

Ch 3

Introduction to Risk Management

QUESTION one (Multiple choice)

- 1- Risk management is concerned with
- a) The identification and treatment of loss exposures
 - b) The management of speculative risks only
 - c) The management of pure risks that are uninsurable
 - d) The purchase of insurance only
- 2- Risk management differs from insurance management in which of the following ways?
- I- insurance management is broader concept than risk management
 - II- Risk management includes all techniques for treating loss exposures
- a) I only b) II only c) both I and II d) neither I nor II
- 3- All of the following are risk management objectives prior to the occurrence of a loss except
- a) Economy
 - b) Continued operations
 - c) Reduction of anxiety
 - d) Meeting externally imposed obligations
- 4- Preloss objectives of risk management include which of the following ?
- I- Preparing for potential losses in the most economical way
 - II- Survival of the firm
- a) I only b) II only c) both I and II d) neither I nor II
- 5- The basic functions of a risk manager include which of the following?
- I- Identify potential losses
 - II- Selecting the appropriate techniques for treating losses
- a) I only b) II only c) both I and II d) neither I nor II
- 6- Sources of information that can be used by a risk manager to identify loss exposures include all of the following except
- a) Risk analysis questionnaires

- b) The firm's price to earnings ratio
- c) Physical inspections
- d) Reports on past losses

7- Loss severity is defined as the

- a) Probable size of the losses that may occur during some period
- b) Probable number of losses that may occur during some period
- c) Probability that any particular piece of property may be totally destroyed
- d) Probability that a liability judgment may exceed a firm's net worth

8- Loss frequency is defined as the

- a) Probable size of the losses that may occur during some period
- b) Probable number of losses that may occur during some period
- c) Probability that any particular piece of property may be totally destroyed
- d) Probability that a liability judgment may exceed a firm's net worth

9- The worst loss that could possibly happen to a firm is referred to as the

- a) Maximum possible loss
- b) Maximum probable loss
- c) Frequency of loss
- d) Severity of loss

10- The worst loss that likely to happen to a firm is referred to as the

- a) Maximum possible loss
- b) Maximum probable loss
- c) Frequency of loss
- d) Severity of loss

11- All of the following statements about avoidance are true except

- a) Certain loss exposures are never acquired
- b) Certain loss exposures may be abandoned
- c) The chance of loss for certain loss exposures may be reduced to zero
- d) It can be used for any loss exposure facing a firm

12- Abandoning an existing loss exposure is an example of

- a) Avoidance
- b) Loss control
- c) Noninsurance transfer
- d) Insurance transfer

13- Which of the following conditions is (are) appropriate for using retention?

- I- Loss are difficult to predict
 - II- The worst possible loss is not serious
- A) I only b) II only c) both I and II d) neither I nor II

14- Which of the following statements about retention levels is (are) true?

- I- A common rule of thumb is that a firm's maximum retention can be equal to 100 percent of its earnings before taxes
 - II- A financially strong firm can have a higher level than a firm whose financial position is weak
- a) I only b) II only c) both I and II d) neither I nor II

15- All of the following statements about captive insurers are true except

- A) they may act as a profit center by insuring parties other than the parent company
- B) they are a method for obtaining types of insurance that are unavailable from commercial insurers
- C) they decrease the volatility of a firm's earnings
- D) they make it easier for a firm to have access to reinsurance

16- Which of the following statements about self-insurance is (are) true?

- I- It is a form of planned retention
 - II- State law usually prohibits its use for workers compensation
- a) I only b) II only c) both I and II d) neither I nor II

17- All of the following are potential advantages of retention except

- a) Lower expenses
- b) Increased cash flow
- c) Encouragement of loss prevention
- d) Protection from catastrophic losses

18- A restaurant owner leased its meeting room to a second party. The lease agreement specified that the second party, rather than the restaurant owner, would be responsible for any liability arising out of the use of the meeting room and that the restaurant owner would be “held harmless “for any damages. The restaurant’s use of the hold harmless agreement is an example of

- a) Retention
- b) Self-insurance
- c) Insurance
- d) Noninsurance transfer

19- All of the following are disadvantages of Noninsurance transfer Except

- a) The party to whom the potential loss is transferred may be unable to pay
- b) The transfer may fail because the contract language is ambiguous
- c) The only potential losses that can transferred are those that are not commercially insurable
- d) The transfer may not reduce insurance costs, since an insurer may not give credit for the transfer

20- ABC Company retains the first \$1 million of each property damage loss and purchase insurance for that part of any property loss that exceeds \$1 million. The insurance for property losses above \$1 million is called

- a) Excess insurance
- b) Liability insurance
- c) Coinsurance
- d) Other insurance

21- Which of the following statements about the use of deductibles is (are) true?

I- They are a form of risk retention

II- They tend to increase the expense of adjusting small claims

- a) I only b) II only c) both I and II d) neither I nor II

22- Factors a risk manager must consider in selecting an insurer include which of the following?

I- The availability of risk management services

II- The financial strength of the insurer

- a) I only b) II only c) both I and II d) neither I nor II

- 23- All of the following are disadvantages of using insurance Except
- a) There is an opportunity cost because premiums must be paid in advance
 - b) Considerable time and effort must be spent negotiating coverage
 - c) It results in significant fluctuations in earnings after a loss
 - d) Attitudes toward loss control may become lax
- 24- Which of the following types of loss exposures may be appropriately handled by technique of insurance?
- I- High frequency , loss severity
 - II- Low frequency , high severity
- a) I only b) II only c) both I and II d) neither I nor II
- 25- Which of the following types of loss exposures are best met by the use of avoidance?
- a) low frequency , low severity
 - b) low frequency , high severity
 - c) high frequency , low severity
 - d) high frequency , high severity
- 26- low frequency , low severity loss exposures are best handled by
- a) avoidance
 - b) retention
 - c) insurance
 - d) loss control
- 27- all of the following statements about the administration of a risk management program are true except
- a) The risk manager is an important part of a firm's management team
 - b) A risk management policy statement can be used to educate top executives about the risk management process
 - c) If a risk management program is properly designed ,periodic review of the program is unnecessary
 - d) In order to properly identify loss exposures ,the risk manager needs the cooperation of other departments
- 28- Mr. Abd Allah was just hired as XYZ Company's first risk manager. Mr. Abd Allah would like to employ the risk management process. The first thing Mr. Abd Allah should do is
- a) Evaluate potential losses faced by XYZ Company.

- b) Formulate a treatment plan for XYZ Company's loss exposures
- c) Identify potential losses faced by XYZ Company
- d) Implement and administer a risk management plan for XYZ Company

29- Tarek decided to review his personal risk management program. His car is 10 years old and Tarek would receive little from the insurer if the car were stolen or destroyed. Tarek decided to drop the physical damage insurance on his car. From a risk management perspective, dropping the physical damage insurance on the car is best described as

- a) Increasing the use of avoidance in risk management program
- b) Increasing the use of noninsurance transfer in the risk management program
- c) Increasing the use of retention in the risk management program
- d) Increasing the use of loss control in the risk management program

30- To gain a better understanding of her company's operations, a risk manager asked a production manager to draw a picture tracing the steps in the production and distribution of each product produced by the company. Based on the diagram provided by the production manager, the risk manager was able to determine crucial points in the production and distribution process that needed safeguarding. The diagram tracing the steps in the production and distribution process is called a(n)

- a) Financial statement
- b) risk management matrix
- c) flowchart
- d) risk management audit

31- In reviewing his company's operations, a risk manager noticed that all of the company's finished goods were housed in a single warehouse. The risk manager feared that if the warehouse was destroyed, the company would lose all of its finished goods. He recommended that the finished goods be divided among 3 separate facilities. Dividing the finished goods among 3 facilities illustrates

- a) risk avoidance
- b) loss reduction
- c) insurance
- d) loss prevention

32- In selecting an insurer, the major consideration should be

- a) the company's attitude toward claims
- b) the cost of company's products
- c) Financial stability
- d) Competence of the company's agents

- e) The company's policy on cancellations

QUESTION Two

TRUE FALSE QUESTIONS

- 1- Risk retention deserves serious consideration when the maximum loss potential is small
- 2- The most important consideration in determining how to deal with a given risk is the potential severity of the loss and one's ability to bear it
- 3- Insurance should be considered as a last resort in risk management ,and should be used only
- 4- When both the potential severity and the probability of loss are high .the most appropriate techniques for dealing with the exposures are avoidance and reduction
- 5- According to the risk management philosophy. the cause of a loss is more important than its effect
- 6- In general ,The risk manager of organization should be someone outside the firm
- 7- The choice of a particular technique to be used in dealing with a given risk should be based on the probability and potential severity of the loss
- 8- The probability that a loss may or may not occur is the most important factor in deciding what should be done about a risk
- 9- In the last analysis for risk manager, there are only 2 approaches to dealing with risk : retention and transfer.
- 10- Risk management and insurance management are synonymous terms

QUESTION THREE (DEFINITIONS)

DEFINE THE FOLLOWING:-

Risk management - Personal risk management - Benefits of Risk Management
- PRE- LOSS Objectives of Risk management - POST- LOSS Objectives of
Risk management

QUESTION FOUR

Fill in

1- -----A systematic handling process, by which pure risks faced by family or organization can be identified and evaluated and the choice the appropriate methods for dealing with these risks by an effective program

Risk management

2- PRE- LOSS Objectives include 1- ----- 2- ----- 3-----

3- POST- LOSS Objectives include 1- ----- 2- ----- 3----- 4- -----

4- The process of risk management involves 6 steps they are -----, -----,-----,-----,---
-----,-----.

5- Personal risk management refers

Applied Case

Given that, you are the risk manager of your family. After your study for the risk management process in an organization (JEDDAH Spinning Factory), write **an essay** indicating in, how you can manage your family's risks.

