



## PERFORMANCE MANAGEMENT IN INSURANCE CORPORATION

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### Abstract

Insurance industry is part of immune and repair systems of an economy. Successful operation of the industry sets impetus for other industries and development of an economy. This article focuses on performance management system in insurance corporations in general, based on the principles of performance management in service organizations. Identifying the managerial practices and measures, those make insurance corporations effective and efficient, is the epitome of this article. Right from strategy formulation to evaluation of performance of organizational units, various aspects of performance management are covered in this article. It is a theoretical attempt to suggest key performance indicators and success factors for performance management in insurance companies.

### Introduction

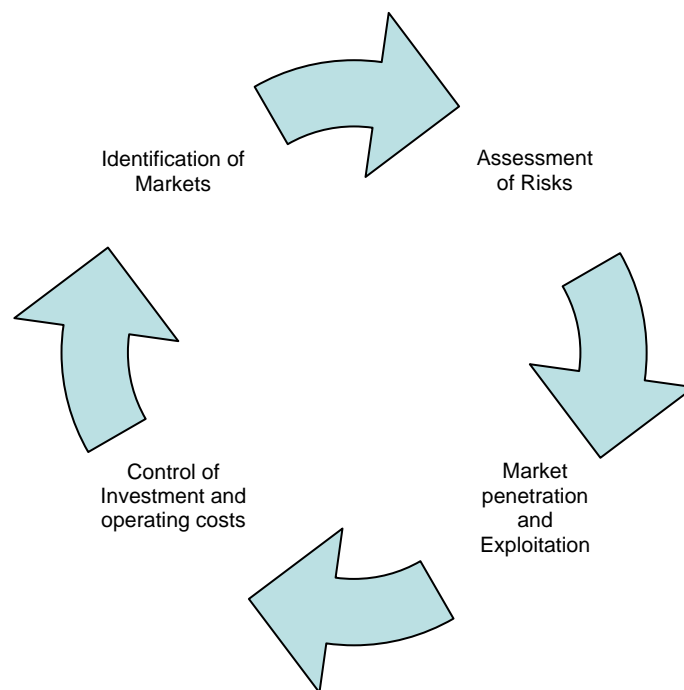
Performance of an organization is the outcome of activities of individuals and units of the organization. Except for the external influences on individual behavior and personal traits, organizations can either influence or control all factors affecting the performance of individuals and units through formal and informal means. Some of the formal means of controlling units' activities are structure, operating manuals, standard operating procedures, charters, and budgets. Greater influence on individuals can be exercised informally through communication, work culture, management style.

An effective control over the performance requires insurance companies to operate the organization divisions and subdivisions. Within each division or subdivision, there can be units responsible for separate activities. One satisfactory way of ensuring better performance of units is delegation of profit responsibility to units at the lowest possible level. Delegation of profit responsibility for a unit is possibility provided that the unit managers have information and control over the revenues and expenses. It may not be possible for all units to exercise control over several factors influencing profits. Expense budgets and setting well-defined objectives ensure cost control and effectiveness of the unit. Units are emphasized to control the cost of services they charge to the corporate office or the other units.

Financial, marketing and human resource policies of the corporations influence the unit managers to make decisions that are in the best interest of the company. Output or performance of insurance company depends on the effectiveness of such policies. Insurance corporations formulate and revise the policies from time to time to ensure that the performance of the managers is in the best interest of the organization.

Success of an insurance company depends on four important functions:

- (a) Identification of markets
- (b) Assessment of risks (of the insured and the insurance corporation) and estimation of losses
- (c) Penetration into and exploitation of markets; and
- (d) Control over investment and operating costs.
- (e)



**Fig.1. Cycle of Functions**

**Identification of Markets**

Continuous surveys on risks to which individuals and institutions are exposed helps identification of markets. Thorough analysis of the trends in various aspects of social and commercial settings functions to broaden the opportunities from time to time. The growing concern for insurance and social security in India is overwhelming the demands for insurance products. It is not exaggerating to say that there can be an exponential growth for the insurance sector as the national income and percapita income are constantly rising in urban India. Conducting surveys on risks and needs of individuals, organizations and associations helps to identify the insurance needs. Birth, education, family possessions, housing and death are common events of life and individuals face financial or emotional risk for one or more of these events. Decrease in family size over the past three decades has brought necessary changes in required needs and possessions. Previously, it was only possible for affluent societies to send children to Europe or America for higher education. Nowadays, a middle class family can afford admitting their children in Western Universities. Family cars, motor vehicles and condominium houses in urban areas have become common feature in Indian societies. All these changes have obviated opportunities to the insurance sector to grow at rapid pace.

Identifying the potential markets such as traditional insurance methods which exist in the society or develop in communities to shield their members, which are to be identified and formalized through the insurance policies. One such example is SEWA (Self Employed Women's Association)<sup>1</sup>. Self-employed women of Gujarat, who formed an association and an insurance pool, are organized by the association that benefits the self employed women and /or family members in case of death or injuries to the insured or her family member. The Association has obtained group insurance coverage with public sector insurance corporations, namely Life Insurance Corporation of India and Untied India Insurance co.Ltd.

Another example is available from the rural insurance practices in Ethiopia and Tanzania where community based group insurance 'iddirs' is prevalent in the era of corporate insurance. Peculiarly the community members obtain insurance coverage to meet funeral expenses, as the funeral is an extravagant affair. Members contribute money and food items to the deceased member's family at the event. The concept is further improved to cover medical expenses and education. Insurance corporations can grow by bringing such groups under group policies or formulating suitable individual package policies catering to the needs of the individuals.

Institutions or organizations are commonly haunted with the fears of becoming bankrupt on non re-payment of debts or insolvency of the customers, disloyalty of employees, and accidental damage to the property or injuries to the employees. Shifts in nature of risks arise out of changes in socio-economics as a result of shifts in culture or practices due to the changes in the business and social environment. For example, in India, the average size of the family has considerably decreased and consumer spending has taken a shift from traditional big cars to small cars in the middle class and well-to-do societies, and televisions replaced transistors among lower societies. Globalization of trade has created both threats and opportunities to the businesses in India, and other developing countries. Small and medium manufacturers are now able to export their goods and small traders can import foreign products.

The ability of a company in understanding and serving the needs of the society is reflected in the types of policies it offers and the rate of success of these policies. For successful

identification of markets, they need to understand the trends in culture and businesses constantly, through conducting research and analysis. They can take this job on their own or assign it to an external agency. Relying on an external agency can be risky due to the questionable loyalty of the agents.

### **Assessment of Risks and Losses**

Efficiency of actuaries and assessors of the insurance policies in fixing premiums and settling claims is foremost an important area for achieving overall efficiency in operations. The quality of assessing the risk and estimation of losses has the largest claim on the performance of an insurance company. Well trained, experienced and expert hands are needed for the operations.

### **Market Penetration**

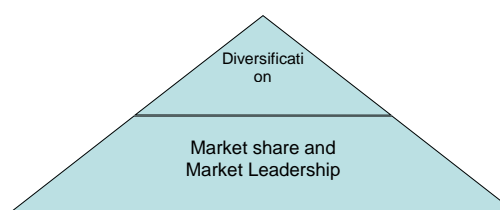
Market penetration or exploitation of a company can be identified with the growth in number of policies in each type of insurance, growth rate in earnings or turnover, company's market share, increase in number of branches and divisions etc. Efforts of the company as a whole and that of the divisions and branches are assessed to measure the effectiveness.

### **Control over the Resources**

Control over resources such as men, machines, and materials at each level of the organization provides measures of efficiency of a unit as well as the organization. Investment control and expense control are dealt separately and the effectiveness of management's decisions at various levels is to be assessed separately.

### **Continuum of Objectives**

The basic measures of performance are economic viability and sustainability. Once this is achieved, insurance company's objectives may turn on long-run profitability, expansion and growth, market share and finally to diversification. Each of these stages requires strategy. The individual interests of the managers and other employees of the organization may not match with the interests of the organization, posing a major problem in attaining the goals of the organization.



## **Fig.2. continuum of objectives**

### **Strategic Planning**

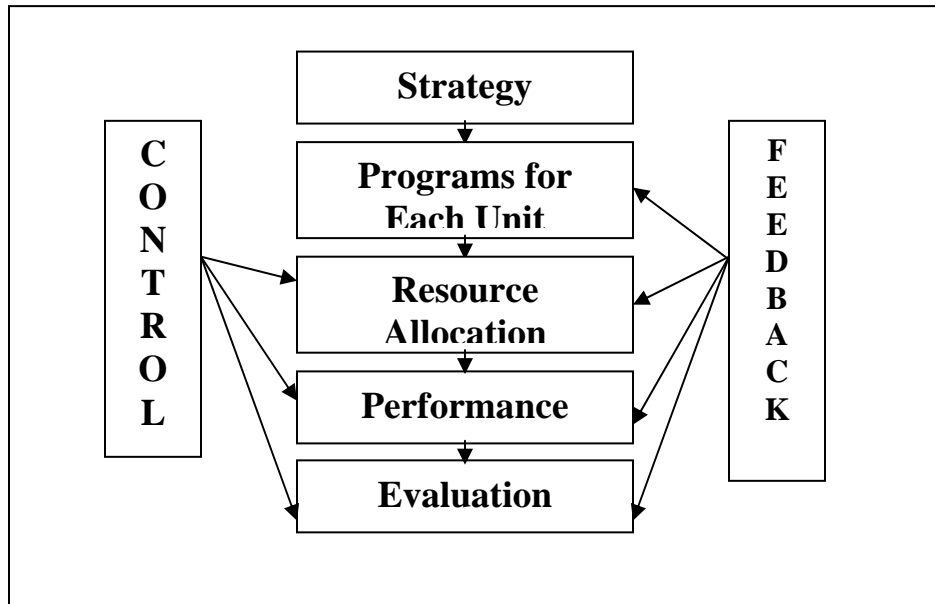
Several factors influence strategy formulation of insurance companies. Some of these are external to the organizations (referred to as environmental factors, and some are internal). Environmental factors are customers, competitors, regulatory and political condition. Front line management of insurance companies constantly updates its knowledge on the external environment to formulate strategies. Potential market for insurance is to be identified and compare the same, with the internal efficiencies of the company as to formulate a strategy.

For example, a study of the average life expectancy and average size of the family is used to identify the family needs and design new insurance policies to expand the market to children education, housing, health and medical insurance policies. Similarly, competitors' strategies may influence the strategies of the company. Changes in the political environment may instigate necessary changes in the business environment and provide an opportunity to the insurance companies. For example, if a political party that favors small scale and cottage industry is likely to form a government, based on the estimated average size and most common types of units, insurance policies may be designed cater to their needs. Changes in the government policies such as labor laws and industrial laws may enforce the manufacturers to make provisions for the deceased employees. Insurance companies can identify the needs of employers and design the policies to help their insurance needs.

Another important consideration, in formulating a new strategy or revising an old strategy, is the internal efficiencies of the insurance company. A study of the internal consistencies and resources helps to identify the fitness of the company to avail the opportunity. Internal efficiency includes the quality of workforce, existing insurance products and product lines, number of divisions and branches, agents' network etc.

Once the strategy is formulated, each division and branch is required to prepare necessary strategic plans and programs to implement the strategies. Strategic plans are usually prepared for a period ranging between 3 to 5 years. The head offices usually design insurance policies, divisional and branch offices sell these products and maintain the records of the customers in their respective divisions and branches. Role of each branch and division is specified along with their jurisdiction or charter. A strategic plan for a branch or division may contain the programs to increase their market share in the local area and provision of a new service or policy to the customers. Usually insurance companies divide charters for each division or branch and limit the size of the policy that offered at a division or branch. Insurance companies appoint agents at branch and division levels to find customers for insurance policies. Insurance Company provides necessary training for agents on the contents and operation of various insurance policies.

### Performance Control



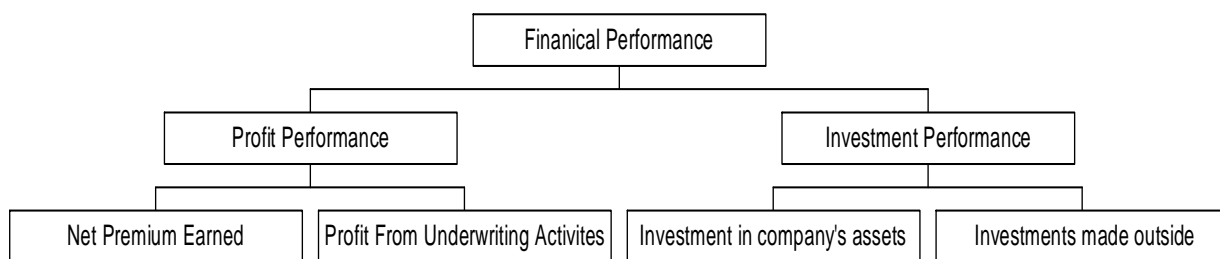
**Fig. 4 Control process**

Strategic plan of each branch specifies the proposed programs with necessary amount of resources needed. Strategic plans at various levels are summarized and compared with the overall strategic plan at the company level. Company staff departments identify the inconsistencies, slack in programs, and require the concerned divisions be required to make necessary changes to their strategic plans. The divisions at their level take similar step on branches. Corporate offices hold meetings with the divisional and branch managers to impart the guidelines and assumptions to be observed in preparation of the strategic plans at all levels. In countries like India, insurance companies operate at four different levels such as corporate, zonal, regional, and divisional and branch levels. Depending on the size of the market, each company determines its operational levels.

Each unit of insurance company prepares budget for implementing the strategic plans, for the planning period, and forwards for approval. In some insurance companies, respective superior level may allocate budgets to their subordinating levels; where as in other companies both the divisional and branch offices jointly prepare budgets. Once all units make the budget, corporate planning offices review and approve them. Corporate planning departments integrate the individual budgets into overall budget of the company. In case the budget figures so obtained from all levels of the organization do not match with the overall budget figures established by company, there must be some thing wrong with the strategic plans at either of the levels. Slack in each budget proposal is identified and eliminated. Even when, the budget outlay so obtained from lower levels exceeds the overall budget, the company may need to either revise its budget or requires the lower levels to drop some of the proposals.

Once the budgets are prepared and approved for strategic plans that are implemented for the next 3 years or more, annual budgets are prepared at each level for implementation of the strategic plans. Annual budgets prepared at each level contain the routine and regular expenses of each branch, and the budget for proposed new programs. In any year, if the company cannot afford the whole budget, the company withholds new and proposed programs or postpones them for later years.

Once the budgets are finalized and approved, each unit is supplied with, the resources required carrying out the proposed plans. Each branch and division reports the progress of strategy implementation from time to time to their respective superior offices. Necessary controls such as rules and procedures exist on the branches and divisions to ensure the desirable performance. Corporate office supplies required information for implementing strategies. Any changes in the environment during implementation of a strategic plan are incorporated in strategic plans. Some insurance companies supply standard manuals for branch and a divisional office that may contain business policies of the company, standard procedures, and operating systems. Report from branches and divisional offices at the end of each financial year reveal the performance helps the corporate office to identify the poor performing and better performing units.



**Fig. 5 Financial Performance**

**Fig.4. Classification of Financial Performance**

Performance of insurance company in financial terms is normally expressed in net premium earned, profitability from underwriting activities, annual turnover, return on investment, return on equity etc.

These measures can be classified as profit performance measures and investment performance measures.

Budget variances measure the financial performance of each unit. Performance of each branch includes both financial and non-financial performance. Financial performance for branches can be divided as profit performance and investment performance. These are expressed in terms of turnover, gross and net profits, return on investment, return on capital employed etc.

### **Profit Performance**

Profit performance includes the profits measured in monetary terms. It is the difference between the revenues and expenses. In assessing profit for a branch, all items that are directly or indirectly influenced by the unit manager are considered. Apart from the expenses at the unit, company head office and divisional office expenses on behalf of a branch are included to motivate the branch managers to cover their share of their expenses at respective higher levels.

### **Investment Performance**

Investment performance can take two different forms. One the return on assets employed in the business other than cash, and two, return on the investment operations of the surplus of cash at various levels earned on operations.

Investment performance of the branches may often be difficult to assess if the branches use common assets. Cost of establishment of communication, and transport system and other services provided to branch offices and the investment in these facilities can be charged against the branches on the amount of services utilized by each branch. Difficulties arise in assessing the share of each branch in the investment and determining the exact investment applicable to a branch. It is also important to see that the impact of depreciating assets on the investment performance of each branch. Necessary adjustments are made or suitable method of comparison is developed in performance measurement system. Certain methods of depreciation may cause dysfunctional actions of the branch managers.

Effectiveness of cost control methods adapted is also considered as a measure of performance of a branch or division. Some of the ratios pertaining to cost control are average transaction cost per policy, expenditure per employee, average annual expenditure of a branch or division, average cost for assessing the loss and average commission paid to agents etc.,

All the financial measures mentioned above pertain to the efficiency of operations of branches and divisional offices and they include only the routine business of these units. If the company allows its branches and divisional offices to deal with accumulated funds to invest in profitable way, average return on investment from each branch or division is another measure of investment performance. Insurance companies may encourage the unit managers to invest accumulated funds in housing finance and other lending operations. This method is much convenient than collecting from branches into, and, investing from central pool at the company's headquarters, because of the following reasons.

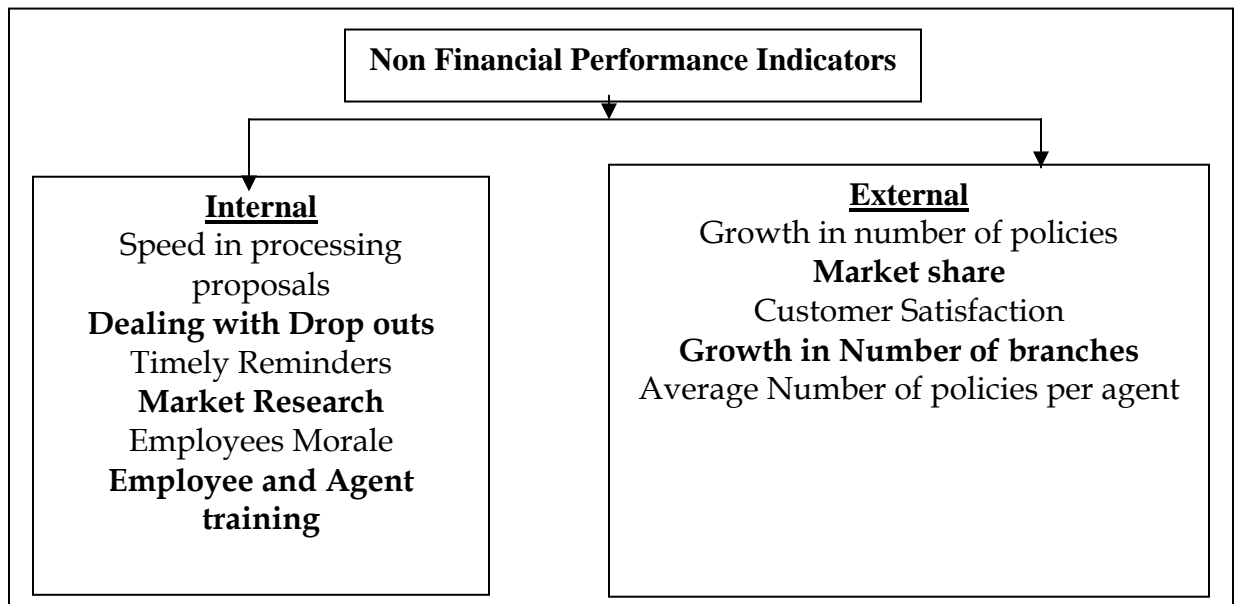


1. The branch managers and divisional managers can have direct contact with their customers in their area so that they can effectively process and decide upon the loan applications.
2. It is easy to operate and control the loan accounts within the branch itself; it reduces the burden to the divisional company head offices.
3. Cost of dealing with the customers will be less in terms of reminders to the late paying customers, collection costs and legal costs for the cases against the default customers etc.,

Performance of each branch manager and divisional manager can be measured in terms of how effectively they are operating the accumulated funds and the number of cases of default shows the ineffectiveness of lending operations of the branch or division.

A simple ratio that measures the investment performance of unit managers is the return on investment of each unit. This investment includes the facilities provided to each branch such as buildings, furniture, office, and communication equipment. Such measure controls the spending of units on the assets.

### Non-financial Performance



**Fig.6. Non-financial Performance Measures**

Some of the non-financial performance measures may include growth in number of policies, market share of the branch or division in the local area, company's market share in total, number of branches and divisions, Speed in policy processing, speed in delivery of the policy notes, timely reminders to the customers, number of drop outs from the policies, growth in products and product lines, customer satisfaction, speed in settlement of claims, employee training, research and development, market intelligence and surveys, number of policies per agent, agents training, retention of efficient agents etc.,

## External Measures

**Growth in number of policies** may vary from one division to another division and from one branch to other branch depends on the changes in income levels, patterns of income distribution and changes in the economic environment. Per capita income of the locality, changes in income levels, growth in industries are important parameters used to compares the growth in number of policies. For example if a geographical area is rapidly being industrialized, the growth in number of policies is observed accordingly, and if, mines are being closed in a mining area, naturally the number policies decline.

**Market share:** The published data of various companies provide a means to compare the market share of branches or divisions of various insurance companies operating in the area. A basic comparison is made with the company's market share in total and taking it as an average market share for all branches and divisions, one can identify the branches and divisions exerting poor performance. Problems of the specific branches and divisions are attended to improve their performance.

**Customer Satisfaction:** Difficulties exist in assessing the customer's satisfaction in insurance contracts. Unlike commodities and other services, such as transport and banking, insurance customers do not consume the product or utilize the service at one point of time, rather, they feel the satisfaction of assurance over a period of time, particularly when they give a thought about the risk they are exposed had they not insured. However, to some extent, customer satisfaction comes from minimization of funds they have committed in insurance premium and possibility to maximize their benefits from a policy. Other facilities or services such as housing loans, easy installments, single and one shot premium are some of the means to make the customers satisfied. Incase of endowment and life insurance policies, payment of the maturity amount is often delayed, causing frustration to the beneficiaries. Any suffering due to delay in providing a financial help to the beneficiaries creates a negative image of the company among customers. Respective branch managers and divisional managers must ensure that the maturity amount reaching the beneficiaries at the earliest.

**Growth in Number of branches:** It is a result of company's growth and the efforts in expanding services to different locations. Conscious estimate of the demand for insurance services need to be assessed, appropriate policies may be designed or the policies are tailored to fit the purpose of the local requirements.

**Average Number of policies per agent:** Efficiency of a branch or unit is often reflected in average number of policies per agent and average size of the policy each agent brings to the branch or Insurance Company. If a branch scores poor in these regards the reasons for such poor performance are analyzed in the light of the economic activity of the location, industrialization and other factors influencing the performance of the unit. As agents' commission depends on policies they catalyze, insurance units recruit as many agents as they can. This practice may involve more work to the units in recording the transactions with the agents. Many insurance companies require the agents to deduct the commission available to the agent at the source itself to reduce the commission payment and records of the agent

## **Internal Measures**

**Speed in Processing:** Insurance companies develop the mechanism for processing the proposals. If such mechanism is effective, it increases the speed of the process. Verification and valuation of assets, health check-up for customers etc., must be quickly made so as to accommodate more customers during the period of performance.

**Dealing with Drop outs:** Number of dropouts from the insurance contracts is observed from time to time and a proper analysis is to be made for analyzing the causes for drop out. Insurance companies may formulate policies to allow the customers to integrate back into the stream. Default customers are given an opportunity on certain penalties and other conditions, such as, persisting health conditions of individuals or the persisting risk for the adjusted value of the properties. Many insurance companies ignore the importance of tracing and customer retention.

**Timely Reminders:** Average time taken for the serving reminders to the customers and average speed in assessing the accounts that have fallen over due etc., need to be observed and controlled to maintain quick disposal of the policies and settlements. Necessary steps are taken for improvement. Average period of clearance of checks and other modes of payment is maintained at minimum. Electronic data processing and Internet and e-mail facilities are utilized for supplying reminders to the customers. Repeated reminder may be supplied at a cheaper cost to the customers. Growth in number of policies is compared with the other branches and divisions of the same company and with that of the competitors'. Causes for poor performance are analyzed and remedial measures are taken.

**Market Research:** One important consideration for the non-financial performance or effectiveness of a unit of insurance company is the research and development. Contribution of each unit in finding the markets and developing new products and product lines must be ensured through incentive packages to the managers of units. It is advisable to encourage the units to conduct surveys on various aspects from time to time that interest the insurance companies. Observing the changes in the business environment also prompts new ideas and opens new areas for insurance companies. The company, which reacts at the earliest for these changes, will have a competitive edge. Managers and staff of the units must be influenced and trained to adapt interactive control system, in which they learn to change their behavior according to the changes in the environment. : Insurance companies conduct business research through a central unit at the company level to identify the needs of the customers. Such research and analysis result in design of new policies which serve the needs of the customers. Research and analysis departments often revise the existing policies and their commercial viability. Small insurance companies may buy such services from external institutions, which are professional in business research and analysis. Performance of such research and analysis wings cannot be determined accurately but the annual expenditure can be controlled through budgets. Progress of various research projects is analyzed and decisions are made whether to continue or discontinue a project or proposal.

**Employees Morale:** Like in other industries and businesses, insurance companies need to assess employees' morale and satisfaction. Dissatisfaction among employees commonly arises in the perquisites and compensation packages available to them. In some companies, perquisites and other fringe benefits are offered on the basis of years of experience of the employees rather than

their achievements. If promotions are based on seniority, it may be discouraging to the new employees. HR policies are normally centralized at the company level. Provision of necessary facilities to the employees to perform their activities will encourage their performance in a better way. Insufficient staff at branch, inadequate facilities to conduct various operations, less growth in career and lower increase in earnings as compared to other industry or other companies is some of the causes for dissatisfaction. Some of the demands of employees may be genuine and rational, need attention of the management. From time to time, pay packages and promotion schemes are revised and implemented.

In manufacturing sector, some large organizations open their own educational institutions and health centers for their employees but in service organizations such provisions are less. One reason is that many insurance company branches are small with a number of employees less than 10 in number. They cannot afford a school or health center of their own. In such cases, a central health center or school may be opened at the divisional or company level to provide education and health to the employees at subsidized expenditure.

**Employee and Agent training:** Employee and agent training are among the essential activities of insurance companies, operating in a competitive and ever changing business environment. Budgets prepared at each unit of insurance company contain necessary provision for this. Effectiveness of such spending on training and development of the employees and agents is separately assessed to measure the readiness and ability of a branch to adapt the changes in the environment. Most of the insurance companies in India recruit employees based on their IQ levels rather than their field of education. Such recruitment is based on the philosophy that intelligent people can be trained and developed in the manner the company desires. Each branch assesses the skills and expertise required for its proposed programs and operations and makes necessary arrangement for training their employees. Agents are appointed based on their abilities to obtain customers, no standard policy is observed in selection of agents. Each agent is offered a commission on the business he brings to the company at a fixed rate. Agents are allowed to continue with the company as long as they meet the targets set by the insurance offices. This often discourages many prospective insurance agents. Agents improve their performance over a period of time, on dealing with different individuals and institutions, and most of the agents are engaged in other economic activities that promise a fair return to them. Usually training camps are organized at the division or company level from time to time, as it is economical to organize such programs centrally. Agents are successively being promoted based on their performance as development officers and are absorbed into the company based on continuous achievements, provided that, they possess the required qualifications. This method produces satisfactory results in insurance companies.

It is important for the managers at all levels of insurance companies to maintain a balance between the financial and non-financial measures as indicators of performance and show how effectively the strategies are implemented. A dash board or a balanced score card can be developed and maintained at each branch, division and at the corporate office, to check the progress of the unit from time to time and to take necessary action to improve the performance. A simple model of a balanced score card is shown below.

#### **Key success Variables**

## **Financial Indicators**

- 1 Gross and Net premium
- 2 Profit from underwriting
- 3 Average profit per branch and per employee
- 4 Average cost per each type of policies
- 5 Average annual cost per employee
- 6 Return on Investment & other lending activities

## **Employee and agents Training**

- 1 Number of employees and agents trained
- 2 Number of employees trained in advanced accounting methods and modern software
- 3 Number of employees trained in market research and analysis
- 4 Number of employees trained for branch and division management
- 5 Actuaries and assessors training and development

## **Research and Development**

- 1 Changes in the business and Individual risks
- 2 Analysis of market
- 3 Statistical research on various issues affecting the socio-economic system
- 4 Competitors' strategies
- 5 Regulatory influences
- 6 New Policies for Growing industries

## **Operational Efficiencies**

Speed in processing –proposal forms  
Average time taken in -settling claims  
Number of dropouts  
Number of reintegration cases  
Number of new branches established per year  
Cost efficiency in reinsurance  
Number of repudiation cases in court  
Number of cases challenged in court and failed

The list of key performance indicators mentioned above is not exhaustive and may not be uniformly applicable for all insurance companies and their units. Based on the specific needs of an insurance company and its units, each of them can develop of a balanced score card of its own as a comprehensive indicator of various measures. Some of these measures may be changed or dropped on the specific circumstances of an insurance company. Variations in measures at different levels arise due to the degree of autonomy given to the unit managers regarding the profit and investment decisions. If properly designed, a control system may warrant all the

important measures can be made applicable to the managers at all levels. For example, research and development activity can be made at all levels, in the form of market intelligence surveys.

### **Rewards and Incentives**

Rewards and incentives to the managers of branches and divisions are to be based on the effectiveness of managers' decisions, in maintaining the balanced scorecard measures at desired levels. Short run achievements that positively influence future profitability and growth of the organization should be identified and suitably rewarded. One problem with many insurance companies is that they transfer the branch managers and divisional managers very often. This policy is far from satisfactory, though it is necessary to promote and change the location of the managers. Each branch or divisional manager must be given considerable time to influence the factors affecting performance in the long run. Frequent changes in the leadership, though not necessarily change the policies of the company, but change the approaches and methods of practice and create difficulties to the other members of units to adapt and change the behavior instantly.

Short-term incentives are usually based on profits for the current year. A careful analysis is needed about the quality of profits. Cutting down employee training, welfare and research activities may shoot up the profits but they have negative long-term implications on the company. A profit earned after maintaining the balanced score card measures at the desired levels, is the real profit earned by a unit.

### **Conclusion:**

Performance management is the key for success of organizations. When the organizations grow larger and larger, complexity increases in controlling them. Establishing a Systematic and well organized performance management systems calls for understanding and analyzing the key success factors. Achieving a success that persistent and enduring is a result of conscious planning and implementation process. Periodical review of performance is the heart of the process. Understanding the indicators of performance, evaluating and interpreting the results assists in timely action and effective management. Every insurance company that flourishes over long run implements a balanced scorecard and constantly improves the measures and results of the corporation. Assigning weights to various measures in a balanced scorecard is case sensitive in consideration with several environmental and internal factors of a corporation. Strategic uncertainties in insurance sector are comparatively less than the unusual abnormal increase in claims flooding of claims such as 9/11 attacks on World Trade Center.

### **Summary**

Performance is evaluated both on financial and non-finical achievements of business. The key success factors vary between the industries, organizations and units of organization. The key success factors for insurance companies on financial and non-financial areas are identified to a greater extent and explained in the article. However, the list of measures is not exhaustive and

these are specific to the strategies, situations, and location of insurance companies. Some common and general factors are explained. Financial performance is understood in terms of various financial ratios, which are divided as profit performance measures and investment performance measures. Non-financial measures include a range of indicators with orientation of customers, growth, and value to the community and societies. Some of the measures reflect short-term performance and other on the long-run achievements of a company. Maintaining a balance between these measures in order to achieve success is a highly growing concern among the managers in modern organizations.

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