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Chapter 3

Contract Vocabulary

Any & all contracts must include the following:
- **Consideration:** the values exchanged
  - **Company –** their promise to pay
  - **Policy owner –** completed application & premium
- **Legal Purpose**
- **Offer & Acceptance –** Policy owner makes offer with consideration
- **Competent Parties –**

Absent any of the above = Void contract; w/o legal affect

The following are only found in insurance contracts, they are unique to insurance.

Aleatory
- There exists an element of chance
- The dollar values exchanged are unequal

Adhesion
- A non-negotiated contract; **take it or leave it;**

Unilateral
- Only one party makes a "promise enforceable by law". The insurance company makes a binding promise, can't get out. The policyowner makes no such promise. Can quit at any time.

Not a Personal Contract
- Ownership of the policy does not increase the risk. The risk is on the insured. Changing ownership does not increase the risk.

Conditional – examples of the conditions:
- If the insured event (death, disability) does not materialize, the company does not pay.
- Policyowner must pay premiums
- Beneficiary must provide proof of death (death certificate)

Valued or Indemnity
- Valued contracts pay a stated amount (life insurance, disability) no more, no less
- Indemnity contracts make the insured whole again, neither gaining nor losing, (Major Medical, homeowners/fire)

Subrogation
- The insurer acquires the right to "go after" the negligent third party when they pay a claim. Ex. Uninsured guy crashes into your car, your company pays, then "goes after" uninsured guy.
- Does not apply to life insurance
- May apply to health insurance

Warranty
- Statements that are guaranteed to be true
- Are "material" to the contract because they affect company's decision to accept the risk
- If a warranty is untrue, the company can cancel the contract

Representations
- Statements the insured believes to be true
- All statements are representations on the application
- Not part of the contract
- If a representati0on is untrue the company can only cancel the contract **IF** the statement was material to the company accepting the risk when the policy was issued

Insurable Interest
- The purpose is to prevent wagering
- Between Policy owner & Insured (potential loss must exist)
- Must exist only at inception
- Everyone has insurable interest in their own life
- If missing, contract unenforceable
- Direct blood; not cousins or aunts/uncles

Stranger Originated Life Insurance (STOLI)
Investor Originated Life Insurance (IOLI)
- Investor loans money to insured to buy life insurance and names investor as beneficiary
- Usually done with senior citizens
- Senior citizens receive up-front cash as incentive
- Prohibited practice in most states (see your law chapter)

Brokers vs Agents
- <u>Agents represent the company</u>
- Brokers represent the buyer
- Both called producers

Professional Liability Insurance
- Errors & omissions insurance
- Similar to what physicians have
- Covers mistakes

Waiver
- Voluntary relinquishment (giving up) of a legal right
- Company cannot later deny a claim because of a violation of that right

Estoppel
- Works with waiver
- If company waives a right, they cannot get that right back

Void/Voidable
- **Void –** without legal affect; never existed; cannot be enforced; premiums returned
- **Voidable – a** contract made be made void.

Fraud
- Can void the contract
- Company has limited time to discover (generally two years)
- After the time limit company can do nothing about it
- Only three exceptions
    1. <u>Intent</u> to murder;   2. <u>Impersonation</u>   **3.** <u>No Insurable interest</u>

Types of authority
- **Expressed;** written in the contract
- **Implied;** not written; boss <u>knows</u> you're doing something and does not <u>say not</u> to do it
- **Apparent;** the appearance of authority; you have biz cards, a rate book etc; clearly obvious

Parol evidence rule - prevents the introduction of evidence of prior negotiations that contradict what is in the written contract. The written contract is enforced, not verbal promises.