Direct Your Learning

14

Reinsurance Aspects of the NAIC Annual Statement

Educational Objectives

After learning the content of this assignment, you should be able to:

- Describe the major assets and liabilities found on the balance sheet of an insurer's National Association of Insurance Commissioners (NAIC) Annual Statement, particularly those that pertain to reinsurance transactions.
- Describe the information contained in the Underwriting and Investment Exhibit of an insurer's National Association of Insurance Commissioners (NAIC) Annual Statement, particularly that pertaining to reinsurance transactions.
- Describe the information contained in Schedule F of an insurer's National Association of Insurance Commissioners (NAIC) Annual Statement.
- Describe the information contained in Schedule P of an insurer's National Association of Insurance Commissioners (NAIC) Annual Statement.

Outline

14 Reinsurance Aspects of the NAIC Annual Statement

REINSURANCE TRANSACTIONS AND THE NAIC ANNUAL STATEMENT BALANCE SHEET

The National Association of Insurance Commissioners (NAIC) Annual Statement is the uniform financial report that all insurers (both primary insurers and reinsurers) file annually with the insurance department of each state in which they are authorized to do business.The Annual Statement is prepared according to statutory accounting principles (SAP) and is designed to provide state insurance regulators with the information needed to regulate insurers' solvency. It is also the means through which state insurance departments are able to obtain nearly uniform financial reporting from all insurers.

The Annual Statement is a complex and lengthy financial document consisting of a balance sheet (assets, liabilities, and policyholders' surplus), a statement of income, and a cash flow statement and is backed by supporting exhibits and schedules.The Annual Statement Blank consists of more than 200 pages, but a completed Annual Statement for a large insurer usually contains additional pages because of schedules listing investment securities and investment transactions. The Annual Statement is the primary source of insurer financial information. See the exhibit "Key Components of the Annual Statement."

Although a comprehensive discussion of the Annual Statement can be useful, this discussion focuses on the elements of an insurer's balance sheet that are affected by reinsurance transactions.

The balance sheet portion of the Annual Statement Blank includes assets and liabilities similar to those found on the balance sheet of any business. For example, cash and real estate are included as assets. It also includes many assets and liabilities that are unique to insurance operations, such as reinsurance recoverable, reinsurance payable, and the unearned premium reserve.

A reinsurer may analyze a primary insurer's Annual Statement balance sheet to measure the primary insurer's financial strength and to determine the primary insurer's reinsurance needs.

Assets

According to statutory accounting principles (SAP), assets are categorized as admitted or nonadmitted.

Key Components of the Annual Statement

The Annual Statement blank contains more than 200 pages of financial statements and supporting exhibits and schedules. Many of the schedules and exhibits themselves have subschedules and supplemental addenda.

- Balance Sheet
  - Assets
  - Liabilities, Surplus and Other Funds
- Statement of Income
- Cash Flow
- Details on Underwriting and Investment Results:
  - Underwriting and Investment Exhibits
  - Exhibit of Premiums and Losses
  - Insurance Expense Exhibits
- Details on Investment Holdings:
  - Schedule A—Real Estate
  - Schedule B—Mortgage Loans
  - Schedule BA—Other Long-Term Invested Assets
  - Schedule D—Bonds and Stocks
  - Schedule DA—Short-Term Investments
  - Schedule DB—Derivative Investments
  - Schedule E—Cash and Cash Equivalents
  - Schedule F—Reinsurance
  - Schedule P—Losses and Loss Expenses
- Notes to Financial Statements
- General Interrogatories
- Five-Year Historical Data

[DA06249]

Admitted assets are those assets that are approved by a state insurance department for inclusion on an insurer's Annual Statement balance sheet. Typically, admitted assets must meet minimum liquidity requirements and have a predictable market value.

Nonadmitted assets are assets that are not permitted by a state insurance department to be shown on an insurer's Annual Statement balance sheet. This is typically because they are not readily marketable. Examples of nonadmitted assets are agents' balances over ninety days past due and investment securities that are in default. Nonadmitted assets are shown on the Annual Statement but not on the balance sheet. Therefore, insurer investments in these assets reduce policyholders' surplus.

The assets side of the balance sheet summarizes the insurer's admitted assets. Supporting schedules provide more detail about particular categories of assets. For most property-casualty insurers, investment securities are the largest admitted asset. Consequently, the first nine items found on the Annual Statement are reserved for investment (or invested) assets, such as bonds and stocks. See the exhibit "Principal Assets on an Insurer Annual Statement Balance Sheet."

Principal Assets on an Insurer Annual Statement Balance Sheet

Assets	Current Year		
	Assets	Nonadmitted Assets	Net Admitted Assets
Bonds (Schedule D)	33,525,000		33,525,000
Preferred stocks (Schedule D)	265,000		265,000
Common stocks (Schedule D)	3,750,000	50,000	3,700,000
Real estate (Schedule A)	1,900,000		1,900,000
Cash (Schedule E) and short-term investments (Schedule DA)	5,250,000		5,250,000
Other invested assets (Schedule BA)	310,000	190,000	120,000
Subtotal cash and invested assets	**45,000,000**	**240,000**	**44,760,000**
Uncollected premiums	4,200,000	150,000	4,050,000
Amounts recoverable from reinsurers	1,750,000	25,000	1,725,000
Funds held by or deposited with reinsured companies	750,000		750,000
Furniture and equipment	415,000	415,000	0
Other assets	2,050,000		2,050,000
Totals	**54,165,000**	**830,000**	**53,335,000**

Note: The above illustration does not include all information contained in the NAIC Annual Statement blank.

Adapted from the NAIC Annual Statement blank. [DA09295]

The assets side of the balance sheet provides only summary information about the insurer's invested assets, but it does give some indication of the insurer's investment risk. An insurer that maintains a low-risk investment portfolio (for example, bonds rather than stocks) may be able to assume relatively higher risk in its underwriting operations and vice versa. An insurer with a high-risk investment portfolio may need additional reinsurance protection to guard against simultaneous losses in its investment and underwriting operations.

The investment portfolio is subject to a variety of risks, including these:

- Potential variation in the market price of investments
- Possible default by the issuers of investment securities
- Lack of **liquidity**

Liquidity
The ease with which an asset can be converted to cash with little or no loss of value.

Insurers sometimes must liquidate investments to pay claims, especially for catastrophe losses.

Bonds

Bonds are typically the largest single invested asset category for a property-casualty insurer. Many insurers, especially small ones, invest a high proportion of their assets in bonds because they are considered the safest long-term investment available.Although a bond's market price can vary widely over time as interest rates change, insurers include bonds at their **amortized value** on their Annual Statement balance sheet. This makes the Annual Statement value of a bond immune from current market prices, which rise and fall with interest rate changes. Consequently, an insurer's policyholders' surplus is not severely affected by a decline in the market price of its bonds unless the bonds must be sold.

Amortized value
A value that reflects the payment of principal and interest over time.

The assets side of the balance sheet does not indicate the quality of an insurer's bond portfolio, the bonds' market value, or their maturity dates. However, detailed information on each bond the insurer holds is shown in Schedule D—Part 1.The information includes the interest rate, maturity date, book value (usually amortized value), par value, fair value (market value), and accrued interest. Part 1A of Schedule D shows the quality ratings and maturities of all bonds in summary form. Other parts of Schedule D show bonds acquired or disposed of during the year.

Bonds with long maturities generally are of higher risk. The market prices of bonds vary inversely with market interest rates, rising when interest rates fall and falling when interest rates rise. This effect is more severe for long-maturity bonds than for short-maturity bonds because a long-maturity bond's interest rate is locked in for a longer time period. If market interest rates rise shortly after a long-maturity bond is issued, the holder is locked into the lower interest rate for a longer time period than the holder of a short-maturity bond, and therefore the market value of the former declines.

Common Stocks

Common stocks typically are the second-largest invested asset category for property-casualty insurers. However, many insurers, especially small ones, do not hold large amounts of common stocks. Common stocks are usually shown on the Annual Statement balance sheet at their market value on the last business day of the year. Fluctuations in stock prices can cause substantial variations in the insurer's policyholders' surplus. Details for common stocks are shown in Schedule D—Part 2—Section 2 of the Annual Statement.

Many insurers invest substantial amounts in the stocks of their subsidiaries and affiliated companies. Usually, no established market exists for these securities, so substantial holdings of the stocks of subsidiaries and affiliates have a significant liquidity risk. The risk is increased if the insurer also has significant reinsurance arrangements with the subsidiaries and affiliates. The value of investments in subsidiaries is usually the value of the subsidiary's policyholders' surplus.

Schedule D—Summary by Country, shown at the beginning of Schedule D in the Annual Statement, shows the total investment in bonds, preferred stock, and common stock of the insurer's parent, subsidiaries, and affiliates. Additional details for stocks of parent, subsidiaries, and affiliates are shown in Schedule D—Part 6.

Short-Term Investments

The third-largest category of invested assets for property-casualty insurers typically is cash, cash equivalents, and short-term investments. This category is a catchall because it includes certain bonds, bills, notes, commercial paper, certificates of deposit, and shares in money market funds.All short-term investments have a maturity period of one year or less. They are usually matched with liabilities that the insurer must pay within a year, such as loss reserves for short-tail types of insurance.

Reinsurance-Related Assets

In many cases, only three asset items on an insurer's Annual Statement balance sheet deal directly with reinsurance. These are "Amounts recoverable from reinsurers," "Funds held by or deposited with reinsured companies," and "Other amounts receivable under reinsurance contracts."

The "Amounts recoverable from reinsurers" entry on the assets side of the balance sheet is used by primary insurers to show the total amounts recoverable from all reinsurers. Recoverables by individual reinsurers are listed in the primary insurer's Schedule F—Part 3 of the Annual Statement.

For regulatory purposes, an unauthorized reinsurer may deposit assets equal to the unearned premiums and losses payable (including loss reserves) under its reinsurance agreements with primary insurers. The "Funds held by or deposited with reinsured companies" entry on the assets side of the balance sheet is used by a reinsurer and represents those funds deposited with a primary insurer. These amounts are an asset of the reinsurer.

The "Other amounts receivable under reinsurance contracts" entry on the assets side of the balance sheet is used for amounts recoverable under reinsurance contracts that do not fit into the "Amounts recoverable from reinsurers" entry.

Other Annual Statement assets that may involve reinsurance transactions include these two entries, which are typically small amounts for most insurers and reinsurers:

- "Uncollected premiums and agents' balances in the course of collection"—includes a reinsurer's uncollected premiums from primary insurers
- "Receivables from parent, subsidiaries and affiliates"—includes some reinsurance elements if a reinsurance relationship exists among the parent, the subsidiary, and affiliates, especially if a parent purchased reinsurance centrally for the benefit of all subsidiaries and affiliates

Liabilities, Surplus, and Other Funds

The liabilities side of the balance sheet summarizes the insurer's liabilities, policyholders' surplus, and other funds. See the exhibit "Principal Liabilities on an Insurer Annual Statement Balance Sheet."

Principal Liabilities on an Insurer Annual Statement Balance Sheet

Liabilities, Surplus, and Other Funds	Current Year
Losses	22,165,000
Reinsurance payable (Schedule F)	2,510,000
Loss adjustment expenses	2,250,000
Commissions payable	1,800,000
Unearned premiums	8,400,000
Ceded reinsurance premiums payable	2,005,000
Funds held by company under reinsurance treaties (Schedule F)	1,955,000
Provision for reinsurance (Schedule F)	1,200,000
Total liabilities	**42,285,000**
Common capital stock	2,000,000
Gross paid in and contributed surplus	5,250,000
Unassigned funds (surplus)	8,510,000
Treasury stock	-1,500,000
Surplus as regards policyholders	**14,260,000**
Totals	**56,545,000**

Note: The above illustration does not include all information contained in the NAIC Annual Statement blank.

Adapted from the NAIC Annual Statement blank. [DA09296]

The principal liabilities of insurers are loss reserves, loss adjustment expense reserves, and the unearned premium reserve. Reserves for losses and loss adjustment expenses (LAE) usually constitute the largest liability of a property-casualty insurer. The unearned premium reserve is usually the second-largest liability, but it may be the largest liability of an insurer that sells only property insurance.

Losses and Loss Adjustment Expense Reserves

The "Losses" entry on the liabilities side of the balance sheet represents the insurer's liability to make payments for losses that have already occurred but have not yet been settled. This liability is usually called the loss reserve. The "Reinsurance payable on paid loss and loss adjustment expenses" entry shows the amount a reinsurer is obligated to pay under reinsurance it has assumed for losses that have already been paid by the primary insurers. The "Loss adjustment expenses" entry shows an insurer's obligation to pay LAE-related losses that have already occurred. This liability is usually called the loss adjustment expense reserve. Together, these three entries constitute the insurer's loss and LAE reserves.

The total reserve for losses is supported by detailed loss information (by type of insurance) shown on the Underwriting and Investment Exhibit, Part 2A, Column 8. Additional details of loss reserves are shown in Schedule P of the Annual Statement. The total reserve for unpaid LAE also appears on Part 2A, Column 9 of the Underwriting and Investment Exhibit. Additional details about LAE, by type of insurance, can be found in Schedule P—Part 1 of the Annual Statement.

Unearned Premium Reserves

The "Unearned premiums" entry on the liabilities side of the balance sheet represents the amount of premiums received from policyholders that are not yet earned. This total is supported by Part 1A of the Underwriting and Expense Exhibit, which shows unearned premium by type of insurance. Calculating the unearned premium reserve is a straightforward procedure. However, the unearned premiums are based on the premiums charged by the insurer. If those premiums are inadequate to pay losses and expenses, then the unearned premium reserve will be inadequate to pay future losses and expenses.

The other liabilities shown on the Annual Statement balance sheet of a property-casualty insurer do not differ significantly from those shown on the balance sheet of any other business.

Reinsurance-Related Liabilities

These are the items on the liabilities side of an insurer's Annual Statement balance sheet that deal directly with reinsurance:

- "Reinsurance payable on paid loss and loss adjustment expenses"—Represents the amount that the reinsurer filing the statement must pay under assumed reinsurance for losses already paid by primary insurers. The amount indicated is taken from Schedule F—Part 1, Column 6 of the Annual Statement. This liability is the counterpart of the "Amounts recoverable from reinsurers" entry that a primary insurer would show on the assets side of its balance sheet.
- "Ceded reinsurance premiums payable"—Indicates premiums owed by the primary insurer filing the statement to its reinsurer. It is the counterpart of the "Uncollected premiums and agents' balances in course of collection" entry on the assets side of the balance sheet.
- "Funds held by company under reinsurance treaties"—Represents funds from reinsurers that the primary insurer filing the statement holds under reinsurance treaties. These funds are usually held so that the primary insurer filing the statement can take credit on its Annual Statement for reinsurance purchased from unauthorized reinsurers just as it can when dealing with authorized reinsurers.Only the total funds are reported, but details can be found in Schedule F—Part 3. This is the counterpart of the "Funds held by or deposited with reinsured companies" entry on the assets side of the balance sheet.
- "Provision for reinsurance"—Represents the total provision for overdue reinsurance and for any collateral deficiency requirements for unauthorized and certified reinsurers. The amount indicated is taken from Schedule F—Part 8.

The exhibit summarizes the reinsurance-related assets and liabilities found on the Annual Statement. Where one entry is the counterpart of another entry, those entries are placed side by side. See the exhibit "Reinsurance-Related Assets and Liabilities."

Surplus

Treasury stock
A corporate stock issued as fully paid to a stockholder and subsequently reacquired by the corporation to use for business purposes.

Surplus can be classified into three major parts: contributed surplus, unassigned surplus, and **treasury stock**. Contributed surplus is money that outside parties have invested in the organization. Unassigned surplus is the undistributed or unappropriated surplus amounts.

The entries for an insurer's policyholders' surplus are similar to those shown in that section of the balance sheet for noninsurance businesses. The major difference is the inclusion of the "Surplus as regards policyholders" entry, which is not used in most noninsurance businesses.

Reinsurance-Related Assets and Liabilities

Primary Insurer	Reinsurer
Assets	**Liabilities**
Amounts recoverable from reinsurers	Reinsurance payable on paid loss and loss adjustment expenses
Receivables from parent, subsidiaries, and affiliates*	
Other amounts receivable under reinsurance contracts	
Liabilities	**Assets**
Funds held by company under reinsurance treaties	Funds held by or deposited with reinsured companies
Ceded reinsurance premiums payable	Uncollected premiums and agents' balances in course of collection
Provision for reinsurance	

*Used by a primary insurer if it has reinsurance arrangements with its parent, subsidiaries, or affiliates.

[DA09297]

UNDERWRITING AND INVESTMENT EXHIBIT

Insurers prepare several different schedules and exhibits to provide details on the assets and liabilities reported on the balance sheet and income statement of their National Association of Insurance Commissioners (NAIC) Annual Statement. These schedules and exhibits can provide a substantial amount of information about an insurer's financial condition and reinsurance operations.

The Statement of Income included in the NAIC Annual Statement measures an insurer's earnings over the course of a year and serves as the basis for determining the insurer's federal income tax liability. The summary values reported in the Statement of Income are supported by various exhibits that provide detail on the source of the underwriting, investment, and other income for the year.

The Underwriting and Investment Exhibit is one of the supporting documents in the Statement of Income's Underwriting Income section, the elements of which are affected by reinsurance transactions.

Statement of Income

The Statement of Income is similar in structure to income statements used by noninsurance businesses, although much of the terminology is specific to the insurance business. The Statement of Income includes premiums earned, losses and expenses incurred, and the resulting net underwriting gain or loss. A reinsurer is interested in a primary insurer's income statement because it is one indicator of the primary insurer's financial strength.

The Statement of Income shows profit or loss for only the current year and the prior year. However, the Five-Year Historical Data Exhibit (which appears later in the Annual Statement) shows income for the current and previous four years. See the exhibit "Principal Elements of a Statement of Income."

Principal Elements of a Statement of Income

		Current Year
	Underwriting Income	
	Premiums earned	8,500,000
–	Losses incurred	5,600,000
–	Loss adjustment expenses incurred	1,500,000
–	Other underwriting expenses incurred	2,200,000
	Net underwriting gain (loss)	(800,000)
	Investment Income	
	Net investment income earned	850,000
+	Net realized capital gains (losses)	45,000
	Net investment gain (loss)	**895,000**
	Other Income	
+	Other income (expense)	200,000
–	Policyholder dividends	50,000
	Net income before income taxes	**245,000**
–	Federal and foreign income taxes	(55,000)
	Net income	**300,000**

Note: The above illustration does not include all information contained in the NAIC Annual Statement blank.

Adapted from the NAIC Annual Statement blank. [DA09289]

Underwriting and Investment Exhibit

The Underwriting and Investment Exhibit provides supporting information for the Underwriting Income section of the Statement of Income. It consists of three parts that summarize the Annual Statement schedules that relate to the Statement of Income. The Underwriting and Investment Exhibit also develops information that appears on the balance sheet.

Part 1—Premiums Earned

Part 1 of the Underwriting and Investment Exhibit shows premiums earned by type of insurance. It also shows the components of premiums earned.

The premiums earned figure is calculated by adding net premiums written in the current year and unearned premiums as of December 31 of the prior year, and then subtracting unearned premiums of the current year. The "Premiums Earned" entry on the Statement of Income is the total in Part 1, Column 4. See the exhibit "Underwriting and Investment Exhibit: Part 1—Premiums Earned Illustration."

Underwriting and Investment Exhibit: Part 1—Premiums Earned Illustration

Line of Business	1 Net Premiums Written per Column 6, Part 1B	2 Unearned Premiums December 31 Prior Year–per Col. 3, Last Year's Part 1	3 Unearned Premiums December 31 Current Year–per Col. 5, Part 1A	4 Premiums Earned During Year (Col. 1+2-3)
Fire	195,000	80,575	95,000	180,575
Allied lines	93,600	38,000	48,500	83,100
Homeowners multiple peril	1,150,000	585,000	640,000	1,095,000
Commercial multiple peril	245,000	120,000	125,000	240,000
Inland marine	350,000	26,950	37,750	339,200
Workers compensation	2,000,000	25,000	64,500	1,960,500
Private passenger auto liability	2,005,225	950,000	1,020,000	1,935,225
Commercial auto liability	300,000	115,000	140,000	275,000
Auto physical damage	815,000	650,000	700,000	765,000
Reinsurance—nonproportional assumed property	150,000	15,250	17,325	147,925
Reinsurance—nonproportional assumed liability	55,000	12,500	5,800	61,700
All other lines of business	1,091,175	881,725	556,125	1,416,775
Totals	**8,450,000**	**3,500,000**	**3,450,000**	**8,500,000**

Note: The above illustration does not include all information contained in the NAIC Annual Statement blank.

Adapted from the NAIC Annual Statement blank. [DA09290]

Part 1B—Premiums Written

Part 1B of the Underwriting and Investment Exhibit shows premiums written by type of insurance. It also shows the components of net premiums written. The net premiums written figure is calculated by adding direct business and reinsurance assumed (from affiliates and nonaffiliates) and subtracting reinsurance ceded (to affiliates and nonaffiliates). See the exhibit "Underwriting and Investment Exhibit: Part 1B—Premiums Written Illustration."

Underwriting and Investment Exhibit: Part 1B—Premiums Written Illustration

		Reinsurance Assumed		Reinsurance Ceded		
	1	2	3	4	5	6
Line of Business	Direct Business	From Affiliates	From Non-Affiliates	To Affiliates	To Non-Affiliates	Net Premiums Written (Cols. 1+2+3-4-5)
Fire	26,965	303,820	10,825	68,750	77,860	195,000
Allied lines	18,130	163,500	10,275	36,095	62,210	93,600
Homeowners multiple peril	26,000	2,390,500	1,500	408,000	860,000	1,150,000
Commercial multiple peril	114,500	299,000	51,000	114,500	105,000	245,000
Inland marine	2,115,000	55,000	13,000	128,000	1,705,000	350,000
Workers compensation	190,750	3,020,000	89,250	875,000	425,000	2,000,000
Private passenger auto liability	440,000	2,383,000	17,375	710,150	125,000	2,005,225
Commercial auto liability	66,500	379,500	10,500	108,000	48,500	300,000
Auto physical damage	295,000	1,660,755	2,895	1,080,000	63,650	815,000
Reinsurance—nonproportional assumed property	XXX	119,000	81,000	50,000	0	150,000
Reinsurance—nonproportional assumed liability	XXX	1,000	73,300	19,300	0	55,000
All other lines of business	1,383,655	1,084,010	69,450	869,315	576,625	1,091,175
Totals	**4,676,500**	**11,859,085**	**430,370**	**4,467,110**	**4,048,845**	**8,450,000**

Note: The above illustration does not include all information contained in the NAIC Annual Statement blank.

Adapted from the NAIC Annual Statement blank. [DA09291]

Reinsurers can use Part 1B to evaluate a primary insurer's mix of business. This view of a primary insurer's policy portfolio is often examined in conjunction with Schedule T—Exhibit of Premiums Written, which shows written premium allocated by state (or territory). Reinsurers can use Schedule T to determine the geographic distribution of the primary insurer's policy portfolio.

The Underwriting and Investment Exhibit and Schedule T together provide a comprehensive overview of a primary insurer's operations.

Parts 1 and 1B of the Underwriting and Investment Exhibit list all the types of insurance an insurer could sell, including entries for excess of loss reinsurance. Pro rata reinsurance, whether assumed or ceded, is shown by the type of insurance to which it ~~pertains. For example~~, an insurer's quota share reinsurance transactions (ceded and assumed) for fire business would be shown in the "Reinsurance Assumed" and "Reinsurance Ceded" columns on the "Fire" line of business line. ~~Nonproportional~~ assumed reinsurance transactions are categorized as property, liability, and financial.

Part 1B of the Underwriting and Investment Exhibit becomes even more useful when analyzed in conjunction with Part 2, which shows loss experience by type of insurance.

Part 2—Losses Paid and Incurred

Part 2 of the Underwriting and Investment Exhibit shows losses by type of insurance. Losses paid and incurred are categorized as either direct business, reinsurance assumed, or reinsurance recovered. These categories do not distinguish between reinsurance transactions with affiliates and those with other reinsurers. ~~Part 2 uses premium earned data from Part 1 to calculate the loss~~ ratio for each type of insurance.

Part 2A—Unpaid Losses and Loss Adjustment Expenses

Part 2A of the Underwriting and Investment Exhibit shows total estimated losses and loss adjustment expenses (LAE) by type of insurance. The supporting details for these totals appear in Schedule P. See the exhibit "Underwriting and Investment Exhibit: Part 2A—Unpaid Losses and Loss Adjustment Expenses Illustration."

Part 2A shows unpaid net losses, excluding the incurred but not reported (IBNR) losses in Column 4 but including IBNR in Column 8. The loss data from Parts 2 and 2A, when combined with the premium data from Part 1B, can roughly indicate an insurer's profitability from reinsurance operations. Unfortunately, the data on incurred losses for reinsurance transactions with affiliates cannot be separated from those with nonaffiliates.

Column 8 of Part 2A shows net unpaid losses by type of insurance and in total. The total figure from Column 8 is carried over to the liabilities section of the balance sheet. Column 9 of Part 2A shows the reserve for unpaid LAE by type of insurance and in total. This total is also carried over to the liabilities section of the balance sheet.

Part 3—Expenses

Part 3 of the Underwriting and Investment Exhibit provides supporting documentation primarily for the Statement of Income. It allocates expenses by

Underwriting and Investment Exhibit: Part 2A—Unpaid Losses and Loss Adjustment Expenses Illustration

Line of Business	Reported Losses				Incurred But Not Reported				
	1	2	3	4	5	6	7	8	9
	Direct	Reinsurance Assumed	Deduct Reinsurance Recoverable From Authorized and Unauthorized Companies	Net Losses Excl. Incurred But Not Reported (Cols. 1+2-3)	Direct	Reinsurance Assumed	Reinsurance Ceded	Net Losses Unpaid (Cols. 4+5+6-7)	Net Unpaid Loss Adjustment Expenses
Fire	850	116,250	36,500	80,600	5,600	45,000	20,000	111,200	9,500
Allied lines	9,100	54,950	42,070	21,980	15,250	17,100	12,250	42,080	4,000
Homeowners multiple peril	4,750	290,000	140,000	154,750	2,250	285,000	134,000	308,000	87,900
Commercial multiple peril	90,950	215,000	127,500	178,450	12,200	127,500	60,500	257,650	86,100
Inland marine	48,500	17,500	47,300	18,700	170,500	9,225	155,450	42,975	7,250
Workers compensation	1,118,000	5,910,000	2,945,450	4,082,550	830,000	5,527,000	3,010,000	7,429,550	1,050,000
Private passenger auto liability	150,000	1,260,000	550,000	860,000	78,500	770,450	245,000	1,463,950	335,000
Commercial auto liability	60,000	315,000	130,000	245,000	66,500	250,000	141,000	420,500	66,350
Auto physical damage	1,500	575	650	1,425	4,000	7,550	3,500	9,475	42,700
Reinsurance—nonproportional assumed property	XXX	83,000	21,700	61,300	XXX	78,300	20,550	119,050	2,000
Reinsurance—nonproportional assumed liability	XXX	120,000	30,550	89,450	XXX	310,000	81,000	318,450	20,950
All other lines of business	713,850	852,725	715,280	851,295	1,503,550	1,828,725	1,604,250	2,579,320	538,250
Totals	2,197,500	9,235,000	4,787,000	6,645,500	2,688,350	9,255,850	5,487,500	13,102,200	2,250,000

Note: The above illustration does not include all information contained in the NAIC Annual Statement blank.

Adapted from the NAIC Annual Statement blank. [DA09292]

three major functional areas (loss adjustment, other underwriting, and investment) and by numerous expense groupings, such as claim adjustment services, commission and brokerage, advertising, salaries, and others, but there is no analysis of expenses by line of insurance. See the exhibit "Underwriting and Investment Exhibit: Part 3—Expenses Illustration."

The net LAE from claim adjustment services and the net other underwriting expenses from commission and brokerage are calculated by adding the expenses from direct business and reinsurance assumed and subtracting the expenses from reinsurance ceded.

Underwriting and Investment Exhibit: Part 3—Expenses Illustration

	1 Loss Adjustment Expenses	2 Other Underwriting Expenses	3 Investment Expenses	4 Total
Claim adjustment services:				
Direct	515,000	0	0	515,000
Reinsurance assumed	900,000	0	0	900,000
Reinsurance ceded	505,000	0	0	505,000
Net claim adjustment services (1.1+1.2-1.3)	910,000	0	0	910,000
Commission and brokerage:				
Direct, excluding contingent	0	250,000	0	250,000
Reinsurance assumed, excluding contingent	0	600,000	0	600,000
Reinsurance ceded, excluding contingent	0	450,000	0	450,000
Contingent—direct	0	7,500	0	7,500
Contingent—reinsurance assumed	0	105,000	0	105,000
Contingent—reinsurance ceded	0	35,000	0	35,000
Net commission and brokerage (2.1+2.2-2.3+2.4+2.5-2.6)	0	477,500	0	477,500
Salary and related items:				
Salaries	385,000	904,425	44,190	1,333,615
Payroll taxes	23,150	80,000	1,485	104,635
Employee relations and welfare	81,700	280,000	6,000	367,700
Rent and rent items	27,000	93,700	1,815	122,515
Equipment	10,650	54,450	985	66,085
All other expenses	62,500	309,925	50,525	422,950
Totals	1,500,000	2,200,000	105,000	3,805,000

Note: The above illustration does not include all information contained in the NAIC Annual Statement blank.

Adapted from the NAIC Annual Statement blank. [DA09293]

SCHEDULE F

Schedule F of the National Association of Insurance Commissioners (NAIC) Annual Statement contains information pertinent to the insurer's reinsurance activities. It shows specific information about ceded and assumed reinsurance, as well as portfolio transfers. It also includes a restated balance sheet, which shows the insurer's assets and liabilities on a gross basis before the effects of reinsurance transactions are netted out.

Schedule F consists of nine parts:

- Part 1—Assumed Reinsurance
- Part 2—Premium Portfolio Reinsurance
- Part 3—Ceded Reinsurance
- Part 4—Aging of Ceded Reinsurance
- Part 5—Provision for Unauthorized Reinsurance
- Part 6—Provision for Reinsurance Ceded to Certified Reinsurers (Section 1) and Provisions for Overdue Reinsurance Ceded to Certified Reinsurers (Section 2)
- Part 7—Provision for Overdue Authorized Reinsurance
- Part 8—Provision for Overdue Reinsurance (authorized over 20 percent)
- Part 9—Restatement of Balance Sheet to Identify Net Credit for Ceded Reinsurance

Parts 1 through 3 provide the supporting data for the insurer's assumed and ceded reinsurance accounting entries. Parts 3 through 7 provide data for the provision for reinsurance appearing in Part 8. Part 9 restates the statutory balance sheet from a net to a gross basis.

One significant purpose of Schedule F is to calculate the provision for reinsurance located on the liabilities side of the primary insurer's balance sheet. When an insurer posts a liability to the balance sheet without a corresponding increase in assets, its policyholders' surplus is reduced. Therefore, an insurer will want to minimize this provision for reinsurance.

Schedule F—Part 1

Schedule F—Part 1 shows the reinsurance assumed by the reinsurer. It includes paid and reserved loss and loss adjustment expense (LAE) amounts as well as funds deposited with, and letters of credit posted on behalf of, the primary insurer.

Schedule F—Part 1 is shown in the exhibit. As an example, two primary insurers are listed: ABC Insurance and XYZ Insurance. The total reinsurance on paid losses and LAE ($15,010,000) in Column 6 is an amount payable that appears on the liabilities side of the reinsurer's balance sheet. See the exhibit "Schedule F—Part 1."

Another significant item in Schedule F—Part 1 is in Column 12, "Funds Held By or Deposited With Reinsured Companies." This is the amount the reinsurer deposits with the primary insurer, and the total amount is posted on the assets side of the reinsurer's balance sheet. For the reinsurer filing the sample schedule in the "*Schedule F—Part 1*" exhibit, the total amount deposited with ABC Insurance and XYZ Insurance is $21,328,000.

Schedule F—Part 1

Assumed Reinsurance as of December 31, Current Year (000 Omitted)

1	2	3	4	5	Reinsurance On			9	10	11	12	13	14	15
					6	7	8							
Federal ID Number	NAIC Company Code	Name of Reinsured	Domiciliary Jurisdiction	Assumed Premium	Paid Losses and Loss Adjustment Expenses	Known Case Losses and LAE	Cols. 6 + 7	Contingent Commissions Payable	Assumed Premiums Receivable	Unearned Premium	Funds Held By or Deposited With Reinsured Companies	Letters of Credit Posted	Amount of Assets Pledged or Compensating Balances to Secure Letters of Credit	Amount of Assets Pledged or Collateral Held in Trust
		ABC Insurance			10,010	14,000	24,010				14,658	0	0	
		XYZ Insurance			5,000	6,000	11,000				6,670	0	0	
9999999		**Totals**			**15,010**	**20,000**	**35,010**	**0**	**0**	**0**	**21,328**	**0**	**0**	

Schedule F—Part 2

Schedule F—Part 2 shows all of the insurer's ceded and assumed portfolio reinsurance transactions during the current year. Portfolio reinsurance transactions involve blocks of business already written by insurers. A portfolio reinsurance transaction can involve either known losses (loss portfolio transfers) or known and unknown losses.

Loss portfolio transfers are usually extraordinary events, and this schedule highlights those transactions for additional scrutiny. Schedule F—Part 2 shows the name of the portfolio reinsurer, the date of the reinsurance contract (agreement), the amount of the original (underlying) premium, and the amount of the reinsurance premium.

Schedule F—Part 3

Schedule F—Part 3 provides details about reinsurance ceded by the insurer. Authorized, unauthorized, and certified reinsurers should be listed. Amounts are shown for reinsurance recoverables on paid losses and paid LAE; known case loss and LAE reserves; incurred but not reported (IBNR) reserves and LAE reserves; unearned premiums; and contingent commissions, sometimes called "profit commissions." Column 19, "Funds Held by Company Under Reinsurance Treaties," shows the amounts that reinsurers deposited with the primary insurer. The total amount is posted on the liabilities side of the primary insurer's balance sheet.

The example shows three reinsurers: Alpha Re, Beta Re, and Gamma Re. The figures shown are carried through subsequent exhibits to illustrate how a provision for reinsurance is calculated. Columns 7 and 8 show that the paid losses and paid LAE recoverables total $21,606,000 ($20,400,000 + $1,206,000). The amounts in Columns 9, 10, 11, and 12 which total $45,400,000 ($9,900,000 + 0 + $35,500,000 + 0) are those that are yet to be recovered from the reinsurers on outstanding loss reserves. Columns 16 and 17 show the ceded balances payable to reinsurers, which are subtracted from the total recoverables to determine the net amount recoverable from reinsurers in Column 18. Column 19 shows the amount held by the primary insurer under its reinsurance treaties; in this exhibit, $12,767,000 is held under the treaty with Gamma Re. See the exhibit "Schedule F—Part 3."

Schedule F—Part 4

Schedule F—Part 4 illustrates the aging of ceded reinsurance recoverables on paid losses and paid LAE. The amount recoverable is divided between the amount that is current (Column 5) and the amount overdue by a certain number of days (Columns 6 through 10). For example, for Beta Re, $1 million is overdue for more than 120 days. The percentage overdue is calculated in Column 12 by dividing the total overdue (Column 10) by the total due (Column 11). The longer that reinsurance recoverables remain uncollected,

Schedule F—Part 3

Ceded Reinsurance as of December 31, Current Year (000 Omitted)																		
						Reinsurance Recoverable On									Reinsurance Payable			
1	2	3	4	5	6	7	8	9	10	11	12	13	14	15	16	17	18	19
Federal ID Number	NAIC Company Code	Name of Reinsurer	Domiciliary Jurisdiction	Reinsurance Contracts Ceding 75% or More of Direct Premiums Written	Reinsurance Premiums Ceded	Paid Losses	Paid LAE	Known Case Loss Reserves	Known Case LAE Reserves	IBNR Loss Reserves	IBNR LAE Reserves	Unearned Premiums	Contingent Commissions	Cols. 7 through 14 Totals	Ceded Balances Payable	Other Amounts Due to Reinsurers	Net Amount Recoverable From Reinsurers Cols. 15 – [16 + 17]	Funds Held by Company Under Reinsurance Treaties
Authorized Reinsurers																		
		Alpha Re			2,430	6,000	700,	4,000	0	8,200	0			18,900	2,100	0	16,800	0
		Beta Re				5,100	365	3,800	0	6,100	0			15,365	0	0	15,365	0
Certified Affiliates – U.S. Intercompany Pooling																		
		Gamma RE				9,300	141	2,100	0	21,200	0			32,741	0	0	32,741	12,767
2799999		Total Certified				9,300	141	2,100	0	21,200	0	0	0	32,741	0	0	32,741	12,767
2899999		Total Authorized, Unauthorized, and Certified			2,430	20,400	1,206	9,900	0	35,500	0	0	0	67,006	2,100	0	64,906	12,767
9999999		Totals			2,430	20,400	1,206	9,900	0	35,500	0	0	0	67,006	2,100	0	64,906	12,767

NOTE: A. Report the five largest provisional commission rates included in the cedant's reinsurance treaties. The commission rate to be reported is by contract with ceded premium in excess of $50,000:

	1 Name of Reinsurer	2 Commission Rate	3 Ceded Premium
1)	....	....	....
2)	....	....	....
3)	....	....	....
4)	....	....	....
5)	....	....	....

B. Report the five largest reinsurance recoverables reported in Column 15, due from any one reinsurer (based on the total recoverables, Line 9999999, Column 15, the amount of ceded premium, and indicate whether the recoverables are due from an affiliated insurer.

	1 Name of Reinsurer	2 Total Recoverables	3 Ceded Premiums	4 Affiliated
1)	....	....	....	Yes [ ] No [ ]
2)	....	....	....	Yes [ ] No [ ]
3)	....	....	....	Yes [ ] No [ ]
4)	....	....	....	Yes [ ] No [ ]
5)	....	....	....	Yes [ ] No [ ]

the more likely it is that the insurer will not be able to collect them. See the exhibit "Schedule F—Part 4."

Schedule F—Part 5

Schedule F—Part 5 calculates the provision for unauthorized reinsurance, which is part of the overall provision for reinsurance that a primary insurer reports on the liabilities side of the balance sheet.

The effect of the provision for reinsurance is to reduce policyholders' surplus. Therefore, the requirement to include unauthorized reinsurance amounts may act as a disincentive for primary insurers to do business with an unauthorized reinsurer.

If the reinsurer provides the primary insurer with collateral in respect of reinsurance recoverables, then the amount of the provision for unauthorized reinsurance may be reduced. The amounts of collateral are listed on Schedule F—Part 5 and include funds that a reinsurer deposits with the primary insurer and letters of credit furnished by a reinsurer to the primary insurer. However, even if all the recoverables are fully secured, a provision for unauthorized reinsurance would still have to be made if any amounts are either more than ninety days past due or are in dispute. In practice, a primary insurer may redeem some or all of the collateral so that no losses are overdue by more than ninety days.

Schedule F—Part 6

Schedule F—Part 6 was added as a result of reforms the NAIC adopted to reduce reinsurance collateral requirements for reinsurers that meet certain criteria for financial strength and business practices and that are domiciled in qualified jurisdictions. The reform provides a process for states to certify and rate reinsurers. Certified reinsurers are required to post collateral ranging from 0 to 100 percent based on their rating.[1] Primary insurers can receive credit for reinsurance placed with certified reinsurers.

Schedule F—Part 6—Section 1 calculates the provision for reinsurance for certified reinsurers due to collateral deficiencies, which then becomes part of the overall provision for reinsurance that a primary insurer reports on the liabilities side of the balance sheet.

The amount of collateral required for full credit is based on the certified reinsurer's assigned rating (1 through 6). The amount of credit allowed for net recoverables (Column 22) is based on the amount of recoverables subject to collateral requirements for full credit (Column 10) multiplied by the percent credit allowed on recoverables subject to collateral requirements (Column 21). This percentage is calculated by dividing the percent of collateral provided for recoverables subject to collateral requirements (Column 20) by the percent collateral required for full credit (Column 7), not to exceed 100 percent. The total provision for reinsurance with certified reinsurers due to

Schedule F—Part 4

Aging of Ceded Reinsurance as of December 31, Current Year (000 OMITTED)

1	2	3	4	Reinsurance Recoverable on Paid Losses and Paid Loss Adjustment Expenses							12	13
				5	Overdue					11		
					6	7	8	9	10			
Federal ID Number	NAIC Company Code	Name of Reinsurer	Domiciliary Jurisdiction	Current	1 to 29 Days	30 - 90 Days	91 - 120 Days	Over 120 Days	Total Overdue Cols. 6 + 7 + 8 + 9	Total Due Cols. 5 + 10	Percentage Overdue Col. 10/ Col. 11	Percentage More Than 120 Days Overdue Col. 9/ Col.11
Authorized Reinsurers												
		Alpha Re		4,300	1,400	1,000	0	0	2,400	6,700	36%	0%
		Beta Re		1,800	900	965	800	1,000	3,665	5,465	67%	18%
Certified Affiliates – U.S. Intercompany Pooling												
		Gamma RE		2,000	2,400	2,641	900	1,500	7,441	9,441	79%	16%
2799999		Total Certified		2,000	2,400	2,641	900	1,500	7,441	9,441		
2899999		Total Authorized, Unauthorized, and Certified		8,100	4,700	4,606	1,700	2,500	13,506	21,606		
9999999		Totals		8,100	4,700	4,606	1,700	2,500	13,506	21,606		

collateral deficiency (Column 23) is the difference between the amount of recoverables from reinsurers (Column 8) and the amount of credit allowed for recoverables (Column 22).

The exhibit, for example, shows that Gamma Re, with a certified reinsurer rating of 3, posted a sufficient amount of collateral to receive full credit for its reinsurance recoverables. See the exhibit "Schedule F—Part 6—Section 1."

However, even if all the recoverables are fully secured, a provision for overdue reinsurance would still have to be made if any amounts are either more than ninety days past due or are in dispute.

Schedule F—Part 6—Section 2 establishes the provision for overdue reinsurance ceded to certified reinsurers. It also determines whether a certified reinsurer can be categorized as "slow-paying" by reference to a particular percentage. This percentage is calculated by dividing the reinsurance recoverables on paid losses and paid LAE more than ninety days overdue (Column 5) by the sum of reinsurance recoverables on paid losses and paid LAE (Column 6) and the amounts received in the prior ninety days (Column 7).

If the percentage in Column 8 is less than 20 percent, a penalty for overdue reinsurance is calculated. The penalty is 20 percent of reinsurance recoverables overdue by more than ninety days (Column 9) plus 20 percent of any amounts in dispute (Column 10), limited to the total amount of credit allowed for net recoverables (Column 11).

If this percentage is 20 percent or more, the certified reinsurer is categorized as slow-paying. The penalty is the greater of 20 percent of the recoverable amounts ninety days overdue plus 20 percent of any amounts in dispute, or 20 percent of net unsecured recoverables for which credit is allowed (Column 14), limited to the total amount of credit allowed for net recoverables (Column 11).

In the "Schedule F—Part 6—Section 2" exhibit, the percentage in Column 8 for Gamma Re is 23 percent, which exceeds the 20 percent benchmark. Therefore, Gamma Re is categorized as a slow-paying reinsurer. The example shows the calculation of Gamma Re's provision for overdue reinsurance ceded to certified reinsurers (Column 15), which is $2,326,000. This amount becomes part of the overall provision for reinsurance that a primary insurer reports on the liabilities side of the balance sheet. See the exhibit "Schedule F—Part 6—Section 2."

Schedule F—Part 7

Schedule F—Part 7 establishes the amounts overdue from each authorized reinsurer. It also determines whether a reinsurer can be categorized as slow-paying by reference to a particular percentage. This percentage is calculated by dividing the reinsurance recoverables on paid losses and paid LAE more than ninety days overdue (Column 4) by the sum of reinsurance recoverables

Schedule F—Part 6—Section 1

Provision for Reinsurance Ceded to Certified Reinsurers as of December 31, Current Year (000 OMITTED)

Line Number	1 Federal ID Number	2 NAIC Company Code	3 Name of Reinsurer	4 Domiciliary Jurisdiction	5 Certified Reinsurer Rating (1 through 6)	6 Effective Date of Certified Reinsurer Rating	7 Percent Collateral Required for Full Credit (0% – 100%)	8 Net Amount Recoverable from Reinsurers (Sch. F Part 3 Col. 18)	9 Catastrophe Recoverables Qualifying for Collateral Deferral	10 Net Recoverables Subject to Collateral Requirements for Full Credit (Col 8 – Col 9)	11 Dollar Amount of Collateral Required (Col 10 × Col 7)
Certified Affiliates – U.S. Intercompany Pooling											
			Gamma Re	NY	3	1/1/X1	20%	32,741	0	32,741	6,458
99999999		Totals		0				32,741	0	32,741	6,458

Provision for Reinsurance Ceded to Certified Reinsurers as of December 31, Current Year (000 OMITTED)

	Collateral Provided								20	21	22	23
	12	13	14	Letter of Credit Issuing or Confirming Bank			18	19				
				15	16	17						
Line Number	Multiple Beneficiary Trust	Funds Held by Company Under Reinsurance Treaties	Letters of Credit	American Bankers Association (ABA) Routing Number	Letter of Credit Code	Bank Name	Other Allowable Collateral	Total Collateral Provided (Col. 12 + 13 + 14 + 18)	Percent of Collateral Provided for Net Recoverables Subject to Collateral Requirements (Col. 19 / Col. 10)	Percent Credit Allowed on Net Recoverables Subject to Collateral Requirements (Col 20 / Col 7, not to exceed 100%)	Amount of Credit Allowed for Net Recoverables (Col. 9 + (Col. 10 x Col. 21))	Provision for Reinsurance with Certified Reinsurers Due to Collateral Deficiency (Col. 8 - Col. 22)
Certified Affiliates – U.S. Intercompany Pooling												
		12,767	8,345					21,112	64%	100%	32,741	0
99999999		12,767	8,345				0	21,112		Totals	32,741	0

Schedule F—Part 6—Section 2

Provision for Overdue Reinsurance Ceded to Certified Reinsurers as of December 31, Current Year (000 OMITTED)

1	2	3	4	5	6	7	8	9	10	11	Complete if Column 8 is 20% or Greater			15
											12	13	14	
Federal ID Number	NAIC Company Code	Name of Reinsurer	Domiciliary Jurisdiction	Reinsurance Recoverable on Paid Loss and LAE More Than 90 Days Overdue (a)	Total Reinsurance Recoverable on Paid Losses and LAE (b)	Amounts Received Prior 90 Days	Percent More Than 90 Days Overdue	20% of Amounts in Col. 5	20% of Amounts in Dispute Excluded from Col. 5	Amount of Credit Allowed for Net Recoverables (Sch. F Part 6 Section 1 Col. 22)	Total Collateral Provided (Sch. F Part 6 Section 1 Col. 19) not to Exceed Col 11	Net Unsecured Recoverable for Which Credit is Allowed (Col. 11 -Col. 12)	20% of Amount in Col. 13	Provision for Overdue Reinsurance Ceded to Certified Reinsurers (Greater of Col. 9 + Col. 10 or Col.14) not to Exceed Col. 11
Certified Affiliates – U.S. Intercompany Pooling														
		Gamma Re		2,400	9,441	1,000	23%	0	0	32,741	12,112	11,629	2,326	2,326
99999999				2,400	9,441	1,000		0	0	32,741	12,112	11,629	2,326	2,326

(a) From Schedule F – Part 4 Columns 8 + 9, total certified, less $_____________ in dispute.

(b) From Schedule F – Part 3 Columns 7 + 8, total certified, less $_____________ in dispute.

on paid losses and paid LAE (Column 5) and the amounts received in the prior ninety days (Column 6).

If this percentage is 20 percent or more, the authorized reinsurer is categorized as slow-paying. If the percentage is less than 20 percent, then a penalty of 20 percent of the amount overdue by more than ninety days plus 20 percent on any amounts in dispute is added to the provision for reinsurance.

In the example, the percentage figure for Alpha Re is 0 percent, while for Beta Re it is 19 percent. Schedule F—Part 7 calculates the 20 percent penalty amount for Beta Re in Column 11 ($360,000). If the percentage is greater than 20 percent, the penalty is calculated in Schedule F—Part 8. See the exhibit "Schedule F—Part 7."

Schedule F—Part 7

Provision for Overdue Authorized Reinsurance as of December 31, Current Year

1 Federal ID Number	2 NAIC Company Code	3 Name of Reinsurer	4 Reinsurance Recoverable on Paid Losses and LAE More Than 90 Days Overdue (a)	5 Total Reinsurance Recoverable on Paid Losses and Paid LAE (b)	6 Amounts Received Prior 90 Days	7 Col. 4 divided by (Cols. 5 + 6)	8 Amounts in Col. 4 for Companies Reporting less than 20% in Col. 7	9 Amounts in Dispute Excluded from Col. 4 for Companies Reporting less than 20% in Col. 7	10 20% of Amount in Col. 9	11 Amount Reported in Col. 8 × 20% + Col. 10
Authorized Reinsurers										
		Alpha Re	0	6,700,000	900,000	0%	0	0	0	0
		Beta Re	1,800,000	5,456,000	3,900,000	19%	1,800,000	0	0	360,000
99999999		Totals	1,800,000	12,165,000	4,800,000		1,800,000	0	0	360,000

(a) From Schedule F – Part 4 Columns 8 + 9, total authorized, less $__________ in dispute.

(b) From Schedule F – Part 3 Columns 7 + 8, total authorized, less $__________ in dispute.

Schedule F—Part 8

Schedule F—Part 8 achieves two different objectives. The top part of the schedule calculates the provision for overdue authorized reinsurance for those contracts that exceed the 20 percent benchmark on Part 7. This penalty, if any, is then combined with any applicable penalties calculated in Schedule F—Part 5, Schedule F—Part 6, and Schedule F—Part 7 at the bottom of the schedule to determine the total provision for reinsurance that is ultimately reported on the liabilities side of the balance sheet.

In the example, while neither Alpha Re nor Beta Re exceeded the 20 percent benchmark for overdue authorized reinsurance, the total provision for reinsurance ($2,686,000) is determined at the bottom of the schedule. See the exhibit "Schedule F—Part 8."

Schedule F—Part 8

Provision for Overdue Reinsurance as of December 31, Current Year

1 Federal ID Number	2 NAIC Company Code	3 Name of Reinsurer	4 Reinsurance Recoverable All Items	5 Funds Held By Company Under Reinsurance Treaties	6 Letters of Credit	7 Ceded Balances Payable	8 Other Miscellaneous Balances	9 Other Allowed Offset Items	10 Sum of Cols. 5 through 9 but not in Excess of Col. 4	11 Col 4 Minus Col. 10	12 Greater of Col. 11 or Schedule F - Part 4 Cols. 8 + 9
Authorized Reinsurers											
99999999		Totals	0	0	0		0	0	0	0	0

1. Total	0
2. Line 1 × .20	0
3. Schedule F – Part 7 Col. 11	360,000
4. Provision for Overdue Authorized Reinsurance (Lines 2 + 3)	360,000
5. Provision for Unauthorized Reinsurance (Schedule F – Part 5, Col. 20 × 1000)	0
6. Provision for Reinsurance Ceded to Certified Reinsurers (Schedule F, Part 6, Section 1, Col. 23 × 1000)	0
7. Provision for Overdue Reinsurance Ceded to Certified Reinsurers (Schedule F, Part 6, Section 2, Col. 15 × 1000)	2,326,000
8. Provision for Reinsurance (sum Lines 4 + 5 + 6 + 7) (Enter this amount on Page 3, Line 16)	2,686,000

The exhibit summarizes how the total provision for reinsurance is determined. See the exhibit "Schedule F Provision for Reinsurance."

Schedule F—Part 9

Schedule F—Part 9 is a restatement of the balance sheet to identify ceded reinsurance. Assets and liabilities are restated to show the insurer's balance sheet gross of ceded reinsurance. The figures in this part are intended to indicate the effectiveness of a primary insurer's reinsurance program.

SCHEDULE P

Evaluating an insurer's loss reserves is important in determining the insurer's financial condition. The total estimated liabilities for losses and loss adjustment expenses (LAE) appear on the liabilities side of the balance sheet and in Part 2A of the Underwriting and Investment Exhibit. The supporting data for this information are contained in Schedule P of the National Association of Insurance Commissioners (NAIC) Annual Statement.

Schedule P

The NAIC Annual Statement Schedule that shows detailed historical information on paid and reserved losses and LAE.

The importance of loss reserves is emphasized by the size and complexity of **Schedule P**. Schedule P—Analysis of Losses and Loss Expenses consists of seven parts plus interrogatories. This discussion focuses on Parts 1 through 4. Each of these four parts is composed of subparts for each type of insurance. Part 1 also has a summary of Parts 1 through 4, which includes all classes of insurance combined.

Schedule P—Part 1

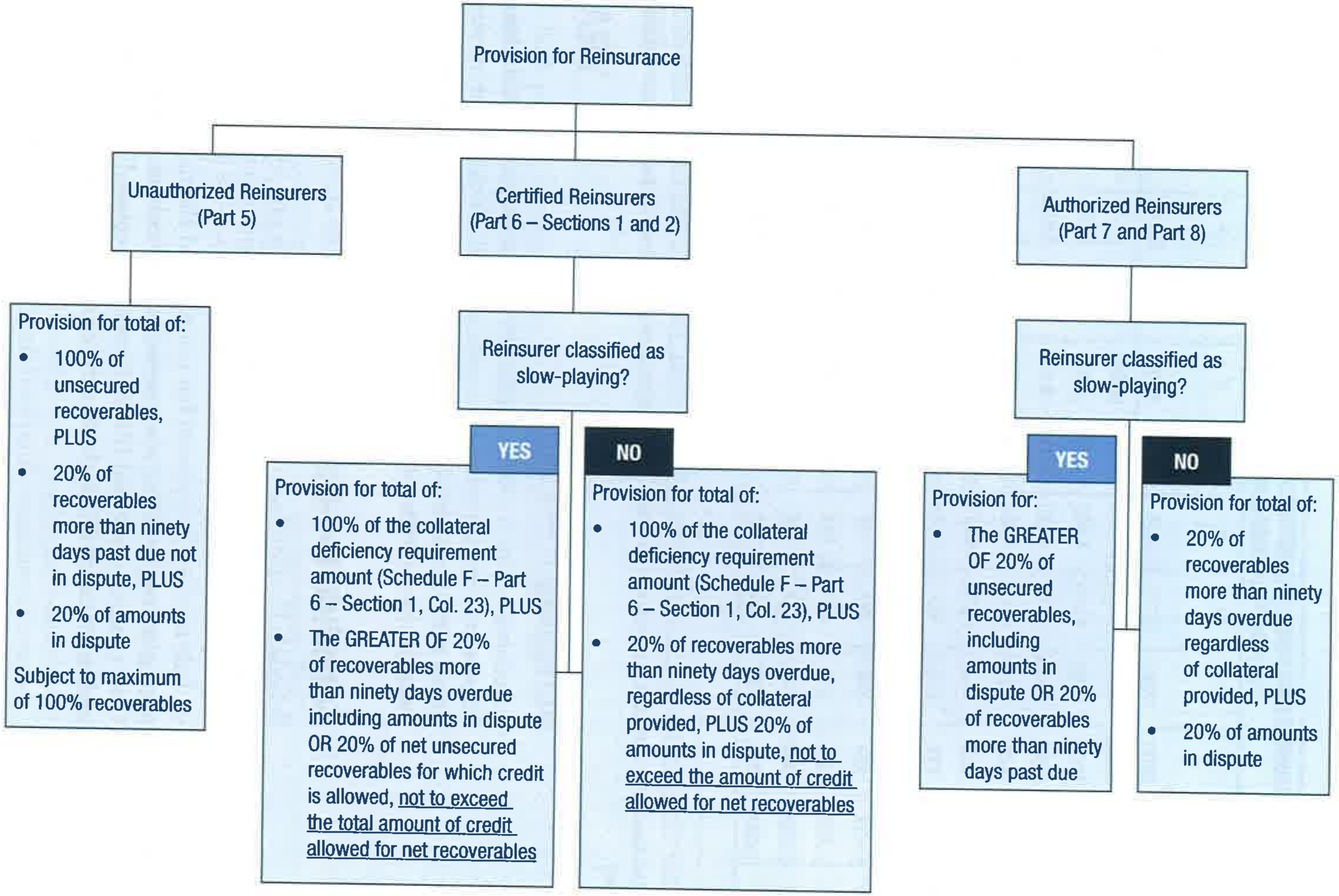
Schedule P—Part 1 provides detailed information on historical losses and loss expenses. It provides an analysis of earned premiums and of losses and loss expenses. Schedule P—Part 1—Summary includes premiums earned, loss and loss expense payments, losses unpaid, defense and cost containment unpaid, adjusting and other unpaid, and total losses and loss expenses incurred.

Relevant data are shown by year for the most recent ten years. An additional line is included on the schedule that shows aggregate data for all years before the past ten. The parts of the schedule that should not contain numerical data are marked "XXX."

Schedule P—Part 2

Schedule P—Part 2 provides a history and development of incurred net losses and defense and cost containment expenses. As with Schedule P—Part 1, Schedule P—Part 2 contains subparts for each type of insurance. In each subpart, Column 11 shows the amount of loss development during the past year, and Column 12 shows the loss development over the past two years. A positive number in either column indicates an increase in incurred losses, while a negative number indicates a decrease. See the exhibit "Schedule P—Part 2—Summary."

Schedule F Provision for Reinsurance



[DA09318]

Schedule P—Part 2—Summary

Years in Which Losses Were Incurred	INCURRED NET LOSSES AND DEFENSE AND COST CONTAINMENT EXPENSES REPORTED AT YEAR END ($000 OMITTED)										DEVELOPMENT	
	1	2	3	4	5	6	7	8	9	10	11	12
	2X02	2X03	2X04	2X05	2X06	2X07	2X08	2X09	2X10	2X11	One Year	Two Year
1. Prior	9,195	9,925	10,660	11,380	11,800	12,315	12,290	12,605	12,575	12,875	300	270
2. 2X02	4,575	4,325	4,350	4,475	4,565	4,600	4,625	4,620	4,630	4,645	15	25
3. 2X03	XXX	4,790	4,305	4,200	4,425	4,490	4,490	4,515	4,515	4,510	(5)	(5)
4. 2X04	XXX	XXX	4,810	4,475	4,350	4,365	4,355	4,350	4,370	4,360	(10)	10
5. 2X05	XXX	XXX	XXX	5,230	4,975	4,850	4,775	4,775	4,760	4,755	(5)	(20)
6. 2X06	XXX	XXX	XXX	XXX	5,350	5,110	5,010	4,985	4,945	4,925	(20)	(60)
7. 2X07	XXX	XXX	XXX	XXX	XXX	5,715	5,575	5,435	5,425	5,395	(30)	(40)
8. 2X08	XXX	XXX	XXX	XXX	XXX	XXX	6,525	6,470	6,345	6,400	55	(70)
9. 2X09	XXX	XXX	XXX	XXX	XXX	XXX	XXX	5,625	5,730	5,705	(25)	80
10. 2X10	XXX	XXX	XXX	XXX	XXX	XXX	XXX	XXX	5,590	5,695	105	XXX
11. 2X11	XXX	XXX	XXX	XXX	XXX	XXX	XXX	XXX	XXX	5,950	XXX	XXX
										12. Totals	380	190

Schedule P—Part 3

Schedule P—Part 3 provides a history of cumulative net paid losses, as well as defense and cost containment expenses. It also includes the number of claims closed with loss payment and without loss payment. Again, there are subparts for each type of insurance.

Schedule P—Part 4

Schedule P—Part 4 contains a history of bulk and incurred but not reported (IBNR) reserves by type of insurance. The data shown in Part 4 form a loss development triangle. The bulk and IBNR reserves for losses and expenses include reserves for incurred but not reported claims, reopened claims, and aggregate reserves on newly reported claims without specific case reserves. Over time, the bulk and IBNR reserves are replaced by case reserves reported and claim payments made. See the exhibit "Schedule P—Part 4—Summary."

Schedule P—Part 4—Summary

Years in Which Losses Were Incurred	BULK AND IBNR RESERVES ON NET LOSSES AND DEFENSE AND COST CONTAINMENT EXPENSES REPORTED AT YEAR END ($000 OMITTED)									
	1 2X02	2 2X03	3 2X04	4 2X05	5 2X06	6 2X07	7 2X08	8 2X09	9 2X10	10 2X11
1. Prior	2,225	1,650	1,300	1,445	1,450	1,535	1,250	1,390	900	1,035
2. 2X02	1,395	550	250	190	145	125	95	75	60	50
3. 2X03	XXX	2,000	825	375	430	400	330	300	260	240
4. 2X04	XXX	XXX	2,205	1,230	820	635	515	430	395	365
5. 2X05	XXX	XXX	XXX	2,360	1,285	850	600	465	365	320
6. 2X06	XXX	XXX	XXX	XXX	2,465	1,445	970	715	550	445
7. 2X07	XXX	XXX	XXX	XXX	XXX	2,625	1,600	1,050	760	570
8. 2X08	XXX	XXX	XXX	XXX	XXX	XXX	2,750	1,675	1,115	825
9. 2X09	XXX	XXX	XXX	XXX	XXX	XXX	XXX	2,495	1,625	1,120
10. 2X10	XXX	XXX	XXX	XXX	XXX	XXX	XXX	XXX	2,425	1,470
11. 2X11	XXX	XXX	XXX	XXX	XXX	XXX	XXX	XXX	XXX	2,405

SUMMARY

All insurers, both primary insurers and reinsurers, are required to file an NAIC Annual Statement with the insurance department of each state in which they are authorized to do business. The Annual Statement is a complex and lengthy financial document consisting of a balance sheet, a statement of income, and a cash flow statement and is backed by supporting exhibits and schedules.

The largest categories of assets on an insurer's Annual Statement balance sheet are typically bonds, common stocks, and short-term investments. The most common reinsurance-related asset for a reinsurer is funds deposited by the reinsurer with primary insurers, and for a primary insurer, it is amounts recoverable from reinsurers.

The largest liability on an insurer's Annual Statement balance sheet is typically losses and loss adjustment expense reserves. The most common reinsurance-related liability for a reinsurer is the amount payable by the reinsurer on losses and loss adjustment expenses already paid by the primary insurer. For a primary insurer, key liabilities are the funds held under reinsurance treaties, the provision for reinsurance, and the unearned premium amount.

The Statement of Income in the NAIC Annual Statement measures the insurer's earnings over the course of a year, indicating a primary insurer's financial strength to a reinsurer. The Underwriting and Investment Exhibit supports the Statement of Income and shows premiums earned, premiums written, losses paid and incurred, and unpaid losses and LAE, all by type of insurance, in addition to expenses.

Schedule F of the NAIC Annual Statement shows specific information on ceded and assumed reinsurance, as well as portfolio transfers. It establishes the primary insurer's provision for reinsurance based on reinsurance ceded to authorized, unauthorized, and certified reinsurers. Schedule F also includes a restated balance sheet, which shows assets and liabilities gross of ceded reinsurance and indicates the primary insurer's dependence on reinsurance.

Schedule P of the NAIC Annual Statement shows detailed information by type of insurance on losses and LAE, both paid and reserved. It also contains historical losses in a loss triangle format and is therefore useful in calculating the insurer's IBNR amount.

ASSIGNMENT NOTE

1. "NAIC Adopts Revisions to Reinsurance Models: Key Changes Permit Reduction in Reinsurance Collateral Requirements for Non-U.S. Reinsurers," www.naic.org/Releases/2011_docs/naic_adopts_revisions_to_reinsurance_models.htm (accessed October 26, 2012).