10. (2 points)

A state uses an assigned risk plan to provide insurance for consumers who are unable to obtain coverage in the voluntary market. This year, there were 5,000 applicants to the assigned risk plan.

The following table gives data for insurance companies in the voluntary market (all values in thousands of dollars):

| Company | Written Premium | Earned Premium | Surplus |
|---|---|---|---|
| A | 5,000 | 6,000 | 3,333 |
| B | 3,000 | 2,500 | 1,500 |
| C | 2,000 | 1,500 | 605 |

a. (0.5 point)

Calculate the number of applicants assigned to insurance company B.

b. (1.5 points)

Explain how coverage is obtained under the following residual market plans, with respect to the applicant and the insurer:

- An assigned risk plan
- A reinsurance facility
- A Joint Underwriters Association

CONTINUED ON NEXT PAGE

- The program being expected to continue indefinitely
- The program not being fully funded
- The benefit formula favoring certain groups such as large families, older people, and disabled people

b. A wide range of correct answers were accepted. As this question refers to a possible policy change which could be implemented in different ways, answers were accepted that could refer to the policy change under a variety of assumptions.

- The program will continue to be compulsory (as the question made no reference to any change)
- The program will no longer be compulsory as individuals choosing to invest their own contributions would effectively be opting out of the current program
- Benefits will be more skewed to higher wage earners since the "bended" benefit formula will no longer apply
- Actuarial equity will be enhanced; social adequacy will be reduced
- The formula will no longer favor groups such as larger families, older workers, and the disabled
- Benefits will be inherently more unstable if based on the performance of individually managed accounts.
- Wealthier participants will tend to have more investment expertise, which can increase the discrepancy in benefit levels for different earnings cohorts.
- Wealthier participants may have other sources of retirement income and therefore be able to comfortably take more risk and earn greater returns, while less wealthy participants may need the benefits more and be unable to risk their accounts in higher-yield investments
- There may no longer be a minimum floor of benefits
- Wealthier recipients may have less incentive to invest wisely if there is a benefit cap and they would not personally benefit from gains in their accounts beyond a certain level
- There would no longer be intergenerational transfer
- The program would now be fully funded
- Since current contributions would go to individual accounts, there would be no source for payments to current recipients
- Beneficiaries living longer would no longer be protected with a lifetime income

9. Examiner's Report

a. This part was answered successfully by many candidates, as a candidate who read and absorbed the material would succeed on this part most of the time. Common errors included providing overlapping answers – for example, not fully funded is another explanation of intergenerational transfer.

b. A wide range of correct answers were accepted, and candidates who made reasonable assumptions and provided logical conclusions in support of those assumptions received credit.

10. Sample Answers

a.

Sample 1

Company writes 3,000 of the (5000+3000+2000) WP in the market = 30% of market (voluntary)

5000 x 0.3 = 1500 applications will be assigned to company B.

Sample 2

Assigned base on market share premium
A – 5M / 10M = 50% x 5000 = 2500
B – 3M / 10M = 30% x 5000 = 1500 # of applicants
C – 2M / 10M = 20% x 5000 = 1000

b.

Sample 1

Assigned Risk Plan

1. Insured applies to company in voluntary market
2. Voluntary market denies coverage
3. Insured applies to the assigned risk plan
4. Assigned risk plan assigns the insured to a company
    a. # of insured assigned to each company depends on voluntary market share

Reinsurance Facility

1. Insured applies to company in voluntary market
2. Company decides whether to write as voluntary risk or to write & cede to the risk to the reinsurance facility

Joint Underwriting Association

1. Insured applies to company in voluntary market
2. Company decides whether to write as voluntary or forward to one of the carriers who service the JUA
3. If forwarded, the carrier will service account for the JUA

Sample 2

Assigned Risk Plan: The insured applies to the assigned risk plan after being rejected by the voluntary market. He or she if than assigned to an insurer based on market share of WP.

Reinsurance Facility: Insured applies to a company but is too high a risk than what the company normally accepts. The company writes the insured but then cedes all premiums and loss to the reinsurance facility.

Joint Underwriting Association: The insured applies to an insurer who would reject them due to their high risk, so the insurer passes the application on to the Joint Underwriters Association who proceeds to write them.

10. <u>Examiner's Report</u>

a. This question applied a straightforward concept (allocation of assigned risk policies among insurers) to a specific example. Most candidates did well on this part. The most common error was the allocation of assigned risk policies by earned premium.

b. Although this question was similarly straightforward, candidates sometimes confused the processes used by the various residual market plans.

<u>Assigned Risk Plan</u>

Each candidate needed to describe how the applicant obtains insurance under the ARP, which includes the following three elements

1 – Applicant applies to insurer
2 – Insurer denies the applicant
3 – Applicant applies to the ARP

Common errors on this portion included applicant applies to the insurer, gets denied, and then assigned directly to the ARP. Other answers neglected that the applicant must be rejected in the voluntary market first before applying to the ARP.

Each candidate needed to describe how the insurer obtains coverage under the ARP. Responses needed to mention the assignment of residual market applicants to insurers by the ARP. The most common error here was candidates not being clear who was assigning the residual policies to the insurer.

<u>Reinsurance Facility</u>

Each candidate needed to describe how the applicant obtains insurance under the RF. Candidates must mention the applicant applies for insurance in the voluntary market. Common errors on this portion included not addressing what the applicant does or applying directly to the RF.

Each candidate needed to describe how the insurer obtains coverage under the RF. Responses must illustrate the insurer has to make the decision on whether or not to cede the risk to the facility. A common error was to imply that all applicants were then ceded to the facility after they applied to an insurer. Candidates using insurer actions other than 'cede' were required to explain what they meant. These responses used terminology like sends, forwards, gives policies or applicants to the RF. For these responses acceptable clarification needed to include that the insurer handles all claims and services the policy or that the candidate understands that the policy if being reinsured and not physically moved to the RF.

<u>Joint Underwriting Association</u>

Each candidate needed to describe how the applicant obtains insurance under the JUA. Acceptable answers must mention the applicant applies for insurance in the voluntary market. Common errors on this portion included not addressing what the applicant does or the applicant applying directly to the JUA.

Each candidate needed to describe how the insurer obtains coverage under the JUA. Responses must demonstrate that the insurer has the decision on whether or not to forward the applicant to a servicing carrier of the JUA. Common errors include the applicant applying directly to the JUA or if they applied to an insurer they were automatically forwarded to a JUA carrier. Candidates implying other verbiage such as send, pass, give, cede in lieu of 'forward the applicant' was required to explain that they understood the policy was given to one of the servicing carriers to write and service the policy.

11. <u>Sample Answers</u>

**Property-casualty insurance plans**

NFIP

a. NFIP Program
b. Gov't acts as U/W, voluntary sector services policies only without bearing any U/W risk through WYO program
c. Fill unmet need
   OR
   Achieve social purpose
d. Successful to a certain extent but flood coverage is still not available in some areas that local authority doesn't cooperate
   OR
   Still has to borrow heavily from government after Hurricane Katrina
   OR
   Rates are inadequate