student

Automobile and Home Insurance
Workbook

www.investprogram.org

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Fires…Floods…Earthquakes…Tornadoes…Hurricanes…Car Accidents…Burglaries… …the list is nearly endless when you consider the many risks you face in your daily life. Luckily, you don't need to face them alone! For each of these situations, insurance is available to help you pay for damage to your property, or to pay others on your behalf when you injure someone or damage their property.

This chapter is designed to give you a foundation for your study of automobile insurance through the InVEST program. Just as you must learn a new language when you decide to move to a foreign country, it is important for you to have a basic understanding of the fundamentals of property and casualty insurance, of which automobile insurance is a part. Insurance has a language of its own, and once you master the basic vocabulary, you're well on your way to understanding the important role insurance plays in our economy and society.

This chapter is designed to give you a foundation for your study of automobile insurance through the InVEST program.

The insurance industry is exciting and dynamic, changing on an almost daily basis. It is also a complex topic to study, but learning more about how insurance works will help you become a more informed consumer when you purchase insurance throughout your life.

LEARNING OBJECTIVES

When you complete this chapter, you should be able to:

- Describe how insurance began and the way it has evolved over time
- List the benefits and costs of insurance
- Explain how the insurance industry is organized
- Describe the two general principles of insurance
- Define basic insurance terms

HOW INSURANCE BEGAN

The insurance industry has a long and rich history dating back several centuries. In fact, the earliest forms of insurance occurred when merchants along the Yangtze River in China determined that it was too risky to put all their merchandise on a single boat and sail it down the river. Instead, they split the shipment into many pieces and placed a portion on each of several vessels. They recognized that the likelihood all the boats would sink was very small, assuring them that at least the majority of their goods would reach their destination unharmed. This informal, but very clever arrangement, eventually led to the formation of insurance organizations who also recognized that if they "spread the risk," the chance of a loss to each unit was minimized. Indeed, if they collected a small amount of money from many individuals and pooled it, they could reimburse those few unfortunate people who suffered a loss. Voilà, the insurance industry was begun!

> **If the house** had the same symbol that appeared on the truck, the fire company would stop and extinguish the fire, but if not, they would keep on going!

The more formal insurance industry had its origins at a coffee house near London, England owned by Edward Lloyd. In the late 1600s, wealthy merchants were engaged in a great deal of transoceanic shipping, particularly to the "new world." Worried that they could be wiped out financially if a shipment was lost, they began to make arrangements with each other to share their risks of loss. When a shipment was scheduled to depart, the merchants would meet at the coffee house and pass around an agreement whereby each of them would agree to reimburse the shipper for a percentage of the value of their cargo. One by one, each person would sign his or her name beneath a description of the shipment, and set forth the percentage of loss he or she was willing to pay. When the total reached 100 %, the vessel would sail. These individuals became known as underwriters, because they had pledged their financial backing by signing under the voyage description. If there was a loss, each person would reimburse the shipper for his or her percentage of the value, but if the voyage was successful, each would receive a bonus or a premium.

This, of course, was the beginning of Lloyd's of London, which has continued to do business in almost the same way for over 300 years and upon which our American insurance industry is based. Lloyd's is still a major participant in the insurance industry, providing policies insuring risks ranging from large ocean-going vessels carrying crude oil to Madonna's voice, and virtually everything in between.

The U.S. insurance industry owes much of its current structure to a very familiar person in U.S. history: Benjamin Franklin. Along with bifocal lenses, the postal department, and lightning rods, Franklin is also credited as the “inventor” of the U.S. insurance industry. In 1752, he organized one of the first fire insurance companies in the country, one that is still in operation to this day. Franklin’s company, the Philadelphia Contributorship for the Insurance of Houses from Loss by Fire, has a long name, but tells the story of what fire insurance is all about. Rather than insurance as we now think of it, this was really an arrangement where a person would place a plaque near the front door of his or her home indicating that they had purchased “insurance” from a fire company. The plaque contained the symbol, or logo, of one of the fire companies that had been formed, including Franklin’s. When a fire occurred, all the fire companies would get in their fire trucks (horse drawn, of course) and go by the house looking for the symbol. If the house had the same symbol that appeared on the truck, the fire company would stop and extinguish the fire, but if not, they would keep on going! If you visit the eastern United States, look for the symbols, called fire marks, near the doorways of older buildings. They are still there and serve as a reminder of the earliest days of fire “insurance.”

Quick Quiz 1.1

Match the terms to their description.

_____ Benjamin Franklin	1. The amount of money charged for an insurance policy.
_____ Lloyd’s of London	2. A person who pledges financial backing of a risk.
_____ Underwriter	3. The father of modern insurance in the United States.
_____ Premium	4. A symbol placed on a building to signify that it is insured.
_____ Fire Mark	5. An organization of individuals who insure large and unusual risks.

BENEFITS AND COSTS OF INSURANCE

There are many positive aspects to the products and services provided by the insurance industry. Rather than providing the direct benefit of actually putting out the fire, as we did in Ben Franklin’s day, today’s insurance products function primarily as a means to reimburse people when their property is damaged or they suffer some other kind of unforeseen loss. Insurance helps individuals and business owners resume their normal standard of living and operations, which is actually a benefit to society as a whole. If your home burned down, and you had no means to pay for the repairs, it is unlikely you would have the funds to make other purchases. Not only would you be affected, but others from whom you ordinarily buy things would also be impacted. There would be a negative, ripple effect, on the economy. The proceeds of an insurance policy benefit everyone by restoring the insured person or organization to the same financial condition they were in before the loss happened—it indemnifies them.

Another way insurance benefits society is by encouraging activities and devices that will reduce the amount of losses and their economic impact. For example, it has been proven that seat belts and other passive restraints in automobiles significantly reduce the extent of injuries suffered by vehicle occupants involved in auto accidents. Insurance companies were the major force behind requiring seat belts as standard equipment in all cars. The efforts of insurers to eliminate or reduce the amount of loss and human suffering date back to the earliest days of the insurance industry.

Of course, insurance is not without its costs. In addition to the obvious consumption of resources, both human and otherwise, insurance can also create a situation where losses become more likely to occur. For example, who would be tempted to burn down their own house if they would have to bear the entire financial burden themselves? The fact that they have insurance has caused some unscrupulous people to commit the crime of arson, which means to intentionally burn down a building, simply to access the insurance policy proceeds. This certainly would not happen if there was no insurance policy, and so it is considered a cost of insurance.

Similarly, some people aren't as careful to prevent losses when they are insured. They don't cause the losses intentionally, as the arsonist does, but they are indifferent as to whether or not a loss occurs. These are people you may have heard say, "Oh well, if something happens to my property, so what, that's what I have insurance for!" As you will learn, this indifference to loss leads to damage and injury that could be prevented and thus is also considered a cost of insurance.

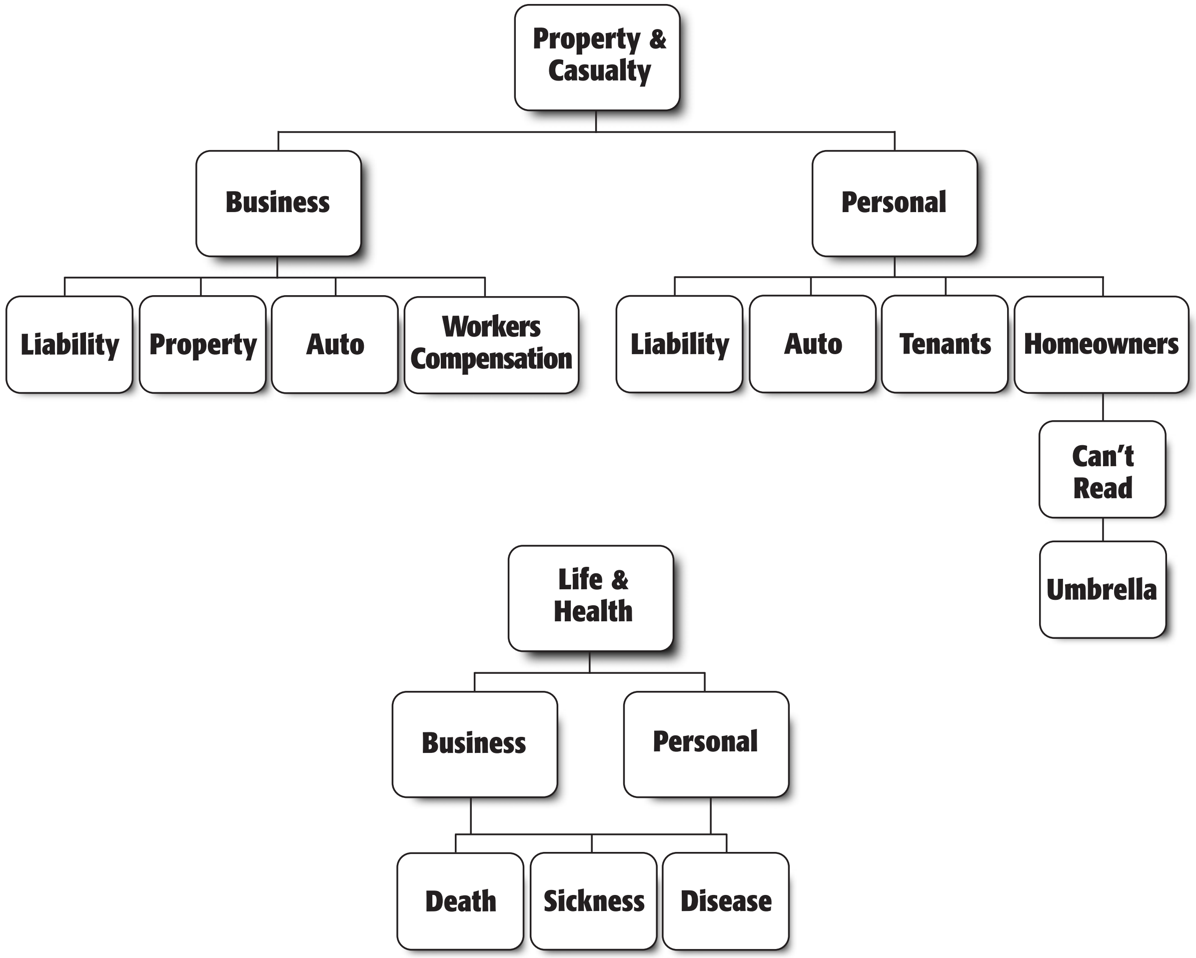
Quick Quiz 1.2

List three ways insurance benefits society:

1. ____________________
2. ____________________
3. ____________________

List three ways insurance creates costs to society:

1. ____________________
2. ____________________
3. ____________________



HOW THE INSURANCE INDUSTRY IS ORGANIZED

Insurance is part of the larger financial services industry, and is divided into two major divisions: property and casualty insurance and life and health insurance. Property and casualty insurance provides protection to businesses and individuals for loss to their assets, both physical and financial. Life and health insurance protects people from financial loss due to premature death, sickness or disease.

Within the property and casualty industry, there exist additional divisions. Commercial insurance (also called commercial lines insurance) involves protection for businesses and organizations. Included in this section are property insurance, liability insurance, workers compensation, automobile insurance and a variety of other policies designed to protect the assets of the organization in the event of an unexpected loss. For example, the corner donut shop purchases commercial insurance to protect its equipment from loss due to fire or theft, liability insurance in the event someone is injured on their property or becomes ill after eating one of the donuts, workers' compensation insurance in case an employee is hurt on the job, and automobile insurance for the company van. They might also secure insurance for cash they have in the register if they are robbed, for their loss of income if they are shut down due to a fire at their location, or for a lawsuit brought by one of their employees for discrimination.

Personal insurance (also known as personal lines insurance) provides protection to individuals and families from risks of loss to their assets. This is probably the form of insurance with which you are most familiar, since it is the type you must purchase for yourself. Automobile insurance is required in most states in order to operate a motor vehicle. Homeowners insurance must be purchased if you buy a home with the help of a bank or other lender in order to protect their collateral. Additionally, you may own jet skis, a boat, or an ATV (all terrain vehicle), all of which are insured by personal insurance policies. The focus of this book is on personal automobile insurance.

GENERAL PRINCIPLES OF INSURANCE

Just like when you build a house, the study of insurance must begin with a foundation. This foundation consists of the guiding principles that underlie all other topics we will discuss in this book.

The first guiding principle is known as the doctrine of insurable interest. Under this doctrine, or rule, an insurable interest is said to exist whenever the occurrence of a certain event, such as a fire or theft, results in a financial loss to a person or organization. In order to purchase legally valid insurance, one must possess an insurable interest in the item being insured. If you own a car, and that car is damaged in an automobile accident, the value of the car declines and you suffer a financial loss. Therefore, you possess an insurable interest in that car and may purchase insurance to protect against the financial loss.

Another part of the foundation is called the principle of indemnity, the second guiding principle of insurance. This is similar to insurable interest, but rather than defining under what circumstances you can collect on an insurance policy, the principle of indemnity determines how much you can collect. Let's say your car is damaged in an auto accident. While you might want the insurance company to replace your car with a new one, this would violate the principle of indemnity since a new car is more valuable than an older one in most cases. So, the insurance company determines the value of your damaged automobile (including a deduction for depreciation) and pays you that amount. You are indemnified.

Under this rule, insurance policies are considered to be contracts of indemnity, meaning they are designed to put someone back in the same general financial condition he or she was in before the loss occurred. In other words, you shouldn't be able to profit by collecting the insurance. You may have heard the phrase "insurance is to make you whole." This is a euphemism for the principle of indemnity. You're no better off than you were prior to the loss, but neither are you any worse.

Without each of these underlying principles, there is little that would separate the purchase of insurance from gambling. Think what would happen if people did not need to have an insurable interest in the houses they insured for loss by fire. You would simply drive around town, find the oldest, most rundown house you could, buy a fire insurance policy and wait for the place to burn down. It's the doctrine of insurable interest that prevents you from doing that. In order to collect the insurance, you had to have suffered a loss in the first place.

BASIC INSURANCE TERMS

Among the most fundamental insurance concepts are the meaning of the words risk, peril, hazard, loss, insurance, and insurance policy.

Risk

A risk exists whenever there is uncertainty about the outcome. "Taking a risk" means not knowing exactly what will happen. Facing risks is part of life, and it is the basic problem dealt with in insurance. Risk, however, comes in two forms, only one of which is addressed by insurance.

Pure risk exists whenever there are only two possible outcomes: loss, or no loss. This is the type of risk insurance deals with. Your home burns (loss) or it does not (no loss). Your car is damaged in an accident (loss) or it is not (no loss).

The other type of risk is called speculative risk. With speculative risk, there is a third possible outcome: gain. When you purchase a company's stock, the value of the stock could decline (loss), it could stay the same (no loss), or it could appreciate (gain). When a company comes up with a new product, it could be a flop (loss), they could break even (no loss), or they could have a huge success (gain). Insurance does not deal with speculative risk, since the potential for gain or profit contained in these situations would be a violation of the general principles of insurable interest and indemnity.

Peril

A peril is the cause of a loss. Fire, flood, theft, and earthquake are all perils or events that can cause a loss to property and people.

Hazard

A hazard is a condition that makes a peril more likely to happen or that increases the seriousness of a loss. Leaving the door to your house unlocked when no one is there is a hazard since it increases the likelihood that a theft will take place. Building houses with wood shake roofs increases the amount of damage that the structure will suffer if there is a brush fire and is, therefore, a hazard. Some hazards are the result of the physical characteristics of property, such as old wiring in a home that could lead to a fire. Other hazards are created by people, such as when a person burns down his or her own house or when someone files a false insurance claim. This is called a moral hazard, since it arises out of a person's habits or tendencies and increases the likelihood of losses. The person who is indifferent to loss represents a morale hazard, since it is his or her carelessness that raises the likelihood of loss.

Loss

Loss is simply a decline in value. When there is a reduction in the quantity, quality, or value of something, a loss is said to occur. This can occur to tangible items, such as houses, cars, or equipment (direct loss), or it can result from damage to tangible items (indirect loss). An example is when you must take up residence in a hotel (indirect loss) because your house was damaged by fire (direct loss) or when you have to rent a car (indirect loss) while yours is in the shop being repaired following a collision (direct loss).

Insurance

Insurance is a social and contractual device that transfers the risk of financial loss from individuals or businesses to an insurer. The insurer collects small amounts of money from each of the individuals or businesses (premium) and "pools" them into a large sum of money out of which losses will be paid. The organization that arranges and administers the pool of funds is generally referred to as an insurer, and the individuals or businesses that transfer their risks are called insureds. The contract that makes the transfer is referred to as the insurance policy.

Insurance Policy

An insurance policy is a document issued by an insurance company to its policyholder that provides details about what is covered under the contract. The type of coverage (such as automobile liability insurance), the limits (maximum amount that will be paid for a particular loss), and any deductibles (amount the insured must pay his or herself) are all stated in the policy.

Quick Quiz 1.3

Complete each sentence below using the following list of words. Not all words are used.

personal	property and casualty	insurable interest	pure risk
commercial	life and health	indemnified	loss
peril	hazard	speculative risk	insurance

1. The type of insurance that protects business firms and other organizations is called ______________________________ insurance.
2. When a person stands to lose financially if a loss occurs, they are said to have an ______________________________ in the risk.
3. A social device that transfers the risks of loss from an individual to an insurer is called ______________________________.
4. A ______________________________ is a condition that increases the chance that a loss will occur.
5. When an insurance company puts someone back in the same general financial condition they were in prior to a loss, the person is said to be ______________________________.
6. A ______________________________ is defined as the cause of a loss.
7. The type of risk that has no chance for gain is called ______________________________.
8. When someone is concerned about the risk of loss due to premature death or disability, they may purchase ______________________________ insurance to protect themselves.
9. When a piece of property is damaged and declines in value, it is said to have suffered a ______________________________.

Summary

The insurance industry dates back hundreds of years, with Lloyd's of London serving as one of the oldest insurance organizations. Many of the terms used in modern insurance, such as underwriter and premium, had their origin at the coffee house of Edward Lloyd.

Insurance in the United States was based on British principles and started with fire insurance. Fire marks were symbols placed near the doorway of buildings to indicate which fire company would stop to extinguish a fire.

The modern insurance mechanism has both benefits and costs. While insurance provides payment for loss and encourages loss control, it also consumes physical and human resources. Some people may intentionally cause a loss or be less careful because insurance exists.

Insurance is divided into property and casualty and life and health divisions. Commercial insurance provides coverage for businesses and other organizations, while personal insurance protects the assets of individuals and families.

Some of the primary principles upon which the insurance industry is founded are the doctrine of insurable interest and the principle of indemnity.

There are many terms that are essential to the study of insurance. A thorough understanding of these terms will assist you in your study of risk management and insurance.

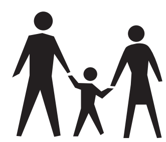
CHAPTER 2

Managing Risk

Key Terms

- **Direct loss**
- **Indirect loss**
- **Legal liability**
- **Loss**
- **Loss exposures**
- **Loss frequency**
- **Loss prevention**
- **Loss reduction**
- **Loss severity**
- **Negligence**
- **Peril**
- **Personal property**
- **Pure risk**
- **Real property**
- **Speculative risk**

Risk exists whenever there is uncertainty about outcome. If you knew for certain that you would become a millionaire by purchasing the stock of a particular company, there would be no risk involved since you would know in advance what was to occur. Likewise, if you knew that you would never be involved in an automobile accident, you would likely not purchase insurance since the uncertainty would be removed from the situation. Of course, none of us can perfectly predict the future, so we must take steps to reduce the risks in our lives.



This chapter will discuss the types of risks faced by individuals and families.

While insurance is certainly an important method used by many individuals to manage the risks they face, there are many other things a person can do to deal with risk. In fact, some of the methods for treating risk are used at the same time as insurance as you will see in this chapter. Others are used independent of insurance and may, in fact, eliminate the need for insurance.

This chapter will discuss the types of risks faced by individuals and families. In order to suffer a loss, three things are essential:

- An item can suffer loss (such as a building, personal wealth, or a person's health)
- A cause of the loss (fire, a lawsuit, or a disease); and
- Financial impact of the loss (decline in the building's value, cost of hiring attorneys, or medical expenses)

LEARNING OBJECTIVES

When you complete this chapter, you should be able to:

- Distinguish between pure and speculative risks
- Identify the major property loss exposures faced by individuals and families
- Identify the major liability loss exposures faced by individuals and families
- Identify some of the human loss exposures faced by individuals and families
- Recognize the major categories of loss causes
- Give specific examples in each category of loss causes
- Identify the impact of losses
- Identify the risk management methods that can be used to treat the risks faced by individuals and families
- Determine which risk management method is best suited to a particular type of loss exposure

RISK AND LOSS

Whenever you are faced with a risk, there are three possible things that can happen. First, the outcome can be positive. When you risk your money buying a lottery ticket you could win (called a gain). Second, the outcome could be negative and produce a loss. When you face the risks associated with driving a car, you could have an accident. The accident is a loss, because you may have to pay to have your car repaired or may be responsible to pay for the damage you cause to someone else's car. Third, the outcome could be neutral—neither positive nor negative. There's no loss, but there's no gain either.

When there are only two possible outcomes to a risk, loss or no loss, it is referred to as pure risk. When there is a third possible outcome, gain, the risk is called speculative risk. Insurance is designed to treat pure risk exposures. Speculative risk, because it has a potential for gain, is not the subject of insurance. The purpose of insurance is to protect against loss. If no loss occurs or there is potential for gain, insurance usually cannot be purchased. For example, if you start a business, it can be successful or unsuccessful…insurance, in general, cannot be purchased to ensure the success of your business, though it can if your business is threatened by a peril (e.g., fire) where the only possible outcomes are loss or no loss.

IDENTIFYING LOSS EXPOSURES

Whenever someone faces the possibility of a loss, they are said to be "exposed" to the loss. In other words, while we don't know for sure that a loss will take place, it is a possibility. What are the types of loss exposures with which you are faced? In order to answer that question, let's consider the case of Manuel, a high school senior.

Property Loss Exposures

Manuel and his family face many property loss exposures. First, the home in which they live may be damaged or destroyed. A house or other building is considered to be an item of real property, a term you may be familiar with due to its use in the real estate industry. Real estate means ownership of real property—houses, buildings, and structures of various kinds. Real property is defined as land and anything that is attached to or growing on the land. So, if there is a built-in swimming pool, a carport, or a garage on the property owned by Manuel's family, these are all items of real property. If the family is in the farming industry, their crops are considered real property while they are still growing in the field.

Similarly, Manuel has exposure to loss of personal property. Personal property is distinguishable from real property in that it is not affixed to land directly. Examples of personal property are clothing, furniture, appliances, jewelry, computers, and televisions. Personal property might be stolen from inside Manuel's home or from his locker at school. Any crops that have been harvested are also considered personal property since they are no longer attached to the land. For many people, loss of their home and personal belongings is the largest property loss exposure they have.

An automobile is also an item of personal property, so another property exposure faced by Manuel is damage to his car as a result of an accident. If the family owns boats, trailers, or farm equipment they face loss of those items of property as well.

Liability Loss Exposures

While loss of property is certainly serious, an even greater potential for loss exists when a person or family becomes legally obligated to someone else. Let's consider how someone might become legally responsible to pay another person.

Manuel has just turned 17 and he has been given the privilege of driving the family's automobile. While going to school one morning, Manuel briefly takes his eyes off the road and looks down to change radio stations. BAM! Startled by the impact, Manuel looks up to find that he has hit the car in front of him.

Everyone who operates a motor vehicle is required to do so in a manner that does not endanger other people or the property of others. In other words, you must be a careful and responsible driver and if you are not, you could be held legally responsible for any injuries or damage you cause to others. The term used for this responsibility is liability. When you become liable to someone, you must reimburse them for any damages they suffer as a result of your carelessness. The legal term for carelessness is negligence, meaning you had a duty to behave in a certain way and you breached that duty. Manuel had a legal duty to operate his car in a safe manner and not to injure anyone or damage their property. His momentary glance at the radio, instead of the vehicle in front of him, represented negligence on his part. He may be legally responsible for any damage he caused to the other car, as well as for any injuries that the other driver suffered.

There are other ways that a family can face liability loss exposures. Visitors to the family's home may be injured due to an unsafe condition such as a loose railing. The activities Manuel and his family enjoy might also create liability loss exposures. For example, while camping Manuel and his family light a fire to cook their dinner. The fire gets out of control and before they know it, flames have damaged the trailer located on the next campsite and smoke from the fire has damaged the contents of the trailer. Manuel's family could be held legally responsible to pay for the damage.

The main difference between liability and property loss exposures, is that while the amount of a potential loss to property can rather easily be estimated prior to the loss, the amount of a claim for liability is not determined until after something has happened. Even then, it is difficult to predict what a judge or jury might determine a person must pay to another as compensation for damage or injuries. You have probably read or heard stories about very large jury awards being given to the victims of accidents and you may have been surprised at the amounts. One woman, who was burned by a cup of hot coffee served by a fast food restaurant, was awarded millions of dollars for her injuries. It was determined that the coffee had been served at a temperature that exceeded the norm. While this is certainly not common, the fact that it could happen to anyone represents a substantial risk (and the need for insurance is evident.)

Human Loss Exposures

Many people, particularly teenagers, fail to recognize one of the most significant loss exposures they face—risk of losing their health and being unable to earn income. One of the biggest assets any person has is their potential earning capacity. If that potential is interrupted by ill health, disability, or death, there is a significant loss, not only to that person, but to others who are dependent upon them. Manuel is currently planning to go on to college and possibly law school after that. If he were seriously injured in an auto accident it could delay or prevent him from achieving his goal of becoming an attorney. The amount of money he would have earned each year multiplied by the number of working years he anticipates represents the amount of his loss.

$30,000 average annual earnings x 50 years (retiring at age 65) = $1,500,000

If he had a wife or child at the time of the accident, they too would lose the financial support Manuel would have been able to provide for them.

In addition to lost income, serious illnesses can also result in large medical bills for treatment. Just being wheeled into the emergency room of the local hospital could cost Manuel hundreds, if not thousands, of dollars. If he requires physical rehabilitation or ongoing medical care, the total cost could be enormous. Death results in funeral and burial expenses that must be paid by the survivors of the deceased person.

Quick Quiz 2.1

List below examples of real property.

1. ____________________
2. ____________________
3. ____________________
4. ____________________
5. ____________________

List below examples of personal property.

1. ____________________
2. ____________________
3. ____________________
4. ____________________
5. ____________________

The Causes of Loss

Just having an item of property that is exposed to loss does not mean you will actually suffer a loss. There must also be a cause of the loss, or peril. There are many different types of perils that fall into one of three broad categories: natural, human and economic.

The causes of loss do not only affect property loss exposures. Negligence, a human peril, can result in liability losses.

You might notice that fire appears on both the natural causes and human causes list. That's because some fires, such as wildfires, can be caused by lightning strikes in dry, forested areas during warm summer months – a cause of nature. Other fires are caused by humans, either through carelessness or intention to cause damage, such as when someone burns down a building in an attempt to hide some other crime.

Natural Causes of Loss Caused by Nature	Human Causes of Loss Caused by People	Economic Causes of Loss Caused by Changes in the economy
Wind	Theft	Inflation
Rain	Vandalism	Depreciation
Earthquake	Negligence	Recession
Flood	Fraud	Obsolescence
Fire	Murder	Stock market declines
Lightning	Discrimination	Technological changes
Drought	Fire	Currency fluctuations
Erosion	Malpractice	Changes in tastes and preferences

The list of perils is nearly endless and is being expanded constantly as the world changes. Just think – at one time "virus" would have been considered a natural peril that caused human loss, but now it can also mean a human peril that results in damage to computer systems.

The Costs of a Loss

You can see that property, liability, and human losses can be expensive. In addition to the financial impact, or *direct loss*, there may also be other costs that are not as obvious. For example, a fire at Manuel's home that requires several weeks of repair might cause the family to temporarily relocate to a hotel. The cost of the hotel, plus any additional travel, food, or other expenses are an *indirect loss*, or a consequence of the direct loss to the home. Time spent participating in a trial following an automobile accident is an indirect cost of the loss. There is also the physical and mental strain that is suffered by those people who have been involved in serious or traumatic events. It is difficult to put a dollar amount on these indirect losses, but they can represent a substantial amount of money, in some cases even more than the direct loss itself.

How Can You Manage Risks?

There are five methods a person can use to manage their risks of loss.

Avoidance

This risk management technique means that you eliminate the loss exposure or never acquire it in the first place. For example, if you fear having your car stolen, you might consider not owning a vehicle. If you already own the car, you could sell it.

When used as a risk management technique, avoidance is very effective. In fact it ensures that a loss will not happen. However, it is not always practical and some loss exposures, such as death, simply can't be avoided.

Loss Control

For risks that cannot be avoided, ***loss control*** can reduce the number of losses ***(loss frequency)*** or the cost of losses that do occur (loss severity). Burglar alarms are an example of a loss control device that reduces the number of losses that occur to property. A person intent on breaking into a home may see that the house has an alarm and decide not to commit the crime (at least to that house)!

Seat belts and airbags in automobiles are examples of loss control devices that are designed to reduce the cost of a loss. While their use does not keep auto accidents from happening, when used by vehicle passengers these restraints generally result in less serious injuries.

> **Choosing among the risk** management techniques can be a challenge. When the risks of loss are enormous, avoidance may be most appropriate. For losses that don't happen very often, but are costly when they do, insurance may be the best choice.

Loss control measures that reduce the number of losses are called ***loss prevention*** methods. When the purpose is to reduce the cost of a loss, the device is referred to as a ***loss reduction*** technique, because the dollar amount of the loss is less than it would be otherwise.

Transfer to Others

Some risks can actually become the responsibility of someone else using a transfer such as contract or agreement. When you rent a car, the rental car company requires you to sign a contract in which you agree to pay for any damage to the vehicle. Rather than suffer the loss itself, the rental car company transfers that risk to you, the renter.

Retention

The risk management method of retention means paying some or all of the losses that occur out of your own personal current income or from a personal savings account. An example of the individual paying for the loss or sustaining the damage without correcting the problem is in the case of small losses, such as cracks in a car windshield. The owner of the car may retain the loss (pay out of pocket) since it does not happen frequently and does not result in a large dollar amount of loss. It is also possible that the damage will not be repaired and the person will simply have a vehicle worth less money due to the cracked windshield. Either way, the burden of the loss falls on the owner of the vehicle.

Insurance

The last risk management method to be considered is insurance, or transfer of the cost of loss to an insurance company. Understanding how insurance operates as a tool of risk management is the primary purpose of this book and will be dealt with in some detail in the following chapters.

Quick Quiz 2.2

For each of the following loss exposures, indicate the risk management technique(s) that is (are) most appropriate for treating the risks of loss.

1.____ A vehicle owner travels frequently on roadways with heavy trucks and worries about the possibility of getting a cracked windshield.
2.____ An athlete is concerned that playing two sports in high school may result in an injury that could jeopardize a college scholarship to play one sport.
3.____ The tires on a vehicle have become worn and could result in a blow-out and collision or overturn of the vehicle.
4.____ A beginning driver is worried that an automobile accident could result in serious injuries to passengers in the vehicle or to others.
5.___A contractor is concerned that he might be sued for damages as a result of something done by a subcontractor at a construction site.

Which Risk Management Method is Best?

Choosing among the risk management techniques can be a challenge. When the risks of loss are enormous, avoidance may be most appropriate. For losses that don't happen very often, but are costly when they do, insurance may be the best choice. Retention should be used when the person can afford the losses that are expected to occur. For any losses that cannot be avoided, loss control is always a wise choice and should be used along with either retention or insurance. The following chart may help to clarify when to use each risk management method.

	Happens Often (High Frequency)	**Seldom Happens (Low Frequency)**
Costs a Lot (High Severity)	Avoidance	Insurance
Costs Little (Low Severity)	Retention	Retention

Summary

Risk exists whenever there is an uncertain outcome. There are various types of risk faced by individuals and families. Some risks produce a positive outcome, such as when an investment increases in value. Others produce negative outcomes, for instance when a car is destroyed in an accident. Still others produce no change in circumstance at all; the person or family is the same after encountering the risk as they were before.

Risks that produce only two possible outcomes, loss or no loss, are called pure risks. Those that have the potential for a third outcome, gain, are referred to as speculative risks. Insurance, when used as a risk management tool, only deals with pure risks.

People face exposures to loss of property, real and personal, liability loss exposures, and human loss exposures. There are many different things that cause losses. Some of these causes, or perils, are natural, like earthquakes and floods. Other losses, such as theft, negligence, or discrimination are caused by people. Inflation, recession, and depreciation are examples of economic causes of loss.

When a loss occurs, it may have two different results. There is the direct cost of the loss, like the loss in value of a damaged car. There could also be indirect costs of a loss, such as the cost to rent a car while yours is being repaired.

There are five different methods people can use to manage their risks. Avoidance means eliminating an exposure or never acquiring one. Loss control is an attempt to eliminate losses (loss prevention) or reduce the amount of a loss (loss reduction). Sometimes loss exposures can be transferred to another person or firm. If a loss is paid out of the person's own resources, it is called retention. Retention can be complete or partial. A deductible contained in an insurance policy is an example of partial retention. Insurance is the final risk management method.

Choosing among the risk management methods can be a challenge. When risks present the possibility of devastating losses, avoidance can be best. For losses that happen seldom, but can be very costly, insurance is a good choice. Any losses that cannot be avoided should have some type of loss control device used on them.

CHAPTER 3

Issues in Automobile Insurance

Key Terms

- **Assigned risk plan**
- **Automobile insurance plan**
- **Compulsory insurance law**
- **Financial responsibility law**
- **Graduated licensing**
- **No-fault law**
- **Tort system**
- **Uninsured motorists coverage**

We will now turn our focus to the one insurance product with which you are probably most familiar—automobile insurance. There is more automobile insurance written in the United States than any other type. In other words, it's big business!

There are actually two categories of automobile insurance: personal and commercial. Commercial automobile insurance deals with coverage for business firms or organizations. Personal automobile insurance is the type purchased by individuals and families. Our study will be limited to personal automobile insurance.

Of course, automobile insurance did not really become popular until after the turn of the 20th century, making it a relative newcomer to the insurance industry. Until vehicle travel was common, the need for auto insurance was limited.

This chapter will begin with a discussion of some of the important issues in society that have an effect on automobile insurance. We will then discuss some of the laws that relate to auto insurance and how victims of car accidents are compensated for their injuries or damage to their vehicles. The chapter ends with an overview of how the insurance industry is regulated.

This chapter will discuss important issues and laws that have an effect on automobile insurance and how victims of car accidents are compensated for their injuries or damage to their vehicles.

LEARNING OBJECTIVES

When you complete this chapter, you should be able to:

- Discuss the current issues in automobile insurance
- Identify the way victims of auto accidents are compensated, including the method used in your state
- List the things youthful drivers can do to reduce the risk of auto accidents
- Explain some of the restrictions on the way in which personal automobile insurance companies operate

CURRENT ISSUES IN AUTOMOBILE INSURANCE

Each year, thousands of people are injured, disabled, or killed on America's roads and highways. Car accidents can have a profound financial impact on a family. In addition to the high costs of medical treatment for accident victims and the cost to repair automobiles and other property damaged in an accident, the sudden death of a family member can completely change the way a family lives when it results in a loss of income.

The statistics are particularly sobering when it comes to teenagers: automobile accidents are the #1 cause of death for people aged 15 to 24. Over the last 10 years, more young people have been killed in motor vehicle accidents than have died from all other causes combined. Young drivers represent about 13% of the total number of drivers, but are responsible for over 25% of all fatal accidents. What are the reasons for these sad figures? Let's look at some of the problems.

Irresponsible Drivers

A large part of the problem with automobile insurance is the percentage of people who are considered irresponsible drivers. These are individuals who drive under the influence of drugs or alcohol, do not purchase automobile insurance, or have a higher than average number of tickets and accidents.

Driving Under the Influence (DUI)

Although alcohol-related deaths are down nationwide, there is still a problem with drinking and driving. It is estimated that 3 out of every 10 Americans will be involved in an alcohol-related accident some time in their lives. Look around the room—that probably means about 9 or l0 of your classmates.

In 1999, 15,786 people were killed in auto accidents involving the use of alcohol—38% of all fatalities for that year! Drivers aged 16 to 24 account for 57% of all fatal crashes involving an intoxicated driver. Although the legal drinking age in all states is 21, more than one fourth of the teen drivers killed in auto accidents was drinking. Furthermore, every state has a "zero tolerance" law, which means teenage drivers who have any blood alcohol concentration will lose their driving privilege if caught.

Driving Without Insurance

Despite the fact that drivers and vehicle owners are required to carry auto insurance in most states, many people fail to comply with the law. When you are hit by an uninsured driver, either you or your insurance company are most likely to have to pay for any injuries or damages you sustain.

High-Risk Drivers

This category includes drivers who have a number of moving violations, an above-average number of accidents, convictions for serious offenses such as drunk or reckless driving, or a combination of these factors. High risk drivers sometimes have problems getting insurance coverage because the insurance company is more likely to have to pay a claim for a driver with a bad driving record than for someone who has had no tickets or accidents. If insurance is available for high-risk drivers, it is usually a great deal more expensive than the price charged good drivers.

Increasing Number of Auto Accidents

According to the National Safety Council, there are approximately 13,000,000 automobile accidents a year involving over 21,000,000 people. This is understandable given the number of vehicles on the road and the amount of time spent driving. Although fatality rates have remained low in recent years, the frequency of auto accidents is on the rise. Air bags, seat belt usage, and a reduction in alcohol-related incidents are all contributing to the reduction in the number of deaths and serious injuries; however, there is still much room for improvement. Crash rates for teenage drivers are double those of cars used only by adults.

High Cost of Auto Accidents

The economic cost of automobile accidents alone is nearly $200 billion annually. This is due to several factors including rising medical costs, the increasing cost to repair higher-valued vehicles, and the tendency to engage in legal battles following accidents. Economic losses also include loss of wages and cost to administer insurance claims.

In 1998, the estimated average cost of a motor vehicle accident was:

- Accident involving death $980,000
- Accident involving other than fatal injuries $ 35,600
- Accident involving only property damage $ 6,400

Young Drivers

In 1999, 5,749 teenagers were killed in car accidents. Youthful operators of motor vehicles are disproportionately affected by automobile accidents. Their accident rates are higher, their fatality rates are higher, and the incidence of alcohol-related deaths is higher than in the general population, although teens are less likely to drive after drinking. The main reason for these problems is inexperience. Driving is one of those things that can only be learned by doing, so the older you get, the better driver you become, on average.

What can you do to reduce the likelihood that you will become a statistic? Following are examples of things teen drivers can do to reduce the risk of being killed or injured in automobile accidents:

- **Slow down**—45% of accidents in which young people are killed involve speeding
- **Wear your seat belt**—teenagers are less likely than adults to use seat belts
- **Reduce nighttime driving**—about half of all fatal accidents involving teenagers occur at night, especially on the weekend
- **Drive alone**—the risk of being involved in an accident increases with the addition of each passenger
- **Don't drink and drive**—alcohol combined with inexperience at driving is a deadly combination

Graduated Licensing

Many states have now enacted laws for graduated licensing of youthful drivers. The idea behind these laws is to limit the exposure of young people and thus reduce the number of accidents. Graduated licensing is designed to provide newer drivers with an opportunity to gain experience behind the wheel under conditions that minimize risk. Florida was the first state to adopt this type of law and a majority of states now have some form of graduated licensing. An evaluation of those early adopters of the law shows a sharp reduction in accidents involving youthful operators.

Activity 3.1

Do research to see if your state has a graduated licensing law. If you do, list the restrictions. If not, choose a state that does and list the restrictions for that state.

COMPENSATION OF AUTO ACCIDENT VICTIMS

Under our legal system, those people who suffer injuries or have their property damaged as a result of automobile accidents are entitled to some form of compensation. There are a number of ways to provide this compensation.

Financial Responsibility Laws

Every state has what is called a financial responsibility law. These laws require a person to provide proof that they are financially responsible in certain circumstances:

- Following an accident in which someone is injured

- Following an accident in which there has been property damage in excess of a certain amount, usually $500
- After conviction for a serious driving offense, such as a DUI, reckless driving, or vehicular manslaughter
- When a driver's license has been suspended or revoked, prior to its reinstatement
- If the driver has failed to pay money owed from previous accidents

Financial responsibility laws vary by state, but all involve an amount of money for each person injured in an accident, a total amount for all persons injured in an accident, and a separate amount for damage to property. A list of financial responsibility limits is included in the Appendix at the back of this textbook. The highest amount of financial responsibility is required in Alaska, where a person must provide $50,000 for injuries to each person, $100,000 for the total of all injuries, and $25,000 for damage to property. The lowest requirement is in Mississippi, which only requires $10,000 per person and $20,000 per accident for injuries and $5,000 for damage to property.

The most common method used to demonstrate financial responsibility is with an automobile insurance policy.

Compulsory Insurance Laws

All but a few states also have a compulsory insurance law, making it illegal to operate a motor vehicle without insurance. Compliance with the law can be checked at various points in time, for example:

- When a vehicle is registered
- When a driver's license is issued or renewed
- When a driver is stopped by a law enforcement officer
- When the driver has been involved in an accident

In states with compulsory insurance laws, no automobile insurance policy can be issued with a limit less than the state's financial responsibility law.

Negligence and Automobile Accidents

In most jurisdictions, a person who has caused an accident is legally responsible to compensate the victim or victims. This type of system involves the concept of negligence, which was discussed in the previous chapter. Following an accident, an investigation determines which of the parties was at fault and that person is considered legally liable to the other(s) for any injuries or damages. If both parties are at fault, the responsibility is shared based on the laws of the state. This system is referred to as the tort system. In the law, a tort is a wrongful act committed by one person against another and for which the negligent party is held responsible. Remember when Manuel rear-ended the car in front of him while adjusting his radio? Under the tort system, Manuel is legally liable because his negligent operation of a motor vehicle caused the injury or damage to the person in front of him.

No-Fault Auto Laws

In a few states, the tort system has been replaced with a no-fault law. Under this method, each person involved in an accident is responsible for his or her own injuries or damage and they seek compensation from their own automobile insurance company. The thought behind no-fault laws is that the amount of time spent investigating accidents and then pursuing legal action against negligent parties delays payments to victims and adds to the overall cost of vehicle accidents. This in turn increases the cost of automobile insurance. Under a no-fault system, a person is only entitled to pursue legal action against another person in limited situations, thus making accident settlements quicker and less costly. The effectiveness of no-fault laws has been hotly debated since they were first enacted over thirty years ago.

Uninsured Motorists Coverage

If an uninsured driver hits you, you may be able to obtain compensation under your own automobile insurance policy using the Uninsured Motorists coverage. In some states, Uninsured Motorists coverage is mandatory whenever liability coverage is purchased. The details of this important coverage will be discussed in greater detail in the next chapter.

Activity 3.2

Research your state's financial responsibility law and determine if insurance is compulsory in your state. Answer the following additional questions:

- **What are your financial responsibility limits?**
- **Is your state a tort or no-fault state?**
- **If you are currently a no-fault state, when did that change take place?**
- **What has been the impact on insurance premiums?**
- **Is uninsured motorists coverage required whenever liability insurance is purchased? Can you reject the coverage?**

Also research the laws in the states that are adjacent to yours. What are the differences?

Activity 3.3

Write a position paper that deals with the issue of no-fault coverage versus a negligence-based system to compensate auto accident victims. Which system do you favor and why?

REGULATION OF AUTOMOBILE INSURANCE

Insurance is primarily regulated by each of the states. Personal insurance is much more highly regulated than other types of insurance. The reason for this high level of scrutiny is that consumers of personal insurance products are considered to be less familiar with the complex business of insurance than are business firms.

Regulation of Personal Insurance Prices

The market for personal automobile insurance is very competitive, because there are many insurance companies who wish to insure good drivers. One of the major objectives of any insurance company is to earn a profit by providing insurance to the public. The economic laws of supply and demand govern a truly competitive market. If an insurance company charged too much for insurance, they would have no customers. If they charged too little, they would have a lot of customers, but would likely go out of business for failure to earn a profit.

Insurance regulators in each state, called commissioners, directors or superintendents, are responsible for:

- Ensuring that insurance coverage is available to people who must purchase it
- Making sure insurance companies do not charge excessive prices
- Determining if insurance companies are charging too low a rate and possibly going out of business

Insurance companies are not free to charge any price they wish. If prices are too low, the company may go out of business, leaving people who purchased insurance from them without any coverage for accidents they have. If prices are too high, the public will think that companies are "gouging" them for a product that is required by law. Neither of these situations is desirable for regulators, and so they review the rates charged by all insurance companies to determine if they are appropriate.

Regulation of Policy Denial, Cancellation or Nonrenewal

Since automobile insurance is required by law in most states, a marketplace must exist.

Insurance regulators also control the manner in which insurance may be denied, cancelled, or not renewed.

In some states, any person who qualifies as a "good driver" must be insured in the company of his or her choice. Once insured, a person cannot be cancelled or refused a renewal policy, except in a limited number of circumstances. If a person has a lot of accidents or receives a number of traffic violations, an insurance company is permitted to refuse a renewal policy since that person no longer qualifies as a good driver. The ability to deny, cancel, or refuse to renew personal automobile insurance is severely restricted by state laws.

INSURANCE FOR HIGH-RISK DRIVERS

In some cases, no insurance company might be willing to offer automobile insurance to a driver who has a long list of motor vehicle violations or several accidents, yet the law in most states requires these individuals to have automobile insurance. How can a person comply with the law until they have had a chance to clear up their past driving record?

Most states have a program, called an assigned risk plan or automobile insurance plan, which enables people to obtain insurance when they have been denied coverage from three or more insurance companies. The plan must accept the applicant (provided he or she has a valid driver's license), however the premium charged is substantial due to the higher risk represented by the driver. In addition, coverage is usually limited to the amount required by the state's financial responsibility law. Supplemental policies are often purchased to provide complete protection. The assignment usually lasts for three years, after which the insured may reapply to a standard insurer for coverage, assuming the driving record of the individual has shown improvement.

Summary

Automobile insurance is a significant part of the property and casualty insurance industry. Automobile accidents annually account for many injuries and death and a considerable amount of damage to vehicles and other property.

Some of the current problems with automobile insurance include irresponsible drivers, the increasing number of auto accidents, the high cost of repairing vehicles and healing injured people, and youthful operators who tend to have a higher-than-average chance of loss. Some states have enacted graduated licensing laws that attempt to deal with some of the issues pertaining to newer drivers.

Most states require that a driver be financially responsible for injuries or property damage caused by an automobile accident. These financial responsibility limits vary from state to state. In many states, insurance is required to provide proof of financial responsibility.

There are two major systems to compensate the victims of automobile accidents. One is the tort system in which there is a determination made as to who was primarily responsible for the accident. This person must then pay for the portion of injury or damage they caused to others. In the other system, no-fault laws, each person is responsible for his or her own injuries or damage. Since some people do not purchase automobile insurance, others must have Uninsured Motorists coverage to help pay the costs involved in accidents with uninsured drivers.

Automobile insurance is highly regulated. Both the prices charged and the manner in which insurance companies may refuse to issue or cancel policies is determined by the law in each state.

Plans are available in most states to allow people with poor driving records to purchase mandatory insurance coverages. Although costly, these plans are necessary to ensure that coverage is available when required by law.

CHAPTER 4

The Personal Auto Policy

Key Terms

- **Bodily injury**
- **Conditions**
- **Declarations page**
- **Deductible**
- **Definitions**
- **Endorsement**
- **Exclusions**
- **Family member**
- **Insurance Services Office**
- **Insuring agreement**
- **Medical payments**
- **Newly acquired auto**
- **Private passenger auto**
- **Property damage**
- **Temporary substitute auto**
- **Uninsured motorist**

This chapter contains a discussion of the Personal Auto Policy (PAP) that is used by many insurance companies. Every insurance company is different—in fact, most companies pride themselves on the distinctions between them and their competitors. In personal insurance, however, these distinctions are not nearly as substantial as they are for business customers. The Personal Auto Policy is one of the most standardized policies in insurance.

This chapter is designed to help you distinguish between (PAP) coverage offered by various insurers.

But there are differences and informed consumers must distinguish between the coverage offered by various insurers. Price alone should not be the sole determinant in choosing an insurance company or agent. As we said earlier, the personal auto insurance market is very competitive and it is a good idea to shop around and make sure that you are receiving the most value for your insurance dollar. That does not mean that you will change insurance companies or agents for a few dollars of premium savings. Rather, it means that you have given careful evaluation to the protection, service, and price of any insurance product you purchase.

LEARNING OBJECTIVES

When you complete this chapter, you should be able to:

- Describe the various parts of the Personal Auto Policy
- Explain the importance of the definitions section of the policy
- Describe the coverage provided by the various parts of the Personal Auto Policy
- Determine who is insured by each section of the Personal Auto Policy
- Discuss the miscellaneous provisions of the Personal Auto Policy

OVERVIEW OF THE PERSONAL AUTO POLICY (PAP)

The Personal Auto Policy (PAP) was first introduced in 1977. There were other policies prior to that time, and the PAP itself has been revised several times since then. The policy is written in plain language, without a lot of technical terms and is easier to understand than previous versions. The policy is a package, or bundle, of insurance coverages put together in one policy and designed to meet the needs of individuals and families who own automobiles.

The policy we will discuss in this text is the one developed by the Insurance Services Office (ISO). ISO is a non-profit organization that develops policy forms for member insurance companies. Although the policies developed by ISO are used by many companies, you should keep in mind that there are variations among insurers and the specific terms and conditions of any policy must be reviewed before deciding whether or not coverage is provided.

In order to discuss the PAP in more detail, it will first be necessary to review some of the basics of all insurance policies.

Sections of an Insurance Policy

Like other insurance policies, the PAP contains sections that combine to provide the necessary coverage. The sections of the PAP are:

Declarations Page

The declarations page is the front page of the policy where you will find the name of the person or persons insured, his or her address, a description of the vehicles covered, and other personal information. It is called a declarations page because it contains information that is declared by an applicant to the insurance company when applying for coverage. You will hear people refer to this part of the policy as the “dec page.”

Insuring Agreement

All policies contain an insuring agreement, which is a broad statement of the insurance company’s obligations under the policy along with the responsibilities of the insured or policyholder. It is usually brief, sometimes only a single sentence and may read like this: “If you (the insured) agree to pay your premiums, we (the insurance company) will pay your covered claims.”

Definitions

All modern insurance policies contain a definitions section, or glossary of terms used in the contract. When a term has been defined in a policy, it has been given special meaning. These words are shown in a policy by using italics, bold face type, or quotation marks. Some of the important definitions contained in the PAP are discussed in later parts of this chapter.

Conditions

Insurance policies are conditional contracts. This means that the insurance company is not obligated to pay all losses an insured might suffer. Coverage is provided only under certain conditions. For example, a vehicle is covered while it is operated in the United States, its territories and possessions (e.g., Guam), Puerto Rico, or Canada. Thus, if you drive your car to Mexico and it is damaged or you injure someone, there would be no coverage under your Personal Auto Policy. You can think of conditions as the “strings” attached to the insurance company’s promise to pay as stated in the insuring agreement.

Exclusions

Since the insuring agreement is so broad, the policy contains a list of exclusions that more clearly define the coverage provided by the policy. Insurance companies do not put exclusions in policies simply to get out of paying legitimate claims. Exclusions are designed to eliminate coverage that should be provided by other policies the insured purchases, to eliminate coverage for catastrophic or uninsurable events such as nuclear war, or to keep premiums reasonable by covering only those events that are potentially serious for the insured. There is no reason an insurance policy could not cover absolutely every situation—except for the fact that no one could afford to pay the premium.

Endorsements

Insurance policies are designed with the average policyholder in mind. Since people have special needs, policies must be modified or tailored using endorsements. An endorsement is a policy change.

Quick Quiz 4.1

Match the terms to the example given or their description.

_____ Declarations page	1. A policy provision that eliminates coverage.
_____ Insuring agreement	2. The glossary of terms used in a policy.
_____ Definitions	3. Where the insured's address is found.
_____ Condition	4. A broad description of what the insurer will do.
_____ Exclusion	5. A document that changes an insurance policy.
_____ Endorsement	6. A requirement that claims be promptly reported.

Who Can Purchase a Personal Auto Policy?

The Personal Auto Policy is intended for individuals and families who own or lease private passenger automobiles. A private passenger automobile is a car, van, station wagon, pick-up truck, or sport utility vehicle (SUV). The PAP has some restrictions on pick-ups and vans. They must weigh less than 10,000 pounds and not be used to deliver merchandise. The reason for the restriction is simply to ensure that commercial-type vehicles are not covered using a Personal Auto Policy. A separate policy is available for businesses and other organizations that own commercial vehicles.

Individuals and married couples who own or lease private passenger automobiles may be insured under the PAP. Unrelated people who live in the same household and share ownership of a vehicle also may be insured by the PAP, provided each is listed as an individual.

Summary of Coverage in the Personal Auto Policy

In addition to a declarations page, an insuring agreement, and a definitions section, the Personal Auto Policy contains six additional sections or parts:

Part A—Liability Coverage

This section provides protection when you are held legally responsible to others for bodily injury or property damage that is caused by an auto accident. Coverage is generally provided when:

- You or your family members are using your own car ("your covered auto")
- You are using someone else's vehicle (a non-owned auto)
- Other drivers are using your car with permission

You are covered when you use any auto. You have coverage under your own auto policy while driving your own car, when you borrow a friend's car, or when you rent a car.

Also, people who use your car with your permision are covered by your policy. Let's say you loan your SUV to a friend who uses it to go skiing. While returning from the ski trip, she has an accident and injures several people who are in another vehicle. She would be insured under your Personal Auto Policy. The insurance policy that covers the car is considered the primary insurance. Any coverage the driver has is secondary.

Let's look at the definition of some of the terms used in this part of the policy:

Bodily Injury (BI) is bodily harm, sickness, or disease, including death. This coverage applies when your car injures people in other vehicles, pedestrians or bicyclists, or passengers in your vehicle.

Property Damage (PD) is physical injury to or destruction of or loss of use of tangible property. This coverage does not only apply to other vehicles, but also to buildings, telephone poles, fences, or any other property you might damage with your vehicle. The last part of this definition is important. If you hit someone and it takes 5 days to repair their vehicle, they will probably have to rent a car to get to work or school. The cost of their rental car is covered under your property damage coverage since it represents the "loss of use" of the vehicles.

Your Covered Auto includes four different types of vehicles that are covered under the PAP:

- The vehicles listed in the declarations (your car)
- A newly acquired vehicle (subject to certain restrictions), which means a new car you purchase in addition to one you already own or as a replacement for one you own
- A trailer you own
- A temporary substitute vehicle, which is one being used by you while your car is out of service due to breakdown, repair, servicing, loss, or destruction. If you take your car to the shop and they loan you a vehicle while yours is being fixed, it is considered a temporary substitute auto.

You means the person whose name is shown on the declarations page and your spouse if they reside with you.

Family Member means a person related to you by blood, marriage, or adoption who lives in your household.

These definitions are also important for the following sections of the PAP.

The limit of coverage under Part A is expressed as a dollar amount per person for Bodily Injury, a total amount of Bodily Injury for each accident (no matter how many people are hurt), and an amount for Property Damage for each accident. The minimum limit under any policy is the state financial responsibility limit.

Let's look at an example of how this coverage applies in the event of an accident. Let's say you live in California, where the minimum limit for an auto policy is $15,000 per person for BI, $30,000 per accident for BI, and $5,000 for PD. One rainy day, while driving your best friend to school, you swerve to avoid a pothole in the road. Unfortunately, you don't notice the car in the next lane until it is too late. You hit the other vehicle, causing it to swerve off the road, striking a fence. There is a mother and her small child in the other car. As a result of your negligence, the following injuries and damage occur:

Injuries to your best friend in your vehicle:	$ 3,000
Injuries to the small child:	$ 10,000
Injuries to the other driver:	$ 25,000
Damage to the other vehicle:	$ 15,000
Damage to the fence:	$ 2,000

The maximum amount that can be paid to any one person is $15,000. Therefore, the policy will pay your friend's claim for injuries in full. The injuries to the child will also be paid in full. The medical costs for the other driver, however, will only be paid up to the per person limit of $15,000—leaving you to pay the balance of $10,000 out of your own pocket. The total of all injuries payable under the policy ($3,000 + $10,000 + $15,000) is $28,000, less than the per accident limit of $30,000.

As far as Property Damage, the total amount available under the policy is only $5,000. The cost of all the damage, however, is $17,000. This leaves you responsible for $12,000, plus the $10,000 in Bodily Injury you owe. We will discuss the importance of having adequate limits in a later section of this text.

Quick Quiz 4.2

Briefly explain what is meant by the following terms in an automobile insurance policy:

1. Bodily Injury

___

2. Property Damage

___

3. Your Covered Auto

___

4. You

___

5. Family Member

___

Part B—Medical Payments Coverage (Med Pay)

Medical payments coverage pays for medical expenses for you, your family members, and passengers in your car that result from auto accidents. You are also covered when you are a passenger in another vehicle or when you are a pedestrian if a vehicle hits you. This coverage is not based on fault, so you are entitled to the coverage even if you are the cause of the accident.

The limit for Medical Payments applies per person, and there is no limit on the number of persons. Most people purchase a limit of between $1,000 and $5,000 for this coverage, although higher limits are available.

Part C—Uninsured Motorists Coverage (UM)

Uninsured Motorists coverage pays you if you are struck by someone who does not have insurance. It also would pay if you were hit by a hit-and-run driver. The fact that you don't know who hit you means you are unable to determine whether or not they have insurance, so it is assumed they do not. Coverage is also provided if you or your family members are struck as pedestrians by a vehicle that is not insured.

You will collect whatever amount of injuries or damage the other person is legally responsible for. Note that you cannot collect from your insurance company simply because the other person's insurance company refuses to pay your claim. When this happens, it is usually due to the fact that the other party's insurer feels their policyholder was not at fault, and therefore is not legally responsible for the accident. In addition, by definition, they are not uninsured.

The limits for UM coverage are usually the same as those under Part A—Liability. They may be increased in most cases. In most states, an insurance company must include UM coverage in every policy that provides liability protection, unless the insured rejects the coverage by signing an acknowledgment that they do not wish to have the coverage. Given the large number of automobiles driven by people who do not carry insurance, it is usually an unwise decision to refuse UM coverage.

Underinsured Motorists Coverage (UIM)

Think about this situation—if you are hit by an uninsured driver, you may be able to collect under your own Uninsured Motorists coverage. Let's say your UM limits are $25,000 per person, $50,000 per accident. What if the person who hits you is insured, but their liability limits are only $15,000/$30,000. You would be better off if they had no insurance at all, because your Uninsured Motorists coverage would pay more than their liability limits! To rectify this situation, insurers also include what is called Underinsured Motorists coverage. If you are hit by a driver whose liability limits are less than your UM, the UIM coverage will pay the difference between the amount covered under their policy and your UM limit.

Given the large number of automobiles driven by people who do not carry insurance, it is usually an unwise decision to refuse UM coverage.

An example might be helpful. Let's say you insure your automobile with $50,000 per person and $100,000 per accident Uninsured Motorists coverage. You are struck by a vehicle and the driver carries only the minimum financial responsibility limits required in the state, $25,000 per person, $50,000 per accident. You are seriously injured and your medical bills amount to $35,000. The other driver has only $25,000 in coverage available to pay for your injuries. The balance, $10,000, would be paid by your Underinsured Motorists coverage, since the limit of the other person's insurance is less than yours.

Part D-Damage to Your Auto

The final section of the Personal Auto Policy is Damage to Your Auto. There are actually two different coverages provided by this section of the policy:

- Collision, which covers damage caused by impact with another vehicle or object, or overturn of your vehicle;
- Other Than Collision, also called Comprehensive coverage, which provides protection from theft, fire, windstorm or hail, flood, falling objects, collision with a bird or animal, and virtually all other types of physical loss to the vehicle EXCEPT:
- Road damage to tires (a flat tire or blowout)
- Mechanical breakdown (the engine just quits running)
- Wear and tear (the car simply gets old)

There is no limit in this section of the policy. The amount you will receive if your car is damaged is the actual cash value of the vehicle, or the cost to repair the damage. In some cases the amount to be paid by the insurance company is simply the cost to make repairs to the vehicle and a check is usually issued to the body shop. In other cases, the vehicle is "totaled", meaning the cost to repair it is more than the value of the car. In this case the insurance company will pay a sum of money as compensation for the loss of the car. Determining the actual cash value of an automobile can be tricky. We always think our car is in better shape than the average car and therefore, expect to be reimbursed based on our estimation of what the car is worth. The insurance company will probably determine the value of the car based on what similarly equipped vehicles are selling for in the used car market. That may be more or less than you think is a fair settlement.

You may remember discussing the risk management technique of retention in Chapter 2 of this textbook. Part D of the Personal Auto Policy contains a deductible provision, or an amount you must be responsible for when you have a loss. You must retain $100, $250, or $500 of each loss. You may choose the deductible that represents your ability to pay in the event of a loss. That means that if you have a very small loss, such as a broken window or a scrape on your fender, your insurance company would pay nothing and you would have to absorb the cost yourself.

Section D of the policy is not required and there may be certain situations when you would decide not to have this coverage under your policy. For example, if you have an old car that has a very low value, you might forego physical damage insurance since the cost of the coverage over time might be more than the value of the car if it is damaged. If you could replace the car for $4,000 and the cost of Comprehensive and Collision coverage was $800 per year, you would probably decide to not have the coverage since in five years the total amount of the insurance premiums would equal the value of the car. You could just save the $800 each year, put it in a savings account, and withdraw the money when you need it to buy another car. Hopefully, you are able to go five years without an accident, so the value of your savings account would be $5,000 plus interest!

Uninsured Motorists Property Damage (UMPD)

Uninsured Motorists coverage was originally designed to pay for your injuries when struck by an uninsured driver. However, if the other party has no insurance, who will pay for the damage to your car? If you carry insurance for Collision, your policy would pay, but you would be responsible for the first $100, $250, or $500 of the damage due to your deductible. If you don't carry Collision insurance, as we discussed above, you would have to pay the damages yourself. Since that situation seemed unfair to policyholders, insurance companies began to include UMPD coverage as an option. When you buy UMPD, you will receive one of two types of compensation if you are involved in an accident with an uninsured driver:

- A waiver of your Collision deductible (CDW); OR
- Up to $3,500 for damage to your auto

Part E and Part F—Duties After an Accident or Loss and General Provisions

The final two portions of the Personal Auto Policy outline certain duties of the policyholder and the company in the event of an auto insurance claim. When you have a claim you must:

- Notify the company of when and where the accident happened, including the names of any people injured or witnesses to the accident
- Cooperate with the insurance company as they attempt to settle your claim
- Notify the police if struck by a hit-and-run driver
- Notify the police if your vehicle is stolen
- Allow the insurance company to inspect the damage to your auto before it is repaired

You may cancel your auto insurance at any time you wish by notifying the company or your agent. The insurance company may cancel your insurance if they notify you in writing of their desire to do so. They may do this when you fail to make premium payments or when you have your driver's license suspended or revoked.

Quick Quiz 4.3

Answer the following questions.

1. An insurance coverage that provides payment for doctor and hospital bills for people riding in your vehicle who are hurt in an automobile accident is:

A Bodily injury liability
B Damage to your auto coverage
C Medical payment coverage
D Property damage

2. Each of the following is included in Part D—Damage to Your Auto EXCEPT:

A theft
B fire
C wear and tear
D collision

3. If you have an uninsured motorists limit of $100,000/$300,000 and you are struck by a vehicle with liability limits of $50,000/$100,000, what is the maximum amount of underinsured motorists coverage your insurance company will pay for injuries you and your passengers suffer:

A $100,000/$300,000
B $50,000/$200,000
C $50,000/$100,000
D nothing since the other vehicle is insured

4. All of the following are duties of the policyholder following a loss EXCEPT:

A report a stolen vehicle to the police
B submit to a medical examination
C allow the insurance company to inspect the damage
D notify the company of where and when the accident occurred

Summary

The Personal Auto Policy (PAP) designed by the Insurance Services Office is the standard contract used by many insurers. Like all insurance policies, the PAP contains a declarations page, an insuring agreement, definitions, conditions, and exclusions. Changes that are made to a policy after it is issued are done using an endorsement.

The PAP is designed to meet the needs of individuals and families who own private passenger type automobiles, pick-ups, vans, and sport utility vehicles. The policy is not designed for commercial trucks or vehicles owned and operated by businesses.

The Personal Auto Policy contains six sections including Part A—Liability Coverage, Part B—Medical Payments, Part C—Uninsured Motorists Coverage, and Part D—Damage to Your Auto. Parts E and F contain provisions that require policyholders to do certain things in the event of an accident or claim. These duties include notifying the company when a loss has occurred, cooperating with the company in settling the claim, notifying the police if a crime has been committed, and allowing the insurer to inspect damage to the insured vehicle before it is repaired.

CHAPTER 5

Marketing and Selling Auto Insurance

Key Terms

- Direct response company
- Exclusive agent
- Independent insurance agent
- Market segmentation
- Mixed marketing system
- Niche marketers
- Prospect
- Quote
- Regional companies
- Specialty insurers
- Target marketing

This chapter discusses the various ways personal automobile insurance is marketed and sold to the public.

Insurance companies vary greatly in the way they choose to market their products and services to consumers. We will examine the marketing process that an insurance company uses to determine which customers will be served, what products will be developed, and how the product will enter the market place.

One of the biggest changes taking place in the insurance industry is the way insurance companies distribute their products. We will discuss the various distribution methods used by insurance companies and the reasons they select different methods.

Finally, we will discuss how to shop for insurance and what you should consider before you enter into an insurance contract.

This chapter discusses the various ways personal automobile insurance is marketed and sold to the public.

LEARNING OBJECTIVES

When you complete this chapter, you should be able to:

- Describe the steps an insurance company takes in order to market its products
- Describe how an insurance company uses market segmentation and target marketing
- Discuss how an insurance company decides what products to sell
- Discuss the advantages and disadvantages of each distribution method
- List the questions to consider when shopping for automobile insurance

THE INSURANCE MARKETING PROCESS

In order to achieve their business objectives, insurance companies must develop a marketing strategy. If they don't sell something, nothing else matters, so the sales and marketing function in the company is of paramount importance. Like organizations in other industries, insurance companies must follow a process that includes the following steps:

- Identify the customers or potential customers to whom the company wishes to sell
- Determine what products will be sold based on the customers' needs and desires
- Develop the products and determine the appropriate price that will ensure the organization reaches its goals and complies with regulatory requirements
- Select the distribution method that will be used to sell the products

Identifying Customers

Insurance companies determine a basic profile of the type of customer they think they can best insure at a profit. In order to do this they conduct market research to identify the size of the potential market and the buying habits of persons in the market place. They may segment the market into distinct categories, such as baby boomers, Gen Xers, or retired persons. By segmenting the market they are able to match products and distributors to the needs of those markets. The insurance needs of young adults and retired people are vastly different, and identifying potential market segments is generally very beneficial to an insurance company.

Some insurance companies only do business in certain geographical areas. They are referred to as regional companies, and they insure only those individuals who reside within their chosen territory. Because they only do business in a certain territory, these companies may better understand their customers' needs and can react quickly to changes in the local marketplace.

Other insurers do business on a national basis, but only with certain types of clients. They are called specialty insurers, or niche marketers, since they specialize in only certain types of insurance or certain types of customers. A company that only writes personal insurance or one that insures only retail stores or farms is an example of a specialty insurer.

Market Segmentation

A general term for deciding what portion of the market to serve is market segmentation. A market segment is a group of consumers who share some common characteristics, such as where they live, what their lifestyle is like, or what they like to do for recreation. Insurance companies then use target marketing, which is aimed at only one of the identified market segments, to prepare a list of potential customers or prospects. Deciding to write insurance only for high school students is an example of market segmentation. The target market would then be anyone who attends high school, provided the individual otherwise meets the insurance company's requirements such as being a licensed driver, having a good driving record, or maintaining a "B" average.

Activity 5.1

Do research to find examples of specialty insurance companies. For example, Progressive Insurance Company is a national insurer that specializes in personal insurance. USAA is a company that provides insurance only to members of the U.S. military and their families. There are companies that specialize in doctors, dentists, churches, agriculture, high-risk drivers, and auto dealers. Who are the companies and where do they operate?

Determining What Products to Sell

In order to be successful in marketing its products, an insurance company must be able to offer those types of insurance products that potential customers wish to buy. Therefore, it is important to determine the customers' needs and desires. When purchasing insurance for the first time, a high school student may only be interested in obtaining the minimum amount of insurance required by law (although, as we have discusssed previously, this is generally not a good decision). Since he or she may purchase an older vehicle, physical damage insurance (collision and other than collision) may not be desired. Therefore, it is important that the insurance company offer a variety of coverage options so the customer can tailor the policy to fit their individual needs.

Some people feel that personal insurance is a commodity, meaning it doesn't matter from whom the product is purchased, it will all be the same. This is not really the case, since part of what is purchased along with an insurance policy is the service that will be received from the company's representatives. Although personal insurance products are somewhat standardized, they still contain variations that may be important to you as a buyer. Insurance companies use product and service differentiation as a competitive advantage in marketing and selling.

Developing the Products and Determining an Appropriate Price

Since insurance is a highly regulated business, insurance companies are not free to design policies without seeking the approval of the insurance department in most states in which the product will be sold. This can be a time-consuming process, but is a legal requirement that must be met. The insurance contract, called a form, must be broad enough to provide the protection sought by the policyholder and be reasonably easy to read and understand. Insurance regulators ensure that the forms meet these requirements.

Pricing the insurance product is equally difficult. Insurance is one of the few products sold where the ultimate cost is unknown until long after the price is determined. Think about it this way—when an insurance company is determining the amount of premium to charge, it is probably months or even years before they will be able to sell the first policy. This is due to the length of the regulatory process in obtaining approval for the policy. Even when the product is in the market place, the amount of money the insurance company may have to spend to settle claims under the policy is yet to be determined. If you are involved in an auto accident, it may take years to determine the exact amount for which you are liable, meaning the company will not know its' ultimate cost of providing the insurance until many years after the price was determined. If the insurance company charged too high a price, they are usually unable to make a refund to the policyholder. If they charged too little, they cannot go back and ask the customer to pay more. Contrast insurance with a fast-food restaurant. If you are selling hamburgers, fries, and soft drinks, you can easily determine the cost of purchasing those items in the wholesale market. You also know what your labor cost is, as well as the cost to buy or build a restaurant location. When you know what your costs are, you can easily determine your desired profit margin and then set the price of hamburgers and other items at a level that will cover your costs as well as produce a profit for you. This is not so in insurance!

In general, insurance regulators require that companies charge a price that is sufficient to cover any claims that occur. It would not be in the public's best interest if the insurer went bankrupt and was unable to pay its policyholder's claims. The regulator is also concerned that the company not charge too much for insurance. Companies are allowed to make a fair rate of return, but may not charge an excessive amount. The final requirement for insurance pricing is that the rates charged not unfairly discriminate among policyholders. Insurance is a discriminatory business—insurance companies seek to differentiate their policyholders based on the chances of their suffering a loss. Teenage drivers, due to their higher than average chance of being involved in an auto accident, pay higher rates. People with poor driving records are charged more than those with clean records. These are all forms of price discrimination and are legal and appropriate given the underlying chance of loss. Unfair discrimination, however, is not based on chance of loss and is therefore illegal. This is a form of discrimination that uses gender, ethnic group, or national orgin solely as the basis for determining whether or not to insure someone or what to charge for the insurance. If prices are different for male and female drivers, it must be based on accident statistics, not simply the fact that one person is a different gender than the other. The terms used by insurance regulators for these features of rates are:

- Adequate (not too low)
- Not excessive (not too high)
- Not unfairly discriminatory

As long as a company can demonstrate that these three requirements are met, they will be allowed to offer coverage at the price they wish to charge. More discussion on pricing personal automobile insurance will be included in the next chapter.

Activity 5.2

Review magazines, newpapers, and other publications and choose an insurance company advertisement. Write a brief paper that answers the following questions:

1. What is the company's geographic area of operation (local, regional, national)?

2. What type of customer does the company target (business, personal)?

3. What is your opinion of the effectiveness of the company's marketing strategy?

4. Determine a marketing strategy you would use if you were operating an insurance company or agency.

Selecting the Distribution Method To Be Used

There are many ways to distribute insurance products and not all methods are used by each insurance company. The major distribution methods used by companies are:

- The independent agency system
- The exclusive agency system
- The direct response method

Each system has its advantages and disadvantages and the insurance company must choose the distribution channel that best fits its style of doing business, marketing objectives, customers' needs, and geographic area of operation.

Independent Agency System

An independent insurance agent is one who represents a number of insurance companies. When a client buys insurance from him or her, the agent determines which of the companies he or she represents is best suited to the needs of the customer. In effect the agent becomes the comparison shopper for the customer, obtaining the best price based on the needs of the client and the products and services offered by the companies represented. The ultimate purchasing decision is always made by the client, however, with the agents advice and counsel. (To locate an independent insurance agent, go to www.iiaa.org and click on "Find an Agent".)

Exclusive Agency System

When a company uses an exclusive agent, the agent is contractually obligated to represent only that company. Therefore, if the insurance company does not wish to insure the prospect, the agent must also decline the insurance. State Farm is an example of an exclusive agency company, since the State Farm agent may only sell policies offered by that company and may not write policies for people who do not qualify for the company's products. (To locate an agent for State Farm, go to www.statefarm.com and click on "Find an Agent".)

Direct Response System

Some companies have decided not to use agents at all. Instead, they sell insurance using company employees who work in a company-owned facility. In most cases, marketing and selling is done exclusively by mail or phone and the customer is unable to visit the agent's office. Obviously, if the person selling insurance is an employee, they are obligated to sell only their company's products. GEICO, and Nationwide are examples of direct response insurance companies. (To access direct response companies, go to www.GEICO.com or www.Nationwide.com.)

Emerging Distribution Systems

Because customer needs are constantly changing, some companies try to adapt by making alternative distribution systems available to purchase their products. When a company uses independent agents, but also sells products direct through company employees, they are said to use a mixed marketing system. Many companies are currently using these types of arrangements in hopes of appealing to a broader range of consumers.

Internet Sales

Many people are comfortable shopping for insurance online. They can access a number of websites that give them a comparison of the rates charged by various insurers. They also can access the website of a particular company and get a premium quote or indication. Although many people use the Internet to obtain information about insurance prices, they may still use the services of an agent after they have done the initial research.

Sales Through Banks

Recent legislation passed by the U.S. Congress and signed into law by the President has made it possible for insurance to be sold by banks and other types of financial institutions. This "blending" of the financial services industries has opened up opportunities to insurers and their agents. Agents who partner with banks may be able to access the database of the bank to obtain new customers. Banking customers are able to complete loan applications and apply for insurance products in a single location.

Kiosks

In some areas, insurers are experimenting with a system similar to the bank ATM. If you wish to purchase insurance, you simply go to a kiosk in a mall or other high traffic area, enter information using a touch screen, and get a premium quotation. This system has been used in England for a number of years. If you wish to purchase the policy, you can transmit your application to the company and you will be notified by phone, fax, mail, or e-mail of your acceptability.

Which Method is Best?

How you choose to purchase insurance is dependent on several factors. Most people do not feel they know enough about the product to complete the transaction without using an agent. Others seek convenience and low prices, so they are likely to use an 800 number or the Internet.

When an insurance company selects a distribution method, they must consider the wishes of their target customer group. If the target group is younger and the company specializes in personal insurance, Internet access might be required. If, on the other hand, the company focuses on businesses that generally require more complex products, an independent agent system of distribution might make more sense.

There is no one best method and many companies are currently using a combination of methods in an attempt to meet the varying needs of their customers. One thing is certain, however—purchasing insurance can be a very time-consuming and complicated task without professional help. Just as you would not think of taking out your own appendix or filling your own cavity, you should consider getting sound, professional advice when you purchase insurance.

SHOPPING FOR AUTOMOBILE INSURANCE

Because it is a competive business, shopping around can result in your paying less for auto insurance. A good starting point is to check with your state's insurance department, either by phone or via the Internet. Many states have consumer brochures specifically designed to help you ask the right questions. In general, it is usually less expensive to be added as a driver on your parents' automobile policy than to have one of your own, but there may be reasons why this is not possible.

Based on the earlier discussion of how insurance is distributed, you must then determine whether to approach a direct response company, an exclusive agent company, an independent agent, or a combination. You may also wish to do some comparison shopping on the Internet. Whichever method you choose, be sure you have all the appropriate information ready. You can use the sample application and the information contained in this textbook to help you.

Remember that price is not the only consideration when purchasing insurance. You must be comfortable with, and confident in, the agent who will represent you. Ask your family or friends for a referral to an agent they have been happy with in the past. Also important is the company's ability to pay any claims you may have. You should inquire about complaints that have been filed against the company and their financial stability. This information can be obtained from your state department of insurance.

Activity 5.3

Using the Internet, obtain three quotations for automobile insurance. If you don't own a car, select your "dream car". Be sure to include coverage for liability, medical payments, uninsured motorists, underinsured motorists, and damage to your auto (comprehensive and collision). Compare the three prices you get and try to determine why they vary. What is the type of distribution system used by each company? [CAUTION: Do not purchase anything! The purpose of this activity is to help you understand how various insurers price their products.]

Activity 5.4

Investigate your state's insurance department website. What type of information is contained there? If possible, perform the following activities:

- **See if the department publishes complaint ratios for the companies you obtained quotations from in Activity 5.3. What are those ratios? Are they good or bad?**
- **Does the department include a comparative rater or other means to compare prices offered by the various insurers operating in your state?**
- **What type of information is available to assist consumers in shopping for automobile insurance?**

Summary

Marketing and selling are two of the most important activities conducted by an insurance company. Marketing is the process of identifying which customers a company will serve and what products will be offered. It is important to determine the needs of the consumer and develop products that fit those needs at a cost that is competitive.

Insurance is a highly regulated business. The price charged for insurance is subject to much regulatory scrutiny. In all states, insurers are required to charge premiums that are adequate to pay for covered losses. In addition, premiums charged must not be so high that they produce excessive profits. In every case, insurance companies may not discriminate against applicants or insureds based on a factor that does not directly relate to the chance of a loss occurring.

An important marketing decision for an insurance company to make is how its products will be distributed. The primary distribution methods for property and casualty insurance are independent insurance agents, exclusive agents, and direct response systems. Each method has advantages and disadvantages. Insurers are currently investigating other methods of distribution, such as the Internet, sales through banks, and affiliations with other organizations.

When shopping for insurance, it is important to compare prices from a variety of insurers. Although price should not be the sole determinant of where you buy your insurance, it is wise to shop around. In the end, you must be confident that the insurance you have purchased is the right type and amount to meet your needs.

CHAPTER 6

Determining the Price of Personal Auto Insurance

Key Terms

- **Actuary**
- **Application**
- **Base rate**
- **Class rates**
- **Good student discount**
- **Insurance premium**
- **Law of large numbers**
- **Primary rating factor**
- **Rate**
- **Secondary rating factor**
- **Underwriting**
- **Underwriting guidelines**

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This chapter will discuss the underwriting process, the various risk factors that affect the cost of insurance and how insurance, companies use the money paid to them by policyholders.

Surely one of the most frustrating parts of being a teenager is discovering how much you will have to pay for automobile insurance. You've just passed the state test, you've got your license, you're all set to go, and then someone informs you that in addition to gasoline and vehicle maintenance, you must pay for insurance too.

In most states, automobile insurance is compulsory, meaning it is against the law to operate a motor vehicle without insurance. Although it is costly, there are ways to reduce your automobile insurance premiums. This chapter will provide a discussion of how insurance companies determine both who they wish to insure and how much they will charge for the coverage.

You will learn about one of the most important processes an insurance company completes—the underwriting process. We will also discuss how insurance companies use the law of large numbers to arrive at the price to be charged each policyholder.

Finally, the text will discuss the various risk factors that affect the cost of insurance and how insurance companies use the money paid to them by policyholders.

LEARNING OBJECTIVES

When you complete this chapter, you should be able to:

- Understand the underwriting process used by insurance companies
- Describe the use of underwriting guidelines in determining if an applicant is acceptable
- Discuss the role of an insurance actuary
- Describe how an insurance company uses statistics to develop rates
- Calculate an insurance premium given a rate
- Identify the factors that can control the cost of automobile insurance

One of the biggest concerns young drivers have is the cost of automobile insurance. Why do guys pay more than girls? Why do young people pay more than adults? And why is car insurance so expensive? Let's take a look at how an insurance company operates and how the price of insurance is determined.

How an Insurance Company Decides Who to Insure

Unlike the sale of other products, insurance companies are very selective about who becomes their customer. They "interview" each applicant to determine if the person fits the company's profile. That profile is important, because it represents the company's best chance to make a profit in the long run by selling insurance policies to particular individuals who will not suffer higher-than-average losses.

This interview is conducted using an application and the opinions of the company's agent, customer service representative, or other person who assists you in filling out the application. The application asks for information about your driving experience, tickets, accidents, age and type of vehicle, vehicle use, etc. It is important that you be completely truthful when completing an application for insurance. If you use your car to deliver pizza at night, the company has a right to know that information since that kind of activity could result in a higher number of losses than using a vehicle to go back and forth to school during the daytime.

When a completed and signed application is received by the insurance company, it is reviewed by an underwriter. Underwriting is the process an insurance company uses to determine who will be offered an insurance policy and at what price. Every insurance company has guidelines to assist underwriters in determining whether or not the applicant represents the kind of risk the company believes will result in a long-term profit. These underwriting guidelines detail the company's criteria for acceptance or rejection of an applicant. Since they are guidelines, as opposed to rules, the underwriter must still use his or her sound judgment to determine an applicant's acceptability.

Underwriters may do one other thing in addition to accepting or rejecting an applicant. Sometimes a risk that appears to be unacceptable could be made acceptable if it was modified. For example, perhaps a person has had a number of relatively small claims. This would be of concern to an underwriter, who must attempt to write business that will be profitable for the company. If the insured would accept a higher deductible, the likelihood of small claims would be greatly reduced. What would previously have resulted in a rejection is now acceptable by making a minor modification to the coverage requested.

Once the underwriter has determined that the applicant is acceptable, the next step is to figure out how much to charge for the insurance.

How an Insurance Company Determines the Price of Insurance

Determining the price to charge a policyholder is a complex issue. As we discussed in Chapter 5, insurance is a very competitive business. Insurance companies are concerned that they charge a price that will enable them to sell products while still making a profit for the company. In addition, insurance is a highly regulated business and insurance companies are not free to charge any price they wish.

To help them figure out these complex issues, insurance companies use the services of an actuary. An actuary is a person who has received many years of specialized training in mathematics and statistics and has been certified by the Casualty Actuarial Society. He or she will review the past loss history of a group of people, look at their risk characteristics, make projections about the future, and develop a rate that the company will charge for all customers who have similar risk factors. The rate must be sufficient for the company to pay claims in the future, pay its expenses, and make a reasonable profit.

Insurers use the law of large numbers to estimate the losses a certain group of insureds may have in the future. Using statistics, the actuary looks at losses that have occurred in the past and determines that approximately two out of 100 policyholders will have a claim. Thus, if the company writes 100 automobile policies, they may expect to pay two claims. You may recall that this is referred to as loss frequency. The other thing the actuary must determine is the average cost of claims over time, or loss severity. If the average claim resulted in the company paying $1,000, then the actuary will predict that total losses for the upcoming year will be $2,000 (2 claims for $1,000 each). The law of large numbers states that as the number of policyholders increases, the more assured the company can be that the actuary's prediction will turn out to be true. Therefore, insurance companies attempt to acquire a large number of similar policyholders who all contribute to a fund out of which the losses of the few will be paid.

An illustration may help you better understand the law of large numbers and how it relates to insurance. Suppose you had a standard deck of cards containing 52 cards, 13 in each suit. What are the chances that you could pick one card and pull out the ace of spades? It's one in 52, because there is only one such card in the deck. If someone told you he'd give you $100,000 if you could pick the ace of spades with a single draw, but that you would owe him $100,000 if it was not there, would you take that bet? How about if the person said you could draw four times? Ten times? Wouldn't you be more confident taking that offer if you knew you could improve your odds by making more draws? Well, insurance is much the same. The insurance company may know that on average two out of 100 homes will burn in a given year, but they will be much more confident in this prediction if they insure 1,000 homes and even more confident if they insure 100,000 homes. The more chances you get, the more likely you will achieve the desired outcome.

The law of large numbers benefits policyholders by allowing them to transfer their risk of loss to the insurance company. If we all had to pay our own claims, we would never know if the claim was going to be a small fender-bender that might cost $500 or a serious vehicle accident that results in bodily injuries of $500,000. Therefore, we transfer the uncertain loss to the insurance company in exchange for a known and certain loss, the cost of the insurance.

Insurance rates are not the same as premiums. An insurance premium is a payment that is made by the owner of a policy to the insurance company. An insurance rate is the price of insurance for each unit of coverage. Units can be either the limits contained in the policy or the number of items exposed to loss.

The first thing an insurance company does to determine a premium for insurance is to establish a base rate. The base rate is the established rate for certain levels of coverage and the for the number of insured units. As an example, you may pay $1,200 per year for your auto insurance. This is your total insurance premium, and you can sometimes arrange to pay monthly, spreading the payments over an entire year. Insurance rating is the method the insurance company uses to determine your total premium of $1,200. Then, they apply a rate (determined by the actuary) to the number of "units" of insurance you wish to purchase. If you have two vehicles and the rate is $600 per vehicle, the premium is determined by multiplying $600 x 2 units = $1,200. All individuals who possess the same risk characteristics pay the same rate, although the premium will vary based on the number of units insured.

Units may also be the amount of insurance selected. A liability limit of $50,000 will not result in as high a premium as a limit of $500,000. Insurers apply the rate to the limit by saying the rate is "$X per $1,000 of coverage". One important feature of rates for liability insurance is that they increase at a decreasing rate as you get higher and higher limits. Therefore, the rate for $500,000 is not 10 times the rate for the $50,000 limit. In fact, it may even be less than two times the rate. This is because large claims are not as common as smaller claims.

When an actuary develops rates, he or she takes into consideration all of the relevant risk factors. Thus, if male drivers have, on average, more accidents than female drivers, the rate charged will be higher for boys than for girls. If you are female, your rate may be only $400 per unit. Likewise, if you have a clean driving record, your rate will be lower than another person who has received several speeding tickets. Rates vary based on the likelihood that the insurance company will have to pay claims. More claims means the insurance company must collect more premium in order to maintain its profitability. Insurance ratemaking is, therefore, objective since it is based on the analysis of statistics. Underwriting, on the other hand, because it allows an underwriter to use judgment, is somewhat subjective.

Most insurance rates are called class rates. This means that the insurance company has divided customers into categories or classifications based on their risk characteristics. Within each class, everyone pays the same rate. To do otherwise would be unfair discrimination, since the chance of loss is the same for each individual in the category.

Exhibit 6.1 shows factors that are used to classify and determine premiums for individuals. For people with the same rating characteristics, the price per unit of coverage (rate) would be the same. Exhibit 6.2 shows a subclassification system based on vehicle use.

Exhibit 6.1

Determining Classifications

The rating process places all potential customers and current customers into classifications which reflect individual degrees of risk. Major factors that determine rates are:

Primary Rating Factors	Secondary Rating Factors	Other Rating Factors
1. Age, gender, marital status of operator	1. age, make, model of auto	1. limits of liability
2. Annual miles vehicle is Used	2. number of autos	2. deductibles
3. Use of the auto	3. garaging location of vehicle	3. discounts (airbags, anti-lock brakes, alarms)
4. Driver Training/Good Student		
5. Driving record of operators		

Exhibit 6.2

Use of the Vehicle

Depending upon the use of the insured vehicle, the probability of an accident increases or decreases. There are five sub-categories applied to the use of the vehicle, depending upon the state.

- **Business Use –** This means that the use of the auto is required by or customarily involved in the duties of the insured or any other person customarily operating the auto, in an occupation, profession or business, other than going to or from the principal place of occupation, profession or business.

- **Farm Use –** This means the auto is principally garaged on a farm or ranch and is not customarily used in going to or from work other than farming or ranching or driving to or from school. It is not used in any occupation other than farming or ranching.

- **Pleasure Use –** This means personal use including driving to or from work or school less than 3 road miles one way or 3 or more, but less than 15 road miles one way for not more than 2 days per week or not more than 1 week in any 5 week period. NO BUSINESS USE.

- **Work less than 15 miles –** This means personal use including to or from work or school 3 road miles or more, but less than 15 road miles one way if such usage is more than 2 days per week or more than 2 weeks per 5 week period or 15 or more road miles one way, for not more than 2 days per week or not more than 2 weeks in any 5 week period. NO BUSINESS USE.

- **Work 15 or more miles –** This means personal use including driving to or from work or school 15 or more road miles one way more than 2 days per week or more than 2 weeks in any 5 week period.

Factors That Impact the Cost of Insurance

There are many factors that influence the rates charged for insurance. With personal automobile insurance, some of the relevant factors are:

RISK FACTOR	HIGHER RISK	LOWER RISK
The age of the driver	Under 18 (youthful operator)	Over 25
The number of years the driver has been licensed	Less than 3	3 or more
The gender of the driver	Male (youthful operator)	Female
The marital status of the driver	Single	Married
The driver's motor vehicle records	Tickets, Accidents	Clean record
The place where the vehicles are usually driven	Congested urban area	Farm
The number of miles the vehicle is driven annually	Over 20,000	Less than 7.500
The use of the vehicle	Business	To and from school less than 3 miles
The type of vehicle	SUV, sports car	4-door sedan
Vehicle safety devices	Seat belts	Air bags
Relationship to vehicle	Owner	Occasional user

Some of the rating factors are based on characteristics of the driver and others are based on the vehicle to be insured. Still others pertain to the type of coverage selected. In general, insurance companies determine primary rating factors, such as age, gender, annual miles driven, years licensed, use of the vehicle, and driving record, and then add secondary rating factors such as location of the vehicle, vehicle type, and safety features. Although both types of factors affect the final price of insurance, they are not given equal weight. Other factors that ultimately determine the cost of insurance include the limits chosen, deductible amounts selected, and the presence or absence of discounts for such things as good grades or driver training classes.

When calculating final insurance premiums, primary rating factors are added to secondary factors and the sum of these factors is then multiplied by the base rate. In the example given earlier, the base rate was $600 per vehicle. We then said that female drivers (a primary rating factor) generally pay less than male drivers. Thus, the base rate of $600 was multiplied by a rating factor of .667 to determine the final premium of $400 (rounded).

Base Rate x Rating Factors (Primary + Secondary) = Premium

$600 x .667 = $400

If the insured was a male driver, the premium would increase since the primary rating factor for male drivers is higher than that for females. Thus, a teenage boy may have a primary rating factor of 1.10, producing a final premium as follows:

$600 x 1.10 = $660

The type of automobile driven represents a secondary rating factor. Sports cars are more expensive to insure than sedans. Using the same examples as above, notice the effect on final premiums when the secondary factor is applied:

Female Driver—Sports Car
$600 x (.667 + .50) = $700
Male Driver—4 Door Sedan
$600 x (1.10 + .25) = $810

Although the premiums are still higher for the male driver, the fact that the female is operating a higher rated automobile narrows the gap between their insurance premiums.

Over the past several years, there has been much public debate with regard to some of these rating factors. Some consumer groups and others argue that it is unfair to discriminate against drivers based on factors over which they have no control, like age or gender. Others feel that using the place where a vehicle is operated is also an unfair discrimination. Some states have passed laws that severely limit an insurance company's use of various factors in determining the rates charged for insurance. In some cases the only relevant factors are driving record and number of miles driven annually.

Controlling Risk Factors

Since lower risk means lower premiums, it is important that you do everything possible to reduce or eliminate the chance that you will have a claim. Since a driver's motor vehicle record is a primary rating factor for insurance companies, obeying the traffic laws will reduce the chance of having a higher-than-average risk factor. If you use your vehicle constantly and rack up a lot of miles, you will pay more. You might consider public transportation as an economical alternative to using your car. Maintaining a "B" average in school may also afford you a good student discount and taking and passing an approved driver's training course may also result in a rate credit.

Unfortunately, there's nothing you can do to gain more driving experience except drive. Over the course of time, all other things being equal, your insurance premiums will drop simply because you are getting older and have gained more experience behind the wheel.

For each of the following pairs of situations, indicate whether it is an example of a primary or secondary rating factor. For each risk factor, also indicate if it represents a higher or lower risk relative to the other.

Risk Factor *Higher Risk or Lower Risk*	**Primary Rating Factor**	**Secondary Rating Factor**
1	Teenage driver	Senior citizen
2	Newly licensed	Licensed 5 years
3	Female driver	Male driver
4	Single	Married
5	Clean driving record	Two speeding tickets
6	Rural area	Urban area
7	Seat belts	Side-impact air bags
8	Farm use	To and from work
9	SUV	Station Wagon
10	“C” student	“A” student

WHERE THE INSURANCE PREMIUM DOLLAR GOES

Some people think insurance is a “rip off” because they believe insurance companies charge excessive premiums and then keep the money, earning high profits. In fact, nearly 70 cents of every dollar collected in insurance premiums is returned directly to policyholders in the form of claim payments. About 28 cents is used to pay the insurance company’s expenses, including the agent’s commission, the salaries of their employees, and other overhead items such as utilities, rent and the like. That leaves about 2 cents for profit. Many insurance companies would be very happy with a profit of 2 %, but in reality some make no profit at all by writing insurance. When an insurance company pays out more money in claims and expenses than it takes in in premium, the company is considered to have suffered an underwriting loss. This can sometimes occur when unusual events take place that actuaries could not have predicted such as a major earthquake, tornado, or hurricane. If there is still money left over after paying these items, the company has experienced an underwriting profit.

How can an insurance company stay in business if they have an underwriting loss? Insurers have another source of income. Since you must pay insurance premiums in advance, the insurance company is able to invest the money until the time comes to pay your claim. In the meantime the company earns interest on the funds. This is called the company’s investment income and it can be used to offset losses if claims exceed the company’s expectations. Insurance companies sometimes earn all their profits on investments.

Insurance company investments are very conservative and are regulated by law. You would not want your insurance company to take your premium and invest it all in the stock market and then be unable to pay your claim. Companies typically invest in low-risk securities such as U.S. Treasury notes and bonds.

Summary

Insurance companies use the process of underwriting to determine which applicants to insure and which to reject. In some cases, the underwriter may modify the type of coverage offered rather than reject the application. Underwriting guidelines help the underwriter make this important decision. When an applicant is determined to be eligible for insurance, the underwriter must then detemine the price to charge.

Actuaries use statistics to determine the appropriate price to charge for insurance. Although the future cannot be predicted with certainty, the law of large numbers allows the insurance company to more accurately estimate the number and cost of future claims.

Final premiums for insurance are determined by applying rates to either the amount of coverage or the number of units insured. Base rates are first developed that take into account the average expected losses for the company. Primary and secondary rating factors are then applied to base rates to modify premiums based on individual risk characteristics.

There are many factors that determine the final cost of automobile insurance. Some of these factors, such as age and gender, are considered primary rating factors. Others, like vehicle safety features and location are deemed to be of secondary importance. Insurers offer additional discounts for good students and those who complete approved driver training courses.

Insurers who accurately estimate future losses and collect sufficient premium dollars to cover the cost of claims and their underwriting expenses generate an underwriting profit. Those who have claims and expenses that exceed total premiums suffer underwriting losses.

CHAPTER 7

Insurance Agency Operations

Key Terms

- ACORD forms
- Agency management system
- Budgets
- Cancellation
- Cancellation request
- Comparative rating
- Customer Service Representative (CSR)
- Diary system
- Draft authority
- Endorsement
- Goals
- Mission statement
- Nonrenewed
- Objectives
- Policies
- Procedures
- Producer
- Strategies
- Suspense system
- Vision statement

We have focused the previous chapters on the history of insurance, the way insurance companies operate, and the most significant insurance product purchased by consumers, the Personal Automobile Policy.

We now need to examine how an insurance agency operates, since a major goal of InVEST is to familiarize you with the specific activities that are involved in selling to and servicing the needs of insurance consumers.

This chapter will introduce you to the way insurance is marketed and sold by insurance agents, how the business is processed within the agency, and how customer service is provided when a customer's insurance needs change. The insurance agency business is challenging, exciting, and important to protect the assets of firms and individuals. It is also complex and requires many years of training and education.

Although the context of this course is the insurance agency, many of the topics covered in this chapter apply to virtually any business in which you may work.

This chapter will introduce you to the way insurance is marketed and sold by insurance agents, how the business is processed within the agency, and how customer service is provided when a customer's insurance needs change.

LEARNING OBJECTIVES

When you complete this chapter, you should be able to:

- Understand the concept of a customer life cycle
- Describe the basic functions performed in an insurance agency
- Describe the role of an insurance agent and a Customer Service Representative (CSR) and how those roles relate to the functions performed in an insurance agency
- Distinguish between the selling and servicing of insurance
- List the various job positions in a typical insurance agency
- Understand the use of computers in selling and servicing insurance policies

We have previously discussed the various methods insurance companies use to distribute or sell their products. Those methods include the independent agency system, the exclusive agency system, and the direct response system. Regardless of the type of marketing system used by the insurance company or whether the agent represents a single company or several, most of the functions of an insurance agency are the same. This chapter will focus on the activities conducted in an independent insurance agency.

PREPARING A BUSINESS PLAN

The first step any business owner needs to take is to develop a strategic plan that will identify the purpose of the organization, what will be sold and to whom, how customers will be served, what types of computer systems will be used, and what financial goals must be achieved. The basic sections of a business plan are:

- Vision or mission statement—a sentence or brief paragraph that answers the question "why does this organization exist?"

Examples of mission statements designed by insurance agents are:

Sample Mission Statement #1

ABC Agency, Inc. is an employee-owned organization that provides high-quality and creative solutions to the problems faced by insurance buyers. Every client's account is handled in a confidential, professional, and thoughtful manner. Our major objective is to provide adequate profits to sustain our continued growth, allow our employees to develop their professional expertise, and continue to serve the risk management and insurance needs of our valued clients.

Sample Mission Statement #2

The ABC Insurance Agency is the oldest and largest independent insurance agency in the Tri-Counties area. We offer a full range of financial services products to our personal and business clients. Through our main office location and our branches, we are able to respond to the needs of our clients in a timely and efficient manner.

We employ a highly trained and professional staff and are devoted to helping them achieve extraordinary outcomes in their insurance careers. We focus on the maintenance of long-term customer relationships through personal contact and outstanding customer service.

We are associated with insurance companies and other professional firms who offer a wide array of products at competitive prices that meet the needs of our customers. We place a high value on integrity and deal only with other organizations that share our core values.

- **Strategies—**examples of an agency's strategies might be to become the largest agency in a local area, to control a high percentage of a certain market, or to serve customers in a particular industry. Strategies are usually broadly stated and may involve dealing with competitors. Agencies need to obtain a "competitive edge" in order to gain enough customers to make the business successful.
- **Goals and Objectives—**an agency determines various goals that are specific and measurable, such as financial goals relating to the amount of profit the firm expects to produce, or the number of customers the agency will serve. These goals are designed to help the agency achieve its strategic objectives. Strategies are important, but without the specific goals and objectives that support strategy, it would be difficult to manage an agency on a daily basis.
- **Budgets—**an insurance agency is like any other business in that it must take in sufficient funds to cover its expenses and leave an amount of profit for the firm's owners. Budgeting also helps the firm determine the number of employees and job functions that will be necessary to serve the agency's customers.
- **Policies and Procedures—**in order to operate any business, the organization must have ways of doing things that the individuals in the firm follow. For example, it may be an agency's policy to offer high deductibles to individuals with expensive automobiles, or high liability limits to people with substantial financial assets. In order to obtain an insurance policy from one of the companies that the agency represents, a procedure must be followed to ensure that the policy is issued and delivered to the customer in a timely manner. There are many policies and procedures necessary to operate an insurance agency. We will examine each of the major procedures.

Match the terms to their definition.

Quick Quiz 7.1

_____ Budget	1. A statement that answers the question "why do we exist"?
_____ Mission statement	2. Broad statements that deal with an agency's direction.
_____ Strategies	3. The methods used to perform the various functions in an insurance agency.
_____ Procedures	4. Specific and measurable business objectives.
_____ Goals	5. A financial report that estimates an agency's revenue and expenses.

THE CLIENT LIFE CYCLE

Just as in other businesses, there is a natural customer life cycle that is followed in the insurance agency. Customers are "born" when they are first acquired by an insurance agency. They "die" when they terminate their relationship with the agency. This occurs for a variety of reasons, including moving, passing away, or simply becoming dissatisfied with the service provided by the agency or company. In between, their accounts must be serviced in order to keep the protection up to date and appropriate for the needs of the individual or family. Also, claims may occur that must be handled and paid.

INSURANCE AGENCY PROCEDURES

Having a plan is an important first step when forming an insurance agency. Executing the plan is, however, the key to running a successful organization. The primary activity that must be completed in any business is to identify prospects, or people who might purchase insurance from the agency, and convert them into customers. Therefore, sales activities that lead to the generation of new revenue for the agency are vitally important. Equally important, however, is retaining or keeping customers who are already doing business with the agency. This function in an agency, called customer service, is important from a financial standpoint because it is much more profitable for an agency to serve its existing customers rather than acquire new customers.

New Business Procedures

Obtaining a new customer is referred to as "new business" in the agency environment. Just where will those customers come from? A person whose primary job functions involve prospecting, or looking for potential customers, marketing or soliciting prospects for insurance, and selling policies is referred to as a producer. The name is derived from the fact that the person is responsible for production of new business. These individuals are also called agents, brokers, or salespeople.

All states require that an insurance producer obtain a license in order to sell insurance. A license is issued to people who qualify by taking and passing a written exam, having a minimum number of years experience, and/or possessing a professional designation or degree in insurance. The Insurance Commissioner or other head of the state insurance department is responsible for the licensing of agents.

In order to obtain an insurance policy, it is necessary to complete an application for coverage. The standard application for personal automobile insurance is shown in Exhibit 7-1. Insurance salespeople collect completed applications from prospects and send them to the insurance company's underwriter to determine if the applicant is acceptable and to determine the proper price for the policy. In some cases, the agent is authorized to determine the applicant's acceptability and to compute the price.

If the prospect decides to purchase the policy, a premium payment is made and the insurance policy is ordered from the company. When the policy is delivered to the customer, the new business process ends.

Policy Change Procedures

There are many occasions when a change must be made to an insurance policy that has already been issued. An example is when you purchase a new car. You must have the old car removed from the policy (you don't want to pay insurance premiums on a vehicle you no longer own) and add the new vehicle. If you move, the address on your insurance policy must be changed.

These policy changes are handled by an agency's Customer Service Representative (CSR). When a change is needed, the CSR requests an endorsement from the insurance company. An endorsement is the formal name for a change to a policy.

Claims Procedures

People buy insurance to protect themselves against a financial loss. No time in the client life cycle is more imporant than when a claim occurs. Therefore, this is also an important time in the life of an agency.

When a customer calls the agency to report a claim, the claim must be reported to the company using a loss notice. Remember, it is the insurance company that is responsible to pay the policyholder what is due under the policy. Therefore, an agent's responsibility is to take the information from the insured, report the claim to the company, and monitor the progress of the claim until it is settled. Also, the agent is the advocate for his or her insured, making sure the customer is satisfied with the outcome.

Some insurance companies allow agents to handle small claims in their office. This allows the insured to receive payment more quickly and helps the insurance company keep its costs down. This is called draft authority, and is usually only given to a select group of the company's agents who have demonstrated their ability to determine appropriate payments. A claim for damage to a vehicle windshield would be an example of a situation where an agent could use his or her draft authority to settle a loss.

Renewal Procedures

Insurance policies are usually issued for a term of six months or one year. If you wish to have continuous insurance protection, your policy must be renewed at the end of each term. This process is usually handled automatically by the insurance company. Approximately 60 or 90 days before the end of the term, the insurance company sends an offer to renew to the policyholder. If the renewal premium is paid, the coverage continues until the end of the next policy period. In some cases, the agent must order the renewal policy from the insurance company. This renewal procedure begins when the agency prints a list of upcoming renewals from the agency's management system and ends when the renewal policy is received from the insurer.

Cancellation and Nonrenewal Procedures

Despite the best efforts of the agent, some policyholders will decide to cancel their insurance policies. This may occur because they are unhappy with the service received from the agency or the way a claim was handled. In other cases, the insurance company may decide that it does not wish to continue coverage for the insured. This happens because the risk factors may have changed (such as adding a high-performance automobile to a policy insuring a teenage driver) or because there has been a lot of claims activity. When a policy is terminated prior to its normal expiration date, it is referred to as cancellation. When a policy is not continued beyond its expiration, it is said to be nonrenewed.

Insurance agencies need to have procedures for handling cancellation and nonrenewal of policies. This usually involves having the insured sign a cancellation request or returning his or her original policy. If the premium has been paid in advance, there is a refund due the insured and the agency must process that credit or obtain a check from the insurance company.

All states have regulations that govern when and why an insurance policy may be cancelled by the insurance company. These laws often vary based on the type of insurance involved, such as automobile, residential property, and commercial insurance policies.

Activity 7.1

Research the cancellation and nonrenewal provisions of your state's insurance code. Answer the following questions:

- **Under what circumstances may an insurance company cancel a person's automobile insurance?**
- **What is the number of days advance notice that must be given to a person before their policy can be cancelled?**
- **Are there different rules for refusing to renew a policy that has already been issued?**
- **Does the insurance company have to give the insured a reason for the cancellation or refusal to renew?**
- **Does the insured have any recourse to have the decision overturned?**

COMPLETING TRANSACTIONS

Like many businesses, an insurance agency finds itself completing many similar tasks on a routine basis. In order to expedite the processing of the many transactions discussed above, standard forms have been developed to allow agents to communicate with insurance companies.

These standard forms were created by the Association for Cooperative Research and Development (ACORD), a nonprofit organization that serves the insurance industry. The forms are referred to simply as ACORD forms. These forms are either obtained from ACORD, or they reside in an agency's computer system and are printed when necessary. Standardization and automation of forms makes the agency's procedures more efficient and allows for better communication between agents and insurers.

Each of the standard forms used in personal automobile insurance is included in the exhibits at the end of this chapter.

Quick Quiz 7.2

For each of the following situations, identify the appropriate form(s) that would be used to complete the transaction:

Application	Cancellation Request	Loss Notice	Change Request
Medical Statement	Young Driver Questionnaire	Certificate of Insurance	
Good Student/Driver Training Application			

__________ 1. The insured has purchased a new vehicle to replace one that is already covered by the policy.

__________ 2. The insured has had an automobile accident.

__________ 3. The customer wishes to cancel a policy prior to its normal expiration date.

__________ 4. The insured's son has turned 16 and is now a licensed driver using one of the family's vehicles.

__________ 5. The insurance company wishes to obtain new underwriting information in the process of renewing the insured's auto policy.

__________ 6. The customer has leased a new automobile and the leasing company needs evidence that the vehicle is insured.

__________ 7. The insured's daughter has just attained a "straight-A" report card.

__________ 8. Following an accident, a senior driver is asked to provide details about a heart condition that may have led to the accident.

__________ 9. The insured's wife purchased automobile insurance on the family vehicles not knowing that her husband had already placed coverage with another insurer.

__________10. The insured has moved to a new house in a nearby town.

JOB FUNCTIONS IN THE INSURANCE AGENCY

All of the procedures discussed above must be handled by someone in the agency who has the experience and ability to best meet the customers' needs. Although most agencies are relatively small businesses and job functions may be blurred, there are transactions that are typically handled by people filling certain roles.

Insurance Agents, Brokers and Producers

The person in the agency who is responsible for selling new accounts is the agent, broker, salesperson, or producer. People who sell insurance must be licensed by the state in which the transaction takes place. The role of the salesperson involves marketing, prospecting, and completing the sale of insurance policies and other financial products. After a sale is made, the producer usually turns the account over to a member of the service staff to handle ongoing tranactions. The producer may still be involved in the account, especially if there is a problem or when the policy renews.

Customer Service Representatives

The person who handles the day-to-day transactions in an insurance agency and explains coverage to an insured is the Customer Service Representative (CSR). As we discussed previously, it is very important to an agency's profitability to maintain the customer base over time. Therefore, clients must be happy with the service they receive from the agency. Transactions that are handled promptly and efficiently will earn a customer's loyalty. The CSR works with the producer to provide a premium quotation to the prospect, prepare binders and order policies from the insurance company, and transmit the policy to the insured when it is received. In addition, CSRs handle requests from policyholders and insurers for changes to policies that are necessary after the policy begins. In some cases they also handle claims.

Claims Representative

In some agencies, the claim function is handled by the Customer Service Representatives since it is really a service function. Others handle this function by having an in-house claim representative. However this role is filled, it involves taking claim reports from customers, transmitting the information to the insurance company, and following up to ensure that the claim is properly handled and settled.

Other Positions

Sales and service are the core functions in an insurance agency. Additionally, an agency will employ people who perform accounting functions, those who handle clerical functions such as data entry, and individuals who provide management and support to the organization.

COMPUTERS IN THE INSURANCE AGENCY

Today's insurance agency environment is heavily dependent upon the use of computers and technology. Being comfortable with the use of computers and knowing how to use technology to better serve customers is a key to running a successful agency and providing excellent customer service.

Use of Computers in Sales

The presence of the Internet and the availability of inexpensive software has made it possible for an insurance producer to use technology in the sales function. Contact management software such as ACT! and Gold Mine are used by many producers to keep track of prospects. Hand-held computers and devices like Personal Digital Assistants (PDAs) like and laptops have made it possible for producers to be in contact with customers and the office while not requiring that they be physically present. The ability to search for and obtain a list of prospects using a database available on the Internet, prepare multiple marketing letters and distribute them at a low cost, and track the results of a marketing campaign are all a huge benefit to an agency attempting to expand by writing new business.

Another important use of computers in sales is comparative rating of insurance policies. In an independent insurance agency, the producer can offer coverage for the client in more than one company. After entering basic underwriting information, an agency's computer system can generate price estimates with a number of companies. While selecting the company with the lowest price is not always best for the customer, a comparative rating system allows the producer to compare prices between companies and provide the customer with the best protection at the lowest premium.

> **One of the most** important activities a business can conduct is the preparation of a strategic business plan. The plan is a blueprint for the agency's personnel to follow as they perform the various functions required to sell and service insurance.

Use of Computers in Service

Equally important to the agency is the ability to provide high-quality service at the lowest possible cost. Most agencies use industry-specific software, called an agency management system, to store information about current customers. When a customer calls the agency to make a request or obtain information, the CSR need only access the client's electronic file to provide service or answers. All documentation is placed in the system so that any person may view the client's file and see what transactions are pending or have been made in the past. For example, when a customer calls the agency to report a claim, the CSR will first access the client's electronic account, determine which policy is affected, and "open" that policy on the computer screen. A claim form will be opened and the information contained in the agency's database will be automatically filled in on the claim form. The CSR will take additional information from the customer and complete the form. At the end of the conversation, a form letter can be sent to the insured acknowledging receipt of his or her claim and advising what the next steps are in the claim process. The claim form will be transmitted to the insurer from the CSR's desktop using e-mail or fax technology. A minimal amount of paper will be created and the entire transaction may only take minutes to complete. This efficiency in handling service functions allows a CSR to focus on the customer without being burdened with unnecessary paperwork.

Other Uses of Computers in the Agency

One of the first functions performed by agency management software was accounting. This is still an important use of technology in operating an insurance agency. In a matter of moments, the agency can see exactly what business has been written, what the commission income is on those policies, and when they will renew. Since the agency holds the customer's money in trust and must turn it over to the insurance company at some point, it is important to maintain a proper accounting of all money received.

Time is also an important factor in an insurance agency. Prompt service builds customer loyalty. When a customer makes a request or files a claim, it is important to follow-up on those items to see that they are properly handled by the agency or company. The method used to follow up on transactions is a suspense or diary system. After handling a transaction on the computer, the CSR or producer will be asked to create a suspense item. This is simply a date in the future when the item will be reviewed to see if further action is necessary. Let's say a claim is filed on June 25. The CSR wishes to contact the customer and the insurance company to see if everything is being handled appropriately. After entering the information on the claim form and transmitting it to the insurance company, the system prompts the CSR to enter a suspense date. The CSR enters July 5, 10 days in the future, at which time the transaction will appear on the CSR's computer screen or be distributed as a paper document to follow-up with the insured and the company.

Insurance agencies generate lots of form letters and other standard documents that must be sent to customers and insurance companies. All these documents can be completed and stored in the agency's management system. In addition, incoming correspondence and documents may be scanned and attached to electronic files. The proper use of an agency management system involves using electronic files as much as possible and eliminating the use of paper. The use of e-mail to correspond with companies and clients has greatly improved efficiency in the insurance agency. It also has the potential to provide better customer service since transactions can be handled quickly and communication can remain open between the producer, CSR, customer, and insurance company.

The application of technology will continue to be an important part of agency operations.

Activity 7.2

Become familiar with the basic functions of the agency management system used in your classroom. Complete an ACORD form for a client you have set up in the system.

Summary

One of the most important activities a business can conduct is the preparation of a strategic business plan. The plan is a blueprint for the agency's personnel to follow as they perform the various functions required to sell and service insurance. The basic sections of a business plan include the mission or vision statement, strategies, goals and objectives, budgets, and policies and procedures.

From the time new customers are acquired to the time they leave the agency, which occurs for a variety of reasons, many individual transactions must be completed. There are various procedures that take place in an insurance agency including new business, policy changes, claims, renewals, and cancellations. Each of these procedures involves a number of individual steps that are completed by the agency's personnel. Producers, sometimes called agents or brokers, are primarily responsible for new business procedures. Customer Service Representatives generally handle all service needs of the client after they have been acquired. In some agencies, claims are handled by specialists who have developed the skills necessary to deal with customers who have suffered a loss.

Computers and automation are a vital part of the agency's operations. In addition to assistance with marketing and selling, an agency management system can also support service functions by storing and retrieving information in a timely and efficient manner. Automation will continue to provide agents with a valuable resource, although full utilization of these tools can also present a challenge to the agency's owners, managers, and staff.

CHAPTER 8

A Career in Insurance

Key Terms

- **Actuary**
- **Career**
- **Casualty Actuarial Society**
- **E-file**
- **Ego-drive**
- **Empathy**
- **Ethics**
- **Etiquette**
- **Independent adjuster**
- **Job**
- **Prioritization**
- **Public adjuster**
- **Staff adjuster**

Choosing what you will do to earn money in the future is definitely one of the most important decisions you will ever make. The possibilities are literally endless. Odds are, until now, you may not have ever considered a career in insurance or risk management.

The most important aspect of running a successful insurance agency is identifying the people who will help the agency provide outstanding sales and customer service. A variety of supporting functions are also necessary to achieve excellence.

In addition to the jobs available in insurance agencies, the insurance industry is in constant need of talented people to fill positions in insurance companies, brokerage operations, claims adjusting firms, risk management offices, and a variety of other organizations.

Deciding if any of these jobs fit your goals, talents, and abilities is a big task. There are several steps involved, beginning with a discussion with your parents, teachers, counselors, and other adults who have already had to make this important decision. Next, you must do some research on the available careers and what types of skills and abilities are required for each position. Then, of course, you must apply, be interviewed, and decide if the job is for you.

This chapter will examine the various careers available in the insurance and risk management fields. It will discuss the skills, knowledge, and commitments that are necessary to achieve success in that position.

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LEARNING OBJECTIVES

When you complete this chapter, you should be able to:

- Distinguish between a job and a career
- List the steps to take to find a career that suits your skills and abilities
- List the 10 questions to ask before beginning to look for a job
- Identify the general business skills required for a career in insurance
- Describe the major careers available in insurance

A JOB OR A CAREER?

We sometimes use these terms interchangeably, although they can mean vastly different things. Generally speaking, a job is what you do to earn money—it's more or less something you have to do to obtain other things you desire. A career, on the other hand, is the pursuit of constant achievement, something you train for and progress through—it is more of a "calling" and more permanent than a job. In your lifetime you may have many jobs, but only a few careers.

Do you think people are happy in their jobs because they are successful or are they successful in their jobs because they are happy? In other words, when you hear people say "I love my job", is it because they have achieved success in that position, or is it the success that makes them feel such affection for what they do? These are difficult questions to answer, but the most important thing to remember is that you will never do anything better than when you're doing what you love to do. That means it's critically important to match your personality, skills, talents, and abilities to any job you choose. You can earn money doing any number of things, but to achieve professional success, you have to decide on what career path you will follow.

INTERESTS AND ABILITIES

Careers vary widely and involve all types of interests, skills, and abilities. Some careers depend heavily on interaction with people on a daily basis. These jobs require excellent communication skills. Jobs in sales and service require someone who enjoys being around diverse groups of people. Other careers involve the use of equipment and machinery and do not require constant interaction with people. Computer programmers, heavy equipment operators, and mechanics are skilled individuals who enjoy working with "things" rather than with other people. Of course, there are virtually no jobs that don't involve interaction with other people internally, but many do not require the person to work with the public. Communication skills are important for all people, but for some they're more critical than others. We will discuss communication in more detail later in this chapter.

There are two important steps you can take to make sure your interests and abilities match well with your intended career. The first is to determine what your personality style is and the type of career to which you are best suited. Your school counselor may be able to provide you with a basic personality test, such as the Myers-Briggs Type Indicator Test, or you may be able to find one on the Internet. The first step in determining if a career is right for you is to determine who you are!

Take The "I" Test

Here are 5 basic questions about your attitude toward your career.

1) For the most part, I would prefer work that puts me in touch with:
a. Machines exclusively
b. Both people and machines
c. People exclusively

2) For the most part, I would prefer a career where I:
a. Work from 9 to 5
b. Work roughly from 9 to 5
c. Set my own schedule

3) I would prefer the kind of career which provides me:
a. Total job security in a big company or bureaucracy.
b. Some security in a growth industry or in a medium-sized company
c. Limited security

4) I would prefer a job in which I:
a. Work in an office regularly
b. Travel locally or regionally
c. Travel exclusively

5) I would prefer a career with upward mobility:
a. In which I climb to the top of an existing structure
b. In which I make the structure of my enterprise grow and I grow with it
c. O.K. we couldn't resist the pun.

Your Answers

The answers to the "I" test are not as obvious as you think. Each one has weighty implications.

Question 1 addresses a serious consideration. Some people prefer the limited responsiveness of the machine and are motivated by mechanical invention. Some prefer dealing with people almost 100% of the time. And some prefer a mix of people contact and machine technology.

If your answer was (b) your "independence quotient" is best served. You prefer harnessing technology for your people-to-people contact and you prefer working with both human and hardware resources.

Question 2 contrasts the total independence of an entertainer, answer (c), with the regularity of the 9 to 5 worker. In the center lies a happy medium, answer (b) - the job which relies upon your initiative and is yet part of a larger, structured system.

Question 3 illustrates your job security motivation. A career should not be a gamble. But there are extremes. Answer (a) implies the total security situation in a large corporation or governmental bureaucracy. Answer (b) implies some security such as that offered by a medium-sized company. If you chose (c) you are independent, but be careful! If you chose (b) you may be headed for the security that comes from being part of the decision-making team of an independent company.

Question 4 illustrates the extremes of your willingness to travel, from (a) virtually "none" to (c) "exclusively". If you chose (b), you are ready for the success that comes from personal contacts on a local and regional level.

Question 5 really asks whether you prefer (a) climbing up an existing corporate ladder or (b) making your own enterprise grow - and you with it. The independent thinker will probably choose (b).

Our purpose in illustrating these choices is to interest you in a career that combines the following opportunities:

1. working with people and with the latest technology;
2. advancing within a growth system in which you are your own boss but not totally alone;
3. relying upon your own initiative but not starting from zero all by yourself;
4. traveling locally and regionally to make personal contact;
5. using all of your ability to make it on your own, instead of climbing an existing corporate ladder.

The career that offers these opportunities is that of an Independent Insurance Agent. Independent Agents are entrepreneurs who...

- represent several insurance companies;
- hold written contracts allowing them to represent these companies;
- select from these companies the kinds of insurance and policies that suit their clients' needs;
- work for their own success directly, as part of the Independent Agency System;

Many Independent Agents own their own businesses and work for themselves and their clients. But they also work with the companies they represent, including some of the largest and most prestigious insurance companies in the world today.

And there's much more to it. That's why the Independent Insurance Agents of America wants to interest you in a career in this rapidly growing, demanding field. Our industry needs bright, forward-looking young people who can be INDEPENDENT.

We have developed the means for you to become a part of this challenging and rewarding profession.

The next step is to examine the individual tasks that are required in various positions and the specific skills that are necessary to excel in that field. A later portion of this chapter will discuss some of the major insurance careers and what types of skills, abilities, and interests are necessary for each one. We must also consider any educational requirements for each position.

Before you begin your job search, consider these ten important needs that may be met by any job you take:

1. Salary. How much does the job pay? What will be the net amount you will receive after deductions for taxes and other items?

2. Location. Where is the job located? Will it involve travel other than to and from work? Do you have transportation or is there convenient access to reliable public transportation?

3. Benefits. Will the employer provide health insurance, dental insurance, vision care, retirement benefits, paid vacations, etc.?

4. Timing. Is the job available immediately? Do you have time to carefully consider your options and make a decision?

5. Chance for Advancement. Is there a career path through the organization? What must you do to advance?

6. Co-workers. Have you met other people in the organization? Do you feel you could get along with those people?

7. Kinds of Tasks. What are the every day duties of the job? How will those duties fit with your likes and dislikes?

8. Amount of Responsibility. How much supervision will you receive? How much do you like? Are you self-motivated or do you require someone to keep you on track?

9. Hours. Are you available to be at work during the assigned time? Is there overtime required. Will you have to work nights and/or weekends? Is full or part-time employment available?

10. Working Conditions. Will you be working in an office or outdoors? Is the environment well maintained and safe? Will you be standing or sitting?

These are very important things for you to consider before taking any position. Some things will be revealed in the first interview, such as salary and benefits. Others may require your asking. In some cases, it is best to wait until the second interview to ask detailed questions about benefits, hours, conditions, and co-workers.

Since insurance exists within the business environment, it is important to recognize the general skills that are desirable to all employers in the insurance industry.

GENERAL BUSINESS SKILLS

Some skills are necessary regardless of the specific career path that is pursued. These general business skills already exist in a number of people—they are what we call "naturals" when it comes to certain characteristics. Others must work to refine their skills in order to achieve success in any business endeavor.

Communication Skill

One of the most important traits an individual can exhibit is excellent communication skills, either verbal or written. The ability to communicate complex insurance concepts in terms the prospect or policyholder will understand is important to nearly everyone in the insurance industry. Most communication in the industry is by telephone, fax, conventional mail, or e-mail, and it is important that everyone understand the importance of professional communication. We are often judged not by the knowledge we possess, but by our ability to demonstrate that knowledge to others through the words we speak and write. A poorly written letter, full of typographical and grammatical errors, will leave the recipient thinking we are unable to handle their needs. Not everyone has the ability to communicate well with others, but everyone can work toward improving their communication skills. Basic writing classes are available in high schools, community colleges, and business schools. If this is a weakness for you, consider enrolling in a class to improve your skills in this essential area. One thing is certain: the way to improve your communication skills is to practice them every day.

Telephone Communication

The telephone remains the predominant form of business communication. In fact, now that most people have cell phones, this mode of communication is perhaps more significant than ever. The following are some tips to help you in your phone communications:

- Speak slowly and clearly so the other person can understand you
- Listen carefully to what the caller has to say—don't interrupt
- Confirm your understanding of what was requested—"if I understand you correctly, you'd like me to add this new vehicle to your policy today, is that right?"
- Always identify yourself and the purpose of your call
- Decide what you want to say beforehand—write out a brief script if it will help you
- Eliminate the distractions from your speech—"umms", "uhs", and "you knows" only lengthen the conversation and lead the caller to believe you were not well prepared for the conversation
- If you cannot answer a question immediately, offer to return the call at a convenient time rather than put the caller on hold

- Always let the other person hang up first

Remember, the customer is the biggest asset any firm has and proper use of telephone techniques is important. Likewise, the relationship between agent and company is also crucial. Your voice on the telephone is your calling card—it signals to people your ability, enthusiasm, and confidence. Refer to the telephone procedures manual at the end of this chapter.

Written Communication

Verbal communication is often supplemented with written documents. One of the most effective tools a businessperson has is a written confirmation following a telephone conversation. This allows each person to review what was discussed and, most importantly, what steps will take place next. It is entirely possible for two people who have spoken to have entirely different conversations. This occurs because we all filter the information we receive and sometimes are distracted and not paying careful enough attention to the other person. A quick follow-up memo, letter, fax, or e-mail can help to avoid misunderstandings.

E-mail has become a very common form of business communication, but it is not appropriate in every situation. Reserve e-mail for important items that are time-critical. The same is true for use of fax machines. The purpose of a fax machine is to convey information in a timely manner. If your document is not urgent, use regular mail. This also has the benefit of higher quality communication, since e-mail and a fax often distort the original document.

In general, all communication with a client or company should be confirmed in writing, particularly if there could be a coverage issue at some point in time. For example, if a client calls to make a policy change, send a confirmation that day. That way, if there was an error in your understanding, it can be corrected before any harm is done. Also, send a written communication to the company to request the change. If you have a conversation with the underwriter in which you ask approval for something, such as writing a high-valued automobile, confirm the underwriter's agreement in writing. It may seem that written confirmation doubles the workload in the office, but it can also save time down the road by reducing errors and rework. Some tips for written communication include:

- ***Use form letters or templates whenever possible.***
- ***Use a conversational tone in your communication—instead of "please be advised that we have received your automobile claim", say "we are processing your auto claim and will contact you within the next five days".***
- ***or bullet points to emphasize key points or action items.***
- ***Be concise—state your business in the minimum amount of words it takes to make your point—don't ramble.***
- ***Avoid clichés—phrases that are commonly used but don't have much meaning, like "Please feel free to contact me should you have any questions". A better approach is to say "I'll be happy to answer any questions".***
- ***Use the spell-check feature in your word processor, but don't rely on it completely.***
- ***Have another person read your correspondence before you send it.***

Organizational and Time Management Skill

Like many other businesses, the insurance industry is fast-paced and active. Most people working in the industry have more things to do than they have time in which to do them. This requires that everyone have a method by which he or she can prioritize work so the most important tasks get done first. The most important skill in this area is the ability to recognize which items should receive immediate attention and which can wait. Prioritization involves making a list of tasks to be accomplished and placing them in the order they must be completed. Most people keep a "to do" list that details what they must accomplish in a given day. This is a first step in time management. The next step is to prioritize the items so that critical tasks are completed first, important but not critical items are next, and less important items are done as time permits. Without a prioritization system, many people finish their day feeling they were busy, but with important tasks left undone.

Etiquette

Every culture has its own way of conducting business. In the United States, many business transactions are conducted over lunch, dinner, or other social occasions. Business etiquette becomes an important skill to develop. Not everyone knows how to behave when faced with a business situation that involves dining, gift giving, or other courtesies. To complicate matters, different racial or ethnic groups observe different rules when conducting business. What is appropriate in one culture may be completely offensive in another. The good news is that these behaviors can be practiced and learned. There are many videotapes and courses available that discuss business etiquette. If you feel this is an area in which you need to improve, help is available. Ask your teacher or counselor for assistance.

Customer Relations

The insurance business is highly customer-oriented. As we have discussed previously, insurance is a personal business and requires trust and good faith between the parties involved. A keen sense of customer needs is essential to everyone involved in delivering insurance services. You may already know whether or not you have a customer orientation. If you work in a service business, such as a retail store, movie theater, or restaurant, you probably have a natural tendency to provide good customer service. This skill can be developed and improved. Some people forget that the customer is king in the business situation. They may not always be right, but they are always the customer. As such, what they say is important to our success. Having good customer relation skills means knowing how to deal with difficult customers, how to negotiate win-win solutions, how to deal with complaints, and how to actively listen to a customer's problems and issues.

Problem-solving Skills

When a customer calls, writes, or otherwise communicates with an insurance agency or company, it is usually because they have a problem. This is when an insurance person can really demonstrate his or her ability to deal with the many situations that arise each day in insurance operations. In order to solve problems, it is first important to be able to put yourself in the customer's position. Think about what they are asking and ask yourself "how can I help this person solve his or her problem". Most people do not call with impossible situations. They have real-life issues that require quick answers. The ability to solve problems for your customers is related to your experience with past situations that were similar, your composure, your reasoning ability, and your customer relations skill. All of the business skills listed above must come together to provide an effective solution for the customer. Unfortunately, customer problems don't often mimic what has been learned in a textbook. Creativity in solving a customer's problems is vitally important to success in an agency or company.

Computer Skills

The use of computers in business has become so commonplace that it is expected that employees will have a certain minimum competency in using various hardware and software. Although insurance agencies and companies use special, customized software in some cases, they also use standard "off the shelf" software programs for word processing, contact management, calendars, spreadsheets, and other functions. It is important that you be relatively skilled in using standard applications such as Microsoft Windows, Word, Excel, and Outlook, since these tools underlie many of the agency management software used today. Keyboarding skill is also crucial. If you have not taken a class in keyboarding, consider doing so to increase your speed and accuracy.

Foreign Language Skills

The United States has a truly varied and diverse population. We are referred to as a "salad bowl", filled with unique individuals from different cultures who are mixed together in communities and workplaces. The needs of prospects and customers must be handled in a manner that makes it comfortable for them to interact with insurance industry professionals. This means that people who can speak the native language of customers will have a decided edge in competing for jobs in the future.

Quick Quiz 8.1

True or False.

_____ 1. A job is more permanent than a career.

_____ 2. When determining if a job is right for you, you should consider your likes and dislikes.

_____ 3. When dealing with a customer by telephone, it is a good idea to hang up before the other person to save time.

_____ 4. You should confirm conversations with customers and insurance companies in writing to avoid misunderstandings.

_____ 5. Form letters and templates should be avoided since they may seem "canned" and insincere.

_____ 6. When organizing your day, you should complete simple or easy tasks first and delay important items until later in the day.

CAREERS IN INSURANCE

One of the best aspects of the insurance, risk management, and financial services industries is that they require a broad range of people who possess a variety of talents and interests. That means there's a place for nearly everyone in the insurance industry.

Insurance Agent

An insurance agent or broker (also referred to as a producer) is primarily concerned with selling policies to new clients. This is a "people" position and personality is an important factor in determining success. Most people buy insurance from people they like. Of course, they must also feel confident that the person has the knowledge and ability to meet their needs. Selling insurance involves identifying suspects, converting them into prospects, and then turning them into customers. Different agencies have different methods of obtaining new clients and producers may be involved in all or only a portion of the sales process. Studies of successful insurance producers indicate that they possess the following qualities, known as the "five E's":

Ego-Drive or Persuasive Motivation

This does not mean that the person is egotistical. It means that what motivates the person is the ability to persuade other people to their point of view. Again, people buy insurance from people they like, so the ability to be likeable is important.

Empathy

This is the ability to sense another person's feelings—not to feel the way they do (which is sympathy), but to understand how they feel. Being empathetic is a very important trait for a good producer.

Energy

Selling anything requires a person who is not afraid of hearing "no". It requires a persistence that is not possessed by every individual. To be successful in insurance sales, a producer must not fear rejection because it is part of the job.

Economic Need

Some have said that the most successful producers have high mortgages and big families! Since most insurance producers are compensated based on a percentage of the commission income on the account, economic need can be a powerful motivator.

Ethics

Economic need can sometimes lead people to make bad choices in terms of what course of action to pursue. In insurance, a business that requires a high degree of trust, ethics is an important component of a successful person. In order to balance personal economic need with the needs of the consumer, a producer must be ethical in his or her dealings.

Education: High school degree is a must, Associate or Bachelor's degree may also be required.

Skills, Knowledge and Commitments: Excellent communication skills, verbal and written. Self-motivated, enthusiastic. Customer-focused. Computer-literate. Licensed.

Customer Service Representative (CSR)

The CSR in an agency is the primary person who has contact with the agency's customers. Like a producer, the CSR position requires a lot of interaction and requires a high degree of communication skills. A CSR must also possess a great deal of empathy and be a good listener. In many agencies, the CSR is responsible for taking claim reports from customers. CSRs process a large number of transactions and must be detail-oriented in order to accomplish their daily tasks. While most CSRs do not see themselves as salespeople, a large part of the job involves sales to existing customers. Recognizing the changing needs of his or her clients, a skilled CSR will recommend coverage upgrades and cross-sell other lines of business as needed. This requires a high degree of insurance knowledge.

Education: High school degree is a must, Associate or Bachelor's degree is desirable.

Skills, Knowledge and Commitments: Excellent communication skills, verbal and written. Customer-focused. Detail-oriented. Able to work in a team environment. Computer skills, including use of agency management systems. Must be licensed in most states.

Receptionist

The receptionist is the "director of first impressions" in most agencies and companies and as the saying goes, you only get one chance to make a first impression. This person answers telephone calls, directs the call to the appropriate person, and answers basic questions. The receptionist greets customers and other visitors to the agency and may also have other duties such as data entry, mail distribution, or clerical functions.

Education: High school degree, computer training, general office experience.

Skills, Knowledge and Commitments: Good verbal and oral communication skills. Positive attitude. Ability to work with people. Pleasant voice. Organized.

Underwriter

One of the most important jobs in an insurance company is that of an underwriter. He or she is responsible for deciding which risks to insure and which to reject. The underwriter is therefore in the position to obligate the company's assets and increase its income. In order to perform at a high level, the underwriter must be able to read and analyze insurance applications, ask the right questions to determine the true exposures presented, and determine the appropriate price for insurance based on the exposures of the applicant. Although insurance companies produce underwriting guidelines or manuals for their use, the underwriter must still develop an instinct to determine average, above average, and below average risks.

Education: High school degree a must, Associate or Bachelor's degree preferred.

Skills, Knowledge and Commitments: Analytical thinking. Detail-oriented. Negotiation skills. Good verbal and written communication skills. Curious. Well-organized.

Claims Adjuster

When it comes to policyholder service, no job is more important than that of the claims adjuster. This is the person who deals with the insured in their moment of greatest need. Adjusters may work on behalf of a single insurance company (staff adjuster) or they may contract with insurers to handle claims on an outsourced basis (independent adjuster). An adjuster makes an initial investigation of the facts surrounding a reported claim, determines if coverage applies and in what amount, and recommends payment to the insured. In many cases, the adjuster is the only person from the insurance company the insured ever sees in person. From the insurance company's standpoint, it is important that the adjuster pay what is owed to the client, but also protect the assets of the company. Some policyholders hire their own adjusters, called public adjusters, to represent their interests in handling claims. In most states, public adjusters must be licensed.

Education: College degree preferred. Insurance-specific courses in claims are desired. Public adjusters usually require licensing.

Skills, Knowledge and Commitments:
Excellent verbal and written communication skills. Empathetic. Organized and with a sense of urgency. Negotiation skills.

Actuary

An actuary determines the rates that should be charged for various types of insurance and for different customers, thus supporting the underwriting function of the company. They study past claims information and make predictions about future losses. In addition to their role in rate-making, actuaries are also involved in claims by certifying loss reserves and attesting to their accuracy. Increasingly, actuaries are involved in the management of the company and assist in the investment of the firm's assets. The role of the actuary is highly specialized and for that they are also handsomely rewarded in terms of compensation. Actuaries may be among the highest paid people in the industry.

Education: Bachelor's degree in statistics or mathematics. To receive certification, actuaries must pass a series of examinations administered by the Casualty Actuarial Society (CAS).

Skills, Knowledge and Commitments: Detail-oriented. Highly developed mathematical, analytical, and statistical skills.

Technology Specialist

Today's insurance agency and company are heavily dependent on computers for their day-to-day business operations. In insurance agencies, the electronic file (e-file) has replaced the paper file as the primary source of information. Producers often use laptop computers to transmit information obtained in the field to the servicing office. Insurers store huge amounts of data about their customers and use data warehousing and data mining to extract information and increase revenue. Both agencies and companies are using the Internet as a communication device with each other as well as the insurance-buying public. A technology specialist may be required to perform any of the various technology functions necessary to keep agencies and companies operating at peak performance. This may include data entry, programming, network administration, customer support, systems analysis, or systems design. Of major importance is the ability to translate business needs into technology solutions. These are all highly specialized fields that require extensive training and education to achieve maximum potential.

Education: Bachelor's degree in business or computer science. Certification in systems, administration, or software applications is desirable.

Skills, Knowledge and Commitments: Analytical. Detail-oriented. Results-oriented.

Other Careers in Insurance

There are a number of other careers available in insurance and related fields. Many exist in other industries as well, since they are basic functions that must be performed in any type of business.

The following is a list of possible insurance careers:

Accident Reconstructionist	Graphic Artist	Payroll Auditor
Accountant	Human Resources	Photographer
Advertising Specialist	Specialist	Printer
Appraiser	Insurance Investigator	Public Relations Specialist
Arson Investigator	Investment Analyst	Purchasing Agent
Attorney	Law Enforcement Officer	Rater
Auditor	Lobbyist	Receptionist
Bookkeeper	Loss Control Consultant	Research Specialist
Building Engineer	Management Consultant	Risk Manager
Business Manager	Marketing Representative	Scuba Diver
Claims Examiner	Marketing Specialist	Statistician
Economist	Mathematician	Systems Analyst
Electrician	Nurse	Trainer
Executive Assistant	Office Manager	Writer
Financial Analyst		

Activity 8.1

Research the job openings in the fields of risk management and insurance in your area. You may do this using the want ads in your local paper, or you can use a number of websites dedicated to job searching. Answer the following questions:

1 What is the salary range being offered?

2 What education and experience requirements are there?

3 Are employee benefits provided?

4 Is a license of special training needed?

Summary

Although you may not have considered it before you took this class, a career in insurance can be exciting, challenging, and rewarding. Before deciding to take on any position, however, it is important to consider your interests, skills, and abilities. When people are mismatched to the tasks involved in their occupation or profession they generally become frustrated and do not excel in their work.

There are many questions to consider before undertaking a job search. The salary, location, benefits, availability, training, work hours and conditions are all important concerns.

Working in the insurance industry requires many different skills and abilities. Communication skills, written and verbal, organizational and time management skills, and computer literacy are all very important in today's dynamic environment.

There are many career paths in the fields of risk management and insurance. Although some people think you have to be a salesperson to make money and advance, this could not be further from the truth. The industries employ people in all facets of business, from accountants and attorneys to technology professionals and trainers. In addition, many people are employed to provide support to insurance organizations, such as nurses, economists, and graphic artists to name just a few. There is almost no skill or talent that cannot be used effectively in providing insurance and risk management services to consumers.

CHAPTER 9

Property Insurance for Homeowners and Renters

Key Terms

- **Actual cash value**
- **Depreciation**
- **Dwelling**
- **Floater**
- **Homeowners policy**
- **Indirect loss**
- **Insurance Services Office (ISO)**
- **Loss settlement provision**
- **Moral hazard**
- **Named perils**
- **Open perils**
- **Personal property**
- **Real property**
- **Replacement cost**
- **Residence premises**
- **Structures**

The most important asset most people possess is their home or the personal property located inside their home, whether owned or rented. Home ownership or the signing of a lease or rental agreement also exposes individuals to the liability of others for events that take place on the property and the activities of the people who reside there. These activities may take place either on or off the premises. In addition, if a person's residence is damaged by fire, tornado, hurricane, or other peril, it forces him or her to temporarily live elsewhere while the residence is being repaired.

For these reasons, insurers have created the ***Homeowners Policy***, which is designed to protect the physical assets owned, leased, rented, or used by individuals and families. Homeowners policies also provide protection for legal obligations owed to others and for the additional expenses involved in living elsewhere when the insured residence has suffered damage. Along with automobile policies, a Homeowners policy is an important part of a complete portfolio of financial protection.

Homeowners Coverage

When you studied the Personal Auto Policy (PAP), you learned a great deal about the way insurance policies are written. There was, however, only one policy or contract that was designed to fit the needs of most people. Although many people live in homes that they own, others rent houses or apartments. Some live in homes that they own jointly with other families, such as town homes, condominiums, or cooperatives ("co-ops"). Because the needs of individuals and families vary when it comes to the ownership of houses and personal property, and in order to offer options, insurers,

LEARNING OBJECTIVES

When you complete this chapter, you should be able to:

- Identify the various types of homeowners policies and the intended market for each
- Explain who is eligible to purchase a homeowners policy
- Explain the coverage provided under Section I of the homeowners policy
- List the property covered and not covered under Coverage C—Personal Property of the homeowners policy
- Briefly describe the types of property to which limited amounts of insurance apply under Section I
- Distinguish between the various homeowners forms based on their covered causes of loss
- Explain the relationship between the limits provided under a homeowners policy
- List the major exclusions of the homeowners policy
- Calculate how much would be paid in the event of a loss

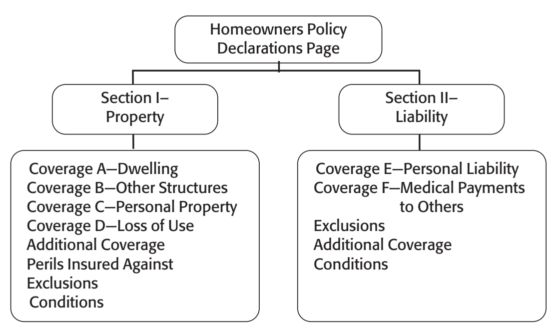
in conjunction with the ***Insurance Services Office*** (ISO), have designed several different types of policies that are all referred to as "homeowners insurance". The policies are designated by the initials "HO" (short for homeowners) and a number followed by a description of the basic coverage provided by the contract. Thus, the titles of the various policies we will discuss in this unit are:

HO-2 Homeowners Broad Form
HO-3 Homeowners Special Form
HO-4 Contents Broad Form
HO-5 Homeowners Comprehensive Form
HO-6 Unit-Owners Form
HO-8 Homeowners Modified Coverage Form

HO-2, HO-3, HO-5, and HO-8 are all designed for owners of one and two-family homes. A two-family residence is sometimes referred to as a duplex. The reason for offering a number of different types of policies is to provide the policyholder with coverage and price options. The major difference between these policies is the number of causes of loss or perils that apply to the property insured under the policy. HO-2 and HO-8 provide the least coverage under the homeowners program, while HO-3 and HO-5 are much broader and therefore more costly.

By far, the most commonly used policy is the HO-3 Homeowners Special Form. HO-4 Contents Broad Form is frequently referred to as a Tenants Policy or Renters Policy. It is used to insure those people who live in rented houses or apartments. The Unit-Owners policy, HO-6, is for owners of condominiums and other types of shared-ownership locations. HO-8, the Modified Form, is designed for the owners of older homes who may not wish to rebuild in the same location following a total loss.

Like the Personal Auto Policy (PAP), Homeowners policies contain a number of different sections that together provide a package of protection for the insured. The following diagram depicts the layout of the Homeowners policy: .



The coverage included in the policy is divided into two major sections: Section I—Property and Section II—Liability. As we discussed above, not everyone lives in a home that they own. Therefore, the specific coverage contained in each of the homeowners policies varies based on the needs of the insured. These difference will be discussed in a later section.

Quick Quiz 9.1

Match the Homeowners Policy to its intended customer.

A. Resident of a single family home	1. HO-3
B. Tenant in a rented house	2. HO-4
C. Owner or a 40-year-old home	3. HO-6
D. Owner of a cooperative apartment unit	4. HO-8
E. Owner of a two-family residence	5. HO-7

Who Can Purchase a Homeowners Policy

Eligibility for a homeowners policy is limited as it was with the Personal Auto Policy. To purchase a homeowners policy, a person must both own and occupy the residence. If the structure is a duplex, the owner must live in at least one of the units. If there are more than two living units, a business policy must be purchased instead of a homeowners policy. If the individual or family resides on a farm or ranch, a separate policy designed for their unique needs is available.

If you own a residential structure that you rent to other people, it must be insured under a special policy called a Dwelling Policy. The fact that such a residence is not owner-occupied disqualifies it for coverage under the homeowners program.

Of course, people who rent a home or apartment from others are eligible for the Tenant or Renters policy.

Section I–Property

The property portion of the Homeowners policy is further divided into four distinct sections:

Coverage A—Dwelling
Coverage B—Other Structures
Coverage C—Personal Property
Coverage D—Loss of Use

Coverage A–Dwelling

Coverage A applies to the ***dwelling*** that is located on the ***residence premises*** and any ***structures*** that are attached to the dwelling, such as an attached garage. "Dwelling" is the insurance word for a house or home and "residence premises" refers to the land on which the home is located. When you purchase a homeowners policy, you determine the amount of insurance you wish to carry for Coverage A. This amount is determined based on the cost to replace the home if it is destroyed.

Coverage B–Other Structures

Coverage B protects against damage or loss to structures located on the residence premises that are not attached to the dwelling. Examples of these types of structures are built-in swimming pools, sheds, fences, gazebos, and garages that are separated from the house (detached). You will note that insurers use the word "structure" as opposed to "building". A building has walls, a roof, and a floor. A structure, on the other hand, may not have any of these features. All buildings are structures, but not all structures are buildings. Both buildings and structures are referred to as ***real property***.

The amount of insurance on Coverage B is determined by the insurance company based on the Coverage A limit. The limit for Coverage B is 10% of the Coverage A limit. Therefore, if a dwelling is insured for $200,000 (the Coverage A limit), then the amount of insurance on other detached structures is automatically $20,000 (10% of $200,000). This amount may be increased if needed.

People who rent do not face a loss exposure for real property items, and therefore Coverage A and Coverage B are not included in the HO-4 Contents Broad Form policy.

Coverage C—Personal Property

You should recall from your study of Chapter 2 that real property consists of land and anything attached to it. ***Personal property*** is anything other than real property. To distinguish between the two, think of turning your house upside down and shaking it. Whatever falls out is personal property and whatever stays in is real property. The personal property insured by a homeowners policy may be owned by the insured or simply used by him or her. For example, suppose you borrow an item from a neighbor. While it is in your possession, it is damaged. Your homeowners policy would pay for the damage to the neighbor's personal property. The coverage for personal property is provided on a worldwide basis. So, if you travel to Europe and take clothing, cameras, and other items with you, your homeowners policy would protect you from loss to those items. Of course, whatever caused the loss either to the neighbor's property or to yours while located in another country must be a covered cause of loss.

Some types of personal property represent an increased hazard to the insurance company because they are more likely to be stolen or damaged, their loss may be difficult to prove, or they are not considered common to most people who purchase the policy. The homeowners policy places specific dollar limits on these categories of property and the most you can be paid for loss to these items is limited. The special limits that apply to these items of personal property are:

- $200 on money
- $1,500 on securities, personal records, passports and other valuable papers
- $1,500 on watercraft of all types (including their trailers)
- $1,500 on trailers, other than those used with watercraft
- $1,500 on THEFT of jewelry, watches, furs, precious and semiprecious stones
- $2,500 on THEFT of firearms and similar equipment
- $2,500 on THEFT of silverware, goldware, platinumware, and pewterware
- $2,500 on personal property on the premises and used primarily for business
- $500 on personal property off the premises used primarily for business
- $1,500 on electronic apparatus used primarily for business away from the premises, other than in a motor vehicle (such as a laptop computer)
- $1.500 on electronic apparatus used in motor vehicles if the apparatus can also be operated from another power source (such as portable CD players, TV sets, and similar equipment that can draw power from the car cigarette lighter or from a home electrical outlet)

Note that the limitations on jewelry, firearms and silverware apply only when the cause of loss is theft. This is based on the fact that a home is more likely to be burglarized if these types of items are contained in the residence, but the house is no more likely to suffer a fire or windstorm based on their presence.

Many people have items whose value exceeds these limits. A special endorsement to the homeowners policy, or a separate policy called a "floater" is available to provide coverage in excess of these limits.

Some types of personal property are not covered at all by Coverage C of the homeowners policy. In most cases the property is either better covered under another type of policy, such as the Personal Auto Policy, or the insurer does not feel that the insured possesses sufficient control over the property to insure it. Examples of property not covered by the homeowners policy include:

- Animals, birds, or fish—valuable animals may be insured by a type of health and life insurance policy issued by specialty insurers and generally available through veterinarians
- Motor vehicles—with the exception of vehicles used exclusively around the residence, motorized vehicles are covered under the PAP
- Aircraft and hovercraft—special policies are available to insure those individuals who own airplanes and similar items
- Property of others such as people who rent rooms in the insured residence
- Property that is rented to others off the residence premises, such as a ski rental shop operated by the insured
- Business records in computers or on paper—these may be insured by business insurance policies

Despite these exclusions, the personal property coverage of the homeowners policy is very broad and applies to most of the types of property you might own, such as your clothing, stereo, television, CD player, Playstation‰ or X-Box‰, snowboard, golf clubs, and the like.

As with Coverage B, the limit on Personal Property is determined by the amount of insurance on the dwelling under HO-2, HO-3, HO-5, and HO-8. The amount of coverage on personal property is automatically 50% of the Coverage A limit. Thus, our $200,000 home would include $100,000 of coverage on personal property. This amount of insurance may be increased for an additional premium.

If the insured is a renter, the amount of insurance for Coverage C is selected by the insured.

Quick Quiz 9.2

For each of the following, indicate which of the Section I Coverage (A, B, or C) would apply:

1. A tool shed located at the rear of the insured's property. _____
2. A satellite dish installed in the insured's back yard. _____
3. A carport connected to the insured's house with a common roof. _____
4. Lawn furniture located around the insured's swimming pool. _____
5. A child's jungle-gym located in the back yard. _____
6. Sporting equipment stored in the insured's detached garage. _____
7. A patio cover attached to the rear of the house. _____
8. A fence that surrounds the insured's property. _____
9. A greenhouse located behind the insured's home. _____
10. Light fixtures mounted near the doorways of the house. _____

Covered Causes of Loss

The major difference between the various homeowners policies is in the covered perils or causes of loss. With the exception of HO-5 Homeowners Comprehensive Form and HO-8 Homeowners Modified Form, all of the policies are issued on an ***open perils*** basis for the real property (dwelling and other structures) and a ***named perils*** basis for personal property. Form HO-5 is considered an open perils policy for all coverage. HO-8 is a named perils policy for all coverage. You should recall that the difference between these two types of coverage is that named perils only insures those causes of loss that are listed in the policy while open perils insures all causes of loss except those that are listed as excluded by the policy. The following chart summarizes the coverage provided by each of the homeowners policies. In reviewing the chart, note the differences between the policies in the limits, perils covered, and loss settlement provisions.

FORM	HO-2 Broad Form	HO-3 Special Form	HO 5 Comprehensive Form	HO-8 Modified Form	HO-4 Contents Broad Form	HO-6 Unit Owners Form
Sec I-Property						
A-Dwelling	Selected by insured	Selected by insured	Selected by insured	Selected by insured	N/A	$1,000 flat
B-Other Structures	10% of A	10% of A	10% of A	10% of A	N/A	Included in A
C-Personal Property	50% of A	50% of A	50% of A	50% of A	Selected by insured	Selected by insured
D-Loss of Use	30% of A	30% of A	30% of A	10% of A	30% of C	50% of C
Causes of Loss (Perils Covered)	Fire Lightning EC VMM Theft Glass Falling objects Weight of ice, snow or sleet Accidental discharge of water Sudden tearing apart Freezing Artificially generated electrical current	Open Perils Coverage A & B Broad Form Coverage C	Open Perils Coverage A,B,C	Fire Lightning EC VMM Theft ($1,000) Glass Volcano	Broad Form (same as HO-2)	Broad Form (same as HO-2)
Loss Settlement	Replacement Cost Coverage A,B ACV Coverage C	Same as HO-2	Same as HO-2	ACV Coverage A&B ACV Coverage C	ACV Coverage C	ACV Coverage A ACV Coverage C

Exclusions

All insurance policies contain exclusions for certain perils. The reasons for excluding certain causes of loss include their catastrophic nature, the inability of the insurance company to accurately predict losses, the fact that the loss can be expected, or the need to separately price certain coverage.

Although the homeowners policy is a very broad contract that covers many of the situations faced by owners of property, they typically exclude the following perils:

- Ordinance or Law—that portion of a loss that is caused by changes in building ordinances, zoning laws, and the like is not covered, except for a small amount included in the Additional Coverage section of the policy. For instance, if a home suffers a fire and the city requires that it be rebuilt using fire-resistive roofing material, the additional amount of the loss that is attributable just to the change in the law is not covered. This coverage is available for an additional premium.
- Earth Movement—many areas of the country are prone to earthquakes, landslides, mudslides, and other types of earth movement. If coverage is desired for this potentially catastrophic exposure, it can be included by endorsement to the homeowners policy or under a separate policy.
- Water Damage—damage to the home from flooding is excluded. Since 1968, flood coverage has been available exclusively under a government insurance program called the National Flood Insurance Program (NFIP). A separate policy is required for coverage from this important cause of loss. Also, water that backs up through sewers or drains is excluded. This coverage may be purchased by endorsement to the homeowners policy.
- Power Failure—if a utility interruption takes place away from the insured's premises, coverage is not provided under a homeowners policy. For example, a car hits a utility pole several miles from the insured's residence, causing a power outage that results in a loss to frozen food located in the insured's freezer. This loss would not be covered. Some insurers will make this coverage available for an additional premium.
- Neglect—if the insured fails to use reasonable means to protect insured property from damage, the loss would not be covered. If a portion of the roof blows off and the insured does not take steps to have the hole covered, a subsequent loss to the furniture in the home when rain comes through the hole would not be covered.
- War and Nuclear Hazard—these types of losses are not considered insurable due to their catastrophic nature.
- Intentional loss—sometime a policyholder will intentionally cause a loss in order to collect the insurance. Arson caused fires are an example of this situation, which constitutes a ***moral hazard***. The insurer is prohibited by public policy from paying such a loss, since to do so would encourage this type of activity.

Additional Coverage

Like most insurance policies, the homeowners policy includes some extra coverage that are needed by the typical policyholder. These are included at no additional cost. Examples of additional coverage under the homeowners program include a limited amount of coverage for removal of debris, loss to trees, shrubs, lawns and plants, the cost to make reasonable repairs following a loss, landlord's furnishings located in rental units, and ordinance or law coverage as previously mentioned.

Deductible

Like the physical damage portion of the Personal Auto Policy, a homeowners policy contains a deductible that applies to every loss to covered property. The minimum deductible is $250, but this amount may be increased, resulting in lower insurance premiums.

Determining the Amount of the Loss

Whenever a person's property is damaged, there are three important questions that must be answered in order to determine whether or not their insurance will provide coverage for the event:

- Is the event a covered cause of loss?
- Is there an exclusion or limitation in the policy that applies?
- How much should be paid?

The first two questions are answered by examining the type of policy (HO-2, HO-3, etc.) and the causes of loss covered and excluded in the policy, as well as special limits such as those that apply to business property, watercraft, and the like. The last question involves a section of the policy known as the ***loss settlement provision.*** It is important to understand the method that is used by the insurance company in adjusting or paying claims. In property insurance, there are two basic ways to value property: replacement cost or actual cash value. Replacement cost is just what the name implies—it is the cost to purchase new property to replace older property that was lost or damaged. Actual cash value, on the other hand, considers the typical useful life of a piece of property and the way that property physically depreciates over the course of time. In paying a claim, the insurance company will begin with replacement cost and then subtract or deduct the amount of physical deterioration the property has suffered as of the date of the loss. The balance is the actual cash value. As an example, suppose you purchased several shirts that are damaged in a fire.

If your insurance policy pays replacement cost, you simply go to the store and find shirts that are of a similar type and quality. The insurer will pay you the cost to buy new shirts. If the policy agrees to pay only the actual cash value of the shirts, the insurance company will first determine how long the shirts would have lasted you had they not been damaged. For clothing, a typical life expectancy might be only three years. If the loss occurs when the shirts are two years old, they are two-thirds "used up" or depreciated. In other words, even if they weren't damaged in a fire, you would only have been able to use them for one more year. If the cost of replacing the shirts is \$60 and they are two-thirds depreciated, the insurance company deducts \$40 and pays you only \$20. The mathematical formula used to determine the amount of actual cash value is:

Replacement Cost – Depreciation =
Actual Cash Value

Depreciation is calculated as follows:

$$\frac{\text{Age of property at the time of the loss}}{\text{Useful life of the property}} = \text{Percentage of depreciation}$$

As you can see, the deduction for depreciation can leave you short following a loss. It does, however, reflect the amount of money that indemnifies you for your loss. If you recall our earlier discussion of the principle of indemnity, the insurer attempts to return you to the same financial position you were in prior to a loss. This is indemnification. Before the loss to your shirts, you had two year old shirts. Following the adjustment of the loss on an ACV basis, you have the value of two year old shirts (\$20). Although that puts you back in the same place, it makes your shopping trip a little difficult. Because of this problem, insurers offer replacement cost insurance that will reimburse you on the basis of "new for old" and not require the deduction for depreciation. When deciding whether to purchase a policy on a replacement cost or actual value basis, ask yourself this question: following a loss, do you want to go shopping at the local department store and buy new things, or would you rather make your purchases at the thrift or second-hand store?

A homeowners policy automatically provides replacement cost coverage for the dwelling and other detached structures as long as the amount of insurance you purchase is equal to at least 80 % of the replacement cost of the structures at the time of the loss. Personal property, however, is covered on an actual cash value basis unless you request an endorsement to change the loss settlement provision to replacement cost. Insurers charge an additional premium to make this change. Form HO-8, since it is designed for older homes when the owner may not wish to rebuild, provides Actual Cash Value coverage on both real and personal property.

Quick Quiz 9.3

For each of the following items of property, calculate the amount of the depreciation and the actual cash value:

Item	Estimated Useful Life	Age at Time of Loss	Replacement Cost	Depreciation	ACV
Sweater	4 years	1 year	$40		
Shoes	2 years	6 months	$60		
Draperies	10 years	7 years	$350		
Set of dishes	7 years	5 years	$280		
Television	6 years	18 months	$800		
Chair	8 years	3 years	$200		
CDs	2 years	2 years	$15		
Tennis racket	3 years	2 years	$75		
Bedroom set	10 years	3 years	$1200		

Loss of Use Coverage

We have not yet discussed the coverage provided by Coverage D—Loss of Use in the homeowners policy. This important section of the policy provides money for you and your family to live elsewhere when you can't live in your home following a covered loss. If you have a fire in your kitchen, you may need to move out temporarily while the repairs are being made. Unfortunately, you will still have to pay your mortgage payment or rent. The additional amount of money it costs you to live in a hotel or motel, eat in restaurants, and use the Laundromat would be paid under Coverage D. The amounts must be reasonable and necessary to maintain your normal standard of living, and must be in addition to your normal expenses.

The limit on Coverage D varies depending on the type of homeowners policy purchased. It is determined based on the limit on Coverage A or Coverage C. Refer to the chart above for the specific percentages.

There are no causes of loss that apply to the loss of use coverage part. That's because loss of use is considered indirect loss coverage. You may recall from your earlier study that indirect losses are the result or consequence of direct losses to property. The only time you may collect under Coverage D is if a covered loss has damaged the property covered under Coverage A, B, or C and results in making the residence uninhabitable.

Summary

The coverage provided under Section I of the homeowners policy is very broad and intended to fit the needs of most people who own or rent property. Coverage includes the dwelling, any attached or detached structures on the property, personal property owned, rented, leased, or used by the insured and loss of use coverage in the event the property must be vacated during repairs. There are different types of homeowners policies available that vary based on price, coverage, and the needs of the insured.

CHAPTER 10

Homeowners Liability Insurance

Key Terms

- **Bodily injury**
- **Damages**
- **Insured location**
- **Occurrence**
- **Personal injury**
- **Property damage**
- **Protection class**
- **Residence employee**
- **Vicarious liability**

Many of the activities engaged in by individuals can create liability loss exposures. The very fact that people own and occupy residences can lead to legal responsibility for accidents that happen on the premises through the occupant's negligence. Consider the following scenario: the owner of a home installs an underground swimming pool in his back yard. Before he can complete the fence around the pool, a neighbor's child wanders into the back yard and falls in the pool. The child is seriously injured. Is the homeowner legally responsible for this injury? Most people would say "yes". Owners of property have a duty to protect people who are on the premises for legitimate purposes from harm. When they fail to do so, they can be held legally responsible.

We often become liable to others for injuries and damage that occur away from our own home. While playing golf on a municipal course, a woman's shot careens off a tree and breaks the windshield of a car parked in a nearby lot. She would be legally responsible for the damage to the vehicle.

Homeowners insurance policies provide protection for legal liability to others from bodily injury or property damage that arises out of the premises where the insured resides or his or her activities that take place away from the insured location.

Section II—Liability Coverage

As discussed in the previous chapter, a homeowners policy is a package of protection for those who own or rent property. This package includes both property and liability insurance. Unlike the coverage provided under Section I—Property, the liability section is the same regardless of the form or type of policy that is purchased by the insured. Therefore, the liability coverage provided for homeowners under HO-2, HO-3, HO-5 or HO-8 is identical to that for renters under HO-4 and unit-owners under HO-6.

Section II is divided into two different types of coverage:

Coverage E—Personal Liability

Coverage F—Medical Payments to Others

LEARNING OBJECTIVES

When you complete this chapter, you should be able to:

- Know what is required for a claim to be paid under Coverage E of the homeowners policy
- Identify the basic limit of liability for Coverage E and Coverage F
- Discuss who is insured under the liability section of the homeowners policy
- Describe the key definitions contained in Section II of the homeowners policy
- Describe how Medical Payments to Others applies
- List some of the exclusions contained in Section II of the homeowners policy
- Identify some of the endorsements available to a homeowner and the purpose for each
- Understand what factors affect the price of homeowners insurance

Coverage E—Personal Liability

The insuring agreement of Coverage E contains two important elements of protection for an individual. The first is to pay for ***damages*** for which the insured is legally responsible. The second is to provide a defense to the insured for any suits brought against him or her alleging bodily injury or property damage, provided the loss is not otherwise excluded by the policy. The first part of the promise, to pay damages, is limited by the amount of insurance purchased by the policyholder. The second, the duty to defend suits, is not limited. The cost to defend the insured is paid by the insurance company and is not subject to any dollar limit. It is paid in addition to any amounts paid as damages.

There are several things that must happen to "trigger" the coverage provided by a liability insurance policy.

- The insured must be legally liable for the damages
- The damages must arise out of an "occurrence" that takes place during the time the policy is in force
- The damages must be within the policy's definition of "bodily injury" or "property damage"
- There must be no exclusion that applies to the loss

If each of the above conditions is met, coverage is provided by the policy.

The basic amount of insurance provided under Coverage E is $100,000, although this amount can, and probably should, be increased by endorsement to the policy and payment of a small additional premium.

As an example of how the limits and defense costs apply under the homeowners policy, consider a situation in which a visitor to the insured's home is injured due to a dangerous condition on the property. The visitor sues the property owner for negligence and a court awards the victim $75,000 for medical expenses and an additional $35,000 for loss of income and services that must be purchased from others because the injured person can no longer perform them. The insurance company spends $22,000 in legal fees to defend the insured. The policy limit is $100,000. Because the total amount of damages ($110,000) exceeds the policy limit, the insurer will only pay $100,000. However, the cost to defend the lawsuit ($22,000) is not included within the policy limit, but is in addition to it. Therefore, the insurer is responsible to pay the entire $22,000 along with $100,000 of the judgment.

Who is Insured

One might think that the obvious answer is the person whose name appears on the policy's declarations page. However, other people are insured under the homeowners policy by virtue of their relationship to the named insured. These other people include the spouse of the insured (if they reside in the same household), any other relatives of the insured who live in the household, any person under the age of 21 who is in the care of the insured or a resident family member, and students under the age of 24 who are relatives of the named insured and enrolled in school on a full-time basis. Therefore, the following individuals would be included in the definition of "insured":

- The wife of the named insured if she resides with him in the household
- Anyone related to the insured by means of blood, marriage, or adoption (in-laws, stepchildren, etc.)
- Any other relative of the insured who lives in the household (uncles, aunts, grandparents, cousins, etc.)
- Anyone under the age of 21 in the care of the insured (foreign exchange students, foster children, etc.)
- The children of the insured who are under the age of 24 and are away at school full-time (as defined by the school) who were residents of the household before they went away to school

It is important to include minors who are in the custody of the insured for coverage. This is because a parent or guardian is legally responsible for the acts of those minors. This type of liability is called vicarious liability. In other words, it is not the actions of the insured that causes the injury or damage, but those of someone for whom the insured is responsible. The liability is "imputed" or transferred to the insured. You may have heard stories about teenagers who vandalize public property, injure classmates, or simply cause damage to a neighbor's property by hitting a baseball through the window. The liability for these activities rests with the adult who is responsible for the conduct of the minor.

Definitions

It is important to the understanding of liability insurance to examine some of the key definitions contained in the homeowners policy.

"Bodily injury" means bodily harm, sickness or disease, including required care, loss of services and death that results from injury. In other words, not only the amount of money required to heal the injured person, but any additional expenses they have for childcare, housekeeping, yard work, etc. that results from the injury.

"Property damage" means physical injury to, destruction of, or loss of use of tangible property. Similar to the definition of bodily injury, property damage also includes the cost of substitute property that is required while the damaged property is being repaired. If the "victim" of our runaway golf ball that crashed through the car window needed to rent a car while the automobile is being repaired, the cost of the rental car would be included under property damage.

"Occurrence" means an accident, including continuous or repeated exposure to substantially the same general harmful conditions, which results during the policy period in bodily injury or property damage. Note then that the injury or damage must take place between the effective date and expiration date of the policy, but coverage also applies to situations where the insured continuously or repeatedly does something that causes bodily injury or property damage. Say, for example, the insured has been burning trash on their property for many years. The prevailing wind causes the smoke to blow to an adjacent piece of property. The constant exposure to smoke has resulted in a neighbor's chronic bronchitis. This would be included within the policy's definition of "occurrence" as long as the bronchitis (injury) is discovered during the policy period.

"Insured location" is the residence premises (property on which the covered dwelling is located), and other places where an insured temporarily resides (such as a hotel), a secondary residence (a beach house or mountain cabin owned by the insured), vacant land, or a location rented by an insured (for example, a church or hotel ballroom in which a wedding or party is held).

Other definitions will be discussed throughout this chapter.

Coverage F—Medical Payments to Others

It is important not to confuse this coverage with the Medical Payments coverage we discussed under the Personal Auto Policy. In the case of the PAP, medical payments is provided for the insured and people who are riding in the insured vehicle. Quite the opposite, this portion of a homeowners policy never applies to anyone included within the definition of "insured". The purpose of medical payments coverage under the homeowners policy is to provide some level of protection for accidents that occur on the premises or arise out of the insured's activities away from the premises, but for which the insured may or may not be legally responsible. Imagine how you would feel if a neighbor's child was playing with your younger brother or sister and got injured on your property. Although you or your parents may not be legally liable, you might feel morally obligated to pay the urgent care bill. And remember our not-so-proficient golfer? What if instead of a car, her errant shot had hit another golfer and injured them? Medical payments coverage is designed for just these types of situations. The basic limit for this coverage is $1,000, but this amount can be increased by an endorsement to the policy. It is not necessary to establish legal liability for medical payments to apply. In fact, it is hoped that the voluntary payment of medical expenses will convince an injured person not to sue for additional damages.

Quick Quiz 10.1

Complete the following sentences:

1. In order to have liability protection under a homeowners policy, the insured must be ____________ __________ for the damages.
2. The minimum liability limit under Coverage E of the homeowners policy is $___________.
3. Section II—Liability is ____________ under each of the different homeowners forms.
4. A situation where a parent becomes legally responsible for acts committed by his or her minor children is called ______________ _____________.
5. The property on which the insured dwelling is located is referred to as the ______________ _______________.
6. Medical payments coverage is included in a homeowners policy for a basic limit of $__________, which may be increased by endorsement.
7. The two types of damages covered under Coverage E are _______ _________ and __________ __________.
8. In order to be covered by a homeowners policy, the __________ must take place between the effective date and expiration date of the policy.

Exclusions

The exclusions in Section II apply in three different ways: some apply only to Coverage E, some exclusively to Coverage F, and some to both coverage.

Coverage E Exclusions

Among the Coverage E exclusions are liability assumed under contract (except contracts involving the ownership, maintenance, or use of an "insured location"), damage to property owned by an insured (since this would be covered under the property section of the policy), workers' compensation, nuclear, and injury to an "insured".

Coverage F Exclusions

There are only four exclusions that apply to Coverage F. No coverage is provided for injuries to ***"residence employees"*** who are injured somewhere other than an "insured location". A "residence employee" could be a maid, housekeeper, gardener, or other person who provides services that would ordinarily be done by the homeowners themselves. Also excluded are workers' compensation, nuclear, and injury to anyone who is a regular resident of the household.

Exclusions that Apply to Both Coverage E and Coverage F

The following list identifies some of the important exclusions that apply to all coverage under Section II:

- Motor vehicles—most motor vehicles are covered under the Personal Auto Policy. An exception is made (and therefore coverage does apply) to those vehicles used only on the residence premises, designed to assist the handicapped, or golf carts while being used to play golf.
- Watercraft—liability coverage is provided for very small boats that do not have large engines, such as rafts, rowboats, and fishing boats. Wave Runners, jet skis and ski boats, however, should be insured under a separate Watercraft Policy.
- Aircraft and Hovercraft—since most policyholders don't own these items, coverage is unnecessary under the homeowners policy. Separate aircraft liability policies are available to those who do own, rent, or lease aircraft.
- Injuries expected or intended by the insured—such as assault and battery when the insured meant to cause harm to the victim.
- Business exposures—these should be insured with a business policy.
- Professional liability—if the insured is a physician, attorney, accountant, or insurance agent, their liability for professional misconduct should be insured under a separate policy.
- Any location not included within the definition of "insured location" as stated above.
- War
- Transmission of communicable diseases
- Sexual molestation and physical or mental abuse
- Sale, manufacture, delivery, or possession of a controlled substance

The last three exclusions have only recently been added to the policy and reflect some of the social issues of our time. Clearly insurance companies do not wish to insure people for behavior that is generally prohibited by law or is considered socially unacceptable. Insurance is not meant to replace personal accountability.

Additional Coverage

Similar to Section I of the homeowners policy, Section II also contains some additional coverage at no cost to the insured. The most significant of these additional coverage is the Damage to Property of Others provision, which provides up to $1,000 when an insured causes damage to property owned by someone else. Situations in which this coverage would apply are when the insured's children throw a rock that breaks a neighbor's window or the insured's pet digs up a neighbor's shrubs. You may or may not be legally liable for the damage, but establishing liability is not required for this limit to apply. Simply feeling morally obligated is sufficient.

The following chart summarizes the coverage provided under Section II of the homeowners policy:

HOMEOWNERS SECTION II-LIABILITY AND MEDICAL PAYMENTS COVERAGE

	Coverage E-Personal Liability	Coverage F-Medical Payments
Coverage	Claims made or suits brought against an insured for damages because of Bodily Injury or Property Damage caused by an occurrence to which this insurance applies.	Necessary medical expenses that are incurred or medically ascertained within 3 years from the date of an accident causing bodily injury.
Basic Limits	$100,000 per occurrence	$1,000 per person
Persons Insured	named insured –resident relatives –under 21 in care of above –relatives under 24 away at school –person or organization responsible for animals or watercraft –residence employees and others using a covered vehicle	EXCLUDES: insured and residence employees COVERS: –persons on insured location with permission –persons off premises if BI: 1) caused by insured's activities 2) caused by residence employee 3) caused by animal owned or in care of insured
Locations Insured	–"residence premises" –other locations used as a residence shown in declarations or acquired during policy period –nonowned where insured is temporarily residing –vacant land –land where a home is being constructed –cemetery plots and burial vaults –part of premises rented to insured for other than business purposes	–residence premises –other locations as noted above
Exclusions	–loss assessments (except under Additional Coverage) –contractual (except incidental) –PD to property owned by insured –PD to property in CCC of insured except due to fire, smoke, explosion –workers' compensation –nuclear –BI to insured –expected or intended –business pursuits including day care –rental property (with exceptions) –professional services –not an insured location –motor vehicles (with exceptions) –watercraft (with exceptions) –aircraft –war –communicable diseases –sexual molestation/abuse –controlled substances	–residence employee off premises –workers' compensation –nuclear –person, other than residence employee, regularly residing on premises Same
Conditions	Limit of Liability Severability of Interest Duties After a Loss Suit Against Insurer Bankruptcy of Insured Other Insurance	Limit of Liability Duties of Injured Person Same Same Not included Payment of Claim

Endorsements to Homeowners Policies

We have previously discussed how insurance policies are designed for a "typical" insured. Therefore, if you have exposures that the average person does not possess, you may need to purchase endorsements to your policy in order to tailor it to your needs. The following is a list of some of the major endorsements available under the homeowners program.

Earthquake Endorsement

If you live in an area where earthquakes are common, you may wish to purchase this optional coverage. In addition to coverage for earthquakes, the endorsement also provides protection in the event of landslides, volcanic eruption, and other types of earth movement. A deductible applies and varies depending on the location of the property and the insurer.

Personal Property Replacement Cost Endorsement

In our earlier discussion of the loss settlement provision under Section I we described how a loss to personal property would be paid under a homeowners policy. Since replacement cost applies only to the real property (dwelling and other structures), an endorsement is necessary to provide the same coverage for personal property. Without this endorsement, any Coverage C losses will be adjusted on an actual cash value basis, with a deduction for depreciation. When this endorsement is attached to the policy, most insurers require that the insured purchase a higher limit for Coverage C, typically 70% or 75% of the dwelling limit (as opposed to the standard 50%).

Scheduled Personal Property Endorsement

Some of the Coverage C limits, such as the one applying to jewelry, may be too low. Many people have wedding or engagement rings that well exceed the $1,500 limit provided in the basic policy. Therefore, they may need to purchase this endorsement that provides a specific limit for any items that are of value. A list of the items to be insured is included in the endorsement and a limit is chosen for each. The coverage is provided on an "open perils" basis and no deductible applies.

Personal Injury Endorsement

Section II of the homeowners policy only provides coverage for bodily injury and property damage. This important endorsement broadens that coverage to include such things as libel, slander, defamation of character, violation of the right of privacy, false arrest, wrongful entry and wrongful eviction. How important is this coverage? Suppose you call someone a name in public. They could sue you for slander. Since there is no actual injury to their body, just their reputation and feelings, no coverage would be provided under Section II unless this endorsement is attached to the policy.

Shopping for Homeowners Insurance

The market for homeowners insurance can be very competitive or may be somewhat limited in your area. As with all other insurance products, it is important that you understand how the pricing is determined and the need to shop for the best value.

Property Coverage

Since fire, windstorm, and theft are the primary causes of loss under homeowners policies, the insurance company develops premiums based on the home's exposure to these types of losses. The main factors involved in pricing homeowners insurance are:

- The age and type of construction of the dwelling
  - Wood frame
  - Steel frame
  - Brick, stone, or masonry veneer (a thin covering over wood)
  - Brick, stone, or masonry
  - Frame with plastic or aluminum siding

List five exclusions under Section II of the homeowners policy:

1. ______________________________
2. ______________________________
3. ______________________________
4. ______________________________
5. ______________________________

Describe two endorsements to the homeowners policy:

1. ______________________________
2. ______________________________

Quick Quiz 10.2

- Type of roof (shingle, wood shake, tile, composition)

The more fire resistive the structure, the lower the cost of homeowners insurance. Roofing material, for example, can vary from wood shake which is highly flammable to tile which is much more fire-resistive.

- The location of the dwelling
  - Miles from fire department
  - Feet to fire hydrant
  - Public fire protection

Generally speaking, a home located in an urban area may receive better fire protection than one located in a rural area. All property in the United States is assigned a public fire ***protection class***. This number is from 1 to 10, with one being the best fire protection and 10 being unprotected. The lower the protection class, the lower the premium. Other factors in determining the price of insurance are:

- The Coverage A limit
- The deductible chosen
- The type of policy (HO-2, HO-3, HO-5, etc.)
- The options and endorsements chosen

Liability Coverage

The bulk of a homeowners policy premium is developed based on the property insured. However, the factors that influence the cost of Section II include:

- The limit of liability chosen
- Any unusual hazards (animals, ponds, pools, etc.)
- The options and endorsements chosen

We have included a copy of the homeowners application for you to review. This will give you additional information about what is important to the insurance company when determining eligibility and pricing of homeowners insurance. Also included is a copy of a homeowners policy.

Summary

Just as people who own or use automobiles are subject to legal liability arising out of their use, owners and occupants of property are also exposed to loss when they become legally responsible for injuries or damage to others that result from the property itself or the activities of the individual. Section II of the homeowners policy provides protection to individuals and families on a very broad basis. In addition to payment for damages, an important aspect of liability protection is the defense of the insured against allegations of negligence.

Homeowners policies are very flexible, using endorsements to modify basic coverage to fit the needs of policyholders. Pricing for homeowners coverage varies based on the insurance company selected, the limits of the policy, the type and location of the dwelling, and the presence or absence of liability exposures.

Supplemental Material: Case Studies

The case studies on the following pages may be used in a number of ways. Some involve an analysis of a family's loss exposures that include automobile and other property and liability situations. Students could work in groups to identify and analyze the loss exposures and suggest methods to treat them. Although the cases may go beyond the material presented in the text, they are based on real-life situations and therefore will give students a chance to use their analytical and problem-solving abilities. Students can provide you with written reports, or could make a presentation to the class. A discussion involving the entire class will no doubt cast the case in a different light and reveal additional exposures.

You can also use the cases to do "brainstorming" sessions with the class. See how many ideas they can come up with, without judging the quality of their answers. The purpose is to get as many concepts as you can in a short period of time. Then, the class could be broken into groups that would take the results of the brainstorming session and provide further detail.

Some cases are short and involve only specific exposure areas, such as automobile. Others are based on claims that have taken place. Each of these cases will enable the students to apply the new knowledge they have acquired and direct their own learning. You may wish to supplement the material with any information you have or cases of which you are aware. These cases can also be used for extra credit or as homework assignments.

At the end of each case are suggested questions that the students should consider when analyzing the facts of the case. These are only suggestions and you may wish to add, delete, or change the questions to better suit your class. We have also included some suggested answers, although you and the class may come up with many others.

Case Study #1

Alex and Pam Rodriguez are the owners of a home in eastern Missouri that has a replacement value of $250,000. It is located in a newer neighborhood that was recently developed near a river. The home is located in a gated community and the Rodriguez' belong to a homeowners association that controls the property located in the community. They have a mortgage of $200,000 and have saved enough money to furnish the home with nice furniture, artwork, and some antiques. There is a pool in the backyard, a beautiful patio area, and a large gazebo. The four-car garage is detached from the house. Alex is an attorney in private practice and works out of an office located in their home. He has a part-time employee who comes to the house once a week. He earns approximately $120,000 annually in his law practice. In addition, due to his occupation, Alex has been asked to serve on the board of directors of several local organizations, including the little league and the board of a private school attended by Alex and Pam's three children. Alex is 35 and Pam is 33. Pam is an accomplished musician and provides music lessons in their home several afternoons a week. She is paid a modest amount for these lessons. She also volunteers to help in the children's classrooms at school as often as possible. Several years ago Pam was diagnosed with multiple sclerosis (MS), but she is in a period of remission and is able to keep up a full schedule at this time. To help out with the housework and children, the Rodriguez family employs a housekeeper 10 hours per week.

The Rodriguez children, Paul (age 17), Sara (age 15), and Alex, Jr. (age 10) attend a local private school. All are active in athletics and various after-school activities including band, dance, and martial arts. Pam frequently provides transportation to and from various school and other events for her children as well as others. Paul will graduate this year and will be attending a private four-year college in Southern Illinois in the fall. He will live in a dormitory on campus.

Pam drives a 2001 minivan which is leased and Alex owns a 2002 Lexus convertible. Pam uses the minivan to run errands and take the children to school and other events. Since Alex works at home, his use of the Lexus is for pleasure and to drive back and forth to a client's home or office. Paul has a 1998 Toyota which he will be taking to school with him. He uses it to drive himself and, occasionally, his brother and sister back and forth to school.

For recreation, the Rodriguez family often takes their ski boat out on the local rivers and lakes. The children are all avid water skiers and they frequently bring friends along. Alex, Jr. is a star shortstop on the local little league team, and Alex, Sr. helps to coach the team. Sara is very involved in music and dance and has appeared in some local stage productions. Pam is often asked to help with the productions due to her musical background. Paul was the captain of his school's swim team and has earned a partial scholarship based on his academic and athletic achievements.

- What are the property loss exposures faced by the Rodriquez family?
- What are the liability loss exposures faced by the Rodriquez family?
- What are the personal (life and health) issues faced by the Rodriquez family?
- What could the family do to reduce its loss exposures?
- What type of insurance products should the Rodriquez' purchase?
- What type of deductible do you think they should use? Why?

Case Study #2

Ellen Smith drives a 1997 Honda Civic. One day when Ellen is returning home from work, she encounters a large object in the roadway ahead of her. Since it is dusk, visibility is limited, and not knowing exactly what the object is, Ellen swerves to avoid contact. Ellen's car hits some loose gravel on the side of the road, the vehicle skids, hits a fence, and comes to rest against a tree. The driver-side window is shattered and there is extensive damage to Ellen's car door. She hits her head on the steering wheel and suffers facial injuries and also has cuts from the broken glass. Another motorist sees Ellen hit the tree and calls 911. Since the door is badly damaged, the fire department is dispatched to use the "jaws of life" to rescue Ellen from the vehicle. She is taken by ambulance to a local hospital, where she is released later that evening. When she is interviewed by a police officer taking a report of the accident, Ellen remembers having seen a gravel truck ahead of her just prior to the accident. The skid marks show that Ellen may have been exceeding the posted speed limit at the time of the accident.

Ellen has purchased a Personal Auto Policy from Upstate Mutual Insurance Company. The policy includes liability, medical payments, uninsured motorists, collision and other than collision coverage.

- Is Ellen legally responsible for the accident? Why or why not?
- What is the extent of the bodily injuries and property damage involved in this loss?
- What coverage is available to Ellen under her automobile insurance policy? Why?
- Is there anyone else who may be legally responsible? Why?
- Does uninsured motorists coverage apply to this accident?
- What options does Upstate Mutual have in handling this claim?

Case Study #3

Raymond is a college student who works part-time as a delivery driver for Hometown Pizza. Usually Raymond drives his Chevrolet pick-up truck to deliver pizzas, however, when his truck is at the shop being repaired, Patrick, Raymond's boss and the owner of the pizza parlor, loans him a company car to make the deliveries. Raymond is insured under a PAP policy with no special endorsements. One evening, while driving the company car, Raymond is involved in a serious accident. Returning from a delivery, Raymond takes his eyes off the road for a second and rear-ends a woman driving a compact car. Her young daughter, who was riding in a rear seat, is injured. There is significant damage to the rear of the other party's vehicle, as well as moderate damage to the front of Hometown Pizza's vehicle. When Raymond submits the claim to his insurance company, he is told that there is no coverage for the accident because he was not the owner of the vehicle he was driving at the time of the incident.

- Using the PAP policy, determine whether or not you think Raymond's auto insurer was correct in their position regarding coverage for the accident. Why or why not?
- What specific insuring agreements, conditions, or exclusions apply to this situation?
- What endorsement(s) are available for use with the PAP that should have been offered to Raymond?
- How would a policy issued to Hometown Pizza affect the outcome of this case? Is it possible that both policies would apply to the loss? Why or why not?
- What do you feel is the best way to handle a similar situation where an employee drives a vehicle owned by his or her employer?

Case Study #4

Millie is a single mother with two young children. She lives in a small home that she rents from an old family friend. The home is located in an older, well-maintained neighborhood. Recently, there have been a number of burglaries in the neighborhood during the daytime while the occupants of the homes are away at work. Nothing of substantial value has been taken, but Millie is concerned since it seems to be happening with more frequency. The burglars usually enter through a rear door or window. In addition, Millie sometimes works a second job at night, leaving the children with a babysitter. There is no garage, so Millie parks her early model car on the street each night. A neighbor told Millie that she has recently seen some teenagers driving through the area late at night.

- What loss control steps would you recommend Millie take with regard to her home?
- Do you feel the landlord has any responsibility for loss control of the property? Why or why not?
- What precautions can Millie take with respect to her automobile?
- What other loss control measures could be enacted in this situation?
- Are there any other people or organizations who should participate?

Case Study #5

Jessica is a 21-year-old junior in a local private university. She lives on campus in a dorm room that she shares with Claudia, her roommate. The girls have furnished their room nicely with a refrigerator, big-screen television, stereo, video game equipment, and comfortable chairs. Both girls are athletic and also have snowboards, tennis rackets, and other sporting equipment. Jessica works part-time as a waitperson in a restaurant a few blocks from campus. Although her parents have set aside sufficient money for Jessica's tuition, she is responsible for her personal spending while away. Jessica has an older model Acura that she uses to drive back and forth to work when the weather is bad, or to go to the mountains or beach for recreation. Jessica and Claudia frequent a local sports bar on the weekend, to relax and unwind from their week. Jessica has been known to drink too much on occasion, but she is very protective of her car, so she drives both she and Claudia home. Both girls are considered good students and have made the dean's list for their academic accomplishments.

- Identify the property loss exposures.
- Identify the liability loss exposures.
- Identify the personal (life and health) loss exposures.
- Suggest loss control (prevention and reduction) techniques that the girls could implement for each of the exposures you identified above.
- What is an appropriate risk management tool to use for each of the loss exposures? Why?

Case Study #5A

Using the facts in case study #5, consider the following loss scenario.

One Friday night, Jessica and Claudia are out partying. Although Jessica has had quite a bit to drink, she insists on driving herself home. Claudia reluctantly goes along. Before they even get out of the parking lot at the bar, Jessica realizes she should not be driving, so she asks Claudia to drive. About a block from the university, Claudia sees someone in a crosswalk in front of her. She thinks she has sufficient time to stop, and applies the brakes. Unfortunately, the Acura's brakes are not as good as those on her own vehicle, and Claudia hits the person in the crosswalk, throwing him about 100 feet in the air. The girls immediately call 911 to report the accident and request an ambulance. The pedestrian is awake and appears to not be seriously hurt, but he is unable to stand and walk. The Acura suffers major damage due to the impact. The police arrive and begin to question Claudia and Jessica about the accident. When they smell the alcohol on their breath, they administer a field sobriety test and determine that Claudia was operating the vehicle under the influence at the time of the accident. Both girls are taken into police custody and the Acura is impounded. The pedestrian is taken to the emergency room, where he is later pronounced dead from head injuries.

At the time of the accident, Jessica's parents are still the legal owner of the Acura and it is insured under their PAP with the following limits:

$300,000 Combined Single Limit for Bodily Injury and Property Damage
$10,000 Medical Payments
$100,000 Uninsured Motorists
$1,000 deductible Collision and Other Than Collision

Claudia owns her own car, and also has a PAP with the state minimum limits of $10,000 Bodily Injury each person, $20,000 Bodily Injury each accident, and $10,000 Property Damage. She also has $10,000/$20,000 Uninsured Motorists. Because her vehicle is older, she does not carry Collision or Other Than Collision coverage.

The family of the pedestrian sues Jessica, Claudia, and Jessica's parents. They are awarded $1,500,000 in general damages (pain and suffering), $15,000 in special damages (medical and other bills), and $5,000 for funeral expenses.

- How will each of the PAP policies respond to the damages in this case?
- Which policy will pay first and which will pay second?
- Are there any amounts that would not be covered by the policies? How will those be paid? Who will be responsible?
- Does it matter that the girls were DUI at the time of the accident? Why or why not?
- Are there any provisions of the PAP policy that would restrict or limit coverage for this accident?
- What responsibilities do Jessica's parents have in this situation?
- What would you recommend to Jessica's parents for insurance in the future?

Glossary

A

ACCEPTANCE
Agreeing to an offer made by another so that a legal contract is formed and the parties to the contract are bound. With an insurance contract, the offer is usually made by the applicant and accepted by the company. See Contract.

ACCIDENT
A sudden and unexpected event that results in a financial loss. See Occurrence.

ACT OF GOD
Accident or event resulting from natural causes, without any human intervention such as flood, lightning, earthquake, or storms.

ACTUAL CASH VALUE (ACV)
Replacement (current) cost minus depreciation from wear and tear or obsolescence.

ACTUARY
A mathematician who specializes in the field of insurance. The actuary determines, on the basis of existing experience, the expected value of events that may occur in the future.

ADDITIONAL INSURED
Individual or business (such as a bank or loan institution), other than the named insured, who has a financial interest requiring protection under the terms of the insurance contract, e.g., the spouse of the insured or the lienholder on the loan for a car.

ADDITIONAL LIVING EXPENSE INSURANCE
Insurance coverage to pay for extra necessary living costs spent during the time it takes to repair or replace insured property that has been damaged or destroyed by an insured peril.

ADJUSTER
Salaried employee of an insurance company, or an independent contractor representing an insurance company, who is responsible for determining the cause and amount of a loss, the insurance company's liability for the loss, and satisfactory agreement on the amount of loss from the parties involved. Also called a claims adjuster or independent adjuster.

ADMITTED COMPANY
Insurance company licensed to transact business in a given state. A Certificate of Authority has been issued by the state of domicile.

ADVERSE SELECTION
Tendency of less desirable risks to purchase or renew insurance to a greater extent than better risks; selection against the best interests of the insurance company.

AGENCY
The legal principle that allows an individual or organization to represent another individual or organization. Also, an organization that sells and services insurance policies for consumers.

AGENCY MANAGEMENT SYSTEM
The computer software used by an insurance agency to manage customer accounts, perform word processing, accounting, and other functions.

AGENT
A person licensed by the state insurance authority to sell insurance produces. The agent represents the insurance company in all transactions. See Broker and Producer

AGGREGATE LIMIT
The maximum limit of liability the company is obligated to pay for all claims within a specific time period, usually one policy year. See Occurrence.

AGREED VALUE COVERAGE
An option for property policies where the insured and the company agree to the value of property prior to a loss.

AIRCRAFT HULL INSURANCE
Coverage for direct loss or damage to aircraft.

ALEATORY
Contract in which one party may obtain greater value under the agreement than the other party, and in which payment depends upon a fortuitous event. An insurance contract is an aleatory contract. See Consideration.

ALIEN INSURANCE COMPANY
Insurance company incorporated and organized under laws of a foreign nation, state, province, or territory, rather than under the laws of the United States.

ALL RISK COVERAGE
Common term for broad property or liability insurance coverage against "all risks" of loss, except those causes excluded or limited in the policy. Also known as Open Perils.

ALLIED LINES
Lines of insurance generally related to property insurance, such as sprinkler leakage, glass, water damage, and earthquake coverage.

ANNUAL STATEMENT
Insurance company's yearly financial report required by various state insurance departments. Covers the calendar year period and is made according to a form agreed upon by the National Association of Insurance Commissioners.

APPARENT AUTHORITY
The authority the general public assumes an agent has due to his actions, regardless of whether the authority has been given to the agent by law or contract.

APPLICATION
The questionnaire completed by an applicant for insurance that will be used during the underwriting of the policy. The application is considered the "offer to purchase". See Contract

APPORTIONMENT CLAUSE
See Other Insurance Clause

APPRAISAL
Estimate of the amount of loss, or damage, or value to insured property. If the insured and the company cannot agree as to the value of the property or damage, they will seek agreement through the Arbitration Clause. See Arbitration.

APPRAISAL CLAUSE
Provision in an insurance policy setting forth duties of the insured and the insurance company when there is a dispute over the amount of loss. For example, a fire insurance policy provides for appraisal at the demand of either party after a loss. See Arbitration.

ARBITRATION
Settling differences relating to loss under an insurance policy between the insured and the insurance company (first party losses). Each party selects a representative who, in turn selects a disinterested arbitrator(s) whose decision or award is binding upon both parties to the insurance contract.

ARSON
The act of deliberately burning property. Arson is a felony is most jurisdictions.

ASSESSMENT
Additional fixed charge or proportionate share of claims expenses sometimes levied against policy owners by an assessment mutual insurance company when premiums are insufficient to meet its costs of operations.

ASSIGNED RISK
An individual or company that is uninsurable will be assigned an insurance company from a pool of insurers (usually all that hold Certificates of Authority in a specific state). The company must accept the risk, however can charge an appropriate premium.

ASSIGNMENT
Legally transferring a policy owner's rights or interests in an insurance policy to another party. The insured requests the assignment, however the company can either accept or reject the request.

ASSUMPTION OF RISK
When an insured accepts the risk presented to him or her, accepting full responsibility for any loss that may occur.

ASSURED
Another term for the insured under an insurance policy.

ATTORNEY-IN-FACT
Person empowered to act for another party; chief administrative officer of a reciprocal insurer who is given authority to exchange insurance with other insureds in the reciprocal exchange. See Reciprocal Exchange.

ATTRACTIVE NUISANCE
Something that, although normally harmless, may attract people who do not understand its uses and may cause injury. Typically this doctrine applies to children who may be attracted to things such as swimming pools or animals that can cause them harm.

AUTHORIZED COMPANY
An insurer who meets the licensing criteria of the state they wish to do business in and is in receipt of a Certificate of Authority. Also known as an Admitted Company.

AUTO POLICY
Policy providing coverage for specified vehicles, usually including liability, physical damage, medical payments, and physical damage.

AUTOMATIC COVERAGE
Common term for coverage provided automatically in property and liability policies, generally for a limited time and amount, for newly acquired property such as an automobile.

AUTOMOBILE INSURANCE PLAN
Another term for Assigned Risk.

B

BAD FAITH
An allegation made against an insurance company by a policyholder that it has not acted in good faith.

BAILEE
A person or firm who accepts the property of others for repair, cleaning, or other services, such as a dry cleaner.

BAILOR
Owner of property who delivers it in trust to a bailee for a special purpose, such as a customer who leaves clothing with a dry cleaner.

BANKRUPTCY
Court proceedings for distribution of property of an insolvent person or company among his or her creditors. After distribution, he or she is relieved of all liability to these creditors even though payment to some of the creditors may be less than the full obligation.

BANKRUPTCY CLAUSE
Clause in an insurance policy providing that bankruptcy or insolvency of the insured does not relieve the insurance company of any of its obligations under the policy.

BENEFIT
A term for the coverage provided under an insurance policy, usually referring to life or health insurance.

BEST RATING
A rating given to an insurance company based on its financial status and dealings with customers. Provided by the A. M. Best Company.

BETTERMENT
A term used by claims adjusters to refer to the payment of a loss on a replacement cost basis, rather than the depreciated value of the property.

BINDER
Temporary evidence of insurance until a policy is issued by the insurance company. A binder may be written or oral.

BLANKET INSURANCE
Property insurance that extends to more than one location or more than one type of property. See Specific Insurance.

BOATOWNER'S POLICY
Hull physical damage and liability coverage for losses arising out of the ownership, maintenance, or use of a watercraft. See Yacht Coverage.

BODILY INJURY (BI) LIABILITY COVERAGE
Liability coverage protecting the insured from financial loss in the event he or she is liable to pay damages because of bodily injury, sickness, or disease resulting from an accident or occurrence.

BOND
Written agreement under which a surety agrees to pay a financial loss of another party, called the principal.

BOOK OF BUSINESS
A company or agency's total amount of insurance issued in a particular line of business, such as automobile insurance.

BREACH OF CONTRACT
Failure to comply with terms or conditions of an insurance policy that may result in restricted coverage or may void the policy.

BROKER
One who, for a commission from the insurance company, solicits, negotiates, and services insurance policies on behalf of the person buying the insurance. See Agent and Producer.

BUDGETS
Financial reports that estimate the amount of income and expenses a firm will receive and spend in a future period of time.

BURGLARY
Forcible entry into or exit out of the premises of another with the intent to steal property. There must be visible signs of forced entry or exit.

BUSINESS AUTO POLICY
Insurance for commercial automobile risks against legal liability, physical damage, medical expenses, loss from uninsured motorists, physical damage, and personal injury protection or other equivalent no-fault coverage. Coverage can be extended to owned, leased and borrowed vehicles.

BUSINESS INCOME INSURANCE (BUINESS INTERRUPTION INSURANCE)
Coverage for loss of earnings resulting when a business must shut down or curtail its operations after damage or destruction of property by an insured peril. Applies for the length of time it takes to rebuild, repair, or replace the damaged or destroyed property so that business operations can be resumed.

BUSINESS PURSUITS ENDORSEMENT
An attachment to a Homeowners policy (HO) that provides liability coverage for business conducted at and away from the residence. See Homeowners Coverage

BUSINESSOWNERS POLICY (BOP)
A package policy designed for retail, service firms, and other small businesses to provide property and liability coverage.

C

CANCELLATION
Termination of a policy before the end of the policy period by the insurance company or the insured according to the terms of the policy. Also see Nonrenewal, Pro Rata Cancellation and Short Rate Cancellation.

CANCELLATION REQUEST
The document signed by a policyholder that requests termination of an insurance policy.

CAREER
One's chosen profession and for which a person has received specialized training and education.

CARRIER
The insurance company or insurer.

CASUALTY ACTUARIAL SOCIETY
The professional organization to which actuaries belong.

CASUALTY INSURANCE
The generic term for nonproperty insurance coverage, such as liability, crime, workers' compensation insurance, fidelity, and surety. In some states, accident and sickness insurance are considered casualty coverage.

CATASTROPHE
Sudden, unexpected, unavoidable, and severe disaster involving a large population, or an event causing loss of an extraordinarily large amount. Examples would include flood, earthquake or hail.

CERTIFICATE OF AUTHORITY
The insurer's license to conduct the business of insurance; the legal certificate issued by a state insurance department granting an insurance company legal power and right to issue contracts of insurance within the state.

CERTIFICATE OF INSURANCE
Evidence that insurance has been arranged, usually given to someone other than the policyholder, such as a bank or mortgage company.

CLAIM
Notification to the insurance company that a loss has occurred and demand for payment for the loss, as provided by the terms of the insurance policy.

CLAIMANT
One who has a claim according to the provisions of an insurance policy. The policyholder is considered a first-party claimant and others are considered third-party claimants.

CLAIMS ADJUSTER
See Adjuster.

CLASS
Group of risks with the same general characteristics and exposures to a peril that are grouped together for rating purposes.

CLASS RATE
Rates that apply to all members of a certain group, such as youthful male drivers of automobiles.

COINSURANCE CLAUSE
(A) For property and casualty policies, a provision requiring a specified amount of insurance based on the value of the insured property. There may be a penalty in the event of a partial loss when the insured fails to comply.
(B) For health insurance, a coinsurance provision obligates the insured to absorb a specified percentage of medical expenses that otherwise would be paid by the insurance company.

COLLISION INSURANCE
Automobile coverage for direct and accidental loss to the insured automobile resulting from upset or impact with another vehicle or other object, usually paid without regard to fault.

COLLUSION
Secret agreement and cooperation between two individuals or corporations, to the detriment of others and for fraudulent and deceitful purposes.

COMBINED SINGLE LIMIT (CSL)
Combining the liability limits of bodily injury and property damage into a single limit of liability for both. Example: $25,000 per person/$50,000 per occurrence for bodily injury and $15,000 for property damage liability is equivalent to $65,000 ($50,000 + $15,000) combined single limit of liability for BI and PD.

COMMERCIAL INSURANCE (COMMERCIAL LINES INSURANCE)
Common term for insurance written to cover the exposures to loss faced by businesses and other organizations. See Personal Lines Insurance.

COMMISSION
Compensation paid by an insurance company to an insurance agent or broker for sale or service of a policy.

COMMON LAW
Law derived from common usage or from court decision.

COMPARATIVE NEGLIGENCE
A type of state law that compares the responsibility of two parties involved in an automobile accident and assigns each a degree of fault.

COMPARATIVE RATING
A computer software application that allows an agent or policyholder to obtain insurance quotations from a number of different insurance companies based on the same set of underwriting facts.

COMPREHENSIVE COVERAGE
(A)Common term for a broad form or extensive amount of insurance coverage under one insurance contract.
(B) For Auto Insurance, also known as "Other than Collision", providing coverage for theft, vandalism, fire, collision with a missile or falling object, or animal. See Other than Collision, and Collision.

COMPULSORY INSURANCE
Insurance required by law, such as automobile liability or workers' compensation.

CONCEALMENT
Deliberately withholding material facts that would affect the validity of an insurance policy or a claim under the policy.

CONCURRENT INSURANCE
Two or more insurance policies covering the same property at the same location under the same terms and conditions, with the same types of coverage. However, the policies may be of different amounts. See Other Insurance Provision.

CONDITIONS
Part of an insurance policy detailing the rights and duties of the insured and the insurance company in the policy. See Declarations, Insuring Agreement, and Exclusions

CONDOMINIUM POLICY
A type of Homeowners insurance designed for owners of townhomes, condominiums, or cooperatives who share ownership of certain items of property with an association consisting of all property owners in the development.

CONSEQUENTIAL LOSS
Indirect loss by an insured peril, after and as a result of other loss. For example, the loss of use of an automobile that has been damaged in an accident and requiring the insured to seek other transportation.

CONSIDERATION
Inducement for completion of a contract; the premium paid by the insured and the promise to pay by the insurer. See Contract.

CONTRIBUTORY NEGLIGENCE
A legal doctrine that prevents an injured party from recovering damages from another party to an accident if the party was in any manner responsible for his or her own injury or damages.

CONTRACT
Another name for an insurance policy. Chief requirements for formation of valid contract are: (1) parties having legal capacity to contract; (2) offer and an acceptance of the offer; (3) valuable consideration (premium and promise to pay); (4) the absence of any statute or other rule making the contract void (legal reason); and (5) the absence of fraud or misrepresentation by either party. An insurance contract meeting these requirements qualifies as a contract.

CONTRACT OF ADHESION
Contract prepared by one party, without negotiation with the other party, and either accepted or rejected by the other party. An insurance policy is an example, as the insured has little control over the terms. Also a unilateral contract.

CONTRACT OF INSURANCE
Legal and binding unilateral contract whereby an insurance company agrees to indemnify an insured for losses, provide other benefits, or render services to or on behalf of an insured. This is often called an insurance policy, but the policy is merely the evidence of the agreement.

COUNTERSIGNATURE
Signature of a licensed insurance agent or representative of an insurance company necessary to validate the contract.

COVERAGE
Guarantee against specific losses provided under the terms of an insurance policy; amount and extent of insurance afforded under a contract of insurance. Often used to mean insurance or insurance contract. Used synonymously with the words insurance or protection.

CUSTOMER SERVICE REPRESENTATIVE (CSR)
The person in an insurance company or agency who is responsible for handling the daily service needs and transactions of a policyholder.

D

DAMAGES
Amount claimed by or awarded to an injured party as compensation for liability because of bodily injury or property damage. Damages may be based on actual expenses (special damages), pain and suffering (general damages), or an attempt to punish a person who causes injury or damage (punitive damages).

DEBRIS REMOVAL COVERAGE
Protection for reasonable expenses incurred by the insured for removal of debris after a loss caused by a covered peril.

DECLARATIONS
Part of an insurance policy containing representations of the applicant and other information pertinent to the risk, and on the basis of which the policy is issued. See Conditions, Insuring Agreement, and Exclusions.

DEDUCTIBLE
Provision in a policy whereby the insured is required to pay a specific amount or percentage of a loss, the insurance company paying on an excess basis over the deductible amount.

DEFINITIONS
The glossary of terms contained within an insurance policy.

DEPRECIATION
Decrease in value of property due to use, age, obsolescence, wear and tear, deterioration, etc.

DIARY SYSTEM. See Suspense System.

DIRECT LOSS
Loss resulting immediately and directly from a hazard insured against.

DIRECT RESPONSE COMPANY (DIRECT WRITER)
Insurance company dealing directly with insureds and selling its policies directly to insureds through insurance agents who are salaried employees or commissioned agents for that company exclusively. Also called a captive agent. See Independent Agent.

DISCRIMINATION
The failure of an insurer to charge the same rates to groups or individuals of the same risk, usually due to age, sex, national origin, race, location or legal occupation (including military service).

DOMESTIC COMPANY
An insurance company writing business in the state or province of its incorporation or charter.

DWELLING
The structure occupied by a property owner as his or her principal residence. Coverage A of the Homeowners policy.

DWELLING PROPERTY (DP) FORMS
A series of forms providing basic, broad, or special form coverage for dwelling buildings and contents or coverage for household contents only. Usually written for either hard to place homeowners or for owned property rented to others.

E

EARNED PREMIUM
The premium paid for the expired portion of the policy term. See Unearned Premium.

EARTH MOVEMENT
Earthquake, landslide, mudslide, sinking, shifting or rising of land.

EFFECTIVE DATE
Date on which a policy is put in force and protection is furnished. Also called the inception date.

EGO DRIVE
A trait or characteristic generally considered necessary for in insurance producer.

ELECTRONIC FILE (E-FILE)
A customer's information that is contained in an automated system such as an agency management system.

EMBEZZLE
To appropriate fraudulently, to one's own use, money or other property entrusted to one's care or control.

EMPATHY
A trait or characteristic generally considered necessary for in insurance producer.

ENDORSEMENT
Written amendment attached to a policy with the insurance company's approval making a change to the policy's terms.

ERRORS AND OMISSIONS INSURANCE
Professional liability insurance primarily for nonmedical professionals such as insurance agents to pay for losses or for defense of suits instituted against them for malpractice.

ETHICS
A code of professional conduct that is agreed to by members of a group.

ETIQUETTE
A manner of conducting one's self that is appropriate for a certain situation. Also called manners.

EXCESS INSURANCE
Coverage against loss in excess of a stated amount or in excess of coverage provided under another insurance contract.

EXCLUSION
Provision in an insurance policy eliminating coverage for certain risks or otherwise limiting the scope of coverage; certain causes and conditions listed in the policy that are not covered. See Conditions, Declarations, and Insuring Agreement.

EXCLUSIVE AGENT
An agent who represents only one insurance company under contract. See Independent Agent.

EXPENSE RATIO
The cost of soliciting, underwriting and servicing a policy of insurance in term of a percentage of the premium.

EXPERIENCE RATING
A modification of the insurance rate based on the loss experience of an individual insured.

EXPIRATION DATE
Date on which coverage under a policy terminates, usually at 12:01 a.m. that date.

EXPOSURE
Open to risk or the possibility of loss to a risk.

EXPRESSED AUTHORITY
The authority given to an agent or agency directly by means of the agency agreement or contract.

EXTENDED COVERAGE
Additional, broader protection against loss or damage to property, offered in conjunction with fire insurance, and usually covering against the perils of windstorm, hail, smoke, explosion, riot, civil commotion, vehicles, and aircraft.

F

FAMILY MEMBER
A person related to the insured by blood, marriage, or adoption, and who is a resident of the named insured's household, including a ward or foster child.

FIDUCIARY
One who occupies a position of special trust and confidence, as in handling or supervising affairs or funds of another. Examples are trustees, executors, administrators, corporate directors, insurance agents, etc.

FIDUCIARY RESPONSIBILITY
The trust responsibility (usually financial) of the insurance professional to both the insurer and the insured.

FINANCIAL RESPONSIBILITY LAW
A state law that requires operators of motor vehicles to pay for injuries or damages they cause up to a specified limit.

FIRE
A spark, glow, or flame, which is "hostile" in nature, caused by combustion or arson. See Hostile Fire

FIRE INSURANCE
Coverage for losses to insured property resulting from fire or lightning, as well as the resultant damage caused by smoke and water.

FIRE MARKS
Symbols placed near doorways of buildings to indicate that a particular company insured the structure.

FLOATER POLICY
An insurance policy under which the coverage follows the movement of the insured property.

FOREIGN COMPANY
An insurance company operating in any state other than the one in which it is incorporated or chartered.

FORTUITOUS EVENT
An unintended accident; not deliberate.

FRANKLIN, BENJAMIN
Considered the father of modern insurance, Franklin formed one of the first American mutual insurance companies providing fire insurance.

FRAUD
An intentional false representation or concealment of a material fact that may be acted upon by another party. The purpose of the act is to take something of value or to force the surrender of a right.

FREQUENCY

The number of times a loss occurs in a given period of time.

G

GENERAL LIABILITY INSURANCE
Protection for commercial risks against legal liability arising from ownership, maintenance, or use of business premises, defects in manufactured products and operations. See Commercial General Liability.

GOALS
The specific tasks that a person hopes to accomplish in a given period of time.

GOOD STUDENT DISCOUNT
A premium reduction offered to young drivers who maintain a certain grade point average, often a 3.0 and better.

GRADUATED LICENSING
A system used by states to defer certain driving privileges until a new driver has attained a particular age and amount of driving experience.

H

HAZARD
A specific situation or condition that creates or increases the probability of a loss, such as a poor driving record increasing the likelihood of an automobile accident. See Increase in Hazard.

HOLD HARMLESS AGREEMENT
Contractual agreement, usually written, whereby one party assumes legal liability on behalf of the other party.

HOMEOWNERS POLICIES (HO)
A series of policies for homeowners (tenants and owner-occupants) combining insurance for dwellings and/or household contents with personal liability insurance.

HOSTILE FIRE
Fire producing a visible spark, flame, or glow and leaving the area in which it was intended to be kept; also must be the immediate or proximate cause of the loss to be covered by fire insurance (the cause of the loss can be traced directly to the fire, with no new and independent source intervening and causing the loss).

I

IMPLIED AUTHORITY
The authority the general public reasonably believes an agent has.

INCREASE IN HAZARD
Increase in risk by the insured beyond the intent of the insurance company when the original policy was issued.

INDEMNIFY
To restore the one who suffers a loss, in whole or in part, by payment, repair, or replacement, to the same condition they were in prior to the loss.

INDEMNITY
Payment of an amount to offset all or part of an insured loss.

INDEPENDENT ADJUSTER
See Adjuster.

INDEPENDENT CONTRACTOR
Someone performing work for another under contract and who is not an employee of the party for whom the work is performed.

INDEPENDENT INSURANCE AGENT
An agent who represents more than one insurance company under contract.

INDIRECT LOSS
Contingent loss; loss resulting from a peril, but not directly and immediately caused by it. See Consequential Loss.

INFLATION GUARD ENDORSEMENTS
Endorsements to property insurance policies that for additional premium increase the amount of coverage by a specified percentage at specified times.

INHERENT VICE
Characteristic in property itself causing it to depreciate, spoil, break, become defective, disintegrate, or destroy itself, such as the tendency of metal to rust.

INLAND MARINE INSURANCE
Coverage is provided for jewels, furs, collectibles, and other items that may not remain at a single location.

INSURABLE INTEREST
Interest from which monetary loss will result if the peril insured against occurs; possibility of financial loss that can be protected against through insurance.

INSURABLE RISK
A risk that can be defined in terms of: (1) definite loss, (2) accidental in nature, (3) part of a large homogeneous group, (4) not subject to a catastrophic loss, (5) calculable loss, and (6) the premium must be reasonable for the risk.

INSURANCE
A contractual means of transferring the payment of a loss to a third party by means of a contract and the pooling of similar risks.

INSURANCE SERVICES OFFICE (ISO)
A private, nonprofit organization that develops and provides standardized forms, rates, and inspections for its members.

INSURED
One for whom insurance is written. See Named Insured

INSURED LOCATION
A term in a homeowners insurance policy to specify which locations occupied or used by an insured are included for liability coverage.

INSURER
Company granting the insurance. The insurance company.

INSURING AGREEMENT
Clause in a policy defining and describing the scope of the coverage provided and limits of indemnification. See Conditions, Declarations, and Exclusions.

J

JOB
The occupation a person undertakes in order to earn income.

K

L

LAPSE
Policy terminated because of nonpayment of premiums.

LAW OF LARGE NUMBERS
A statistical principle that indicates that the larger the number of examples, the more accurate and predictable the statistic will be. This is one of the main principles involved in determining actuarial tables for insurance purposes.

LEGAL PURPOSE
The concept that the purpose of a contract must be legal, moral and in the public good. See Contract.

LESSEE
One to whom a lease is granted; a tenant.

LESSOR
One who grants a lease; a landlord.

LIABILITY
Condition of being bound by law or contract to do something that may be enforced in the courts; obligation, usually financial; probable cost of meeting an obligation.

LIBERALIZATION CLAUSE
Clause in a policy providing that if, during the policy period, the insurance company adopts a change in the contract or there is a change in law that extends or broadens coverage, the insured will receive the benefit of this change in the same manner as if the endorsement had been made without increasing the premium until renewal.

LIFE AND HEALTH INSURANCE
Insurance issued to individuals or groups to protect against accident, illness, injury, sickness, disease, death, or disability.

LIMIT OF LIABILITY
Maximum amount an insurance company is willing to insure under a given form of insurance on any particular risk. The maximum amount payable for a given loss or occurrence or aggregate limit.

LLOYD'S OF LONDON
Association of syndicates with similar interests who insures specialized risks. Each syndicate is made up of individual or corporate investors who become financially responsible for any incurred loss. Each person or firm is responsible for only the share of the risk that he or she assumes.

LOSS
Basis of a claim for indemnity under provisions of an insurance policy. A loss is measured in terms of the reduced value of the property, the amount of medical and other related expenses, or the amount of the claim made against an insured.

LOSS SETTLEMENT PROVISION
A provision in a property insurance policy that determines the method to be used to value covered property, such as actual cash value, replacement cost, or agreed value.

M

MARKET SEGMENTATION
A process by which a seller categorizes the people or firms it wishes to approach in an attempt to sell products or services.

MARKET VALUE
The amount a willing seller will accept for his or her property from a willing buyer. See Actual Cash Value.

MARKETING SYSTEM
The method a firm uses to distribute its products or services.

MATERIAL FACT
Vital information required for making an insurance underwriting decision; statement of something done or existing of such importance that disclosure of it would alter an underwriting decision or loss settlement.

MISREPRESENTATION
False statement of material fact known at the time.

MISSION STATEMENT
A written statement by a firm that describes why it exists.

MOBILE HOME INSURANCE
Protection for the owner-occupant of a residential mobile home.

MORAL HAZARD
Effect of personal reputation, character, associates, living habits, financial responsibility, criminal history and environment on the risk to be insured.

MORALE HAZARD
The general indifference to loss.

MORTGAGE CLAUSE
Provision in or attached to fire policies covering mortgaged property, defining the mortgagee's rights and privileges under the policy.

MORTGAGEE
One who holds a mortgage (loan) on property.

MULTI-LINES
An insurance company, insurance agency, or insurance agent in the business of selling and servicing more than one type of insurance, usually property and casualty insurance and life insurance.

MULTI-PERIL POLICY
A policy that provides coverage for more than one type of loss. See Package Policy

MUTUAL COMPANY
Insurance company owned by its policyholders and managed by a board of directors chosen by the policyholders.

N

NAMED INSURED
One specifically designated by name as the insured on the declarations page of a policy.

NAMED PERIL POLICY
A policy specifying the perils insured against as opposed to an "all risk" or open perils policy.

NATIONAL ASSOCIATION OF INSURANCE COMMISSIONERS (NAIC)
Association of state insurance commissioners active in analysis of insurance regulations and in formation and recommendation of uniform and model legislation and regulations.

NATIONAL FLOOD INSURANCE PROGRAM
Federal program established through the Housing and Urban Development Act of 1968 (HUD) to make flood insurance available to individuals and businesses in flood-prone communities adopting certain land use and flood loss control measures.

NEGLECT
Failure to use all reasonable means to save and preserve property at and after a loss or when property is endangered.

NEGLIGENCE
Not acting as a reasonable and prudent person, under the same circumstances with the same knowledge, to prevent an accident or injury.

NEWLY ACQUIRED AUTO
An additional or replacement vehicle obtained by an insured after the effective date of a policy.

NICHE MARKETING
A determination by a company to serve only a limited portion of an entire group of potential customers.

NO-FAULT AUTOMOBILE INSURANCE
Insurance designed to replace or limit tort liability from automobile accidents. Generally part of a state's financial responsibility laws, to require liability and limited medical, rehabilitation and wage loss reimbursement for any person injured in an automobile accident.

NONADMITTED COMPANY
Insurance company not licensed to write business in a particular state. Also known as a Surplus, Excess, or Excess and Surplus (E&S) Company.

NONCONCURRENCY
The situation that exists when a number of insurance policies, intended to cover the same property against the same hazard or hazards, are not identical as to the extent of coverage or the interest insured.

NONINSURABLE RISK
Risk that cannot be measured actuarially or in which the chance of loss is so high that insurance cannot be written against it.

NONRESIDENT AGENT
Insurance agent licensed in a state in which he or she does not reside.

NONRENEWAL
The determination not to continue coverage on the expiration date of the contract by the insurer or insured. See Cancellation.

O

OCCURRENCE
A happening taking some length of time; series of accidents, including exposure to injurious conditions, that can be connected through common cause. See Accident.

OCCURRENCE COVERAGE
A policy providing liability coverage only for injury or loss that occurs during the policy period regardless of when the claim is actually made.

OFFER AND ACCEPTANCE
A requirement of a contract, the offer is an offer to purchase, generally the completion of the application for insurance. The acceptance is the accepting of that offer, usually by the insurance company. See Contract.

OPEN PERILS
A form of insurance in which all causes of loss are presumed covered, unless the cause is specifically excluded. See also NAMED PERILS.

ORDINANCE OR LAW COVERAGE
Usually attached to a personal or commercial property policy, providing protection for the cost of demolition or increased costs of construction required by a government authority following a covered loss.

OTHER INSURANCE CLAUSE
Provision in a policy stating what is to be done when another contract of insurance provides the same coverage or covers essentially the same property.

P

PACKAGE POLICIES
Insurance policies offering several coverages included in one contract, typically property and liability.

PAIR OR SET CONDITION
A provision that indicates that the loss of one item of a pair or set does not represent the loss of the entire set. The method of valuing the claim may vary between contract, but it is usually based on the reduced value of the set, when a single piece of that set was damaged or lost.

PARTIAL LOSS
Loss not completely destroying insured property or exhausting the insurance limits applying to that property.

PERIL
Event insured against; cause of a possible loss. See Hazard.

PERSONAL CONTRACT
A characteristic of an insurance contract indicating the insurance usually follows the individual, not the property. This provision is not always true under “no-fault” or Personal Injury Protection for a personal auto, where the insurance may follow the insured vehicle.

PERSONAL AUTO POLICY
Automobile policy in simplified style providing protection for liability, physical damage, medical payments and the automobile for both owned and nonowned vehicles.

PERSONAL INJURY
Coverages for libel, slander, invasion of privacy and other types of intentional torts. Usually included in personal liability and commercial liability policies.

PERSONAL INJURY PROTECTION
See “No-Fault”

PERSONAL LIABILITY INSURANCE
Protection against legal liability arising in connection with personal, nonbusiness activities both on and off insured premises. Coverage is extended to the named insured, relatives of the named insured who reside in the named insured’s home, and injuries caused by pets (e.g., a dog bite).

PERSONAL INSURANCE (PERSONAL LINES INSURANCE)
Insurance coverages designed for risks of an individual, personal, or nonbusiness nature.

PERSONAL PROPERTY
The contents of a home or apartment, including clothing, food, appliances, furniture, etc. See Real Property.

PHYSICAL HAZARD
A hazard arising out of the use, condition or occupancy of the insured property.

PLAINTIFF
Party to a lawsuit who brings charges against another party, the defendant.

POLICIES
The contracts issued by an insurance company to an insured. The practices and methods of doing business of a firm or organization.

POLICY
The insurance contract and all attached endorsements.

POLICYHOLDER
The insured under an insurance contract.

POLICY PERIOD
Length of time during which the policy contract affords protection; also called the policy term. Policies are usually written for an annual policy period, though premiums may be payable on a monthly basis or semi-annual basis.

POOL
Group of insurance companies joining together to share certain risks on an agreed-upon basis.

PREMIUM
Designated amount payable by the insured to the insurance company and required to keep the contract in force. See Consideration.

PREVENTION (LOSS PREVENTION)
A loss control measure designed to reduce the number of losses.

PRIMARY RATING FACTOR
An important factor, such as driving record, that is used to determine the price of insurance.

PRINCIPAL
The one (usually the insurer) from whom an insurance agent derives authority.

PRIORITIZATION
Arranging a series of tasks in an order from most to least important.

PRIVATE PASSENGER AUTO
An auto designed and used for noncommercial purposes.

PROCEDURES
The methods used to perform certain tasks in an insurance agency.

PROPERTY DAMAGE
Liability coverage providing protection in the event of loss of property, including loss of use, owned by someone other than the insured.

PRO RATA CANCELLATION
Termination of a policy with a return of premium charged for the exact time the protection was in force equal to the ratio of the total premium to the total policy period. See Short Rate Cancellation.

PRO RATA LIABILITY CLAUSE
Property insurance clause that makes each company insuring the same interest in a property liable according to the proportion that its insurance bears to the total amount of insurance on the property.

PRODUCER
A general term for an insurance sales representative, including agents and brokers.

PROOF OF LOSS
Formal document containing the signed and sworn statement of the insured in regard to a loss for which claim has been filed.

PROPERTY INSURANCE
Protection against loss to physical property, including both direct and indirect losses. Also called fire insurance.

PROPERTY AND CASUALTY INSURANCE
Provides protection to individuals, businesses, and other organizations for loss of assets.

PROTECTION CLASS
A rating system used to evaluate the quality of fire protection in a given area, from 1 (best) to 10 (worst). Used by insurance companies to determine fire insurance rates.

PROVISIONS
The written terms or conditions of a policy.

PROXIMATE CAUSE
Immediate causes that in a natural and continuous sequence, unbroken by any intervening cause brings about the loss and without which the loss would not have happened.

PURE RISK
Uncertainty as to whether loss will occur; offers no chance for gain. Insurance may be provided against many types of pure risk. See Speculative Risk.

R

RATE
Cost of a given unit of insurance.

REAL PROPERTY
Land and generally whatever is permanently erected or growing upon or affixed to the land; that not of a personal and movable nature. See Personal Property.

RECIPROCAL EXCHANGE
Association of individuals known as subscribers, managed by an attorney-in-fact, who agree to exchange insurance risks.

REDUCTION (LOSS REDUCTION)
A loss control measure that is designed to limit the amount of a loss.

REGIONAL COMPANY
An insurer that does business on a limited geographical basis.

REINSURANCE
Sharing or spreading of a risk too large for one insurer by passing part of the risk to a reinsurer. The insurance company obtaining the reinsurance is called the "ceding" company; the insurance company issuing the reinsurance is called the "reinsurer."

RELEASE
Discharge from further liability under an insurance policy.

REMOVAL COVERAGE
Coverage afforded under a fire insurance policy for damage resulting when property is removed for its own protection from premises endangered by an insured peril, as required in the policy.

RENEWAL
Continuing coverage under an insurance policy beyond its original term.

REPLACEMENT COST
The actual cost of replacing property without a deduction for depreciation. Current value. See Actual Cash Value.

REPRESENTATION
Statement of material fact that is reasonably accepted as substantially true. See Warranty.

RESIDENCE EMPLOYEE
A person who is employed by a homeowner to perform services that the homeowner would ordinarily perform, such as housekeeping, gardening, caretaking, etc.

RESIDENCE PREMISES
The land upon which a person's home is located.

RESPONDEAT SUPERIOR
General rule in law that a principal or employer is liable for an agent's or representative's acts performed on behalf of the principal's business.

RETURN PREMIUM
Amount of unused premium due the insured after a policy is canceled, reduced in amount, or its rate is reduced. See Pro Rata Cancellation and Short Rate Cancellation.

RISK
Condition in which there is a possibility of loss. Also a term indicating the person or property insured.

RISK MANAGEMENT
Attempt to identify, measure, control, transfer or retain pure risk exposures in order to protect future income and reduce long-range costs against accidental or unintended loss.

S

SALVAGE
Damaged property recovered and sold by an insurance company to reduce its loss.

SCHEDULED POLICY
Insurance contract that includes a specific listing of the items insured in the policy.

SECONDARY RATING FACTOR
A factor that is taken into account when determining the price of an insurance policy, but is not of primary importance.

SELF-INSURANCE
Providing a fund to pay losses that are intentionally not insured.

SEVERITY
The measure of the size of a loss.

SHORT RATE CANCELLATION
Termination of a policy by the insured before the end of the policy period, with the earned premium plus administrative expenses retained by the insurance company.

SNOWMOBILE COVERAGE
An endorsement to an auto or homeowners policy that provides coverage for physical damage and liability arising out of the use of owned and nonowned snowmobiles.

SPECULATIVE RISK
A situation that when it occurs may produce loss, gain, or no change in a person's condition.

SPLIT LIMITS
Separating Bodily Injury and Property Damage as specific limits of liability ($50,000 BI and $15,000 PD). See Combined Single Limit

SPREADING OF RISK
Underwriting principles requiring the insurance company to spread its risk to as many geographic locations as possible.

STAFF ADJUSTER
See Adjuster.

STOCK COMPANY
An insurance company owned by its stockholders. Also known as a Capital Company or a Capital-Stock company.

STRATEGIES
The tactics a firm uses to accomplish its business purpose.

STRUCTURES
Real property items situated on a piece of land, such as swimming pools, pump houses, decks, gazebos, and other items that are constructed and attached to the land.

SUBROGATION
Assigning or substituting rights of one party to another in collecting a debt or claim, as an insurance company is assigned an insured's rights of recovery from a third party who has caused a loss.

T

TARGET MARKETING
The process used by a firm to identify a specific group of potential customers to whom the firm will sell its products or services.

TEMPORARY SUBSTITUTE AUTO
An automobile being used by an insured while the vehicle covered by the policy is out of service due to repair, breakdown, or theft.

TERM
Period of time for which a policy or bond is written.

THEFT
Any illegal act of taking or stealing, or attempting to take or steal, of someone else's property, including such crimes as larceny, burglary, and robbery.

TORT
Civil wrong other than a breach of contract for which legal action may be taken; for example, negligence or assault.

TORT SYSTEM
A system that assigns responsibility to persons and organizations that commit legal wrongs.

U

UMBRELLA LIABILITY INSURANCE
Coverage for legal liability for bodily injuries and property damage that exceeds basic liability policies such as automobile and homeowners coverage.

UNDERINSURED MOTORIST (UIM)
Auto coverage providing protection in the event an insured in involved in an accident and the other party is at fault, however is carrying insurance coverage lower than the amount of the damages and lower than the claimant's UIM.

UNDERLYING INSURANCE
Amount of primary insurance on a risk before the next higher excess layer of insurance attaches.

UNDERWRITER
A person employed by an insurance company to determine which risks to insure and which to reject.

UNDERWRITING
Process of researching, evaluating and determining the insurability of a risk.

UNDERWRITING GUIDELINES
The documents developed by an insurance company to provide underwriters with an idea of the type of customers the company wishes to insure.

UNEARNED PREMIUM
Portion of an insurance premium covering the unexpired term of the policy.

UNILATERAL CONTRACT
Distinguishing characteristic of an insurance agreement in that only the insured must perform (pay the premium) while the company makes only an enforceable pledge.

UNINSURED MOTORIST (UM)
Coverage provided by auto insurance providing protection incase the insured is involved in an accident where the other party is at fault, but not insured. See Underinsured Motorist

UTMOST GOOD FAITH
The principle of a contract when part of the consideration is a promise to pay. All insurance contracts are contracts of utmost good faith.

V

VALUATION CLAUSE
Provision in a policy defining the bases for establishing the value of insured property.

VALUED POLICY
Policy in which the value of the property insured and amount to be paid in case of total loss are determined at policy inception.

VICARIOUS LIABILITY
Liability that is transferred from one person, such as a minor child, to another person (parent, guardian, etc.). The liability is said to be "imputed" from one to another.

VISION STATEMENT
See Mission Statement.

W

WARRANTY
Literal promise and guarantee, either expressed or implied (i.e., concerning the condition of property to be insured), made for the purpose of risk evaluation by the insurance company; if found to be untrue, may provide the basis for voidance of the policy.

Y

YACHT COVERAGE
Watercraft insurance for large vessels.

Appendix

ACORD VIRGINIA PERSONAL AUTO APPLICATION

PRODUCER	APPLICANT'S NAME AND MAILING ADDRESS (Include county & ZIP+4)	NAIC CODE
		TELEPHONE NUMBER
	REGISTERED OWNER IF DIFFERENT FROM ABOVE:	
CODE: SUBCODE:	CO/PLAN	POL#:
		ACCT#:
AGENCY CUSTOMER ID	EFFECTIVE DATE / EXPIRATION DATE / DIRECT BILL / AGENCY BILL / MAIL POLICY TO AGENT / MAIL POLICY TO APPL	PAYMENT PLAN

DATE (MM/DD/YY)

RESIDENCE CURRENT RESIDENCE IS OWNED RENTED — **GARAGE LOCATION IF DIFF FROM ABOVE (Inc county & ZIP)**

YRS AT CURR	ADDR REPT	PREVIOUS ADDRESS (If less than 3 years)	VEH #	

VEHICLE DESCRIPTION/USE TOTAL NUMBER OF VEHICLES IN HOUSEHOLD:

VEH	YEAR	MAKE, MODEL AND BODY TYPE	VIN/REGISTERED STATE	HP/CC	DATE LEASED	DATE PURCH	NEW/USED

VEH	COST NEW	SYMBOL AGE GRP	TERR	MILES 1 WAY W/SCHOOL	DAYS/WEEK	DAYS/MONTH	WAGE	PERFORM	MULTI-CAR	CAR POOL	CAR USED	ODOMETER READING	ANNUAL MILEAGE	COUNTRY DRIVER	DRIVER USE % (Each veh must equal 100%)						CLASS

VEH	PASSIVE SEAT BELT	AIRBAG DRIVER/BOTH	ANTI-LOCK BRAKES	ANTI-THEFT DEVICES	CREDITS AND SURCHARGES	VEH	PASSIVE SEAT BELT	AIRBAG DRIVER/BOTH	ANTI-LOCK BRAKES	ANTI-THEFT DEVICES	CREDITS AND SURCHARGES

COVERAGES/PREMIUMS

COVERAGES	LIMITS OF LIABILITY	VEHICLE #	VEHICLE #	VEHICLE #	VEHICLE #
SINGLE LIMIT LIABILITY (CSL)	$ EA ACCIDENT	$	$	$	$
BODILY INJURY LIABILITY	$ EA PERSON $ EA ACCIDENT	$	$	$	$
PROPERTY DAMAGE LIABILITY	$ EA ACCIDENT $ DEDUCTIBLE	$	$	$	$
PERSONAL INJURY PROTECTION	$ EXT MED EXP	$	$	$	$
	$ INCOME LOSS	$	$	$	$
MEDICAL PAYMENTS	$ EA PERSON	$	$	$	$
UNINSURED MOTORISTS CSL/BI	$ EA PERSON $ EA ACCIDENT	$	$	$	$
PD	$ EA ACCIDENT	$	$	$	$
COMPREHENSIVE DED	$ $ $ $	$	$	$	$
COLLISION DED	$ $ $ $	$	$	$	$
ACV UNLESS AMOUNT STATED	$ $ $ $	$	$	$	$
TOWING & LABOR	$ $ $ $	$	$	$	$
TRANS EXP/RENTAL RE	$ / $ / $ / $ /	$	$	$	$
ADDITIONAL COVERAGES/ENDORSEMENTS (Include limit, deductible, premium)	POLICY FEE: $ TOTAL PER VEHICLE	$	$	$	$
		ESTIMATED TOTAL $	DEPOSIT $		BALANCE DUE $

RESIDENT & DRIVER INFORMATION [List all residents & dependents (licensed or not) and regular operators]

#	NAME (AS IT APPEARS ON LICENSE)	SEX	MAR STAT	REL TO APPLIC	DATE OF BIRTH	OCC	DATE LIC	STDT >100	GOOD STDT	DRV TRAIN	ACC PREV CRS DATE	DRIVERS LICENSE #/LIC STATE	SOCIAL SECURITY #

ACCIDENTS/CONVICTIONS (Note: Your driving record is verified with the state motor vehicle department and other insurers)

HAS ANY DRIVER SHOWN ABOVE HAD AN ACCIDENT, REGARDLESS OF FAULT, OR BEEN CONVICTED OF A MOVING VIOLATION WITHIN THE LAST ____ YEARS? YES NO — IF YES, INDICATE BELOW. ALSO INCLUDE COMPREHENSIVE INSURANCE LOSSES.

DRV #	DATE OF ACCIDENT/CONVICTION	DESCRIPTION OF ACCIDENT OR CONVICTION	PLACE OF ACCIDENT/CONVICTION	INJ/DEATH YES	INJ/DEATH NO	AMOUNT OF PROPERTY DAMAGE

READ YOUR POLICY. THE POLICY OF INSURANCE FOR WHICH THIS APPLICATION IS BEING MADE, IF ISSUED, MAY BE CANCELED WITHOUT CAUSE AT THE OPTION OF THE INSURER AT ANY TIME IN THE FIRST 60 DAYS DURING WHICH IT IS IN EFFECT AND AT ANY TIME THEREAFTER FOR REASONS STATED IN THE POLICY.

ACORD 90 VA (2/96) PLEASE COMPLETE REVERSE SIDE

ADDITIONAL INTEREST

VEH #		ADDL INT / LOSS PAY	NAME AND ADDRESS	LOAN NUMBER
VEH #		ADDL INT / LOSS PAY	NAME AND ADDRESS	LOAN NUMBER

EMPLOYMENT INFORMATION (* If less than 2 years, provide name of previous employer and previous occupation under Remarks)

APPLICANT'S EMPLOYER (State nature of business if self-employed)	ADDRESS OF EMPLOYMENT	WORK PHONE NUMBER	YEARS W/ CURR EMPL	YEARS W/ PREV EMPL
CO-APPLICANT'S EMPLOYER (State nature of business if self-employed)	ADDRESS OF EMPLOYMENT	WORK PHONE NUMBER	YEARS W/ CURR EMPL	YEARS W/ PREV EMPL

PRIOR COVERAGE

PRIOR CARRIER AND PRODUCER	# OF YEARS W/COMPANY	PRIOR POLICY NUMBER/EXPIRATION DATE

GENERAL INFORMATION

EXPLAIN ALL "YES" RESPONSES IN REMARKS	YES	NO	EXPLAIN ALL "YES" RESPONSES IN REMARKS	YES	NO
1. WITH THE EXCEPTION OF ANY ENCUMBRANCES, ARE ANY VEHICLES NOT SOLELY OWNED BY AND REGISTERED TO THE APPLICANT?			9. ANY HOUSEHOLD MEMBER IN MILITARY SERVICE? (Driver number)		
			10. ANY DRIVERS LICENSE BEEN SUSPENDED/REVOKED?		
2. ANY CAR MODIFIED/SPECIAL EQUIPMENT? (Incl customized van/pickup; indicate cost)			11. ANY DRIVER HAVE PHYSICAL/MENTAL IMPAIRMENT? (List driver number)		
3. ANY EXISTING DAMAGE TO VEHICLE? (Include damaged glass)			12. ANY FINANCIAL RESPONSIBILITY FILING? (Driver number and date of filing)		
4. ANY OTHER LOSSES INCURRED (not shown in Accident/Conviction area)?			13. HAS INSURANCE BEEN TRANSFERRED WITHIN AGENCY?		
5. ANY CAR KEPT AT SCHOOL?			14. ANY COVERAGE DECLINED, CANCELLED, OR NON-RENEWED DURING THE LAST 3 YEARS?		
6. ANY CAR PARKED ON STREET?					
7. ANY OTHER AUTO INSURANCE IN HOUSEHOLD? (Include any provided by employer)			15. IS THIS BROKERED BUSINESS TO THE AGENT?		
8. ANY OTHER INSURANCE WITH THIS COMPANY? (List policy number)			16. HAS AGENT INSPECTED VEHICLE?		

REMARKS

FOR COMPANY USE ONLY

ATTACHMENTS

- [ ] YOUNG DRIVER QUESTIONNAIRE
- [ ] DRIVER TRAINING CERTIFICATE
- [ ] GOOD STUDENT CERTIFICATE
- [ ] ANTI-THEFT DEVICE CERTIFICATE
- [ ] MEDICAL STATEMENT
- [ ] MOTOR VEHICLE REPORT
- [ ] PHOTOGRAPH
- [ ] BILL OF SALE

BINDER/SIGNATURE

INSURANCE BINDER	
EFFECTIVE DATE	EXPIRATION DATE
TIME	12:01 AM / NOON
COVERAGE IS NOT BOUND	

IF THE "BINDER" BOX TO THE LEFT IS COMPLETED, THE FOLLOWING CONDITIONS APPLY:

THIS COMPANY BINDS THE KIND(S) OF INSURANCE STIPULATED ON THIS APPLICATION. THIS INSURANCE IS SUBJECT TO THE TERMS, CONDITIONS AND LIMITATIONS OF THE POLICY(IES) IN CURRENT USE BY THE COMPANY.

THIS BINDER MAY BE CANCELLED BY THE INSURED BY SURRENDER OF THIS BINDER OR BY WRITTEN NOTICE TO THE COMPANY STATING WHEN CANCELLATION WILL BE EFFECTIVE. THIS BINDER MAY BE CANCELLED BY THE COMPANY BY NOTICE TO THE INSURED IN ACCORDANCE WITH THE POLICY CONDITIONS. THIS BINDER IS CANCELLED WHEN REPLACED BY A POLICY. IF THIS BINDER IS NOT REPLACED BY A POLICY, THE COMPANY IS ENTITLED TO CHARGE A PREMIUM FOR THE BINDER ACCORDING TO THE RULES AND RATES IN USE BY THE COMPANY. THE QUOTED PREMIUM IS SUBJECT TO VERIFICATION AND ADJUSTMENT, WHEN NECESSARY, BY THE COMPANY.

NOTICE OF INSURANCE INFORMATION PRACTICES

PERSONAL INFORMATION ABOUT YOU, INCLUDING INFORMATION FROM A CREDIT REPORT, MAY BE COLLECTED FROM PERSONS OTHER THAN YOU. SUCH INFORMATION AS WELL AS OTHER PERSONAL AND PRIVILEGED INFORMATION COLLECTED BY US OR OUR AGENTS MAY IN CERTAIN CIRCUMSTANCES BE DISCLOSED TO THIRD PARTIES. YOU HAVE THE RIGHT TO REVIEW YOUR PERSONAL INFORMATION IN OUR FILES AND CAN REQUEST CORRECTION OF ANY INACCURACIES. A MORE DETAILED DESCRIPTION OF YOUR RIGHTS AND OUR PRACTICES REGARDING SUCH INFORMATION IS AVAILABLE UPON REQUEST. CONTACT YOUR AGENT OR BROKER FOR INSTRUCTION ON HOW TO SUBMIT A REQUEST TO US.

- [ ] COPY OF THE NOTICE OF INFORMATION PRACTICES (PRIVACY) HAS BEEN GIVEN TO THE APPLICANT.

APPLICANT'S STATEMENT: I HAVE READ THE ABOVE APPLICATION AND ANY ATTACHMENTS. I DECLARE THAT THE INFORMATION PROVIDED IN THEM IS TRUE, COMPLETE AND CORRECT TO THE BEST OF MY KNOWLEDGE AND BELIEF. THIS INFORMATION IS BEING OFFERED TO THE COMPANY AS AN INDUCEMENT TO ISSUE THE POLICY FOR WHICH I AM APPLYING. IN ADDITION, IF THE AUTO PLAN OR COMPANY DESIGNATED IN THIS APPLICATION IS NON-STANDARD, I CERTIFY THAT I UNDERSTAND THE RATES FOR THIS COVERAGE ARE HIGHER THAN NORMAL, AND THAT THEY ARE ACCEPTABLE TO ME AS I HAVE BEEN UNABLE TO OBTAIN COVERAGE DESIRED THROUGH THE NORMAL INSURANCE MARKET.

PRODUCER'S STATEMENT: I CERTIFY TO THE BEST OF MY KNOWLEDGE AND BELIEF THAT THE SIGNATURE OF THE APPLICANT IS THE PERSONAL SIGNATURE OF THE APPLICANT. | HOW LONG HAVE YOU KNOWN THE APPLICANT?

I ACKNOWLEDGE I HAVE BEEN OFFERED UNINSURED MOTORISTS COVERAGE UP TO THE LIMIT(S) OF MY BODILY INJURY LIABILITY COVERAGE. I HAVE SELECTED THE LIMITS INDICATED IN THIS APPLICATION.

INITIALS OF NAMED INSURED(S)

I UNDERSTAND THAT THE COVERAGE SELECTION AND LIMIT CHOICES INDICATED HERE WILL APPLY TO ALL FUTURE POLICY RENEWALS, CONTINUATIONS AND CHANGES UNLESS I NOTIFY YOU OTHERWISE IN WRITING.

APPLICANT'S SIGNATURE		DATE (MM/DD/YY)	PRODUCER'S SIGNATURE

ACORD 90 VA (2/96)

ACORD™ PERSONAL AUTO POLICY CHANGE REQUEST

PRODUCER	PHONE (A/C, No, Ext): FAX (A/C, No):	COMPANY	NAIC CODE:
		ATTENTION:	
CODE: AGENCY CUSTOMER ID	SUB CODE:	POL#:	
NAMED INSURED		ACCT#:	
INSURED'S NAME AND MAILING ADDRESS (Inc ZIP+4), IF CHANGED		EFFECTIVE DATE OF CHANGE / INCEPTION DATE OF POLICY / EXPIRATION DATE	
		CHANGE BILLING PLAN TO: ☐ DIRECT ☐ AGENCY	PERMISSIBLE `TYPE OF CHANGE` CODES: (A) ADD, (C) CHANGE, (D) DELETE

DATE (MM/DD/YYYY)

VEHICLE DESCRIPTION/USE

TYPE OF CHANGE	VEH	YEAR	MAKE, MODEL AND BODY TYPE	VIN/REGISTERED STATE	HP/CC	DATE LEASED	DATE PURCH	NEW/USED

COST NEW	SYMBOL AGE GRP	TERR	MILES 1 WAY W/SCHL	# DAYS WEEK	# WKS MONTH	USAGE	NON FOUR	MULTI-CAR	CAR POOL	CAR USED	ODOMETER READING	ANNUAL MILEAGE	GOVERN DRIVER	DRIVER USE % (Each veh must equal 100%)						CLASS

PASSIVE SEAT BELT	AIRBAG DRV/BOTH	ANTI-LOCK BRAKES	ANTI-THEFT DEVICES	CREDITS AND SURCHARGES

GARAGE LOCATION (If different than mailing address)

TYPE OF CHANGE	VEH #	

VEHICLE COVERAGES/PREMIUMS

COVERAGES	TYPE OF CHANGE	VEH #:	TYPE OF CHANGE	VEH #:
SINGLE LIMIT LIAB (CSL)		$ EA ACCIDENT		$ EA ACCIDENT
BODILY INJURY LIAB		$ EA PERSON $ EA ACCIDENT		$ EA PERSON $ EA ACCIDENT
PROPERTY DAMAGE LIAB		$ EA ACCIDENT $ DEDUCTIBLE		$ EA ACCIDENT $ DEDUCTIBLE
NO FAULT COVERAGES		$		$
		$		$
		$		$
MEDICAL PAYMENTS		$ EA PERSON		$ EA PERSON
UNINSURED MOTORIST CSL/BI		$ EA PERSON $ EA ACCIDENT		$ EA PERSON $ EA ACCIDENT
UNINSURED MOTORIST PD		$ EA ACCIDENT		$ EA ACCIDENT
UNDERINSURED MOTORIST CSL/BI		$ EA PERSON $ EA ACCIDENT		$ EA PERSON $ EA ACCIDENT
UNDERINSURED MOTORIST PD		$ EA ACCIDENT		$ EA ACCIDENT
COMPREHENSIVE DED		$		$
COLLISION DED		$		$
ACV UNLESS AMT STATED		$		$
TOWING & LABOR		$		$
TRANS EXP/RENTAL RE		$		$
		$		$

GENERAL INFORMATION (Explain all `yes` responses in remarks)

IF A VEHICLE IS BEING ADDED, ANSWER QUESTIONS 1-5	YES	NO	IF A DRIVER IS BEING ADDED, ANSWER QUESTIONS 6-10	YES	NO
1. WITH THE EXCEPTION OF ANY ENCUMBRANCES, ARE ANY VEHICLES NOT SOLELY OWNED BY AND REGISTERED TO THE APPLICANT? IF YES, (List vehicle number(s) and name(s) as it appears on registration.)			6. ANY HOUSEHOLD MEMBER IN MILITARY SERVICE? (Driver number)		
			7. ANY DRIVERS LICENSE BEEN SUSPENDED/REVOKED?		
2. ANY CARS MODIFIED/SPECIAL EQUIPMENT? (Include customized vans/pickups; indicate cost)			8. ANY DRIVERS HAVE PHYSICAL/MENTAL IMPAIRMENT? (List driver number)		
3. ANY EXISTING DAMAGE TO VEHICLES? (Include damaged glass)			9. ANY FINANCIAL RESPONSIBILITY FILINGS? (Driver number and date of filing)		
4. ANY CARS KEPT AT SCHOOL?			10. ANY COVERAGE DECLINED, CANCELLED OR NON-RENEWED DURING THE LAST 3 YEARS? NOT APPLICABLE IN MO		
5. ANY CARS PARKED ON STREET?					

REMARKS

INSURED'S SIGNATURE		DATE (MM/DD/YYYY)	PRODUCER'S SIGNATURE	

ACORD 71 (2002/01)

DRIVER INFORMATION

TYPE OF CHANGE	#	NAME (AS IT APPEARS ON LICENSE)	SEX	MAR STAT	REL TO APPLIC	DATE OF BIRTH	OCC	DATE LIC	STDT %	GOOD STDT	DRV TRAIN	ACC PREV CSE DATE	DRIVERS LICENSE #/LIC STATE	SOCIAL SECURITY #

ACCIDENTS/CONVICTIONS - IF DRIVER ADDED (Note: Your driving record is verified with the state motor vehicle department)

HAS ANY DRIVER SHOWN ABOVE HAD AN ACCIDENT, REGARDLESS OF FAULT, OR BEEN CONVICTED OF A MOVING VIOLATION WITHIN THE LAST ____ YEAR(S)? [ ] YES [ ] NO IF YES, INDICATE BELOW. ALSO INCLUDE COMPREHENSIVE INSURANCE LOSSES.

DRV #	DATE OF ACCIDENT/CONVICTION	DESCRIPTION OF ACCIDENT OR CONVICTION	PLACE OF ACCIDENT/CONVICTION	BI OR DEATH YES	BI OR DEATH NO	AMOUNT OF PROPERTY DAMAGE

ADDITIONAL INTEREST [ ] ADD [ ] CHANGE [ ] DELETE

VEH #	[ ] ADDL INT [ ] LOSS PAY	NAME AND ADDRESS	LOAN NUMBER

ADDITIONAL INTEREST [ ] ADD [ ] CHANGE [ ] DELETE

VEH #	[ ] ADDL INT [ ] LOSS PAY	NAME AND ADDRESS	LOAN NUMBER

Any person who knowingly and with intent to defraud any insurance company or another person files an application for insurance or statement of claim containing any materially false information, or conceals for the purpose of misleading information concerning any fact material thereto, commits a fraudulent insurance act, which is a crime and subjects the person to criminal and [NY: substantial] civil penalties. (Not applicable in CO, HI, NE, OH, OK, OR, or VT; in DC, LA, ME, TN and VA, insurance benefits may also be denied)

REMARKS

ACORD 71 (2002/01)

ACORD GOOD STUDENT/DRIVER TRAINING

PRODUCER	NAME AND MAILING ADDRESS (INCLUDE ZIP CODE)		DATE (MM/DD/YY)
CODE: SUB CODE:	CO/PLAN	EFFECTIVE DATE	EXPIRATION DATE
AGENCY CUSTOMER ID:	POLICY #:	NEW	RENEWAL

STUDENT INFORMATION

NAME OF STUDENT	FULL TIME / PART TIME	NAME AND ADDRESS OF SCHOOL
FRESHMAN / SOPHOMORE / JUNIOR / SENIOR		

GOOD STUDENT CERTIFICATE

TO BE COMPLETED BY SCHOOL OFFICIAL

The scholastic records for the immediately preceding semester (or comparable period) show that this student has attained one or more of the following:

- ☐ ranked among the upper 20% of their class scholastically; or
- ☐ in a school using letter grades, had a grade average of "B" (if the system of letter grading cannot be averaged, no grade shall be below "B"); or
- ☐ had a grade average of at least 3 points on a 4 point scale (or its equivalent); or
- ☐ was included in "Dean's List" or "Honor Roll" (or other comparable list for scholastic achievement).

DRIVER TRAINING CERTIFICATE

TO BE COMPLETED BY REPRESENTATIVE

This is to certify that the student has successfully completed:

_____ clock hours of classroom instruction; AND

_____ clock hours on the average per student for actual driving experience in the practice driving phase (exclusive of observation time in the car); AND/OR

_____ clock hours on the average per student in an approved device which simulates practice driving.

DATE (MM/DD/YY)	NAME AND TITLE OF SCHOOL OFFICIAL	AUTHORIZED SIGNATURE

ACORD 91 (3/93)a

ACORD™ INSURANCE BINDER

DATE

THIS BINDER IS A TEMPORARY INSURANCE CONTRACT, SUBJECT TO THE CONDITIONS SHOWN ON THE REVERSE SIDE OF THIS FORM.

PRODUCER

PHONE (A/C, No, Ext):

CODE: SUB CODE:

AGENCY CUSTOMER ID:

INSURED

COMPANY

BINDER #

EFFECTIVE DATE	EFFECTIVE TIME		EXPIRATION DATE	EXPIRATION TIME
		AM		12:01 AM
		PM		NOON

THIS BINDER IS ISSUED TO EXTEND COVERAGE IN THE ABOVE NAMED COMPANY PER EXPIRING POLICY #:

DESCRIPTION OF OPERATIONS/VEHICLES/PROPERTY (Including Location)

COVERAGES

LIMITS

TYPE OF INSURANCE	COVERAGE/FORMS	DEDUCTIBLE	COINS %	AMOUNT
PROPERTY CAUSES OF LOSS BASIC BROAD SPEC				

TYPE OF INSURANCE	COVERAGE/FORMS	LIMITS	AMOUNT
GENERAL LIABILITY		EACH OCCURRENCE	$
COMMERCIAL GENERAL LIABILITY		FIRE DAMAGE (Any one fire)	$
CLAIMS MADE / OCCUR		MED EXP (Any one person)	$
		PERSONAL & ADV INJURY	$
		GENERAL AGGREGATE	$
	RETRO DATE FOR CLAIMS MADE:	PRODUCTS - COMP/OP AGG	$
AUTOMOBILE LIABILITY		COMBINED SINGLE LIMIT	$
ANY AUTO		BODILY INJURY (Per person)	$
ALL OWNED AUTOS		BODILY INJURY (Per accident)	$
SCHEDULED AUTOS		PROPERTY DAMAGE	$
HIRED AUTOS		MEDICAL PAYMENTS	$
NON-OWNED AUTOS		PERSONAL INJURY PROT	$
		UNINSURED MOTORIST	$
			$
AUTO PHYSICAL DAMAGE DEDUCTIBLE	ALL VEHICLES / SCHEDULED VEHICLES	ACTUAL CASH VALUE	
COLLISION:		STATED AMOUNT	$
OTHER THAN COL:		OTHER	
GARAGE LIABILITY		AUTO ONLY - EA ACCIDENT	$
ANY AUTO		OTHER THAN AUTO ONLY:	
		EACH ACCIDENT	$
		AGGREGATE	$
EXCESS LIABILITY		EACH OCCURRENCE	$
UMBRELLA FORM		AGGREGATE	$
OTHER THAN UMBRELLA FORM	RETRO DATE FOR CLAIMS MADE:	SELF-INSURED RETENTION	$
WORKER'S COMPENSATION AND EMPLOYER'S LIABILITY		WC STATUTORY LIMITS	
		E.L. EACH ACCIDENT	$
		E.L. DISEASE - EA EMPLOYEE	$
		E.L. DISEASE - POLICY LIMIT	$
SPECIAL CONDITIONS/ OTHER COVERAGES		FEES	$
		TAXES	$
		ESTIMATED TOTAL PREMIUM	$

NAME & ADDRESS

MORTGAGEE ADDITIONAL INSURED

LOSS PAYEE

LOAN #

AUTHORIZED REPRESENTATIVE

ACORD 75-S (1/98) **NOTE: IMPORTANT STATE INFORMATION ON REVERSE SIDE**

ENFORCEMENT OF COMPULSORY AUTO LIABILITY INSURANCE LAWS
(As of July 2004)

State	Insurance Required (a)	Minimum Liability Limits (b)	Proof of Insurance Required (c)				Penalties for Non-Compliance (First Offense)
			At Registration	At Time of Accident	At All Times in Vehicle	Insurer Verification of Insurance (d)	
PA (f)	BI & PD Liab, Med	15/30/5	No	Yes	Yes	1	License and registration suspension, confiscation of plates
IA	BI & PD Liab	20/40/15	No	Yes	Yes	1	$100 fine
ND	BI & PD Liab, PIP, UM	25/50/25	No	No (e)	No	1	$150 fine, registration revocation, license suspension (f)
MT	BI & PD Liab	25/50/10	No	Yes	Yes	1	$250 fine or not more than 10 days in jail (f)
ME	BI & PD Liab, UM, UIM	50/100/25 (j)	No	Yes	Yes	1	$100-$500 fine, 30-day license and registration suspension
OH	BI & PD Liab	12.5/25/7.5	No	Yes	Yes	1	90-day license suspension, $75 reinstatement fee
OK	BI & PD Liab	25/50/25**	Yes	Yes	Yes	1	Less than $500 fine, less than 6 months jail (f)
MS	BI & PD Liab	10/20/5	No	Yes	Yes	1	$1,000 fine, license suspension
MI	BI & PD Liab, PIP	20/40/10	Yes	No	No	1	$200 fine (f)
MA	BI & PD Liab, PIP, UM	20/40/5	Yes	No	No	1	$500 fine (f)
TN	FR only	25/50/10 (o)	No	No	Yes (p)	1	$100 fine
SD	BI & PD Liab, UM	25/50/25	No	Yes	Yes	1	1-year license suspension (f)
WA	BI & PD Liab	25/50/10	No	No	No	1	$480 fine
WV	BI & PD Liab, UM	20/40/10	Yes	Yes	Yes	1	90-day license suspension, registration revocation (f)
WI	FR only, UM	25/50/10	No	No	No	1	License and or registration revocation (f)
WY	BI & PD Liab	25/50/20	Yes	Yes	Yes	1	Up to $750 fine; up to six months in jail
GA	BI & PD Liab	25/50/25	Yes	Yes	Yes	1	60-day license suspension, registration suspension
VT	BI & PD Liab, UM, UIM	25/50/10	No	Yes	Yes	1	Less than $100 fine (f)
TX	BI & PD Liab	20/40/15	Yes	Yes	No	1	$75 fine; license and registration suspension (f)
UT	BI & PD Liab, PIP	25/50/15 (q)	No	Yes	Yes	1	$400 fine; up to $1,000, license and/or registration loss (f)
AK	BI & PD Liab	50/100/25	No	No (e)	Yes	2	Registration suspension/revocation (f)
CA	BI & PD Liab	15/30/5 (h)	Yes	Yes	Yes	2	$100 fine; registration suspension
KS	BI & PD Liab, PIP, UM	25/50/10	Yes	No	No	2	$100 fine (f)
MN	BI & PD Liab, PIP, UM, UIM	30/60/10	No	Yes	Yes	3	License and/or registration revocation for 6 months (f)
NJ	BI & PD Liab, PIP, UM	15/30/5 (1)	No	Yes	Yes	4	$300 fine, community service, 1-year license suspension, vehicle impoundment
KY	BI & PD Liab, PIP	25/50/10	Yes	Yes	Yes	4*	Registration revocation, $50 fine, up to 90 days in jail (f)
IN	BI & PD Liab	25/50/10	Yes	Yes	No	1,2	90 day license suspension, $150 reinstatement fee
NM	BI & PD Liab	25/50/10	Yes	No	No	1,3	$100 fine (f)
RI	BI & PD Liab, UM	25/50/25 (n)	No	No	No	1,3	$500 fine, confiscation of plates
OR	BI & PD Liab, PIP, UM	25/50/10	No	Yes	Yes	1,3	License suspension and/or revocation (f)
MO	BI & PD Liab, UM	25/50/10	Yes	Yes	Yes	1,3	License and registration revocation (f)
MD	BI & PD Liab, PIP (k), UM	20/40/15	Yes	No	No	1,3	$150 fine (f)
ID	BI & PD Liab	25/50/15	No	Yes	Yes	1,3	$75 fine (f)
DC	BI & PD Liab, UM	25/50/10	Yes	No	No	1,3	$100 fine or maximum 30 days jail
DE	BI & PD Liab, PIP	15/30/10	No	Yes	Yes	1,3	$150 fine; registration suspension, confiscation of plates (f)
IL	BI & PD Liab, UM	20/40/15	No	Yes	Yes	1,3	60-day registration suspension (f)
CO	BI & PD Liab	25/50/15	Yes	Yes	Yes	1,4	License suspension, $500 fine
FL	PD Liab, PIP	10/20/10 (i)	Yes	Yes	Yes	1,4	60-day license revocation, vehicle impoundment for subsequent offense and confiscation of plates in Dade, Broward and Hillsborough counties (f)
CT	BI & PD Liab, UM, UIM	20/40/10	Yes	Yes	Yes	1,4	Registration/license suspension/revocation, confiscation of plates, vehicle impoundment, $110-$250 fine
SC	BI & PD Liab, UM	15/30/10	Yes	Yes	Yes	1,4	Less than 30 days jail, registration suspension (f)
NC	BI & PD Liab	30/60/25	No	No	No	1,4	60-day registration suspension (f)

ENFORCEMENT OF COMPULSORY AUTO LIABILITY INSURANCE LAWS
(As of July 2004)

State	Insurance Required (a)	Minimum Liability Limits (b)	Proof of Insurance Required (c)				Penalties for Non-Compliance (First Offense)
			At Registration	At Time of Accident	At All Times in Vehicle	Insurer Verification of Insurance (d)	
NE	BI & PD Liab	25/50/25	Yes	Yes	Yes	1,4	$500 fine (f), license and registration suspension
NV	BI & PD Liab	15/30/10	No	Yes	Yes	1,4	$100 fine (f)
LA	BI & PD Liab	10/20/10	Yes	No (e)	Yes	1,4	$25 fine, up to $500 fine, confiscation of plates (f), vehicle impoundment
VA	BI & PD Liab, UM	25/50/20	No	No	No	1,2,3	None
AZ	BI & PD Liab	15/30/10	No (g)	Yes	Yes	1,2,4	$250 fine
NY	BI & PD Liab, PIP, UM	25/50/10 (m)	Yes	Yes	Yes	1,4	1-year license revocation
AR	BI & PD Liab	25/50/25	Yes	No	No	None	$250 fine; registration suspension, confiscation of plates (f)
HI	BI & PD Liab, PIP	20/40/10	No	Yes	Yes	None	$1,000 fine
AL	BI & PD Liab	20/40/10	Yes	Yes	Yes	None	$500 fine, license suspension
NH	FR only, UM	25/50/25	No	No (e)	No	None	None

(a) FR—Financial responsibility only. Insurance not compulsory.

Compulsory Coverages:

BI Liab—Bodily injury liability

PD Liab—Property damage liability

UM—Uninsured motorist

PD—Physical Damage

Med—First party (policyholder) medical expenses

UIM—Underinsured motorist

PIP (Personal Injury Protection)—Mandatory in No-Fault states. Includes medical, rehabilitation, loss of earnings and funeral expenses. In some states PIP includes essential services (such as child care).

(b) The first two numbers refer to bodily injury liability limits and the third number to property liability.For example, 20/40/10 means coverage up to $40,000 for all persons injured in an accident, subject to a limit of $20,000 for one individual, and $10,000 coverage for property damage.

(c) Proof of valid insurance. The form of evidence varies by state and may take the form of an insurance policy, binder, certificate of self-insurance, surety bonds, or certificate of deposit. Many states require insurance identification cards issued by the insurer. Self-certification, where the driver is required to identify the insurer and policy number in writing rather than in person, is not included.

(d) 1. Insurer must notify Department of Motor Vehicles or other state agency of cancellation or nonrenewal.

2. Insurer must verify financial responsibility or insurance after an accident or arrest.

3. Insurer must verify randomly selected insurance policies upon request.

4. Insurers must submit entire list of insurance in effect, which may be compared with registrations at a state agency. Also known as a computer data law.

(e)Insured must provide evidence of insurance at some point after the accident to the Department of Insurance, other state agency, or law enforcement officer.Deadlines vary among the states.

(f)Penalties are provided for in the law but may not be mandatory for first offenses.

(g)Proof of insurance must be presented within 30 days of registration.

(h) Low-cost policy limits for Los Angeles and San Francisco low-income drivers in the California Automobile Assigned Risk Plan are 10/20/3; pilot program effective January 1, 2000 until January 1, 2007.

(i) Instead of policy limits, policyholders can satisfy the requirement with $30,000 combined property damage liability and bodily injury liability.

(j) In addition, policyholiders must also carry at least $1,000 for medical payments.

(k) May be waived for the policyholder but is compulsory for passengers.

(l) Basic policy (optional) limits are 10/10/5. Uninsured and under-insured motorist coverage not available.

(m) In addition, policyholders must have 50/100 for wrongful death coverage.

(n) Instead of policy limits, policyholders can satisfy the requirement with a $75,000 combined single limit policy.

(o) Instead of policy limits, policyholders can satisfy the requirement with a $60,000 single limit policy.

(p) Although legally defined as financial responsibility, Tennessee's law is similar to a compulsory law because drivers can be fined if stopped by police or after crashes if they cannot show proof of financial responsibility.

(q) Instead of policy limits, policyholders can satisfy the requirement with a $65,000 combined single limit policy.

*Effective January 1, 2006. **Effective November 1, 2004.

Sources: Property Casualty Insurers Association of America, state departments of insurance and motor vehicles.

* This information is located on the Insurance Information Institute Inc. website at www.iii.org