**B.COM 2ND SEMESTER CBCS (HONORS)**

**(UNDER GAUHATI UNIVERSITY)**

**INSURANCE AND RISK MANAGEMENT**

**COM-GE-2046(B)**

**UNIT – II**

***TOPICS TO BE COVERED UNDER UNIT- II***

* ***CONCEPT OF INSURANCE***
* ***NEED FOR INSURANCE***
* ***GLOBALISATION OF INSURANCE SECTOR***
* ***REINSURANCE AND COINSURANCE***
* ***ASSIGNMENT AND ENDOWMENT***

**CONCEPT OF INSURANCE**

There are no certainties or guarantees in life. There is no [guarantee](https://www.toppr.com/guides/business-laws-cs/indian-contract-act-1872/contract-of-guarantee/) that the business will not suffer an unexpected loss or damages. So while we cannot protect our interests against all risks, we can opt for some insurance. Insurance is defined as a contract, which is called a policy, in which an individual or organization receives financial protection and reimbursement of damages from the insurer or the insurance company. At a very basic level, it is some form of protection from any possible financial losses.

 The basic principle of insurance is that an entity will choose to spend small periodic amounts of [money](https://www.toppr.com/guides/general-awareness/money-and-money-market/introduction-to-money/) against a possibility of a huge unexpected loss. Basically, all the policyholder pools their risks together. Any loss that they suffer will be paid out of their premiums which they pay.

 Thus, a contract of insurance is a contract under which the insurer (i.e. insurance company) in consideration of a sum of money paid by the insured (called the premium) agrees.

i) To make good the loss suffered by the insured against a specific risk (for which the insurance is effected), such as fire or,

ii) To pay a pre-fixed amount to the insured or his/her beneficiaries on the happening of specified event e.g. death of the insured.

**DEFINITION OF INSURANCE**

 According to Oxford English Dictionary insurance is “undertaking, (by a company, society or the state), to provide safeguard against loss, provision against sickness, death, etc., in return for regular payments.”

**SIGNIFICANCE OF INSURANCE**

We can highlight the significance of insurance, in terms of the following advantages offered by it:

**(i) Concentration on Business Issues:** Insurance help businessmen to concentrate their attention on business issues, as their risks are undertaken by the insurance company. Insurance gives them peace of mind. Thus, due to insurance, business efficiency increases.

**(ii) Better Utilization of Capital:** Businessmen, in the absence of insurance, will maintain funds for meeting future contingencies. Insurance does away with this need to maintain contingency funds by them. Thus businessmen can better utilize their funds for business purposes.

**(iii) Promotion of Foreign Trade:** There are many risks in foreign trade much more than involved in home trade. Insurance of risks involved in foreign trade gives a boost to it volume, which is a healthy feature of economic development.

**(iv)Feeling of Security to Dependents:** Life insurance provides a feeling of economic security to the dependents of the insured, on whose life insurance is affected.

**(v) Social Welfare:** Life insurance also provides for policies in respect of education of children, marriage of children etc. Such special policies provide a sense of security to the poor who take these policies. Thus life insurance is a device for ensuring social welfare.

**(vi)Speeding up the Process of Economic Development:** Insurance companies mobilize the savings of community through collection of premiums, and invest these savings in productive channels. This process speeds up economic development. Huge funds at the disposal of LIC (Life Insurance Corporation) available for investment purposes support the above-mentioned point of advantage of insurance.

**(vii) Generation of Employment Opportunities:** Insurance companies provide a lot of employment in the economy. This is due to the ever growing business done by insurance companies.

**NEED FOR INSURANCE**

Insurance plans are beneficial to anyone looking to protect their family, assets/property and themselves from financial risk/losses:

* Insurance plans will help you pay for medical emergencies, hospitalization, contraction of any illnesses and treatment, and medical care required in the future.
* The financial loss to the family due to unfortunate death of the sole earner can be covered by insurance plans. The family can also repay any debts like home loans or other debts which the person insured may have incurred in his/her lifetime.
* Insurance plans will help your family maintain their standard of living in case you are not around in the future. This will help them cover costs of running the household through the insurance lump sum payout. The insurance money will give your family some much needed breathing space along with coverage for all expenditure in case of death/accident/medical emergency of the policy holder.
* Insurance plans will help in protecting the future of your child in terms of his/her education. They will make sure that your children are financially secured while pursuing their dreams and ambitions without any compromises, even when you are not around.
* Many insurance plans come with savings and investment schemes along with regular coverage. These help in building wealth/savings for the future through regular [investments](https://www.iciciprulife.com/investments.html). You pay premiums regularly and a portion of the same goes towards life coverage while the other portion goes towards either a savings plan or investment plan, whichever you choose based on your future goals and needs.
* Insurance helps protect your home in the event of any unforeseen calamity or damage. Your home insurance plan will help you get coverage for damages to your home and pay for the cost of repairs or rebuilding, whichever is needed. If you have coverage for valuables and items inside the house, then you can purchase replacement items with the insurance money.

**GLOBALIZATION OF INSURANCE SECTOR**

There’s no stopping the globalization train. It’s already here and it’s going to go further and wider. How has globalization affected the insurance markets and insurance companies all over the world?

1. **Competition in the Insurance Markets -** First and foremost, local insurance companies started facing more widespread competition – not only from within the country, but also from the region and from international conglomerates. Now, this is great news for the customer. After all, they now have the opportunity to choose from a range of products and services that are best suited to their individual requirements. To sharpen the competitive edge, insurance firms have also tweaked their offerings to make them more tempting. This can range from improving coverage to reducing premiums.

 With competition come greater challenges. Insurance companies now look beyond the local market to acquire customers. In addition to a comprehensive suite of products, they strive to give their brand an international outlook while paying attention to local context and cultural sensitivities.

## ****Growth in Opportunities** -** The thing about globalization is that it has caused other industries to expand as well. This has resulted in a plethora of opportunities for insurance companies. Today, a standard insurance firm doesn’t have to limit itself to a limited number of products or services.

 With globalization, consumers’ demands change and their needs become more varied. There are also more opportunities for wealth creation and preservation. For instance, more organized labor means more healthcare coverage for employees. Wider globalization means more opportunities for overseas investments, and thus more investment-linked plans.

1. **New Industry Trends in Insurance -** Insurance companies are also beginning to experience centralization processes, thanks to partnerships with banks and reinsurance companies, and mergers with smaller or larger competitors. There’s a growth in the type of insurance services and products as well. For instance, we are seeing insurance products for newer risks such as informational risk, political risk, security risks, and even military risks.
2. **Increased Consumer Demand for Insurance -** As more and more foreign insurance companies enter a local insurance market, customers’ awareness tends to grow. Their knowledge of possible insurance and investment plans becomes richer. Needless to say, this creates a demand for more products. Consumers are not willing to make do with what was available anymore. They expect comprehensive coverage plans, low premium rates, and flexible policies.
3. **Increased Customer Satisfaction -** With globalization, there’s a renewed focus on customer satisfaction and trust. As customers get savvier and educated about insurance products, the need to gain their trust and build strong relationships becomes imperative to the top line. In the name of competition, insurance firms are putting in extra effort to provide better products and [clearer communications](https://www.translations.sg/Translations/financial-translation-services-singapore.html) driven towards meeting the expectations of both local and international customers.

## Impact of Globalization of Insurance Sector on India- Opportunities

* Opening up of the sector will ensure a large flow of funds in two ways. More investment will take place in the sector and further through competition
* After the nuclear tests, the government needs to hold out a hand of friendship to the West to achieve aims related to national security. Insurance will be a visible gesture
* From the view point of the capital markets, opening up of the insurance will have a bullish impact
* The biggest benefit will be to the stock market because of the actual investment flowing into infrastructure development
* The opening up of the insurance sector by the Government of India to private and global players

## Impact of Globalization of Insurance Sector on India- Threats

* There is a fear that there will be a flight of capital from India; to ensure against this we should stipulate that capital and dividend repatriation should start only after some years. It is also necessary to ensure that domestic capital raised through premium is not repatriated.
* The other fear is that the foreign insurers will cream the market.
* The biggest fear is ownership that is foreign insurers do not control the management of the insurance company through backdoor.

# REINSURANCE - Reinsurance is the insurance of insurance, where one or more insurance companies agree to indemnify the risk, partially or altogether, for the policy issued by other one or more insurance companies. Reinsurance indicates to the process where the original insurer accepted the risk from the original insured gets the risk covered by another insurer or reinsurer for the same reason the original insured got protection for.

## Q What is Reinsurance or Reassurance?

**Answer** - This means insurance of insurance. The original insurer gets the risk, assumed from the original insured (primary insured), and covered (reinsured) with another insurer (known as reinsurer) for the same reason as the primary insured does. The primary insurer, here, in fact, becomes the insured (known as reinsured) and the person or body or company giving him the protection becomes the insurer (known as reinsurer).

**KEYPOINTS**

* In simple terms reinsurance is insurance for Insurance companies.
* It is a means by which an insurance company can protect itself from risks.
* The company who requests for the cover is called the cedant and the reinsurer is called the ceded.

## Reinsurer or Reassurer – Reinsurer is the person, body or company giving reinsurance cover. They protect the interest of the insurer in case of loss/damage of the property or subject matter insured and for which the insurer is liable under the policy of insurance.

**Co-Insurance -** In [insurance](https://en.wikipedia.org/wiki/Insurance), co-insurance or coinsurance is the splitting or spreading of risk among multiple parties.

## Q What is Coinsurance?

**Answer** - Coinsurance is the amount, generally expressed as a fixed percentage, an insured must pay against a claim after the deductible is satisfied. In health insurance, a coinsurance provision is similar to a co-payment provision, except co-pays require the insured to pay a set amount at the time of the service. Some property insurance policies contain coinsurance provisions.

## Q How Coinsurance Works

**Answer** - One of the most common coinsurance breakdowns is the 80/20 split. Under the terms of an 80/20 coinsurance plan, the insured is responsible for 20% of medical costs, while the insurer pays the remaining 80%. However, these terms only apply after the insured has reached the term's out-of-pocket [deductible](https://www.investopedia.com/terms/d/deductible.asp) amount. Also, most health insurance policies include an out-of-pocket maximum that limits the total amount the insured pays for care in a given period.

## Example of Coinsurance

 Say suppose Raju has taken a health insurance policy with an 80/20 coinsurance provision, Rs 2000 out-of-pocket deductible and Rs 6000 out-of-pocket maximum. Unfortunately, he requires an emergency surgery that cost Rs 10,000. Since he has not yet met with his deductible, he must pay the first Rs 2000 of the bill. After paying Rs 2000 deductible, then he is only responsible for 20% of the remaining bill Rs 8000 (Rs 10000-Rs2000) or Rs 1600. His insurance company will cover 80%, the remaining balance.

**Q State the essential difference between Reinsurance and Coinsurance.**

**Answer** – The differences are as follows:

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| **Reinsurance** | **Coinsurance** |
| Reinsurance is providing insurance for the risk that has been already taken up by an insurance company. | Coinsurance refers to sharing one risk amongst multiple[insurance companies](https://www.wishpolicy.com/insurance-companies/). |
| Under reinsurance, the reinsurer has no direct connection to the policyholder or insured. | Under coinsurance all insurers have a direct connection with the policyholder or insured. |
| In India, reinsurance is a statutory provision to cover all types of insurance under reinsurance. | It is an optional mechanism to different insurers who agrees on mutual agreement because of business connections. |
| Reinsurers are not obliged to pay any sum of money to insured in case of occurrence of loss rather only primary insurer is liable to pay claimed money. | All coinsurers are liable to compensate the amount of loss in their agreed proportions. |
| It is not necessary to have more than one reinsurer. | There must be atleast two coinsurers or more than that. |

## ****Q What are the tax benefits on insurance?****

**Answer-** Apart from the safety and security benefits of buying insurance, there are also the income tax benefits that you can avail.

* Life insurance premium of up to Rs 1.5 lakh can be claimed as a tax-saving deduction under [Section 80C](https://cleartax.in/s/80c-deductions).
* Medical insurance premium of up to Rs 25,000 for yourself and your family and Rs 25,000 for your parents can be claimed as a tax-saving deduction under [Section 80D](https://cleartax.in/s/80c-80-deductions).

 These claims have to be made at the time of e-filing income tax returns.

**Q What do you understand by the term Assignment in insurance?**

**Answer-** As per Tomiln’s Law Dictionary, ‘Assignment’ is transferring the interest a man has in anything to other. In other words assignment means the transfer of the right of claim on property to another.

 In the context of insurance, assignment means transfer of interest or right under an Insurance policy to a third party. Assignee is one to whom an assignment has been made; one to whom rights have been transmitted by particular title through transfer. The person by whom the assignment is made is called the ‘assignor’.

**Q What are the salient features of Assignment in insurance?**

**Answer-** Following are the salient features of assignment:

1. For effecting a valid assignment a notice should be furnished by the assignor in writing to the insurance company expressing the consent to assignment. Policy document should also be enclosed for necessary endorsement by the insurance company.
2. The assignment can be conditional or absolute.
3. The assignment must not be opposed by any law.
4. The assignee should not have any legal disqualifications.
5. An assignment may be done by noting the name of the assignee(s) in the policy document itself or by a separate deed.
6. The document of assignment must bear the signature of the assignor, assignee and should be attested by witness.
7. The assignment becomes effective only when insurance company(insurer) registers the assignment in its record and give a written acknowledgement of the receipt of such notice.

**Q What are the types of Assignment in insurance?**

**Answer-** Theassignment of an insurance policy can be made in two ways:

* Absolute assignment, and
* Conditional assignment

These are discussed below-

1. **Absolute Assignment** – An absolute assignment is an assignment where all rights, title and interest of the assignor in the policy pass to the assignee. The assignee can deal with the policy in the way he likes without the consent of the assignor. So here transfer of rights is absolute and the assignor (original holder) loses control completely until the policy is re-assigned to him.

 For example, Mr. S Kalita has a life insurance policy of Rs 50 lakhs and now he intends to gift this policy to his wife. He wants to make absolute assignment of his life policy in his wife’s name so that the death benefit or maturity proceeds can be directly paid to her. Once the absolute assignment is made, Mrs. S Kalita will be the owner of the policy. She may again transfer or assign this policy to someone else or to her husband.

1. **Conditional Assignment** - Under this type of assignment, the transfer of rights will happen from the Assignor to the Assignee subject to certain conditions. If the conditions are fulfilled then only the policy will get transferred from the Assignor to the Assignee. Conditional assignment may also take the form of ‘Collateral Assignment’ which means assigning the insurance policy as collateral security against loan from financial institutions.

For example, Mr. Das has an endowment insurance policy of Rs 60 lakh. He wants to apply for a home loan Rs 50 lakh. His banker has asked him to assign the term policy in their name to get the loan. Mr. Das can conditionally assign the policy to the home loan provider to acquire home loan. If Mr. Das meets an untimely death during the loan tenure, the banker can receive the death benefit under this policy and get their money recovered from the insurance company. Where the death benefit received by the banker is more than the outstanding loan amount, the insurer will pay the bank the outstanding dues and pay the balance to the nominee directly. The balance amount (if any) will be paid to Mr. Das’s beneficiaries (nominee/legal heirs). If Mr. Das himself repays the entire home loan amount, he can get back his insurance policy from the bank. The policy would be re-assigned to Mr. Das on the repayment of the loan.

**Q Who can make an assignment?**

**Answer-** A policyholder who has policy on his own life can assign the policy to another person. However, a person to whom a policy has been assigned can reassign the policy to the policyholder or assign it to any other person. A nominee cannot make an assignment of the policy. Similarly, an assignee cannot make a [nomination on the policy](https://accountlearning.com/nomination-life-insurance-policy/) which is assigned to him.

**Q What happens to the ownership of the policy upon Assignment?**

**Answer** - When a policyholder assigns a policy, he loses all control on the policy. It is no longer his property. It is now the assignee’s property whether the policyholder is alive or dead, the assignee alone will get the policy money from the insurance company. If the assignee dies, then his (assignee’s) legal heirs will be entitled to the policy money.

**Q What do you understand by the term reassignment?**

**Answer** – The assignee may, while the policy is in force, re-assign the interest in the policy to the previous assignor. Such reassignment will have the effect of cancelling the earlier assignment and the interest in the policy will revert back to the previous assignor.

**Q Can assignment be changed or cancelled?**

**Answer-** An assignment cannot be changed or cancelled. The assignee can of course, reassign the policy to the policyholder who assigned it to him. He can also assign the policy to any other person because it is now his property. We can think of a bank reassigning the policy to the policyholder when their loan is repaid.

**Q What do you understand by the term Nomination and mention the differences between ‘Assignment’ and ‘Nomination’.**

**Answer-** According to Cambridge Dictionary, term nomination means the act of officially suggesting someone or something for a job, position or prize.

 In insurance, the term nomination is used in Life Insurance. It means the process of naming a person to whom the proceeds of the insurance policy should be paid in case of death of the life insured. The person nominated is called nominee.

 Following are the differences between assignment and nomination:

|  |  |  |
| --- | --- | --- |
| **BASIS FOR COMPARISON** | **NOMINATION** | **ASSIGNMENT** |
| Meaning | Nomination implies appointment of a person, by the policy holder to receive the policy benefits, on the event of death. | Assignment alludes to, ceding of right, title and interest of the policy to another person. |
| Attestation | Attestation is not required in nomination. | Attestation is required in assignment. |
| Consideration | It does not involve consideration. | It may involve consideration. |
| Right to sue | Nominee has no right to sue under the policy. | Assignee has the right to sue under policy. |
| Purpose | To help beneficiary recover the policy amount when it becomes due for payment. | To transfer all rights and interest in favor of the assignee. |
| Revocation | Can be changed or revoked several times. | Can be revoked one or two times during the term of policy. |
| Favor | Generally, made in favor of immediate relatives. | Can be made in favor of immediate relatives or to external party. |

**Q What do you understand Endowment Plan? Discuss the features of Endowment Plan.**

**Answer-**Endowment plan is life insurance policy which provides the insured with a combination of the elements of both protection and savings. In other words, endowment insurance policy combines both insurance cover, as well as savings plan. It helps the insured in saving regularly over a specified period of time, so that he/she is able to get a lump sum amount on the maturity policy, if the policyholder survive the policy term i.e. the policyholder gets his/her sum assured on a fixed date in future as per the policy terms and conditions. However, in case of sudden death of the policyholder during the continuation of the policy, the insurance company will pay the sum assured (plus the bonus, if any) to the nominee of the policyholder.

 Following are the features of Endowment Plan –

* **Dual purpose**- An Endowment plans serves dual purpose savings and protection. On maturity, a pre-determined will be paid to the policyholder.
* **Death along with survival benefits**- In case of demise of the insured, the beneficiary/nominee of the policy gets the sum assured along with the bonuses. Also, the insured is allowed to get the sum assured if he/she outlives the policy.
* **Policy period** – Endowment policies are issued for specific time duration which is usually of very long term like 15, 20, 25 or 30years.
* **Premium payment frequency** – The policyholder can make payment of the premium based on the policy chosen by him/her. Payment can be done monthly, quarterly, half-yearly, and on yearly basis.
* **Tax benefits**- The policyholder is entitled to get tax exemption on both premium payments under Section 80C and the amount received on maturity or death under Section 10(10D) of the Income Tax Act, 1961.
* **Loan eligibility** – These policies are eligible for loans within the surrender value of the policy.

**Q What are the different types of Endowment Plan?**

**Answer- The different types of Endowment Plan are briefly discussed below-**

* **Pure** **Endowment Policy: Under this policy the sum assured is payable to insured on maturity or his /her death whichever occurs earlier.**
* **Single Endowment Policy: Under this policy only one premium is paid to protect life for a particular time period. This policy provides an effective combination of both family protection and investment.**
* **Participating Endowment Plans (PEP):** In this Endowment Policy, the insured ‘participates’ in the company’s profits which are given as bonuses and this bonus is decided by the insurance company from which the insured has taken/purchased his/her insurance policy.
* **Non-Participating Endowment Plan:**In This Endowment Policy the participants don’t participate in company’s profit. All the proceeds payable under this policy are guaranteed at inception.
* **Unit Linked Endowment Policy: In** This Endowment Plan the company gives different ways of risk coverage along with the various types of investment plans like invest in stocks, bonds or mutual funds as decided by the insurer.
* **Low Cost Endowment Policy:**These policies are basically used to cover any existing loans or mortgages. This type of policy pays a minimum value which will cover the loan amount either on death or on maturity.

 **Q What are the advantages and disadvantages of Endowment Plan?**

**Answer -** The advantages of endowment policy are:

* An endowment policy serves dual purpose. It provides life insurance protection together with a large savings and investment element.
* The policyholder is entitled to get tax exemption on both premium payments under Section 80C and the amount received on maturity or death under Section 10(10D) of the Income Tax Act, 1961.
* Endowment policies are considered as a relatively safer option of investment over other types of investments.
* An endowment policy offers long term savings. One can choose a policy term ranging from 10, 15, 20, 30 to 40 years.
* Insurance companies also declare bonuses for the policyholders which means insurance companies shares a part of their surplus with the policyholders having ‘with- profit policies’. The bonus declared is added to the sum assured at the time of maturity claim or death claim.

 The disadvantages of endowment policy are:

* It only provides protection for a specified period.
* The premium payable is usually much higher than that of whole life insurance or term insurance.
* The surrender value of policies under this plan is lower than the premium paid

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