15. (4.25 points)

Given the following excerpts from an insurance company's 2015 Balance Sheet and Income Statement:

	Current Year
Stocks	281,000
Premiums earned	220,000
Losses incurred	147,000
Losses unpaid	135,000
Cash	113,000
Bonds	76,000
Unearned premiums	60,000
Loss adjustment expenses unpaid	36,000
Other underwriting expenses incurred	34,000
Uncollected premiums and agents' balances in the course of collection	32,600
Current federal and foreign income taxes unpaid	30,000
Loss adjustment expenses incurred	23,000
Net realized capital gains (losses) less capital gains tax	14,500
Other expenses unpaid	9,000
Advance premium	830
Ceded reinsurance premiums payable (net of ceding commissions)	600
Amounts recoverable from reinsurers	400
Provision for reinsurance	170

a. (3.5 points)

Calculate the insurance company's 2015 policyholders' surplus using the balance sheet items above. Assume all assets are admitted.

b. (0.75 point)

Assume that 10% of uncollected premiums and agents' balances in the course of collection become more than 90 days past due. Fully describe the impact this would have on the company's policyholders' surplus as well as net income.

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QUESTION 15	
TOTAL POINT VALUE: 4.25	LEARNING OBJECTIVE: C1

SAMPLE ANSWERS

Part a: 3.5 points

Sample answers include:

Sample 1

PHS = (Stocks + Cash + Bonds + Uncollected premiums and agent's balances in the course of collection + Amounts recoverable from reinsurers) – (Losses unpaid + Unearned premiums + Loss adjustment expenses unpaid + Current federal and foreign income taxes unpaid + Other expenses unpaid + Advance premium + Ceded reinsurance premiums payable (net of ceding commissions) + Provision for reinsurance)

PHS = (281,000 + 113,000 + 76,000 + 32,600 + 400) – (135,000 + 60,000 + 36,000 + 30,000 + 9,000 + 830 + 600 + 170) = 503,000 – 271,600 = 231,400

Sample 2

Assets: 281,000 + 113,000 + 76,000 + 32,600 + 400 = 503,000

Liabilities: 135,000 + 60,000 + 36,000 + 30,000 + 9,000 + 830 + 600 + 170 = 217,600

Surplus: 503,000 – 271,600 = 231,400

Sample 3

281K – 135K + 113K + 76K – 60K – 36K + 32.6K – 30K – 9K – 0.83K – 0.6K + 0.4K – 0.17K = 231.4K

Part b: 0.75 point

Sample answers include:

Sample 1

PHS would decrease by 10% * 32,600 = 3,260 due to those assets now being non-admitted. Net income would not change

Sample 2

10%(32,600) = 3,260

Policyholders surplus would decrease by 3,260 because this would become non-admitted and thus not count toward surplus

Net income would stay the same (assuming the balances are not written off)

Sample 3

10% of Agents Balances = 3,260

This would now be treated as a non-admitted asset and the change in its value would directly impact surplus

The net income would be reduced if the company deemed the 3,260 uncollectible and decided to write it off

EXAMINER'S REPORT

Candidates were expected to use the balance sheet items to calculate the PHS, recognizing which items were assets and liabilities and which were income statement items. They were expected to recognize that agents' balances >90 days past due would become non-admitted assets and would reduce PHS, but not affect net income (unless written-off).

Part a

Candidates were expected to calculate policyholder surplus using all elements provided from the Balance Sheet.

Common errors include:

- Including income statement items in the calculation
- Categorizing an asset as a liability or a liability as an asset
- Not including certain Balance Sheet items – most commonly Advance Premium

Part b

Candidates were expected to recognize that the amount > 90 days past due would become non-admitted causing a direct charge to surplus of $3,260, and would have no effect on net income (unless assumed it was written-off).

Common errors include:

- Not mentioning the specific amount by which PHS would be reduced
- Saying net income would be reduced without stating the assumption that the company decided to write off the non-admitted asset
- Not recognizing that the 10% would become a non-admitted asset