

Statutory Issue Paper No. 65

Property and Casualty Contracts

STATUS

Finalized March 16, 1998

Original SSAP and Current Authoritative Guidance: SSAP No. 65

Type of Issue:

Property and Casualty

SUMMARY OF ISSUE

1. Current statutory accounting for property and casualty insurance contracts is provided in Chapters 10, 11, 12, 14, 17 and 21 of the Accounting Practices and Procedures Manual for Property and Casualty Insurance Companies (P&C Accounting Practices and Procedures Manual). Property and casualty insurers may issue contracts that have unique features or require specific accounting treatment. Policies may be issued on a claims-made basis, certain claims may be of the nature that it may be appropriate to discount the liabilities established, or such that the claim can be satisfied by purchasing an annuity or similar type investment to fund claim payments. Title insurance is a property and casualty insurance contract that is unique and is therefore specifically addressed in *Issue Paper No. 57—Title Insurance*.

2. GAAP guidance is provided in *FASB Statement No. 60, Accounting and Reporting by Insurance Enterprises* (FAS 60), *FASB Statement No. 113, Accounting and Reporting for Reinsurance of Short-Duration and Long-Duration Contracts* (FAS 113), *AICPA Audit and Accounting Guide: Property & Casualty Insurance Companies* (AICPA P&C Audit and Accounting Guide) and in *AICPA Statement of Position 94-5, Disclosures of Certain Matters in the Financial Statements of Insurance Enterprises* (SOP 94-5).

3. The purpose of this issue paper is to establish statutory accounting principles for property and casualty insurance contracts that are consistent with the Statutory Accounting Principles Statement of Concepts and Statutory Hierarchy (Statement of Concepts).

SUMMARY CONCLUSION

4. In recent years insurers have begun offering policies with unique reporting features. Paragraphs 5 through 10 of this issue paper relate to policies commonly referred to as “claims-made” policies. Property and casualty insurance contracts can be written to cover insured events on different reporting bases as follows:

- a. Occurrence - These policies cover insured events that occur within the effective dates of the policy regardless of when they are reported to the insurer.
- b. Claims-Made - These policies cover insured events that are reported (as defined in the policy) within the effective dates of the policy subject to retroactive dates where applicable. Unlike an occurrence policy where a liability is recorded when the event occurs, a liability for a claims-made policy shall be recorded when the event is reported to the insurer.
- c. Extended Reporting - Endorsements to claims-made policies covering insured events reported after the termination of a claims-made contract but subject to the same

retroactive dates where applicable. See paragraphs 7 and 8 for guidance for when premium shall be earned and losses shall be recorded.

Claims-Made Policies

5. When an insured obtains claims-made coverage they are normally replacing existing coverage. The existing coverage may have been a claims-made policy or an occurrence policy. In either case, in an effort to reduce premium costs, the insured may request that the claims-made coverage only cover claims reported within the effective dates of the policy that occur after a specified date. This specified date is referred to as the retroactive date of the claims-made policy. This exclusion eliminates duplicate coverage when converting from occurrence coverage to claims-made coverage.

6. The amount of the liability recorded for an insured event shall be determined in accordance with the provisions of paragraphs 6 through 12 of *Issue Paper No. 55—Unpaid Claims, Losses and Loss Adjustment Expenses* (Issue Paper No. 55).

7. Premiums shall be recognized in accordance with *Issue Paper No. 53—Property Casualty Contracts - Premiums* (Issue Paper No. 53) unless the policy contains tail coverage as discussed in the following paragraphs.

8. An insured may be provided an extended reporting option to allow extended reporting of events. The extended reporting feature is commonly referred to as “tail coverage.” Extended reporting provisions provided on a claims-made policy modify the exposure period of the underlying contract and can be for a defined period (e.g., six months, one year, five years, etc.) or can be for an indefinite period.

9. Issue Paper No. 53 states “*Premiums from property and casualty contracts shall be recognized in the statement of operations, as earned premium using either the daily pro-rata or monthly pro-rata methods...unless a different method is specified in issue papers for specific types of property and casualty contracts.*” Therefore, when extended reporting provisions for a defined period are provided to the holder of a claims-made policy, the insurer shall establish an unearned premium reserve. This liability shall represent the amount of premium charged for the tail coverage that has not yet expired and shall be earned over the tail period regardless of when the tail coverage is elected. When the claims costs and loss adjustment expenses anticipated to be reported during the extended reporting period, together with expected dividends to policyholders and maintenance cost exceed the recorded unearned premium reserve for a claims-made policy, a premium deficiency reserve shall be recognized in accordance with Issue Paper No. 53.

10. When extended reporting provisions are for an undefined or indefinite period the policy has effectively been converted to an occurrence type policy. In such instances the premiums shall be recognized in accordance with Issue Paper No. 53 over the basic coverage period and the insurer shall establish a liability for all insured events that have occurred through the end of the policy period whether or not they have been reported. In establishing such reserves the insurer shall follow the guidance prescribed in Issue Paper No. 55.

Discounting

11. With the exception of fixed and determinable payments such as those emanating from workers’ compensation tabular indemnity reserves and long-term disability claims, property and casualty loss reserves shall not be discounted.

12. Tabular reserves are indemnity reserves that are calculated using discounts determined with reference to actuarial tables which incorporate interest and contingencies such as mortality, remarriage, inflation, or recovery from disability applied to a reasonably determinable payment stream. This definition shall not include medical loss reserves or any loss adjustment expense reserves.

13. When establishing discounted loss reserve liabilities using a non-tabular method the liability shall be determined in accordance with *Actuarial Standard of Practice No. 20, Discounting of Property and Casualty Loss and Loss Adjustment Expense Reserves* (Actuarial Standard of Practice No. 20) but in no event shall the rate used exceed the lesser of the following two standards:

- a. If the company's statutory invested assets are at least equal to the total of all policyholder reserves, the company's net rate of return on statutory invested assets, less 1.5%, otherwise, the company's average net portfolio yield rate less 1.5% as indicated by dividing the net investment income earned, as indicated by line 8 of the Underwriting and Investment Exhibit of the Annual Statement, by the average of the insurer's current and prior year total assets, as indicated on page 2 of the most currently filed annual financial statement; or
- b. The current yield to maturity on a United States Treasury debt instrument with maturities consistent with the expected payout of the liabilities.

14. In accordance with *Issue Paper No. 3—Accounting Changes* (Issue Paper No. 3), a change in the discount rate used in discounting loss reserves shall be accounted for as a change in estimate. The provisions of Issue Paper No. 3 require changes in estimates to be included in the statement of operations in the period the change becomes known.

15. Insurers shall disclose the impact of discounting on the reserves for each line of business and reserve category, if any, the discount rate being utilized, and the tables used if applicable, as well as the impact of any change in the discount rate from the prior period. The disclosures required by paragraph 44 of this issue paper shall be made separately for tabular discounting and non-tabular discounting.

Structured Settlements

16. Structured settlements are periodic fixed payments to a claimant for a determinable period, or for life, for the settlement of a claim. Frequently a reporting entity will purchase an annuity to fund these future payments. Reporting entities may purchase an annuity in which the reporting entity is the owner and payee, or may purchase an annuity whereby the claimant is the payee. When annuities are purchased to fund periodic fixed payments they shall be accounted for as follows:

- a. When the reporting entity is the owner and payee, no reduction shall be made to loss reserves and the annuity shall be recorded at its present value and accounted for as an other-than-invested asset as it meets the definition of an asset described in *Issue Paper No. 4—Definition of Assets and Nonadmitted Assets*. Income from these annuities shall be treated as miscellaneous income. The present value of the annuity and the related amortization schedule shall be obtained from the issuing life insurance company at the time the annuity is purchased.
- b. When a reporting entity has purchased an annuity and the claimant is the payee, the reporting shall reduce the loss reserve to the extent that the annuity provides for funding of future payments. The cost of these annuities shall be recorded as paid losses in such instances.

17. For each year that full financial statements are presented insurers shall disclose the following in accordance with paragraph 43 of this issue paper:

- a. The amount of reserves no longer carried by the insurer because it has purchased annuities with the claimant as payee and the extent to which an insurer is contingently liable for such amounts should the issuers of the annuities fail to perform under the terms of the annuities.

- b. The name, location and aggregate statement value of annuities due from any life insurer to the extent that the aggregate value of those annuities, equal or exceed 1% of the reporting entity's policyholders' surplus. This disclosure shall include all annuities for which the company has not obtained a release of liability from the claimant as a result of the purchase of an annuity. The company shall also disclose whether such life insurers are licensed in the company's state of domicile.

Excess Statutory Reserve

18. Current statutory guidance requires insurers to record an excess statutory reserve computed in accordance with the NAIC Annual Statement Instructions to Schedule P - Part 7. The types of insurance that currently are subject to the excess reserve are:

- auto liability
- other liability
- medical malpractice
- workers' compensation
- credit coverages

19. This issue paper eliminates the requirement to record excess statutory reserves. Excess statutory reserves do not meet the definition of a liability as set forth in *Issue Paper No. 5—Definition of Liabilities, Loss Contingencies and Impairments of Assets* (Issue Paper No. 5) which states:

For purposes of statutory accounting, a "liability" shall be defined as certain or probable¹ future sacrifices of economic benefits arising from present obligations of a particular entity to transfer assets or to provide services to other entities in the future as a result of past transaction(s) or event(s). A liability has three essential characteristics: (a) it embodies a present duty or responsibility to one or more other entities that entails settlement by probable¹ future transfer or use of assets at a specified or determinable date, on occurrence of a specified event, or on demand, (b) the duty or responsibility obligates a particular entity, leaving it little or no discretion to avoid the future sacrifice, and (c) the transaction or other event obligating the entity has already happened. This includes but is not limited to liabilities arising from policyholder obligations (e.g. policyholders benefits, reported claims and reserves for incurred but not reported claims). Liabilities shall be recorded on a Company's financial statements when incurred.

¹ *FASB Statement of Financial Accounting Concepts No. 6, Elements of Financial Statements* (CON 6), states: Probable is used with its usual general meaning, rather than in a specific accounting or technical sense (such as that in *FASB Statement 5, Accounting for Contingencies*, par. 3), and refers to that which can reasonably be expected or believed on the basis of available evidence or logic but is neither certain nor proved...

Policies with Coverage Periods Equal to or in Excess of Thirteen Months

20. Some property and casualty insurance contracts are written for coverage periods that equal or exceed thirteen months. These contracts may be single premium or fixed premium policies. These contracts generally are not subject to cancellation or premium modification by the insurer. The most common types of coverages with such periods offered by insurers are home warranty and mechanical breakdown. Revenues are generally not received in proportion to the level of exposure or period of exposure. In order to recognize the economic results of the contract over the contract period, statutory accounting must focus on establishing a liability for the estimated future policy benefits while taking into account estimated future premiums to be received. Insurers that issue such policies shall report unearned premiums in accordance with paragraph 47 of this issue paper. This guidance is primarily focused on home warranty and mechanical breakdown coverages and is not intended to include multiple year contracts comprised of single year policies each of which have separate premiums and annual aggregate

deductibles. This issue paper rejects current statutory guidance for warranty insurance reserves found in Chapter 12, Unearned Premiums, of the P&C Accounting Practices and Procedures Manual.

High Deductible Plans

21. Recently insurers have begun offering certain coverages, particularly workers' compensation coverage, under high deductible plans. These types of plans are different than self insurance coupled with an excess of loss policy in that state laws generally require the insurer to fund the deductible and to periodically review the financial viability of the insured and make an assessment of the suitability of the deductible plan to the insured. Several issues surrounding these types of plans exist, including the recording of claims below the deductible limit and the recording of the reimbursement of the deductible to the insurer.

22. Reserves for claims arising under high deductible plans shall be established net of the deductible, however, no reserve credit shall be permitted for any claim where any amount due from the insured has been determined to be uncollectible. The insurer shall disclose in the notes to the financial statements the amount of reserve credit that has been recorded for high deductibles on unpaid claims and the amounts that have been billed and are recoverable on paid claims.

23. If the policy form requires the insurer to pay for all claims including those under the deductible limit the insurer is subject to credit risk, not underwriting risk. The reimbursement of the deductible shall be accrued and recorded as a reduction of paid losses simultaneously with the recording of the paid loss by the insurer. Amounts accrued for the reimbursement of the deductible shall be billed in accordance with the provisions of the policy and the billed amount shall be accounted for as an asset. Ten percent of deductible recoverable in excess of collateral specifically held and identifiable on a per policy basis, must be reported in the annual statement as a nonadmitted asset, however, to the extent that amounts in excess of the 10% are not anticipated to be collected they shall be nonadmitted.

Environmental Exposures

24. Environmental exposures are any loss or potential loss, including third party claims, related directly or indirectly to the remediation of a site arising from past operations or waste disposal. Examples of environmental exposures include but are not limited to chemical waste, hazardous waste treatment, storage, or disposal facilities, industrial waste disposal facilities, landfills, superfund sites, toxic waste pits, and underground storage tanks.

25. Insurers that are potentially exposed to asbestos or environmental claims shall provide the disclosures required by paragraph 46 of this issue paper. Reserves for asbestos and environmental exposures shall be recorded consistently with Issue Paper No. 55.

Policyholder Dividends

26. Dividends to policyholders become liabilities of the company immediately when they are declared by the board of directors and shall be recorded as a liability in the annual statement. Incurred policyholder dividends are reported in the Statement of Income.

DISCUSSION

Claims-Made Policies

27. This issue paper requires the recognition of an unearned premium reserve for claims-made policies with defined extended reporting provisions and an unpaid loss reserve for claims-made policies with undefined extended reporting periods, whereas current statutory guidance permits that such liabilities be reported with unearned premiums or loss reserves for those losses that have been incurred but not reported regardless of the nature of the extended reporting feature. This issue paper also requires insurers to record a premium deficiency reserve in instances when claim and loss adjustment expenses anticipated during a defined extended reporting period, together with certain other costs as described in paragraph 9 exceed the unearned premium reserve. Eliminating the option to record these reserves as loss reserves

when there is a defined extended reporting period is consistent with the concept that under claims-made reporting policies, no loss has been incurred until it has been reported to the insurer. This change was made to be consistent with Issue Paper No. 53 which requires premiums to be earned over the period of exposure. Requiring these reserves to be classified as losses when a claims-made policy has effectively been converted to an occurrence policy through an undefined extended reporting period is consistent with Issue Paper No. 55.

Discounting

28. The statutory principles outlined in the conclusion above are consistent with current statutory guidance for property and casualty insurance contracts. It expands current statutory guidance to permit insurers to use a discount rate that can be supported by Actuarial Standard of Practice No. 20 when discounting indemnity reserves established for future cash payments that are both fixed and determinable. Current statutory guidance limits the discount rate to that permitted by the insurer's domiciliary state. This change was made for consistency with the Statement of Concepts which states:

The regulators' need for meaningful, comparable financial information to determine an insurer's financial condition requires consistency in the development and application of statutory accounting principles. Because the marketplace, the economic and business environment, and insurance industry products and practices are constantly changing, regulatory concerns are also changing. An effective statutory accounting model must be responsive to these changes and address emerging accounting issues. Precedent or historically accepted practice alone should not be sufficient justifications for continuing to follow a particular accounting principle or practice which may not coincide with the objectives of regulators.

29. FAS 60 states that the liability for unpaid claims shall be based on the ultimate cost of settling claims and also requires disclosure of amounts of reserves that are discounted as well as the range of discount rates used. No guidance is provided in FAS 60 with respect to the types of reserves that may be discounted. The Securities and Exchange Commission (SEC) permits discounting liabilities for unpaid loss and loss adjustment expenses at the same rates used for reporting to state regulatory authorities with respect to the same claim liabilities. Current practice under GAAP is to follow the SEC guidelines resulting in certain workers' compensation reserves and medical malpractice reserves being recorded at discounted amounts.

Structured Settlements

30. This paper adopts current statutory guidance for structured settlements. GAAP for structured settlements is found in FAS 113. FAS 113 is addressed in its entirety in *Issue Paper No. 75—Property and Casualty Reinsurance*. Statutory accounting and GAAP are consistent for the accounting of structured settlement annuities where the insurer is the owner and payee, and where the claimant is the owner and payee and the insurer has been released from its obligation. GAAP distinguishes those structured settlement annuities where the owner is the claimant and a legally enforceable release from the insurer's liability is obtained from those where the claimant is the owner and payee but the insurer has not been released from its obligation. GAAP requires the deferral of any gain resulting from the purchase of a structured settlement annuity where the claimant is the owner and payee yet the insurer has not been released from its obligation. Structured settlement annuities are an established practice and the pricing of annuities purchased from non-affiliates is dictated by an effective market. As a result statutory accounting views these settlements as completed transactions and considers the earnings process complete, thereby allowing for immediate gain recognition.

Excess Statutory Reserves

31. This issue paper eliminates the requirement to record excess statutory reserves. Historically, the requirement to record excess statutory reserves was a useful method to assist regulators in monitoring insurers and helped provide a level of conservatism in the liabilities established for losses and loss adjustment expenses. Current statutes in most states now require audited financial statements as well as actuarial certifications of the reported liabilities for losses and loss adjustment expenses for property and

casualty insurers. Current disclosure requirements provide regulators with meaningful information with respect to insurer's reserving practices. Therefore the recording of an arbitrary reserve is no longer justified.

32. Excess statutory reserves do not meet the definition of a liability as set forth in Issue Paper No. 5. The conclusion reached in this issue paper is consistent with the Statement of Concepts which states:

Liabilities require recognition as they are incurred. Certain statutorily mandated liabilities may also be required to arrive at conservative estimates of liabilities and probable loss contingencies.

33. This conclusion is consistent with Issue Paper No. 55 which requires management of the insurer to record their best estimate of the liability for losses and loss adjustment expenses. GAAP does not require excess statutory reserves to be recorded and therefore the conclusions reached in this issue paper are consistent with GAAP.

Policies with Coverage Periods Equal to or in Excess of Thirteen Months

34. This issue paper adopts current statutory guidance for policies with coverage periods equal to or in excess of thirteen months and extends the guidance to cover warranty insurance reserves. This is consistent with GAAP which requires that premiums from contracts for which the period of risk differs significantly from the contract period be recognized as revenue over the period of risk in proportion to the amount of insurance protection provided.

High Deductible Plans

35. Current statutory guidance for high deductible plans is limited and practice varies. Some insurers attempt to bifurcate the amounts collected into premiums for the risks above the deductible and an administrative fee for administering the claims below the deductible. This has the effect of eliminating a portion of premium taxes that would otherwise be paid. Some insurers report the claims under the deductible limit as losses while others do not, and some insurers report the deductible reimbursement as premium while others do not. This issue paper requires insurers to record as a reduction of paid losses, all amounts that represent contractual reimbursements to the insurer.

36. Treatment of claims below the deductible limit for high deductible plans as a reduction of paid losses of the insurer is consistent with the insurer having no underwriting risk associated with the deductibles. Although the existence of the deductible does not eliminate the insurer's obligation to pay the claim the accounting treatment afforded the deductible is similar to ceded reinsurance balances.

Environmental Exposures

37. This issue paper adopts current statutory guidance for environmental exposures. While GAAP does not specifically address environmental exposures the Securities and Exchange Commission has issued guidance for public companies that is consistent with the current statutory requirements.

Policyholder Dividends

38. This issue paper is consistent with current statutory guidance for policyholder dividends for property casualty insurers. GAAP, for the recognition of policyholder dividends, is to accrue an estimate for amounts that will be paid even though they have not yet been declared by the board of directors. The accounting in this issue paper is a departure from Issue Paper No. 5 and from GAAP. However, codifying current statutory accounting was deemed appropriate as there are no apparent solvency concerns as a result of current statutory accounting for policyholder dividends.

Disclosure

39. The disclosure requirements of this issue paper provide for disclosures in those circumstances where the accompanying exhibits are not part of the company's financial statements (e.g., annual audit report) and are not intended to provide duplicative presentation in the annual statement filings.

Drafting Notes/Comments

- Reinsurance is addressed in *Issue Paper No. 75—Property and Casualty Reinsurance*.
- Title insurance is addressed in *Issue Paper No. 57—Title Insurance*.
- Discounting is prohibited by Issue Paper No. 55 unless it is specifically provided for in a specific issue paper.
- Financial guaranty insurance is addressed in *Issue Paper No. 69—Financial Guaranty Insurance*.

RELEVANT STATUTORY AND GAAP GUIDANCE**Statutory Accounting**

40. The P&C Accounting Practices and Procedures Manual, Chapter 10, Losses, provides the following guidance:

Structured Settlements

If the company has purchased annuities, of which the company is owner and payee, to fund future payments that are fixed or determinable by settlement provisions or by workings of statutes, the present value of such annuities shall be disclosed in the annual statement as assets under “Aggregate write-ins for other-than-invested assets.” Income from these annuities is to be reported as “Aggregate write-ins for miscellaneous income” on Page 4 of the annual statement. The company shall not treat such transactions as paid losses. If the company discounts the applicable loss reserve as a result of the purchase of such annuity, the appropriate discounting disclosure is required (see Loss Reserve Discounting below.)

If the claimant is the payee, the company may treat such transactions as paid losses. Appropriate disclosure of the contingent liability for such amounts must be disclosed in Notes to the Financial Statements of the annual statement.

Only if the company assigns the obligation to make periodic payments to a third party and obtains a full and complete release from the claimant, may the claim be treated as a paid claim without additional disclosure.

Claims-Made Policies

In recent years some companies have issued “claims-made” policies for some liability coverages. Under these policies, losses are recognized as they are reported to the company rather than as they occur. The annual statement instructions have some special provisions for reporting losses under these policies.

These policies frequently have extended reporting period provisions. The IBNR reserve should include provision for claims which will be reported under the extended reporting period coverage.

Loss Reserve Discounting

Present value discounting of property and casualty loss reserves is not a generally accepted statutory accounting practice except as respects fixed and determinable payments such as those emanating from workers’ compensation tabular indemnity reserves (defined below) and long-term disability claims. In the event, however, that an insurer is authorized by its domiciliary state to discount its liability loss reserves, the insurer should complete annual statement Schedule P as required by the annual statement instructions. The insurer should also complete the annual statement Note — Discounting of Liabilities for Unpaid Losses or Unpaid Loss Adjustment Expenses as required by the annual statement instructions.

Tabular reserves are indemnity reserves that are calculated using discounts determined with reference to actuarial tables which incorporate interest and contingencies such as mortality, remarriage, inflation, or recovery from disability applied to a reasonably determinable payment stream. This definition shall not include medical loss reserves or any loss adjustment expense reserves.

Statutory Reserve Computation — Schedule P

Minimum statutory reserve calculations are made for auto liability, other liability, medical malpractice, workers' compensation, and credit coverages. Except for credit, the statutory reserve amount is calculated by comparing total losses and loss expenses incurred to earned premiums. Required ratios are set forth in the annual statement instructions for Schedule P.

The statutory reserve for credit is computed in accordance with annual statement instructions.

If a statutory reserve is required, it is shown as a liability on the annual statement. The offsetting charge is to surplus.

41. The P&C Accounting Practices and Procedures Manual, Chapter 12, Unearned Premiums, provides the following guidance:

Claims-Made Extended Reporting Coverage Options Relating to Death, Disability or Retirement

Some claims-made policies provide extended reporting coverage at no additional charge in the event of death, disability or retirement of a natural person insured. In such instance, a policy reserve is required to assure that amounts collected by insurers to pay for these benefits are not earned prematurely and that an insurer with an aging book of business will not show adverse operating results simply because an increasing portion of insureds is earning the benefits for which it has paid.

Insurers providing future benefits under this endorsement should include an incremental premium charge for this coverage. It is important that a proportion of each year's premiums be set aside to fund this liability. The concept of level funding, applied to these grants of extended reporting coverage is that the indicated incremental premium should not vary because an insurer: is just starting to write this business and does not expect any extended reporting options to be claimed in the near future; or has provided this type of coverage for several years and continues to write new business; or has ceased writing substantial amounts of new business but continues to renew existing accounts, expecting to grant increasing amounts of extended reporting coverage options without additional premium. Periodically insurers should re-evaluate the actuarial assumptions underlying the level premium charge based on any relevant information available at that time.

The amount of the policy reserve, when combined with premium appropriate for an on-going book of business, including some charge for extended reporting coverage, should be adequate to pay for all future claims arising from these coverage features. These future claims include those covered by future grants of extended reporting coverage, without diminishing future profitability below normal expectations for on-going business. If the loss rates for providing this coverage to an aging population are low enough to indicate a negative reserve, then the policy reserve should be set at zero.

Reserve estimates will normally assume that a portion of the existing population of insureds will not continue with the same insurer until qualifying for the benefit and exercising the option. Funding should not anticipate vesting or cash values for individual insureds unless specifically provided by contract.

These additional factors should be considered in estimating the reserve:

1. Loss trends;
2. Time value of money;
3. Nonrenewal rates;
4. Age and tenure eligibility requirements in the contracts;
5. Age and tenure demographics of the insured population;
6. Mortality considerations;
7. Morbidity considerations;
8. Pricing differentials (if any) related to age of insured;

9. Expected claim costs in relation to age of the insured and the number of years until retirement;
10. Waivers (if any) of charges for specialty changes before retirement;
11. Partial benefits (if any) for termination by either the insured or the insurer prior to retirement; and
12. Other factors that impact the value of future benefits.

Insurers may want to use policy reserving techniques that incorporate elements of life actuarial models in addition to the standard property and casualty actuarial techniques in establishing this policy reserve. This reserve, entitled extended reporting endorsement policy reserve, is most appropriately classified as a component part of the unearned premium reserve and should be considered to run more than one year from the date of the policy. The amount of the policy reserve and the accounting/actuarial policies used in determining it should be disclosed in a footnote to the financial statements. When the policy reserve is reviewed or computed at the close of each accounting period, the change in the policy reserve will flow into the net underwriting gain or loss which will result in a better matching of income and expense over the accumulation period of the policy benefit. In addition, an IBNR loss reserve will be established for those insureds which have exercised the extended reporting coverage option.

This reserve may alternatively be considered a claims reserve and included with unpaid losses by an insurer which has obtained authorization to do so from the commissioner of the state of domicile.

Unearned Premiums - Annual Statement Reporting

The Underwriting and Investment Exhibit of the annual statement shows the development of the unearned premium reserve, by line of business, net of reinsurance premiums assumed and ceded. The exhibit displays unearned premiums for policies running one year or less and for policies running more than one year. In addition, the exhibit shows the unearned premium reserves associated with advance premiums and with rate credits and retrospective adjustments. Advance premiums result when policies have been processed, and the premium has been paid prior to the effective date. These advance premiums are considered to be fully unearned. This unearned premium reserve is reported in the Liabilities, Surplus and Other Funds Exhibit of the annual statement.

As an alternative, companies may accumulate advance premiums in a suspense account until the effective dates of these policies. In this case, companies must then report the amount of the suspense account as a separate liability, Advance Premiums, on Page 3 of the annual statement under aggregate write-ins for liabilities. Using this treatment, companies would not include advance premiums in either written premium or the unearned premium reserve.

Unearned Premium - Warranty Insurance Reserves

For purposes of this rule, warranty insurance is defined as insurance covering mechanical breakdown, service contract agreements or maintenance agreements. At any point before the expiration of the insurance contract or policy the company is required to establish a portion of the premium as a liability to cover the remaining policy term. The unearned premium reserve shall equal the gross premium (after proportional reinsurance) multiplied by the ratio of expected future losses and expenses from the unexpired term of the contract to the total expected losses and expenses under the contract.

42. The NAIC Annual Statement Instructions to Schedule P provide the following guidance with respect to calculating the excess of statutory reserves over statement reserves:

SCHEDULE P - INTERROGATORIES

- (I) Computation of excess statutory reserves over statement reserves. A percentage minimum loss and loss expense ratio is determined which is then applied to the net

earned premiums. The result is then compared to the net losses and loss expenses incurred to give the required excess statutory reserves. If the company has permission from its state of domicile to discount loss and loss expense reserves, the company should compute the excess of statutory reserves over statement reserves using its discounted loss and loss expense reserves rather than the undiscounted reserves. The computation is required only for Auto Liability (Private Passenger and Commercial), Other Liability (including Products Liability), Medical Malpractice, Workers' Compensation, and Credit.

If the company was not in existence for the full five years prior to the statement date, this calculation should be based on the years in which the company was in existence.

Private Passenger Auto Liability and Commercial Auto Liability must be combined before calculating the statutory percentage. Occurrence and claims-made coverages must be combined for Other Liability (including Products Liability) and Medical Malpractice, respectively, before calculating the statutory percentage.

- (a) Other than Credit. The percentage to be used is based on the company's actual loss and expense ratios in the five years immediately prior to the most recent three, provided that at least three of the five years have at least \$1 million in net earned premium. See Schedule P, Part 1, Column 4 for premiums and Column (30) for loss and expense ratios. Use the lowest ratio of losses and loss expenses incurred for these years using only years which have at least \$1 million in net earned premium. If the lowest qualifying ratio is less than 60%, then use 60% (65% for Workers' Compensation). If the lowest qualifying ratio is more than 75%, then use 75%. If at least three of the five years do not have at least \$1 million in net earned premium, use 60% (65% for Workers' Compensation). Round percentage to nearest tenth of one percent. Indicate percentage used. The same percentage should be used for the three most recent years. The excess statutory reserve over the statement reserve is this percentage times the earned premium in Column 4 less the incurred amount in Column 27 for the required years. If negative, enter zero. Do not include premiums and losses for non-proportional insurance shown in Parts IN, IO, IP, and 1Q.
- (b) Credit. Use the following formula and carry the result over to the annual statement.
1. Net unpaid losses on policies expired prior to October 1, current year
 2. Reserve for Losses on policies expired in October, November and December, current year:
 - (a) Net Premiums written on such policies
 - (b) 50% of (a)
 - (c) Net losses paid under such policies
 - (d) Difference (b)-(c)
 - (e) Net losses unpaid under such policies
 - (f) Difference (d)-(e), show zero if negative
 3. Reserve for accrued losses on policies in Force December 31, current year:
 - (a) Net Premiums earned under such policies
 - (b) 50% of (a)
 - (c) Net losses paid under such policies
 - (d) Difference (b)-(c)
 - (e) Net losses unpaid under such policies
 - (f) Difference (d)-(e), show zero if negative
 4. Excess of Statutory Reserve over Statement Reserves 2(f) + 3(f)
(Carry result over to annual statement.)

43. The NAIC Annual Statement Instructions, Note 14, provide the following guidance with respect to disclosure of structured settlements:

14. Structured Settlements

a. Instruction:

If the company has purchased annuities, under which the company is owner and payee, to fund future payments that are fixed or determinable by settlement provisions or by workings of statutes, the present value of such annuities shall be disclosed as assets under "Aggregate write-ins for other-than-invested assets" on Page 2 of the annual statement. The present value of the annuities should be obtained from the issuing life insurance company at the time the annuity is purchased. At the same time, an amortization schedule should be obtained since annual adjustments to the annuity's carrying value are necessary. If the total value of all annuities due from one life insurer equals or exceeds 1 percent of the Company's policyholders' surplus, list: the life insurer's name and location (headquarters); whether the life insurer is licensed in the company's state of domicile (i.e., yes or no is the requested response); and the statement value (i.e., present value) of the annuity(ies). The requested information is illustrated below. In addition, show the aggregate amount (i.e., present value) of annuities due from all life insurers.

<u>Illustration:</u>	Licensed in	Statement
Life Insurance	Company's	Value (i.e.,
<u>Company and Location</u>	State of	Present
	Domicile	Value) of
	<u>Yes/No</u>	<u>Annuities</u>

b. Instruction:

If the company has purchased annuities of which the claimant is payee but for which the company is contingently liable, the amount of such contingent liability shall be disclosed in the Notes to Financial Statements, Note #8. This contingent liability is the amount of the liability due to the various claimants that have been offset by the purchase of the annuity. This liability may be measured by the amortized value (i.e., the present value obtained from the life insurer) of the annuities offsetting the liabilities. If the total value (i.e., present value) of all annuities due from one life insurer equals or exceeds 1 percent of the company's policyholders' surplus, list the life insurer's name and location (headquarters) and the amount of the reserve eliminated when the annuity was purchased. Report the total amount of loss reserves eliminated by annuities. This reserve is measured by the amortized value of the annuities offsetting the reserve. The requested information is illustrated below. In addition, show the aggregate amount (i.e., the present value which is obtained from the life insurer) of annuities due from all life insurers.

<u>Illustration:</u>	Loss Reserves
Life Insurance	Eliminated by Annuities
<u>Company and Location</u>	
i. Total	\$

44. The NAIC Annual Statement Instructions, Note 19, provide the following guidance with respect to discounting:

19. Discounting of Liabilities for Unpaid Losses or Unpaid Loss Adjustment Expenses

Instruction:

State whether or not any of the liabilities for unpaid losses or unpaid loss adjustment expenses are discounted, including liabilities for Workers' Compensation. If the company

is required to respond to this note in the affirmative for non-tabular discounting, it must also respond in the affirmative to Schedule P Interrogatory #5, and complete Columns 31 and 32 of Part 1, Part IA, etc., of Schedule P.

If the answer is in the affirmative, furnish the following information for each line of business affected:

- a. If a tabular basis is used:
 1. Identify table used.
 2. Rate(s) used to discount.
 3. The amount of discounted liability carried in the annual statement.
 4. The amount of tabular discount, disclosed by line of business and reserve category (i.e., case and IBNR).

Definition of Tabular Reserves:

Tabular reserves by accident year are indemnity reserves that are calculated using discounts determined with reference to actuarial tables which incorporate interest and contingencies such as mortality, remarriage, inflation, or recovery from disability applied to a reasonably determinable payment stream. This definition shall not include medical loss reserves or any loss adjustment expense reserves.

- b. If a non-tabular basis is used:
 1. Rate(s) used to discount and the basis for the rate(s) used.
 2. Amount of non-tabular discount disclosed by line of business and reserve category (i.e., case, IBNR, Allocated Loss Adjustment Expense and Unallocated Adjustment Expense).
 3. The amount of non-tabular discounted liability carried in the annual statement.
- c. If the rate(s) used to discount prior accident years' liabilities have changed from the previous annual statement:
 1. Amount of discounted current liabilities at current rate(s) assumption(s). (Exclude the current accident year.)
 2. Amount of discounted current liabilities at previous rate(s) assumption (s). (Exclude the current accident year.)
 3. Change in discounted liability due to change in interest rate(s) assumptions.(1-2)
 4. Amount of non-tabular discount, disclosed by line of business and reserve category (i.e., case, IBNR, allocated loss adjustment expense and unallocated loss adjustment expense).

Illustration:

The Company discounts the liabilities for unpaid losses for Workers' Compensation and Medical Malpractice claims. The Company does not discount unpaid loss adjustment expenses.

Reserves for Workers' Compensation claims have been discounted on a tabular basis using the _____ Table at ____%. The December 31, 19XX and December 31, 19XX liabilities include \$_____ and \$_____ of such discounted reserves, respectively. The amount of discount for case and IBNR reserves at December 31, 19XX is as follows:

	Tabular Discount Included in Schedule P	
Schedule P Lines of Business	Part I *	
	(1)	(2)
	Case	IBNR
(1) Homeowner/Farmowners		
(2) Private Passenger Auto Liability/Medical		
(3) Commercial Auto/Truck Liability/Medical		
(4) Workers' Compensation		
(5) Commercial Multiple Peril		
(6.1) Medical Malpractice – occurrence		
(6.2) Medical Malpractice – claims-made		
(7) Special Liability		
(8.1) Other Liability – occurrence		
(8.2) Other Liability – claims-made		
(9) Special Property		
(10) Auto Physical Damage		
(11) Fidelity, Surety		
(12) Other (including Credit, Accident & Health)		
(13) International		
(14) Reinsurance A		
(15) Reinsurance B		
(16) Reinsurance C		
(17) Reinsurance D		
(18.1) Products Liability – occurrence		
(18.2) Products Liability – claims-made		
(19) Financial Guaranty/Mortgage Guaranty		
(20) Total		
* Must exclude medical loss reserves and all loss adjustment expense reserves		

Medical Malpractice unpaid losses have been discounted on a non tabular basis using rates of from ____% to ____%. The discount rates used are based upon _____. The amount of the discount as of December 31, 19XX and December 31, 19XX respectively is \$ _____ and \$ _____ for losses and \$ _____ and \$ _____ for loss adjustment expense. The amount of discount at December 31, 19XX for case, IBNR, allocated LAE and unallocated LAE is as follows:

B. Non-Tabular Discount

	Non-Tabular Discount *			
Schedule P Lines of Business	(1)	(2)	(3)	(4)
			Allocated	Unallocated
	Case	IBNR	LAE	LAE
(1) Homeowners/Farmowners				
(2) Private Passenger Auto Liability/Medical				
(3) Commercial Auto/Truck Liability/Medical				
(4) Workers' Compensation				
(5) Commercial Multiple Peril				
(6.1) Medical Malpractice – occurrence				

(6.2)	Medical Malpractice – claims-made				
(7)	Special Liability				
(8.1)	Other Liability – occurrence				
(8.2)	Other Liability – claims-made				
(9)	Special Property				
(10)	Auto Physical Damage				
(11)	Fidelity, Surety				
(12)	Other (including Credit, Accident & Health)				
(13)	International				
(14)	Reinsurance A				
(15)	Reinsurance B				
(16)	Reinsurance C				
(17)	Reinsurance D				
(18.1)	Products Liability – occurrence				
(18.2)	Products Liability – claims-made				
(19)	Financial Guaranty/Mortgage Guaranty				
(20)	Total				
* Should include medical loss reserves and all loss adjustment expense reserves, whether reported as tabular or non-tabular in Schedule P					

The rates used to discount Medical Malpractice unpaid losses at December 31, 19XX have changed from the rates used at December 31, 19XX. At December 31, 19XX, the amount of discounted Medical Malpractice unpaid losses, excluding the current accident year, is \$ _____. Had these unpaid losses been discounted at the rates used at December 31, 19XX the amount of discounted liabilities would be \$ _____. The reduction in the discounted liability due to the change in rates is \$ _____.

This illustration neither regulates, permits, nor prohibits the practice of discounting liabilities for unpaid losses or unpaid loss adjustment expenses.

45. Chapter 21, Dividends to Policyholders, of the P&C Accounting Practices and Procedures Manual provides the following guidance with respect to policyholder dividends:

Most state insurance statutes establish the conditions under which dividends may be declared and paid to the policyholder. In general, they provide that dividends to policyholders become liabilities of the company immediately when they are declared by the board of directors. The dividends may be paid only out of unassigned (earned) surplus, in accordance with the rates approved by the board of directors. No dividend may be declared or paid when the surplus of a company is less than the minimum original surplus that is required for the kind or kinds of business which the company is authorized to transact. Also, no dividend may be declared or paid when the payment would reduce the company’s surplus below its required minimum. No dividend may be declared or paid that is contrary to any restriction contained in the company’s articles of incorporation. Certain states have additional restrictions on declaration of dividends to policyholders.

State statutes usually provide that a company’s board of directors or trustees may declare dividends to its policyholders and, in so doing, may establish reasonable classifications or groupings of policyholders and reasonable plans for the distribution of such dividends. This may be done for each general kind and group or class of insurance, and may establish reasonable territorial divisions upon policies expiring during a fixed period.

In establishing the liability for dividends declared and unpaid, the dividend scale approved by the board of directors is applied to all policies in the designated groups or classes.

The amount of policyholder dividends declared and unpaid should be recorded as a liability in the annual statement. Incurred policyholder dividends are reported in the Statement of Income; the amount so reported includes the paid amount (typically recorded as paid in the ledger asset reconciliation) plus the amount accrued at the end of the year (the dividends declared and unpaid), less the amount accrued at the beginning of the year.

46. The NAIC Annual Statement Instructions, Note 24, provide the following guidance with respect to environmental disclosures:

24. Asbestos/Environmental (Mass Tort) Reserves

Instruction:

If the company is potentially exposed to asbestos and/or environmental claims (mass tort), full disclosure of the reserving methodology for both case and IBNR reserves is required. Disclosure of the amount paid and reserved for losses and LAE for asbestos and/or environmental claims, on a gross and net of reinsurance basis, is also required.

Does the company have on the books or has it ever written an insured for which you have identified a potential for the existence of a liability due to asbestos and/or environmental losses? Yes () No ()

If yes, describe the lines of business written for which there is potential exposure, the nature of the exposure or exposures and the company's methodology for reserving for both reported and IBNR losses.

If yes, complete the following information, separately for asbestos-related and environmental losses (including coverage dispute costs) for each of the five most current calendar years on both a gross and net of reinsurance basis (more detailed breakdowns are acceptable):

Beginning reserves:	\$ _____
Incurred losses and loss adjustment expenses:	_____
Calendar year payments for losses and loss adjustment expenses:	_____
Ending reserves:	\$ _____

If yes, complete the following, separately for asbestos-related and environmental reserves:

Does the company hold reserves for unreported claims? Yes () No ()

Does the company hold reserves for future allocated loss adjustment expenses (including coverage dispute cost)? Yes () No ()

Definition of Environmental Loss

Any loss or potential loss (including third-party claims) related directly or indirectly to the remediation of a site arising from past operations or waste disposal.

Examples of Environmental Exposure:

- Chemical Waste
- Hazardous Waste TSD Facilities (Treatment, Storage and/or Disposal)
- Industrial Waste Disposal Facilities
- Landfills
- Superfund
- Toxic Waste Pits
- Underground Storage Tanks

47. The Financial Condition (EX4) Subcommittee adopted the following guidance at the June 7, 1995 meeting of the Subcommittee. The guidance was adopted by the full membership of the NAIC at the September 11, 1995 Plenary Session.

Unearned Premium Reserve - Single or Fixed Premium Policies with Coverage Periods in Excess of Thirteen Months

This rule shall apply to all contracts or policies (contracts), excluding financial guaranty contracts, mortgage guaranty products, and surety contracts that fulfill both of the following conditions:

1. The policy or contract term is greater than or equal to 13 months.
2. The insurer can neither cancel the contract, nor increase the premium during the policy or contract term.

At any valuation date prior to the expiration of the contracts, the company is required to establish an adequate premium reserve, to be reported as the unearned premium reserve for the contracts, on all appropriate annual statement lines and exhibits. Each of the following three tests shall be calculated, for all direct and assumed contracts, in the aggregate by policy year for each line of business with the gross premium reserve being equal to the greatest of the following calculations for each policy year for each line of business. Any reserve credit applicable for reinsurance ceded shall be appropriately reflected in the annual statement with the resulting net premium reserve being established by the company. For reporting net information on the NAIC financial reporting blank, the UPR shall be recalculated on a net basis, which may include appropriate statutory permitted credits for reinsurance, salvage and subrogation.

1. The best estimate of the amounts refundable to the contractholders at the valuation date.
2. The gross premium multiplied by the ratio of (a) over (b), where:
 - (a) equals the best estimate of future expected gross losses and expenses to be incurred during the unexpired term of the contracts; and
 - (b) equals the best estimate of the total expected gross losses and expenses under the contracts.

The future and total expected losses and expenses are to be re-estimated no less frequently than annually, and the most recent estimate of these expected losses is to be used in this test.

3. The amount of the present value of the future expected gross losses and expenses to be incurred during the unexpired term of the contracts, reduced by the present value of the future guaranteed gross premiums, if any. In the calculation of the present value:
 - (a) Discounting is only permitted for future expected losses and expenses, and not incurred but unpaid losses and expenses.
 - (b) Losses and expense provisions may be discounted from the expected date the loss or expense is incurred, not from the expected date of payment, unless such lines of business are permitted to be discounted by the state of domicile.
 - (c) The rate of interest used to calculate the present values shall be reviewed and changed as necessary at each valuation date determined as not to exceed the lesser of the following two standards.
 - (i) if the company's statutory invested assets are at least equal to the total of all policyholder reserves, the company's net rate of return on statutory invested assets, less 1.5%, otherwise, the company's average net

portfolio yield rate less 1.5% as indicated by dividing the net investment income earned, as indicated by line 8 of the Underwriting and Investment Exhibit of the NAIC Annual Statement, by the average of the insurer's current and prior year total assets, as indicated on page 2 of the most currently filed annual financial statement; or

- (ii) the current yield to maturity on a United States Treasury debt instrument maturing in five (5) years as of the valuation date.

For the purposes of tests (2) and (3) above, "expenses" shall include all incurred and anticipated expenses related to the issuance and maintenance of the policy, including loss adjustment expenses, policy issuance and maintenance expenses, commissions, and premium taxes.

This unearned premium methodology will result in premium earning patterns which are inconsistent with the assumptions implicit with the excess of statutory reserves over statement reserve calculation. Therefore, contracts subject to this rule will not be required to be included in such Schedule P Interrogatories calculation.

This section shall immediately apply to all inforce and subsequent business. At the company's option, the impact of this rule with regard to the choice of the interest rate under section 3 may be uniformly phased in over a three year period. The amount phased in shall be limited to the difference between the amounts calculated by using the rate mandated by this rule and the rate actually used by the company for discounting as of 12/31/94, so long as the latter rate does not exceed the constant treasury maturity rate determined by using yields from treasury bills with durations which match the duration of the company's existing liabilities for the inforce which is affected by this rule.

Additionally, where this rule produces a higher reserve than the company would have established through the use of their previous methodology, the company may request a phase in period, of not to exceed three years, from its domiciliary Commissioner. Such phase in period shall only be permitted if the company is able to demonstrate to the satisfaction of the Commissioner that it would not be operating in a hazardous financial condition and that there is not adverse risk to its insureds.

Generally Accepted Accounting Principle

48. The AICPA P&C Audit Guide provides the following guidance:

Accounting Principles

3.29 The specialized industry accounting principles for insurance enterprises are specified in FASB Statement No. 60. The following is a brief discussion of the principles and policies relating to the premium cycle. Readers should refer to the FASB Statement for specific guidance. Most property and liability insurance contracts are classified as short-duration contracts, and this guide generally focuses on such contracts.

Revenue Recognition

3.30 Premiums from a short-duration contract ordinarily should be recognized as revenue over the period of the contract in proportion to the amount of insurance protection provided. This generally results in premiums being recognized as revenue evenly over the contract period. Under a few kinds of contracts, the period of risk differs significantly from the contract period. An example is insurance policies for recreational vehicles issued for an annual period, covering claims that are incurred primarily in the summer months. Under other kinds of contracts, the amount of coverage declines over the contract period on a scheduled basis. In those cases, the premium is recognized as revenue over the period of risk in proportion to the amount of insurance protection provided. Unearned premiums, that portion of the premium applicable to the unexpired period of the policy, are included as an unearned premium reserve within the company's balance sheet.

3.31 As discussed in FASB Statement No. 60, some premiums are subject to subsequent adjustment (for example, retrospectively rated or other experience-rated insurance contracts). In these cases, the premium is determined after the period of the contract and is based on claim experience, or reporting form contracts, for which the premium is adjusted after the period of the contract based on the value of insured property. If, as is usually the case, the ultimate premium is reasonably estimable, the estimated ultimate premium should be recognized as revenue over the period of the contract. It should be revised to reflect current experience. However, if the ultimate premium cannot be reasonably estimated, the cost-recovery method or the deposit method may be used until the ultimate premium becomes reasonably estimable. Under the cost-recovery method, premiums are recognized as revenue in amounts equal to estimated claims as insured events occur until the ultimate premium is reasonably estimable, and recognition of income is postponed until then. Under the deposit method, premiums are not recognized as revenue and claims are not charged to expense until the ultimate premium is reasonably estimable, and income recognition is postponed until that time.

The Loss Reserving and Claims Cycle Accounting Practices

4.01 The specialized industry accounting principles for insurance enterprises are described in *FASB Statement No. 60, Accounting and Reporting by Insurance Enterprises*, *FASB Statement No. 97, Accounting and Reporting by Insurance Enterprises for Certain Long-Duration Contracts and for Realized Gains and Losses from the Sale of Investments*, *FASB Statement No. 113, Accounting and Reporting for Reinsurance of Short-Duration and Long-Duration Contracts*, and *SOP 92-5, Accounting for Foreign Property and Liability Reinsurance*.

4.02 Under GAAP, liabilities for the cost of unpaid claims, including estimates of the cost of claims incurred but not reported, are accrued when insured events occur. The liability for unpaid claims should be based on the estimated ultimate cost of settling the claims (that is, the total payments expected to be made) and should include the effects of inflation and other social and economic factors. Estimated recoveries on unpaid claims, such as salvage and subrogation are deducted from the liability for unpaid claims. A liability for those adjustment expenses expected to be incurred in the settlement of unpaid claims should be accrued when the related liability for unpaid claims is accrued. Changes in estimates of the liabilities resulting from their periodic review and differences between estimates and ultimate payments are reflected in the income of the period in which the estimates are changed or the claim is settled. If the liabilities for unpaid claims and claim-adjustment expenses are discounted (that is, the liabilities are not recorded at their ultimate cost because the time value of the money is taken into consideration), the amount of the liabilities presented at present value in the financial statements and the range of interest rates used to discount those liabilities are required to be disclosed. For public companies, the SEC staff issued *Staff Accounting Bulletin No. 62, Discounting by Property/Casualty Insurance Companies*, which discusses the appropriate accounting and financial reporting when a company adopts or changes its policy with respect to discounting certain unpaid claims liabilities related to short-duration insurance contracts. The SEC issued *Financial Reporting Release No. 20, Rules and Guide for Disclosures Concerning Reserves for Unpaid Claims and Claim Adjustment Expenses of Property-Casualty Underwriters*, which requires additional disclosures concerning the underwriting and claims reserving experience of property-casualty underwriters. The SEC staff also issued *Staff Accounting Bulletin No. 87, Contingency Disclosures on Property/Casualty Insurance Reserves for Unpaid Claim Costs*, which provides guidance concerning those uncertainties surrounding property and casualty loss reserves that may require FASB Statement No. 5, *Accounting for Contingencies*, contingency disclosures and *Staff Accounting Bulletin No. 92, Accounting and Disclosures Relating to Loss Contingencies*, which provides the SEC staff's interpretation of current accounting literature relating to the following:

Offsetting of probable recoveries against probable contingent liabilities

Recognition of liabilities for costs apportioned to other potential responsible parties

Uncertainties in estimation of the extent of environmental or product liability

The appropriate discount rate for environmental or product liability, if discounting is appropriate

Accounting for exit costs
Financial statement disclosures and disclosure of certain information outside the basic financial statements

Salvage and Subrogation

4.30 After a claim has been settled, the possibility of salvage or subrogation may exist. Perhaps the simplest approach to determining the anticipated receivable is to estimate loss reserves using loss data that is net of salvage and subrogation recoveries. Many of the reserving methods for losses and loss adjustment expenses, however, can also be used to estimate salvage and subrogation recoveries.

RELEVANT LITERATURE

Statutory Accounting

- Statutory Accounting Principles Statement of Concepts and Statutory Hierarchy
- Accounting Practices and Procedures Manual for Property and Casualty Insurance Companies, Chapters 10, 11, 12, 14, 17 and 21
- NAIC Annual Statement Instructions to Schedule P
- *Issue Paper No. 3—Accounting Changes*
- *Issue Paper No. 4—Definition of Assets and Nonadmitted Assets*
- *Issue Paper No. 5—Definition of Liabilities, Loss Contingencies and Impairments of Assets*
- *Issue Paper No. 50—Classifications and Definitions of Insurance or Managed Care Contracts In Force*
- *Issue Paper No. 53—Property Casualty Contracts - Premiums*
- *Issue Paper No. 55—Unpaid Claims, Losses and Loss Adjustment Expenses*
- *Issue Paper No. 57—Title Insurance*
- *Issue Paper No. 66—Accounting for Retrospectively Rated Contracts*
- NAIC Annual Statement Instructions to notes 14, 19, and 24
- Minutes to the Financial Condition (EX4) Subcommittee meeting of June 7, 1995.

Generally Accepted Accounting Principles

- *FASB Statement No. 60, Accounting and Reporting by Insurance Enterprises*
- *FASB Statement No. 113, Accounting and Reporting for Reinsurance of Short-Duration and Long-Duration Contracts*
- *AICPA Audit and Accounting Guide: Property & Casualty Insurance Companies*
- *AICPA Statement of Position 94-5, Disclosure of Certain Matters in the Financial Statements of Insurance Enterprises*

State Regulations

- Texas Alternative Calculation for Schedule P reserves for High Deductible Plans
- Arkansas Insurance Department Bulletin 14-93 Guidelines for Implementation of Large Deductible Workers' Compensation Programs
- Florida Regulations FAC Rule 4-189.006 Guidelines for Large Deductible Workers' Compensation Filings
- Massachusetts Regulations 211 CMR 113.04 Workers' Compensation Deductibles Plan

Other Sources of Information

- *Actuarial Standard of Practice No. 20, Discounting of Property and Casualty Loss and Loss Adjustment Expense Reserves*