

Insurance and Risk Management Practice Test

1. Pure risk may be said to create an economic burden in all except which one of the following ways?
 - a. pure risk results in gambling, which is a destructive social force
 - b. pure risk may deprive society of certain goods or services determined to bear excessive risk
 - c. pure risk can result in feelings of mental unrest and worry that can drain human energies
 - d. reserve funds may be necessitated that may not yield the highest rate of return available
2. The risk of potential losses to others as a result of injury or damage you may have caused is:
 - a. property risk
 - b. insurance
 - c. liability risk
 - d. personal risk
3. Examples of physical hazards include:
 - a. dishonest employee
 - b. building fire, oily rags, and a dishonest employee
 - c. oily rags and a gas leak
 - d. a building fire
4. Ken fell asleep while driving late at night. He crossed the center line and hit a car approaching from the other direction. The following losses occurred:
 - a. the car that Ken hit was a total loss
 - b. Ken's car sustained \$5,000 in damages
 - c. Ken incurred \$5,000 in medical expenses
 - d. the driver of the other car suffered \$30,000 in bodily injuries
5. Which one of the following losses would be covered under the medical payments coverage of the Homeowners 3 policy?
 - a. injury to a resident employee at the insured's home
 - b. injuries to another person arising out of the insured's negligent operation of a vehicle
 - c. medical payments resulting from the transmission of a communicable disease
 - d. workers compensation medical payments
6. A provision in disability insurance that specifies the conditions under which the insured is automatically considered disabled is:
 - a. partial disability

- b. presumptive disability
 - c. temporary disability
 - d. total disability
7. _____ is the likelihood that an event will occur.
- a. Peril
 - b. Hazard
 - c. Probability
 - d. Risk
8. Kathy entered into an insurance contract with XYZ Insurance Company. When the agent who sold the coverage witnessed Kathy doing something that violated the terms of the contract, he threatened to sue her to make her comply with terms of the contract. Which distinct legal characteristic of insurance contracts states that only the insurer's promise to perform is legally enforceable?
- a. unilateral contracts
 - b. personal contracts
 - c. contracts of adhesion
 - d. aleatory contracts
9. In what career would a person assess the cost of replacing or repairing damaged property?
- a. agent
 - b. appraiser
 - c. claims adjustor
 - d. risk manager
10. Jan is employed by an insurance company. She reviews applications to determine whether her company should insure the applicant. If insurable, Jan assigns the applicant to a rating category based on the applicant's degree of risk. Jan is a(n):
- a. actuary
 - b. claims adjustor
 - c. underwriter
 - d. loss control engineer
11. A peril that relates to a dynamic risk is:
- a. an increase in the consumption of cholesterol by society
 - b. death
 - c. riot
 - d. an earthquake
12. A peril that involves pure risk is:
- a. a building fire that burns one of several company owned office buildings
 - b. the purchase of a stock with a high degree of price fluctuation
 - c. a competitor's attempt to take market share from a business

- d. betting that the Dallas Cowboys will win the Super Bowl at the beginning of the football season
13. A misrepresentation:
- a. has a different legal effect from a concealment
 - b. voids a contract if it is material
 - c. always voids a contract
 - d. usually renders the contract voidable at the option of the insurer if it is material
14. A life insurance company based in Canada was licensed to operate in Massachusetts. When operating in Massachusetts, the Canadian insurer would be considered a(n):
- a. domestic insurer
 - b. alien insurer
 - c. captive insurer
 - d. foreign insurer
15. Taylor Tobacco Company is concerned that the company may be held liable in a court of law and forced to pay a large damage award. The characteristics of the judicial system that increase the frequency and severity of losses is known as:
- a. legal hazard
 - b. particular risk
 - c. moral hazard
 - d. speculative risk
16. A higher deductible results in:
- a. cancellation of the policy
 - b. tax savings
 - c. a lower premium
 - d. a higher premium
17. Which method would be more useful to discover a dollar estimate of losses?
- a. flowcharts
 - b. statistical analysis
 - c. financial statement analysis
 - d. contract analysis
18. Which one of the following is not a way to reduce auto insurance costs?
- a. reduce frequency of accidents
 - b. restrict payments to injured parties
 - c. build stronger cars
 - d. increase speed limits on interstate highway
19. Seat belts:
- a. are better than airbags
 - b. are very cost-effective if there is a high utilization rate
 - c. can be effective when combined with television ads designed to encourage seat belt use
 - d. are very cost-effective

20. The two major categories of automobile insurance are:
 - a. no-fault and assigned-risk insurance
 - b. automobile liability insurance
 - c. medical payments and collision insurance coverage
 - d. personal injury and property damage coverage
21. This type of auto insurance coverage pays for physical injuries sustained by the insured and passengers in the insured's auto.
 - a. comprehensive
 - b. transportation expense
 - c. liability
 - d. medical payments
22. This type of life insurance policy provides lifetime-long insurance protection.
 - a. endowment insurance
 - b. permanent insurance
 - c. group insurance
 - d. term insurance
23. This cost is to rebuild a structure or replace a piece of destroyed property.
 - a. book value
 - b. actual cash value
 - c. replacement cost
 - d. market value
24. This is auto insurance coverage that compensates insured's for damages caused by someone with insufficient limits of coverage for the insured's losses.
 - a. property damage liability coverage
 - b. bodily injury liability coverage
 - c. uninsured motorist coverage
 - d. underinsured motorist coverage
25. What is reinsurance?
 - a. personal insurance coverage above and beyond normal coverage
 - b. insurance for insurance companies to protect against large losses
 - c. automatic renewal of an individual's policy
 - d. the ability for an insurance company to modify an insurance contract
26. COBRA is a law dealing with:
 - a. the taxation of employee benefits
 - b. employment discrimination against elderly and handicapped individuals
 - c. qualification rules for employee benefits
 - d. the continued participation of terminated employees in group plans
27. An insurance agent who sells the products of only one insurance company is known as a(n):
 - a. broker

- b. independent agent
 - c. direct writer
 - d. exclusive agent
28. The doctor designated by the insured to be most directly responsible for his or her care is called:
- a. specialist
 - b. health maintenance organization
 - c. primary care physician
 - d. point-of-service organization
29. This federal retirement insurance program pays monthly benefits to eligible workers in retirement.
- a. Medicare
 - b. Medicaid
 - c. Unemployment
 - d. Social Security
30. What is a decrease in or disappearance of value?
- a. physical hazard
 - b. speculative risk
 - c. peril
 - d. loss
31. Insurance authors have traditionally defined risk as:
- a. any situation in which the probability of loss is zero
 - b. any situation in which the probability of loss is one
 - c. uncertainty concerning the occurrence of loss
 - d. the probability of a loss occurring
32. Abandoning an existing loss exposure is an example of:
- a. avoidance
 - b. non-insurance transfer
 - c. loss control
 - d. insurance transfer
33. Which one of the following statements about mutual insurers is true?
- a. They are legally organized as partnerships.
 - b. They are owned by their stockholders.
 - c. They may pay policy dividends or give rate reductions in advance.
 - d. They have a board of directors which is selected by state insurance departments.
34. The policy provision requiring the filing of proof of loss with the insurer is an example of a(n):
- a. insuring agreement
 - b. miscellaneous provision

- c. condition
 - d. declaration
35. When using the needs approach, several “special needs” should be considered. One special need is money to cover unexpected events, such as major car repairs, dental bills, or home repairs. Money set aside for this purpose is called a(n):
- a. emergency fund
 - b. readjustment period fund
 - c. mortgage redemption fund
 - d. estate clearance fund
36. Antonio is a claims adjustor for LMN Insurance Company. After the insurer is notified that there has been a loss, Antonio meets with the insured. The first step in the claims process that Antonio should follow is to:
- a. delay paying the claim if the claim is covered
 - b. verify that a covered loss has occurred
 - c. attempt to reject the claim regardless of whether he believes the claim is covered
 - d. determine the amount of the loss
37. Mark has been an underwriter for twenty years. An application he recently reviewed looked odd to him. The building value in the application seemed far too high, and Mark suspected the applicant might be planning to destroy the property after it is insured. Mark contacted an outside firm and hired someone to investigate the applicant and to prepare a report about the applicant. This report is called a(n):
- a. binder
 - b. physical inspection
 - c. agent’s report
 - d. inspection report
38. By misrepresenting the true facts, Gretchen was able to convince a client to drop a life insurance policy with another company and to purchase a policy from the company that Gretchen represents. Gretchen has engaged in the practice of:
- a. twisting
 - b. retaliating
 - c. rebating
 - d. bait and switch
39. A false statement made by an applicant for insurance is an example of a:
- a. lack of offer and acceptance
 - b. concealment
 - c. misrepresentation
 - d. breach of warranty

40. In what career would a person develop business strategies and presentations to promote the sale of different insurance products?
- underwriter
 - customer service representative
 - risk analyst
 - marketer
41. Which one of the following is NOT an element of a typical insurance plan?
- Pooling of Losses
 - Payment of Fortuitous Losses
 - Safety Deposits
 - Indemnification
42. _____ is the pooling of fortuitous losses by transfer of such risks to insurers who agree to compensate insureds for such losses, to provide other monetary benefits on their occurrence, or to render services connected with the risk.
- Insurance
 - Rebate
 - Tax Return
 - Tangible Repairs
43. _____ is when the losses of the few are spread over the group and the average loss is substitute for actual loss.
- Cooperative Agreement
 - Insurance
 - Pooling
 - Tax Deduction
44. _____ is a contractual obligation by which one person or entity agrees to reimburse another for loss or damage arising from specified liabilities.
- Insurance
 - Risk Transfer
 - Payment of Fortuitous Losses
 - Indemnification
45. _____ are unforeseen and unexpected losses that occur as a result of chance.
- Planned Losses
 - Fortuitous Losses
 - Volatile Losses
 - Insured Losses
46. _____ is a risk management and control strategy that involves the contractual shifting of a pure risk from one party to another.
- Risk Transfer

- b. Risk Reversal
 - c. Risk Movement
 - c. Risk Attainment
47. Which of the following is NOT a characteristic of a pure risk/ideally insurable risk?
- a. Small number of exposure units
 - b. Loss must be accidental and unintentional
 - c. Loss must be determinable and measurable
 - d. Loss should not be catastrophic
48. Which of the following is NOT a benefit of insurance to society?
- a. Indemnification for loss
 - b. Source of Investment Funds
 - c. Loss Prevention
 - d. Apprehension
49. A hazard is a condition that _____ the chance of loss.
- a. increases
 - b. decreases
 - c. has no effect on
 - d. is unrelated to
50. The _____ is the cause of loss.
- a. hazard
 - b. peril
 - c. objective risk
 - d. subjective risk
51. Lightning strikes your car and the car catches fire. What is the peril?
- a. Lightning
 - b. Fire
 - c. Car
 - d. Money
52. This type of loss control involves activities to reduce the frequency of losses
- a. Prevention
 - b. Preparation
 - c. Fortification
 - d. Reduction
53. This type of loss control involves activities to reduce the severity of losses
- a. Prevention
 - b. Preparation
 - c. Fortification
 - d. Reduction
54. _____ is a special form of planned retention by which part or all of a given loss

- exposure is retained by the firm
- a. active risk retention
 - b. passive risk retention
 - c. self insurance
 - d. none of the above
55. A _____ company is an insurance company owned entirely by its policyholders.
- a. franchised
 - b. unshared insurance
 - c. mutual insurance
 - d. exclusive insurance
56. Which of the following is NOT a reason to regulate insurers?
- a. Prevent insurer solvency
 - b. Compensate for inadequate consumer knowledge
 - c. Ensure reasonable rates
 - d. Make insurance available
57. Which of the following is an advantage of insurance?
- a. The cost of the payment of premiums
 - b. The time and effort spent in negotiating insurance coverages
 - c. Risk managers feeling less incentivized to follow the loss program
 - d. Insurance premiums are tax deductible
58. Which of the following is NOT a type of personal loss exposure?
- a. Personal
 - b. Environmental
 - c. Property
 - d. Liability
59. Ratemaking is performed by a(n):
- a. underwriter
 - b. actuary
 - c. rate-maker
 - d. accountant
60. T/F Ratemaking concerns the pricing of insurance and the calculation of insurance premiums.
61. T/F Mergers is a trend that is changing the corporate structure of mutual insurers.
62. T/F One of the benefits of passive retention is the avoidance of the administrative costs associated with seeking insurance from another party.
63. T/F An insurance deductible is a common example of risk retention to save money.

64. T/F Hedging increases portfolio risk or business risks involving future transactions.
65. T/F Insurance does not transfer pure risk.
66. T/F The 3 major forms of non-insurance risk transfer is by contract, hedging, and, for business risks, by incorporating.
67. T/F The formation of a corporation does not prevent the extension of the company's liabilities to its investors.
68. T/F Smoking cigarettes can be considered a form of passive risk retention.
69. T/F A forward contract does not guarantee the exchange rate for a future date.
70. T/F Risk refers to property and life being injured.
71. T/F A risk is the uncertainty of something and concerns a loss.
72. T/F A speculative risk is defined as relative variation of actual loss from expected loss
73. T/F An objective risk is defined as uncertainty based on a person's mental condition or state of mind.
74. T/F The four types of hazards are physical, legal, moral, and morale.
75. T/F A subjective probability is a probability derived from an individual's personal judgment about whether a specific outcome is likely to occur.
76. T/F Subjective probabilities contain formal calculations.
77. T/F A moral hazard is characterized as dishonesty or character defects in an individual that increases severity of loss.
78. T/F A morale hazard is characterized as carelessness or indifference to a loss because of the existence of insurance.
79. T/F A legal hazard is characterized as a tangible condition that increases the chance of loss.
80. T/F The risk categories include pure, speculative, fundamental, partial, and enterprise.
81. T/F A pure risk is a situation where there are only possibilities of loss or no loss.
82. T/F An example of a pure risk is medical expenses.
83. T/F A fundamental risk is a situation in which only profit or loss is possible.
84. T/F A particular risk affects only individuals and not an entire community.
85. T/F An enterprise risk affects the entire economy or large numbers of people.
86. T/F A strategic risk is uncertainty regarding the firm's financial goals and objectives.
87. T/F The major types of pure risk include personal risks, property risks, and liability risks.
88. T/F A financial risk refers to uncertainty of loss because of adverse changes in commodity prices, interest rates, foreign exchange rates, or value of money.
89. T/F An indirect loss refers to financial loss from the physical damage, destruction, or theft of property.
90. T/F Active retention occurs when no money is set aside to cover expected losses.
91. T/F Passive retention is the practice of protecting against a loss via the designation of

- specific funds to pay for the expected amount of the loss.
92. T/F The methods of handling risks include avoidance, loss control, retention, non insurance transfers, and insurance.
 93. T/F Loss control reduces frequency and severity of losses.
 94. T/F The Law of Large Numbers states that if the number of exposure units increases, the less closely the actual loss experience will approach the expected loss experience.
 95. T/F A premature death is the death of a family head with unfulfilled financial obligations that surviving members have to deal with.
 96. T/F Matters that need tended to after premature death include funeral expenses, medical bills, estate settlement costs, and taxes on large estates.
 97. T/F Downsizing is often the result of favorable economic conditions.
 98. T/F Downsizing results in increasing labor costs.
 99. T/F Tangible things that come with premature death include grief, loss of role model, counseling and guidance for children.
 100. T/F Enterprise risk management (ERM) is the process of planning, organizing, leading, and controlling the activities of an organization in order to minimize the effects of risk on an organization's capital and earnings.