FUNDAMENTALS OF INSURANCE
(UNIT-VI)
THE GENERAL INSURANCE CONTRACTS

1. INTRODUCTION

Hello students. Let's study fundamentals of insurance. This is unit 6. Today we will study the general insurance contracts.

2. INSURANCE

Now let's study first the basic definition of insurance so as to proceed to the contracts. Insurance will be defined as the contract between parties whereby one party called insurer undertakes for an exchange for a fixed sum, called premium, to pay the other party, called insured, a fixed amount of money after happening of a certain event. So what is insurance? Insurance is basically a contract between two parties, where there is a company and a client. Both enter into agreement. The client pays the premium and the company pays the kind of the fixed amount or the return, after happening of a certain event. Insurance policy is legal. Insurance policy is a legal contract and its formation is subject to the fulfilment of the request of the contract defined under the Indian Contract Act 1872. So this policy is regulated by the Indian Contract Act of 1872, where you have to generally get into agreement of compliance with the laws to have the crystallisation of the money, in a fair and a effective way.

Contract Act:- According to the act, a contract may be defined as an agreement between two or more parties, to do or to abstain from doing an act, with an intention to create a legally binding relationship. Since insurance is a contract, certain sections of the Indian Contract Act are also applicable. Contract is type of an agreement. it is a type of a fair deal between two people. It is exchange of money for something, that is, you give money to some other party or you exchange kind of an issue with each other. Let's see what is the issue and the faith required for a contract.

Essentials of the Commercial Contract:- The elements of the general contract basically involves

I. Offer and acceptance
II. Consideration
III. Legal capacity to contract or competency
IV. Consensus at idom , and
V. Legality of object

Here, there has to be offer. The offer is basically given by the company, and the client accepts it. Get into a legal issue of good faith, give information to each other, consumers pay money and company gives returns.

Insurance business in India:- Insurance is a federal subject in India. Insurance business is primarily regulated by two statutory that is the insurance act of 1938 and the Insurance and Regulation and Development Act of 1999. So, insurance business is not very old in India. This is regulated by the act of 1938 and another IRDA act which came in 1999. The elements of special contract relating to insurance- one is life insurance and other is general insurance. Life insurance is based on utmost good faith and insurable interest. General insurance is also based upon utmost good faith and insurer's interest. So when we talk about life insurance that is LIC and GIC, they both deal with the kind of faith with the customer, and there has to be kind of interest which needs to be insured.

Classification of Insurance Business:- The insurance business is classified into four classes:

I. Life insurance business
II. Fire insurance
III. Marine insurance
IV. Miscellaneous insurance

Let's study the legal framework. Insurance is made available to the public through the medium of contracts that details the rights and duties if the parties to the insurer's agreement. Most of the insurance contracts are expressed inviting event when an oral binder initiates the transaction. Insurance cannot be the kind of subject which is studied orally or verbally. A contract is legal so the legal sections are written, though the practice is followed on the basis of the norms, but still the legal contract binds the parties to get into the fulfilment of the laws which are associated with the agreements. Insurance contracts are technical. Insurance contracts are complicated because of the technical nature of the subject matter. The statutory requirement is that, a certain language should be employed, and the need to avoid terms that may be considered as ambiguous. Laws are technical because the language cannot be changed, and the language needs to avoid words with double meaning or the words which generally convey kind of a deceptive meaning. So, laws need to be defined in a way which is understood by the public and they can be implemented in easy way.

3. TORTS, CRIMES UNFAIR PRACTICES, INDIAN CONTRACT ACT 1872, INSURANCE ACT 1932 & POWER OF CENTRAL GOVERNMENT

Let’s study what are trots. A trot is a private wrong. It occurs whenever someone acts or fails to act in such a manner that an individual’s peace of mind and rights are jeoparadised. It refers to individual’s action that effectively deprives another of his right to security of person, reputation or property. Trots are important in insurance business because they are major source of loss covered by liability insurance. See it is a kind of a private wrong, that is, something happens wrong in business, and where the right of the consumer is rejected. So this trot should be reduced in business so that the company maintains a reputation in the market.

Crimes:- Some crimes that are recognised by the statutory are specific to insurance, while others are relevant to insurance law, because they are crimes committed to obtain funds illegally for insurance company. A few examples of crimes are rebating and twisting, filing of false claim and unlicensed insurance activity. When this business, generally, is flourishing in any country, and the faith is reduced, this business can lead to lot of crime in the country also. Because, when insurance is done people can claim for unfair claims or unfair money or people can also indulge in the illegal death of the people who are insured. Like most of the woman in dowry cases, generally are involved in these kinds of crimes. So government of India has stopped to insure woman, who are married and is not working. This is basically business which is done in the good faith, and is it is not controlled legally; it can do more harm to country than goodness. Let’s see what are the unfair practices which govern the business?

I. Defamation
II. Homicide
III. Breach of trust
IV. Unfair discrimination
V. Conspiracy

This business though involves lot of money, but it is generally impacted by the unfair practices in the market where defamation, taking more money or negotiating in a way where loss has not actually happened, but you claim for higher money. So, these are the practices which impact the industry. Both the company and clients generally have to suffer a kind of a bad reputation and a loss.

Indian Contract Act of 1872:

Insurance contracts are agreements between insurance company and insured for the purpose of transferring from the insured to the insurer, a part of the risk of loss arising out of contingent event. Therefore all the provisions of Indian Contract Act of 1872, in general are applicable to insurance contracts also. The General Contract Act of 1872, which is applicable to most of the commercial and business organisations, carries its impact to the insurance also. Because insurance is also kind of service, for the money taken from the consumers.

Insurance Act of 1938:

This act was passed in 1938. After that the act has been amended a number of times including those in 1950 and 1968. Important provisions in act relate to Section 2C prohibit to carry on insurance business, until, is a public company or a registered society. So the insurance act of 1938 prohibits people to work without licence. It is only public company or registered society, who can govern or generally, enter or involve into the insurance business of India.

Power of central government: the central government is empowered to exempt any insurer or any person, for the purpose of carrying out the business of granting super. Allowances and annuities as per section 211C or for the purpose of carrying general insurance business, exempted insurer after the promulgation of IRDA Act 1990 only Indian insurance company can carry insurance businesses. Now when we talk about the evolution of insurance business, prior to independence the insurance scene was different. But when the central government was formed after the democratic set up was done, it was only the approved society and the public company called LIC, which came into existence, and it was the only lawful body which was generally doing the business of insurance in India.

Licensing conditions: only Indian insurance companies to be granted licences under the act. It is mandatory that only an Indian insurance company can carry on an insurance business in India. Now the conditions have changed. Privatisation has come and many private companies from foreign market have entered the Indian market, but this act had defined the central government initially had power to Indian companies to do business of insurance in India.

4. INDIAN INSURANCE COMPANY, ACCOUNTS AND RETURNS, TARIFF ADVISORY COMMITTEE, FAIR TREATMENT, PRINCIPLES OF INSURANCE, NATURE OF CONTRACT

Indian Insurance Company:

An Indian insurance company is a company registered under the company's act of 1956, where the aggregate foreign equity share holding does not exceed 26% and wholesale purpose is to carry on life, general or reinsurance business. So, according to the companies act of 1956, insurance is a kind of the business, which generally is done by an Indian company, needs to have licence from the government to carry this kind of legal activity.

Stages of Registration:

a) Requisition for registration
b) Application for registration
c) Fulfilling the licensing criteria
d) Fulfilling the capital licensing issues
e) Capital requirement, and
f) Foreign stake

When you enter into registration, obviously, you apply for registration. You need to fuflfill the licensing criteria according to the companies act by the insurance act, that is the laws governing the businesses, and then you also have to fulfil the kind of the money and the capital required for the investment of the company.

Accounts and Returns:

An insurer is required to keep a separate account of all receipts and payments in respect of each class of insurance like fire, marine and miscellaneous insurance. So any company who is dealing with insurance business in India, needs to maintain a fair account statement, where all the receipts related to fire life and marine insurance has to be classified and the details have to be prepared in terms of the cash taken and cash given.

Preparation of the prescribed forms:

Every insurer is required to prepare at the expiration of each financial year in prescribed forms- a balance sheet, a profit and loss account and a revenue account for each class of insurance business. So, this is the basic aspect which an insurance company needs to fulfil, that you need to give a kind of the balance sheet and the account of statement which generally depicts the cash flow and the kind of the money paid to the clients.

The tariff advisory company:

The tariff advisory company established under the act, is empowered to control and regulate the rates, terms etc, that may be offered by insurers in respect of any risk or of any category of risk. So the tariff advisory company is basically trying to rate the kind of the control and the regulation of the rate it is defined to do insurance business in India.

Fair treatment:

It is providing that in fixing, amending or modifying such rates, the committee shall try to ensure as far as possible that there is no unfair discrimination between risks of essentially the same hazard of also that consideration is given to past and perspective loss experience. Every insurer is required to make payment of the track of the prescribed annual fees. That is, generally a kind of experience is built up when an agent is there and what is the amount of loss that has been incurred on his client, that has to be calculated. So if the losses are very high, the agents also lose the reputation, because that takes up lot of capital from the company. So what is the evaluation in terms, what is the risk involved when you give a policy to a very good investor and what could be the profit to the company and what could be the risk associated with the policy holder. Both need a kind of a detailed evaluation because this is a financial transaction impacting the balance sheet of the company.

Principles of Insurance Contracts:

The principle function of an insurance contract is

a) To define the risk that is to be transferred
b) To state the conditions under which the contract applies, and
c) To explain the procedure for settling losses

Firstly, the insurance contract is basically a contract or written agreement between two parties, it is to state the condition and the risk involved. It is also to state the rate at which the risk is covered.

Nature of contract:

An insurance contract has four attributes:

a) Entity: all the terms and conditions are to be found in the policy document. If the terms and conditions are oral or not stated explicitly, they are difficult for parties to prove. Entity is everything, whatever is related to the act, law, information, policy, everything has to be written down. This is the essential element of the contract act.

b) Personal: the contract follows the person, the insured, rather than the property. What is personal? A person has to exist in this world. You cannot take tangible item without the ownership of the person. So if there is no ID proof of the legal existence of the person, things cannot be insured.
c) Unilateral: After the insured pays premium, the performance is obligatory is important for one party that is the insurer. The performance is generally liable for the company when the premium comes and after the premium only the obligations start.
d) Alienator: Performance is conditional upon an event that may or may not happen. The performance is obviously conditional that is if something happens then only you can get the benefit of the insurance.

5. ELEMENTS OF INSURANCE

Elements of insurance:

The basic elements of every contract are:

1) Application
2) binders
3) policy forms consisting of heading, body, pact
4) Endorsement

So this is the basic theory about insurance that what is contract. It generally has a kind of application form which has to be filled by the information related to the consumer and the client.

Registration and licensing of insurance:

Any applicant desiring to carry on the insurance business in India has to make application to the authority. Separate two applications has to be made for life insurance business, consisiting of linked or not linked businesses, or both. Registration is important that is if you want to get into the process of getting a policy, you need to go to the company by a registration form. The policies could be linked business policies or could be non linked business policies. Non linked business policies are fixed policies with a fixed rate of interest, but linked policies are generally related to the stock market or the equity market where the rates change according to the investment which is done through the mutual funds, and here the business rates are changing sccording to the ups and downs of the markets.

General insurance:

General is insurance business includes health insurance business. The paid up capital of the insurer shall not have more than 26% shares in form of foreign equity. So general insurance business relates to other aspects that is health and other issues of life.

Essentials of contract act:

1) Offer and acceptance: In life insurance, offer can be made either by the insurance company or the applicant that is, the proposal and the acceptance will follow. Offer is the kind of the advertisement which the company puts into the newspaper and floats the new policies in the market. And if people generally get interested then they enter into registration, this is acceptance. Offer is you offer something to the client.
2) Consideration: There is no validity of the contract if there is no consideration, which is the act or promise which is offered by one party and accepted by the other as the price of his promise. Generally, consideration has to be there, one has to offer a promise and other has to pay the price for it. There could be no contract if there was no promise or no price.
3) Premium payment: in insurance contracts, the consideration is the premium that the insured pays to the insurer, as the price of the promise that the insurer has made, that he shall indemnify the insured. Hence premium payment is the consideration on part of the insured and the promise to indemnify is the consideration on the part of insurer. Premium is the kind of the instalment or the money which you pay to the company. The obligations of the company can only start if you pay something. The promise cannot crystallise if the money is not paid to the company.

4) Legal capacity to contract or competency: For an agreement to be binding on all parties, the parties involved must have the legal capacity to enter into a contract. With respect to the insurer, if the company is formed as per laws of the country and empowered to solicit insurance, then insurer is capable of entering into an agreement. This is legal competency, that is the company must have a licence and registration and then only the offer can float in the market. The competency is built up by the legality of the act.
5) Qualifications of the persons to enter into contract: with respect to the insured, the person should be of legal age, that is 18 years and of sound mind. Thus he must have sound mind and he must be of 18 years of age. That is mentally retarded people or people who are mentally not well or they are admitted into the hospital, they cannot enter into the contract. Because then it will be beneficial on the part of the company to take advantage of these people. And the people must be of 18 years of age to enter into any kind of contract in India. If a contract is made with an underage, the application may be held unforcible if the minor decides to repitate it at a later date. In insurance contract, the insurer is bound by the contract, as long as the underage wishes to continue. If the minor repidates his contract, the law will allow him. A refund of the entire premium paid up, that is, if sometimes it happens that the underage person is there and if he wants to reverse the business, the company will pay the premium back to him.
6) Agreement to the contract: Both parties of the contract should be of the same mind and there might be consent arising out of the common intention. Both parties should be clear about what the other is saying. The insurer should know what the insured wants and the insured should know what the insurer is offering and both should agree on this. That is when the offer and acceptance is there, generally the agreement happens because the vested interest of both parties needs to be crystallised. Obviously the company needs profit to work in the market and the client needs better returns on the policies which he has got from the company. If the vested interest of both the parties is

generally crystallised then only the agreement can convert into a business option.

7) Deregulation of insurance sector: until 1999, there was no private insurance company in India. The government then introduced the Insurance Regulatory and Development Authority Act in 1999, thereby deregulating the insurance sector and allowing private companies. So this is the year after the impact and crystallisation of IRDA Act 1999, the privatisation if insurance sector starts and many other companies also enter into the market. Furthermore, a foreign investment was also allowed and capped at a 26% holding in the insurance companies in India. In 2015, the limit of FDI in insurance sector has been raised to 49% subject to certain conditions. So this is the kind of rise which is happening in the indian market through the private companies also and not only the government companies which are functioning in India but the business has opened to wider options for the public and the business has got greater trends to happen in the future market.

6. SUMMARY

Now let us study the summary of this lecture. In this we have studied the general contracts of insurance. The contract act or the companies act is generally impacting the insurance business. Thus insurance is also a commercial aspect where service is given to client and here the client pays money. So the company is bound to act in a fair and honest way. Though generally the business is impacted by crimes and torchs but still the honest practices has led this business to open up new options of converting premiums of people in lucrative investments. The foreign direct investment has come to India because the deregulation of the sector started very early through the IRDA Act of 1999. The deregulation and the globalisation of the economy have opened new options of business for this sector. I hope the students must have understood the various laws of the general insurance contract act and also the kind of the market actions growing up in India.

Thank you students!