



Insurance Institute
Canada

CIP PROGRAM
EXAMINATION
April 2003

C72 INTRODUCTION TO RISK MANAGEMENT AND COMMERCIAL LINES INSURANCE

IMPORTANT

The time allowed for this exam is 3 hours.

Total marks: 200

You must hand in this paper and any paper used for rough work to the supervisor when you leave the examination room. Failure to do so may result in disqualification.

Section A: Multiple-Choice Questions

Question 1. For the following multiple-choice questions, fill in the circle of the letter that identifies the most correct answer.

Example: (A) (B) ● (D)

DO NOT MARK THE ANSWERS ON THESE PAGES.

USE THE FIRST PAGE OF YOUR ANSWER BOOK.

1. For an organization to achieve peace of mind it must operate within its tolerance level for uncertainty, which is the
- (A) measure of value an organization places on safety as opposed to physical assets.
 - (B) degree to which a business can fail to satisfy a customer demand and survive.
 - (C) extent to which a company feels it can self-insure a portion of risk with little real chance of loss.
 - (D) threshold beyond which an organization cannot survive financially.

continued over

2. The major financial responsibility for an organization following a loss is to
 - (A) maintain as many employees on the payroll as possible.
 - (B) survive.
 - (C) maintain market share.
 - (D) cover the costs to achieve operational continuity.

3. Change in consumer taste is an example of
 - (A) an economic peril.
 - (B) a physical peril.
 - (C) a human peril.
 - (D) a natural peril.

4. Which of the following is both a pre-loss objective and a post-loss objective of risk management?
 - (A) Social responsibility
 - (B) Peace of mind
 - (C) Survival
 - (D) Externally imposed obligations

5. The post-loss objective for a business that cannot survive even a few days of downtime is
 - (A) stable earnings.
 - (B) sustained growth.
 - (C) survival.
 - (D) operational continuity.

6. Almost nil, slight, moderate, and definite are classifications assigning the likely frequency of loss using the
 - (A) Law of Large Numbers.
 - (B) Key Factor Method.
 - (C) Frequency Forecast Model.
 - (D) Prouty Measures.

7. Regular inspection and testing of machinery, safety training programs and safety guards on machinery are
 - (A) exposure avoidance activities.
 - (B) risk transfer activities.
 - (C) loss reduction activities.
 - (D) loss prevention activities.

8. A passive retention is an exposure that is retained because
- (A) it is not insurable.
 - (B) the chance of loss is so remote it is insignificant.
 - (C) it was never identified.
 - (D) the likelihood of loss is predictable but the consequences will not be too serious.
9. An organization has a number of sources of funds to choose from to meet the costs of retained losses. When an account is set up on the balance sheet of the organization allocating funds for retained losses, but no cash or other assets are earmarked for it, the source is known as
- (A) loss expense.
 - (B) unfunded reserve.
 - (C) funded reserve.
 - (D) loss loan.
10. The **insurance method**, as a technique to minimize the effects of exposures, involves
- (A) sorting the kinds of insurance as essential, desirable, and available and then buying coverage starting with the essential, until the budget is used up.
 - (B) calculating the minimum and maximum expected losses and buying coverage starting with the minimum, until the budget for insurance is used up.
 - (C) considering the cost of each risk management technique and estimating the results of applying each technique to potential losses.
 - (D) evaluating other risk management alternatives to determine the potential for saving premium dollars through their use.
11. The major problem in applying the minimum expected loss method as a technique minimizing the effects of exposures is that,
- (A) it ignores risk management methods other than insurance.
 - (B) to be effective, the program requires regular re-evaluation and change as new exposures develop and old exposures change or are eliminated.
 - (C) loss costs are difficult to predict and capital expenditures for loss control must be adjusted to the short term.
 - (D) if a large capital expenditure is required the plan may have to wait until the company's next budget review.
12. A tangible benefit for the producer in using the risk management approach is
- (A) securing and retaining customers by providing value-added service.
 - (B) higher premiums making the producer more valuable to insurers.
 - (C) a reduction in the time and effort required to service clients.
 - (D) a more knowledgeable consumer leading to an improved public image of the industry as a whole.

13. Select the group of property that is confronted by the most perils and most severely endangered by those perils.
- (A) Buildings, bridges, dams and towers
 - (B) Furniture, fixtures and large display cases
 - (C) Office equipment, cash registers and books of account
 - (D) Contractor's equipment, factory work in progress and watercraft
14. Extra expense as a business interruption coverage includes
- (A) additional expense incurred by a business that must remain in operation despite a loss.
 - (B) additional cost to rent premises when the building will not be rebuilt following a loss.
 - (C) expense of paying sales staff to retain them when they temporarily have nothing to sell following a loss.
 - (D) costs that continue to accrue following a loss even though business operations stop.
15. An employee negligently carries out an assigned task and injures a third party. The employer is generally
- (A) not responsible for an act that is carried out in a negligent way.
 - (B) not responsible if the manner in which the task was completed was expressly forbidden.
 - (C) responsible for the employee's negligence along with the employee.
 - (D) solely responsible for the acts of the employee.
16. Professional bailees owe a greater degree of care than do gratuitous bailees because
- (A) of reliance on their expertise by the public.
 - (B) goods placed in their care are usually high in value and the resulting risk requires greater care.
 - (C) they hold other people's property for a fee.
 - (D) they perform a service on property for the benefit of the bailor.
17. In insurance, **real property** includes
- (A) concrete property as opposed to something intangible such as one's reputation.
 - (B) property subject to movement but not intended for frequent movement.
 - (C) property intended for frequent movement.
 - (D) land, buildings and other permanent structures on the land.
18. Which of the following methods of exposure identification maps the sequence of business activities through the use of graphic representation?
- (A) Financial statement
 - (B) Survey form
 - (C) Flow chart
 - (D) Questionnaire

19. Claims that arise out of the business activities of an employer, its employees and agents, either on or off its premises are
- (A) premises claims.
 - (B) operations claims.
 - (C) completed operations claims.
 - (D) contractual liability claims.
20. The **small loss principle** conveys the idea that
- (A) an insurer will take in what it pays out in losses.
 - (B) devastating exposures to loss should always be transferred.
 - (C) in most cases retaining liability exposures is unwise because outcomes are unpredictable.
 - (D) insurance on small, frequent losses is expensive.
21. With respect to risk management, the minimum expected loss method
- (A) analyzes the costs of different risk management techniques and estimates the cost of applying each technique to potential losses.
 - (B) is used to predict the amount of potential claims.
 - (C) involves the calculation of the cost of all possible insurance coverages and prioritizes them as essential, desirable or available.
 - (D) does not consider risk management methods other than insurance.
22. Rental value insurance indemnifies
- (A) the owner of a property if the owner's rental income is interrupted by an insured peril.
 - (B) tenants whose long-term lease is expiring and who must pay an increase, in excess of a stated percentage, under new rental terms.
 - (C) the owner/occupier of a property for the loss of use of premises, damaged by an insured peril.
 - (D) tenants' claims against the owner of a property for the loss of business profits.
23. The operation of a coinsurance clause is designed to
- (A) penalize those insureds that do not carry insurance close to full value.
 - (B) protect the insurer from paying the policy limits.
 - (C) index policy limits according to inflation rates.
 - (D) increase policy premiums mid-term.
24. Manuscript wordings for property
- (A) have been developed over the years to cover risks with distinctive needs.
 - (B) are specially drafted as a joint effort of the insurer and the insured, usually a large corporate client.
 - (C) are insurers' own versions of standardized named perils and all risks policy forms.
 - (D) allow a policy to be customized by adding riders, appropriate for the particular risk, to a standard basic form.

25. The major perils that one can usually expect to be covered on an all risks policy that are not found on the basic named perils form include
- (A) fire, vandalism, and leakage from fire protective equipment.
 - (B) explosion, water damage, and mechanical breakdown.
 - (C) theft, water damage, and transportation risks.
 - (D) earthquake, employee dishonesty, and marine shipments.
26. A waiver of subrogation on behalf of a tenant is achieved by
- (A) a repairs clause in a lease that makes the tenant responsible for repairs except for damage caused by fire and certain other perils.
 - (B) a clause in which the insurer agrees not to take over any right the landlord may have against a tenant for damage.
 - (C) a lease agreement that transfers the obligation for insuring the building to the tenant.
 - (D) an agreement between tenant and landlord stipulating the lessor is responsible for repairing or rebuilding following damage or destruction by an insured peril.
27. Personal injury coverage on a liability policy covers liability arising from
- (A) slander or libel of a person or organization.
 - (B) injury or property damage to a third party when the insured is legally liable.
 - (C) a moral obligation for injury that occurs on the insured's premises.
 - (D) injury, sickness or disease sustained by a person, including death resulting from any of these.
28. Umbrella liability policies are generally designed to
- (A) provide broader coverage in addition to increased limits.
 - (B) rely on the wording of the primary policy in determining the extent that coverage is provided.
 - (C) provide coverage that is either identical to or more restrictive than the primary policy.
 - (D) provide the same coverage as the primary policy with a cushion of limits at a higher level.
29. The Non-owned Automobile Policy exists because
- (A) a company car may occasionally need to be replaced by a temporary substitute automobile.
 - (B) an employee may drive his or her car to and from work even though it is not insured.
 - (C) when an automobile is used on an employer's behalf, the employer can be held accountable for its operation.
 - (D) an employer has a responsibility to hire drivers that are capable and competent.
30. The Profits approach to business interruption provides income restoration
- (A) until the damaged property has been restored.
 - (B) unless loss of profit results from application of a bylaw.
 - (C) during the period that results are affected by an insured peril.
 - (D) and the extra expenses incurred to keep a business going in spite of the loss.

31. A fire clause in a lease agreement
- (A) allows a landlord to cancel the lease if premises suffer a specified percentage of damage or will take more than a specified time period to repair.
 - (B) provides that if the premises are rendered wholly or partly untenantable, the rent either ceases or reduces in proportion to the damage.
 - (C) appears on long-term leases where a reduced rent has been agreed to and requires that rent continue unaffected should the premises be damaged.
 - (D) provides that rent continue unaffected should the premises be damaged as a result of the tenant's negligence.
32. Which of the following policies covers building and construction materials during construction?
- (A) Builders' Risk
 - (B) Commercial Building Form
 - (C) Wrap-up General Liability
 - (D) Commercial General Liability
33. Indirect losses
- (A) are excluded by insurance policies because they are one step removed in the chain of causation.
 - (B) may continue to accumulate long after the event that caused the loss is over.
 - (C) are hidden claims losses that cannot be quantified or recovered such as the time lost in having your car appraised following a collision.
 - (D) occur from external perils such as wind and hail rather than directly from the property itself.
34. The operating expenses that continue or may continue in the event of a partial or total shutdown of business covered under Profits business interruption coverage are called
- (A) average daily value.
 - (B) standing charges.
 - (C) daily indemnity.
 - (D) extra expense.
35. Which of the following would cover loss to maps and drawings including the cost of reworking them?
- (A) Building, Equipment and Stock form
 - (B) Office Contents Floater
 - (C) Valuable Papers and Records policy
 - (D) Commercial Property Floater

36. The Peak Season Endorsement, used to increase stock coverage at specified times of the year, is most effective for
- (A) small retail risks where stock values fluctuate seasonally.
 - (B) manufacturers where the product may be in various stages of completion.
 - (C) large retail risks where the stock amount fluctuates frequently.
 - (D) retail risks where the amount of stock throughout the year is fairly stable.
37. Which of the following risks would NOT be eligible for a package policy?
- (A) Motels
 - (B) Retail stores
 - (C) Condominiums
 - (D) Restaurants
38. A plate glass rider usually covers
- (A) interior shelving and mirrors in addition to exterior glass.
 - (B) damage during alterations.
 - (C) increased cost or repairs due to bylaws.
 - (D) glass lettering and ornamentation.
39. A liability policy that is written on an occurrence basis provides coverage for
- (A) claims that are made during the policy term.
 - (B) events that occur during the policy term.
 - (C) claims that occur prior to the policy term but are reported during the policy term.
 - (D) losses that occur within a retroactive period.
40. Insurance against the loss of earnings resulting from the delayed opening of a business because of damage during construction
- (A) is not available because it is not an insurable risk.
 - (B) is covered under Advance Profits on a Gross Earnings policy.
 - (C) is covered under Delayed Opening on a Profits policy.
 - (D) could also cover if a major supplier created the delay as a result of an insured peril.

(2 marks each = 80 marks)

SECTION B: NARRATIVE QUESTIONS

- Question 2. Describe the objectives of an organization's risk management program. (20 marks)

- Question 3. (a) What information is required by an insurer for the underwriting and rating of a property risk? (10 marks)
- (b) What coverage should be provided on a property risk in order to cover additional costs arising from the operation of local by-laws? Explain why. (10 marks)
- Question 4. Electronic data processing equipment is exposed to various perils that are not covered under all-risk policies. Describe the coverage provided by an all-risk policy and outline the additional coverages that should be provided to an insured in order to ensure adequate protection. (20 marks)
- Question 5. (a) With respect to business interruption insurance, outline the differences between the Period of Indemnity on a **Profits** form and that on a **Gross Earnings** form. (8 marks)
- (b) Describe the advantages and disadvantages of commercial business package policies. (12 marks)
- Question 6. (a) What property is covered by a Commercial Property Floater? (4 marks)
- (b) Explain why co-insurance clauses exist and their effect. (10 marks)
- (c) What purpose is served by a Stated Amount clause in a property policy? (6 marks)

Section C: Application Question

- Question 7. Norcan Delivery Ltd. is a business that buys and stores foodstuffs for distribution to outlets of a major department store chain operating within your province. The foodstuffs include spices, pasta, dry soups and sauces. They specialize in just-in-time delivery; promising to fill requests for product anywhere in the province within 24 hours. The company's storage facility consists of a large, sprinklered warehouse.
- Apply risk management principles to develop a risk management program for the physical assets of building, stock and equipment. Use the headings of Exposures, Loss Prevention, Loss Control and Retention in discussing your program. You may display your answer in chart form. (20 marks)

