LEARNER GUIDE

Unit Standard Title:	**Apply Technical Knowledge and Understanding of Business Insurance**
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Apply technical knowledge and understanding of Business Insurance

Introduction

After completion of this module, you would be able to:

- Analyse the assets of a business to determine the required cover.
- Differentiate between the insurance of assets, liabilities, profits and stock.
- Identify the processes in a business and their related risk.
- Interpret a policy wording for business insurance

Module 1

The assets of a business to determine the required cover

This Module deals with:

- The insurance of buildings with reference to the insurer and type of cover
- The contents or assets covered under business insurance categorised to identify the type of cover applicable to each
- The valuation of assets with reference to the sum insured, average and additional costs

1.1 The insurance of buildings with reference to the insurer and type of cover

- **Buildings Combined Section**

This section of a policy also includes cover for theft of parts of the building, and property owner's liability. Buildings combined is meant for buildings in less hazardous occupation, such as flats, offices, schools, professional rooms, hospitals and medical suites, museums, art galleries, and libraries. Sometimes a special form of policy is used for sectional title developments.

Insurers will have an underwriting guide specifying the full list of occupations for which they are prepared to give 'Combined' cover. Some buildings are occupied partly as shops and partly as flats or offices. Ideally, the commercial section should form a separate fire risk, but this is no longer generally true.

A survey should be done to determine the degree of commercial exposure and the terms on which the insurer is prepared to write the business. The fire perils insured are similar to the fire section, but simplified due to the type of property for which the policy is meant. The section has a similar extension for accidental damage to public supply connections.

Accidental damage to sanitary ware is covered subject to a R250 excess.

- Cover is subject to the pro rata condition of average.
- Water damage does not exclude sprinklers, so there is no need for a sprinkler leakage extension.
- There is automatic cover against loss of rent due to any of the “fire” perils. Rent is calculated on the rent payable or the rental value, immediately before the damage, and is limited to 25% of the sum insured. (Sub-section C).
- If stated in the policy, this includes loss or damage to property within a 10 km radius that prevents or hinders access to the property insured.

Body Corporate Wording

Body Corporate, or Sectional Title developments are increasing in number and the provisions of the Sectional Titles Act need special consideration. Each owner has an interest in his own unit and there is usually a bond in favour of a financial institution. All share in the common property such as boundary walls, entrance development and facilities such as Laundromat and swimming pool.

It is preferable that one policy be issued, in favour of the Body Corporate. A schedule is attached showing the sums insured for the separate units, and for the common property. However, there is nothing to prevent an individual owner from taking out separate insurance on his unit.

1.2 The contents or assets covered under business insurance categorised to identify the type of cover applicable to each

The wording does not form part of a Commercial Multi-peril policy (previously known as Multimark,) and differs from the usual “Combined” section in several important respects.

Defined events

There must be actual physical loss or damage to the insured property. Any special provisions of the Sectional Titles Act do not affect the interpretation of the policy.

Sub-section A Property

The policy includes some additional cover and provisos:

1) Bursting or overflowing of water pipes apparatus or pipes including damage to such apparatus or pipes. This cover is given under domestic “House owners” policies, so is included here.
2) Theft of building fixtures and fittings is covered, except from vacant units or when the entire property is vacant.
3) Accidental breakage or collapse of radio or television aerials or masts is included. This, too, follows the “House owners” practice.
4) Accidental breakage of fixed glass or sanitary ware, but excluding damage of a cosmetic nature.
5) Accidental damage, not exceeding an amount as specified in the policy wording, to swimming pool machinery or borehole motors by:
   a) Crushing or stress from pressure
   b) Sudden electrical or mechanical breakdown
   c) Accidental outside causes, but excluding:

i) the first amount payable of any claim

ii) repair or replacement necessitated by gradually operating causes, or for cosmetic reasons.

(Similar to cover available in domestic policies)

6) Escape of oil from any fixed oil-fired heating installation or connected apparatus. Remember that we are only concerned with damage to the building, which normally includes fitted carpets. The oil itself is not insured - only the resultant damage.

Office Contents

Practice among insurers differs, but generally office contents insurance is suitable for the contents of offices and consulting rooms, but not for those forming part of trade premises. In this module, we are concerned with the fire perils, but the Office contents section also includes some accident and liability cover.

- Pro rata average applies.
- There is a simplified list of fire perils, and sprinkler leakage is not excluded.
- Rent cover is automatic, restricted to the period necessary to make the premises habitable, and to a maximum of 25 % of the sum insured. Cover against prevention of access applies to any premises in the vicinity, damage to which prevents or limits access to the office premises.

There are sections to cover loss or damage to documents, (All risks basis) and increased cost of working.

1.3 The valuation of assets with reference to the sum insured, average and additional costs

Assets

Business's assets are those items, which are used to earn income for the business. They are crucial to the proper functioning of the business and thus need to be insured for protection against theft or damage. The following are some of the assets of a business, which may need to be insured: buildings, equipment, machinery, motor vehicles, stock, and goods in transit, office contents and tools. Costs incurred as a result to damage to or destruction of assets could thus be recovered in the unfortunate event of an accident, crime or natural disaster.

All Risks

Large business corporations find it almost impossible to keep track of schedules of property insured, and are also able to absorb quite large portions of the loss themselves, rather than insure it. They do not take out separate insurance against fire, accidental damage, and so on, but a special policy wording is drawn up.

The cover is based on their overall assets values and includes a wide range of circumstances, with special provisions for certain kinds of assets. The deductibles (first amounts payable) are very large, and might vary between the different divisions of the corporation's business.

The values at risk will run into many millions of Rands, and the business will be shared among a number of insurers.

Average

Average relates to *under insurance,* which is putting an item on cover for less than its real replacement value. It is important to note that here is a vast difference between the usage and application of 'Average' under a Marine policy, and under other short-term insurance policies. Average does not apply to long-term policies in the same way, except as a method of determining the median for any group of people:

- Average age
- Average income
- Average life expectancy

In Marine and other policies, Average has nothing to do with the above definitions. There are a number of uses of the word "Average" in Marine insurance, and these are as noted hereunder:

- Average. Partial loss or damage due to perils insured, a principle of maritime law according to which the owners of ship and cargo share in a loss incurred voluntarily
- General Average Contribution. The proportionate shares of the vessel owner and each of the cargo owners in order to make up the expenditure or sacrifice incurred for the common good.
- General Average Sacrifice. The voluntary destruction of part of the vessel or the cargo, or the deliberate expenditure of funds in time of grave peril, which is successful in avoiding total disaster
- Particular Average. A loss, which falls on the particular property insured, as opposed to a "general average," which is a loss for the account of all interests

In other classes of short-term insurance, the Average condition applies where the sum insured on certain items is too low, according to the New Replacement Value. The Insured is therefore underinsured.

The Average condition does not apply to all classes of insurance, but only to:

- Fire
- Buildings Combined
- Office Contents
- Business Interruption
- Glass
- Business All Risks (in respect of certain items only
- Accidental Damage
- Electronic Equipment
- House Owners (Buildings)
- Household Contents

These classes require that the Insured cover his items insured for their replacement value.

The application of the Average condition causes much confrontation at claim time, because its application is often misunderstood by Insureds. When insuring a building under a Fire policy, for example, the Insured could have several different values that he thinks may be the insured value:

- The price he paid for an item
- The amount he could expect to sell the item for
- The amount he still owes on the item
- Any other valuations such as municipal value.

None of these is correct. He needs to insure for the amount that it will cost to replace the item with brand new material, if it were totally destroyed. The replacement costs must include the amount required to clear away all the rubble from the property as well. Included in the value must be additional charges, such as airfreight costs to bring parts or items in from overseas, if that is where they were originally obtained, the fees payable to expert advisors, such as architects, and engineers, and payment for work done on holidays and weekends.

The reason that the Average condition exists is not just to punish the Insured, but to ensure that all Insured s contribute the correct amount of funding to the pool, based on the actual values at risk. If Insured s could contribute based on any amount at risk, there would be an incorrectly calculated statistical base for charging the premiums and for determining the level of risk of a given insured risk.

You will know which section the average condition applies to: the policy wording says so. If there is no mention of the Average condition, it is not applicable to that section. Classes of business to which the Average condition does not apply are:

- Theft
- Money
- Fidelity
- Goods in Transit
- Business All Risks (for specified items)
- Public Liability
- Stated Benefits
- Group Personal Accident
- Motor
- Personal All Risks

The application of average in cases of underinsurance:
The Average condition, which relates to claims settlement costs states that the Insured, must insure for the replacement value of his items – the costs to rebuild after damage in the exact same format as the item was before a loss, but using new materials. If the Insured does not insure for replacement value (if the sum insured is too low), then he will not be paid in full for damage suffered ,as he did not contribute a fair premium to the insurance pool and is prejudicing other insureds.

Average has two factors in its application:

- If the item is totally destroyed, then insurers will pay the amount of the sum insured. An example would be a building insured for R 1 million, but which costs R 1 5 million to rebuild. Insurers would pay R 1 million, and the Insured would have to find the other R 500 000 himself to replace the building.

- If there is partial damage to an item that is underinsured, then the following formula is applied to the claim settlement:

<u>Sum Insured % X Amount of the loss</u> Replacement Value

Find the percentage amount, which the sum insured, bears to the replacement value.

Multiply this percentage amount by the claim amount and the result will be the settlement amount.

An example would be: The sum insured on an item is R 1 million.

After damage arising to the item from an insured peril, it is found that the replacement value of the item is R 2 million. The sum insured is therefore 50% of the replacement value. If the amount of the claim is R 25 000, the Insured will receive R 12 500 in settlement. (R 25000 X 50% = R 12 500).

Module 2

The insurance of assets, liabilities, profits and stock

This Module deals with:

- The concept of a liability with examples
- The concept of stock with examples
- The concept of profits with examples
- Reasons why profits, stock, liabilities and assets are insured differently from standard insurance with examples

2.1 The concept of a liability with examples

- **Definition of Liability**

Amounts you are legally liable to pay because of injury to other people, or damage to their property. We all have to live, work, and do business with one another. Every person and every business must take proper care that they are not a danger to others because of what they are doing, or because they have not taken proper precautions to prevent loss or injury.

This is important for a Risk Manager to know about, but for this course you are not expected to be an expert. Common sense can often avoid a dangerous situation. Sometimes, a look around the client's premises can show dangers that they have become used to, and simply do not notice any more.

Trades using power-driven machinery, especially cutting machines, are more hazardous than, say, office jobs. Employees become used to the danger and become careless. Road accidents are a major cause of death and injury. Some occupations involve more road travel than others, but most policies are issued on a "24 hour" basis, so that they will cover road accidents and spare-time hobbies, and activities, except those specifically excluded by the policy.

Everyone, and every business, runs the risk of incurring legal liability due to their actions or omissions, or defects in the goods supplied. Members of the public visit the firm's premises, and the firm, through its employees, may be on the premises of others.

Each business is open to its own special types of risk. In America, Mac Donald's fast food chain paid substantial damages to a customer who spilt hot coffee in her lap, and they now print a warning about hot liquids, on their cups. We have not yet reached such extremes, but the courts tend to be sympathetic toward the injured party, court awards are increasing, and our public is becoming more conscious of legal rights.

Even where a potential claim turns out to have no chance of success, the insurer may need to carry out preliminary investigations into what happened, and get legal advice. This is not a legal course, but you need to understand a few of the principles so that you will know what the policy covers.

Legal Principles

- The policy covers amounts for which you are legally liable. (It does not matter whether or not you feel you are responsible).
- You are legally liable to another party; you cannot be liable to yourself.
- Liability arises out of contract, by statute, or in delict.
- Employers can be held liable for the actions of their employees in the scope and course of their employment. This is further explained below.

2.2 The concept of stock with examples

Stock declaration conditions (if stated in the schedule to apply):
The value of stock may vary considerably throughout the year. If the insured takes out cover for the maximum amount, this sum insured will often be more than needed. On the other hand, insuring for the average value at risk will mean there are times of under insurance, and average will be applicable in the event of loss.

The stock declaration conditions can take care of this.

- A provisional premium is charged, calculated on 75 % of the sum insured.
- At the end of each month/quarter (as stated in the schedule) the insured gives the insurer a written declaration of the market value of stock and materials in trade. This must be done within 30 days from the month/quarter end, otherwise the insured is deemed to have declared the full sum insured.
- Claims are settled on the basis of the market value immediately prior to the damage.
- At the end of each period of insurance, the final premium is calculated on the average sum insured, i.e. the total of the values declared or deemed declared, divided by the number of declarations that should have been made, resulting in an additional or a refund premium.
- Up to 50 % of the provisional premium is refundable, so the insured is very unlikely to pay more premium than necessary (unless the required declarations were not made).
- The sum insured is the limit of the insurer's liability, and premium is not receivable on values in excess of this. Any additional premium under the adjustment cannot be more than 1/3 of the provisional premium.
- These specific conditions apply separately to each item to which stock declaration conditions apply.

Example of stock declaration adjustment		
Sum Insured (maximum at risk)		R800 000
Rate, 300%		
Provisional premium R800 000 x 300% x 75%		R 1 800
Monthly declarations:		
January		R800 000
February		R700 000
March		R650 000
April	No declaration, so sum insured used	R800 000
May		R500 000
June		R400 000
July		R550 000
August		R550 000
September		R600 000
October		R700 000
November		R800 000
December	R900 000 but limited to	**R800 000**
Total		**R7 850 000**
Average		**R654 167**
Premium on R654 167 @ 300%		R1 962,50
Provisional premium paid		R1 800,00
Additional premium due		R 162,50

The premium calculation is simple, but there are some additional aspects.

- Insurers and intermediaries should follow up outstanding declarations, and if any declaration exceeds the sum insured they should suggest that this be increased immediately.
- Losses are automatically reinstated. The additional premium for this is separately charged, and does not form part of the declaration adjustment.
- If after the occurrence of damage it is found that the last declaration is less than it should have been, the amount recoverable under the claim is reduced in such proportion as the amount of the declaration bears to the amount that ought to have been declared or to the sum insured, whichever is the lesser amount. This operates cumulatively with average.

The operation of this is best shown by an example.
The calculation is made in two stages:

Last declaration..................................	R 9 000 000
Should be..	R 12 000 000
Loss...	R 5 000 000
Sum insured....................................... .	R 10 000 000

The specific sum insured is R10 000 000, so this is the maximum according to the conditions.

A declaration of R 9 000 000 is 90% of this maximum, so the amount payable is 90% of the loss.

This amount, R 4 500 000, is taken for the calculation of average.

Sum insured: R 10 000 000	x	R 4 500 000
True value: R 12 000 000		
Total claim payment	R 3 750 000	
Insured is own insurer for		R 1 250 000

We can see that this is correct, because the declaration was only 3/4 of the right amount.

2.3 The concept of profits with examples

When a new enterprise is planned or a major expansion to an existing business is decided upon, there is usually a stage when damage or delay affecting the works, key plant and equipment at the premises of the insured or his suppliers, or even in transit, could cause serious financial loss.

The protection of this risk is called advance profits. Payment of any claim does not take place until the date the business would have started, were it not for the damage.

The risks involved might be fire and perils, engineering (accidental damage to plant, including installation and testing risks) and marine and transit. Usually, the various underwriters concerned assess an overall premium, and this is then apportioned in some way between the departments concerned.

- **Business Insurance: What is Loss of Income/Profit Insurance?**

Losses in income can be due to a number of reasons including business interruption, employee theft, bad debts and loss of cash on premises or in transit. It is therefore advisable to consider taking out business insurance, which covers losses in income and /or profit.

2.4 Reasons why profits, stock, liabilities and assets are insured differently from standard insurance with examples

- **Contract**

Parties are free to enter into contracts as long as these are not illegal, or against public policy and good morals. For example, we cannot issue an insurance contract indemnifying someone against the risk of speeding fines.

To a large extent, the parties to the contract can agree on their own terms, and there can be contractual liabilities exceeding those imposed by the common law. For this reason, liability policies usually exclude liability under contract, unless it would have arisen anyway, under common law.

- **Statute**

Some duties and penalties are imposed by statute, e.g. under the Occupational Health and Safety Act. Failure to comply results in a criminal charge. We can cover defence costs against this, but if the defence does not succeed we cannot indemnify the insured against the fines and penalties laid down by the State. Sometimes the statutory remedy and penalty is the only one. In other cases, a statutory offence also provides grounds for a separate civil action under delict.

- **Delict**

We all have a general legal duty not to harm the person or property of others by our action or neglect. The wronged party (plaintiff) brings a civil action against the party (defendant) that caused his loss or injury. To succeed in this, the plaintiff must be able to show that there was:

- a wrongful act or omission (intentional or negligent) by the defendant
- a link (causal nexus) between this and the loss or damage
- a loss (harm) that can be expressed in terms of money (patrimonial loss).

The court must then consider whether or not the harm that resulted could reasonably have been foreseen and avoided by a normally prudent person in the position of the defendant. (The forseeability test and the reasonable man test).

If it finds the defendant responsible, the court awards the plaintiff compensation (damages) to be paid by the defendant. “Damages” include consequential loss. Often there is no need to go to court; settlement is negotiated by the parties concerned.

- **Vicarious liability**

Usually, one person cannot be held liable for the actions of another, but an employer can be held liable for the actions of employees, arising out of the scope and course of their employment. This even includes actions forbidden by the employer, if they are still connected to the general character of the employee’s work.

- **Defenses**

If any of the above elements (an act or omission that can be directly linked to a loss or harm), can be shown to be missing, there is no case to answer. For example, the defendant may be able to prove that there no negligence, or show that the act was actually committed by some other person altogether.

The following are some other possible forms of defense:

1. **Contractual exclusions**

   Contracts usually attempt to exclude some forms of liability. We have all seen notices at entrances saying “vehicles are parked at owner’s risk”, “swimming is dangerous”, “paving slippery when wet”, or there may be clauses in the agreements we sign.

   These “disclaimers” do not work in every case, because further precautions may be needed.

2. **Apportionment of damages**

   The plaintiff might be partially to blame for the accident. This will reduce the amount of the damages awarded against the defendant.

3. **Capacity**
Children, especially those under seven years old, are regarded by the law as unable to understand the consequences of their acts. The same might apply to someone who is mentally deficient.

4. **Private defense**
You may defend yourself, your family and property. This must be reasonable in the circumstances.

5. **Necessity**
To prevent harm. As an example, A breaks down the door of B's burning house to rescue C, trapped inside.

6. **Inevitable accident and Act of God (vis major)**
The accident or loss could not have been prevented by any reasonable precautions.

7. **Consent**
The legal term is *volenti non fit injuria* - "a willing person is not harmed". The courts will not easily agree that a person consented to harm or the risk of harm, you must be able to show that this was understood and agreed to.

2.4.1 The Purpose of Liability Insurance

Liability insurance is meant to indemnify the insured against civil claims arising from the unintended or unexpected consequences of their actions (or neglect), together with the associated legal charges and expenses.

This will be further explained when we look at the policy wording. Now that you know the main principles and have studied the general public liability wording, the liability cover provided by other sections of the Commercial Multi-peril policy wording, is easily explained. There are also some specialist forms of cover not provided by Commercial Multi-peril policy wording, and you should have an idea of these.

Buildings Combined Section
Because this section covers buildings, it has a liability sub-section covering liabilities in, on, or about the property insured, and arising from the ownership thereof, up to a limit of R1 000 000.

The owner of a building and the land on which it stands has a responsibility to maintain it in a reasonably safe condition. Claims commonly arise from defects such as faulty stairways and railings, or people slipping and falling in the passages, but there could also be damage to other peoples' property. (The relationship with tenants depends on the terms of the lease agreement, but this does not apply to visitors and their property).

An insured whose only business is the ownership of a building insured under the combined section will not need a general public liability cover, unless it is felt that the R1m limit is not enough.

The Multimark policy has a provision stating that the insurers will not be liable for the same happening under more than one section of the policy. This means that the indemnity limit under Buildings combined and that under a public liability section would not be cumulative.

Office Contents Section
There are special sub-sections available to cover loss or damage to documents, the insured's own or belonging to clients, at the office, and legal liability as a direct consequence of this. Liability under contract is excluded, so the cover is against liability arising in delict.

People entrusted with temporary possession of the property of others are liable to compensate the owner for loss or damage to the property. They can avoid liability if they can prove that they took all reasonable care in the circumstances, and the damage occurred in spite of this.

Employer's Liability Section
Under the previous Workmen's Compensation Act, "workmen" were defined as those earning less than a specified annual rate. These employees could claim compensation for occupational injuries and illness from the Workmen's Compensation Fund, so were not allowed to sue their employer.

The Employers' liability section provided cover on claims made basis for liability for occupational injury to employees who were non-workmen. The Occupational Injuries and Diseases Act, which came into operation on 1st March 1994, changed this. Almost all employees fall under the terms of the new Act.

2.4.2 Exceptions / Exclusions

The only exceptions are:

- People such as police and defence force personnel and trainees, (who fall under the Police Act or the Defence Act)
- Independent contractors (people who contract to carry out work, and hire other people to work under them).
- Domestic employees in a private household. (Household and/or personal liability policies provide cover against possible claims.)

In South Africa, the need for Employers' liability falls away, except as a kind of contingency cover.

2.4.3 Professional Liability

The Commercial Multi-peril Liability section, and similar forms of general liability cover, excludes advice or treatment of a professional nature. Apart from this, claims for professional negligence do not always involve accidental injury, or damage to tangible property, so a special form of policy wording is needed.

Nowadays, any business where advice or service is given needs professional liability cover. *Apart from the recognised professions, think of:*

- translators - wrong translation in a technical brochure
- information technology - infringement of copyright, delayed delivery, viruses
- advertising and marketing - mistakes in publicity material.

2.4.4 Directors and Officers' Liability

Some duties are imposed by statute, and there is a general common law duty to exercise the skill and care that would normally be expected. A special form of policy protects the directors and officers in their personal capacity, in circumstances where they cannot claim from the company, and the company itself, where it is required or allowed to indemnify directors.

- **Libel Policies**

A"libel" is a published false statement damaging a person's reputation. In South African law, both written and spoken publication of this kind is called "defamation". The optional extension to the Multimark policy provides for ordinary circumstances, but publishers of newspapers and periodicals, and others with large potential exposures, need a special policy with a much higher limit of indemnity.

- **Construction Risks**

The risks involved in demolition, excavation and construction are insured by companies that specialize in this field.

- **Product Recall**

Product liability cover operates only in respect of the damage or injury actually caused by the defective product. Product recall insurance is to cover the cost of retrieving products considered or suspected to be dangerous from the market place, before harm, or further harm, can result.

We often read that a particular model of car has been recalled for modifications. Other examples include Perrier (mineral water suspected of being contaminated), Tylenol (pharmaceutical tampered with), and Coca-Cola in Belgium (cans contaminated).

There are expert underwriters specializing in this business, and now cover can also be bought for:

- extortion (somebody threatens to sabotage the product)
- loss of profit due to the recall
- loss of market share, and loss of image
- the cost of the product itself.

- **Pollution and Environmental Impairment (EIL)**

There are social and legal problems associated with pollution. There is stricter legislation than in the past, and the general concept that the "polluter pays". Pollution is not always "sudden and accidental", as provided in the ordinary liability wording.

A wider form of insurance protection is known as environmental impairment liability, or EIL. This is intended for normal injury or property damage claims as well as impairment or interference with any other right or amenity protected by law, but is not meant to cover deliberate pollution.

- **Vehicle Risks**

Cover is available in the Motor, Aviation and Marine markets against liabilities arising from the use or operation of land, sea, and air vehicles, including aircraft hangars and private landing strips.

- **SASRIA**

SASRIA cover does not apply to liability insurance. Liability policies contain“war” exclusion, different from the “riot” exclusion that applies to other sections. There is no cover for injury, damage or liability directly or indirectly caused by, related to, or in consequence of war invasion act of foreign enemy, hostilities (whether war be declared or not), civil war mutiny, insurrection, rebellion, revolution, or military or usurped power.

Module 3

The processes in a business and their related risk

This Module deals with:
- The processes in a selected business analysed to determine the type of business risk
- Reasons why some industries or businesses constitute a high risk with examples

3.1 The processes in a selected business analysed to determine the type of business risk

The matter of financial interest applies in short-term insurance where physical property or finances forms the risk, such as:
- Buildings
- Plant and Machinery
- Rental (receivable or payable)
- Motor vehicles
- Money
- Stock and Contents
- Computer Equipment
- Glass

Even in respect of Liability claims, if the third party cannot prove that damage that is measurable financially has been caused, there is no benefit payable under a policy.

In terms of Personal Accident and life policies, remember that financial loss does not have to be proved. An Insured can choose a limit in respect of certain benefits (according to the affordability thereof) and obtain benefits if an occurrence covered by the policy anises.

An example would be an Insured who selects a permanent disability benefit based on R 100 000 in respect of accident cover. If he loses a hand, and the policy determines that injury to attract benefits of 100%, he will receive R 100 000 for that accident, even though he may have been unemployed at the time of the accident. He des not have to prove he is R 100 000 worse off as a result of the accident.

Three case studies to determine whether there is insurable risk:
There is a difference between ***undesirable*** risks and ***uninsurable*** risks, and it is important to recognise what the difference is. Uninsurable risks are those risks that:
- Have no financial measurement attached, where the subject matter of the insurance is a physical entity.
- Are against the law or are against public policy
- Have no statistical base or pooling arrangement that can be used to determine the type of risk
- Will inevitably lead to loss or damage

- Are speculative risks?
- Have such massive financial potential that insurers would not be able to cope with losses, even with generous support from reinsurers
- Have specific exclusions of cover in respect of these arising
- Require a premium so large to protect the interests of insurers that the price becomes unaffordable.

The types of risks illustrated above may all be perfectly acceptable as far as protections go, and there may even be a very low loss history attached to them. Nevertheless, they remain uninsurable for the various reasons already outlined.

Undesirable risks, on the other hand, are those that generally conform to the rules of 'insurability' such as them:

- Arise fortuitously (by accident)
- Are pure risks
- Have enough of a spread of risk to provide statistical records about the risk
- Are financially measurable
- Have an insurable interest on the part of the Insured
- Can be met by funding from risk pooling and reinsurance

However, they may need a specific risk management plan put in place to improve the risk to the extent that it becomes more attractive to insurers.

Some methods of changing undesirable risks into desirable ones are:

- Improving housekeeping at the premises
- Regular servicing and maintenance of the machinery and equipment
- Stacking and storage in acceptable ways that will reduce the chance of a loss arising
- Proper focus on methods of operation
- Installation of fire and theft protection mechanisms
- Training of staff and labour to perform tasks better
- Compliance with legal and insurance requirements in terms of the occupation
- The removal of physical hazards from the workplace
- A sharing of the responsibilities for risk control and elimination
- Adherence to general rules of cleanliness and tidiness

3.2 Reasons why some industries or businesses constitute a high risk with examples

<u>Types of risks that will never be insured:</u>

These risks are those that:

- Have no financial measurement attached, where the subject matter of the insurance is a physical entity.
- Are against the law or are against public policy
- Have no statistical base or pooling arrangement that can be used to determine the type of risk
- Will inevitably lead to loss or damage
- Are speculative risks

- Have such massive financial potential that insurers would not be able to cope with losses, even with generous support from reinsurers
- Have specific exclusions of cover in respect of these arising
- Require a premium so large to protect the interests of insurers that the price becomes unaffordable.

Insurance is a method of transferring risk, but it does not make the risk go away. This is just as well, because if we were able to make risks disappear, there we would be no need for risk transfer, and therefore no need for insurance.

Some of the ways to reduce these uninsurable risks may be to:

- Break down component values so that each part of a risk is smaller in terms of financial potential
- Put in place advanced and sophisticated levels of protection so that the inevitability of loss becomes more manageable
- Participate in a public fund that raises community awareness and funding for fundamental risks
- Transfer the risk to competitors, where possible
- Dispose of the items that are at risk, and so dispose of the risks themselves

The following Risks are uninsurable:

- War. The SA government operates a War Damages Fund, as the potential for damage is too great for insurers to bear, even with reinsurance support. Also, insurers feel that wars can be caused over the specific holding of certain values by a government, which may not even be acceptable to the majority of the populace. According to current affairs magazines and programmes the popularity of US President George W Bush is at its lowest level ever. Yet he saw fit to enter a war against Iraq. Insurers are aware that political will can have a major impact on the extent of risks, particularly Fundamental Risks
- Nuclear Risks. Again the potential damage from a nuclear accident or explosion could be enormous, with clean up costs and pollution as well as material damage to property and costs for death of civilians running into billions of Rands. Nuclear risks are also potentially tied in with War risks, for obvious reasons.
- Terrorism. This is excluded under most standard material damage policies in South Africa, and cover is offered by the State.

Module 4

Interpret a policy wording for business insurance

This Module deals with:

- A policy document and schedule analysed to determine the cover
- Exclusions in the policy with reference to the specific risks in a selected business
- Optional covers and extensions with reference to a specific business
- The terms and conditions of a policy interpreted for a specific business

Aspects common to all sections of the Commercial Multi-peril policy are grouped together, to avoid repetition. The individual sections then have their own "defined events" against which cover is given, and their specific extensions and exceptions.

There is a main, typed schedule giving the details that apply to the individual insured, and further schedules with the specific descriptions and sums insured/limits for the separate sections of cover.

- **The Main Schedule**

Usually, this includes the following important details.

(i) **Insurer's identification**: The name of the insurer and a physical address to which correspondence can be delivered and legal notices can be served. Only registered insurers (including Lloyd's underwriters) are allowed to carry on insurance business.

(ii) **Insured's name, title and address**: The policy is a legal document, and these details must be correct. The insured might be an individual, a partnership, a close corporation, or a company, and there might be insurable interest other than as owner, e.g. as trustee or bondholder.

(iii) **Territorial limits**: The area in which the cover will apply. (The various sections also have their own territorial limits).

(iv) **The business of the insured**: This must be correctly and fully stated, because it affects the nature of the insured risk - manufacturer, distributor, retailer, property owner, and so on.

(v) **Period of insurance and renewal/anniversary date**.

(vi) **Attestation**: Here, or elsewhere in the document, the policy is signed by authority of the insurer.

- **The Operative Clause**

The insurer agrees:

- if the premium has been paid when it was due, (late payments are accepted at the option of the insurer)
- subject to the terms, exceptions and conditions of the policy
- to indemnify or compensate the insured (there must be some kind of loss)
- if the events insured against occur
- during the period of insurance (some sections like Fidelity and Liability, have special provisions)

- but not exceeding the sum insured or policy limit.

At the option of the insurer (not at the insured's choice) **indemnity** can be by payment, replacement, reinstatement, or repair. **Compensation**, applicable to personal accident insurance, is by payment only.

- **General Exceptions**

Grouping together the exceptions and conditions applicable to most sections of the policy saves repetition, but you must remember these when studying the rest of the policy wording.

1 (A) The Riot

This refers to loss or damage to **property** related to or caused by any of a long list of events, mainly related to riot, strike, public disorder, and warlike operations of any kind. War is a national concern, where Government becomes involved, but for other kinds of disorder, political or non-political, cover is usually available from SASRIA (South Africa) or NASRIA (Namibia), and in other ways.

1 (B) War Damage

The policy also excludes loss or damage caused directly or indirectly by any occurrence for which a fund has been established in terms of the South African War Damage and Compensation Act, or similar Acts in other territories.

2 The Nuclear Exclusion

The policy does not cover any loss of, or destruction or damage to property, any consequential loss, or any legal liability arising from radiation contamination by nuclear fuel, nuclear waste from the combustion of nuclear fuel, or nuclear weapons material. This is because no one insurer could carry such a large risk.

Remember that other sources of radiation, such as radioisotopes, particle accelerators, X-ray apparatus and lasers, are in use in industry, medicine and research. The exclusion does not apply to these. Such risks must be carefully considered, but can be underwritten in the ordinary material damage and liability policies.

- **General Conditions**

Many of these modify or reinforce the position at common law, so that there is less chance of disputes developing.

1. **Misrepresentation**, misdescription and non-disclosure of material particulars renders the particular section or item **voidable** at the insurer's discretion.

2. **Other insurance -** the policy will pay only its ratable share of the loss, in other words, the insured himself must also claim from each of the other policies, (rather than claim from only one, and then leave the insurers to sort out contribution between themselves). Also provides for the "importation" of average, where this does not already apply to both policies.

   2 (a) **Cancellation -** immediately, by the insured (normal short period or minimum premium may be charged) or on 30 days' notice by the insurer, subject to a pro rata refund.

2 (b) Continuation of cover - if premium is paid by debit order, the insurance automatically lapses if the debit order is not met, unless it can be shown that this was due to an error by the bank. The condition makes provision for monthly, quarterly, half-yearly or annual premium payments.

3. Premium adjustment - annual adjustment of premium on some sections of the policy, based on the insured's declarations.

4. Prevention of loss. The insured cannot be expected to prevent all losses (there would be no point in having the insurance), but the precautions and action taken must be reasonable in the circumstances.

5. Claims.

(a) As soon as reasonably possible, the insured must give notice of any event that may result in a claim. This is especially important in connection with liability risks, or where the insurer might want to insist on extra precautions.

If a **claim** then results, the insured must, as soon as possible:

- submit full details in writing
- provide the required proof and documentation, and immediately forward any third party claim or summons to the insurer to deal with
- in case of theft, notify the police, and cooperate in trying to recover the stolen property.

(b**)** Insurers cannot allow an unlimited time between the event, and a claim being made. Unless they agree specially, the maximum allowed is 24 months. This limit does not apply to business interruption, fidelity, personal accident/ stated benefits, third party liability and where there is pending legal action, but some sections of the policy have their own special requirements.

(c) If the claim is rejected, the insured has only six months, from the date of repudiation, to start legal action against the insurer. It is not enough to give notice of legal action; the insured must also pursue this to finality.

(d) Insured, if asked to do so, has to assist the insurer in the recovery of lost or stolen property. If he does not do so, he must refund the claim settlement.

6. Company's rights after an event.

(a) (i) Insured cannot abandon property to the insurer, but insurer can take possession of damaged property. They must deal with the property in a reasonable manner; otherwise they can be liable for any further damage that results from their actions.

(ii) Subrogation. Insurer can take over the rights of the insured immediately, and commence recovery against third parties. (In common law, they could do this only after payment of the insured's claim).

(b) Subrogation proceedings will be at the insurer's expense, but the insured must cooperate.

(c) Liability to third parties. This might exceed the limit under the policy, so the insurer has the option of paying the insured the limit of indemnity and withdrawing from the claim.

7. **Fraudulent claims**. Any fraudulent claim is forfeited. This includes those insured who, for example, intentionally set fire to their own property, or arrange to have it set fire to or stolen.

8. **Reinstatement after loss**. Insureds, and even some brokers, do not always understand that payment of a loss generally reduces the available cover, for example, if contents are insured for R60 000 and R20 000 is then lost, only R40 000 is left for later claims during the same period of insurance. If replacement property is bought, the original sum needs to be reinstated. This condition makes this plain, and provides for reinstatement to take place automatically, so that the client is not left with insufficient cover. Normally, an additional premium is due, but insurers often reinstate small losses free of charge.
***Note**: this condition does not apply to Personal Accident/Stated Benefits. Stock declaration conditions under the Fire section, and the Fidelity insurance section have special provisions for reinstatement.*

9. **Breach of conditions**. A breach of conditions affects only the particular section, not the policy as a whole.

10. **No rights to other persons**. Emphasises that the contract of insurance is between the insurer and the insured. No rights are given to any third parties.

11. **Collective insurances**. Some large policies are issued by a panel of insurers, each of them named in the policy together with their percentage. One insurer takes responsibility for the issue and administration of the policy, and is called the "leading insurer" The condition makes provision for this.

- **General Provisions**

Claims preparation costs
Automatically provides 10% of claim, with a maximum of R1 000, for claims preparation costs. This is in addition to any amounts specifically shown in the various sections.

Payments on account
At the insurer's discretion, interim payments may be made to the insured, pending finalisation of a claim.

First amount payable
The policy excess, as it features in some sections of the policy.

Members
If the insured is a close corporation, rather than a company, “member” is used instead of “director”.

Liability under more than one section
This is to guard against accumulation of cover under the different than liability sections, but is not meant to penalise an insured that may have insured the same risk under two policy sections, e.g. rent under Fire as well as under Business Interruption.

Meaning of words
Policy wordings, schedules and endorsements must be read together with one another, and any specific meaning applied throughout. (People who draw up policies have to take care that this does not result in a meaning they did not intend).

Premium payment
Premium is payable on or before the inception date or renewal date. Insurers do not have to accept late payments, this is at their choice.

Holding covered
To form a valid contract, the terms including the premium must be agreed. If insurers are holding covered, they will not reject a claim merely because the premium has not yet been agreed.

Schedule sums insured blank
This makes it very clear that if the sum insured/limit of indemnity is left blank, or shown as ‘nil’ or ‘not applicable’, this means no cover, not “no limit to the cover”.

Security firms
This does not mean that the policy now covers the security firm, but that:
- The insured’s rights under the policy are not prejudiced by entering into the contract required by the security service, and
- If this contract prevents the insured from claiming against the security firm for loss or damage caused by its employees, the insurers will, likewise, not exercise their rights of recourse against this firm.

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