

1. Explain each of the following characteristics of a typical insurance plan.
 - A. Pooling of losses - the loss that spreads throughout the whole of a group from the few, the actual loss is then taken over from the average loss
 - B. Payment of fortuitous losses - losses that are unanticipated by the insured
 - C. Risk transfer - a pure risk that is transferred from a stronger financial position to someone who needs their loss paid for
 - D. Indemnification - is a contractual method of transferring risk. The indemnitor agrees to take financial responsibility for any type of liability or loss that occurs under the contract.

2. Explain the law of large numbers.

Large numbers are used to predict the risk of loss or claims of some participants so that the premium can be calculated appropriately. The law of large numbers states that if the amount of exposure to losses increases, then the predicted loss will be closer to the actual loss.

3. Pure risk ideally should have certain characteristics to be insurable by private insurers. List the six characteristics of an ideally insurable risk.

1. The chance of loss must be able to be calculated.
2. The loss can not be catastrophic.
3. Loss should not be unintentional or accidental.
4. The loss must have a large number or exposure risk.
5. The premium must be economically feasible.
6. The loss must be determined and measurable.

4. Identify the approaches the insurers can use to deal with the problem of catastrophic loss exposures.

- Reinsurance can be one way that insurers can deal with the problem of catastrophic loss exposures. This means that insurers can avoid the risk by using a method that allows them to cover over a very big amount of geographical area. Catastrophic losses can be dealt with by instruments(financial).

5. Why are most market risks, financial risks, production risks, and political risks considered difficult to insure by private insurers?

- Insurable risks are much harder to meet and complete. However, all of these risks are unsafe and share characteristics of a risk that is known to be insurable.

6. What is the meaning of adverse selection?

- Is the tendency of those in dangerous jobs or high-risk lifestyles to purchase products like life insurance. To fight adverse selection, insurance companies reduce exposure to large claims by limiting coverage or raising premiums.

7. What are the two major differences between insurance and gambling?

- One difference is that gambling opens the door to much more risk. Insurance on the other hand, is already taken care of a risk that is already there and not creating more on top of it.

8. What are two major differences between insurance and hedging?
- First, an insurance transaction is completely different because it transfers for the pure risk since insurable risk falls in place together with each other. They can generally get along well with each other. Second, there are more serious consequences that can really harm you such as adverse selection and moral hazard. These two are bigger problems that can get in the way of insurers than for speculators who buy or sell future contracts.

9A. Identify the major fields of private Insurance.

- Property Insurance, Health Insurance and Life Insurance

B. Identify several property and casualty insurance coverages.

- Provides legal liability towards Personal properties of those individuals and families(Personal Lines). Property and Casualty coverages for business firms, nonprofits organizations, and government agencies(Commercial Lines).

10A. Explain the basic characteristics of social insurance programs.

- They have well-defined eligibility requirements and benefits, have provisions for program incomes and expenses, are funded by taxes or premiums paid by participants, and have mandatory or heavily subsidized participation.

B. Identify the major social insurance programs in the United States.

- Medicare is a huge part of our country's Social Security Program and covers the expenses of many individuals over the age of 65 and a specific disabled people under the age 65
- Unemployment insurance program provides individuals a weekly payment who are unemployed.

Chapter 3

1A. What is the meaning of risk management?

- The forecasting and evaluation of financial risks together with the identification of procedures to avoid or minimize their impact.

2. Explain the objectives of risk management both before and after a loss occurs

- Pre-Loss: First objective - Prepare for the most economical way and its potential.
Second objective - reduce anxiety
Final objective - Make sure all legal obligations are met and in place.
- Post-Loss: First objective - firm survival. Second objective - make sure everything is up and running. Third Objective - Earnings Stability. Fourth Objective - The main objective is to make sure loss is very low and is minimized as much as possible.

3. Describe the steps in the risk management process.

- Identify loss exposures
- Measure and analyze the loss exposures
- Select and appropriate combinations of techniques for treating the loss exposures
- Implement and monitor the risk management program

4A. Identify the sources of information that a risk manager can use to identify loss exposures.

- Credit line
- Unfunded Reserve
- Funded Reserve
- Current Net Income

B. What is the difference between the maximum possible loss and probable maximum loss?

- Maximum Loss - is the worst thing that can happen to a firm. It is something that just does not help at all.
- Probable Loss - is most likely the worst thing that can actually occur and happen.

5A. Explain the meaning of risk control.

- Is the set of methods by which firms evaluate potential losses and take action to reduce or eliminate such threats.

B. Explain the following risk-control techniques.

- Diversification - is a strategy that mixes a wide variety of investments within a portfolio.
- Separation - is a risk technique that involves dispersing key assets.
- Duplication - is a risk control technique that entails the utilization of backups or spares.
- Loss Reduction - a loss control activity focusing on reducing the severity of losses.
- Loss prevention - is the act of taking proactive measures to prevent or abate identified risks which, if left unmitigated, may result in university claim expenditures.
- Avoidance - is an approach that eliminates any exposure to risk that poses a potential loss.

6A. Explain the meaning of risk financing.

- Is the determination of how an organization will pay for loss events in the most effective and least costly way possible.

B. Explain the following risk-financing techniques.

- Retention - is the assumption of risk of loss or damages.
- Noninsurance Risk Transfer - the transfer of risk from one party to another party other than an insurance company.
- Insurance - is the assessment and quantification of the likelihood and financial impact of events that may occur in the customer's world that require settlement by the insurer; and the ability to spread the risk of these events occurring across other insurance underwriter's in the market.

7. What condition should be fulfilled before retention is used in a risk management program?

- The worst thing that can happen is a loss. However, the worst loss would not be serious anyways.

8A. What is captive insurance?

- Is a property and casualty insurance company established to provide coverage primarily for a parent company.

B. Explain the advantages of using a captive insurer in a risk management program?

- Much lower costs
- Easier access to a reinsurer
- Favorable regulatory environment

9A. What is self-insurance?

- Is a management technique in which a company or individual sets aside a pool of money to be used to remedy an unexpected loss.

B. What is a risk retention group?

- Is a state-chartered insurance company that insures commercial businesses and government entities against liability risks.

10A. Explain the advantages of using insurance in a risk management program.

- Prevention and minimization of financial losses
- Promotes business continuity
- Risk Sharing
- Valuable risk services
- Loss exposure analysis
- Claims adjusting

B. Explain the disadvantages of using insurance in a risk management program.

- Premiums are a major cost
- Great amount of time and effort must be invested
- Risk manager may have less incentive to implement loss control measures