UNIT – II

Principles of Insurance Law

Good Faith • Insurable Interest • Indemnity • Contribution • Subrogation • Causa Proxima

SYNOPSIS

Unit Overview

This unit covers the core doctrines that make insurance contracts unique. These principles protect the integrity of the risk-transfer mechanism and prevent moral hazard and wagering.

Topics:

- Uberrimae fidei (utmost good faith) – non-disclosure & misrepresentation
- Insurable interest
- Principle of indemnity (and difference from guarantee)
- Contribution and subrogation
- Loss minimisation and causa proxima
- Premium, days of grace, forfeiture, return of premium and assignment of subject matter

LEARNING OBJECTIVES

What You Will Learn

01 Good Faith

Duty of disclosure and consequences of breach

02 Insurable Interest

When it must exist and why it is required

03 Indemnity

Measure of indemnity and distinction from guarantee

04 Contribution

Sharing of loss among multiple insurers

05 Subrogation

Insurer’s right of recovery after payment

06 Causa Proxima

Proximate cause rule for determining liability

UBER RIMAE FIDEI

Principle of Utmost Good Faith

Every insurance contract is a contract of uberrimae fidei. The proposer must disclose all material facts that would influence a prudent insurer in deciding whether to accept the risk or in fixing the premium.

Material Fact

Any circumstance that would affect the judgment of a prudent insurer on acceptance or rate.

Non-Disclosure

Failure to reveal a material fact, even if not asked, can render the contract voidable.

Misrepresentation

False statement of a material fact, whether innocent or fraudulent.

Consequence

Insurer may avoid the policy from the beginning; claim can be repudiated.

The Requirement of Insurable Interest

Insurable interest is the legal or equitable relationship between the insured and the subject matter of insurance such that the insured benefits from its safety or is prejudiced by its loss.

Life Insurance	Interest must exist at the time the policy is taken. Own life, spouse, children, debtor, etc.
Property / General	Interest must exist at the time of loss. Owner, bailee, mortgagee, consignee, etc.
Purpose	Prevents wagering contracts and moral hazard. Without interest the contract is void.
Indian Position	Section 6 of Marine Insurance Act 1963 and judicial decisions recognise the requirement in all classes of insurance.

PRINCIPLE OF INDEMNITY

Indemnity and Its Limits

Core Idea	The insured should be restored to the same financial position as before the loss — no profit, no loss.
Application	Applies strictly to general (property and liability) insurance. Life and personal accident policies are contracts of fixed benefit, not indemnity.
Measure	Market value, reinstatement value, or agreed value depending on policy terms and type of cover.
Difference from Guarantee	Guarantee is a secondary obligation; indemnity is a primary obligation to make good the loss.
Exceptions	Valued policies, new-for-old covers, and certain agreed-value marine policies modify pure indemnity.
Case Law	Courts consistently refuse to allow the insured to recover more than the actual loss suffered.

Principle of Contribution

When the same subject matter is insured with more than one insurer against the same risk, the insurers must share the loss rateably so that the insured does not recover more than the actual loss.

Conditions

Same subject matter, same interest, same risk, policies in force at the time of loss.

Rateable Proportion

Each insurer contributes in proportion to the sum insured under its policy.

Right of Contribution

An insurer who has paid more than its share can recover the excess from co-insurers.

Policy Condition

Most policies contain a contribution clause that reinforces the common-law principle.

SUBROGATION

Principle of Subrogation

After paying a claim, the insurer steps into the shoes of the insured and can exercise any rights the insured had against third parties responsible for the loss. This prevents the insured from recovering twice.

When it Arises	Only after the insurer has paid the full indemnity (or agreed amount).
Forms	Simple subrogation, subrogation-cum-assignment, and express assignment of rights.
ETO Case (2010)	Supreme Court clarified that the insurer can sue in its own name or in the name of the insured depending on the form used.
Limits	Insurer cannot recover more than it has paid; any surplus belongs to the insured.

CAUSA PROXIMA

Proximate Cause of Loss

The insurer is liable only if the proximate (nearest and dominant) cause of the loss is an insured peril. Remote causes are ignored. The rule is applied with common sense and in the light of the policy wording.

Test

What is the efficient, dominant and operative cause of the loss?

Concurrent Causes

If two causes operate together and one is excluded, the exclusion usually prevails.

Chain of Events

The last cause in time is not necessarily the proximate cause.

Policy Wording

Modern policies often define or modify the proximate-cause rule by express terms.

Premium – Payment, Grace, Forfeiture & Return

Definition	The consideration paid by the insured for the insurer’s promise to cover the risk.
Method of Payment	Cash, cheque, electronic transfer, or as agreed. Payment is a condition precedent to cover in many cases.
Days of Grace	Extra period allowed after the due date during which the policy remains in force if premium is paid.
Forfeiture	Non-payment within the grace period can lead to lapse or forfeiture of the policy.
Return of Premium	Possible on cancellation, avoidance for non-disclosure, or short-period cancellation according to policy terms.
Assignment of Subject Matter	Transfer of the insured property does not automatically transfer the policy; notice and consent are usually required.

LOSS MINIMISATION

Duty to Minimise Loss

The insured has a duty to take all reasonable steps to minimise the loss once the insured event has occurred. This duty is both contractual (often expressed in the policy) and based on the principle of indemnity.

- The insured must act as a prudent uninsured person would act.
- Expenses reasonably incurred in minimising the loss are recoverable from the insurer (sue and labour in marine insurance).
- Failure to take reasonable steps can reduce the amount recoverable or, in extreme cases, lead to repudiation.
- The duty does not require the insured to take extraordinary risks or incur disproportionate expense.

This principle works together with the doctrines of indemnity and causa proxima to keep the insurance mechanism fair and efficient.

LANDMARK CASES

Key Judicial Decisions

Economic Transport Organisation v. Charan Spinning (2010)

Supreme Court clarified the doctrine of subrogation and the different forms it can take under Indian law.

General Assurance Society v. Chandumull Jain

Classic exposition of the nature of insurance and the duty of utmost good faith.

United India Insurance v. Harchand Rai

Interpretation of policy terms; ambiguity resolved against the insurer (contra proferentem).

Castellain v. Preston (English but followed)

Foundational case on the principle of indemnity – insured cannot recover more than the loss.

SALIENT FEATURES

Core Doctrines at a Glance

01 **Utmost Good Faith**
Higher duty of disclosure than ordinary contracts

02 **Insurable Interest**
Essential to validity; prevents wagering

03 **Indemnity**
No profit from loss (general insurance)

04 **Contribution**
Rateable sharing among co-insurers

05 **Subrogation**
Insurer recovers from third-party wrongdoers

06 **Causa Proxima**
Dominant cause determines liability

ESSENTIALS

Must-Know Rules

Good Faith	Material non-disclosure or misrepresentation makes the policy voidable by the insurer.
Interest	Life – at inception; Property – at the time of loss.
Indemnity	Insured cannot recover more than the actual financial loss.
Contribution	Multiple policies → rateable proportion among insurers.
Subrogation	After payment the insurer acquires the insured’s rights against third parties.
Proximate Cause	Only the dominant insured peril triggers liability.

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Inter-relationship of the Principles

The principles operate as a coherent system:

- Utmost good faith ensures the risk is correctly priced and accepted.
- Insurable interest ensures the contract is not a wager.
- Indemnity ensures the insured is compensated but not enriched.
- Contribution and subrogation prevent the insured from recovering twice and allow the ultimate loss to fall on the correct party.
- Causa proxima determines whether the insured event has in fact occurred.
- Loss-minimisation duty keeps the overall cost of insurance under control.

Together they form the doctrinal backbone of insurance law and appear in almost every dispute.

KEY HIGHLIGHTS

Sections & Main Points

Uberrimae Fidei	Material disclosure required; breach → voidable policy
Insurable Interest	Life at inception; property at loss
Indemnity	No profit; life policies are exception
Contribution	Rateable sharing when multiple policies
Subrogation	Insurer steps into insured’s shoes after payment
Causa Proxima	Dominant cause decides liability
Premium	Grace period, forfeiture, return rules
Assignment	Subject-matter transfer needs insurer’s consent

PRACTICAL APPLICATION

How These Principles Appear in Disputes

- Claim repudiation almost always begins with an allegation of non-disclosure or misrepresentation.
- Insurable-interest challenges appear in life and marine cases when the relationship is remote.
- Quantum disputes turn on the measure of indemnity and betterment deductions.
- Contribution claims between insurers are common when the same risk is covered by multiple policies.
- Subrogation actions are the main route for insurers to recover from negligent third parties.
- Proximate-cause arguments decide whether an excluded peril or an insured peril is responsible.

Mastery of these six principles enables accurate analysis of virtually any insurance dispute.

COMPARISON

Indemnity vs Guarantee vs Life Assurance

Aspect	Indemnity	Guarantee	Life Assurance
Nature	Primary obligation	Secondary obligation	Fixed benefit contract
Purpose	Make good actual loss	Secure performance of another	Pay fixed sum on event
Interest	Required at loss	Not the same concept	Required at inception
Measure	Actual loss only	Amount of default	Agreed sum
Subrogation	Yes	Limited	No

SUMMARY POINTS

Must-Remember Points

- Insurance contracts are contracts of utmost good faith — material non-disclosure voids the policy.
- Insurable interest is essential; without it the contract is a wager and void.
- Indemnity restores the insured to the pre-loss position; life policies are fixed-benefit contracts.
- Contribution ensures rateable sharing among co-insurers.
- Subrogation allows the insurer to recover from third parties after payment (ETO case).
- Causa proxima (proximate cause) decides whether the insurer is liable.
- Premium rules, grace periods and assignment of subject matter complete the contractual picture.

SUMMARY

Key Takeaways

1. The six core principles form the doctrinal foundation of insurance law.
2. Utmost good faith and insurable interest protect the integrity of the risk-transfer system.
3. Indemnity, contribution and subrogation prevent unjust enrichment of the insured.
4. Causa proxima provides the causal test for liability.
5. These principles appear in almost every insurance dispute and statute.

Next Unit: Life Insurance, Motor Insurance and related statutory frameworks.