Foreword

To facilitate teachers in teaching the topic Risk Management of Financial Management covered under the Business Management Module of the Business Accounting and Financial Studies (BAFS) curriculum, the Technology Education Section of Curriculum Development Institute, Education Bureau developed this learning and teaching resource materials to provide teachers with a variety of learning and teaching examples for reference.

This resource materials include lesson plans, PowerPoint presentation slides, case study and other teaching activities, in-class exercise and home assignment as well as quiz with suggested answer, with suggested answers.

This resource materials are by no means exhaustive. Teachers are advised to update any business data/information adopted in this resource materials if deemed necessary.

Teaching plan for lesson 1:

Meaning of risk and the difference between speculative risk and pure risk

1. Objectives:

   Upon completion of the lesson students should be able to:

   a) Explain different concepts of risk
   b) Describe the meaning of risk
   c) Demonstrate the ability to measure the magnitude of a risk
   d) Differentiate speculative risk from pure risk and provide examples
   e) Explain the importance to distinguish speculative risk from pure risk

2. Suggested teaching schedule

	Content	PowerPoint	Remarks	Estimated time
1	The silver bond	2-3	Introductory case	3 mins
2	Meaning and magnitude of risk	4-9		13 mins
3	Pure risk vs Speculative risk	10-15		12 mins
4	A closer look at the pure risk	16-17		4 mins
5	Discussion and conslusion	18		8 mins
	Total			40 mins

Teaching plan for lesson 2:

The insurable vs non-insurable risks

1. Objectives:

   Upon completion of the lesson students should be able to:

   a) Describe the meaning of insurable risk and non-insurable risk
   b) Explain different criteria applied to distinguish insurable risk from non-insurable risk
   c) Differentiate insurable risk from non-insurable risk and provide examples

2. Suggested teaching schedule

	Content	PowerPoint	Remarks	Estimated time
1	Boycott the cosmetic company	2-3	Introductory case	5 mins
2	How speculative and pure risk relate to risk insurability	4	Revision	2 mins
3	Insurable risk vs Non-insurable risk	5		5 mins
4	Criteria for insurability	6-11		15 mins
5	Recall the introductory case	12-13	Group discussion	8 mins
6	Conclusion	14		5 mins
	Total			40 mins

Teaching plan for lesson 3:

Risk Management Strategy I

1. Objectives:

   Upon completion of the lesson students should be able to:

   a) Explain the meaning of risk management
   b) Describe the importance of risk management
   c) Differentiate different risk management strategies
   d) Illustrate how to apply risk prevention/reduction strategy with examples

2. Suggested teaching schedule

	Content	PowerPoint	Remarks	Estimated time
1	Contaminated pig	2-3	Introductory case	5 mins
2	Meaning of risk management	4		2 mins
3	Contents of risk management	5		2 mins
4	Why risk management	6		2 mins
5	Overview of Risk management strategies	7-8		5 mins
6	Risk reduction: concept and applications	9-18		20 mins
7	Summary	19		4 mins
	Total			40 mins

Teaching plan for lesson 4:

Risk Management Strategy II

1. Objectives:

   Upon completion of the lesson students should be able to:

   a) Explain the meaning of risk avoidance strategy and how it can be applied
   b) Illustrate how to finance the loss when the hazards happen
   c) Demonstrate how the risk assumption and risk transfer strategies can be applied to business operations with examples
   d) Analyse how different risk management strategies can be combined in application so that risk faced by the firm can be minimized at a reasonable cost

2. Suggested teaching schedule

	Content	PowerPoint	Remarks	Estimated time
1	The cyber attack	2-3	Introductory case	5 mins
2	Risk avoidance	4-5		3 mins
3	Strategies in preparing financing in case the loss occurs	6		2 mins
4	Risk transfer	7-8		5 mins
5	Risk assumption	9-14		15 mins
6	Recall: Cyber Attack Case	15-17	Group discussion	8 mins
7	Conclusion	18		2 mins
	Total			40 mins

Teaching plan for lesson 5:

The Risk Management Process

1. Objectives:

   Upon completion of the lesson students should be able to:

   a) Explain each step of the risk management process
   b) Illustrate how different types of risks can be identified and measured
   c) Demonstrate the considerations of costs and benefits of different risk management strategies
   d) Analyse how different risk management strategies can be applied with reference to different situations and characteristics of risk

2. Suggested teaching schedule

	Content	PowerPoint	Remarks	Estimated time
1	Convenience store robbery	2-3	Introductory case	5 mins
2	The risk management process – identify the risks	4-5		3 mins
3	The risk management process – analyse the risks	6		2 min
4	The risk management process – develop and evaluate different risk management strategies	7-11		15 mins
5	The risk management process – select the risk management strategies	12-15		10 mins
6	Implement and evaluate	16		3 mins
7	Conclusion	17		2 mins
	Total			40 mins

Teaching plan for lesson 6:

Insurance concept – an overview

1. Objectives:

   Upon completion of the lesson students should be able to:

   a) Describe the meaning of insurance from different perspectives
   b) Illustrate different important concepts of insurance with examples
   c) Explain different impacts of pure risk on business before and after the occurrence of hazards
   d) Demonstrate how insurance can help cover different direct and indirect losses involved in business operations with examples
   e) Apply the rules for considering whether insurance should be taken out or not

2. Suggested teaching schedule

	Content	PowerPoint	Remarks	Estimated time
1	Fire in mini-storage warehouse	2-3	Introductory case	5 mins
2	Meaning of insurance	4		2 mins
3	Common terms in insurance	5-8		10 mins
4	Impacts of pure risk on business	9		3 mins
5	Risks commonly faced by business – direct loss	10-11		6 mins
6	Risks commonly faced by business – indirect loss	12		4 mins
7	Risks commonly faced by business – liability	13		5 mins
8	Considerations before taking out insurance	14		3 mins
9	Conclusion	15		2 mins
	Total			40 mins

Teaching plan for lesson 7:

Common types of insurances for business I

1. Objectives:

   Upon completion of the lesson students should be able to:

   a) Describe the meaning and application of comprehensive insurance for business
   b) Distinguish the coverage of and conditions of different types of motor insurance
   c) Illustrate the implications of motor insurance on business
   d) Explain the meaning and coverage of fidelity insurance

2. Suggested teaching schedule

	Content	PowerPoint	Remarks	Estimated time
1	Introducing topics to be covered	2		2 mins
2	Comprehensive insurance for business	3		2 mins
3	Risk of operating a company owned vehicle	4		3 mins
4	Motor insurance: coverage and situation	5-7		10 mins
6	Implications on business	8-9		8 mins
7	The autonomous vehicle	10-12	Case discussion	8 mins
8	Fidelity insurance	13		5 mins
9	Conclusion	14		2 mins
	Total			40 mins

Teaching plan for lesson 8:

Common types of insurance for business II

1. Objectives:

Upon completion of the lesson students should be able to:

a) Explain the meaning of liability to business and various common areas in which business liability may occur
b) Describe employer's liability to employees' compensation
c) Explain the meaning and implications of employees' compensation insurance
d) Illustrate how employees' compensation insurance can be applied under different situations with examples
e) Analyse how the rising insurance costs of employees' compensation can be tackled
f) Describe the meaning of public liability insurance and its applications in business

2. Suggested teaching schedule

	Content	PowerPoint	Remarks	Estimated time
1	Court case on industrial accident	2-4	Introductory case	8 mins
2	Liability insurance and common types of liability for business	5-6		5 mins
3	Common types of liability insurance for business	7		3 mins
4	Employees' compensation insurance	8-10		8 mins
5	Increasing industrial accidents in Hong Kong	11-12	Case discussion	8 mins
6	Can the liability on employees' compensation be transferred	13		3 mins
7	Public liability insurance	14		3 mins
8	Conclusion	15		2 mins
	Total			40 mins

Lesson 1:

1

Meaning of risk and the difference between speculative risk and pure risk

Introductory case: The Silver Bond

2

The Government launched the First Silver Bond for subscription by Hong Kong residents aged 65 or above on July 26, 2016.

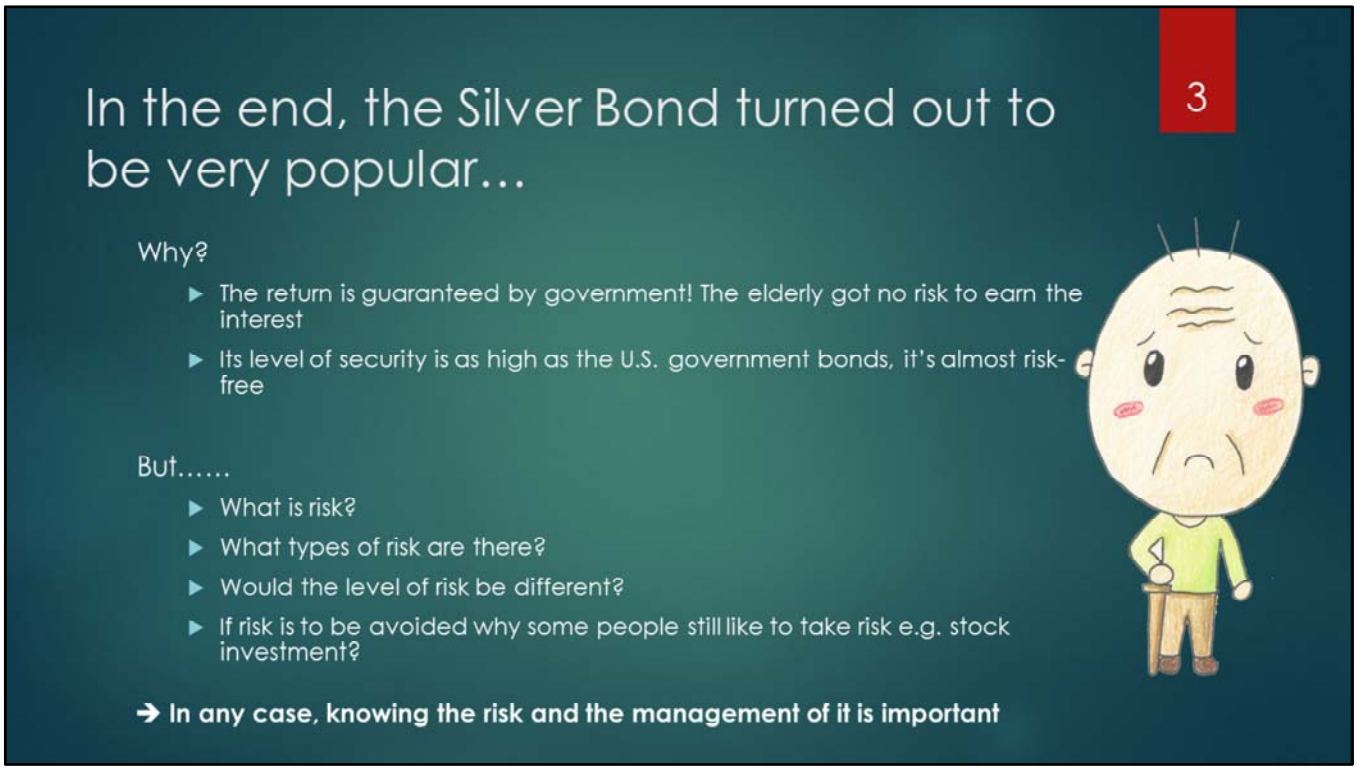
At that time, Secretary for Financial Services & the Treasury Prof KC Chan mentioned that: "The issuance of the Silver Bond aims to provide an investment product with steady returns for senior residents in Hong Kong and at the same time encourage financial institutions to tap into the immense potential of this silver market by introducing a wider spectrum of appropriate products. The target issuance size of the first Silver Bond will be $3 billion, it will have a tender of three years, bond holders will be paid interest once every six months at the rate linked to the inflation of Hong Kong, subject to a minimum rate of 2%."

Unlike the iBond, the Silver Bond cannot be traded on the secondary market.

It carries a guaranteed yield of 2%, compared to 1% offered by the iBond.

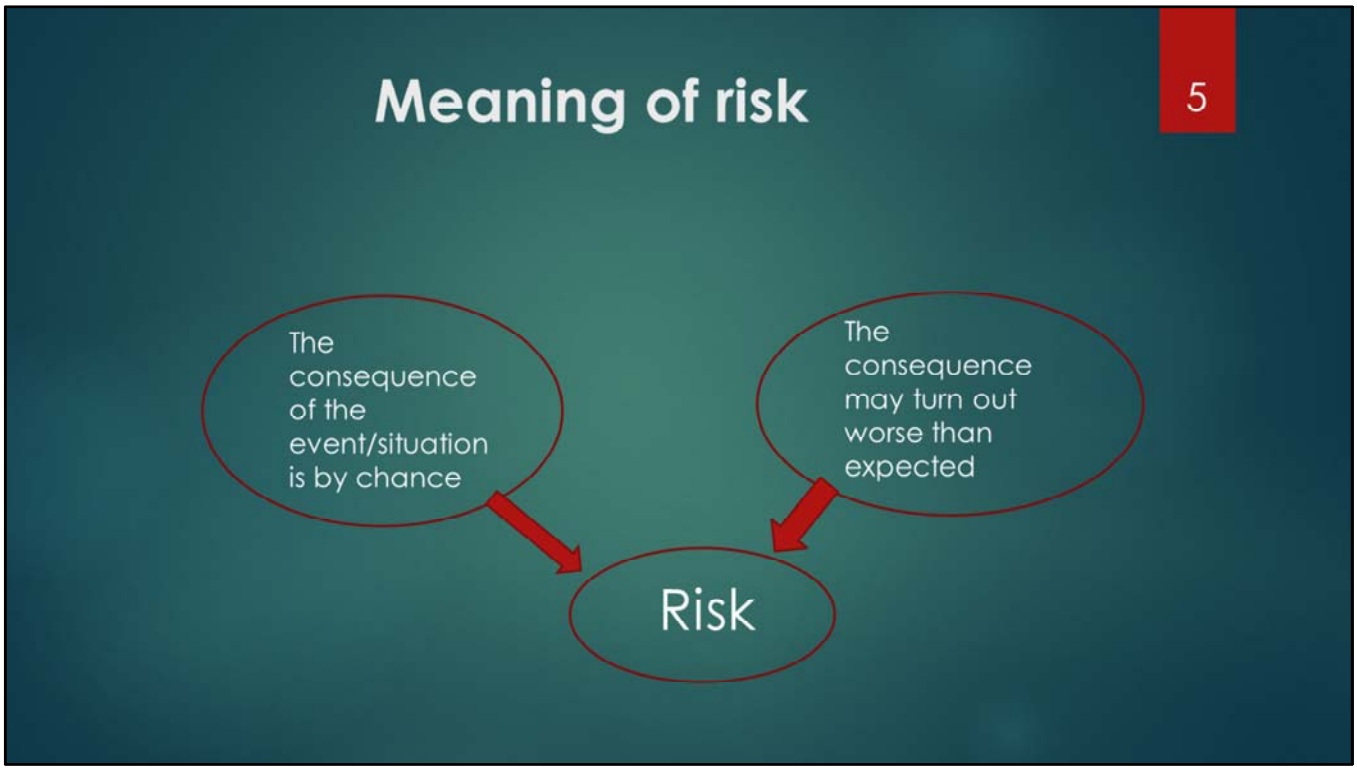
The subscription period started at 9am on 26 July 2016 and ended at 2pm on 3 August 2016. The bond was issued on 12 August, 2016.
(Source: News.gov.hk, 15 July 2016)

- Start the lesson and mention the topic of this lesson
- Use a real-life case as an introduction
- Explain the silver bond according to the contents in the PowerPoint



- Tell the students that the bond turned out to be very popular
- Ask why the bond is so popular
- Try to bring out the idea of risk
- Explain that different people or different organizations may have different preference to risk
- Meanwhile, no body would like to take risk without any preparation no matter on avoidance or taking it as a trade-off

- Explain the topics to be covered in this lesson



- Risk means the possible consequence of an event or situation is subject to chance, a random situation
- One of the possible consequence of the situation could be worse than what we expect
- After all, as there is no formal definition of risk, it is popular and widely accepted to interpret risk as a situation in which the outcome of an event is uncertain that a loss would be incurred

Meaning of risk

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Examples of risk:

- Risk in running a business
  - (A) What are the possible consequences?
  - (B) What is the possible consequence that is worse than expected?
- Risk in operating a machine
  - (A) What are the possible consequences?
  - (B) What is the possible consequence that is worse than expected?

Any difference between (A) and (B) in each example of risk?

- Ask students what difference that they can find between these two kinds of risk
- Highlight that risk in running a business could end up with a profit or a loss
- Worse than expected could mean the amount of loss incurred larger than expected
- Risk in operating a machine could be having a breakdown or having no breakdown
- Worse than expected should be having an accident

Meaning of risk

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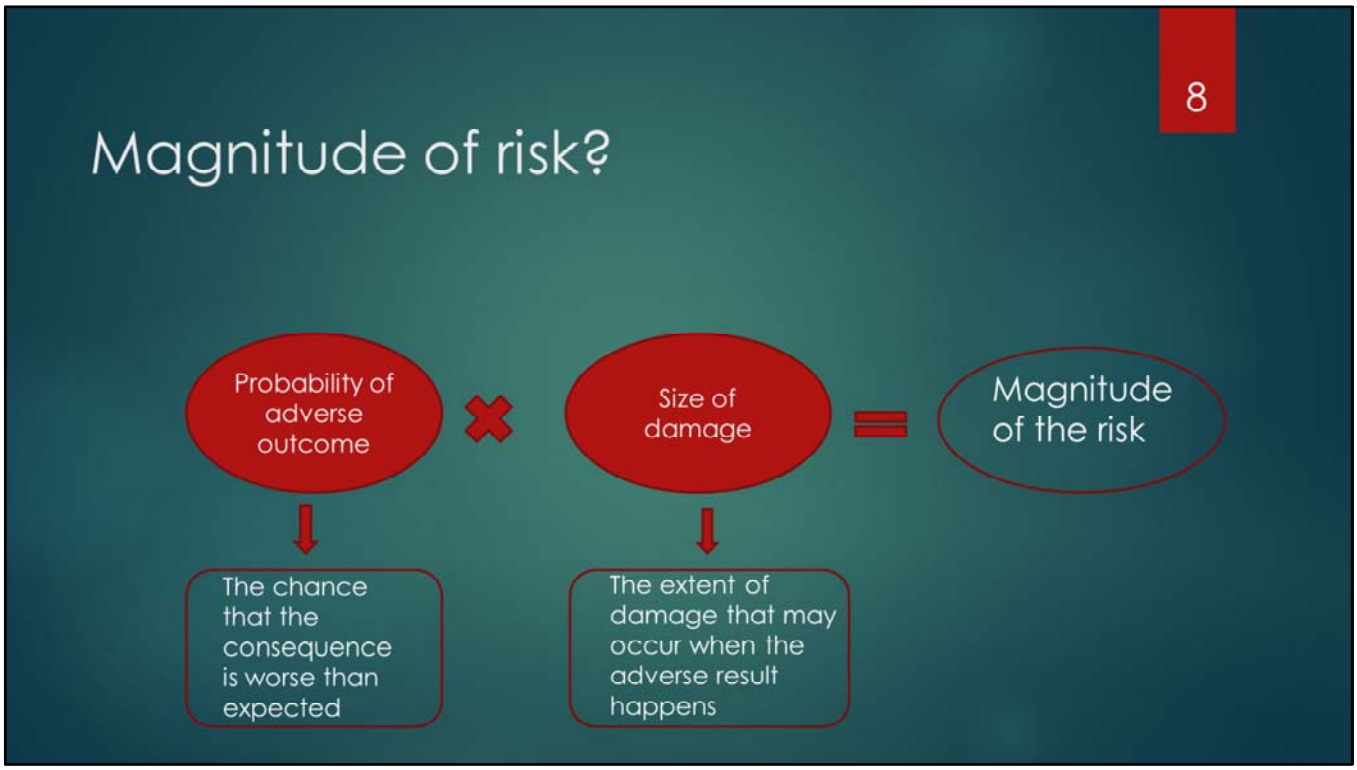
- Recall the case on the Silver Bond, could you point out the difference between (A) and (B)?

- Going back to the Silver Bond case, what is A and B?
- A: possible consequence – get the interest or cannot get the interest
- B: possible consequence worse than expected – the bond defaults
- Since the occurrence of A and B is close to zero, the bond can be said as risk-free



- There are many risks that we may encounter both as an individual or as a company
- There could be some risks which are very serious but many others with minor impact
- Before deciding how to deal with them, it would be better to find out how serious they could be
- There are two components in assessing a risk
- The probability that the risk could happen and the size of damage that the risk could cost once happened
- If a serious earthquake happens, the consequence could be catastrophic. But since the chance of having it in HK is nearly impossible, the magnitude of this risk to HK is minimal or negligible
- A way to calculate the magnitude of the risk is to multiply the probability that is between 1 and 0 by the size of potential damage
- Given the same size of possible damage, the higher the possibility of the risk, the greater the magnitude of the risk.
- In case the probability is 1, it would not be a risk since its happening is not by chance but certain

How large is the risk?

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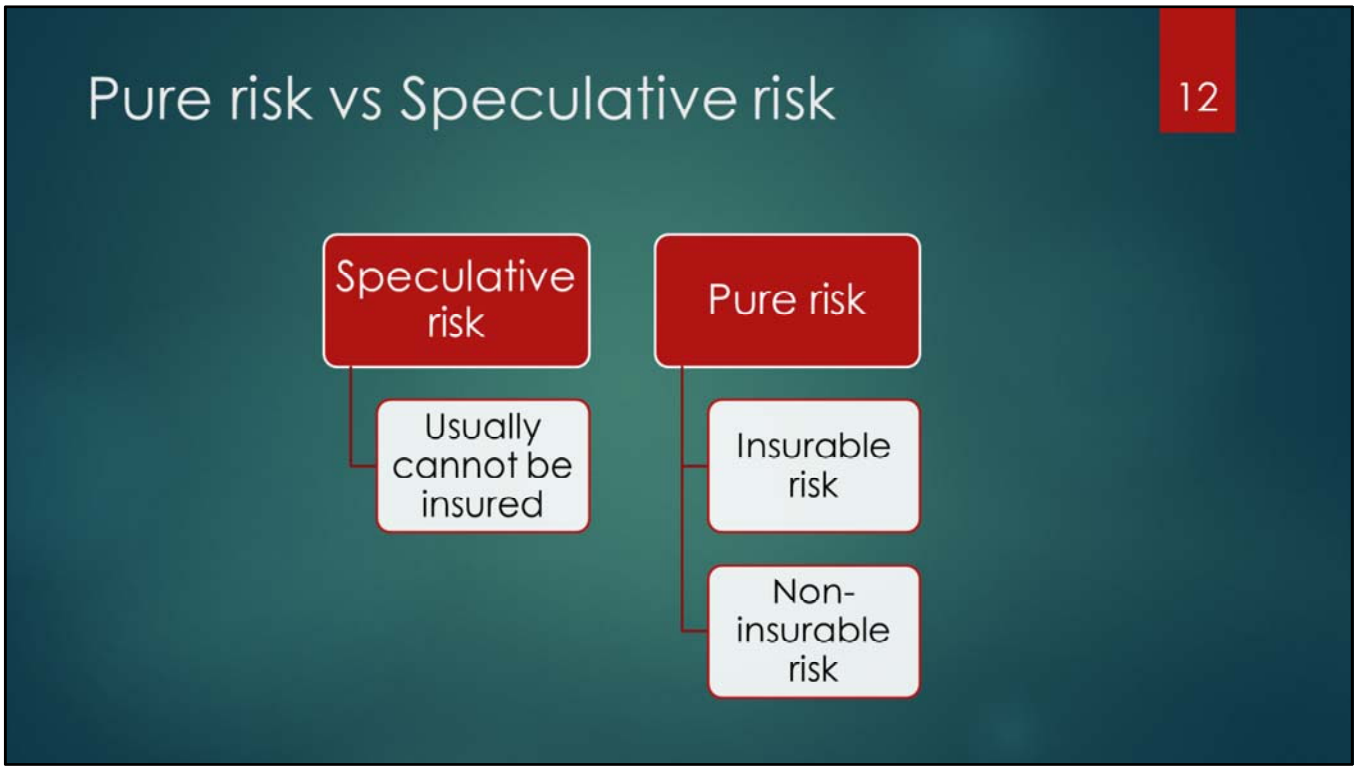
Probability of adverse outcome	Size of damage	Magnitude of risk
↓	↓	Lower
↑	↑	Higher
↓	↑	Pending / Uncertain
↑	↓	Pending / Uncertain

- Based on the calculation, there could be four possible situations
- Low probability and small size of damage means lower risk e.g. freezer at a convenience store is out of order due to electricity cut
- High probability and large size of damage means higher risk e.g. people engaged in high risk job such as a stuntman, getting hurt in a
- High probability and small size of damage means the risk is uncertain e.g. shoplifting in a Jewel shop
- Low probability and large size of damage also means the risk is uncertain e.g. earthquake in Hong Kong

- There are different classifications of risk and one of the most common way is to differentiate the risk into pure risk and speculative risk
- Pure risk refers to those cases in which the outcome of an event could only be a loss or without a loss
- Speculative risk refers to those cases in which the outcome could be a gain or a loss
- Students could be asked to raise examples of pure risk and speculative risk and justify their answer according to the definition mentioned above

- Why it is important to separate pure risk from speculative risk
- Would it be very arbitrary?
- Ask students to raise different ideas about why
- E.g. some may say speculative risk is necessary since it is commonly known that the higher the risk the higher the return
- Therefore certain level of speculative risk is inevitable though excess risk relative to expected return should be avoided
- However, pure risk can only result in a loss if it is not being well-managed
- Thus, pure risk need to be minimized at acceptable costs in whatever cases



- Following the logic in the previous PowerPoint, sometimes speculative risk is inevitable but pure risk should always be minimized
- A major reason to distinguish pure risk from speculative risk is that speculative risk is generally not insurable while many pure risks can be
- Normally insurance is only for pure risks and speculative risks are generally not covered
- It should be mentioned that even for pure risks not all are insurable
- Whether the pure risk is insurable or not will be discussed in details in later lessons

- Other differences between pure risk and speculative risk:
- Speculative risk usually involves many different factors / complicated situations. Such risk will lead to a gain as well as a loss
- Minimization of speculative risk is very complicated and difficult. It would involve many departments and operations in the process
- Since there may be gains in some cases, it may be worthy for taking such risk

- Comparing with the previous PowerPoint:
- Relatively pure risk is based on simpler factors and situations
- Normally the probabilities of occurrence of pure risk can be predicted
- Measures can be taken to reduce the pure risk
- Management of pure risk can be confined to some departments
- Thus, management of speculative risk vs pure risk is very different
- Furthermore, in many cases pure risk would not only affect the party involved but also the general public e.g. when the factory is on fire the neighborhood would be affected too
- Thus, pure risk also involves a social concern

Pure risk vs Speculative risk

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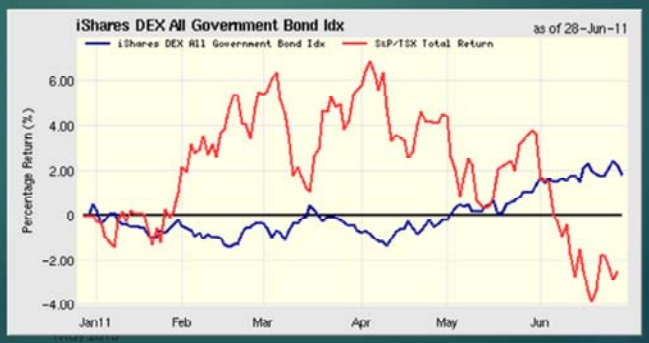
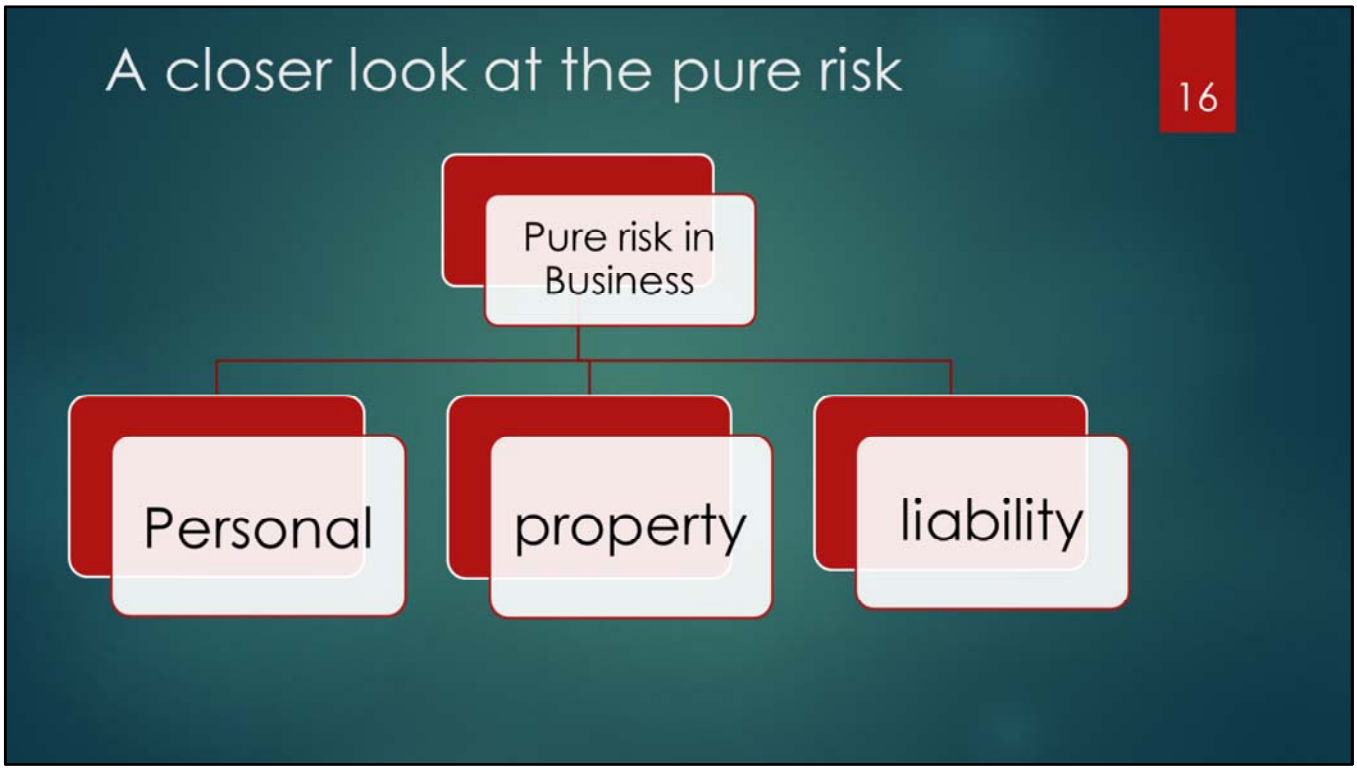
- Recall the case on the Silver Bond
- Is the risk associated with the Silver Bond speculative or pure?



- Theoretically the buying of Silver Bond could be a speculative risk since there could be a gain (getting the interest) or a loss (the bond defaults) though the chance of a loss is close to zero.



- We know that there are pure risk and speculative risk, and it is the pure risk that management of risk would mainly concern about
- Now we go further to know more about the different kinds of pure risk faced by a business
- There are mainly three major types of risks: personal, property and liability
- Personal: mainly due to illnesses or accident of employees and key staff of the company
- Property: direct and indirect losses due to damage of properties
- Liability: harms to other person or damage to other people's property owing to the firm's carelessness

Causes of pure risk

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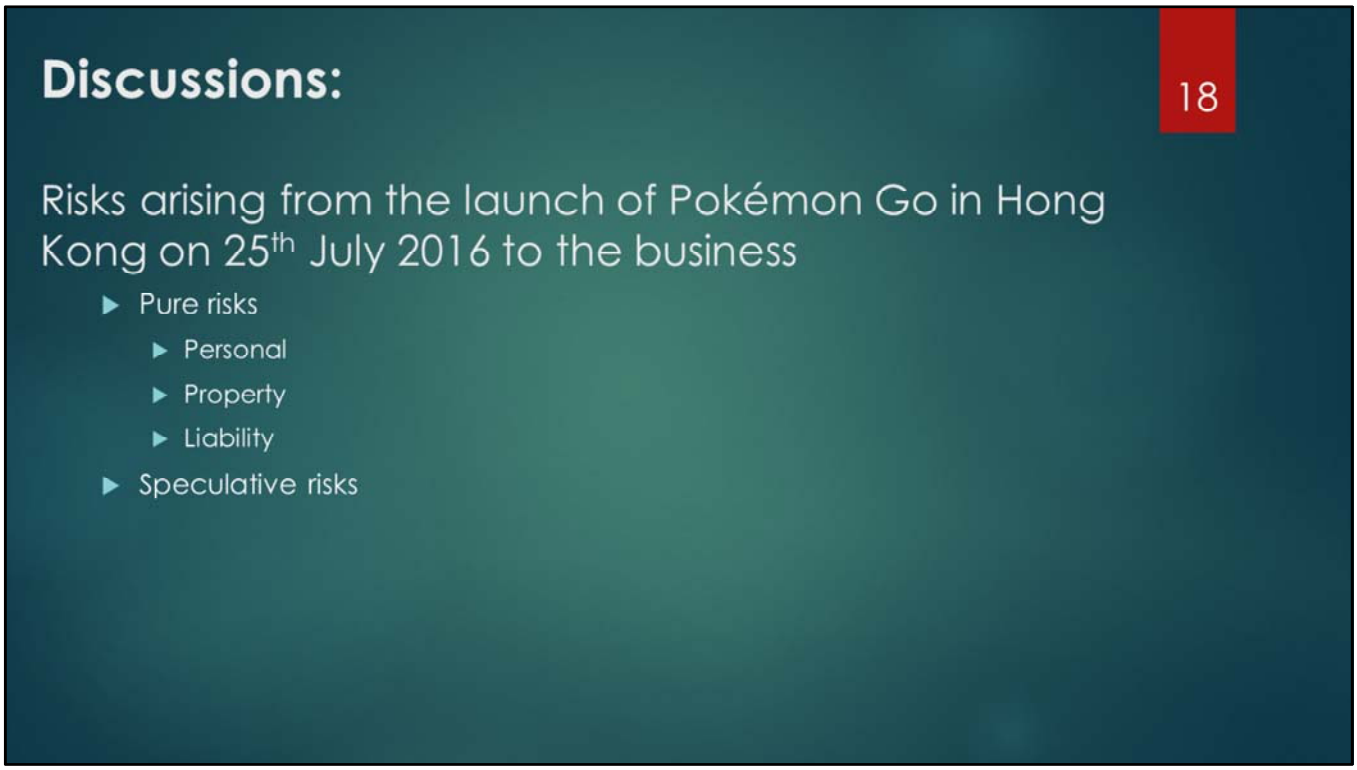
- Personal: life injury, diseases, accident etc
- Property: fire, flooding etc
- Liabilities: product safety, negligence of employees during work etc

- Describe in details about the causes mentioned in the PowerPoint e.g. product safety refers to product defects or harmful ingredients
- Pure risk of property refers not only to the direct loss associated (e.g. the fire may burn down the whole premise) but also the indirect loss incurred (e.g. no place to continue the business for a period of time)
- Ask students to raise different examples of pure risk under the three categories



- Ask students to have a discussion on the case shown in the PowerPoint
- For pure risks:

  Personal: injury, bad health of staff due to addiction in playing the game

  Property: delivery van crashed due to bad health of staff

  Liability: trespass to private area of the business by stranger who is playing the game (lawsuit to Nintendo)
- For speculative risk:
- Nintendo may get high profit by launching the Pokémon Go
- Some firms pay for having the Pokémon located in their premises in order to increase traffic may earn handsome profit

- Ask students to highlight what they have learned in this lesson
- Meaning of risk: different definitions of risks covered
- Magnitude of risk: probabilities and size of damage of the risk
- Differentiation of pure risk from speculative risk with examples
- Importance to distinguish pure risk from speculative risk
- The kind of risk that traditional risk management mainly concern

Lesson 2:

1

The Insurable vs Non-insurable Risks

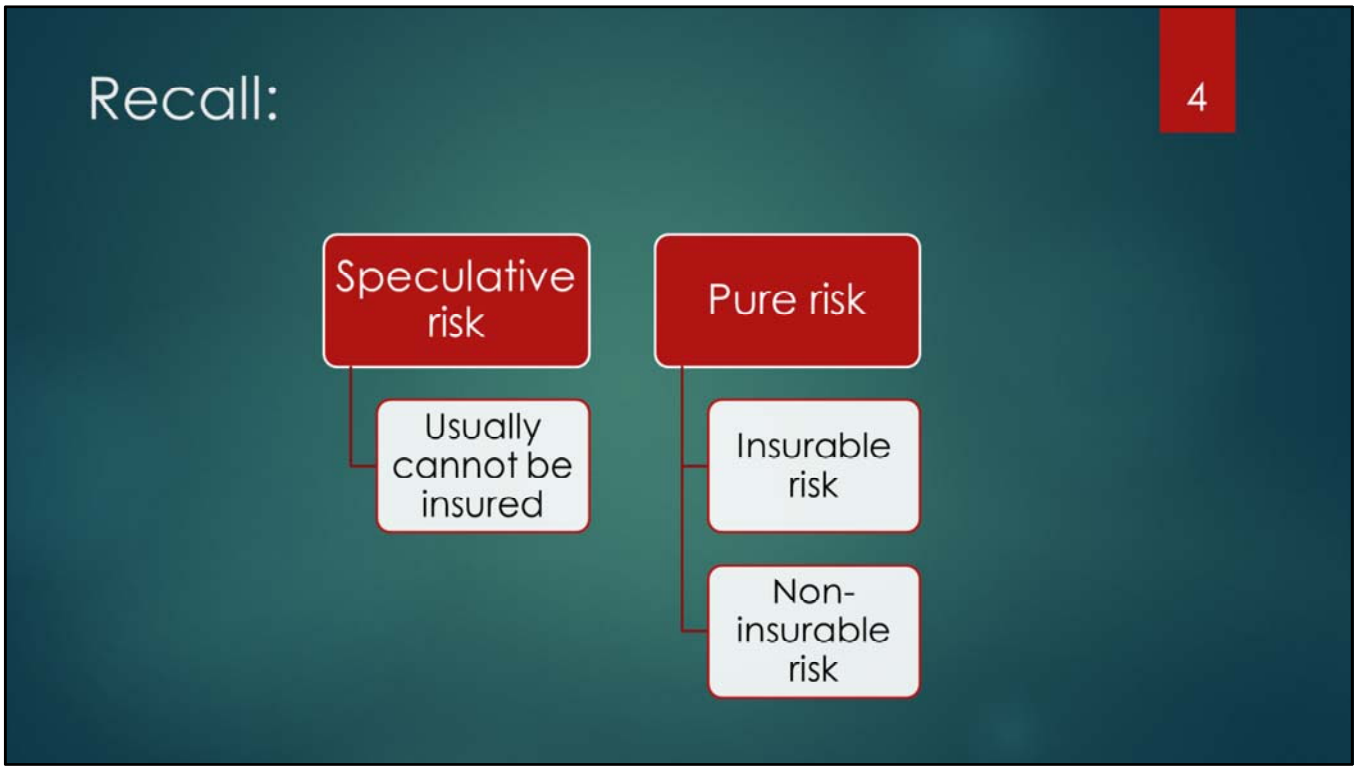
Introductory case: Boycott the Cosmetic Company

2

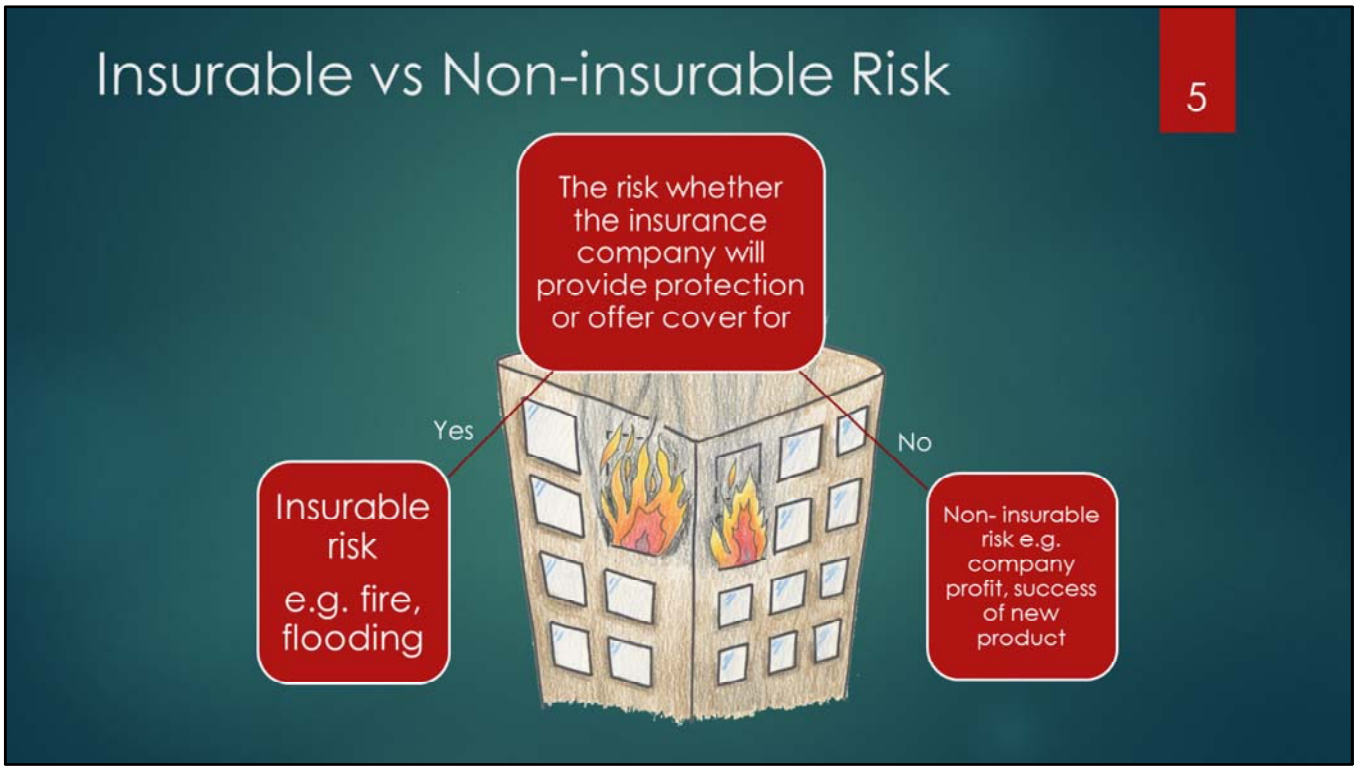
- In summer 2016, a French cosmetics company cancelled a concert organized for a Hong Kong singer for some sensitive reasons. The decision triggered massive sentiment against the company. More than twenty thousand people signed up online requesting the company to reconsider its decision. Also, the news was picked up by international media. As the company did not change its position many people called for boycott of the company's product through social media.
- Question: Is it possible for the company to insure for such kind of risk? What would be the criteria for an insurance company to accept the offer?

- Start lesson 2 by mentioning that there is other classification of risk apart from the pure and speculative risk
- That is insurable vs non-insurable risk
- It is important to know about this classification especially when many risks are supposed to be dealt with through insurance
- Before going on, use the real-life case from above to aid illustration
- Ask the students whether it is possible for the company to insure against the loss due to such damage on its image

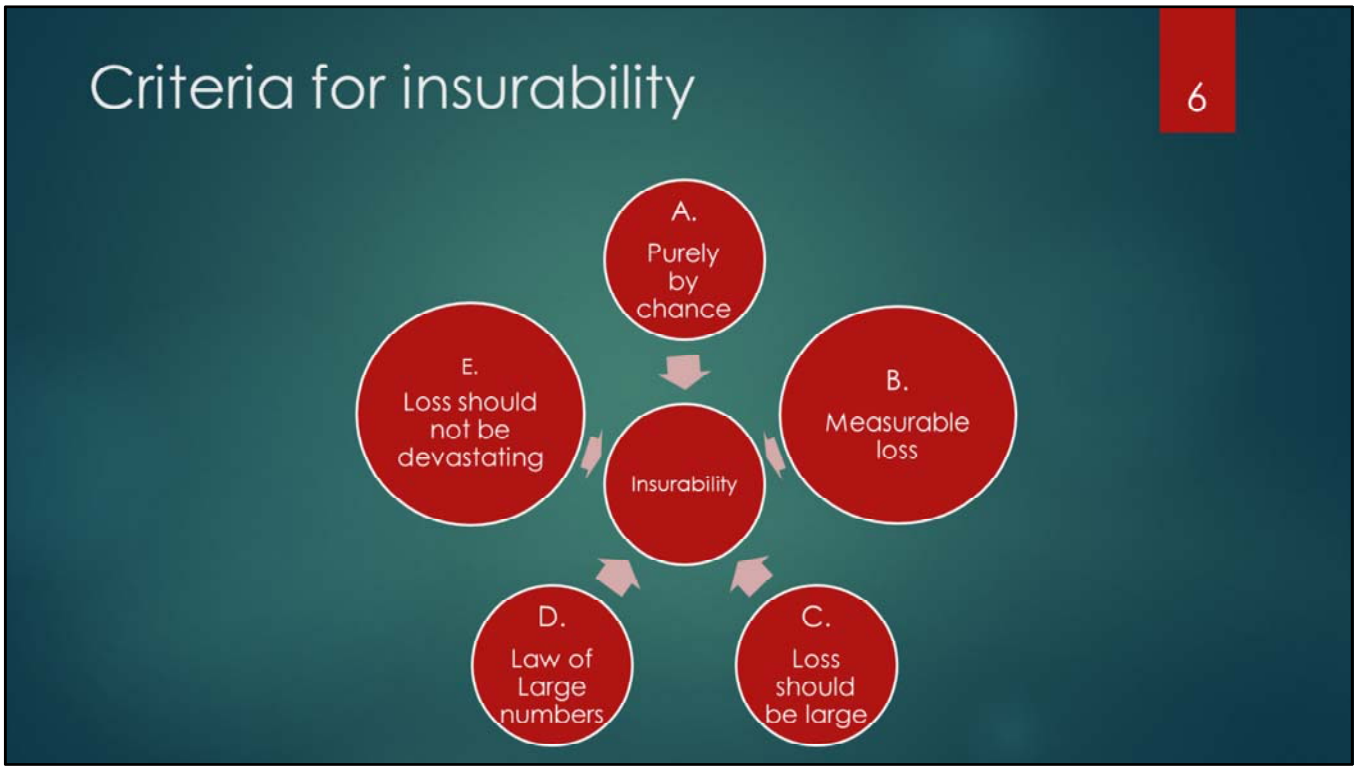
- Explain the topics to be covered



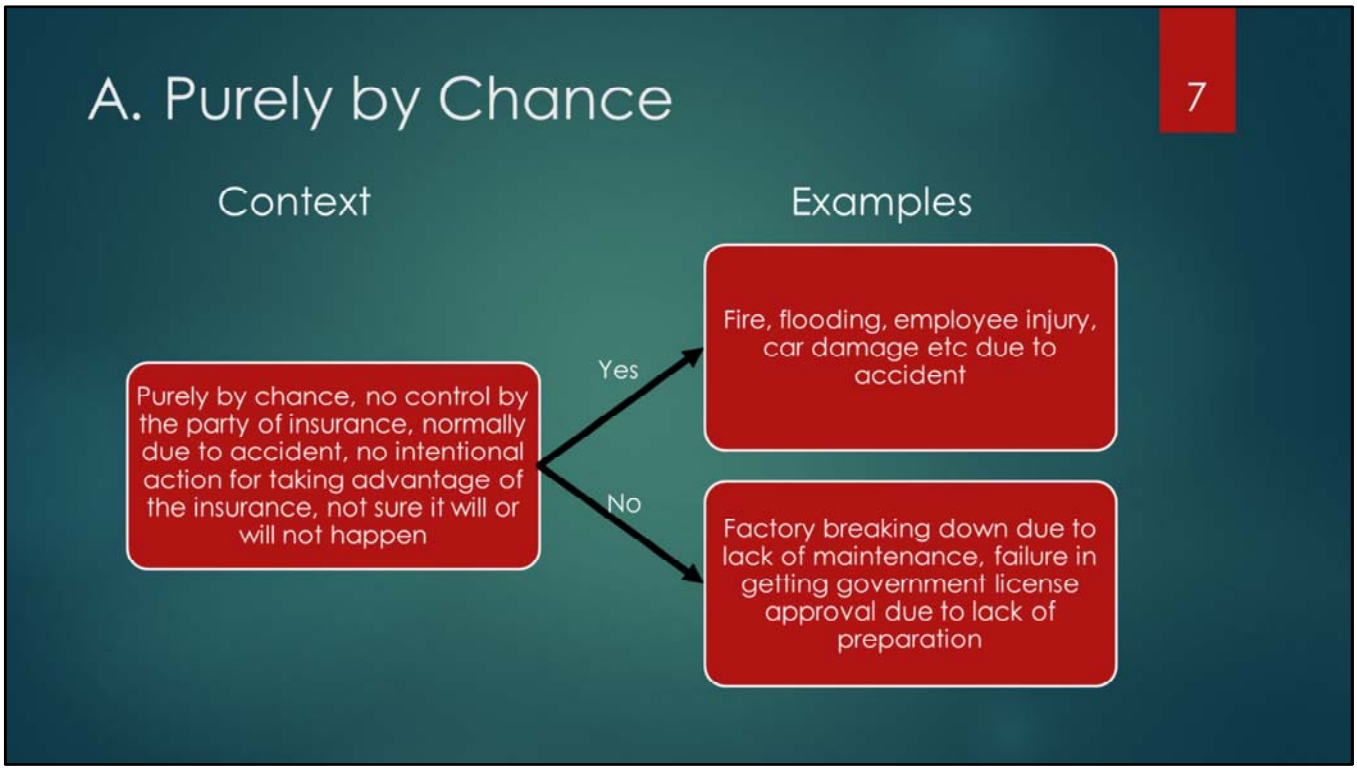
- Recall what have been learned in lesson 1 about one of the major differences between pure risk and speculative risk
- Normally insurance is only for pure risk
- Speculative risk are generally not under insurance coverage
- It should be mentioned that even for the pure risks not all of them are insurable
- The reason for some pure risks are insurable but some are not will be discussed in coming ppt.



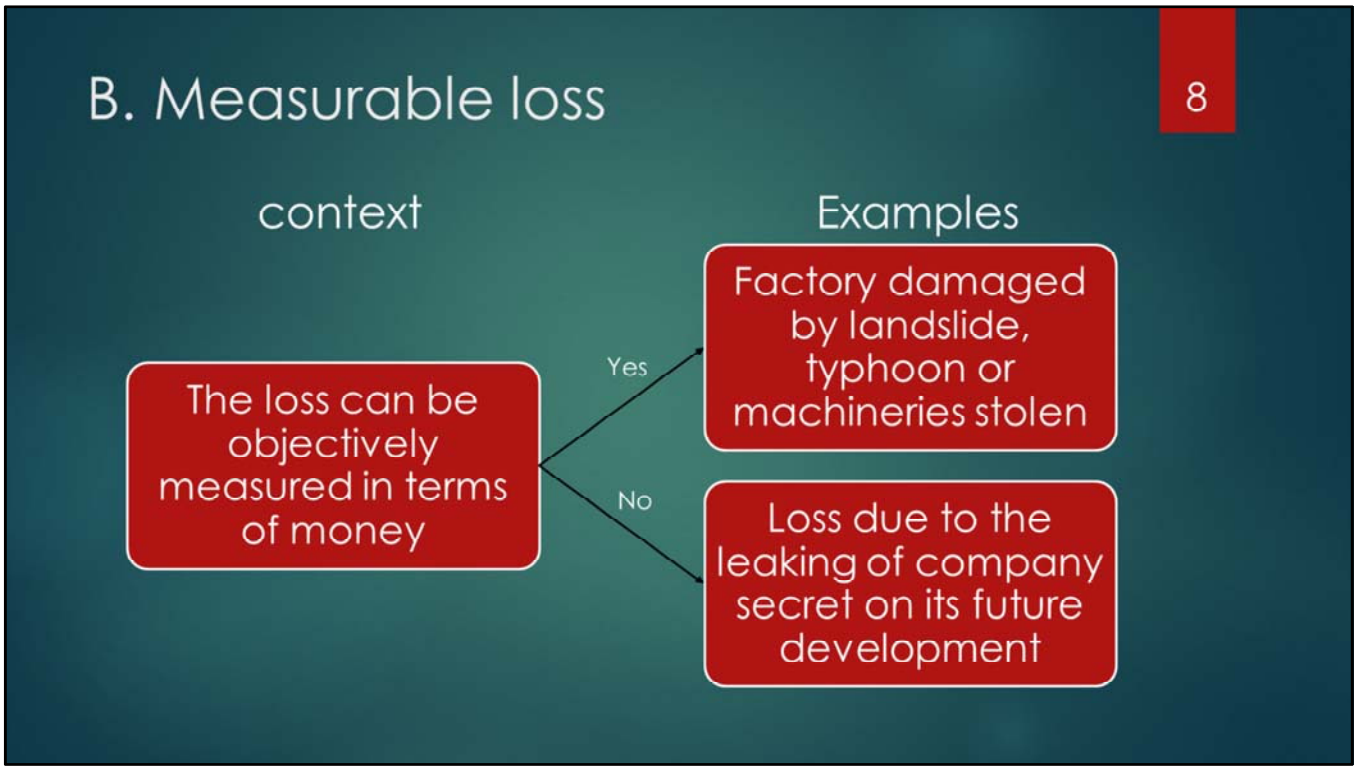
- The meaning of insurable risk is the risk that the insurance company will provide cover for
- It is important to distinguish what risk is insurable and what risk is non-insurable
- It is because one the major means to deal with risk is through insurance
- As mentioned before pure risk is normally insurable with some exception, while speculative risk is generally not insurable
- The examples shown are those pure risks that are insurable, and those speculative risks that are non-insurable



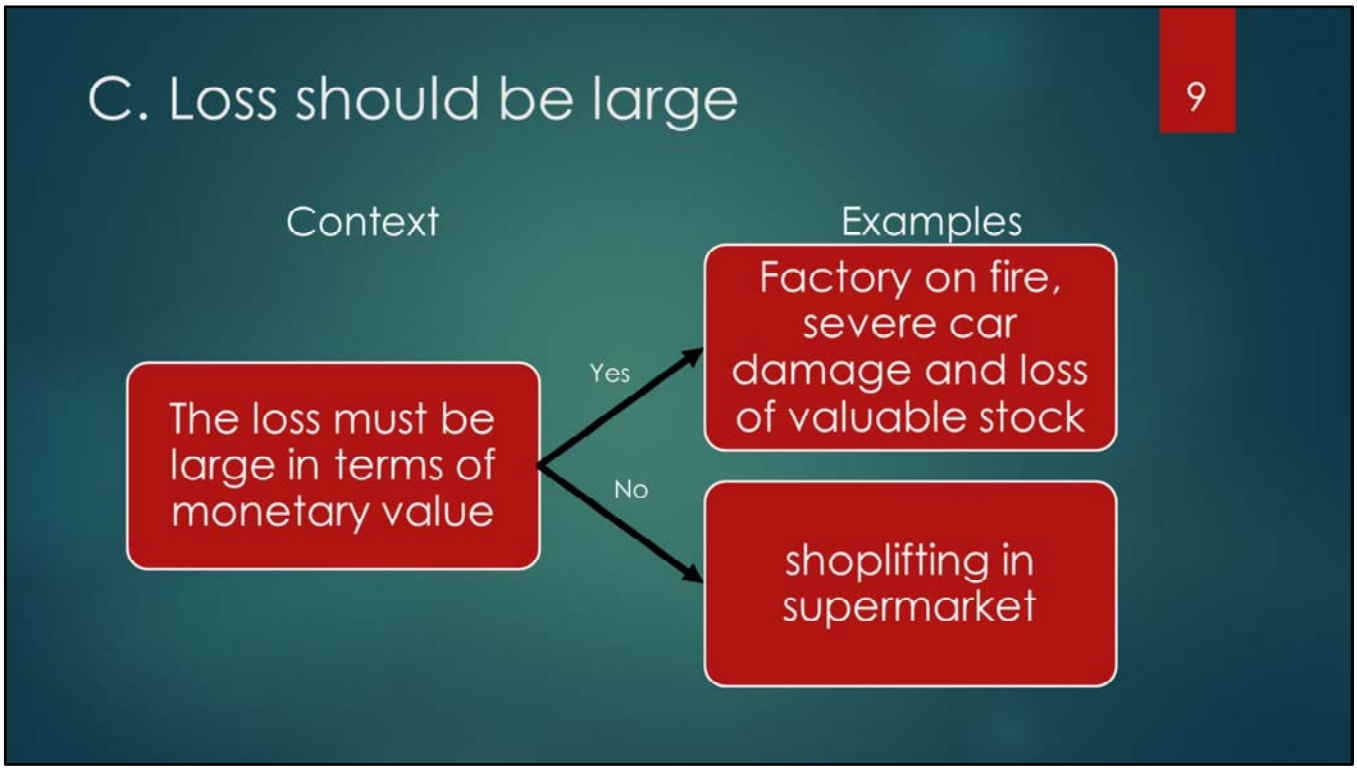
- What constitute insurability especially when not all pure risks are insurable?
- Five criteria are used to examine whether certain pure risk is insurable or non-insurable
    - Purely by chance, random cases
    - Measurable loss
    - Large, significant loss
    - Law of large numbers
    - The loss should not be devastating
- The criteria list is by no means exhaustive but is generally applied



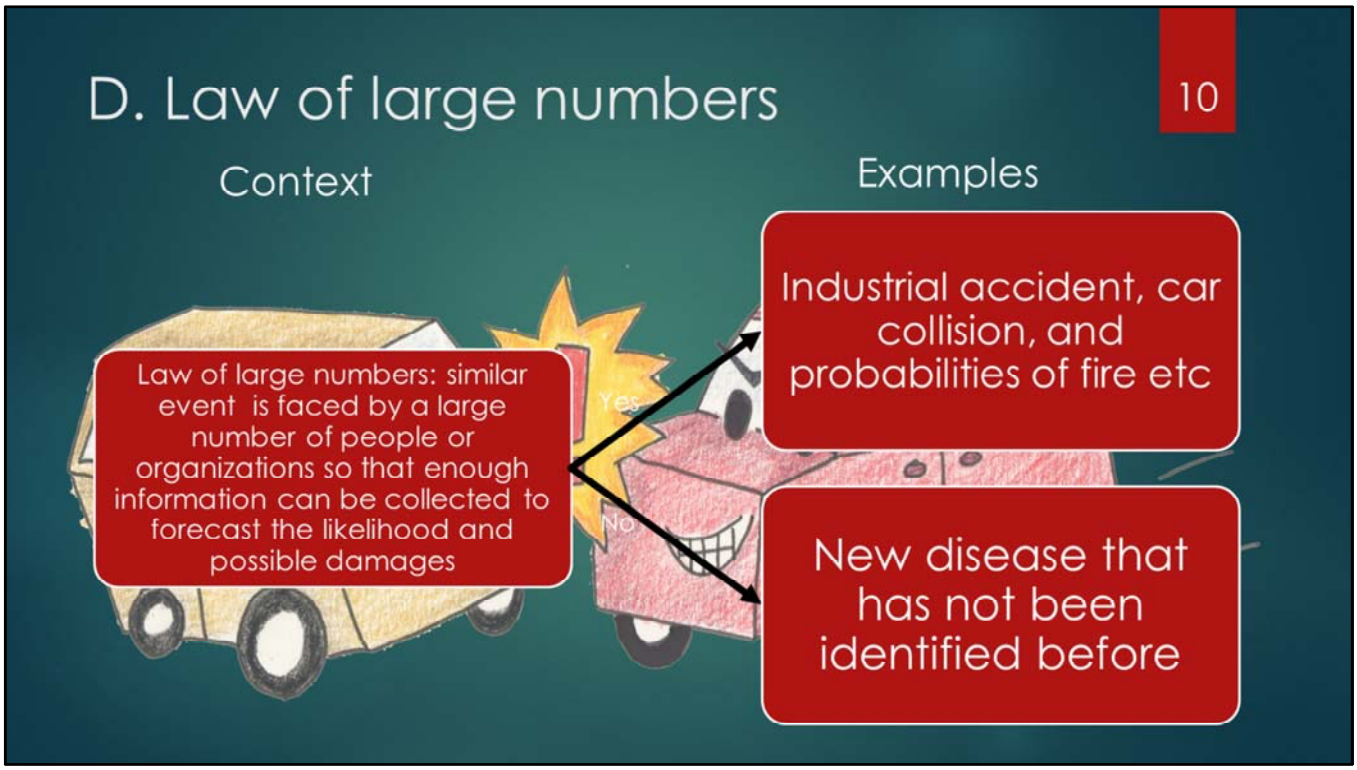
- Students may argue that people may take deliberate action in order to get the benefit of compensation from insurance (e.g. intentional personal injuries or destruction to property)
- In such case, once proved, the insure will not get the compensation, and may be liable for imprisonment too



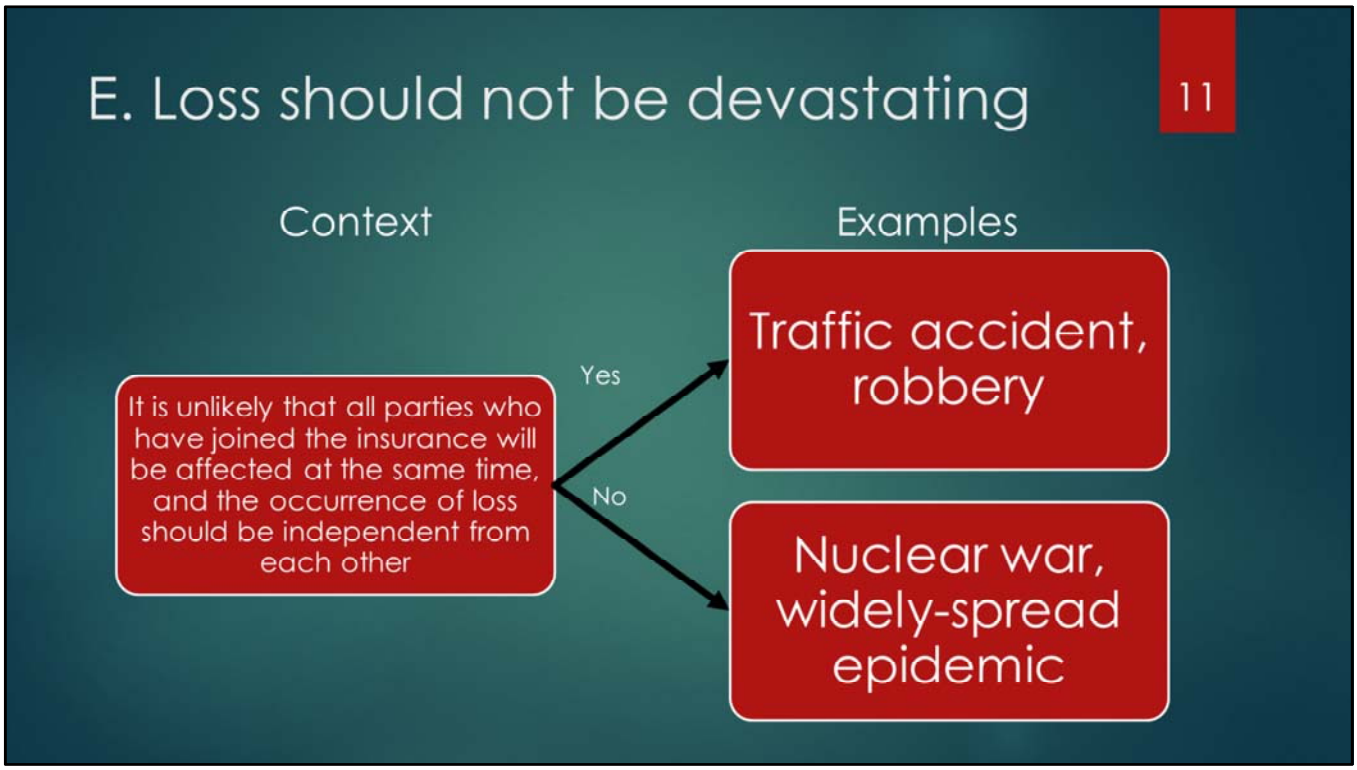
- The insurer needs to know the value of the potential loss so that it can determine the premium
- The introductory case used in the beginning of the lesson can help illustrate this point



- The rationale of having this criteria is that if the loss value is too small, the administrative costs involved in the calculation may even higher than the loss value
- That is why many insurance companies will apply deductibles
- Of course, whether the amount is large enough or not could be subjective in some cases
- Ask students to raise other examples



- It will be difficult for insurance as it is mostly difficult to apply the law of large number relating to a change in government policy
- It is because the policy of a government in one place can be very different from the others, and the effectiveness on each policy is indeed greatly affected by many different factors over different periods of time
- Students may argue about insurance against harms to the beautiful leg taken by the a movie star (shown on a TV series)
- It may be because the insurer can join with many other underwriters undertaking such case so that the risk can be spread.
- Also, the premium could be very high to protect the insurer



- In fact, the main point is that the insurer needs to maintain a situation in which not all or majority of the insured will be affected at the same time
- Thus being geographically scattered could be one of the ways to spread the risk
- The risk should not be catastrophic otherwise the insurer cannot survive

Discussion

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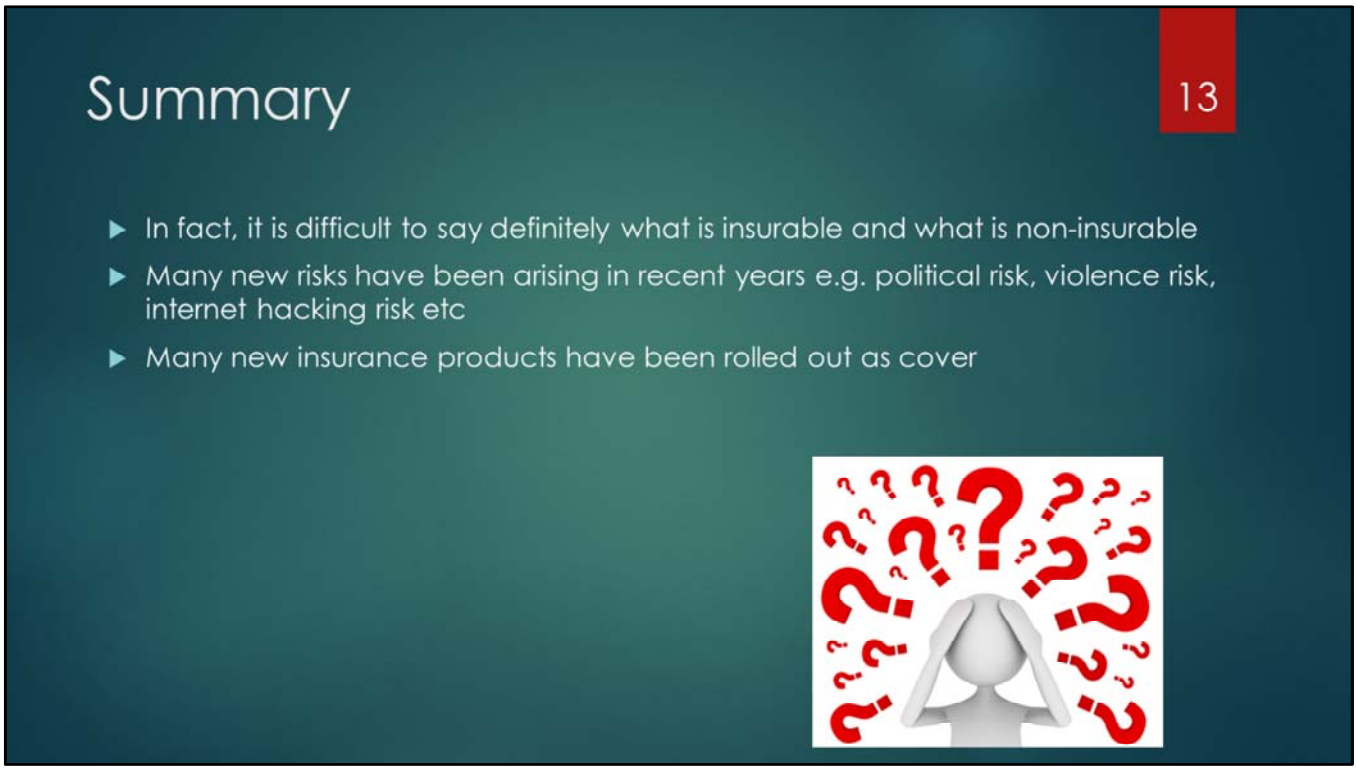
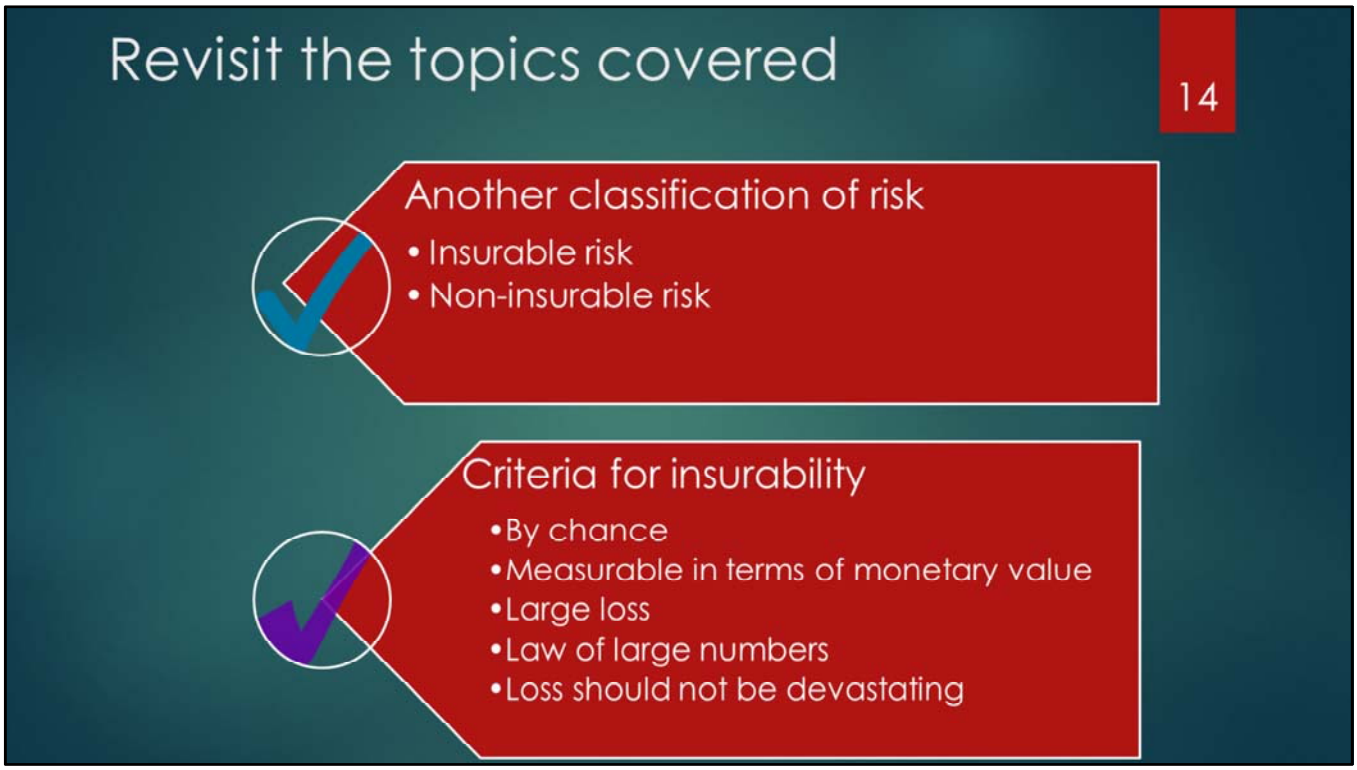
- Recall the introductory case on the cosmetics company
- Do you think the "loss on image" could be insured?

- Students are divided into groups for discussion
- The key would be whether the loss is measurable
- Since it difficult to measure the loss on image arising from the boycott in monetary term, the probability of it got insured would be slim



- It is not easy to determine definitely what risk (pure risk) is insurable or non-insurable since many new risks keep appearing and at the same time many new insurance products are being developed
- Political risk is generally regarded as something very difficult to get insured
- However, new products are developed lately to cover different aspects of political risk e.g. asset seized by new government, default payment due to political disturbance
- Still many other aspects of political risk are not well-covered



- Review all the topics learnt in this lesson
- Another major classification of risk: insurable vs non-insurable risk
- Criteria for insurability and examples

Lesson 3

1

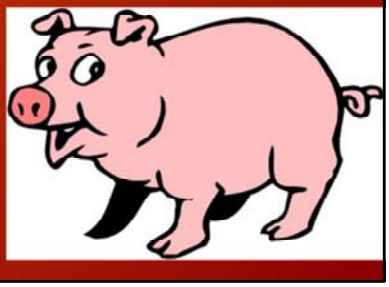
Risk Management Strategy I

- Topic of the lesson
- There are three lessons altogether on the topic of risk management
- This is the first one

Introductory case: Contaminated pig

2

- In August 2016, the government discovered that 319 pigs imported from Jiangxi province were injected anti-asthma drugs and 40 of them had been distributed to the market. The concerned department took immediate action to destroy 3500 kilos of pork and pig. The current practice is that live pigs shipped to Hong Kong will be checked randomly. Once the pigs pass the test they will be auctioned and slaughtered. However, some involved people mentioned that certain pigs could have been auctioned before checking completed owing to time pressure and massive orders for shipments.
- What could have been gone wrong in such case that made the government fail to prevent the contaminated pig from distributing to the market?



- Illustrate the real-life situation shown in the PowerPoint to stimulate students' interest in how risk can be prevented or reduced.
- Ask students to suggest what could have been done wrong for having the contaminated pig being distributed to the public
- Possible causes:
    - People: unable to follow the procedure or negligence
    - Procedure: not following the prescribed procedure, or the procedure is not practical
    - Method: random selection error, or test sample not large enough
    - Equipment: errors in testing equipment

- Explain the topics to be covered in this lesson
- They are:
    - Meaning of risk management
    - Why risk management is important
    - Start exploring some risk management strategy

Meaning of risk Management

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- A rational and systematic approach to reduce and eliminate loss associated with those risks faced by business.
- Risk management objective: determine the best management strategy for certain risk to minimize loss
- Traditionally, primary concern of risk management is pure risk
- Emerging idea of total risk management including speculative and pure risk in recent years

- Emphasize that traditionally risk management focuses on pure risk
- Recently people start talking about total risk management and intend to include speculative risk under the umbellar of risk management, because they think that the delineation between the pure risk and the speculative risk is arbitrary
- Moreover, since a company should try to minimize all kinds of risk it is facing, speculative risks should also be included
- Even so, it should be noted that the job of managing pure risk is very different from that of the speculative one as mentioned in previous lessons, it would be difficult for the same team of people to handle both types of risks

- The task of risk management is to identify and analyze different pure risks involved, and apply different strategies to minimize them
- The objective is to minimize the risk faced by the company and guarantee that the company can still in operation even suffering from the loss associated with the risk

Why risk management?

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- Traditionally risk management = insurance
- Risk not by chance
- Causes of risk can be found and actions can be taken to reduce, prevent or even avoid it
- Risk can be managed ➔ costs of risk can be minimized

- It is a brief history about risk management
- Traditionally people treat risk management as insurance management
- After the Second World War people started to note that risk is not purely by chance
- There are reasons and causes behind different kinds of loss
- Actions can be taken to prevent or at least to reduce the risk
- Though risk cannot possibly be totally eliminated but it is possible to manage it so that the costs can be minimized
- Therefore rational and systematic approach to deal with risk is helpful

- There are four commonly applied risk management strategies, namely:
    - Risk avoidance
    - Risk prevention/reduction
    - Risk transfer
    - Risk assumption/retention
- They can be classified according to different criteria
- Some strategies are aiming at preventing the chance or reducing the severity of the risk before the hazard happens
- These strategies aim on control and would be in the domain of operation management
- Some other strategies are aiming for protecting the company after the hazard taken place
- These strategies concern more on the financial aspect and their major objective is to minimize the loss the company will suffer and guarantee that the company can still survive even after those damages

Overview of Risk Management Strategies

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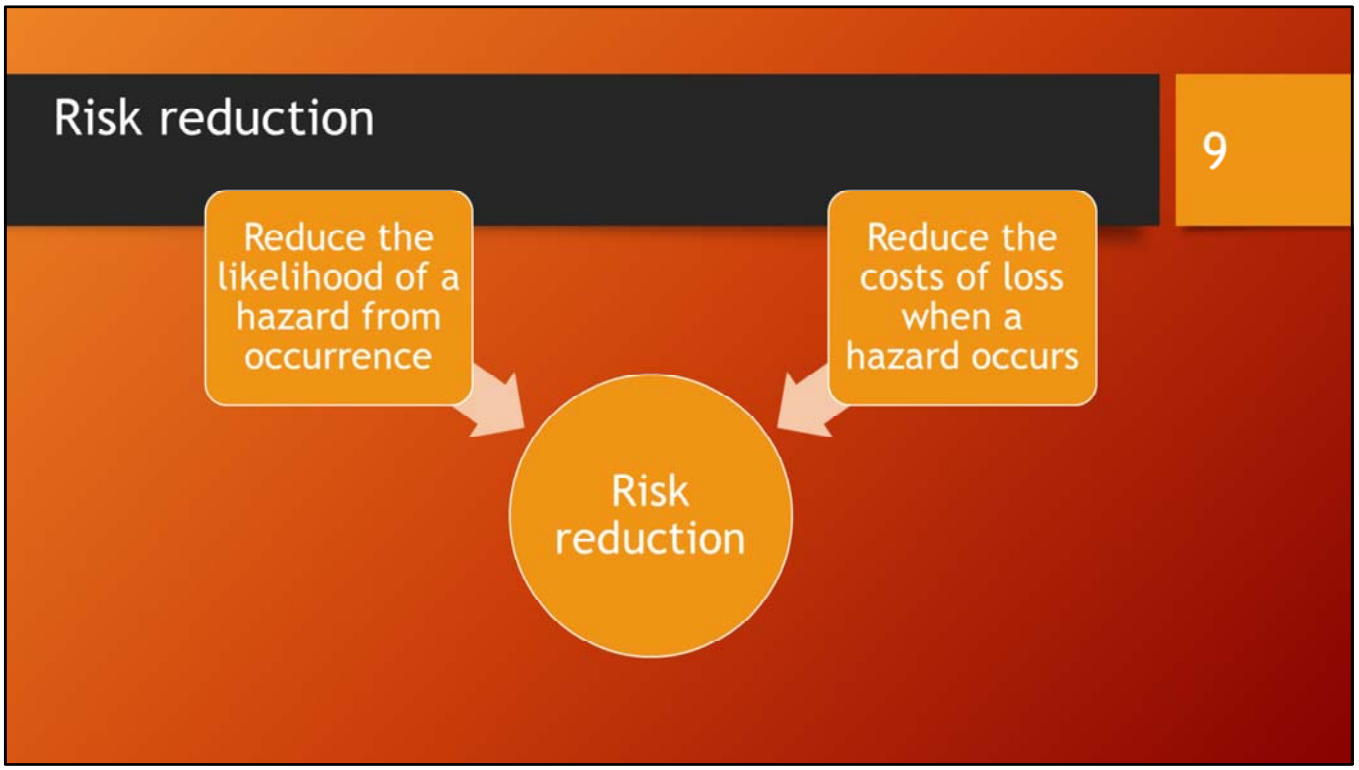
1. Risk avoidance
2. Risk reduction

- measures taken to prevent the chance from happening or to reduce the severity of the loss
- mainly the concern in operation management

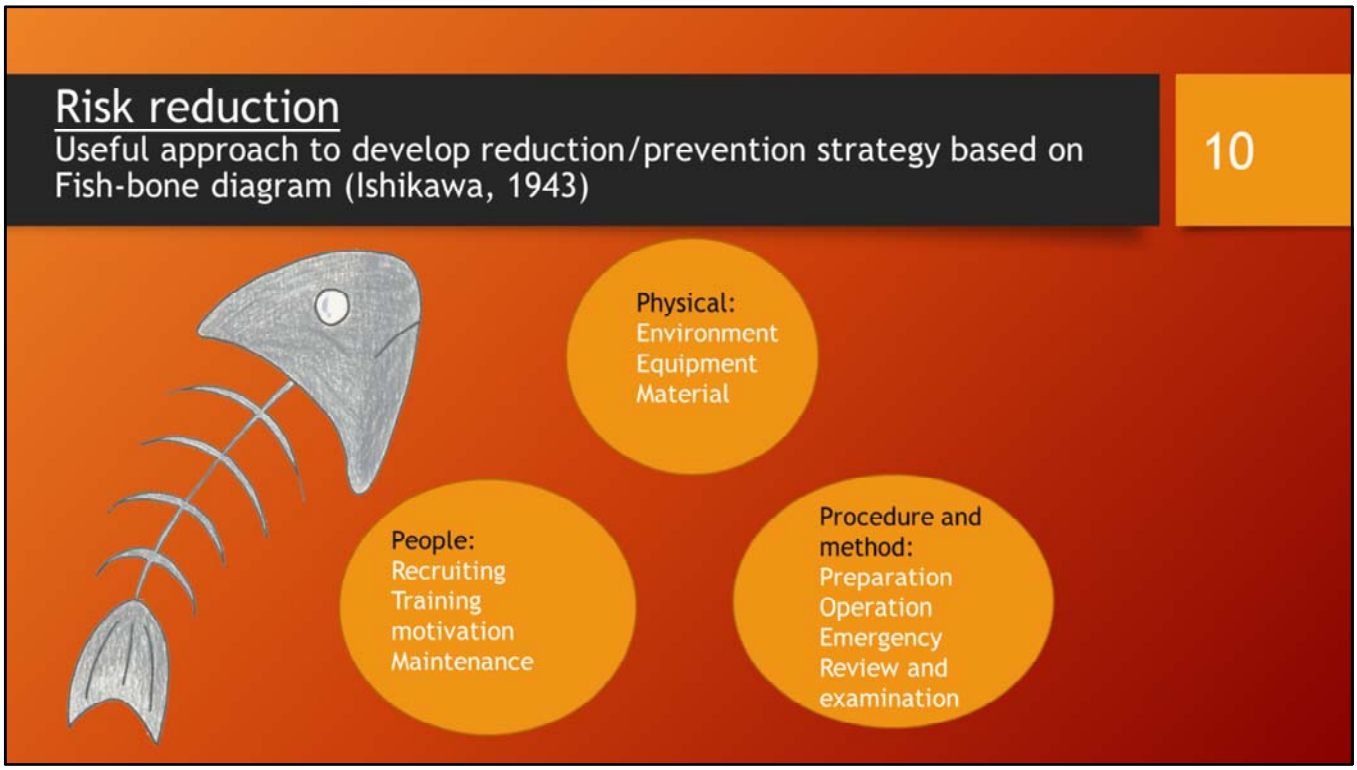
3. Risk transfer
4. Risk assumption

- aim to protect the company after the hazard has taken place
- concern more on the financial aspect
- minimize the financial loss the company will suffer or guarantee the company to continue operation even after the hazard

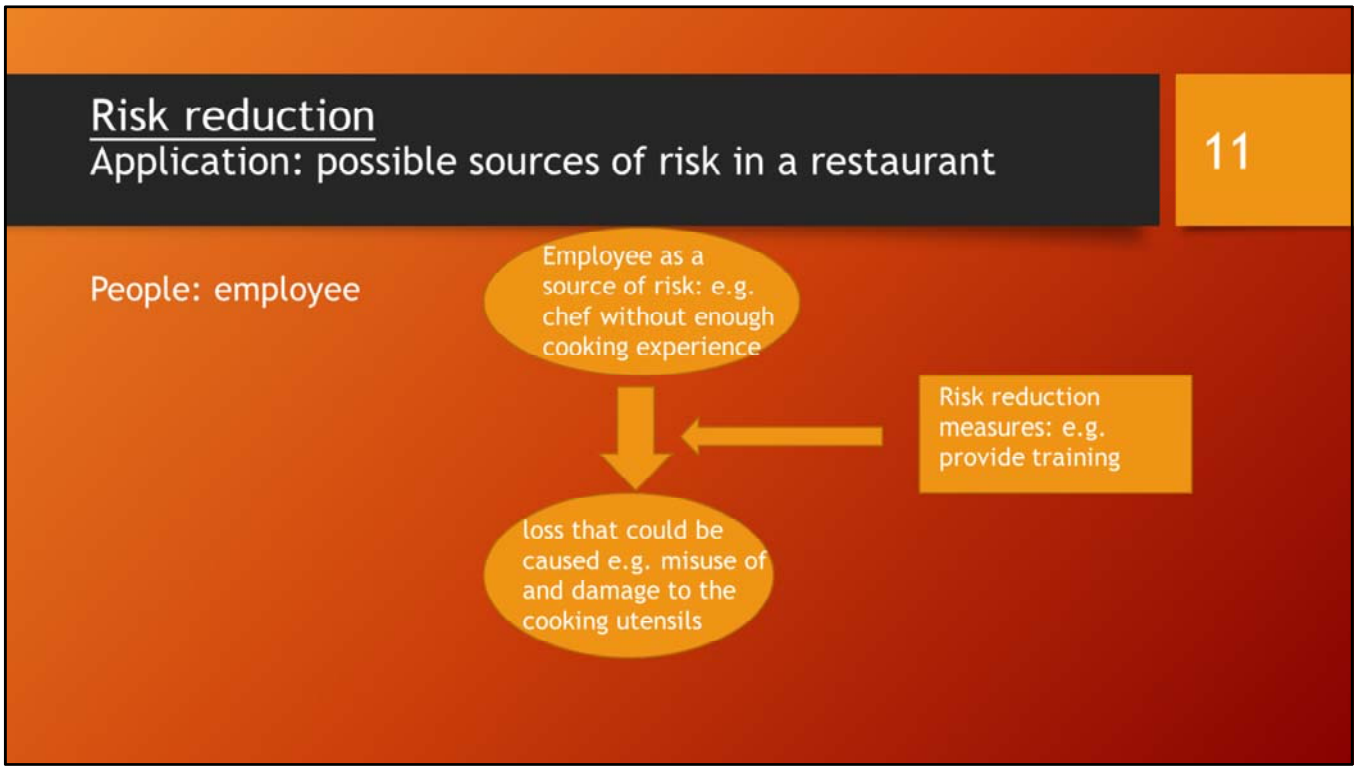
- The risk management strategies can be divided into two types according to their purpose and management functions adopted.



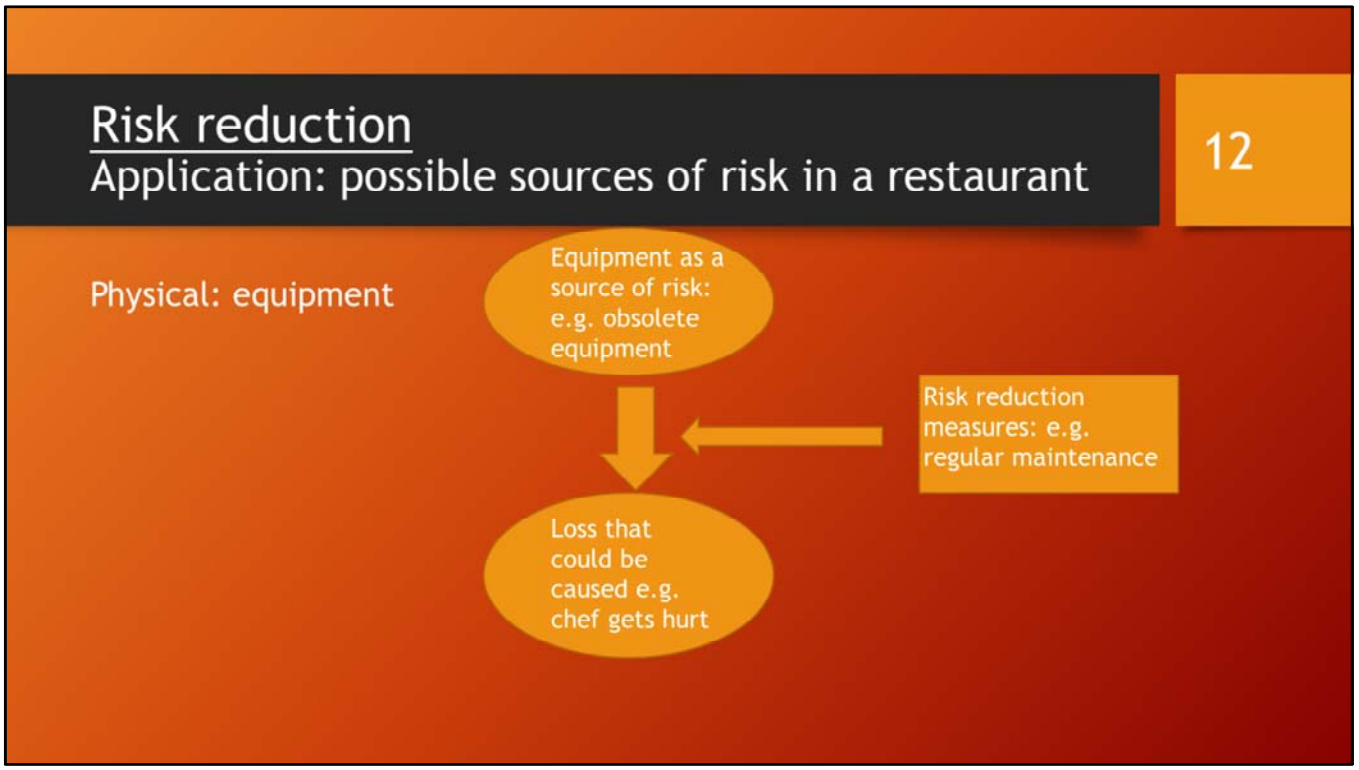
- Risk reduction strategy
- Mainly two major aspects: reduce the chance of happening and reduce the loss when the hazard really takes place
- Some textbooks specifically refer reducing chance of happening as risk prevention while reducing the costs of loss as risk reduction
- Examples of reducing occurrence probability e.g. employing only qualified employee for operating specialized equipment
- Examples of reducing costs of loss when happening e.g. never put all valuable assets together in one place



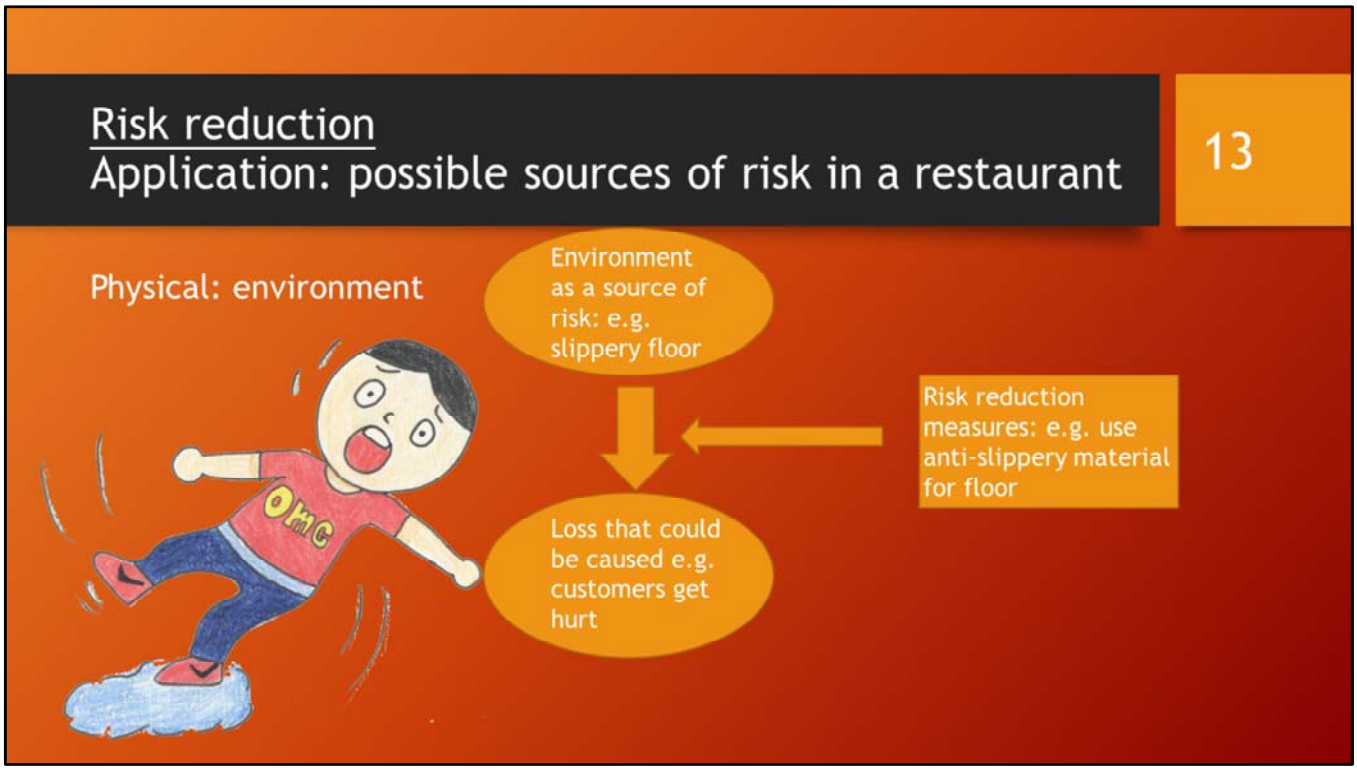
- There are many different areas that a company can work on to prevent or reduce risk
- One of the ways is to follow the fish-bone diagram developed by Ishikawa for locating different major areas in which the prevention/reduction work can take place
- The three common areas for risk reduction are namely physical, people and procedure/method



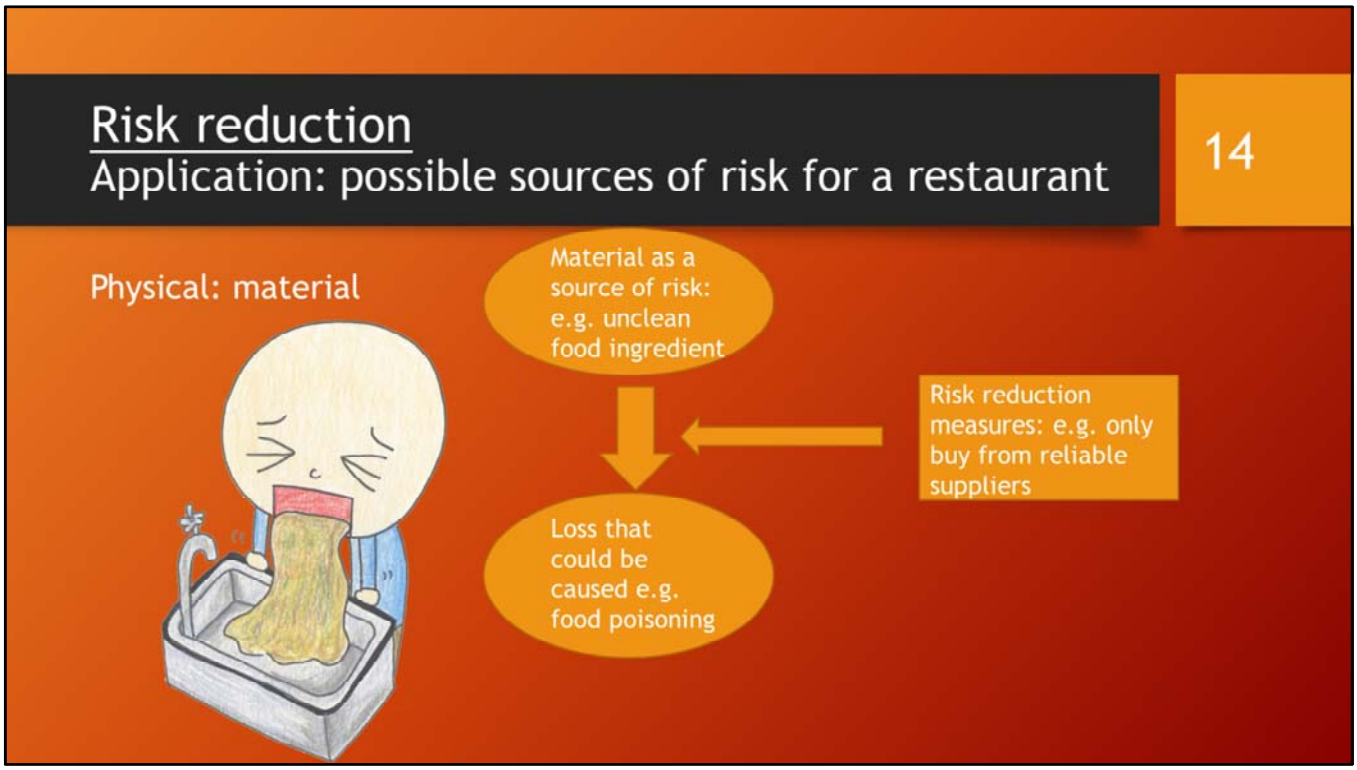
- Using a restaurant as an example to show how people may lead to loss and what measures can be taken to prevent the risk
- Ask students to suggest examples of risk that are caused by people (e.g. avoid customer got hurt by careless waiter) and suggest ways to improve the situation (e.g. looking for a more careful candidate in the recruitment process, or to have a clearer guidelines in serving customers)



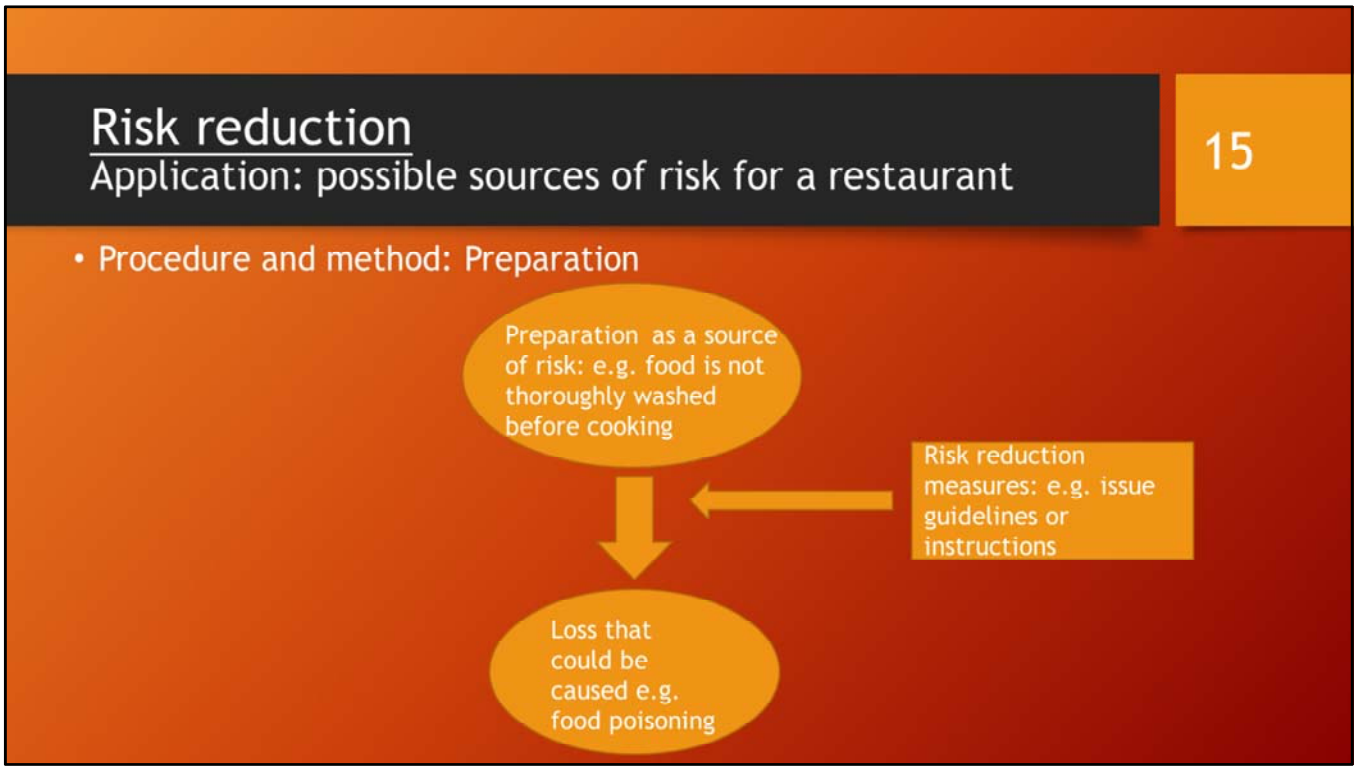
- Using a restaurant to illustrate how equipment can be a source of risk and how such situation can be improved
- Ask students to suggest other example in which equipment can be a source of risk e.g. unsuitable cookware, worn-out table or chair etc
- Suggest ways to improve e.g. have regular checking or replace the broken equipment



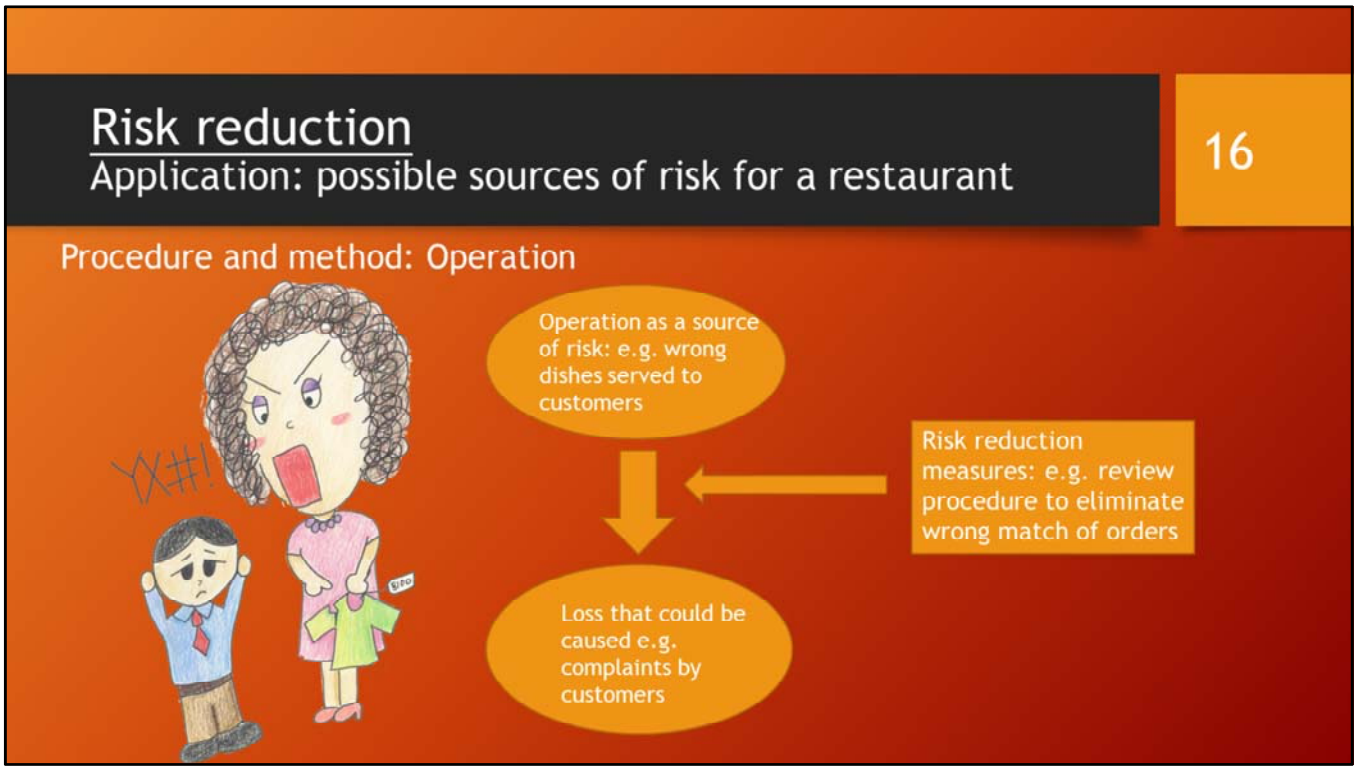
- Using a restaurant as an example to illustrate how environment could be a source of risk and how it can be fixed
- Ask students to suggest other example in which environment can also be a source of risk e.g. dim lighting, dangerous floor layout, noise etc
- Suggest ways to improve e.g. suitable level of lighting, improve floor plan etc



- Based on the case of a restaurant illustrate how material can be a source of risk and how it can be fixed
- Ask students to suggest other possible situations in which material can also be a the source of risk e.g. outdated foodstuff, contaminated foodstuff etc
- Suggest ways to improve e.g. standard procedure in food storage and disposal



- Using a restaurant as an example to illustrate how insufficient preparation can be a source of risk and how it can be fixed
- Ask students to suggest other possible ways through which method can be a source of risk e.g. some cooking method could be dangerous especially for some less skilled employees, ways to deliver dishes
- Suggest ways to improve e.g. change the method or only allow skilled employees to use those methods



- Using restaurant as an example to illustrate how procedure can be a source of risk and how it could be fixed
- Ask students to suggest other cases in which procedure can also be a source of risk e.g. collection procedure on kitchen waste may lead to over-piling of dishes in the same location etc
- Suggest ways to improve e.g. refine the procedure by having another location for storage to avoid over-piling

Some tools to aid the risk reduction

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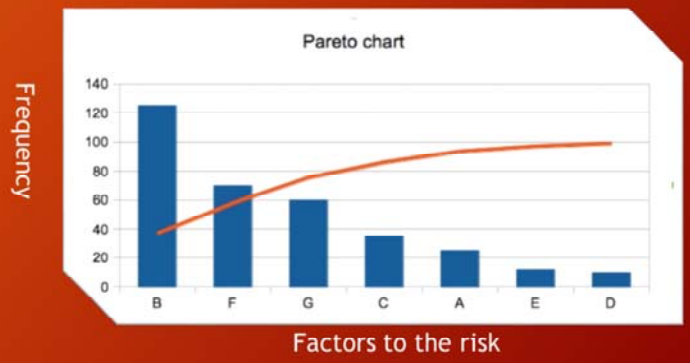
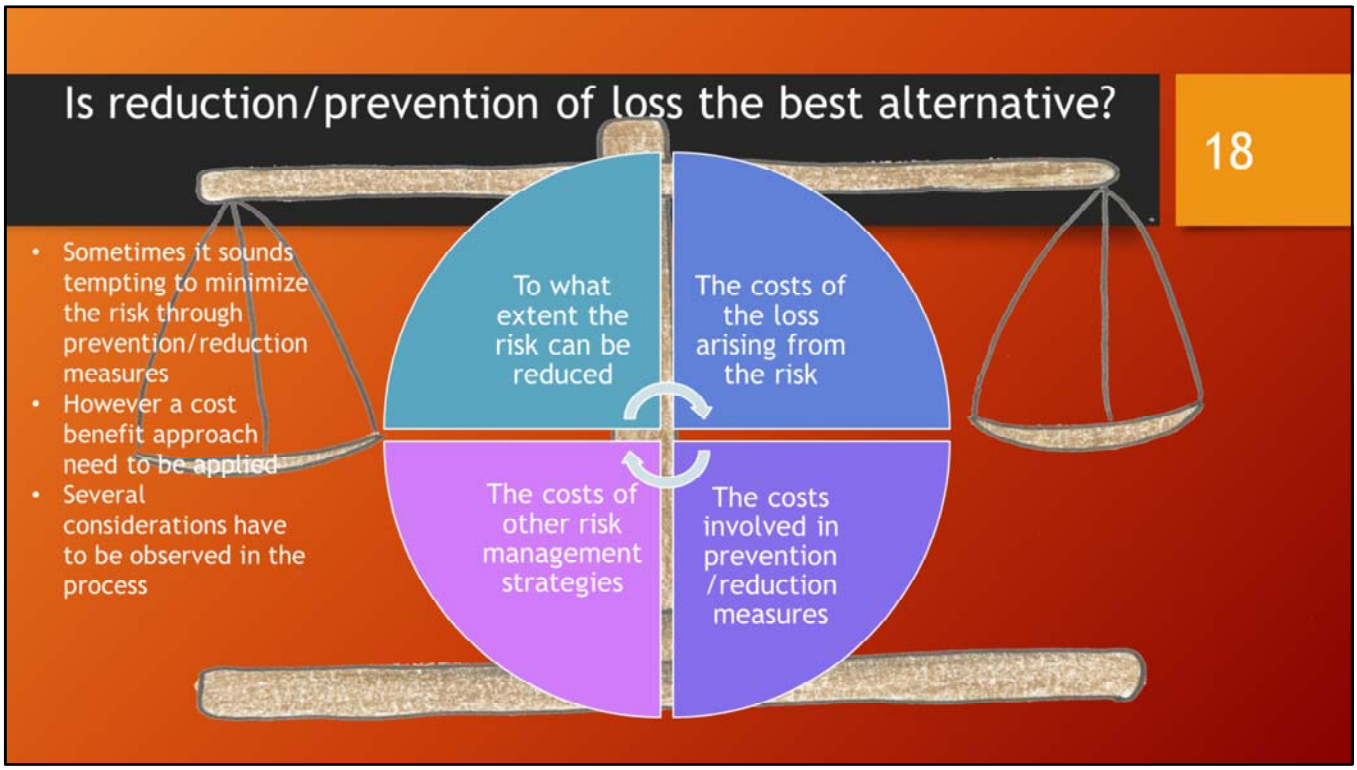
- Pareto analysis
  - Identify the major reasons for the risk through statistical analysis on past incidences
- Emphasizing on strategic risk



- It should be noted that a risk could be due to many different possible causes
- However, some causes are more dominant than the others
- The pareto analysis helps to identify which causes are critical by using statistics to show which type(s) of cause responsible for the highest frequency of the occurrence of loss
- E.g. human error is the most frequent cause leading to accidents in the kitchen, then more training or better recruitment should be applied
- The second important concept is that strategic effort should be directed to risk areas paramount to the success or survival of the organization
- E.g. food safety is one of the most important consideration in operating a restaurant, greater effort should be applied to assess risks in this area and corresponding prevention and reduction measures should be developed



- Sometimes people believe that it would be the best if all the risk can be prevented or reduced beforehand
- In fact, we should apply a cost benefit analysis in this aspect
- Several factors need to be considered:
    - The costs of loss if no prevention/reduction measures taken
    - The costs of prevention/reduction measures
    - The costs of other management strategies
    - The costs that could be reduced after applying the prevention/reduction measures

- Revisit all the topics covered
- Review the concepts and main points mentioned in previous PowerPoint

Lesson 4

1

Risk Management Strategies II

- Mention that it is the continuation of the last lesson that the other 3 risk management strategies would be introduced

Introductory case: The Cyber Attack

2

- Cyber attack has become very serious and severe nowadays. Some case was that the hackers invaded the company's system and disguised as the top management issuing instructions to subordinates making transactions to other bank accounts through email. Many people who didn't double check fell as victims. The head of the Hong Kong Monetary Authority warned about the issues particularly on the security measures taken by the banks. He cited that there were 5000 cyber attacks recorded and many of them were done through the smart phone in 2015. Altogether, these cyber crimes had costed HK$1.8 billion for that year. The situation would be even worse since smart phone has become a necessity to people and that provides a very good leeway for hackers. IT experts had warned people changing their using habits of smart phone.
- Looking into the future it is quite sure that anything that can be connected to internet would become targets of hackers.
- Question: Apart from adopting risk reduction strategy, how could the risk from such be managed?

- Ask students what are the potential risks caused by cyber attacks and what could be the losses
- Discuss with students how can these be managed
- Prevention and reduction is a normal strategy
- However, it seems not possible to eliminate all the risk
- Thus, what other risk management strategies can be applied
- Introduce the content of the next PowerPoint slide

Topics to be covered

3

- Risk avoidance
- Risk assumption
- Risk transfer

Risk avoidance

4

- Eliminate the chance of hazard arising from the risk
- Passive approach
- Last choice after exhausting all other possible options
- May not be practical and feasible especially when the company is already in business

- The second risk management strategy is risk avoidance
- Need to emphasize that it is a passive approach since taking risk is one of the condition for doing business
- It is commonly known that risk is proportional to return
- Therefore this risk management strategy should only be the choice if there is no other acceptable way to reduce risk and that the risk is too much for the company

Risk avoidance

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Examples:

- Not doing business in certain countries or districts so that some particular risks in those regions can be avoided e.g. political or regulation risk
- Not getting into certain industry or trade so that certain risks associated with those industry or trade can be avoided e.g. No manufacturing business to avoid industrial related risks
- Not pursuing certain business initiatives e.g. do not develop new product to avoid the risk of product failure

- Illustrate different examples of avoidance strategy
- Ask students to raise other examples of avoidance

The risk management strategies in preparing financing in case of loss incurred

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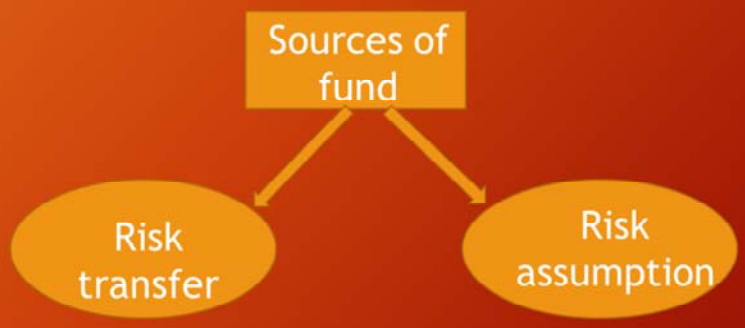
- A business need to prepare enough fund for the loss incurred from the risk so that it can go on to continue its operations even after suffering from the damage



- The other two risk management strategies emphasize on how to deal with the loss after the damage has occurred
- There could be two ways to prepare for such unwanted situation, one is to having risk transferred to a third party, and the other is to assume the risk by the company itself. In both cases, the objective of the strategies is to enable the company to keep operating even after the damage has happened
- In short,
    - Risk transfer: some other party will take the whole or part of the loss through some prior arrangements
    - Risk assumption: company/organization/individual will take all the loss

Risk transfer

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- It is the transfer of risk to another party so that the loss incurred will be borne by another party
- Normally the transfer would be specified in the form of a contract and the loss to be indemnified would be subject to certain limit spelt out beforehand.

Ways of risk transfer
- Insurance
- Subcontract
- Contract specification

- The third risk management strategy is risk transfer
- A very common way of risk transfer is through insurance
- Other ways include shifting certain activities to other party so that the risk will be borne by another party e.g. subcontract the transportation function so that all risks related to transportation can be shifted, or agreeing with suppliers that the product or parts will not be delivered until the last moment so that all the risks related to storage will be shifted to the suppliers.
- Sometimes, the firm may shift the financial burden to another party by contract e.g. Having a term in the contract that the buyer has to bear all the losses arising from the damages of a product upon delivery

Risk transfer

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- Insurance is a very common way of transferring risk so that once the loss occurs the company can get the compensation from the insurance company
- However, insurance also has costs, a company should carefully consider the costs of insurance against the potential loss from the risk before taking the insurance

- Of course, when thinking about taking insurance the risk should be insurable and that is why knowing what is insurable and what is non-insurable is very important
- Also, insurance is not a must though it is a common strategy used to deal with risk, a cost benefit analysis is important when considering taking out insurance against certain risk

Risk assumption

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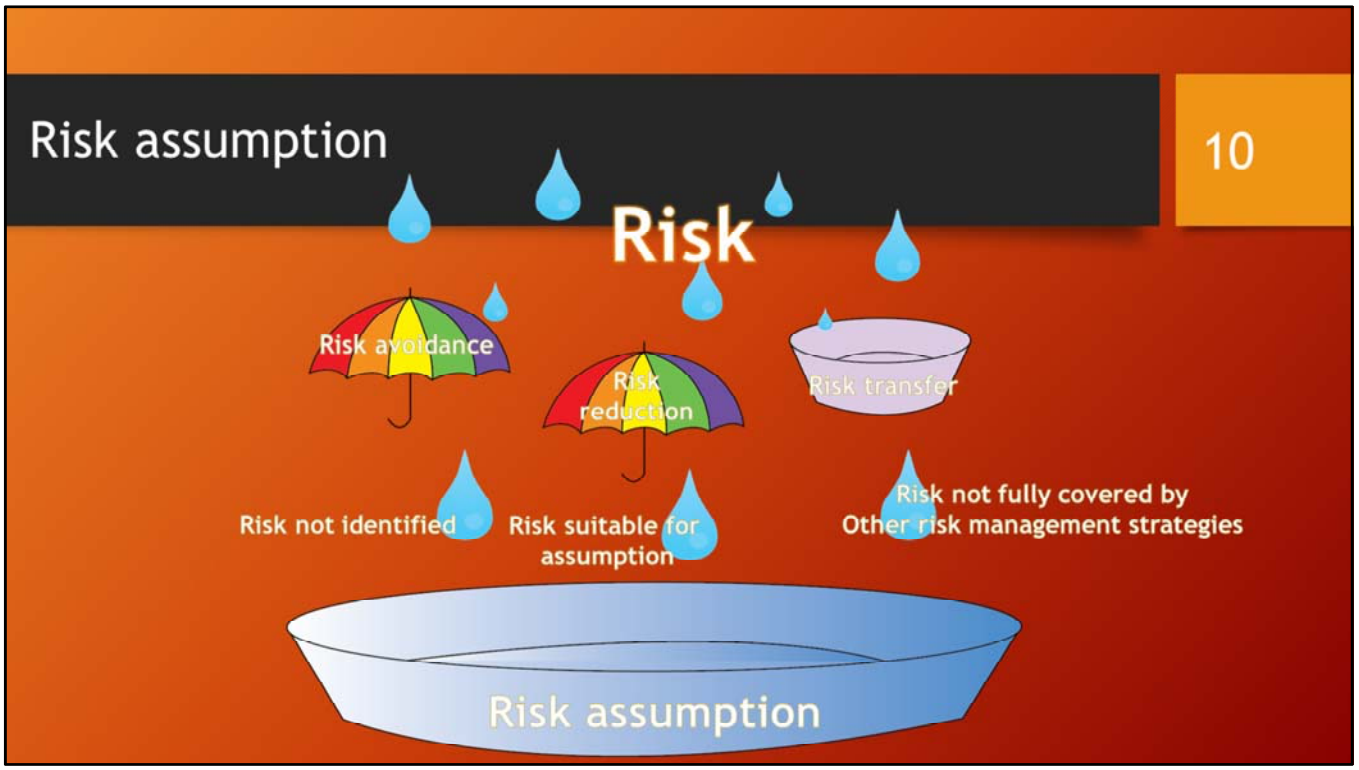
- It is the strategy that the company will bear all the losses arising from the risk
- It is one of the most common risk management strategies

Examples:

- loss of stationeries in the office will normally be borne by the company
- Loss owing to change in government policy is always difficult to avoid, prevent/reduce or transfer, and thus would be borne by the company

- The above is the forth risk management strategy



- No matter how the loss could be dealt with by the other risk management strategies, the remaining loss (if any) will be left to the business itself
- Risk assumption is actually a very common risk management strategy because for most of the time, risk avoidance may not be practical particularly for business which is already in operation; and the risk prevention and reduction measures fail to remove all the risks
- There are also limitations to risk transfer in many cases e.g. some risks even pure are non-insurable
- Many risks actually exist but are unrecognized by business,
- All of these risks would fall onto the business in the end
- It should be noted that the diagram is just to show that risk assumption is always the residual strategy but it does not mean that it is the procedure or steps that risk management should go through in choosing the suitable risk management strategy

Risk assumption

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- It is not the strategy to be used as the last resort, rather it suggests that when no other method is suitable, risk assumption method will be applied
- However, in case other options are also applicable it doesn't mean risk assumption method will not be adopted
- The decision rule is: Cost/benefit analysis
- For example, if insurance is possible but the premium cost is too high relative to the costs involved when self assumption method is used, then risk assumption method will be adopted.

- We need to go through a cost benefit analysis to determine which risk management strategy is more appropriate
- Sometimes, for some risks we may find insurance too expensive even it is available (e.g. insurance on political risk in some unstable countries)
- For some very large corporations such as large international retail chains, they can apply self-insurance, i.e. set aside some funds for any potential loss that occurred to its branches. The fund can earn interest when no loss occurs. It is just similar to the case of an insurance company

Risk assumption

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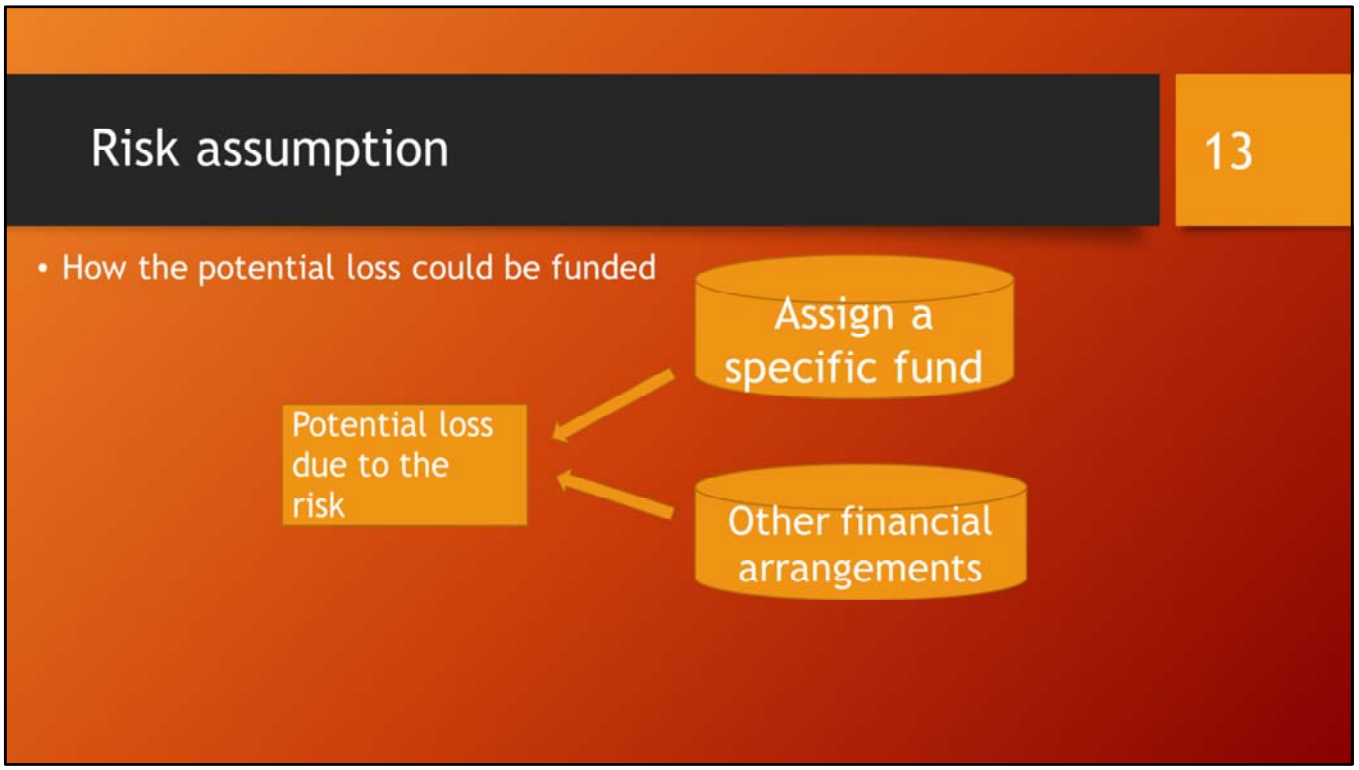
Points to note:

- ✓Risk assumption could happen consciously or unconsciously
- ✓Consciously – choose the best alternative after evaluating different risk management strategies
- ✓Unconsciously – not aware of the potential risk or planned to be covered by other strategies but fail to materialize in practice
- ✓If the risk assumption method is applied under unconscious situation the company could be in big trouble since the risk and its potential costs are not well anticipated beforehand and thus the company will be caught totally unprepared

- The risk management should try the best to avoid unintentional risk assumption



- Generally there are two ways to apply risk assumption strategy
- Assign a specific fund could be an emergency fund for covering some loss caused by some specific risks, or contribute yearly to build up a reserve fund which is interest bearing for the purpose of covering some specific risk (self-insurance)
- Other financial arrangement could be creating an insurance company by the firm itself for not only covering the firm's own risk but also other businesses' risks; or treating the potential loss as part of the running costs or expenses of the business
- For large corporations particularly those with large cash reserves, risk assumption could be a good option
- For small company which is short in cash, being totally uncovered could be a disaster

Risk assumption
- other financial arrangements

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Self-insurance: contribute yearly to build up a reserve fund which is interest bearing for the purpose of covering losses from some specific risks

Self-created insurance company: creating an insurance company by the firm itself for not only covering the firm's own risk but also other businesses' risks

Assumed as running costs/expenses: treating the potential loss as part of the running costs or expenses

- For self-insurance or creating a insurance company by the firm itself, it would be only applicable to large corporations especially those with strong financial supports.
- The feasibility of assuming the losses of risk as part of the running costs depends on the nature of the risk.
- For some insignificant losses such as loss of stationeries in office, many firms can adopt such strategy. However, if the loss is expected to be large, the company needs to be careful.

Recall: Cyber Attack Case

15

- What risk transfer and risk assumption strategies could be adopted to deal with the cyber attacks?

- Discuss with students on the possible methods under each risk management strategy e.g. transfer: through insurance or outsource the whole section of IT to third party and make agreement that the outside party will bear all the risks
- After all if the above measures are not quite feasible the company may need to bear the risk by itself

Combination of risk management strategies

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- Basically it is not quite possible for a business to apply a single risk management strategy to deal with risks
- Combined strategies are needed

- In fact, normally companies will adopt combination of risk management strategies to deal with the risks they are facing
- Ask students why it is basically not quite possible to apply a single risk management strategy

Combination of risk management strategies

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- For risk avoidance, it seems that if the risk has been avoided no other strategies will be needed
- However, avoidance is not quite feasible in many cases unless the company wants to be out of business, risk is the fact of life for business
- If only risk assumption strategy is applied the costs could be huge if there is no prevention and reduction strategies adopted as backup, also when extreme case happens the costs might be too high for even a large corporation to bear
- A company also cannot rely solely on insurance without the consideration of the prevention/reduction strategy. If so, the premium costs would be sky high and the company may find it difficult to get insured, also some risks are actually non-insurable
- Lastly, it is very difficult to have just prevention/reduction strategy since there is no guarantee that all risks can be prevented, also extreme measures taken to prevent or reduce the risk would mean very high costs too, so other risk management strategies e.g. risk transfer as supplement might be needed

- Review the concepts covered in this lesson with special attention to the following points:
- Strategies preparing for what would happen – refers to those strategies mainly on financing the losses that could arise
- Risk transfer: need to know the meaning of risk transfer and by what ways that the risk can be shifted, lastly some considerations that need to be taken when taking out the insurance
- Risk assumption: need to know its meaning, what are the ways that could be used for absorbing the risk and under what conditions that such strategy would be more appropriate
- Lastly, it should be emphasized that usually a combination of strategies will be adopted to deal with company risks

Lesson 5

1

The Risk Management Process

Introductory case: Convenience store robbery

2

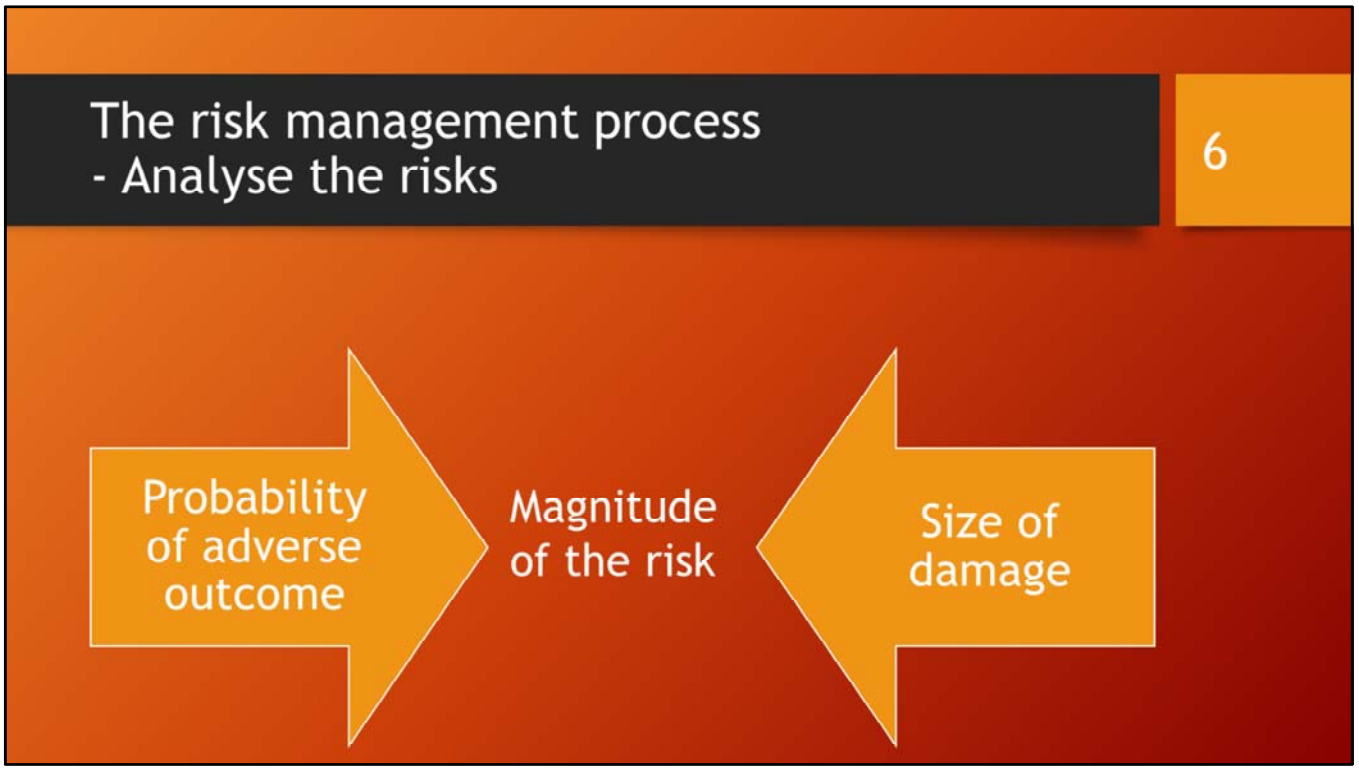
- Convenience stores have recently become a highly vulnerable target of robbery. There were 3 attacks within one single month. According to the news, two common characteristics have been identified among all these robberies. The incidence happened mostly after mid-night when there were a few customers. Secondly, the robbers mainly targeted female cashiers. In these cases, it was quite often that the robbers just took away the money from the cash register. However, there was a case in which the robber stabbed the store keeper who died later. Apart from robberies, it is also very common to have shoplifting in those stores.
- How should the convenience store design its risk management plan in response to the above?

- Explain the case and ask students to discuss on how the convenience store can design its risk management strategies
- First, students need to identify the risks that convenience store has to face from robbery and shoplifting
- Then, try to analyse the seriousness of the risks as follows
- Shoplifting always happen but not severe
- Robbery has become common but the loss of money is not too much
- However, the loss of life is a very serious one although it is less frequent
- Students can then try to figure out what strategy(ies) would be appropriate for each of the above risk(s).
- For shoplifting, risk assumption would be better since the loss tends to be minor, it may not be insurable. Also, prevention/reduction can be applied as supplementary strategies to reduce the frequency of occurrence.
- Life loss is very severe but should not be frequent, may be insurance is better, of course prevention/reduction strategies such as training of storekeeper would be helpful

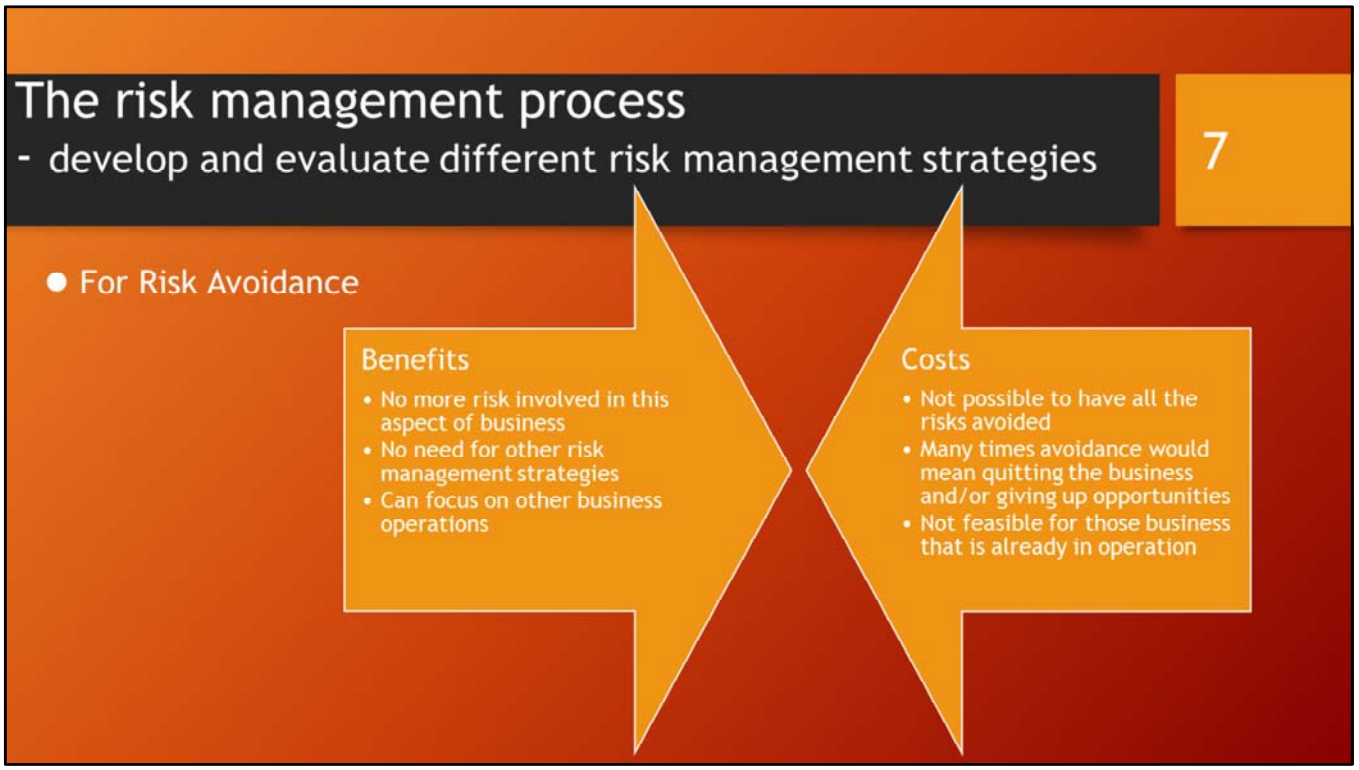
- The process of risk management:
- First, to identify possible risks, since different companies have their own operation process and different business environment, they need to identify their own risks, among those in common.
- Then the risk need to be analysed to find out how serious they are
- After that, different risk strategies will be developed (i.e. the four strategies covered in previous lessons) and their benefits and costs will be considered
- Risk management strategies will be chosen according to the different risks and their situations faced by the company
- Strategies will then be implemented, and after certain period of time evaluation will need to be conducted
- The whole process will repeat again in view of new situations faced by the company over time

- The first step is to identify the risks involved
- The check list provided can help to find out the kinds of risks that a company may face, yet, the items are just examples and should be far from exhaustive
- Ask students to raise examples according to the check list by specifying a context e.g. a fast food shop. Examples are as follows:
- Employee health would affect the business of the restaurant
- Direct loss: refers to damage to the premise e.g. fire in the kitchen
- Indirect loss: refers to something like disruption of business e.g. no business after the restaurant is destroyed by fire
- Liability refer to risks causing losses to other party due to the fast food shop's negligence e.g. unsafe food, slippery floor etc
- Teacher may try other example such as hotel, fitness center etc

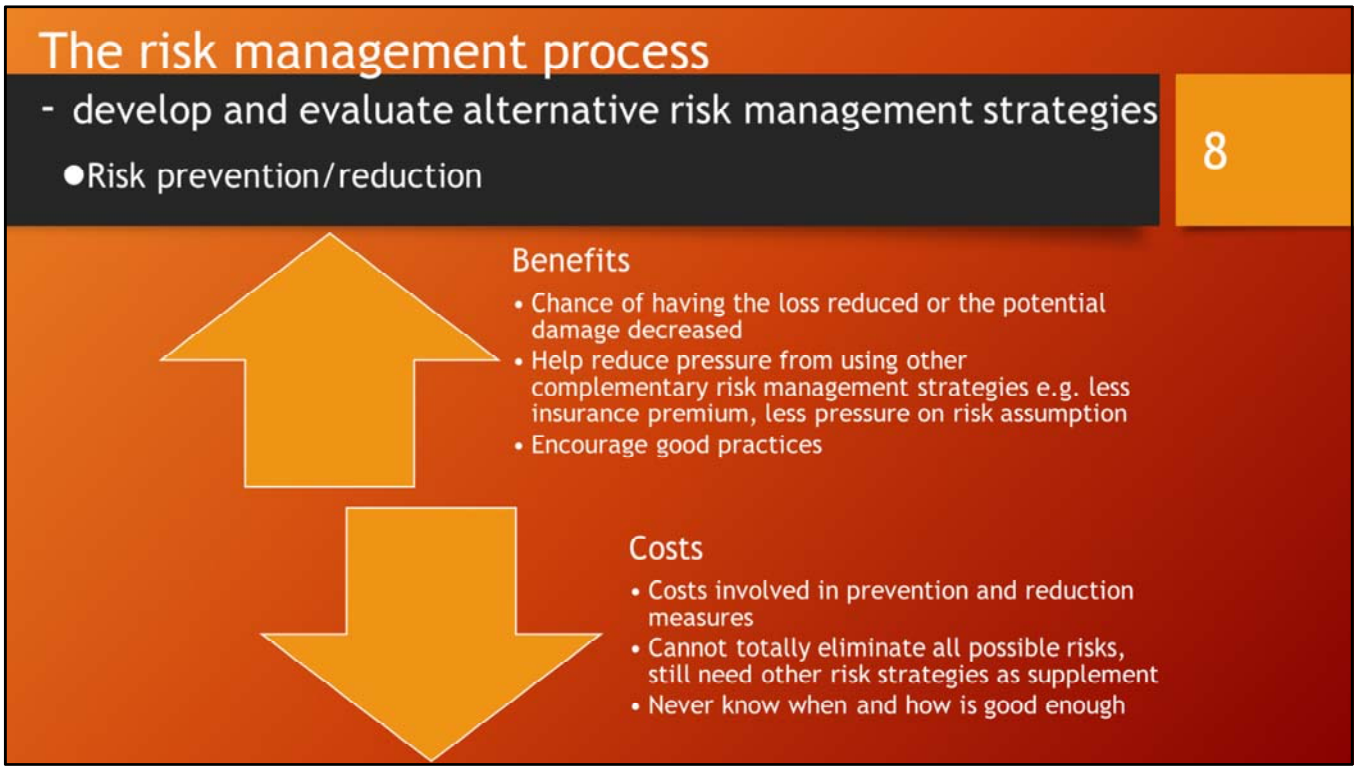
- Some tools can be used to help identify the possible risks faced by the company
- Going through the whole operation process is good since different company may have different operating process and thus would be exposed to different kinds of risk that may not be similar to other company even in the same trade
- Insurance policy checklist is helpful since it includes many possible risks, yet, the company should also beware of some risks that are specific to its business
- In such case, questionnaire can be developed for risk finding



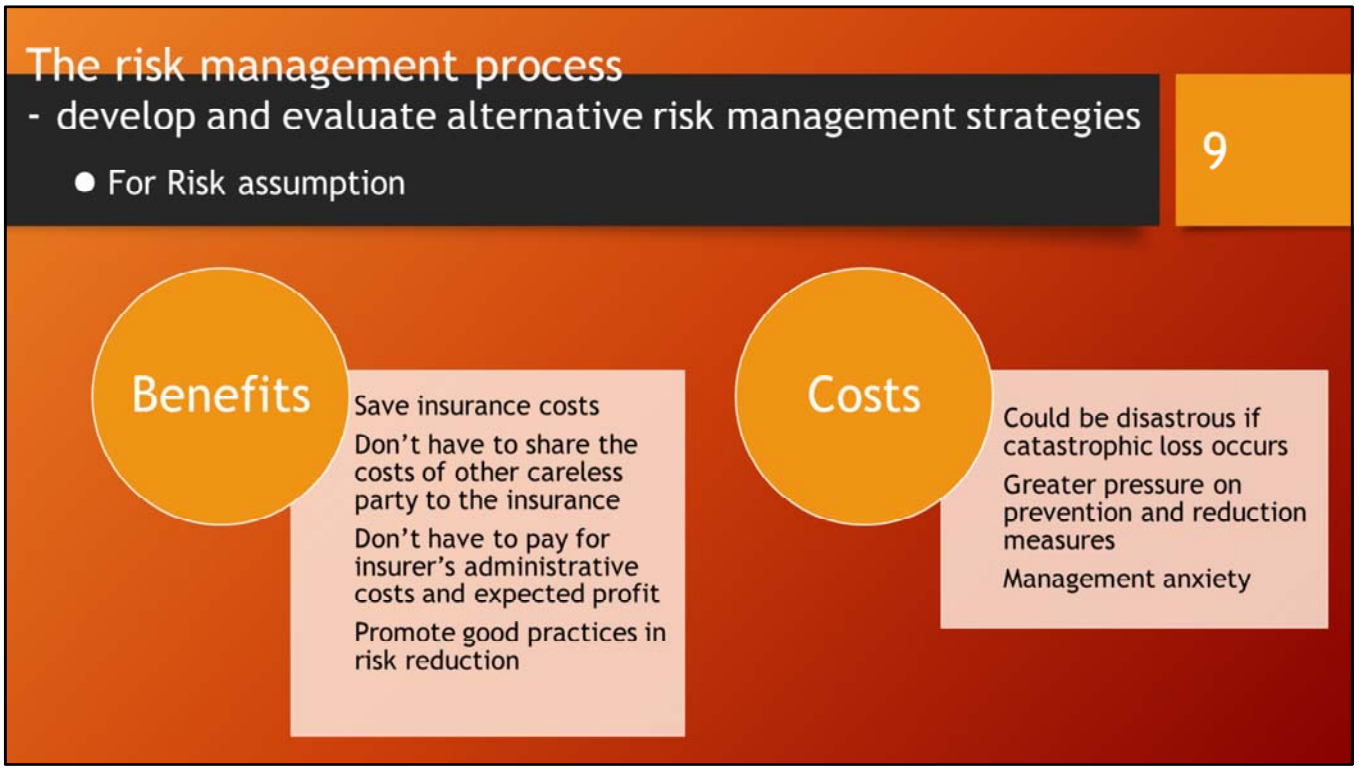
- After identifying the risks faced by a company, the severity of these risks should be assessed for designing corresponding risk management strategies
- The analysis should emphasize on how frequent that the loss would occur and the size of the loss would possibly be incurred
- Normally we will go for the largest possible loss in the estimation



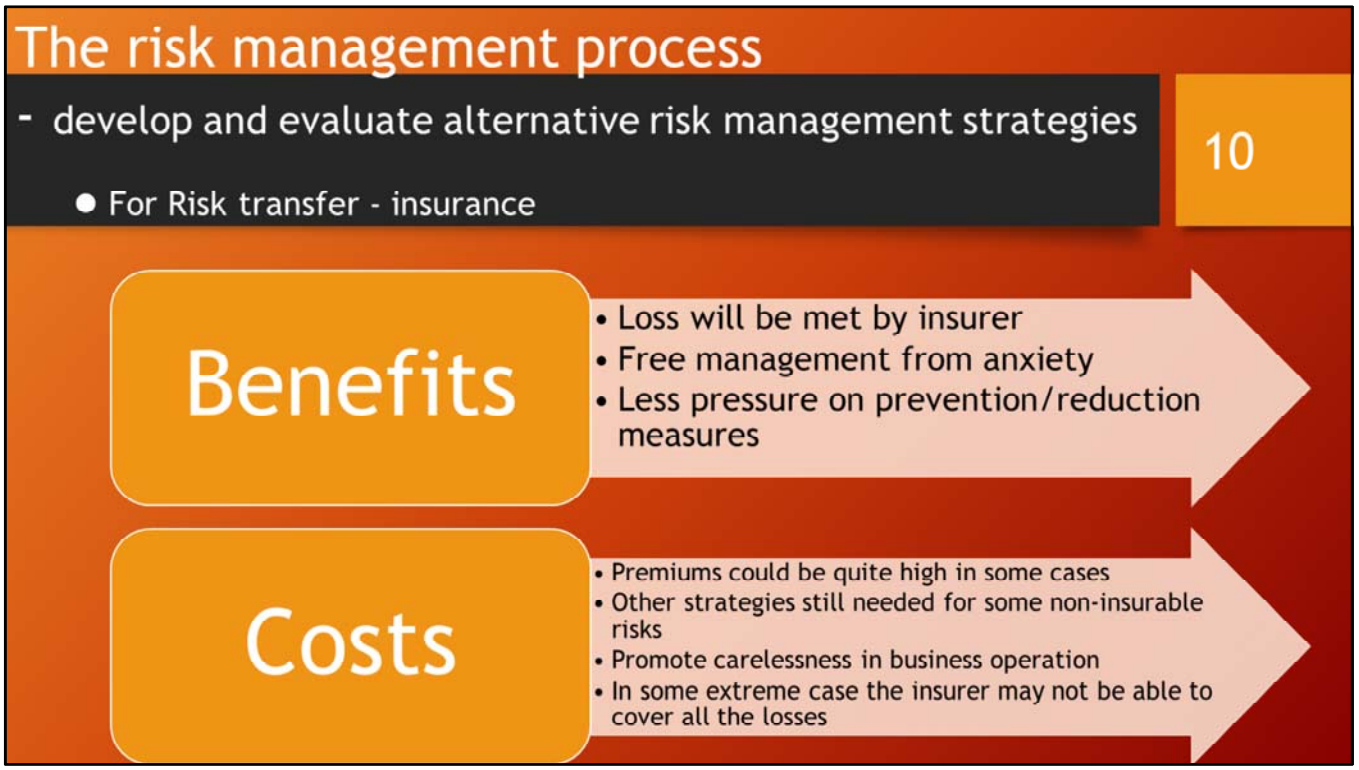
- We need to find out what strategy is good for which kind of risk
- The four risk management strategies mentioned before have their benefits and costs
- In developing the risk management plan, different risk management strategies should be evaluated thoroughly with respective to their costs and benefits
- For risk avoidance:
- Benefits:
    - the company can be free from any risk associated from that particular type of business when avoidance strategy has been applied e.g. no political risk will be involved if the company avoid doing business in politically unstable places
    - No other strategies will be needed as all risks have been avoided
    - Then the company can focus on other aspects of the business e.g. strengthening their businesses in politically stable countries or places
- Costs:
    - In reality it is not possible to avoid all risks e.g. even in politically stable place there still could be political risks
    - When the risk is avoided it would mean quitting the business or giving up opportunities
    - Sometimes it is not possible to quit some areas or aspect of business if the company has been already operating in those areas or aspects



- For risk prevention/reduction strategy
- Benefits:
    - Help to reduce the chance and size of the loss
    - Good prevention/reduction measure can help reduce insurance premium or less burden for risk assumption
    - It helps to develop a good culture on preventing and reducing risks
- Costs:
    - It could be quite costly when implementing prevention and reduction measures e.g. equipment, environment and people
    - Since it is impossible to eliminate all possible risks just through prevention and reduction measures. Other strategies are still needed and costs would be invloved
    - There is always room to improve, thus it is hard to say when and how is good enough

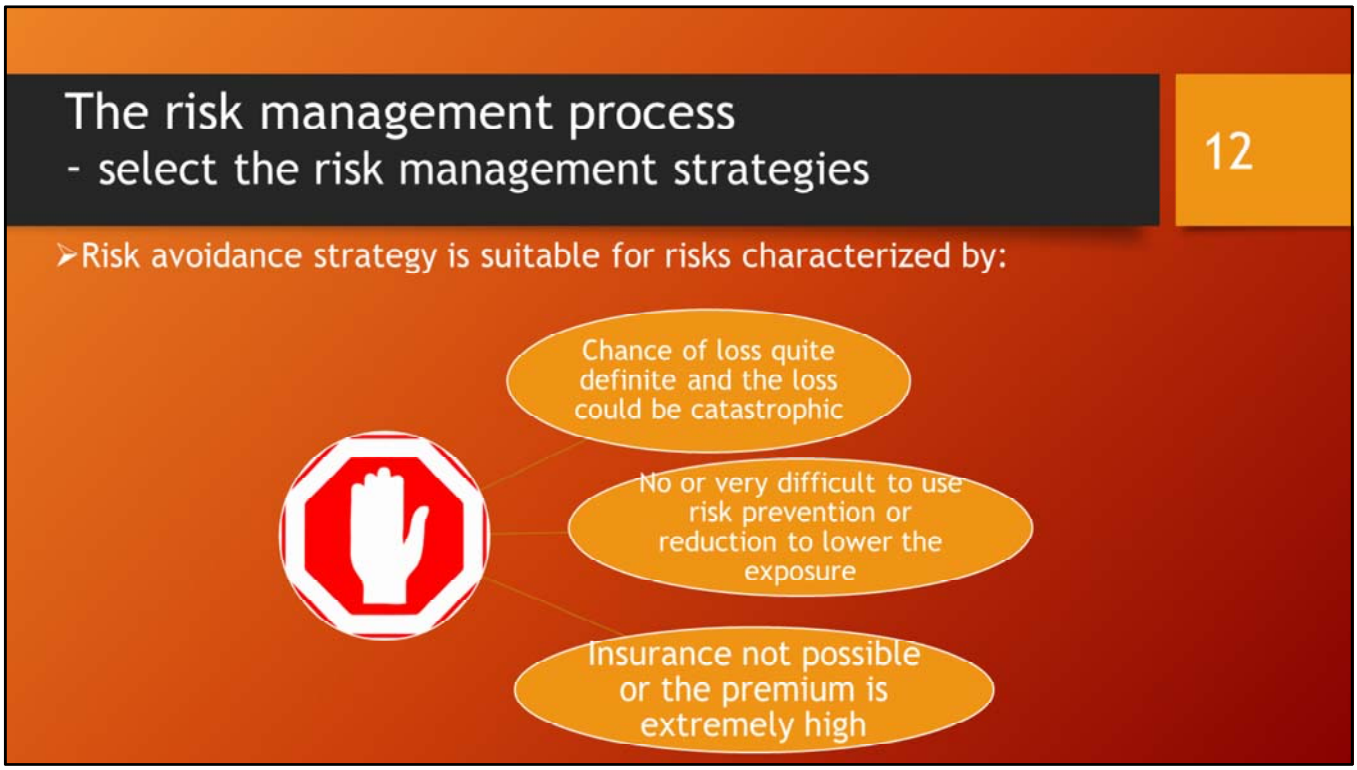


- For risk assumption strategy:
- -Benefits:
    - No need to pay for the premium
    - Since insurance is based on large number of insured parties spreading the risk the premium is based on the general coverage. Once there is any careless insured party committing error and leading to huge losses the premium could be increased and the other decent parties will be unduly affected
    - Premium also includes insurer's administrative costs and their expected profit and therefore would be higher than the costs of self-insurance maintained by the involved company itself
    - Company would emphasize on good practices for preventing and reducing the chance of loss if risk assumption is applied
- Costs:
    - It is hard to say, sometimes there could be catastrophic loss and the company has to bear without coverage from insurance company
    - Prevention and reduction measures would be under greater pressure and more costs will be involved to safeguard any possible loss
    - The company might be troubled by the uncovered risky position and that might affect other strategic decisions



- For using risk transfer (insurance) strategy:
- Benefits:
    - Loss will be covered
    - Company would be free and can have greater motive to pursue more challenging objectives and opportunities
    - No great pressure on strict risk prevention and reduction measure
- Costs:
    - Premium costs could be high especially when some disasters had just happened
    - Some risks could be non-insurable and still need to be taken care of
    - People tend to be careless and pay less attention to prevention and reduction of the possible loss
    - It is still a possibility that the insurer may not be able to pay off especially when the loss is sky-high

- For risk transfer strategy:
- Benefits:
    - No premium is needed
    - Sometimes it is less costly to shift the activity that the company is not familiar with to subcontractor. It is because the subcontractor who is specialized in doing that kind of activity can do the same job at a much lower costs
    - No worry on this aspect of business and the firm can be freed to focus on its major domain
- Costs:
    - Some earning will be shifted to sub-contractors, or the party who bear the financial burden
    - The sub-contactor or the contracted party may default when loss really occurs, the final burden could be still on the company itself
    - Costs would be involved to search, negotiate, and monitor the contracted party for taking up the risk from the company

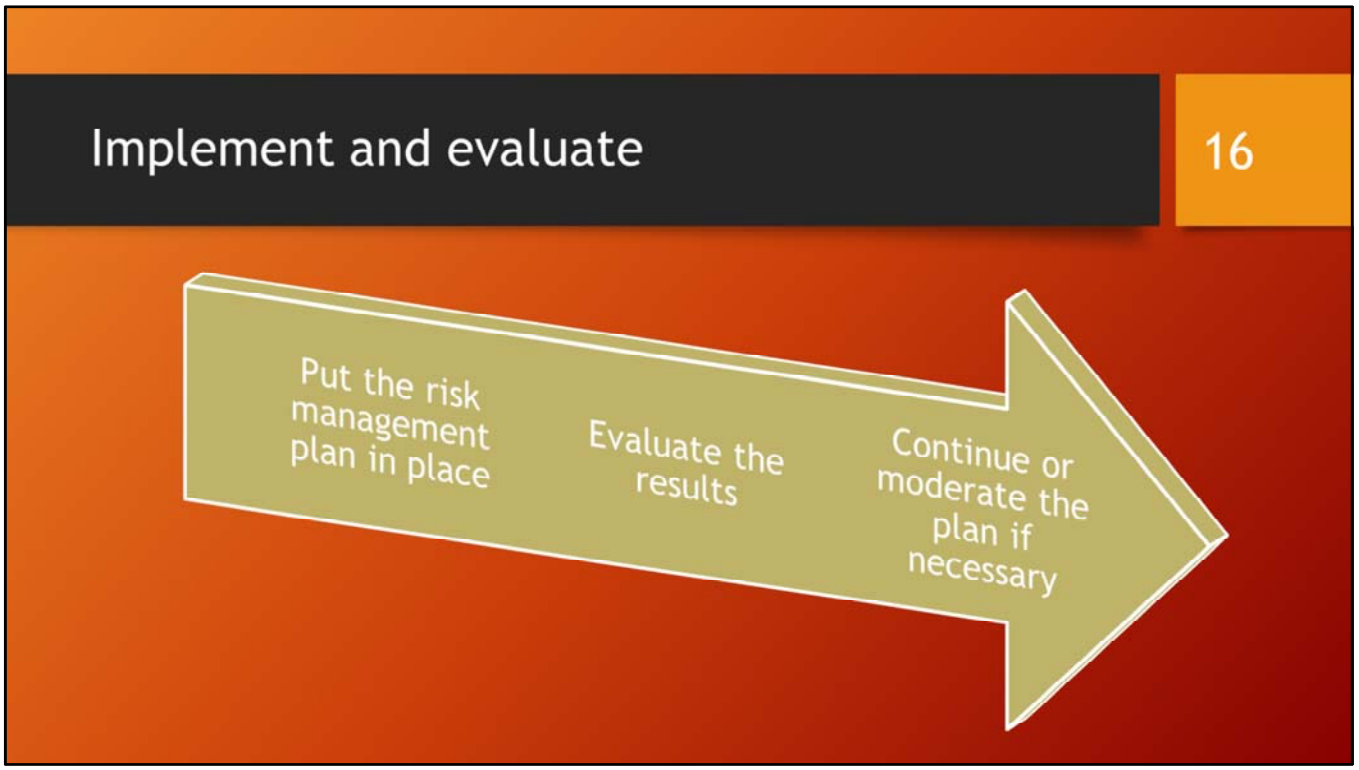


- Before implementing the plan, a careful look at the characteristics of risk under each management strategy is deemed appropriate
- Types of risk that are suitable for applying risk avoidance strategy:
    - High possibility of having the loss and the size of the loss is huge The risk is difficult or basically not quite possible to be reduced even with good efforts in prevention or reduction
    - No insurance or the premium is extremely high and that make it unworthy to go ahead
- E.g. doing business in a highly political unstable area or the place deeply troubled by serious epidemics

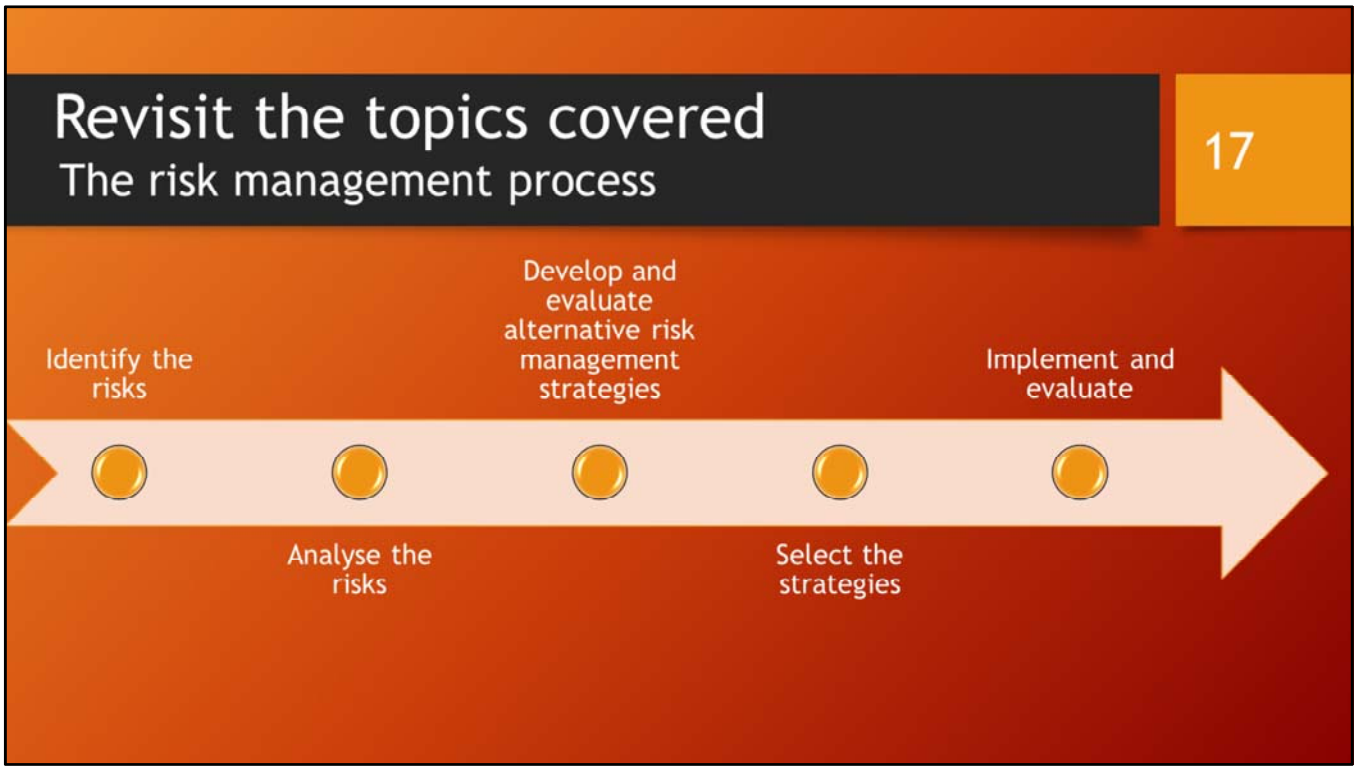
- Types of risks suitable for reduction strategy:
- Frequency of occurrence is high but the loss from which is not too big. In such case, taking out insurance for the risk may not be justified because the administrative costs incurred may be higher than the compensation received for the loss
- Risk assumption strategy is not preferred since the loss accumulated from each occurrence may not be small. Therefore, adopting risk reduction strategy is the way out to reduce the chance the size of loss
- Company which has the technology, personnel and financial capacity to launch effective prevention and reduction measures is more able to reduce risk
- The reasons for the loss are generally traceable and the chance of happening predictable, then the prevention and reduction measures could be effective
- Students can suggest examples according to the conditions specified e.g. industrial accidences, product defects etc

- Risk can be transferred if they are:
- Chance of happening infrequent by once happens the loss could be huge.
- The premium is acceptable as the frequency is not too high and of course the risk itself is insurable
- The risk cannot be reduced substantially by only applying prevention and reduction strategy and external coverage is needed
- Students can give examples e.g. severe fire or typhoon attack

- Risk assumption is suitable when the risk is under certain situations:
- Loss is very minor and the chance could be infrequent
- If the chance is in infrequent and the loss is very negligible there is no need to pay attention to it ➔ assumption by default
- When the insurance cost is relatively more expensive it would be better self-insured, of course it only happens for large corporation that has a large number of exposures and can afford self-insurance financially e.g. large retail chain can self insure against hazards like fire by setting up its own insurance company
- For some sorts of risks that can be largely reduced through prevention and reduction strategies, risk assumption as a complementary is acceptable e.g. convenience store has CCTV and close communication with police plus very few cash kept in the register
- Of course, it is difficult to say the risk has really effectively reduced since risk is always something unknown
- Also, as mentioned before when there is no other risk management strategy feasible risk assumption is the only choice.



- After choosing appropriate risk management strategies the company will need to put them into practice by assigning the tasks and specifying the responsibilities to concerned people and department
- After implementing the strategies for a period of time there should be periodic review of the situation
- There might be some problems arising or new situations appear e.g. new kinds of risk such as cyber attack and political problems
- Then the whole process of risk management will be repeated again
- The company need identify all possible risks especially those emerged due to new environmental changes, analyse the risk and design suitable risk management strategies accordingly, then put them into operation for some time and lastly review and evaluation again



- Review the major topics covered in this lesson and summarize what have been covered in each topic briefly
- Ask students if there is any questions for any of the topics covered

LESSON 6:

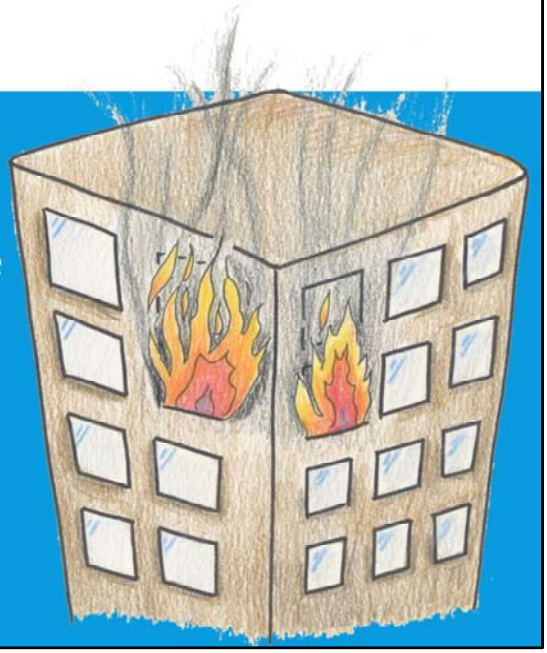
Insurance Concept- An Overview

1

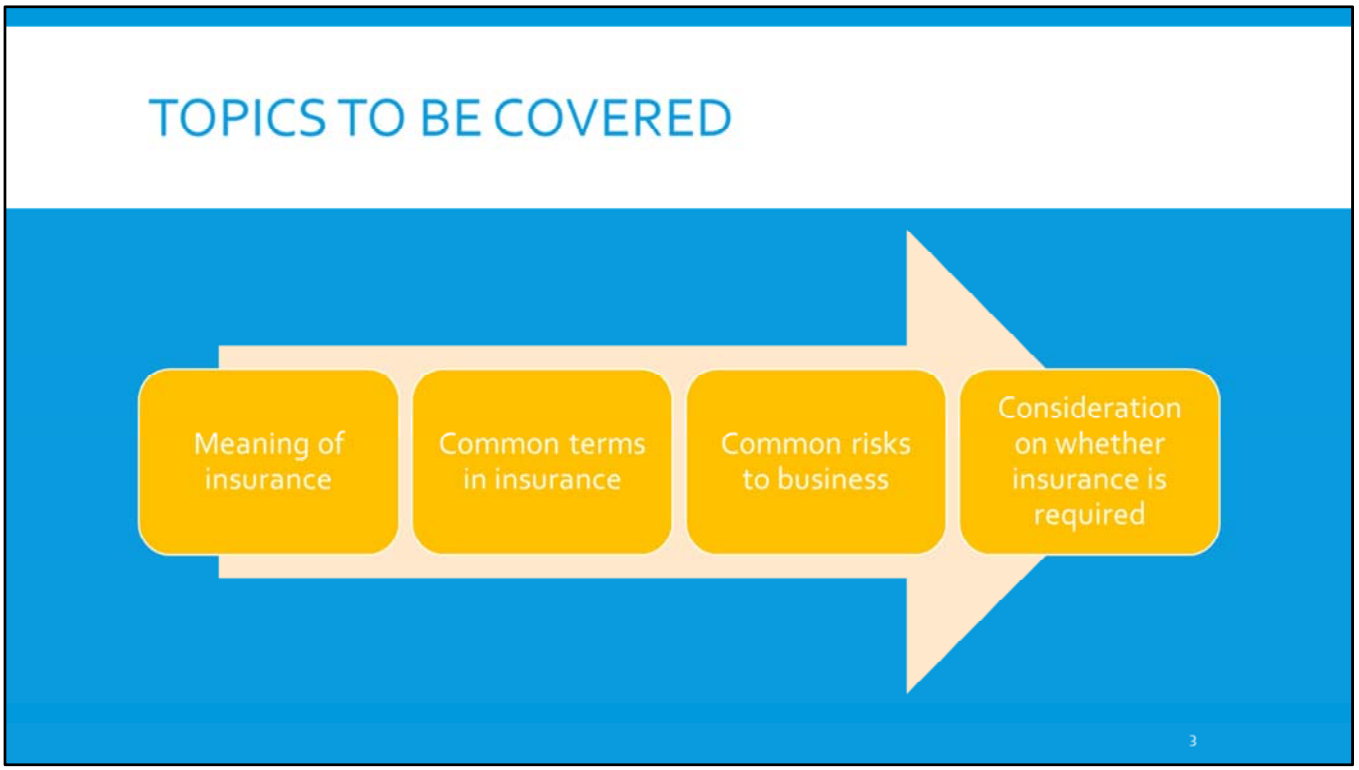
- Introduce the title of this lesson
- Insurance is important for risk management
- It is because for many small and medium firms, insurance tends to be their major means for handling business risk since they may not have enough scale and capital to apply risk assumption, while risk prevention and reduction would demand a lot of efforts and involve expertise.

INTRODUCTORY CASE: FIRE HAPPENED IN MINI-STORAGE WAREHOUSE

- In June 2016, a deadly fire happened in a mini-storage warehouse in Kowloon Bay and killed two firemen. The warehouse is located in an old industrial building with around 200 storage units congested on a single floor. According to the news the operator of the warehouse has not taken out any insurance against fire and the occupants of the storage unit were not reminded to insure on their belongings.
- What is insurance?
- When and why business needs insurance?



- Explain the case contents: the incident happened in Hong Kong
- Ask students what is insurance?
- Students may answer that it is a transfer of risk or spread of risk among similar risk-takers
- When and why business needs insurance?
- There could be different answers e.g. insurance is for something that may not happen so often but could mean a lot of damages
- But then why the multi-storage warehouse did not buy the insurance?
- That would lead to the point that people usually overlook potential risk
- It is particularly true for individual and small businesses
- In fact, risk management is important and not just for large corporations but also to everyone including individual, family and organization of whatever size
- Also insurance is the most common form or the minimum form of risk management that should not be overlooked



- Explain the topics that would be covered in the lesson
- Firstly the meaning of insurance will be introduced so that students can have a better idea about what insurance is though it is actually a very common term
- Insurance in fact involves many technical aspects and therefore different terms and their meanings plus implications should be known
- Then we will move to explain some common risks in running a business that could usually be handled by taking out insurance
- However, insurance is not always the first priority in managing risk, some considerations have to be made before taking out relevant insurance policies

MEANING OF INSURANCE

- An individual or a company can, at a cost, shift the risk to another party who pool all the parties facing similar risk together to share the loss in case the hazard happens. From individual point of view, it is a risk transfer measure while from society perspective it is a way to spread out the risk through pooling.

4

- The operation of insurance is that you pay the insurance company to cover certain risk e.g. fire happened in your factory
- Once the loss occurs you can claim back the compensation so that the loss would not jeopardize your business from continuing operation
- To generalize such process, it can be conceptualize that for individual or firm, insurance is actually a kind of risk transfer through which the risk can be shifted to another entity who would bear the loss incurred for a premium
- For society, insurance would be risk sharing through pooling all the possible cases together

COMMON TERMS IN INSURANCE

Principle of indemnity	• It sets out that the insured after the happening of the hazard cannot collect from the insurer more than the actual value of the loss arising from the event
Insurable risk	• Details of its meaning have been covered in lesson 2. It should be noted that not all pure risks are insurable and there are five criteria under consideration
Adverse selection	• It is an additional condition for insurability, which refers to the case that the chance of some individuals/firms suffering from loss is greater than average (e.g. business engaging in dangerous operations) , making the taking out of relevant insurance difficult

- Explain the meanings of the three terms in the PowerPoint which are self-explanatory
- Provide examples for illustration wherever applicable
- May ask students to give examples first
- E.g. for principle of indemnity: there is a theft in the office and the actual value of loss is $10,000 while the coverage limit is $100,000, then only $10,000 will be compensated
- E.g. for insurable risk: generally five criteria can be used to determine whether a pure risk is insurable. For example a company car accident can be insured if it fulfills the large numbers rule; the loss incurred is quite large but not catastrophic; the occurrence is purely accidental; and the loss can be readily measured in monetary terms
- E.g. for adverse selection: a company doing transportation business in a war area would find it difficult to get insurance

COMMON TERMS IN INSURANCE

Insurance policy

- Formal agreement between insurer and insured about the risks covered for the insured and the cost (premium) incurred
- Other terms and conditions of the agreement also included

Underwriting

- The procedures through which the extent of coverage and the amount of premium will be determined by the insurance company. The procedures may differ from company to company owing to different experiences and objectives

Insurable interest

- the potential that the insured may directly/indirectly suffer from a loss in an event, even in case that impairment or damage of the insured object is absent

- Explain each term according to the PowerPoint:
- Meaning of insurance policy and underwriting are quite straight forward
- For insurable interest: need to emphasize that it is also a condition for getting insurance. Normally insurance could not be taken out if no loss is incurred to the insured in an event. However, insuring for the life of family members is acceptable since the loss could be on the insured though he or she may not suffer from death. But in case when the hazard happens the insured will not suffer any loss (in monetary terms) out of it e.g. the fire happened to a totally unrelated premise, it would be difficult to take out relevant insurance

COMMON TERMS IN INSURANCE

Coverage limit:

The highest amount that the insurer would pay for a claim within the coverage of the insurance policy

Premium:

The cost that the insured need to

pay to the insurer for the coverage

Deductible:

Agreed between insurer and insured that certain amount of loss need to be bear by the insured first before insurer pay for the loss in excess of it

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- Meanings of coverage limit and premium are also self-explanatory
- For deductible: need illustrations with some examples e.g. in an insurance policy covering car collision with $2000 being the deductible, suppose the car collides and a loss of $5,000 is incurred, the insured need to bear the first $2,000, before the insurer will pay for the rest
- The major purpose of having deductible is to reduce the claim for insignificant amounts which is considered administrative uneconomical

COMMON TERMS IN INSURANCE

Cost justification, affordability

- If the costs of insurance is too high, it is not possibly feasible for people seeking insurance as a way of dealing with risk
- Another consideration for insurability

Actuaries

- Specialist working in insurance company, responsible for assessing and estimating the costs of losses and the required premiums for insurance policies

8

- Although insurance is a very common form of risk management, it should also be justified with reference to cost benefit analysis
- Thus if the cost of insurance is too high, business would probably consider other forms of risk management
- In fact, in order to get more business, insurers are actually competing on pricing though it could be quite risky
- As for actuaries, meaning of it is also self-explanatory

- Finally we come to conclude on how pure risks affect business
- It can be on two aspects i.e. before the hazard occurs and after the hazard occurs
- Before the hazard occurs:
    - Costs need to be involved for adopting different risk management strategies to deal with the risks e.g. insurance premiums, opportunity costs of keeping reserve for risk assumption and costs involved when applying risk prevention/reduction strategies
    - Apart from actual costs, pure risk also poses uncertainties that may annoy company management – mental anxiety
    - It arises because there is always some sorts of risk overlooked by the company. When such case happens the company will be exposed to risk unprepared. Of course risk assumption can take care of it but it is surely not desirable. Such anxiety would deter the investment or development plans of the business
- After the hazard occurs:
    - Direct loss such as damage to property and indirect loss such as loss of sales and profit to the company will be incurred
    - Besides, there may have losses from liability to other people or their properties
    - That may include compensation to people died or injured/damage of properties. Sometimes, legal costs will also be incurred
    - Hopefully all these costs could be met by insurance or other risk transfer arrangements, if not, the company needs to absorb all these costs on risk overlooked before

- After explaining the common risks faced by business in operation, now move on to introduce losses that could be handled by insurance
- There could be direct loss and indirect loss to a company
- Common causes for direct loss:
  ->Damages to property or contents in the property by fire and other natural disasters
  -> Loss due to fraudulent acts of employees, robbery and accident
- Relevant insurance could be taken out for protection

RISKS COMMONLY FACED BY BUSINESS: DIRECT LOSS -- (EXAMPLES)

Fire and other natural disasters

- Damages to building and the properties within it, either partially or completely owing to fire or other natural disasters

Fraudulent act of employees

- Money or valuable stock stolen by staff

Burglary, robbery and theft

- Cash or valuable inventory being stolen or robbed

Accident

- equipment damaged in an industrial accident

11

RISKS COMMONLY FACED BY BUSINESS: INDIRECT LOSS

Loss owing to business interruption

Causes:	Impacts:	Insurability:
Indirect losses owing to the direct incidences e.g. fire, flooding, robbery etc	Short term: loss of immediate business opportunity Long term: could be far-reaching impacts e.g. loss of customers, business relationship or market share	lost profit and payments of unavoidable fixed costs

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- Direct loss could also lead to indirect loss to a company
- For example: the damage to the premise of a restaurant would lead to indirect loss such as closure of premise for certain period of time
- Business interruption could have short term and long term impacts on the business
- In normal case, lost profit and payments of unavoidable fixed costs can be protected by taking out relevant insurance since the losses tend to be quite measureable

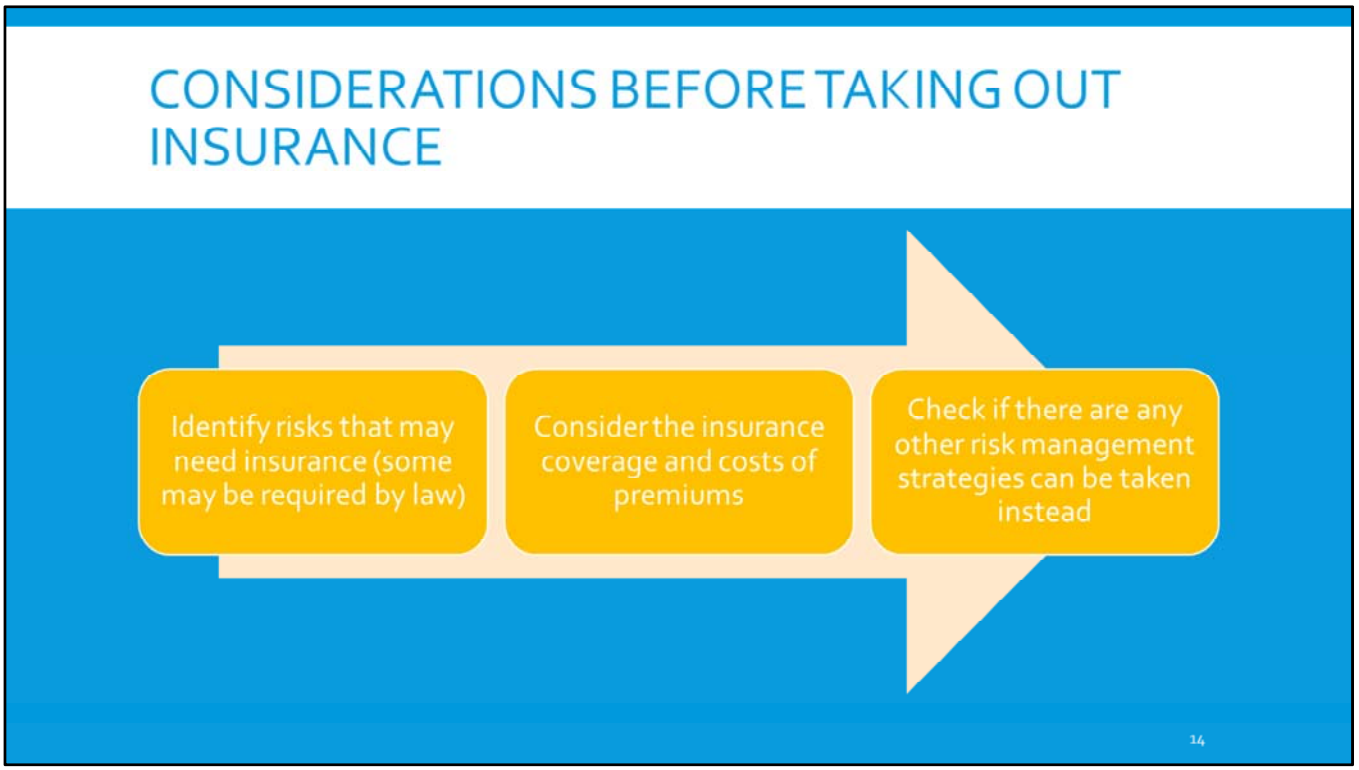
RISKS COMMONLY FACED BY BUSINESS: LIABILITY

- Claims from third party for the damages to property and/or injury suffered when the insured business is held liable
- Examples:
  - Customers' belongings damaged because of the carelessness of the employee
  - Company car knocked down a pedestrian and/or damage his belongings
  - Company's product turned out to be harmful to health
  - Employees injured during work

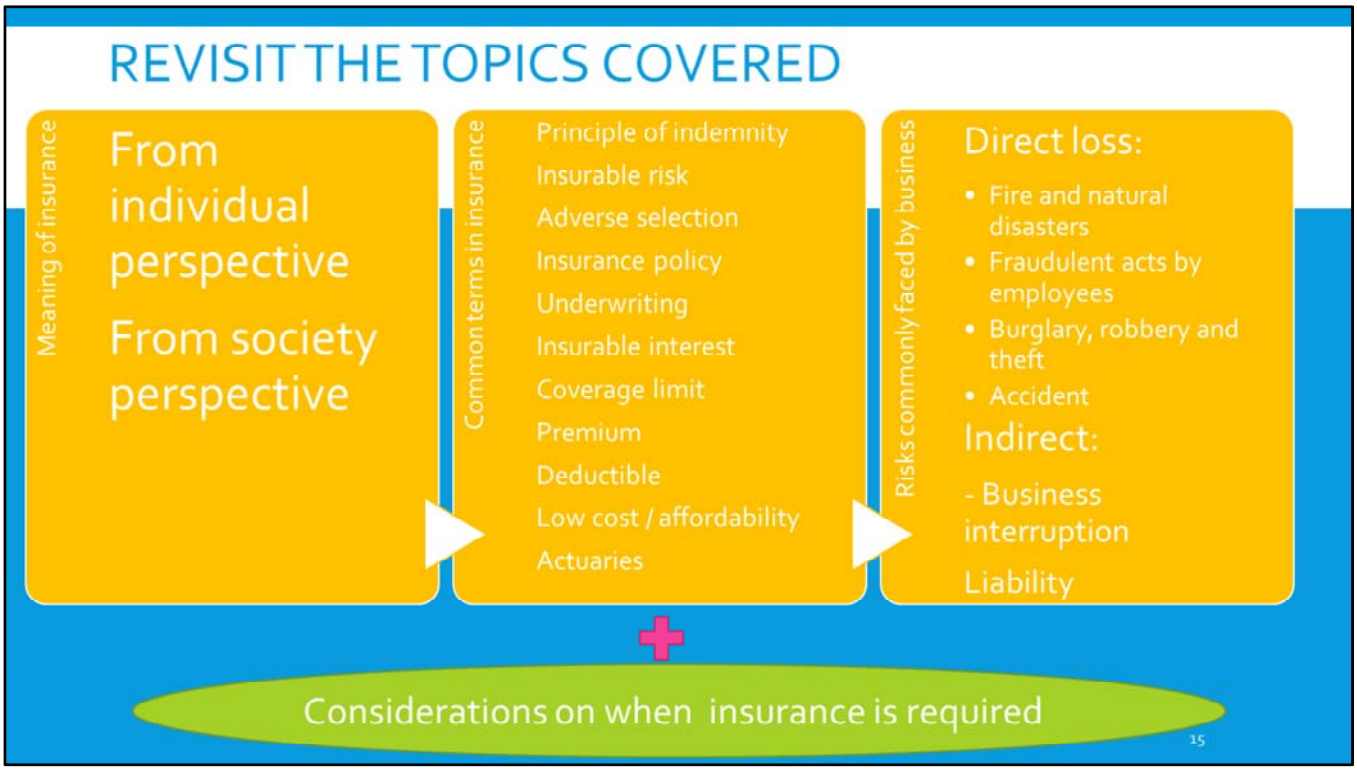
All of the above costs can generally be met by taking out relevant insurance

13

- Another kind of risk that a company usually face is the claim from third party for liability
- That could be arisen from any third party getting injured or his/her property damaged due to the fault of the insured company or its employees
- The examples can be used to illustrate different possible kinds of liability



- When deciding on taking out an insurance some considerations need to be taken:
- Firstly identify what risk need to be insured
- Particular attention may need to be directed to some insurances that are required by law (compulsory) e.g. motor insurance covering third party and employees' compensation insurance
- These types of insurance cannot be compromised
- For the others, the costs of insurance need to be considered
- Risk management is not identical to insurance and the ultimate purpose of the former is to minimize the risk at an acceptable cost
- Then the risk management has to consider is there any other strategies that can be taken to take care of the risk, for example to replace or reduce the scope of the insurance, or at least to minimize the insurance costs
- Of course the main point is to consider the cost benefit of different risk management strategies
- For example, some risks could be better and more economically handled if risk assumption or self-insurance is applied



- Summarize all the topics covered in the lesson
- Remind again the meaning of insurance especially on the different approaches adopted by individual and society
- Briefly explain again the common terms in insurance that have been covered in the lesson and those that have impact on the insurability e.g. criteria for insurability, adverse selection, insurable interest and affordability
- Review the risks commonly faced by business: direct loss, indirect loss and liability
- Remind that some risks can be generally covered by insurance
- Lastly mention that certain considerations have to ben taken before deciding on taking out insurance policies as means for handling risks faced by the business

LESSON 7

Common types of insurance protection for business I

1

- Introduce the title
- Mainly concern the common types of insurance that business will usually take out
- It will be of two parts discussed in two lessons

TOPICS TO BE COVERED

Comprehensive insurance for business

Motor insurance

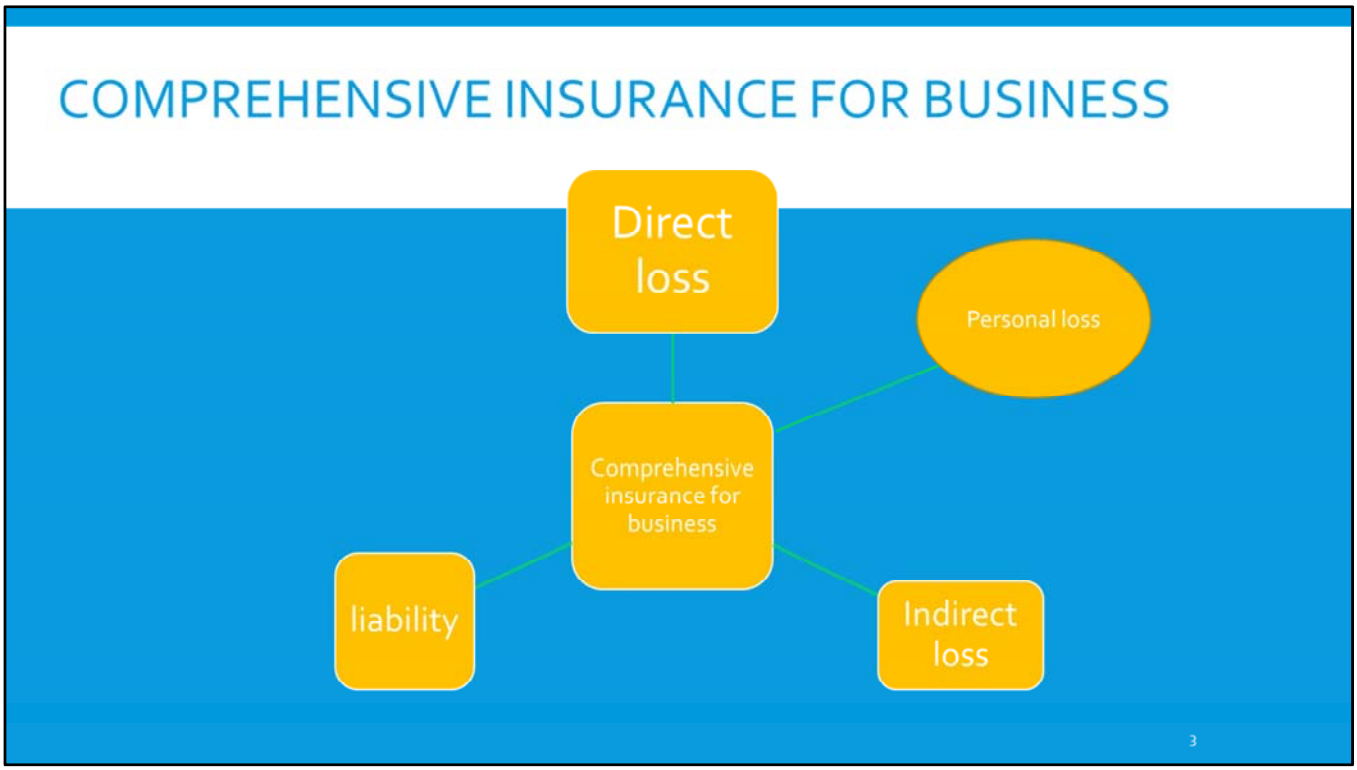
- Compulsory part for covering third party risks
- Comprehensive coverage

Fidelity insurance

- Cover loss due to dishonest employees

2

- Briefly explain the contents to be covered in this lesson
- After explaining the concepts of insurance the remaining parts of these two lessons will be focused on illustrating several major insurance policies that companies usually take out and their implications
- This lesson will concentrate in motor insurance and fidelity insurance
- Apart from the above, there are other kinds of liability insurance and in the next lesson the public liability and employees' compensation liability will be discussed owing to their significance to general business operations



- Based on different kinds of risk faced by a company as mentioned in last lesson, some companies may simply take out a blanket-type insurance policy, i.e. comprehensive insurance, for protection against many common hazards faced by a company.
- It is a “all-risk” insurance and the coverage depends on different terms
- Some could be very extensive to cover different kinds of risk including those costs due to direct loss, indirect loss and liability
- Some may also include personal losses such as the health of employees and loss of key executives
- However, different firms may have different special features and may face different operational environments, a standard comprehensive insurance may be too general, expensive and not well-adjusted to specific requirements of the needs of a particular company
- Thus firms may consider adopt different insurance policies catering for different potential risks according to their needs

MOTOR INSURANCE - RISKS FROM OPERATING A COMPANY'S OWNED VEHICLE

Major areas of risk involved

Risk relating to the insured vehicle and person in operation	• Damage to the vehicle • Injury or death of the person in operation
Risk relating to third parties	• Injury or death of other people • Damages to other vehicles or properties of other people

4

- Ask students when a car is running on a road what kinds of risk would be involved and what are those parties that might have losses or damages when accident happens
- Two major areas of risk involved when one is driving a car for business :
- First is about the insured vehicle and the person in operation when the accident happens
- Second is about all other people or properties damaged when the accident happens
- Insurance should be taken out in consideration of the loss incurred to parties in these two major areas

MOTOR INSURANCE - TWO MAIN COVERAGES

1. Physical damage of the insured vehicle

2. Motor liability

A. Coverage on liability for body injuries

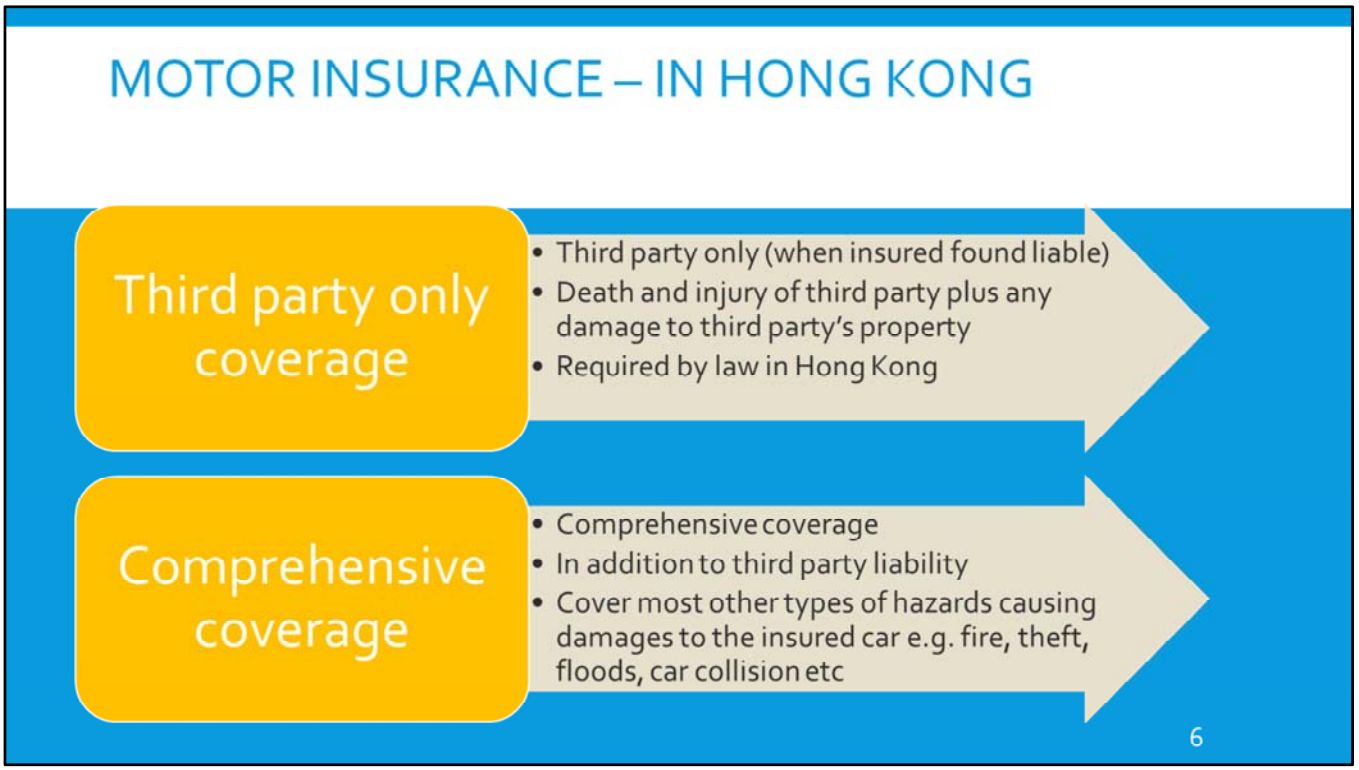
- Costs involved for injuries or death of other people due to the vehicle accident in which the insured is found liable

B. Coverage on liability for physical damages

- Costs for compensating the damages to other people's properties caused by the insured car

5

- Following the previous PowerPoint
- Major coverage of motor insurance will be mainly on two areas:
- First is to cover the loss or damage of the insured vehicle
- Second is being the motor liability which covers the liabilities to other people injured or killed and/or to other properties that could be damaged during an accident caused by the insured vehicle



- In Hong Kong, motor insurance with third party coverage is compulsory as it is required by the law in Hong Kong
- It compensates the costs arising from the death or injury of the third party as well as damage to third party's property when the insured is judged to be liable to the accident
- To get better protection, comprehensive coverage can be adopted
- It covers different kinds of hazards causing damages to the insured car e.g. fire, theft, floods, car collision etc, in addition to third party liability protection
- Whether to have comprehensive coverage is up to the desire of the insured and is not compulsory

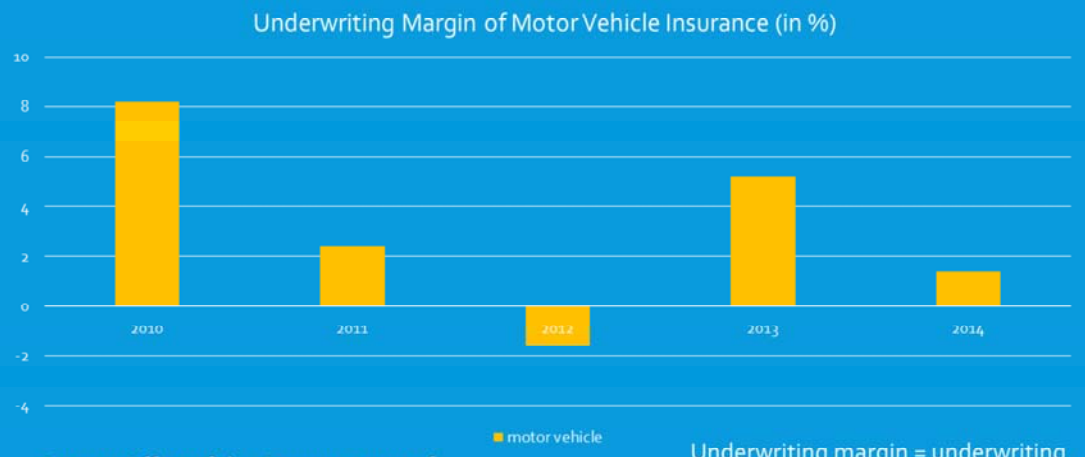
MOTOR INSURANCE – IN HONG KONG

- Insurance with third party only coverage can deal with most of the claims from liability caused by the insured vehicle
- Insurance with comprehensive coverage can handle the physical damages to the insured vehicle or even when the car is stolen
- For private motor car insurance with comprehensive coverage medical expenses are available to the insured and other occupants of the car in case of accident
- For commercial vehicle the arrangement would be different and subject to different situations

7

- Matching the insurance with the potential risks we can see that the third party coverage can deal with most of the liability claims from third parties
- At the same time the comprehensive coverage would cover the loss of or damage to the insured vehicle plus medical expenses to the insured and other occupants of the car in case of accidents, but that is only for private vehicles
- For commercial motor vehicles, additional coverage is needed for costs involved due to the driver's and passengers' injury or even death but it differs from case to case

IMPLICATIONS ON BUSINESS

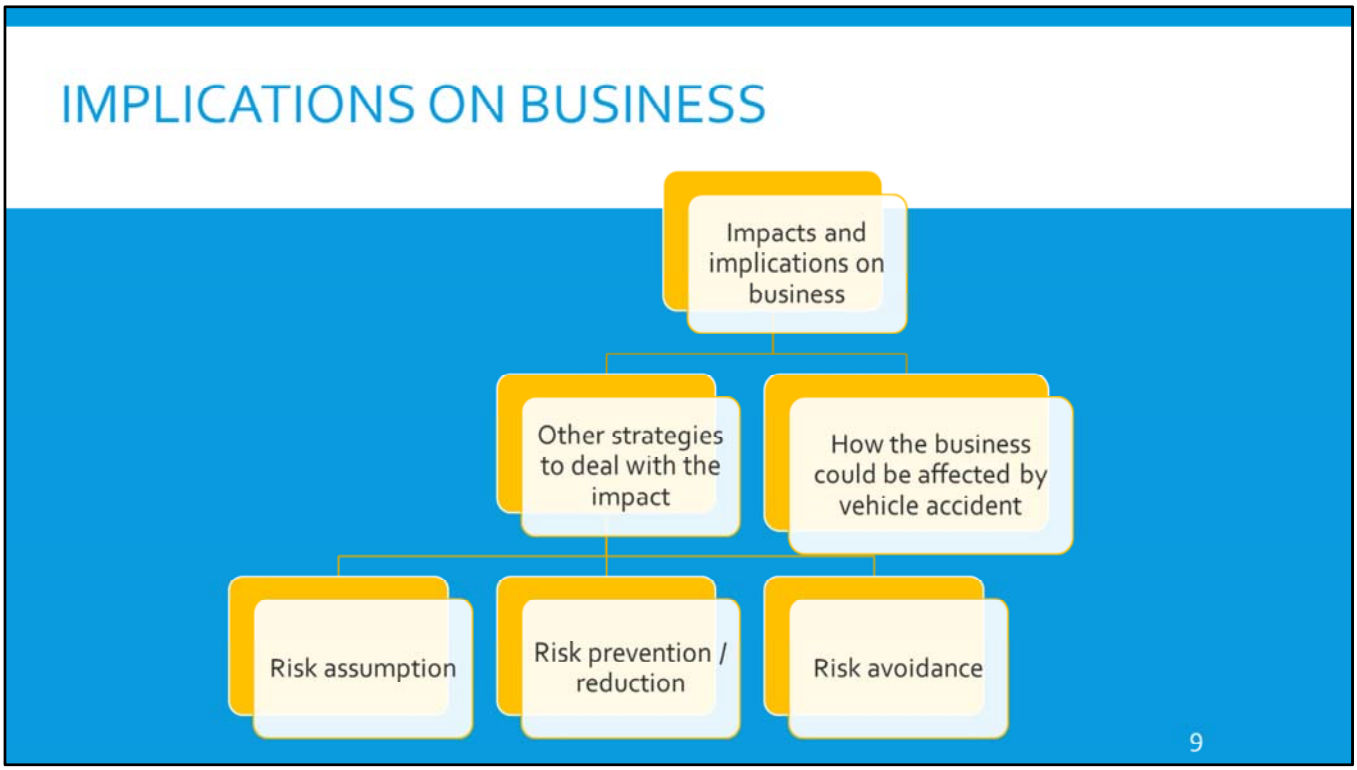


Source: Office of the Commissioner of Insurance Annual Report, 2015

Underwriting margin = underwriting profit/loss expressed as a percentage of earned premiums

8

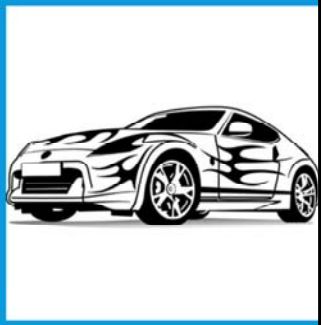
- The graph shows that the underwriting margin for motor vehicle insurance keeps decreasing in past five years with 2013 the only exception
- The trend was mainly due to increasing number and value of claims for car accidents
- As such, there is a growing pressure on increasing the premium of relevant policy by the insurance companies so as to maintain their level of profit margin
- Therefore, it is expected that the cost of making motor insurance by businesses will go up in the future



- Car accident is actually very common in Hong Kong and the risk associated to those companies with frequent use of vehicles e.g. transportation companies is high, making the costs of insurance very high too
- Thus other strategies need to be considered in the hope to reduce costs:
    - Risk assumption: it could be possible for large firm with a lot of vehicles on the road for business e.g. logistic companies. The risk could be assumed in the form of self-insurance or setting up of its own insurance company, or to have a large repairing center to repair all the damages to their insured cars
    - Risk prevention / reduction: better training and hiring of experienced drivers can help reduce the possibilities of car accidents; keeping good maintenance on the cars and having effective human resources management can also be helpful
    - Risk avoidance: one of the way is to quit from any business involving use of vehicles, but that might not be realistic
- In addition, when accident happens there could be indirect effect on the business rather than just direct damages to vehicle, property or injury to people
- Some business activities might be affected.
- There are some kinds of insurance enabling car rental so that the company can continue the business

CASE FOR DISCUSSION: AUTONOMOUS VEHICLE

- Also known as driverless car or self-driving car, which is the vehicle that can find its own way by using various sensor systems detecting the surrounding environment and move on without any human control. The autonomous car integrate and analyse all the information received from its environments and make decisions on the path getting to its destination. There are different levels of automaton and the highest one is that the car can determine what path to go after the destination being set. It can go anywhere which is allowed by law without any human intervention.
- While many car manufacturers and IT firms are working hard in developing and launching the autonomous vehicle many governments are trying to get the legislation compatible to such new and revolutionary move.
- In 2016, California had initiated a law that would allow completely driverless vehicles operating on the road
- One of the major arguments is who should be liable when accident happens and what insurance policy should be taken out for such cases



10

- Introduce the case contents
- Explain the meaning and operation of autonomous vehicle
- Describe the development of the autonomous vehicle and the latest situation worldwide
- Legislation is on the way for the launch of autonomous vehicle but one of the major concerns is from the insurance industry

CASE FOR DISCUSSION: AUTONOMOUS VEHICLE

- The autonomous vehicle is found to be very helpful in reducing accident rate
- In U.S. the analysis found that around 90% of accident is mainly due to human error and costs associated was about 212 billion dollars in 2012
- It was estimated that the autonomous vehicle can reduce the costs by 190 billion dollars
- In addition, the introduction of autonomous vehicle would stimulate much higher demand for cars since many people who are not suitable or incapable of driving would like to buy one because they no longer need to acquire all the driving skills and pay constant attention to the road situations.

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- Explain that the autonomous vehicle can help reduce the accident rate dramatically
- Huge costs saving can be achieved
- Also large demand for such cars is expected

CASE FOR DISCUSSION: AUTONOMOUS VEHICLE

Questions:

- Who should be held responsible in case an accident happens due to the malfunction of the autonomous vehicle?
- Who should pay for the damages of other people's property and injuries of other people when the autonomous vehicle is liable for the accident?
- Who should pay for the damage of the autonomous vehicle and the loss of driver when the vehicle itself is liable for an accident?
- What insurance is needed and who should be the policyholder?

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- Ask students what do they think about the introduction of autonomous vehicle
- Particularly on responsibility for third party as well as the driver and the car manufacturer
- Ask students for the implications on insurance underwriting
- Basically both the driver and the car manufacturer should have responsibilities
- The car manufacturer should be responsible for technical errors while the driver also held responsible because the car should not be really totally autonomous that he/she should have some last moment control in case accident happens
- However the driver may not be vigilant to the environment and the alarm system of the car may not be functioning, thus the car manufacturer should have greater share of responsibility
- As for the insurance there could be drastic change in the business model. The insurance may need to be sold to the manufacturer instead of to the driver
- Instead of dealing with millions of drivers the insurance agents may only need to have business with several major car manufacturers
- Of course, there could be possibility that the car manufacturers will set up their own insurance company to take over all the potential losses

FIDELITY INSURANCE – COVER LOSS DUE TO DISHONEST EMPLOYEES

- Loss or damages caused by dishonesty of employees (with/without external parties)
- In Hong Kong it is covered by fidelity (guarantee) insurance
- Only cover loss due to employee's cheating behaviours e.g. stealing money from cashier but not mistakes or errors owing to incompetence of employees
- Coverage could be for all staff or specified individual or group/posts
- In determining granting or continuing related policies, the insurance company would consider whether sufficient risk prevention and reduction strategies have been employed by the company

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- Then move to another common type of insurance usually taken out by businesses
- Loss or damages caused by employees' dishonest actions could be covered by fidelity guarantee insurance
- It only covers deliberate cheating from employees
- But not for those mistakes and errors owing to employees' incompetence e.g. loss of customers because of poor service quality
- The coverage can be directed to a specific person or a post, or to a group of people/posts, or to all staff in general
- Of course the insurance company need to pay close attention to the security system of the firm and also how well that the firm would deal with people who have unclean records when determining granting and/or continuing the policy

REVISIT THE TOPICS COVERED

Common types of insurance available to businesses I

Comprehensive insurance for business

Motor insurance: the compulsory part for third party cover and the comprehensive part for the loss and damages to the insured vehicle

Implications on business

Fidelity insurance: cover the loss due to dishonest employees

14

- Recap what have been discussed in this lesson
- Mention that there are several common types of insurance for business operation
- Comprehensive insurance is a “all risk” type insurance policy covering many different possible areas of risks that a company may face
- Motor insurance is very common especially for those business involving use of vehicles, illustrate the two areas it covers i.e. liability to other people and their property and the loss and damages of the insured vehicle plus the passengers
- In Hong Kong, it should be emphasized that motor insurance on third party liability is required by the law, while the comprehensive protection against the loss or damage to the insured vehicle, in addition to third party coverage, is optional
- Since car accidents are very common, other risk management strategies should be considered to reduce the loss exposure and strike a better balance between cost and benefit
- Lastly, the loss due to dishonest behavior of employee can be covered by fidelity insurance

Lesson 8

1

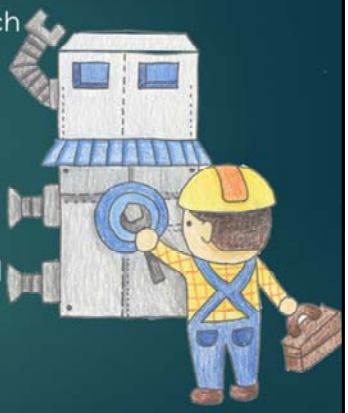
Common types of insurance protection for business II

- Introduce the title of the lesson
- It is the continuation of the last lesson on the common types of insurance for businesses

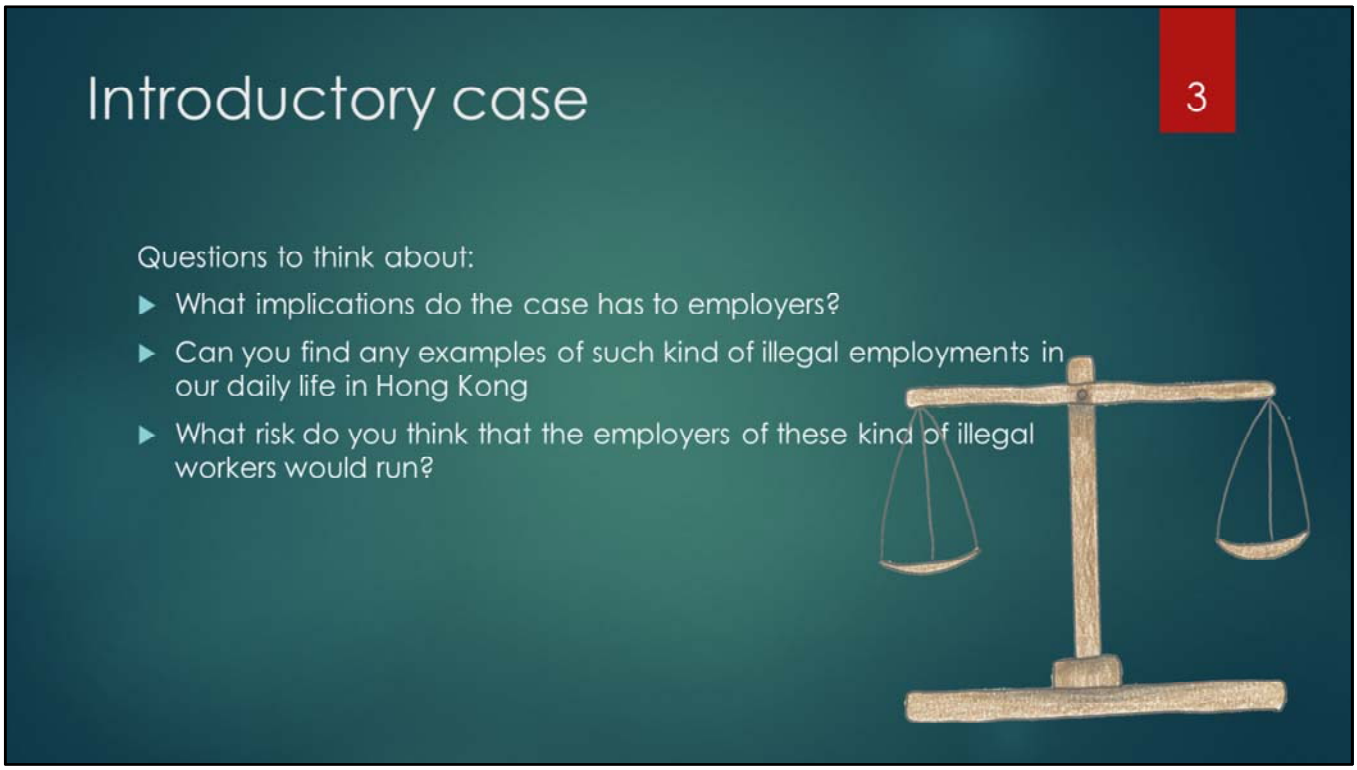
Introductory case: court case on industrial accident

2

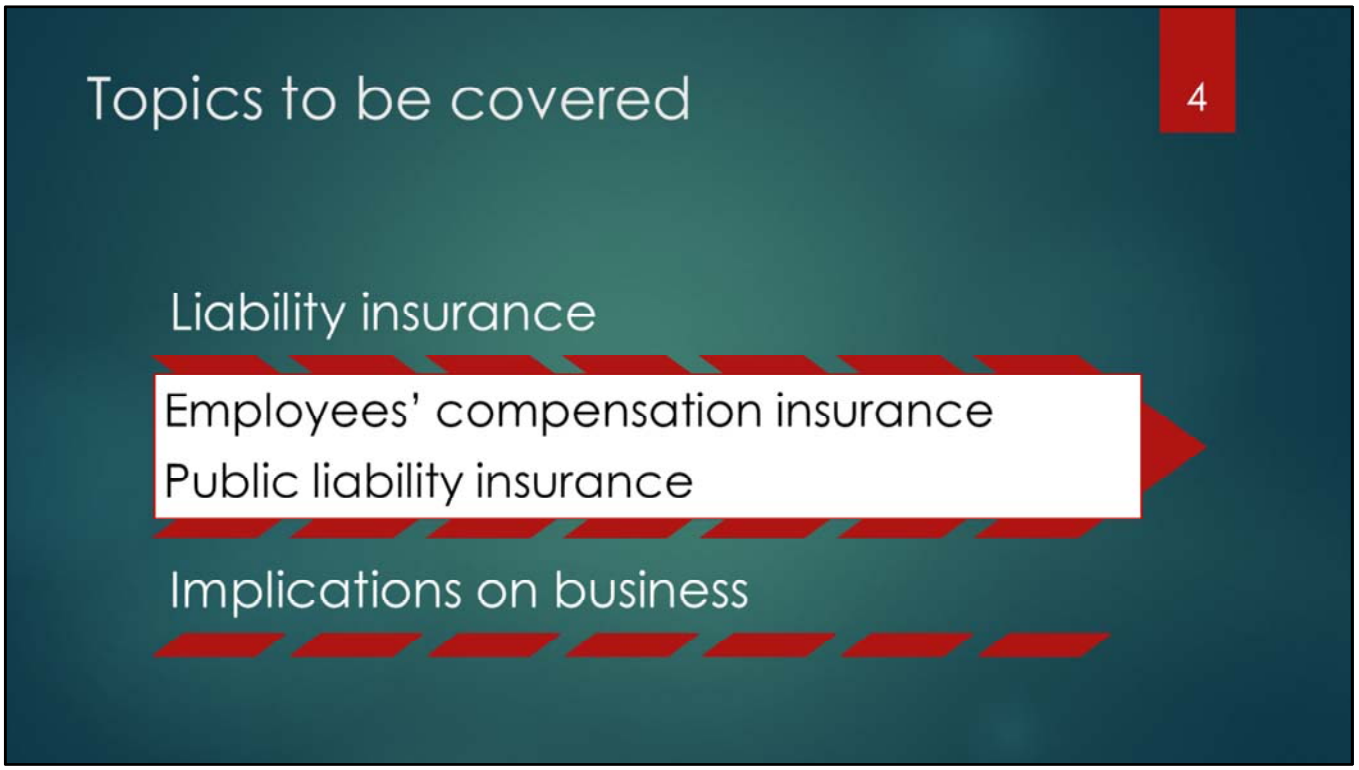
- A Mainland Chinese visited Hong Kong with a two-way permit which means that employment in Hong Kong is not allowed. However he got employed and worked in a construction site. Unfortunately he was injured during his work. It was then a problem whether the employer should be held liable to somebody's injury when the employee working status is in doubt
- In fact the Employment compensation ordinance has a provision allowing the court to make discretion, with consideration of related circumstances to treat the illegal contract as if it is a valid contract of service
- Finally, the court ruled that compensation should be paid to him



- Introduce the case to the students
- Emphasize that the court has used discretion to rule that the illegal contract as if it is legal when the compensation to the employee's injury is the major concern
- To show to the students the law on employees' compensation concerns more on sending out a message to employers that this obligation should never be overlooked
- Thus even for illegal workers compensation would also be in force



- Based on the previous case ask students what implications are there for employer
- Basically it is a strong message telling the employer that even in illegal cases, issues relating to employees' compensation is of paramount importance and cannot be ignored
- In fact, there are similar cases happening in different businesses in Hong Kong
- Ask students to raise examples they have seen in their daily lives
- Examples: people hire illegal workers in transportation business, or ask their domestic helper to work in their factory or restaurant etc
- For the case of domestic helper, it should be mentioned that though they are legally employed in Hong Kong, they are not supposed to work in commercial settings, thus these kinds of work are also illegal, unless they are employed for such purpose
- Ask students what risk would be involved when the employer hire this kind of workers
- Answer: they will be sued for illegal employment once discovered, and if the illegal worker gets hurt they might be held responsible. In such case. it should be emphasized that there would not be any insurance covering for the employment and the employer would be exposed to high risk



- Introduce the topics to be covered in this lesson
- State that liability insurance will be the focus of this lesson, of which the employees' compensation insurance, and the public liability insurance are the two common types of liability insurance in Hong Kong
- Emphasize that the implication and importance of liability insurance to business, especially that on the employees' compensation insurance, because of the law's requirement and the rising cost concern in recent years

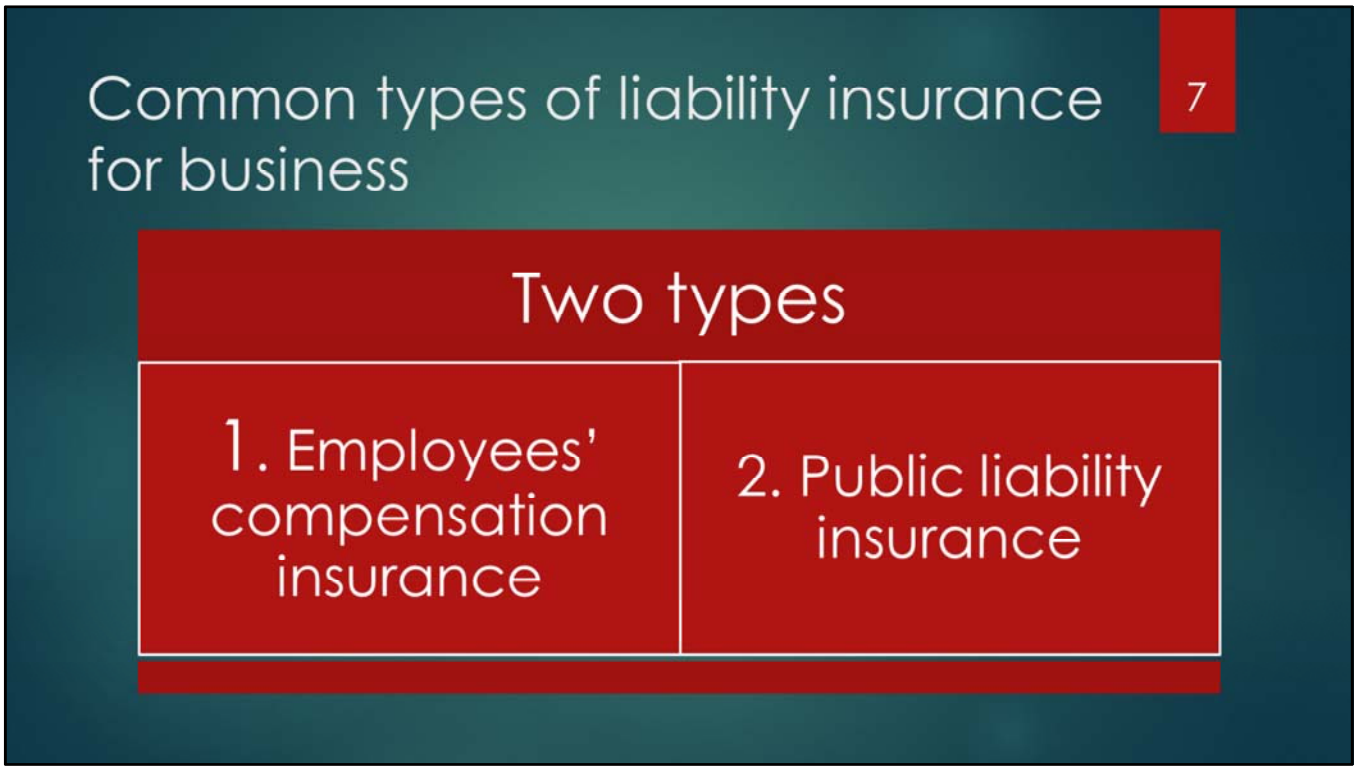
Liability Insurance

5

- It covers the loss of or damage to other peoples' assets caused by the insured (the company or its employees) as well as other person's (including those employed by the insured) injury or even death due to the negligence of the insured.

- Now comes to another major type of insurance that a business commonly encounter
- Explain the meaning of liability insurance as shown in PowerPoint
- Liability insurance is actually a large category of insurance consisting many different types of insurance
- Two major types will be covered in this lesson

- Describe the major types of liability usually faced by a business
- Product liability refers to liability caused by the use of product or service
- Employees' compensation liability refers to the liability incurred to the employees
- Professional liability refers to the liability arising from malpractice of professionals
- Public liability refers to any other liability caused to the general public due to the operation of the business, it is actually very broad but exclude those liabilities covered in previous lessons



- Tell students that the lesson will focus on the two major types of liability insurance as shown in the slide

Employees' compensation Insurance

8

Employer's Liability to employees' compensation in case of:

- Injury by Accident:
  - If an employee sustains an injury or dies as a result of an accident arising out of and in the course of his employment, his employer is in general liable to pay compensation even if the employee might have committed acts of faults or negligence when the accident occurred.
- Occupational Disease
  - An employee suffering incapacity arising from an occupational disease is entitled to receive the same compensation as that payable to an employee injured in an accident arising out of and in the course of employment, if the disease is one due to the nature of any occupation in which he was employed at any time within the prescribed period immediately preceding the incapacity caused.

(Source: A Concise Guide to the Employees' Compensation Ordinance, March 2015, Hong Kong, p. 4-5)

- According to the Employees' Compensation Ordinance, employers are liable for the injury of their employees in an industrial accident and costs involved from occupational disease
- Explain the meaning of the liability of the employer related to employees' injury by accident
- It should be emphasized that the employer is liable for any employees' injury no matter it is due to the fault of the employee or not
- Of course if the injury is caused by employee's deliberate self-harming behavior that would be different
- The list of occupational diseases covered by the Ordinance can be found in the Second Schedule of the Ordinance. The detailed contents can be found at: http://www.labour.gov.hk/eng/public/ecd/pco360.pdf

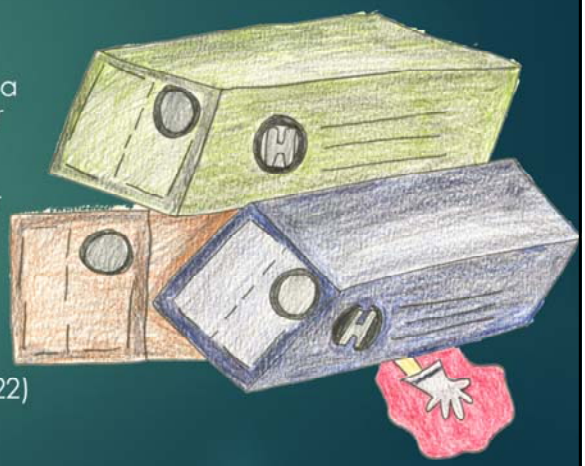
Employees' compensation insurance

9

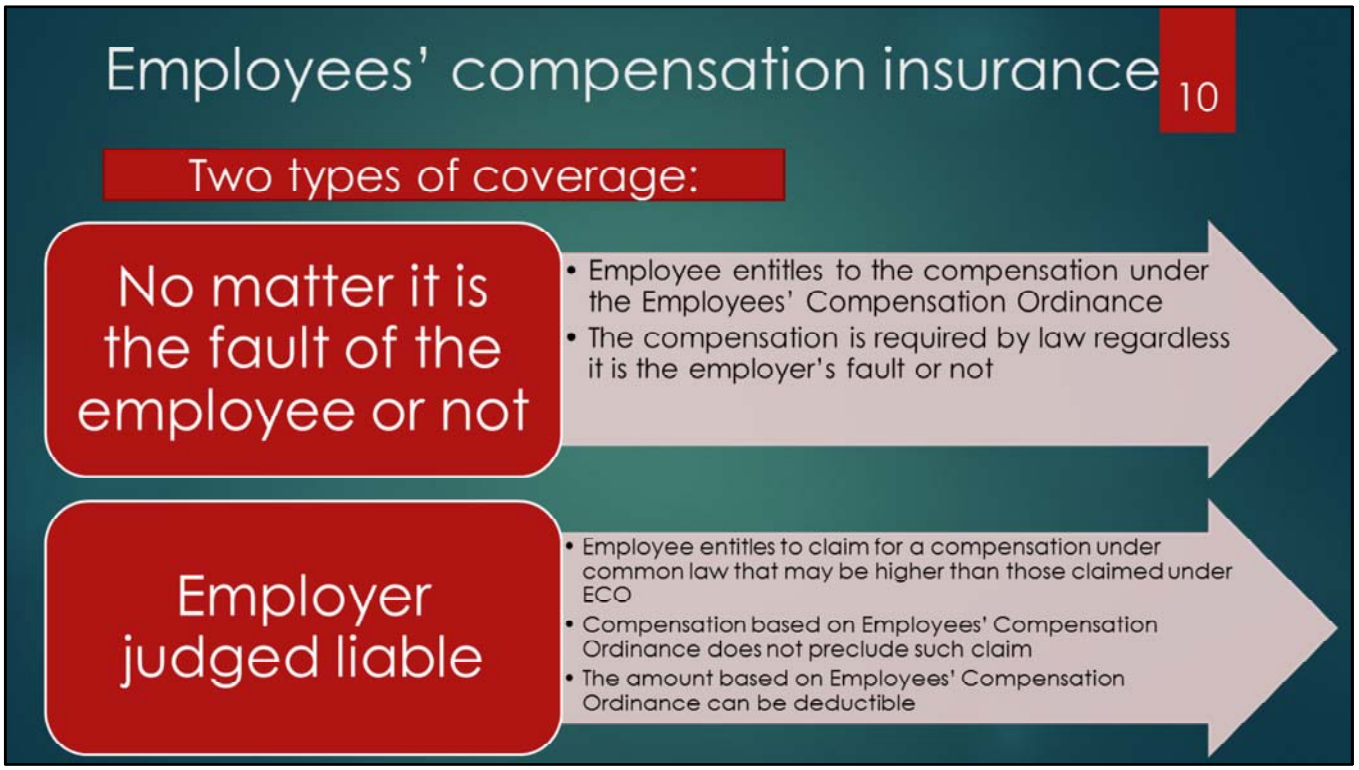
A compulsory insurance

- As required by law, no employer shall employ any employee in any employment unless there is in force a policy of insurance to cover their liabilities both under the Employees' Compensation Ordinance and at common law for injuries at work in respect of all their employees, irrespective of the length of employment contract or working hours, full-time or part-time employment. Should there be any queries on legal liability, employers should seek professional legal advice.

(Source: A Concise Guide to the Employees' Compensation Ordinance, March 2015, Hong Kong, p. 22)



- According to the Employees' Compensation Ordinance in Hong Kong employer has to take out employees' compensation liability insurance if employment exists
- It is an offence to the law if no such insurance was taken out when employment continues
- It should be emphasized that the Ordinance applies widely to different kinds of employment including full-time, part-time, permanent, temporary and different length of working hours



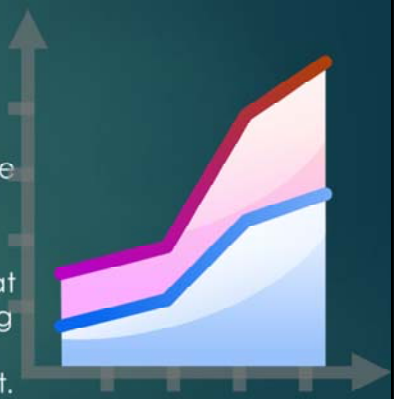
- The insurance covers two levels of liability:
- The first level is relating to the liability arising from the Employees' Compensation Ordinance (ECO)
- Based on the Ordinance, no matter whether the injury is caused because of the fault or negligence of the employee, the employer is held liable except under certain situations e.g. employees' deliberate self-harming behavior, compensation is almost a must in most cases
- The second level is about whether the injury is caused by the negligence of the employer
- For this aspect the employee needs to prove that the responsibility is on the part of the employer
- If it is found that the employer is responsible, the employee can claim for a compensation under the common law since the employer has the responsibility to provide safe working environment to employees and the amount could be larger than that under the specifications of ECO mentioned above
- The compensation made under the ECO does not preclude the employee from claiming the compensation under the common law if the employee thinks that it is the fault of employer causing the injury
- If the case that negligence of the employer can be established, a compensation will be decided by the court and if the amount is larger than the compensation under ECO, the employee will get the amount net of that from the ECO

Case for discussion: Increasing industrial accidents in Hong Kong

11

According to the news published in 2016, a study revealed that the industrial safety in Hong Kong is a severe issue. The local death rate is 5.2 per 10,000 workers which is three times that of in Australia and more than two folds that of in Singapore.

The costs associated with employees' compensation has been increasing rapidly in recent year. In a research report, it was found that the claims shot up at a rate of 20% to 30% per year owing to ever-rising number and seriousness of employee injuries. In view of such trend some major insurers have in fact planned to withdraw from this market. The result is inevitable increase of premiums and it is expected that such cost will keep rising in coming years unless some measures can be taken promptly.



- It was found that the costs of employees' compensation keep increasing in recent years and in fact the workplace safety record in Hong Kong is not quite satisfactory
- In the end it is the employers to bear the rising insurance costs on employees' compensation
- Thus firms need to take actions to solve such problems
- Below is the figures on industrial accidents in Hong Kong based on the Labour Department Annual Report 2014
- The figures show that the fatal cases increased drastically in recent years particularly from 2012 to 2014
- In fact, the rate would keep increasing since there are many infra-structure projects going on in Hong Kong in foreseeable future

Year	Minor cases*	Non-fatal cases	All non-fatal cases	Fatal cases
2010	16, 165	42, 429	58,594	197
2011	15, 944	40, 857	56, 801	195
2012	16, 266	40, 304	56, 570	193
2013	16, 096	38, 868	54,964	204
2014	15, 531	38, 173	53,704	213

- Ask students for their answers
- The impacts are quite obvious: high premium costs and loss of productivity
- Normally, improving workplace safety is the best way to tackle the problem
- Most risk prevention and reduction measures can be applied
- Post-injury strategies would also be helpful
- Many times the injured employees do not know how to deal with their injury and many companies just leave it to the employees themselves
- In fact if the injury can be well taken care of, the employee can recover sooner and it would help reduce medical expenses and improve productivity sooner

Can the liability on employees' compensation be transferred?

13

- Is it possible to make agreement/contract with employees such that all the costs involved to the injured employee when industrial accident happens would be borne by the concerned employee himself or herself?
- It is not allowable since employer's liability to employees' compensation when industrial accident occurs has been specified by statue law and that will override agreements or contracts entered to the contrary

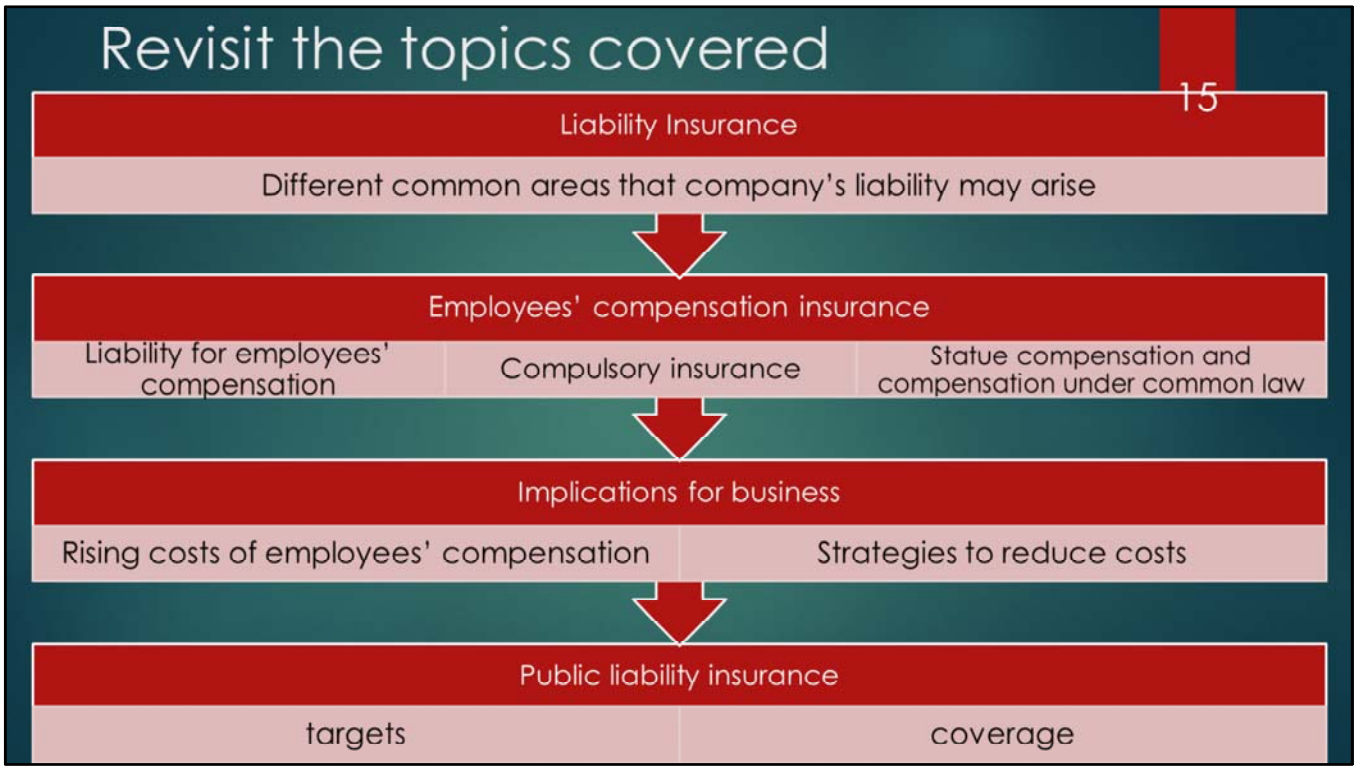
- It is not possible and unfeasible to try to transfer the costs of injury in industrial accidents to employees through private contract or agreement

Public liability insurance

14

- It provides coverage to the insured company when injury of other people and/or damage to other people's property occurs during the process of the company's operations
- Also the insured company or its employees are held responsible
- e.g. a customer knocked down in a restaurant due to the carelessness of the waiter

- Now comes to another major type of liability insurance
- Explain the meaning of public liability insurance
- Many businesses which premises would be accessed by large number of general public would take out such insurance e.g theatre, restaurant etc
- That is why some insurance policies specify their coverage on hazards happened on the insured's premise
- Ask students to raise examples e.g. the waiter carelessly pour a cup of hot water onto the body of a customer in the restaurant
- Give another example i.e. a customer get hurt when testing a product in a shop due to the improper instructions given by the shop keeper
- Public liability insurance is very common since such hazard will happen all the time especially for those business with large number of visitors or customers getting onto their premise



- Summarize all the topics covered in this lesson
- Recall the meaning of liability insurance
- Review the related concepts of employees' compensation insurance, its coverage, applications and restrictions
- Revisit the public liability insurance and briefly review its meaning and coverage

Risk Management

Classwork (Lessons 1 to 2)

A. Multiple Choices: (10 marks)

1. For risk:
   I. Consequence of the event is by chance
   II. Consequence of the event is only loss
   III. Consequence of an event is for sure
   IV. Consequence of the event could be loss
   a) I and II
   b) I and IV
   c) II and III
   d) II and IV
   Ans: b

2. Which of the following will not involve any business risk:
   a) Closing down the business
   b) Diversifying the business
   c) Inventing a new product
   d) Inviting wealthy partner
   Ans: a

3. Which of the following option will affect the degree of a risk?
   a) The probability that adverse result will happen
   b) The size of damage when adverse result happens
   c) Both of above
   d) None of above
   Ans: c

4. Which of the following would involve higher risk:

	Probability that adverse result would happen	***size of damage***
a)	1.0	$10,000
b)	0.8	$10,000
c)	0.6	$12,000
d)	0.5	$20,000

ans: d

(Probability = 1 means something definitely happen, no risk at all)

5. Pure risk is:
   a) The outcome of the event can only be loss
   b) The outcome of the event can be gain or loss
   c) The outcome of the event can only be no loss
   d) The outcome of the event can be no loss or loss

   Ans: d

6. Speculative risk is:
   a) The outcome of the event can only be loss
   b) The outcome of the event can be gain or loss
   c) The outcome of the event can only be no loss
   d) The outcome of the event can be no loss or loss

   Ans: b

7. Keeping money in business's safe instead of its time deposit account could most likely be:
   a) A pure risk
   b) A speculative risk
   c) Both speculative risk and pure risk
   d) None of the above

   Ans: a

8. Which of the following most likely involves a pure risk
   a) The company's CEO has diagnosed a cancer
   b) The company publish and sell a book about how its CEO fight the cancer
   c) Buying Hong Kong Bank shares as company's investment
   d) Buying a new flat as company's additional asset

   Ans: a

9. Which of the following most likely involves a speculative risk
   a) Launch new product to the market
   b) Keep the products in a new warehouse
   c) Drive a car to deliver the products to the retailer
   d) Operate a machine to produce products

   Ans: a

10. Which of the following makes it important for business to distinguish speculative risk from pure risk:
    a) Business only deal with pure risk
    b) Business only deal with speculative risk
    c) Normally only pure risk can be insured
    d) Normally only speculative risk can be insured

    Ans: c

(1 mark each, total = 10 marks)

A. Short questions (classwork): (15 marks)

1. Give an example of pure risk that one may encounter when running a book store and explain why it is a pure risk. (5 marks)

   Ans:

   Having theft could be an example of pure risk since the outcomes to this situation can only be "no loss" or "having loss" to the book store.
2. Give an example of speculative risk that one may encounter when running an ice-cream shop and explain why it is a speculative risk (5 marks)

   Ans:

   Introducing new style of ice-cream would be a speculative risk since the situation can be a gain (well-received by customers) or loss (negative response from customer)
3. Explain the meaning of law of large numbers in risk context (5 marks)

   Ans:

   Given a similar risk, the law of large numbers refers to the situation when the sample size of people or organizations concerned is large enough, the potential to collect information to ascertain the possible damage increases.

B. Essay question (classwork): (15 marks)

In order to be insurable from the viewpoint of an insurance company the loss arising from an event should not be catastrophic nor too insignificant. Explain the above with an example for each criterion.

Ans:

It should be noted that insurance company is a business that must try to achieve cost economies in order to be profitable. At the same time the insurance company also needs to deal with its own risk too. (5 marks)

If the loss is catastrophic e.g. a pandemic affecting large population of people which then leads to huge claims, the insurance company would find it unprofitable to go for it. (5 marks)

Meanwhile, if the loss is too insignificant, the insurance company would find it uneconomical to accept after taking all the administrative costs in consideration e.g. loss of stationeries in an office. (5 marks)

Risk Management

Homework (Lessons 1 to 2)

A. Multiple Choice (10 marks)

1. Traditionally, risk management in a company concerns mainly on:
   a) Speculative risk
   b) Pure risk
   c) Both speculative risk and pure risk
   d) None of them
   Ans: b

2. Insurable risk is
   a) A kind of risk that have to be insured
   b) A kind of risk that insurance company will offer cover for
   c) A kind of risk that can only be protected through insurance
   d) A kind of risk that can be covered by most types of insurance
   Ans: b

3. Non-insurable risk is
   a) A kind of risk that should not be covered by insurance
   b) A kind of risk that can only be covered by measures without any insurance elements
   c) A kind of risk that insurance company will not offer cover for
   d) Actually a speculative risk that cannot be insured
   Ans: c

4. It is unlikely to have insurance against depreciation of an machinery operating in a company's factory because:
   a) The value of the depreciation loss cannot be measured in monetary terms
   b) The probability of the loss cannot be estimated
   c) The depreciation is for sure to happen but not by chance
   d) The loss could be catastrophic
   Ans: c

5. The owner of a company insured against damages to a valuable asset in the company and then the following happened:
   I. The owner of the company damaged the asset on purpose out of personal emotion

II. An employee damaged the asset on purpose out of personal emotion

Will insurance compensation be made in the above situations?

	Case I	Case II
a)	Yes	Yes
b)	Yes	No
c)	No	Yes
d)	No	No

Ans: c

6. Why the law of large numbers is important for insurability?
   a) Large number enables more correct estimations on the loss be made
   b) Large number enables more clients be reached
   c) Large number enables more premium payments be obtained
   d) Large number enables more claims be avoided

   Ans: a

7. With reference to the concept of insurability, the major reason for an insurance company trying to have policies covering the same risk scattered over many different geographical areas because:
   a) The company wants to become a global insurance enterprise
   b) The company cannot make profit from one single area
   c) The company wants to economize its administrative costs
   d) The company wants to spread out the risk

   Ans: d

8. It is hard to get insurance for risks happened frequently with loss amount small in value because it is:
   a) Hard to justify the administrative costs
   b) Hard to measure the monetary value of the loss
   c) Hard to predict the chance
   d) Hard to justify the loss is caused by intentional actions

   Ans: a

9. It would be difficult to insure against pandemic because of the reasons below except:
   a) It could affect large proportion of population
   b) It could affect large geographical area
   c) It could lead to catastrophic loss
   d) It could be controlled and the outbreak is not by chance

Ans: d

10. It is important for a risk to be measureable in order to get insured because:
    a) The insurance company needs to calculate how much the administrative costs
    b) The insurance company needs to determine the premium based on the amount of loss
    c) The insurance company needs to calculate the probability of the loss occurrence
    d) The insurance company needs to calculate how much money need to be kept as reserve

    Ans: b

(1 mark each, total = 10 marks)

B. Short questions (homework): (15 marks)

1. With reference to a fashion shop, illustrate the criteria for the occurrence of an event to be insurable. (5 marks)

   Ans:

   In order to be insurable the happening of such event should be accidental, the occurrence of the outcome should be by chance and none can be sure of it. Besides, it should not be intentional act for taking advantage of the insurance compensation. For a fashion shop if fire is broken out by accident it is insurable but if the fire is set up by the owner who do it on purpose, then the accident cannot get any compensation.

2. Is it possible to identify certain pure risk as definitely non-insurable? Why or why not? (5 marks)

   It is getting more and more difficult to conclude a certain pure risk as definitely non-insurable since there are many new kinds of risk appearing day by day, and the insurance company have to face fierce competition that makes them try hard to roll out new products covering more and more types of pure risks.

3. Distinguish between a car collision on the road from a car collision in a car durability test by referring to different types of risk. (5 marks)

   Ans:

   A car collision on the road is a pure risk since there could only be no damage (no loss) or damage (loss). However, for the car collision test, the result could be successful (gain) or unsuccessful (loss) and therefore it would be a speculative risk.

C. Essay question (homework)

Give one example of insurable risk for each of the areas below for a shopping mall and explain why it is insurable. (15 marks)

a) Property
b) Liability

Ans:

a) Water damage: it is insurable because
   - Happens purely accidental unless the owner do it on purpose
   - The loss from damages on furniture and fixture in the property can be measured in monetary value
   - The loss would not be catastrophic
   - The loss would not be too insignificant (if the loss is too small, normally insurance company can use deductible to reduce the administrative costs)
   - Many similar cases occurred before and the probability of its happening can be estimated

(2 marks each, max = 7 marks)

b) Public liability e.g. It is the responsibility of the shopping mall to avoid people from falling down onto the floor due to slippery floor. It is insurable because:
   - Purely accidental though it is the fault of the shopping mall
   - The loss can be measureable e.g. the injury and the medical expenses and other related expenses
   - The loss would not be catastrophic
   - The loss would not be too insignificant (medical expenses usually will not be too insignificant, again deductible will be applied for really insignificant cases)

(2 marks each, max = 8 marks)

Risk Management

Classwork (Lessons 3 to 5)

A. Multiple choice questions (10 marks)

1. Which one of the following is correct?

a) Risk is purely by chance and there is nothing to do to minimize the associated loss
b) Risk can be managed so that the loss associated can be reduced
c) Risk and the loss associated can only be handled by insurance
d) There is no way to find out the causes underlying the risk

Ans: b

2. Which two of the following strategies are aiming at reducing the chance of having hazards?

I. Risk avoidance
II. Risk reduction
III. Risk transfer
IV. Risk assumption

a) I and II
b) I and III
c) II and III
d) III and IV

Ans: a

3. Which two of the following strategies are aiming at preparing finance for the loss arising from the hazards?

I. Risk avoidance
II. Risk reduction
III. Risk transfer
IV. Risk assumption

a) I and II
b) I and III
c) II and III
d) III and IV

Ans: d

4. Withdrawing from a political unstable country as a way to deal with the risk involved when doing business in that country belongs to which of the following strategies?

a) Risk avoidance
b) Risk reduction
c) Risk transfer
d) Risk assumption

Ans: a

5. A restaurant sources its food stuff supply only from reliable suppliers in order to avoid the risk of food poisoning. Which of the following strategies is the restaurant applying?

a) Risk avoidance
b) Risk prevention/reduction
c) Risk transfer
d) Risk assumption

Ans: b

6. A convenience store treats the costs of shoplifting as part of its operating expenses. Which of the following strategies is the convenience store applying?

a) Risk avoidance
b) Risk reduction
c) Risk transfer
d) Risk assumption

Ans: d

7. A large multinational corporation never allows all members of its top management team travelling in the same flight when going out for meetings. Which of the following strategies is the corporation adopting?

a) Risk avoidance
b) Risk reduction
c) Risk transfer
d) Risk assumption

Ans: b

8. A large supermarket chain makes contracts with its suppliers that the stock purchased will remain in the suppliers' warehouse until the last moment upon request for the delivery. Which of the following strategies is the supermarket applying?

a) Risk avoidance
b) Risk reduction
c) Risk transfer
d) Risk assumption

Ans: c

9. Risk avoidance is not a very practical and realistic strategy because:

a) It is not possible to avoid all the risks for a running business
b) It is not possible to apply avoidance strategy owing to its complicated procedures
c) It is not possible to cover all the risks with risk reduction strategies, nor can they be avoided
d) It is not possible for all firms to avoid risk since only large corporation can have such capability to do so

Ans: a

10. Under what conditions that risk assumption would be an appropriate strategy?

I. When the loss is insignificant
II. When there is no other risk management strategy feasible
III. When the company wants to control the risk by itself

a) I and II
b) I and III'
c) II and III
d) I, II and III

Ans: a

(1 mark each, total = 10 marks)

B. Short questions (course work): (15 marks)

1. Explain with an example the meaning of risk reduction strategy. (5 marks)

Ans:

Risk reduction is the use different methods to reduce the chance of its occurrence or the costs of loss when it happens e.g. better training of worker so

that industrial accident can be reduced /avoid putting all the valuable inventories together in one place.

2. Explain the meaning of risk avoidance strategy with an example. (5 marks)
   Ans:
   Risk avoidance is to use different methods to eliminate any chance of loss from happening e.g. don't enter the market in a country where there is a war.
3. Distinguish between risk transfer strategy and risk assumption strategy by giving one example to each strategy. (5 marks)
   Ans:
   Risk assumption means the company itself will absorb all the losses when the hazard happens e.g. a restaurant may absorb the costs of stolen cutleries. Risk transfer means that the concerned company will use some ways to shift the financial burden to other party if the hazard happens e.g. buying insurance for loss of property owing to theft.

C. Essay question (course work): (15 marks)

John is planning to establish a fitness center in central. He is very concerned about the safety of the center because the compensation to customers if getting injured could be tremendous. After checking, he finds insurance cost on relevant risk is quite high. Suggest five ways through which the risk can be prevented or reduced.

Ans:

The five ways are:

a) People: the trainer of the fitness center should be qualified and have received good training especially on how to operate the equipment safely
b) Equipment: the equipment should be well maintained, having checked frequently and receiving immediate repair once any defect is discovered
c) Procedure: detailed and comprehensive guidelines and instructions should be issued to the trainers as well as customers, adequate briefing and training should be conducted before allowing free usage
d) Method: only well-tried and commonly used training methods will be taught to the clients
e) Environment: the place should be kept safe e.g. no wet floor, the layout of equipment should be spacious enough to avoid hazards

(3 marks each, total = 15 marks)

Risk Management

Homework (Lessons 3 to 5)

A. Multiple Choice (10 marks)

1. Which of the following is NOT the benefit of applying risk reduction strategy?
    a) Reduce chance of having loss
    b) Lower insurance costs
    c) Promote safety culture
    d) Eliminate all possible risks

    Ans: d

2. Which of the following is NOT the problem of applying risk assumption strategy?
    a) Could be disastrous to the business if catastrophic loss occurs
    b) Great pressure on risk reduction measures
    c) Relationship with insurance company turns bad
    d) Management would be anxious about the possible loss

    Ans: c

3. Which of the followings is the most favorable condition for applying the self-insurance strategy?
    a) The firm is very large and have good financial support
    b) The firm has good estimate about the loss
    c) The firm is facing a lot of risks
    d) The firm have an effective risk reduction strategy

    Ans: a

4. Which of the following is NOT one of the steps in risk management process?
    a) Identifying the risks
    b) Analysis of the risks
    c) Developing risk management strategies to deal with the identified risks
    d) Evaluating which risk is speculative leading to gains for the company

    Ans: d

5. Which of the following is not the benefit of taking Insurance to shift risk:
    a) Loss will be paid by insurer
    b) Less pressure on prevention and reduction measures
    c) No need to be anxious about the possible loss

d) Guarantee that the firm will not fail in its business

Ans: d

6. Self-insurance belongs to which of the following risk management strategies:
   a) Risk avoidance
   b) Risk reduction
   c) Risk assumption
   d) Risk transfer

   Ans: c

7. Those risks that have not been identified and taken care of in the risk management process will most likely be settled by which of the following risk management strategies?
   a) Risk avoidance
   b) Risk reduction
   c) Risk transfer
   d) Risk assumption

   Ans: d

8. In which of the following situations would risk avoidance strategy be regarded as a better choice to business:
   a) When the company is facing non-insurable risk
   b) When the risk is remote but would lead to a huge loss
   c) When the chance of loss is quite certain and the amount of it is tremendous
   d) When the company does not want to pay for the insurance premium

   Ans: c

9. Which of the following statement is correct?
   a) Risk reduction strategy can be used alone since it can prevent all possible risks
   b) Risk avoidance is the best strategy since all risks associated with business can then be avoided
   c) Risk assumption strategy would cover all losses which have not been fully settled by other risk management strategies
   d) Risk transfer strategy can transfer all possible risk to other party

   Ans: c

10. A production firm outsources its delivery function to another company is a _____ strategy

    a) Risk avoidance
    b) Risk reduction
    c) Risk transfer
    d) Risk assumption

    Ans: c

    (1 mark each, total = 10 marks)

B. Short questions (homework): (15 marks)

1. Briefly describe the steps involved in the risk management process. (5 marks)

   Ans:

   The steps are:

   - Risk identification
   - Risk analysis
   - Development and evaluation of alternative risk management strategies
   - Selection and implementation of the strategies
   - Evaluation of the effectiveness of the strategies used

2. Suggest two ways by which an online retailer can adopt to transfer the risk of having inventory being stolen. (5 marks)

   Ans:

   Firstly: don't keep any stock, by asking the producer to ship the product to the customer directly, thus the risk of theft of inventory lied on the producer

   Secondly: buy insurance for stolen inventory

3. Explain what risk management strategies would be more appropriate for managing the loss from shoplifting in a stationery shop. (5 marks)

   Ans:

   In such case, risk avoidance is not quite feasible since the shop does not have a control on when will the theft be happened and when will its business be stopped. As for risk transfer, since the loss amount incurred in shoplifting is usually insignificant, insurance company will find it unworthy to accept after taking into consideration its administrative costs involved. In view of such, risk reduction strategies e.g. installing anti-theft device such as CCTV can be applied to reduce the chance of theft from happening. And the remaining loss can be picked up by risk assumption strategy.

C. Essay question (homework): (15 marks)

Mark is joining with some friends to set up a guest house specializing in providing lodging services to Mainland visitors. He thinks that there is no need to identify all the potential risks involved in the company's operation, nor to analyse them or design appropriate risk management strategies since it would be too time consuming to do so. He concludes that all the company needs to do is to take out insurance for all the common types of risk a normal firm may encounter.

Explain to Mark what problems may the company run into by following his view.

Ans:

There could be several problems even with insurance policies covering the general business risks in the above case:

a) Since no business is exactly identical to each other, insurance applicable to general business operation may not be exhaustive. Mark and his friends may be exposed to some risks that are specific to their business if no risk identification has been done

b) Even all risks specific to the company have been identified in the insurance policies, the degree of each risk may not be the same as other regular companies. There could be the case that the loss is much larger than perceived and out of the coverage limit of the insurance taken out.

c) In rare but real case, the loss may be catastrophic and go beyond the capability of the insurance company to cover. Default issue happens.

(5 marks each, total = 15 marks)

Risk Management

Classwork (Lesson 6-8)

A Multiple Choice: (10 marks)

1. A firm engaging in retail business in a country suffering from civil war will be difficult to get accepted by insurance company for taking out insurance protection on its property because such is:
   a) A speculative risk
   b) A pure risk
   c) An adverse selection
   d) Lack of Insurable interest
   Ans: c

2. A firm may find it difficult to take out a fidelity insurance policy for a worker working for a totally unrelated company because such is
   a) A speculative risk
   b) A pure risk
   c) An adverse selection
   d) Lack of insurable interest
   Ans: d

3. A cake shop has a motor insurance policy of coverage limit up to $1 million. The vehicle was damaged last month and the actual loss was $0.2 million. Based on the principle of indemnity, how much compensation would the cake shop normally get:
   a) $ 0.2 million
   b) $ 0.8 million
   c) $ 1 million
   d) $1.2 million
   ans: a

4. An employee stole the money from the cash register. Such loss can be covered by
   a) liability insurance
   b) public liability insurance
   c) employees' compensation insurance
   d) fidelity insurance
   Ans: d

5. An employee teamed up with outside parties to steal money from the company. Such loss can be covered by
   a) liability insurance
   b) public liability insurance
   c) fidelity insurance
   d) employees' compensation insurance
   Ans: c

6. Which of the following would be the indirect loss of a restaurant after its whole kitchen was destroyed by a fire?
   a) Loss of the fixtures in the kitchen
   b) Loss of the cookware in the kitchen
   c) Loss of business due to no kitchen
   d) Loss of foodstuff in the kitchen
   Ans: c

7. Which of the following insurances can help a business to cover the damage on the company's lorry during a car accident caused by the company driver during the course of business?
   a) Motor insurance with third party coverage only
   b) Motor insurance with comprehensive coverage
   c) fidelity insurance
   d) Employees' compensation insurance
   Ans: b

8. Which of the following insurances is required by the law in Hong Kong?
   a) Fidelity insurance
   b) Public liability insurance
   c) Motor insurance on third party coverage only
   d) Motor insurance on comprehensive coverage
   Ans: c

9. Liability insurance is for covering
   a) loss incurred when a company fails to pay off its debts
   b) loss incurred when a company fails to collect its loans
   c) loss due to the claim from third party for the damage done to which the company is not liable

d) loss due to the claim from third party for the damage to which the company is held liable
Ans: d

10. Which of the following is true:
    a) The motor insurance covers death or injury to third party
    b) The motor insurance is required by law in Hong Kong
    c) The motor insurance will pay compensation to third party regardless who cause the accident
    d) The motor insurance will pay compensation to third party only when the insured is liable
    Ans: d

(1 mark each, total = 10 marks)

B Short questions (classwork): (15 marks)

1. Explain the concept of insurable interest with an example. (5 marks)
   Ans
   Insurable interest refers the potential that the insured may suffer from a direct/indirect loss in an event, even in case that impairment or damage of the insured object is absent
   e.g. Tom would have insurable interest of his factory because he would suffer if the factory is on fire.
2. Illustrate with an example the protection provided by a motor insurance with third party coverage only. (5 marks)
   Ans:
   It covers the loss on death and injury of the third party plus damage to his/her property from the car accident that the insured is liable e.g. the insured car knocked down a pedestrian because of the fault of the insured
3. Describe what losses will the employees' compensation insurance cover. (5 marks)
   Ans:
   It covers the liabilities to employees who die or injured as a result of an accident arising out of and in the course of employment both under the Employees' Compensation Ordinance and the common law

C Essay question (classwork): (15 marks)

Alfred is thinking about establishing a school bus team serving mainly secondary schools in Kowloon. However, he found that the motor insurance premium is quite high to cover such a large team of vehicles. Evaluate if other risk management strategies can be adopted to replace the insurance or reduce its insurance premium.

Ans:

Evaluation:

- Risk avoidance should not be applicable since Alfred's major business involves vehicle, avoiding vehicle related risks would mean totally out of business
- Risk prevention/reduction strategy could be adopted:
    - Having good maintenance on vehicles
    - Hiring of well-trained drivers
    - Monitoring drivers' behavior closely
    - Better scheduling and job allocation to reduce driver fatigue and depreciation of vehicles
    - Avoid overloading the vehicles

      ➔ lower accident rate can surely reduce insurance costs

(3 marks each, max = 9 marks)

- Risk assumption:
    - Motor insurance with third party coverage cannot be waived
    - Damages to school buses can be repaired by the company

      ➔ part of the insurance costs can be absorbed

(3 marks each, max = 6 marks)

Risk Management

Homework (Lesson 6-8)

A. Multiple Choice (10 marks)

1. In a cinema, an employee failed to dry the floor after some customers had split their drinks on the floor. Later on another customer fell on the spot owing to the slippery condition. Will public liability insurance cover such situation?
   a) Yes, because it is the employee's fault
   b) No, because it is the employee's but not the owner's fault
   c) No, because it is the fault of other customers
   d) No, because it is the fault of the fallen customer
   Ans: a

2. Which of the following insurances does NOT help cover a business's potential liability to injured people:
   a) Public liability insurance
   b) Employees' compensation insurance
   c) Fidelity insurance
   d) Motor insurance
   Ans: c

3. Employer is liable to the compensation under Employees' Compensation Ordinance for any injury to his employee as a result of an accident
   a) Arising out of and in the course of employment regardless whether it is employee's fault or not
   b) Arising out of and in the course of employment but not due to employee's fault
   c) Arising out of and in the course of employment but should be to other people's fault
   d) Arising out of and in the course of employment but should be due to employer's fault
   Ans: a

4. Which of the following is correct?
   a) The employees' compensation insurance covers only full-time employees
   b) The employees' compensation insurance covers only those who work for

certain amount of hours for the company per month

c) The employees' compensation insurance covers only permanent employees

d) The employees' compensation insurance covers all employees, irrespective of the length of employment contract or working hours, full-time or part-time employment

Ans: d

5. Which of the following are covered by the public liability insurance taken out by a coffee shop?

   I. A customer gets hurt in the shop due to the fault of the store's owner
   II. A customer gets hurt in the shop due to the fault of the store's employee
   III. A customer gets hurt in the shop due to the fault of another customer
   IV. A customer gets hurt in the shop due to the fault of himself

   a) I and II
   b) I and III
   c) III and IV
   d) II and IV

   Ans: a

6. Which of the following will most likely be covered by public liability insurance taken out by a toy shop?

   a) A customer gets hurt when playing with the toy after purchase in the shop owing to incorrect instructions given by the shop keeper
   b) With no instruction given by the shop keeper, a customer gets hurt when playing with the toy after purchase in a public area
   c) A customer gets hurt when playing with the toy after purchase at home
   d) A customer gets hurt when playing with the toy after purchase on the road when going back home

   Ans: a

7. The injured employee can claim compensation under common law if

   a) He can prove it is not his fault for getting injured during work
   b) He can prove it is the employer's fault for his injury during work
   c) He is injured during work
   d) He has tried his best to avoid getting injured during work

   Ans: b

8. An employer can do the following to reduce the possible claims for public liability except:
   a) train the employees well in doing their work
   b) improve the environment to reduce potential hazards
   c) maintain the facilities in good conditions
   d) prohibit any employee from entering the company's public area
   Ans: d

9. Insurance can help cover the following loss of a fashion shop except:
   a) Damage to the premise due to fire
   b) Loss of inventory due to fire
   c) Loss of sales due to bad weather
   d) Damage to the company car due to bad weather
   Ans: c

10. For company with employees, which of the following insurances cannot be waived even if the magnitude of the associated risk is minimum?
   a) Employees' compensation insurance
   b) Public liability insurance
   c) Fidelity insurance
   d) Motor insurance with comprehensive coverage
   Ans: a

(1 mark each, total = 10 marks)

B. Short questions (homework): (15 marks)

1. What insurance needs to be taken out to deal with the cheating behavior of employee? Explain the coverage of this insurance. (5 marks)
   Ans:
   Fidelity insurance should be taken out for losses owing to dishonesty act of employee. It covers also the joined act between dishonest employee and outside party. However, it will not cover the loss due to employee's incompetence
2. Distinguish between motor insurance with third party coverage only and motor insurance with comprehensive coverage. (5 marks)
   The third party part covers the loss due to the death or injury of third party as well as damage to his property during a car accident in which the insured is held liable. The insurance is required by the law in Hong Kong. Meanwhile, the comprehensive part covers all the losses due to many other types of

hazards causing damages to the insured car such as fire, theft, floods etc in addition to third party coverage. However, it is not compulsory by law.

3. Distinguish between compensation under the Employees' Compensation Ordinance and the common law? (5 marks)

   Ans:

   Employee can get a compensation under the Employees' Compensation Ordinance if he was injured at work during employment regardless it is his fault or not. However, compensation at common law can only be awarded when the employee can prove that it is the employer's fault causing the injury. The compensation under the Employees' Compensation Ordinance does not preclude employee's right to take action for common law's compensation. If the employee can get a claim under the common law, the amount compensated under the Employees' Compensation Ordinance should be deducted.

C. Essay question (homework) (15 marks)

Explain the ways through which a central kitchen can reduce the possible claims arising from the employees' compensation liability against the company.

Ans:

The company can reduce the claims by improving the safety of the central kitchen through the following measures:

- Environment: e.g. the layout design should include safety as one of the consideration
- People: more training on food processing
- Equipment: must be kept in good condition
- Material: safe material for food processing e.g. no harmful gas emitted during the process
- Procedures and Instructions: provide detailed instructions for using the equipment and production process so that hazards due to misusage can be avoided
- Methods: the production methods should be safe

(3 marks each, max = 15 marks)

Risk Management

Quiz (time allowed: 40 minutes)

Part A: Multiple Choice (10 marks)

1. Michael has just established a fast food shop in Wanchai. He is very concerned about the hazard of fire and is thinking about different possible strategies to deal with it. Which of the following strategy is the least feasible for Michael:
   a) Use risk assumption strategy to absorb the loss if fire happens
   b) Use risk reduction strategy to reduce the opportunities of having fire
   c) Use fire insurance to cover the possible loss if fire happens
   d) Use risk avoidance strategy to find a premise where fire has never happened there

   Ans: d
2. Which of the following is incorrect:
   a) Normally, still a number of pure risks are non-insurable
   b) Speculative risks are generally non-insurable
   c) Pure risks are generally insurable
   d) Normally, still a number of speculative risks are insurable

   Ans: d
3. Which of the following insurance is required by law in Hong Kong
   a) Fidelity insurance
   b) Comprehensive insurance
   c) Employees' compensation insurance
   d) Public liability insurance

   Ans: c
4. Unconscious risk assumption occurs when:
   a) The potential risk has not been identified
   b) The loss cannot be avoided
   c) The loss cannot be accurately calculated
   d) The potential risk is identified but haven't been taken care of

   Ans: a
5. Insurable risk is:
   a) A risk that the insurance company would offer cover for the loss
   b) A risk that should be insured according to law
   c) A risk that getting insured is the best way for dealing with it
   d) A risk that the concerned company can choose to insure against it or not

   Ans: a

6. Fidelity insurance is designed to cover:
   a) The loss to the company due to the mistakes committed by employees
   b) The loss to the company due to the dishonest act of employees
   c) The loss to the company due to the dishonest act of business partners
   d) The loss to the company due to the mistakes committed by the owner
   Ans: b

7. All risks concerned with a business having risk management are considered to be taken care of because:
   a) Any risk not taken care of by other strategies will automatically be picked by the risk avoidance strategy
   b) Any risk not taken care of by other strategies will automatically be picked by the risk prevention/reduction strategy
   c) Any risk not taken care of by other strategies will automatically be picked by the risk transfer strategy
   d) Any risk not taken care of by other strategies will automatically be picked by the risk assumption strategy
   Ans: d

8. A TV manufacturing company has sold a TV to its employee. The TV exploded when the employee was watching it at home. The employee was injured and it was found that the reason for the accident was owing to the defect of the TV. Which type of insurance that the company can take out for compensating the employee's claim?
   a) Public liability insurance
   b) Fidelity insurance
   c) Employees' compensation insurance
   d) None of above
   Ans: d

9. Which of the following is a correct description about risk management strategies:
   a) Risk prevention/reduction strategy is to eliminate all chance of loss from happening
   b) Risk avoidance strategy is to avoid spending too much on managing a risk
   c) Risk transfer strategy is to transfer all the risk to its competitors
   d) Risk assumption is to assume the loss by the company concerned
   Ans: d

10. The following are the reasons of having periodic review on the risk management process except:
    a) many new risks keep emerging into the market
    b) many new insurance products keep being rolled out in the market
    c) many new safety technologies keep appearing in the market
    d) many new investors keep injecting cash into the market

    ans: d

(1 mark each, total = 10 marks)

Part B: short questions (30 marks)

1. Outline two major impacts of pure risk on a business before the hazard actually occurs. (10 marks)

   Ans:

   The two major impacts would be on costs and mental anxiety:

   Costs:

   - Premium for insurance costs
   - Opportunity costs for reserve funds
   - Costs on risk prevention/reduction measure (5 marks)

   Mental anxiety:

   Pure risk always poses as an uncertainty to the business since there are always some sorts of risk overlooked and the company would be exposed to risk unprepared. Of course risk assumption can take care of it but it is surely not desirable. Such anxiety would deter investment or development plans of the business (5 marks)

2. "Since after applying risk reduction strategy, the risk of having hazards will be largely reduced and that the rest of the loss could be absorbed by using risk assumption strategy, leaving risk transfer strategy unnecessary." Explain with reason two scenarios under which the above statement may not be true (10 marks)

   Ans:

   It may not be true under following situations:

   a) The potential loss from some hazards, even after risk reduction, could be still substantial e.g. public liability. In that case risk assumption alone may not be able to bear the burden and risk transfer is deemed appropriate to cover the loss.

      (5 marks)

   b) Some risks, as required by law, should be protected by insurance e.g. motor insurance with third party coverage and employees' compensation. Therefore risk transfer is still inevitable.

      (5 marks)

3. Describe three ways, each with an example, through which the risk faced by a firm can be transferred to other party. (10 marks)

   Ans:

   There are three ways of transferring the risk:

   a) Transfer to insurance company through taking out insurance policy e.g. buying a motor insurance with comprehensive coverage to protect against damages to the vehicle arising from many different causes (2 marks)
   b) Transfer the risk-bearing activity to another party e.g. requiring the supplier holding the inventory until the last moment upon request by the firm, so that the potential loss associated with inventory holding stays with the supplier. (4 marks)
   c) Transfer the financial burden to another party through agreement e.g. for industrial market asking the buyer to bear all the risk once the product has been shipped out. (4 marks)

Part C: Essay question (60 marks)

Question 1: (30 marks)

Paul is planning to establish a courier company specializing in delivery documents and small parcels within Hong Kong. In view of the congested traffic in Hong Kong and cost consideration, Paul decides that all the delivery services will be done through public transportation. Since the delivery service would involve a lot of people who are mostly working out-door, Paul concerns very much about the risk arising during the delivery process. He has some knowledge about risk management but concludes that it is not possible to avoid these risks unless he quits the business.

With reference to the different steps of risk management process, advise how Paul can develop an effective risk management strategy for the delivery service.

Ans:

The risk management process is as follows:

a) Identification of risk: there could be the risk of having the delivery employee getting injured and loss of the document or parcel in the delivery process (5 marks)
b) Analysis of the risk: getting injured could happen from time to time though it may not be very frequent. Yet, the cost of injury could be very high once happen; loss of document or parcel could be more frequent but the value of loss would be difficult to determine (5 marks)
c) Develop alternative strategies: risk avoidance is ruled out in the very beginning but the other three strategies could be used (3 marks)
d) Selection of appropriate strategies and implementation:
   - For injury of employee: risk transfer should be adopted since employees'

compensation insurance is compulsory. However, in order to reduce the cost of insurance and protect the employees, risk reduction strategy should be adopted e.g. no overloading for delivery people, more training on carrying heavy stuff, better scheduling and routing to avoid heavy traffic

- For loss of documents and parcels: risk reduction can be applied e.g. suitable loading, secure packaging, effective procedure for checking. For the compensation of loss, the company may apply risk transfer by taking insurance or limit the amount of compensation in the agreement and the rest be borne by risk assumption.

(12 marks)

e) Evaluation: evaluate the risk management strategies from time to time especially when new scope of business has been added, and the whole process should be reviewed to see if there is any improvement that can be made. (5 marks)

(Total = 30 marks)

Question 2: (30 marks)

Agnes is a housewife who is very good at making cakes and many friends keep asking her to set up her cake shop. Finally Agnes made up her mind to establish a cake shop but found it very expensive to rent outlets to sell her cakes. She talked to her son Michael for opinions one day.

Michael said, “Why not sell the cakes online so that people can order them and make payments through internet or smart phone direct. All you need is to keep a kitchen that is just for manufacturing but not opened to customers. Thus you don’t have to pay high rent for leasing a place for the cake shop.”

Agnes replied, “It looks workable but I’m worried about the risks involved in running an online cake shop. Let alone the above, we will then need to deliver the cake to the customers, by which I have to buy a lorry and hire a driver for the delivery. Will it lead to even more risks?”

Michael said, “Don’t worry, there is always risks associated with doing business. Some are speculative risks while others would be pure risks. For the pure risks, we can take out insurance to protect against them.”

Questions:

a) What is speculative risk and pure risk and why these two have to be distinguished? Give one example for each with reference to Agnes’ cake shop. (6 marks)

b) What risks do you think Agnes may involve if she buys a lorry and hires a driver for delivery. Suggest corresponding insurance that Agnes can take out. (12 marks)

c) Let alone Michael’s view, what other risks do you think Agnes may need to face even if she sells her cakes online? Suggest one corresponding insurance that she can take out as protection.

(12 marks)

Suggested answer:

a) Speculative risk is a kind of risk that will result in either a gain or a loss (1 mark) e.g. Agnes's cake shop may not succeed though Agnes is good at making cakes but there is no guarantee that general public would like it (1 mark)

Pure risk is a kind of risk that will result in either loss or no loss (1 mark) e.g. Agnes' kitchen may be on fire (1 mark)

It is important to distinguish speculative from pure risk since speculative risk generally cannot be insured while many pure risks can be protected through insurance (2 marks)

(Total = 6 marks)

b) The risks involved for buying a lorry and hiring a driver for delivery:

- The lorry may knock down passenger or damage other people's property
- The lorry may be damaged by accident
- The driver may be injured

(2 marks each, total = 6 marks)

Insurances that can be taken out:

- motor insurance with third party coverage since it covers the injury to third party and damage to third party's property
- motor insurance with comprehensive coverage since it also covers the damages of Agnes's lorry caused by many different reasons
- Employees' compensation insurance since it covers injury to employee when working

(2 marks, total = 6 marks)

c) Other risks

- The kitchen may be on fire
- Visitors e.g. Agnes's friends to the kitchen may be injured
- Employees in the kitchen may get injured
- Employee may steal the food stuff from the kitchen

(Any three, 2 marks each, total = 6 marks)

Insurance applicable:

- Comprehensive insurance for business
- Public liability insurance
- Employees' compensation insurance
- Fidelity insurance

(Any three, 2 marks each, total = 6 marks)

(All together = 30 marks)