



SOCIETY OF FINANCIAL EXAMINERS™

Supplemental Background Material

NAIC Examiner Project

Course CFE 3

Reinsurance

The passing score for this test is 74

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Society of Financial Examiners
Reinsurance

Unit: 1

Topic: Reinsurance: Indemnifying Insurers

Text
Required: Reinsurance; edited and published by Robert W. Strain; Revised Edition,
1997

Assigned
Readings: Strain, pp. 9-32

Introduction

- I. Reinsurance
 - A. Definition
 - B. Inapplicability
 - C. Relationship between the parties – two or more insurers
 - D. Eligible reinsurers
 - E. Purpose – insurance for insurers

- II. Difference from Primary Insurance
 - A. Reinsurance tends to be less regulated.
 - B. More internationally oriented.
 - C. Transactions of large monetary value and risk.
 - D. Reinsurer relies on the reinsured to produce proper underwriting at proper rates.
 - E. Right to inspect records of the reinsured
 - F. Utmost good faith
 - G. Relies on reinsured to produce a profitable book of business.

- III. Reinsurance Contract
 - A. Kinds
 - 1. Proportional – pro rata
 - 2. Nonproportional – excess of loss

B. Types of Contracts

1. Treaty – covers losses on policies in one or more specific classes
2. Facultative – covers certain individual policies on a stand-alone basis

C. Classes of Insurance Business Reinsured

D. Retrocession – reinsuring reinsurance

IV. Fundamentals of Reinsurance and Customary Practices

A. Mutual Trust

B. Utmost Good Faith

C. Follow the Fortunes

D. Declaratory Judgment Actions

E. Dispute Resolution by Arbitration

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Reinsurance

Unit: 2

Topic: Pro Rata Property Treaty

Text Required: Reinsurance; edited and published by Robert W. Strain; Revised Edition, 1997

Assigned Readings: Strain, pp. 36-52

Origins and Functions of Treaties

- I. Proportional Reinsurance functions
 - A. Increase underwriting capacity
 - B. Provide protection against losses from catastrophes
 - C. Provide relief in the short run financing or acquisition costs
 - D. Stabilize underwriting performance.

- II. Types of Pro Rata Property Treaties
 - A. Quota Share
 - 1. Benefits to ceding company
 - a. Replenish policyholders surplus
 - b. Encourage new lines of business
 - c. Afford fronting
 - d. Provide catastrophe coverage
 - e. Increase insurance liability retention
 - 2. Portfolio v. running account
 - 3. Net v. gross account
 - 4. Guaranteed profit quota share.

 - B. Surplus Share
 - 1. Definition
 - a. Varying percentages
 - b. Varying obligatory requirements
 - 2. Purpose
 - a. Maximum limit per risk
 - b. Multiples of net retention

- c. Minimum retention required
- 3. Advantages

III. Pricing

- A. Flat commission
- B. Contingent commission
- C. Sliding scale commission

IV. Significant Concepts and Practices

- A. Transfer of Risk
- B. Retention warranties
- C. Coverage and limits
- D. Attachment of liability
- E. Risk definition
- F. Follow fortunes, settlements and original conditions
- G. Protecting the surplus treaty
- H. Reporting transaction
- I. Termination

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Unit: 3

Topic: Property Per Risk Excess of Loss Reinsurance

Text Required: Reinsurance; edited and published by Robert W. Strain; Revised Edition, 1997

Assigned Readings: Strain, pp. 79-120

- I. Purposes and Characteristics
 - A. Increase capacity
 - B. Legal requirements
 - C. Financial rating requirements
 - D. Stabilize underwriting results
 - E. Economy of use

- II. Relationship to Other Reinsurance

- III. Determining Retention and Limit.
 - A. Reported claim counts
 - B. Experience rating
 - C. Ruin Model
 - D. Monte Carlo Simulation

- IV. Common Contract
 - A. Retention and limit
 - B. Net retained lines
 - C. Exclusions
 - D. Definition of Risk
 - E. Net Loss
 - F. Definition of occurrence
 - G. Allocated loss adjustment expenses
 - H. Losses in excess of policy limits, extra contractual obligation and punitive damages

- V. Rating Plans

- A. Prospective
- B. Retrospective
- C. Rating methodology
 - 1. Experience rating
 - a. Loss trending
 - b. Excess loss development
 - c. Benchmark data
 - d. Allocated LAE
 - e. Premium adjustments
 - f. Reinsurer loading
 - 2. Exposure
 - a. Property exposure rating scales
 - b. Expected loss component
 - c. Allocated LAE
 - d. Discount factors

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Unit: 4

Topic: Casualty Excess of Loss Treaty Reinsurance

Text Required: Reinsurance; edited and published by Robert W. Strain; Revised Edition, 1997

Assigned Readings: Strain, pp. 123-201

I. Purposes

- A. Write larger risks.
- B. Protect from large catastrophes
- C. Stabilize underwriting results

II. Types of Casualty Reinsurance Contracts

- A. Quota share
- B. Working layer excess of loss (per risk, per occurrence)
- C. Clash, excess of loss (per occurrence) catastrophe excess of loss
- D. Aggregate excess stop-loss

III. Considerations in using Casualty Excess

- A. Lines of insurance affected and reinsurance desired
- B. Ultimate net loss and expenses
- C. Integration of other reinsurance
- D. Methods of attachment and termination
- E. Retention and limits (loss caps and reinstatements)
- F. Definition of occurrence and loss trigger
- G. Event coverage or interlocking
- H. Aggregate extension and aggregate extraction
- I. Pricing tools
- J. Other issues
 - 1. Structured settlements
 - 2. Treaty special acceptance
 - 3. Loss notice requirements
 - 4. Errors and omissions

5. Loss settlement discretion (following fortunes or settlements)

IV. Evaluation and Contributions

1. Services
2. Claim audits

B Insurer

1. Management
2. Underwriting
3. Claims
4. Estimating reserve liabilities

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Unit: 5

Topic: Catastrophe Reinsurance

Text Required: Reinsurance; edited and published by Robert W. Strain; Revised Edition, 1997

Assigned Readings: Strain, pp. 206-242

I. Purposes

- A. To protect policyholder surplus
- B. Stabilize underwriting results.

II. Catastrophe Perils

- A. Large fires
- B. Earthquakes
- C. Winter Freeze
- D. Floods
- E. Riot
- F. Hurricanes
- G. Tornadoes

III. Occurrence Treaty contract provision

- A. Contract percentage coverage
- B. Layered coverages
- C. Reinstatements
- D. Exclusions
- E. Application of coverage.
- F. Definition of loss occurrence
- G. Claims
- H. Rating

IV. Designing the Catastrophe Program

- A. Catastrophe limit and retention

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Unit: 6

Topic: Aggregate Excess or Stop-Loss Reinsurance

Text Required: Reinsurance; edited and published by Robert W. Strain; Revised Edition, 1997

Assigned Readings: Strain, pp. 245-276

- I. Nature, Purpose and Benefit
- II. Criteria for Establishing Retention and Limit
 - A. Reinsured retention
 - 1. Insurance underwriting experience
 - 2. Reinsurance limit desired
 - 3. Strength of inuring reinsurance
 - 4. Primary insurance pricing validity
 - B. Reinsurer's limit
 - 1. Lesser of percentage of premium or dollar amount
 - 2. Other underwriting consideration
- II. Pricing
- III. Loss Settlement Provisions
 - A. Cutoff
 - B. Runoff
- IV. Clauses
 - A. Warranted reinsurance
 - B. Quota share reinsurance
- V. Suitability of Coverage

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Unit: 7

Topic: Financial Reinsurance

Text Required: Reinsurance; edited and published by Robert W. Strain; Revised Edition, 1997

Assigned Readings: Strain, pp. 279-292

Assignment Seven:

- I. Cause of Growth
- II. Optimum Environment for Financial (Finite Risk) Reinsurance
 - A. Single vs. Multi-year loss horizons
 - B. Profit sharing
 - C. Comparison with traditional covers
- III. Cost and Stability Trade-Off
- IV. Applications
- V. Regulations

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Unit: 8

Topic: Facultative Reinsurance

Text Required: Reinsurance; edited and published by Robert W. Strain; Revised Edition, 1997

Assigned Readings: Strain, pp. 295-319

I. Characteristics

- A. Reinsures individual risks
- B. Allows individual risk negotiation and is non-obligatory
- C. Operates in an environment of adverse risk selection

II. Uses of Facultative Reinsurance

- A. Increase Capacity
- B. Protect the reinsured's net lines
- C. Protect the reinsured's treaty
- D. Reduce loss from Catastrophe
- E. Offset treaty exclusions
- F. Provide underwriting assistance
- G. Provide marketing accommodation
- H. Achieve growth and expansion
- I. Permit withdrawal

III. Structures of Coverage

IV. Underwriting

- A. Primary Layer
- B. Buffer/working excess layer
- C. Catastrophe layer

V. Contracts used in Facultative Reinsurance

- A. Certificate of reinsurance
- B. Automatic and Program

VI. Facultative Marketplace

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Unit: 9

Topic: Pricing Reinsurance

Text Required: Reinsurance; edited and published by Robert W. Strain; Revised Edition, 1997

Assigned
Readings: Strain, pp. 404-469

- I. Experience rating Excess of Loss
 - A. Premium adjustments
 - 1. Exposure base
 - 2. Rate changes
 - 3. Deviation changes
 - B. Loss adjustments
 - 1. Incurred versus frequency and severity
 - 2. Trend
 - 3. Development
 - C. Burning Cost Ratio
 - D. Time value of money
 - E. Loadings
- II. Exposure Rating Excess of Loss
 - A. Casualty covers
 - B. Per risk property covers
- III. Alternative Rating Structures
 - A. Retrospectively rated treaties
 - B. Aggregate deductible treaties
- IV. Casualty Contingency (Clash)
 - A. Basic Charge
 - B. Surcharges
 - C. Reinstatements
 - D. Extra contractual obligation and excess of policy limits
 - E. Allocated loss adjustment expense
 - F. Stacking policy limits
 - G. Other exposures
- V. Property Catastrophe

- A. Experience rating
- B. Exposure rating models
- C. Reinstatements

VI. Pro Rata Pricing

- A. Ceding commission structure
- B. Estimating ultimate loss ratio

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Unit:	10
Topic:	Markets and Marketing
Text Required:	Reinsurance; edited and published by Robert W. Strain; Revised Edition, 1997
Objectives:	To be able to describe the categories of reinsurance and transactions. To describe the accounting for reinsurance transactions and their effect on the ceding company.
Assigned Readings:	Strain, pp. 481-495

I. Distribution System

- A. Broker markets
- B. Direct markets

II. Services

- A. Actuarial
- B. Reinsurer financial security
- C. Letters of credit
- D. Contract wording
- E. Claims advise
- F. Accounting
- G. Information system

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Unit: 11

Topic: Underwriting the Reinsured

Text Required: Reinsurance; edited and published by Robert W. Strain; Revised Edition, 1997

Assigned Readings: Strain, pp. 501-543

I The Reinsured

- A. Banking Concept
- B. Living Business Enterprise
- C. Continuity

II. Measuring the Reinsured's Fiscal Health

- A. Sources of information
- B. Interpreting the
- C. Effects of the reinsured's insolvency on the reinsurer

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Unit: 12

Topic: Claims Management

Text Required: Reinsurance; edited and published by Robert W. Strain; Revised Edition, 1997

Assigned Readings: Strain, pp. 550-593

I. Introduction

- A. Individual loss
- B. Bordereau reports

II. Origin of Claims

- A. First-party claims
- B. Claims by third parties
 - 1. Claims by claimants on policies reinsured
 - 2. Parties to assumption agreements
 - 3. Cut-through endorsements
- C. Reasons for claim management
 - 1. Establishing validity
 - 2. Acknowledging prompt reporting and assessing the claim.
 - 3. Establishing a loss reserve
 - 4. Reporting reserves to underwriting and actuarial departments
 - 5. Developing reserves with adjustments
 - 6. Informing retrocessionaires

III. Functions

- A. Auditing
- B. Reserving and Development
- C. Recording and Reporting

IV. Common Contractual Provisions

- A. Retention
- B. Liability
- C. Loss notice
- D. Loss settlement (follow settlements made by company)
- E. Arbitration
- F. Business covered
- G. Commencement and term
- H. Loss settlements (pro rata or ultimate net loss)
- I. Loss adjustment expense
- J. Net retained lines
- K. Access to records
- L. Claim cooperation
- M. Loss occurrence
- N. Aggregate extension
- O. Loss in excess of original policy limits
- P. Extra contractual obligation
- Q. Errors and omissions
- R. Offset
- S. Insolvency
- T. Most favored terms
- U. Nondisclosure of settlements

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Unit: 13

Topic: Reinsurance Accounting

Text Required: Reinsurance; edited and published by Robert W. Strain; Revised Edition, 1997

Assigned Readings: Strain, pp. 600-693

Insurance Company Financial Analysis

- I. Dual Accounting Systems – SAP versus GAAP
 - A. Authorized vs. Unauthorized
- II. Reinsurance Accounts
 - A. Reinsurance Premium
 - B. Losses and Loss adjustment expenses
 - C. Commissions
- III. Differences between Insurance and Reinsurance Accounting
 - A. Accounting periods
 - B. Premium Bases
 - C. Terminating losses: cutoff or runoff
- V. Government and Self Regulation of Accounting
 - A. NAIC Accounting Practices and Procedures Manual
 - B. Schedule F
 - C. Terms of the reinsurance agreement
 - 1. Proportional treaties
 - 2. Nonproportional treaties

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Unit: 14

Topic: Life Reinsurance

Text Required: Reinsurance; edited and published by Robert W. Strain; Revised Edition, 1997

Assigned Readings: Strain, pp. 702-720

- I. Reinsurance Agreements
 - A. Indemnity
 - 1. Yearly renewable term
 - 2. Coinsurance
 - 3. Modco
 - B. Nonproportional
 - C. Assumption Reinsurance (Novation)
- II. Important Treaty Clauses
 - A. Parties to agreement clause
 - B. Oversight clause
 - C. Extra Contractual Damage
 - D. Jumbo limit
 - E. Termination
 - F. Follow the fortunes

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Unit: 15

Topic: Accident and Health Reinsurance

Text Required: Reinsurance; edited and published by Robert W. Strain; Revised Edition, 1997

Assigned Readings: Strain, pp.731-740

- I. The Reinsurance Treaty
 - A. Quota share
 - B. Excess of loss
 - C. Catastrophe coverage
 - D. Facultative

- II. Reinsuring Accident and health Coverages
 - A. Long-term disability income
 - 1. Total disability
 - 2. Partial disability

 - B. Special risk reinsurance
 - 1. Personal accident
 - 2. Occupational accident

 - C. Medical expense reinsurance
 - 1. Portfolio medical excess
 - 2. Multiple employer trusts (METs)
 - 3. Organ transplant
 - 4. Reinsuring other medical

 - D. Stop-loss insurance
 - 1. HMOs
 - 2. Physician hospital provider excess

E. Long-term care expenses

- 1 Portfolio aggregate stop-loss
- 2 Proportional A & H quota share
3. Proportional claim only
4. Excess of loss

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Unit: 16
Topic: Life, Deposit-Type and Accident and Health Reinsurance
Text Required: Accounting Practices and procedures Manual as of March 2000
Assigned Readings: SSAP 61

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Unit: 17

Topic: Property and Casualty Reinsurance

Text Required: Accounting Practices and procedures Manual as of March 2000

Assigned Readings: SSAP 62