**Leaving Cert Business Chapter 12 Notes – Insurance and Taxation**

**Learning objectives – Insurance**

1. Distinguish between Insurance and Assurance
2. Principles of Insurance (Rules that govern Insurance)
3. Insurance Premiums – factors and calculations
4. Insurances a Business should have
5. Importance of business insurance
6. Insurance a Household should have
7. Compare and Contrast insurance for Business and Households

**1. Distinguish between Insurance and Assurance**

**Insurance** is protection against something that might happen

Eg: fire, theft.

**Assurance** is protection against something that will happen

**eg:** death or retirement

It is an agreement *(contract)* between an individual who is afraid of incurring a loss or damage (*insured*), and an insurance company (*insurer*). In return for a fee (*called a premium*), the insurer will compensate the insured if this damage or loss occurs.

* The Insurer is the insurance company who sells insurance/assurance
* The Insured is the person purchasing insurance/assurance
* The Premium is the fee paid by the insured to the insurer to purchase insurance
* Compensate means to make a payment to make amends/make good

**2. Principles of Insurance**

**1. Insurable Interest**

* A person must benefit from the existence of an item and suffer from its loss if it is to be insured

**Insurable Risks** are risks that can be insured against

**Eg:** you can insure your own house as its loss would cause you financial suffering

**Non Insurable Risks** are risks that cannot be insured against as it’s impossible to calculate the risk

Eg: You cannot insure your neighbour’s house as its loss wouldn’t cause you financial suffering

**2. The Principle of Utmost Good Faith**

This states that you must give all material facts on the proposal form which could influence the insurer’s decision to give you insurance cover. A driver must give age, address, previous experience and claims, engine size

**A material fact** is a piece of information that will help the insurance company to

1. estimate the risk involved
2. Decide whether or not to insure the risk
3. Calculate the premium to charge
* The greater the risk involved, the greater the premium charged
* If lies are told and a claim arises, the insurance contract is declared void and the insurer will not pay any compensation because the principle of utmost good faith will have been broken.
* The insured agrees to this principle when signing the proposal form

**3. The Principle of Indemnity**

This states that the insured cannot gain/make profit from making an insurance claim.

The insured is only entitled to receive compensation for the loss suffered and which will place him/her in the same position after the loss as they were in before it was incurred.

EG

A house valued and insured in 2006 for €300,000 burns down in 2012. It’s current market value is only €150000. The insurer will only pay €150000 compensation as this is how much it will cost to reinstate the house.

This principle also affects those who are underinsured (common during house value increases)

A house valued at €300000 and insured for €200000 is only 2/3 insured. A fire causes €60000 worth of damage however the compensation will only be 2/3 or €40000.

**4. The Principle of Contribution**

This states that if a risk is insured by two or more insurance companies, any compensation payable will be shared between the companies. Each company pays compensation in relation to the amount of risk it covered

Compensation paid by each insurance company is calculated by the following formula

Eg:

* + A house is worth €300,000
	+ It is insured with Company A for €125,000
	+ It is insured with Company B for €175,000
	+ The house is damaged by fire and the damage amounts to €42,000

Company A would pay €17,500 compensation

125,000 X 42,000 = €17,500

300,000

Company B would pay €24,500 compensation

175,000 X 42,000 = €24,500

300,000

***Also see example on page 216***

**5. The Principle of Subrogation**

* This passes on the legal right to the insured to recover any loss suffered over to the insurer
* When the insurer pays out compensation, the insurer can claim from someone else who might have caused the loss.
* After paying compensation for a loss suffered, the insurance company is entitled to take over any property.

Eg:

* + An insurance company pays compensation to a business whose stock is destroyed by a fire caused by a negligent electrician.
	+ The insurance company can sue the electrician for the amount of compensation it had to pay out.
	+ The insurance company can sell any remaining stock to recover some of its compensation

**3. Insurance Premium – the cost of insuring an item usually every year.**

**Factors that affect the cost of an Insurance Premium**

1. **Risk**

The greater the risk the higher the premium will be. Eg – young male drivers statistically are more at risk of an accident therefore their insurance premium is higher. Location of a property also comes under this factor.

1. **Value of the Item**

The higher the value of an item the higher the premium will be. A sports car worth €80000 will have a higher premium tha a V.W. Golf valued at €10000.

1. **Claims**

If a person has previous claims their premium will be higher. Also if the insurance company is paying out more in claims or costs then they increase premiums to cover this. Eg Health Insurance in Ireland has skyrocketed due to increase claims and costs.

1. **Profit**

The insurance company is a Business and therefore needs to make a profit. If Profits decrease they wil increase premiums the following year.

1. **Government Taxes**

The government charges a Levy on all private insurance premiums. This is to cover costs such as hospital and emergency services associated with accidents.

**4. Insurance a Business Should Have:**

1. **Theft Insurance** – to cover risk of items being stolen
2. **Public Liability Insurance** – to protect business from claims by any member of public for compensation for injury caused while on their property.
3. **Product Liability Insurance** – to protect business from claims by any member of public for compensation for injury/harm caused while using/consuming their product.
4. **Employers Liability Insurance** – To protect the business financially from any harm or injury caused to an employee during the course of their work.
5. **Motor Insurance** – to financially protect the business if damaged is caused to vehicles in an accident caused by their employee – also protects other drivers on the road.
6. **Fidelity Insurance** – to protect the business from suffering financially from theft or fraud by an employee.

**5. Importance of Insurance for a Business:**

**Business Survival**: Insurance will ensure the business is not forced to close permanently due to an unforeseen event. For example if a factory unit burns down then the insurance company will pay for costs involved in reopening the factory

**Risk Management**: Insurance helps a business to lower its risks. The business must assess all its risks before deciding what level of cover it requires. To lower its premium a business can take steps to lower these risks. For example training for employees will reduce risk of claiming under Employers Liability and will lower the premium cost.

**Improved Cash Flow.** Paying a small annual premium which can be split up monthly is far better than having to pay out one large sum in the event of an accident or claim against the company.

**Stakeholder Confidence**: A Business without insurance will not appeal to investors or lenders in terms of Finance. It will not appeal to employees during the recruitment process or suppliers who provide credit for stock and materials.

**6. Insurance a Household Should Have:**

1. **Health Insurance**

If any member of the family becomes ill health insurance will cover most costs depending on the level of cover provided. Families should shop around and be very careful when selecting their insurer as there is a lot in ‘the small print’. Many families have given up their health insurance policies as they have become so expensive in recent years. This puts extra pressure on Government finances to provide adequate cover in the public health system.

1. **Life Assurance**

A life insurance policy can be taken out to provide a financial lump sum for remaining spouse and children upon the death of a parent. Banks will insist on Life assurance to cover the cost of a mortgage, upon the death of a mortgage holder the mortgage will be paid off.

1. **Buildings and Contents Insurance:**

This is essential to prevent loss in the case of fire, flood or theft. It is important that families shop around and monitor the value of the building and its contents. Overvalued will result in higher premiums while undervalued will result in some loss.

1. **Motor Insurance**: All drivers must have at least 3rd party insurance to cover others in an accident they caused. Comprehensive insurance will cover all parties in the event of an accident.
2. **Mortgage Protection Insurance:**

Many Mortgage holders will take out a policy to protect their mortgage payments in the event of redundancy from work or sick leave. The policy will last up to 12 months and will ensure the house does not go into arrears.

**7. Household and Business Insurance Comparison**

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| **Similarities** | **Differences** |
| By Law both must pay Motor Insurance | Businesses face more risks than households and therefore must take out more types of insurance policies. |
| Both must obey all Principles of Insurance | Businesses tend to be worth more than households and therefore they pay higher premiums |
| Both have to fill in proposal forms when applying for insurance |  |
| Both must fill in claim forms to make a claim from the insurance company |  |