# Revisiting Motor - Liability Insurance: The Indian Context

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*Motor- Liability Insurance or third-party liability cover is an insurance policy that covers the insured's legal liability for death or disability to a third-party or damage to the third-party property. Evolving automobile sector and the dynamic consumer preferences in the Indian markets call for the need to analyze the existing practices in the Motor-liability insurance in the market and adapt them according to the changing scenario. The article addresses the problems with the existing practices and makes a few suggestions for adapting the liability insurance for the evolving market.*

*Keywords: Dynamic Consumer Preferences, Insurance, Motor-Liability insurance, Policy, Pricing.*

## I. Introduction

Motor-Liability insurance or third-party liability cover is an insurance policy that covers the insured's legal liability for death or disability of third-party loss or damage to the third-party property. It is referred to as 'third-party' cover since the beneficiary of the policy is someone other than the two parties involved in the insurance contract (the car owner and the insurance company). Unlike the other insurance products available in the market, it is a statutory requirement under the Motor Vehicle Act.[1] The law mandates that every vehicle plying on the road has to have a valid third-party insurance. Since the third-party insurance cover is mandatory, all general insurance providers are obligated to provide this cover. This paper analyses the current practices and features of the third-party insurance in the India to understand how the existing systems can be detrimental for the growing automobile sector and changing market scenario mainly due to the changing consumer preferences and the recent policy changes.

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## II. Background of the Third-Party Insurance

Like the introduction of the formal insurance, the credit for introducing the third liability insurance can also be credited to England. Before 1930, third party insurance was not mandated by law. However, with the rise of industrialization and the automobile sector, cases of accidents were on the increase. As and when an accident took place, the injured used to take actions against the vehicle owner for compensation. However, most often, in such cases, it turned out that the owner was unable to compensate the injured or deceased as he had no means to give out the required compensation. Under these circumstances, the 'Third Parties' Rights Against Insurance Act, 1930,' was enacted, which made the third party liability insurance compulsory for motor vehicles.

Further, in 1939 Motor Vehicle Act was enacted in India for the first time under the British Rule, which inculcated compulsory third party vehicle insurance in the country for every motor vehicle plying on the road. This provision gave the right to the third party to approach the insurer directly for any compensation in case of any accidental injury, life loss, or damage caused by vehicle holding a valid a Third-Party insurance. Later, after independence, this provision of the 1939 Act was engrafted into the Motor Vehicle Act, 1988, by the Indian Parliament. Since the Act mandates this particular insurance, third-party insurance is called 'Act Only' cover. Thus the tradition of insuring a motor vehicle for third party insurance continues to date.

Early days after the nationalization of the insurance companies, third-party insurance covers were provided by the four public sector insurance companies. Later, when the market opened up for private players, it was made mandatory for all the general insurance companies to provide 'third party insurance cover.[2]

Like India, in most countries of the world, it is compulsory by law to have the vehicle insured against third-party liabilities even though the implementation differs from country to country. Some countries, like the US and Australia relate third-party insurance to both vehicles and driver characteristics while in others it depends on the vehicle type and other features of the vehicle. Also, in certain countries like, Bangladesh, limits of the liability is fixed while others are not. Unlike the common practice of mandating the vehicle owners to insure their vehicle against third-party liability, countries, like New Zealand, South Africa, compensate in case of a road accident from a common pool of fund collected through levies on petrol and through vehicle licensing fee.[3]

In the following section, certain notable features of the third-party insurance in India are discussed.

## III. Important Features of Third-Party Insurance in India

Some of the notable features of the third party insurance are as follows:

1. Each third-party insurance is linked to a vehicle and not the owner of the vehicle or person driving the vehicle. If the owner decides to sell the vehicle, then linked-insurance is also transferred along with the vehicle to buyer.
2. The parties involved in the insurance contract are the insurers and the registered owner of the vehicle (insured). Thus, it is the responsibility of the registered owner to make sure that the vehicle has a valid insurance.
3. The beneficiary of the third-party insurance is someone else other than the parties involved in the contract. The insurance cover gives the right to third-party persons involved in a motor vehicle accident to approach the insurer for any loss or injury caused by the vehicle holding a valid insurance cover.
4. An insurance premium is a specified amount which the insured needs to pay to maintain the insurance cover. It is a reflection of the probability of any claim and extent of the claim amount, which can arise during the coverage period. Hence, in practice, the risk of claim occurrence is directly proportional to the premium charged by the insurer on an individual basis. However, the premium for a third party insurance policy is fixed and revised annually by the regulatory authority based on the type of the vehicle.[4] For example, for two-wheelers and Light Motor Vehicles (LMVs), the premium is based on the cubic capacity of the vehicle, while for Goods-carrying vehicles, the premium is based on the gross weight of the vehicle. Thus, while pricing the insurance policy, many risks associated with driver characteristics and driving behavior, which play a significant part in any road accident are ignored.
5. The extent of the liability in a third party insurance policy is unknown to the insurer, unlike the other insurance products.[4] The liability is determined on a case-to-case basis by the legal authority, based on the earning capacity of the third party person involved and the extent of the damage caused. There is no limit to the liability of the insurer under third-party insurance cover. Compensation is also determined by the legal authority based on the extent of the damage caused and the earning capacity of the third party. As the number of vehicles plying has increased tremendously in the past decades and the number third-party claims have also increased drastically.

## IV. Changing trends in the Automobile Sector and Third Party Insurance

Over the past decades, there had been significant changes in the automobile market. India is expected to grow into the third-largest passenger vehicle market by 2021.[5] This section overviews the significant changes in the automobile market, which has occurred over the years and how the changing trends demand the change in the traditional practices in the third-party insurance. The section also describes how specific features of the existing liability insurance can negatively affect the automobile market scenario and in turn, affect the economy.

1. **Dynamic regulatory environment**: Even though India is traditionally looked upon as a manufacturing center by the major automobile players, the recent adoption of specific regulatory policies in the market is directly impacting the cost of manufacturing and in turn, the cost of the vehicle. Major regulatory interventions recently proposed are:

   a) Adoption of BS-VI norms in India by 2020 for all new four-wheelers.

   b) Change in the Tax structure - the introduction of GST.

   c) Adoption of safety standards in line with the international norms.

   d) Implementation of Corporate Average Fuel Efficiency norms under which manufacturers need to improve the fuel efficiency of the vehicles by 10% between 2017 and 2021 and 30% or more by 2022.

   The adoption of these measures is leading to a need for the manufacturers to shift in vehicular technology, which is demanding significant investment in developing various technical requirements that are relevant for changing the production process. Hence, these changes are drastically increasing the cost of production of the vehicles.

2. **Emerging Mobility-as-a-Service (MaaS) Landscape**: Increased penetration of digital technology in India has enabled the emergence of shared mobility markets like e-hailing taxis, self-drive-car rentals, vehicle pooling. These technology-enabled mobility solutions are enabling rapid growth in India. These shared mobility platforms are giving cheaper and affordable travel solutions to the people. Readily available mobility solutions are incentivizing consumers to depend on such mobility shared options rather than buying a personal vehicle. Even though the growth of MaaS solutions had been limited to Tier 1 cities in India, rapid urbanization of Tier 2/3 cities in the days to come gives scope for more growth in MaaS.[6]

3. **Mandatory Long-Term Liability Cover for Vehicles**: A new regulatory measure proposed mandates the vehicle owners to purchase a long term Third-party insurance cover for three years for a newly purchased vehicle, unlike the usual cover period of one year. These measures have given rise to a steep increase in the initial cost of purchasing a new vehicle.[6]

Thus, the changing regulatory environment combined with affordable MaaS solutions is bringing in a shift in consumer preferences for owning a vehicle. As discussed, the prevailing system of third-party insurance scheme burdens the vehicle owners with the responsibility for getting the vehicle covered against any legal liability even if the vehicle is used by someone else. Thus, the current system fails to incentivize the person behind the wheels to adopt responsible driving behavior as he is assured that the legal liability arising from any accident will be taken care of by the insurer or the vehicle owner. The rapidly changing automobile sector scenario is expected to create a pool of drivers and cars for rentals in the market, rather than vehicle owners. Furthermore, the evolving MaaS gives a scope of more entrepreneurial opportunities for buying vehicles and leasing out for adding into the MaaS pool. However, the existing third-party insurance scheme adds to the cost of doing such businesses. Besides, it burdens the investor with the responsibility of third-party damages caused by the vehicle. Thus, the existing insurance practices demotivate such entrepreneurial ventures, which create more employment opportunities in the changing scenario. This transformation in the mobility space calls for the need to re-examine the current third-party insurance practice currently prevailing in the market. Additionally, there is a strong need for devising a third-party insurance scheme, which makes this pool of drivers more responsible on the road.

The following section provides some suggestions for improvising the existing third-party insurance scheme for making it more effective for the dynamic automobile landscape.[7]

## V. Driving License-Linked Liability Cover

As discussed, more often, vehicle accidents are associated with driving behavior, and the extent of the damages depends considerably on the driver's presence of mind in handling the incriminating circumstances. The drivers play an essential role in any vehicle accidents and damage caused. Thus, linking the third-party liability with the driver is a promising scheme covering the risk involved in legal liability arising from vehicle accidents. The following are the key points for the proposed third-party liability scheme.

1. Instead of insuring each vehicle against any legal liability towards any third-party accidental damage, each driving license can be insured against any legal liability. Logically, there are more licensed drivers in the country compared to vehicles on the road. Hence, an insurance cover against driver's license creates a more extensive insurance pool compared to the insurance pool generated by the existing vehicle-linked third-party insurance, which can help in compensating any legal liability case.
2. Each Driver's license can be insured for its validity period and made to renew it in case the license is to be renewed. The consumers can be given the option of paying the premium in one shot while getting a license or paying the premium in installments so that users are not burdened by a considerable premium for the long-term cover. At the same time, devising a long-term cover, which lasts till the validity of the license period, ensures that there is no break in the cover, unlike the current practice.
3. The premium for the cover can be devised based on the driver's characteristics, like age of the driver, health conditions of the person, and so forth, which add to various risks while on the road. The rapid digitization and the integration of the existing records can help in recording traffic violations by each driver on the road. Furthermore, such information regarding each person can also be used for determining the premium and devising-premium based incentivizing scheme to make the drivers more careful and respect the traffic rules.
4. For the consumers choosing to pay the premium in installments, a discount in premium installment, based on the driver's previous claim records can be considered. Such systems can also incentivize people to drive more carefully on the roads.
5. As per the current system, a private driving license has a validity of 20 years, while commercial driving has a validity period of 3 years only. Having a liability cover linked with a license for the entire validity period can ensure that there will not be any break in the cover for the entire period.
6. If the proposed liability cover is designed to be an endowment plan for these long periods, where the insured is assured of a return after the cover gets expired with no claim for the entire period, then consumers will be motivated to maintain the liability cover. Thus, the investing nature of the consumers can be harnessed for making the drivers more responsible on the road and towards society.

Identifying the driver responsible for driving the vehicle in the case of an accident is quite important in order to avoid the false accusation against any licensed driver and the claim settlement from his license-linked policy. Even though, currently India lacks proper databases or recording systems to identify the driver in case of an accident, the emerging car-rental services, and other emerging M-a-a-S gives scope of a robust database with the driver details. For example, the taxi service providers like Ola and Uber keep details of the driver of the vehicle registered with them. Additionally, the budding AI and big data analytics scenario provide the hope of having better technologies for recording the real-time functioning of the vehicle on the road and help identify the driver.

Laws and policies can become obsolete, if proper amendments and measures are not taken to accommodate changes in society. So a regular up-gradation of the policies and law is an essential measure for a dynamical society. Growing mobility market demands to review the existing policies regarding third-party insurance policies. A meticulously designed driver- license linked liability cover is a promising strategy for better implementation of the liability coverage in the changing mobility scenario and by adapting such a policy can set an example for the other countries in the world.

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