

## C47 REINSURANCE

### IMPORTANT

The time allowed for this exam is 3 hours.

Total marks: 200

**You must hand in this paper** and any paper used for rough work to the supervisor when you leave the examination room. Failure to do so may result in disqualification.

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### Section A: Multiple-Choice Questions

Question 1. For the following multiple-choice questions, fill in the circle of the letter that identifies the most correct answer.

Example: (A) (B) ● (D)

**DO NOT MARK THE ANSWERS ON THESE PAGES.**

**USE THE FIRST PAGE OF YOUR ANSWER BOOK.**

1. Treaty reinsurance evolved to
  - (A) facilitate the trading of treaties between two insurers.
  - (B) cover individual risks.
  - (C) cover blocks of similar risks grouped together.
  - (D) assist a retrocessionnaire in placing business.
  
2. When a reinsurer wishes to reduce its own liability on a particular risk, it does so by arranging a
  - (A) cession.
  - (B) concession.
  - (C) retrocession.
  - (D) treaty.

3. **A front company is**
- (A) an insurance company usually created for the purpose of writing the parent company's insurance.
  - (B) the company used by some reinsurance pools when one member's name is used for all documentation and all the other participants reinsure that member.
  - (C) a reinsurer from another country that is unlicensed in Canada that undertakes to reinsure Canadian insurance companies.
  - (D) an insurance intermediary that negotiates reinsurance.
4. Which of the following statements is true?
- (A) Insurers are unable to include the reinsurance in the insurer's own financial statements when the reinsurer is licensed in Canada.
  - (B) Reinsurers not licensed in Canada are subject to Canadian regulations.
  - (C) An unlicensed reinsurer has unsatisfactory security.
  - (D) Regulatory authorities require a detailed financial report at least once per year from each licensed reinsurer.
5. In proportional reinsurance,
- (A) a percentage of the risk is transferred to the reinsurer and the reinsurer receives the same percentage of the premium.
  - (B) the insurer pays all the losses up to an agreed amount.
  - (C) the reinsurance premium is always negotiated through a reinsurance broker.
  - (D) there is no relationship between the premium charged and the amount of loss the reinsurer agrees to pay.
6. In non-proportional reinsurance, the portion of the loss payable by the insurer is called its
- (A) assumption.
  - (B) degree of risk.
  - (C) profit.
  - (D) retention.
7. Which of the following is true of a facultative obligatory treaty?
- (A) The agreement is facultative on the part of the insurer but obligatory for the reinsurer.
  - (B) The agreement is obligatory for the insurer but facultative on the part of the reinsurer.
  - (C) The operation of such a treaty is very similar to that of facultative reinsurance.
  - (D) The agreement is facultative for both the insurer and the reinsurer.
8. Which of the following is a true statement?
- (A) The net account approach is more advantageous than the gross account approach.
  - (B) The per event excess of loss treaty is used strictly in the casualty classes.
  - (C) The per risk excess of loss treaty is used mainly in the property classes.
  - (D) The per risk excess of loss treaty must be used separately—not in conjunction with other treaties.

9. An unearned premium is
- (A) an asset on the books of the insurer.
  - (B) the portion of the original premium equal to the expired time.
  - (C) the portion of the original premium for the unexpired term.
  - (D) used as a cushion in case of a high loss ratio.
10. The financing function of reinsurance can be provided by many types of reinsurance EXCEPT
- (A) a quota share treaty.
  - (B) a surplus treaty.
  - (C) a proportional facultative reinsurance.
  - (D) non-proportional facultative reinsurance.
11. The type of treaty that protects the insurance company against an unusually high frequency of medium-sized losses and permits the insurer to distribute a loss of one bad year over one or more profitable years to the reinsurer is named a
- (A) spread loss cover.
  - (B) catastrophe excess of loss treaty.
  - (C) stop loss treaty.
  - (D) per risk excess of loss treaty.
12. Which of the following is NOT a function of reinsurance?
- (A) Capacity
  - (B) Resource protection
  - (C) Stabilization
  - (D) Leveraging
13. The Cessions Article specifies when treaty coverage is effective. Which of the following statements is FALSE?
- (A) In quota share treaties, coverage is simultaneous and automatic with the acceptance of the risk by the insurer under its original acceptance.
  - (B) For a surplus treaty, coverage is simultaneous and automatic with the acceptance of the risk by the insurer as soon as the amount of insurance exceeds the insurer's risk retention.
  - (C) Reinsurance may attach prior to the inception date of the treaty if the insurance policy commenced at an earlier date.
  - (D) Reinsurers are bound to any modifications made in the original policy effective from the time the insurer accepts them as long as they conform to the terms and conditions of the original policy.

14. Where an agent erroneously charged a lower premium, the reinsurer may have to share the loss. This is known as
- (A) technical insurance fortunes.
  - (B) facultative obligatory.
  - (C) the premium article.
  - (D) the reinsurance commission article.
15. In proportional reinsurance, the reinsurer
- (A) does not have to contribute to ex-gratia payments.
  - (B) must be compensated if the insurer's agent inadvertently quoted a lower premium.
  - (C) must share in the bad debts of a defaulting agent.
  - (D) pays only its share of losses that are going to be paid by the insurer.
16. Which of the following would NOT be a consideration when transferring a loss portfolio to another reinsurer?
- (A) The past record of loss reserving
  - (B) The class or classes of business
  - (C) The interest that could be earned on the loss reserves before actual payment is made
  - (D) The amount payable in commissions between the two reinsurers
17. Non-proportional treaty reinsurance wordings must specify the limit of the reinsurer's liability once a loss exceeds the insurer's retention. This is addressed in the
- (A) Arbitration Article.
  - (B) Basis of Cover Article.
  - (C) Loss Occurrence Article.
  - (D) Net Retained Lines Article.
18. Which of the following is found only in non-proportional treaty agreements?
- (A) Accounts and Statistics Article
  - (B) Attachment of Cessions Article
  - (C) Follow the Fortunes Article
  - (D) Ultimate Net Loss Article
19. When the reinsurance premium is calculated as a fixed percentage of the insurer's total premium for the classes of business covered under the treaty, the insurer's total premium is termed
- (A) gross net premium income.
  - (B) variable basis of rating.
  - (C) flat premium.
  - (D) minimum premium.

20. What amount would the reinsurer pay if the insurer has a catastrophe excess of loss treaty for \$10,000,000 excess of \$5,000,000 and as a result of an ice storm suffers a series of losses totaling \$7,000,000?
- (A) \$2,000,000
  - (B) \$7,000,000
  - (C) \$5,000,000
  - (D) No payment would be made
21. The reinsurer is sometimes prepared to waive a particular exclusion if complete underwriting information on the specific risk is submitted and approved by the reinsurers. This is known as a
- (A) cession.
  - (B) retrocession.
  - (C) special acceptance.
  - (D) waiver and release.
22. One of the parties to a reinsurance agreement may terminate the agreement if it
- (A) goes into liquidation or has a receiver appointed.
  - (B) loses the whole or part of its paid-up capital.
  - (C) merges or passes under another financial control.
  - (D) all of the above
23. Which of the following is INCORRECT regarding the Alterations Article?
- (A) Both parties to the treaty can make changes whenever both agree to do so.
  - (B) Alterations to the treaty are made only at an annual review.
  - (C) Alterations to the treaty may be made by a formal addendum accepted by both parties.
  - (D) Alterations to the treaty may be made in the form of an exchange of correspondence between both parties.
24. The article that sets out the procedure to be adopted in the event the two parties to a treaty are unable to agree on an operational question is known as the
- (A) Intermediary article
  - (B) Books and Registers article
  - (C) Insolvency article
  - (D) Arbitration article
25. If a first surplus treaty has capacity to a maximum of two lines or \$8,000,000, whichever is less and under the quota share treaty the maximum capacity of \$5,000,000 is used, what is the maximum capacity available under the first surplus treaty?
- (A) \$ 8,000,000
  - (B) \$ 3,000,000
  - (C) \$10,000,000
  - (D) \$ 5,000,000

26. An insurer has a quota share treaty in which 25% of a maximum capacity of \$4,000,000 is ceded to reinsurers. On a specific risk where the maximum capacity of the quota share has been used, facultative reinsurance has been arranged for \$2,000,000 excess of \$2,000,000. How much will the facultative reinsurer pay in the \$2,000,000 loss?
- (A) \$ 333,333
  - (B) \$1,000,000
  - (C) \$ 0
  - (D) \$ 500,000
27. Choose the reason some proportional treaty reinsurers would NOT permit insurers to place facultative reinsurance on an excess of loss basis.
- (A) They want to be placed in a first loss position.
  - (B) They want to be placed in a primary position.
  - (C) They do not wish to share in all the losses below the retention of the facultative reinsurer.
  - (D) They wish to share in all the losses below the retention of the facultative reinsurer.
28. Which of the following statements is true about casualty reinsurance?
- (A) There is a per risk basis of loss or coverage.
  - (B) An insurer's retention will depend on how much the insurer can afford to lose in a single occurrence excluding claims expenses.
  - (C) An occurrence may involve more than one policy.
  - (D) The retention need not reflect a catastrophe exposure.
29. The amount by which the rate of reinsurance commission exceeds the original commission the insurer paid to its agent is termed
- (A) flat commission.
  - (B) overriding commission.
  - (C) profit commission.
  - (D) sliding commission.
30. Which of the following is not deducted from earned premiums to determine the profit or loss in a profit commission statement?
- (A) Outstanding losses
  - (B) Paid losses
  - (C) Reinsurance commission
  - (D) Written premiums
31. Expressing the excess of loss premium as a percentage of the amount of coverage is called the
- (A) payback approach.
  - (B) proportional approach.
  - (C) rate on line approach.
  - (D) reinstatement approach.

32. The advances in rehabilitating people left with severe disabilities after automobile accidents or injuries in the workplace is an example of
- (A) social inflation.
  - (B) underreserving of larger claims.
  - (C) economic inflation.
  - (D) late reporting of claims.
33. Which of the following statements is true of the Considerations of the Insurer in the reinsurance relationship?
- (A) Underwriting assistance should be limited to a single risk in facultative reinsurance.
  - (B) The value of the reinsurer is that it can handle a claim without ever consulting with the insurer.
  - (C) The willingness of a reinsurer to pay losses at the time of negotiating facultative reinsurance is more important than the ability to pay at the time of the loss.
  - (D) One of the values of a reinsurer is its knowledge of the changing market conditions.
34. Which of the following statements is NOT true of the Considerations of the Reinsurer?
- (A) An increase in profits will cause the reinsurer to restrict its operations.
  - (B) The results of reinsurance agreements create statistical information that is invaluable for the reinsurer's relationships with other insurers.
  - (C) The insurers with which the reinsurer does business should be financially stable.
  - (D) A reduction in profits will cause the reinsurer to restrict its operations.
35. When entering into a relationship with a specific insurance company, the reinsurer would examine FIVE (5) basic areas. Which of the following is NOT one of those basic areas?
- (A) Management
  - (B) Underwriting
  - (C) Mix of business
  - (D) Accounting
36. The document that sets out the intermediary's terms of reference for the insurer and the intermediary and provides the reinsurer with a clear picture of the intermediary's mandate is known as a(n)
- (A) broker's letter of record.
  - (B) sub-broker contract.
  - (C) retrocessionnaire's agreement.
  - (D) insurer's contract.

37. In marine insurance, a stop loss treaty
- (A) requires the insurer to report details of each risk where the amount of risk exceeds the retention.
  - (B) applies when the retention is low enough to expose the treaty to claims on a single original risk.
  - (C) applies to losses arising from the same event that involve more than one interest or class of business.
  - (D) applies in the same way as an aggregate excess of loss treaty.
38. Which of the following is a true statement about aviation reinsurance?
- (A) Liability limits are covered on a split basis: bodily injury and property damage limits for passenger legal liability and third-party liability.
  - (B) General aviation insurance risks tend to be heterogeneous.
  - (C) Quota share treaty is used extensively in the aviation market because it provides the best spread of risk for the reinsurers.
  - (D) Surplus treaty is the favoured method of reinsuring aviation risks.
39. Which of the following is true of life reinsurance?
- (A) A part of the life premium is used to set up reserves to meet the eventual claim.
  - (B) Most life policies are short-term and are generally cancellable.
  - (C) Some types of life policy offer neither protection nor savings.
  - (D) The annual premium for most life policies varies throughout the period.
40. Which of the following is NOT true of hail insurance or reinsurance?
- (A) Hail insurance may include coverage for insect damage.
  - (B) Hail insurance on growing crops is designed to provide protection during the entire growing period, including harvest.
  - (C) Quota share treaties are often used in hail business.
  - (D) Stop loss treaties are never used in hail business.

(2 marks each = 80 marks)

## Section B: Narrative Questions

Question 2. Explain how the following types of treaty function in property reinsurance.

- (a) Quota Share Treaty (10 marks)
- (b) Surplus Treaty (10 marks)

continued on next page

- Question 3. Briefly explain the purpose of and outline the provisions usually found in the following proportional treaty wordings:
- (a) Attachment of Cessions Article (10 marks)
  - (b) Follow the Fortunes Article (10 marks)
- Question 4. (a) Identify SIX (6) circumstances under which the special termination provision found in most reinsurance treaties may be invoked. (8 marks)
- (b) Briefly describe the following articles frequently found in proportional and non-proportional reinsurance treaties:
- (i) Insolvency Clause (8 marks)
  - (ii) Signature Clause (4 marks)
- Question 5. Discuss what an insurer would consider in deciding whether to use a reinsurance intermediary in the reinsurance process. (20 marks)
- Question 6. Describe the following types of non-proportional treaty used in marine insurance.
- (a) Working Excess of Loss (5 marks)
  - (b) Reporting Excess of Loss (6 marks)
  - (c) Aggregate Excess of Loss (5 marks)
  - (d) Backup Contracts (4 marks)

### Section C: Application Question

- Question 7. You are a reinsurance broker. One of your clients is a regional farm mutual insurer wishing to expand into the casualty business on a national basis. The insurer will be relying on your expertise in arranging its first reinsurance cover. As part of the consultative process, you have been asked for the following information.
- (a) Explain the differences between registered and unlicensed reinsurers for your client. (10 marks)
  - (b) Why would a reinsurer choose not to become licensed in Canada? (5 marks)
  - (c) Under what circumstances might your client consider buying coverage from an unlicensed reinsurer? (5 marks)

