirth and pregnancy
- Hazardous sports or pastimes
- War, invasion or rebellion
- Pre-existing defection of infirmity
- Being under the influence of drugs, alcohol or insanity
- Nature treatment
- Intentional self-inflicted injury or attempted suicide

COLLEGE OF INSURANCE
Driven by distinction

PERMANENT HEALTH

- This policy may also be known as income protection insurance policy.
- It pays out the sum insured if the insured is not able to work due to illness or injury.
- It provides a regular income to replace the income that the insured may no longer be able to earn. It insures one's health rather than one's life.

- The policyholder decides what level of cover the family will require to continue living at the same standard.
- This is determined by benefits paid by an employer or under a pension scheme taking into account other benefits, which would provide an acceptable level of income to the family.
- It is a long-term contract since as long as the insured pays premiums and complies with policy conditions, the insurer cannot terminate the policy or increase the premium no matter how many claims are made

1.Disability

- Under the policy, benefits will only be paid if the insured is disabled as defined in the policy.

Typical Definition of Disability

The insured is totally unable by reason of sickness or accident, to follow the occupation stated in the policy and is not following any other occupation.

Deferred Period

- This is the waiting period or the first number of days in which no benefit will be payable under the policy.
- The benefit will only be paid if the insured has been disabled for a specific period.
- The length of deferred period will depend on the insured's circumstances and is chosen by the insured.
- The longer the period, the cheaper the premiums as the duration and frequency of claims are reduced

To encourage claimants to resume work, cover is provided stating that

- having been disabled from previous occupation, the insured who
- engages in another occupation, benefits will continue proportionate to the reduction in earnings.
- Similar provisions may exist when part- time work is undertaken.
- This to ensure that an insured will not be better off financially by claiming,
- most insurers put a limit on the benefits that are payable

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- The most common deferred periods are 4, 13, 26 or 52 weeks
- In the event that the insured becomes disabled again from the same cause, most insurers will not reapply the deferred period thus allowing benefits to recommence immediately
- Benefits cease once the insured recovers and resumes work

COLLEGE OF INSURANCE
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Exclusions

- The most common exclusions under the policy are:
- War, invasion, act of foreign enemy, riot, military or usurped power
- Intentional, self-inflicted injury or attempted suicide
- Taking alcohol or drugs unless under the direction of a registered medical practitioner
- Participation in any criminal act

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- Pregnancy, childbirth or any complication arising there from
- Aviation other than as a fare-paying passenger in a normal scheduled flight
- HIV/AIDS
- Failure to follow medical advice
- Pre-existing defect or infirmity

RIDERS

- These are supplementary covers, which are usually added to standard life assurance policies.

The common riders are:

Accidental Deaths or Double Accident Benefit

- This provides for double payment of the ordinary sum assured in the event of the accidental death of the life assured as defined in the policy.

Disability Benefit

- The sum assured is payable on permanent disability as well as on death.
- The payment depends on proof that the assured is permanently unable to follow normal occupation due to illness or injury

COLLEGE OF INSURANCE
Driven by distinction

3 Premium Waiver Benefit

- This benefit provides that if the assured is suffering from disability and is unable to follow normal occupation due to illness or injury, all future premium payments will be waived.
- The policy will remain in force as the life office bears the premiums on behalf of the policyholder

Increasing Cover Option

- This form of rider enables the policyholder to increase the cover by certain amounts at certain times.
- increase every three or five years by a total amount not greater than the original sum assured.
- medical evidence is not required on increase but the premium will be increased according to the office's ordinary rates at the time of exercise of the option.
-

COLLEGE OF INSURANCE
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- the option provides for the increase in cover to be through a new policy rather than an increase to the existing policy.
- Some options are triggered by events such as marriage, birth of a child or receiving an inheritance and the like.

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CRITICAL ILLNESSES OR DREAD DISEASE COVER.

- sold as a rider to whole life, endowment or term assurance.
- can be sold on a "stand alone' basis.
- The purpose of critical illness cover is to pay a lump sum benefit on the diagnosis of any of the illnesses or diseases specified in the policy.

List of common of illnesses:

- Cancer
- Stroke
- Coronary artery disease
- Heart attack
- Major organ transplant
- Paralysis
- Multiple sclerosis and blindness
- Major burns and
- Loss of limbs

HIV/AIDS is excluded unless contracted through blood transfusion or/accident.

PERSONAL ACCIDENT POLICIES

- It pays a sum of money in the event of the insured's disablement or death **by accident**.
- Given as a rider or on a 'stand- alone' basis.

N.1 The Insured Event

- Cover is provided against bodily injury caused by violent, accidental, external and visible means, which shall be solely, and independently of any other cause result in death or disablement.

- The policy may be extended to cover death or disablement by certain specified diseases. Such a policy is usually known as accident and sickness policy.

- Where there is no visible injury, the physician’s or medical practitioner's report or death certificate will be required to show the cause of injury or death.

-

2.Benefits under the Policy

1.Death

- capital sum is payable,

-the death must occur within a stated period (normally one year) from the date of accident

2.Permanent Total Disability

-This is absolute disablement from engaging in or giving attention to the insured's profession or occupation.

- an appropriate percentage of selected sum specified in the policy schedule.
- Some insurers would pay the total capital sum insured and no further payment in the subsequent death.

3. Temporary Total Disability

- This is absolute disablement from engaging in or giving attention to the insured person's ordinary profession or occupation for a period of time normally two years (104 weeks).
- benefits are given in the form of weekly payments that do not exceed the actual weekly earnings of the insured.
- paid for a maximum of 104 weeks in respect of any one accident to the insured.
-

4.Medical Expenses

- The amount paid is the actual cost of treatment of the insured approved by the doctor but not exceeding the medical limit covered.
- Its is subject to the principle of indemnity.

Exclusions

- War, invasion, acts of foreign enemy, hostility, civil war, rebellion, revolution, insurrection etc
- riot or strike
- Suicide or attempted suicide
- Big game hunting, mountaineering, winter sports and racing (other than on foot)
- Pregnancy, childbirth or any complication arising there from

- aviation except as a fare paying passenger on a recognized airline operating on regular scheduled route or established charter service
- Willful exposure to needless peril, except for the purposes of saving human life
- Indulgence in alcohol, narcotics or drugs not prescribed by a qualified medical practitioner
-

Funeral Benefit Cover

- also know as the last expense benefit
- extension to an individual life policy,

\- medical policy, or a group life cover.

\- on a stand-alone basis.

- paid out as soon as the life assured dies or when proof of death is produced.
- to meet the cost of funeral expenses.
- On the life assured only or may include spouse, children, parents or even members of the extended family.

COLLEGE OF INSURANCE
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Capital Disability Benefit

- If the life assured is totally and permanently disabled the life cover to which this benefit is linked pays as if the life assured has died. The benefit can be linked to the total sum assured or to only a part of it.

Inflation Provision

The benefit goes under different names;

- escalator,
- update,
- inflation cap
- Automatic inflation manager etc

-no premium charged

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- To counter the effects of inflation, most life offices allow the proposer to choose the rate at which his/her premiums should increase every year.
- The rates vary from 5 to 20% with some offices giving a chance to vary the rate upwards or downwards every year.

SUPERANNUATION

- Group Schemes- Group Term Assurance
- Retirement Benefit Schemes

Examples of Group Term Assurance

- Group life assurance
- Group personal accident
- Group credit assurance
- Group mortgage protection

GROUP LIFE SCHEMES

- Group life policy refer to group term assurance policy taken by employer on lives of employees for the purpose of securing lump sum death benefits upon death of an employee.
- This amount is paid to the family or dependents of a deceased employee.
- The policy may be arranged in two ways;
  - as part of benefits in a retirement scheme or
  - as a policy which is not part of a retirement scheme.
- An employer has an insurable interest in the life of an employee limited to the value of salary for the period of employment, for this reason employers arrange these policies.

Other reasons why an employer starts a group life policy

1. To attract, retain and motivate the employees, this enables the organization to attract competent staff;
2. Create good image of employer;
3. Social responsibility;
4. For their own peace of mind;
5. To create good relations with employees;
6. As a benefit for employees as part of their remuneration package.

1 Features of Group life policy

- Master Policy
- Fixed Scale of benefits
- Exclusions
- Free cover limit
- Underwriting as a group
- Individual underwriting
- Premium payment
- Provision for individual cover on withdrawal
- Renewal

Master Policy

- Master Policy is issued to the insured who is the employer. Master policy is the policy documents with all policy sections.

2.Application of Individual Underwriting

- Individual underwriting applies only to lives whose benefits exceed non-medical limits or the Free Cover Limit.
- Sub-standard lives may be underwritten individually depending on the terms of cover.
- However, cover is usually provided to the members of the group on the basis of application forms or information supplied by the group sponsor, that is, the employer.

COLLEGE OF INSURANCE
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3. Contribution

- Members of group schemes are not always required to contribute towards the premium payment. In most cases, premiums are paid by the employer.
- Where the scheme is non-contributory, a policy could well provide a very useful fringe benefit for employees.

4. Requirement for Continued Individual Cover

- Cover for individual members are dependent upon their remaining in the group or employment and normally ceases on their departure from the group or employment.

5. Provision for Individual Cover on Withdrawal

- A provision is often made for an individual withdrawing from the group to arrange a continuation of assurance on one's own life.
- If the withdrawing member exercises this option, they will be expected to pay the appropriate premiums commensurate with the cover based on individual rates, not group rates.

COLLEGE OF INSURANCE
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6. Fixed Scale

- Group benefit is normally written on a fixed scale, i.e., a specified amount per member.
- This may be arranged on a flat amount per member or as a multiple of individual salary, say five years salary.

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7. Exclusions

- Although most group schemes do not have as much exclusions as in individual policies, there are some hazards for which it would be unwise to provide cover, however, for example, HIV/AIDS.

8. The Free Cover Limit

- The free cover limit is a common feature of group life schemes.
- This refers to the level of sum assured which a life office can accept on the basis of a proposal form only i.e., without medical examination.
- It is also known as non-medical limit and depends on the number of members involved and the average benefit provided.

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9. Renewal

- Group life policies are normally annual renewable contracts.
- Some policies have an extra benefit of guaranteed renewal for three to five years.

BENEFITS

Under group life policies, the benefits payable are

- Main benefit is death benefit
- Policy may be extended to offer a disability benefit.

Retirement Benefit Schemes

- Not an insurance contract.
- Long term business.
- Insurance companies play the roles of administrators, fund managers.

AIM

To help individuals save for retirement.

Types of Retirement Benefit Schemes

Provident Fund	Pension Scheme
• Pays lump sum on retirement	• Pays income on retirement

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May be:

Defined Benefit Scheme

Benefit payable defined in Trust Deed and Rules.

Defined Contribution Scheme

Contributions payable stated in policy. Benefit not known until retirement and will be based on the total value of contributions plus interest.

THANK YOU

- END OF PART - ONE
- QUESTIONS?

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Unit – 5-2

General Insurance

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NATURE OF EACH CLASS OF INSURANCE

1: SHORT TERM/GENERAL INSURANCES

CATEGORIES OF GENERAL CLASSES OF INSURANCE

1. Property insurances
2. Liability insurances
3. Transport insurances
4. Pecuniary Insurances
5. Guarantee insurances
6. Accident insurances
7. Health insurances
8. Agriculture insurances

1.PROPERTY INSURANCES

- Fire and perils
- Engineering and construction
- Domestic package
- “All risk “insurance
- Industrial all risk insurance
- Theft/Burglary insurance
- Goods in transit
- Glass insurance

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1:FIRE INSURANCE

Introduction

- Characterized by low frequency and huge loss – severe consequences
- There are direct and indirect losses arising from fire occurrence.

1. Indirect losses
   - ✓ Lost employment
   - ✓ Loss of production – Business interruption
   - ✓ Medical costs
   - ✓ Demolition
   - ✓ Legal fees
   - ✓ Aesthetic/ Sentimental value
2. Direct costs
   - ✓ Property damage
   - ✓ Deaths and injuries

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1.1;The Standard Fire Policy

Covers 3 perils:-

a) Fire
b) Lightning
c) Limited Explosion

a. Fire Peril

- Conditions
  - Actual ignition (Combination of heat, light, flames and smoke)
  - There must be something on fire that ought not to be on fire
  - The fire must be accidental or fortuitous in origin in as far as the insured is concerned

b.Lightning

- Damage caused by lightning is covered whether fire occurs or not.

;Limited Explosion

- Explosion of appliances used for domestic purposes is covered.

Extended Fire Perils

- Classified as social, chemical, natural and miscellaneous perils

1. Social perils – caused by human activity
   - Riot and strike excluding war like activities
   - Malicious damage
2. Chemical perils
   - Explosion
   - Spontaneous fermentation or heating e.g. coal.

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3.Natural perils

- These are perils originating from nature and beyond human control
    - Storm and flood
    - Earthquake – fire, shock or full earthquake
    - Subterranean fire
    - Subsidence

4.Miscellaneous Perils

- Escape of water
- Aircraft
- Impact damage

Exclusions

- Theft during or after occurrence of fire
- Own fermentation, natural heating or spontaneous combustion
- Fire caused by its undergoing any heating or drying process
- Earthquakes, volcanic eruptions or convulsions of nature
- Subterranean fire
- Explosions of boilers or gases used for trading purposes

1.2 BUSINESS INTERRUPTION INSURANCE

Also referred to as:-

- Consequential loss
- Loss of profits
- Gross profit insurance
- Gross revenue insurance
- Gross earnings insurance

BI; ctd

Business interruption insurance covers:-

- Loss of income or earning power of an enterprise following a fire loss.
- Standing charges/ fixed costs that must be incurred before restoration
- Additional costs of operation

- Material damage warranty

1.3;DOMESTIC PACKAGE INSURANCE

Introduction

- Comprehensive insurances
- They represent a widening of the scope of cover

A domestic liability policy is issued to cover a private dwelling house and its contents, owners and tenant's liability and domestic servants.

The policy has six sections, namely:-

1. Buildings
2. Contents
3. "All Risks"
4. Workmen's compensation
5. Owner's liability
6. Occupier's liability

COLLEGE OF INSURANCE
Driven by distinction

A; BUILDINGS

This section covers loss, damage or destruction to a private dwelling house or a private flat including domestic outbuildings, fixtures, walls, gates and fences on the same premises caused by:-

- ✓ Natural causes – earthquakes, storms and tempests, lightning and floods;
- ✓ Human causes – riots & strikes, malicious damage and theft;
- ✓ Chemical related causes – explosion of domestic gas cylinders
- ✓ Miscellaneous causes – bursting and overflowing of water tanks, apparatus, pipes, impact by road vehicles and animals not belonging to or under the control of the insured or their agents.

- In addition , where applicable, the policy also covers loss of rent or alternative accommodation as a result of the perils.

COLLEGE OF INSURANCE
Driven by distinction

B;CONTENTS

- Covers loss , damage or destruction to:-
  - Furniture
  - Household goods
  - Personal effects

  Belonging to the insured or any member of the family normally residing with the family.
  - Fixtures and fittings owned by the insured or which he is legally responsible
- Theft of insured's contents – forcible and violent entry or exit
- Extends to cover contents when they are temporarily removed and when in other buildings
- Additional expenses of alternative accommodation and loss of rent.

C;"ALL RISKS"

- Covers loss or damage of specified portable items such as:-
  - Cameras
  - Radios
  - Jewellary
  - Sports kits etc
- Covers all perils not specifically excluded.
- The items are covered when carried by the insured anywhere in the world.

COLLEGE OF INSURANCE
Driven by distinction

D;WORKMEN'S COMPENSATION

- Covers domestic servants like house help, watchmen, grounds men, gardeners and drivers.
- Cover provided is in respect of injury, death or disease arising out of and in the course of their employment.
- Provided for under the Workmen's Compensation Act that requires that all employers should compensate employees for injuries, death or diseases arising out of and in the course of employment.
- The Work Injury Benefits Act , 2007 came in to effect in January, 2008 and repealed the Workmen's Compensation Act .

E; OWNER'S LIABILITY

- Covers legal liability of the insured towards third parties arising out of ownership of the building causing bodily injuries or death and damage to property.
- E.g. stone falling from a building injuring a passer by.

F; OCCUPIER'S LIABILITY

- Covers legal liability of the insured towards third parties arising out of their occupation causing bodily injuries or death and property damage.
- Example of third parties – meter readers, visitors and service providers.
- The occupier must be legally liable to compensate them.

1.4 "ALL RISKS" INSURANCE

- Widest cover available for property
- The "All Risks" insurance covers accidental loss, damage or destruction of property from any cause not specifically excluded.
- Some of the exclusions under the "All Risks" policy are:-
    - Wear, rear, gradual deterioration, atmospheric conditions, moth, vermin or insects
    - Mechanical or electrical breakdown or derangement unless caused by accidental external means
    - Money and related items
    - Theft from a motor vehicle unless the items were contained in a locked boot or locked locker forming an integral part of the motor vehicle
    - Loss or damage due to or arising from delay, confiscation or detention by customs official or other authorities
    - Any property undergoing process of repair, renovation or restoration.
  - Each item is identified with sum insured
  - Agreed values for items such as jewelry
  - Some items based on valuations
  - "pair or set" clause – limits insurers' liability to any article forming part of a pair or set to the value of the part(s) lost or damaged.

1.4;THEFT INSURANCE

- What is covered:-
  - Loss or damage to insured property arising from forceful entry or exit from premises. Evidence of force at point of entry or exit required.
  - Damage to premises, if insured is responsible for repairs – doors, windows, roof etc.
  - Hold up extension – theft accompanied by threat of assault or violence to insured/ employees without forcible entry/exit.
- Some insurers offer limited cover such as " theft following forcible and violent entry" – can be due to bad claims experience or nature of property.
- **Forms of theft policies**

1. Full value theft policies
   - Sum insured based on full value e.g. Kshs. 10m.
2. First loss policies
   - Issued when only a part of the property can be stolen.
   - First loss sum insured = max amount that can be stolen at any one time.
   - Full value at risk must be declared.

Exclusions

- **Lo**ss or damage by fire, however caused
- Damage to plate glass
- Money and other securities
- Collusion with insiders, employees or members of insured's household.
- Loss unless alarms or protective devices are present
- Consequential loss

1.5;GOODS-IN-TRANSIT INSURANCE

- Covers the insured against loss, destruction, or damage to property insured while in transit arising from fire, theft and accidental means.
- Cover is on goods during loading or unloading from any motor vehicle or train or while the conveyance temporarily stops in the ordinary course of transit.
- May be restricted to road risks – loss, destruction or damage by fire due to collision, overturning of the vehicle including loading and unloading.
- Three types:-

1. **Single transit policy**
   - One-off cover – for specific conveyance per trip.
2. **Individual vehicle policy**
   - Covers own vehicles which are specified
   - Sum insured per motor vehicle
3. **Declaration policy**
   - Issued under situations where the value of goods transported fluctuate during the period.
   - Estimated annual carry – given by insured and used for premium computation.
   - Actual carry declared at end of period and premium adjusted accordingly.

- **Exclusions**
- Delay, loss of market, or any consequential loss
- Money and related items
- Wear and tear, depreciation, gradual deterioration, moths, insects, vermin, mildew, rust, or any defect of the insured goods
- Theft or pilferage by insured employees
- Confiscation by government or any lawful authority

1.7;GLASS INSURANCE

- “All Risks” cover against accidental breakage of fixed glass, windows, and doors from any cause not specifically excluded.
- Cover is on all kinds of fixed glasses e.g. sheets, silvered, wired, ornamental and lettered glass. Can be in form of:-
  - External glass
  - Internal glass
  - Sanitary fixture and fittings
  - Other special glass

GLASS INSURANCE...Cont.

Exclusions

- Damage to window frames or other fittings
- Cost of removal or replacement of any fitting, fixture, frame or framework
- Fire / explosive damage or any loss that could be covered under fire
- Cracked or imperfect glass or scratches on any plate
- Embossed, silvered, lettered or any glass other than plain glass
- War and related perils
- Business interruption

1.8;ENGINEERING AND CONSTRUCTION INSURANCE

1. Boiler Explosion cover
2. Machinery Breakdown
3 .Machinery Business Interruption
4. Electronic Equipment
5. Erection “All Risks”
6. Contractors “All Risks”

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Driven by distinction

1. BOILER EXPLOSION COVER

- Boiler plant includes all equipment that can explode e.g.:-
  - Steam boiler
  - Economizers
  - Steam boilers
  - Bakers' ovens
  - Ironing machines
  - Pressure plants etc.
- **Insured peril – scope of cover**
- The insurer pays for damage caused to the machine and other properties belonging to the insured due to explosion or collapse of the insured machine.
- Cover includes periodic inspection service by the insurer.
- Insurer meets cost of boiler installation.
- Extensions under the standard cover:-
  - Flue gas explosion
  - Cracking or weld failure
  - Overheating of boilers and tubes
- Cover may be extended to include third party liabilities.

2. MACHINERY BREAKDOWN

- This is an "All Risks" policy which provides cover against unforeseen and sudden physical damage by any extraneous cause to the insured property except what is specifically excluded.
- Operative while the machine is at work or at rest.
- Covers loss or damage due to:-
  - Faulty design
  - Electrical short circuit
  - Faulty operation
  - Destruction due to centrifugal force – i.e. force that causes an object to fly away from its anchor.
- Cover excludes fire and theft losses.

3. MACHINERY BUSINESS INTERRUPTION

- The policy covers the insured against loss of profit, standing charges and increased costs of working during the period of interruption following a machinery breakdown covered under the material damage policy (machinery breakdown).
- The insurer undertakes to indemnify the insured against the following losses:-
  - Loss of profits
  - Increased cost of operations due to breakdown
  - Business expenses or standing charges.
- A time excess is usually included to avoid short period breakdowns which may be frequent.
- Can be issued as an extension of the machinery breakdown policy or a separate policy.

4. ELECTRONIC EQUIPMENT

- "All Risks" policy issued to cover sudden and unforeseen losses physically affecting the electronic equipments insured caused by whatever peril not specifically excluded.
- Examples:-
  - Computers
  - Printers
  - Laptops etc.

5. ERECTION "ALL RISKS"

- Covers plant and machinery erection from start to completion including the period of testing.
- Can be extended to cover machinery during selected maintenance period.
- Includes insured's legal liabilities to third parties who may be injured or whose property may be damaged.

6. CONTRACTORS "ALL RISKS"

- Covers:-
  - Unfixed materials on site
  - Construction machines, equipment and tools
  - Temporary works e.g. site construction, mess accommodation, workers' camp workshops and their contents
  - Permanent works
  - Employees personal effects
  - Third party bodily injury and property damage from any peril not specifically excluded.
- Cover operates during the period of construction and until work is handed over by the contractor to the principal and may extend to subsequent maintenance period.

2:PECUNARY INSURANCES;
2;1MONEY INSURANCE

- All risks policy against loss of money from any cause not specifically excluded.
- Money – refers to cash, bank and currency notes, cheques, postal orders, money orders, telephone cards, current postage and revenue stamps.
- Risks covered subject to specified limits:-
  - Cash in transit to and from bank
  - Cash in insured premises out of a safe during working hours.
  - Money while in insured premises in a locked safe or strong room outside normal working hours
  - Money in residence of the insured or any partner and authorized officials.
  - Loss or damage to safe and strong room
  - NHIF stamps
- The insured provides estimated annual cash carry

COLLEGE OF INSURANCE
Driven by distinction

MONEY POLICY…Cont.

- The policy has two important clauses:-

1. Key clause

– States that the insurer shall not be liable for loss resulting from a safe or strong room being opened by a key which has been left on the premises when premises is closed.

– Keys must be kept safely under custody of the insured or responsible officer.

2. Escort Warranty Clause

   – Specifies amount of money carried under different circumstances e.g.

     – Upto Kshs.100,000.00 – messenger
     – 100,000 – 500,000.00 – two employees, one senior
     – 500,000.00 – 2,000,000.00 – security firm
     – More than 2m – security firm with police escort

COLLEGE OF INSURANCE
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MONEY POLICY…Cont.

Exclusions

- Fraud or dishonesty of insured’s staff not discovered within three working days after occurrence
- Shortage due to error or omission
- Loss of money from safe/strong-room using a key
- Loss of money from unattended motor vehicles
- Loss arising outside the geographical area

2.2;CREDIT INSURANCE

- The insurer undertakes to compensate the insured for losses incurred by reason of insolvency or protracted default where goods are sold on credit terms.
- No cover for non-payment through unwillingness to pay or through the policy holder's inability to collect.
- The risk covered is that of the debtor's inability to pay, insolvency, usually because of going into liquidation or ceasing to exist or to trade.
- Amount settled less than total debt – to encourage prudence in allowing credit and pursuing debtors.
- No cover against credit to individual members of the public because such risks cannot be accurately assessed.
- Underwriting factors
  - Customer base
  - Credit control policy

COLLEGE OF INSURANCE
Driven by distinction

3.GUARANTEE INSURANCES

1.Fidelity Guarantee

2.Bonds

a. FEDILITY GUARANTEEINSURANCE

Fidelity guarantees relate to situations where employees handle their employer's money or other property ie employees holding position of trust

- Handling cash as a cashier or sales assistant does; or
- Being involved in record keeping.

It is possible for the employee to divert the employer's money or property to somewhere it is not supposed to go - such as the employee's pocket or bank account.

- This is the sort of fraud and dishonesty that is insured by a fidelity guarantee.
- A money policy gives a very limited amount of fidelity guarantee cover in respect of theft by employees.

COLLEGE OF INSURANCE
Driven by distinction

Risk

The fidelity guarantee policy involves three parties:

i. the insurer;

ii. the insured (the employer);

iii. the applicant or insured person whose fidelity is guaranteed (the employee).

- The insurer becomes a guarantor in respect of the insured person and if the insured person commits a fraud or dishonesty against the employer, the guarantor must make a payment to make good that fraud or dishonesty.

Cover

The cover applies during:

- the currency of the policy;
- during the 'discovery period' - a period during which a theft employment, or dies.
- The cover will indemnify the insured in respect of loss of money or other goods and property caused by the fraud or dishonesty of the insured person.

Cover will also often include:

- auditors' fees incurred in substantiating the amount of the loss;
- the cost of rewriting or amending computer programs to avoid future losses.

COLLEGE OF INSURANCE
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- A policy may cover fraud committed before a policy commenced but not discovered until the policy operates provided that there has been continuous fidelity insurance.
- Fidelity guarantee policies may be subject to an excess or deductible.

FIDELITY GUARANTEE

There four types of fidelity guarantee policies:-

1. Individual policy
2. Collective policy
3. Blanket policy and
4. Position policy

Individual policy

This is issued where one employee is covered by name and for a specified amount

Collective policy

There are two types of this policy

i. **Named** collective and

ii. **Unnamed** collective

COLLEGE OF INSURANCE
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FIDELITY GUARANTEE

1:Named collective

- This incorporates a schedule containing the names and duties of guaranteed individuals
- The amount of guarantee is set against each name which can be an individual sum or a floating sum over the whole schedule

2:Unnamed collective

- Employees are covered by categories (e.g 1 manager, 10 cashiers, 5 clerks)
- The amount of guarantee can either be on per capita (per head) or floating basis

3: **Blanket policy**

- This is a form of unnamed policy which includes all employees without showing names or positions
- It is suitable for an employer with a substantial number of employees

4:Position policy

- This is issued to cover a certain position for a specified amount without naming the official
- This is important because changes in the person holding the position does not affect the cover

COLLEGE OF INSURANCE
Driven by distinction

FIDELITY GURANTEE : EXCLUSIONS.

1. Losses discovered after the expiry of the stated discovery period
2. Where there is change of employees and possible drop in supervision – insurer will not pay for losses arising from the change
3. Change of business and the insurer’s consent has not been obtained
4. Where an insured staff had left and was re engaged without consent of the insurer
5. Losses arising outside the specified duties of insured employees
6. Loss of goods or money not belonging to the insured
7. Losses caused by errors or omissions due to accounting mistakes

b. CREDIT INSURANCE

- It relates to an area of business where heavy losses can be sustained and yet many businesses are uninsured.
- Money owed to a business by its customers is often one of the largest single items on a balance sheet.
- If the money owed is not paid, the business likely suffers a loss. This potential loss through non-payment can be insured by means of a credit insurance policy.

Risk

The risk covered is that of:

i. the debtor's inability to pay,
ii. insolvency, usually because of going into liquidation, or
iii. Ceasing to exist or to trade.

NOTE: Credit insurance does not cover non-payment through unwillingness to pay, or through the insured's inability to collect.

- Its intention is to cover the risks existing between traders that do most of their business on credit terms.
- Policies are not generally available to retailers selling to the final consumer.

COLLEGE OF INSURANCE
Driven by distinction

Cover

Generally there are two types of policy available to the proposer;

i. **The whole turnover policy** - insuring the whole of their turnover against the risk of debtors defaulting;

ii. **The specific account policy** - insuring just those accounts that, for one reason or another, are felt to be at risk.

For specific account policies:

- insurers recognise that if only specific accounts are insured, there is selection against them;
- the dangerous accounts are being insured " those on which the insured thinks there may be a loss;
- as a result, the premium will be appropriately increased;
- the unseen danger for the insured is that they can get it wrong, i.e. the customer they think can never get into difficulty and default does so.
- It is probably more economical for a proposer to have a whole turnover policy.

COLLEGE OF INSURANCE
Driven by distinction

C:BONDS

- What is a bond? – **a bond is a contract issued under seal by an insurer which commits them to paying a sum of money if the conditions of the bond are broken.**
- What is the difference between bonds and an insurance policy?
  - Bonds – specialty contracts under seal. An effect of this is that once issued, it is binding and the insurers cannot cancel it.
  - Insurance policy – simple contracts
  - Bonds are often issued by insurers, but can also be issued by any other organizations or persons e.g. a bank.
  - An insurer issuing a bond agrees to pay a sum of money if the bond holder fails to perform a specific duty or fails to perform that duty properly e.g. dutiable goods leaving a bonded warehouse without payment of duty.
  - The premium for a bond is a flat fee that lasts the lifetime of the bond.

Risk and cover

Issuing a bond will mean that the provider, i.e. the insurer, will agree to pay a sum of money if the:

i. bondholder fails to perform a specific duty;

ii. bondholder fails to perform a duty properly;

iii. subject of the bond is dishonest, i.e. this type of bond has similarities to fidelity guarantee covers-

- The cover does not mention indemnity; a bond will have specific settlement details and is unlikely to delink with the principles of indemnity.
- In the event of certain circumstances, the bondholder will ask for payment (possibly by providing a certificate), as per details contained in the bond.
- Payment negotiation or loss adjustment will not take place, payment under the bond as per the settlement details will be met in full.

COLLEGE OF INSURANCE
Driven by distinction

Types of Bonds

1: Performance bonds

- These bonds guarantees performance of the contract, and an agreed fixed compensation will be payable if specific conditions are not met. This type of bond is common in the construction industry.

2: Bid or Tender Bonds

- Bid or tender bonds are used when the cost of new tendering has to be incurred should the highest bidder fail to take up an offer.

  Conditions for Bid Bonds

  – request for bids
  – general information and instruction
  – detail specifications
  – bid form

3: Immigration or Security Bonds

- Immigration or security bonds are issued to non-citizens whose conduct insurers guarantee.
- Should one fail to be of good conduct, an insurance company undertakes to pay the cost of deportation and/or the consequences of their bad conduct?

4: Court Bonds

- Court bonds are used when a court has the responsibility of administering the affairs of persons unable to manage their affairs due to mental incapacity or minority.
- The court appoints a receiver to administer the affairs of the estate of the person.
- The court will ask the receiver to provide a bond that will take care of any maladministration that might take place.

COLLEGE OF INSURANCE
Driven by distinction

5: Customs Bonds

- Customs bonds ensure that dutiable goods on which no duty has been paid do not find their way into the local market.
- Should the goods find their way into the market the insurer will meet the duty the insured has not paid.

6: Excise Bonds

- These bonds apply to finished products assembled locally and are meant for export and therefore duty is waived.
- Should these goods be sold locally the government will be compensated for the loss of the duty waived.

7: Warehouse Bonds

- Bonded warehouses are premises where dutiable goods are stored. Warehouse bonds guarantee payment of duty when goods leave the warehouse

COLLEGE OF INSURANCE
Driven by distinction

4.ACCIDENT INSURANCES

- Personal accident
- Group personal accident
- Travel insurances

4.1;PERSONAL ACCIDENT

- The policy pays benefits following accidents causing bodily injury or death to the insured person.
- **Terminology and benefits**

1. Bodily injury
   – Includes death and organic injuries or disease proximately caused by accident.
2. Accident
   – An unexpected, unplanned event caused by an external agent which must be visible and violent.

PERSONAL ACCIDENT…cont.

Policy Benefits

1. Death benefits
   – The sum insured is payable in the event of death occurring within a specified period – usually one year from the date of accident.
2. Permanent total disability
   - The policy pays a capital sum following irreversible disability that makes one unable to pursue gainful employment.
3. Permanent partial disability
   - This is disability that is irreversible but only prevents the insured from attending to a definite part of their occupation. A percentage of the capital sum is payable dependant on the degree of disability.
4. Temporary total disability
   - Total disability for a temporary period only leading to loss of earning. Settled in terms of weekly earnings. Payslip or bank statement required for proof of weekly earnings payable.
5. Medical expenses
   - Cost of medical treatment for injuries sustained following an accident.

PERSONAL ACCIDENT…cont.

Exclusions

- Suicide, attempted suicide and self inflicted injuries
- Influence of alcohol or intoxicating liquors or drugs
- Aviation unless as a fare paying passenger
- Hazardous sports as a professional e.g. motor racing, motor cycling, mountaineering, big game hunting
- Sickness existing before accident
- Childbirth and pregnancy related illness
- HIV/AIDS, venereal diseases and insanity
- War, poison and related incidents
- Insured committing any breach of law

GROUP PERSONAL ACCIDENT

- Group personal accident
  - ✓ Policy taken out by an employer for the benefit of employees.
  - ✓ Insured – employer; insured person = employee
  - ✓ Benefits and premium based on annual salaries.
  - ✓ Can be on named employees or unnamed employees basis.

TRAVEL INSURANCE

- Business travel insurance **covers those employees that are sent on business trips abroad** for the purposes of the business

- Similar insurances are also taken out by **individuals going for holidays**

- The policy may be for :-
  - A **single journey** or
  - It may be an **annual policy**

TRAVEL INSURANCE --COVER

- **Personal accident**
- **Emergency medical**, dental and other related expenses up to limit
- **Baggage and personal money** cover will include:-
  - Personal property accompanying the insured person against loss or damage up to certain specified amount
  - Some policies may include business samples and equipment as personal property
  - Some limited amount of money may be allowed including, travelers cheques, tickets, vouchers and passports

COLLEGE OF INSURANCE
Driven by distinction

TRAVEL INSURANCE –COVER……

- **Cancellation and curtailment costs**
  - **If the journey is cancelled** because of domestic disaster, illness or accident to the insured person or specified close relatives, friends and business associates, the policy will **pay loss of irrecoverable deposits and any other amounts that legally have been paid** up to a certain specified amount per insured person
  - **The costs associated with delayed travel with a minimum of 12 hours delay and any costs connection therewith**
- **Personal liability**:-there is legal liability cover for death and any bodily injury caused by the insured person to the third party, subject to a limit
- **Legal expenses**:- this is respect of food or advise incurred to pursue a civil action to recover damages for personal injury or death of an insured person subject t a certain specified amount

COLLEGE OF INSURANCE

Driven by distinction

HEALTH INSURANCE

INTRODUCTION

- This policy provides cover for the cost of
  - private medical treatment for
  - illness and
  - other medical conditions.
- Individuals and employers have two main options to handle medical costs:
- self-funding
- Insurance.

Medical / Health insurance

- The purpose of medical (health) insurance is to provide cover against the course of secondary healthcare. It aims to provide cover for 'acute' illness or injury that requires relatively short-term treatment that in turn leads to recovery.
- It does not cover primary care provided by dentists or general practitioners or the functions that support them e.g. practice nurses.
- Medical Insurance policies are contracts of indemnity as they enable the insured to claim not more than the cost of treatment subject to maximum sum insured

Classes under health insurance

The products that are issued based on an individual's health are:

i. Health Insurance
ii. Critical Illness Insurance
iii. Permanent Health Insurance
iv. Personal Accident and Sickness Insurance

Benefits of health insurance

The following expenses are generally paid:

1. Doctor's and consultant's fees
2. Anesthetist's fees
3. Hospital bed and ward charges-bed, accommodation and food
4. Drugs and like requirements e.g. gloves, syringes etc used.
5. X-rays, CT Scan and laboratory tests and other diagnostic procedures
6. Nursing services
7. Theatre services

Definitions

Eligible treatment

- This refers to surgical or medical procedures, which is the cure or relief of **acute** illness or injury, including diagnostic procedures.
- The immediate purpose of which is the cure of **acute** illness and not the alleviation or management of long-term illness.

Acute conditions

- This is a condition that generally comes on quickly and does not last a long time and so is not chronic or a single episode of an illness or injury.
- The treatment has a clearly defined end point, and the patient recovers and returns to his normal or previous state of health.
- For some insurers, this applies to acute episodes of a chronic disease e.g. a diabetic coma in a patient with diabetes.

Chronicle illness

- A long-term condition that cannot be cured and so treatment can only relieve the symptoms.
- It is an illness or injury having one or more of the following characteristics:
- It is permanent.
- It leaves residual disability.
- It causes an irreversible permanent change to bodily or mental condition.
- It requires special training or rehabilitation
- It needs an indefinite ongoing period of supervision, observation or care.
- A point has been reached where no further intensive treatment will make any improvement and at therapy is aimed at maintaining that state without further deterioration. There may be a need for regular drugs to control the static state.
- Insurers usually make concessions and the first episode of chronic illness is usually covered and excluded thereafter. Cancer may be covered for the first year of discovery or until it is declared to be terminal.

Conditions and Exclusions

1. Age Limit 18 to 60 years.
2. Dependent Children 6 months to 18 years.
3. Waiting period first 28 days.
4. Family planning, infertility and child birth.
5. Cosmetic or plastic surgery.
6. Dangerous sports.
7. Obesity etc.
8. Homeopathy, chiropractic acupuncture, herbal medicine.
9. Depression or emotional or mental or related disorder.
10. Venereal Diseases or Suicide, Alcohol

1:Comprehensive Policies

- These are ‘full cost’ or ‘full refund’ policies. They have the widest range of benefits and services and are expensive.
- They may cover inpatient, outpatient and day case treatment of eligible medical conditions as well as:
- Alternative or complementary medicine.
- Dental treatment by a specialist up to a specified annual amount.
- Optical care up to a specified annual amount
- Provision of a guest room for a parent to accompany a child during hospital stay per night.
- Home nursing services.
- Private ambulance service

2:Standard Policies

- They are similar to comprehensive policies but with some of the benefits reduced or excluded completely in order to contain treatment costs and to reduce premiums.
- They may require patients to receive treatment in pre-specified hospitals or with pre-specified doctors with whom they have negotiated favorable rates for accommodation and services

COLLEGE OF INSURANCE
Driven by distinction

4:Budget Policies

- These allow customers to buy medical cover at low premium.
- They may have limited benefits so that customers buy cover for only the more important and expensive types of treatment.
- The treatment must be only at a specified network of hospitals which the insurer has negotiated favorable rates.
- Cost is reduced because cover is strictly limited and also the hospitals are specified

COLLEGE OF INSURANCE
Driven by distinction

5:International Policies

- These allow customers to buy medical cover at low premium.
- They may have limited benefits so that customers buy cover for only the more important and expensive types of treatment.
- The treatment must be only at a specified network of hospitals which the insurer has negotiated favorable rates.
- Cost is reduced because cover is strictly limited and also the hospitals are specified.

6:SENIOR MEDICAL INSURANCE

- These are policies specially designed to cater for senior citizens, usually those above retirement age;
- The purpose of these policies is to encourage elderly persons who are more likely to require medical treatment to insure themselves against the cost of private treatment.

Critical Illness or Dread Disease Cover

- The cover is usually sold as an extension to a life policy, but can be sold on a "stand alone" basis.
- The purpose of critical illness cover is to provide a benefit to aid the policyholder to return to good health.
- If the policy is sold on "free standing" / " stand alone", payment of the benefit will only be made if the life assured survives a minimum period from the date of diagnosis, usually 15 to 30 days. For a disease to be covered it must be capable of being carefully defined.

The policy will pay out the sum assured on diagnosis of certain specified critical illnesses such as:

- Cancer
- Stroke
- Kidney failure
- Coronary artery disease
- Heart attack
- Major organ transplant

Agriculture Insurance

Classes of Agriculture Insurance

1. Livestock insurance
2. Blood stock insurance
3. Poultry insurance
4. Forestry insurance
5. Green house insurance
6. Aquaculture insurance

COLLEGE OF INSURANCE
Driven by distinction

Livestock insurance

- Provides cover to dairy, poultry, beef cattle, horses, sheep, goats and any animal of economic value.
- A broad cover to livestock accidental mortality caused by
  - fire and smoke,
  - lightning,
  - flood & windstorm,
  - diseases of terminal nature and epidemics,
- emergency slaughter on a vets advice.
- Theft of stock raised may also be covered.

Sum insured is based on the value of the insured animal and can be reduced based on animals age.

Blood stock insurance

- Provides cover for very high value animals mainly horses, it’s a minor business line Animals can be insured on individual basis or collectively
- The insured events include
  - mortality,
  - disability,
  - infertility,
  - medical treatment and surgery.

The sum insured is based on the market value of the animal

COLLEGE OF INSURANCE
Driven by distinction

General exclusions

- Willful misconduct.
- Famine or Malnutrition.
- Feed Poisoning.
- Culling.
- Prior Accidents or Diseases.
- Animal Shows & Exhibition.
- Mysterious disappearance

POULTRY INSURANCE

- ‘Poultry' refers to poultry units consisting of chicks/ hens/ cocks /ducks, Turkeys, Quails and such other domesticated birds' reared for eggs and/or meat. It includes

(a) layer birds

(b) broilers (c)

- Hatchery birds (Breeding Stock).

The insurance covers losses to stock during

– Rearing period
– Egg laying period
– Broilers up to maximum specified age e.g 6 weeks
– Breeders up to maximum specified age e.g. 64 weeks

Indemnity

  - Indemnification scale for broilers
  - Indemnification scale for breeders
- Indemnification scale for breeders for loss of potential egg
- Reared poultry is covered against losses due to
  - Infectious diseases.
  - Accidental death due to Suffocation, freezing, heat stroke, fire and accompanying risks.
  - Limited emergency slaughter against epizootic outbreaks.
  - Theft of stock.

Forestry Insurance

- It protects standing tree crop against losses due to
  - Fire, lightning, explosion and aircraft impact
  - Coverage can be extended to damage caused by volcanic eruption, windstorm,
  - Fire fighting expenses and debris removal are also covered and are capped at an annual aggregate limit
  - Can cover natural forests as well as plantations.
- **Sum Insured (Forestry)**
- Trees increase in value as they grow and therefore the sum insured increases as trees continue to mature.
- It is necessary to verify the method of establishing the value of the crop at various stages of growth with the insurer at inception of the policy.

Basis of indemnity

- **Partial Loss**
- A partial loss is when the insured tree crop is carried to harvest following the occurrence of a peril insured against.
- **Total loss**
- Any insured field on which the insured tree crop is damaged to the extent that it would not be feasible to carry the timber up to harvest.

COLLEGE OF INSURANCE
Driven by distinction

Greenhouse

- A greenhouse is a building in which plants are grown. These structures range in size from small sheds to very large buildings
- It is a structure with different types of covering materials, such as a glass or plastic roof and frequently glass or plastic walls.

Perils covered

- The infrastructure is insured against damage from
- storm (including weight of ice/ hail storm),
- water, fire, smoke, lightening explosion, malicious damage, aircraft impact and earthquakes.

- Cover may be extended to cover business interruption.
- Provides comprehensive cover for material damage to structures, irrigation equipment, crop, breakdown in water filtration systems and pack house machines

COLLEGE OF INSURANCE
Driven by distinction

- **Greenhouse sum insured and indemnity**
- The sum insured is commonly based on agreed value.
- Indemnity is calculated as a percentage of damage to both structures and contents

AQUACULTURE

- This is the growing of aquatic organisms in warm fresh water, cold fresh waters and in marine waters.

Aquaculture insurance

- Cover farmers engaged in breeding and raising aquatic fauna and growing aquatic flora.
- A major part of it involves fish rearing in artificial ponds inland It is becoming increasingly important as human population increases and fish etc decreases due to over exploitation.
- Cover for loss of stock is offered on named peril or all risk bases.
- Covered perils include meteorological events, diseases, pollution, predator attacks, collision, oxygen depletion, changes in pH and salinity, theft and escape. Both offshore case systems and inshore pond cultures are covered

COLLEGE OF INSURANCE

Driven by distinction

5: LIABILITY INSURANCES

1. Public liability
2. Product liability
3. WIBA/EMPLOYERS LIABILITY
4. Professional indemnity
5. Directors and officers

INTRODUCTION

- Liability policies serve to meet the need to have potentially crippling liabilities protected.
- Liability insurance provides indemnity to the insured in respect of financial consequences of legal liabilities towards third parties arising out of their business activities.
- The policy indemnifies the insured against:-
  - Legal liability under law
  - Claimant's costs and expenses
  - Defense costs

COLLEGE OF INSURANCE
Driven by distinction

5;1.**PUBLIC LIABILITY**

- The public liability policy covers the policyholder in respect of legal liability to third parties for both bodily injury and for loss of or damage to property arising out of business activities.
- Cover includes claimants costs and expenses incurred with the insurer’s consent
- Can be arranged on a limit of indemnity per event or per year.
- Examples:-
  - Contractor damaging telephone cables
  - Building collapsing injuring people

PUBLIC LIABILITY…Cont.

- Exclusions
  - Judgments delivered outside the geographical area
  - Loss or injury arising from employment
  - Motor vehicle losses
  - Liability assumed under contract
  - Liability for property held in trust
  - Professional liability
  - Product liability
  - War related liabilities
  - Liability due to pollution and defective sanitation – that is not accidental as it may occur over time

5.2.PRODUCT LIABILITY

- Products liability insurance relates to the insured's legal liabilities for bodily injury to persons or loss of or damage to material property caused by products or goods sold, supplied, repaired or tested by the insured.
- Can be issued alone or as an extension to the public liability policy.
- Policy operates after goods have left the insured's premises
- The occurrence must be accidental
- Examples:-
  - Food causing sickness in hotels
  - Obnoxious objects in packed/tined food e.g snail, flies etc.
  - Defects in ladders
  - Farm chemicals – clear instructions
  - Faulty electrical appliances
  - Bursting tires

PRODUCT LIABILITY…Cont.

Exclusions:-

- Injury to employees
- Damage to property belonging to the insured or in the custody of the insured
- Cost of replacement of any products giving rise to a claim
- Product recall liabilities
- Liabilities assumed under an agreement unless such liability would still have attached notwithstanding the agreement
- Defective design, plan or formula – uninsurable trade risks
- War related risks
- Liabilities arising from products sold prior to the retroactive date as shown in the policy schedule.

COLLEGE OF INSURANCE
Driven by distinction

5.3. PROFESSIONAL INDEMNITY INSURANCE

- Covers professional persons or firms for their legal liabilities to third parties arising from their professional negligence or that of their employees.
- Examples of professions applicable:-
  - Lawyers
  - Accountants
  - Architects and surveyors
  - Insurance brokers, stock brokers
  - Doctors, dentists and other medical practitioners
- Professionals are expected to exercise skill and care beyond the normal “duty of care”.
- Sources of professional negligence
  - Contracts
  - Tort
  - Vicarious liability – where a professional is held liable for the negligent acts of their employees which arise out of and in the course of the employees’ performance of their duties.

COLLEGE OF INSURANCE
Driven by distinction

5.4;WORK INJURY BENEFITS ACT, 2007

- Enacted to provide for compensation of employees against injury, death or diseases arising out of and in the course of employment.
- Introduces compulsory insurance by all employers against accidental injury or death or occupational diseases to employees arising out of an in the course of employment.
- Settlement based on 96 months earnings
- Outlaws litigation by injured employees due to employment related accidents/ diseases

5.5. EMPLOYERS’ LIABILITY INSURANCE

- Covers legal liability of an employer that relates to bodily injury or disease sustained by an employee arising out of and in the course of their employment.
- The claimant must prove negligence of the employer in court – unlike WCA where benefits are automatic
- All employees covered irrespective of earnings
- If already paid under WCA, amount reduced from the employers’ liability settlement.
- Arranged based on limits of liability
  - Any one person
  - Any one occurrence
  - Any one year

5.6.DIRECTOR'S & OFFICERS' LIABILITY

- The policy indemnifies the directors and officers against their legal liabilities towards shareholders and other stakeholders arising out of negligence in discharging their duties causing financial losses.
- Liability may arise out of lack of care and skill in the performance of the duties e.g.
  - Negligent advise or mis-statement especially in merger or take over
  - Acting beyond the company's constitution – memorandum of association
  - failure to arrange proper insurance
- Cover is against wrongful acts in official capacity.

COLLEGE OF INSURANCE
Driven by distinction

6:TRANSPORT INSURANCES

- Motor insurance
- Marine insurance
- Aviation Insurance

COLLEGE OF INSURANCE
Driven by distinction

6.1;MOTOR INSURANCE

B. LEVELS OF COVER

- Four levels:-
  i. Act only
  ii. Third party only
  iii. Third party fire and theft
  iv. Comprehensive

i. Act only

- Covers legal liability of the motorist to third party bodily injuries including death while the motor vehicle is being **driven on public roads.**
- Unlimited cover
- Minimum level of cover required under the Act.

ii. Third Party Only

- Provides cover against third party injuries or death and property damage arising from motor vehicle accidents.
- Liability for injury covered regardless of where the motor vehicle is being driven.
- Limit of liability imposed on third party property damage.

iii. Third Party, Fire & Theft

- TPO cover plus loss or damage to the insured's motor vehicle arising from fire or theft.

iv. Comprehensive Cover

- Widest motor cover incorporating third party fire and theft as above and in addition covers accidental loss or damage and malicious damage to the insured's motor vehicle.

COLLEGE OF INSURANCE
Driven by distinction

C. TYPES OF MOTOR POLICIES

1. Private car insurance

Consider various uses of the private car:-

- For social and domestic purposes and pleasure purposes;
- By the policyholder in person in connection with their business and that of their employer;
- By other people apart from the policyholder
- For commercial traveling and motor trade - **excluded**
- For carriage of goods for hire or reward - **excluded**

C. TYPES OF MOTOR POLICIES…Cont.

2. Commercial Vehicle Insurance

Various classifications:-

- **Goods carrying vehicles**
  - ✓ May carry own goods or for hire and reward.
- **Passenger carrying vehicles**
  - ✓ Private passenger vehicles e.g. staff bus
  - ✓ Public service vehicles – (public hire) e.g. matatus, taxis
    1. Private hire – car + driver
    2. Self drive hire – no driver
- **Agricultural and forestry vehicles**
  - Used solely for forestry and agricultural purposes
  - Can be exempted from taking the required motor cover – public liability would be appropriate.
- **Motor trade insurance**
  1. Road risks – used when vehicle is under road test.
     - Special number plate (KG Plate) issued by government agencies
  2. Internal risks – loss or damage to motor vehicles in the garage arising from fire, theft, accidental damage and floods.

D. POLICY EXTENSIONS

1. Protected No Claim discount
    - Applies to policyholders who have earned maximum no claim discounts and may want to protect it in the event of an accident.
    - Additional premium charged.
2. Windscreen cover
3. Radio cassettes and personal effects
4. Personal accident – for insured and spouse in respect of motor related accidents.
5. Loss of use – for hire of alternative car while damaged vehicle is under repair

NB. A claim under a policy extension does not affect no claim discount nor is it subject to compulsory policy excess.

E. COMESA YELLOW CARD

- The Common Market for East and Southern Africa (COMESA) comprising 21 states was formed in 1994. Secretariat in Lusaka, Zambia.
- Agreed to promote regional integration through trade, growth and development of their natural and human resources for the mutual benefit of their people.
- Kenya is among the COMESA countries which signed the protocol establishing the Yellow Card.
- At present the scheme is operational in thirteen (13) countries namely **BURUNDI, DJIBOUTI, DRC, ERITREA, ETHIOPIA, KENYA, MALAWI, RWANDA, SUDAN, TANZANIA, UGANDA, ZAMBIA AND ZIMBABWE.**
- Objective of the Yellow Card:- to allow motorists passage through member states by providing the minimum compulsory third party motor vehicle insurance cover as those required by laws in force in the territories of each of the participating states party to the Yellow Card Scheme.

Cont.

- The scheme was intended to:-
  - Facilitate inter-state traffic movements
  - Enable accident victims to be compensated promptly
  - Trade incentive
  - Enhance greater cooperation between insurance companies in the member states.
- **Scope of cover**
  - Compulsory Third party motor cover
  - Has been enhanced to include liability for third party property damage where the cover is not compulsory
- Each member state has a national bureau responsible for management and control of the COMESA Yellow Card by:-
  - Acting as issuing authority
  - Handling agency – for claims occurring within the country
- Each insurer must submit monthly returns of Yellow Cards issued to the national bureau which in turn submits the yellow cards to the COMESA Secretariat.

6.2.MARINE INSURANCE

- Risk areas:-
1. Hull – vessel and its equipment and spare parts.
2. Cargo – goods carried by the vessel
3. Freight – amount paid for transporting the goods or for hire of the ship.
- Most marine policies in the region relate to the cargo.
- Goods cover effective from port of origin to destination.
- Extend to include destination to inland town.
- Hull cover in the region is for small harbor craft, pleasure craft an fishing vessels.
- Hull cover includes the vessel, machinery ad their equipment and sometimes third party liability.

MARINE INSURANCE… Cont.

- 4 categories of marine insurance:-

1. **Time policy**
   – Issued for a fixed term usually not exceeding 12 months.
2. **voyage policy**
   – Covers the period of the voyage. In respect of cargo, cover is from warehouse of departure to the warehouse of arrival.
3. **Mixed policy**
   – Covers the subject matter for the voyage and a period of time thereafter.
4. **Open cover policy**
   – A general marine policy covering cargo issued in general terms. Taken out where goods will be imported from time to time.
   – Details of cover:-
     - Nature of cargo to be covered e.g. food items
     - Perils covered
     - Applicable rate
     - Maximum amount covered per vessel
     - Basis of cover e.g. warehouse to warehouse.
   – No fixed period. Goods declared by insured per shipment and a certificate of insurance is issued and premium charged for each consignment.
   – The certificate bears details of the vessel, value of goods, and the voyage.

6.3;AVIATION INSURANCE

- Limited to small aircraft only in East Africa.
- Large aircraft insured with more established markets in Europe and the USA.
- Issued mostly on "All Risks" basis.
- **What the policies cover**

1. The hull – aircraft and equipment
   - Covers accidental loss of or damage to the aircraft.
   - Cover includes disappearance if aircraft is unreported for sixty days after the commencement of the flight.
2. Liability to passengers
   - Passenger legal liability governed by international conventions for international flights and domestic legislation for national/ local flights.
   - There are two main international agreements governing air travel:-
     1. The Warsaw Convention (1929) – made signatories liable to passengers without negligence subject to certain maximum limits
     2. The Hague Protocol (1955) – raised some of the limits under the Warsaw Convention.

Cont.

- The passenger legal liability cover pays for:-
  - Accidental bodily injury to passengers while entering, on board or alighting from the aircraft
  - Loss or damage to baggage and personal articles of passengers following an aircraft accident.

1. **Liability to others**
   - This is essentially legal liability towards third parties arising from accidental injuries, death or damage to their property e.g.
     - Owners of airports
     - Airport employees
     - Members of the public at large.

END

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DIP 101 – Unit 6

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RISK MANAGEMENT

LECTURE- OUTLINE

i. Concept of risk management
ii. Importance of risk management
iii. Risk management processes
iv. Risk management techniques
v. Nature of personal and corporate risk management

Concept of risk Management

- Risk is unavoidable and is present in every human situation
- It is present in daily lives, public and private sector organizations.
- Depending on the context (insurance, stakeholder, technical causes), there are many accepted definitions of risk in use. (unit 1)
- The common concept in all definitions is uncertainty of outcomes.
- Where they differ is in how they characterize outcomes.

Description of risk

- ***Risk refers to the uncertainty that surrounds future events and outcomes.***
- ***It is the expression of the likelihood and impact of an event with the potential to influence the achievement of an organization's objectives.***

- Some describe risk as having only **adverse** consequences,
- while others are **neutral.**

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DEFINITION: RISK MANAGEMENT

- "The identification, analysis and control of those risks which can threaten the operations, assets and other responsibilities of an enterprise.'

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OBJECTIVES OF RISK MANAGEMENT

- Risk Management is an integral component of good management and decision-making at all levels of an organization.
- All departments in an organization manage risk continuously whether they realize it or not, sometimes more rigorously and systematically, sometimes less.
- Risk management has objectives before and after a loss occurs referred to as :
  - Pre-loss objectives and
  - post-loss objectives.

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Pre-loss objectives include to:

- Prepare for potential losses in the most economical way,
- Reduce anxiety,
- Meet any legal obligations

Post-loss has the following as the objectives:

- Ensure survival of the firm
- Continue operations
- Stabilize earnings
- Maintain growth
- Minimize the effects that a loss will have on other persons and on society

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The Importance of Risk Management to an organization

- Risk management provides a framework for addressing risks in consistent ways
- Creates an environment where informed decisions about your organization's risks are made in open and transparent way
- Gives assurance on the achievement of objectives by:
  - reducing uncertainties;
  - effectively managing threats to an acceptable/tolerable level;
  - making informed decisions about exploiting opportunities, where they exist

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Three steps in Risk management process

1. Identification:
   – Identification techniques
2. Analysis/Evaluation:
   – Measure the likely impact;
   – Considers frequency and severity
3. Control:
   – Financial Measures
   – Physical measures

RISK MANAGEMENT PROCESS: 3 STEPS

IDENTIFICATION

Risks should be identified	Various techniques to do this

ANALYSIS

Measure the likely impact of the risk	Considers frequency and severity

CONTROL

Financial-a Retention OR Transfer	Physical- Elimination OR Minimisation

1: RISK IDENTIFICATION

- Risk identification is the process of getting to know what the organization is up against
- It seeks to answer such questions as:
  – What stands between the organization and its objectives or goals?
  – What can go wrong?
  – What has gone wrong in the past?

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Importance of Risk identification

- This is important because nothing can be done about any risk until it has been identified.
- To identify a risk is to acknowledge that the risk exists in the organization and it poses a danger.
- An organization is faced with a variety of risks whose presence requires to be acknowledged.
- There are risk identification techniques that can be used to highlight areas where an organization is likely to suffer.
- There are Common features of risk identification which require to be noted and appreciated. This is because they explain the core purpose of the risk identification.

Common Features of Risk Identification

- The task of risk identification must be given proper priority in the organization because unless risks are identified, then nothing can be done about
- There is a range of techniques available for risk identification and none of them can be used in all situations;
- It is a continuing process and not a one-off exercise. it should take place continuously as the one-off approach is of little value in many practical situations;
- There must be efficient record keeping of the risks identified;
- Other people such as employees, in addition to the risk identifier, should be involved in the process of risk identification whenever possible so that they become part of the solution to the problems posed by risks;
- The cost of risk identification must be borne in mind at all times in the risk identification process;

1.Physical Inspections

- This involves the inspection of plants, processes or premises by a risk identifier. It is important that the identifier does some preparations before the actual exercise commences.
- Such preparations will involve, for example:
  - Finding out what processes are carried out in the premises;
  - Finding out the nature of the work done in the premises;
  - Finding out the type of equipment in use in the premises;
  - Finding out the processes carried out there in; and
  - Finding the layout of premises.

The Outcome

- The outcome of such as inspection would be:
  - A form detailing the premises visited;
  - An structured inspection report for all the areas inspected; and
  - Details of the faults and risks identified.

Advantages

1. One does not rely on another person telling them what the risk is like as they will have seen it themselves;
2. An outsider can be used. This is important as there is a tendency for those who are close to the risk to underrate its importance.
3. It allows the person carrying out inspection to build a good relationship with people at the site.
4. Inspection can be done at a very short notice. There is no need for elaborate preparation.

Disadvantages

1. It is time consuming to carry out physical inspections-
   – Needs preparation including visiting premises
   – A company may also have many premises, which may necessitate many days of inspection.
2. There could be a tendency for those on site to believe that the person who carries out the physical inspection is the one whose job is to identify risk.
3. There must actually be something for the risk identifier to inspect. Accordingly, physical inspection would be of no value when premises are still at designer stage.

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2.Organizational Charts

- This shows the basic organizational structure of an organization or company.
- It shows the **concentration of activities** and the **distribution of powers** and also **dependency** among sections of the organization.
- A chart may highlight a weakness in an organization.
  - For example if there is only one accounting department for several regional offices then a weakness or failure in this area could intervene with the operations of the entire organization.

Advantages

1. It helps the risk identifier to become familiar with the structure of the company itself and it therefore becomes easy to understand any weakness which may introduce or enhance a risk;
2. If employees are involved in the construction of the chart, this may encourage them to think about risks from the perspective of the whole organisation;
3. It is good at highlighting areas of particular dependency, concentration or consideration of risk.

Disadvantages

1. It is too broad in its identification to enable specific solutions to be suggested for specific risks. It is may be a useful as a first step to risk identification, but would really have to be associated with some other technique or techniques to fully identify risk facing a organisation;
2. It can be too simplistic as the management structure of many organisations can be very complex and the danger is that an over-simplified chart may omit a lot of important details.

3.Flow Chart

- Flow chart is a chart showing the flow/route taken by ingredients of the final products to completion and final delivery. These are processes indicating activities.
- It shows the route and illustrates possible bottlenecks or single point of risk. Thus, adds value by highlighting any market exposures at the delivery level.
- The chart is a type of diagram that represents process, showing the steps as boxes of various kinds, and their order by connecting them with arrows.
- This diagrammatic representation illustrates a solution to a given problem. Process operations are represented in these boxes, and arrows; rather, they are implied by the sequencing of operations.
- Flowcharts are used in analysing, designing, documenting or managing a process or program in various fields

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Advantages

1. Allows complicated parts and processes to be broken down into smaller and more manageable parts;
2. The flow chart is more detailed analysis than the other techniques above;
3. Flow charts are qualitative rather than being dependant on mathematical calculations.
4. As such, they are relatively simple to follow and to understand and can be used with a range of managers and other people who may have quantitative skills.

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Disadvantages

1. They can be time consuming and the end result may not seem to be an adequate recompense for the effort;
2. They can become too simplistic in their approach. This is particularly true where there is a very complex plant or process. The problem is that aspects will be omitted because they cannot easily be accommodated by the chart;
3. The risks, which are identified, are still very general. They are risks such as “fire”, “explosion” or “breakdown”. This may not be adequate in many cases;
4. No mathematical measure of the likelihood or probability of events is included. Events are talked about as if they all had an equal chance of occurring, which is not the case.

4.Checklists /Questionnaire

- A questionnaire is a list of questions send to the people concerned that elicit responses.
- The risk officer may draft questionnaire and send to the people in operations to fill. The information collected is then used to establish the exposures.
- A checklist is a tool used especially in attempting to understand compliance. Certain aspects (which may be standards, laws or practice) regarding areas of concern are understood, agreed upon and written down which acts as yardsticks against which the reality is checked against.
- The checklist method involves sending a designed questionnaire to the site for completion by someone there.
- It involves asking questions about the activities of the company.
- The questions evolve around the risks which an organization could be exposed to.

Advantages

1. The questions provide a standardized way of management of risk. Good for comparison and benchmarking
2. Can be adapted to individual areas of risk
3. Useful for putting diverse information sources into common format
4. Useful as an aid to help remember by the risk team – ease of recording
5. Eases delegation of risk management work
6. Can be adapted very easily to changes in the makeup of a business;
7. New questions can be added and redundant ones removed;
8. Efficient way of gathering data from a widely spaced locations and variety if any.

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Disadvantages

1. Preparation requires care and thought. Designing of questions not ease
2. Answers are directed by the questions- not looking out of box
3. Interpretation of questions may not be ease hampering collection of data - ambiguity
4. Can focus the users' attention on the questions not think objectively
5. Check list can be in the form of survey reports by risk surveyors which focuses on individual exposures like safety, security procedures etc
6. The design of checklist does not take into account the technical skills of users
7. One can never be sure of the manner in which the form was completed .It is hoped that it was done with care and attention to detail. It is however, possible that people completed the checklist in a hurried and less than accurate manner simply to get the job out of their way.

Other Techniques

Other techniques of identifying risks include:

- Fault trees;
- Hazard Analysis; and
- Operability Studies.

- These methods are mathematical in nature and place a probability on the chance of occurrence of the risk and its likely severity.
- Their detailed study is, however beyond the scope of this course

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2. RISK EVALUATION

- Once the risk has been identified, the next step **is to measure the impact one feels the risk is likely to have to the organization**; to evaluate a risk is therefore to assess or to analysis its effect.
- Evaluation addresses the question of how important the risk is in financial terms because as a rule, losses must be thought of in financial perspectives.
- Inevitably, assessing a risk also determines the methodology the organization will adopt in order to control it.
- For example, is the risk one that the organization can assume at a little cost or is it one with catastrophic proportion?

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Benefits of risk analysis

1. It helps in understanding and describing risks, both qualitatively and quantitatively.
2. Measuring risks carried against risk levels acceptable to the organisation. Organisations for instance insurance do have acceptable levels of risks as agreed upon that they are able to take or have appetite for.
3. Helps stimulate and support decisions about risk reduction measures. The risk analysis provides useful information about risks. Risks are described and measured clearly thus clearing ensuring that the treatment of such risks is done based on information.
4. Analysing risks assists an organisation present risk concepts clearly and in a consistent way. Concepts and terms are well defined that help those concerned to read from one script.
5. This process also encourages good decisions about contingency planning. Emergencies that may arise are defined well and possible controls put in place. Decisions concerning the management of emergencies or contingencies can be arrived at with ease.

Risk Assessment Methodologies

- Risk analysis and risk assessment are often used interchangeably.
- Risk analysis is the process of assessing risk magnitude and weighing the cost/benefit of implementing counter measures to mitigate the risk.
- We have two basic techniques used to assess the risks namely **quantitative and qualitative risk** analysis techniques.

a; Quantitative risk assessment

- In quantitative risk analysis, the likelihood of occurrence of particular threats and the risks or loss associated with these particular threats are estimated and assessed according to predetermined measurement scales.
- The analyst will attempt to provide financial loss calculations that can be mathematically measured.
- Quantitative analysis requires significant time to associate cost and assemble the required metrics.

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Features of quantitative risk assessment

- It yields results in terms of financial impact;
- It emphasizes remediation based on cost of remediation versus potential cost of loss;
- All findings are expressed in monetary values, percentages and probabilities;
- It allows for more control and understanding regarding procurement and budgeting;
- It requires larger organisational cooperation;
- It is very time intensive.

Advantages of quantitative risk assessment

1. Assessment and results are based substantially on independently objective processes and metrics. Thus, meaningful statistical analysis is supported;

2. The value of information is expressed in monetary terms, with supporting rationale and is better understood. Thus, the basis for expected loss is better understood; and

3. A credible basis for a cost/benefit assessment of risk mitigation measures is provided. Thus, information security budget decision-making is supported.

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The **disadvantages** of quantitative risk assessment

1. Calculations are complex. If they are not understood or effectively explained, management may mistrust the results;

2. A substantial amount of information about the target information and its IT environment must be gathered and

3. There is not yet a standard, independent developed and maintained threat population and frequency knowledge base.

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a; Qualitative

- This is the evaluation of a risk without quantitative analysis i.e. without use of statistical data.
- It involves making judgment on the frequency and severity of the risk.
- In some cases e.g. where there are no records this is all that can be possible.
- Experience of similar events or situations is important.

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The features of qualitative risk analysis

- It requires less time and is, therefore, less costly;
- It is a quicker process to complete;
- Findings are simple in nature;
- Focus is on specific exposures to the affected assets;
- Values of loss are perceived and not quantified;
- Exposures are rated subjectively; and
- Focus is on understanding the risk and often includes recommendations for mitigation based on analysts’ knowledge and expertise.

The **advantages** of qualitative risk analysis

1. Calculations are simple and readily understood and executed;
2. It is not necessary to determine quantitative threat frequency and impact data;
3. It is not necessary to estimate the cost of recommended risk mitigation measures and calculate cost/benefit; and
4. It is a general indication of significant areas of risk that should be addressed is provided.

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The **disadvantages** of qualitative risk analysis

1. Risk assessment and results are essentially subjective in both process and metrics – the use of independent metrics is avoided;
2. No effort is made to develop a monetary basis for value targeted information assets;
3. No basis is provided for cost/benefit analysis of risk mitigation measures – there is only subjective indication of the problem; and
4. It is not possible to track risk management performance objectives when all measures are subjective.

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3:RISK CONTROL

- This is the third and final step in the risk management process and **it is the objective** of the whole process of risk management.
- Its aim is to limit the total cost of losses to the lowest level by implementing measures which:

1. Prevent losses from occurring, for example by reducing the level of risks which might cause a loss;
2. Protect people or and/or property from loss;
3. Detect and limit the extent of loss that may occur;
4. Maximize the recovery from any loss that has occurred;
5. Limits the extent of any loss and maximizes the recovery from losses; that have occurred. Such measures can either be passive or pro- active.

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Methods of risk control

Broadly, methods of risk control can be categorized into two- physical and financial.

1:Physical control of risk

- Among the key methods of physical risk controls are:

Cont.

a)Elimination/ Avoidance

- One sure way of not having a loss is to eliminate the possibility altogether.
- However, in the real nature of the (business) world, it is not possible to eliminate all the risks facing an organization other than by closing down the organization all together. This inability therefore leads us to consider how best the risk or loss can be minimized.

b)Minimization

- Since not all risks can be eliminated, the best alternative is to consider how best to minimize the risk or loss.
-

Pre-Loss Minimization.

- Here the effects of the loss are anticipated and steps taken to ensure that the frequency and/or severity of the loss are reduced to the minimum.
- Examples include use of safety belts in a car, use of protection guards on dangerous machinery and installation of extractor fans in a paint-spraying booth to minimize the risks of injury to health and fire damage.

Post-Loss Minimization.

- Where a loss has taken place, steps can still be taken to minimize the loss. 00Examples include installation of automatic sprinklers to minimize effects of fires and employment of salvage measures to safeguard property saved from burning buildings.

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Cont.

2)Financial Control of Risk

- The main methods here are:

a) Retention

- The best way to treat losses, which are predictable, is to retain them.
- The cost of these can be paid out of current income and charged as part of the cost of production.
- Alternatively, a separate fund could be set up to meet such losses.
- Such a fund is what is known as self-insurance. Others may opt to form captive insurance companies.

b) Transfer

- For unpredictable risks, the best way to deal with them is to transfer them to somebody else.
- The most common form of risk transfer is by way of **insurance**.
- It is advisable to transfer risks, which are catastrophic in nature i.e. risks of low frequency but high severity nature.
- High frequency, low severity risks should be retained.
- Lower levels of more serious losses should be retained by means of deductibles or captive insurance.

Personal Risks

Personal risks relate to an individual, for instance :

i. premature death,

ii. dependant old age,

iii. sickness or disability,

iv. unemployment, and

v. loss of one's property through fire or theft etc.

All of them have financial implications that are undesirable to the individuals.

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Business risks

- Business risks relate to the business firm.
- They include :

i. the factory burning down,

ii. stock being stolen,

iii. strikes hampering production, and

iv. death of a key person etc.

They, too, are undesirable to the firm.

Classification of risks

- Recall classification of risks in Unit 1(general classification and Insurable risks)
- **Note risks may be handled differently depending on how they have been classified.**
- Please note that classifications are **not conclusive.**
- A certain risk can assume characteristics failing under more than one category of risks.
  - For instance, loss of property by fire is an objective risk. In addition, it is financial. Static, particular and pure in nature.
  - Furthermore, it could be personal or business!

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Personal Risk Management

- The individual in his personal and domestic risk situation, or the small trader with his business interests, can follow similar techniques stated above.
- Flow charts check lists, etc; can be used to identify risks and professional advice sought on the best physical and financial tools to be used to handle them.
- It is important that a conscious effort is made to study and control the risks which face us daily.
- Large-scale retention of risk is unlikely to be financially acceptable, but much can be done to arrange a more satisfactory insurance Programme than would be the case without adopting such techniques.

Insurance company risks

- Insurance companies, like any other financial institutions, face several risks.
- While some risks are similar across the financial services sector others are unique to a particular industry of the financial sector.
- For instance risks of strategy and legal and regulatory may be similar,
- The insurance risks are unique to insurance companies considering the nature of their business.
- The following is a list of major and significant risks that an insurance company faces.
- Note the list does not provide exhaustively the other minor risks an insurance company may be exposed to.

List of risks

1. Insurance risk;
2. Operational risk;
3. Liquidity risk;
4. Strategic risk;
5. Balance sheet and market risk;
6. Legal and regulatory risk.

- **Insurance risks:**
  - Insurance business operates on pooling risks of for different classes of business.
- **Operational risk**
  - When operating a company, there is need to provide the necessary systems, infrastructure, policies that will drive the company.
  - Also important to consider is the element of human capital.

- **Liquidity risk**
  - Cash management in the company
  - The significant functions of financial management.

- **Strategic risk**
  - Risks associated with long term and short term plans of the company.

- **Balance sheet and market risk;**
  - Balance sheet risk arises when the balance sheet prepared overstates values and hence the financial strength of the organisation is not as advised
- **Legal and regulatory risk.**
  - These are risks relate to litigation. There are chances of a firm being taken to court as a result of its operations.eg in case of a disputes which may end up in litigation. Such litigations may be costly and time consuming. This could give rise to legal action.
  - Risks of not complying with regulator either directly by officers of the company or indirectly by agents may lead to fines, penalties and worse still closure of a firm.

Risk exposures Common in Financial Institutions (FI)

- Financial institutions due to their special role of intermediation are faced with a uncountable risks which are mostly financial in nature.
- These include

i. Interest rate risks,
ii. Credit risk,
iii. Market risks,
iv. Foreign exchange risks,
v. Off-balance sheet risks,
vi. Liquidity risks,
vii. Technology and
viii. Other operational risks.

Cost of neglect of Risk management

Death and injury

↓

Loss of physical valuables

↓

Loss of intellectual assets

↓

Loss of reputation, confidence and destruction of brand value

↓

Inappropriate insurance protection

QUESTIONS

INSURANCE REGULATORY

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DIP 101 UNIT-7 SURPERVISION

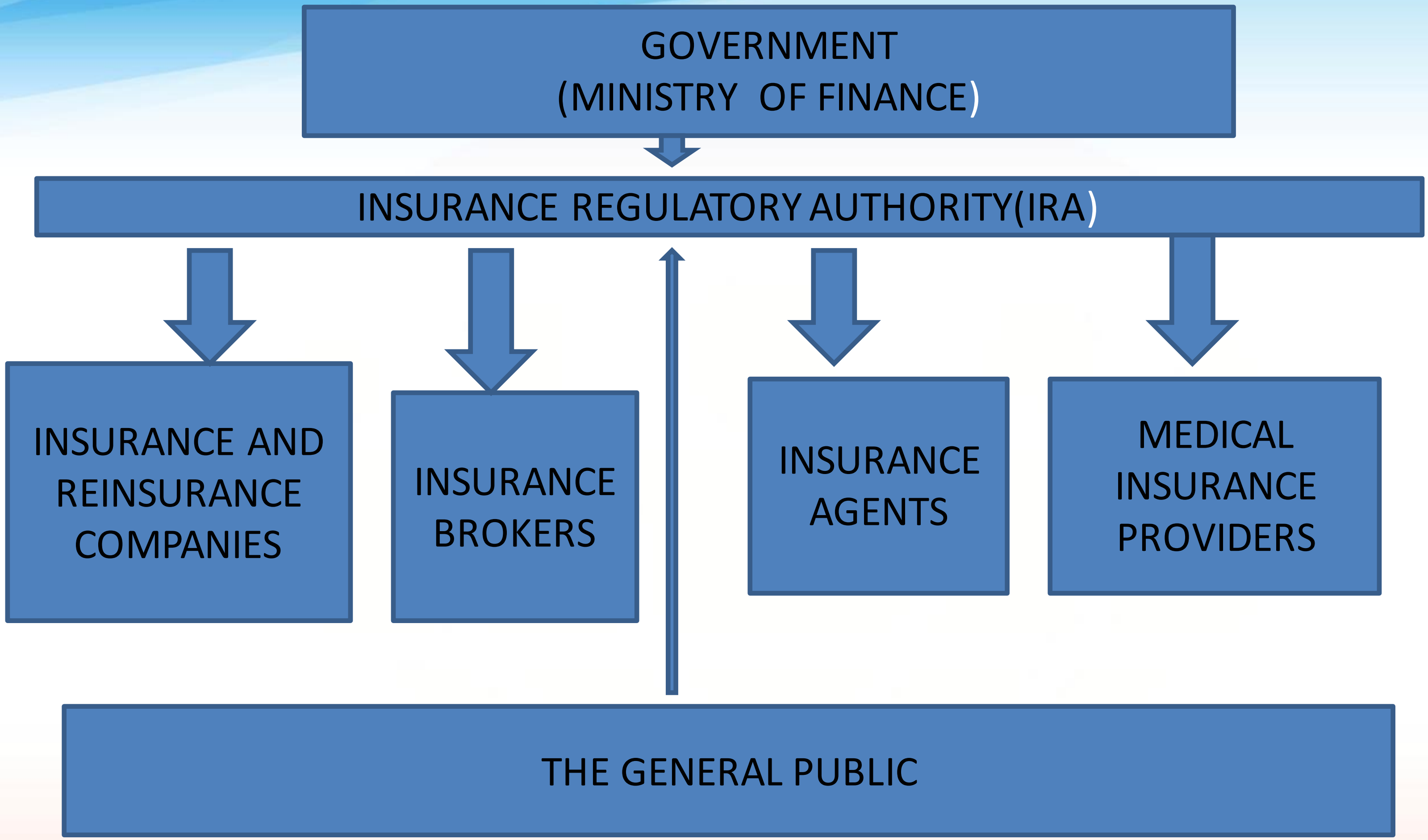
The Role of the IRA in Insurance Regulation, Supervision and Development in Kenya

- The initials IRA stands for the Insurance Regulatory Authority.
- The IRA is an autonomous government institution created through an Act of Parliament in 2006 and became effective on 1st May 2007.
- It took over the functions of the former Department of Insurance of The Ministry of Finance.

- The IRA is financed by a levy on insurance premium.
- It is also mandated to collect fees from the regulated members of the industry.
- The IRA has been able to recruit and retain more qualified technical staff to discharge it’s mandate.

- The IRAs mandate is to regulate, supervise and develop the insurance industry in Kenya.
- It is governed by the Board of Directors who are responsible of overseeing the running of the Authority.
- It is run on day to day basis by the Commissioner of Insurance, who is also the Chief Executive Officer of the Authority.

Structure of insurance supervision



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Functions of the IRA

The key functions of the IRA are to:

- Ensure effective regulation, supervision, and development of insurance in Kenya;
- Formulate and enforce standards of conduct of insurance business;
- Issue licences to qualified persons;
- Protect the interests of insurance policyholders and insurance beneficiaries;

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- Promote the development of the insurance sector in Kenya;
- Ensure prompt settlement of claims by insurers;
- Investigate and prosecute insurance fraud;
- Improve efficiency in handling of complaints against members of the insurance industry by the insuring public.

How the IRA Regulates and Supervises the Insurance Industry

The IRA regulates and supervises the insurance industry by:

- Ensuring compliance with the Provisions of the Insurance Act, Cap 487 of the Laws of Kenya;
- Licensing of insurers, insurance brokers, agents and service providers in respect of the requirements of each category as required by the insurance Act;

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- Ensuring that all members of the insurance industry conduct their business ethically and in accordance with the provision of the insurance Act.
- Approving all insurance products/policies before they are launched for sale by insurance companies.

Reasons Why the Insurance Industry is Regulated and Supervised

1. Business of Trust

- Insurance involves taking money from members of the public, who thereby become policyholders, in return for promise of payment on the occurrence of some future event or, in the case of life assurance, at some future date.
- If there was no mechanism in place to check this kind of system, then some persons might be tempted to collect premiums and divert them without bothering to honour their promises.
- This would make the public lose faith and develop a negative perception of the insurance industry.

2. Need to Maintain Financial Stability

- As an insurance company is required to pay claims in the future, there is need to preserve long-term financial stability of an insurer i.e. to ensure that the insurer will be in a financially sound position to pay claims when the loss occurs.
- This is more so in life business where, for example, claims could become payable many years after the date of the contract.
- This is done by continuously monitoring capital adequacy and solvency levels of an insurer.

3. Maintain Solvency

- This relates to the assets and liabilities of a company.
- The Insurance Act requires that the margins between assets and liabilities of an insurer remain positive within the prescribed ratio to ensure that the company is able to pay claims as they occur.

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4.Fair treatment of customers

- The IRA ensures that insurance related complaints are well addressed.
- It also regulates the insurance industry so that customers are fairly treated.
- It has a Consumer Protection Department where policyholders and others who might be dissatisfied with the way claims are handled can forward their complaints.
- IRA does its best to try and sort out such issues.

5. Fairness among the market players

- IRA has a duty to ensure that all market players conduct their business in accordance with the provisions of the insurance Act.
- It also has the mandate to ensure that companies operate ethically.

- **To achieve these objectives, IRA ensures following is not practiced by the industry players:**
  - Delayed claim settlement;
  - Non payment of taxes and levies;
  - Not keeping proper records of business transactions;
  - Charging of uneconomical premiums; and
  - Rejecting claims which fall within the provisions of the policy.

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6. Competence

- Unlike physical products, insurance is an intangible product because it only offers a promise of payment in exchange of payment of premium.
- The IRA objective is to ensure that those who are employed by members of the insurance industry are competent, fit and proper persons and are able to fulfill the pledges made.

7. Registration of Insurance Industry Members

- As already noted, one of the main duties of the IRA is to license members of the insurance industry.
- They are only licensed after meeting certain requirement prescribed in the Insurance Act.
- Registration is renewed every year.
- The players who can be licensed and the requirements of registration for each type are now briefly described.

Registration of a new Insurance Companies

- To be licensed as an insurance company, the applicant:
- Must be a company incorporated under the Companies Act;
- One third share holding and at least one third of directorship must be held by citizens of EAC member states;
- Must submit an application form in the prescribed format;
- Should pay the appropriate registration fee;
- Should submit Articles and Memorandum of Association;
- Must have subscribed the minimum paid-up capital;

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- Should submit the Curriculum Vitae of the proposed principal officer, directors and top management staff;
- Need to provide the name of the proposed auditors, lawyers and actuaries where applicable;
- Should provide policy specimen of all the classes of business they intend to transact;

- Must submit manuals for premium rates they intend to use;
- Should provide details of their reinsurance arrangements;
- Should give evidence of deposits with the Central Bank, as required by the Insurance Act;
- Should submit proposed contractual documents to be signed with agents and brokers; and
- Should provide a statement of how the company intends to cover its initial costs.

Insurance Broker/Medical Insurance Provider

- Before being registered as a broker or medical insurance provider, an applicant should meet the following requirements:
- Submit an application in the prescribed format;
- Pay the appropriate registration fee;
- Be a company incorporated under the Companies Act;
- Obtain a bank guarantee from a commercial bank or a deposit with the Central Bank of Kenya as prescribed by the Insurance Act;
- Have a at least 60 per cent of its shares held by citizens of EAC member states;
- Have a minimum paid up capital ;
- Have a technically qualified Principal officer;
- Have a Professional Indemnity policy as prescribed by the Insurance Act.

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Requirement for Registration of an Insurance Agent

To be registered as an insurance agent, one must fulfill the following requirements:

- Complete an application form which is in a prescribed format;
- Pay the applicable registration fee;
- Submit statements of business form from the principals for whom the agent transacts business;
- Provide a certificate by insurer in the prescribed form;

- Be a Citizen of an EAC Member state or a Company whose shareholders are Citizens of EAC Members states;
- Pass or be exempted from Certificate of Proficiency(COP) examination or Executive Certificate of Proficiency (ECOP);
- Submit a certificate of registration of business name when such a name is proposed to be used;
- Submit annual audited accounts in case of corporate agents.

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Service Providers

- There are requirements for registration of the various categories of service providers in the insurance industry such as loss adjusters, risk surveyors, motor assessors, claim settling agents and investigators.

The key ones are:

- Must be qualified for the category of the service provider that they seek to be registered,
- pay the registration fee
- Should not have been involved in any unethical behavior(certificate of good conduct)

Steps Taken by the IRA to Enhance the Growth of the Insurance Industry in Kenya

1. **Consumer Education**

- The IRA conducts consumer education campaigns to create awareness among members of the public about risk and insurance.
- The objective of these public education campaigns is to inform the public on the benefits of insurance and the importance of risk management.
- The aim is to make the public appreciate the role of insurance in their lives.

- At the moment, the number of people with insurance policies of any type in Kenya is very low.
- It is expected that it will gradually increase by the year 2030.
- The campaigns are also aimed at reversing the negative perceptions Kenyans have towards insurance.
- The insurance profession will also become more attractive to many young Kenyans.

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2. The Policyholders Compensation Fund (PHCF)

- The Policyholders Compensation Fund (PHCF) was established in 2004 under the Insurance Act.
- The purpose of the Fund is to compensate policyholders in the event of collapse of an insurance company due to insolvency.
- Its broad object in to create confidence in the insurance industry by guaranteeing the public that even if an insurance company collapses, their claims will still be settled.
- It is funded by a levy payable by both the insurers and policyholders.
- The level of compensation to policyholders is determined by the board of trustees of the fund.

3. Insurance Fraud Investigation Unit (IFIU)

- Insurance fraud is deeply rooted and involves unethical lawyers-sometimes called ‘ambulance chasers’-, police officers, doctors, motor vehicle garages, employees of insurers and many other participants.
- Fraud increases the cost of insurance (premium) because ultimately, the cost of fake claims has to be financed somehow.

Cont'd

- The IRA has therefore established the IFIU.
- This is because the incidences of fraudulent claims are quite frequent in the insurance industry.
- The role of the IFIU is to investigate and prosecute persons perpetuating fraudulent activities in the insurance industry.
- The Unit is manned by highly trained Police officers.

4. Training of Traffic Police Officers

- Motor accidents account for a high percentage of claims paid by general insurance companies.
- Accidents occur on roads and traffic police officers can play a significant role in controlling them.
- Traffic police officers can also help insurers (or their agents) while gathering information about motor vehicle accidents as they are the first to arrive at accident scenes.

- Training of traffic police officers in motor insurance claims is therefore important and the IRA has undertaken this responsibility.
- The IRA aims at training traffic police officers on how to handle motor insurance cases and what they need to look for while on the road.

5. Training of Insurance Agents

- The IRA has commenced training of insurance agents in the country.
- It aims at training agents in each of the 47 Counties.
- The broad objective of this exercise is to increase the number of insurance salespersons so as to enhance the availability of insurance services to the Kenyan people.

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- It is also a way of creating employment for Kenyans and involving Kenyans in the development of the insurance industry and the economy at large.
- Agents serve prospective clients directly in insurance sales.
- They can also educate the people about insurance in their local languages.
- The objective of the IRA is to have insurance salespersons among all the communities and regions of the country-hence the training.

Why does the IRA undertake all These Measures?

- Ensure availability of insurance services throughout the country
- Ensure that all players in the insurance industry conduct their businesses ethically and that companies settles all payable claims promptly;
- Protect the interest of policyholders, their beneficiaries and the general public;
- Ensure that financial stability exists in the insurance industry;

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- Ensure that ordinary people understand insurance policies and are able to make informed choices when buying insurance;
- Ensure that incidences of fraud are reduced within the insurance industry as this would reduce the overall level of claims and may, in the long run, lead to reduced premiums;
- Enhance confidence in the insurance industry;
- Guarantee that Kenyans and their assets are well secured through insurance.

Other Regulatory Authorities in the Financial Sector

- There are several players in the Kenya financial sector. These include retirement benefits, banks, capital markets and SACCOs.
- To maintain the degree of trust, there are several regulatory authorities. Among these are:

1. **Retirement Benefits Authority (RBA)-**This supervises the retirement benefit sector.
2. **The Central Bank of Kenya (CBK)-**The CBK regulates banks, building societies, non- bank financial institutions and micro finance institutions.

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Cont'd

3. The Capital Markets Authority (CMA)

- This regulates the securities exchanges, custodians, the investment banks, stockbrokers, listed companies, etc.

4. The SACCO Societies Regulator Authority (SASRA)

- This is a state corporation which regulates cooperative societies.

MAIN AREAS FOR SURPERVISION AS PER THE INSURANCE ACT

- VALUATION
- RESERVES
- SOLVENCY
- COMMISSIONS
- RATES
- POLICY CONTRACTS
- LOST POLICIES
- CLAIMS PAYMENTS
- INVESTMENTS
- INSOVENCY AND WINDING UP

IRA Guideline on valuation

"set of principles for the consistent measurement and reporting of the insurance liabilities of all general insurers"

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Key Requirements on valuation

- Statement from the Appointed Actuary on the valuation
- Insurance liabilities include Claims Reserves, and Premiums Reserves
- Ultimate responsibility of the Board

Reserves

- Provisions set aside by an insurer to meet liabilities arising out of insurance contracts
- **Types of reserves**

Claims Reserves

Premium reserves

Contingency reserves

1:Claims Reserves

a.Outstanding claims incurred and reported

- Claims incurred prior to the calculation date, which have been reported and not yet settled

b. IBNR

- incurred but not yet reported

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a.Outstanding claims

- Reserves in respect of outstanding claims incurred and reported shall be determined prudently by using
  - *Case Estimate Method,*
  - *Average Cost per Claim Method*
  - *or other methods recognized by the Authority*

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b.IBNR

- Reserves in respect of incurred but not reported claims shall be valued and determined;
  - *prudently by using* ***at least two methods***
  - *Method to consider the* ***risk nature, risk distribution and experiential data*** *of the insurance lines*

2:Premium Reserves

UPR

(Unearned Premium Reserve)

- Portion of ***premium that has been paid in advance*** for insurance that has not yet been provided
- Caters for any premium refund in the event that a contract is terminated during the policy yea

URR

Unexpired Risk Reserves

- Portion set aside in order to provide for the ***claims and expenses which will emerge from unexpired risks*** and which is over and above the Unearned Premium Reserve

a.UPR (Unearned premium reserve)

- Requirement to determine and disclose a value for its UPR for each class of business.
- Test the adequacy of the reserves
- Method used to determine the UPR should be consistent i.e. not be changed arbitrarily

b.URR(Unexpired Risk Reserve)

- Determined by estimating the difference between the Claims Expected to be incurred after the Valuation Date on policies with Unexpired Exposure Periods compared to the established reserves for unearned premiums

- Requirement to determine and disclose a value for its UPR for each class of business

3:Contingency reserves

Reserve to deal with unknown risks and accepted known risks.

It is used as a buffer for dealing with unidentified risks

a:Catastrophe Reserve

b:Claim Equalization Reserve

Why hold reserves?

- Timing of premiums receipt and claims payment does not coincide
- Delay between claim event and the claim settlement dates
- For the insurer to be able to quantify its liability if it is to assess its financial position correctly
- Assessment of solvency and profitability
- Modern societies are becoming increasingly litigious leading to increase in number and cost of new claims

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3.SOLVENCY

- Demonstrates **financial strength** of an insurer/ institution
- Solvent businesses have enough **assets** to cover their **liabilities**
- Demonstrates **reliability/ability** of an insurer to **pay claims** as they fall due
- Associated with **credit rating/ low risk of default**
- Promotes **confidence**

RISK BASED CAPITAL

- An insurance company must have **adequate capital** to provide a **cushion** for **above** average losses beyond the coverage of policy reserves.

- The calculation of the **RBC** takes into account the relative **risk** contained within the insurance company's balance sheet

- The **RBC** quantifies the minimum amount of **capital** that an insurance company must **hold**.

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MOTIVATION FOR RISK BASED CAPITAL

- Improve risk & capital management and the need to be pro active
- More sensitive to risk
- Improve credit rating
- Improved public confidence
- Provide better cushion for above average losses beyond the coverage of policy reserve
- Timely intervention by regulator

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DRIVERS OF RBC

- Lines of insurance business transacted
- Assets invested in
- Diversification i.e. products/business lines, assets invested in,…
- Perceived/actual risks associated with various assets and insurance business lines
- Rating of Reinsurers
- Catastrophe charge

CHALLENGES

- Lack of consistent valuation methods of assets & liabilities
- Lack of adequate and complete data
- Challenges of accessing additional capital
- Poor or inadequate investment strategies
- Availability of variety investment channels
- Changes in Macro economic factors
- Shortage of resources e.g. Actuaries, ICT,…

3. Investment of Assets

- **Section 50** of the Act provides that the assets of an insurer shall be invested in Kenya with sufficient regard to consideration of security, liquidity, and income.
- Investments in unsuitable areas are not recognized as assets under the Act.
- An insurer may not invest its assets with any other insurer.
- The Act has specified guidelines on areas where an insurer may invest it s assets. Below is a brief summary on the same.

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Long term insurance business

- Twenty per cent of the assets must be invested in:
  - Government securities;
  - Prescribed statutory bodies; or
  - Local authorities;
  - Any other prescribed organization;

A further proportion amounting to not less than 65 per cent shall be invested in:

- Any of the area specified above;
- Mortgages or unencumbered immovable property in Kenya;
- Debenture, preference shares or ordinary shares of public companies whose shares are quoted on the Stock Exchange in Kenya;
- Instrument of title to immovable property in Kenya.

- The balance may be invested in Kenya as the insurer may deem
- appropriate.

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General Insurance business

The assets of general insurance companies shall be invested as follows

- Ten per cent in either of the following areas:
- Government securities;
- Prescribed statutory bodies;
- Any other prescribed organization.

At least 30 per cent in:

- The areas specified above;
- Mortgage on unencumbered immovable property in Kenya;
- Preference or ordinary shares of public companies whose shares are quoted in the Stock Exchange;
- Deposits in financial institutions licensed under the Banking Act.
- The balance in such investments as the company may deem appropriate.

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- Further, the Act specifies the maximum deposit that an insurer can hold in any one bank as 10% of its deposits for general insurance companies and 5% for life insurance companies.
- It also provides that the maximum investment a company can have with any one company or group of companies is 5% for long term business and 10% for general business.

4. Management and Expenses

Management

- **Section 68** provides that every registered person shall at all times while registered have a principal officer who shall be resident in Kenya and be responsible for the general control, direction and supervision of the Kenyan business and shall represent the registered person for the purposes of the Act.
- The principal officer shall be “fit and proper”. This is determined by taking into account the following particulars of the Principal Officer:
  - Work experience;
  - Academic and professional qualifications;
  - Whether the principal officer has ever been adjudicated bankrupt.

4. 2. Expenses

- Supervisory authorities have to monitor the company's expenses of management.
- These include:
  - salaries,
  - traveling expenses,
  - contribution to staff programs,
  - various fees, rent, and the like.
- The aim is to avoid over-expenditure on these items to the detriment of claim payment which is really what concern the insured in particular and the public in general.
- Towards this end, Section 70 of the Act provide for maximum permitted expenses which are fixed depending on the company's gross premium.

In general insurance business for example, the maximum permitted expenses are

- 25% of the first five million shillings of the gross direct premium;
- Twenty two and a half percent of the next 7.5 million;
- 20% of the next 7.5 million;
- Seventeen and a half percent of the next 10 million; and
- Fifteen percent of the balance

5. Commissions Payment

- A critical component of the management expenses is the commission payable to intermediaries who introduce business to the company.
- To avoid excessive expenditure on this item, the Act prescribes the maximum agency commissions payable for each class of business.
- For example, the maximum commission payable for liability and personal accident insurances is 20 per cent of the premium while that of motor is 10 per cent.

- In ordinary life, the maximum commission payable is 50 per cent of the first year premium, 20 per cent of the second year and 5 per cent of the 3^{rd} to 10^{th} year premiums.
- It must be emphasized, however, that the Act only prescribes maximum commission rates; a company is therefore free to pay any commission rate below the prescribed amounts.

6. Rates, Policy Terms and Claims Settlement

1. Premium Rates

- The Act prohibits insurers from charging premium other than in accordance with Section 75 of the Act.
- **The aim of this provision is to ensure that the premiums charged are fair and equitable.**
- It provides for different methods of rating in general and life businesses.

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Life Premium rates

- Life insurance premium rates are prepared by **an actuary.**
- The rate and the actuarial bases, together with the actuary's certificate should be filed with the IRA at least 30 days before their taking effect.
- The insurer cannot vary the actuarial rates without the permission of the IRA.

Premium Rates for General Insurers

- The insurer shall **file a schedule or manual of rates** of premium proposed to be used for each class of business.
- Should they desire to change the schedule or the manual of rates already filed with the IRA, they will, before effecting the alteration, file the revised schedule or manual and the reasons for the change at least 60 days before effecting the revision.
- The IRA may require the insurer to file the statistical data and other information on the basis of which any revision is based.
- They may also require the insurer at any time to modify or revise such rating manuals or schedules.

7. Law applicable to Contract of Insurance and Places of Payment

- **Section 76** provides that notwithstanding any agreement to the contrary, a holder of an insurance policy issued by an insurer in respect of an insurance business carried on by him in Kenya has a right to receive payment of any sum secured by the policy in Kenya and to sue for any relief in respect of the policy in Kenya, and any question of law in connection with the policy or proceedings shall be heard in and determined in accordance to the law in force in Kenya.

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6. Amounts and values in policies to be expressed in Kenya Shillings

- Any amounts and values in policies and other insurance documents, unless expressly otherwise agreed, or the IRA has in writing approved, shall be in Kenya shillings except for marine and aviation policies.

7. Payment of Premiums

- A risk only attaches to the insurance company when the full premium has been paid by the proposer, broker or the agent. The purpose of this stipulation is to ensure that the company has the resources necessary to pay claims as they fall due.

8. Inaccurate or Misleading Statements

- Section 80 of the Act stipulates that insurance proposal forms and policy documents or any form of written matter from an insurer describing the terms or conditions of or the benefits likely to be deprived from a policy shall not contain anything inaccurate or incomplete or likely to mislead a proposer of a policy.

8; Premium taxes / Training levy

1. Monthly Premium Tax

- Premium tax is charged and levied on gross direct premiums written by all insurers registered or authorized under the Insurance Act to carry on insurance business in Kenya.
- The tax is computed as a percentage of the gross direct premiums written by an insurer at a rate of 1.5%.
- At the end of each calendar month, an insurer shall prepare, in accordance with the prescribed form, a monthly premium tax showing the total premium tax due from the insurer for that particular month.
- The tax is payable at the end of each month in which the premium was received by the insurer and is payable by such an insurer not later than the last day of the first month succeeding that in which the tax becomes due.

2. Insurance Training Levy

- This levy is collected by the IRA on behalf of the 'Insurance Training and Education Trust'.
- The levy is imposed on the gross direct premiums written on general business by every insurer, at a rate of 0.20 per cent, which is charged on the policyholders and collected by the insurer.

10. Statutory Provisions Relating to Insurance Contracts

- This section will briefly discuss the main provisions of the Insurance Act which regulates policies and insurance documents.

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9. 1. Incorrect statements in the proposal forms

- **Section 81** of the Act provides that a life policy shall not be avoided just because of an incorrect statement in the proposal or other policy documents on the faith of which the policy was issued or reinstated by the insurer unless the statement was material to the insurer and: Was made in the knowledge that it was untrue or with no reasonable belief that it was true;
- Was made within a period of three years immediately preceding the date on which the policy is sought to be avoided or the date of the death of the life assured whichever is the earlier;

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- Where the agent or servant of the insurer writes or fill the proposal or has written or filled in particulars in the proposal form, then a life assurance policy issued in pursuance of such a proposal
- Shall not be avoided by reason only that an incorrect or untrue statement contained in the particulars
- Written or filled was incorrect unless the incorrect statement was in fact made by the proposer to the agent or servant for the purposes of the proposal and
- The burden of proving that statement was so made shall be upon the insurer.

9. 2. Effect of suicide or capital punishment on a life policy

- The Act provides that a life policy shall not be avoided merely on the grounds that the person whose life is assured died by his own hand or act, sane or insane, or suffered capital punishment, if, upon the true construction of the policy, the insurer had thereby agreed to pay the sum assured in the events that have happened.

- This provision lead to the introduction of the suicide clause in the life policies which provides that if death occur by suicide, the claim is payable if the death occurs within one or two years from the commencement date of the policy.

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Cont.

9.3. Particulars as to Age of the Proposer

Section 83 of the Act stipulates that a proposal of life assurance shall be framed so as to require a person making a proposal to specify the place and date of birth of the person whose life is proposed to be assured, and the person making the proposal shall supply the information to the best of their knowledge and belief.

9. 4. Notice Regarding Proof of Age

- **Section 84** of the Act provides that where an insurer issues a policy of life assurance which provides that proof of age of the life insured is a condition precedent to the payment of the sum assured, the insurer shall, unless the age of the life assured has already been admitted by it, issue with the policy a printed notice stating that proof of age of the life assured may be required prior to the payment of the sum assured.

10. Lost Policies

- **Section 106** of the Act provides that where the insured person claims that the policy is lost or has been destroyed, the insurer, upon application and having been furnished with sufficient evidence of loss or destruction shall issue a special policy in substitution of the original policy.
- A special policy shall:
- Be a copy, as nearly as can be ascertained of the original policy issued;
- Contain copies of endorsement on the original policy registered by the insurer;
- State the reason for the issue of the special policy.

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- Any discharge of a policy given to the insurer by the transferee shall be valid, notwithstanding the existence of any trust, right, equity or interest of any other person;

- The insurer shall not be required to concern, inquire or ascertain the circumstances in which or the consideration for which the transferee or any person previous transferee became a transferee or the moneys so paid.

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11. Claim Payment

- **Section 203 of the Act provides that an insurance company shall settle claims arising out of the policies it has issued with 60 days on:**
  - Admission of liability;
  - Agreement on quantum;
  - Identification of the claimant.

- Amendments have recently been introduced to strength claim settlement. Among these are the provisions that:

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- Where liability of an insurer is determined by the court, settlement of the claim must be effected within **30 days**;
- This amendment s contained in the 2016/2017 Budget

- Where the amount of such a claim remains unpaid on expiry of such period or any extension thereof, a penalty equal to 5% of the claim shall forthwith become due;
- If the insurer fails to pay the claim and any penalty thereon due, the insurer shall be deemed to be unable to pay its debt and be liable to be put under receivership.

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12. Claims on Small Life Policies

- In the event of a dispute relating to the settlement of a claim on a policy of life assurance assuring a sum not exceeding one hundred thousand shillings (exclusive of any profit bonus) arising between a claimant under the policy and the assurer who issued the policy or has otherwise assumed liability in respect thereof,
- The dispute may at the option of the claimant, be referred to the IRA for decision.
- The IRA may, after giving the parties an opportunity to be heard and after making such further enquiries as they may think fit, decide on the matter.
- The decision of the IRA shall be final and shall not be called in question in any court, and may be implemented by the High Court as if it were a decree passed by that court.

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13. Other Statutory Provision Relating to Insurance Companies

14. 1. Calling for Information

- **Section 7(1)** equips the supervisory authority with powers to call for information on insurance business from a member of the insurance industry. Hence under this provision, the authority can access insurance correspondence used by the company and check whether the company transacted business in accordance with the provisions of the Act and sound insurance principles and practices.

14. 2. Failure to Comply

- If supervisory authorities form the opinion that a certain player is unable or unwilling to comply with the stipulations of the Act, then several remedial measures can be taken

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Examples of such measures are:

1. Restructuring management and the board;
2. Providing for more frequent reporting;
3. Demanding that shareholders increase the paid up capital. The Insurance Act; Section 25(1) has been amended to allow investors to inject other forms of capital other than ordinary shares
4. Putting the company under statutory management.

14. Insolvency and Winding Up

- An insurer carrying on long term business shall not be wound up voluntarily.
- The Act provides that where a petition for the winding up is presented by a person other than the IRA, a copy of the petition shall be served to the IRA and they shall be entitled to be heard on the petition.
- An application for winding up of an insurer may be based on the following grounds:

The insurer is insolvent if:

1. The insurer has been found guilty of an offense of carrying on business without registration;
2. In the case of a new insurer, they have not issued a new policy for a period of 12 month and IRA considers that the continuation in the business of the insurer is likely to lead to insolvency, or is otherwise contrary to the interest of the policy holders;
3. On the grounds that the insurer is unable to pay its debts within the meaning of the Companies Act;
4. If IRA determines that the insurer is unable to fulfill the reasonable expectations of policyholders or potential policyholders;
5. That it is just and equitable in the interest of the policyholders that the insurer be wound up.

Q&A

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Unit - 8

SOCIAL INSURANCE

Unit; 8

- Introduction
- The National Social Security Fund (NSSF)
- The National Hospital Insurance Fund (NHIF)
- Nationalization.

CONTENT

- Nature of Social insurance
- Administrative structure of NHIF
- Membership of the fund and their benefit
- Nationalization.

Introduction

- National insurance is the insurance that is provided by the government or one which the government has made compulsory for all citizens or at least a well defined segment of the population.
- Its overriding objective is to provide a benefit to the target group.
- Commercial insurance, on the other hand, is the insurance practiced by the private sector and is profit driven.

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The purpose of Compulsory Insurance

- The government would like to ensure that some funds are available to assist the victim when incidents which may cause injuries or personal incapacity occur;
- The availability of funds to cater for the injured and the aged eases the state burden and the social pressure for the government to offer some assistance;
- Most of the compulsory Insurance is in areas which tend to concern the public such as health and old age. This is the reason why the government feels compelled to arrange some form of compulsory Insurance;
- It can also be argued that by making insurance compulsory the insured is availed of all the expertise of the insurer in loss prevention.

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Nationalization

- Nationalization is the compulsory acquisition of private property by the government.
- It is a central believe and practice of communist regimes and has therefore fallen out of favor since the collapse of communism in the early 1990s
- However, when most African countries became independent in the early 1960s, this philosophy was very much in favour.
- In the East Africa region, Tanzania took this route following the Arusha Declaration of 1967 and only agreed to license private insurers in the late 1990s.
-

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Advantages

- Government control of funds would be to the benefit of the society at large;
- It would be possible to introduce some element of uniformity in the wording of Insurance policies and other documents;
- The government could be able to offer more competitive premium rate as it is not profit driven;
- The cost incurred in setting up supervision mechanisms would be eliminated;
- As the government has more resources the need to reinsure would be eliminated. This would result in saving of foreign currency outflow and is especially beneficial to countries with local reinsurance companies;
- The government would be in a better position to offer most forms of compulsory Insurance

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Disadvantages

- It is difficult to nationalize the business of Insurance because of its international nature. Reinsurance is always required and many private companies would be reluctant to trade with a government owned Insurance sector;
- Insurance has grown and developed in private hands for many centuries and there is no reason to believe that the government can offer a better system;
- Experience of the nationalized companies in many developing countries is one of inefficiency, red tape, lack of innovation and overloaded bureaucracy;
- Lack of competition encourages inefficiency;
- The current taxes paid by the private Insurance industry would be lost in the event of nationalization;
- No government has the required experience in underwriting of insurable risks;
- The large scale nature of any state corporation would lead to rigidity in practice and strictness in interpretation of various provisions and this would not be beneficial to the public.

NHIF. The National Hospital Insurance Fund

- The NHIF was established by an Act of Parliament (of similar name) **in 1966.**
- It is a state parastatal established as a department under the **Ministry of Health.**
- The original Act of Parliament that set up the Fund has over the years been reviewed to accommodate the changing healthcare needs of the Kenyan population and restructuring in the health sector.
- **It is a state medical insurance scheme.**

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Main Function

- NHIF's core function is to collect contributions from all Kenyans earning an income of over Ksh 1000 and pay hospital benefits out of the contributions to members and their declared dependants (spouse and children).

Membership

- It is compulsory for all employees earning more than Kshs. 1000 and over the age of 18 to become members of the Fund.
- The Act requires employers to deduct the mandatory contribution from an employee's salary before payment and then forward the same to the NHIF.

- Under the **NHIF Act No. 9 of 1998** which replaced the **1966 Act**, besides those who are compulsory members, any person interested in becoming a member is free to do so.
- Those who join like this are **voluntary members**.
- This gives a chance to members of self help groups, small scale farmers, traders, the retired, the retrenched and the self employed artisans to access benefits of the Fund regardless of age.
- **The scheme operates under the social principle that 'the rich should support the poor, the healthy should support the sick and the young should support the old'**

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- It has a mandate to enable all Kenyans access quality and affordable healthcare services.
- Has braches in major towns across the country which offers all services.

Contributions

- Contribution is on an ascending scale depending on one's salary.

As fromApril 2015;

  - Those earning Kshs 5999 and below contribute Kshs 150 per month
  - Those earning kshs 100,000 and above contribute Kshs 1700 per month
  - The self employed pay Kshs 500 per month

- By end of 2015 the fund had 5.7 million members and serving 51,000 employers

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Benefits

As already noted, Members of NHIF includes

- employees,
- their spouses and children
- dependent children.
- Voluntary members are also covered.

The Fund pays(Costs) for

- hospitalization expenses including those of the HIV positive persons,
- the elderly,
- those in informal employment,
- Chronicle illness eg diabetics,
- maternity expenses, and heart patients.

In other words, all medical expense is included

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- Payments are made for a maximum of 180 days of hospitalization.
- Claims are submitted by hospitals directly to NHIF after the contributors have been discharged from the hospitals.
- The claims are examined by the Fund to ensure validity before payment.
- A claim can, however, be rejected and the hospital informed accordingly to incorporate either the missing documents or to address the abnormalities identified.
- The Fund strives to pay claims within 14 days upon receipt of the claim from the hospitals.

- Members who opt to clear the bills with the hospital may launch a general claim directly to NHIF for reimbursement.
- However, the fund now cater for in-patient and out- patient treatment.
- It offers **three forms** of in-patient treatment payments as follows:

i. **Contract A**

ii. **Contract B**

iii. **Contract C**

Contract A

- This provides a comprehensive medical scheme, which includes surgical and maternity expenses.
- It applies in all government hospitals.

Contract B

- This applies in hospitals in which NHIF has an agreement with.

It covers medical expenses but excludes surgical charges.

Contract C

- This applies to high cost private hospitals where the NHIF pays an agreed amount per day on admission to a recognized hospital for a maximum of 180 days.

Out –patient cover

This covers

- General consultations
- Diagnostic and treatment of common ailments
- Laboratory and investigation charges
- Dental services
- Prescribed drugs administration and dispensing
- HIV/AIDS,diabetes,asthma,hypertension and cancer management
- health care counselling
- Radiology
- Family planning
- etc

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In- Patient treatment

This covers

- Consultation
- Hospital charges
- Nursing charges
- Laboratory charges
- Doctors charges
- Prescribed drugs
- Dressing charges

Payment is made for a maximum of 180 days of hospitalization. Claims are submitted by hospital directly to the NHIF after the contributors have been discharged from the hospital.

Other Contributions Health

- The NHIF supports hospital financially and through **donations** wherever it resources allows.
- Investing in hospitals is meant to improve services for contributors who use the services.
- The most common donations are **ambulances to public and mission hospitals.**

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Challenges and Shortcomings

- Contributions are based on salary while benefits are the same for all contributors;
- The fund does not cater for outpatient medical costs under their Contract C which, in some cases, may proof to be even more challenging to a member;
- Benefit payable under contract C are not adequate to cater for medical treatment in many private hospital in Kenya;

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- The NHIF has suffered many losses due to wrong investment decisions and fraudulent claims most of them made by claimants working in cohort with hospitals and sometimes even the fund’s employees;

- The level of service accorded to members in many government hospitals leaves a lot to be desired as the hospitals are ill stocked with drugs and more often than not are under-staffed.

- The fund current membership is about 1.5 million people. This is a very low number as it potential is estimated to be over four million people. There are therefore efforts being made to widen the membership of the Fund;

- Claims can only be entertained in hospital that the NHIF has a agreement with. At the moment, there are approximately 400 such hospitals spread through out the country.

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D. Civil Service Pension Scheme

- The Pensions Act (cap 189) was enacted to provide for the grant and regulation of pensions, gratuities and other allowances in respect of public service officers under the Government of Kenya.
- Section 3 empowers the relevant government ministry to grant pension in accordance with the pension Regulations under the Act, to officers who have been in the service of the Government.

- Employees of the government who qualify are paid a pension after retirement for the rest of their lives.
- This scheme is not funded and, therefore, the pension is paid from the **Consolidated Fund** i.e. it operates on **pay- as- you- go- bases.**
- The main group of persons to whom the Pension's Act does not apply includes employees on non-pensionable contract terms or employees in government institution declared as public service but covered by their own separate pension schemes.
- Therefore it is apparent that some public officers, depending on their terms of employment are not covered by the scheme.

- The civil service pension scheme has about **450,000** members and accounts for **approximately 22 per cent** of the retirement benefit industry in the county while occupational retirement schemes offered by different employers take about 230,000 members and account for 12 per of industry.
- Individual retirement schemes with just below 10,000 members account for about 0.8 per cent.

- However, as the number of retired people increase, it has become clear that the continued payment of the pension from the consolidated Fund may over- stretch the government resources in future.
- For example, in the 2008/2009 financial year Treasury set aside Kshs 26 billion from the annual National Budget as provision for pension payment to former government employees.
- This amount constituted 3.7% of the budget and is expected to increase to over Kshs 100 billion in 2030 while it was only 1.5 billion in the 1993/1994 budget.

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- The funded contribution public service superannuation scheme will commence in the near future.
- Civil servants and teachers will be expected to contribute a percentage of their salary to which the government will add its contribution.
- This will free the Treasury off the burden of having to set aside money in the National Budget to pay the government pensioners.

THE PUBLIC SERVICE SUPERANNUATION SCHEME

- The Public Service Superannuation scheme was established under the Public service superannuation Act 2012.
- It is a Contributory scheme to provide retirement benefits to employees in the public service. The object of the scheme is to:

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The objectives of the scheme

1. Pay retirement benefits to members of the Scheme;
2. Ensure that every member of the Scheme receives his retirement benefits as and when they become due;
3. Assist to improve the social security of members of the Scheme by ensuring that the members save in order to cater for their livelihood during their retirement.

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- This scheme is mandatory for the said employees.
- Every member of the Scheme shall contribute to the scheme a prescribed rate per month to which the government adds a prescribed amount.

NSSF IN KENYA

- NSSF was established by an Act of parliament Cap 258, **Laws of Kenya in 1965**
- It began operations in 1966 as a department in the Ministry of labor and was **converted into a state corporation by an Act of parliament in 1998**.
- New Act No. 2013ct transformed the NSSF FUND from a Provident fund to a Pension Scheme
- It established two funds

i. The pension fund and

ii. The provident fund

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Contributions

- The pension contribution is 400/- of the pensionable wages made up of two equal portions of;

i. 200/- from the employee and

ii. 200/- from the employer

iii. The employee contribution shall be drawn directly from his salary and wages while the employers contribution shall come directly from the employer

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Membership

- Employers
- Employees- over 16years
- Voluntary members – over 18 years registered as a self employed (voluntary) member

- Compulsory for all workers in the formal sector (public/ private)

Register as a member: In Employment

- If you are in **employment**, all you need is to visit any **NSSF Office** closest to you with:
- Your original **National Identity Card** (ID Card), **Alien Card** or **Passport** and a copy of it
- An introduction letter from your employer
- We will record your details and register you. You will then be issued with an NSSF membership card. Your employer will require the **NSSF Number** on your card to enable them to make contributions to your account.
- You can also top up your contributions at any time through **MPESA**.

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Voluntary Contributions

- Payable in respect of voluntary members in the informal sector, pensional employees of government local authorities, universities and members of disciplined forces
- Payable from a minimum of Ksh 100 to any maximum amount.
- Annual figure for voluntary contributions is Ksh 4,800

Special contributions

Payable in respect of casual workers at the rate of 5% of total wages paid per month.

- Contributions not deductible from casual workers' salary.
- Levied to discourage engagement of casual workers by employers for prolonged periods.

Benefits payable under NSSF

1.Age Benefit

Qualifications

- **Eligibility:** Members are eligible for this benefit when they reach the age of 55 years, or when they ultimately retire from regular paid employment.

2.Survivors Benefit

This benefit is paid to:

This benefit is payable to the survivor(s)/dependant(s) relative(s) of a deceased member.

3.Withdrawal Benefit

Qualifications

- **Eligibility:** Members are eligible for this benefit if they are at least 50 years of age and they have retired from regular paid employment. A member would opt to apply for this benefit (over the age/retirement benefit) if they retire before attaining 55 years of age.

4.Invalidity Benefit
Cont'

Qualifications

- **This benefit is paid to:**
- Members who are certified to be permanently incapable of working because of physical or mental disability.
- Members who are at least 50 years of age and suffer from a partial incapacity of a permanent nature that prevents them from undertaking employment.
- **Required documents/ Standard processing requirements:** A certified copy retirement (on medical grounds) letter
- Medical/treatment records from the hospital you attend(ed)
- Bank account number and bank name and address
- A certified copy of your retirement letter OR certificate of service OR termination letter

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5.Funeral Grant Cont'

<u>Qualifications</u>

- **This benefit is paid to:**
- The grant is payable to a dependant of a deceased member. This dependant must be nominated by the family and must be identified by local administration.
- The deceased member must have been a member of the fund who made at least three (3) monthly contributions to NSSF.
- The deceased/beneficiary has not yet been paid his/her benefits.
- This is money given by NSSF to assist in the burial of a deceased contributor. It is not deducted from the deceased's account.
- The amount payable for this grant currently stands at **Kshs 2500**
- The grant must be paid within three (3) months of a member death

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4.WORK INJURY BENEFIT (WIBA)ACT

- Work Injury Benefits (Compulsory)Act 2007 Insurance covers the legal liability of an employer relating to bodily injury or disease sustained by an employee arising out of and in the course of employment.
- The policy does not extend to cover damage to third party property
- The loss must arise during the policy period
- It must arise in connection with the insured's business. This business must be disclosed in the proposal form.

Limits of liability

- Any one employee- Kshs. 4 million
- Any one occurance- Kshs. 25 million
- Any one year- Kshs. 50 million

Maximum liability of an insurer

- Damages awarded to the claimant
- Costs and expenses incurred with the insurer's written consent
- Known as cost inclusive cover
- No restriction on the number of insured events

Benefits

1. Death-96 months earnings subject to the maximum amounts
2. Permanent Total Disablement-Percentages as set out in the First Schedule
3. Temporary Total Disablement-Maximum of twelve months earnings
4. Medical expenses-Limited to Kshs. 100,000 per employee
5. Funeral expenses-Kshs. 30, 000 per deceased employee

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Clauses

- Excess clause-Insured to be responsible for the first Kshs. 5,000 of each and every claim excluding claims for funeral expenses
- The policy is subject to the reinstatement clause but the same is optional

The Insurance (Motor Vehicle Third Party Risks) Act

- Makes it compulsory for a motorist or owner of a vehicle driven on Kenyan public roads to have in force a policy covering third party risks.
- Third party policy covers the insured against legal liability arising from death or bodily injury to any person caused by or arising out of the use of a motor vehicle on public roads.

Main provisions of the Act

1. Compulsory third party motor insurance
2. Criminal consequences – fine or imprisonment for failure to comply with insurance requirement
3. Issue of certificate of insurance as evidence of insurance policy
4. Proper display of the motor insurance certificate – vertical position behind windscreen or rear side window
5. Return of cancelled certificate within 7 days; make statutory declaration for lost/ destroyed certificate
6. Insurer must pay claims for death or bodily injury irrespective of defects in cover.

NO CLAIM IS PAYABLE UNDER THE FOLLOWING CIRCUMSTANCES

- In respect of judgment, unless before or within 14 days after the happening of the event giving rise to a claim under the policy, the insurer had notice of bring the proceedings;
- In respect of judgment, so long as execution thereon is stayed pending an appeal;
- The policy had been cancelled by mutual consent;
- After the happening of the event, but before the expiration of a period of fourteen days from the tasking effect of the cancellation of the policy, the certificate was surrendered to the insurer;

- Either before or after the happening of the event, but within a period of twenty eight days from the taking effect of the cancellation of the policy, the insurer had notified the Registrar of Motor Vehicles and the Commissioner of Police of the failure to surrender the certificate;
- The insurer has obtained a declaration that he is entitled to avoid the policy, on the grounds that it was obtained by non-disclosure of material facts. Such a declaratory suit has to be filed before or within there month after the commencement of the proceedings in which judgement is given.

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A Claim can not be rejected based on the following

- The age or physical or mental condition of the person driving the vehicle; or
- The condition of the vehicle; or
- The number of persons that the vehicle carries; or
- The weight or physical characteristics or the goods that the vehicle carries; or
- The times at which or the areas within which the vehicle is used, or
- The horse- power or value of the vehicle; or
- The carrying on the vehicle of any particular apparatus; or
- The carrying on the vehicle of any particular means of identification other than any means of identification required to be carried by or under the Traffic Act.

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Shortcoming

The operations of this Act have been criticized on the following grounds:

- The Act does not cover damage to property;
- It gives rise to a fault system which means that claimants must prove that the vehicle that they were involved in an accident with was in breach of duty owed, which leads to delay because of negotiations
- Many claim ends up in courts where further delays occur.

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- The Act provides only for payment of victims of accidents which happen in public roads. Accidents that may happen in private lands, public car parks and beaches are not catered for;
- Until recently, there was no maximum amount of compensation. Parties therefore took an inordinate amount of time arguing as most claimants would want to be paid as much as possible.
- This has now been rectified though an amendment to the Act providing for three million shillings as the maximum amount payable on death or total disablement;

PROFESSIONAL INDEMNITY FOR INSURANCE BROKERS

- The Professional Indemnity Policy covers awards arising out of court judgments, defence costs, loss of documents, fees and expenses.
- This policy protects Insurance Brokers who are professionals in the Insurance market.
- This is so because brokers represent the clients/policyholders
- Tis policy protects them from legal liability for any acts of negligence they may commit in the course their duty. (refer to unit 4)
- It is compulsory for Insurance Brokers

- The insured will choose a limit of cover in line with the nature of service that they normally undertake or the size of the pension scheme funds that they manage.
- The Limit of liability for Insurance brokers-is 10million.

Scope of cover

i) Court judgments/awards
ii) Defence costs
iii) Fees and expenses
iv) Loss of documents

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Unit- 9

THE INTERNATIONAL INSURANCE MARKET

Insurance Situation After Independence

- At independence, the African insurance industries were least developed.
- In 1960, the gross premium written in Africa was US $ 370.
- Excluding South Africa, the premium was a lowly US$170 millions.
- This increased to $3.4 billion in 1980, $12.4 billion in 1988 and $ 25 billion in 1996. South Africa accounted for about 60% of the total premium in Africa.

See Table pg 255-256 TB

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The independent African countries adopted different strategies in efforts to address the state of their under- developed insurance sectors.

The main approaches were:

1: Nationalization

- This involved the government taking over the private insurance companies and creating a state owned company with the mandate to handle all types of insurance within the country.
- Examples: Tanzania, Egypt and Madagascar.
- Outside Africa ; India and the former Soviet Union countries.

The expectation was that governments could drive the growth of the insurance industries faster the private sector.

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2: Local Incorporation

- This favored the local incorporation of the foreign owned companies and encouraged the growth of fully locally owned companies
- Kenya, Nigeria and most of the West African countries took this route.
- The expectation was that such companies could be more inclined to invest locally.

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3: Mandatory Cession in Reinsurance

- This became common after the United Nations Conference on Trade and Development (UNCTAD) produced a paper in 1975 encouraging the establishment of national reinsurance companies with the aim of reducing foreign exchange outflow due to reinsuring overseas.
- Kenya established a reinsurance company in 1971 and Nigeria Reinsurance Corporation was established in 1978.

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4.Placing Restriction on the Overseas Reinsurance Arrangements

- This was especially common in countries which had established a state owned reinsurance company.
- A minimum reinsurance had to be placed or ceded to the state reinsurance company.

5. Encouraging the Growth of Private and Regional Insurers and Reinsurers

- This is what encouraged the growth of ZEP and Africa Reinsurance Corporations.
- The aim was to retain reinsurance premium in the region or within Africa.

6. Discouraging the Placing of Insurance Business Overseas

- This has been one of the key strategies of availing business to the local insurers.
- Section 20 of the Insurance Act provides that no insurer, broker, agent or other person shall directly or indirectly place any Kenyan insurance business, other than reinsurance business, with an insurer not registered under the Act without the prior approval of the IRA.

Comparison of Life and General Insurance Industries in Africa

1. Factors Favoring the Growth of General insurance Business

- Existence of some forms of **compulsory** motor and employees' compensation insurances in many countries;
- Existence of **legislation** requiring some form of compulsory professional indemnity insurances;
- Many **donor funded programs** for purchase and development of properties have some conditions that require insurance for such properties to be arranged;
- **Banks** require insurance of **collaterals** such as cars and houses before they can grant loans against them;
- Some modern business such as **aviation and Marine** must have some form of insurance before they can be undertaken because of their international nature.

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2. Factors that Seem to Discourage the Growth of Life Assurance Business

- **Low economic standards** in most African countries deny many people **disposable income** especially where in some countries there are communities still living at subsistence level;
- **Widespread poverty** in many areas with large percentages of the population living below the poverty line;
- Persistent belief particularly during the colonial period that the **life expectancy** in Africa was too low to sustain a vibrant life assurance industry;
- **Poor investment** environment has made returns unattractive from the point of view of enlightened policy holders as bonuses paid on life policies tend to be very low;
- **Declining and stagnant economies** fail to create an atmosphere conducive to long term investment which is key to the development of life assurance;

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- Some **cultural and religious** practices discourage the buying of life assurance
- **For example**, the Muslims belief that modern life assurance, as currently practice, is not appropriate for Muslims because:
  - **The insurance contract has some elements of wagering;**
  - **it is a contract of uncertain nature;**
  - **The values exchanged between the insured and the insurance companies are not equal.**

- A high rate **of inflation** especially in the late 1970's and most of the 1980's compounded the investment environment further by reducing the value of sums assured;
- Lack of **tax concession** from governments;
- **Poor sale methods** and use of agents who are not well trained;
- Substantial levels of HIV/AIDS infection rate not only increases **mortality rate** but also make life assurance more expensive;
- Government inability to provide **proper health care** as a result of which diseases are widespread. This reduces life expectancy rates, hence making life assurance expensive in many African countries;
- **Political instability** (and in some cases armed conflicts) in many African countries has tended to discourage long term investments.

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Insurance Penetration

- Insurance penetration is the percentage of insurance premium in a country expressed as a percentage of the Gross Domestic Product (GDP).
- It shows the size of the insurance sector relative to GDP and can be worked out separately for life and general business, or indeed for any class of insurance business.

Insurance Density

- Insurance density shows the average amount of money spent by one person in the country on insurance.
- It is arrived at by dividing the gross insurance premium of the country by its population and can be worked out separately for life and general businesses.
- It is an indicator of the efficiency of the insurance industry sector in a country.

The Africa Reinsurance Industry

- The African reinsurance industry remained almost non-existent until the mid 1970's.
- During the colonial period, the foreign owned companies transferred business to their home offices by way of more than 95% of the premium being reinsured overseas.
- Until the early 1970s, the United Nations Conference on Trade and Development (UNCTAD) started appealing to the developing countries to set up their own state owed reinsurance firms with obligatory reinsurance cessions.
- The aim was to increase market retentions by reducing overseas reinsurance

Why a high percentage of the total reinsurance is purchased from outside Africa:

- **Low capitalization of African** insurance companies;
- High propensity of the large number of subsidiaries of **multi-nationals** to reinsure outside the country;
- Preference of **outside ''products**" by many consumers;
- Risks such as aviation, heavy industries, engineering, business interruption, oil and energy are, in most cases, too big for most local markets to retain anything more than a token share. As such they are placed in the international markets;
- Existence of only a few reinsurance companies.

  For example

  -Tanzania has only recently established a reinsurance company

  - Uganda is in the process of establishing one.

  -Rwanda and Burundi, on the other hand, do not have reinsurance companies
- Lacks of technical knowhow to underwrite some of the big risks.

The current major international players in Africa market are

- Munich Re, Swiss Re and Hannover Re.
- The regional players are Africa Re, CICA Re and SEP Re.

The national state reinsurers are:

- Nigeria Re, Egypt Re, Kenya Re, SEN Re, ZIM Re, and more recently TAN Re.

There are also private companies are:

-Universe Re, Global Re and Continental Re in Nigeria and East Africa Re in Kenya.

The leading Africa reinsurance market is provided by South Africa.

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Growth and Development of African Insurance Industries

Some measures that the African countries can take to enhance the growth of their insurance industries are:

- Enhance **insurance education** at all levels so that people can become aware of the critical role that insurance plays in the socio-economic development of a country;
- **Design insurance products** that meet the diverse needs of the African people.
- **In this regard one can suggest the following:**

  -Life assurance products where premiums are payable at irregular intervals as many people such as farmers and livestock keepers do not have a regular income

  -Life assurance products with low premium which majority of the people who are generally poor can afford.

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- Allow generous tax relief on life assurance and annuities so as to create a financial incentive for their uptake;
- Simplify proposal forms and policy documents and even have them written in national of local languages that the less educated can understand;
- Have insurance distributed through alternative channels such as supermarkets, retail shops, garages and petrol filling stations. In this respect the rapidly growing trend of banks selling insurance products- the concept of banc assurance- is a step in the right direction;
- Have legislation which strengths the financial base of insurance companies so that collapsing of insurers and the resultant tarnishing of the image of the insurance industry is curtailed or altogether stopped;

- Strengthen the supervision of all players in the industry so that fair play and ethical practices can be adopted by all. This would enhance the image of the insurance in the eyes of the public and hopefully lead to increased sales;
- Strengthen claim payment through industry cooperation and legislation as this is an area that seems to create a lot of complaint against the insurance industry.
- Accelerate the overall rate of economic development as there seems to be a strong positive correlation between a country economic level of development and the amount of insurance purchased.

- **International Insurance Markets**
- **Specific Insurance Markets**

- **South Africa**
- **The UK**

  -Specially-The Lloyd's of London
- **The USA**

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The International Role of Insurance

- Insurance by its very nature, is transacted beyond the national boundaries.
- Historically therefore trading nations have always established insurance agencies and branches in other countries to service their business.
- There are also definite advantages and challenges accruing in the development of international trade.
- Some of these are discussed below.

Advantages of International Development

- The basic concept of insurance is that by **spreading risk**, the effect of loss will be carried by the insuring public as a whole rather than the one individual who incurs the loss.
- The risks of one country are also shared by others particularly where some risks may be of a catastrophic nature when viewed from the capacity of one country's insurance market;
- The underwriting results of particular countries tend to operate in cycles of heavy losses and reasonable profits.
- Viewed internationally, there are usually favorable results in some markets while at the same time there are disastrous ones in others.
- An international spread of risks by the insurers in each country will help to even out the markets fluctuations leading to more stable markets.

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- This in the long run benefits policyholders everywhere;
- In the developed countries, there are likely to be multinational commercial organization requiring cover on a worldwide basis.
- If the insurance market of the parent company is to retain the business, it is essential that staff is experienced in the risks of foreign countries and are aware of the pertaining insurance regulations.
- There is no better way to achieve expertise required than to participate actively in as many countries as possible and with as wide a portfolio as possible.

- Where a nation has a large amount of foreign trade, it is desirable that its financial services are developed in parallel, not only to facilitate that trade, but as foreign currency earners in their own right.
- For example, Japan developed as a major trading nation and also became a major provider in international insurance cover at the same time.

Challenges of International Development

- Insurance companies which have been established overseas for many years are finding that the legislation being introduced is rapidly making it more and more difficult to continue operating with the same volume of business; for example nationalism in some developing countries and aggressive marketing by locals and other foreign companies have reduced Britain's share in many markets in its former colonies.
- In certain countries, there is active political prejudice against foreign companies and the rates of premium they can charge.
- The same economies of scale in operating costs are not possible at home, or as available to the national companies in the country of operation. The result if that the foreign company is less competitive.

The Purpose of International Insurance Transactions

- The basic rule is that people tend to want to insure with an insurer established in their own country.
- This is because local underwriters may issue policies in the local language and, in most cases, the policy will have to conform to local regulations.
- It is easier to follow up on claims with a locally based company than one based outside the country.
- The local market may offer concessions to encourage people to insure locally.

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Why people may still insure abroad :

- When the risk **is too large** or unusual or the local market does not have technical know-how to handle it.
- Most countries allow businesses to insure overseas if cover is **not available locally**.
- When a cover is illegal in the local market e.g. kidnap and ransom insurance **is illegal** in some countries as some people think that it would encourage these crimes.

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- Ehen the cover is more expensive locally. Local tariffs may maintain premium rates at an artificially high level. In order to avoid paying tariffs rates, some insured's may be prepared to use an overseas insurer;

- Insurance may also be expensive where insurers are too small to obtain the advantages of economies of scale;

- The insured is not a local citizen. In such a case, the insured may prefer to insure with an insurer located in the home country because of patriotism and other considerations.
- where an insurer is co-coordinating a global insurance programme for the insured.

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Insurance buyers in the country may want to deal with an insurer based overseas because:

- Buyers who are foreigners may want to deal with a local subsidiary of an insurer based in their home country;
- Others may be attracted to overseas insurers because they could be offering new or more flexible products which may not be available in the local market;
- The local buyers may neither know nor care about the ownership of the company e.g. because the company has been bought by a foreign company but has not changed its name;
- International movement of merchandise and personnel naturally break down borders. It is a case of insurance following trade.

A Foreign owned insurer may seek establishment in a local insurance market because:

- **Cross – border business is prohibited or discouraged** – many countries prohibit cross – frontier insurance.
- **Cross – border business would not be profitable**. It is not possible to profitably sell direct business especially personal lines and small commercial insurance contracts across the borders.
- Direct insurance requires direct contact with the insured in order **to survey the risk**, provide advice and investigate and settle claims. Reinsurers also prefer local establishment in markets.

- There is an **opportunity for profits and growth**. An insurer may seek to establish in a foreign market that appears to have greater prospects for growth.

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Q&A