



## MR. MAINAK GHOSAL

B.COM, LL.B, PGDBL, PGDADR,  
MBA(Finance), FCMA, FICA, FIV

# A STUDY ON THE ROLE OF VALUATION IN INSURANCE INDUSTRY OF INDIA

### INTRODUCTION

The Insurance Regulatory & Development Authority of India (IRDA) recently issued a press release that IRDA is set on a mission for insurance for all by 2047 and has since been taking proactive steps to achieve the objective. Moreover, the IRDA said that India is set to become the 6th largest insurance market by 2032 from the 10th largest currently but the country needs to infuse Rs.50k crores of capital per year to its insurance industry [1]. Also Rs.50k crores of capital is needed every year to double its penetration rate in this country.

Looking at the facts, the Economic Survey released by the Government of India on 31st January, 2023 records that overall insurance penetration in India has risen from 2.7% in 2000 to 4.2% in 2020 but dipped in 2012 to 3.2%. However, this dip may be attributed to the Covid 19 pandemic which had turned most of the assets to non performing ones.

To delve deeper, Insurance Penetration rate in Eastern Zone is about 2.8% but is low considering all India average being 3.8%. It is reported that

countries like Taiwan(14.8%) & SouthAfrica(12.2%) along with the developed countries like USA(11.7%) & UK(11.1%) fare much better than us. In order to increase the penetration, there is a dire need of regular discussion & adoption of new technologies based on socio-economic conditions, adopting regional language in writing claim settlements, language policies, renovation in operation of Arbitration, Consumer forum judgement, Ombudsman operation as well as out of court claim redressal & assistance so that present LEVEL OF TRUST between the Insured & Insurer can be increased thus in turn increasing the penetration rate of the Eastern Zone[2]. But herein the question arises – What is Valuation & how it is related to Insurance?

According to Henry A. Babcock, “ Valuation is determination of the money value, at some certified date, of the property rights encompassed in an ownership”. The term monetary value would refer to a market in which goods & services are available through a certain mechanism. The principle of indemnity value applies here wherein the insured after the loss is placed in the same financial position which he enjoyed before

the loss. Here the loss means – financial & measurable loses only but only to the extent of insurable interest. The insurable interest is defined as the legal right to insure arising out of a financial relationship recognised under the law between the insure & the subject matter of insurance. It may be noted that the insurable value is the full value of the interest at the inception of the insurance.

#### Brief Discussion

Improvement is essence of growth and that is possible by attempting to increase the penetration rate. The meaning of penetration rate should be made clear. The definition itself shall spell out duties & responsibilities of Insurers, Intermediaries like Brokers, Agents, Surveyors and institutions like Banks. The penetration rate is a non-unit scalar measurement and is defined as  $\text{Penetration Rate} = \frac{\text{Number of Customers}}{\text{Size of Target Customers}} \times 100$  The ideal market penetration rate in domestic segment should be 2% to 6%(which includes intangible products also) & for industrial segment minimum is 10% & can be up to 25%. Government is slowly moving towards the regime of NO TAX DEDUCTION & the industry must gear up to face the future

challenges. Already, FM has announced the in the last Budget 23' to increase in the slab limit to Rs7 Lakhs where no deduction can be claimed & the new tax regime has been made a default. It's a matter of discussion & research as to how the consumer will react in the new scenario and what should be the next action plan of Insurance Companies. Recently while speaking at CII Insurance & Pension Summit the IRDA Chairman Mr. Debashish Panda asked the players to engage with the housing regulators to try and make property insurance compulsory, or impress upon the need for property insurance with the Union Housing Ministry.

He said that the insurers will have to go beyond the present distribution managements with scheduled commercial banks, and have bancassurance arrangements with non-bank lenders, co-operative banks & also payment aggregators. Time has come when we need to increase the awareness level of consumers & convince them about the protection aspects of insurance rather than focussing on taxation benefits. Panda also asked the insurers to create grievance redressal cells with separate

set of officials in place. So, the mindset of the agency force needs to be changed 180° and they must convince customers to buy insurance as a protection product rather than an investment product [1]. This protection gap opens a new world of possibilities for insurtech start-ups to develop new insurance products grounded in technology says Mr. Arup Chatterjee ,Principal Financial Sector Specialist, Asian Development Bank.

As already discussed, the issues of Eastern Zone is that it comprises of states like West Bengal, Orissa, Assam, Jharkhand & Bihar. 70% of population in these states live in villages & live on agricultural incomes. In villages, there are mostly small units of agriculture based such as cold storage, rice mill whose income states that there are conversion units of unbranded FMCG products & consumer eatables by conversion of agricultural produce like mango, pine apple, tomato & they mostly cater niche market. Some advanced villages have Gobar Gas Plants. Most of the population are not engaged in agriculture or partly agriculture activities but are engaged in trading businesses.

They are dealers of pesticides, cement, bricks, steel materials whose controlling offices maybe outside the state but they operate as SSUs (Small Scale Units). In reality farmers have two wheelers while goods carriers have vehicles such as Light Weight Model Tractors, etc. Electrical Substations are Government or Big House controlled & have their discussion centres at cities while small captive units for power generation exist in big villages.

In Eastern India, the loss making perils that mostly affect the domestic segment in nonurban segments having future potential are health related issues, fire, theft/burglary, Act of God (frequent occurrence like Cyclones, etc.), riot & breakdowns while allied infrastructures under Pradhan Mantri & State Government Schemes which are traditionally executed through civic bodies/ Panchayet via local contractors there are various fixed assets like Houses, Road, Sewerage Pipeline & Overhead Water Tank Projects, small span Bridges, River Protection Projects[2]. Take the case of Housing, which is the historically most popular insurance product amongst the fixed assets. Conventionally speaking,

be it any parts of India, many land lords do not insure their house against the risk of fire, flood, earthquake etc. Even the owners who insure the house against such perils, they under insure their houses, not intentionally but out of ignorance and carelessness. However, the valuer should estimate and allow appropriate and adequate insurance premium in every case, as an outgoing in the interest of safety and continuity of rental income in future, from the house.

Generally, fixing of the insured sum for buildings and plant & machinery is not a simple task. There are four accepted standard valuations namely – (i) Original Value, (ii) Written Down Value(Original Cost - Depreciation) (iii) Market Value or Fair Market Value and (iv) Reinstatement Value. Insurance on any of the first two values shall result in 'underinsurance' hence it is arranged either on Market Value or Reinstatement value Generally, fixing of the insured sum for buildings and plant & machinery is not a simple task. There are four accepted standard valuations namely – (i) Original Value, (ii) Written Down Value(Original Cost - Depreciation) (iii) Market Value or Fair Market Value and (iv) Reinstatement Value.

ment Value. Insurance on any of the first two values shall result in 'underinsurance' hence it is arranged either on Market Value or Reinstatement value.

The bases of Reinstatement Value are as follows-

- It is the Sum insured to represent replacement cost of same type or kind of the property.
- Review of sum insured on each renewal – Revaluation or with the help of RBI index.
- Slight modification of principle of 'Indemnity' as insured gets 'new' in place of 'old'- without application of depreciation.
- Reinstatement of property lost is must, otherwise claim is to be settled on market value basis.
- Condition of Average still applicable, therefore sum insured to be fixed carefully. And the Reinstatement Value Clauses are as follows
- Applicable to Building, Machinery & Fixed Assets only
- Insured to opt for this clause
- Sum insured to represent replacement cost of same type or kind of the property
- In case of claim, replacement by same type or kind of the property, improvements not paid for
- Depreciation is not applicable
- Reinstatement of property lost is must, otherwise claim is to be settled on market value basis
- Condition of Average is applicable
- Reinstatement to commence and carried out with reasonable dispatch,
- To complete within 12 months or agreed extended period, provided insurer's liability is not increased
- Reinstatement at another site is permitted with no increase in liability

#### CONCLUSIONS

There exists a great deal of confusion regarding which value to choose, what are the logical bases for choosing that value and what are the relevant clauses for the chosen value. Herein the role of insurance brokers, surveyors & agents and their constraints under present situation & regulation in respect of increasing penetration with revamp

ing the present eco system like consumer redressal, grievance cell, Ombudsman operation, Arbitration procedure as well as Private claim redressal & closing communication gap with solicitation should be well addressed. So, there is an increasing need to train the insurance agents

along with effective day to day monitoring & operation of BIMA SUGAM portal with a one-stop destination for all insurance needs, providing services like buying insurance policies, portability facilities, change of insurance agents and settling of claims[3].

