

GLOSSARY

Adverse selection: A situation in which the insured has more information about his or her risk of loss than does the insurance provider and is better able to determine the soundness of premium rates. As a consequence, the level of risk in the insured population is higher than in the total population (Harwood et al 1999a).

Agricultural production contract is a contract by which a producer (sometimes called a "grower") agrees to sell or deliver all of a designated crop raised in a manner set forth in the agreement to a contractor and is paid according to a formula established in the contract.

Asymmetric information: relates to the problem that the buyer of insurance and the insurance company may not have the same information as regards the probability of losses occurring. Asymmetric information refers to one or both of these problems: Adverse selection and moral hazard.

Blanket insurance: A single insurance policy that covers one or more broad classes of persons or property, without identifying the specific subjects of insurance in the contract.

Bonus/malus: Premium discounts/charges when over a certain period of time no claims/claims are made.

Co-insurance or coinsurance: An insurance policy provision under which the insurer and the insured share costs incurred after the deductible is met, according to a specific formula. More generally it consists in a sharing of risk between the insurer and the insured. It can also refer to the case where a number of different insurers subscribe to a single insurance policy.

Consequential losses due to an animal disease: In insurance contracts, consequential losses are indirect losses, a reduction in the value of property that is a result of a direct damage loss. Usually are associated with a time element, or to other remote or indemnification type losses. Consequential losses are different than ensuing losses since consequential losses are indirect losses not direct damage losses, whereas ensuing losses are further or additional direct damage losses that have been initiated by the original direct damage cause of loss.

Co-reinsurance: A requirement that the reinsured bears, in addition to the deductible, a portion of the coverage under the treaty un-reinsured and for its own account. It intends to ensure that the reinsured retains an interest in loss minimisation even after the deductible has been exceeded.

Cumulative loss ratio: means the ratio of total indemnities to total earned premiums during the base period expressed as a decimal.

Deductible or excess (French: *Franchise*): The portion of an insured loss to be borne by the insured before he is entitled to recovery from the insurer. It may be in the form of an amount of euros, a percent of the value of the insured property (**straight deductible**) or a percent of the loss (**relative deductible**). // In a policy providing a deductible clause, the amount which must first be subtracted from the total damage incurred before determining the insurance company's liability. There are several types used.

Direct losses due to animal disease: Direct financial loss due to mortality or morbidity of livestock or crop plants can vary from insignificant to catastrophic. In many cases the direct losses would be modest and would fall on a small number of farms. One of the major determinants of the magnitude of the direct losses will be the rapidity with which the disease is noticed and diagnosed.

Disappearing deductible: Establishes the insurer's liability for an increasing proportion of the loss, as the total damage rises above the deductible, until the deductible finally "disappears". Then the insurer is liable for the entire amount.

Franchise or franchise deductible: Deductible in which the insurer has no liability if the loss is under a certain amount, but once this amount is exceeded, the entire amount is paid in full. Deductible below which nothing is payable and beyond which the entire amount of the sum insured is payable. The franchise deductible establishes the insurer's liability for the entire amount of damage once the deductible amount is exceeded in a loss.

Insurance policy: A contract of insurance, describing the term, coverage, premiums and deductibles.

Loss ratio: Ratio of the annual claims paid by an insurance company to the premiums received expressed as a decimal.

Moral hazard: In the case of insurance, moral hazard refers to an individual's change in behaviour after having taken out an insurance policy. The change in behaviour results in an increase in the potential magnitude and/or probability of a loss.

Tools insurance companies generally use to minimise moral hazard include:

- Deductibles or co-payments (the insured has to bear part of the loss: a fixed amount or a percentage of the total loss);
- No-claim bonuses (see bonus/malus);
- Checks to verify whether the insured takes the precautionary measures agreed upon to prevent losses;
- Indemnification based on an objective index which cannot be influenced by the insured.

On Spot Market it's a market in which commodities, such as grain, gold, crude oil, are bought and sold for cash and delivered immediately.

Premium: A regular periodic payment for an insurance policy.

Quota-share provisions: specify what percentage of premiums and loss exposure the private company will retain, with the residue being passed on to the reinsurer.

Reinsurance: Reinsurance main types are two: excess of loss or stop-loss reinsurance and proportional or pro-rata reinsurance. Stop-loss reinsurance: see Stop loss provisions. Proportional reinsurance: there are four types of proportional insurance structures: quota share reinsurance, variable quota share reinsurance, surplus reinsurance and surplus reinsurance with a table of lines. Quota-share reinsurance is the most common: The reinsurer assumes a set percentage of risk for the same percentage of the premium, minus an allowance for the ceding company's expenses.

Relative deductible (French: *Franchise relative* or *Franchise proportionnelle*): Deductible consisting on a percentage of the loss to be borne by the insured

Risk: Uncertainty (i.e. imperfect knowledge or predictability because of randomness) in outcome that might involve adversity or losses. Two aspects of risk can be distinguished: variability and downside risk, i.e. the probability of extreme low values. (Hardaker et al.1997)

Risk aversion: Economic agents are risk averse when they have a preference for a certain outcome over an uncertain outcome with equal expected value. (Hardaker et al.1997)

Stop Loss provisions: specify the maximum amount of loss that the company will have to cover before the reinsurer covers the additional losses (Skees and Barnett, 1999).

Straight deductible or deductible (French: *Franchise absolue* or *Franchise déduite*): A deductible that is a constant value (as a specified amount).

Systemic risk: As opposed to risks like fire and burglary, systemic risks are dependent risks. A lot of people suffer a loss at the same time. Systemic risks result in many people making a claim at the same time with the effect that the premia paid into a pool are not sufficient to cover the loss incurred, which may threaten the solvency of the insurance pool. An example for systemic risks is price risk. All producers suffer from price downturns at the same time. Measures insurance companies can take to deal with systemic risks include re-insurance, geographic spreading and the use of capital markets.

Trigger: See franchise.