14. (2.5 points)

The following information is reported on an insurance company's 2016 Schedule F, Part 9 (all figures are in thousands of dollars).

		As Reported (Net of Ceded)
ASSETS		
1	Cash and Invested Assets	900
2	Premiums and considerations	80
3	Reinsurance recoverable on loss and LAE payments	50
4	Funds held by or deposited with reinsured companies	150
5	Other assets	20
6	Net amount recoverable from reinsurers	0
7	**Totals**	**1,200**
LIABILITIES		
8	Losses and LAE	500
9	Unearned premiums	100
10	Advance premiums	10
11	Dividends declared and unpaid	80
12	Ceded reinsurance premiums payable	30
13	Funds held by company under reinsurance treaties	100
14	Provision for reinsurance	60
15	**Total Liabilities**	**880**
16	**Surplus**	**320**
17	**Totals**	**1,200**

- Ceded loss and loss adjustment expense reserves are 250 in Schedule P, Part 1.
- Ceded unearned premium reserves are 40 in Schedule F, Part 3.

a. (2 points)

Restate the balance sheet above to a gross of ceded basis.

b. (0.5 point)

Briefly describe one strength and one weakness of using Schedule F as a solvency monitoring tool.

CONTINUED ON NEXT PAGE

- There is a large proportion of non-admitted assets meaning they can't be liquidated quickly and could be at risk of being uncollectible.

EXAMINER'S REPORT

Candidates were expected to complete the bond carrying values on a balance sheet and use the balance sheet to evaluate any concerns on the financial health of the insurance entity.

Part a

Candidates were expected to calculate the carrying value of each bond. This meant the use the amortized cost for the bond rated 1, and the minimum of the fair value and amortized cost for bonds rated 3 & 6.

Common errors include:

- Using the amortized cost for the bond rated 3
- Using amortized cost for the bond rated 6
- Using the actual cost for the bond rated 6.

Part b

Candidates were expected to identify and explain three concerns with the balance sheet.
Common errors include:

- Identifying a concern, but not giving an explanation on why it is concerning
- Only identifying 2, 1, or no concerns
- Listing the proportion of preferred to common stocks as a concern, but not the amount of total stocks as a concern
- Listing that the 6 rated bond was a concern, but not the overall mix of bond ratings.
- Listing amount recoverable from reinsurance. There is not enough information available, without looking at Schedule F, to determine whether the level of recoverables is problematic

QUESTION 14	
TOTAL POINT VALUE: 2.5	**LEARNING OBJECTIVE: C1**

SAMPLE ANSWERS

Part a: 2 points

Sample 1

1) 900
2) 80
3) 0
4) 150
5) 20
6) 150
7) 1300

8) 500+250=750
9) 100+40=140
10) 10
11) 80
12) 0
13) 0
14) 0
15) 980
16) 320
17) 1300

Sample 2

If not listed below, those items remain the same.

	Assets	Adjustment	gross basis
Item:	3.	-50	0
	6.	+150	150
		+100	

(Assume no pooling)

Liab		
8	+250	750
9	+ 40	140
12	− 30	0
13	−100	0
14	− 60	0
	100	

total liab: 880+100=980
surplus = 320 ~ assets = 980+320=1300
1300=1200-50+net amount recovered from reinsurer
~ asset item 6=150

Part b: 0.5 point

Sample Responses for Strength

- formulaic and easy to compare (& understand) between years and between companies
- It is formulaic, so not easy to manipulate
- provides information regarding slow paying and unauthorized reinsurers, which may present a credit risk
- Allows review of impact on surplus if all contracts were cancelled
- Retrospective, not prospective, so won't consider changes because of growth of catastrophe potential

- it shows the amounts that are in dispute w/ reinsurers. This can be indicative of a company trying to overcollect from reinsurers because they are in financial trouble

Sample Responses for Weakness

- Doesn't take into consideration the reinsurers' financial strength
- It is purely formulaic and doesn't consider management input
- Provision for reinsurance penalizes unauthorized reinsurers even though they may be more financially strong or more affordable
- The calculation of the provision for reinsurance has no statistical/actuarial basis so it could give a false sense of reinsurance collectability
- Gives false sense of accuracy due to complexity

EXAMINER'S REPORT

Candidates were expected to demonstrate an understanding of the impact of reinsurance on the statutory balance sheet, as well as strengths and weaknesses of Schedule F in monitoring solvency.

Part a

Candidates were expected to restate the given statutory balance sheet to a gross basis by identifying which of the provided items required adjustment, and by how much.

Common mistakes include:

- Adjusting surplus instead of net amount recoverable from reinsurers as a balancing item
- Providing a restated balance sheet that does not balance (no balancing item)
- Adjusting premiums and considerations instead of/in addition to unearned premiums
- Adjusting the funds held by or deposited with reinsured companies asset to 0
- Not adjusting the funds held by company under reinsurance treaties liability to 0
- Making adjustments in the wrong direction – for example subtracting 250 from losses and LAE (arriving at 250) instead of adding (to arrive at 750)

Part b

Candidates were expected to provide one strength and one weakness of using Schedule F as a solvency monitoring tool.

Common mistakes include:

- Noting a strength or weakness without supporting rationale – for example "formulaic" was a common response, which could be argued either way
- Noting the lack of qualitative information as a weakness without identifying an example (financial strength rating, management input, etc.)
- Noting that the provision for reinsurance provides an incentive for insurers to require quick reimbursement – while true, this does not relate to the use of Schedule F as a solvency monitoring tool
- Describing the general intent of Schedule F without supporting specific strengths – for example, "provides a net view of potential uncollectability in the provision for reinsurance"