QUIZ #7 – CHAPTER 7

1. Pure premium is defined as
   a) The premium required to pay claims.
   b) The premium required to pay claims and underwriting expense.
   c) The premium required to pay claims and all administrative expenses.
   d) The premium required to pay claims, administrative expenses and allow for a profit.

2. Rates are developed by
   a) Underwriters in consultation with insurance brokers.
   b) The marketing department.
   c) Actuaries.
   d) Claims adjusters.

3. The process of rate discrimination attempts to
   a) Identify the probably frequency and severity of loss of risks within a rating class.
   b) Exclude risks belonging to classes containing excessive numbers of risk.
   c) Identify risks within a class that are least in need of insurance.
   d) None of the above.

4. The best exposure base for the rating of premises liability for a record store would be the
   a) Square footage of the building.
   b) Number of customers entering the premises.
   c) Amount of street frontage involved.
   d) Number of hours during which the store is open.

5. One example of a long tail situation arises when losses are incurred during the policy period
   a) And result in claims requiring immediate payment.
   b) And the expected payout is immediately known.
   c) But are not discovered and reported until later.
   d) And are denied by insurers when presented as claims.

6. Underwriting profit is defined as the amount by which
   a) Earned premium exceeds the cost of incurred claims and expenses.
   b) Earned premium exceeds the cost of incurred claims.
   c) Written premium exceeds the cost of incurred claims and expenses.
   d) Written premium exceeds the cost of incurred claims.

7. Loss statistics for most insurance sold in Canada is gathered and reported by the
   a) Insurers Advisory Organization.
   b) Federal government.
   c) Provincial government.
   d) Insurance Bureau of Canada.

8. What is the definition of pure premium?

The premium required to pay claims/insurance losses.

9. What is the difference between development factors and trend factors?

current * Development factors are adjustments to current reserves for claims that have yet to be settled to reflect the estimated final cost of those claims

future * Trends factors are adjustments applied to all losses to reflect what they would probably cost if they were to occur next yr. rather than having occured at some time in the past.

10. What is the difference between the rate and the premium for an insurance policy?

Rate = Price per unit of insurance for policy period

Premium = Total cost of insurance. = rate × amt. of insurance

11. What are the major components of a rate?

Anticipated cost of settling claim, acquisition (commission) costs of business

Administering cost including taxes.

12. What are the two conditions for rate accuracy?

- The actuarial forecast of future losses based on past losses must be accurate for population
- The sample must be representative of the population.

13. What is the exposure base of a risk? Ideally, what should it reflect?

The denomination in which the unit of exposure is expressed.

Should reflect the frequency + severity of loss the risk experienced.

14. How is the premium rate or unit cost of insurance calculated?

Dividing the total premium by the exposure unit.

15. Explain the law of large numbers and the theory of probability.

Probability becomes more reliable the larger the # of trials or cases in the sample

The likelihood of an occurence expressed by # of actual occurrences ÷ # of possible occurences.

16. Describe the general process for all ratemaking.

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17. What is class rating? When is it used? → personal auto & small business. homogeneous risk

used when large number of risks that share common characteristics

Programmed computers programs to rate automatically for certain classes of insurance. It eliminates virtually the element of judgement in rating & streamlines the policy-issuing process, thus reducing production cost.

18. What is schedule rating? When is it used?

Individually rated/because of complexity & the need for U/W judgement

When the body of statistical data is too fragmented to permit class rating. large commercial risk

19. Explain the process of fixing and modifying the base rate of insurance.

Debits & credits are applied based on factors that make the risk either better or worse than the average risk of its type.

Modified from time to time based on statistical exhibits that contain cells broad enough in scope to produce a credible indication of future claims costs.