General Principles of Law of Insurance

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Description of Module

Items	Description of Module
Subject Name	Law
Paper Name	Law of Insurance
Module Name /Title	General Principles of Law of Insurance
Module No.	II

General Principles of Law of Insurance

Objective: After reading this module, the learners will have a clear picture of :

The aim of all types of insurance is to make provision against such risks. In this way, life insurance is a social device to share the risk of loss of life.

Learning Outcomes:

It means an agreement in which one party agrees to pay a given sum of money upon the happening of a particular event contingent upon duration of human life in exchange of the payment of a consideration.

MEANING AND DEFINITION

Insurance is a co-operative device to spread the loss caused by a particular risk over a number of persons who are exposed to it and who agree to insure themselves against the risk. The aim of all types of insurance is to make provision against such risks. In this way, life insurance is a social device to share the risk of loss of life. In simple words, it means an agreement in which one party agrees to pay a given sum of money upon the happening of a particular event contingent upon duration of human life in exchange of the payment of a consideration.

Insurer: The person who guarantees the payment is called *Insurer*, the amount given is called *Policy Amount*, the person on whose life the payment is guaranteed is called *Insured* or *Assured*. The particular event on which the payment is guaranteed to be given may be *Death* or *Life*. The consideration is called the *Premium*. The document evidencing the contract is called *Policy*.

"Life insurance contract is a contract whereby a person (insurer) agrees for a consideration (that is payment of a sum of money) or a periodical payment, called the premium to pay to another (insured or his estates) a stated sum of money on happening of an event dependent on human life.

The best explanation of the definition and nature of life insurance contract undoubtedly occurs in the case titled ***Dalby* v. *India and London Life Assurance Company*.** The basic

fact about life insurance recognized in this case is that a contract of life insurance is not a contact of indemnity (against a loss). One of the effects of life insurance not being a contract of indemnity is that on happening of the event insured against the insurer should pay the agreed amount irrespective of whether the assured suffers any loss or not.

The essential features of life insurance can be summed up as under:

(i) It is a contract relating to human life

(ii) The amount is paid at the expiration of certain period or on death of the person.

TYPES OF INSURANCE

The risks which can be insured have increased in number and extent due to the growing difficulty of the present day economic system. Insurance occupied an important place in the modern world.

Generally insurance is divided in to two main branches;

(a) Life insurance.

(b) General Insurance.

a. Marine insurance

b. Fire insurance

c. Motor vehicle insurance

d. Miscellaneous insurance

Utmost good faith

Most commercial contracts are subject to the principle of *caveat emptor* (**let the buyer beware**). Under these contracts, there is no need to disclose information that is not asked for. Insurance contracts are different in that they are based on facts which are within the knowledge of the insured; the law imposes a duty of ***uberrima fides*** or 'utmost good faith'. The principle of utmost good faith requires anyone seeking insurance to disclose all relevant facts. Where material non-disclosure can be proved, a contract can be voided.

Insurable Interest

Interest in the object: The principle of insurable interest states that the person getting insured must have insurable interest in the object of insurance. A person has an insurable interest when the physical existence of the insured object. In simple words, the insured person must suffer some financial loss by the damage of the insured object.

For example: The owner of a taxicab has insurable interest in the taxicab because he is getting income from it. But, if he sells it, he will not have an insurable interest left in that taxicab. From above example, we can conclude that, ownership plays a very crucial role in evaluating insurable interest. Every person has an insurable interest in his own life. A merchant has insurable interest in his business of trading. Similarly, a creditor has insurable interest in his debtor.

The classical definition of insurable interest was given by Lawrence, J., in *Lucena* v. *Craufurd* which is as under:
“The having some relation to, or concern in, the subject of the insurance.

CAUSA PROXIMA:-

More than one causes: Principle of Causa Proxima (a Latin phrase), or in simple English words, the Principle of Proximate (i.e Nearest) Cause, means when a loss is caused by more than one causes, the proximate or the **nearest or the closest cause** should be taken into consideration to decide the liability of the insurer. General Principles and Concepts of Insurance The principle states that to find out whether the insurer is liable for the loss or not, the proximate (closest) and not the remote (farest) must be looked into.

For example: A cargo ship's base was punctured due to rats and so sea water entered and cargo was damaged. Here there are two causes for the damage of the cargo ship - (i) The cargo ship getting punctured beacuse of rats, and (ii) The sea water entering ship through puncture. The risk of sea water is insured but the first cause is not. The nearest cause of damage is sea water which is insured and therefore the insurer must pay the compensation. However, in case of life insurance, the principle of Causa Proxima does not apply. Whatever may be the reason of death (whether a natural death or an unnatural death) the insurer is liable to pay the amount of insurance.

DOCTRINE OF SUBROGATION:-

The doctrine of subrogation is a result to the principle of indemnity and as such applies only to fire and marine insurances. In the case of **Simpson Vs. Thomson 22**, Lord Cairns defined subrogation thus: "a right founded on the well known principle of law that where one person **has agreed to indemnify another,**

Example: the owner of a motorcar having a comprehensive insurance cover, has got two alternative in case of an accident with another car or person (third party) who caused the accident. Firstly, he can claim for the damages from the Insurance Co. or from the **third party.** If the car owner decides to collect compensation from the Insurance Co., his right against the third party is subrogated to the Insurance Co. so that the company can afterwards claim the damages from the third party.

Reinsurance

Two or more insurance companies: Reinsurance is a contract between two or more insurance companies by which a portion of risk of loss is transferred to another insurance company called the reinsurer. Usually, an insurance company insures a profitable venture that comes in its way, even if the risk involved is beyond the capacity. But if at a particular stage it feels that the risk undertaken by

it is **beyond its capacity**, then it may retain the risk which it can bear and transfer the balance.

Under the reinsurance method, if an insurance company receives an insurance proposal worth Rs. 10 crore, where its risk bearing capacity is of Rs. 5 crore only, it has two options either to reject the proposal or to accept it. After accepting the proposal, the insurer can limit his liability by getting re-insured for Rs. 5 crore with another insurer. In case of complete loss the original insurer makes the payment of claim to the insured for Rs. 10 crore and then claims Rs. 5 crore from the re-insurer(s).

Double Insurance

Double insurance refers to the method of getting insurance of **same subject matter with more than one insurer** or with same insurer under different policies. This means that a person may get two or more policies on same subject matter and can claim the amount of all these policies. However, the insured cannot profit from this arrangement because the insurers are legally bound only to share the actual loss in the same proportion in which they share the total premium. It is also called dual insurance. Double insurance is possible in all types of insurance contract. A person can insure his life in different policies for different sums. In life insurance the assured can claim the sum insured with different policies on maturity or to his nominee after his death. This becomes possible in life insurance because life insurance is not indemnity insurance.

Indemnity

Indemnity means guarantee or assurance to put the insured in the same position in which he was immediately prior to the happening of the uncertain event. The insurer undertakes to make good the loss. It is applicable to fire, marine and other general insurance. Under this the insurer agreed to compensate the insured for the actual loss suffered. Indemnity means security, protection and compensation given against damage, loss or injury. According to the principle of indemnity, an insurance contract is signed only for getting protection against unpredicted financial losses arising due to future uncertainties. Insurance contract is not made for making profit else its sole purpose is to give compensation in case of any damage or loss.
In an insurance contract, the amount of compensations paid is in proportion to the incurred losses. The amount of compensations is limited to the amount assured or the actual losses, whichever is less. The compensation must not be less or more than the actual damage.

Compensation is not paid if the specified loss does not happen due to a particular reason during a specific time period. Thus, insurance is only for giving protection against losses and not for making profit. However, in case of life insurance, the principle of indemnity does not apply because the value of human life cannot be measured in terms of money.

Definition of Condition

Certain terms, obligations, and provisions are imposed by the buyer and seller while entering into a contract of sale, which needs to be satisfied, which are commonly known as Conditions. The conditions are indispensable to the objective of the contract. There are two types of conditions, in a contract of sale which are:

Expressed Condition: The conditions which are clearly defined and agreed upon by the parties while entering into the contract.

Implied Condition: The conditions which are not expressly provided, but as per law, some conditions are supposed to be present at the time making the contract. However, these conditions can be waived off through express agreement. Some examples of implied conditions are:

The condition relating to the title of goods.

Condition concerning the quality and fitness of the goods.

Condition as to wholesomeness.

Sale by sample

Sale by description.

Definition of Warranty

A warranty is a guarantee given by the seller to the buyer about the quality, fitness and performance of the product. It is an assurance provided by the manufacturer to the customer that the said facts about the goods are true and at its best. Many times, if the warranty was given, proves false, and the product does not function as described by the seller then remedies as a return or exchange are also available to the buyer i.e. as stated in the contract.

A warranty can be for the lifetime or a limited period. It may be either expressed, i.e., which is specifically defined or implied, which is not explicitly provided but arises according to the nature of sale like:

Warranty related to undisturbed possession of the buyer.

The warranty that the goods are free of any charge.

Disclosure of harmful nature of goods.

Warranty as to quality and fitness.