

## Chapter 6

### Insurance Company Operations

#### QUESTION one ( Multiple choice)

- 1- The function of an actuary is to
- a) Adjust claims
  - b) Determine premium rates
  - c) Negotiate reinsurance treaties
  - d) Invest insurance company assets

Answer

- 2- Insures obtain data that can be used to determine rates from
- a) Pricing pools
  - b) Insurance advisory organizations
  - c) Banks
  - d) Reciprocal exchanges

Answer

- 3- Which of the following statements about underwriting policy is(are) true?
- I- A company must establish an underwriting policy that is consistent with company objectives
  - II- underwriting policy is usually very subjective and allows the underwriter considerable flexibility with respect to lines to be written and forms to be used
- a) I only      b) II only      c) both I and II      d) neither I nor II

Answer

- 4- All of the following statements about underwriting standards are true  
Except
- a) The basic purpose of underwriting standards is to reduce adverse selection against the insurer.
  - b) The underwriter should select only those insureds who are expected to have no losses
  - c) The underwriter should select a book of business so that there is a proper balance within each rate classification.
  - d) Equitable rates should be charged so that each group of policyowners pays its own way in terms of losses and expenses

Answer

5- The underwriting process begins with the

- a) agent
- b) desk underwriter
- c) inspection report
- d) acceptance of application

Answer

6- Common sources of underwriting information for life and health insurance include all of the following Except

- a) The application
- b) A physical examination
- c) The medical information Bureau
- d) The insured's income tax return

Answer

7- Information contained in an inspection report may include all of the following Except

- a) How long the agent has known the applicant
- b) The applicant's marital status
- c) The applicant's police record
- d) Whether the applicant has ever declared bankruptcy

Answer

8- Information provided to life insurance underwriters by Medical Insurance Bureau includes which of the following?

- I- The previous underwriting decisions of member companies
- II- Health impairments about which member companies have knowledge

- a) I only
- b) II only
- c) both I and II
- d) neither I nor II

Answer

9- Factors that may result in more restrictive underwriting decisions include which of the following?

- I- Inadequate rates
- II- The unavailability of reinsurance on favorable terms

- I only
- b) II only
- c) both I and II
- d) neither I nor II

Answer

10- All of the following are functions of marketing department of an insurance company Except

- a) To advertise the insurer's products.
- b) To develop new products
- c) To identify production goals
- d) To make final underwriting decisions

Answer

11- Which of the following statements about claim settlement is (are) true?

- I- The fair payment of claims requires an insurer to adopt a very liberal claims policy.
- II- To prevent possible lawsuits, an insurer should provide no personal assistance to a claimant other than that which is required by contractual obligations

- a) I only
- b) II only
- c) both I and II
- d) neither I nor II

Answer

12- All of the following statements about adjustors are true Except

- a) agents may have the authority to settle claims
- b) independent adjustors may be used in a geographic area where the volume of business is too low for an insurer to have its own adjustors
- c) company adjustors are salaried employees who work for one insurer
- d) a public adjustor is usually paid a flat fee that is independent of the size of a claim

Answer

13- Which of the following statements about adjustment bureau is (are) true?

- I- They are frequently used to settle claims when a large number of losses in a given geographic locations as a result of a catastrophic event
- II- Their major advantage is low cost because of the use of part-time adjustors.

- a) I only
- b) II only
- c) both I and II
- d) neither I nor II

Answer

14- All of the following statements about the steps in the settlement of a claim are true Except

- a) The insurance policy usually has a provision specifically how a notice of loss is made to the insurance company.

- b) One-step in the investigation of a claim is to determine whether the policy was in force when the loss occurred.
- c) The adjuster must file the proof of loss, which is a sworn statement supporting his or her decision regarding a claim
- d) A policy provision may determine how disputes regarding claim settlements are resolved.

Answer

15- All of the following statements about reinsurance are true Except

- a) A reinsurer may also purchase reinsurance
- b) Reinsurance involves the shifting of all or part of the insurance originally written by one insurer to another insurer
- c) The insurer transferring business is called the ceding company.
- d) The amount of insurance given to a reinsurer is called the net premium.

Answer

16- All of the following are reasons for the use of reinsurance by primary insurer Except

- a) To increase the unearned premium reserve
- b) To increase underwriting capacity
- c) To protect against catastrophic losses
- d) To stabilize profits

Answer

17- The unearned premium reserve of an insurer is

- a) An asset that represents the investments made with premium income
- b) A liability that represents the unearned portion of gross premiums on outstanding policies
- c) A liability that represents claims that have been incurred but not yet paid.
- d) The portion of the insurer's net worth that belongs to policyowners

Answer

18- A reinsurer contract that is entered into on a case-by- case basis after an application for insurance is received by a primary insurer is called

- a) Reinsurance pool
- b) An automatic treaty
- c) A retrocession
- d) Facultative reinsurance

Answer

19- Which of the following statements about treaty reinsurance is true?

- a) The reinsurer is required to underwrite each individual applicant that is reinsured.
- b) The reinsurer must accept all business that falls within the scope of the treaty.
- c) The ceding insurer can choose which business falling within the scope of treaty it wishes reinsure.
- d) It protects the reinsurer by requiring the ceding insurer to charge adequate premiums.

Answer

20- Which of the following statements about treaty reinsurance is true?

- a) Under a surplus share treaty, 100 percent of the ceding insurer's liability must be transferred to reinsurer.
- b) The use of quota-share treaty increases the ceding insurer's unearned premium reserve.
- c) Under an excess of loss treaty ,the reinsurer pays losses in full only if they are less than the ceding insurer's retention limit.
- d) The use of a reinsurance pool provides the financial capacity to write large amounts of insurance.

Answer

21- Delta insurance company has a surplus share treaty with Misr Reinsurance. Delta has a retention limit of \$200,000 and nine lines of insurance are ceded to Misr. How much will Misr pay if a \$1,600,000 building insured with Delta suffers an \$800,000?

- a) \$600,000
- b) \$700,000
- c) \$720,000
- d) \$800,000

Answer

22- Huge Insurance Company is a property insurer that is interested in protecting itself against cumulative losses that exceed \$20 million during the year . this protection can be obtained with

- a) A quota share treaty
- b) A surplus share treaty
- c) An excess of loss treaty
- d) Facultative reinsurance

Answer

- 23- All of the following statements about life insurance investments are true Except
- a) Funds for these investments are derived primarily from premium income ,investment earning ,and maturing investments that must be reinvested.
  - b) Income from these investments reduce the cost of insurance
  - c) A primary objective in making these investments is safety of principal
  - d) The majority of these investments are short-term.

Answer

- 24- Which of the following statements about the investments of property and liability insurers is (are) true?

- I- Income from these investments is important in offsetting unfavorable underwriting experience.
- II- Because the premium income is continually being received ,the investment objective of liquidity is of little importance.

- a) I only      b) II only      c) both I and II      d) neither I nor II

Answer

- 25- Functions of an insurance company legal department include which of the following?

- I- Lobbying for legislation favorable to the insurance industry
- II- Drafting policy provisions

- a) I only      b) II only      c) both I and II      d) neither I nor II

Answer

- 26- Abeer is employed by an insurance company. She reviews applications to determine whether her company should insure the applicant. If insurable, Abeer assigns the applicant to a rating category based on applicant's degree of risk. Abeer is a(an)

- a) Underwriter
- b) Actuary
- c) Producer
- d) Claims adjustor

Answer

- 27- Ahmed is a claim adjustor for LMN insurance Company. He is periodically contacted by LMN or by an insured and told that there has been a loss. The first step in claims process that Ahmed should follow is to

- a) Determine the amount of the loss

- b) Attempt to deny the claims regardless of whether he believes the claim is covered
- c) Verify that a covered loss has occurred
- d) Delay paying the claim if the claim is covered

Answer

28- Little liability insurance Company (LLIC) traditionally has written small liability loss exposures. Recently, a regional airline approached LLIC to see if the company would be interested in writing the airline's liability coverage. Before agreeing to write the coverage, LLIC shopped for reinsurance that would apply only to the airline coverage. LLIC found a reinsurer and entered into an agreement an agreement to reinsure the airline's liability exposure. Under terms of the agreement, LLIC would retain 25 percent of the premium and pay 25 percent of the losses and the reinsurer would receive 75 percent of the premium and would pay 75 percent of the losses. This reinsurance arrangement is best described as

- a) Excess of loss
- b) Surplus share
- c) Quota share
- d) Reinsurance pool

Answer

29- Mahmoud studied engineering in college. After graduation ,he went to work for an insurance company. Mahmoud visits properties insured by his company . he conducts inspections on behave of the insurer and makes recommendations about alarm systems,sprinkler systems,occupational health and building construction. In what functional area of the insurance company does Mahmoud work?

- a) Underwriting
- b) Loss control
- c) Data processing and management
- d) Claim adjusting

Answer

30- Samy heads the legal staff of a large property and liability insurance company. Samy's staff is most likely involved in all of the following activities Except

- a) Reviewing policy wording before policies are adopted and marketed.
- b) Recouping subrogation recoveries from third parties who injured individuals insured by Samy 's company

- c) Providing legal advice about marketing, taxation, and insurance law.
- d) Reviewing applications to determine if the company should insure the risk.

Answer

31- Mohamed Osman double majored in mathematics and statistics while in college. He also enrolled in a number of finance courses. After graduation, Mohamed Osman was hired by Misr Insurance Company. His job is to calculate premiums rates for life insurance coverages. Mohamed Osman is a(an)

- a) Actuary
- b) Underwriter
- c) Claims adjuster
- d) Producer

Answer

32- Al taawania Insuranc Company requires insureds who suffer a loss to submit a sworn statement to substantiate that a loss occurred and to describe the conditions under which the loss occurred. This sworn statement is called a

- a) Binder
- b) Proof of loss
- c) claims report
- d) notice of loss

Answer

33- All of the following are methods that a property and liability company can use to protect against catastrophic losses Except

- a) Sale of catastrophe bonds
- b) Purchase of common stock
- c) Purchase of reinsurance
- d) Purchase of catastrophe insurance options

Answer

34- Which of the following is (are) true with respect to catastrophe bonds?

I- These bonds are issued by U.S. Government .

II- These bonds pay relatively high yields

- a) I only
- b) II only
- c) both I and II
- d) neither I nor II

Answer

- 35- All of the following statements about regulatory objectives of insurance ratemaking are Except
- a) One purpose of rate adequacy is to maintain the solvency of insurers
  - b) Rates are adequate if they are high enough to pay all losses and expenses.
  - c) Insurers know in advance if the coverages marketed will be profitable ,so rate regulation is not needed
  - d) Rates are excessive if policyowners are paying substantially moer than the actual value of their protection

Answer

- 36- All of the following statements about business objectives in designing a rating system are true Except
- a) The rating system should encourage loss control activities.
  - b) The rating system should be independent of long-run changes in economic conditions
  - c) The rating system should be simple to understand.
  - d) The rating system should be stable over short periods so that consumer satisfaction can be maintained

Answer

- 37- The unit of measurement used in insurance pricing is called the
- a) Unit rate
  - b) Premium
  - c) Exposure unit
  - d) Experience unit

Answer

- 38- The portion of an insurance premium allocated to expenses ,profit,and a margin for contingencies is called
- a) Loading
  - b) Pure premium
  - c) Gross premium
  - d) Experience rate

Answer

- 39- All of the following statements about class rating are true Except
- a) Exposure with similar characteristics are placed in the same underwriting class

- b) The rate charged for each class reflects the average loss experience for that class
- c) The complexity of class rating make its use inappropriate for the personal lines market
- d) It is based on the assumption that future losses to insureds will be determined by the same classification factors currently in use

Answer

40- The gross premium for a participating life insurance policy is determined by adding a loading allowance to the net level premium. This loading allowance includes all of the following Except a

- a) Margin for dividends
- b) Provision for expenses
- c) Margin for contingences
- d) Provision for death claims

Answer

## **QUESTION Two**

### **TRUE FALSE QUESTIONS**

- 1- Public adjusters represent insurance companies in those areas where the insurer does not maintain a staff of adjusters.
- 2- The primary purpose of underwriting is to avoid adverse selection
- 3- Class rating is used when the loss producing characteristics of the exposures units to be insured vary widely.
- 4- The agent's role in underwriting is generally greater in property and liability field than in the field of life insurance
- 5- The gross premium is derived by adding the net premium to the pure premium
- 6- the use of the term "underwriter " in reference to an agent is more common in the field of life insurance than in the field of property and liability.

- 7- The financial status of the applicant is an important underwriting factor in both property insurance and life insurance.
- 8- Public adjusters represent the policyholders in the loss adjustment process.
- 9- Class rating is the most common approach used in insurance industry today and is used in both the life insurance industry and in the property and liability field.
- 10- Judgment rating is used primarily in the life insurance and health insurance

**QUESTION THREE (DEFINITIONS)**

**DEFINE THE FOLLOWING:-**

- 1- Ratemaking
- 2- Difference between insurance pricing and pricing in other industries.
- 3- Actuary
- 4- Underwriting
- 5- Production in insurance companies
- 6- Reinsurance
- 7- Retrocession
- 8- Facultative reinsurance
- 9- Treaty reinsurance
- 10- the Pro rata method
- 11- the Excess method
- 12- Quota-share treaty
- 13- Surplus-share treaty
- 14- Facultative treaty reinsurance
- 15- loss ratio
- 16- Expense ratio

17- Insurance company`s combined ratio

18- Insurance company`s investment income ratio

**QUESTION FOUR**

**Fill in**

- 1- The premium can be determined based upon -----and -----
- 2- premiums are determined by multiplying ----- by -----
- 3- Insurance pricing has some basic objectives, some of these objectives by statute .they are -----,-----,and-----
- 4- Class rates mean-----
- 5- The premium that the insured pays is called-----
- 6- The main objective of underwriting process is-----
- 7- Adverse selection means-----
- 8- To achieve objective of the underwriting three important principle are followed, they are:-----,-----,and-----
- 9- Underwriting is based number of principles , they are ----,----,and
- 10- The information of the underwriter comes from:-----,-----,-----  
----,-----,-----,-----,-----and-----
- 11- Production in insurance companies refers to-----
- 12- in insurance companies the agents are referred to as-----
- 13- Claim adjusting means-----
- 14- The employees who settle the losses are called-----
- 15- The adjusters include-----,-----,-----,-----,-----  
-,and-----
- 16- the settlement of a claim has four steps, they are:-----,-----  
-----,-----,-----,and-----
- 17- The Major types of claims adjustors include-----,-----  
-,-----,-----,-----,-----and-----
- 18- The ceding company is ---- and the reinsurer is -----

- 19- Benefits of reinsurance are -----,-----,-----,-----  
----,and----
- 20- Kinds of reinsurance are -----,---,-----,and----
- 21- Advantages of Treaty reinsurance include-----,----- -----,and--
- 22- Securitization of risk means -----,but Catastrophe bonds  
means -----,
- 23- Life insurance investments have an important economic and  
social impact on the nation for several reasons , they are ----,-----,--  
--,-----,-----and ---
- 24- Insurance companies also perform other functions. They  
include-----,-----,-----,-----,and----
- 25- Measurement of the performance of insurance company is  
illustrated by simple measurements , they are ----,-----,-----,-----  
and ---

### **QUESTION Five**

#### **First Applied Case**

If you are an underwriter for ABC Insurance. You received a life insurance proposal for medical insurance with premium payment. The prospect disclosed that he had undergone surgery to correct a cataract. As an underwriter, what would be your decision with respect to the case?

#### **Solution**

#### **Second Applied Case**

Mohamed Osman is a property claims adjustor for a large property insurer. Abeer is a policyholder who recently notified the company that the roof of her home incurred substantial damage because of a recent hail storm. Abeer owns her home and is insured under a standard homeowners policy with no special endorsement. What questions should Mohamed Osman ask before the claim is approved for payment by his company?

#### **Solution**

**Third Applied Case**

Delta insurance is a property insurer that entered into a surplus – share reinsurance treaty with Eversafe Re. Delta has a retention limit of \$200,000 on any single building , and up to nine lines of insurance may be ceded to Eversafe Re. A building valued at \$1,600,000

is insured with Delta. Shortly ,after the policy was issued ,a severe windstorm caused a \$800,000 loss to the building

- a- How much of the loss will Delta pay?
- b- How much of the loss will Eversafe Re pay?
- c- What is the maximum amount of insurance that Delta can write on a single building under reinsurance agreement? Explain your answer.

**Solution**