Study Unit 01

Define and explain - Risk: Risk is the uncertainty of loss.
Unfavourable deviation from the expected.

Define Risk Management: A means of removing some or all of the uncertainty

Differentiate between :

<u>Pure / Event Risk</u>	**<u>Speculative Risk</u>**
There is either a Loss or No Loss	Taken out in the hope of some gain.

Particular risk: Affects only you of your family, not society as a whole. Break in.
Fundamental risk: Affects society as a whole. War. Earthquake.

Risk Management Control – 2 core **activities**:

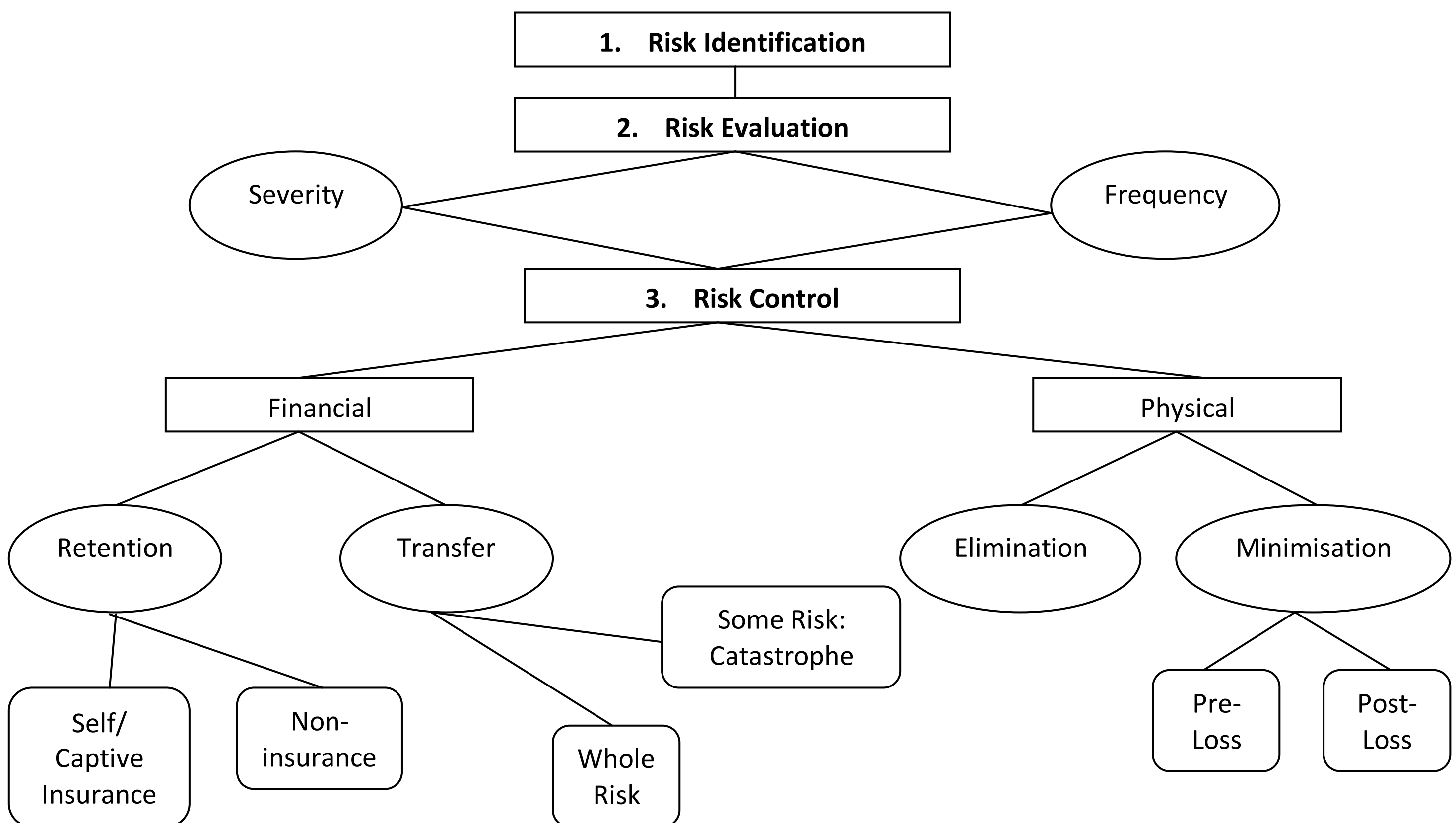
- **Risk Financing:** Retention
  Transfer
- **Risk Control:** Avoidance / Elimination
  Reduction / Minimisation

Risk sharing: Special case – risk is transferred from the individual to the group

****Risk cannot be transferred – only the financial consequences of the risk are transferred to the insurer.**

How does insurance fit into risk management: Risk control – Financial – Transfer of risk

Steps in the risk management process: 3 Phases in the risk management process:



Risk identification by means of:
- Physical inspection
- Organisational charts
- Flow charts
- Check lists

Skills required to identify risks:

How to evaluate risk quantitatively and qualitatively:

- Quantitative Measures: Using statistics – number of loss incidents; cost of losses
- Qualitative Measures: Investigation – causes of losses

Difference between:

	Non - Insurance	**Self - Insurance:**
Fund:	No Fund allocated for any losses	Fund set up to cover losses
Risk improvements:	May or may not have been improvements	Most likely have identified problem areas and will have taken some steps to improve
Handling of losses:	Pay for losses as they occur	Staff and procedures will be in place

Excess: Payable with each and every claim
Franchise: Applies to each and every claim, but if the claim exceeds the franchise amount, the claim will be paid out in full.

Study Unit 02

Define Insurance: The transfer of the financial consequences of risk and sharing the loss that occurs equitably
Combining many risk exposures with the cost of losses being shared by all the participants.

Identify and explain two essential features of insurance / 2 Functions of insurance:

- The transfer of the financial consequences from an individual to a group
- The sharing of losses on some equitable basis by all member of the group

Why is the term 'self-insurance' a misnomer?

- The essence of insurance is the transfer and share and no one can transfer to or share with himself.

Explain what is meant by "adverse selection" and why is it a problem for insurers?

- The tendency among people with a greater probability of loss than the average, to seek insurance.
- PROBLEM: The greater losses than expected for the insurer

How to identify an insurable risk (7):

- *Similar Risks*: Experience of similar risk is necessary to establish a fair premium.
- *Measurable and Definite loss*: Must be able to tell when a loss occurred to attach a particular value to it.
- *Fortuitous / Accidental loss*: Loss is due to accident or chance.
- *Inevitable loss*: Although death is inevitable, the timing of death is uncertain and therefore insurable.
- *Non-catastrophic loss*: Catastrophes such as drought and famine are therefore not insurable.
- *Insurable Interest*: You can only insure things with which you have a legally recognised financial relationship.
- *Public Policy:* Law states that contracts may not be against public policy.

Explain how the law of large numbers support the operation of the insurance mechanism:

- The law of large numbers states that the greater the number of predictions of an event based on chance, the greater is the chance that the actual result will be the same as the expected results.

Insurers is affected by the Law of Large numbers in two ways:

1st If the probability of a loss if to be estimated accursedly, a large number of cases should be considered.

2nd After the probability has been estimated, the estimate can only be used as a basis for

predicting future losses when the insured is dealing with large numbers.

Advantages of Self-Funding:

1. Avoids expenses associated with traditional commercial insurance (broker commission & premium taxes)
2. Saves on high insurance premiums.
3. Gives better control over the claims process.
4. Allows for investments returns.

Disadvantages of Self-Funding:

1. Could leave the company exposed to catastrophic loss – purchase reinsurance.
2. The company could lose available insurer services.
3. Losses could vary considerable from one year to the next.
4. Possible adverse employee and public relations cold arise from adjusting losses.

The **Ceding company** transfers its risk to the **Reinsurer.**

Retention: The amount the ceding company is willing to bear.

Significance of reinsurance for the Insured:

1. Reinsurance spreads the risk and increases the financial stability of insurers.
2. Reinsurance facilitates placing large or unusual risks with one company.
3. Reinsurance helps small insurance companies to stay in business.

Study Unit 03

List the participants in the short term insurance market:

- Buyers: Private clients; Commercial clients; Public Bodies
- Intermediaries: Agents; Brokers; Banks; Reinsurance brokers; Lloyds Brokers
- Insurers: Proprietary & Public company; Captive Insurers; Lloyds; Underwriting Managers
- Reinsurers: Reinsurers; Mutual Indemnity Associations; Protection & Indemnity Associations
- Regulators: Financial Services Board; FAIS Ombudsman; Short Term Ombudsman
- Other players: Loss adjusters; Motor assessors; Risk Manager

Explain the difference between noninsurance and self-insurance:

Non Insurance:
No Fund
No guidelines as how to handle losses
Cover losses from operational income

Self-Insurance:
Fund from which claims are paid
Dedicated personnel to handle claims
Guidelines as how to handle claims

List the advantages of self insurance:

- Premiums are lower and the saving in premiums can be invested to cover future claims.
- Premiums don't increase because of others peoples' claims
- Strong incentive to reduce claims and control losses
- When there is a loss there will be no disagreement with the insurer over Settlement

List the disadvantages of self-insurance:

- A Catastrophic loss could occur and deplete the fund
- The aggregated effect of many losses during the year may also have a catastrophic effect on the fund.
- Capital is tied up – Could have used it for business operations
- Technical advice of professional insurers could be lost
- premiums based on very narrow base of claim statistics
- Temptation to use money from the fund.
- Might need to employ insurance specialists – COSTLY

Describe a captive insurance company:

Relevant when choosing to Self-Insure. 3 Options:

- Establish a fund to administrate it and handle claims
- Establish a separate company – captive (usually overseas for tax benefits) to underwrite and handle their insurance
- Set up a fund with an existing insurer and make use of the admin facilities and insurance license of the insurer.

Describe the operations of Lloyds in SA:

- Among the largest property and liability insurers & reinsurers in SA
- Operations are worldwide
- Remains a Trust account in SA as extra security for SA policy holders

Differentiate between a mutual indemnity association and a Protection and Indemnity club (P&I Club):

- Mutual Indemnity Association only accepts business from members of a particular trade – Marine
- P&I Club is a form of Mutual Indemnity Association.

Describe the functions of the loss adjuster:

- Contact and visit client and look at: * damage caused by the peril
  * Point of entry and method of entry where the loss is theft
  * Supporting documentation, as the insured must proof his loss
- Obtain quotes for replacement articles
- Find contractors to carry out repairs
- Liaise with the police and other involved parties
- Ensure post-loss protection and minimisation efforts are carried out

Describe the functions of the motor assessor: Inspect the damage and negotiate with panel beater

Explain reinsurance and collective insurance:

Reinsurance: - When the risk is bigger than the insurer wants to take on, he takes out Reinsurance with another Company to insure the amount that exceeds his capacity. He is then the insured.

Collective insurance:
- Two or more insurers underwrite a policy.
- Each insurer takes a share
- Lead insurer issues a policy
- Claims are handled by the lead insurer

Study Unit 04

Required elements for a contract to be legal:

- Consensus between parties: Offer and acceptance.
- Parties must be competent to contract.
- Performance must be possible and legal.
- Prescribed formalities must be complied with.
- Both parties must exchange consideration – what each party promise to do.

****Insurer offers to be insured.**

Purpose of THE PROPOSAL: Invitation to do business

1. To elicit information – to decide whether to accept or decline + how to price the premium + what terms.
2. To make a legal offer – offer must be made before contract can be concluded + offer can be made verbally.
3. To elicit a quotation – when insured need insurance quotation; insurer's quotation is then a legal offer.
4. To describe the cover available
5. To advertise – advertise other products available
6. To establish a warranty –serves as warranty

SASRIA: South African Special Risk Insurance Association – cover risk against riots and strikes.

Define Indemnity: The insured is financially restored to the same position he or she was in before the loss. Cannot make a profit from a loss.

Define contribution: When two policies are in force, each pays its rateable portion of a loss. The insured cannot recover the full amount from both insurers.

Define subrogation: To stand in the place of. When the insurer claims from a third party on behalf of the insured after they paid out the financial loss to the insured.

Fundamental risk: Effects large part of society/world. Commercially uninsurable. Earthquakes, War, Riots, unemployment, recession. (SASRIA – political riot & strike risk)

Pure risk: Either a loss or No loss. You either have a car accident or you don't.

In order for a risk to be insured:

- Cause of the loss must be accidental or fortuitous.
- There must be insurable interest.
- The risk must be one of a number of similar risks.
- Must not be against public policy.
- Not insuring the article itself, but the cost of replacing it.

Explain 'average' and when it applies:

- Relevant when insured is under-insured.
- Insured is self-insured for the portion that the asset is underinsured.
- If claim is smaller than the insured value, the insured bears a portion of the loss.

Demonstrate how the principle of contribution operates:

- When two policies are in force, each pays its rateable portion of a loss.
- The insured cannot recover the full amount from both insurers.
- If claimed from one insurer, that insurer has the right to claim from their co-insurers a pro-rata portion of the amount they have paid.

Explain how the principle of indemnity is supported by subrogation and contribution:

- **Indemnity** states that the insured must be financially restored to the same position he or she was in before the loss, but cannot make a profit from the loss.
- **Contribution** states that when two policies are in force, each pays its rateable portion of a loss. The insured cannot recover the full amount from both insurers.
- **Subrogation** means 'to stand in the place of' and happens when the insurer claims from a third party on behalf of the insured after they paid out the financial loss to the insured.

Explain why the principle of utmost good faith applies to insurance contracts:

- For the insurer to decide whether to accept the risk or not.
- For the insurer to decide on the premium and the terms.
- To allow for the insured to pay his or her fair share into the common pool.

Describe the process of arranging cover, from application to payment of a premium:

- Broker requests a quotation
- Receives the proposal with premium amount, terms, additional protection (Trellidoor) and valuations
- Clients accept + make necessary improvements for theft (if any) + signs debit order.
- Policy document is issued by the insurance company and forwarded to the broker/client.

Describe the factors that are taken into account when underwriting domestic insurance:

- Occupation
- Details of previous claims
- Insurance declined or terms imposed
- Details of the risk
- SASRIA needed?

Householders Policy Factors to consider:

- Sum insured
- The Area
- The Construction
- The Burglary Protection at the risk

Explain when a premium is payable for short-term insurance:

- New policy = on the inception date
- Endorsement / Marine declaration = 1st day of the month following the date upon which documentation is issues
- Renewal premium = on the renewal date, but **Natural Persons** must be allowed **at least 15 days grace.**

List and explain the parts of a short term policy:

- **Heading**: Name of insurer + head office details
- **Preamble / Recital clause**: Names of the parties to the contract + states that the preample is the basis of the contract + Premium payment conditions.
- **Operative clause**: Where insurer agrees to pay a claim when a loss occurs.
- **Exceptions**: might include some exception (riots, strikes – SASRIA).
- **General conditions**: Info to the insured on what to do in certain circumstances + what insurers must do in certain circumstances.
- **Disclosure notice**: Name + contact details of product supplier; Contractual relationship between product supplier and FSP + equity interest; Restriction imposed on FSP by product supplier; Full details of FSP.
- **Policy Schedule (personal for each client)**: full details of the RISK, INSURED, PERIOD, EXCESS PAYABLE, POLICY NUMBER, SPECIAL TERMS AND CONDITIONS.

Study Unit 05

Describe the renewal process, from receipt of the advance list until despatch of the renewal documents:

1. Underwriter receives a list with policies due for renewal two months before the renewal date (Advance listing)
2. Underwriter considers the number of recent claims + Size of the claims;
3. Underwriter tries to identify trends: Insured claims regularly, Geographical area claims
4. Renew or not?
5. What will the new premium and terms be. Terms: adjust excess; ask for improvements; request survey.

List the steps taken by the underwriter-insurer in the renewal process:

1. Review Policy
2. Determine the new premium + terms

List the steps taken by the Broker in the renewal process:

1. Receive / request renewal documentation.
2. Receive details if policy will be renewed, new premium and terms.
3. If policy is not renewed, Broker will place the business elsewhere.
4. Check new rates and terms to determine if they are fair.
5. When satisfied with the information, Broker will call the client to discuss the renewal.

List the steps taken by the Client in the renewal process

1. Inform Broker / Insurer of any relevant changes.
2. Receive information regarding the renewal.
3. Make decision to renew or not.

Describe the steps required for SASRIA cover when the policy is renewed:

- SASRIA cover is not automatically given
- For all classes of insurance, except motor, there must be an underlying policy that has fire as one of its perils.
- Request must be in writing.
- Insurer issues coupon within 30 days.
- Coupon must be paid once requested.
- Coupon cannot be cancelled.

Study Unit 06

Define Reinsurance:
- Insurance of the insured.
- The shifting of risk or part of the risk by a primary insurer (**Ceding Company**) to another company (**Reinsurer**)
- Risk retained by the ceding company called "**Line** OR **Retention**"
- The portion that is reinsured is called the "**Cession**".

Cedant: Insurance company placing the risk
Reinsurer: Company that accepts that part of the risk.

Reasons for Reinsurance:

1. Enlarged the Ceding Company's financial capacity to accept risk.
2. Stabilises profits and evens out losses.
3. Reduces the Ceding Company's reserve requirements.
4. Offers a way for an insurer to retire from underwriting a given segment of its insurance business.

Two classes of reinsurance:

1. Proportional (Participating): Reinsurer pays a **fixed percentage** of total claims.
   - Quota Share Treaty: Agreement whereby the cedant is bound to cede and the reinsurer is bound to accept a **fixed portion of every risk** underwriten in the class of business to which the treaty relates.
   - Surplus Treaty: Only the amount of excess of the cedant's normal capacity for a particular risk is ceded to the reinsurer. Not a fixed portion of every risk.
2. Non-Proportional (Non-Participating): Reinsurer pays only losses **above an agreed amount**.
   - Stop-loss Reinsurance:
   - Excess-of-loss Reinsurance:
   - Catastrophe Excess-of-loss Reinsurance:

Describe two types of proportional reinsurance:

1. Facultative: **Each risk must be negotiated** with the reinsurer separately, they can **accept or decline** the business.
2. Treaty **All business** which falls within certain parameters can be placed to the treaty without individual authorisation and the **reinsurer must accept**.
   a. Open Treaty: Cedant has to pass details of individual cession to reinsurer.
   b. Blind Treaty: Reinsurer is never advised of individual risk, premium is merely paid over. Based on trust between insurer and reinsurer.

Reasons for quota share reinsurance:

1. New Insurance company who needs significant amounts of reinsurance until it has gained experience and has establish credibility.
2. Existing insurer who branches into a new field of class of business.
3. Following significant losses, this might be the only reinsurance it can negotiate.
4. A way of passing inter-business between subsidiaries.

List the advantages of quota share reinsurance:

1. No selection against the reinsurer, they get a share of all of the accounts.
2. High commission rates for the Cedant
3. Reinsurer will normally make more profit on a quota share treaty because it gets an equal share of good and bad business.

List the disadvantages of quota share reinsurance:

1. Cedant has no choice but to cede business which it could have normally kept for its own account.
2. Cedant can only put those risks that fall within the parameters of the treaty to the treaty.
3. Cedant has to keep a set percentage, not an amount of any one risk. Lead to high and low exposures.

Explain the operation of a surplus treaty:

- Arrangement whereby **only the amount of excess of the cedant's normal capacity** for a particular risk is **ceded to the reinsurer**, not a fixed portion of every risk.
- The reinsurer base the amount they wish to hold on the net retention of the insurer. Expressed as a number of lines. 9 Line Treaty: The reinsurer is taking 9 times what the insurer is holding.
- **5 Line Treaty**: Normal Retention: R 5 000 / Reinsurer retention: R 25 000 / Gross Retention: R30 000

Distinguish between proportional and non-proportional reinsurance:

- Proportional Reinsurance: Reinsurer pays a **fixed percentage** of total claims.
- Non-Proportional: Reinsurer pays only losses **above an agreed amount**. Layers.

Why are Non-proportional reinsurance so popular?

1. Simple to operate
2. Relatively inexpensive to purchase
3. Allow the reinsurer to charge a specific rate, rather than having to take a proportion of the cedant's original premium.

Explain the operation of a stop-loss reinsurance: normally for classes like 'HAIL'.

- An Insurer tries to protect a certain ***class*** **of business** from **severe fluctuations** in results, where **losses exceed premiums by an unacceptable level** in any one period.

Stop-Loss = PERFECT reinsurance, but very expensive.

Explain excess-of-loss reinsurance:

- Insurer tries to protect an individual risk from **severe fluctuations** in results, where **losses exceed premiums by an unacceptable level** in any one period.

Explain catastrophe excess-of-loss reinsurance:

- On a layered basis. Losses from a SINGLE event.
- Questions: At what point will the reinsurance cover begin? How far will the protection go?
- Amount kept by the cedant before excess of loss = **Priority or the deductable**.
- Amount carried by reinsurer called **security**.

What is meant by "layering" in excess-of-loss reinsurance?

- The insurer must decide how much of the risk he can carry himself and at what point he will need the reinsure's responsibility to begin.
- The Security (Reinsurers portion) will be divided into different layers.
- Premium varies for each layer as reinsurers in the higher level will only have to pay when a very large loss happens.

Advantages of layered reinsurance:

1. Reinsurers are much happier with a defined range of exposure.
2. Cedants are more likely to be able to place cover.
3. As the higher layers are more remote from losses, the premium for the cover will be cheaper.
4. Reinsurers are able to accept larger amounts in these higher layers.

Study unit 07

3 Basic requirements for a claim to be valid:

1. There must be a **Policy in force (and Premium paid)** that covers the item lost or damaged?
2. Is the proximate **cause an insured peril**?
3. Have the policy **terms and conditions been compiled with**?

Define the concept of "proximate Cause":

- Cause of the loss, **dominant cause**.
- In the insurance contract it states the perils that are covered or excluded.
- Insurer is liable only for losses proximately caused by an insured peril.

Explain the operation of "Proximate Cause":

- Risk insured against must actually take place.
- Further damage to the subject-matter due to attempts to minimise a loss already taking place, **is covered**.
- No new act must intervene.
- Last straw case. Original cause will be the proximate cause even though the last straw came from another source.

Explain with whom the burden of proof rests under different circumstances:

- Loss caused by a peril insured against = INSURED must proof
- Cause was included in Exceptions of policy = INSURER must proof
- Only part of the loss came from the exception clause = INSURED must proof

Personal Accident Fund: Policy of c***ompensation*** and not of indemnity (put back in the same fin pos. as before).

Define what "prescription" means: Notification of any occurrence likely to give rise to a claim.

Describe the different prescription periods:

- Normal claims: two years
- Third party claims: three years

Describe the four basic methods of dispute resolution in respect of claims:

1. Negotiation
2. Arbitration
3. Litigation
4. Ombudsman

Define an *ex gratia* payment and why subrogation and contribution do not apply:

- A claim is paid out to the insured *even though* the claim was not covered for technical reasons or where there has been a genuine misunderstanding.
- Subrogation and contribution does not apply since a ex gratia payment is not an indemnity payment.

Define "Average", why it applies, and demonstrate the use of the average calculation:

- When the insured is not insured for the correct amount based on the value of the asset insured, Average will apply whereby the settlement amount will be proportionately paid out based on the sum insured divided by die Value at risk:

$$\frac{\text{Sum Insured}}{\text{Value at risk}} \times \text{Loss} = \text{Settlement}$$

* Average does not apply to policies of compensation, only indemnity policies.

Describe the steps that are taken or may be taken by an insurer after a loss has been settled:

- Post loss survey
- Reduction or deletion of a no claim bonus
- Reinstatement of the sum insured
- Deletion of the lost item

Study Unit 08

Why should be Short Term Insurance Market be regulated?

- To ensure that policies are entered into, executed and enforced in accordance with sound insurance principles and practice in the interest of the parties and the public.

List the various duties of the Short Term Insurer in terms of the Short Term Insurance Act of 1998:

1. Submission of statements and accounts
2. Statement of assets
3. Statement of liabilities
4. Solvency margin regulations
5. Commission rates for intermediaries

Describe the various statements and accounts that have to be submitted:

- Audited annual return, including statements of assets and liabilities **within 4 months.**
- Spreadsheet showing gross and net underwriting results for each main class of business **within 1 month.**
- Copy of a duly audited account or Balance sheet required to be submitted to shareholders in terms of the Companies Act, **within 6 months.**

Describe what the statement of liabilities has to contain:

- Rand value amount of claims outstanding.
- A reserve of the claims incurred but not reported.
- The estimated tax liability.

Explain why a correct claims estimate is important:

- For the insurer to put the sufficient money in reserve so that it can fully meet its liabilities.
- If too high, the money could have been used to expand the business, the loss ratio looks worst than it really is, and it can affect the share price.
- If too low, the insurer is giving false or misleading information to the Registrar as there may not be enough money in the reserve to cover claims.

Explain the importance of premium collection with respect to company assets:

- The insurer’s statement of assets may not include any amount for goodwill
- No premium outstanding for more than 2 months may be included in the asset statement
- If premiums are outstanding, this effects the insurers solvency margin and ability to trade.

Explain the importance of the solvency margin and how it is calculated:

- Solvency margin = Difference between the assets and outstanding liabilities.
- If the Registrar feels that the solvency margin of the company is too low, he can put the company under curatorship. The company’s ability to trade may then be in jeopardy.

Detail the solvency requirements in terms of the Act:

- Insurer must hold assets with a total value not less than its total liabilities PLUS then greater of:
    - R 5 000 000, OR
    - 15% of the greater of
        - its premium income in the previous financial year
        - its premium income in the previous 12 months before the calculation

Explain how VAT applies to premiums and claims, including recovery and third party:

- VAT is payable by each and every vendor (Turnover of R 1 000 000+).
- VAT is payable on commission if the intermediary is registered for VAT.
- VAT is payable on premiums paid to reinsurers.
- NO VAT on premiums or claims to overseas insurers (Lloyds).
- Third Party claims and Recoveries are not subject to VAT.

List short term policies that are exempted from VAT:

- Policies with overseas insurers, Reinsurers.

List examples of statutes governing compulsory forms of insurance:

- Road Accident Fund
- Nuclear Energy Act
- The Prevention and Combating of Pollution of the Sea by Oil Act
- UIF
- Export Credit Insurance Corp.
- Compensation for Occupational Injuries and Diseases Act

List the reasons for compulsory insurance:

1. Provision of funds
2. Easing of the State's burden
3. Public attitude
4. Protection of the insured

Explain some of the differences between state insurance and commercial insurance:

1. Mainly administered by Gov.
2. Rates and contributions may be altered by Gov
3. State can supplement, by way of grants, the amounts paid in contributions
4. State guarantees the solvency of the scheme
5. No underwriting of the risk
6. Often no policies are written, reduces cost
7. In the case of UIF, COID and Road Accident Fund, all persons affected must join

Study Unit 09

Describe the cover available in terms of the various sections of a personal lines policy:

1. Homeowners insurance (Buildings)
   - buildings of the residence
   - Outbuildings + fixates and fittings for which policy holder is responsible as **owner** (not tenant)

2. Householders insurance (Contents)
   - Covers items belonging to the policy holder and his family, excluding business items.
   - Items must be in the building or outbuilding.

3. Motor vehicle insurance:

4. All-risk insurance:
   - Gives cover on a worldwide basis. Policy of exclusions.

5. Personal liability insurance:
   - Compensates the insured for injury or death caused by a violent *external and visible* means as a direct **result of an accident**. Illness not covered.
   - Policy of compensation, not indemnity.

6. Personal accident insurance
   - Indemnify the insured or a member of his family for legal liability the insured incur (away from home).

Why is excess payable: To avoid small claims + gives the insured a reason to take more care and prevent losses.

Explain the difference between a policy in inclusions and a policy of exclusions:

- ***Policy of inclusions***: Any occurrence not specified as a peril is not covered.
  Homeowners + Householders Policies+ Fire Policy
- ***Policy of exclusions***: Any occurrence not specifically excluded is covered.
  All-risk insurance + Personal accident + Personal liability insurance + Asset All-Risk Policy.

Study Unit 10

List the advantages of multiperil policies:

1. One renewal date - Insured does not have to worry about different renewal dates.
2. One Premium – Premium is paid for all the insurance at the same time.
3. Less costly to issue for the insurer.
4. Less chance of overlooking one form of cover.

Standard exceptions to the multiperil policy:
- Loss or damage arising from **war, riot and labour disturbances**.
- Loss or damage arising from the use of **Nuclear materials**.
- Cover for property also covered in terms of Marine Policy.

General conditions to the multiperil policy:

- Policy voidable if there has been misrepresentation or disclosure
- Insured must take all reasonable precautions to prevent a loss
- Any event that may result in a claim must be notified to the insurer immediately. Theft must be reported to the police.
- The contribution condition
- The subrogation condition
- No cover for fraudulent claim
- Insured must enforce his rights against any third party involved
- A cancellation condition.

Different covers available under the multiperil policy:

1. Fire
2. Buildings combined
3. Business interruption
4. Office Premises
5. Accident
6. Liability
7. Public Liability cover
8. Professional Liability cover
9. Business All insurance
10. Goods in transit
11. Money insurance
12. Fidelity guarantee insurance
13. Glass insurance
14. Group Personal Accident insurance
15. Other

List the perils covered under the different sections of the multiperil policy:

- Fire
- Lighting
- Explosions
- Storm, wind, hail, water, snow
- Aircraft & Aerial devices
- Impact by animals, trees or vehicles
- Earthquakes
- Subsidence & Landslides
- Sprinkler leakage
- Malicious damage (deliberate damage by thieves while breaking in)

Exclusions from cover under the different sections of the multiperil policy:

Damage by:

- Earthquakes & Volcanic eruptions
- Damage by explosions or heating/drying process

Define theft from a legal point of view: The act of taking someone's property with the intention of depriving him of it permanently.

Define theft from an insurance point of view: Losses following forcible and violent entry or exit from the premises (Shoplifting not included).

Explain the difference between the legal definition and the cover available in terms of a theft policy:

- There must be forcible and violent entry or exit from the premises.
- A hold up (armed robbery) is included.

Explain what "first-loss-basis" means with respect to theft insurance:

- Insured must decide the amount that thieves will be able to steal before being discovered.
- Insurer covers losses above this amount.
- Depends on Security & Type of goods.

Give examples of what may be covered in terms of a business all-risk policy: (Policy of Exclusions)

- Doctors' bags
- Professional Photographers equipment
- Tools and equipment
- Car radios in Business vehicles
- Two way Radios
- Travellers' samples
- Cellular telephones

Study Unit 11

Types of Motor Policy:

1. Third party only cover: Only covers damage to someone else's vehicle the insurer caused and is liable for. No cover for the vehicle of the insured.
2. Third party, fire and theft: Third party cover + the vehicle of the insured for loss or damage arising from fire, self-ignition, lighting, explosion or theft.
3. Comprehensive cover: Third party cover + Cover for the vehicle of the insured + cover for accidental damage + some medical expenses.

Explain cover in terms of the Road Accident Fund Act 56 of 1996:

- Third Parties are compensated for personal injury claims in which fault or **negligence** is involved in.
- Only covers claims for personal injury, including loss of earnings and support.
- Premium is collected by a levy on motor fuel.

Define the limit of liability under the Act:

- Claims limited to serious injuries.
- No claims for any damage to property can be claimed.
- No cover for vehicles or third party property.
- Loss of income- or support-claim limited to R 160 000.
- Emotional shock from secondary victims excluded.
- No claim from a passenger from the same vehicle that caused the accident.
- Exclusion of claims from the same household for the same accident.

Explain when the limit of liability does not apply:

- When undergoing military service

Define the three basic forms of cover under a motor policy:

1. Third Party Cover (must be a true 3rd party and not be related or employee)
2. Third party, Fire and Theft
3. Comprehensive cover

List the categories of "First amount payable" under a motor policy:

- Basic for every claim
- Where the vehicle does not qualify for a No Claim Bonus
- While being driven by someone under the age of 21.
- While being driven by someone over the age of 21, but under 25.
- While being driven by someone over the age of 25, but under the age of 30.
- While being driven by someone who has had a licence for less than 2 years.
- For Theft if the vehicle is not fitted with a tracking device.
- Hijacking.
- Windscreen excess.

Explain what "cumulative first amount payable" means:

- All first Amounts payable are added together, except for windscreen excess.

List the cover in terms of the Motor Traders' Internal and Motor Traders' External policies:

- Motor Traders' Internal Policy: Covers vehicles while **on the road.**
  Temporarily garaged in the course of a journey.
  Insured's **own vehicles** and those **in his control** are covered.
  No cover when vehicle is at the **insured premises**.

- Motor Traders' External Policy Covers only vehicles damaged **at the premises.**
  Only the Insured's **own vehicles are covered**.
  Cover to **customer's vehicles only** due to **negligenc**e by insured or his employees or **defect in the premises** or plant or machinery.

Rating for Motor Traders Insurance:

EXTERNAL POLICIES

1. Named driver basis – Drivers are named.
2. Trade Plate basis – per motor.
3. Wages basis – rated on annual wages of employees & directors.

INTERNAL POLICIES

1. Size of the insured's premises – amount of floor space.
2. Wage basis - rated on annual wages of employees & directors.

Factors to consider when rating a motor car policy:

1. Cover required – comprehensive?
2. Area
3. Type of car
4. Value of vehicle
5. Use of the vehicle
6. No claim bonus
7. Age of the driver

Factors to consider when rating a commercial vehicle policy:

1. Cover required
2. Area
3. Carry capacity
4. Value
5. Use of vehicle
6. No Claim Bonus

Factors to consider when rating a motor cycle policy:

1. Cover required
2. Are
3. Size of engine
4. Value
5. Type of use

Claim Process – Commercial Vehicles:

1. Insured obtains quotes
2. Assessor sent to panel beater
3. Assessor inspects vehicle + checks quote
4. Vehicle is repaired
5. Insured pay excess
6. Insured signs release form
7. Insured takes vehicle home
8. Panel beater sents claim to insurer
9. Insurer pays Panel beater

Explain what is meant by an "aggregate excess":

- Insured is his own insurer up to a certain limit for all claims
- If claims (added up) exceed the limit, insurer will become liable for claims in the normal way

Study unit 11

List the type of SASRIA coupons available:

1. Material Damage – Risks such as Fire, Glass, Marine, Goods in transit and Money.

2. Contract Work / Construction Plant – Engineering type risks.

3. Consequential Loss – Business interruption, but net profit cannot be insured, Only standing charges.

4. Motor policy – All motor types

5. Mining risk

6. Money Risk

Explain which SASRIA covers require an underlying policy:

- All the coupons except Motor Cover.

Explain which SASRIA covers do not require an underlying policy:

- Motor Cover do not require an underlying policy.

Describe when SASRIA cover may be issued:

- When the interest of the insured in the property ceases.

Define who are not covered in terms of the COID Act of 1993:

- People undergoing military service or training.
- SAPS and Defence Force members on active service.
- Contractors.
- Domestic employees.

List the types of cover available in the engineering department:

- Machinery breakdown
- Business interruption following machine breakdown
- Contract works (roads, buildings)
- Project delays resulting from contract work accident
- Plant All Risk (Earth moving equipment being used as a tool of trade)
- Dismantling, transit and erection of machinery
- Computer and electronic equipment
- Deterioration of stock in cold rooms, due to failure of the machinery or electrical supply or by contamination by the refrigerant gas.

Explain the concept and scope of construction insurance:

- Construction insurance is not cancellable.
- is an All Risk Cover and caters for physical loss or damage in transit by road during the period of Construction and up to 12 months after completion of the project.
- Only for the truly unexpected loss or damage, not the expected loss or damage like expected rain.

List the types of policies issued for marine insurance:

1. Hull insurance: Vessels itself + third party liability.
2. Cargo insurance: Loss or damage to the goods carried.
3. Freight insurance: Loss of charges for carrying the goods, as a result of accident to the goods along the way.
4. Small craft policies: Small vessels used for private pleasure purposes only.

List the cover that may be arranged in aviation insurance (mostly written through Lloyds):

1. Aircraft Hull
2. Liability to passengers
3. Liability to other people
4. Cargo the aircraft transports, unless under a Marine Policy.

Explain "bank assurance":

Domestic and small commercial insurance offered by Banks.

Explain group scheme business:

Benefits include: Preferential rates & Wider Cover.

Disadvantages: Claims experience is measured by the **whole group** and **not as an individual**.

List the cover available under travel policies:

1. Medical expenses
2. Cancellation
3. Personal liability
4. Death / Permanent disability
5. Hijack
6. Hospital cover
7. Travel delay
8. Baggage and Baggage delay
9. Cash and Documents

Study Unit 13

Risk Financing: Arranging a source of finance to provide for the fortuitous losses of a business.

3 Types of losses:

- ***Type 01:*** Stable over time.
  No disturbing effect on company's finances.
  Small in size. Predictable. High in Frequency.
  Self Funded through Operating expenses.

- ***Type 02***: Bigger losses that the Company can still carry within one year and remain a going concern.
  Medium is size. Somewhat predictable.
  Self Funded through a Fund.

- ***Type 03***: Large losses. Not predictable.
  Finance through Insurance.

Risk Aversion: Avoiding Risk beyond the expected limited risks.

Which risks can be Self-funded?

Type 01 Risks. Small in size + High in Frequency.

List the advantages of self-funding:

1. Reduce Insurance cost through participation:
   - Proportional (10% of every loss) = Co-insurance
   - Non-Proportional (Insured pays an agreed amount with every claim)

   * Insured's share of the loss = Deductable or Excess.
2. To improve Cash flow
3. To provide the opportunity to earn investment income
4. To increase the scope of risks funded – Wider range of risks.
5. Reduce agent commission and premium taxes.
6. Control over the claims process.

Disadvantages of self-funding:

1. Expose the company to Catastrophic Loss.
2. Losses may vary considerably from one year to the other.
3. Insurer services are lost.
4. Adverse employee and public relations may arise from adjusting losses.

Study Unit 14

Financial factors to consider to determine a company's ability to absorb losses:

1. Working Capital – Liquidity of a company
2. Total Assets
3. Earnings
4. Earnings per share
5. Sales

- All depends on Risk Aversion of Management.

Determine how much self funding a company can afford:

- 1-25 % of Net Working Capital
- 1-5% of Total Assets
- 1-3% of current year's earnings + 1-3% of preceding 5 years pre-tax earnings
- 10-15% of Earning per share
- 0.5 – 2% of Sales / Turnover

Study Unit 15

Risk retention: A company intentionally or unintentionally decides to retain the financial consequences of losses for its own account.
Funded retention – A special fund is created to finance these losses.
Unfunded retention – Losses are funded from cash flow.

Deductable (excess): Part of an insured loss a company retains for its own account.

An Extensive deductable program may offer the following advantages:

1. Administrative duties are still provided for by the insurer (compared to a captive).
2. Cash-flow benefits: Discount on the full premium cost to the insured in return for the insured's contribution to the cost of a loss (Deductible)
3. Cash-Flow protection: Using a deductible places a ceiling on the amount the company has to contribute to settle each loss, and reduces the disruption of cash flows.

Describe the different types of deductibles:

1. Straight Deductibles: Applied to each loss.
   Subtracted before a loss payment is made.
2. Aggregate Deductibles: Applies for an entire year.
   Insured absorbs all losses until the deductible level is reached.
   Insurer pays for all the losses over the specified amount.
3. Disappearing deductible: Size of the deductible decreases as the size of the loss increases until the deductible completely disappears.
   Losses are adjusted in terms of a formula**: P = (L-D) x (1+R)**
   P = Payment by insurer
   L = Loss
   D = Deductible
   R = Recapture factor
4. Franchise deductible: Percentage of value OR in rands
   No liability on the part of the insurer unless the loss exceeds the stated amount. When the loss exceeds this amount, however, the insurer must pay the entire claim. Common with insurance for ships and their cargo.

Determine the most cost-effective deductible level:

- The least-cost Rule: Cost of pure , event risk to a company = insurance premium + cost of losses retained in terms of deductible.
  TEC = P +qD
  P = Insurance premium
  D = Deductible level
  q = Average annual frequency of loss occurrences for the exposure

  $$q = \frac{\text{Annual number of incidents}}{\text{Annual average number of vehicles}}$$

Describe contingency risk policies: Client's premium is placed in a fund which is used to reimburse the insurer for losses paid within the deductible layer.
The fund earns interest at a predetermined rate and at the end of the contract, any excess is returned to the insured.

Study unit 16

Explain " a Captive": An insurance or reinsurance company which is owned or controlled by a noninsurance company and which is established to insure or reinsure the risk of its parent company or affiliated companies.

Explain how a captive works: Captives function like commercial insurers – insure, reinsure and invest funds.
Primary difference: A Captive concentrates on the risk of the parent company.

Two Arrangements exist:

1. Direct method: Premiums are remitted directly to the captive who retains a portion according to the liability it decides to carry, and cedes or reinsurers the remainder
2. Indirect method: Risks are directly insured with a conventional commercial insurer who then, by specific agreement, reinsures all or some of the risk with the captive.
   Process/arrangement called **"Fronting".**
   Reasons for fronting: where the captive is unable to get a licence.

Reasons for establishing a Captive:

1. If owner believes that his own losses are likely to be less than conventional insurers' calculations of premium rates demonstrate, the owner must self-insure to get a payback for his risk control expenditure.
2. Owner can invest premiums and the return on investment should cover the administrative cost.
3. Avoid premium fluctuations that are due to noninsurance factors such as investment income or interest rates.
4. To eliminate inadequate or incorrectly designed cover + unacceptable exclusions.
5. Cash Flow – No upfront premiums will have to be paid. Company can earn investment income.
6. Interpretation – Interpretation of policy wording and timing becomes internal decisions.
7. Cost – Size and cost of administration is directly controlled. Sales and marketing function fall away.
8. Size and Nature of business of captive often enable direct access to reinsurance markets. Reinsurance commission falls away.
9. Tax free or nominal tax situations in some countries (Bermuda) so that captives are able to build up reserves faster.
10. Expertise regarding owning and managing captives can be acquired fairly economically.

A basic feasibility study for setting up a captive will be based on:

- An effective and appropriate **risk control programme** must be in place and must have prove statistically to produce a better than average loss experience.
- The above mentioned statistics must be **available for at least a three-year period**.
- A detailed analysis is required of the characteristics of the various risks to which the company is exposed and of unsatisfactory features of existing insurance arrangements **to decide** about the **nature and limit of risks to be insured** in order to determine the equity capital and the premium income needs.
- The required **capital** of the captive will be **based on rate of return expected on capital invested** and the net retained risk and net retained premiums to be received.
- **Projection of premium and claims, cash flow, investment income and net operating profit.**

Describe a rent-a-captive company:

- An insurance company established by a corporate owner to insure the risks of unrelated organisations (lessees) with the express purpose of returning underwriting profits and investment income to the lessees.
- Rent-a-captive owners earn their income from management fees and rental paid by the participants.

List the relative advantages of a rent-a-captive company:

1. Ability to **recapture underwriting profits** and investment income without having to establish and manage your own captive.
2. Offers **flexibility** to an insured who needs only a short-term specific insurance cover.
3. **Costs are lower** than wholly-owned captives.
4. Small-premium-participants may **receive the benefit of the pooled investment returns**.
5. **No initial capital** might be required.
6. **Faster participation** than with a wholly-owned captive.

Study unit 17

Explain Finite Risk insurance: Alternative risk-financing technique combining insurance and self-funding, with emphasis on the time value of money.
Captive arranges *finite risk insurance* programs with reinsurers.

How do Finite Risk insurance differs from Conventional insurance?

Finite Insurance	***Conventional Insurance***
- Multiyear contracts	- Normally one year only
- Insurer's exposure is limited	- Usually unlimited
- Higher premiums	- Lower premiums
- Substantial return of premiums if the loss in terms of the contract is lower than expected.	- Possible No Claim Bonus

Major types of finite products:

1. Loss Portfolio Transfers (LPTs): Focus on timing risk.
2. Adverse development covers (ADCs): Cover cedents losses of the past + increase corporate value.
3. Finite Quota Shares (FQSs): Smooth the underwriting results of the insured.
4. Spread Loss Treaties (SLTs) Losses are distributed over a multi-year period.
5. The guaranteed cost approach Fixed premium is established prior to the policy's effective date.
6. Retrospectively rated programmes: (retro-rated programmes) Premium based on the insured's actual loss experience

Describe the capital market instruments that are used in the funding of catastrophic-type risk:

1. Catastrophe bonds (CAT BONDS):
   - Returns based on insurance events, rather than financial events.
2. Insurance derivatives:
   - Hedge by purchasing catastrophe futures. If the unexpected catastrophe occurs, the value of the index will rise. This will help offset the unexpected cost of losses.
3. Catastrophe Risk Exchange (Catex):
   - Electronic system for trading risk. A trader can swop California earthquake risk for Florida hurricane risk. Allow insurers and reinsurers to diversify their portfolios.
4. Catastrophic-event-triggered equity put:
   - Buy a put option. When the catastrophic event happens, the put holder sells equity instruments to the institution who sold the put. This will restore shareholders' equity and financial leverage ratios. The sale of the put ensures a much needed supply of standby capital after the catastrophic event.

***** Go through all the questions at the back of each study unit in the study guide as well as the short and essay questions at the back of each chapter in the prescribed book.***