



Insurance Institute  
Canada

CIP PROGRAM  
EXAMINATION  
December 2003

## C11 PRINCIPLES AND PRACTICE OF 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.

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### 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. An unearned premium is that portion of the policy premium that
- (A) covers the policy period that has not yet expired.
  - (B) has not been paid out as a loss.
  - (C) has not been paid out as losses or as agents' or brokers' commission.
  - (D) is left over after the payment of all losses, commissions and expenses.

2. Which of the following is NOT a hazard?
- (A) Slippery floors
  - (B) Faulty heating system
  - (C) Robbery
  - (D) A poorly maintained car
3. In insurance, the term **liability** broadly implies
- (A) the chance of a loss.
  - (B) our obligations to other people.
  - (C) accidental injury.
  - (D) risk.
4. The primary function of the general insurance industry is to
- (A) assume the liability of others.
  - (B) provide protection from perils.
  - (C) provide protection from hazards.
  - (D) spread the losses of the few among the many.
5. The largest single class of general insurance sold in Canada is
- (A) automobile insurance.
  - (B) commercial property insurance.
  - (C) fire insurance.
  - (D) personal property insurance.
6. Insurers try to achieve a balance of premiums to losses by
- (A) having a good spread of risk.
  - (B) insuring a small number of superior risks.
  - (C) specializing in one or two kinds of risk.
  - (D) writing as much business in one location as possible.
7. Insurance that is carried by a business to cover lost earnings as a result of an insured peril is
- (A) casualty insurance.
  - (B) business interruption insurance.
  - (C) surety insurance.
  - (D) fidelity insurance.
8. Pure premium is
- (A) that part of all the premiums for a particular class of insurance business that remains after all the losses have been paid.
  - (B) that part of the premiums that is required to pay the losses that have occurred.
  - (C) the premium required to pay the anticipated losses.
  - (D) the rate or unit of premium required.

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9. A captive insurance company
- (A) has to conform to Canadian insurance law.
  - (B) is a Canadian subsidiary of a foreign insurance company.
  - (C) is a tax evasion scheme.
  - (D) may only insure its owners.
10. The price of a unit of insurance for a period of one year is called a
- (A) premium.
  - (B) rate.
  - (C) tariff.
  - (D) loading.
11. A mutual insurance company
- (A) cannot insure anyone who is not a member of the community.
  - (B) insures mostly its shareholders.
  - (C) is owned by its policyholders.
  - (D) is owned by its shareholders.
12. Insurance company income comes from
- (A) investment income and dividends.
  - (B) premiums and investment income.
  - (C) reserves.
  - (D) premiums and government subsidies.
13. Common law
- (A) is a system of law found in all Canadian provinces except Québec and the territories.
  - (B) is unwritten law based on precedent.
  - (C) is law created by statute in all provinces except Québec.
  - (D) overrides all statute law dealing with the same point.
14. An insurance pool is
- (A) a contractually-based, risk-sharing arrangement with members that agree to share in the payment of each other's losses.
  - (B) made up of various insurers who agree to pay a fixed proportion of any loss.
  - (C) a contractually-based risk-sharing arrangement.
  - (D) an insurance company created by a business to pay for future losses.
15. Which of the following is responsible for monitoring federally-licensed insurance companies to ensure that they are solvent?
- (A) The Minister of Finance
  - (B) The Office of the Superintendent of Financial Institutions
  - (C) The President and the Board of Directors of each individual insurance company
  - (D) The Superintendent of Insurance of the province in which an insurance company's head office is located

16. Lloyds of London is
- (A) a co-operative association.
  - (B) a group of underwriting members.
  - (C) a mutual insurance organization.
  - (D) the world's largest insurance broker.
17. Which of the following is NOT a loss prevention activity in which the insurance industry is involved?
- (A) Fire loss prevention
  - (B) Burglar alarm monitoring
  - (C) Road safety and safe driving education
  - (D) Crime and fraud prevention
18. The Statutory Conditions under common law are
- (A) binding on the insurer but not on the insured.
  - (B) determined and designed by each individual insurer.
  - (C) required on all policies.
  - (D) required on those policies insuring certain classes of risk.
19. Which of the following is NOT deemed to be a binding contract of insurance?
- (A) A certificate of insurance
  - (B) A signed application
  - (C) An interim receipt
  - (D) An oral binder
20. The regulation of all insurance intermediaries falls under
- (A) federal and provincial jurisdiction.
  - (B) federal jurisdiction.
  - (C) provincial jurisdiction.
  - (D) the Insurance Companies Act.
21. A binder
- (A) cannot be terminated once it has been issued.
  - (B) is a memorandum of an agreement to insure.
  - (C) is an all-inclusive insurance package.
  - (D) must always be in writing.
22. The proximate cause of a loss is the
- (A) effective cause in a chain of events leading to the loss.
  - (B) final cause in a chain of events leading to the loss.
  - (C) first cause in a chain of events leading to the loss.
  - (D) remote cause in a chain of events leading to the loss.

23. The Insurers Advisory Organization
- (A) investigates losses where arson is suspected.
  - (B) is controlled by and reports to the Office of the Superintendent of Financial Institutions.
  - (C) provides actuarial consulting services.
  - (D) provides services only to insurance companies.
24. A precedent is
- (A) case law.
  - (B) an act of the legislature declaring, commanding or prohibiting something.
  - (C) the equivalent of a statute.
  - (D) written law.
25. Substantive law
- (A) deals with the rights of corporations.
  - (B) establishes the rights and duties of individuals.
  - (C) protects and enforces the rights and duties of individuals.
  - (D) regulates the important or substantial aspects of life in society.
26. Common law
- (A) has largely been replaced by statute law.
  - (B) is not now as important as it was in earlier times.
  - (C) is often relied upon for the resolution of legal disputes.
  - (D) never changes.
27. The Civil Code of Québec is
- (A) a system of inherited laws.
  - (B) law enacted by the National Assembly of Québec.
  - (C) the only law in Québec.
  - (D) the Québec equivalent of the common law.
28. Under common law, when one party to a contract fails to fulfill his or her obligations under the contract, the contract could be discharged as a result of a(n)
- (A) breach.
  - (B) agreement.
  - (C) frustration.
  - (D) mistake.

29. A man fills out an application for automobile insurance and neglects to indicate that the vehicle would be used primarily as a taxi. After the policy is issued, the insurer learns that the insured failed to disclose the material facts about the use of the vehicle. At the time that the insurer obtains the accurate information, the automobile policy is
- (A) void.
  - (B) discharged.
  - (C) voidable.
  - (D) breached.
30. A valued insurance contract
- (A) implies that, because of the higher premium, the contract is a valued one.
  - (B) implies that the amount to be paid in the event of a loss is determined when the policy is written.
  - (C) is a life insurance policy under which an agreed amount will be paid on the death of the insured.
  - (D) is a replacement cost contract.
31. Decisions of the Supreme Court of Canada may be overruled by the
- (A) Appeal Division of the Federal Court of Canada.
  - (B) Federal Cabinet operating and in session as the Privy Council.
  - (C) House of Commons.
  - (D) none of the above
32. Under The Civil Code of Québec, the four requirements of a valid contract are
- (A) acceptance, agreement, capacity and offer.
  - (B) acceptance, cause, consent and mutual agreement.
  - (C) capacity, cause, consent and object of contract.
  - (D) capacity, consideration, co-operation and lesion.
33. The actual cash value of an item that has been lost or destroyed, can be described as the
- (A) original purchase price of the item.
  - (B) replacement cost of the item at the time of loss.
  - (C) value of an equivalent item of the same age and condition.
  - (D) item's value to the insured at the time of loss.
34. A contract of compensation
- (A) is the equivalent of a contract of indemnity.
  - (B) states that a preset amount is payable when an event occurs.
  - (C) states that an amount is predicated on the values at the time of the loss.
  - (D) states that an employer must pay a specific amount when an employee is injured.
35. For which of the following classes of insurance is a written application NOT obligatory?
- (A) Accident and sickness insurance
  - (B) Automobile insurance
  - (C) Life insurance
  - (D) Property insurance

36. The term **contra proferentem** means that
- A (A) any ambiguity in a contract will be interpreted against the offeror of the contract.  
 (B) any ambiguity in the policy will be interpreted in favour of the insurer.  
 (C) if an insured makes a mistake on the insurance application, the policy may be voided.  
 (D) the insurance contract may be voided in the event of ambiguous wording.
37. A certificate of insurance
- C (A) is a copy of part of the policy.  
 (B) is a copy of the policy.  
 (C) is a modified form of the policy.  
 (D) replaces the original policy when the insured requests a copy.
38. When a reinsurer wishes to reduce its own liability on a particular risk, it may do so by arranging a
- (A) cession.  
 (B) concession.  
 (C) retrocession.  
 (D) treaty.
39. Subrogation
- (A) arises on all contracts of insurance.  
 (B) rights arise after a claim for indemnity has been paid by an insurer.  
 (C) is the right of an insurer to take action against the insured in the case of fraud.  
 (D) is an insurer's right to collect paid loss amounts from other insurers who insured the same loss.
40. Statutory limitations that set out the time period within which specific legal actions must be taken, describe which of the following terms?
- (A) Estoppel  
 (B) Prescription  
 (C) Subscription  
 (D) Waiver

(2 marks each = 80 marks)

**Section B: Narrative Questions**

Question 2. (a) Define the following terms:

- (i) Insurance *ch. 1 pg 17* (3 marks)  
 (ii) Indemnity *ch. 1 pg 16* (2 marks)  
 (iii) Reserves *ch. 1. pg 18* (5 marks)

(b) Describe the steps in the risk management process. (10 marks)

*ch. 1 pg 11-15*

continued over

- Question 3. (a) Describe the purpose and contents of a **proof of loss** form? (5 marks)  
*ch. 11 pg 7-8*
- (b) Briefly describe the role of the claims department of an insurance company. (4 marks)  
*ch 11*
- (c) Describe the methods by which an insurer may achieve a good spread of risk. (11 marks)
- Question 4. (a) Why does the federal government supervise the financial affairs of insurers that operate in Canada? (4 marks)  
*ch 4 pg 13-*
- (b) Outline the various ways in which the federal government of Canada supervises the affairs of insurance companies. (16 marks)  
*Ch. 4 p. 14-16*
- Question 5. Describe the FIVE (5) necessary elements of a legally binding contract under common law. (20 marks)  
*Ch. 7 pg 3-10*
- Question 6. (a) Under what circumstances, would an insurance policy be canceled short-rate and how would the return premium be calculated? (5 marks)
- (b) Describe the process by which an insurance policy must be canceled when initiated by the insurer. (5 marks)
- (c) Describe the role and functions of an independent adjuster in the claims process. (10 marks)

### Section C: Application Question

- Question 7. Harry and Alice Palmer sustained a serious fire in their home and make a claim under their homeowners policy. Describe how the adjustment of their claim might proceed from start to finish. In your answer, describe the responsibilities of both the Palmers and their adjuster. (20 marks)

