

**EXAM 6 – CANADA, FALL 2012**

15. (1.5 points)

a. (0.5 point)

Briefly describe two objectives of Employment Insurance (EI).

b. (0.5 point)

Explain how the EI program is financed.

c. (0.5 point)

Briefly describe the tax treatment of EI with respect to premiums and benefits.

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c)

Most candidates correctly identified that area-based uses the average production for an area while individual yield uses the insured's farm only. Many candidates only received partial credit because they did not also identify that in the individual yield program, compensation is based on the farm's total output so better than expected production on some fields can offset worse than expected production on other fields.

## Question 15

### Answer key:

a)

- Employment Insurance provides individuals with temporary income replacement as a result of employment interruptions
- It promotes active re-employment assistance to help unemployed workers to find and create jobs

b)

- Contributions from employers and employees
- Some programs funded with general tax revenues

c) Any 2 of:

- EI premiums are a tax-deductible expense to the employer
- EI premiums paid by employers do not give rise to taxable income for the employee
- EI Premiums paid by employees receive tax credit
- EI benefits are taxable income for recipient

### Actual candidate answer for full marks:

a.

- 1) provide temporary income replacement for those lost their jobs not from their own fault
- 2) encourage people to go back to the workforce. For example, some training programs are provided.

b. It is financed by employees, employer, and general revenue tax

c.

Premium paid by employers are tax-deductible expense.

Premium paid by employees can receive tax-credit

Benefits are taxable income.

### Examiner's report:

a)

This question was generally well done. Some candidates gave two variations on the theme of "temporary income replacement as a result of employment interruptions" (such as job loss / disability / maternity) and did not mention re-employment assistance – these candidates received partial credit.

b)

Candidates were required to mention that contributions come from both employers and employees in order to receive credit. Many candidates correctly identified contributions from employers and employees but did not mention general tax revenues – these candidates received partial credit.

c)

This question was generally well done. Because the question was not specific in asking for two points, full credit was given for any response that contained two correct points, even if it also contained some incorrect points. The most common error was stating that “contributions are tax-deductible” without specifying whose contributions (employer’s or employee’s).

## Question 16

### Answer key:

a)

- Under an optional system, the barrier has been adverse selection. (Candidates not required to use the specific term “adverse selection” as long as they explain the concept.)
- Insurers may select against homeowners by only making the policy available in areas considered to be safe, OR homeowners may select against insurers by only buying the policy in areas they consider prone to flooding.
- Also accepted:
  - Insurers would not be able to offer affordable premiums, premiums would be too high
  - Homeowners may select against insurers by only buying the policy in areas they consider prone to flooding.

b)

- Include flood insurance (bundle it) into standard homeowner insurance policies

c)

- Rates : should be risk based (commensurate with the risk), not all the same
- Deductibles : Higher risks customers should be subject to higher deductibles
  - Could vary depending on area (higher risks)
- Eligibility : 1 of the 2 following
  - Some very high risk flood risk might be uninsurable (excluded)
  - The industry should strive to covers most homes

d)

- Risk based premium will ensure the program is sustainable
- High deductibles will serve as a deterrent to occupy flood risk are
- Eligibility : 1 of the 2 following
  - Disincentive for development/location in high flood risk
  - Reduce the burden on the insurance community after a large event
  - Help ensure that insurance coverage for low risk property owners remains affordable

Also Accepted:

- Fair
- Reduce morale hazard
- Will avoid adverse selection

e)

Against: government prescribed rates (uniform) might not encourage risk reducing behavior

Also Accepted:

- Private insurers are more efficient