Accounting Data

LEARNING OBJECTIVES	KNOWLEDGE STATEMENTS
A.5. Calculate the underwriting expense provisions underlying the overall rate level indication. *Range of weight: 0-5 percent*	**a. Expense categories (e.g., commission, general, other acquisition, taxes, licenses, and fees)** **b. Sources of data and selection criteria**

This section will discuss the expenses of an insurer that may not be able to be attributed to an individual policy or an individual claim. This will be a very short section, and exam problems do not generally come from this section.

Types of Data from Accounting

In addition to the detailed policy and claim data that we've previously discussed, some data of interest to actuaries is only available from accounting. Accounting primarily stores the data at a level needed for financial reporting, and as such the data is highly summarized.

The types of data that can be obtained from accounting include the following items that relate to an insurance company's income:

- **Summarized policy and claim data:** This would include total premiums, losses, and ALAE broken down by line of business and various types of years (accident year, calendar year, report year, policy year). Actuaries typically prefer to obtain this information at a more granular level directly from the policy and claims databases. Furthermore, accounting may not even have exposure data since exposures are often not reported on financial statements.
- **Reinsurance data:** In some cases when reinsurance applies to a group of policies or claims, the data cannot be obtained at a policy or claim level. In those cases, the reinsurance data can still be obtained from accounting.
- **ULAE:** The costs for things like claims adjuster salaries and the rent for claims office buildings can usually only be attained from accounting. Even though this data is not at the claim level, it typically must still be allocated to line of business for financial reporting.
- **Underwriting expenses:** These are the expenses in the acquisition and servicing of policies. This will be further discussed on the next page.
- **Investment data:** This would include information about the insurer's investment expenses and income from investing money in things like stocks, bonds, and real estate.

Underwriting Expenses

Underwriting expenses, also known as operational and administrative expenses, can be broken down into 4 categories:

1. **Commissions and brokerage:** These are the amounts paid to insurance agents or brokers as compensation for selling policies. Commissions are usually based on written premium, and can vary by insurer, line of business, distribution channel (exclusive or independent agents), and between new policies and policy renewals. While some commissions can be obtained at the policy level, bonuses for generating high quality or a high volume of business cannot generally be thought of at the policy level.
2. **Other acquisition:** These are costs, other than those included in commissions and brokerage, to attract or retain customers. This would largely include media advertising, whether through television, printed mailings, or internet advertisements. Also, note that for insurers that have a direct distribution channel that don't pay commissions to agents, their acquisition costs would primarily fall in this category.
3. **General:** This includes all other costs associated with running the insurance company excluding investment costs. In terms of personnel as an example, this includes the salaries of accounting, actuarial, janitorial, underwriting, human resources, and the CEO.
4. **Taxes, licenses, and fees:** This includes premium taxes and fees, but does NOT include federal income tax for the insurer.

Accounting Allocations

Policy and claims data is granular, so we know which line of business each claim or policy is classified under. This granularity for line of business is not readily apparent for most accounting data.

For example, take the salary of the CEO of an insurer. It is natural to express the total salary on a calendar year basis. However, if for an analysis or financial reporting purposes you wanted to break down the CEO's salary by line of business for that calendar year, you would need some method of allocating the salary to that level of granularity. In the case of the CEO, you might use something like earned or written premium for the calendar year by line of business to allocate the salary to a line of business level.

These types of allocation rules may be set by the insurer's finance, accounting, or actuarial departments. Sometimes the allocations are obvious, such as when an underwriter only works on personal auto policies, or when a claims office only contains homeowners claims adjusters. In other cases, the allocations can be based on any measure chosen by the insurer.

In terms of financial reporting, all insurer expenses have to be allocated to line of business for the Insurance Expense Exhibit. Also, all Unallocated Loss Adjustment Expenses must be allocated to accident year for Schedule P of the Annual Statement, though this allocation is done by formula.