CHARTERED INSURANCE INSTITUTE OF NIGERIA

ADVANCED DIPLOMA

OCTOBER 2015 EXAMINATION PAPER

SUBJECT A510
RISK, REGULATION AND CAPITAL ADEQUACY

QUESTION 1

a. **State whether this statement represents discrete data or continuous data: 'The yearly incomes of Managing Directors of Insurance companies in Nigeria'.**
b. **The arithmetic mean of four numbers is 8. Three of the numbers are 4, 7 and 11. What is the fourth number?**
c. **Express the number 1.86 x 10^5 without using powers of 10.**
d. **Find the mode for the following set of numbers: 3,5,2,6,5,9,5,28,6.**
e. **Give one example of those who might be interested in the reporting of information relating to risk.**
f. **In the context of dispersion, what is meant by the term 'range'?**

SOLUTION TO QUESTION 1

(a) Discrete
(b) Ten (10)
(c) 18,600,000
(d) 5
(e) Board of directors, Business units, individuals, stakeholders (Any 1)
(f) The range is the distance between the smallest and largest values of the variable.

QUESTION 2

Identify the names given to the four parts of a group frequency distribution.

SOLUTIONS TO QUESTION 2

The names given to the four parts of a group frequency distribution are:

- Class interval;
- Class limit
- Stated limits

- True limits

QUESTION 3

What are the disadvantages of organizational charts as a method of risk identification?

SOLUTIONS TO QUESTION 3

Disadvantages of Organizational Charts:

- It is too broad in its identification to enable specific solutions to be suggested for specific risks.
- It can end up being too simplistic
- It is useful as a first step, but would have to be associated with some other technique or techniques.
- The structure of many organizations can be very complex. The danger is that an over-simplified chart is produced which omits more than it reveals.

QUESTION 4

What types of risks are most suitable for risk transfer?

SOLUTIONS TO QUESTION 4

Types of risks most suitable for risk transfer:

- Employers' liability risks;
- Workers compensation;
- Motor third party risks;
- Public liability risks;
- Professional liability risks.

QUESTION 5

Explain what is measured by a 'co-efficient of correlation'. In this context, interpret:

P = +1

P = 0

P = -1

SOLUTIONS TO QUESTION 5

Coefficient of correlation: A measure of the strength of the relationship between X and Y in a scatter diagram. Range -1 to +1.

P = +1 Means positive correlation between the variables, as x increases, y decreases, the nearer to 1, the stronger the relationship between the variables.

P = 0 Means no relationship between the variables.

P = -1 Means negative correlation between the variables, as x increases, y decreases, the nearer to -1, the stronger the relationship between the variables.

QUESTION 6

a. **Risk and chance are commonly seen as similar. Distinguished between them.**
b. **Distinguished between peril and hazard.**

SOLUTIONS TO QUESTION 6

a. Risk implies some form of uncertainty about an outcome in a given situation. An event might occur and if it does, the outcome is unfavourable or unpleasant to us. It is not an outcome that we desire. The word risk implies both doubt about the future, and the fact that outcome could leave us in a worse position than we are at the present. Examples: the risk of an accident or the risk of losing one's job.

   Chance also implies some doubt about the outcome in a given situation. The difference is that the outcome is normally a favourable or pleasant outcome. Examples: the chance of winning the first prize in a lottery or the chance of passing an examination.

b. The peril is the prime cause which gives rise to the loss. Examples: fire, theft, earthquake, storm and flood etc.

   Hazard relates to factors which may influence the outcome of the loss. Examples: inflammable liquids, constructions made out of wooden materials in relation to fire.

QUESTION 7

Apart from the level of expected claims, outline four (4) factors usually considered when establishing premium rates for any class of general insurance business.

SOLUTIONS TO QUESTION 7

The factors include:
- Operational expenses
- Profit margin
- General inflation

- Claims inflation
- Interest rates
- Exchange rates
- Competition

QUESTION 8

A variable y is determined from a variable x according to the equation $y = 2x - 3$ (where the 2 and 3 are exact). Construct a table showing the values of y corresponding to $x = -2$ to 4.

SOLUTIONS TO QUESTION 8

The equation given is:

$y = 2x - 3$

Set up a table as follows:

x values	-2	-1	0	1	2	3	4
y values	-7	-5	-3	-1	1	3	5

QUESTION 9

Q Wide Cover Insurance Plc wants to review its rate for Comprehensive Motor Insurance. A set premium is charged for a given age and sex. Statistics for the previous 5 years produce the following frequency distribution:

No of Accidents	No. of females aged 30 having an accident
0	450
1	380
2	115
3	35
4	15
5	5

a. **Construct a probability distribution from the frequency distribution.** **(10 marks)**

b. **Determine the expected number of accidents per individual, showing all your workings.** **(5 marks)**

The statistics also provide the following severity distribution:

Cost of Accidents (N)	No. of Accidents
0<200	336
200<400	176
400<600	128
600<800	80
800<1000	48
1000<1200	32

c. **Construct the probability distribution. (10 marks)**

d. **Determine the expected value of the accident, showing all your workings. (5 marks)**

e. **Calculate the expected total cost of an accident for a given individual. (5 marks)**

f. **If the insurer wishes to build in a 25% margin to cover expenses and profit, what is the minimum premium they should charge? (5 marks)**

g. **Indicate, by showing your workings, how you would check that you have calculated the minimum premium correctly. (10 marks)**

SOLUTIONS TO QUESTION 9

a. Set up a table as follows - Table 1

X	f	Rel. f(%)	P(x)	xp(x)
0	450	45.0	0.450	0.000
1	380	38.0	0.380	0.380
2	115	11.5	0.115	0.230
3	35	3.5	0.035	0.105
4	15	1.5	0.015	0.060
5	5	0.5	0.005	0.025
TOTAL	**1000**	**100.0**	**1.000**	**0.800**

(10 marks)

b. Expected number of accidents per individual is 0.800 or 0.8 **(5 marks)**

c. Set up a table as follows – Table 2

Cost of Accident (₦)	(f)	Rel. f(%)	P(x)	Midpoint (x)	xp(x)
0 < 200	336	42.0	0.42	100	42.0
200 < 400	176	22.0	0.22	300	66.0
400 < 600	128	16.0	0.16	500	80.0
600 < 800	80	10.0	0.10	700	70.0
800 < 1000	48	6.0	0.06	900	54.0
1000 < 1200	32	4.0	0.04	1100	44.0
TOTAL	**800**	**100.0**	**1.00**		**356.0**

(10 marks)

d. Expected cost of accident is ₦356.0, that is xp(x) from the above table. **(10 marks)**

e. Expected cost per accident per individual is:

0.80 x₦356.00

= ₦284.80

[xp(x) Table 1] x [xp(x) Table 2] **(5 marks)**

f. If the insurer is seeking to cover expenses and profit with a margin of 25%, the insurer should charge:

₦284.80 x 1.25

= ₦356.00 **(5 marks)**

Check answer by calculating the total cost of accident, dividing this by the total of individuals.

To do this, take the following steps:

Cost of Accident (₦)	(f)	Midpoint (x)	Total cost (₦)
0 < 200	336	100	33,600
200 < 400	176	300	52,800
400 < 600	128	500	64,000
600 < 800	80	700	56,000
800 < 1000	48	900	43,200
1000 < 1200	32	1100	35,200
TOTAL	**800**		**284,800**

Therefore:

₦284,800 / 800

= ₦356.00 **(10 marks)**

When the margin allowance of 25% is applied to the above figure, we obtain ₦356.00 (that is, ₦284.80 x 1.25)

Answer THREE (3) out of the following FIVE (5) questions. Each question carries marks as appropriately allocated. The marks are allocated as indicated.

<u>QUESTION 10</u>

a. Explain the reasons why there is State Intervention through the National Insurance Commission (NAICOM) in the Nigerian Insurance market. (20 marks)

b. What powers of enforcement are available to the Commissioner for Insurance under the Insurance Act 2003? (14 marks)

SOLUTIONS TO QUESTION 10

a. The following are reasons why there is state intervention in the Nigerian Insurance market:

- **To protect the insuring public:**
  The advantages of state intervention in insurance business include:
- **To maintain solvency margin of insurers:** This prevents certain person with fraudulent intentions from providing insurances. It also acts as a continual monitor of those already transacting insurance business
- **Equity:** An element of fairness must exist between insurers and policyholders. A contract of insurance is a complex contract. It is essential that controls exist for the protection of policyholders.
- **Competence**: Insurance is an intangible product. At the time of purchase, the insurer is only making a promise to provide indemnity, or an exact compensation.
  It is therefore necessary that all those who deal in such promises are competent persons who are able to fulfill their obligations when the need arises.
- **Insurable Interest:** Insurable interest is one of the basic principles of insurance. Any element of gambling is a prohibition into insurance contracts. It is therefore forbidden for a person to effect a policy of insurance where he has no insurable interest.
- **Provision of certain forms of insurance**: certain classes of insurance have been made compulsory. Example: Motor third party legal liability insurance. There is state provision as to the nature of cover required.

b. Power of enforcement

- Withdrawal of authorization to operate as an insurer.
- A temporary suspension of authorization to operate as an insurer.
- A fine for violation of a rule relating to the transaction of insurance business.
- Criminal prosecution under the Insurance Act 2003.
- Remedial action requirements: actions required to correct the problem.

QUESTION 11

a. What are flow charts?

b. Indicate the conditions or rules to follow when drawing flow charts, illustrating your answer with a practical example. (12 marks)

c. Briefly describe the Four (4) main steps involved in the preparation of flow charts. (10 marks)

d. Give Two (2) advantages and Two (2) disadvantages of flow charts. (8 marks)

SOLUTIONS TO QUESTION 11

In many organizations, there are some kinds of flow. The following are examples:

- Production flow (raw material to finished product)
- Service flow (Flow of people in a hotel)
- Money flow (bank or insurance company.)

In each case, there are various stages in the flow. At each stage, there are risks, which could disrupt the flow. Any interruption to the flow will have consequences for revenue and profit.

A flow chart can be used to identify the key stage and structure in the analysis of the risks at each stage. The most common form of flow is the production flow. **(4 marks)**

There are four main steps in flow charts:

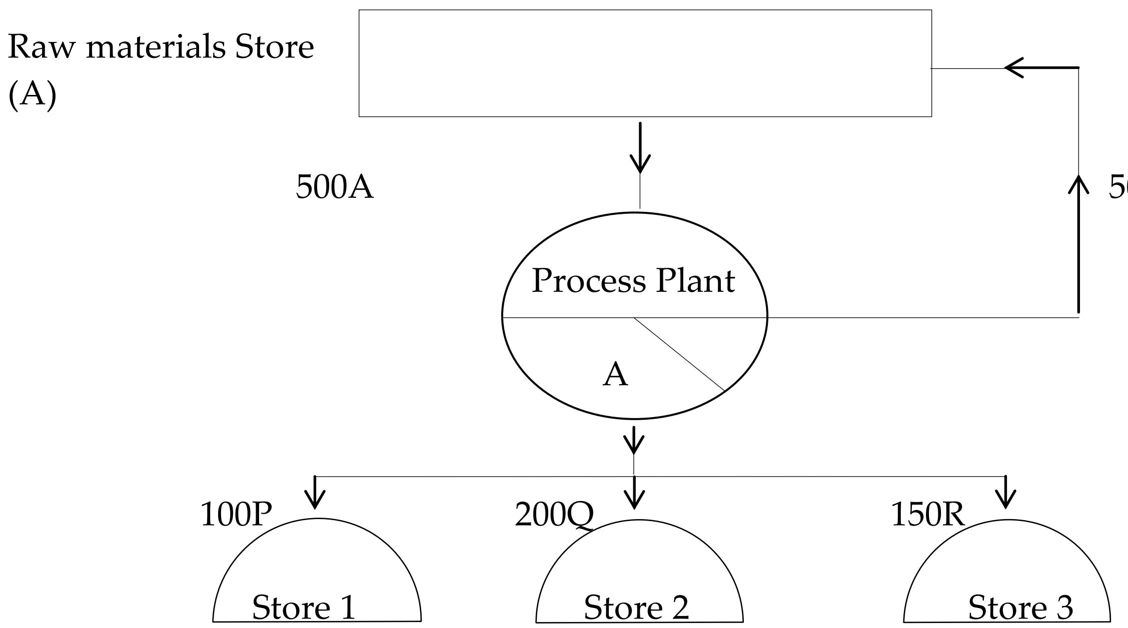
- The first step is to understand the flow
- The second step is to represent the flow
- The third step is the risk flow chart
- The fourth step is structured analysis of the chart. **(10 marks)**

The conventions or rules to be followed include:

- The start or input stage of a flow should be depicted by a square or rectangular box.
- A process stage is depicted by a circle
- An end stage is shown by a half circle.
- The product or material which is flowing is represented by letters and the quantities involved can be included as numbers.

A practical example illustrates these conventions or rules.

A PRODUCT FLOW CHART



(12 marks)

Advantages of flow charts:

- They allow complicated plant and processes to be broken down into smaller units.
- The flow chart is a more detailed analysis when compared to some other techniques of risk identification
- Flow charts are qualitative.
- They do not depend on mathematical or statistical calculations.

Disadvantages of flow charts

- Flow charts are time consuming to construct.
- The end result may prove to be inadequate to the effort expended.
- They can become too simplistic in their approach.
- The risks, which are identified, are still very general
- No measure of the probability of events is included **(4 marks)**

QUESTION 12

a. **Briefly explain the non-insurance and insurance methods of risks transfer. (20 marks)**

b. **Why is insurance the most widely used of all risk transfer methods? (14 marks)**

SOLUTIONS TO QUESTION 12

a. Non-insurance and insurance methods of risk transfer: The following illustrate risk transfer methods:

- **Transfer of risk by non-insurance means**: By using contract terms, an organization may attempt to transfer responsibility or legal liability for a wrongful act to the other party. The organization may seek to make the other bear the financial consequence of the act.

  Certain contingencies can be provided for and the terms may determine which party is to carry the risk or the cost should some consequent event make performance of the contract impossible. Example: A road carrier's responsibility for perishable goods in the event of a strike preventing normal delivery.

  Terms or clauses used to effect transfer of risks can be classified as exclusion clauses, limitation clauses, disclaimers and indemnity clauses.

- **Risk Sharing**: Some types of organization lend themselves to the sharing of risks between them. Each party to the arrangement pay a contribution into a common fund from which losses are paid. The contribution is revised regularly to ensure that it is adequate to cover the expected costs of losses and of the administration.

- **Examples of users of risk sharing:** Lawyers, accountants and medical doctors. They commonly use such self-funding mechanisms to provide for professional indemnity claims.

- **Insurance:** The insurance market still provides a valuable risk funding mechanism. Commercial insurances are placed into the market place by use of a broker. Brokers and insurers are responding to changing needs and have set up risk management, captive management and other services. Insurers to larger clients are increasingly responding to a need to look across individual risks, combine risk products and consider multiple year covers.

In all risk expenditure, the organization will want to compare the cost of insurance with the perceived benefits. A cost-benefits analysis will be undertaken by the organization. The total cost will include the premiums to be paid and the fees charged by the broker. **(20 marks)**

b. **Advantages of using Insurance**:

There are a number of advantages of using insurance:

- Insurance provides an economic vehicle for the sharing of exposures with a large number of other organizations;
- It brings to the organization a wealth of experience in risk and risk funding mechanism.
- The insurer can provide claims services which will release the organization from detailed tasks for which they are not best skilled and which might otherwise divert management from the mainstream demands of the organization itself.
- Indemnifications against unexpected losses.
- Reduction in uncertainty
- Release of funds for more productive use; and
- Access to specialist risk management services provided by insurers.

(14 marks)

QUESTION 13

a. **Risk assessment is an important task in the risk management process. What does the underwriter need to know in assessing a risk? (10 marks)**

b. **The underwriter would require information that is specific to each class of risk and this falls into two broad categories. Identify and distinguish between these two broad categories.** **(4 marks)**

c. **Give three (3) examples in each of the categories identified in (b) above.**

<u>SOLUTIONS TO QUESTION 13</u>

a. The underwriter needs to know:
- The identity of the proposer;
- The insured activity;
- The location of the risk;
- The extent of cover; and
- Any previous claims experience **(10 marks)**

b. The two broad categories are:
- Physical hazards; and
- Moral hazard **(4 marks)**

c. Physical Hazards: are those attaching to the physical characteristics of the subject matter of insurance
Examples:
- Property loss or damage: the construction of a building or the adequacy of firefighting equipment. Buildings of wooden construction represent a much higher level of physical hazard than ones built of brick.
- Liability: the presence of dangerous chemicals in the workplace or the absence of suitable guards on machinery, excessive noise or dust.
- Motor: people who have a very high mileage (sales representatives) present a higher physical hazard than someone who has a very low mileage.
- Life assurance: people with certain potentially dangerous, occupation may present a high physical hazard. A person who has a recurring illness is another example of a high physical hazard.

Moral hazards: These are the hazards which attach to the attitude of the insured, rather than the subject matter of insurance Examples:
- One of the most common example of moral hazard is lack of care on the part of the insured.
- Evidence of moral hazard can also be seen in the regular claimant. These people look upon insurance as an investment. They believe they can make claims each year.

- There is the case of the dishonest insured. The dishonesty could manifest itself either at the time of the proposal or at the time when a claim is being made. **(20 marks)**

QUESTION 14

a. **The probability that a man aged 55 years will be alive till 2035 is 0.625, while the probability that his wife aged 53 years will be alive in 2035 is 0.833.**
Determine the probability that in 2035;
(i) Both will be alive;
(ii) At least one of them will be alive;
Only the wife will be alive. **(12 marks)**

b. **What do you understand by:**
   i. **A symmetrical frequency distribution and a skew frequency distribution?**
   ii. **Draw a diagram for each of the above distributions and mark on each diagram the positions of the mode, the median, and the arithmetic mean.**

c. **The following information concerns persons for whom pension contributions were payable in 2012 under the National Insurance Pension Scheme. The figures are in millions.**
There were 23.78 employed, of whom 15.60 were males; and 1.48 self-employed, of whom 0.10 were females. The remainders were non-employed. Although there were 17.10 males and 8.43 females.
Present this information in a table, showing persons by class of contribution and by sex.

SOLUTIONS TO QUESTION 14

(a)

(i) Both will be alive;
The probability that both will be alive:
= 0.625 x 0.833
= 0.52

(ii) At least one of them will be alive:
= 1 minus probability that both will be dead:
= 1 – (0375 x 0.166)
= 1 – 0.062
= 0.938

(iii) The probability that only the wife will be alive:

= Probability of husband dead and probability of wife alive

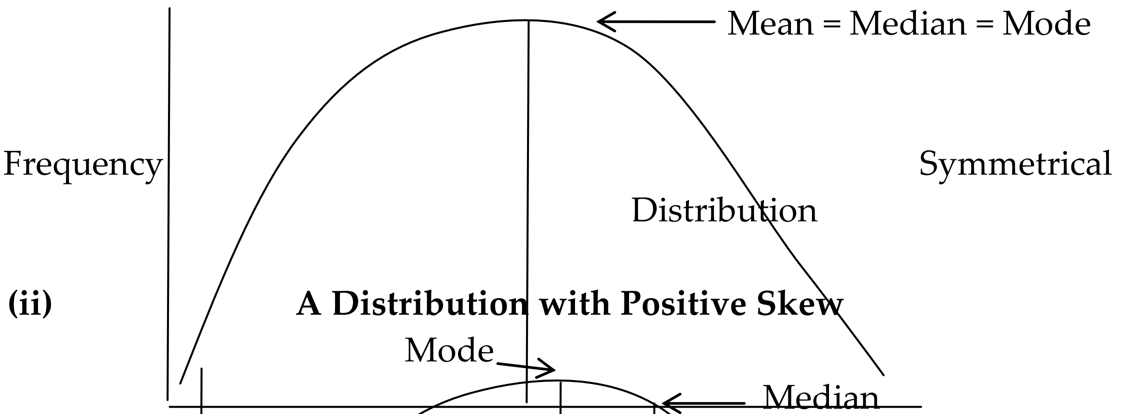
= 0.375 x 0.833

= <u>0.312</u>

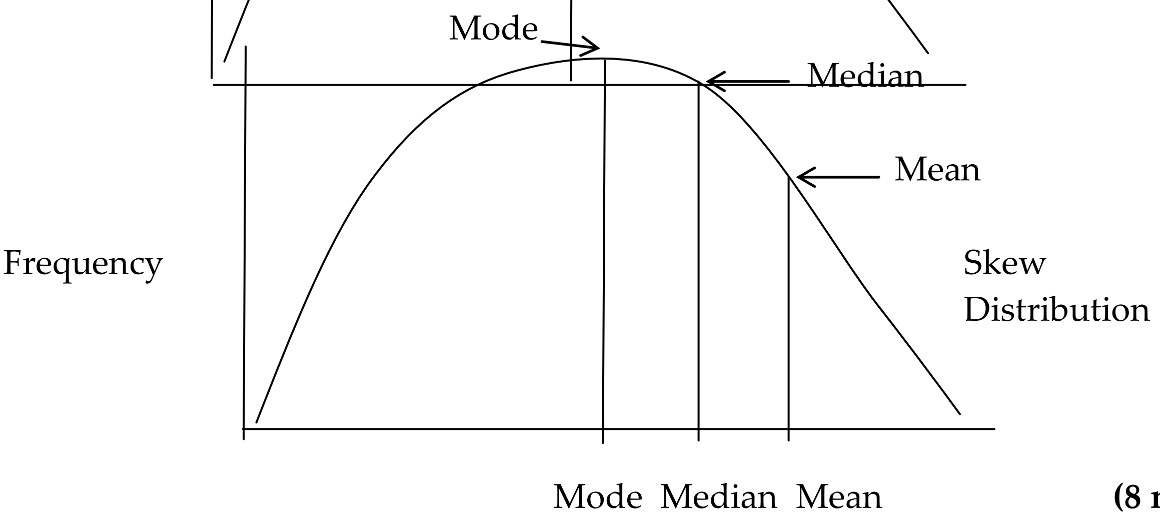
(b) A symmetrical frequency distribution and a skew frequency distribution:

- A symmetrical frequency distribution is one in which the class-frequencies decrease symmetrically on either side of the mode.
- Skew frequency distribution is one in which the class-frequencies decrease more rapidly on one side of the mode than on the other. A curve can have either positive or negative skew.

(i) Symmetrical Distribution



(ii) A Distribution with Positive Skew



(8 marks)

(c) **<u>National Insurance Pension Scheme</u>**
<u>Contributions Payable in 2012</u>

Class	Male	Female	Total
Employed	15.60	8.18	23.78
Self-employed	1.38	0.10	1.48
Non-employed	0.12	0.15	0.27
Total	17.10	8.43	25.53

(Nos in million)

(14 marks)

CHARTERED INSURANCE INSTITUTE OF NIGERIA

ADVANCED DIPLOMA

OCTOBER 2015 EXAMINATION PAPER

SUBJECT A530
BUSINESS AND ECONOMICS

Part I
Answer ALL questions in Part I
Each question carries six (6) marks.
Note form is acceptable where this conveys all the necessary information.

QUESTION 1
State Four (4) factors that can affect the demand for non-life Insurance.

SOLUTION TO QUESTION 1
Factors affecting the demand for non-life Insurance are:

a. Price /premium charged
b. Mode of premium payment
c. Income of the Insured
d. Taste and preference
e. Economic situation
f. Product awareness (advertising)
g. Legal requirement.

(1 mark each for any 6pts = 6 marks)

QUESTION 2
The demand function and supply function for non-life insurance product are represented by the equation:

D = 200 – 6p
S = 40 – 2p

Find the equilibrium price (P) and quantity (Q) supplied.

SOLUTION TO QUESTION 2

At equilibrium, D = S

Therefore 200 – 6p = 40 + 2P

i.e. 8P = 200 – 40

8P = 160

P = 160/8 = 20

When P = 20

Qs = 40 + 2(P) = 40 + 2 (20)

= 40 + 40 = 80 **(6 marks)**

QUESTION 3

Distinguish between:

a. Local Area Networks and Wide Area Networks

b. Give example each of (a) above.

SOLUTION TO QUESTION 3

(i) Local Area Network (LAN) - enable information, computing and communications resources to be shared between directly connected computers, often in the same building or close vicinity e.g. a computer section of an insurance company situated in one building. While

(ii) Wide Area Network (WAN) cover larger distance communication and geographical locations. They may use telephone lines or communication provided by a common carrier e.g. NICON Insurance offices located in State capitals. **(6 marks)**

QUESTION 4

a. Define the term 'Exchange rate'

b. Differentiate between Floating Exchange Rate and Fixed Exchange rate.

SOLUTION TO QUESTION 4

a. An exchange rate is the price of a currency expressed in terms of how much that currency can buy of another. **(2 marks)**

b. The floating exchange rate is determined by the supply and demand markets. **(2 marks)**
Whereas the government does not allow the exchange rate to fluctuate freely according to market forces. Instead, the government uses policies designed to maintain the exchange rate at a prearranged level hence it is known as fixed exchange rate. **(2 marks)**

QUESTION 5

Identify Two (2) potential benefits of a single European Currency to Insurance firms.

SOLUTION TO QUESTION 5

Potential benefits/opportunities of single European currency (euro) to insurance firms.

1. Reduced foreign exchange risk.
2. Increase transparency. **(3 marks)**

QUESTION 6

List Four (4) advantages of Large Scale Production.

SOLUTION TO QUESTION 6

Advantages of large scale production include:

1. Marketing economies
2. Financial economies
3. Administrative economies
4. Efficiency in the use of factors of production
5. Can lead to research and development
6. Will promote welfare of workers. **(6 marks)**

QUESTION 7

Information is a vital tool in any insurance company. List and explain Six (6) parties that may be interested in such information.

SOLUTION TO QUESTION 7

Other interest parties are:

1. Trade unions - to judge the viability of wage demand
2. Potential employees - important for job applications.
3. Existing employees – to have a good understanding of their employer
4. Stockbrokers – to advice on share prices and prospects.
5. Bankers – to advise on mergers and take-overs.
6. Lenders – to produce a credit check for a loan
7. Suppliers – when providing trade credit i.e. 90-day payment period.
8. Trade association – to produce numbers and statistics to interested parties.
9. Rating agencies – to measure the claims paying ability of insurers and reinsurers. **(6 marks)**

QUESTION 8

Indicate which of the following statements is True (T), False (F) or Uncertain (U) and give reasons for your choice.

- **i. Profits from cooperative societies are taxable.**
- **ii. Price discrimination is possible when elasticity of demand for a commodity is not the same in two separate markets.**
- **iii. The liability of shareholders in a private limited company is limited.**
- **iv. A public corporation holds annual general meeting.**
- **v. Demand for labour is a derived demand.**
- **vi. A market is the physical geographical location where exchange takes place between buyers and sellers.**

SOLUTION TO QUESTION 8

- i. F - profits from cooperative societies are not taxable.
- ii. T- it is only not possible in same in 2 markets
- iii. T – it is limited to the value of shares held.
- iv. F – Public corporations do not hold AGM
- v. T – demand for labour is a derived demand
- vi. F – a market is not limited to a physical geographical location e.g. internet can be used as a market place i.e. e-commerce.) **(6 marks)**

QUESTION 9

- **a. Explain the term 'Budget'. (4 marks)**
- **b. Advance Four (4) reasons for the preparation of a budget. (12 marks)**
- **c. Detail out the steps involved in the setting out of a budget for business purposes. (18 marks)**
- **d. Explain in details what you understand by the term 'variance' in relation to budgets. (4 marks)**

SOLUTION TO QUESTION 9

a. Budget is a plan expressed in financial or quantitative form. A budget is active in that it is something to be achieved. It will be prepared in advance of activity and will relate to a specific time period. **(4 marks)**

b. Reasons for preparing budget

- i. To provide a financial statement of objectives
- ii. To identify claims upon, and the availability of resources
- iii. To reveal future risks, such as potential cash-flow problems.
- iv. To provide a measure for actual performance
- v. To motivate staff to achieve budgeted objectives. **(12 marks)**

c. Ways to set out budget for business purposes are:

i. Define objectives

ii. Make specific employees responsible for the achievement of those objectives.

iii. Determine strategies and policies to ensure the achievement of objectives.

iv. Prepare the budget

v. Obtain approval for the budget and commit resources

vi. Implement the strategies and policies above.

vii. Conduct variance analysis – this is a process of measuring actual performance against budgeted performance.

viii. Draw up strategies and policies in the light of the results of the variance analysis.

ix. Adopt strategies to manage achievement of budget despite variances.

(18 marks)

d. A variance is the difference between actual and budgeted performance, and must be expected unless the budget was remarkably accurate. The variance may be positive (budget exceeded) or negative (budget not met).

<u>QUESTION 10</u>

a. i. Define the term 'Taxation'.

ii. State the two types of taxation and distinguish between them with two (2) examples each. (10 marks)

b. Differentiate between

i. Primary and Secondary Production

ii. Demand-Pull and Cost-Push Inflation

iii Monetary and Fiscal policy

iv. Balance of Payment and Balance of Trade (28 marks)

<u>SOLUTION TO QUESTION 10</u>

a

(i) Taxation is a compulsory levy imposed on individuals or companies by government. **(2 marks)**

(ii) Two types of taxes are:

- **<u>Direct taxes</u>**: are those that are levied directly on individual income and properties e.g. personal income tax and land use change. **(2 marks)**
- Indirect taxes are levied on the goods and services they consume e.g. tax on food item and entertainment. **(2 marks)**

b.

(i) Primary production involves the process of extracting basic materials from the resources given by nature such as land while **(3 ½ marks)**

Secondary production involves changing of the basic raw materials got (or extracted) from primary production activities into acceptable forms for use by the final consumers e.g. petroleum. **(3 ½ marks)**

(ii) Demand-pull inflation is caused by excessive amounts of aggregate demand within the economy. **(3 ½ marks)**

While
Cost-push inflation is caused by manufacturers accepting rising production costs (wages, raw materials etc) and then passing these costs on to consumers (who then pay the increase). **(3 ½ marks)**

(iii) Monetary policy involves controlling the money supply and altering the country's interest rate in order to achieve policy goals of the country such as reducing the country's inflation rate. **(3 ½ marks)**

While
Fiscal policy involves using government's budget to affect the level of spending within the economy. This is done through raising of revenue via taxation and government levies and pattern of spending. **(3 ½ marks)**

(iv) Balance of payment – is the balance sheet of all the external transactions entered into by a country in a given period, usually a year. It gives the total picture of the value of the visible and invisible exports and imports as well as monetary movements in an out of a country. **(3 ½ marks)**

While
Balance of trade is the difference in value between a country's imports and exports. **(3 ½ marks)**

<u>QUESTION 11</u>

a. List Four (4) examples of Interactive Information Systems. (4 marks)

b. **Explain briefly the term 'Electronic Performance Support'** **(3 marks)**

c. **Write short notes on the following:**

   i. **Internet**

   ii. **World Wide Web**

   iii. **Computer systems**

   iv. **Web site** **(20 marks)**

   v. **State Five (5) advantages of e-commerce for the customer.** **(10 marks)**

SOLUTION TO QUESTION 11

(a) Examples of interactive information systems are:

1. Home banking
2. Home shopping
3. Education
4. Education training. **(4 marks)**

(b) Electronic performance support is a combination of computer based training and on-line help for users of a comport user. **(4 marks)**

(c)

(i) Internet – The internet is a global computer network made up of hundreds of smaller networks linked by the international telephone system. The networks are run by governments, academic institutions, corporations and 'providers' (companies connected to the internet that provides access for smaller companies and individuals). **(6 marks)**

(ii) World Wide Web – is a system of millions of hypertext pages (pages linked using associative networks) databases can be searched, information can be accessed and files can be downloaded to a connected anywhere in the world. **(5 marks)**

(iii) Computer systems: are the physical components which enable computerized information systems to run. They are often referred to as hardware, and the programs which run on them are known as software. The information processed is known as data. **(5 marks)**

(iv) Website – is a location on the internet that maintains one or more webpages. A website is always developed for a particular business or firm. **(4 marks)**

(d) The advantages of e-commerce for the customer are as follows:

1. Offer cheaper insurance
2. Saves time in purchasing insurance
3. Allows comparisons of premium level
4. Supports a chosen brand image
5. Improves understanding of insurance **(10 marks)**

QUESTION 12

a. **Which organ is responsible for the election of Directors to the Board of Directors in a Limited company? (2 marks)**

b. **Distinguish between Executive Directors and Non-Executive Directors. (8 marks)**

c. **State two (2) ways in which Non-Executive Directors can contribute meaningfully to the success of the company. (6 marks)**

d. **Identify Four (4) jobs that are associated with Head office or Regional office of an Insurance company. (10 marks)**

e. **Explain the three (3) broad types of organizing insurance companies. (12 marks)**

SOLUTION TO QUESTION 12

a. The shareholders are responsible for the election of Directors.

b. Executive directors are full-time employees of the company. Each executive director is responsible for running a specific department or division within the company. Each can have input into any decisions made by the board while Non-executive director is not an employee of the company. Instead, they tend to be seasoned managers who have valuable experience or contacts with other companies or organizations.

c. Non-executive directors can contribute to the success of the company in 2 ways as follows:

1. They can be as sharp independent external critics of the firm's management and its strategies, ensuring that the needs and requirements of the shareholders are never allowed to come second to the personal interests of the directors.
2. Non-executive directors should be able to contribute knowledge and experience from a wider area. **(4 marks)**

d. The job of those working in the head or regional offices include:

1. To communicate strategies decided by the Board down to branch level.
2. To set and monitor performance targets for the organization at branch level
3. To provide the branches with support in the field e.g. training

4. To make day-to-day operational decisions.
5. To achieve the objectives set down by the head or regional office
6. To collect performance dates which are them communicated back up the hierarchy. **(10 marks)**

e. Three broad types of insurance companies are:
1. A composite company – an insurance company that transact all or several of the major classes of insurance, including long-term business and general business.
2. A specialist company – a company transacts only a class of insurance
3. A proprietary company – a company owned by shareholders.
4. A mutual company – a company owned by policyholders.
5. A captive company – which is a company that has a parent company owner whose business is not in insurance.
6. A life company – a life assurance company that is only able to transact long-term business.
7. A general insurance company- an insurance company that is only able to transact general business. **(Any three)**

QUESTION 13

Identify and discuss the External constraints that can mitigate against the operation of business from achieving its objectives.

SOLUTION TO QUESTION 13

The factors that can affect a firm's success are:
1. Economy – Trading conditions within the economy fluctuate greatly over time. The main cause of these fluctuations is the trade cycle. Trading conditions within the economy are clearly and example of an external constraint; there is nothing a single firm can do in order to prevent a recession. This will lead to a fall in profitability caused by a decrease in demand for their products.
2. Government policy – changes to the fiscal and monetary environment will obviously affect firms. The government may also pass laws and regulations that act as external constraints on firms e.g. minimum wage law passed by government. The minimum wage is an external constrain beyond the firm's control.
3. Competition – in order to survive, firms must be able to fight off the threats posed to them by competitors at home and abroad.
   Different firms have attempted to deal with this problem in various ways viz:
   i. Some decide to relocate their more labor-intensive activities to lower-cost locations.

ii. others decide to pull out of these operations altogether and buy them in from firms who are able to do it better. This is called outsourcing. **(8 marks)**

4. Infrastructure –The quality of a country's infrastructure may have a profound effect on a firm's competitiveness. This is usually provided by the state. In Nigeria where firms have to provide infrastructure, this will add to the cost of production thereby affecting the firm's productivity level and cost of production will be high. **(7 marks)**

5. Exchange rates – As an organization grows, the domestic markets may become unattractive due to competition and the managers look overseas to do business. In many cases, these markets can be extremely profitable. However, a serious constraint can be the fluctuations within the currency exchange rates. This can lead to either increase or decrease in profit due to nature of the fluctuation (i.e. positive or negative). **(8 marks)**

QUESTION 14

a. State Five (5) ways by which insurance businesses can contribute to the economic growth in Nigeria. (20 marks)

b. Identify five (5) reasons for take-overs and mergers of insurance companies.

SOLUTION TO QUESTION 14

a. Ways by which insurance businesses can constitute to the economic growth in Nigeria include:

1. They provide sources of capital for investment as they buy and sell services with the money collected from clients which yield large interests (i.e. helps to stimulate investment level)
2. They provide the means of a collateral security for individuals or organizations when required by banks
3. They provide employment.
4. They promote bilateral and multi-lateral trade through reinsurance with foreign firms.
5. They assist in providing diversification of the economy.
6. Provision of risk covers on economic activities.

(20 marks)

b. Reasons for insurance company takeovers and mergers are as follows:

1. Synergy – the whole has a greater value than the sum of the parts e.g. savings in IT costs.
2. Provide for geographical spread
3. Provides for economies of scale
4. The resultant company has a larger capital base
5. The merged companies can act as non-stop shopping for customers
6. A friendly merger may be a defensive measure against a hostile take-over by an unwanted competitor.
7. Can provide expertise in an area. **(18 marks)**

CHARTERED INSURANCE INSTITUTE OF NIGERIA

ADVANCED DIPLOMA

OCTOBER 2015 EXAMINATION PAPER

SUBJECT A655
RISK MANAGEMENT

Part ALL questions in Part I
Each question carries six (6) marks.
Note form is acceptable where this conveys all the necessary information.

QUESTION 1
What are the factors that can influence the attitude to risk?

SOLUTIONS TO QUESTION 1

- Financial strength and scale of the organization that will allow a certain level of financial loss to be absorbed.
- Culture of the organization, culture of the country, its unique market place and governing board.
- The flexibility within an organization that will enable it to meet urgent needs.
- The options available within the organization to cope with a risk incident in different ways.

QUESTION 2
Explain any three of the followings:

i. Pure Risks
ii. Speculative Risks
iii. Fundamental Risks
iv. Particular Risks
v. Operational Risks

SOLUTIONS TO QUESTION 2

i. Pure risks are those risks that have only the tendency of loss or no loss situation.

ii. Speculative risks that have the tendency of loss, no loss or break-even and a profit.
iii. Fundamental risks are those risks that have their impacts on the society at large.
iv. Particular risks are those risks that have their origin and impacts on an identifiable individual.
v. Operational risks are those that affect the operations of an organization.

<u>QUESTION 3</u>
What is dependency modeling and for what purpose is it best used

<u>SOLUTIONS TO QUESTION 3</u>

This type of modeling is a look backwards, from what needs to be achieved, at the key dependencies. It takes as view of how (and to what extent any scenario, or a combination of scenarios, will divert the organization from achieving their objectives.

<u>QUESTION 4</u>
What are the factors that can influence an organisation's attitude to risk?

<u>SOLUTIONS TO QUESTION 4</u>

- The financial strength and scale of the organization that will allow a certain level of financial loss to be absorbed.
- The culture of the organization, the culture of its origin, of its unique market place, and of the board itself.
- The flexibility within an organization that will enable it to meet urgent needs and the option to cope with a risk incident in different ways.
- The impact of each risk incident on the future trading activities of the organization.

<u>QUESTION 5</u>
What challenges can a Risk Manager face when trying to protect the good name of the organization in the face of a major media attack?

<u>SOLUTIONS TO QUESTION 5</u>

- The speed needed to respond
- Stopping misinformation (especially from own staff who may not be aware of the whole or the latest picture)

- Getting consistent information out to what is sometimes just a scrum of reporters.
- Ensuring that the spokesperson has the latest, trusted, information from within a fast developing situation.
- Providing a base of information that may be consistently valuable to a whole range of different audiences (and by necessity, stakeholders)
- Protecting sensitive information from a resourceful profession.

<u>QUESTION 6</u>
What is Risk Register?

<u>SOLUTIONS TO QUESTION 6</u>
The database of risks and consequences. The risk register may or may not include a database of risk incidents that have occurred.

<u>QUESTION 7</u>
List important things that Risk Policy Statement should address.

<u>SOLUTIONS TO QUESTION 7</u>

- Roles and objectives of the risk management functions
- How risks are to be identified, measured and prioritized for action.
- Decisions on which risks and levels of impact that can be retained within the organization.
- The lives of authority and responsibility.
- How risks are to be reported upwards and through the board.
- The methods by which change is monitored within the organization, particularly risks carried are identified for decisions.

<u>QUESTION 8</u>
What are the disadvantages of using Questionnaires to obtain information about risks?

<u>SOLUTIONS TO QUESTION 8</u>
The disadvantages are that they can:

- Be completed by someone who may not be skilled in the subject of the questionnaire.
- Be completed by someone who may not understand precisely the objectives and ultimate use of the answers.

- Focus the user's attention simply on the question themselves rather than in the wilder sense, on the actual task in hand.
- Be at risk of being completed too quickly, and thus without much thought, by someone who considers that their own time is better spent elsewhere.
- Be at risk of being completed by someone who may have their own reasons to suppress risk information.

QUESTION 9

a. **Write a memo to your Managing Director explaining how brainstorming can assist you as the company's Risk Manager.**

b. **You are addressing members of the Board of your company and a newly inaugurated member (who is to work on the Board's risk management Committee) ask this question: - "As a risk manager, do you set out to remove all risks?" Write your reports responding to the enquiry.**

c. **In a large group of companies mention key officers that should be members of Group Risk Committee, specifying their functions.**

SOLUTIONS TO QUESTION 9

Candidate should answer the question in memo form.

- Explanation of brainstorming is important and mention of who should be involved.
- The nature of the business of the organization will determine how regular with relevant department brainstorming can be organized.
- Person who understands a particular risk, risk incident and cost must be identified within the local environment and be involved in brainstorming.
- Brainstorming when conducted properly and in a conducive environment brings out wealth of knowledge, experience and understanding, that enable company to come out with blue prints
- Brainstorming will help in creation of Risk management committee and necessary risk policy statement can be drawn up easily.
- Brainstorming is one way of tapping into understanding the company's risk exposure and how to handle such.
- Outcome of brainstorming usually provide education and better understanding for those concerned including all other staff within the organization.

b. **Candidate should define risk management**

- Management of risks that threatens the Assets, operation and responsibilities of the organization.
- Options available to organizations in managing risk effectively without wastage of scare fund.
- The answer to the board member question is clear **No.**
- Risk manager sets out to reduce the probability or severity of risk incidents, down to a level that will be commercially acceptable to the organization.
- Risk manager draws attention of all stakeholders to identified risk.
- Risk manager identifies, analysis, monitor and reduce negative effect of risk on organization
- If risk manager is not there, identification and control might be taken for granted and killer risk will come as quaver worm to destroy the organization.

c. **Risk Director:** Director at the board of group individuals companies in charge of risk management.

Companies Director: In charge of compliance to avoid sanctions.

Group Internal Auditor: In charge of internal control.

Legal Director: In charge of secretariat, law and perfections.

Finance Director: To handle issue of fund security and management.

Public Affairs Director: Handling image for organization.

The committee receives reports and brainstorm accordingly. However, other managers and for external advisers can be seconded for specific/ individual matters of business.

<u>**PART III**</u>

Answer THREE (3) out of the following FIVE (5) questions. Each question carries 34 marks.

<u>**QUESTION 10**</u>

a. **What are the fundamental steps in setting out to create effective risk management in an organization?**

b. **Mention and discuss at least six (6) external sources of information available to the risk manager.**

SOLUTIONS TO QUESTION 10

- Understand what threats there are.
- Understand the potential of those threats to damage the company and its stakeholders.
- Understand the likely frequency of risk damage.
- Decide on the risk levels and frequency levels that are acceptable.
- Take action on risks deemed unacceptable.

b. The sources are:

- Crime prevention department of the local police service.
- Crime liaison panels.
- Fire liaison.
- Government departments.
- Insurers and reinsurer.
- Business associations and organization.
- Risk management associations.
- Consultants.
- Newspaper and magazines.
- Company reports
- The internet

QUESTION 11

a. Explain what a risk manager is trying to achieve with risk control.

b. The Health and Safety Executive booklet on fire gave necessary steps for assessing fire risks, state and explain the steps.

SOLUTIONS TO QUESTION 11

a. Reduce the frequency of damaging incidents, or reduce or remove the chances of the targeted risk incident occurring at all.

- Reduce or remove the extent of damage that may develop within one incident or over a period of time.
- prepare beforehand so that an organization can respond quickly and effectively to a damaging incident

b

The steps are:

Step 1 – Identify the location of people and assets at risk from fire.

Step 2 – Identify the fire hazards.

Step 3 – Evaluate the risks.

Step 4 – Record findings, prepare emergency plans and inform and train employees.
Step 5 – Update and revise assessment as necessary.

QUESTION 12

a. How can poor quality products cause significant damage to an organization?
b. Summarise the key aspects of risk management.

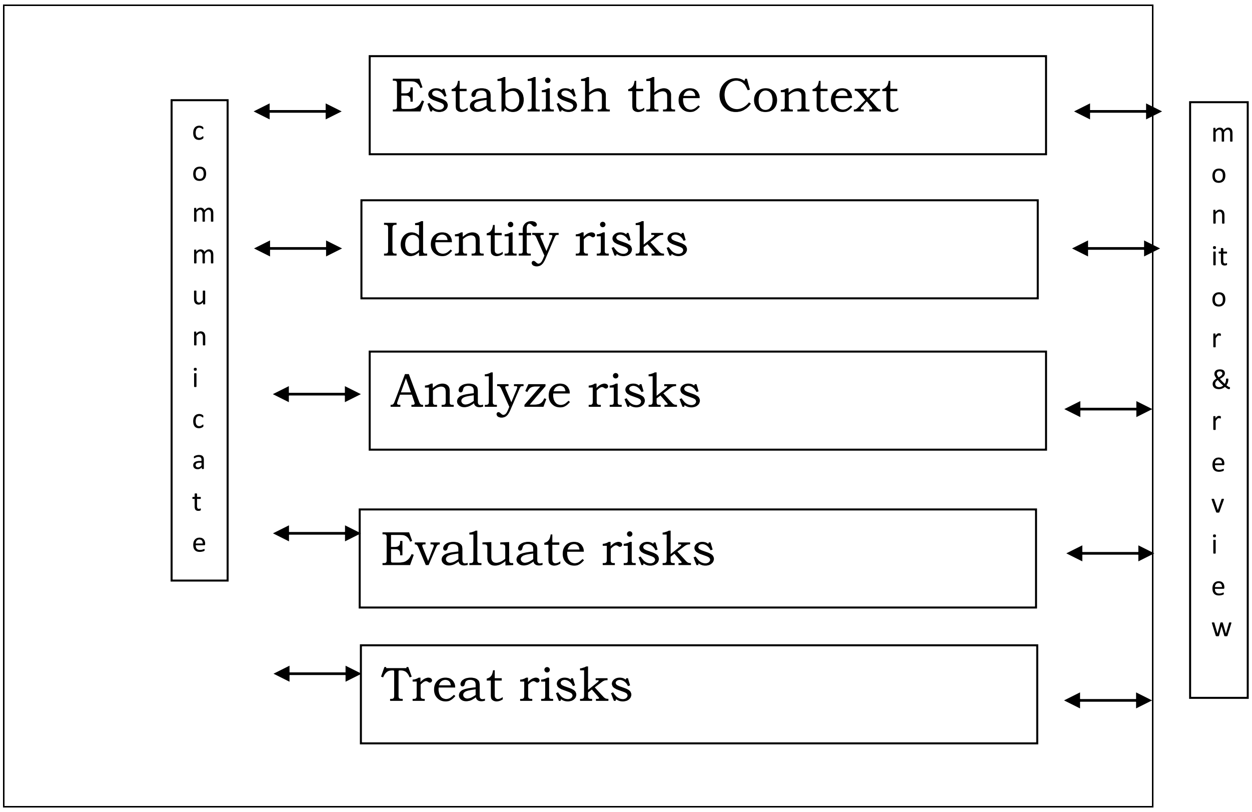
SOLUTIONS TO QUESTION 12

a.

- An impaired product may need to be recalled back to the factory for alteration or destruction. The process of recovering a large number of widely distributed products is in itself expensive and could cause damage to relationship.
- Such a public recall can bring long- term damage to the confidence the public holds in the product and the brand name.
- A poor quality product may also cause damage and loss in a way that could bring about litigation against the manufacturer.

b.

Step I Identify the locations of people and assets at risk from fire.
Step II Identify the hazards
Step II Evaluate the risks
Step IV Record findings, prepare emergency plans and inform & train employees.
Step V Updates and revise assessment as necessary.



QUESTION 13

a. **What aspects of a risk incident can affect the amount of the resultant financial loss?**

b. **State the advantages and disadvantages of setting review periods for individual aspects of risks.**

SOLUTIONS TO QUESTION 13

Monetary Costs:

a) The cost of replacing capital assts.
b) Loss of income, continuing costs and possibly increased cost whilst factories and other assets are being replaced.

- Timing of litigation and other necessary payments.
- Repeated incidents within one accounting period.
- Criticality to the business of the amount of time needed to reinstate services and
- Administration costs and opportunity costs in the diversion of resources from main stream operational needs.

b.

ADVANTAGES:

- Sets management standards for individual units.
- Ensures that risks come back unto the agenda regularly.
- The assessment of risk isn't put off until a more "convenient" moment.

DISADVANTAGES

- The risk may damage between the review periods.
- Operational units may feel that they do not have to consider the impact of any changes between review periods.
- Risk understanding is not considered as an integral part of the changes.

QUESTION 14

a. **How can a HAZOP Study assist the understanding of risk? What are its consequences?**

b. **What can a fault tree achieve?**

SOLUTIONS TO QUESTION 14

The hazard and operability (HAZOP) study is a tool that can be used where a crucial piece of equipment has been identified.

The study involves itself with four key questions:

- What is the part intended to achieve?
- What deviations are possible away from the usually expected delivery?
- What could be the causes or combination of causes to create those variations?
- What could be the consequences of those variations?

This provides useful working information for the risk manager.

b.

- It can look at flow chart from the point of view to risk and begin to assess the chances of that supply chain being broken; and
- It can look at risk within a process or piece of machinery and take a view on the potential for damage.

CHARTERED INSURNACE INSTITUTE OF NIGERIA

ADVANCED DIPLOMA

OCTOBER 2015 EXAMINATION PAPER

SUBJECT A735
LIFE ASSURANCE

QUESTION 1

a. **Who possess the legal interest in Trust Property?**

b. **State four (4) conditions under which a new trustee can be appointed as a replacement.**

SOLUTIONS TO QUESTION 1

(a)

- A Trust is a means of arranging property for the benefit of other persons without giving them control over it.
- the trustees have legal interest in the trust property. **(2 marks)**

(b) Under the Trustee Act 1925, a new trustee can be appointed to replace another one under the following conditions:-

- Death
- Desires to be changed
- Refusal to act
- Unfit or incapable of action e.g. insanity
- A minor (an infant) **(4 marks)**

QUESTION 2

a. **What is Underwriting in Life Insurance Business and what types of Medical factors will the underwriter look out for?**

b. **State six (6) of such factors.**

SOLUTIONS TO QUESTION 2

a.

- Underwriting is the process of assessing a proposal and deciding whether to accept the risk and if so, at 'what rates of premium' **(1 mark)**
- The Underwriter will look out for medical factors that can cause premature death of the proposer by illness or disease. **(2 marks)**

b. The medical factors include:
- Heart diseases
- Circulatory diseases
- Cancer
- Liver diseases
- Respiratory diseases
- Mental disorder
- Diabetes mellitus
- HIV/AIDS
- Eye disease
- Tropical diseases
- Kidney diseases
- Digestive system diseases
- Diseases of the nervous system
- Respiratory diseases
- Glandular diseases **(3 marks)**

<u>**QUESTION 3**</u>

a. What is Mortgage?

b. List four (4) of the conditions commonly found in Mortgages of Life Assurance Policies.

<u>**SOLUTIONS TO QUESTION 3**</u>

a. Mortgage is a type of assignment used in connection with a loan.
Life policies are commonly mortgaged to Banks, Building Societies, Life Offices as collateral security

b. The following conditions must be met:
- Mortgagor to pay premiums as they fall due,
- Must restore the policy if it lapses
- Mortgagor must ensure that the policy is valid, and if it becomes void, he must effect an equivalent new policy and mortgage same to the lender.
- Lender is empowered to pay outstanding premium due and add same to the principal loan,

- The lender can exercise the power of sale by surrendering the policy to the life office.
- Loan can only be granted on the security of the policy that can or has acquired surrender value.
- Maximum loan is 90% of Surrender value. **(4 marks)**

QUESTION 4

a. Outline the main differences between Life Assurance and Annuity contract.

b. Describe Annuity Contract when it is guaranteed.

SOLUTIONS TO QUESTION 4

a.

- Annuity deals with survival rather than death benefits, the premature death of an annuitant is therefore to the advantage of the life office. **(1 mark)**
- In life assurance, individual pays small contributions (premium) to receive lump sum later, whereas, in annuity, the individual pays lump sum in order to receive smaller amounts called annuities for as long as the contractual agreement permits. **(2 marks)**

b. When guaranteed for a period of time, it means that even if the annuitant dies before that period, the instalmental payment will be continued to be paid to his/her estate.

QUESTION 5

Illustrate the principles behind Resulting Trust.

SOLUTIONS TO QUESTION 5

A resulting Trust arises where there is a trust on which the property is held.

- Where the purpose of the trust can no longer be fulfilled, it is termed a resulting Trust for the creator of the trust.
- Therefore, the ownership of the property will revert to the person **(3 marks)**

Example:

- A man effected a policy on his own life on trust for his wife if living at his death but otherwise for his estate.
- He was murdered by his wife and a claim was made against the life office
- The claim was turned down as it is against public policy to allow a person to benefit from their own criminal act
- The trust has therefore failed and there was a Resulting trust of the policy money for the husband's estate. **(3 marks)**

QUESTION 6

a. **What is P.I.A?**

b. **List four (4) Investment Business regulated by P.I.A.**

SOLUTIONS TO QUESTION 6

a.

- P.I.A. means Personal Investment Authority
- It is a self-regulatory organization (SRO) which regulates long-term Insurance business and unit trust.

b. The Investment business regulated by P.I.A includes:

(i) Life Assurance
(ii) Unit linked income protection Insurance
(iii) Annuities
(iv) Unit trusts **(4 marks)**

QUESTION 7

a. **Describe Risk Premium Reassurance contract and**

b. **State who has the right of claim under a reassurance contract.**

SOLUTIONS TO QUESTION 7

a.

- Under a level premium system of premium payment, a reserve is built on a yearly basis.
- The difference between the sum assured and the reserve is the Death strain which also reduces every year.
- The Risk Premium reassurance reassures only the death strain and not a fixed proportion of the original sum assured.
- As the yearly reserve increases, the Death strain reduces so also is the Risk Premium cover
- Risk Premium reassurance does not cover liability for surrender or maturity claims as they are paid out of the office's reserve under the policy. **(5 marks)**

b. It is the principal office that has the right of claim against the reassured. **(1 mark)**

QUESTION 8

State six (6) uses to which computer processing may be put in the New Business department of a Life office.

<u>SOLUTIONS TO QUESTION8</u>

New Business Department:

- Produce quotation
- Check limit of non-medical
- Produce and issue acceptance letters
- Set up initial policy records
- Maintain lives assured names alphabetically
- Pay commission to company representatives
- Update commission account **(6 marks)**

Compulsory Question

This question carries 50 marks

<u>QUESTION 9</u>

a. As an Underwriter, you have been asked to assess a proposal for Life Assurance Cover on the life of Mr. Dickson, aged 45 years, an employee of XYZ Nigeria Ltd.

The completed proposal form has been submitted by his employer for a sum of 75 million naira for a term assurance policy with a term of 25 years.

i. Describe the key issues you would consider when assessing the risk.

ii. Identify and explain the evidence you would seek and the recommendations to give when assessing the risk.

b. Describe the main features of the following policies and the uses to which each can be put:

i. Family Income policy

ii. Low cost whole life assurance policy

<u>SOLUTIONS TO QUESTION 9</u>

- Proposer – XYZ Nigeria Ltd
- Life proposed - Mr. Dickson
- Relationship – Employee
- Age of life proposed – 45 years
- Cover proposed – Term Assurance
- Sum Assured – N75,000,000 = (N75m)
- Term /Duration – 25 years.

a. i. The issues to be considered when assessing the risk include:

a) The proposal is on the life of another person, hence the appropriate portions of the proposal must be duly signed by the life proposed to ensure that he is a party to the contract.

b) The purpose for the proposed assurance must be clear.

c) Do the employers have adequate insurable interest up to the proposed sum assured on the employee?

d) Check the relationship between the employee and the employer.

e) Ascertain the duties and the expertise of the employee to justify the proposed assurance (e.g. a marketing Executive, An inventor or an employee with valuable contacts)

f) Obtain the Memorandum of Association, 3 years Annual Financial Reports of the company in order to determine the setup, the operations, turnover and its profit levels etc.

g) Check the size of the sum assured proposed in line with other information in order to rule out over selling.

h) Check the state of health and other moral hazards of the life proposed that could be material facts for assessment. **(15 marks)**

(ii)

a. The life proposed will undergo medical examinations because of the
    a. The size of the sum assured proposed,
    b. Advanced age (45) years at entry because the basis of premium calculation is on the older the life, the higher the risk of death

b. The purpose of the proposed assurance must be made clear to enable the underwriter recommend the appropriate policy that would meet the needs of the company.
c. Insurable interest in the employee must be adequate for the proposed sum assured to guide against the possibility of fraud
d. It is important to confirm the extent of the relationship between Mr. Dickson and XYZ Nig. Ltd as a check against collusion against the life office and to facilitate the possibility of the company being granted tax relief.
e. Memorandum of Association of the company will confirm the existence and reveal the capability of the company to justify the proposed sum insured.
f. Instead of a 25years term assurance, I would recommend a Term Keynan Assurance, on a 5 year renewable basis with the option to renew every 5 years for as many times as required, without further evidence of health, up to age 65 years.
g. In view of the above, the 25 years term proposed by the employer may not be tenable since the maximum age at expiration of Life Assurance is 65 years.
h. The term of the proposed assurance will therefore be maximum of 17 years.

(20 marks)

b.

1. **Family Income Policy**

- A contract that provides a capital sum payable by instalments for a selected period to replace the income which the life assured would produce for their family if they were still alive.
- The policy pays out an equal amount each year from the death of the life assured until the expiry date of the policy.
- The instalments can be monthly, quarterly or yearly.
- A commuted value (lump sum) can be paid instead of the instalments
- The cover decreases over the term of the policy; the nearer the life assured gets to the expiry date, the less will be total of the instalments payable.

(5 marks)

2. Low cost whole Life Assurance Policy

- A with profit whole life contract with a guaranteed level of cover
- It is written with two sums assured
- Amount payable at death is the greater of
  - The basis sum assured plus bonuses or
  - The guaranteed death sum assured

- Bonuses are calculated on the basis sum assured, so the basic sum assured increases yearly with the declaration of bonuses until it overtakes the guaranteed death sum assured.
- The contract is in effect a with profit policy, incorporating a decreasing term assurance element which decreases as the bonuses increase.
- Premiums are lower than for ordinary non-profit whole life contracts.
- The benefits will not be as high as those of a full with profit whole life policy.
- The difference between the basic and the guaranteed death sums assured may be converted into the basic sum assured subject to the appropriate increase in premium
- The policy is used for family protection and inheritance tax funding.

(10 marks)

PART III

Answer three (3) out of the following five (5) questions. Each question carries 34 marks

QUESTION 10

a. Explain and comment on the basic Form usually used by Life office to process application for Life Assurance Contract.

b. Outline the Underwriting and the new business procedure of a Life office from receipt of a completed proposal to issuance of policy document.

<u>SOLUTIONS TO QUESTION 10</u>

- The basic form used to process life assurance contract is the Proposal form.
- The proposal form gives the basic information needed to assess the application.
- It must be duly completed and signed by the proposer.
- The form is divided into three sections:
  1st part identifies the life of the proposer
  2nd part specifies the details of the contract
  3rd part gives details of the risk.
- The declaration must be signed and dated to declare that the answer given to the questions on the proposal form to be true and it also allows life office approach the bankers and the doctors of the proposer for any further information.

(b) The procedure includes:

- The completed proposal form is received
- Check the office index if proposal has been made earlier on same life.
- If so, the documentation for those proposals is obtained to support the underwriting of current proposal.
- The proposal must be checked to ensure that all questions have been answered and the relevant declaration signed.
- The papers are then passed to the underwriter
- The underwriter will check the information on the form and decide if the proposal can be accepted at ordinary rates of premium without further investigation.
- The proposal is therefore passed to the policy issuing department. **(20 marks)**

<u>QUESTION 11</u>

a. Who may [not] insure under a Life Assurance Contract?

b. What are the Conditions that guide the Insured and the Insurer.

<u>SOLUTIONS TO QUESTION 11</u>

a. Those who may not insure under a life assurance contract include:

   i. Minors: A person under 18 years of age
      - Contracts by minors are not enforceable against them
      - Contracts for necessaries and certain contracts of employment beneficial to the minor are enforceable.
      - Other contracts are valid unless the minor repudiates the contract either before age 18 or within a reasonable time thereafter

- Insurance policies fall within this class
- Most life offices will not do business with proposer under 18 years unless subject to parental consent.
- The minor can still decide to repudiate the contract at age 18 years

(8 marks)

ii. People of unsound mind
- Contract is binding if the disability of unsound mind is not known by the other party
- Where it is evident at the time of the contract that one party is insane, the contract can be repudiated. **(8 marks)**

iii. Companies
- Have a legal identity separate from that of its members
- Powers to contract can be found in its constitution (memorandum & Articles of association
- Companies are bound by their contracts even if technically they have no power to enter into them.
- A company has the power to effect a policy on the life of a director or an employee, subject to insurable interest. **(8 marks)**

b. The conditions that guide the Insurance companies stipulate that the company must be authorized under the National Insurance Commission to do long term Insurance business.
- The insured too must have insurable interest
- And legal capacity to contract **(10 marks)**

QUESTION 12

a. Outline the process and procedure in the payment of a Death Claim.

b. What will you be concerned with as claims manager if a death claim is notified three (3) months into the life of the policy?

SOLUTIONS TO QUESTION 12

(a)

- Check index of lives assured to ascertain policy existence
- Exact date of death must be obtained to determine the level of bonus
- Proof of death
- Cause of death, to show validity of claim
- Check that premiums are paid to date
- Production of policy document
- Proof of age (where not earlier admitted)

- A duly completed and signed discharge form from the claimant.
- Claimant to prove title. **(18 marks)**

(b)

- The office must note the cause of death on the death certificate produced
- Death may have occurred from causes excluded from the cover provided
- Since in this case, death occurred within 3 months of the issue of the policy, there may be a possibility of non-disclosure of material facts.
- If evidence confirms that the cause of death was due to non-disclosed material facts, the office can repudiate liability.
- If non-disclosure is fraudulent, the claimant has no legal right to recover premium
- Where it is non-fraudulent, premiums may be refunded without interest.

(16 marks)

QUESTION 13

Q Mr. Kenneth Okoh has eleven (11) children, one of which is the only three (3) years old son, Jude. He has asked you for a life assurance on the life of the only male child for his own benefit to show how much he loves the child.

a. Discuss if Mr. Okoh has legal right with respect to insurable interest to do so.
b. Give five (5) examples, with reasons, where insurable interest will be present in life policies effected by one person on the life of another.
c. Explain why insurable interest must only exist at the inception of a life assurance contract but necessarily at the time of claim.

SOLUTIONS TO QUESTION 13

a. Mr. Kenneth Okoh, as a parent has an obligation to love and take care of his children but that does not confer on him the legal right in respect of insurable interest, to insure the life of his only son Jude for his own benefit.
Insurable interest only exist where there is a loss measurable in monetary terms. In the event of the death of his son, no quantifiable financial loss would be suffered by Mr. Okoh.

The love shown by him to his only son is only sentimental and it is of no financial value.
However, Mr. Kenneth Okoh has the unlimited insurable interest in himself to insure his life for the benefit of his children, for instance in the areas of their education. **(12 marks)**

b. Insurable interest will be present in life policies effected by one person on the life of another in the following cases:

(i) Husband on Life of a wife
A man has unlimited insurable interest in the life of his wife as with a wife, on the life of her husband. The death of one spouse will cause a great loss, including financial, to the other.

(ii) Creditor on the life of a debtor
A creditor has insurable interest on the life of his debtor to the extent of the amount of the debt owed because should the debtor die without paying off his debt, the creditor will suffer some financial loss.

(iii) Partner on the life of other partner
The death of a partner could cause some financial loss to the surviving partners of a firm. They therefore have the insurable interest to assure the life of each other to protect against such potential loss.

(iv) Employer in the life of employee
- An employer has insurable interest on an employee for the value of services agreed to be rendered.
- He can effect life policy on key employees for the loss the company will suffer in the event of the death of the key employee.
- There may be interest for the amount of any death benefit payable under a Pension Scheme.

(v) A done of a life time gift in the life of the donor
Insurable interest exists for 7 years in the life of the donor of a life time gift for inheritance tax, payable should the donor die within 7 years of passing the gift
(3 marks each = 15 marks)

(c) Insurable interest need not exist at the time of claim because life assurance is not a contract of indemnity. A contract of indemnity provides that the amount of claim payable at the time and place of claim will be determined by the insured's actual financial loss, so as to place him in the position the insured was before the loss, subject to the adequacy of the sum assured.

The above situation does not apply to life assurance business as it is impossible to equate life to a precise financial value to an exact financial compensation.

Life assurance business is a benefit contract. **(7 marks)**

QUESTION 14

a. **A proposer for Life Assurance has been required to undergo Medical examinations. State the factors usually considered by the underwriter in requesting for medical examination.**

b. **Describe the procedure usually followed by Life Office for the conduct of medical examination.**

c. **What are the rights of the life proposed under the Access to Medical Reports Act 1988.**

SOLUTIONS TO QUESTION 14

a

The factors usually considered include:

(i) The size of the sum assured:
The larger the sum assured proposed, the higher the risk of loss.

(ii) The age of the proposer at entry
The mortality tables are based on the fact that the risk of death increases with age. Hence, the higher the age of the proposer, the higher the premium that is payable.

(iii) The information on the completed proposal form may set the underwriter an enquiry for further opinion.

b

- List of field medical Doctor to carryout Medical examination requirements on proposer.
- Doctor in the proposer's area will be requested to conduct the examination
- The proposer will contact the doctor for an appointment
- The doctor will then conduct the specified medical examinations and report same on the standardized Medical Examiner's Report.
- The 1st part of the report completed is based on the information given by the proposer.
- 2nd part is from the results of the medical tests
- The life office will pay the doctors fee for the examination. **(12 marks)**

c

- Life office reserves the right to apply for the medical report from the doctor who has attended a proposer for life assurance.
- Under the access to Medical Reports Act 1988, life proposed has the right to refuse to allow a life office to obtain report of medical tests conducted on him

- The demerit of this right if exercised is that the life office would be unable to process and accept the application.
- If the proposer consents to the life offices request, and the medical report is to be obtained, he can also indicate whether or not he would wish to see the report.
- If the proposer does not wish to see the report, the doctor can then return it to the life office.
- The Act allows the proposer to change his mind and request to see the report at any time within 6 months where the doctor has already forwarded the report to the life office, a copy of the report can be made available to the proposer within 21 days.
- If the proposer indicates at the onset that he wishes to see the medical report, this may delay processing the application since the doctor will need to give an appointment of 21 days to arrange to see it.
- The doctor is allowed to charge the proposer a fee to cover the cost of supplying the report. **(13 marks)**

CHARTERED INSURANCE INSTITUTE OF NIGERIA

ADVANCED DIPLOMA

OCTOBER 2015 EXAMINATION PAPER

SUBJECT A745
PRIN. OF PROPERTY & PECUNIARY INSURANCE

PART I
Answer ALL questions in part I.
Each question carries six (6) marks.

QUESTION 1
In what circumstances may an insured ask for a Collusion extension?

SOLUTIONS TO QUESTION 1

A theft policy covers involving
a. Forcible and violent entry and/ or exit.
b. Assault or violence (or threat thereof) to insured or staff.

Therefore, Collusion by staff (e.g. facilitating forcible and violent entry/ exit) is often asked for as an extension to the above / basic cover.

QUESTION 2
As an Underwriter, what do you understand by the term:

- **(a) Gross Premium**
- **(b) Net Premium**
- **(c) Earned Premium**

SOLUTIONS TO QUESTION 2

a. **Gross Premium** = Total premium paid by insured
b. **Net Premium** = Gross Premium less commission paid to intermediaries.
c. **Earned Premium** = That portion of the net premium defined in (b) which relates to the time which has elapsed from inception (or last renewed dates of each policy current in force, to the date to which the earned premium is required to be calculated.

QUESTION 3
What are the main covers usually insured under a Combined Policy?

SOLUTIONS TO QUESTION 3

- Business Interruption
- Theft
- Money
- Glass
- Liabilities

QUESTION 4
Give four (4) examples of those who can present risk to an underwriter for insurance cover.

SOLUTIONS TO QUESTION 4

- Agents
- Proposer
- Bank
- Solicitor
- Another Insurance Company
- Insurance Department of an organization.

QUESTION 5
Where you are expected to review a total portfolio, what will be your 'Burning Cost' of an accountant for a particular class of business?

SOLUTIONS TO QUESTION 5

Burning Cost: $\dfrac{\text{Total of all claims paid in the class}}{\text{Total sum insured written in the class}}$

QUESTION 6
What is a Valued Policy?

SOLUTIONS TO QUESTION 6

Valued Policy is used for the insurance of works of art and other objects whose true value is otherwise often a matter of dispute at the time of a claim. In time the value (usually fixed by a professional valued approved by the insurer) of the subject matter is agreed at the onset between the insured and insurer and the sum insured i.e. fixed accordingly.

QUESTION 7
Briefly describe what a Bond seeks to insure.

SOLUTIONS TO QUESTION 7

A bond is issued by surety (or insurer) to provide an indemnity to be protected party (or insured) in the event of the principal appointed by the protected party to perform a stated duty or function failing to perform that duty or function. The indemnity is the amount of the bound stated in the bound.

QUESTION 8
What is an Indemnity Period?

SOLUTIONS TO QUESTION 8

Indemnity Period: The period beginning with the occurrence of the insured damage and ending not later than the maximum period specified in the policy after that date during which the results of the business insured are affected in consequence of the damage.

Part II
Compulsory question
This question carries 50 marks

QUESTION 9

a. **The following figures were supplied by an Insured's Accountant.**

   The policy is written on a Standard sum insured basis and is based on a 12 months maximum Indemnity Period.
   The business is expected to grow by 12% next year and by 15% the following year.
   Inflation is thought to be in the region of 5%

TRADING ACCOUNT

	₦		₦
Opening Stock	**200,000**	**Turnover**	**2,670,000**

Opening work-in-progress	110,000	Closing Work-n-progress	325,000
Purchases	1,544,000	Closing stock	178,500
Sub-contract costs	324,000		
Direct wages	413,000		
Power costs	73,500		
Packaging materials	214,000		
Carriage	29,000		
Gross Profit	265,000		
	3,173,500		3,173,500

PROFIT AND LOSS ACCOUNT

	₦		₦
Salaries & Indirect wages	69,510	Gross Profit (from Trading Account)	265,000
Rent and Rates	100,000	Discount on Purchases	21,500
Advertising	12,500		
Postages & Telephone	6,000		
Stationery	3,300		
Lightening & Heating	11,000		
Insurance	12,000		
Bank charges	4,500		
Net Profit	67,690		
	286,500		286,500

Showing all workings, determine:

a. The Gross Profit

b. Use the following information to calculate, showing all your workings, the loss payable following a recent fire incident.

   i. Cover is written on a sum insured basis and a 12 month indemnity period ₦750,000
   ii. Additional increase in cost of working item ₦220,000
   iii. Turnover in the last financial year prior to the loss ₦2,500,000
   iv. Gross profit in the last financial year prior to the loss ₦835,000
   v. Standard turnover ₦1,750,000
   vi. Turnover achieved during indemnity period which avoids ₦450,000 reduction in turnover N200,000
   vii. Savings made during the indemnity period ₦30,000

SOLUTIONS TO QUESTION 9

The following figures were supplied by an insured's Accountant.

The policy is written on a standard sum insured basis and is based in a 12 months maximum indemnity period. The business is expected to grow by 12% next year and by 15% the following year.

Inflation is thought to be in the region of 5%

TRADING ACCOUNT

a.		**₦**		**₦**
Opening Stock		200,000	Turnover	2,670,000
Opening work in progress		110,000	Closing work-in- progress	325,000
Uninsured Variable Cost:			Closing Stock	178,500
Purchases		1,544,000		
Less Discount	21,000	1,522,500		
Sub- contract cost		324,000		
Packaging Materials		214,000		
Carriage		29,000		
Gross profit		773,000		
		3,173,500		**3,173,500**

Gross Profit ₦773,000

An additional allowance should be made for the effects of growth within the business during the indemnity period, the business is expected to grow by 12% next year and by 15% the following year.

An allowance for inflation should be made in the sum insured.

Therefore, ₦773,000+ 12% +15% +5% +5%

= ₦865,760 + 15% = ₦995,624

= ₦995,624 + 5% = ₦1,045,405.20

=₦1,045,405 + 5% = ₦1,097,675

b

i) Calculate rate of Gross profit

$\frac{GP}{T/0} \times 100$

$= \frac{835,000}{2,500,000} \times 100 = 33.4\%$

ii) Reduction in Turnover:

Standard Turnover – Turnover achieved
₦1,750,000 – ₦1,350,000 = ₦400,000
= ₦400,000 X 33.4% = ₦133,600

iii) Increase in cost of working ₦200,000 increased cost which avoided a reduction in turnover of ₦450,000

Apply rate of gross profit to turnover avoided N450,000 X 33.4% = ₦150,300.

iv) Adjusted loss before the Application of average

	N
Reduction in Turnover	133,600
Increased costs	150,300
	283,900
Less Savings	30,000
	253,900

v) Application of Average

$$\frac{\text{Sum Insured}}{\text{Rate of Gross Profit X Annual Turnover}} \text{ X Loss}$$

$$= \frac{750,000}{33.4\% \text{ X } 2,500,00} \text{ X } 253,900$$

$$= \frac{750,000}{835,000} \text{ X } 253,900$$

= ₦228,054

vi) Application of the additional increase in cost of working item:

	N
Cost Incurred	200,000
Amount covered	150,300
	49,700

vii) Total Adjusted Loss
228,054
49,700
277,754

Part III

Answer three (3) out of the following five (5) questions.
Each question carries 34 marks.

QUESTION 10

a. **Explain the cover provided by an additional increase in cost of working item and why it may be requested by an insured. (17 marks)**

b. **Explain the cover provided by increase in cost of working only and the advantages and disadvantages of this form of cover to a professional insured. (17 marks)**

SOLUTIONS TO QUESTION 10

a. This increase in cost of working cover provided as part of gross profit is restricted by economic limit. This is expressed as an amount "not exceeding the sum produced by applying the rate of gross profit to the amount of the reached thereby avoided"

It can be referred to as spending no more than "a naira to save a naira". However, there are some businesses that may require more than this to regain customers. E.g. in a particularly competitive market, a company may need to spend more than the economic limit to regain customers. Hence, there is the need for the additional increase in cost of working item.

This States: The insurance under this item is limited to additional expenditure necessarily and reasonably incurred for the sole purpose of avoiding or admonishing the reduction in turnover which but for the expenditure would have taken place during the indemnity period in consequence of the damage.

b. Increase in cost of working on cover is used where a business can continue earning revenue dispute a loss of premises.

An example may be a small firm of solicitors who can continue to act for clients and hence earns fees without premises.
Increase in cost of working only, provides cost to continue the business for items such as:

- The cost of obtaining new premises
- The cost of staff to recreate records
- The additional rental costs for equipment.

The advantages of this cover are that it assists an insured to maintain their business in the event of damage but without the additional premium associated with a full gross profit or revenue cover.

One disadvantage however is that of setting the sum insured. It may be that the insured for it difficult to set an adequate amount and it may be advisable to review it each year, not just for inflation but the costs it may have to meet.

QUESTION 11

In connection with consequential Loss Insurance:

i. **Define Turnover** **(6 marks)**

ii. **An insured has asked for your advice as their broker on how to set the maximum indemnity period. Describe the factors that should be considered.** **(16 marks)**

iii. **The insured decides to take a 36 months Indemnity Period, but are concerned about the effects of inflation on the sum insured as a result of the application of average.**

Explain how the cover could be amended to give the insured some comfort and how this revision in cover would operate. **(12 marks)**

SOLUTIONS TO QUESTION 11

i. **Turnover** is defined as the money paid or payable for foods sold and delivered and for services rendered in the curse of the business

ii. **Maximum Indemnity Period (M.I.P)**

Factors include the following:

- What would be the maximum extent of the physical damage to the premises?
- Consider damage at worst time for largest assessed reinstatement hire.
- Seasonal issues to be considered
- Reinstatement time of building including planning, rebuilding, ease of transfer to other sites.
- Reinstatement time of machinery including ordering time, ease of transfer of production.
- Any specialist machinery
- How long would it take to replace stock? what better stock is kept.
- Is there another suitable facility in the vicinity firm which to operate temporary.

iii. Declaration linked policy should be suggested here:

- The insured estimate the sum insured they feel is reasonable and concurrent with the period of insurance
- Time is then adjustable in reflect the length of the indemnity period.
- A limit of liability applied 133.33%

QUESTION 12

As an underwriter, you are asked to present a paper on Day One Reinstatement.

a. **Explain what is meant by Day One basis of Reinstatement and what its benefits are to an insured. (12 marks)**

b. **What is the meaning of 'Declared Value' and what should an insured include when fixing this amount? (12 marks)**

c. **Explain how a non-adjustable basis would work and give an example of the calculation. (10 marks)**

SOLUTIONS TO QUESTION 12

a. The premium is adjusted at year and based on actual figures earned.
Up to 50% is allowed as a rebate, full amount is charged if the sum insured exceeds the estimate.

This is a way of giving reinstatement cover on a simple basis that the previous schemes that need to allow for inflation of sum insured. These applied to building and content but not stock. The sum insured consists of two parts:

- A declared value which is the cost of reinstatement at day were at inception or renewal of policy.
- An inflation factor being an amount to cover the effect of inflation on the cost of rebuilding during the policy period and any subsequent rebuilding period.

Benefit to Insured

- The insured does not need to forecast the cost of rebuilding at future date.
- There is no need for professional valuation
- Average only applied to the day one require.

b. Declared Value means the cost of reinstatement of the property insured arrived at per the basis of settlement- reinstatement clause at the level of costs applying at the start of the period of insurable.

What the insured should include

- Additional cost of reinstatement to comply with public authority requirements.
- Professional Fees.
- Desire removal costs.

c. The premium is calculated by the insurer by applying the risk rate to the declared value set at the state of the period of insurance.

This will produce the basic premium. A load accreting to what figure is chosen by the insured for the inflation amount is added to the basis premium.

The total basic premium and the loading is the premium charge.

Example of a calculation of a non- adjustable basis.

Declared Value:	₦1,000,000
Risk Rate	0.2%
Basic Premium	₦1,000,000 X 0.2% = ₦2,000
Inflation Figure	50%: Loading 15% 15% of ₦2,000 = ₦300
Total Premium	₦2,,000 + N300 N2,300
Sum Insured	N1,000,000 X 15% = N150,000

Sum Insured + Loading N1,150,000

Therefore; Sum Insured N1,150,000

QUESTION 13

State the objectives of the following legislation, to which equipment they apply and the duties imposed on owners and users of plant affected.

i.	**Pressure Systems Safety Regulation 2000**	**(14 marks)**
ii.	**Electricity at Work Regulations 1989**	**(10 marks)**
iii.	**Lighting Operations and Lighting Equipment Regulation 1998**	**(10 marks)**

SOLUTIONS TO QUESTION 13

a. Pressure System Safety Regulation 2,000

Objectives: To prevent the risk of serious injury from the sudden and uncontrolled release of stored energy in a pressure system or any part of it. The regulations are only concerned with the contents of the system where they are under pressure. Except for steam, they are not concerned with other aspects of the contents such as toxicity.

They do not apply to the whole system and not just for the pressure vessels themselves.

The regulations define a pressure system in two parts:

- First a system with pressure vessels, associated pipework or a pipeline, all which contains or can contain a relevant fluid.
- Secured, the relevant fluid being steam, a fluid above a given pressure a gas or liquid in given states e.g. LPG.

There are four main duties and they apply to users of fixed plant and owners in case of mobile plant.

- To establish and use the plant within safe operating limits.
- To establish a written scheme for periodic examination by a competent person.
- To conduct examination in accordance with the written scheme.
- Action in case of imminent danger either immediate repairs or written report.

b. Electricity at Work Regulation 1989

Objective: To require precautions to be taken against the risk of death or personal injury from electricity in work activities.

The regulations apply to any electrical equipment and any work activity having a bearing on electrical safety.

Duties are imposed on both employers and employees.

They fall under various headings, such as construction of electrical systems, their strength, insulation, earthling, connections, means of cutting off supply, working on or near equipment and persons being competent to prevent danger.

c Lighting Operations and fitting equipment regulation 1998

Objective: To provide a simple set of regulation replacing those previously applying.

This is to remove anomalies apply under Health and Safety Legislation, replace previous lifting regulations. Lifting equipment defined as work equipment (any equipment used for work) for lifting or lowering loads and including it attachments used for anchoring fixing or supporting it.

The regulations require the employer to ensure the equipment has periodic thorough examinations and inspections.

This should be every 6 months for equipment involving lifting people and 12 months for other types.

QUESTION 14

Business Interruption insurers in Nigeria have shown great concern that loss settlements under their policies have been reduced owing to inadequate sums insured.

As a Research Consultant, advise Insurers on steps to be taken to provide an Insurance to meet this problem. (34 marks)

SOLUTIONS TO QUESTION 14

- Business interruption insurers should advise insurers to take up the Declaration Linked Business Interruption Insurance.
- Insurers require the insured to provide an estimated Gross profit sum insured for the Insurance year.
- Insurers should charge a provisional premium.
- Insurer provide cover for 133 $^{1/3}$% of the sum insured

This is the limit of liability

- All losses up to the limit of liability are paid in full

- Average does not apply
- If the policy has extensions e.g. suppliers or customers extensions and are started in percentages, the percentages apply to the limit of liability not sum insured.
- The policy is adjustable on the submitted audited amounts
- If return premium, the maximum refund is 500% of the provisional premium paid.
- If additional premium, there is no upper limit.
- The policy provides for automatic reinstatement of sum insured.

CHARTERED INSURANCE INSTITUTE OF NIGERIA

ADVANCED DIPLOMA

OCTOBER 2015 EXAMINATION PAPER

SUBJECT A755
LIABILITY INSURANCE

Part I
Answer ALL questions in part I.
Each question carries six (6) marks.

QUESTION 1
What do you understand by the term 'Professional Negligence'?

SOLUTIONS TO QUESTION 1
Professional negligence is the error, omission, wrong advice, mistake etc. which is committed by people in professional practice in the conduct of their business. Failure of people in professional practice to exercise high degree of skill and care expected of them will result in professional negligence.

QUESTION 2
Briefly explain the followings in relation to Risk Management:
a. Frequency
b. Severity
c. Risk Control

SOLUTIONS TO QUESTION 2
a. Risk frequency explains how often a given event will occur or happen. Risk is inherent in all business ventures which may result in financial loss when they occur. Some risk occurs frequently (often) while some occurs occasionally.
b. Severity is the financial impact which the occurrence or happening of an event will have on the company some event occurs often (motor accident) with less severity of impact while some event occurs occasionally (air disaster) with high severity of impact.
c. Risk control involves treatment of risk or loss exposures which have been identified and evaluated. Risk control process also entails making decision on cost versus benefit basis.

QUESTION 3
Tort is a civil wrong. List six (6) forms of tortuous liability.

SOLUTIONS TO QUESTION 3
They are: Negligence, Nuisance, Breach of statutory duty as well as the rule on Rylands V. Fletcher, strict liability and tort of defamation (libel and slander).

QUESTION 4
Distinguish between Physical hazard and Moral hazard.

SOLUTIONS TO QUESTION 4
- Physical hazard relates to the physical or tangible aspect of the subject matter of insurance which are likely to influence the occurrence and/ or severity of loss.
- Moral hazard is concerned with the attitudes and conduct of the people which is capable of influencing the occurrence and/ or severity of loss.

QUESTION 5
The maxim 'res ipsa loquitur' is based on two (2) main criteria. Mention them.

SOLUTIONS TO QUESTION 5
- The object that caused the damage is under the direct control of the dependant or their servants or agents.
- The accident must be such that in the ordinary course of things it could not have occurred without negligence.

QUESTION 6
Define and explain the rule in Ryland V. Fletcher.

SOLUTIONS TO QUESTION 6
The rule of Ryland V Fletcher 1868 state that "An occupier who brings onto and keeps on his land anything which is likely to cause damage if it escapes is under strict obligation to prevent its escape and is liable for any damage caused as a result of its escape.

QUESTION 7
Explain the meaning of this term 'Territorial Limit'.

SOLUTIONS TO QUESTION 7

Territorial Limit concerns the territory or geographical area where a policy will operates. It is usual to stipulate that the bodily injury, death, illness/disease, damage to property etc. must be sustained within a particular area. Insurer will pay or honour claims which occur within the territory or geographical area of the policy.

QUESTION 8

a. **What is the English translation of the Latin Maxim: "volenti non fit injuria"? Give example.**

b. **What is the limitation period for claims involving personal injury?**

c. **How is the failure of a product to fulfill the intended purpose described?**

SOLUTIONS TO QUESTION 8

a. No injury is done to a willing person.

b. Three (3) years

c. Efficacy Risk.

Part II

Compulsory question

This question carries 50 marks.

QUESTION 9

a. **M & J is a Public Liability Company that is involved in many commercial activities such as manufacturing of household consumable goods, importation, distribution of textile materials, and professional Consultancy services on health related issues. The company business activities cover all the States of Nigeria.**

Requirement:

As a liability Underwriter, you are required to critically examine the operation of this company and answer the following questions:

i. **Identify and explain five (5) sources by which the company's potential legal liability may arise. (15 marks)**

ii. **Name liability policies that will be appropriate to cover the sources of potential liability you identify in (i) above. (10 marks)**

iii. **Explain briefly the cover provided for each of the liability policies you mention in (ii) above. (15 marks)**

b. **What is the purpose of Employers' Liability (Compulsory Insurance) Act 1969. (5 marks)**

c. **Explain the concept of 'Contributory Negligence' (5 marks)**

SOLUTIONS TO QUESTION 9

a.i. Potential liability of their company may arise as follows:

- Ownership of motor vehicles. The vehicles used by the company in their operations are sources of legal liabilities such as third party's death, bodily injury and damage to property.
- Employment of employees. The employees employed by the company can constitute a source of legal liability. Example, employees can sustain injury or death in the course of their employment, the company will be liable.
- Through their operations nationwide, negligence of their employees may result in bodily injury, death and property damage to third party for which the company is liable.
- Any defect in the product manufactured or distributed by the company is another source of their potential liability.
- Through the consultancy services they rendered, the company is also open to liability from their customer which may arise from their professional negligence. **(15 marks)**

ii. The following places will be appropriate:

- Motor Third party Insurance
- Employer's liability Insurance
- Public liability insurance
- Product liability insurance
- Professional indemnity insurance **(10 marks)**

iii. a. Candidates are expected to explain the cover provided by the liabilities policies they recommend. **(15 marks)**

b. The purpose of employers liability (compulsory Insurance) Act 1969 is to provide security for employees if they meet with an accident or incur an illness in the course of their employer is responsible. **(5 marks)**

c. **Contributory Negligence:-**This is one of the defenses to an action in negligence cases. Before 1945, it was a full defense i.e. if it could be shown that the plaintiff was partly to blame for the accident, they would recover nothing. This was amended by the law reform (contributory Negligence) Act 1945 which stipulates that damages will be reduced to such an extent as the court thinks equitable. **(5 marks)**

Part I

Answer three (3) of the following five (5) questions
Each question varies 34 marks

QUESTION 10

a. **Explain clearly that the occurrences that are covered in public liability policy.** **(15 marks)**

b. **Distinguish between occurrence and claim made basis.** **(10 marks)**

c. **In Employers' Liability Insurance, Regulation No. 2 prohibits some conditions from the policy. Mention and explain the conditions.** **(14 marks)**

SOLUTION TO QUESTION 10

a)

i. **INJURY:** Public liability policy will provide indemnity to the insured arising from bodily injury suffered by a third party. The injury must be physical. However, bodily injury has now been extended to includes psychological injury such as mental anguish, stress, shock etc. some policy provide cover for personal injury such as wrongful arrest, malicious prosecution, defamation etc.

ii. **DAMAGE:** Public liability policy provides indemnity to the insured arising from the damage or loss to tangible property. Some policies may extend cover to consequential loss in connection with the damage to the property. This is subject to foresee ability test. **(15 marks)**

b. **Occurrence Basis:** This provides that the accident or event causing injury or damage must occur during the period of insurance.

Claim Made Basis: This provides that the claim must be made on the insured during the period of insurance; the date of the negligent act is irrelevant. **(10 marks)**

c. **The conditions that are prohibited are:**

- Breach of policy terms and conditions by the employer e.g. failure or delay in claim notification.
- Any lack of reasonable care by the employer to protect employees against the risk of bodily injury or disease.
- Any breach of any enactment or regulations concerning the protection of employees.

- Failure by the employer to keep proper records as required by the policy for the purpose of premium adjustment. **(14 marks)**

QUESTION 11

Write short notes on any five (5) of the followings

(a) Negligent Misstatement
(b) Animal Act 1971
(c) Vis Major – Act of God
(d) Premium Adjustment
(e) Discovery period
(f) Damnum sine injuria
(g) Housekeeping **(7 marks)**

SOLUTION TO QUESTION 11

a. **Negligence Mis-statement**

Legal liability now attach for negligent misstatement which result in financial loss. A person who give advice whether verbal or in writing will be liable if another person rely or acted on the advice which result in financial loss.
In Hedley Byrne V. Heiler and Partners 1963, the court rules that a duty of care is owned to avoid negligence misstatement and advice.

b. **Animal Act 1971**

Animal Act 1971 contains the law relating to ownership or possession of animals. A person may be negligent in their activities in relation to animals. This act replaced certain areas of the common law on animal. The most important section is section 2 which introduced strict liability for certain animals.

c. **Vis Major- Act of God**

This is one of the defence to an action in tort. Act of God is an event due to natural causes directly and exclusively without human intervention and which could not have been prevented by any amount of foresight, pains and reasonable care. Examples are rainfall, storms or tornadoes.

d. **Premium Adjustment**

Premium adjustment is a clause in employers' liability insurance policy. The premium charge on this policy at inception based on the estimate of salaries and wages of employees will be adjusted at the expiry of the risk based on the variations in the risk exposures. At the end of the period, the insured is obligated to declare the actual salaries paid and the premium will then be adjusted by the insurer. The premium adjustment may require the insured to pay additional premium or the insurer may be required to make a refund subject to minimum premium chargeable for the risk.

e. **Discovery Period**

This is peculiar to professional indemnity insurance and it is extension granted by the insurer after a policy has lapsed. The period may be three months or more and it is intended to discover claims (negligent acts) which occurred during the period of insurance but which do not come to light until after the policy has lapsed.

f. **Damnum Sine Injuria**

Damnum sine injuria means wrong done without the commission of a Legal wrong. In tort, breach of duty which causes injury or damage will lead to a claim. However, not all actions which cause injury or damage give the right to a claim in tort. For example, there is no duty to serve a person drowning even if one can swim well.

g. **Housekeeping**

Housekeeping involves good management of the insured's premises, state and proper training of employees. It also involves training and education of staff on safety procedure. Good housekeeping involves cleanliness of office premises, good maintenance culture, good communication at all level and good supervision of employees.

QUESTION 12

a. Who is a Director? (4 marks)

b. Explain three (3) ways by which liability of a director may arise. (15 marks)

c. Directors' and Officers' (D&O) liability insurance can be arranged in two parts. Explain. (15 marks)

SOLUTIONS TO QUESTION 12

a. A director is an officer of a company with managerial responsibility. The management of a company is essentially in the hands of the directors. A director works with the company secretary and other executives to manage the affairs of the company. **(4 marks)**

b. Liability of a director may arises in the following ways:

- Negligent advice or misstatement.
- Any act which goes beyond the limits of the company's constitution.

- Error of judgment
- Negligent supervision of delegated responsibility.
- Imprudent investment **(15 marks)**

c. D& O liability insurance can be arranged in two parts as follows:

i. Directors' & Officers' Liability

This provides indemnity to the director and officers' for their wrongful act committed during the period of insurance which resulted in financial loss to the company.

ii. Corporate Reimbursement

This provides indemnity to the company for financial loss suffered during the period of insurance arising from the directors' negligent. **(15 marks)**

QUESTION 13

a. Discuss the following in relation to Public Liability Insurance Policy

i. Defence cost

ii. Multi-Tenanted Premises

iii. Limit of indemnity

iv. Wages, Salaries and other Earning

v. Pollution

b. Discuss the liability of Hotel Proprietor.

SOLUTIONS TO QUESTION 13

i. **Defence Cost**

Most liability policies provide cover for defence cost. These are costs involved in investigating incidents and for defending the claim on behalf of the insured. Legal cost incurred in defending the insured is an example of defence cost.

ii. **Multi- Tenanted Premises**

When a premise is multi – tenanted, the liability risk may be very high because various business operations will be on at the premises and present various degrees of hazards. In multi-tenanted premises, the risk of fire spreading is eminent and their increases the potential liability to third party.

iii. **Limit of Indemnity**

Most liability policies have limit of indemnity for any one occurrence which represent the insurer maximum amount payable to the insured. Limit of indemnity is wholly fixed by the insured which represent their legal liability to third party for bodily injury, death or damage to property.

iv. **<u>Wages, Salaries and Other Earning.</u>**
This means the employees' total remuneration including basic salaries, allowances, bonuses, overtimes and any other benefit in kind or money recurred by employees in connection with contract of employment.

v. **<u>Pollution</u>**
Pollution involves the discharge of harmful waste product into air, land or water. Waste substances discharge into water is harmful to fish while such substances discharge on land kills crops. Pollution may take the form of excessive noise which disturbs the peace of the community. **(20 marks)**

b. **<u>Liability of Hotel Proprietor</u>**
At common law, hotel proprietor has a strict liability for the safety of his guest and their personnel effects. This is contains in the Hotel proprietor Act 1956. The Act does not impose a strict liability but imposes monetary limits of £50 for any one article of a guest lip to an aggregate if £100. These limits can only be relied upon if the hotel displays a statutory notice providing details of the Act in a conspicuous place in their premises. **(14 marks)**

<u>QUESTION 14</u>

a. Explain why prompt claim notification is important in Employers' Liability Insurance.

b. An employee sustained bodily injury in a factory accident. He was admitted in the hospital, treated, discharged and place on sick leave for four (4) weeks.
Thereafter, medical examination certified him fit to resume normal duties.
List relevant claims supporting document that will be required to process the claim. (10 marks)

c. Briefly explain the role of Arbitration in the settlement of liability claims. (9 marks)

<u>SOLUTIONS TO QUESTION 14</u>

a. **<u>Important of Prompt Claims Notification</u>**

- To comply with the notification condition on the policy
- It helps the insurer to conduct investigation when the matter is fresh and when eye witness account will be readily available.

- It enables the insurer to reserve for the claim and also notify their re-insurer or co-insurers accordingly.
- It enables quick processes and settlement of the claim. **(15 marks)**

b. **<u>Claim supporting Document for bodily Injury</u>**

- Completed claim form.
- Medical examination report
- Medical bill
- Exercise duty certificate
- Discharge certificate
- Employee pay slip **(10 marks)**

c. **<u>The Role of Arbitration</u>**

Arbitration is very important in the settlement of liability claims especially where there is dispute between the insured and the insurer in connection with the quantum of the claim.

Liability policies contains arbitration clause which requires dispute to be referred to arbitrator for settlement instead of legal proceeding. **(9 marks)**

CHARTERED INSURANCE INSTITUTE OF NIGERIA

ADVANCED DIPLOMA

OCTOBER 2015 EXAMINATION PAPER

SUBJECT A770

PRINCIPLES OF MARINE INSURANCE

Part I

Answer ALL questions in part I
Each question carries six (6) marks

QUESTION 1

a. **What is the full form of each of the following abbreviations?**
   i. **DWT**
   ii. **VLCC**
   iii. **GRT**

b. **In full Risk rating, how is 'ex-total loss' premium determined?**

SOLUTIONS TO QUESTION 1

i) Dead Weight Ton
ii) Very Large Crude Carrier
iii) Gross Register Tonnage

b. A figure in pound sterling or US dollars is multiplied by the deadweight tonnage of the vessel.

QUESTION 2

List any six facts that a broker must disclose to the underwriter when placing a Marine Cargo Insurance

SOLUTIONS TO QUESTION 2

Any six of the following:

- Name and address of the assured.
- Business
- Subject matter to be insured
- Type of packing

- If containerized, the type of shipment – LCL or FCL?
- Whether self- packed, or the name of the professional packers used. Value of the interest and sum to be insured.
- Voyage, including connections, land transits and/ or transshipment
- Storage if specially arising
- Name of vessel or shipping line to be used.
- If the vessel is to be chartered, the terms of the charter party, and
- Insurance conditions required.

QUESTION 3

State any six (6) of the major liabilities covered by a Protection and Indemnity Club.

SOLUTIONS TO QUESTION 3

Any six of the following:

- Cargo e.g. claims for short delivery, loss or damage to cargo.
- Crew e.g. medical expenses, repatriation, compensation for death or injury.
- Collision: to the extent such claims are not covered under hull policies.
- Fixed and floating objects e.g. damage to docks.
- Third party injury and death claims e.g. stevedores, passenger, etc.
- Oil pollution.
- Miscellaneous e.g. Fines, wreck removal etc.
- Costs and expenses of investigating and handling covered claims

QUESTION 4

What are Jack-up Units?

SOLUTIONS TO QUESTION 4

- Jack- up units are self- elevating platforms which can float freely with legs retracted by a jacking system for movements in tow.
- Sometimes the legs are shortened for stability in oceans tows.
- They may have three or more legs depending on the design.
- To operate, the rig is jacked up to provide sufficient air gap between the base of the platform and sea surface.
- Its successful use depends on the design, the nature of sea bed, the method of coping with penetration of the legs in soft or uneven bottom areas.
- Majority of its causalities occur during tows or whilst jacking up or down.
- It is used mainly in shallower waters of the world.

QUESTION 5

a. **What is the insurable interest of a direct insurer in the reinsurance he has effected?**

b. **What is a Retrocessionnaire?**

SOLUTIONS TO QUESTION 5

a.

- The liability of the direct insurer to pay claims to his various insured.
- He protects himself against the risk of his inability to meet his liability to pay claim in the event of large claims or accumulation of claims.

b.

- The reinsurer who accepts the risk ceded out by a reinsurer in order to protect himself, known as retrocession, is called retrocession are.
- Retrocession ire can also retrocede to another retrocessionire and the process can go on ad infinities.

QUESTION 6

a. **What is Non-proportional Reinsurance?**

b. **Mention three (3) types of Non-proportional treaties.**

SOLUTIONS TO QUESTION 6

a.

- It is a reinsurance which pays to the reinsured, losses up to an agreed limit when the reinsured has incurred a loss or losses above an agreed amount specified.
- The premium is usually a set percentage of the reinsured's premium or a float premium.

b. **Any three of the following:**

- Working (exposed) Excess of Loss.
- Catastrophe Excess of Loss
- Reporting Excess of Loss
- Aggregate Excess of Loss
- Stop Loss and
- Back- up contracts.

QUESTION 7

State any three (3) types of the duties of a Reinsurance Broker.

SOLUTIONS TO QUESTION 7

Any three of the following:

- Advising the reassured and constructing the reinsurance programme.
- Considering the potential reinsurance market with particular reference to security.
- The actual marketing of the business.
- The construction of the contract wording.
- Arbitrating in the event of problems or disputes.
- General administration including claims collection.

QUESTION 8

What are the main advantages of 'Alternative Risk Market' over the Traditional Reinsurance Market?

SOLUTIONS TO QUESTION 8

- Simplicity of handling, and
- The security is the "Financial Market" which has funds/ reserves many times greater than the reinsurance market.

Part II

Compulsory question

This question carries 50marks

QUESTION 9

a. **List the 'stages' of cargo transit analysis for the purpose of improving loss prevention.**

b. **How do the following types of losses occur?**

   i. **Pilferage**
   ii. **Spillage/Wastage**
   iii. **Deterioration**
   iv. **Disappearance**
   v. **Breakage.**

SOLUTIONS TO QUESTION 9

a.

- Preparation and packing at the outset.
- Loading
- Land transport (and groupage when applicable)
- Unloading, port storage and handling, export clearance.

- Loading on the carrying vessel or air craft.
- Carriage.
- Transshipment where applicable.
- Unloading, storage and handling, import clearance.
- Loading on next and final stages of transport.
- Arrival at destination, unloading and checking.

b.
- Inadequate port fencing
- Commodity easily identified, and
- Bags easily opened by port workers.

i)
- Bags split open when dropped

- Occasional hook damage
- Smooth plastic sacks caused top bags to slide off, fall and burst.
- Rain damage to contents of jute bags stored in the open whilst bottom sacks content are damaged by standing water.
- Bags opened for pilferage lead to further spillage, and

- Contents of split bags open to deterioration.

ii)
- Plastic sacks – occasional damage from high moisture content resulting from temperature changes during transit and storage, and
- Jute sacks – damage through high local humidity.

iii)
- Occasional theft of small consignments as a result of inadequate supervision by ship's crew during stowage and unloading.

- Goods discharged at wrong port etc.
- Chaotic stacking of discharged goods so consignment cannot be found.
- Markings obliterated by rain.

iv)
- Inadequate packing case.
- Suspected rough treatment by outward port.
- Poor handling and stowage by carrier, with considerable damage to cases and contents during storms, and
- Occasional accident during discharge.

Part III

Answer three (3) out of the following five (5) questions.
Each question carries 34 marks

QUESTION 10
What are the roles of the Reassured and the Reinsurer in Loss Settlement under a Proportional treaty?

SOLUTIONS TO QUESTION 10
- The reassured and the reinsurer are on the same footing both in coverage and claim settlement.
- The reassured however has full discretion in the investigation, compromise or settlement of claims.
- The reinsurer follows the fortune of the reassured and thus pays to the assured its proportional share of all settlement, compromises, possibly including ex gratia settlements by the reassured, all costs, expenses and other payments for which the reassured may become liable except office expenses and salaries of the reassured's staff.
- The reinsurer shall however participate proportionally in all refunds and/ or salvage recoveries received by the reassured.

QUESTION 11
a. **Under the Institute Time Clause-Hulls 1/11/95, how is the damage to a vessel through the fault of the Tug or pilot, who were engaged by the vessel, treated by the insurer of such vessels?**
b. **What is 'Salvage Charges'?**

SOLUTIONS TO QUESTION 11
a. The vessel's insurers are prepared to accept without prior agreement, the waiver or modification of their subrogation rights against the tug on the pilot.
b.
- Charges recoverable under maritime law by a salvor, independent of contract.
- They do not include the expenses of salvage rendered by the assured or their agents or person hired by them to avert a peril insured against.
- Such expenses are recoverable as particular charges or general average loss.

QUESTION 12
a. **What are the limitations to the 'All Risks' Cover provided by the Institute Cargo Clauses (A)?**
b. **Why is the York Antwerp Rules often stipulated in contracts of affreightment for the adjustment of General Average?**

SOLUTIONS TO QUESTION 12

a. It does not cover:

- Inherent vice
- Mere wear and tear
- British capture
- Loss which the insured brings about by his own act.

b. In the absence of any stipulation to the contrary in the contract of affreightment, the law governing the adjustment of general average is the law of the country of the port of destination or of the place where the voyage is broking up.

- Owing to the differences between the laws of various countries in respect of General Average, York Antwerp Rules are used to minimize such differences and protect cargo interests in both general average and salvage charges.

QUESTION 13

a. What are Classification Societies?

b. What is the importance of classification to insurers in Underwriting Risks and Settlement of Claims?

SOLUTIONS TO QUESTION 13

- They are organizations which supervise the construction of vessels or survey constructed vessels which are to be classed with them to ensure that they meet with the criteria laid down in the societies' rules for vessels carrying their classification notation.
- The societies appoint surveyors to survey parts of the hull and machinery in order to maintain a ship in the society it belongs.
- Classification surveyors also carry out damage surveys as well as maintenance surveys, sending reports to the society's head office and ship owners.

b. Underwriters are very willing to insure classed vessels, knowing that a high standard of maintenance will be achieved.

- Under writers always insist on the production of a certificate from a classification society that the vessel maintained its class with them, before settling any claim.

QUESTION 14

a. How does a Constructive Total Loss of Cargo arise, according to MIA 1906, S.60?

b. How does the insurer handle Constructive Total Loss Claim?

<u>SOLUTIONS TO QUESTION 14</u>

a. It arises when the assured is deprived of the possession of their goods and the cost of recovering the goods will exceed their value when recovered, and

- When the goods damaged, the cost of reconditioning and forwarding them to the destination will exceed the value on arrival.

b. The assured gives notice of intention to claim for constructive Total Loss.

- Where the insurer accepts such notice, he becomes entitled to all proprietary right and salvage.
- The insurer often rejects the notice but agrees to place the assured in the same position as if a writ had been issued on the same day.
- The underwriter pays the insured value to the assured, notwithstanding the CIF value or market value at destination.
- Where perils other than those insured against prevented the assured from forwarding the damaged cargo to the destination, there is no claim on underwriters.

CHARTERED INSURNACE INSTITUTE OF NIGERIA

ADVANCED DIPLOMA

OCTOBER 2015 EXAMINATION PAPER

SUBJECT A780
AVIATION INSURANCE

Part I
Answer ALL questions in part I
Each question carries six (6) marks

QUESTION 1
List six (6) functions of Lloyd's Signing Office.

SOLUTION TO QUESTION 1
Any six from the following:

i. Check and numbers transactions (including additional premiums etc)
ii. Sign or produce policies
iii. Provide a service to Lloyd's market for the operation of special schemes or facilities
iv. Develop improvements in quality and timelines in respect of insuring documentation for Lloyd's
v. Operate central accounting scheme
vi. Provide additional services derived from one activity – including reporting on insurance premium tax and terrorism premium.
vii. To provide advice and research on technical insurance matters, central accounting requirements – Lloyd's Policy Signing office procedures and statistical requirements.
viii. To provide the necessary statistical and taxation data for insurance legislators and taxation authorities world-wide.

QUESTION 2
List any six (6) of the contents of the Standard Slip.

SOLUTION TO QUESTION 2

i. Name of insured
ii. Period of Insurance
iii. Interest
iv. Sum insured
v. Conditions
vi. Territorial limits
vii. Deductibles
viii. Uses/pilots
ix. Premium/brokerage
x. Other information (which can be "not warranted")

QUESTION 3
Briefly explain the 'Deep Pocket Theory'.

SOLUTION TO QUESTION 3
Deep pocket theory is defined as "the person with the most funds available pays the most, irrespective of their share of liability". In products liability cases, there may be a manufacturer which is targeted, not because they are responsible but because they have the most funds to meet the claim. This encourages liability claims and eventually pushes up premium.

QUESTION 4
Explain briefly the 'Tort of Bad Faith'.

SOLUTION TO QUESTION 4
The tort of bad faith came about in the USA to try to encourage insurers to meet their obligations to settled/defended claims. It was felt that the insurance industry had a practice of denying claims or accepting settlement offers. If the courts found that Insurers should have acted differently, the insured was only entitled to have the obligation performed. This tort was introduced to remedy this and allows changes for economic loss and mental distress.

Punitive damages were also added on "proof of malice" later amended to conscious indifference.

Failure of the liability insurer to offer a fair settlement within policy limits would expose them to paying the entire claim if the final award were greater than the policy limits.

QUESTION 5

Explain the difference between AVN6A and AVN5A.

SOLUTION TO QUESTION 5

Notice the difference between this clause and AVN 5A. If an installment is missed, cancellation will not be automatic but notice of cancelation may be given via the appointed broker. Other interested parties (example: lessors of aircraft for example) are also given notice. Most aircraft financing agreements will contain provisions that they must have prior notice of cancellation or alterations of cover.

QUESTION 6

Outline the use and application of the '70/30 formula'.

SOLUTION TO QUESTION 6

70/30 Clause is used to allow insurers to load a premium to provide a premium on older aircraft which reflects the greater chance that any loss will be settled as a total loss.

To arrive at a more equitable premium the 70/30 Clause involves an additional payment at the rate of 30% of the difference between manufacturers' cost price and insured value Aviation Insurers estimate that 70% of Claims expenditure is on total losses.

Occasionally, rates of 75/25 or 80/20 could be used.

QUESTION 7

Describe the typical exclusions found in Aviation Hull Policies regarding Foreign Object Ingestion and Damage.

SOLUTION TO QUESTION 7

Damage to an aircraft engine caused by foreign objects ingestion that is attributed to a single incident recorded in the aircraft technical log is covered by aviation hull policies. Damage caused over a period of time, including progressive or cumulative damage, is excluded, but resultant damage to other parts of the aircraft would be covered. Mechanical breakdown would be excluded, but consequent damage to the aircraft would be covered.

QUESTION 8

a. **What is Loss of License Policy?**

b. **List four (4) exclusions found under a Personal accident Insurance Policy.**

SOLUTION TO QUESTION 8

a. This is a specialist class of business usually underwritten by a small number of companies and Lloyd's syndicates and sometimes forms part of a combined life, loss of licence and temporary total disability policy.

b.

- War and Civil war;
- Radioactive contamination;
- Hazardous occupations and pleasure pursuits;
- Air travel except as a passenger in a multi-engine aircraft operated by a licensed commercial air carrier.
- Attempted or actual suicide
- Intentional self-injury or injury arising through a state of insanity
- AIDS or AIDS-related complex.
- Deliberate exposure to exceptional danger.

Part III

Compulsory question.

This question carries 50 marks.

QUESTION 9

A prominent African Airline flying from Botwsana via Kenya to Lagos overshoots the runway on a scheduled stop at Lagos Terminal 1 Airport and breaks up, resulting in death or injury to many of the passengers.

(a) Describe the actions a Surveyor appointed by Insurers should take, up to final settlement of the Hull Claim.

(b) What rights and remedies that are available to the injured and to dependents of the deceased?

SOLUTION TO QUESTION 9

(a)

i. The surveyor must as soon as possible go to the scene of the accident and take photographs, including one clearly identifying the aircraft, if possible the Surveyor should examine the wreckage components by component to establish the components' serviceability and if they can be repaired. He must consider if components were airworthy at the time of the accident. If a part malfunctioned, there may be possibilities of subrogation.

ii. Having looked at the damage and taken into account the position of the aircraft, the surveyor must decide if the aircraft can be repaired.

As the aircraft crashed at a major airport, clearing the runway for use will also be a major concern.

iii. The surveyor will write a preliminary report containing the necessary details.

iv. In view of the aircraft breaking up, it is probable that the aircraft will be declared a total loss. Salvage offers would then need to be considered. If the aircraft were deemed repairable, the surveyor would need to keep insurers informed of any hidden damage as it comes to light. If repairs are made, the surveyor would be responsible for checking and ensuring only charges attributable to the loss are paid.

v. The surveyor would prepare an interim and then a final report, which should cover the following details.

   a. The identification of the aircraft involved in the accident
   b. The time, date and place of the accident
   c. Where and when the survey took place.
   d. The name, age and address of the pilots, their total experience with details of all the aircraft that they have flown.
   e. Full details as above of all other crew members
   f. Full details of the airframe together with the date of manufacture, total flying time since last overhaul and total permitted time between overhaul
   g. Full details of engine as above.
   h. Full details of the accident and written and signed statements from the members of the crew.
   i. Weather and other factors affecting the accident
   j. Details of the damage sustained by the aircraft, preferably with photographs, and photographs of the surrounding countryside
   k. The possible cause of the accident and the possibility of subrogation
   l. Recommendations concerning the time to repair, the requirement for stage payments, a calculation to show whether it would be more economical for the insurers to declare the aircraft a total loss and sell the salvage, and any reserve necessary for the insurers to set aside to pay the claim
   m. Any breach of regulations and the result of any investigations carried out by regulatory authority.
   n. Copies of any agreements likely to affect the repair of the aircraft or possible subrogation
   o. Details of ownership, including leases, liens or encumbrances.

(b) Remedies include:

The first point to consider is the nationality of the carrier and whether EU2027/97 would apply. It should be noted that even if the carrier was not Western European the provisions – could still apply.

Depending on the application of "2027" a distinction may need to be made between international carriage is not subject to the Warsaw convention and the hague protocol

If EU202/97 applied, the following is relevant:

i. There is no artificial ceiling on awards, unlike the Warsaw convention and Hague protocol.
ii. All defenses are waived for the first SDR100,000 (with exception of contributory negligence)
iii. There are requirements for advance payments
iv. There is a minimum payment in respect of death

If the Warsaw convention and Hague protocol apply, the following is relevant

i. Defenses
ii. Limits, and how they can be breached
iii. Jurisdiction
iv. The situation concerning any non-international carriage which was taking place.

The conventions impose strict liability but plaintiffs would have to go before courts to prove the degree of their loss. Jurisdiction is of significance. Possible headers that an award would be made under (economic/non-economic loss) should also be considered.

<u>Part III</u>

Answer THREE (3) out of the following five (5) questions.
Each question carries 34 marks.

<u>QUESTION 10</u>

Describe the extent of War Cover available in the London Aviation market.

<u>SOLUTION TO QUESTION 10</u>

Limited cover is available via AVN 51. This provides for the write back of paragraph (c), (e) and (g) of AVN 48B (strikes etc, malicious acts and hijacking). This clause provides for the completion of an aggregate limit. If there are two top values at risk insurers will frequently be prepared to negotiate on this and many risks have a higher limit and often no aggregate is applied at all insurers have the ability to issue seven days' notice to cancel this cover.

Cover is provided for losses arising from following

(a) War etc
(b) Strikes, riots or civil commotion
(c) Act of one or more persons for political or terrorist purposes
(d) A malicious act or an act of sabotage
(e) Confiscation and the like
(f) Hijacking

Market War Agreement (1982) and subsequent amendments affected the coverage provided by paragraph (a) Two are not specially mentioned in the wording. These are

- No hull may be covered until it has first been airborne
- Period may never exceed twelve months; extension up to 18months are allowed provided the twelve month limitation at any time is not broken.

Policy excludes the following

- War between the five major powers
- Confiscation by the government of registry of the aircraft
- Any debt (required for confiscation type cover)
- Repossession by any title holder or arising out of a contractual agreement
- Delay and loss of use
- Direct or indirect loss arising out of the detonation of any nuclear weapon

Policy contains the following cancellation

i. Insurers can give seven days' notice of amendment to premium or geographical limits
ii. Automatic review of terms or cancellation premium, geographical limits and condition. If the insured declines to accept, policy cancelled
iii. Cancellation by notice – seven days' notice by either party at the quarter dates
iv. Automatic termination – policy automatically cancelled if war breaks out between the major powers. Cover does remain in force for any aircraft airborne at the time until it first lands.

QUESTION 11

A pleasure flight in Nigeria crashes, killing some of the occupants and injuring the rest. Investigation showed that the plane was over loaded.

Discuss:

i. **The overloading of the plane; (5 marks)**
ii. **The scope and make-up of any award which may be made by the courts; (20 marks)**
iii. **The liability of the Insurers of the Aircraft operator. (9 marks)**

SOLUTION TO QUESTION 11

i. Although the aircraft is overloaded, the insurer is still liable as the insurance is a compulsory insurance however on the payment of the claim the insurer may sue the insured for a reclaim if they so want.

ii. In all likelihood, this flight was not international and would thus be subject to Nigeria law by Nigeria Civil Aviation Authority (NCAA) rather than strictly international conventions.
Nigerian law is based on English common law.
In fatal injury cases, the following may claim
   i. The remaining spouse
   ii. The children
   iii. The parents/grandparents/grandchildren.

Award to a widow would be on the basis of "the widow is entitled to an award of each amount as well assure her the comforts and station in life which she would have enjoyed but for the untimely death of her husband".
The award to a widow would be reduced by an amount to take into account
- Possibility of remarriage
- Possibility of widow's death prior to expiry of life expectancy.

For total permanent disability claims

Court may adopt following guidelines

- Compensation for pain suffering (including in the future)
- Loss of amenities of life
- Loss of life expectancy
- Loss of future earnings.

(iii) Insurers may be in a position to decline the claim because the plane was overweight and thus in breach of its airworthiness certificate. This will depend to a degree on who knew about the breach and the exact wording of the policy documentation.

QUESTION 12

Explain the key factors affecting the setting of a premium rate for Hull Insurances. Describe the methods of rating utilized.

SOLUTION TO QUESTION 12

The key objectives to set a rate that commensurate with risk will include an element of profit.
Insurers will be aware of level of compensation and capacity available. Deductible level will also have a bearing.

Some factors are unique to a particular type of operator, others are more generic

Factors include **large operator**

i. Type and value of aircraft
ii. Training infrastructure or organization which will be providing training
iii. Loss record
iv. Geographical operational scope.

Small operator include charter airlines

As above plus the following
How many different types of aircraft utilized?
Airfield used?

Industrial Aid Aircraft

Two major factors are:

i. Type of aircraft and
ii. Pilot experience. In addition, value of aircraft and loss record should be considered.

Flying Clubs factors include:

i. Type and value of aircraft
ii. Pilot experience
iii. Number of members
iv. Claims record of club
v. Location (geographical)
vi. Facilities
vii. Utilization
viii. Experience of Chief flying instructor
ix. Maintenance provider

Uses

Certain uses introduce greater level of risk i.e. crip spraying, or powerline petrol and should be rated accordingly.

Type of aircraft

Special rating consideration apply to certain types of aircraft, for example
Floatplanes can sink after even a slight damage

Helicopters are subject to high repair costs
Gliders can include home built (from kits), there is also the transit risk.

QUESTION 13

a. **Describe the role of the Reinsurance Market. (12 marks)**

b. **The role of the various types of Reinsurance available in respect of Aviation. (22 marks)**

SOLUTION TO QUESTION 13

Reinsurers play a crucial role in insurance by supporting direct underwriters by providing additional capacity. Another critical aspect is needed to spread the risk of loss.

Reinsurance can be undertaken in a number of ways

i. Facultative
ii. Excess of loss
iii. Quota share treaty (surplus lines)
iv. Stop loss

In all cases, reinsurers will "follow the fortunes" of the direct insurers.

Facultative reinsurance

This is "one off" specific insurance on a given risk or part of it. The reinsurers will state their premium terms which could well be as original and subject to overrider generally split between brokers and reinsuring underwriter.

Quota Share (Surplus lines)

The direct insurer will reinsure an agreed proportion of all risks in a defined class of business. This can be arranged on the basis of a fixed or variable monetary amount. The cessions to the treaty would be proportional to the direct insurers own writings and the reinsurer premium payment would be the same percentage of the net premium that equates to the cession.

This type of treaty is advantageous to a direct insurer as it allows them to write bigger lines on the original business.

Excess of Loss

This type protects a direct insurer for losses above an agreed retention for all amounts they are liable for arising out of one occurrence up to another specified amount.

Premium would either be a fixed amount or generally as amount adjustable at a percentage of the direct insurance overall net premium.

Purchase in layers (e.g. 25,000 excess 50,000/50,000 xs 75,000)

Stop Loss

Protects direct insurers from losses in excess of their net premium income. It protects against the aggregation of loss in any given class (other than from one occurrence in the case of excess of loss cover). Direct Insurer decides their retention (e.g. 120% of net premium income). It will protect direct insurer for amount above the retention up to another set percentage of the next premium income (e.g. 160%).

The premium will normally be a percentage of applicable net premium income.

QUESTION 14

Discuss the liability of Airport and its Insurers in each of the following cases:

a. **Theft of Cargo stored on the airport's premises.**

b. **An outbreak of food poisoning traced to the Airport's negligence which necessitates the closure of the airport for an extended period of time.**

c. **A serious fire which destroys Cargo and baggage in the Airport's custody and which necessitates the closure of the Airport for an extended period of time.**

SOLUTION TO QUESTION 14

a. Liability of the airport will depend to a large extent on whose care, custody and control the cargo was in.

   If airport responsible for security this will affect them if negligence were involved. Airport's position may well be altered by contractual provisions.

   There could be circumstances where responsibility could be apportioned and the share of the blame and financial costs would be apportioned.

   Generally speaking, this type of loss would not be covered if cargo were in the care, custody or control of the insured.

b. The airport's position would be dependent on
   i. Ownership of the restaurant or who is responsible for its operation.
   ii. Any contractual agreements that affect the position.

iii. What caused the problem: preparation, storage or actual foodstuff itself – other parties could be called in at least to contribute.
Insurers will be liable if the insured were found to be liable under the premises section.

Again, contractual position must be considered especially as the policy contains a blanket exclusion.

c. Liability of the insured would depend on

i. What or who caused the fire e.g. contractor
ii. Condition on the fire detection and sprinkler system and firefighting equipment.
iii. Contractual provisions
iv. Contractual factors

If goods were in care, custody of the insured, this would be excluded from coverage under the terms of the form. If they were not in other care, then cover could apply if fire was started by contractors, the policy would not respond unless insured had previously agreed to provide cover.

Coverage could also depend on any contractual provision and insurers may in certain circumstances look forward the condition precedent to liability contained within the wording.

CHARTERED INSURANCE INSTITUTE OF NIGERIA

ADVANCED DIPLOMA

OCTOBER 2015 EXAMINATION PAPER

SUBJECT A785
PRINCIPLES OF REINSURANCE

Part I
Answer ALL questions in part I

QUESTION 1

Within the reinsurance markets, there are various buyers and sellers of reinsurance services. Briefly list out the various buyers of reinsurance services/products.

SOLUTIONS TO QUESTION 1

Common buyers of reinsurance services/products are

i. Direct insurance companies
ii. Lloyd's Syndicates
iii. State Insurance Confiscations
iv. Captive Insurance Companies
v. Reinsurance Companies
vi. Reinsurance Pools

QUESTION 2

Explain the term Facultative Reinsurance. State the advantages and disadvantages of Facultative Reinsurance.

SOLUTIONS TO QUESTION 2

a. **Facultative Reinsurance**

Facultative reinsurance is a form of proportional reinsurance. It is an optional contract entered into between the insurer (called the cedant) and another (called the reinsurer) for the reinsurance of an individual risk. Both parties have a free choice as to whether to enter into the contract. Each risk which is the subject facultative reinsurance is considered individually with the original insurer determining whether they wish to place it as reinsurance and the reinsurer also freely determining whether they want to accept the risk.

The premium accrued to the original risk is shared in the same proportion as the risk was share. Usually there is a reinsurance commission charged by the cedant to compensation it for the administration expenses. Also claims incurred by the original insurer (cedant is recovered from the reinsurer in the proportion the risk and premium were ceded to them.

b. **Advantages of Facultative Reinsurance**

- Risks are considered individually. That means reinsurers can negotiate a suitable premium.
- Facultative reinsurance increases the insurers' competitive edge within its chosen market.
- There is freedom of office any risk by the reinsured which may be declared (by the reinsurance).
- An insurer's treaty reinsurance could be protected by facultative reinsurance of particular risks to ensure a better overall result and lower premiums in the long term.
- An insurer might benefit from the specific knowledge of facultative reinsurer with regard to the nature and potential of the risks,
- There is an opportunity for both parties to develop a successful professional relationship.

Disadvantages of Facultative Reinsurance

- Cedant cannot be certain of the placement as cession is not automatic
- Involves high administration cost
- There is freedom of office any risk by the reinsured which
- The cedant has to disclose full information facultative reinsurance of particular risks to ensure a better overall result and lower premiums in the long term.
- An insurer might benefit from the specific knowledge of facultative reinsurer with regard to the nature and potential of the risks,
- There is an opportunity for both parties to develop a successful professional relationship regarding its underwriting of the risk. This is dangerous for competition reason.
- Reinsured may loss control over the handling of the risk.

<u>QUESTION 3</u>

a. **What do you understand by the term Facultative Obligatory Reinsurance Treaty?**

b. **How is Facultative Obligatory Reinsurance different from Facultative Reinsurance?**

<u>SOLUTIONS TO QUESTION 3</u>

a. **<u>Facultative Obligation Reinsurance</u>**

Facultative obligation reinsurance is a facility cession. The details of the contract are concluded in advance in the form of a treaty but the insurer has the option whether to cede a risk to the treaty or not. The obligatory element rests with the reinsurer, who must accept the risk once ceded to the treaty.

b. Facultative Obligatory Reinsurance is different from facultative reinsurance in that facultative reinsurance does have any element of obligation in the offer and acceptance of the risk. Both parties have free choice to as to whether to cede the risk and to accept the risk.

<u>QUESTION 4</u>

a. **Distinguish between a Warranty and a Condition Precedent.**

b. **State the effects of their breach in a Contact of reinsurance.**

<u>SOLUTIONS TO QUESTION 4</u>

a. A warranty is a contractual promise by a reinsured either as to an existing state of affairs or as to the things that the reinsured will do in the future.

If the reinsured breaches a warranty the reinsurer is discharged from liability from the date of the breach.

Thus, if there is breach as to an existing state of affairs, the other party is discharged from inception. However, if a breach relates to a warranty as to future conduct, the contract is discharged from the time the breach occurs. E.g., a breach of premium payment warranty within 90 days will terminate the contract after 90 days.

On the other hand a condition precedent is a contractual term which must either be performed in order to bring into force a valid policy or more usually, to make the reinsurer liable under the policy. Example, when it is a condition precedent for liability that the reinsured notifies a reinsurer of a claim within 14 days of the occurrence failure to give notice as stipulated would render the reinsurer not liable to pay the claim. However, subsequent claims where project notice are given would still be payable.

b. The effect of a breach of a warranty means that the contract is void ab nitio while that of condition is at the mercy of the reinsurer.

QUESTION 5

a. What is the effect of an 'Event Limit' in a Risk Excess of Loss Reinsurance Programme.

b. ABC Insurance Plc has a property Risk excess of Loss Treaty of 2,000,000 Xs N500,000 with an event limit of N6,000,000. If four houses are damaged by a storm and each loss is above the N2,500,000 total insured limit. Apportion the claim between the reinsured and the reinsurer.

SOLUTIONS TO QUESTION 5

a. **Event Limit**

One problem that reinsurers experience with risk excess of loss reinsurance is that possibility the insurers could claim more than once for the same loss event. The reinsurance market in order to prevent this incorporates event limits clause. Thus preventing the reinsurer from been called upon to pay an aggregate claim amounting to several times the reinsurance cover due to a series of individual risk being involved in losses caused by on event.

b.

Risk XL Treaty	– ₦2.0m x ₦500,000
Event Limit	– ₦6,000,000
Four losses all above	– ₦2,500,000

NOW

Total Gross Claims - ₦2.5m x 4	= ₦10,000,000
Reinsure's Retention - ₦500,000 x 4	= ₦2,000,000
Risk XL Liability – ₦2.0m x 4	= ₦8,000,000

The Reinsurer's Liability has exceeded the Event limit of ₦6,000,000. Therefore the apportionment if the loss would be as follows:

Reinsured's Retention	-	₦2,000,000
Risk XL Max Liability	-	₦6,000,000
Reinsured bears the remaining	-	₦2,000,000
		₦10,000,000

<u>QUESTION 6</u>

Distinguish between the terms 'Deposit Premium' and 'Minimum Deposit Premium' as used in Excess of Loss Reinsurance Treaties.

<u>SOLUTIONS TO QUESTION 6</u>

Deposit Premium:- this is an agreed amount of money paid by the insurer under a non-proportional reinsurance when the contract is agreed.

When an excess of Loss Reinsurance provides for Deposit Premium, it means that when the actual reinsurance premium is computed at the end of the treaty year, the difference will either results in a return premium to reinsurance or additional premium to the reinsurer.

On the other hand, where the treaty provides to minimum and deposit (M&D) premium, the cedant will not receive any premium required even if the actual premium is lower than the M & D paid. However, if the actual premium computed at the end of the treaty year is greats than the M & D paid, the insured will pay the difference as additional premium to the reinsurer.

<u>QUESTION 7</u>

Give reasons why an insurer or reinsurer might want a rating agency to give an opinion in respect of its financial strength. List examples of rating agencies commonly used for Insurance Institutions financing rating.

<u>SOLUTIONS TO QUESTION 7</u>

The basic reason for rating insurance institutions is to assess and monitor the financial strength and claims paying ability of the institution at any given period of time. Good financial ratings give brokers and customers the confidence and assurance in placing their risks with the insurance institution. Any country's regulatory authority is also interest in the financial ratings of the reinsurance's companies that are expected to participate in the provision of reinsurance securities for the local market in certain classes of risks.

Rating Agencies commonly used for rating Insurance Institutions are:

i. A & M Best Rating Agency
ii. Standard and Poor's Rating Service
iii. Global Credit Rating C.
iv. Augusto & Co
v. Moodays Investors Services
vi. Fitch IBCA, DUFF & Phelps Rating Agency
vii AIO

QUESTION 8

a. **What is Profit Commission in Reinsurance?**

b. **State the items usually found in the Income and Outgo sides of a typical Profit Commission Statement.**

SOLUTIONS TO QUESTION 8

a. **Profit Commission in Reinsurance**

Profit Commission is an additional commission the reinsurer offers to the cedant to encourage the cedant to write profitable accounts or risks to which are ceded to the treaty. This is payable in addition to normal reinsurance commission.

The items usually found in a typical profit commission statement are follows:

Income = Premium included in the account for the year.
+ unearned premium reserves of the end of preceding year.
+ o/s loses reserves at the end of preceding year.

Outgo = Losses & Loss expense ceded during the year.
+ Commission paid during the year.
+ Any other deduction Range
+ Unearned Premium reserves at the end of current year.
+ o/s loss reserves at the end of current year.
+ Allowance for reinsurers expense (usually 5-10%) of the premium ceded.

The agreed Profit Commission rate of say 15% - 25% is then applied on the treaty results pay above computations to produce the profit commission payable.

Part II

Compulsory question

This question carries 50 marks

QUESTION 9

a. **What is Deductible?**

b. **Excess Insurance Co. Ltd has a maximum of N5,000,000 sum insured per risk and a 12-line surplus treaty. The retention is further protected by a per risk Excess of Loss treaty for N4,000,000 Xs N1,000,000**

The company underwrites a fire with a sum of N80 million and retains N4,000,000. Excess also intends to purchase a Facultative reinsurance to protect the proportion not ceded to the treaty.

i. **Compute the overall capacity of Excess Insurance Company under the Surplus Treaty Programme.**

ii. **Apportion the fire risk sum insured between the Stakeholders.**

iii. **If a loss of N40 million occurs due to fire accident to the factory, apportion the loss.**

iv. **Calculate Cedant's (Excess Ins. Co. Ltd) Net retained liability on this claim.**

c. **What factors influence the decision of a director insurer in choosing a reinsurer for its reinsurance programme?**

<u>SOLUTIONS TO QUESTION 9</u>

a. A deductible is a monetary amount that the insurer is expected to bear in the event of a loss under an Excess of Loss Reinsurance.

E.g. ₦10,000,000 Xs ₦5,000,000

This means if a loss event affects the treaty limit the reinsured will bear up to the deductible amount of ₦5,000,000 before the reinsurer is called upon to pay the amount over and above ₦5,000,000.

b. Excess Insurance Company Limited

<u>Given:</u>

Maximum Retention per Risk	-	₦5,000,000
Treaty Capacity	-	12 line surplus
Risk XL	-	₦4,000,000Xs₦1,000,000
Risk Sum Insured	=	₦80,000,000
Retention	=	₦4,000,000

i. Overall capacity of Excess Insurance Company Limited maximum Retention + Treaty Capacity.

₦5,000,000 + (5,000,000 x 12lines)

₦5,000,000 + ₦60,000,000

= ₦65,000,000

ii. Apportionment of Fire Risk Sum Insured.

Retention	-	₦4,000,000	5%
Treaty Surplus	-	₦4,000,000 x 12lines	

	=	₦48,000,000	60%
Facultative	=	₦28,000,000	35%
		₦80,000,000	100%

iii. Loss Apportionment

Loss Amount	-	₦4,000,000		
Retained Loss	-	5% x 40,000,000	=	₦2,000,000
Treaty Liability	-	60% x 40,000,000	=	₦24,000,000
Facultative Reinsurance	-	35% x 40,000,000	=	₦14,000,000
		100%		**₦40,000,000**

iv. As the cedant had purchased a Risk Excess of Loss treaty of ₦4,000,000 Xs ₦1,000,000, its Net Retained liability under this claim will be as follows:

Gross Retained Loss	-	₦2,000,000
:. Net Retained Loss	=	₦1,000,000 X ₦1,000,000
	=	**₦1,000,000**

Factors to be considered in choosing a reinsurer include but not limited to the following:

- Business philosophy of the reinsurer
- Easy Communication with decision males
- Type of reinsurance required
- Business acceptance policy of the reinsurer
- Standard of security required
- Authorization of the reinsurer for the type of business
- Strength of the reinsurer's balance sheet and solvency margin
- Reputation of the reinsurer
- Reinsurer experience and the quality of its management.
- Reinsurer's Underwriting policy
- Retrocession policy of the reinsurer
- Financial strength rating of the Reinsurer
- Ownership structure of the reinsurer

Part III

Answer THREE (3) out of the following FIVE (5) questions.
Each question carries 34 marks.

<u>QUESTION 10</u>

a. What are binding authorities?

b. What are the basic duties of a Broker?

c. How would you differentiate between Binding authorities and URe slips

<u>SOLUTIONS TO QUESTION 10</u>

a. **<u>Binding Authorities</u>**

It is common for reinsurance brokers to obtain reinsurance covers enabling them to place reinsurance on behalf of their clients with certain reinsurers. The broker accepts risk on behalf of the reinsurance companies participating in the cover for which they receive a commission. The participating reinsurer is obliged to accept all risks falling within the scope of the cover, while the broker has no obligation to place any particular risk under the cover as the contract gives the broker the authority to bind reinsurers in respect of certain types of risk.

b. **<u>Duties of Reinsurance Brokers</u>**

The duties of a reinsurance broker include but not limited to the following.

i. Advise its client on their reinsurance needs and risk management.

ii. Advise its client on their current accounting position with their reinsurer.

iii. Inform the reinsurers of any large losses that may impact on the relationship between them and the insurer.

iv. Collect and pass on any claims that may fall due to settlement

v. Pay any premium that may fall due promptly.

vi. Advice regarding the preparation of reinsurance contract wordings.

vii. Educate and train cedant's reinsurance staff on the aspects of their job functions.

c. The origin and basis of URe slips is basically similar to Binding Authorities. The main difference is that the broker does not have the authority to accept risks on behalf of participating reinsurers. Rather the broker must submit risks to the leading reinsurer who decides whether or not the risk is acceptable. Subject to the agreement of the lead reinsurer, all other reinsurers are obliged to accept risk placed under the facility.

The reinsurers who must follow have the assurance that the skilled leaders have seen the risks before they are placed in the facility.

The advantage is that, a reinsurer with small capacity in a particular field is given an opportunity to participate on the risks that they may not have been interested by the broker.

QUESTION 11

Consider a company with a Fire Surplus Treaty details are as follows:

Retention	**-**	**N25,000,000**
Treaty Capacity	**-**	**20 Lines**
Reinsurance Commission	**-**	**37.5%**
Accounts	**-**	**Quarterly**
Panel of Reinsurers	**-**	**Continental Re - 30%**
		African Re - 25%
		Nigeria Re - 25%
		WAICA Re - 20%
		100%

At the close of business on 30th September 2015 the company generated the following statistics:

Months	**Premium 1st Surplus**	**Losses Paid 1st Surplus**
July 2015	**16,540,200**	**4,800,100**
August 2015	**12,800,500**	**3,900,000**
September 2015	**18,200,000**	**5,000,000**
Total	**47,540,700**	**13,700,100**

(a) **Using the statistics above, prepare the 3rd quarter 2015 quarterly Treaty statement and show the balances due to reinsurers.**

(b) **Upon review of the Treaty programme the company is worried about maintaining a high retention of N25,000,000 per risk. Discuss the options you would recommend to reduce the retention by 50%**

SOLUTIONS TO QUESTION 11

a. Fine surplus treaty statement of Account for 3rd October. 2015

	Dr N	Cr N
Premium ledged		47,540,700
Commission 37.5%	17,827,763	
Losses Paid	13,700,100	
Balance	16,012,837	
	47,540,700	47,540,700

Apportionment of Balance		₦
Continental Re	30%	4,803,851
Angland Re	25%	4,003,209

Nigeria Re	25%	4,003,209
WAICA Re	20%	3,202,568
	100%	16,012,837

b. Upon review of the treaty programme the company is worried about keeping a relation as high as N25, 000,000 per risk

One option of reducing the relations by at least 50% is to percentage an additional working excess of loss reinsurance to provide protection for the company is retention in the event of a loss on an individual original policy which is greater than the monetary limit the company wou~~ld co~~mfortably retain for its own account.

In the particular case, the company can purchase a Risk Excess of loss layered a follows.
₦12,500,000 xs ₦12,500,000 their arrangement will limit the company to a loss exposure of ₦12,500,000 any one loss.

QUESTION 12

Write short notes on the following:

i. Alternative Dispute Resolution
ii. Implied Terms
iii. Ultimate Net Loss Clause
iv. Retrocession Market
v. Reinsurance Brokers
vi. Sliding Scale Commission.

SOLUTIONS TO QUESTION 12

i. Alternative Dispute Resolution - this is one aspect of dispute resolution which is attracting increased interest, not only among those who are involved as parties in disputes but also among the judiciary.

It defers from formal dispute resolutions procedures in that there is no judge or Arbitrator. The parties themselves arrive at a solution or accommodation. This however may not always reflect the true legal standings of the parties, but will be a solution that all parties can accept.

These are several forms of ADR Namely
- Negotiation
- Mediation

- Conciliation
- Expert evaluation\Early neutral evaluation
- Mini-trial or Executive Hearing

ii. **Implied Terms**

When a dispute arises regarding the terms of a reinsurance contract especially before the wordings have been agreed, one or both parties to the contract may ask the court or Arbitration panel to imply terms into the contract.

A Term will be implied of it is shown that

- It is necessary to give efficacy to the contract
- It is consistent with the express terms of the contract
- It would have been agreed to by both parties to the contract.
- It is universally accepted in a particular trade, business or market.

iii. **Ultimate Net Loss Clause**

The ultimate Net loss is the amount of ceding company's loss which is eligible for recovery under the terms of the treaty.

The purpose of the clause is to define the parameter of calculating the ultimate Net loss. Example UNL shall mean the sum actually paid by the reinsures in respect of any loss occurrence including expenses of litigation it any and all other loss expenses excluding office expenses and salaries, but salvages and recoveries including recoveries from all reinsurances and retrocession, other than underlying reinsurance provided for herein, shall be first deducted from such losses to arrive at the amount of liability.

iv. **Retrocession Market**

A retrocession is a Reinsurance of reinsurance. Reinsures, like direct insures do have need to seek protection for the risk they have accepted. Any risk or part there of that falls outside their own retention level, either by valve or class or type of cover are considered for passing on to other reinsures. This arrangement is called retrocession and the security providers is the case are called Retrocessionaire

v. **Reinsurance Broker**

A reinsurance broker is an intermediary between the reinsured and the reinsurer in a reinsurance contract.

The position of a reinsurance broker is such that he could be regarded as the agent of the reinsured as in where he negotiates and places risk on behalf of the reinsured. These are however, other situation where a reinsurance broker may be regarded as acting for the reinsurer as in when a broker is granted an authority to except business on behalf of the reinsurer.

vi. **Sliding Scale Commission**

The sliding scale commission is also one method of rewarding a reinsured for good treaty result. However, unlike other commissions, the sliding scale commission method also imposes a penalty on the reinsured for a bad loss experience. The practice in the method is for the treaty to provide for a provisional commission and when the actual loss ratio is calculated based on agreed formula, the commission is then adjusted according to the loss ratio for the treaty. Sometime, losses may be carried forward for many years.

QUESTION 13

a. Explain the term Enterprise Risk Management.

b. List the typical Material risks which an Insurer or reinsurer may be exposed.

SOLUTIONS TO QUESTION 13

a. Enterprises Risk Management (ERM) is defined by the committee of sponsoring Organization of the tread way commission (COSO) as a process, effected by an entity's board of directors, management and other personnel, applied in strategy-setting and across the enterprise, designed to identify potential events that may affect the entity and manage risk to be within its risk appetite, to provide reasonable assurance regarding the achievement of entity objectives.

The process risk management includes the following

- Risk Identification
- Risk Assessment and control
- Risk Monitoring and Reporting

b. The typical material risk which an insurer or reinsurer may be exposed.

- Market Risk
- Credit Risk
- Operational Risk
- Liquidity Risk
- Reinsurance Risk
- Underwriting Risk
- Provisioning\Reserving Risk
- Claim Management Risk

- Business Risk
- Reputation Risk
- Legal Risk.

QUESTION 14

a. What does a Special Cancellation clause allow for and why?

b. What is the importance of a reinsured establishing correct reserve?

SOLUTIONS TO QUESTION 14

a. This will allow the reinsurance agreement to be immediately terminated by either party because of a major alteration to the character of either party and hence to the reinsurance agreement or to the commercial and/or political background against which the reinsurance agreement was originally concluded.

b. The importance could be summed up as:

- The claims reserves are entered in the annual accounts
- The claims reserves serve for estimating the results in the current premium rates
- The claims reserves are required in order to determine correct premium rates
- The claims reserves provide a signal to the underwriting department should rehabilitation measures be required.
- The claims reserves affect the effect the experience of the reinsurance treaties
- The claims reserves may have very annoying fiscal consequences should they be falsely estimated or established at the wrong level

CHARTERED INSURANCE INSTITUTE OF NIGERIA

ADVANCED DIPLOMA

OCTOBER 2015 EXAMINATION PAPER

SUBJECT A825
APPLICATIONS OF REINSURANCE

Part I
Answer ALL questions in part I

QUESTION 1
What is Ex-Gratia Payment?

SOLUTIONS TO QUESTION 1
Payment made as a favour and essentially implies that the loss falls outside the terms and conditions of the policy contract.

QUESTION 2
What are the three main ways of collecting claims data?

SOLUTIONS TO QUESTION 2
- Losses occurring basis
- Claims made basis
- Risk incepting basis

QUESTION 3
How can the profitability of a treaty be expressed?

SOLUTIONS TO QUESTION 3
- Ratio of management expenses and other costs to ceded written premium
- Ratio of gross ceded premium to net ceded or written premium
- Ratio of Commissions and other costs to ceded or written premium
- Ratio of net(or gross) claims incurred to earned premiums

QUESTION 4
Discuss the determinant factors considered by Underwriters when assessing a Non-Proportional Liability Treaty.

SOLUTIONS TO QUESTION 4

- Required capacity of the treaty
- Claims experience and reserving
- Premiums and price
- Other terms and Conditions

QUESTION 5

Discuss the key factors that affect reserving on claims process.

SOLUTIONS TO QUESTION 5

- Inflation
- Exchange rates
- Data Quality
- Litigation
- Legislation

QUESTION 6

a. What is Over-riding Commission?

b. Define Original Gross Rate (OGR)

SOLUTIONS TO QUESTION6

Overriding Commission is money paid by the reinsurers to the reinsured in order to cover the reinsured's administrative costs incurred by the reinsured in ceding the business to the reinsurers.

Amount granted is dependent on profitability of the treaty account and the management expenses of the reinsured. OGR is the rate of premium applied under the original business to the sum Insured.

The result of the original gross rate times the sum insured equals the original gross premium. No deductions are made for commissions or brokerage

QUESTION 7

What might a new Insurance company put its entire capital base at risk in the first years of its operation?

SOLUTIONS TO QUESTION7

A new Insurance company might put its entire capital base at risk in its first year of operation because commercial pressure may require it to offer a larger capacity than normal or to apply competitive premium levels though lack of reserves and high expenses offer no financial cushions

QUESTION 8

Discuss the various forms of Non-proportional Reinsurance Programmes.

SOLUTIONS TO QUESTION8

1 Working Excess of Loss or risk Excess
2 Catastrophe Excess of Loss
3 Stop Loss and Aggregate Excess of Loss

Part II

Compulsory question.
This question carries 50 marks.

QUESTION 9

ABC Insurance Co. Ltd has a maximum fire retention of N500,000 with a 12 line surplus treaty cover. Meanwhile the retention is protected by a per risk Excess of Loss treaty for N400,000 excess of N100,000.
A risk of N8,000,000 was written by the Reinsured while it retains N400,000 and buys additional pro rata Faculataive reinsurance for the proportion of the risk that cannot be ceded to the treaty.

i. **Show by way of calculation how the risk would be allocated among the Reinsured, the Treaty Reinsurer as well as Facultative reinsurers.**
ii. **If there was a loss of N5,000,000 how would the loss be apportioned?**
iii. **Show the allocation if the protection in excess of loss basis for the common account of the reinsured and the reinsurers.**

SOLUTIONS TO QUESTION 9

(i)

	Amount	**%**
Retention	400,000	5%
Surplus Treaty	4,800,000 (12 lines)	60%
Facultative Reinsurance	2,800,000	35%

ii. A loss of #5,000,000 would be allocated in the same proportion as follows:

Retained Loss	5% of 5,000,000	=	250,000
Surplus Treaty Loss:	60% of 5,000,00	=	3,000,000
Facultative Loss 3	5% of 5,000,000	=	1,750,000

Meanwhile, since ABC Insurance company has protected its retention, the 'per risk' excess of loss treaty would pay #100,000 being the amount in excess of its deductible of

iii

Original sum Insured	#8,000,000	
Retention	400,000	5%
Surplus treaty	4,800,000	60%
Total Treaty Liability	5,200,000	
Facultative Reinsurers	2,800,000 in Excess of 5,200,000	

Loss: the loss of N5,000,000 is below the deductible of facultative reinsurance (5,200,000) hence there is no recovery from the local facultative reinsurers. Thus the loss would be allocated between the reinsured and the treaty reinsurers thus:

Total Loss amount		5,000,000	
Gross retained Loss	5%	=1/13 =	384,615.38
Treaty Reinsurers	60%	= 12/13 =	4,615,384.62

Reinsured	100,000
Excess of Loss reinsurers	284,615.38

Part III

Answer three (3) out of the following five (5) questions.
Each question carries 34 marks.

QUESTION 10

List and describe three (3) types of proportional reinsurance treaties available as well as features that differentiate one from the other.

SOLUTIONS TO QUESTION 10

a. Quota Share
Surplus
Facultative obligatory

b. **Quota Share**

Every business is shared in agreed percentage or ratio
There is usually a defined upper limit ratio 60:40 subject to say N10million
The premium, claim and expenses are shared in predetermined proportion
Commission rate is higher

Surplus

The reinsured takes a retention which forms a line whilst the reinsurer grants capacity which is multiple of that line

The risk, premium and claims are proportionately shared between the reinsured and the reinsurers. It provides a larger capacity

Facultative Obligatory Treaty

Not compulsory for cedant to cede but when ceded, the reinsurer is under compulsion to accept in as much as it falls within the stated terms and conditions of the reinsurance contract

It operates like other types of proportional treaties in the sharing of premiums, claims and other expenses.

<u>QUESTION11</u>

a. **Discuss the underlying factors that should be considered by an Insurer in fixing his retention limits.**
b. **Discuss five (5) environmental factors that affect insurers loss ratio in any year which must be considered by fixing retentions.**

<u>SOLUTIONS TO QUESTION11</u>

(i)

a. Size and nature of the portfolio, premium income and profitability
b. Assets, Capital, free reserves and Solvency
c. type of risks and pattern of losses

(ii)

- Inflation
- Recession
- Competition
- Changes in employment levels
- Certain technological developments
- Increase in court awards
- Increase in life expectancy

QUESTION12

Distinguish between Underwriting Year Basis and Clean Cut or 'Year of Accounts Basis of Reinsurance' accounting on proportional treaties.

SOLUTIONS TO QUESTION 12

Underwriting year basis:

year of origin of the cession of the risk is of paramount importance whatever year the claim arises, time claim is closed to the year in which risk was ceded to the treaty inception date of the original policy is used in accommodating claims that fall under that year as separate statement of account is prepared for each underwriting year

Year Of Account "Clean Cut basis':

Premiums, Commissions, expenses and Losses are accounted for in the year irrespective of year of origin of the cession

Irrespective of year of origin of the loss

Allowance is made for unearned premium and outstanding losses

QUESTION13

Discuss three (3) of the following:

i. **Interlocking Clause**
ii. **Co-reinsurance Clause**
iii. **Hours Clause**
iv. **Event Limit**
v. **Two risk warranty**
vi. **Applicable law clause**

SOLUTIONS TO QUESTION 13

Interlocking Clauses: if a loss falls under policies that relates/ incepts in two different years, the cedant is not penalized nor benefits from having to run two deductibles or two limits. A loss is prorated over the involved policies

Co-Reinsurance Clause: The reinsured bears a fixed percentage say 5% of all losses; it encourages prudent underwriting; Catastrophe reinsurance contracts often contains co- reinsurance clause

Hours Clause: Used on catastrophe loss cases; the treaty covers all damage arising from the same insured event within a specified number of hours; Also applies to property treaties where weather perils can affect property over hundreds of square kilometers and last several days; commencement of hours is chosen by the reinsured, varies from perils to perils; there might be more than one treaty claim arising out of an event but periods of cover by hours clause must not overlap

Event Limit: Reinsurers liability is restricted to a specific sum e.g., four total losses under the treaty arising out of a particular event e.g., storm/hurricane

Two Risk Warranty: More than one risk has to be damaged by the insured peril before catastrophe treaty cover would operate.
The Reinsured would ensure that deductible for the event cover is not less than double under a 'per risk' /working treaty

Applicable Law Clause: If there is no clear jurisdiction most suitable to place the contract, the local jurisdiction is most appropriate and should apply but not the subject matter of reinsurance contract which is governed by the acts in force clause

QUESTION14

a. **What is sliding scale commission? Show the variables that are considered in calculating sliding scale commission,**
b. **What is Profit Commission and show what factors constitute Income and outgoing in calculating Profit Commission?**

SOLUTIONS TO QUESTION 14

A.
Sliding scale commission is a form of Commission granted to the reinsured under a proportional treaty
It automatically rewards the reinsured for a good result but also penalizes it for a bad loss result
The reinsurer is debited with a provisional commission usually agreed at the minimum rate. At the end of the year the commission is adjusted given the loss ratio for that year.

Formula:

$$\frac{\text{Incurred Losses for the year}}{\text{Earned premiums for the year}} \times 100$$

Variables:
Incurred Losses = losses paid plus expenses by the reinsurer in the year
Add: Outstanding Losses reserve at the end of the current year
Less: Outstanding Losses reserve at the end of previous year

Earned Premium:= Premium for the current year.
Add: Unearned premium reserve at the end of the preceding y,
Less: Unearned premium reserve at the end of the current year

B. Profit Commission:

It is an additional profit Commission granted the reinsured for writing a profitable account

Income = premiums included in the account for the year
+ unearned premium reserve at the end of the preceding year
+ outstanding loss reserve at the end of the preceding year

Outgo = losses plus expense paid by the reinsurer during the year
+ commission included in the year
+ unearned premium reserve at the end of the current year
+ outstanding loss reserve at the end of the current year
+ Management expenses incurred by reinsurers

CHARTTERED INSURNACE INSTITUTE OF NIGERIA

ADVANCED DIPLOMA

OCTOBER 2015 EXAMINATION PAPER

SUBJECT A935
MANAGEMENT

Answer ALL questions in part I
Each question carries six (6) marks)

QUESTION 1
Itemise four (4) likely obstacles to Global Trade.

SOLUTIONS TO QUESTION 1

Obstacles to Global Trade are:
- State Intervention
- Poor transportation
- Poor communication
- Non- standardization of business practices laws, tariffs etc.
- Lack of respect for rule of law.
- Currency and exchange rate risk **(6 marks)**

QUESTION 2
A business is made up of three (3) main components; one of which is 'material resources'. What is Material Resources?

SOLUTIONS TO QUESTION 2

Material resources refer to all physical resources such as **plant**, **equipment**, **office space**, vehicles that are at the disposal of the business and can be used to help it achieve its objectives. **(6 marks)**

QUESTION 3
Identify four (4) characteristics of a Successful Project.

SOLUTIONS TO QUESTION 3

A successful project one which:

- Achieves stated objectives
- Is delivered on time
- Within budget
- Performs to agreed specifications
- Meets predefined success criteria
- Satisfied the sponsor and beneficiaries **(6 marks)**

QUESTION 4

The external environment of business can be divided onto four (4) main sub-environment acronym STEP. What is the full meaning of STEP?

SOLUTIONS TO QUESTION 4

- S Social
- T Technological
- E Economic
- P Political 1 ½ x 4 **(6 marks)**

QUESTION 5

Define Fixed Cost, Variable Cost and Sunk Cost, giving an example of each.

SOLUTIONS TO QUESTION 5

- **Fixed Cost -** Costs that do not vary with the organizations output e.g. office rent
- **Variable Cost -** Costs that vary with the organization's output e.g. Manpower.
- **Sunk Cost -** Costs that have no bearing on whether or not the organization should continue to provide its services. e.g. Irrelevant costs/ Past costs.

2 x 3 **(6 marks)**

.

QUESTION 6

In order to ensure that Benchmarking is successful, certain essentials have to met. Identify three (3) of these essentials.

SOLUTIONS TO QUESTION 6

Essential of Benchmarking

- Comprehensive and accurate information is available on comparison industries.
- They are based on industry best practice
- They are flexible and can be altered it the external environment charges.
- They relate to company's corporate strategy and plan
- These are sound internal audit process in place. 2 x 3**(6 marks)**

QUESTION 7

What is Total Quality Management (TQM)?

SOLUTIONS TO QUESTION 7

TQM is a strategic approach to quality which permeates the entire organization. It encompasses the notion of continuous improvement.

TQM is a quality plan which offers a structured disciplined approach to quality within the organization. **(6 marks)**

QUESTION 8

Balanced Scorecard is an approach that looks at the activities of a business from four (4) perspectives. What are these perspectives?

SOLUTIONS TO QUESTION 8

Balanced scorecard 4 perspectives

- Financial perspectives
- Internal perspectives
- Customer Perspectives
- Learning and Growth 1½ x 4 **(6 marks)**

Part II

Answer four (4) out of the following six (6) questions.

Each question carries 38 marks.

QUESTION 9

Organizational Structures can range between two extreme types viz Mechanistic and Organic.

Based on the above you are required to:

a. **State three (3) elements of a Mechanistic Structure.** **(15 marks)**

b. **State three (3) elements of an Organic Structure.** **(15 marks)**

c. **Explain the functional structure in an organization.** **(8 marks)**

<u>SOLUTIONS TO QUESTION 9</u>

Mechanistic Structure:

- Clear job demarcation and division of labour
- infrequent delegation of authority
- department with great uniformity of work activities
- Narrow spam of individual control **(15 marks)**

Organic Structure:

- Low job specification and more multi- skilling
- Greater delegation of authority to employees
- Low uniformity among employees in work units
- Wide spa or individual control **(15 marks)**

Functional Structure:

- Created according to specification of jobs
- Employees perform aspects of the same functions
- Suited to single product or service firms **(8 marks)**

<u>QUESTION 10</u>

a. **Explain the term Corporate Culture.** **(5 marks)**

b. **What are the three (3) components of Corporate Culture?** **(15 marks)**

c. **Discuss five (5) dangers of a Bureaucratic Culture.** **(18 marks)**

<u>SOLUTIONS TO QUESTION 10</u>

a. "The way we do things here" **(5 marks)**

b. **<u>Norms</u>**

The behavior which is most acceptable to the organization e.g. approaches to problem solving, time keeping, dress code etc.

Briefs and Values e.g. "We stand for quality". "Timely delivery is our watchword" etc.

Management Style: e.g.
Open door policy, hierarchical, patermistic, democratic etc. **(15 marks)**

c.

- The individual employee becomes "a little cod in a big machine"
- There is a sense within employees that personal liberty has been lost.
- It is difficult for employees' experience to grow
- It is harder for the organization to adapt to change
- There is over- conformity and obeying rules become the goal **(18 marks)**

QUESTION 11

Stakeholders have different types of interests and expectations in a business.

a. Identify five (5) examples of Stakeholders to a business. (10 marks)

b. Discuss the responsibilities of the business to any five (5) of the identified stakeholders. (28 marks)

SOLUTIONS TO QUESTION 11

- Customers
- Shareholders
- Government
- Public
- Employees
- Suppliers/ Creditors
- Unions
- Consumers
- The Law 2x5 **(10 marks)**

(b)

Customers: Quality products, value for money prices, warranties guarantees, service delivery, after- sales services.

Shareholders: High Roi, Increase growth, increased share value, profitable products, cost- effective operations.

Government: Tax Revenue, openers, job creation, new technologies.

Public: Environmental responsibility, safety, ethics, good neighbor policies.

Employees: Good salaries, staff benefits, job security career advancement, good working conditions.

Suppliers/Creditors: Prompt payment, Reasonable delivery expectations, Long term company solvency.

Consumerists Product safety, fair treatment of customers, good service, product information, redress.

The law Proper application of HSE and other legislation, No corruption, fair competition, sanctity of contracts and contract law.

Unions: Negotiation rights, fair treatment of members, import to company policies and strategies. **(28 marks)**

QUESTION 12

a. What is Strategic Management? (8 marks)

b. Discuss the five (5) stages of a Strategic Planning. (30 marks)

SOLUTIONS TO QUESTION 12

a. Strategic management is the formulation and implementation of a general plan for the way the organization will deploy its competence and resources in order to achieve its overall objectives .

b. **STAGE 1 External Analysis:**

- Social environment
- Technological environment
- Economic environment
- Competition
- Political environment
- Legal environment
- Environmental threat and opportunity profile (ETOP)

STAGE 2 Internal Analyses:

- Performance measures
- Finance
- Organization structure
- Human resources
- SWOT Analysis

STAGE 3 Strategy Formulations:

- Business idea
- Mission & Vision Statements
- Strategic direction

- Main objectives
- Critical success factors
- Overall plan
- Unit- level plans
- Contingency plans

STAGE 4 Organizations and Implementation
- Allocation of material and resources
- Budgets

STAGE 5 Controls:
- Monitoring
- Reappraisal and evaluation

QUESTION 13

Human Resource Management (HRM) is extremely broad in scope and covers many areas critical to the success of an organization. Identify and discuss ten (10) of these areas.

SOLUTIONS TO QUESTION 13

Scope of Human Resource management:
- Recruitment and Selection
- Reward system
- Organization and job design
- Employee Development
- Team building
- Change management
- Organizational Effectiveness
- Manpower and succession planning
- Manpower Development
- Employee Communication
- Performance management
- Career path management
- Counseling
- Incentive and benefit schemes **(38 marks)**

QUESTION 14

a. **What is marketing? Distinguish between Marketing and Advertising. (10 marks)**

b. **The Marketing Mix in a financial institution is depicted by the 6Ps.**

List them. **(18 marks)**

c. **What is Market Research compared to Competitor Research?** **(10 marks)**

SOLUTIONS TO QUESTION 14

Marketing is a series of management process based on a person's or an organization's interaction with, and understanding of, existing and potential customers; that makes it possible to provide customers with what they need and want.

Advertising on the other hand, is to inform customers; existing and potential, about the products and services on offer and encourage them to buy. **(10 marks)**

b.

- Product
- Price
- Promotion
- Place
- People
- Process **(18 marks)**

c. Market Research is a scientific method aimed at collecting and interpreting qualities and qualitative information about the buying behaviour of existing and potential customers

- Competitor research involves discovering as much as possible about the activities of a competitor through its own corporate literature, financial statements, industry reviews and the experiences of its customers. **(10 marks)**