

CPCU 520

Appendix B

Insurance Operations, Regulation, and Statutory Accounting

COURSE LEADER HANDBOOK

First Edition, 2006

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Appendix B

Quizzes

Introduction

One quiz per assignment is provided in this section. A sample answer key is also provided. Please note that because the quiz is in the essay format, the answer key might not address all possible answers. If you want a longer quiz, you might want to supplement with questions from the course guide or SMART exam disk. For tips on creating quiz questions, see page 11 of the general Course Leader Handbook.

Assignment 1—Quiz

1. Briefly outline the steps in the risk management process. (6 points)
2. Briefly describe the law of large numbers. (4 points)
3. Briefly describe three types of proprietary insurers. (12 points)
4. List four types of cooperative insurers. (4 points)
5. List the four principal goals that all insurers share. (4 points)

Assignment 1—Quiz Answers

1. Briefly outline the steps in the risk management process. (6 points, 1 for each step)

Answer:

- 1) Identify loss exposures
- 2) Analyze loss exposures
- 3) Examine the feasibility of risk management techniques
- 4) Select the most appropriate techniques
- 5) Implement the risk management techniques
- 6) Monitor results and make changes as needed

2. Briefly describe the law of large numbers.

(4 points, 1 for each of the concepts or elements in the sample answer below)

Answer: The law of large numbers is a mathematical principle stating that as the number of similar but independent exposure units increases, the relative accuracy of predictions about future outcomes (losses) also increases.

3. Briefly describe three types of proprietary insurers.

(12 points, maximum 4 points for each type, 1 point for naming each type (i.e., stock insurance companies, Lloyd's, and insurance exchanges), up to 3 additional points per type for any of the concepts or elements in the sample answer below)

Answer:

- 1) Stock insurance companies are owned by their stockholders, who elect a board of directors to oversee operations. The board appoints officers who make day-to-day operational decisions.
- 2) Lloyd's, which includes Lloyd's of London and American Lloyds, is an insurance marketplace much like a stock exchange. All of the insurance written at Lloyd's is written by or on behalf of an individual member and backed by his or her personal fortune. Each member belongs to one of 86 syndicates, with day-to-day management delegated to the syndicate manager.
- 3) Insurance exchanges are similar to Lloyd's because they act as insurance marketplaces. Exchange members underwrite any insurance or reinsurance purchased on the exchange. Members can be individuals, partnerships or corporations and they have limited liability. Members belong to syndicates and delegate day-to-day operations to the syndicate manager. The only existing exchange is the Illinois Insurance Exchange.

4. List four types of cooperative insurers.

(4 points, 1 for each type; to earn a point for "other," an example is required.)

Answer:

- 1) Mutual insurance companies
- 2) Reciprocal exchanges
- 3) Fraternal organizations
- 4) Others, including pools and government insurers

5. List the four principal goals that all insurers share. (4 points, 1 for each goal)

Answer:

- 1) Earn a profit
- 2) Meet customer needs
- 3) Comply with legal requirements
- 4) Fulfill duty to society

6. List the six external constraints that might prevent insurers from meeting their goals. (6 points, 1 for each constraint; to earn a point for “other,” at least one example is required)

Answer:

- 1) Regulation
- 2) Public opinion
- 3) Competition
- 4) Economic conditions
- 5) Marketing systems
- 6) Other external constraints such as catastrophe losses, the breakdown of law and order, and legal changes that affect liability claims

7. What is the formula for calculating an insurer’s trade basis combined ratio? (3 points)

Answer: $(\text{Incurred losses} + \text{Loss adjustment expenses} \div \text{Earned premiums}) + (\text{Underwriting expenses} \div \text{Written premiums})$

8. Briefly describe the largest challenge in measuring insurer profitability. (4 points, 1 for each of the concepts or elements in the sample answer below to a maximum of 4)

Answer: The largest challenge in measuring insurer profitability arises from the indefinite nature of loss reserves. Insurers establish reserves for losses that have not as yet been paid, including IBNR losses. Errors in estimating reserve amounts are common and insurers must adjust these amounts as more concrete information becomes known. These errors lead to distortions in insurers’ reported profits.

9. What are the primary goal and the primary responsibility of an insurer’s underwriting department? (2 points)

Answer: Underwriting’s goal is to write a profitable book of business for the insurer. The department’s responsibility is to determine whether the applications received meet the guidelines established by the insurer.

10. Briefly outline the responsibilities of the actuarial function in an insurance company. (6 points, 1 for each of the concepts or elements in the sample answer below to a maximum of 6)

Answer: The actuarial function supplies all of the information required to calculate rates, develop rating plans, and estimate loss reserves. Actuaries might assist with corporate planning and establishing corporate goals. They might also be involved in assessing the insurer’s success in meeting those goals. The actuarial function is also responsible for providing ratemaking information to regulators.

Assignment 2—Quiz

1. Briefly outline six of the principal provisions of the Gramm-Leach-Bliley Act of 1999. (6 points)
2. For what three reasons do insurance regulators try to maintain and enhance the financial condition of private insurers? (3 points)
3. List any five activities in which state insurance departments typically engage. (5 points)
4. Briefly outline the three arguments that proponents of federal regulation of insurance present. (3 points)
5. Briefly outline the licensing requirements for domestic insurers. (6 points)

Assignment 2—Quiz Answers

1. Briefly outline six of the principal provisions of the Gramm-Leach-Bliley Act of 1999. (6 points, 1 for each of the concepts or elements in the sample answer)

Answer:

- 1) Each segment of the financial services business is regulated separately.
 - 2) States continue to have primary regulatory authority for insurance.
 - 3) States cannot prevent bank-related firms from selling insurance on the same basis as insurance producers.
 - 4) Banks cannot underwrite insurance through a subsidiary but can arrange for a financial holding company to create an insurance affiliate.
 - 5) Banks must disclose to customers their policies regarding sharing information with insurance affiliates.
 - 6) States must facilitate insurance producers' ability to operate in more than one state.
2. For what three reasons do insurance regulators try to maintain and enhance the financial condition of private insurers? (3 points, 1 for each of the concepts or elements in the sample answer)

Answer:

- 1) If insurers become insolvent, future claims might not be paid, and the insurance protection already paid for might become worthless.
 - 2) Large numbers of individuals and the community at large are adversely affected when insurers become insolvent.
 - 3) Insurers hold substantial funds for the ultimate benefit of policyholders and regulation is necessary to safeguard such funds.
3. List any five activities in which state insurance departments engage.
(5 points, one for any of the activities listed below, to a maximum of 5)

Answer:

- Approving policy form
- Holding rate hearings and reviewing rate filings
- Licensing new insurers
- Licensing producers
- Investigating policyholder complaints
- Rehabilitating or liquidating insolvent insurers
- Issuing cease-and-desist orders
- Conducting periodic audits of insurers
- Evaluating solvency information
- Performing market conduct examinations
- Fining insurers that violate state law
- Publishing shoppers' guides and other consumer information

4. Briefly outline the three arguments that proponents of federal regulation of insurance present. (3 points)

Answer:

- 1) It would provide regulatory uniformity across the states.
- 2) It would be more efficient.
- 3) It would attract higher-quality personnel.

5. Briefly outline the licensing requirements for domestic insurers. (6 points, 1 for each of the concepts or elements in the sample answer)

Answer:

- Apply for a charter.
- Provide adequate capital and/or surplus.
- Mutuels need minimum book of business.
- Name must not be misleading; include "Mutual."
- Incorporators/directors must be trustworthy.
- Some states require need for additional insurers.

6. What four methods do regulators use to ensure insurer solvency? (4 points)

Answer:

- 1) Establish financial requirements
- 2) Review financial annual statements
- 3) Administer the Insurance Regulatory Information System (IRIS)
- 4) Conduct on-site field examinations

7. What are the three major goals of rate regulation? (3 points, 1 for each goal)

Answer: The three major goals are to ensure that rates are the following:

- 1) Adequate
- 2) Not excessive
- 3) Not unfairly discriminatory

8. Briefly describe a file-and-use law. (3 points)

Answer: This is a state law under which rates must be filed with the state insurance department but can then be used immediately. The department has the authority to disapprove the rates if they cannot be justified or if they violate state law.

9. Briefly describe the four requirements that can arise out of legislative policy regulation. (4 points, 1 for each requirement)

Answer: Legislation may require insurers to do the following:

- 1) Use a standard policy
- 2) Include certain standard mandatory policy provisions
- 3) File policies for approval by the state
- 4) Ensure policies meet a readability test

10. List the four “unofficial regulators” that influence insurer activity. (4 points)

Answer:

- 1) Financial rating agencies
- 2) Insurance advisory organizations
- 3) Insurer trade organizations
- 4) Consumer organizations

Assignment 3—Quiz

1. Briefly describe the two primary types of authority in agency-principal relationships. (4 points)
2. What are the four elements of an insurance product marketing plan? (4 points)
3. Briefly describe the three types of traditional insurance marketing systems. (6 points)
4. List eight functions typically performed by insurance producers. (4 points)
5. What is the most significant result of the Gramm-Leach-Bliley Act? (2 points)

Assignment 3—Quiz Answers

1. Briefly describe the two primary types of authority in agency-principal relationships. (4 points)

Answer: Agency law recognizes two types of authority in agency-principal relationships: actual authority and apparent authority. Actual authority is conferred by the principal under the agency contract. Apparent authority arises when a principal creates a reasonable belief in a third party that an agent has certain authority, even though the agent does not.

2. What are the four elements of an insurance product marketing plan? (4 points)

Answer:

- 1) Product proposal and sales goals
- 2) Situational analysis
- 3) Marketing goals
- 4) Marketing strategies

3. Briefly describe the three types of traditional insurance marketing systems. (6 points)

Answer:

- 1) In the independent agency and brokerage marketing system, producers are independent contractors. They usually represent several insurers, they are paid commissions, and they own their policy expiries.
- 2) In the exclusive agency marketing system, agents contract to sell insurance exclusively for one insurer or associated group of insurers. Producers are paid commissions, although during initial training they may receive a salary, draw, or guaranteed minimum income. Producers typically do not own the expiry dates, although some insurers may grant limited ownership rights.
- 3) In the direct writer marketing system, the sales agents are direct employers of the insurer. They may be compensated by salary, commission, or a combination of both, and they do not own the expiry dates.

4. List eight functions typically performed by insurance producers. (4 points, ½ point per function)

Answer:

- 1) Prospecting
- 2) Risk management review
- 3) Sales
- 4) Policy issuance
- 5) Premium collection
- 6) Customer service
- 7) Claim handling
- 8) Consulting

5. What is the most significant result of the Gramm-Leach-Bliley Act? (2 points)

Answer: The most significant result of the Gramm-Leach-Bliley Act has been the entry of banking institutions into the insurance industry as sellers and distributors of insurance products.

6. Briefly outline five benefits that insurers and producers derive from having an Internet presence. (5 points)

Answer:

- Reduced costs arising out of automated operations
- Streamlined business practices OR Fewer employees are needed
- Increased brand awareness
- Broadened marketing potential
- Lead-generation and cross-selling opportunities

7. Briefly outline five challenges associated with using the Internet as an alternative insurance distribution channel. (5 points, 1 for any of those listed, to a maximum of 5)

Answer:

- Customers assume products will be less expensive if they are bought over the internet
- Competitors are only a click away
- An insurer's ability to quote quickly and easily is essential
- The Internet eliminates intermediaries so a web site must provide information
- The insurer must determine whether the Internet presence will be sales only or sales and service
- The Internet shifts customer focus from service to price
- Some customers are unwilling to transmit personal or financial information over the Internet
- Information posted on the web site must be kept fresh, interesting, and accessible

8. On what two key factors does the selection of a distribution channel depend? (2 points)

Answer: The selection of a distribution channel depends on customer preferences and a firm's operations.

9. What are the three considerations in combining traditional marketing systems and alternative distribution channels? (3 points)

Answer:

- 1) An insurer must send customers the same clear, consistent message about its products and services across all marketing systems.
- 2) The experience a customer has when interacting with an insurer must be consistent across all systems and channels.
- 3) Some marketing systems are more suitable than others based on the product being sold.

Assignment 4—Quiz

1. What is the purpose of underwriting, and how is that purpose achieved? (4 points)
2. Briefly describe the concept of adverse selection. (2 points)
3. Briefly outline the six steps in the underwriting process. (6 points)
4. Briefly describe the four categories of hazard that underwriters identify. (4 points)
5. What is the difference between experience rating and retrospective rating? (4 points)

Assignment 4—Quiz Answers

1. What is the purpose of underwriting, and how is that purpose achieved?

(4 points, 1 for each of the concepts or elements in the sample answer below)

Answer: The purpose of underwriting is to develop and maintain a profitable book of business for the insurer. To achieve that purpose, insurers must minimize the effects of adverse selection.

2. Briefly describe the concept of adverse selection. (2 points)

Answer: Adverse selection is a situation that occurs because people with the greatest probability of loss are the ones most likely to purchase insurance.

3. Briefly outline the six steps in the underwriting process. (6 points)

Answer:

- 1) Evaluating loss exposures
- 2) Determining underwriting alternatives
- 3) Selecting an underwriting alternative
- 4) Determining the appropriate premium
- 5) Implementing the underwriting decision
- 6) Monitoring the loss exposures

4. Briefly describe the four categories of hazard that underwriters identify. (4 points)

Answer:

- 1) Physical hazard is a tangible condition of property, persons, or operations that increases the frequency or severity of loss.
- 2) Moral hazard is a condition that increases the likelihood that a person will intentionally cause or exaggerate a loss.
- 3) Morale (attitudinal) hazard, which is a condition of carelessness or indifference that increases the frequency or severity of loss.
- 4) Legal hazard is a condition of the legal environment that increases loss frequency or severity.

5. What is the difference between experience rating and retrospective rating? (4 points)

Answer: Experience rating is a ratemaking technique that adjusts the insured's premium for the upcoming policy period based on the insured's experience for the current period. On the other hand, retrospective rating adjusts the insured's premium for the current policy period based on the insured's loss experience during the current period.

6. Implementing an underwriting decision typically involves what three steps? (3 points)

Answer:

- 1) Communicating the decision
- 2) Putting coverage into effect
- 3) Recording information for accounting, statistical, and monitoring purposes

7. What are the three primary responsibilities of line underwriters? (3 points)

Answer:

- 1) Implementing the steps in the underwriting process
- 2) Assisting with determining appropriate coverage
- 3) Providing service to producers and policyholders

8. List any five of the responsibilities of staff underwriters.

(5 points, 1 for each responsibility listed to a maximum of 5)

Answer: (Any 5)

- Researching the market
- Researching and developing coverages
- Evaluating underwriting experience
- Reviewing and revising rating plans
- Formulating underwriting policy
- Developing underwriting guides
- Conducting underwriting audits
- Assisting with education and training

9. Briefly describe four factors that make it difficult to evaluate the financial results of underwriting in the short run.

(12 points, 1 for each of the concepts or elements in the sample answer)

Answer:

- 1) The insurance business as a whole is cyclical. During some periods, most insurers are profitable; during other periods, most are unprofitable.
- 2) Major catastrophic losses occur too irregularly to predict, and a major catastrophe is likely to cause an underwriting loss for that year for most if not all affected insurers.
- 3) An insurer's combined loss and expense ratio depends on the insurer's premium volume, and premium volume and underwriting policy are directly related.
- 4) With certain types of insurance, a considerable amount of time can elapse between when a loss is reported and when a claim is settled, resulting in inaccuracies in reserves.

10. List any five nonfinancial measures used to evaluate underwriting results.

(5 points, 1 for each of the measures listed to a maximum of 5)

Answer: (Any 5)

- Selection
- Product mix
- Pricing
- Accommodated risks
- Retention ratio
- Success ratio
- Service to producers

Assignment 5—Quiz

1. List the six ISO construction classes. (6 points)
2. List the six categories into which underwriters have traditionally grouped occupancies. (6 points)
3. Briefly explain the difference between the terms “amount subject” and “probable maximum loss” (PML). (4 points)
4. Briefly describe the two most common types of explosions. (4 points)
5. What are the three major considerations involved in underwriting earthquake exposures? (3 points)

Assignment 5—Quiz Answers

1. List the six ISO construction classes. (6 points)

Answer:

- 1) Fire-resistive construction (Class 6)
- 2) Modified fire-resistive construction (Class 5)
- 3) Masonry noncombustible construction (Class 4)
- 4) Noncombustible construction (Class 3)
- 5) Joisted masonry construction (Class 2)
- 6) Frame construction (Class 1)

2. List the six categories into which underwriters have traditionally grouped occupancies. (6 points)

Answer:

- 1) Habitational
- 2) Office
- 3) Institutional
- 4) Mercantile
- 5) Service
- 6) Manufacturing

3. Briefly explain the difference between the terms “amount subject” and “probable maximum loss” (PML). (4 points)

Answer: “Amount subject” refers to the total value exposed to loss at any one location from any one event; “probable maximum loss” refers to an estimate of the largest likely loss.

4. Briefly describe the two most common types of explosions. (4 points)

Answer: Combustion explosions result when flammable clouds of dust, vapor, mist or gas encounter an ignition source. Pressure explosions result when heat or mechanical compression causes the contents to expand beyond the vessel’s capacity.

5. What are the three major considerations involved in underwriting earthquake exposures? (3 points)

Answer:

- 1) Areas of earthquake activity
- 2) Soil conditions
- 3) Building design and construction

6. What are the two principal underwriting concerns associated with a sprinkler leakage loss exposure? (2 points)

Answer:

- 1) Damageability of contents
- 2) Sprinkler system's design, maintenance, and condition

7. Briefly describe the two steps in determining an applicant's probable maximum business income loss. (4 points)

Answer:

- 1) Evaluate the potential loss magnitude by projecting expected earnings for the coverage period.
- 2) Select a coinsurance percentage that approximates the expected interruption period, should a loss occur.

8. What five factors do underwriters consider when analyzing robbery, burglary, and theft loss exposures? (5 points)

Answer:

- 1) Susceptibility and marketability
- 2) Property location
- 3) Occupancy
- 4) Public protection
- 5) Coverage and price modifications

9. Briefly describe loss control. (3 points)

Answer: Loss control is an approach to risk management that includes both loss prevention and loss reduction. Loss prevention focuses on lowering the frequency of losses, and loss reduction focuses on lowering the severity of those losses that do occur.

10. List six ways in which loss control can help insurers reach their profit goals. (6 points)

Answer:

- 1) Improving underwriting decisions
- 2) Improving premium volume
- 3) Encouraging policyholder loss control
- 4) Reducing insureds' losses
- 5) Providing an additional revenue source
- 6) Reducing errors and omissions claims against the insurer

11. List three loss control services provided by insurers. (3 points)

Answer:

- 1) Conducting physical surveys
- 2) Performing risk analysis and improvement
- 3) Developing safety management programs

Assignment 6—Quiz

1. List the three sources of legal liability. (3 points)
2. What four elements are required to bring a civil suit for negligence? (4 points)
3. Commercial general liability insurance provides coverage for liability loss exposures in five categories. List those five categories. (5 points)
4. Why do underwriters need to consider a policy's settlement conditions when underwriting professional liability insurance? (4 points)
5. What is an attractive nuisance? (4 points)

Assignment 6—Quiz Answers

1. List the three sources of legal liability. (3 points)

Answer:

- 1) Torts
- 2) Statutes
- 3) Contracts

2. What four elements are required to bring a civil suit for negligence? (4 points)

Answer:

- 1) A legal duty owed to the plaintiff to use due care
- 2) Failure to conform to the standard of care required in the situation
- 3) A causal connection between the negligent act and the bodily injury or property damage
- 4) Bodily injury or property damage

3. Commercial general liability insurance provides coverage for liability loss exposures in five categories. List those five categories. (5 points)

Answer:

- 1) Premises and operations
- 2) Personal and advertising injury
- 3) Premises medical payments
- 4) Contractual liability
- 5) Products and completed operations

4. Why do underwriters need to consider a policy's settlement conditions when underwriting professional liability insurance? (4 points)

Answer: Most professional liability insurers insist on the right to settle out of court without the policyholder's consent. However, some professional liability policies contain a condition that requires the insured's consent. The insurer's claim and defense costs could increase if the insurer cannot settle a claim without the insured's consent.

5. What is an attractive nuisance? (4 points)

Answer: A potentially harmful object or structure so inviting or interesting to children that it would lure them onto someone's premises.

6. To ensure that financial resources are available to compensate auto accident victims fairly, what six things has regulation brought about? (6 points)

Answer:

- 1) Financial responsibility laws
- 2) Compulsory auto liability insurance laws
- 3) Shared/residual market mechanisms
- 4) Mandatory uninsured motorists coverage
- 5) No-fault auto laws
- 6) Restrictions on cancellations and nonrenewals

7. Briefly describe the two primary factors that underwriters consider when underwriting workers' compensation coverage. (4 points)

Answer:

- 1) On-premises hazards, such as housekeeping, maintenance, or other hazards specific to the firm such as machines, equipment, materials, or processes
- 2) Off-premises hazards, including duration of travel, mode of transportation, and hazards at remote job sites

8. What is the fundamental difference between excess liability and umbrella liability? (4 points)

Answer: Excess policies increase the limits of liability on one or more underlying policies but do not broaden coverage. In contrast, umbrella policies provide coverage in some situations when underlying coverage does not exist, as well as providing excess liability limits above underlying policies.

9. Define the term "premium auditing." (3 points)

Answer: A methodical examination of a policyholder's operations, records, and books of account to determine the actual exposure units and premium for insurance coverages already provided.

10. In what two ways can premium audits affect the equity and accuracy of class rates? (2 points)

Answer:

- 1) Consistency and accuracy of classification determination
- 2) Measurement of the exposure unit base

Assignment 7—Quiz

1. Rates should ideally have five characteristics. What are they? (5 points)
2. What is an actuary, and what is his or her role? (5 points)
3. What is a pure premium? (2 points)
4. The delay in reflecting loss experience in rates stems from several sources. Briefly outline five of these sources. (5 points)
5. Using the information below, calculate a rate per exposure unit using the pure premium method. (3 points)

Incurred losses	\$2,000,000
Earned exposure units	200,000
Expenses	\$100,000
Profit and contingencies factor	0.05

6. Briefly describe the three ratemaking data collection methods. (6 points)

7. Why do actuaries use loss development factors, and how do they apply them? (4 points)

8. What are the seven items a rate filing must generally include? (7 points)

Assignment 7—Quiz Answers

1. Rates should ideally have five characteristics. What are they? (5 points)

Answer:

- 1) Be stable
- 2) Be responsive
- 3) Provide for contingencies
- 4) Promote loss control
- 5) Be simple

2. What is an actuary, and what is his or her role? (5 points)

Answer: An actuary is a person trained in applying mathematical techniques to insurer operations. They use complex mathematical methods and technology to analyze loss data and other data used in determining insurance rates.

3. What is a pure premium? (2 points)

Answer: A pure premium is the amount included in the rate per exposure unit required to pay losses.

4. The delay in reflecting loss experience in rates stems from several sources. Briefly outline five of these sources. (5 points)

Answer:

- 1) Delays in policyholders' reporting losses to insurers
- 2) Time required to analyze data and prepare a rate filing
- 3) Delays in obtaining state approval of filed rates
- 4) Time required to implement new rates
- 5) Time period during which rates are in effect, usually a full year

5. Using the information below, calculate a rate using the pure premium method. (3 points, 1 for each of the elements in the sample answer below)

Answer:

Incurred losses	\$2,000,000
Earned exposure units	200,000
Expenses	\$100,000
Profit and contingencies factor	0.05

Pure premium	\$10
Expenses per exposure unit	\$1
Rate per exposure unit	\$11

6. Briefly describe the three ratemaking data collection methods. (6 points)

Answer:

- 1) Policy-year method: analyzes all policies issued in a given twelve-month period and that links all losses, premiums, and exposure units to the policy to which they are related.
- 2) Calendar-year method: estimates both earned premiums and incurred losses by formulas from accounting records.
- 3) Accident-year method: uses incurred losses for an accident year, which consist of all losses related to claims arising from accidents that occur during the year, and estimates earned premiums from accounting records.

7. Why do actuaries use loss development factors, and how do they apply them? (4 points)

Answer: Because insurers cannot wait for loss data to mature before revising rates, actuaries evaluate several years of loss data to determine trends in how these data have developed. Data analysis produces loss development factors. Immature data are then multiplied by a loss development factor to produce a sound estimate of the data that will result when losses have fully matured.

8. What are the seven items that a rate filing must generally include? (7 points)

Answer:

- 1) Schedule of the proposed new rates
- 2) Statement about the percentage change in the statewide average rate
- 3) Explanation of why the same percentage change does not apply to all territories and rating classes if applicable
- 4) Data to support the proposed rate changes, including territorial and class relativities
- 5) Calculation showing how investment income is reflected in the rates, if applicable
- 6) Expense provision data
- 7) Explanatory material to enable state insurance regulators to understand and evaluate the filing

Assignment 8—Quiz

1. What are the two primary goals of the claim function? (2 points)
2. Briefly describe why claim information is important to underwriting. (4 points)
3. Briefly describe the advantages and disadvantages of a centralized claim operation. (2 points)
4. Briefly explain the difference between independent adjusters and public adjusters. (4 points)
5. Briefly outline the four steps in the claim adjusting process. (4 points)

Assignment 8—Quiz Answers

1. What are the two primary goals of the claim function? (2 points)

Answer:

- 1) Complying with the contractual promise
- 2) Supporting the insurer's profit goal

2. Briefly describe why claim information is important to underwriting. (4 points)

Answer: A post-loss evaluation could reveal characteristics of the loss exposure that an underwriter should have detected when the application was originally reviewed. It can uncover operations and activities that the underwriter would have investigated more thoroughly had they been apparent on the application. It can also reveal when material aspects of the insured loss exposure have changed since the policy was first underwritten. Losses create opportunities for underwriters to take corrective action through loss control, cancellation, or nonrenewal.

3. Briefly describe the advantages and disadvantages of a centralized claim operation. (2 points)

Answer: Centralized operations can be more efficient than decentralized operations in terms of cost of office rental, supervisory overhead, information systems support, and support staff. However, because many claim tasks, such as property inspections and witness interviews, cannot be done as well from a remote location, claims can never be centralized as effectively as can underwriting or processing support functions.

4. Briefly explain the difference between independent adjusters and public adjusters. (4 points)

Answer: Independent adjusters handle claims for insurers on a case-by-case basis for a fee. Public adjusters represent policyholders to negotiate a settlement with the insurer in exchange for a fee or percentage of the settlement.

5. Briefly outline the four steps in the claim adjusting process. (4 points)

Answer:

- 1) Determine whether the loss is covered by the applicable policy
- 2) Determine the cause of loss and legal liability, if any
- 3) Determine the amount of damages or extent of loss
- 4) Settle the claim

6. Briefly describe the purpose of a reservation of rights letter and a nonwaiver agreement and the difference between them. (5 points)

Answer: Both a reservation of rights letter and a nonwaiver agreement are issued when coverage is uncertain. Both allow the adjuster to continue to investigate a claim without voiding the insurer's right to disclaim coverage later. The only difference is that the reservation of rights letter is issued unilaterally by the insurer, and the nonwaiver agreement contains the signature and consent of the policyholder.

7. Claim reports fall into four categories. What are those categories? (2 points)

Answer:

- 1) Preliminary
- 2) Status
- 3) Summarized
- 4) Closing

8. Bulk reserves are developed to estimate three things. What are those three things? (3 points)

Answer:

- 1) The growth in reported case reserves
- 2) The losses that are assumed to have happened but that have not yet been reported
- 3) The additional cost of claims that are reopened after having been settled and closed

9. List and briefly describe the three methods of establishing case reserves. (6 points)

Answer:

- 1) In the judgment method, the amount that will eventually be paid to settle the claim is estimated by a claim adjuster or another claim specialist.
- 2) In the average value method, a predetermined dollar amount of reserve is established for each claim as it is opened.
- 3) In the tabular method, an “average” amount is established for all claims that have similar characteristics in terms of the claimant’s age, health, and marital status.

10. List eight nonfinancial measures used to evaluate the claim function. (4 points)

Answer:

- 1) Turnover of claims
- 2) Average cost of settlement
- 3) Number and percentage of litigated files
- 4) Litigation win/lose ratios
- 5) Ratio of allocated to unallocated costs
- 6) Average caseload per adjuster
- 7) Staff turnover
- 8) Customer satisfaction

Assignment 9—Quiz

1. Briefly outline the varieties of insurable interests an individual might have in property. (9 points)
2. What three questions can adjusters ask to determine whether a fixture is real property or personal property? (3 points)
3. List four causes of loss for which coverage can be difficult to verify. (4 points)
4. If a fire occurs in a building that has previously suffered extensive and obvious termite damage, how should the adjuster proceed, and why? (6 points)
5. Policies commonly value property in any of four ways. Briefly describe these four methods. (8 points)

Assignment 9—Quiz Answers

1. Briefly outline the varieties of insurable interests an individual might have in property. (7 points, one for each of the concepts or elements in the sample answer below)

Answer:

- An individual might be the sole owner of property, which is a complete interest.
- In joint ownership, owners have an indivisible interest in the property.
- Joint ownership by spouses is referred to as tenancy by entireties.
- In the case of ownership in common, each owner has an identifiable fractional interest in the property.
- A person can have an interest in property that is not an ownership interest; lessees have an interest in the use of property for the life of the lease.
- Custodians, such as bailees, have an interest in property for their fees and for its safe return to its owners.
- Security interests can exist in almost any property.

2. What three questions can adjusters ask to determine whether a fixture is real property or personal property? (3 points)

Answer:

- 1) How permanently attached is it to the real property?
- 2) Is it well adapted to the real property?
- 3) What was the owner's intent?

3. List four causes of loss for which coverage can be difficult to verify. (4 points)

Answer:

- 1) Water damage
- 2) Collapse
- 3) Theft
- 4) Vandalism

4. If a fire occurs in a building that has previously suffered extensive and obvious termite damage, how should the adjuster proceed, and why? (6 points)

Answer: Termite damage would be a gradual cause of loss and therefore excluded. The adjuster must separate the damage caused by the termites from that caused by the fire and pay for only the fire damage. The value of the fire damage would be limited to the extent that the building's value has been diminished by the termite damage.

5. Policies commonly value property in any of four ways. Briefly describe these four methods. (8 points)

Answer:

- 1) Replacement cost is the cost to repair or replace property using new materials of like kind and quality with no deduction for depreciation.
- 2) Actual cash value is the replacement cost of property minus depreciation.
- 3) Stated amount is the least of the actual cash value, the cost to repair or replace, or the applicable amount of insurance for the property.
- 4) Agreed amount is the value that the insurer and insured agree on at the time the policy is written and that will be paid in the event of a total loss to the property.

6. List five of the insured's duties after a loss. (5 points)

Answer:

- 1) Provide prompt notice of loss to insurer
- 2) Protect property from further damage
- 3) Assist with the loss adjustment process
- 4) Provide a written proof of loss
- 5) Submit to examination under oath, when required

7. Following a serious loss to a home, what should an adjuster's three priorities be? (3 points)

Answer:

- 1) Ensuring the physical safety of the policyholder's family
- 2) Ensuring the safety and security of the damaged home and its contents to prevent further damage
- 3) Explaining the coverage and adjustment procedure to the policyholder.

8. When adjusting business income claims, on what three issues should adjusters focus in order to organize and simplify their task? (3 points)

Answer:

- 1) Identifying the best loss settlement approach
- 2) Determining the business income loss
- 3) Determining the period of restoration

Assignment 10—Quiz

1. What are the four steps involved in settling a liability claim? (4 points)
2. When alleging negligence, what must the claimant prove? (4 points)
3. In bodily injury liability claims, settlements include payments for more than just medical expenses. List five other categories of damages an insurer might cover under bodily injury liability. (5 points)
4. What is a bad-faith claim? (4 points)
5. Under what circumstances might a claim adjuster use a structured settlement? (2 points)

Assignment 10—Quiz Answers

1. What are the four steps involved in settling a liability claim? (4 points)

Answer:

- 1) Determining coverage
- 2) Determining legal liability
- 3) Determining damages
- 4) Negotiating and settling the claim

2. When alleging negligence, what must the claimant prove? (4 points)

Answer:

- 1) A legal duty was owed to the claimant
- 2) A breach of that duty caused harm
- 3) A causal connection between the breach and the harm, or proximate cause
- 4) Actual bodily injury or damage on the claimant's part

3. In bodily injury liability claims, settlements include payments for more than just medical expenses. List five other categories of damages that an insurer might cover under bodily injury liability. (5 points, one for any one of the categories listed below)

Answer:

- Loss of earnings
- Pain and suffering
- Permanent injury, or loss of earning capacity
- Disfigurement
- Loss of consortium
- Future damages
- Survival actions
- Wrongful death actions

4. What is a bad-faith claim? (4 points)

Answer: A claim that implies or involves actual or constructive fraud, a design to mislead or deceive another, or a neglect or refusal to fulfill some good-faith duty or some contractual good-faith obligation.

5. Under what circumstances might a claim adjuster use a structured settlement? (2 points)

Answer: When the claimant is likely to experience regular damages into the future, or when the adjuster suspects that the claimant might be unable to effectively manage a lump-sum payment.

6. What is a summons? (3 points)

Answer: A legal document issued by the clerk of the court requiring the sheriff or another officer to notify the person named that an action has commenced against him or her and that he or she must answer the complaint.

7. What two factors are accident reconstruction experts most helpful in determining? (2 points)

Answer: Vehicle speed and what a driver should have been able to see at the time of an accident

8. What do premises liability claims generally involve? (2 points, 1 for minor and 1 for fall-down OR slip-and-fall)

Answer: Premises liability claims are usually relatively minor fall-down or slip-and-fall claims.

9. For claims involving operations liability, what should the claim adjuster try to do immediately? (4 points)

Answer: The adjuster should immediately try to preserve the accident scene through photos, diagrams, and detailed measurements.

10. What type of insurance coverage would apply to third-party-over claims and dual capacity claims? (1 point)

Answer: Employers' liability insurance

Assignment 11—Quiz

1. List the six functions that reinsurance serves. (6 points)

2. Briefly explain the difference between treaty reinsurance and facultative reinsurance. (4 points)

3. Alpha Insurance has purchased a quota share treaty with a \$500,000 limit and a retention of 30 percent. Alpha has written a building policy with a limit of \$200,000 and a premium of \$1,000. The insured suffers a \$60,000 loss. Complete the following table by inserting the appropriate values. (6 point)

	Primary's portion	Reinsurer's portion
Insurance provided		
Premium obtained		
Loss paid		

4. What two types of treaty reinsurance provide surplus relief? (2 points)

5. What type of treaty reinsurance has the main purpose of protecting against catastrophic losses from one event? (1 point)

Assignment 11—Quiz Answers

1. List the six functions that reinsurance serves. (6 points)

Answer:

- 1) Stabilize loss experience
- 2) Improve large-line capacity
- 3) Provide catastrophe protection
- 4) Provide surplus relief
- 5) Provide underwriting guidance
- 6) Facilitate withdrawal from a territory or type of business

2. Briefly explain the difference between treaty reinsurance and facultative reinsurance. (4 points)

Answer: Treaty reinsurance is an agreement in which the primary insurer agrees to cede certain types of loss exposures, and the reinsurer agrees to accept the loss exposures that fall within the treaty. Facultative reinsurance is an agreement that is negotiated separately for each loss exposure the primary insurer wants to reinsure and that gives the reinsurer the right to accept or reject each loss exposure.

3. Alpha Insurance has purchased a quota share treaty with a \$500,000 limit and a retention of 30 percent. Alpha has written a building policy with a limit of \$200,000 and a premium of \$1,000. The insured suffers a \$60,000 loss. Complete the following table by inserting the appropriate values. (6 points)

Answer:

	Primary's portion	Reinsurer's portion
Insurance provided	\$150,000	\$350,000
Premium obtained	\$300	\$700
Loss paid	\$18,000	\$42,000

4. What two types of treaty reinsurance provide surplus relief? (2 points)

Answer:

- 1) Pro rata quota share
- 2) Pro rata surplus share

5. What type of treaty reinsurance has the main purpose of protecting against catastrophic losses from one event? (2 points)

Answer: Excess of loss per occurrence

6. Briefly describe four reasons that primary insurers would use facultative reinsurance. (4 points)

Answer:

- 1) An insurer might not have a treaty covering a particular type of insurance because it rarely writes that type of insurance.
- 2) An insurer can use facultative insurance to cede those loss exposures excluded under its applicable treaties.
- 3) An insurer can cede facultatively the portion of a loss exposure that exceeds the reinsurance treaty's limit.
- 4) An insurer can use facultative reinsurance to protect its treaties from adverse loss experience.

7. Briefly describe finite risk reinsurance. (4 points)

Answer: This is a nontraditional reinsurance agreement for a limited amount of risk on which anticipated investment income is expressly acknowledged as an underwriting component. It can be arranged to protect an insurer against a combination of traditionally insurable loss exposures and traditionally noninsurable loss exposures. It usually transfers very little or no underwriting risk; rather it usually transfers investment risk, timing risk, or both.

8. List the six most important factors to consider when designing a comprehensive reinsurance program. (6 points)

Answer:

- 1) Stability of loss frequency and severity
- 2) Loss exposures subject to catastrophes
- 3) Number of exposure units
- 4) Available financial resources
- 5) Stability and liquidity of investment portfolio
- 6) Growth plans

9. What are a reinsurer's five principal considerations in underwriting a reinsurance treaty? (5 points)

Answer:

- 1) The primary insurer's management characteristics
- 2) The primary insurer's financial strength
- 3) The primary insurer's underwriting policies and underwriting results
- 4) The existence and terms of other reinsurance
- 5) The primary insurer's loss experience

10. What is an intermediary clause in a reinsurance agreement, and what purpose does it serve? (4 points)

Answer: An intermediary clause is a required clause that indicates that the reinsurance intermediary is the reinsurer's agent for collecting reinsurance premiums and paying reinsurance claims. It places the risk of the intermediary's insolvency on the reinsurer rather than on the primary insurer.

Assignment 12—Quiz

1. Briefly outline the four groups of people who use insurer financial statements and the ways in which they use them. (8 points)
2. Outline the principal elements of an insurer's balance sheet, organized in the way they would appear. (6 points)
3. Outline the principal elements of an insurer's income statement, organized in the way they would appear. (4 points)
4. What is included on the Title Page and Jurat of the NAIC Annual Statement? (4 points)
5. Briefly describe what is included in the General Interrogatories section of the NAIC Annual Statement, and provide an example. (2 points)

Assignment 12—Quiz Answers

1. Briefly outline the four groups of people who use insurer financial statements and the ways in which they use them. (8 points)

Answer:

- 1) Corporate managers use financial information in planning, monitoring company performance, and allocating resources.
 - 2) Investors expect a satisfactory return on their investment and will move their investment if expected returns do not materialize.
 - 3) Regulators depend on insurer financial statements to make decisions about the financial requirements, surplus levels, and reserve amounts for individual insurers.
 - 4) Policyholders, producers, and risk managers are interested in the financial stability of the insurers with which they do business.
2. Outline the principal elements of an insurer's balance sheet, organized in the way they would appear. (6 points)

Answer:

Assets	Liabilities
Bonds	Losses
Stocks	Loss Adjustment Expenses
Cash	Unearned Premiums
Premium Balances	Surplus and Other Funds
Reinsurance Recoverables	Surplus as Regards Policyholders (or Policyholders' Surplus)

Note to instructor: This question is not representative of a question we would ask on the exam; however, it opens the door for discussion on a topic students struggle with and also helps them to put all the pieces of financial statements together.

3. Outline the principal elements of an insurer's income statement, organized in the way they would appear. (4 points)

Answer:

Earned Premiums
– Losses Incurred
– Loss Adjustment Expense Incurred
– Other Underwriting Expenses
<hr/> Net Underwriting Gain (or Loss)
+ Investment Income
+ Net Realized Capital Gains (or Losses)
<hr/> Net Income (Before Dividends or Taxes)

Note to instructor: This question is not representative of a question we would ask on the exam; however, it opens the door for discussion on a topic students struggle with and also helps them to put all the pieces of financial statements together.

4. What is included on the Title Page and Jurat of the NAIC Annual Statement? (4 points)

Answer: The Title Page and Jurat includes the legal name and NAIC company code number for the filing company, a contact for the purposes of the Annual Statement, and a list of the directors of the company; it is authenticated and signed by the company's president, secretary, and treasurer.

5. Briefly describe what is included in the General Interrogatories section of the NAIC Annual Statement, and provide an example. (2 points)

Answer: The General Interrogatories explore matters not necessarily revealed by financial statements (i.e., changes in corporate charter or bylaws; dealings with affiliated entities, foreign owners, directors, officers or shareholders; control of capital stock by others; dealings with trade associations; unusual exposures and reinsurance arrangements; receipt of promissory notes and letters of credit in lieu of premium).

6. Briefly outline the basic function of Schedule P, Analysis of Losses and Loss Exposures, in the NAIC Annual Statement. (2 points)

Answer: The crucial purpose of Schedule P is to provide information to analyze loss reserve and incurred loss development.

7. Briefly describe the types of information that should be included in the Supplement to the Annual Statement called "Management Discussion and Analysis." (3 points)

Answer: In this section the insurer's management should explain all material changes in the insurer's financial reports, all material trends, and all material events known to management.

8. What is the difference between admitted and nonadmitted assets under SAP? (4 points)

Answer: Admitted assets are those assets that meet minimum standards of liquidity that an insurer is allowed to report on its balance sheet in accordance with SAP. Nonadmitted assets are those that are not readily marketable and that are excluded from an insurer's balance sheet in accordance with SAP.

9. Briefly describe the main difference in the purpose and focus of GAAP and SAP. (4 points)

Answer: The main purpose of GAAP is to meet the varying needs of the different users of financial statements; the focus is on correctly measuring earnings. The purpose of SAP is to address the concerns of insurance regulators; the focus is on correctly measuring liquidation values and ability to pay claims in future.

Assignment 13—Quiz

1. What does the capacity ratio measure, and what is considered to be an acceptable capacity ratio? (4 points)

2. (a) Which ratio is calculated as follows, (b) what does it indicate about an insurer, and (c) at what value is it considered undesirable? (3 points)

$$\frac{\text{Cash + Invested assets at market value}}{\text{Unearned premium reserve + Loss and loss adjustment expense reserves}}$$

3. What is the formula for calculating an insurer's loss ratio? (3 points)

4. What is the formula for calculating an insurer's trade basis expense ratio? (2 points)

5. What is the formula for calculating an insurer's operating ratio? (2 points)

Assignment 13—Quiz Answers

1. What does the capacity ratio measure? (4 points)

Answer: The capacity ratio, or premium-to-surplus ratio, measures the extent to which insurers can issue policies for new business by comparing an insurer's net written premiums to policyholders' surplus. A ratio of 3-to-1 or less is considered acceptable.

2. (a) Which ratio is calculated as follows, (b) what does it indicate about an insurer, and (c) at what value is it considered undesirable? (3 points)

Answer:

- (a) This is the calculation for the liquidity ratio.
- (b) It measures the extent to which an insurer can meet its obligations as they come due.
- (c) A ratio of less than 1 indicates an undesirable situation.

3. What is the formula for calculating an insurer's loss ratio? (3 points)

Answer: Loss ratio = (Incurred losses + Loss adjustment expense) ÷ Earned premiums.

4. What is the formula for calculating an insurer's trade basis expense ratio? (2 points)

Answer: Expense ratio (trade basis) = Expenses incurred ÷ Net written premiums.

5. What is the formula for calculating an insurer's operating ratio? (2 points)

Answer: Operating ratio = Combined ratio – Investment income ratio.

6. List five of the most useful liquidity tests used by Best's Ratings. (5 points)

Answer:

- 1) Quick liquidity ratio
- 2) Current liquidity ratio
- 3) Overall liquidity ratio
- 4) Operating cash flow test
- 5) Class 3-6 bonds to PHS ratio

7. In addition to liquidity tests, what other types of quantitative tests does Best's Ratings perform to evaluate insurers' financial strength? (3 points)

Answer:

- 1) Leverage tests
- 2) Loss reserve tests
- 3) Capital adequacy tests.

8. List six areas in which Best's Ratings use qualitative tests to evaluate aspects of an insurer's operations. (Any 6, 1 point for each correct answer.)

Answer:

- Capital structure of insurer holding companies
- Reinsurance agreement analysis
- Loss reserve adequacy
- Quality and diversity of investments
- Spread of risk
- Management
- Market position
- Surplus adequacy
- Event risk

9. An insurer scores 25 percent on the NAIC's IRIS surplus aid to policyholders' surplus ratio. What would regulators' reaction be? (2 points)

Answer: Regulators would be concerned about the quality of the insurer's reinsurance treaties and the threat to solvency if treaties are canceled.

10. In the NAIC's IRIS system, what might be indicated by a high one-year reserve development to policyholders' surplus ratio? (2 points)

Answer: A high ratio on this test might indicate that the insurer's loss reserves are inadequate and that its surplus has consequently been overstated.

Assignment 14—Quiz

1. What does a sound investment strategy seek to do? (2 points)
2. How do state regulators promote prudent, well diversified investment portfolios for insurers? (2 points)
3. What is interest rate risk? (3 points)
4. What is cash matching? (2 points)
5. Briefly outline three important characteristics of duration. (6 points)

Assignment 14—Quiz Answers

1. What does a sound investment strategy seek to do? (2 points for either of the correct answers listed below)

Answer:

- Earn the highest possible return for a given level of risk
- Minimize the risk associated with earning a given expected return.

2. How do state regulators promote prudent, well diversified investment portfolios for insurers? (2 points)

Answer: State regulators promote prudent, well diversified investment portfolios through asset restrictions and investment restrictions.

3. What is interest rate risk? (3 points)

Answer: The risk that a security's future value will decline because of changes in interest rates

4. What is cash matching? (2 points)

Answer: The process of matching an investment's maturity value with the amount of expected loss payments

5. Briefly outline three important characteristics of duration. (6 points, 2 for each correct answer)

Answer:

- 1) The greater the duration, the more sensitive the security is to interest rate changes
- 2) The duration of a zero-coupon bond is always equal to its time to maturity
- 3) The duration of a bond that pays interest over its life will always be less than its time to maturity

6. What are the three components of an IBNR reserve? (3 points)

Answer:

- 1) Reserves for unreported losses
- 2) Reserves for losses that have been reported but for which the established case reserves are inadequate
- 3) Reserves for losses that have been settled and then reopened

7. Briefly describe the process of accident-year loss analysis. (5 points)

Answer: This technique uses loss triangles to calculate loss development multipliers for each year of loss experience and each development period. The mean of these multipliers is calculated for each development period. That mean can be used as the selected multiplier, or it can be adjusted to create the selected multiplier. The ultimate multiplier, which is used to project immature loss data to full maturity, is calculated from these selected multipliers.

8. Name and briefly describe the four action levels in the NAIC's risk-based capital system. (4 points)

Answer:

- 1) Company action level—Insurer files a comprehensive plan for corrective action.
- 2) Regulatory action level—Regulator conducts exam as necessary, and insurer files comprehensive plan.
- 3) Authorized control level—Regulator may seize control.
- 4) Mandatory control level—Regulator required to place insurer under regulatory control.

Assignment 15—Quiz

1. What are the four steps in the strategy formulation process? (4 points)
2. What are the Five Forces that Michael E. Porter describes as driving competition? (5 points)
3. List three corporate-level strategies available for companies in a growth mode and three that can be used in a decline mode. (6 points)
4. What four steps are involved in the organizational control process? (4 points)
5. What are six factors a company must investigate and evaluate when considering entering a foreign market? (6 points)

Assignment 15—Quiz Answers

1. What are the four steps in the strategy formulation process? (4 points)

Answer:

- 1) Creating mission and vision statements
- 2) Establishing organizational goals
- 3) Analyzing the external and internal environments
- 4) Determining strategy at different organizational levels

2. What are the Five Forces that Michael E. Porter describes as driving competition? (5 points)

Answer:

- 1) Threat of new entrants
- 2) Threat of substitute products or services
- 3) Bargaining power of buyers
- 4) Bargaining power of suppliers
- 5) Rivalry among existing firms

3. List three corporate-level strategies available for companies in a growth mode, and three that can be used in a decline mode. (6 points, 1 for each strategy)

Answer:

Growth Mode

- 1) Single business strategy
- 2) Vertical integration
- 3) Diversification

Decline Mode

- 1) Harvest strategy
- 2) Turnaround strategy
- 3) Divestiture strategy

4. What four steps are involved in the organizational control process? (4 points)

Answer:

- 1) Establish standards
- 2) Create and apply measurements
- 3) Compare actual results to standards
- 4) Evaluate and implement corrective actions if goals are not met

5. What are six factors a company must investigate and evaluate when considering entering a foreign market? (6 points)

Answer: A company must consider differences in culture, language, regulations, and laws; as well as the country's economic environment, and any political risks.

6. What four methods could a company use to enter the global markets? (4 points)

Answer:

- 1) Exporting
- 2) International licensing
- 3) Franchising
- 4) Foreign direct investment

7. Incidental international loss exposures include those arising from activities conducted outside the U.S. Provide three examples of this type of loss exposure. (3 points, 1 for any of the loss exposures listed below to a maximum of 3 points)

Answer:

- Overseas travel by company representatives
- Sales made in foreign countries
- Participation in foreign trade shows or exhibits
- Small, pilot sales offices
- Imports from foreign countries

8. Outline four advantages and four disadvantages of admitted insurance for multinational loss exposures. (8 points)

Answer:

Advantages

- 1) Favorable local tax laws
- 2) Premiums and losses paid in the local currency
- 3) Easier compliance with government laws and regulations
- 4) Insurance costs reflected according to exposure

Disadvantages

- 1) Higher premiums required
- 2) Policies might be written in a foreign language
- 3) Risk management philosophy may be difficult to establish
- 4) Solvency of locally admitted insurer might be difficult to determine