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A. Purpose/Requirements for Purchase - Credit life insurance is a policy issued on the life of a borrower with the creditor named as beneficiary to cover the **repayment of a loan** in the event the borrower dies before the loan has been repaid. It will pay death benefits whether death occurs accidentally or by natural causes. *Credit insurance may be written as an individual policy covering a single debtor, or it can be sold to a master policy owner on a group basis to cover more than one debtor.*

- ***The death proceeds or face amount of the policy may not exceed the indebtedness at the time of death.***
- All credit insurance must be evidenced by an individual policy, or in the case of group insurance, be a certificate of insurance*.* **It is the responsibility of the insurer that these policies or certificates are provided to the debtor and *must be delivered to the debtor within 30 days upon acceptance of the insurance by the insurance company.***

There are four main types of credit insurance:

- **Credit Life Insurance**: Pays off all or some of the loan if you die during the term of coverage.
- **Credit Disability Insurance**: Also known as credit accident and health insurance, it pays a limited number of monthly payments on a specific loan if you become ill or injured and cannot work during the term of coverage.
- **Credit Involuntary Unemployment Insurance**: Also known as involuntary loss of income insurance, it pays a specified number of monthly loan payments if you lose your job due to no fault of your own, such as a layoff, during the term of coverage.
- **Credit Property Insurance**: Protects personal property used to secure the loan if destroyed by events like theft, accident or natural disasters during the term of coverage. Unlike the first three credit insurance products, credit property insurance is not directly related to an event affecting your ability to repay your debt.

TERMS AND CONCEPTS

1. Incontestability Clause states that after a credit policy has been in force for over two years, the insurance company cannot contest or void the policy except for **nonpayment** of premium. If there is a misrepresentation or concealment discovered in the first two years, it must be ***material*** for the insurance company to deny coverage or to cancel the policy.

Material means that it is a fact that is important enough that had the insurance company known it, it could have changed either the decision to issue the insurance policy, or to issue the policy on ***substantially different terms***. The misstated information is said to be material only if the truth would have resulted in the insurer making a different underwriting decision (i.e., rate–up or a surcharge or declining coverage completely).

The insurance company must ***return all of the premiums*** paid if a policy is denied due to material misrepresentation or material concealment within the first 2 years. After 2 years the full policy benefit is paid. This protects the consumer by limiting the discovery period to 2 years.

2. Types of Risk

Types of Risk is the uncertainty of a loss (specifically, financial loss). Risk could also mean the person or thing insured. Only ***pure risk*** is insurable (the chance of a loss, no gain). With a ***speculative risk*** there is chance of gain as well as a chance of loss. However, a *speculative risk is not insurable* (i.e., investments). **Types of risks include**:

Standard risk - A risk that meets the same conditions of health, physical condition and morals as the tabular risks on which the rate is based without extra rating or special restrictions.

Impaired or Substandard risk -A person whose mortality risk is greater than average for his or her age. Substandard rating factors include various medical conditions such as diabetes, hypertension, and heart ailments; high risk occupations such as loggers.

Preferred risk -A person whose physical condition, occupation, mode of living, and other characteristics indicate an above-average life expectancy and, therefore, who qualifies for a premium rate less than that offered to standard risks.

3. Risk

A. Methods of Handling Risk:

Risk is the potential for or possibility of loss. We face risk every day in our lives whether as quick as 'will the light stay green? Can I make it through? Or as simple as 'is this too hot? At times the risks can be costly. There are many studies on how to deal with, work with, or manage risk, specifically, the financial burden that risk can place on our wallet.

**** STARR: Share, Transfer, Avoid, Retain, Reduce (acronyms may help you remember)**

There are five basic tools of risk management:

i. **Share** (with another entity) –An example of sharing is the fence between my neighbor's house and mine If the wind blows it down, we will share the cost of rebuilding it.

ii. **Transfer** The risk is transferred to another. The party assuming the risk (usually an insurance company) will collect premium from a large number of clients in order to pay for any losses.

iii. **Avoidance**– Watch for and avoid any potential risk. You don't want to be in a car accident, never get into a car. This will work, but it is really not feasible for most people. So perhaps avoid hazardous driving conditions.

iv. **Retention** You pay for any losses. This is fairly common for small losses that may occur every day. You drop a cup and it breaks, that is a loss; you replace it, that is retention. A high deductible could also be considered retention; I pay for the first portion of any expenses covered by insurance.

v. **Reduction and Loss Prevention** – Wear a seatbelt, don't text while driving, annual wellness exams, flu shots and fire detectors, to numbered tags in a dressing room. These items will reduce the chance of a loss.

B. Elements of Insurable Risk

Elements of Insurable Risk: In order for an insurance company to take on any risk, there are certain criteria that need to be met. Not all risks are insurable.

**** Calm Chap: Catastrophic, Large, Measurable, Chance, Predictable**

a) The loss **cannot be *Catastrophic***. This means not catastrophic to the insurance company, not the consumer. The cost of natural disasters such as flood or hurricane must be within the carrier's ability to pay claims.

b) The loss **exposures must be *Large*.** Utilizing the law of large numbers, insurance companies can predict the number of losses and, with that information; they can establish a premium.

c) The loss must be definite and ***Measurable***; we must be able to tell when a loss has occurred and place a value on the loss. e.g.: Bills or receipts for repair.

d) The loss must be due to ***Chance*,** not something that is certain to happen.

e) The loss must be ***Predictable***, meaning it must be of such a nature that its frequency and average severity can be readily determined to establish the required premium.

- *How do predictability and chance both work together? Your insurance company knows how many house fires will happen in your zip code this year based on past experience; that is predictable. They do not know which houses will suffer a loss; that is chance.*

C. Definitions

i. **Risk** – is the uncertainty of a loss, specifically, a financial loss. Only pure risk is insurable (the chance of a loss, no gain). With a speculative risk, there is a chance of gain as well as a chance of loss. However, a speculative risk is not insurable.

ii. **Hazard** – Something that increases the chance of a loss. This can be hazardous hobbies, such as skydiving or SCUBA diving. This could be overgrown bushes in front of windows on a house or flammable materials left next to an open flame.

a. **Physical** – Dirty windshields, broken headlights, exposed wiring, or severely worn car tires.

b. **Morale** – Carelessness of attitude or irresponsibility. This would include failing to lock the front door of a house because any loss would be covered by insurance. A careless person is a morale hazard.

c. **Moral** – Arises from people's habits and values… Dishonesty. Examples of poor moral risks include: intentionally setting a fire in order to collect the insurance, filing false claims, excessive speeding tickets, or poor credit report. A dishonest person is a moral hazard.

d. **Legal** – Arises from court actions which increase the likelihood or size of the loss. For example, the growing tendency of people to file lawsuits and claim enormous sums for alleged damages.

iii. **Peril** – is anything that causes a loss. For example, a wet floor is a hazard, slipping on the floor and falling is a peril.

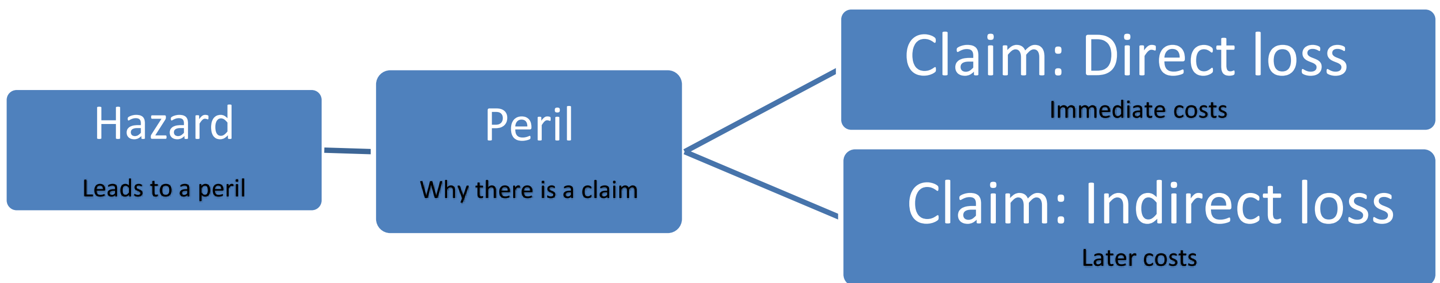
iv. **Direct Loss** – A loss that is a direct consequence of a particular peril. Fire damage to an apartment building is an example of a direct loss.

v. **Indirect Loss** – A loss that is a result of a covered peril but is not caused directly and immediately by that peril. Loss of an apartment building by fire is a direct loss. The loss of rental income as a result of the fire is an indirect loss.

vi. **Proof of Loss** – This is a form completed by the claimant listing the property that has been either lost or damaged due to a covered loss.

**Work a scenario backwards to determine which item is a peril, hazard, etc.

**Know the difference between moral and morale hazards. [Drinking (ale) and driving is careless behavior. morale]



For example, an oily rag left near a furnace causes a fire. The oily rag is the hazard, fire is the peril, the immediate damage from the fire is the direct loss, bills that pop up later (hotel to stay at while the damage is being repaired) are an indirect loss.

Or

I sprained my ankle resulting in a doctor visit. The direct loss was the cost of the visit, the reason for the visit was the sore ankle due to a fall. The fall was the peril. Why did I fall? The dog dug a new hole and I stepped in it, the hole in the yard is the hazard.

4. Elements of a Contract

Insurance Contract… Insurance policies are legal contracts and are enforceable by law. The ***Entire Contract Provision*** states the contract consists of the application, the policy and any riders or endorsements. All statements on an application are deemed to be representations, not warranties.

- The 2 parties in an insurance contract are the insurer and the owner. The owner could also be known as the Named Insured or the First Named Insured (for a contract with multiple owners).

In order for the contract to be considered a legal and binding contract the following elements must be in place.

**** CCOAL: Consideration, Competent Parties, Offer, Acceptance, Legal Object**

A. **Offer…** The applicant makes the ***offer*** to the insurance company. Remember, the legal contract is between two parties, the insurer and the insured. One must make the offer, and the other accepts it. Insurance, even though advertised by a company, must be initiated by the client.

B. **Acceptance…** The insurance company ***accepts*** the ***offer*** by issuing the policy. A ***counter-offer*** is made by the insurance company if it issues the policy other than how it was requested. The applicant ***accepts*** the ***counter-offer*** when the additional premium is paid, and the counter-sheet is signed by the owner/applicant (insured).

Note: Offer and Acceptance together constitute an **agreement.** The agreement is meant to create a legal relationship.

C. **Consideration…** Means that something of value must be exchanged by all parties for the contract to be legal. It is the signed and completed application, plus the premium from the insured. If there is no application, the company does not know what policy you need. The insurance company issues a contract (policy) that represents a promise to pay.

This consideration date is usually the effective date of coverage. The company has the consumers money and signatures and the consumer has the policy or the promise of (binder). The only time you can have coverage without consideration is a verbal binder.

D. **Legal Object…** In order for a contract to be legal, it must be for legal purposes only. This is why *insurance contracts do not cover intentional or criminal acts of the insured,* why there must be insurable interest and why stolen property cannot be insured. A contract to commit a crime is not legal and cannot be upheld in a court of law.

E. **Competent Parties…** The insured must be of legal age, not be under the influence of intoxicants and not be mentally handicapped. Any person 18 years of age or older will be considered of full legal age and may contract for or with respect to insurance. A person under 18 years old will be considered a minor.

- Consent must be freely given in order to enter into the contract.
- The meaning of the contract must be certain
- The contract must be possible. If the act is impossible or illegal the contract is void.

5. Insurable Interest --Loss that would be sustained on death or disability of another, or loss of property sufficient to warrant compensation. ***Indebtedness or financial interest is considered insurable interest for the creditor and debtor.*** Insurable interest is necessary for purchasing insurance. It is an emotional (i.e., spouse) or financial (i.e., business partners or a loan with a bank) tie between two or more people.

Life and Health Insurance = Insurable interest must exist at the time of the policy.

6. Suicide Clause – An insurer may exclude coverage for suicide occurring **within *one year*** after the effective date of the coverage. On an open-ended transaction, an insurer may apply **a new suicide exclusion period** to the portion of a new advance or charge that causes the amount of credit life insurance to exceed the greatest amount previously subject to this exclusion.

7. Transferability (a.k.a. *assignment*) - The insurance company can transfer the insured's interest in an existing policy. For example, the insured can request a change be made but **only** the insurance company can make the change.

8. Creditor – the party to whom money is owned. This may be an individual, a bank, a mortgage company, etc. The lender of money or vendor or lessor of goods, services, properties, rights or privileges, for which payment is arranged through a credit transaction.

9. Debtor - a borrower of money or a purchaser or lessee of goods, services, properties, rights, or privileges for which payment is arranged through a creditor.

10. Indebtedness - the total amount payable by a debtor to a creditor in connection with the loan or other credit transaction. The initial amount of credit life insurance under an individual policy may not exceed the total amount repayable under the contract of indebtedness.

11. Credit Life Insurance means insurance on the life of a debtor in connection with a specific loan or other credit transaction. Credit life insurance is a policy issued on the life of a borrower with the creditor named as beneficiary to cover the repayment of a loan in the event the borrower dies before the loan has been repaid.

Credit life insurance will pay death benefits whether death occurs accidentally or by natural causes. ***The proceeds or face amount of the policy may not exceed the indebtedness at the time of death.***

Under Washington law, all credit insurance must be evidenced by an **individual policy**, or in the case of group insurance, be a **certificate of insurance**. **It is the responsibility of the insurance company that these policies or certificates are provided to the debtor.**

The *certificates must be delivered to the debtor within 30 days upon acceptance of the insurance by the insurance company.*

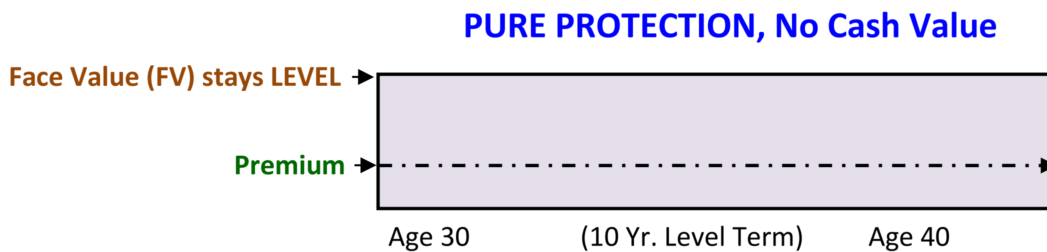
A. **Term Life Insurance** (a.k.a. Pure Protection) is the least expensive of all life contracts. It provides protection for a limited number of years (a term), the face amount being payable upon the death of the insured and nothing in case of survival. The two principal characteristics of term life insurance are: 1) the insured must die for any payments to be made; and 2) by definition at the end of the term the contract expires. There will be an option to renew or convert in most term policies. Any death benefit over the amount owed goes to the individuals estate.

Term policies can be annual renewable term, 5 year term, 10 year term , etc., usually in 5 year increments. The cost of the insurance is based on age at time of application or renewal ,it is very

inexpensive when a person is younger. As you age though, the cost goes up accordingly so it can be unaffordable after age 65.

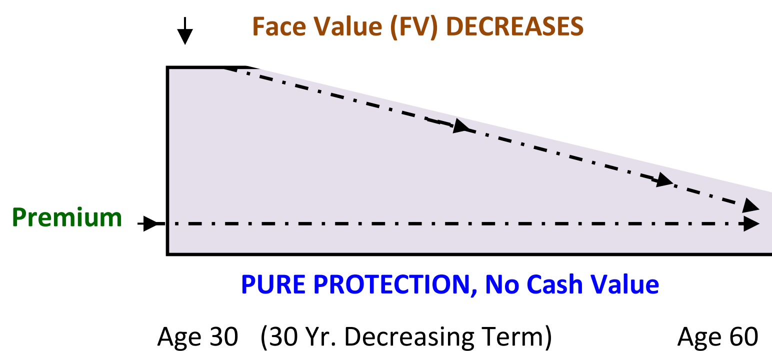
Basic Types of Term Contracts:

i. **Level Term** provides protection that remains constant for the term of the contract. The premiums may increase upon renewal due to an increase in the insured's age. For example, the premium on a five-year term policy will be level for 5 years, but premiums will increase should the policy be renewed due to the fact that the insured is now 5 years older, then they will remain level for 5 years.



ii. **Decreasing Term** provides protection which decreases each year. *The most common use for decreasing term is to cover needs that will decrease over time, such as mortgages and other loans.* The premiums stay level, meaning the premium paid remains the same throughout the life of the contract.

Credit Life Decreasing Term policies are intended to pay off a specific debt if the borrower dies before it is paid. There is a term policy that matched the loan length



iii. **Group term** Is generally what credit life or credit disability actually is.

In order to purchase a group policy you must be part of the group, and you purchase the coverage at the time of the loan. You cannot be required to buy it. Because it is a group plan the underwriting is less stringent than an individual policy, if there is any underwriting done. Rates are the same for everyone covered by the insurance. A consumer applies for coverage through the bank or lender. It is a policy owned by the creditor and the individual insured does not receive a policy, rather they get a certificate of insurance.

Most group plans prohibit the policy owner from being named as the beneficiary. That is the sole purpose of credit plans, to pay off debt and leave an estate intact.

A life insurance policy pays a death benefit to the insureds beneficiaries or estate. Credit life pays the benefit directly to a creditor. A person may have multiple credit life policies as they only pay ONE creditor

12. Credit Accident and Health (Disability) Insurance is insurance on a debtor in favor of a lender intended to make monthly payments on a loan or to pay off the loan balance if the insured becomes disabled or dies accidentally as defined in the policy. Credit insurance may be written as an individual policy covering a single debtor, or it can be sold to a master policy owner on a group basis to cover more than one debtor.

The certificate of insurance for group insurance must be delivered within 30 days.

This policy is similar to a disability income policy in that there is a waiting period before benefits begin and the insured must meet the definition of disability in the policy. The money is paid to to the creditor rather than the insured to make the minimum payments until the insured is able to go back to work or the debt is paid.

The definition of total disability… This definition will vary from policy to policy. The definition is important because it will determine whether the insured is totally disabled and thus eligible for benefits.

Own Occupation… The most protective of your needs is the *own occupation* definition for disability. ***Total disability*** means that you are unable to perform the important duties of your "own" or "regular" occupation, and you are under the regular and personal care of a physician. *For example, if a surgeon is unable to perform surgery, but can still be a doctor, the insurer* ***still must pay*** *the entire benefit.* **With an own occupation definition, it is easier to qualify for being disabled than the any occupation definition**.

Any Occupation is the insured's inability to perform any occupation for which the insured is **reasonably suited** by education, training, or experience. **With an any occupation definition it is harder to qualify for being disabled than the own occupation definition**.

Combinations of the above definitions are common. Since the "Own Occupation" definition is less restrictive, it is more desired by an insured; however, the cost is more expensive. Some policies will have a two-year Own Occupation and thereafter have an Any Occupation provision, thus lowering the premium.

A disability income policy pays an income to the insured if or when disabled, Credit disability pays directly to ONE creditor. An insured may have multiple policies to cover multiple debts.

13. Credit Transaction means an agreement to:

Repay money loaned, Pay for a loan commitment made, Pay for goods, services, or property sold or leased

A credit transaction is a transaction made i.e. payment for goods, with the payment being made by a third party (e.g. VISA) with the promise of repayment in periodic payments made by the consumer to the bank along with the interest is charges.

14. Other Terms

- ✓ An **Affiliate** of, or person "affiliated" with a specific person, is a person who directly or indirectly through one or more intermediaries, controls or is controlled by the person specified.

- ✓ **Average number of life years** means the average number of group certificates or individual policies in force during the experience period times the number of years in the experience period.

- ✓ **Case** includes either a single account case or a multiple account case.

- ✓ **Closed-end Credit** means a loan or extension of credit in which the proceeds are dispersed in full when the loan closes and must be repaid, including any interest and finance charges, by a specified date. The loan may require periodic principal and interest payments, or may require the entire payment of principal at maturity.

- ✓ In this type of loan or credit arrangement, the full amount owed must be paid back by the borrower by a set point in time. Most real estate and auto loans are closed-end credit, while credit cards and home-equity lines of credit are open-end or revolving lines of credit.

- ✓ **Compensation** means any form of payment which results directly from the sale of consumer credit insurance, including:

  (a) Commissions
  (b) Dividends
  (c) Equipment
  (d) Expense allowances or reimbursements
  (e) Experience refunds
  (f) Facilities
  (g) Gifts
  (h) Goods/services

(i) Retrospective rate credits
(j) Service fees

- ✓ **Consumer credit insurance** means credit life insurance or credit accident and health insurance.

- ✓ **Control** means possession, direct or indirect, of the power to direct or cause the direction of the management and policies of a person.

- ✓ **Credibility table** is used for purposes of the standard case rating procedure. An insurer may file rates that are equivalent to the prima facie rates and use those rates without further proof of their reasonableness. However, an insurer must file rates and supporting actuarial documentation if it proposes policy provisions more restrictive than those allowed for prima facie rates or rates higher than those developed according to the standard case rating procedure.

- ✓ **Credit Casualty license** -issued to people or companies who sell insurance covering mortgaged property (such as motor vehicles). Also known as “collateral protection coverage” or “vendor single-interest” insurance. To get this license an individual must pass the Credit Casualty exam.

- ✓ **Credit Life Transaction;** a transaction between a lender and a borrower where the borrower agrees to repay a loan over a period of time subject to minimum a repayment schedule.

- ✓ **Earned premium** means the total gross premiums that become due to the insurance company for insurance coverage. The insurer may reduce earned premium only for refunds due to termination of coverage. The unearned premium is calculated according to the specified refund formula.

- ✓ **Evidence of individual insurability** means a statement furnished by the debtor related to:

    - **The health status, health or medical history of the debtor**.

    - The occupation of the debtor.

    - **Other conditions for the insurance to take effect. Evidence of individual insurability does not include information related to the eligibility of the debtor for coverage.**

- ✓ **Exclusions** - Credit accident and health insurance policies may elect to include age restrictions on people age 66 and older and may end when a person reaches age 66.
  - The insurer may exclude benefits for disabilities that result from elective surgery or a preexisting condition that begins at least six months before the effective date.
  - Also excluded can be injuries or death due to suicide within 1 year, war or any act of war or intentionally self-inflicted injury, or from flight in any aircraft other than a commercial scheduled aircraft.
  - For example, death that results from flying on Alaska airlines is NOT excluded, however, death while flying your own single engine airplane ***is excluded***.
  - All premiums paid are refunded (no interest is required) if a claim is denied or a policy is canceled during the first two years.

- ✓ **Open-End Credit...** A pre-approved loan between a financial institution and borrower that may be used repeatedly up to a certain limit and can subsequently be paid back prior to payments coming due. The pre-approved amount will be set out in the agreement between the lender and the borrower.
  - Open-end credit is also referred to as a "line of credit" or "revolving line of credit".
  - Open-end credit agreements are advantageous to borrowers, as they exert more control over how much they borrow and when. In addition, interest is not usually charged on the part of the line of credit that is not used, which can lead to interest savings for the borrower.
  - Most real estate and auto loans are closed-end credit, while credit cards and home-equity lines of credit are open-end or revolving lines of credit.

- ✓ **Preexisting condition (for credit insurance)** means any condition for which the insured debtor received medical advice, consultation, or treatment within six months before the insurance takes effect.

- ✓ **Premium** means all forms of compensation, including all sums charged, received, or deposited as consideration for an insurance contract or the continuance thereof. Any assessment, or any membership, policy, survey, inspection, service or similar fee or charge made by the insurer in consideration for an insurance contract is deemed part of the premium.

- ✓ **Rights of Debtors...** A debtor has **the right to know about all available credit insurance plans and to provide his own insurance from existing policies** or not to provide insurance

at all. If the policy is a group policy that ends, the insurer must continue coverage for the entire period for which a premium has been paid. **The insurer must provide termination notice to the insured debtor at least thirty days before coverage ends.**

- ✓ **Underwriting** means applying criteria under which the insurer: Issues or refuses to issue; Renews or refuses to renew; and/or Limits coverage. Underwriting also includes decisions by the insurer based on eligibility criteria or evidence of individual insurability.