AAI 81A
Foundations of Insurance Production

Segment A
Principles of Insurance

COURSE LEADER HANDBOOK
First Edition, 2006

720 Providence Road
Malvern, PA 19355
Phone (610) 644-2100 • www.aicpcu.org

Contents

Appendix A—Learning Activities

Appendix A

Learning Activities

Introduction

This section provides some case studies and exercises for each assignment. The material is geared specifically toward this course. Not all assignment objectives will be covered, so you should supplement these exercises with your own material. Module four of the general course leader handbook provides some ideas on how you can create your own exercises.

Students can work on these exercises as a class; they can also work on them in small groups or independently, reporting back their solutions. To add variety in the classroom, include both group and individual work in each class.

In the segment format, you should not expect to conduct more than one or two of these exercises in any single session. A tremendous amount of material is in this segment, and if you have only one day to present information to your class, you may be forced to mainly lecture.

Special Notes

As mentioned, all assignment objectives are not addressed in this handbook. The ones addressed were chosen randomly. They are not of any greater or lesser importance than any other assignment objective.

Vocabulary is a very important part of Institutes exams and is vital to good communication in the industry. While none of the exercises in this handbook specifically address the key words and phrases, you should incorporate them into the exercises that are provided. You may also want to create your own exercises to specifically address them to each assignment.

Assignment 1—The Insurance Business: An Overview

Group Exercise

Relates to Assignment Objective 1

Explain the parts of the "sales trilogy."

Have the group brainstorm ideas for improving their skills and knowledge in each of the three areas that make up the sales trilogy. Examples are given below.

Product Knowledge

- Take AAI courses.
- Meet with company underwriters.
- Study individual company policy forms.
- Study *Best's Underwriting Guide* to determine questions to ask a prospect.

Market Knowledge

- Meet with company underwriters.
- Subscribe to an Internet service or a paper-based service.

Selling Skills

- Attend a sales seminar.
- Take another producer (preferably one who specializes in the prospect's field) along on a sales call.
- Develop a risk-specific questionnaire of potential questions to ask a prospect.

Group Discussion

Relates to Assignment Objective 4

Describe the requisites of an ideally insurable exposure.

Using a variety of perils, such as fire, windstorm (hurricane), earthquake, war, wear and tear, flood, etc., have the group discuss how well they think each of the causes of loss meets the requisites for insurability from the underwriter's standpoint. Be sure to include some perils that are commonly insured (such as fire), some that are insured only under certain circumstances (such as flood), and some that are considered commercially uninsurable (such as war or wear and tear).

Group Discussion

Relates to Assignment Objective 6

Determine whether the insurance producer works in a more competitive or less competitive environment than that found in noninsurance businesses and defend this point of view.

Relates to Assignment Objective 7

Explain how insurance is (a) different from other businesses and (b) similar to other businesses.

One of the important concepts of this assignment is how the insurance business is different from other businesses. A key point is that with insurance, the ultimate cost of the product is not known until long after it has been priced and sold. Divide the class into two groups. Have one group decide on a type of business, other than insurance, that it would like to analyze. Have the other group analyze the insurance business. Give each group some time to discuss the key business issues that face each industry. For example, if the first group chooses the retail furniture industry, some of the issues would be the cost of raw materials, the rising cost of labor, the exporting of jobs overseas, the increasing tendency of people to shop via the Internet, etc. When the two groups are finished with their discussion, have them elect a spokesperson who will present the issues to the entire class. Have the class discuss and debate the similarities and differences between the two business models.

Debate

Relates to Assignment Objective 9

Compare the various insurance distribution systems.

Using the following case, divide the class into three or more groups. Assign each group a different insurance distribution system. Give the group members time to discuss, within their group, why they think that distribution system will best meet the company's needs. Each group will then present it.

> You are the CEO of a newly created insurer in your state. You specialize in providing automobile insurance for "high-risk" drivers. One of the questions the board has yet to resolve is the type of distribution system that the company will use when it enters the marketplace. Your group must justify its position and allow questions from the board members.

When running this exercise, be sure the "board members" ask questions of each group to determine exactly why they thought theirs was the best system to use. You may have to facilitate the discussion at first to get it going, but the groups with opposing positions should be able to come up with their own questions.

Assignment 2—Insurance and the Legal System

Case Study

Relates to Assignment Objective 7

Given an insurance agency case, explain how an agent's authority might be created. In support of this assignment objective, you should be able to illustrate (i) express authority, (ii) implied authority, and (iii) apparent authority. You should also be able to explain the duties that agents owe their principals and the five ways in which an agency can be terminated.

Using the following case, determine what type of authority the agent is operating under with each insurer. Also discuss the agent's duties owed to each company and how the relationship between the agency and the insurer may be terminated.

> The Jones Agency started operations five years ago. John Jones is the agency owner. He left an agency for which he was a producer and formed Jones Agency motivated by a desire to provide superior service to his clients. Although he thought gaining agency appointments would be easy, he has struggled to get contracts with a sufficient number of insurers to serve his clients' needs. Moderate Mutual, with whom he had a prior relationship, gave him a standard agency agreement. John also does business with Protection Insurance Company, although he accesses them using a managing general agent. For high-risk clients, John also uses various excess and surplus lines brokers who allow him to place business with the London insurance market. Although he is working with an additional carrier, Institutional Indemnity, the paperwork has not yet been completed. He has recently bound coverage with Institutional, however, for one of his new clients. The underwriter called John when she received the binder, and she questioned his status with the company. She indicated that John's binder was valid.

Assignment 3—Risk Management and the Producer

Word Mix-Up

Relates to Assignment Objective 1a

Contrast the various goals of risk management.

Before class, write each of the pre-loss and post-loss risk management goals on large Post-It Notes. In the classroom, on the board or a flip-chart, write a heading for pre-loss risk management goals and post-loss risk management goals.

Place the Post-It Notes randomly among the two lists, or hand them out to the class. Have the students arrange the goals under the correct heading.

Case Study

Relates to Assignment Objective 1b

Identify, describe, and give examples of the elements of a loss exposure.

Relates to Assignment Objective 1c

Illustrate each of the steps in risk management and the techniques and methods that may be used with each step.

Using the following case, or one you create, have the students identify the loss exposures, categorize them using Prouty's measures for frequency and severity, and propose an insurance and/or a noninsurance technique to deal with the loss exposures identified. This case will be used throughout this course and the AAI 82 segments.

> Your insured is a large chain of department stores located in multiple states. The stores sell men's, women's, and children's clothing; linens; jewelry; cosmetics; luggage; furniture; household items, such as china and silver, artwork, lamps; and the like. Rather than compete directly with other national retail chains, the firm has intentionally avoided large urban locations for its retail stores, instead favoring "second-tier" cities. The department store firm has a large, highly automated warehouse located in one of the states. The warehouse is approximately 500,000 square feet, and the building is equipped with an automatic sprinkler system. Inventory is received at the warehouse from manufacturers and vendors and is then distributed to the individual store locations. Distribution from the warehouse is handled using company-owned trucks. In some cases, the manufacturers of the products ship their goods directly to the stores using their own trucks or a common carrier. Information of such direct shipments is sent electronically to the warehouse for tracking purposes. Large amounts of merchandise are purchased from overseas and are shipped via air or water. Most of these shipments are received in San Francisco or New York and must be sent to the warehouse via truck or rail transportation. The warehouse is located near a railroad track, and there is a spur to the loading dock. Each store location uses a point-of-sale system to track inventory. Information is uploaded from the store to the warehouse every night. The firm employs a large information technology (IT) staff.

In addition to retail stores, the firm also uses e-commerce, and a large percentage of sales is derived from the online catalog. Paper catalogs are also sent out on a mass-mailing basis, and orders are received via fax and mail. The firm also has a call center located in the warehouse to process telephone orders. The call center uses sophisticated telephone equipment. Orders received electronically or by fax, mail, or phone are shipped using a common carrier, often within 24 hours of receipt.

The retail stores consist of a mixture of leased and owned buildings. Some stores are located in malls, while others are freestanding buildings. In mall locations, the stores are not the key tenant and depend upon other, larger retailers to attract customers to the mall. Stores are open from 9:00 AM to 9:00 PM each day, except Sunday, when they close at 6:00 PM. At the warehouse, the firm employs 100 people who handle inventory, loading and unloading, shipping, clerical work, and sales. A fully staffed human resources department handles the administration of various employee benefit plans, including group health insurance, life insurance, and disability. A 401(k) pension plan is in place for all full-time personnel. Each store has between 25 and 50 employees, mostly consisting of part-timers who are mainly college students. The store manager and assistant manager are responsible for hiring decisions for their stores.

Customers typically pay with cash, checks, personal credit cards, or the department store chain's own credit card that was developed years ago. The store credit card offers cash rebates to customers who spend a certain amount during any calendar year. Cash, checks, and charge receipts are picked up by an armored car service each day and taken to the bank. Each store has a surveillance camera system installed to detect shoplifting, which has been a problem in the past. The store also uses off-duty undercover police officers who pose as shoppers.

The jewelry department, shoe department, restaurant, and hair salon located in the larger stores are not operated by your insured but are leased to others. The insured is compensated by a percentage of the sales received by the lessee. The sporting goods department is one of the most profitable areas of the business. The insured provides repair and maintenance for ski equipment, snowboards, tennis rackets, bowling balls, and similar types of sporting goods, even if the merchandise was purchased from a competitor. The insured also fills scuba tanks. Because this repair work requires expensive, specialized equipment, the insured sometimes must ship the items to the four store locations that have the appropriate equipment.

The firm is publicly traded and has a board of directors consisting of both insiders and outsiders. The officers of the corporation are selected by the board. A major accounting firm is used to perform routine audits and prepare necessary Securities and Exchange Commission (SEC) and other financial filings. Employees are eligible to purchase stock at a discount as an additional employee benefit.

Group Exercise

Relates to Assignment Objective 1d

Explain the techniques of probability useful in risk management.

Bring several pairs of dice or decks of cards to class. Ask the students what the probability is of getting a certain number on a single roll of the dice or a suit and the value on the card (e.g., ace of spades) with a single draw. Have the students work in groups and roll the dice or cut the cards several times and keep track of their results. Have them perform the same activity 10 more times. Did the results change? Have them do it 10 more times. Did the results change again? How is the actual result changing in comparison to the estimated result? How do insurance companies use probability theory?

Assignment 4—Insurance Sales and Account Development

Because this assignment is of a nontechnical nature, it lends itself to a variety of activities and group discussions based on the experiences of the group. If students can use actual examples, it will help drive home the important points in the assignment.

Role Play

Relates to Assignment Objective 2c

Identify the five prospect reactions that might be encountered in a sales call.

Relates to Assignment Objective 2d

Describe a method the producer would use in response to each of the reactions in 2c above.

Using the case in Assignment 3, or one you create yourself, have the students role play an objection drill. Overcoming objections is a key selling skill, and practicing the use of techniques to deal with objections is important. Working in groups of two, have the “buyer” use one of the reactions outlined in the book. Have the “producer” use one of the techniques to overcome the objection. Have them take turns and do several drills. Debrief the exercise as a group. What did each person do that was a good example of dealing with the objection? A word of caution about role playing is that most students dread it when you say that’s what you’re going to do, but students usually end up enjoying the practicality and real-world feel to it once they have done it. Also, when you debrief, have each role play buyer mention only what each producer did well, not what was a weakness. This keeps the discussion positive and allows for each person to show off his or her skills.

Group Exercise

Relates to Assignment Objective 3e

Differentiate between minimum agency standards and minimum account standards.

Working in small groups, have the participants develop reasonable agency standards and account standards for both commercial and personal lines. If they already use these in their own agencies, they are welcome to contribute what those standards are, if they are comfortable in doing so.

Group Exercise

Relates to Assignment Objective 3i

Explain the benefits of account upgrading and total account selling to (i) the agency and the producer and (ii) the client.

Have the group brainstorm a list of advantages to account-rounding activities from the perspective of their own agencies and their insureds.