

EXAM 6 – UNITED STATES, SPRING 2016

15. (5.5 points)

Using only the following year-end 2014 information for an insurance company that started operations in 2013:

Balances as of year-end 2014

Agents' balances less than 90 days past due	14,000	Agents' balances more than 90 days past due	1,800
NAIC Class 2 bond, amortized cost	700,000	NAIC Class 2 bond, fair value	650,000
NAIC Class 4 bond, amortized cost	275,000	NAIC Class 4 bond, fair value	225,000
Cash and cash equivalents	534,000	Deferred acquisition costs	32,500
Net unearned premium	575,000	High-deductible unpaid losses below the deductible	125,000
Admitted deferred tax asset	27,500	Deferred tax liability	12,500

Information from 2014 Schedule P – Part 1 – Summary

		Years in Which Premiums Were Earned and Losses Were Incurred	
		2013	2014
Premiums Earned	Direct & Assumed	1,000,000	1,200,000
	Ceded	90,000	80,000
Loss Payments	Direct & Assumed	300,000	250,000
	Ceded	32,000	26,000
Defense and Cost Containment Payments	Direct & Assumed	22,000	7,000
	Ceded	800	400
Adjusting and Other Payments	Direct & Assumed	50,000	45,000
	Ceded	1,200	900
Salvage and Subrogation Received		19,000	11,000
Losses Unpaid	Case Basis	Direct & Assumed	100,000
		Ceded	10,000
	Bulk + IBNR	Direct & Assumed	150,000
		Ceded	5,000
Defense and Cost Containment Unpaid	Case Basis	Direct & Assumed	25,000
		Ceded	500
	Bulk + IBNR	Direct & Assumed	35,000
		Ceded	1,500
Adjusting and Other Unpaid	Direct & Assumed	12,000	
	Ceded	100	
Salvage and Subrogation Anticipated		8,000	16,000

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EXAM 6 – UNITED STATES, SPRING 2016

15. (continued)

a. (1.75 points)

Calculate the 2014 year-end statutory net admitted assets.

b. (2.75 points)

Calculate the 2014 year-end statutory liabilities.

c. (1 point)

Using only the information provided above, briefly describe how four balance sheet items would be treated differently under GAAP as compared to SAP.

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SAMPLE ANSWERS AND EXAMINER'S REPORT

QUESTION 15	
TOTAL POINT VALUE: 5.5	LEARNING OBJECTIVE: C1 & C3
SAMPLE ANSWERS	
Part a: 1.75 points	
2014 Net Admitted Assets = +14,000 agents balances less than 90 days past due +700,000 Class 2 bonds at amortized cost +225,000 Class 4 bonds min(amortized cost, fair value) +534,000 Cash and cash equivalents +15,000 (27,500-12,500) Admitted deferred tax asset less deferred tax liability = 1,488,000	
Part b: 2.75 points	
2014 Year-End Statutory Liabilities = +Net Unpaid Loss Case AY 2014 =105,000 (120,000-15,000) +Net Unpaid Loss Case AY 2013 = 90,000 (100,000-10,000) +Net Unpaid Loss IBNR AY 2014 = 180,000 (200,000-20,000) +Net Unpaid Loss IBNR AY 2013 = 145,000 (150,000-5,000) +Net Unpaid DCC Case AY 2014 = 29,000 (30,000-1,000) +Net Unpaid DCC Case AY 2013 = 24,500 (25,000-500) +Net Unpaid DCC IBNR AY 2014 = 38,000 (40,000-2,000) +Net Unpaid DCC IBNR AY 2013 = 33,500 (35,000-1,500) +Net Unpaid A&O AY 2014 = 17,800 (18,000-200) +Net Unpaid A&O AY 2013 = 11,900 (12,000-100) +Net Unearned Premium = 575,000 =1,249,700	
Part c: 1 point	
<ul style="list-style-type: none"> • Non-admitted assets are recognized; agents balances more than 90 days past due included as an asset unless deemed uncollectible • Deferred acquisition costs (32,500) are an asset amortized over the life of the policy • Bonds may be held at different values based on intended use (i.e. whether they are held for sale at fair value, held for trade at fair value, or held to maturity at amortized cost) • Reserves are held gross of reinsurance ceded recoverables with a separate reinsurance recoverable asset; reserves are held gross of reinsurance; reinsurance recoverables are an asset • Reserves must be held net of salvage/subrogation • Deferred tax asset is not held to same strict admissibility test; deferred tax asset is recognized and a valuation allowance established when it is more likely than not to be realized • Unpaid losses under high deductible policies are treated as an asset and either loss reserves are grossed up for high deductible losses OR a separate liability for high deductible losses is established 	
EXAMINER'S REPORT	
There were a number of items to include in the calculations, but all items are clearly discussed in the syllabus material. Candidates scored well on sub-part a. and c., but had difficulty with sub-part b.	

SAMPLE ANSWERS AND EXAMINER'S REPORT

Part a
<p>The candidate was expected to know what items are included in statutory net admitted assets. The candidate was expected to provide the correct calculation of net admitted assets. Common mistakes included:</p> <ul style="list-style-type: none">• Not reducing the deferred tax asset by the deferred tax liability in calculating the net admitted tax asset• Improper valuation of bonds• Including extra items (i.e. unearned premium, net earned premium, high deductible unpaid losses below deductible; reinsurance recoverables, deferred acquisition costs)• Omitting agents' balances entirely or including balances greater than 90 days past due
Part b
<p>The candidate was expected to know the items that make up statutory liabilities. Candidates needed to recognize that both accident years 2013 and 2014 net unpaid reserves for loss, DCC and A&O needed to be included in the calculation, as well as net unearned premium reserves. Different methods of calculating the total net reserves were accepted as long as the final figure was correct. Common mistakes included:</p> <ul style="list-style-type: none">• Not including unpaid amounts from accident year 2013 or 2014 in the calculations• Including anticipated salvage/subrogation as a deduction in calculating net loss reserves (if Schedule P shows anticipated salvage/subrogation, these figures have already been removed from the loss reserves)• Including incorrect items (i.e. loss, DCC or A&O payments, high-deductible unpaid losses, deferred acquisition costs, deferred tax liability, salvage/subrogation received)• Calculating change in reserves or incurred amounts (i.e. paid plus change in reserves)• Not subtracting the ceded unpaid amounts
Part c
<p>The candidate was expected to know the difference between SAP and GAAP accounting with respect to the balance sheet items presented in the question. Candidates had to correctly identify four items that would be treated differently under GAAP. Common mistakes included:</p> <ul style="list-style-type: none">• Listing less than four items• Listing the SAP treatment of the item, but not the GAAP treatment• Listing general differences between SAP and GAAP that were not discussed in the question (i.e. discounting of reserves, non-admitted assets like furniture)• Listing that deferred tax asset in not offset by deferred tax liability