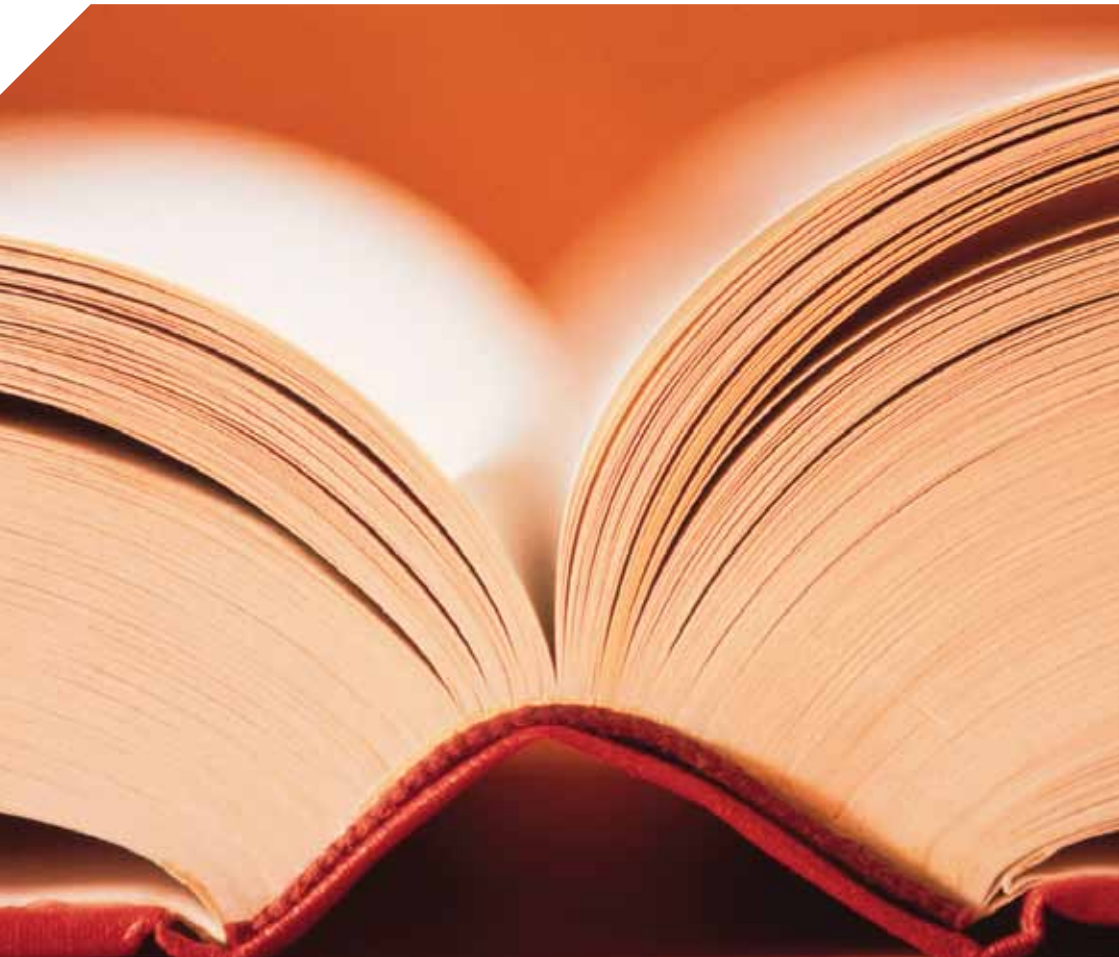


RE•IN•SUR•ANCE:

A Basic Guide to Facultative and
Treaty Reinsurance



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This publication is intended only as a reference tool for the insurance and reinsurance industry. While the publication is designed to provide general information with regard to the subject matter covered, it does not address all of the technical aspects of a defined term or topic and does not constitute a legal consultation or legal opinion. No decision should be made on the basis of the definitions or the overview provided herein. Instead, readers should consult with legal counsel. The definitions or the overview contained herein are intended to apply only to property and casualty reinsurance.

INTRODUCTION

Munich Re stands for solution-based expertise, consistent risk management, financial stability and client proximity. Our clients trust us to develop solutions for the whole spectrum of reinsurance – from traditional reinsurance agreements to the management of complex specialty reinsurance risks.

Our U.S. operations is, on a standalone basis, one of the largest property-casualty reinsurance companies in the United States. Together with our affiliates, American Modern Insurance Group and Hartford Steam Boiler Group, we deal with the issues that affect society and work to devise cutting-edge solutions that render tomorrow's world insurable. Our recipe for success: we anticipate risks early on and deliver solutions tailored to clients' needs, creating opportunities to achieve sustained profitable growth.

This book is intended to be a brief and basic introduction to reinsurance concepts. The numerical examples given are merely to illustrate the concepts discussed, and are not intended to suggest any particular price or condition for any of the reinsurance described. We have also included a comprehensive glossary of terms used to understand these concepts. For additional information, however, the reader should consult more comprehensive reinsurance publications.

Keep in mind that developing a financially sound reinsurance program must take into account the unique risks that an insurer faces. Our professional specialists combine their expertise in applying the fundamental concepts found in this brochure with their extensive experience in designing reinsurance programs to address the unique needs of each client.

Please visit our website www.munichreamerica.com if you would like additional information about Munich Re.



WHAT IS REINSURANCE?

Reinsurance is a transaction whereby one insurance company (the “reinsurer”) agrees to indemnify another insurance company (the “reinsured, “cedent” or “primary” company) against all or part of the loss that the latter sustains under a policy or policies that it has issued. For this service, the ceding company pays the reinsurer a premium.

The purpose of reinsurance is the same as that of insurance: to spread risk. Reinsurance helps protect insurers against unforeseen or extraordinary losses by allowing them to spread their risks. For example, a catastrophic fire at an industrial enterprise could financially devastate its insurer. With reinsurance, no single insurer finds itself saddled with a financial burden beyond its ability to pay.

Functions of Reinsurance

The most common reasons for purchasing reinsurance include:

Capacity Relief

Allows the reinsured to write larger amounts of insurance.

Catastrophe Protection

Protects the reinsured against a large single, catastrophic loss or multiple large losses.

Stabilization

Helps smooth the reinsured's overall operating results from year to year.

Surplus Relief

Eases the strain on the reinsured's surplus during rapid premium growth.

Market Withdrawal

Provides a means for the reinsured to withdraw from a line of business or geographic area or production source.

Market Entrance

Helps the reinsured spread the risk on new lines of business until premium volume reaches a certain point of maturity; can add confidence when in unfamiliar coverage areas.

Expertise/Experience

Provides the reinsured with a source of underwriting information when developing a new product and/or entering a new line of insurance or a new market.

Providers of Reinsurance

Direct Writers

Reinsurers enter into reinsurance relationships directly with the ceding company. The collection of premiums and payment of claims are handled directly by the reinsurer.

Broker-Market Reinsurers

Assume business through reinsurance intermediaries (i.e. brokers) who typically negotiates reinsurance contracts between the ceding company and the reinsurer(s), and provide the production or sales support.

Brokers generally represent the ceding company and receive compensation in the form of commission, and/or other fees, for placing the business and performing other necessary services. The brokerage commission is almost always paid by the reinsurer. Typically, the broker will collect premiums and handle disbursements of claims payments.

Reinsurance Departments of Insurers

A primary insurance company's reinsurance department assumes reinsurance business.

Pools or Associations

Pools or associations consist of individual primary insurers that have banded together to increase their underwriting or large line capacity, premium capacity or to provide coverage for risks which are uninsurable by conventional means. Pools can be organized to provide insurance or reinsurance. Pools or associations are typically managed by a separate company which provides underwriting and loss handling experience and administration.

Regulation

Reinsurers are generally subject to many of the same regulations as primary insurers. Both insurers and reinsurers are mostly regulated at the state level, where state insurance departments create and enforce state regulations. Regulation of both insurance and reinsurance aims at ensuring the solvency of the insurer/reinsurer to pay claims on the contracts that it issues.

State insurance departments also license insurers/reinsurers to do business in their state.

Admitted Company (Authorized Company)

An insurer or reinsurer licensed to conduct business in a given state.

Non-Admitted Company (Un-authorized Company)

An insurer or reinsurer not licensed in a given state.

The National Association of Insurance Commissioners is an organization of the chief insurance regulatory officials of the 50 states, the District of Columbia, American Samoa, Guam, Puerto Rico and the Virgin Islands. Its purpose is to coordinate regulatory activities among these states and territories and provide a forum to discuss insurance issues

REINSURANCE CONCEPTS

Facultative and Treaty

There are essentially two types of reinsurance arrangements:

Facultative Reinsurance

Reinsurance transacted on an individual risk basis. The ceding company has the option to offer an individual risk to the reinsurer and the reinsurer retains the right to accept or reject the risk.

Treaty Reinsurance

A transaction encompassing a block of the ceding company's book of business. The reinsurer must accept all business included within the terms of the reinsurance contract.

Characteristics

Facultative (Individual Risk)	Treaty (Book of Business)
<ul style="list-style-type: none">- Individual risk review- Right to accept or reject each risk on its own merit- A profit is expected by the reinsurer in the short and long term, and depends primarily on the reinsurer's risk selection process- Adapts to short-term ceding philosophy of the insurer- A facultative certificate is written to confirm each transaction- Can reinsure a risk that is otherwise excluded from a treaty- Can protect a treaty from adverse underwriting results	<ul style="list-style-type: none">- No individual risk acceptance by the reinsurer- Obligatory acceptance by the reinsurer of covered business- A long-term relationship in which the reinsurer's profitability is expected, but measured and adjusted over an extended period of time- Less costly than "per risk" reinsurance- One treaty contract encompasses all subject risks

Pro Rata and Excess of Loss

Facultative and treaty reinsurance can be written on either a pro rata or excess of loss basis.

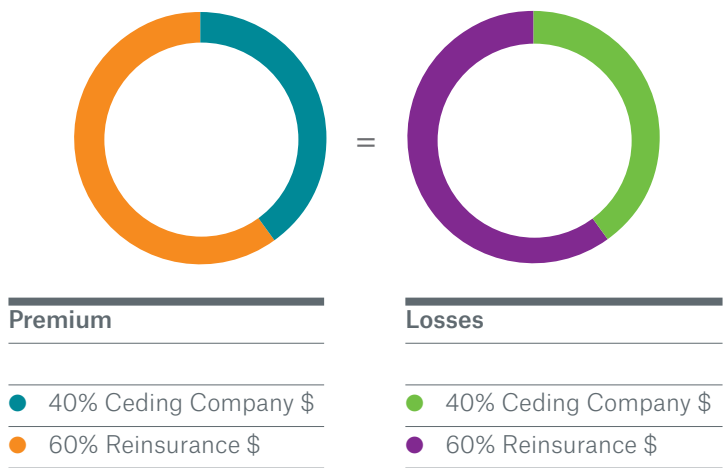
Pro Rata

A term describing all forms of quota share and surplus share reinsurance in which the reinsurer shares the same proportion of the premium and losses of the ceding company. Pro rata reinsurance is also known as “proportional reinsurance”.

Along with sharing proportionally in premium and losses, the reinsurer typically pays a ceding commission to the ceding company to reimburse for expenses associated with issuing the underlying policy.

Advantages

- Easy to administer.
- Good protection against frequency/severity potential.
- Protection of net retention on first-dollar basis.
- Permits recovery on smaller losses.



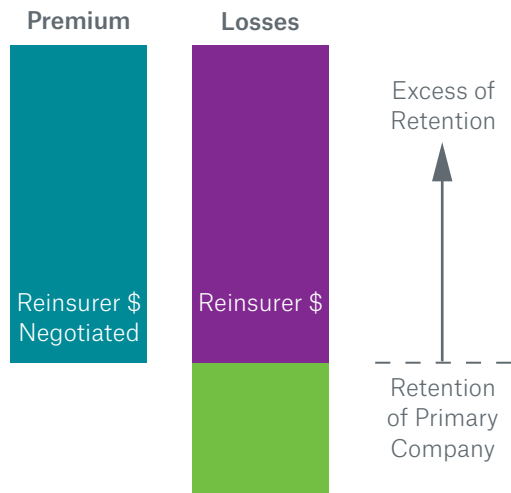
Excess of Loss

A term describing a reinsurance transaction that, subject to a specified limit, indemnifies a ceding company against the amount of loss in excess of a specified retention. Excess of loss reinsurance is also called “non-proportional reinsurance”

In excess of loss reinsurance, premiums are typically negotiated as a percentage of the primary insurer’s premium charge.

Advantages

- Good protection against frequency or severity potential, depending upon the retention level.
- Allows a greater net premium retention.
- More economical in terms of reinsurance premium and cost of administration.



APPLYING THE BASICS: FACULTATIVE REINSURANCE

Pro Rata

The ceding company and reinsured share premium and losses on specific risks in proportion to an agreed percentage.

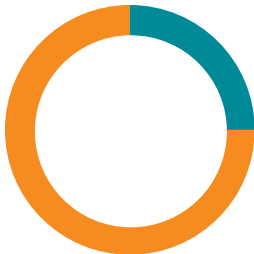
Example 1

Commercial Umbrella Policy Limit	\$1,000,000
Annual Premium	\$10,000

The ceding company retains 25% net and places 75% facultative reinsurance on a pro rata basis. Reinsurance participation is expressed as \$750,000 (75%) part of \$1,000,000.

Premium

The premium due the reinsurer is \$7,500 (75% of \$10,000) less the ceding commission it pays to the ceding company to defray expenses and acquisition costs.



Premium = \$10,000

- \$2,500 Premium (25% Ceding Company)
- \$7,500 Premium (75% Reinsurer)

Losses

If a covered loss of \$400,000 occurs, the ceding company would pay \$100,000 (25% of \$400,000), and the reinsurer would pay \$300,000 (75% of \$400,000).



Loss = \$400,000

- \$100,000 (25% Ceding Company)
- \$300,000 (75% Reinsurer)

Example 2

Restaurant/Hotel, 100% PML (Probable Maximum Loss)

Buildings	\$ 10,000,000
Contents	\$ 2,000,000
Total Insurable Value (TIV)	\$ 12,000,000

Annual Premium	\$ 20,000
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Because of potential high severity of loss from a burn-out situation (100% PML), pro rata protection is appropriate. If the ceding company's net retention is 80% and a reinsurer participates at 20%, a 20% pro rata protection on each and every loss will result.

Premium

The reinsurer receives 20% of the premium (\$4,000) less a ceding commission.

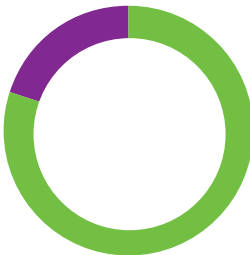


Premium = \$20,000

- \$16,000 Premium (80% Ceding Company)
- \$4,000 Premium (20% Reinsurer)

Losses

Assuming a loss of \$9,000,000, the ceding company would pay 80%, or \$7,200,000, and the reinsurer would pay 20%, or \$1,800,000.



Loss = \$9,000,000

- \$7,200,000 (80% Ceding Company)
- \$1,800,000 (20% Reinsurer)

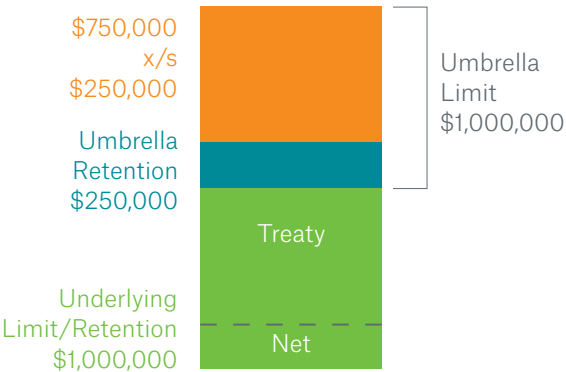
Excess of Loss

Excess of loss facultative placements require an analysis of potential severity of losses. The ceding company selects a loss level compatible with net and treaty guidelines and uses this as its retention. The facultative reinsurer provides a limit of reinsurance in excess of this retention.

Example 1 (see page 8)

Commercial Umbrella Policy Limit	\$ 1,000,000
Annual Premium	\$ 10,000

Assume the ceding company also writes a \$1,000,000 underlying policy. Its net and treaty retention may be limited to \$1,250,000 per risk. Since the total combined limit of the two policies is \$2,000,000, the reinsurance cover is excess of the net and treaty retention, expressed as \$750,000 excess \$250,000 excess underlying (\$1,000,000)



Unlike premium determination for pro rata agreements, where premium to the reinsurer is the same as the percentage of risk assumed, excess layer pricing is based on various formula guidelines, the underwriter's evaluation of risk, primary rates, increased limits rates, and market conditions. Excess pricing may be net of commission or gross (before commission), depending on the arrangements between the ceding company and reinsurer.

Restaurant/Hotel, Fire Resistive 4-story Office Building
(2-story PML)

Because loss severity is not expected (note PML estimate above), excess protection may be the most cost-efficient solution. If the ceding company retains the PML net and facultatively reinsures the remaining limit on an excess basis, the layering and possible price allocation might look like this:

Facultative Reinsurer:
\$6,000,000 excess \$6,000,000 \$5,000 Net Premium

	\$20,000 Premium	\$9,000,000 Loss
\$6,000,000 x/s \$6,000,000	Reinsurer \$5,000 Premium	Reinsurer Pays 3,000,000 (9,000,000 - 6,000,000)
Ceding Company Retention \$6,000,000	\$15,000 Premium	Ceding Company Pays \$6,000,000

Facultative Casualty Reinsurance

Typical Reinsurance Lines Of Business

- General Liability
- Umbrella
- Personal/Commercial Automobile
- Workers' Compensation and/or Employer's Liability
- Excess Liability

Generally, the above lines - except for Umbrella - are reinsured as excess transactions. However, reinsurers may provide pro rata reinsurance of excess layers. Umbrella/Excess Liability can be reinsured on a pro rata or excess of loss basis.

Capacity and attachment requirements vary by risk and reinsurer. Generally speaking, buffer layers can attach as low as \$250,000. Umbrella/Excess Liability often requires a minimum of at least \$1,000,000 underlying policy limits.

Facultative Property Reinsurance

Typical Reinsurance Lines Of Business

Property lines of business are numerous and varied. They can fall into any one of the following categories

- Standard Lines
- Technical Risks
- Excess and Surplus Lines

Property reinsurance is offered on both a pro rata and excess basis. The amount of reinsurance written by a reinsurer depends heavily on individual risk characteristics, including the result of a Probable Maximum Loss (PML) and Maximum Foreseeable Loss (MFL) analysis.

Placement of Facultative Casualty or Property Reinsurance

1. The ceding company provides the reinsurer with their risk information. The reinsurer analyzes the information, which becomes part of the reinsurer's permanent file.
2. If the reinsurer is willing to write the risk, it gives a quote and sends the ceding company a written confirmation.
3. If the quote is accepted, the reinsurer sends a confirmation of binder.
4. The ceding company sends the reinsurer a copy of its policy from which the reinsurer prepares a certificate of reinsurance.
5. If a broker is used by the ceding company, all transactions including exchanging risk information, quotes, and binders occurs through the broker.

Facultative Programs: Casualty and Property

When a ceding company's underwriting standards match the standards of a facultative reinsurer, a "program" approach may provide the greatest benefit to both parties. A "program" provides automatic coverages for the specific line or types of business.

A program may be written to cover a line of business, such as low to moderate hazard commercial umbrellas, or a book of fairly homogeneous classes of property business. Programs terms and conditions are typically documented in more sophisticated binding agreements written up as formal contracts. These contracts often provide the right of rejection on the part of the reinsurer. However, they can also be written on an obligatory basis as well.

Such agreements require the utmost good faith between the parties.

Advantages

- Instantaneous binding by the ceding company.
- Reinsurance terms, including pricing formulas, are predetermined by both a written contract and established underwriting guidelines.
- Bordereau reporting of premiums.
- Lower administrative cost.

APPLYING THE BASICS: TREATY REINSURANCE

Treaty reinsurance is a transaction encompassing a block of the ceding company's book of business. The reinsurer must accept all business included within the terms of the reinsurance contract. As with facultative reinsurance, treaty reinsurance contracts can be grouped into two main categories — pro rata and excess of loss.

Pro Rata

As described earlier, pro rata, also called "proportional," is a form of reinsurance in which the reinsurer shares a proportional part of the original losses and premiums of the ceding company. Pro rata forms are often used in property insurance, since this form provides catastrophic protection in addition to individual risk capacity.

Functions of Pro Rata Reinsurance

- Provide the cedent with automatic reinsurance on every risk to be insured within the applicable classes.
- Increase the cedent's capacity to accept greater limits.
- Finance growth through unearned premium assumption by the reinsurer, reduction in written premium thus improving the written premium to surplus ratio or increasing assets due to the release of equity in the unearned premium reserve.

Characteristics of Pro Rata Reinsurance

- Liability of the reinsurer begins simultaneously with that of the ceding company.
- Premium and losses shared proportionally by ceding company and reinsurer.
- Ceding company is paid a reinsurance commission compensating for acquisition costs, premium taxes, and the cost of servicing the business.

There are two distinct types of pro rata reinsurance - quota share and surplus share.

Quota Share

Quota share reinsurance is a form of pro rata reinsurance whereby the ceding company is indemnified for a fixed percent of loss on each risk covered by the treaty contract. All liability and premiums are shared from the first dollar. "Quota" or "definite" share relates to the fixed percentage as stated in the treaty.

On premiums ceded, the reinsurer pays the ceding company a commission. The commission to the ceding company is an important factor in quota share reinsurance as it provides a financial benefit to the primary company (illustrated on next page).

Also referred to as an "obligatory reinsurance contract," the quota share treaty requires the primary company to cede and the reinsurer to accept each and every policy underwritten by the reinsured. The treaty will usually include a maximum dollar amount over which the reinsurer is not willing to be committed on any one risk.

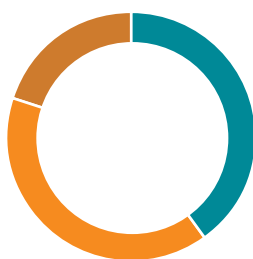
Example

The ceding company has a 60% quota share treaty. Therefore, 40% of all premiums and losses will be retained by the company and 60% of all premiums (less commission) and losses will be ceded to the reinsurer subject to the limit of the treaty. The commission to the ceding company is agreed upon at 30%.

Premium

Assume a risk is written for a limit of \$400,000 at a premium of \$2,000.

Premium retained by ceding company:	40% of \$2,000 = \$ 800
Premium paid to reinsurer:	60% of \$2,000 = \$ 1,200
Commission to ceding company:	30% of \$1,200 = \$ 360

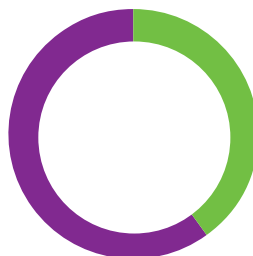


Premium = \$2,000

- \$800 Premium (40% Ceding Company)
- \$1200 Premium (60% Reinsurer)
\$360 Commission Paid Back to Ceding Company

Losses

Assume a total loss of \$400,000 occurs. For this loss, the ceding company would pay \$160,000 (40% of \$400,000) and the reinsurer would pay \$240,000 (60% of \$400,000).



Loss = \$400,000

- \$160,000 (40% Ceding Company)
- \$240,000 (60% Reinsurer)

Financing Function

As a financing mechanism, a quota share treaty is very important to providing surplus relief. Theoretically, barring other negative factors, it makes sense that the more surplus (assets minus liabilities) a company has to “back up” its premium writings, the more financially stable that company will be, particularly when it is growing its new business. Regulators focus on insurer solvency and apply what is known as “statutory accounting principles” which are very conservative. This approach requires that when a policy is issued, the insurer must immediately and fully recognize all the expenses associated with issuing the policy (e.g., taxes, administrative, commissions paid) but can only recognize the premium over the life of the policy.

When a policy is written, an unearned premium reserve (a liability) in the amount of the policy premium must be established. The amount of this reserve shrinks over the life of the policy as the premium becomes “earned”. For example, a 12 month policy issued at 1/1 for \$100 will have an unearned premium of \$100 at 1/1, \$75 at 4/1, 50 at 7/1 and so on until the entire premium is earned and the unearned premium reserve is \$0 at 12/31. This mis-matching of when the assets (premium) and liabilities (expenses) are recognized for accounting purposes results in a situation where the more premium that is written (i.e., the more the business grows), the more surplus shrinks.

A quota share treaty has the effect of “sharing” both the unearned premium reserve (through the insurer ceding part of the written premium to the reinsurer) and the administrative expense (through the ceding commission that the reinsurer pays to the insurer for the portion of the written premium that is ceded). The net effect on the insurance company balance sheet is a replenishment of surplus, the amount of which depends on the amount of business ceded to the reinsurer and the level of ceding commission paid to the insurer by the reinsurer.

Example

A ceding company wants to create surplus relief and strengthen its balance sheet. The reinsurer agrees to assume 50% quota share of all premiums and losses. The reinsurer will pay 30% commission on the premium assumed.

Balance Sheet

(Before the Quota Share)

Assets		Liabilities/Surplus	
Cash/Premium	\$8,000,000	Unearned Premium Reserve	\$8,000,000
Other	\$14,000,000	Other	\$12,000,000
		Surplus	\$2,000,000
	\$ 22,000,000		\$ 22,000,000

(After the Quota Share)

Assets		Liabilities/Surplus	
Cash/Premium ¹	\$ 5,200,000	Unearned Premium Reserve ²	\$ 4,000,000
Other	\$14,000,000	Other	\$12,000,000
		Surplus ³	\$3,200,000
	\$ 19,200,000		\$ 19,200,000

Notes

1	\$8,000,000 Cash before
	\$4,000,000 Paid to reinsurer (50%)
	+ \$1,200,000 Commission from reinsurer (30%)
	<u>\$5,200,000 Cash after</u>

2 Unearned premium reserve (before) less 50% ceded to reinsurer.

3	\$2,000,000 Surplus before
	+ \$1,200,000 Commission received
	<u>\$3,200,000 Surplus after</u>

Premium-to-Surplus Ratio

One of a number of tests applied to an insurance company to ascertain its financial stability is the Premium-to-Surplus Ratio. For example, a ratio of 3:1 or less (premium is three times that of surplus) may be considered acceptable for a given line of business. Quota share reinsurance ceded to a financially sound reinsurer will positively impact the written premium/surplus ratio of the reinsured company.

Note in the example above that the Premium-to-Surplus Ratio before the quota share was 4:1 (\$8,000,000/\$2,000,000). After the quota share, the Premium-to-Surplus Ratio improved to 1.6:1 (\$5,200,000/\$3,200,000).

Surplus Share

Under a surplus share type of treaty, the pro rata proportion ceded depends on the size and type of risk. The ceding company has the right to decide how much it wants to retain on any one risk. This retention is called a “line.” Any risk that falls within this retention or line is handled totally by the primary company. Whenever the company insures a risk that is larger than the retention, the amount over the retention is ceded to the surplus share treaty as a multiple of the retention. All losses between the insurer’s retention on the risk and reinsurer’s participation are pro rated.

Since the ceding company decides how much of each risk it will cede to the treaty, the particular percentage between the insurer and reinsurer will vary. This concept differs from a quota share treaty where the percentage is fixed between the insurer and the reinsurer’s participation, for all risks.

From a reinsurer’s perspective, it is possible to experience adverse selection under the treaty. The ceding company may retain most of the lines on low and moderate hazard risks and may cede most of the lines on high hazard risks to the treaty. As a result, the reinsurer may not experience a good spread of all risks written by the ceding company.

A surplus share treaty can aid the ceding company by helping to build policyholders’ surplus, providing capacity needed to write larger lines, stabilizing results, and minimizing insurer’s exposure to large losses and catastrophic events.

Example

Assume the minimum retention or line is \$50,000. The limit of the treaty is then expressed as a multiple of the line. A 9-line surplus treaty would be (9 x \$50,000) or \$450,000. The total capacity to the insurer is \$500,000.

Any risk with a value of \$50,000 or less is retained and not ceded to the treaty. For risks greater than \$50,000, the insurer determines how many lines it will retain above the \$50,000 and how many lines will be ceded up to the \$450,000 limit.

Risk A

A low hazard risk with a limit of \$350,000. The insurer may retain 5 lines or \$250,000 and cede 2 lines or \$100,000 to the treaty.

Low Hazard \$350,000 Limit

Insurer Retains \$250,000	Insurer Cedes \$100,000
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Risk B

A moderate hazard risk with a limit of \$400,000. The insurer may retain 3 lines or \$150,000 and cede 5 lines or \$250,000 to the treaty.

Moderate Hazard \$400,000 Limit

Insurer Retains \$150,000	Insurer Cedes \$250,000
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Risk C

A high hazard risk with a limit of \$500,000. The insurer may retain 2 lines or \$100,000 and cede 8 lines or \$400,000 to the treaty.

High Hazard \$500,000 Limit

Insurer Retains \$100,000	Insurer Cedes \$400,000
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Excess of Loss

In pro rata type treaties, the operative word is “sharing.” The ceding company and reinsurer share premium and losses according to a predetermined percentage.

In excess of loss, or “non-proportional” treaties the operative word is “retention.” The reinsurer does not get involved with a loss until a predetermined retained limit of loss or retention, which the ceding company will pay, is exceeded.

An excess of loss treaty provides the insurer capacity to write large risks. It primarily provides protection against severity of loss. While casualty reinsurance is generally written on an excess of loss basis, increased application of this approach is being used with property per risk business.

Functions of Excess of Loss Reinsurance

- Provide the cedent with the ability to provide greater coverage limits.
- Reduce the fluctuation in loss experience by limiting the amount of sustained losses.
- Lessen the impact of losses from a single large event with multiple losses or the accumulation of losses from frequent events.

Characteristics of Excess of Loss Reinsurance

- Liability of the reinsurer begins when the insured loss amount exceeds a specified dollar figure (the attachment point).
- The ceding company retains losses less than the attachment point. The reinsurer typically covers all losses above the attachment point (subject to any limitations contained in the reinsurance contract). For complex or high dollar value reinsurance deals, multiple reinsurers may participate at various layers of the coverage.
- Premiums are shared non-proportionally between ceding company and reinsurer. Premiums are typically negotiated as a percentage of the primary insurers premium charge.
- Reinsurers may pay a profit commission (contingent commission) for an insurer’s favorable loss experience.
- It generally involves much less ceded premium than a pro rata structure and therefore does not provide the cedant with meaningful surplus relief as would be the case under a pro rata arrangement.

Example

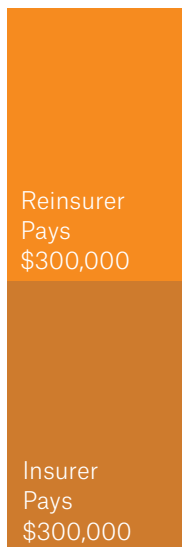
Assume an insurer needs capacity to write casualty business of \$1,000,000 in order to compete in its market niche. Because it is a small company, it determines that it can retain the first \$300,000 loss on any risk. However, it needs reinsurance to apply to that part of any loss that exceeds the retained limit of \$300,000. In this example, an excess of loss treaty would be expressed as \$700,000 x/s \$300,000.

Assume each of these risks is written by the insurer for a limit of \$1,000,000.

Risk A

Has a loss of \$600,000.
The insurer pays the first \$300,000 (retention)
and the reinsurer the remaining \$300,000.

\$600,000 Loss



Risk B

Has a loss of \$250,000.
The insurer pays the entire loss with no indemnification by the reinsurer as the loss is within the retention of \$300,000.

\$250,000 Loss

Reinsurer
Pays
\$0



Risk C

Has a loss of \$1,000,000.
The insurer pays the first \$300,000 (retention) and the reinsurer, \$700,000.

\$1,000,000 Loss



Unlike pro rata treaties, the premium paid for an excess of loss contract has no proportional relationship to the premium paid by insureds to the primary company. Rather, premium charged by the reinsurer is subject to individual analysis and negotiation and may be based on a number of factors. These include the ceding company's prior loss experience, loss potential and premium estimates for the book of business, geographic area for business, underwriting policies, and desired retention level.

Variations

Property Per-Risk Excess Of Loss

The reinsurer indemnifies the primary company for any loss in excess of the specified retention on each risk.

Catastrophe Per-Occurrence Excess Of Loss

The purpose of a catastrophe excess treaty is to protect a primary company against adverse loss experience resulting from the accumulation of losses arising from a single, major natural disaster or event such as a hurricane, tornado, earthquake, flood, windstorm, etc. For a given event, the treaty applies once the accumulation of losses paid by the primary company, less inuring reinsurance (the amount the ceding company expects to receive via other reinsurance agreements), reaches a predetermined retention.

Stop Loss/Aggregate Stop Loss

This excess of loss cover is designed to protect a company's overall underwriting results after application of other types of reinsurance it may have. It provides reinsurance for losses incurred during the treaty term, usually one year, in excess of either a specified loss ratio or a predetermined dollar amount.

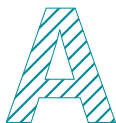


GLOSSARY

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RAA Glossary Of Reinsurance Terms. Relying on a variety of sources, the Reinsurance Association of America (RAA) manages a comprehensive list of terms commonly used in insurance/reinsurance. More information can be found at <http://www.reinsurance.org>. The RAA has been the voice of the reinsurance industry since 1968. Headquartered in Washington, DC, the RAA is a nonprofit trade association committed to an activist agenda that represents the interests of reinsurance professionals across the United States.



Access to Records Clause

A provision in a reinsurance agreement that allows the reinsurer access to the Company's books, records and other documents and information pertaining to the reinsurance agreement. This includes related underwriting and claims information, for purposes of the reinsurer obtaining information concerning the reinsurance agreement or its subject matter.

Accident Year

Accident year means year of loss occurrence. Accident years are necessary for measuring and monitoring the development of losses in comparison to the earned premium income of the same annual period. See Basis of Attachment.

Accident Year Experience

Underwriting experience calculated by matching the total value of all losses occurring during a given 12 month period (i.e., the dates of loss fall within the period) with the premiums earned for the same period. See Calendar Year Experience and Policy Year Experience.

Accounting Year

Financial year in which the accounts are recorded. The reinsurer's accounting year may differ from the ceding company's due to time needed for transferring information.

Accumulation

A build-up of risks which may be triggered by the same event, leading to several claims.

Acquisition Cost

All expenses directly related to acquiring insurance or reinsurance accounts, i.e., commissions paid to agents, brokerage fees paid to brokers, and expenses associated with marketing, underwriting, contract issuance and premium collection.

Act of God

An occurrence exclusively caused by forces of nature that do not lay in the hands and in the power of man. These acts cannot be prevented or escaped from by prudence or foresight (e.g. lightning, tempest, earthquakes, tornadoes).

Administration Expenses

Costs incurred in conducting an insurance operation other than loss adjustment expenses, acquisition costs, and investment expenses.

Admitted Assets

Assets recognized and accepted by state insurance laws in determining the solvency of insurers or reinsurers.

Admitted Company

- 1) An insurer licensed to conduct business in a given state.
- 2) A reinsurer licensed or approved to conduct business in a given state.

Admitted Reinsurance (also known as Authorized Reinsurance)

Reinsurance for which credit is given in the ceding company's Annual Statement because the reinsurer is licensed or otherwise authorized to transact business in the jurisdiction in question. See Non-Admitted Reinsurance.

Advance Deposit Premium

An amount paid by a cedent to a reinsurer that is held for the payment of the reinsured's losses. At some time in the future, any balance in the fund remaining after paying losses and any agreed upon reinsurance expenses will be returned to the reinsured.

Adverse Selection

The conscious and deliberate cession of those risks, segments of risks, or coverages that appear less attractive for retention by the ceding company.

Agent Commission

In insurance, an amount paid an agent for insurance placement services.

Aggregate Deductibles

The total loss amount a ceding company of a non-proportional reinsurance policy keeps on top of normal retention before the reinsurer gets liable.

Aggregate Excess of Loss Reinsurance (also known as Excess of Loss Ratio Reinsurance, Stop Loss Reinsurance)

A form of excess of loss reinsurance which, subject to a specified limit, indemnifies the ceding company for the amount by which all of the ceding company's losses (either incurred or paid) during a specific period (usually 12 months) exceed either 1) a predetermined dollar amount or 2) a percentage of the company's subject premiums (loss ratio) for the specific period.

Alien (Insurer)

An insurer domiciled outside the United States.

Amortization Period

Synonymous with payback period, this term is used in the rating of per occurrence excess covers and represents the number of years at a given premium level necessary to accumulate total premiums equal to the limit of liability of the reinsurance cover.

Annual Aggregate Deductible

See Aggregate Deductibles. The annual aggregate deductible amount is generally an amount or percentage of the reinsured's subject premium for the annual period.

Annual Statement (also known as Convention Blank, Statutory Annual Statement)

The annual report format prescribed by the National Association of Insurance Commissioners and the states.

Arbitrage

Making riskless profit through buying and selling insurance and reinsurance which are differently priced in different markets.

Arbitration Clause

A provision found in reinsurance contracts whereby the parties agree to submit their disputes to a non-judicial adjudicator(s) tribunal rather than a court of law, generally subject to selection criteria and procedures set out in the clause. The arbitration tribunal produces an award ultimately enforceable by a court of law.

As If

A term used to describe the recalculation of prior years of loss experience to demonstrate what the underwriting results of a particular program would have been "as if" the proposed program had been in force during that period.

Association (also known as Pool, Syndicate)

An organization of insurers or reinsurers through which pool members underwrite particular types of risks with premiums, losses, and expenses shared in agreed amounts.

Assume

To accept an obligation to indemnify all or part of a ceding company's insurance or reinsurance on a risk or exposure subject to the contract terms and conditions.

Assumed Portfolio

The transfer of in-force insurance liability by an insurer to a reinsurer (or vice versa) by the payment of the unearned premium reserve on those policies alone, or by the concurrent transfer of liability for outstanding losses under those policies by the payment of the outstanding loss reserve by the insurer to the reinsurer (or vice versa). The former is a premium portfolio, the latter a loss portfolio. See Return Portfolio.

Assumption

A procedure under which one insurance (or reinsurance) company takes over or assumes contractual obligations of another insurer or reinsurer.

Assumption of Liability Endorsement

An endorsement to an insurance policy or reinsurance contract wherein a reinsurer assumes insurance obligations or risks, or both, of existing or in-force policies of insurance. The term is distinguished from a cut-through. See Cut-Through Endorsement.

Attachment Date

The date at which a reinsurance policy becomes operative and the reinsurer is on risk.

Attachment Point

The amount at which excess reinsurance protection becomes operative; the retention under an excess reinsurance contract.

Attritional Loss

A small loss retained by an insurer and not passed on to the reinsurer.

Authorized Reinsurance

See Admitted Reinsurance.



Base Premium (also known as Premium Base, Subject Premium, Underlying Premium)

The ceding company's premiums (written or earned) to which the reinsurance premium rate is applied to produce the reinsurance premium. This term is usually defined in the reinsurance contract.

Gross Net Earned Premium Income (GNEPI)

Generally, the usual rating base for excess of loss reinsurance. It represents the earned premiums of the primary company for the lines of business covered net, meaning after cancellation, refunds and premiums paid for any reinsurance protecting the cover being rated, but gross, meaning before deducting the premium for the cover being rated.

Gross Net Written Premium Income (GNWPI)

Generally, gross written premium less only returned premiums and less premiums paid for reinsurance that inure to the benefit of the cover in question. Its purpose is to create a base to which the reinsurance rate is applied.

Basis of Attachment

A methodology that determines which original policy losses will be covered under a given reinsurance agreement. There are two types of methodologies: policies attaching and losses occurring. The determination may be based on 1) the effective or renewal date of the original policy; or 2) on the date of the loss; or 3) on the date when the reinsured company recorded premium or loss transaction.

Underwriting Year

The effective date of the original policy, rather than the date of loss, determines the basis of attachment. Any losses occurring on policies written or renewed with inception or renewal dates during the term of the given reinsurance agreement will be covered by that reinsurance agreement irrespective when the loss actually occurred. This mechanism is often used with “the policies attaching” methodology.

Accident Year

The date of the loss under the original policy rather than the effective date of the original policy that determines the basis of attachment. Any losses occurring during the reinsurance agreement period on policies in force (if any), written or renewed will be covered by that reinsurance agreement irrespective of the inception or the renewal date of the original policy. This mechanism is often used with “the losses occurring during” the contract period methodology.

Best’s Rating

Rating system that evaluates factors affecting the overall performance of insurance companies. It shows a weighted relative measure of a company’s financial strength, operation performance, competitive market position and ability to meet its current and future obligations to policyholders.

Binder

A record of reinsurance arrangements pending the issuance of a formal reinsurance contract (which then replaces the binder). See Cover Note and Placement.

Blended Covers

In order to limit risk transfer, this type of reinsurance combines elements of traditional and financial reinsurance.

Book Value

The value that is shown in the account (in contrast to market value).

Bordereau (sing); Bordereaux (pl)

Furnished periodically by the reinsured, a detailed report of reinsurance premiums or reinsurance losses. A premium bordereau contains a detailed list of policies reinsured under a reinsurance treaty during the reporting period, reflecting such information as the name and address of the primary insured, the amount and location of the risk, the effective and termination dates of the primary insurance, the amount reinsured and the reinsurance premium applicable thereto. A loss bordereau contains a detailed list of claims and claims expenses outstanding and paid by the reinsured during the reporting period, reflecting the amount of reinsurance indemnity applicable thereto. Bordereau reporting is primarily applicable to pro rata reinsurance arrangements and to a large extent has been supplanted by summary reporting.

Broker

An intermediary who negotiates reinsurance contracts between the ceding company and the reinsurer(s). The broker generally represents the ceding company and receives compensation in the form of commission, and/or other fees, for placing the business and performing other necessary services. See Intermediary.

Broker Market

The collective reference to those reinsurance companies which accept business mainly from reinsurance brokers.

Brokerage Commission

An amount paid a broker for insurance or reinsurance placement and other services.

Buffer Layer

Used in casualty insurance to describe a stratum of coverage between the maximum policy limit that the primary underwriter will write and the minimum deductible over which the excess or umbrella insurer will cover.

Bulk Reinsurance

A transaction sometimes defined by statute through which, of itself or in combination with other similar agreements, an insurer assumes all or a substantial portion of the liability of the reinsured company.

Burning Cost (also known as Pure Loss Cost)

The ratio of actual past reinsured losses to the ceding company's subject matter premium (written or earned) for the same period; used to analyze past reinsurance experience or to project future reinsurance experience.



Calendar Year

All transactions (loss payments) and movements in reserves (new, increases and decreases) which happen in the same year are attributed to the calendar year notwithstanding the point of occurrence. Statistics on calendar year basis are suitable only for financial considerations. However, they can be highly misleading for the assessment of treaty results.

Calendar Year Experience

The evaluation of underwriting experience whereby the total value of all losses incurred during a given twelve-month period (regardless of the dates of loss or the inception date of the policy) is matched with the premiums earned for the same period. As the name implies, Calendar Year Experience is usually calculated for a twelve-month period beginning January 1st. See Accident Year Experience and Policy Year Experience.

Cancellation

Putting a (re-)insurance contract actively to an end, prior to the ending of the contract period.

Capacity

The largest amount of insurance or reinsurance available from a company or the market in general. Also refers to the maximum amount of business (premium volume) that a company or the total market could write based on financial strength.

Captive Insurer

The main purpose of a captive insurer is to insure the risks of its parent organizations. It is fully owned by one or more entities.

Captive Reinsurer

The main purpose of a captive reinsurer is to provide reinsurance capacity for insurance policies taken out by the corporation or the association's members.

Casualty

A type of reinsurance primarily concerned with risks resulting in injuries to persons and legal liability imposed upon the insured for such injury or for damage to the property of others.

Casualty Catastrophe Cover

Reinsurance that is not exposed on a policy limit basis, i.e., the deductible on the treaty is equal to or exceeds the reinsured's maximum net exposure on any one policy. Therefore, such treaties protect against the infrequent loss involving two or more insureds in the same loss occurrence. Another name for clash cover.

Catastrophe Excess of Loss

Catastrophe excess of loss covers are triggered "per event". They include all the individual losses that are attributable to one cause and therefore form an accumulation loss. Typically, catastrophe excess of loss is shortened to Cat XL.

Catastrophe Reinsurance

A form of excess of loss reinsurance which, subject to a specific limit, indemnifies the ceding company in excess of a specified retention with respect to an accumulation of losses resulting from an occurrence or series of occurrences arising from one or more disasters. Catastrophe contracts can also be written on an annual aggregate deductible basis under which protection is afforded for losses over a certain amount for each loss (the attachment point) in excess of a second amount in the aggregate for all losses (otherwise recoverable but for the aggregate deductible) in all catastrophes occurring during a period of time (usually one year).

Cede

To pass on to another insurer (the reinsurer) all or part of the insurance written by an insurer (the ceding insurer) with the objective of reducing the possible liability of the latter.

Cedent (also known as Ceding Company, Reassured, Reinsured)

A reinsured insurance company.

Ceding Commission

An amount deducted from the reinsurance premium to compensate a ceding company for its acquisition and other overhead costs, including premium taxes. It may also include a profit factor. See Overriding Commission and Sliding Scale Commission.

Ceding Company

See Cedent, Reinsured.

Certificate of Reinsurance

A short-form documentation of a reinsurance transaction.

Cession

The portion of insurance ceded by the ceding company to the reinsurer.

Claim

Occurrence or loss under an insurance policy which triggers a request for an indemnity under an insurance contract. A reinsurance claim is a request by the primary insurer to the reinsurer which is defined in a reinsurance contract between the two parties. The claim will be covered if the occurrence or loss is within the contract's terms and conditions.

Claim Expenses (also known as Loss Expenses or Loss Adjustment Expenses)

The costs incurred in processing claims: court costs, interest upon awards and judgments, the company's allocated expense for investigation and adjustments and legal expenses (excluding, however, ordinary overhead expenses of the company such as salaries, monthly or annual retainers, and other fixed expenses that are defined as unallocated loss adjustment expenses).

Claim Frequency

The statistical quantity of occurrences of claims in a time/policy period or in ratio to the number of insured objects.

Claims Made Basis Insurance Agreements

The provision in a policy of insurance that affords coverage only for claims that are made during the term of the policy for losses that occur on or after the retroactive date specified in the policy. A claims made policy is said to "cut-off the tail" on liability business by not covering claims reported after the term of the insurance policy unless extended by special agreement.

Claims Made Basis Reinsurance Agreements

The provision in a reinsurance contract that affords coverage for claims that occur and are made during the contract term, for losses that occur on or after the retroactive date specified in the contract. Claims reported during the term of the reinsurance agreement are therefore covered regardless of when they occurred. A claims made agreement does not cover claims reported after the term of the reinsurance contract unless extended by special agreement.

Clash Cover

A casualty excess of loss reinsurance agreement with a retention level equal to or higher than the maximum limits written under any one reinsured policy or contract reinsured under the reinsurance agreement. Usually applicable to casualty lines of business, the clash cover is intended to protect the ceding company against accumulations of loss arising from multiple insureds and/or multiple lines of business for one insured involved in one loss occurrence. See Contingency Cover.

Class of Business

A homogeneous category of insurance. Most reinsurance markets generally differentiate between Property and Casualty and Life insurance. See Line of Business.

Combination Plan Reinsurance

Elements of two types of reinsurance, Pro-Rata (Quota Share) and Excess of Loss, are combined in one reinsurance agreement usually in order to assist the ceding company in a transition from pure Pro-Rata reinsurance coverage to Excess of Loss. The excess of loss part of the plan protects the company up to a specified limit on each risk, each occurrence excess of a fixed net retained line. The pro-rata part of the plan protects the company's net retained lines under the excess part (i.e. after deducting the excess of loss recoveries), on fixed percentage quota share basis.

Combined Ratio

Sum of the claims, commissions and expenses in ratio of the net earned premium. The combined ratio helps to measure the performance in non-life reinsurance before inclusion of investment return.

Common Account Reinsurance (also known as Joint Account Excess of Loss Reinsurance)

Reinsurance which is purchased by the ceding insurer to protect both the itself and its reinsurer (usually quota share reinsurer) and which applies to net and treaty losses combined.

Commutation Agreement

An agreement between the ceding insurer and the reinsurer that provides for the valuation, payment and complete discharge of some or all current and future obligations between the parties under particular reinsurance contract(s).

Commutation Clause

A clause in a reinsurance agreement that provides for the valuation, payment, and complete discharge of some or all obligations between the ceding company and the reinsurer, including current and future obligations for reinsurance losses incurred.

Contingency Cover

Reinsurance providing protection for an unusual combination of losses. See Clash Cover.

Contingent Commission (also known as Profit Commission)

An allowance by the reinsurer to the reinsured based on a predetermined percentage of the profit realized by the reinsurer on the business ceded by the reinsured.

Continuous Contract

A reinsurance contract that does not terminate automatically but continues indefinitely unless one of the parties delivers notice of intent to terminate. See Term Contract.

Contractors' All Risks (CAR)

Insurance of contract works covering damage to property and third party liability.

Contributing Excess

A form of excess of loss reinsurance where, in addition to its retention, the ceding company has a share of losses in excess of the retention. This form of reinsurance may also apply to subject policies written in excess of underlying insurance or self insured retentions where the reinsurance applies to a share of losses within the policies, with the ceding company or other reinsurers contributing the remaining share. When more than one reinsurer shares a line of insurance on a risk in excess of a specified retention, each reinsurer contributes towards any excess loss in proportion to its original participation in such risk.

Convention Blank

See Annual Statement.

Cover

Insurance and reinsurance protection defined on an insurance or reinsurance policy.

Cover Note

A written statement issued by an intermediary, broker or direct writer indicating that the coverage has been effected and summarizing the terms. See Binder and Placement Slip.

Credibility

Credibility is a form of insurance pricing that is widely used and is a special type or experience rating that employs a weighted average of claims experience on a previously established price to determine a new price for each risk class under consideration.

Credit Carry Forward (CCF)

The transfer of credit or profit from one accounting period, as defined within the reinsurance agreement, to the succeeding accounting period under the existing contract or the replacing contract.

Credit for Reinsurance

The right of a ceding company under statutory accounting and regulatory provisions permitting a ceding company to treat amounts due from reinsurers as assets or reductions from liability based on the status of the reinsurer.

Cumulative Liability

The accumulation of liability of a reinsurer under several policies from several ceding companies covering similar or different lines of insurance, all of which are involved in a common event or disaster.

Cut-Through Endorsement

An endorsement to an insurance policy or reinsurance contract which provides that, in the event of the insolvency of the insurance company, the amount of any loss which would have been recovered from the reinsurer by the insurance company (or its statutory receiver) will be paid instead directly to the policyholder, claimant, or other payee, as specified by the endorsement, by the reinsurer. The term is distinguished from an assumption. See Assumption of Liability Endorsement.



Deductible

The amount of a loss agreed in a non-proportional or facultative reinsurance policy which is retained by the cedent before he can claim on the policy.

Deficit and Credit Carry Forward (DCCF)

See Deficit Carry Forward and Credit Carry Forward.

Deficit Carry Forward (DCF)

The transfer of deficit or loss from one accounting period, as defined within the reinsurance agreement, to the succeeding accounting period under the existing contract or the replacing contract.

Deposit

Amount paid by the cedent to the reinsurer as a guarantee at inception of the risk period. A deposit stands as security for reinsurer's contractual obligations and are usually calculated as pro rata premium reserves and/or loss reserves. See Premium Reserves.

Direct Writer

- 1) In reinsurance, a reinsurer that negotiates with a ceding company without benefit of an intermediary or broker.
- 2) In insurance, a primary insurer that sells insurance through licensed agents who produce business essentially for no one else.

Direct Written Premium

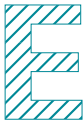
The gross premium income (written instead of earned) of a primary company, adjusted for additional or return premiums but before deducting any premiums for reinsurance ceded and not including any premiums for reinsurance assumed.

Domestic Company

An insurer conducting business in its domiciliary state from which it received its charter to write insurance. (As opposed to a foreign company, an insurer conducting business in a state other than its domiciliary state; or an alien company, one domiciled outside the U.S. but conducting business within the U.S.).

Drop-Down (also known as Second Event Retention)

An approach to establishing the retention level in excess of loss reinsurance (usually catastrophe) under which the amount of the retention is reduced for the second (or subsequent) loss occurrence. The theory is that the ceding company can afford to retain a given retention level on one loss, but for additional loss(es) needs protection over the lower retention.



Early Warning Test

Financial ratio and performance criteria designed by the National Association of Insurance Commissioners (NAIC) to identify insurance companies that may need close surveillance by state insurance departments.

Earned Premium

That portion of written premium equal to the expired portion of the time for which the insurance or reinsurance was in effect. Technically, the following definitions are appropriate:

Accounting Earned

This is the most common and widely understood method. The unearned premium reserve at the beginning of the period is added to the premium written (booked) during the period, and the unearned premium reserve at the end of the period is subtracted. Accounting earned is the figure used in the Annual Statement.

Exposure Earned

This method calculates the premiums that were actually exposed to loss (earned) for the period. The date on which premiums were booked is disregarded. What are significant are the effective date and term to which the premium applies. The portion of the premium written that was exposed to loss (earned) is allocated to the exposure period whether the premiums were booked prior to the period, during the period, or after the period. The exposure earned premium eliminates the deficiency contained in accounting earned premium that results from timing problems in the recording of premium records.

Earned Reinsurance Premium

A reinsurance term that refers to either 1) that part of the reinsurance premium applicable to the expired portion of the policies reinsured, or 2) that portion of the reinsurance premium which is deemed earned under the reinsurance contract.

Entire Agreement Clause

A clause in some reinsurance agreements providing that the reinsurance agreement constitutes the entire agreement between the parties with respect to its subject matter, superseding all previous contracts, written or oral; and that any prior statements, negotiations or representations between the parties are merged into the final, written agreement. The clause may also provide that any modifications or changes in the agreement must be in writing, and executed by both parties.

Equalization Reserve

Reserve built up over a period of time steered by claims experience of the insurer or reinsurer in order to equalize operating results from certain catastrophe risks.

Errors and Omissions Clause

A clause in a reinsurance treaty (requiring some affirmative act by the ceding insurer to activate the reinsurance protection) stipulating that, in the event of inadvertent error or omission, the reinsured shall not be prejudiced in the fulfillment of the agreement, provided that such error or omission shall be corrected as soon as it is discovered.

Estoppel (also known as Non-Waiver Clause)

A provision in a reinsurance agreement which reserves to the reinsurer every right under the reinsurance agreement not previously waived, and to the ceding company every right which had not been forfeited.

Event

Occurrence of an insurance loss. The term "event" in policy wordings is usually used to define claims having a common accidental origin and being aggregated together to form one claim under the policy. See Occurrence.

Evergreen Clause

A term in a Letter of Credit providing for automatic renewal of the credit.

Ex Gratia Payment

Latin: "by favor". A voluntary payment made by the reinsurer in response to a loss for which it is not technically liable under the terms of its contract.

Excess Judgment Loss

The amount paid by a liability insurer in excess of applicable policy limits occasioned by the failure, on account of negligence or bad faith, to settle a claim for an amount within such policy limits.

Excess Limits Premiums

In casualty insurance, premiums for limits of liability added to basic limits, calculated as multiples of basic limits premium. Excess limits premiums were the original (and remain a popular) basis of premium paid for casualty excess of loss reinsurance.

Excess of Line Reinsurance

A form of per-risk excess agreement under which the indemnity is not a fixed dollar limit but a multiple of the primary company's net retention.

Excess of Loss Reinsurance (also known as Non-Proportional Reinsurance)

A form of reinsurance, which, subject to a specified limit, indemnifies the ceding company for the amount of loss in excess of a specified retention. It includes various types of reinsurance, such as catastrophe reinsurance, per risk reinsurance, per occurrence reinsurance and aggregate excess of loss reinsurance.

Excess of Loss Ratio Reinsurance

See Aggregate Excess of Loss Reinsurance.

Excess Per Risk Reinsurance

A form of excess of loss reinsurance which, subject to a specified limit, indemnifies the ceding company against the amount of loss in excess of a specified retention for each risk involved in each occurrence.

Exclusions

Those risks, perils or classes of insurance with respect to which the reinsurer will not pay loss or provide reinsurance notwithstanding the other terms and conditions of reinsurance.

Expense Ratio

Expenses (other than loss adjustment expenses) incurred during a specific period of time divided by premiums written during the same period.

Experience Rating

See Rating.

Exposure

The amount of risk insured, usually over a given period.

Exposure Curves

Scales derived from statistics pertaining to past losses and providing a generic suggestion for the distribution of Ground up premium throughout the layers in a risk.

Exposure Rating

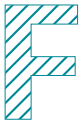
See Rating.

Extended Reporting Period

An additional period of time affording coverage after termination of a claims-made policy during which a claim first made after such termination for injury or damage that occurs on or after the retroactive date, if any, but before the policy termination date is covered. See Retroactive Date.

Extra Contractual Damages (Extra Contractual Obligations, ECO)

In reinsurance, monetary awards or settlements against an insurer for its alleged wrongful conduct to its insured. Such payments required of an insurer to its insured are extra-contractual in that they are not covered in the underlying contract.



Facultative Certificate of Reinsurance

A contract formalizing a reinsurance cession on a specific risk.

Facultative Reinsurance

Reinsurance of individual risks by offer and acceptance wherein the reinsurer retains the ability to accept or reject each risk offered by the ceding company.

Facultative Treaty

A reinsurance contract under which the ceding company has the option to cede and the reinsurer has the option to accept or decline individual risks. The contract merely reflects how individual facultative reinsurances shall be handled.

Financial Reinsurance

A form of reinsurance which considers the time value of money and has loss containment provisions. See Finite Reinsurance.

Financing Function

A purpose of reinsurance in some cases, i.e., whenever the reinsurer relieves the primary company of all or part of the company's responsibility for carrying an unearned premium reserve and the reinsurer allows a ceding commission to the primary company. Because the cash or other statutorily recognized assets being transferred (causing a change in assets) are less than the unearned premium reserve change (causing a change in liabilities), the primary company's policyholder surplus is increased by the amount of the reinsurance commission allowance. See Surplus Relief.

Finite Reinsurance (also known as Financial Reinsurance, Limited Risk Reinsurance, Nontraditional Reinsurance, Structured Reinsurance)

A broad spectrum of treaty reinsurance arrangements which provide reinsurance coverage at lower margins than traditional reinsurance, in return for a lower probability of loss to the reinsurer. This reinsurance is often multi-year and often provides a means of sharing positive or negative claims experience with the cedent beyond that usually provided by traditional reinsurance.

First Loss Policy

An insurance under which the insurer pays up to the sum insured without consideration of the total value at risk. Often the insured risk is of a type that can virtually never be lost in one claim, like theft (it might be impossible to steal the total of a large stock at one time).

First Loss Retention

The amount of loss sustained by the reinsured before the liability of the excess of loss reinsurer attaches, often referred to as Net Retention. See Attachment Point.

First Surplus Treaty

A term exclusive to pro rata reinsurance treaties that defines the amount of each cession as the amount of gross (policy) liability which exceeds, or is "surplus" to, an agreed upon net retention up to the limit of (reinsurance) liability. Often a maximum net retention is specified in the treaty, with the primary company having the option to choose a lesser retention on individual risks. The amount of first surplus reinsurance provided will be limited to a fixed multiple of the selected retention in each case. Larger policy surpluses are termed "second," "third," and so on, each being the amount of reinsurance afforded once the prior surplus reinsurance capacity plus the true net retention have been exceeded. See Surplus Reinsurance.

Flat Commission

A stated commission percentage, payable by the reinsurer to the reinsured, which is not subject to further adjustment under a profit-sharing provision. Common in pro rata facultative reinsurance.

Flat Premium

A fixed premium (absolute amount) for a non-proportional reinsurance contract. This premium is calculated irrespective of loss experience or portfolio development.

Flat Rate

- 1) A fixed insurance premium rate not subject to any subsequent adjustment.
- 2) A reinsurance premium rate applicable to the entire premium income derived by the ceding company from the business ceded to the reinsurer as distinguished from a rate applicable to excess limits.

Follow the Fortunes

Follow the Fortunes generally provides that a reinsurer must follow the underwriting fortunes of its reinsured and, therefore, is bound by the decisions of its reinsured in the absence of fraud, collusion or bad faith. It requires a reinsurer to accept a reinsured's good faith, business-like reasonable decision that a particular risk is covered by the terms of the underlying policy. The term is often used interchangeably with Follow the Settlements, and there may be overlap between the affect of Follow the Fortunes and Follow the Settlements when the "risk" is what generated the loss. Follow the Fortunes is focused on "risk" determination, not necessarily tied to a loss settlement.

Follow the Settlements

Follow the Settlements generally provides that a reinsurer must cover settlements made by the reinsured in a businesslike manner, provided the settlement is arguably within the terms of the reinsured's policy and the reinsurance agreement and the settlement is not affected by fraud, collusion or bad faith. It is an expectation that the reinsurer will abide by the reinsured's good faith determination to settle, rather than litigate, claims under a reinsured policy and not re-litigate a reinsured's settlements ceded to the reinsurance agreement. The term is often used interchangeably with Follow the Fortunes, and there may be overlap between the affect of Follow the Settlements and Follow the Fortunes when the "risk" is what generated the loss. Follow the Settlements is focused on "loss settlement", not necessarily tied to a "risk determination" arising out of follow the Fortunes.

Following Reinsurer

A reinsurer that follows the lead reinsurer on a cover being placed, accepting or rejecting the terms as presented.

Foreign Insurance Company

A U.S. domiciled insurer which is domiciled in a state other than the jurisdiction in question.

Foreign Reinsurer

A U.S. reinsurer conducting business in a state other than its domiciliary state, where it is known as a domestic company (as opposed to an alien reinsurer: one domiciled outside the U.S. but conducting business within the U.S.).

Franchise Covers

A contractual provision, common in hail insurance but also used elsewhere, stating that no loss is payable until the loss exceeds a certain amount, but when that amount is exceeded, the whole loss is paid.

Fronting

Arrangements by which an insurer, for a specified fee or premium, issues its policies to cover certain risks underwritten or otherwise managed by another insurer or reinsurer. The insurer then transfers all, or substantially all, of the liabilities thereunder to such insurers by means of reinsurance.

Funded Cover

A type of excess of loss reinsurance agreement under which the reinsured company pays an agreed upon premium to build a fund (which is held by the insurer or reinsurer pursuant to the terms of the agreement) from which to pay covered losses. Since that fund reduces the reinsurer's risk that losses will exceed the fund, the Reinsurer agrees to accept a reduced reinsurance margin. Any excess monies in the fund will be returned to the appropriate party pursuant to the terms of the contract.

Funds Held Account (or Funds Withheld)

The holding by a ceding company of funds representing the unearned premium reserve or the outstanding loss reserve applied to the business it cedes to a reinsurer.



Gross Net Earned Premium Income (G.N.E.P.I.)

See Base Premium.

Gross Net Written Premium Income (G.N.W.P.I.)

See Base Premium.

GAAP (Generally Accepted Accounting Principles)

A method of reporting the financial results of an insurer more in accordance with the going concern basis used by other businesses. GAAP assigns income and disbursements to their proper period, as distinguished from the more conservative requirements of statutory accounting affecting insurers.

Gross Earned Premium

Gross premium net of this part of the premium being paid in advance for later insurance years.

Gross Line

The total limit of liability accepted by an insurer on an individual risk (net line plus all reinsurance ceded).

Gross Net Earned Premium (G.N.E.P.)

Gross earned premium net of policy cancellations and outwards reinsurance premiums but gross of commissions and expenses.

Gross Net Written Premium (G.N.W.P.)

Gross written premium net of policy cancellations and outwards reinsurance premiums but gross of commissions and expenses.

Gross Premiums

Gross premiums equal the premiums received for one year.

Gross Written Premium (G.W.P.)

The gross written premium describes the total premium on insurance underwritten by an insurer or reinsurer during a period before deduction of premium ceded.

Ground-Up Loss

The total amount of loss sustained by the ceding company before taking into account the credit(s) due from reinsurance recoverable(s).

Group Policy

A single insurance policy covering a group of several persons. The persons insured in the group are generally belonging to the same company or association. The premium of the group is usually calculated on the basis of the specific risk structure of the group, sometimes it may just be derived from individual premiums subject to a discount.

Guarantee Endorsement

An addition to an insurance policy (between an insurance company and a policyholder covering the policyholder's mortgaged property) which requires that, in the event of the company's insolvency, the mortgagee and/or the policyholder be paid directly by the reinsurer either for any loss covered by reinsurance or (as is often provided) for the full insurance protection afforded by the insurance company. Since the full insurance protection afforded by the insurance company may be above the reinsurance that would be payable to a reinsured company, the reinsurer may be assuming an additional risk in such an endorsement. Similar to the cut-through endorsement, the guarantee endorsement is also known as a mortgagee endorsement.



Incurred But Not Reported (IBNR)

Refers to losses that have occurred but have not yet been reported to the insurer or reinsurer. IBNR has two components: (1) a provision for loss and loss adjustment expense ("LAE") reserves in excess of the reserves on claims reported during the accounting period (IBNER); (2) a provision for loss and LAE reserves on claims that have occurred but not yet been reported during the accounting period (IBNYR).

Incurred But Not Enough Reported (IBNER) is a provision in claims and losses already reported for claims reserve increases; decreases can occur although infrequently. It is created because reported claims reserves tend to increase from the time a claims occurs until the claim is settled. Changes in insurance company case reserves, during the accounting period and established by judgment and/or formula, often result from a lag in information on liability and damages.

Incurred But Not Yet Reported (IBNYR) is a provision for loss reserves and LAE on losses and claims that have occurred but have not been made known to the insurer.

Incurred Loss (also known as Loss Incurred)

Incurred loss is calculated as outstanding loss at the beginning of a reinsurance period plus paid and/or outstanding loss reported during that period minus the outstanding loss at the end of the period irrespective of when the loss actually occurred or the original policy attached. See Loss.

Incurred Loss Ratio

The relationship between incurred losses and earned premium, usually expressed as a percentage.

Indemnity

Insurance or reinsurance protecting the insured resp. the reinsured fully from any losses following the occurrence of one or more specified events. In particular the insured resp. reinsured is liable with any deductible.

Indexing

A procedure sometimes incorporated into an excess of loss reinsurance treaty to adjust the retention and limit according to the value of a specified public economic index (for example: wage, price, or cost-of-living).

Insolvency Clause

A provision now appearing in most reinsurance contracts (because many states require it) stating that in the event the reinsured is insolvent the reinsurance is payable directly to the company or its liquidator without reduction because of its insolvency or because the company or its liquidator has failed to pay all or a portion of any claim.

Interest and Liabilities Agreement

A reinsurance contract between the ceding insurer and one or multiple reinsurers in which the percentage of participation of each reinsurer is specified.

Interlocking Clause

A provision in a reinsurance agreement designed to allocate loss from a single occurrence between two or more reinsurance agreements. The provision is intended to be used when the company purchases its excess of loss reinsurance on an “underwriting year” or “risks attaching” basis. The provision allows the reinsured to prorate its retention between two or more reinsurance agreement periods, i.e., when one loss affects policies assigned to different reinsurance periods, so that the company will have one retention and one recovery for the loss involving the two reinsurance periods.

Intermediary

A reinsurance broker who negotiates contracts of reinsurance on behalf of the reinsured, receiving a commission for placement and other services rendered. Under the terms of one widely used intermediary clause, premiums paid a broker by a reinsured are considered paid to the reinsurer, but loss payments and other funds (such as premium adjustments) paid a broker by a reinsurer are not considered paid to the reinsured until actually received by the reinsured. See Broker.

Intermediary Clause

A contractual provision in which the parties agree to effect all transactions through an intermediary and the credit risk of the intermediary, as distinct from other risks, is imposed on the reinsurer.

Intermediate Excess

Used in property reinsurance to describe a cover exposed to both catastrophe (occurrence) losses and to policy limit exposures, excess the probable maximum loss.

Inuring Reinsurance

A designation of other reinsurances which are first applied pursuant to the terms of the reinsurance agreement to reduce the loss subject to a particular reinsurance agreement. If the other reinsurances are to be disregarded as respects loss to that particular agreement, they are said to inure only to the benefit of the reinsured. Example: A ceding insurer has a 50% quota share agreement and a per occurrence excess of loss contract (i.e., catastrophe reinsurance) for \$80 million excess of \$20 million. A catastrophe loss of \$100 million occurs. If the quota share contract inures

to the benefit of the catastrophe reinsurer, of the gross loss of \$100 million, the quota share reinsurer pays \$50 million, the ceding insurer bears the \$20 million catastrophe retention, and the catastrophe reinsurer indemnifies the ceding insurer to the extent of \$30 million.

Investment Income

Money earned from invested assets. May also include realized capital gains, or be reduced by capital losses, over the same period.

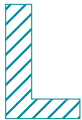
IRIS (Insurance Regulatory Information System) Tests

A series of financial tests developed by the National Association of Insurance Commissioners (NAIC) under its Insurance Regulatory Information System (IRIS) to assist states in overseeing the financial soundness of insurance companies.



Joint Account Excess of Loss Reinsurance

See Common Account Reinsurance.



Law of Large Numbers

A mathematical concept which postulates that the more times an event is repeated (in insurance, the larger the number of homogeneous exposure units), the more predictable the outcome becomes. In a classic example, the more times one flips a coin, the more likely that the results will be 50% heads, 50% tails.

Layer

Term used in an excess of loss cover. A layer indicates a stratum of cover, stating the excess point and the sum insured.

Layer Policy

Insurance policy using layers.

Leading Reinsurer

The reinsurer recognized as the one of several reinsurers on a contract responsible for negotiating the initial terms of the contract. There may be joint leaders on a contract, and the contract may specifically provide to the lead reinsurer the power to bind others to limited changes in or enhancements of the contract during its term.

Leading Underwriter

The insurer recognized as the one of several insurers on a contract responsible for negotiating the terms, conditions and premium rates of the contract. In most cases the leader takes the largest share of the risk.

Letter of Credit

A financial instrument obtained from a bank that guarantees the availability of funds to be collected in the future under a reinsurance contract. In the noncommercial setting, these are known as standby credits in the event of non-performance by the obligor. Uniform Custom and Practices for Document Bearing Credits (1993 rev.) ICC, Pub. No. 500. See Evergreen Clause.

Leveraged Effect

The disproportionate result produced by inflation on a reinsurer's liability in excess of loss reinsurance compared with the ceding company's liability. In other words, inflationary increases in average claim costs of a reinsured usually produce even greater increases for its excess of loss reinsurer, since an increase affecting all losses (those within the retention limit and those above it) multiplies itself when affecting the excess of loss portion above that retention limit. For example, if the reinsured's retention limit average claim cost increases 8%, the reinsurer's increase can be as much as twice or three times that amount, or more. The increase on the reinsurer over the ceding company's increase is referred to as the leveraged effect. The effect is leveraged in that such increases fall more on the reinsurer, proportionately at least, than on the reinsured.

Liability Insurance

Insurance providing compensation for the insured's legal liability to third parties resulting from negligent acts or omissions.

Life Insurance

Insurance providing payment of the insured sum upon death of the insured, or in the case of endowment insurance, upon survival of a specified period. In case of annuity insurance, benefits consist of a regular payment for a specified period. Other products in life insurance expand cover to incidents like critical illness or disability.

Limit

Maximum amount the insurer will pay under the policy coverage.

Limited Risk Reinsurance

See Financial Reinsurance, Finite Reinsurance, Nontraditional Reinsurance, Structured Reinsurance.

Line

- 1) Either the limit of insurance to be written that a company has fixed for itself on a class of risk (line limit), or the actual amount which it has accepted on a single risk or other unit.
- 2) A class or type of insurance (fire, marine or casualty, among others), also known as Line of Business.
- 3) The word "line" in reference usually pertains to surplus reinsurance and means the amount of the reinsured's retention with respect to each risk. Thus, reference to a "two-line reinsurance treaty" pertains to a treaty that affords reinsurance for 200% of the reinsured's retention.

Line Guide

See Line Sheet.

Line of Business

The general classification of business as utilized in the insurance industry, i.e., fire, allied lines, homeowners, etc.

Line Sheet (also known as Line Guide)

A schedule showing the limits of liability to be written by a ceding company for different classes of risk and (usually) also showing the lines which can be ceded to proportional reinsurance treaties.

Line Slip

With a line slip insurers/reinsurers agree with a reinsured/broker that the leading insurer/reinsurer can accept or reject the specified risk on behalf of all insurers/reinsurers who have accepted a share on the line slip.

Lloyd's (or Lloyds)

A kind of organization for underwriting insurance or reinsurance in which a collection of individuals assume policy liabilities as the individual obligations of each. When spelled with an apostrophe, the term refers to Lloyd's of London, the formal name of which is "Underwriters at Lloyd's, London."

Long Tail Business

Insurance business, where the financial outcome of claims can be unknown for a long time, for example in liability insurance. See Short Tail Business.

Long-Tail Liability

A term used to describe certain types of third-party liability exposures (e.g., malpractice, products, errors and omissions) where the incidence of loss and the determination of damages are frequently subject to delays that extend beyond the term the insurance or reinsurance was in force. An example would be contamination of a food product that occurs when the material is packed but which is not discovered until the product is consumed months or years later.

Loss

Event triggering a claim under the respective reinsurance/insurance contract. See Incurred Loss.

Loss Adjuster

Specialist (mostly an independent agent) who investigates into claim requests and negotiates and settles claims on behalf of the insurer/reinsurer.

Loss Adjustment Expense (LAE)

The expense incurred by the ceding insurer in the defense, cost containment and settlement of claims under its policies. They are normally broken down into two categories: Allocated (ALAE) and Unallocated (ULAE). ALAE are often considered part of the loss to the ceding insurer and may be recovered as part of the reinsurance payments from the reinsurer. By contrast, ULAE are considered part of the ceding insurer's overhead and cost of doing business, and should not be subject to reinsurance recovery. The elements of loss adjustment expenses that are covered by reinsurance are specified in the terms of the reinsurance agreement.

Loss Conversion Factor (also known as Loss Loading or Multiplier)

A factor applied to the anticipated losses (or loss cost) for an excess of loss reinsurance agreement in order to develop the reinsurance premium (or rate). This factor provides for the reinsurer's loss adjustment expense, overhead expense, and profit margin. See Rating.

Loss Development

The process of change in amount of losses as a policy or accident year matures, as measured by the difference between paid losses and estimated outstanding losses at some subsequent point in time (usually 12 month periods), and paid losses and estimated outstanding losses at some previous point in time. In common usage it might refer to development on reported cases only, whereas a broader definition also would take into account the IBNR claims.

Loss Excess of Policy Limits

An amount of loss which exceeds the policy limits, but is otherwise under the coverage terms of the policy, for which the insurer is potentially responsible by reason of its action or omissions in defending the insured under the policy.

Loss Incurred

See Incurred Loss.

Loss Loading or Multiplier

See Loss Conversion Factor.

Loss Portfolio Transfer

A financial reinsurance transaction in which loss obligations that are already incurred and which are expected to ultimately be paid are ceded to a reinsurer. In determining the premium paid to the reinsurer, the time value of money is considered, and the premium is therefore less than the ultimate amount expected to be paid. The difference between the premium paid for the transaction and the amount reserved by the cedent is the amount by which the cedent's statutory surplus increases. Other terms used in context with Lloyd's contracts are loss portfolio-rollover and reinsurance to close.

Loss Rating

See Rating.

Loss Ratio

Losses incurred expressed as a percentage of earned premiums.

Loss Reserve

For an individual loss, an estimate of the amount the insurer expects to pay for the reported claim. For total losses, estimates of expected payments for reported and unreported claims. May include amounts for loss adjustment expenses. See Incurred But Not Reported (IBNR) and Incurred Losses.

Losses Occurring

A specific time delineated in a reinsurance agreement when a loss is deemed to have occurred for purposes of determining whether the loss is within the period that reinsurance coverage applies, usually based on the definition of loss occurrence provided for in the agreement.

Losses Outstanding

Losses (reported or not reported) that have occurred but have not been paid.

Losses Paid

The amounts paid to claimants as insurance claim settlements.



Management Fee Expense (also known as Reinsurance Home Office Expense [RHOE], Reinsurer's Expense)

A deduction usually expressed as a percentage of ceded premium, in a calculation of profit or contingent commission. The amount is intended to account for the reinsurer's internal expenses.

Marine and Aviation Insurance

Insurance covering damage to goods carried and to means of transport (excluding motor driven land vehicles) which occasioned during the carriage as well as third party liability by the carrier.

Maximum Aggregate Amount

The maximum liability of the reinsurer in a reinsurance period under an excess of loss contract. The maximum aggregate amount is derived from the number of reinstatements and the occurrence limit.

Maximum Foreseeable Loss

The anticipated maximum property fire loss that could result given unusual or the worst circumstances with respect to the non-functioning of protective features (firewalls, sprinklers, a responsive fire department, etc.), as opposed to PML (Probable Maximum Loss), which would be a similar valuation, but under the assumption that such protective features function normally. See Probable Maximum Loss.

Maximum Possible Loss

The worst loss that could possibly occur because of a single event.

Mediation

A form of alternative dispute resolution in which the parties agree to submit any dispute to a neutral mediator, whose purpose and goal is to achieve a mutually acceptable settlement and compromise of the dispute, rather than issue a formal ruling and decision on the merits as occurs in arbitration. Depending upon the parties' agreement, the results of mediation can be binding, or non-binding.

Minimum Premium

An amount of premium which will be charged (usually for an excess of loss reinsurance contract), notwithstanding that the actual premium developed by applying the rate to the subject premium could produce a lower figure. See Deposit Premium.

Mortgagee Endorsement

An endorsement to an insurance policy covering the policyholder's mortgaged property to provide that, in the event of the insolvency of the insurance company, the reinsurer shall pay directly to the mortgagee and/or the policyholder the amount of loss that would have been recovered from the reinsurer by the insurance company. The endorsement may provide that the reinsurer will pay the full loss amount in accordance with the insurance protection afforded by the insurance company. Similar in concept to the Cut-Through Endorsement.



National Association of Insurance Commissioners (NAIC)

An association of the chief insurance regulatory officials of the 50 states, the District of Columbia, American Samoa, Guam, Puerto Rico and the Virgin Islands.

NBCR

An acronym referring to nuclear, biological, chemical and radiological exposures, which may be defined in the reinsurance agreement, for purposes of excluding, limiting or providing reinsurance coverage.

Net Line

The amount of insurance the primary company carries on a risk after deducting reinsurance from its "gross" line. See Net Retention.

Net Loss

The amount of loss sustained by an insurer after making deductions for all recoveries, salvage and all claims upon reinsurers – with specifics of the definition derived from the reinsurance agreement.

Net Retained Liability

The amount of insurance that a ceding company keeps for its own account and does not reinsure in any way (except in some instances for catastrophe reinsurance).

Net Retention

The amount of insurance that an insurer keeps for its own account and does not pass on to another insurer. In excess of loss reinsurance, the term "first loss retention" may be preferred. See Net Line.

Net Written Premium

Written premiums net of outward reinsurance premiums.

Nine-Months Rule

A contract signature rule adopted by the National Association of Insurance Commissioners generally imposing a nine-month time limit from the effective date of the treaty reinsurance agreement to the time when the treaty reinsurance agreement must be actually executed by the ceding company and the reinsurer or, in the case of multiple reinsurers, the lead designated reinsurer. The rule enables the ceding company to comply with statutory and/or regulatory requirements and receive accounting treatment as prospective, as opposed to retroactive, reinsurance.

Ninety-Day Rule

The National Association of Insurance Commissioners annual statement requirement which provides that an insurer or reinsurer must account for certain balances on Schedule F of the annual statement when it has reinsurance recoverables over ninety days past due for which the company may incur penalties.

No Claims Discount/Bonus

A discount or bonus for the benefit of the reinsured given in excess of loss reinsurance covers applicable after a loss free period for the specified cover.

Non-Admitted Assets

Assets owned by an insurance company that are not recognized for solvency purposes by state insurance laws or insurance department regulations, e.g., premiums due and uncollected past 90 days, and furniture and fixtures among others.

Non-Admitted Company

- 1) An insurer not licensed in a given state.
- 2) A reinsurer not licensed or approved in a given state.

Non-Admitted Insurance

Insurance protection placed with a non-admitted insurer.

Non-Admitted Reinsurance (also known as Unauthorized Reinsurance)

Reinsurance placed with a reinsurer that does not have authorized or equivalent status in the jurisdiction in question. See Admitted Reinsurance.

Non-Life insurance

All classes of insurance which are not written under life insurance, for example property, casualty and marine insurance.

Non-Proportional Reinsurance

See Excess of Loss Reinsurance.

Nontraditional Reinsurance

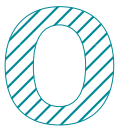
See Financial Reinsurance, Finite Reinsurance, Limited Risk, Structured Reinsurance, Reinsurance.

Non-Waiver Clause

See Estoppel.

Novation

The substitution of a new contract, debt or obligation for an existing one, between the same or different parties. A novation may substitute a new party and discharge one of the original parties to a contract by agreement of all parties. The requisites of a novation are 1) a previously valid obligation; 2) an agreement of all the parties to a new contract; 3) the extinguishment of the old obligation; and 4) the validity of the new obligation.



Obligatory Reinsurance

Also treaty reinsurance. A standing agreement between reinsured and reinsurer for the cession and assumption of certain risks as defined in the treaty, where both parties are obliged to cede / to accept the risk.

Obligatory Treaty

A reinsurance contract under which the subject business must be ceded by the insurer in accordance with contract terms and must be accepted by the reinsurer.

Occurrence

A frequently used term in reinsurance referring to an incident, happening or event which triggers coverage under an occurrence-based agreement. The definition of an occurrence will vary, depending upon the intent and interests of the parties. See Event.

Occurrence Coverage

A policy covering claims that arise out of damage or injury that took place during the policy period regardless of when claims are made. Most commercial general liability insurance is written on an occurrence form. Contrast with claims-made coverage.

Occurrence Limit

A provision in most property per risk reinsurance contracts that limits the reinsurer's liability for all risks involved in one occurrence. See Occurrence.

Offset (also known as Setoff)

The netting of amounts due between two parties as provided for by common law, contract law, statutory law, regulatory law and/or judicial law. Some reinsurance contracts contain a mutual right of offset, while others may operate only for one party's benefit. Offset may be allowed under all contracts between the parties or only under that specific contract.

Operating Income/Profit

The sum of the net investment income and net underwriting income in any reporting period.

Operating Ratio

The arithmetic sum of two ratios: incurred loss to earned premium, and incurred expense to written premium. Considered the best simple index to current underwriting performance of an insurer.

Original Conditions Clause

A provision in a reinsurance agreement which incorporates by reference all of the terms (as well as amendments, modifications, alterations and waivers) of the original policy written by the ceding company that are not otherwise addressed in the reinsurance agreement. See Follow the Fortunes.

Original Terms Basis

Terms for the reinsurers are the same basis as accepted by the leading insurer.

Outstanding Loss Reserve (OLR, O/S)

For an individual loss, an estimate of the amount the insurer expects to pay for the reported claim. For total losses, estimates of expected payments for reported and unreported claims. May include amounts for loss adjustment expenses. See Incurred But Not Reported (IBNR), Incurred Losses and Loss Development.

Outwards Reinsurance

The process of an insurer or reinsurer reinsuring a risk, risks or individual portfolios with a set of various reinsurance companies.

Overriding Commission

- 1) An allowance paid to the ceding company over and above the acquisition cost to allow for overhead expenses and often including a margin for profit.
- 2) A fee or percentage of money that is paid to a party responsible for placing a retrocession of reinsurance.
- 3) In insurance, a fee or a percentage of money that is paid by the insurer to an agent or general agent for premium volume produced by other agents in a given geographic area.



Participating Reinsurance (also known as Proportional Reinsurance, Pro Rata Reinsurance, Quota Share Reinsurance)

A generic term describing all forms of quota share and surplus reinsurance in which the reinsurer shares a pro rata portion of the losses and premiums of the ceding company.

Payback Period

A method of reinsurance rating under which the price is based on how frequently a limits loss might occur over a period of time based on historical or projection indications. Thus, if the indicated or projected loss would occur only once in five years, the price would be set (without regard to expenses and profit margins) to be equal to the limit divided by five and the contract would thus be said to have a "five year payback." Inverse calculation with Rate on Line.

Peril

Possible cause of a loss in property insurance, such as fire, windstorm, earthquake, hail, etc.

Period of Contract

The in force period of an insurance or reinsurance contract.

Per-Risk Reinsurance

Reinsurance in which the reinsurance limit and the retention apply "per risk" rather than per accident, per event, or in the aggregate.

Placement Slip

A temporary agreement of reinsurance terms and conditions arrangements for which coverage has been effected, pending replacement by a formal reinsurance contract. See Binder and Cover Note.

Policy

Another expression for the insurance contract. A legal document which indicates the terms and conditions on which the contract between the insured and the insurer is based on.

Policy Year

The year incepting with the effective date of the policy or with an anniversary of that date.

Policy Year Experience

The segregation of all premiums and losses attributable to policies having an inception or renewal date within a given 12-month period. More specifically, the total value (losses paid plus loss reserves) of all losses arising from (regardless of when reported) policies incepting or renewing during the year is divided by the fully developed earned premium for those same policies. The finally developed earned premium will always equal the written premium for those policies. Policy Year Experience resembles Accident Year Experience in that, while the experience is developing, loss reserves are used in the calculation, but the ultimate result cannot be finalized until all losses are settled. Policy Year Experience is different in that premiums earned from policies incepting during a one-year period of time will earn over the course of both the year of inception and a later year(s). Similarly, losses to be included will be occurring over this same extended time period. See Accident Year Experience and Calendar Year Experience.

Policyholder Surplus

- 1) The net worth of an insurer as reported in its Annual Statement. For a stock insurer, the sum of its surplus and capital. For a mutual insurer, its surplus.
- 2) The amount by which the assets of an insurer exceed the organization's liabilities. Another name for Surplus to Policyholders.

Pool

Any joint underwriting operation of insurance or reinsurance in which the participants assume a predetermined and fixed interest in all business written. Pools are often independently managed by professionals with expertise in the classes of business undertaken, and the members share equally in the premiums, losses, expenses and profits. An "association" and a "syndicate" (excluding that of Lloyd's of London) are both synonymous with a pool, and the basic principles of operation are much the same.

Portfolio

A reinsurance term that defines a body of: 1) insurance (policies) in force (premium portfolio), 2) outstanding losses (loss portfolio), or 3) company investments (investment portfolio). The reinsurance of all existing insurance, as well as new and renewal business, is therefore described as a running account reinsurance with portfolio transfer or assumption.

Portfolio Reinsurance

The transfer of portfolio via a cession of reinsurance; the reinsurance of a runoff. Only policies in force (or losses outstanding) are reinsured, and no new or renewal business is included. Premium or loss portfolios, or both, may be reinsured. The term is sometimes applied to the reinsurance by one insurer of all business in force of another insurer retiring from an agency from a territory or from the insurance business entirely.

Portfolio Return

If the reinsurer is relieved of liability (under a pro rata reinsurance) for losses happening after termination of the treaty or at a later date, the total unearned premium reserve on business less unreinsured (less ceding commissions thereon) is normally returned to the cedent. Also known as a return portfolio or return of unearned premium.

Portfolio Runoff

Continuing the reinsurance of a portfolio until all ceded premium is earned, or all losses are settled, or both. While a loss runoff is usually unlimited as to time, a premium run-off can be for a specified duration.

Possible Maximum Loss

See Probable Maximum Loss.

Premium

The monetary consideration in contracts of insurance and reinsurance.

Premium Base

See Base Premium.

Premium Portfolio Entry

A reinsurer's responsibility for cessions in force at the time at the inception of a reinsurance contract or reinsurance period. For this responsibility the reinsurer is being paid an unearned premium.

Premium Portfolio Withdrawal

On expiry of a reinsurance contract, or at the cancellation of the reinsurance contract, the reinsurer can be relieved of responsibility for any in force contract risks by paying to the reinsured a premium which represents the unearned exposure. The reinsurer is then relieved from any further obligations.

Premium Reserves

A reinsurer deposits the unearned premium with the cedent (also known as: unearned premium reserves). The cedant reserves it for future liabilities (i.e. for the unexpired part of each cession) and is gradually released each quarter after it has been earned. In some countries premium reserves are required by law. See Deposit.

Premiums Earned

When used as an accounting term, premiums earned describe the premiums written during a period plus the unearned premiums at the beginning of the period less the unearned premiums at the end of the period.

Primary

In reinsurance this term is applied to the nouns: insurer, insured, policy and insurance and means respectively: 1) the insurance company which initially originates the business, i.e., the ceding company; 2) the policyholder insured by the primary insurer; 3) the initial policy issued by the primary insurer to the primary insured; 4) the insurance covered under the primary policy issued by the primary insurer to the primary insured (sometimes called "underlying insurance").

Pro Rata Reinsurance (also known as Proportional Reinsurance)

A generic term describing all forms of quota share and surplus reinsurance in which the reinsurer shares a pro rata portion of the losses and premiums of the ceding company. See Quota Share Reinsurance and Surplus Share Reinsurance.

Probable Maximum Loss

The anticipated maximum property fire loss that could result given the normal functioning of protective features (firewalls, sprinklers, a responsive fire department, etc.), as opposed to MFL (Maximum Foreseeable Loss), which would be similar valuation, but on a worst-case basis with respect to the functioning of the protective features. Underwriting decisions typically would be influenced by PML evaluations, and the amount of reinsurance ceded on a risk would normally be predicated on the PML valuation. See Maximum Foreseeable Loss.

Professional Reinsurer

A term used to designate an organization whose business is mainly reinsurance and related services, as contrasted with other insurance organizations that may operate reinsurance — assuming departments in addition to their basic primary insurance business.

Profit Commission

See Contingent Commission.

Proportional Reinsurance

See Quota Share Reinsurance, Participating Reinsurance, Pro Rata Reinsurance, Surplus Reinsurance.

Prospective Rating

See Rating.

Provisional Notice of Cancellation

Cancellation of a reinsurance contract written on a continuous basis. This cancellation can be initiated by either party only on the anniversary date of the contract with prior written notice.

Provisional Rate, Premium, or Commission

Tentative amounts applicable to either rate, premium or commission set at the start of the contract and subject to subsequent adjustment.

Proximate Cause

The proximate cause is the most direct cause of a loss which can be established.

Punitive Damages

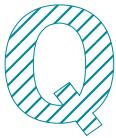
Damages awarded separately and in addition to compensatory damages, usually on account of malicious or wanton misconduct, to punish the wrongdoer and possibly others. Sometimes referred to as “exemplary damages” when intended to “make an example” of the wrongdoer.

Pure Loss Cost

See Burning Cost.

Pure Premium

- 1) That part of the premium which is sufficient to pay losses and loss adjustment expenses but not including other expenses.
- 2) The premium developed by dividing losses by units of exposure, disregarding any loading for commission, taxes and expenses.
- 3) In crop-hail insurance, the ratio of incurred loss to liability, or the dollars of loss per \$100 of insurance in force.



Quota Share Reinsurance

A form of pro rata reinsurance indemnifying the ceding company for an established percent or percentage of loss on each risk covered in the contract in consideration of the same percentage of the premium paid to the ceding company.

Quoting/Quotation

Indication and calculation of the adequate premium level and/or rate for a risk and/or portfolio of risks.



Rate

The percent or factor applied to the ceding company's subject premium to produce the reinsurance premium.

Rate on Line

A percentage derived by dividing reinsurance premium by reinsurance limit; the inverse is known as the payback or amortization period. For example, a \$10 million catastrophe cover with a premium of \$2 million would have a rate on line of 20 percent and a payback period of 5 years.

Rating

There are two basic approaches for pricing of reinsurance contracts usually applied to excess of loss reinsurance contracts: exposure rating and experience rating. Both methods can be used as separate rating approaches or may be weighted together to calculate the price for the contract.

Experience Rating (also known as Loss Rating)

An approach by which the rate is determined based on the ceding company's historical loss experience, actual and reconstructed.

Prospective Rating (also known as Flat Rating)

A formula for calculation of reinsurance premium for a specified period where a fixed rate is promulgated using the ceding company's historical loss experience, actual or constructed, and the premium for the current period is calculated by multiplying the fixed rate by the current period ceded earned (or occasionally written) premium.

Retrospective Rating (also known as Self Rating, Swing Rating, and Loss Rating)

A formula for calculation of reinsurance premium for a specified period where a provisional rate is promulgated using the ceding company's historical loss experience, and is adjusted (subject to minimum and maximum) based on the current period actual loss experience. Premium for the current period is then calculated by multiplying the adjusted rate by the by the current period ceded earned premiums.

Loss Loaded Rating (also known as Expense Loaded)

A type of retrospective rate adjustment using the same period losses multiplied by a loss load and/or expense load.

Margin Plus Rating

A type of retrospective rate adjustment using the same period losses expressed as a ratio of earned premium for the same period plus a fixed margin.

Exposure Rating

An approach by which the rate is determined based on analysis of the exposure inherent in the business being covered by the contract based on industry experience for the same type of business (rather than on the actual historical loss experience of the company).

Cessions Basis (also known as Cessions Made, Cessions Schedule)

A reinsurance pricing mechanism used on casualty reinsurance contracts where a premium for each reinsured policy is ceded to Reinsurer individually based on the exposure of the policy limits to the reinsurance limits (usually based on Increased Limit Factors).

Reassured

See Cedent, Reinsured.

Recapture

The action of a ceding company to take back reinsured risks previously ceded to the reinsurer.

Reciprocity

A mutual exchange of reinsurance between two or more companies.

Recoveries

Amounts received from a reinsurer for a reinsured's losses.

Reinstatement

The restoration of the reinsurance limit of an excess property treaty to its full amount after payment by the reinsurer of loss as a result of an occurrence.

Reinstatement Clause

When the amount of reinsurance coverage provided under a contract is reduced by the payment of loss as the result of one occurrence, the reinsurance cover is automatically reinstated, sometimes subject to the payment of a specified reinstatement premium. Reinsurance contracts may provide for an unlimited number of reinstatements or for a specific number of reinstatements. See Reinstatement Premium.

Reinstatement Cover

A type of reinsurance that provides a ceding company all or a portion of the ceding company's contract or program limits that were eroded under a reinstatement clause in the original reinsurance agreement. The reinstatement cover is normally a separate agreement and the term usually incept at the date of the last loss, running through the end of the original coverage period. Customarily, the reinstatement cover provides only a single limit and is not likely to include a reinstatement provision. For example, after the major windstorms of 2004 and 2005, ceding companies that sustained losses reinsured under their reinsurance contracts may have lacked sufficient reinsurance protection for the remainder of the year. In such an instance, those insurers might attempt to secure reinsurance to replace that no longer available under the original contracts.

Reinstatement Premium

An additional pro rata reinsurance premium that may be charged for reinstating the amount of reinsurance coverage reduced as the result of a reinsurance loss payment under a reinsurance contract. See Reinstatement Clause.

Reinsurance

The transaction whereby the assuming insurer in consideration of premium paid, agrees to indemnify the ceding company against all or part of the loss which the latter may sustain under the policy or policies which it has issued.

Reinsurance Assumed

That portion of risk the reinsurer accepts from the original insurer or ceding company.

Reinsurance Ceded

That portion of the risk which the ceding company transfers to the reinsurer.

Reinsurance Commission

Another name for Ceding Commission.

Reinsurance Conditions

All clauses included in a reinsurance contract.

Reinsurance Home Office Expense (RHOE)

See Management Fee Expense.

Reinsurance Premium

The consideration paid by a ceding company to a reinsurer for the coverage provided by the reinsurer.

Reinsured (also known as Cedent, Ceding Company or Reassured)

A company that has placed reinsurance risks with a reinsurer in the process of buying reinsurance.

Reinsurer

The insurer which assumes all or a part of the insurance or reinsurance risk written by another insurer. See Professional Reinsurer.

Reinsurer's Expense

See Management Fee Expense.

Reports and Remittances Clause

The contract clause that specifies the types, timing and frequency of reports that are due to the reinsurer and usually outlines the format and content of the reports. Stipulates when adjustments and balances (if any) are due to either party.

Reserve

An amount which is established to provide for payment of a future obligation.

Retention

The amount of risk the ceding company keeps for its own account or the account of others.

Retroactive Date

The date on a claims made policy or reinsurance contract which triggers the beginning period of coverage for occurrences commencing prior to the effective date of the policy. A retroactive date is not required. If one is shown on a claims made policy, any claim made during the policy period on a loss that occurred before the retroactive date will not be covered. In reinsurance, losses occurring before the contract term are sometimes covered by the addition of "retroactive" coverage to the contract. See Extended Reporting Period.

Retrocede

The action of a reinsurer of reinsuring with another reinsurer its liability assumed through the issuance of one or more reinsurance contracts to primary insurance companies or to other reinsurers. The reinsurer seeking protection may purchase a reinsurance contract or contracts that will indemnify it within certain parameters for certain described losses under that reinsurance contract or contracts. This action is described as transferring the risk or a part of the risk. The reinsurer seeking protection (the buyer) is called the retrocedent and the reinsurer providing the protection (the seller) is called the retrocessionaire.

Retrocedent

A reinsurer who underwrites and issues a reinsurance contract to a reinsured (either a primary insurance carrier or another reinsurer) and contractually obtains an indemnification for all or a designated portion of the risk from one or more retrocessionaires. See Retrocede.

Retrocession

The reinsuring of reinsurance. A reinsurance transaction whereby a reinsurer, known as a retrocedent, cedes all or part of the reinsurance risk it has assumed to another reinsurer, known as a retrocessionaire.

Retrocessionaire

The assuming reinsurer in a retrocession, where the ceding reinsurer is known as the retrocedent.

Retrospective Rating (also known as Self Rating, Swing Rating)

See Rating.

Return Portfolio

The reassumption by a ceding company of a portfolio of risks previously assumed by the reinsurer. See Assumed Portfolio.

Risk

A term which defines uncertainty of loss, chance of loss, or the variance of actual from expected results as it relates to coverage provided under an insurance or reinsurance contract. Also, the term is used to identify the object of insurance protection, e.g., a building, an automobile, a human life, or exposure to liability. In reinsurance, each ceding company customarily makes its own rules for defining a risk.

Risk Attaching Basis

LORA contract: (losses occurring on risks attaching) A contract type where reinsurance is provided for claims arising from original policies that the cedent incepts during the term of an arrangement, as opposed to a loss-occurring approach (also called LOD contracts: losses occurring during).

Risk Based Capital

A method utilized by insurance regulatory authorities to determine the minimum amount of capital required of an insurer to support its operations and write coverage. The insurer's risk profile (i.e., the amount and classes of business it writes) is used to determine its risk based capital requirement.

Risk Premium

The part of the premium that is purely needed to cover a potential loss. All other expenses like commissions, profits and taxes are not included.

Risk Transfer

A key element of reinsurance, whereby insurance risk is shifted from the reinsured to the reinsurer under a reinsurance agreement. In order for a reinsured to receive statutory and GAAP credit for reinsurance, a threshold of both underwriting risk and timing risk transfer must be achieved. See Risk.

Risk-Based Capital

Risk-based capital is the hypothetical amount of capital that is allocated to operate insurance or reinsurance to ensure that the risk-based part of the business has a reasonably low expectation of becoming financially insolvent. The amount of required capital is calculated by risks and financial-based mathematical models.

Run Off

A termination provision of a reinsurance contract that stipulates the reinsurer remains liable for loss as a result of occurrences taking place after the date of termination for reinsured policies in force at the date of termination until their expiration or for a specified time period.



Salvage

Amount of a paid loss in property insurance that is returned by the insured to the insurer because he could make money out of the damaged asset by using or selling it.

Schedule F

The schedule within the Annual Statement which provides information on a company's reinsurance transactions.

Self-Insurance

Insurance organized by the insured himself usually by building reserves through funds. Often used when insurance capacity is difficult to get or expensive.

Semi-Automatic Treaty

See Facultative Semi-Obligatory Treaty.

Service of Suit Clause

A clause in reinsurance contracts whereby the reinsurer agrees to submit to any court of competent jurisdiction in the United States, which provides a legal basis for the enforcement of arbitration awards. The clause names a U.S. agent to accept service of process on behalf of the reinsurer for purposes of the ceding company gaining U.S. jurisdiction against the reinsurer. It is not intended to supersede the contracting parties' obligation to arbitrate disputes, but to provide a mechanism to enforce awards.

Setoff

See Offset.

Severability Clause

A clause in some reinsurance agreements, providing that should any part of the agreement be found illegal or otherwise unenforceable, the remainder of the agreement will continue in force while the illegal part will be severed from the agreement. Severability may apply to the entire agreement or be limited to a specific provision which may present enforceability issues. For example, in jurisdictions where punitive damages are uninsurable, a severability clause in an Extra Contractual Obligations provision (or as a separate clause) will preserve the overall enforceability of the provision, even though a portion of the ECO provision has been invalidated.

Short Tail Business

Insurance business where claims are typically settled within a few weeks to one year of the loss occurrence. This is often the case in property insurance and rarely in casualty. See Long Tail Business.

Sidecar

A special purpose vehicle designed to allow investors to assume the risk and earn the profit on a group of insurance policies (a “book of business”) written by a particular insurer or assumed by a particular reinsurer (collectively “re/insurer”). A re/insurer will usually only cede the premiums associated with a book of business to such an entity if the investors place sufficient funds in the vehicle to ensure that it can meet claims if they arise. Typically, the liability of investors is limited to these funds. The vehicle is often formed as an independent company and to provide additional capacity to the re/insurer to write property catastrophe business or other short tail lines. The original capacity is usually provided through a quota share or similar type arrangement. The re/insurer normally charges a fee (ceding commission) for originating and managing the sidecar business and may sometimes also receive a profit commission if the book of business is profitable. Because the investors’ capital is usually intended to be invested in this vehicle for a short-term, the sidecar has a limited existence, often for only one year, after which investors may withdraw their investment. These structures have become quite prominent in the aftermath of Hurricane Katrina as a vehicle for re/insurers to add risk bearing capacity, and for investors to participate in the potential profits resulting from sharp price increases in re/insurance.

Sliding Scale Commission

A commission adjustment on earned premiums under a formula whereby the actual commission varies inversely with the loss ratio, subject to stated maximum and minimum percentages.

Slip

A comprehensive document containing details of the risk, the cover period, the premium and the participation of the reinsurer. It is signed by the reinsured and reinsurer. Later on it is replaced by a full reinsurance contract wording describing all details.

Solvency

The ability of insurance companies to ensure that they are always able to meet their liabilities for claims.

Solvency Margin

The assets owned by the insurer have to exceed its liabilities. The calculation method of the required solvency margin is normally regulated by the supervisory authority of a given country.

Special Acceptance

The specific agreement by the reinsurer to include under a reinsurance contract a risk not included within the terms of the contract.

Special Termination Clause

A clause found in reinsurance contracts providing that, upon the happening of some specified condition or event, such as the insolvency, merger, loss in credit rating or decline in policyholder surplus of one party, the other party can fully terminate the contract earlier than would otherwise be required, had such condition or event not happened. The clause should state which party may initiate the termination, the notice requirements, the triggering conditions or events necessary, the effective date of termination, and the method of terminating existing business (i.e., whether on a cut-off or run-off basis).

Standard Premium

The insurance premium determined on the basis of the insurer's authorized rates multiplied by the experience modification factor. The standard premium is usually not the final premium that the insured pays. It excludes the effects of some pricing programs, such as premium discounts, schedule rating, deductible credits, retrospective rating, and expense constants that are reported in statistical classes.

Statutory Accounting Principles (SAP)

Those principles required by state law that must be followed by insurance companies in submitting their financial statements to state insurance departments. Such principles differ from generally accepted accounting principles (GAAP) in some important respects, e.g., SAP requires that expenses must be recorded immediately and cannot be deferred to track with premiums as they are earned and taken into revenue. See GAAP.

Statutory Annual Statement

See Annual Statement.

Stop Loss Reinsurance

See Aggregate Excess of Loss Reinsurance.

Structured Reinsurance

See Financial Reinsurance, Finite Reinsurance, Limited Risk Reinsurance, Nontraditional Reinsurance.

Structured Settlements

The settlement of a casualty or workers' compensation claim involving periodic annuity payments over an extended period of time, rather than in one up-front, lump sum cash payment. There are certain advantages to a claimant under a structured settlement, including favorable tax treatment of interest under the Internal Revenue Code, that are not present under a lump sum cash settlement. Structured settlements are designed to guard against the early dissipation of settlement proceeds by recipients, who are often minors or those in need of life-time care as a result of their injuries.

Subject Premium

See Base Premium.

Subrogation

The assignment of a contractual right of an insured or reinsured by terms of the policy or by law, after payment of a loss, of the rights of the insured to recover the amount of the loss from one legally liable for it. The ceding insurer and reinsurer can agree how subrogation rights and recoveries will be addressed and handled under the reinsurance agreement.

Sunrise Clause

A clause in casualty reinsurance contracts that provides coverage for losses reported to the reinsurer during the term of the current reinsurance contract, but resulting from occurrences that took place during a prior period. Sunrise clauses are used to reactivate coverage that no longer exists due to the existence of a sunset clause. See Sunset Clause.

Sunset Clause

A clause in casualty reinsurance contracts that provides that the reinsurer will not be liable for any loss that is not reported to the reinsurer within a specified period of time after the expiration of the reinsurance contract. See Sunrise Clause.

Surplus Liability

That portion of a reinsured company's gross liability on any one risk which exceeds the amount the company is willing to retain net for its own account.

Surplus Reinsurance (also known as Surplus Share Reinsurance)

A form of pro rata reinsurance under which the ceding company cedes that portion of its liability on a given risk which is greater than the portion of risk the cedent retains (i.e., net line), and the premiums and losses are shared in the same proportion as the ceded amount bears to the total limit insured on each risk.

Surplus Relief

- 1) The result of reinsurance ceded on a portfolio basis to offset extraordinary drains on policyholder surplus.

- 2) A designation of a reinsurance the main purpose of which is to finance new or in-force business, or both. See Financing Function.

Surplus Share Reinsurance

See Surplus Reinsurance, Variable Quota Share Reinsurance.

Surplus to Policyholders

- 1) The net worth of an insurer as reported in its Annual Statement. For a stock insurer, the sum of its unassigned surplus and capital.
- 2) The amount by which the assets of an insurer exceed the organization's liabilities. Another name for Policyholder Surplus.

Swing Rating

See Rating.

Syndicate

An association of individuals or organizations to pursue certain insurance objectives. For example, individual underwriters in Lloyd's of London associate in separate syndicates to write marine insurance, reinsurance life insurance, etc., entrusting the administrative details of each syndicate to a syndicate manager. See Association, Pool.



Target Risk

In property reinsurance certain risks (for example, particular bridges, tunnels, fine arts collections, and property of similarly high value and exposure) that are excluded from coverage under reinsurance treaties.

Such risks require individual acceptance under facultative contracts.

Term Contract

A form of reinsurance contract written for a stipulated term (usually one year). The contract automatically expires at the end of the term and renewal must be negotiated. See Continuous Contract.

Total Insurable Value (TIV)

The total values for insured perils and coverages for a particular risk, whether or not insurance limits have been purchased to that amount.

Total Insured Value Clause

An exclusion that prevents a reinsurer's over-lining on a single large risk (usually excess of \$250 million) caused by a potential accumulation of property limits from two or more ceding companies. The customary exception to the exclusion applies to risks insured 100 percent by one insurer or specifically listed classes (such as apartments, offices, hotels, hospitals, etc.).

Treaty

A reinsurance contract under which the reinsured company agrees to cede and the reinsurer agrees to assume risks of a particular class or classes of business.

Treaty Reinsurance

A standing agreement between reinsured and reinsurer for the cession and assumption of certain risks as defined in the treaty. While most treaty reinsurance provides for automatic cession and assumption, it may be optional or semi-obligatory and is not necessarily obligatory.

Trending

The necessary adjustment of historical statistics (both premium and losses) to present levels or expected future levels in order to reflect measurable changes in insurance experience over time, which are caused by dynamic economic and demographic forces, and to make the data useful for determining current and future expected cost levels.

TRIA/TRIEA

TRIA refers to the Terrorism Risk Insurance Act of 2002. TRIEA refers to the Terrorism Risk Insurance Extension Act of 2005, which extended the originally enacted TRIA, which was due to expire at the end of the 2005 year. Generally, the Act provides for a certain amount of federal reimbursement to insurance carriers for certified terrorism-related losses when a particular industry aggregate loss threshold is met, exclusive of an applicable insurer deductible and co-participation percentage, as defined under the Act.

Trust Agreements

An agreement establishing a trust arrangement, which may be utilized as a mechanism by the reinsurer for purposes of securing its obligations to the ceding company to satisfy securitization requirements that might apply to the reinsurer under the terms of a reinsurance agreement. Under the trust arrangement, a legal entity is created by a grantor (usually the reinsurer) for the benefit of a designated beneficiary (usually the ceding company). The trustee (generally a financial institution) holds a fiduciary responsibility to handle the trust's corpus assets and income for the economic benefit of the beneficiary, in accordance with the terms of the trust. In the event that the reinsurer defaults in its payment obligations to the ceding company under the terms of the reinsurance agreement, the trustee may release funds from the corpus of the trust to satisfy such obligations to the ceding company, in accordance with the terms of the trust. In reinsurance, such an agreement is typically established to permit a licensed ceding company to take credit for non-admitted reinsurance up to the value of the assets in the trust.



Uberrimae Fidei

Literally, of the utmost good faith. A defining characterization or quality of some (contractual) relationships, of which reinsurance is universally recognized to be one. Among other differences from ordinary relationships, the nature of reinsurance transactions is dependent upon a mutual trust and a lively regard for the interests of the other party, even if inimical to one's own. A breach of utmost good faith, especially in regard to full and voluntary disclosure of the elements of risk of loss, is accepted as grounds for any necessary reformation or redress, including rescission. See Utmost Good Faith.

Ultimate Net Loss

- 1) In reinsurance, the measure of loss to which the reinsurance applies, as determined by the reinsurance agreement.
- 2) In liability insurance, the amount actually paid or payable for the settlement of claims for which the reinsured is liable (including or excluding defense costs) after deductions are made for recoveries and certain specified reinsurance.

Umbrella Cover

Reinsurance protection for several classes of business that combines the contracts of different classes of business into one reinsurance contract.

Unauthorized Insurer, Reinsurer

An insurer not licensed, or a reinsurer neither licensed nor approved, in a designated jurisdiction.

Unauthorized Reinsurance

See Non-Admitted Reinsurance.

Underlying

The amount of insurance or reinsurance on a risk (or occurrence) which applies to a loss before the next higher excess layer of insurance or reinsurance attaches.

Underlying Premium

See Base Premium.

Underwriter

An employee of an insurer or reinsurer with the responsibility to negotiate, accept or reject the terms of the (re-)insurance on behalf of his employer.

Underwriting Capacity

The maximum amount of money an insurer or reinsurer is willing to risk in a single loss event on a single risk or in a given period. The limit of capacity for an insurer or reinsurer that may also be imposed by law or regulatory authority.

Underwriting Income

The excess of premiums earned by a reinsurer during any reporting period over the combined total of expenses and losses incurred by the reinsurer during the same period.

Underwriting Result

Premiums earned less insurance losses, adjustment expenses and underwriting expenses (determined on a GAAP or statutory basis). Also referred to as GAAP underwriting result or statutory underwriting result.

Underwriting Year Experience

The effective date of the original policy, rather than the date of loss, determines the basis of attachment. Any losses occurring on policies written or renewed with inception or renewal dates during the term of the given reinsurance agreement will be covered by that reinsurance agreement irrespective when the loss actually occurred. This mechanism is often used with “the policies attaching” methodology.

Unearned Premium Portfolio

The effective date of the original policy, rather than the date of loss, determines the basis of attachment. Any losses occurring on policies written or renewed with inception or renewal dates during the term of the given reinsurance agreement will be covered by that reinsurance agreement irrespective when the loss actually occurred. This mechanism is often used with “the policies attaching” methodology. The sum of all unearned premium for in force policies of insurance under the reinsurance agreement, often with respect to a particular block, book or class of business during a particular period.

Unearned Premium Portfolio Rollover

A term describing an accounting transaction in which an unearned premium portfolio is carried forward from one accounting period to the following accounting period under an existing contract or a renewal.

Unearned Premium Reserve

The reserve amount included in the company’s financial statements for unearned premiums with respect to the insurance policies or reinsurance agreements as of a particular point in time. Unearned premiums are the sum of all the premiums representing the unexpired portions of the policies or reinsurance agreements which the insurer or reinsurer has on its books as of a certain date.

Unearned Reinsurance Premium

That part of the reinsurance premium applicable to the unexpired portion of the policies reinsured.

Utmost Good Faith

One of the basic principles of insurance and reinsurance contracts. A breach of good faith by one party entitles the other to avoid the contract. Giving false information or withholding certain information by an involved party may lead to a breach of good faith. See *Uberrimae Fidei*.



Variable Quota Share Reinsurance

See Surplus Reinsurance.



Warranted No Known or Reported Losses (WNKORL)

A statement made on application for a facultative, excess or catastrophe reinsurance, which is being back-dated, to protect the reinsurer from placement of reinsurance after a loss has occurred.

Working Cover or Layer

That layer of an excess of loss reinsurance program in which loss frequency is anticipated.

Working Excess

A contract covering an area of excess reinsurance in which loss frequency is anticipated, as opposed to loss severity. Thus, a working cover would usually have a low indemnity and would attach above a relatively low retention.

Working Layer

The first layer of an excess of loss program where the excess point is relatively low.

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