



Southwestern Insurance Information Service

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FACT SHEET

THE SEVEN PRINCIPLES OF INSURANCE

1. The assumption of risk is based on the accumulation of homogeneous units.

Companies group various insurance customers into categories where their likelihood of loss best fits others possessing comparable characteristics.

2. There must be a calculable chance of loss based on history.

Insurers develop historical and statistical data which predicts the chance of people having an insured loss. This helps establish fair and equitable insurance rates.

3. A definite and accessible loss must occur which is not easily counterfeited.

Projections of what a claim will cost must be based on an insurer's ability to determine the cost of actual property damage or bodily injury. Insurance fraud costs consumers billions of dollars each year and insurers are continually advancing efforts to fight fraud.

4. The loss must be accidental in nature.

Insurers are in business to compensate the legitimate claims of their customers. Those claims must have taken place as the result of an accident, not manufactured to defraud an insurance company. Fraudulent claims require other customers to subsidize the illegal activity of a few. There is also the issue of a person failing to maintain their property.

Insurance was never intended to pay for routine maintenance of a home or business.

5. A large type of loss means claim dollars to the policyholder.

For Additional Information:

8303 N Mopac, Ste B-231
Austin, TX 78759

Phone: (512) 795-8214
Fax: (512) 795-9363



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The intent of insurance is to pay for large losses that are above and beyond a person's financial means. It is the legitimate role of an insurer to indemnify their customer against catastrophic events.

6. The risk must be economically feasible.

Before an insurer assumes responsibility for paying the claim of a customer, the company must have the financial ability to pay the loss. Having this ability requires insurers to charge an adequate rate. Insurance is provided for situations where there is a risk of loss, not a certainty such as when a hurricane is bearing down on an area, companies do not write new policies for an area which is destined to be affected.

7. Losses must not occur to a large number of customers at the same time.

Insurance is a business of spreading the risk among large groups. If a series of weather-related storms take place over a wide geographic area, the financial consequences for an insurer would not be too serious. But, if a major storm were to strike one city with a high concentration of people, insurer's surplus, similar to a person's savings account, would be severely impacted. Surplus does not mean "extra money." It is set aside to pay claims.

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