16. (2 points)

The following information is provided from an insurance company's 2018 Annual Statement, which was filed on March 1, 2019:

- Policyholders' Surplus is $35,000,000
- Total Unpaid Loss & LAE is $95,000,000

Selected Notes to Financial Statements are as follows:

27. Structured Settlements

The company has purchased annuities, under which the claimant is the payee and the company is the owner of the annuity contract, to fund structured settlements. The statement value of these annuities is $1,300,000 as of December 31, 2018, and no release of liability has been signed.

31. High Deductibles

The company writes high deductible policies for which the total case reserves under the deductible is $15,000,000 as of December 31, 2018.

a. (1 point)

Evaluate the insurance company's credit risk based on the information provided above.

b. (1 point)

Contrast how uncollectible reinsurance is addressed in each of the following:

i. Notes to Financial Statements

ii. Statement of Actuarial Opinion

CONTINUED ON NEXT PAGE

- Vague responses, such as not identifying the purpose and/or holder of the collateral (e.g., saying "total collateral")
- Noting that the transaction related to premiums rather than loss and LAE
- Mixing up the concepts of recoverable and payable

FALL 2019 EXAM 6U, QUESTION 16	
TOTAL POINT VALUE: 2	**LEARNING OBJECTIVES: C1, D1**
SAMPLE ANSWERS	
Part a: 1 point	

Sample 1
For Structured Settlements, contingent liability is 1,300/35,000=3.7% of Surplus which is high considering disclosure is 1% for each life insurer the annuity is from. This is a significant amount of credit risk.
For High Deductible, the total case reserve under the deductible is 15.8% of total reserves and 43% of policyholder surplus. This is a significant portion of reserves and poses a high credit risk to the Company.
Overall the Company is exposed to a significant amount of credit risk from high deductible policies and structured settlements.

Sample 2
Subject to credit risk from the life insurer, as Company is the owner of the annuity, and no release of the liability is signed. The outstanding payment is $1.3 million from the life insurer. This is 3.7% of Policyholder Surplus, is material and requires disclosure on name of life insurer and outstanding payment if the annuity is purchased from only 1 life insurer.
Reserves under the deductible is $15 million, which is 42.9% of PHS and 15.8% of total unpaid loss and LAE reserves. This is material and the Company may not be potentially able to receive this amount, so substantial credit risk exists.

Sample 3
% Structured Settlement=1.3/35= 3.7%
% High Deductible=15/35=42%
There is credit risk from the Structured Settlement since the insurer did not get a signoff release. A 3.7% of surplus could be considered high if it comes from a single company/insured. There is a significant risk from the high deductible policy since it represents 42% of the PHS.

Part b: 1 point

Sample 1
In the notes to the Financial Statements, uncollectibility is a retrospective look at what is written off. In the SAO, it is made after conversations with management and looking at reinsurance companies and structures.

Sample 2

In the notes to the Financial Statements, the retrospective look of uncollectible amounts is shown. In the SAO, it is considering prospective risks posed by future uncollectible reinsurance. This may consider past experiences but also considers reinsurer's financial health.

Sample 3
The notes to the Financial Statements discuss reinsurance that has been deemed uncollectible in the past year; thus it has a retrospective view of collectability of reinsurance. On the other hand, the SAO must discuss the uncollectibility of reinsurance prospectively in order to determine if reserves are adequate including the risk of any collectability concerns of reinsurance.

EXAMINER'S REPORT

Candidates were expected to be able to identify where the credit risk was generated from the Structured Settlements and the High Deductible policies. Also, they were expected to determine the difference in how uncollectible reinsurance is addressed in the Notes to the Financial Statements and the Statement of Actuarial Opinion.

Part a

Candidates were expected to state that there was credit risk for the structured settlements. The candidate had to note the structured settlements credit risk was material by either the 1% standard or noting that it would depend on whether 1 or many life insurers issued the annuities. The candidate had to state that there was credit risk from the high deductible policies. The candidate had to mention that the risk was high or show a calculation of the deductible to surplus or unpaid loss and LAE.

Common errors include:

- Performing an RBC calculation to determine credit risk
- Accounting for structured settlements as paid loss
- Determining that since the company was holding case reserves for the high deductibles there was no credit risk
- Addressing credit risk with IRIS ratios
- Combining the structured settlement and high deductible amounts to determine credit risk

Part b

Candidates were expected to know that the Notes to the Financial Statements display amounts written off during the year and that it shows the history of uncollectible reinsurance. Candidates were expected to know that the SAO is concerned with the future collectability of reinsurance and its impact on the reserves.

Common errors include:

- Discussing the Note to unsecured reinsurance instead of uncollectible reinsurance
- Stating that uncollectible reinsurance was discussed in the Scope section or Opinion Section