Chapter 9

Multiple-Choice Questions

1. **A**
2. **B**
3. **A**
4. **D**
5. **B**
6. **C**
7. **B**
8. **D**
9. **D**
10. **C**

Short-Answer Questions

Question 1

A peril is anything that may cause a loss event. Examples of perils would be fire, windstorms, accidents and robberies.

A hazard is something that will increase the likelihood of a loss event. For instance, drunk driving, defective wiring, flammable materials placed close to gas stoves etc.

Question 2

Suggested answers include:

- Indemnity – Reinstates the insured to his/her financial position prior the occurrence of the loss
- Utmost good faith – Insurer and insured enter into a binding contract in utmost good faith, belief and trust. The insured must disclose all material facts on the risk completely and accurately.
- Subrogation – Transfer of rights from the insured to the insurer to take actions against a third party that caused loss to the insured.
- Insurable interest – To have economic relevance and/or financial dependence on an object or person. Purpose is to avoid/reduce malicious intent in the purchase of insurance policies.
- Contribution – Applies if the insured has multiple insurance policies from more than one insurer covering the same loss. Insurer may exercise this right to recover a proportion of losses from other insurers covering the loss.
- Proximate cause – If the loss is caused by more than one peril, the nearest or most dominant cause of loss should be used to determine the insurer's liability

Question 3

The actual cash value basis of compensation is calculated based on the estimated replacement value less accumulated depreciation. The replacement value means that the tenant is covered for the cost of replacing the item at today's prices.

On the other hand, the reinstatement value basis is based on the cost of a brand-new item without any adjustment for depreciation.

Generally, the premium based on reinstatement value basis of compensation coverage would be higher.

Question 4

Ratio of sum insured to current market value = 500,000/800,000 x 100 = 62.5% < 80%

Apply the larger of actual cash value and sum insured/ (80% replacement cost) x Loss amount

(I) Actual cash value = 95,000 – 95,000 (10/40) = RM71,250

(II) Sum insured/(80% x Replacement cost) X Loss amount

= 500,000/(0.8 x 800,000) X 95,000 = RM74,218.75

As such, the compensation will be the larger of (I) and (II) which is RM74,218.75

Question 5

Based on the schedule of insurance rates in Figure 3, the estimated full insurance premium would be
= 339.1 + 26 (109,000- 1,000)/1000 = 3,147.10

Private Car Schedule of Premiums				
	West Malaysia (RM)		East Malaysia (RM)	
Cubic Capacity (cc) Not Exceeding	*Comprehensive (X – Rate for first RM1,000 sum insured)	Third Party	*Comprehensive (Rate for first RM1,000 sum insured)	Third Party
1400	273.8	120.6	196.2	67.5
1650	305.5	135	220	75.6
2200	339.1	151.2	243.9	85.2
3050	372.6	167.4	266.5	93.6
4100	404.3	181.8	290.4	101.7
4250	436	196.2	313	110.1
4400	469.6	212.4	336.4	118.2
over 4400	501.3	226.8	359.5	126.6

Since Rodney has been accident free for 4 years, he would be entitled to an NCD of 45%
= 45% × 3,147.10 = RM 1,416.20

The total discounted premium = 3,147.10 – 1,416.20 = RM 1,730.90
Add: Sales tax @ 10% 103.85
Add: Stamp duty <u>10.00</u>

Final estimated premium <u>RM 1,844.75</u>

Discussion Questions

Question 1

Suggested answers include:

- Insurable Interest may be defined as the legal right to insure arising out of a financial relationship recognised at law, between the insured and the subject matter of insurance.[1] The key elements contained in this definition is that there must be in existence a subject matter of insurance, the policyholder must have an economic or financial interest in the subject matter of insurance, the interest must be a current interest, not merely an expectancy and the interest must be a legal interest.
- In the absence of insurable interest, there could be instances where individuals use insurance to cover the lives or property belonging to other and then abuse these contracts to gain financially from the miseries suffered by others without incurring financial losses themselves. This opportunity if left unchecked may also lead to these people being tempted into causing premature death or destruction of properties to collect the insurance funds.
- The indemnity principle ensures that the claimant is the key principle in ensuring that the insured is restored to the position that he enjoys before the loss and nothing beyond that. It deals more on the amount of compensation to ensure that the claimant cannot profit from a loss event.
- Insurable interest form part of the foundations of validity of insurance contracts as they ensure that only pure risks can be insured, whereas indemnity deals with equitability of claims for individual losses. Both principles are necessary and complementary in insurance.
- Any other relevant answer.

Question 2

This claim is unlikely to be successful for some of the following reasons:

- Motor vehicle policies exclude the vehicle being used for competitive sports.
- This is an intentional act that is not a fortuitous loss (i.e. loss that occurs by random chance).
- Farid participated in an illegal activity.

Question 3

- Floods are generally considered a catastrophic event and not insurable risk. This is because to qualify as insurable risk the loss has to demonstrate large numbers of exposure, fortuitous losses (i.e. random chance), definite and measurable loss in order for a statistical estimate to be made using predictable probabilities.
- Floods are excluded from standard comprehensive motor vehicle cover.
- However, some insurance companies offer extended flood cover. If Rajan has purchased this extended coverage, he would be able to claim for the loss assuming the car is fully insured.

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[1] Lucena v Carufurd (1806) 2 Bos & PNR at 302; Simcock v Scottish Insurance Co., [1902] 10 S.L.T. 286 OH; Macaura v Northern Assurance [1925] A.C. 619, HL.

Case Study

Question 1

As there is more than one peril in this case (medical/stroke risk and accident risk), the proximate cause principal will be applied. It would be Choo's (the insured) onus to prove the cause of loss.

Question 2

- Since Choo is at fault, the third party will claim for damage of the car and bodily injury (medical bills) of RM27,000 under Choo's comprehensive motor vehicle covered.
- Choo's own car damage loss of RM25,000 can also be claimed under his comprehensive motor vehicle policy.
- Choo's medical bills will be covered under the personal accident policy (since the proximate cause is deemed to be an accident) up to the maximum sum insured of RM10,000, Choo will have to bear the balance of RM15,000 on his own.

Question 3

- Choo will lose his no claim bonus/discount on his motor insurance policy.
- His NCB/NCD will drop to zero.

Question 4

- The betterment clause applies the principal of indemnity stipulates that the reason for insurance is to restore the insured to the position before the loss and not more than this.
- Since the car is 3 years old (< 5 years old), based on the betterment adjustment rates below, in this case, there will be no deduction to the full claim.

Age of Vehicles/ Years	Maximum Rate (%)
Less than 5 years	0
5	15
6	20
7	25
8	30
9	35
10 and above	40