

CHAPTER 2
INSURANCE BASICS
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2.1 CONTRACT BASICS

ELEMENTS OF A LEGAL CONTRACT

2.1a OFFER AND ACCEPTANCE

An insurance policy is a contract between two parties. These two elements provide the basis for a contract agreement. The offering party promises to perform its duties and obligations as outlined in the policy. In return, the accepting party promises to perform its duties and obligations as outlined in the policy.

2.1b CONSIDERATION

Consideration is the cause or impelling influence that induces a contracting party to enter into the contract. It is the basic necessary element for the existence of a valid contract that is legally binding on the parties. The consideration an insurer (the insurance company) gives is its promise to perform in accordance with the policy provisions.

2.1c COMPETENT PARTIES

Competent parties are duly qualified in answering all the requirements, having sufficient capacity, ability or authority and possessing the requisite of physical, mental, natural or legal (at least 18 years of age) qualifications to enter into a legal contract.

2.1d LEGAL PURPOSE

The legal purpose provides a means by which either party to the contract can seek a higher authority, such as the courts, to enforce the policy contract provisions and seek remuneration for breach of contract, etc.

DISTINCT CHARACTERISTICS OF AN INSURANCE CONTRACT

2.1e CONTRACT OF ADHESION

An insurance contract is often called a contract of adhesion. This contract is offered to the consumer on a “**take it or leave it**” basis without affording the consumer realistic opportunity to bargain the contents of the contract.

2.1f ALEATORY CONTRACT

An aleatory contract is a “**mutual agreement**” of which the effects with respect to the advantages and disadvantages to which the parties depend on a uncertain event. An insurance policy is an aleatory contract.

2.1g PERSONAL CONTRACT

A personal contract relates to personal property or which so far involves the element of personal knowledge or personal confidence that it can be performed only by the person with whom the contract is made.

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2.1h UNILATERAL CONTRACT

A unilateral contract is one in which one party makes and expresses engagement or undertakes a performance without receiving in return any express engagement or promise of performance from the other.

2.1i CONDITIONAL CONTRACT

A contract whose very existence and performance depends upon the happening of some contingency or condition expressly stated in the contract.

LEGAL INTERPRETATIONS AFFECTING CONTRACTS

2.1j AMBIGUITIES (VAGUE MEANINGS) IN A CONTRACT OF ADHESION

Once accepted, an insurance policy is a contract of adhesion. Since the contract was drafted by the insurance company, any ambiguities or vagueness in the policy provisions are ruled in favor of the purchaser of the policy.

2.1k REASONABLE EXPECTATIONS

Because one party to the contract considers a provision to be vague doesn't necessarily mean that the provision is vague. Considering that the one party contesting the provision is not likely to be objective, the courts have consistently ruled using the "**reasonable expectations doctrine**". With the knowledge that the purchaser, for the most part doesn't read the policy, the criteria set forth in the doctrine determines whether that coverage existed based on underlying circumstances, such as a promises from the agent that the coverage is included in the policy.

2.11 INDEMNITY

The principle of indemnity provides for recovery in an amount to the extent of the loss. The maximum reimbursement for property losses is limited to the insured's (the policyholder's or purchaser's) interest. The insurable interest limitation denies recovery in excess of the loss. If the insured was able to receive more than the loss is worth, this could create situations where the insured might induce a loss in order to make a profit.

2.1m UTMOST GOOD FAITH

With the knowledge that the insured, for the most part, does not read or might not understand the policy, the insurance company is to operate in **“utmost good faith”** by using **“honesty”** and **“sincerity”** in protecting the insured's rights, as well as their own.

2.1n REPRESENTATIONS/MISREPRESENTATIONS

With the insurance company or their representatives having a distinct advantage over the insured, there is a possibility that the insurance company may misrepresent policy provisions in order to deny or limit recovery on a claim. On the other hand, the insured has a duty to provide accurate information relating to the application for insurance and any loss claim.

2.1o WARRANTIES

The insurance policy is an expressed warranty providing for indemnification of a loss up to the limits of liability as long as the application information is accurate and that the conditions of the policy have been met and the loss is covered.

2.1p CONCEALMENT OR FRAUD

The policy indicates that the entire policy will be void if whether before or after the loss, an insured has intentionally concealed or misrepresented any material fact or circumstances, engaged in any fraudulent conduct or made false statements relating to this insurance.

2.2 INSURANCE PRINCIPLES AND CONCEPTS

2.2a INSURABLE INTEREST

An insurable interest exist when the insured derives a monetary benefit by the preservation and continued existence of property or would suffer a monetary (money) loss from its destruction. If a person could be financially harmed if a property was damaged or destroyed, that person has **“insurable interest”** in that property. To make a claim under an insurance policy, that person must have an insurable interest in the property at the time of loss.

2.2b HAZARDS

1. Physical Hazard

A physical hazard is a material condition that increases the chances for a loss. Such an example would be a gasoline filled container being stored in close proximity to a fireplace or a gas heater.

2. Moral Hazard

A moral hazard is a character defect that causes some people to exaggerate or fabricate losses. One example would be an insured who sets off fire to his/her property to collect the insurance proceeds.

3. Morale Hazard

A morale hazard is present when an insured shows an indifference towards the preservation of his/her property because of the insurance protection afforded by a policy. If he/she didn't have an insurance policy, he/she would be more careful about the maintenance or protection of his/her property.

2.2c CAUSES OF LOSS (PERILS)

Cause of loss are producing agents which damage the insured property. Some examples of the common perils insured against are: fire, lightning, windstorm, hail and explosion. The quality of the policy that is purchased dictates the number of perils insured against.

2.2d NAMED PERIL POLICIES vs. OPEN PERIL POLICIES

A different approach must be taken when analyzing these types of policies. A named peril policy lists a specific number of perils insured against. Two examples of named peril policies are (1) HO-1 Basic Form Policy insures against damages by 10 perils to the Dwelling, Other Structures and Personal Property. Also included are Additional Living Expenses in case the dwelling becomes uninhabitable as a result of a covered loss. Some additional coverages are normally standard with the policy. (2) HO-2 Broad Form Policy insures against damages by 17 perils to the Dwelling, Other Structures and Personal Property. Also included are Additional Living Expenses in case the dwelling becomes uninhabitable as a result of a covered loss. Some additional coverages are normally standard with the policy. The two examples given are typical of policies requiring a loss to fall within the definition of the named perils covered under the policy.

A logical approach to finding coverage under named peril policies would be to determine the cause of loss (peril) that affected the property. Once the peril is determined, then review the perils listed in the policy in order to determine if the actual cause of loss fits one of the perils described in the applicable policy. As an example, the

two named peril policies, previously described, insure against the peril of windstorm. However, there is an additional provision attached to this peril. It states that **“this peril does not include loss to the property contained in the building caused by rain, snow, sand or dust unless the direct force of wind or hail damages the building causing an opening in the roof or wall and the rain, snow, sleet or dust enters through this opening”**.

“Ed” Homeowner has named peril policy and files a claim with his insurance company stating that, last night, the wind driven rain entered through a small crack in the roof causing extensive damage to the second floor of his home. Because he is insured under the named peril policy, “Ed” Homeowner has the burden to prove that the wind created an opening in the exterior of the building and the rain then entered through this opening. Assuming that the small crack in the roof was not caused by wind and if no evidence of wind damage exists, then, in all likelihood, there is no coverage for this loss.

One example of an open-perils policy is a HO-3 Special Form policy which insures on an open-perils basis on the Dwelling and Other Structures, 17 named perils on personal property. Also included are Additional Living Expenses in case the dwelling becomes uninhabitable as a result of a covered loss, special limits of liability to unscheduled personal property and some additional coverages that may increase the policy limits in the case of a total loss.

Analyzing coverages in an open-perils (all risk) policy starts with a surprisingly illogical approach. After searching the policy for perils that cover the dwelling, you might become frustrated to find that there aren’t any perils listed. Actually there is a logical explanation. The purpose of an open-perils (all risk) policy is to provide coverage for any loss that **“not excluded”** in the policy. Thus, a logical approach to finding coverage in an open-perils policy is to determine the cause of loss, then review the **“exclusions”** in the policy. If no **“exclusions”** apply, then the loss is covered. Let’s use the same claim filed by “Ed” Homeowner above by changing his policy to an open-perils (all risk) policy. Because he is insured under an open-perils (all risk) policy. Because he is insured under an open-perils (all risk) policy, the only burden of the homeowners is to prove that a loss occurred. The burden of proving that an exclusion applies now lies with the insurance company. Since there is no exclusion for rain entering small cracks in the roof, this loss would be covered.

2.2d NAMED PERIL POLICIES vs. OPEN PERIL POLICIES (cont’d)

It is important to remember that the open-perils (all risk) policy applies only to the Dwelling and Other Structures coverage. Personal property is covered on a named peril basis. (See Chapter 5—Homeowners Policy Section 1 for more information)

2.2e DIRECT LOSS

Direct loss is damaged caused by the direct result of a covered peril. One example of a direct loss would be a fire destroying the insureds home.

2.2f CONSEQUENTIAL OR INDIRECT LOSS

Consequential and indirect losses occur as a result of a direct loss. Property insurance covers only the value of the damaged or destroyed property, not the loss of use while it is being repaired or replaced. Indirect losses typically are not covered by an insurance policy, however, there are exceptions. If a covered loss damages your dwelling, thus rendering it uninhabitable, a typical insurance policy most likely provides coverage for temporary housing and increased living expenses while your dwelling is being repaired. A house accidentally set on fire would be considered a direct loss. The water damage caused by the fireman extinguishing the fire would be an indirect loss. The water damage would be covered in addition to the fire damage.

2.2g BLANKET vs. SPECIFIC INSURANCE

Blanket insurance is when a single face amount of the policy applies to either two or more locations, to or more types of property or a combination of locations and types of property.

Specific insurance is coverage for a defined location or type of property, such as a homeowner's policy.

2.3 BASIC TYPES OF CONSTRUCTION

2.3a PLATFORM CONSTRUCTION

In platform construction, each story of the house is built as a separate platform. Once the foundation walls are formed, a girder and post system is installed for the length of the house. The sill plates and floor joists are then attached to the foundation to form the first platform. The subfloor is then installed to complete the platform. The first floor exterior walls are built and placed at the perimeter of the platform.

Door and window openings have headers to provide for loads being transferred from above. The interior walls in a house are located to serve both as bearing walls for the ceiling joists and partitions between rooms. If the house has a second floor, joists would be placed on top of the first floor walls. Ceiling joists are used to attach the ceiling to the rooms below and act as floor joists for the flooring above. The interior and exterior walls would be built and installed similar to the first floor. On the top of the second floor walls, a roof system would be installed.

In an "A" frame or gable roof, two common types of construction methods are rafters and ridge board. The ridge board provides support at the peak for the upper rafter ends. The

lower rafter ends are usually notched to fit snugly on the outside top wall plate. The truss method provides an easier assembly of the roof system.

2.3b PLATFORM CONSTRUCTION

Most trusses are pre-assembled at a truss fabrication plant. The triangular shape of the truss provides for each slope of the roof and nailing surface for the ceiling below. They are usually placed on twenty-four inch centers and held in place at the peak with a temporary board. The roof sheathing is then installed to hold all the trusses in place.

2.3c BALLOON CONSTRUCTION

In balloon construction, the wall studs extend from the sill of the first floor to the top plate of the second. In platform construction, the exterior framed walls are completed for each floor. This is a major difference between balloon construction and platform construction. Balloon construction is used primarily in tornado areas, i.e., Mid-West states. This type of construction provides for the greater degree of protection from the force of wind. Because platform construction consists of separate sections of the exterior walls at each floor the high winds could conceivably get under the platform and blow off complete sections of the house. Other than the exterior walls, the rest of the construction is essentially the same.

2.3 JOISTED MASONRY

Balloon and platform construction require the use of wood framing to construct the building whereas joisted masonry consists of brick, stone or cinder block exterior walls and wood joists that form the floors and ceilings at each level. In other words, the building is masonry with combustible roofs and floors.

2.3e FIRE RESISTIVE

Fire restrictive buildings require the use of non-combustible components in their construction. Elements of this type of construction would include cement slabs, brick, concrete, metal or cinder block walls and a metal truss system with corrugated roofs.

2.4 LOSS VALUATION

Insurance policies provide for several ways in which payment is made for damaged property. Below, we will discuss the various methods.

2.4a ACTUAL CASH VALUE (ACV)

Actual cash value is a term commonly used in the valuation of property loss. Many items lose their full value as they age, get abused or become obsolete. This is commonly known as depreciating an item. The most popular way to calculate the actual cash value is to

determine what an item of like kind and quality would cost using current prices, then depreciate the current price using the following formula:

A television with a life expectancy of eight years gets damaged by fire in its fourth years.

The current price of a new television of like and kind quality coat	500.00
The old television was four years into an eight years life expectancy(minus 50%)	<u>-250.00</u>
The actual cash value of the old television is	250.00

2.4b REPLACEMENT COST VALUE (RCV)

As used in the example in 2.4a, the cost of the new television is the replacement cost value. Even if the damaged property is several years old or if its replacement cost now exceeds the original purchase price, the insured is entitled to the current cost to replace the item.

2.4c FUNCTIONAL REPLACEMENT COST

Functional replacement cost is a loss settlement provision that provides for replacing the damaged parts of an older building with current construction materials. For example, a fire damages the plaster walls in a house. Functional replacement cost provisions would allow for the plaster walls to be placed with drywall.

2.4d MARKET VALUE

The market value of an item is the amount at which a knowledge buyer under no unusual pressure would be willing to buy an item and a knowledgeable seller under no unusual pressure would be willing to sell that item. Market value is particularly useful when an object has no real replacement cost, i.e., when no other object of like kind and quality exists, as with antiques, works of art and other collectibles.

2.4e STATED OR AGREED VALUE OR AMOUNT

An agreed value settlement provision requires the insurance company to pay the previously agreed amount for a total property loss. This agreement is between the property owner and the insurance company and takes place prior to the insurance policy being written on the property. As an example, the property to be insured is a valuable painting. The insurance company and the owner of the painting would agree to a dollar amount to be paid in the event of a total loss of the painting. This type of agreement virtually eliminates any disagreements concerning the value after the loss occurs.

2.4f VALUED POLICY

Valued policy laws dictate the amount of recovery the insured can expect in the settlement of a total loss.

Some states have enacted such laws to protect the insured after a loss. Valued policy laws were passed to Ensure a fair amount in settlement based on the total dollars of coverage upon which the insured's premium was based. In theory, if the insured were paying the premium for \$300,000 coverage, then in the event of a total loss, the insured would receive \$300,000. *Pennsylvania is not a Valued Policy state.*

2.5 POLICY STRUCTURE

2.5a DECLARATIONS (DEC) PAGE

The Declarations page is the over sheet/sheets to a policy that contains information specific to the insured.

Typically found on the "Dec" page(s) are the following items of information:

- | | |
|--|---|
| >Policy Number | > The mailing address of the Insured(s) |
| > Inception and expiration dates of the policy | > The address of the covered property |
| > Name of the insurance company | > The policy limits |
| > Name of the insurance agent | > Deductible amount |
| <Name of the Insured | <Mortgage company or secured creditor |
| <Numbers and editions dates of all attached forms and endorsements | |

2.5b DEFINITIONS

The Definitions Section of the policy defines terms used throughout the insurance policy. The typical words or phrases defined in insurance policies are as follows:

- | | |
|-------------------|------------------------|
| >Insured | >Residence employee |
| >Insured location | >Property damage |
| >Business | >Residence premises |
| >Occurrence | >Vacant vs. unoccupied |

2.5c INSURING AGREEMENT

An Insuring Agreement is any policy statement to the effect that, under some circumstances, the insurer will make payment. The broad statement of the insuring agreement, in effect, provides the insurance described in the policy by the insurance company, for the insured's compliance with all applicable provisions of the policy. However, the policy contains many individual insuring agreements that affect specific events. More specifically, the policy may put limitations on how a loss may occur before covering that loss.

2.5d ADDITIONAL/SUPPLEMENTARY COVERAGES

The additional coverages are provided to cover incidental costs associated with a covered loss. These coverages may also include a maximum amount that will be paid for these costs. Some examples of the additional coverages are:

- >Debris removal
- >Reasonable repairs
- >Trees, shrubs or other plants
- >Fire Department service charges
- >Credit card, fund transfer card, forgery and counterfeit money
- >Loss Assessment
- >Collapse
- >Glass or safety glazing material
- >Landlord's furnishings

2.5e CONDITIONS

This section of the policy containing the provisions, would include the following:

- >The Insurer's limit of liability
- >The insured's duties after a loss
- >Loss settlement
- >Loss to a pair or set
- >Mortgage clause
- >Recovered property
- >Appraisal
- >Other insurance
- >Law Suit
- >Loss payment
- >Abandonment of property
- >Nuclear hazard

2.5f EXCLUSIONS

This section of the policy serves to exclude losses that are either considered uninsurable or would be better provided for under another type of policy. Some of the general exclusions are as follows:

- >Earthquake
- >Flood damage
- >War
- >Intentional loss by the insured
- >Building upgrades
- >Neglect by the insured
- >Faulty construction
- >Nuclear hazard

2.5g ENDORSEMENTS

Many endorsements are available for modifying insurance policies to meet a particular need. Endorsements provide a means by which an insured or insurer can add, alter or eliminate coverages. The endorsement numbers are usually located on the Declaration Page of the policy. Some endorsements are state mandated while others include a change in coverage by the insurer or an insured's wish to insure an expensive possession.

2.6 COMMON POLICY PROVISIONS

2.6a INSUREDS: NAMED, FIRST NAMED, ADDITIONAL

The **named insured** is any person or persons, partnerships, corporations, etc., named on the Declarations page of the policy. Their interest is primary and provable by a title.

The **first named insured** applies to commercial type policies. In the case of cancellation, the insurance company must mail the notice to the **first named insured**. If multiple insured's are listed on the Declaration page, only the **first named insured** can cancel the policy.

In a homeowner's policies, **additional insured's** are residents of a household who are the named insured's relatives or other persons under the age of 21 who are in the care and/or custody of the named insured or their relatives.

2.6b POLICY PERIOD

The inception and expiration dates included on the Declarations page determines the policy period. The most common policy period is one year starting with the inception date and the be renewed by the expiration date. Some policies do not provide a fixed expiration date. This type of policy runs continuously until it is cancelled by either the insurer or insured.

2.6c CANCELLATION AND NON-RENEWAL

A policy can be **cancelled** at any time by the **insured**. However, the policy provides for **only the reasons stated below by which an insurer can cancel a policy**. In all instances, 30 days prior notice is required.

- >When the insured has not paid the premium
- >When the policy has been in effect for less then sixty days
- >When a material misrepresentation was made in the application for insurance
- >If the risk to insure your property has changed substantially since the policy was issued

Non-renewal of the policy differs with a cancellation in one important aspect. A cancellation can take effect during any point in the policy period. A **Non-renewal** would take effect on the expiration date of the policy period. Written notice of at least 30 days is required for a non-renewal.

2.6d DEDUCTIBLES

Deductibles serve various purpose. One important purpose is that it causes the insured to share in the loss. In theory, it should provide some motivation to the insured to prevent or at least minimize a loss. **Deductibles** also serve to eliminate the insurer's obligation for

small losses. **Deductibles** to reduce the premiums paid for a policy. An insured can get a higher deductible in order to reduce the premium.

2.6c OTHER INSURANCE

The **Other Insurance** clause becomes operative only in cases where there is more than one insurance policy covering the property. All policies include the **Other Insurance** clause with an explanation on how the loss is to be handled in the event **Other Insurance** also covers the loss claimed.

2.6f PRIMARY/EXCESS INSURANCE

The **Primary/Excess Insurance Clause** would indicate that the policy will provide coverage until the limits are exhausted, then the second policy will pay for any additional loss until that policy is exhausted.

2.6g PRO RATA (PROPORTIONAL)

The **Pro Rata** or **Proportional** other insurance provides for the “share method,” more common to homeowner’s policies. With this method, two insurers contribute to the loss payment in the proportion to which they contribute to the total amount of coverage purchased. The following is an example:

Insurance Company “A” insures the property for \$40,000 and Insurance Company “B” insures the property for \$60,000. John Smith, the homeowner, suffers a \$10,000 loss. The formula below will provide the amount that each insurance company will be responsible to pay.

Step 1: Add the two coverages together

$$\$40,000 (A) + \$60,000 (B) = \$100,000 \text{ (total coverage)}$$

Step 2: Take insurance company A coverage amount and place it over the total amount of insurance

$$\frac{\$40,000}{\$100,000}$$

Step 3: Reducing this fraction will determine that insurance company A’s payment amount is

$$\frac{4}{10} \text{ multiplied by the } \$10,000 \text{ loss} = \$4,000$$

Step 4: Take insurance company B’s coverage amount and place it over the total amount of insurance

$$\frac{\$60,000}{\$100,000}$$

Repeat Step 3: Reducing this fraction will determine that insurance company B’s payment amount is

$$\frac{6}{10} \text{ multiplied by the } \$10,000 \text{ loss} = \$6,000$$

To confirm that your calculations are correct, add insurance company A’s payment and insurance company B’s payment amount. This total should equal the loss amount suffered by the insured.

2.6h POLICY LIMITS

Virtually all insurance policies carry a limit or a maximum amount paid under the policy. For example, a homeowner carries \$100,000 insurance for his dwelling. His dwelling suffers a total loss from a fire and an assessment of the damage reveals a cost of \$110,000 to rebuild the property. The homeowner is entitled to only the \$100,000 limit of liability. The other \$10,000 will have to come from another source.

One notable exception to policy limits is the Guaranteed Replacement Cost Endorsement. This endorsement guarantees the replacement cost of the dwelling even if the cost exceeds the policy limits.

2.6i RESPORATION/NON-REDUCTION OF LIMITS

Although not stated in the policy, during a policy period, a homeowner's policy provides the restoration of the full limits immediately following a loss. For example, an insured with \$100,000 insurance policy suffers a \$60,000 loss by fire. Immediately following the fire, the full \$100,000 would be available for future losses that may affect his/her property during the policy period. To better illustrate this, certain commercial policies provide for an aggregate limit during a policy period. In other words, a commercial building with a \$500,000 aggregate limit means that during that policy period, the total amount of claimed losses cannot exceed \$500,000. Each loss reduces the amount of insurance during that policy period.

2.6j CO-INSURANCE

The **Co-Insurance Clause** is contained in virtually all property insurance policies **Co-Insurance** is a penalty assessed against the insured if enough insurance is not carried on the property. The **Co-Insurance** provision, in theory, is to encourage property owners to carry enough insurance on the property that is owned before a loss occurs; if not, the property owner will share in the loss. The **Co-Insurance Clause** in the policy does not state a specific dollar amount to be carried, it simply states a percentage of coverage to be carried. A typical homeowner's policy would contain an 80% **Co-Insurance Clause**. In this case, the property owner needs to carry 80% of the amount required to replace to property. Since the clause can affect the amount of recovery and its triggered only after a loss has occurred, let's examine how the clause can affect the insured.

John Smith carries only \$40,000 coverage on his home. John sustains a water loss of \$10,000. When the insurance company inspects the damage, they will determine that his house should have been insured for \$100,000. The following formula will determine how John is affected by being underinsured.

Amount of insurance carried

Amount of insurance required X Amount of loss = Amount paid

\$40,000 is the amount of insurance carried by John Smith

\$80,000 is the amount of insurance required by insurance company
(80% x \$100,000)

\$40,000(amount carried)

\$80,000(amount required) X \$10,000 (loss amount) = \$5,000
(amount paid)

In this instance, the insurance company would pay \$5,000 for their share of the loss. John Smith, the property owner, would have to pay the balance of \$5,000 out of his own pocket or from other sources.

2.6k VACANCY vs. UNOCCUPIED

Most property policies distinguish between **vacancy** and **unoccupied** for the purpose of excluding certain losses. A property void of furniture and other contents would be considered **vacant**. Property policies would exclude losses such as vandalism or malicious mischief if the property is **vacant** for 30 or 60 consecutive days.

A property owned by a family on vacation for two weeks would be considered **unoccupied**.

2.6l ASSIGNMENT

Insurance policies usually include an **Assignment Clause** that states that an assignment of the policy will not be valid unless the insurance company gives its written consent. In other words, before a loss occurs, the insured cannot assign his policy benefits to another person entity unless the insurer has knowledge and gives written consent. However, policy benefits can be assigned after a loss occurs. A homeowner who has a damaged roof can assign the anticipated claim payment to pay for a new roof.

2.6m LIBERALIZATION

If the insurance company makes changes which adds coverage to an edition of the policy, then no additional premium will be charged. These changes will automatically apply to the insurance policy as of the date the insurance company implements them in the state, depending on the policy. The implementation date must fall within a predetermined amount of days prior to or during the policy period stated on the Dec page.

2.7 THIRD PARTY PROVISIONS

2.7a MORTGAGE CLAUSE

The **Mortgage Clause** in the policy gives the mortgage company certain rights under the policy. If there is a mortgage company named on the Dec page as a loss payee, the insurance company must put the mortgage company's name on the settlement check for losses involving the Dwelling and Other Structures insured under the policy. If the insurance company cancels the policy, they will give the mortgage company at least 10 days notice before the cancellation takes effect.

2.7b LOSS PAYMENT CLAUSE

The **Loss Payment Clause** states that the insurance company will pay the insured unless someone is named in the policy or is a legally entitled to receive payment for the loss. Losses are payable usually 30 or 60 days after the insurance company receives the insured's proof of loss and reaches an agreement with them.

2.7c NO BENEFIT TO THE BAILEE

The insurance company will not recognize any assignment or grant any coverage that benefits a person or organization holding, storing or moving property for a fee. An example would be a broken television brought in for repair to a service center (the **bailee**). If the television gets damaged by fire while in the care, custody or control of the service center, this insurance policy will not cover the fire damage. The service center's insurance will have to pay the cost relating to the fire damage.

2.8 PENNSYLVANIA LAWS, REGULATIONS AND OTHER PROVISIONS

The insurance policy is essentially a contract between the insurer and the insured. The policy contains provisions that require each party to the policy to perform duties in the event of a loss. However, there may be laws or regulations that conflict with the policy provisions. In the event such laws or regulations conflict with a provision, a law(s) or regulation(s) supersedes the policy provision(s). Included with the following are other rights afforded under an insurance policy that are not necessarily included in the policy.

2.8a PENNSYLVANIA PROPERTY AND CASUALTY GUARANTY ASSOCIATION

One reason that this association is in place is to compensate the insured for a loss in the event the insurance company the policy was purchased from becomes insolvent. The insurance company must be a member of the association in order for the insured to benefit from its services.

2.8b STANDARD FIRE POLICY

Today, the **1943 New York Standard Fire Policy (SFP)** is used verbatim in 35 states with minor variations in the remaining states. The Declarations page of the policy includes the insuring agreement, space for listing the names of the insured, the mortgage company (if any), the perils covered, the amount of the insurance, rates, premium for each coverage, applicable co-insurance percentages and the description and location of the property covered. Stipulations and conditions are on page two. Because they occupy 165 lines, this policy is called the 165-line form. Although the standard fire policy is a point in all fire insurance coverages, the document is not complete, at least one additional form must be attached to have a valid policy.

2.8c CANCELLATION AND NON-RENEWAL

As discussed in **Common Policy Provision 2.6c** the insurance policy contains procedures for the **cancellation** or **non-renewal** of an insurance policy. Recent provisions mandated by the state require the insurance companies to make changes to these provisions. Insurance companies are now required to give at least **30 days** notice for **cancellation** or **non-renewals**. The policy provides a list of reasons for which a policy can be cancelled. This list now applies to **non-renewals** as well.

2.8d DEATH OF A NAMED INSURED

If any person named in the Declarations page or the spouse of a resident of the same household dies, the insurer will insure the legal representative of a deceased, but only with respect to the premises and property of the deceased covered under the policy at the of death.

2.8e BINDERS

A **Binder** is common to all types of insurance. A **binder** is written or oral agreement that immediately provides insurance for a period of no more than **30 days**. During this 30 days, the insurance company can process the application and conduct an investigation to determine if they wish to continue the insurance beyond the 30-day period.

2.8f INSURANCE CONSULTATION SERVICES EXEMPTION

The insurance company may wish to inspect the property the intent to make recommendations regarding the maintenance of the property. The primary purpose of the consultation is to decrease the chance of loss, injury or death by having you install smoke detectors or fix cracks in your pavement. The exemption provides immunity from civil liability to the insurance company or their representative in cases where an overlooked

hazard on the property causes injury, loss or death. Also, any injuries sustained by the owners or other persons carrying out their recommendations are exempted.

Additional Information That Could Be In Your Test

The primary purpose of the Insurance Department is:

1. To provide adequate rate levels and promote solvency
2. To ensure fair and equitable treatment of the public and companies
3. To ensure the public's interest is protected

All of the following are duties of the Insurance Commissioner:

1. Enforce violations of the Trade Practices Act
2. License agents, brokers and companies
3. Regulate rates

All of the following are characteristics of a licensed or admitted insurance company:

1. Must pass state required minimum financial standards
2. Must agree to abide by statutory regulations
3. Produces business through local branches and agents

A licensed or admitted insurance company will not accept surplus and excess lines business.

A representation describes the statements made by an individual at application.

All of the following are examples of types of warranty:

1. Affirmative warranty
2. Continuing or promissory warranty
3. Implied warranty