

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.

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. The trading of reinsurance treaties between insurers is referred to as

- (A) facultative reinsurance.
- (B) reciprocal exchange.
- (C) retrocession.
- (D) treaty reinsurance.

2. A retrocession is

- (A) a cession by a reinsurer.
- (B) a cession by an insurer.
- (C) an additional cession on the same risk to the same reinsurer.
- (D) the termination of a reinsurance contract.

3. An insurance company that is created usually for the purpose of writing the parent company's own insurance is called a
- (A) brokerage house.
 - (B) captive insurance company.
 - (C) fronting company.
 - (D) reinsurance pool.
4. Reinsurers from other countries that are not licenced in Canada may undertake to reinsure Canadian insurance companies. Such reinsurance is considered
- (A) licenced.
 - (B) licenced but not registered.
 - (C) registered and licenced.
 - (D) unlicenced.
5. When an insurer reinsures a part of its liability, it can be said to be
- (A) assuming business.
 - (B) attaining business.
 - (C) ceding business.
 - (D) retroceding business.
6. In insurance terminology, a "cession" is the
- (A) amount of insurance a reinsurer cedes to another reinsurer.
 - (B) amount of insurance an insurer keeps for its own account.
 - (C) amount of insurance an insurer transfers to a reinsurer.
 - (D) maximum amount of insurance an insurer can write.
7. Which of the following is NOT another term for retention?
- (A) Attachment point
 - (B) Excess of loss
 - (C) Excess point
 - (D) Priority
8. A treaty in which the retention is set above the maximum limit for which the insurer issues a policy is referred to as a
- (A) buffer or shock layer treaty.
 - (B) clash layer treaty.
 - (C) stop loss treaty.
 - (D) working layer treaty.

9. Which of the following is NOT a function of reinsurance?
- (A) Capacity
 - (B) Financing
 - (C) Fiscal advantages
 - (D) Resource protection
10. On an insurer's balance sheet, the amount of the liability that the insurer would have to return to its policyholders if all the policies were cancelled as of that date is known as the
- (A) earned premium reserve.
 - (B) unearned premium reserve.
 - (C) outstanding loss reserve.
 - (D) paid up capital reserve.
11. Which of the following is an advantage of using quota share reinsurance for financing?
- (A) A volume of business is being retained that would otherwise be given away.
 - (B) The cost to the insurer is relatively low.
 - (C) There is no dilution of shareholders' equity.
 - (D) There is no need to study long-term requirements.
12. The most important function of reinsurance is to afford protection for such resources as
- (A) capital and outstanding loss reserve.
 - (B) capital, surplus, and loss ratio.
 - (C) loss ratio and underwriting capacity.
 - (D) loss ratio and outstanding loss reserve.
13. The way in which the business is to be transferred to the reinsurer is addressed in the
- (A) Attachment of Cessions Article.
 - (B) Basis of Cession Article.
 - (C) Follow the Fortunes Article.
 - (D) Portfolio Article.
14. Treaty reinsurance wordings must specify when coverage becomes effective for an individual risk ceded to the treaty. This is addressed in the
- (A) Accounts and Statistics Article.
 - (B) Attachment of Cessions Article.
 - (C) Basis of Cession Article.
 - (D) Portfolio Article.

15. If the results of proportional reinsured business have been profitable, the insurance company may also seek an additional amount of commission known as
- (A) flat commission.
 - (B) profit commission.
 - (C) sliding scale.
 - (D) overrider.
16. A provision by which policies that take effect prior to the inception of a treaty can be covered under the treaty is called
- (A) portfolio of cessions in force.
 - (B) ex gratia payments.
 - (C) cash loss limit.
 - (D) unearned premium.
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 only found in proportional treaty agreements?
- (A) Alterations Article
 - (B) Arbitration Article
 - (C) Follow the Fortunes Article
 - (D) Insolvency Article
19. Which of the following is only found in non-proportional treaty agreements?
- (A) Books and Registers Article
 - (B) Exclusions Article
 - (C) Net Retained Lines Article
 - (D) Period and Termination Article
20. In non-proportional treaty agreements 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, it is known as the
- (A) flat premium.
 - (B) flat rate premium.
 - (C) variable rate premium.
 - (D) sliding scale rate premium.

21. 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
22. The effective date of cancellation for treaties negotiated between the insurer and reinsurer would be found in the
- (A) Insolvency Article.
 - (B) Cancellation Article.
 - (C) Arbitration Article.
 - (D) Period and Termination Article.
23. 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) forfeiture agreement.
 - (B) special acceptance.
 - (C) waiver agreement.
 - (D) waiver and release.
24. Which of the following is true under the Books and Registered Article?
- (A) The reinsurer or its representative may examine all the books and records of the insurer.
 - (B) The expense for the inspection is always borne by the insurer.
 - (C) The audit is carried out after normal business hours.
 - (D) An audit is usually informal.
25. The blending of different methods and types of reinsurance to achieve varying degrees of the four functions of reinsurance and to enable the insurance company to pursue its goals and objectives commensurate with the cost and availability of the reinsurance is known as a(n)
- (A) reinsurance program.
 - (B) quota share treaty.
 - (C) per risk excess of loss treaty.
 - (D) insurance program.

26. Under a Quota Share Treaty with a capacity of \$5,000,000, an insurer's retention at 70% and reinsurance at 30%, how much is ceded?
- (A) \$1,500,000
 - (B) \$2,000,000
 - (C) \$3,500,000
 - (D) \$5,000,000
27. A casualty quota share treaty, where the limits are stated in the form of a warranty,
- (A) requires an insurer to issue policies for a stated amount of coverage.
 - (B) restricts an insurer from issuing policies for limits greater than the maximum stated limit.
 - (C) is a separate treaty granting reinstatements in addition to those under the basic treaty.
 - (D) usually has a stated limit per risk.
28. Which of the following is NOT a consideration on which the insurer will base its retention?
- (A) Its capital and surplus
 - (B) Its loss ratio
 - (C) Its premium volume
 - (D) Its territory of operations
29. Which of the following is NOT deducted from the earned premiums to determine the profit (or loss)?
- (A) Outstanding losses
 - (B) Paid losses
 - (C) Reinsurance commission
 - (D) Written premiums
30. Which of the following is FALSE of property per risk treaties?
- (A) Future changes must be looked at to see how they will affect the experience for the period for which the treaty cover is being negotiated.
 - (B) The payback and rate-on-line approaches are commonly used in such treaties.
 - (C) The reinsurance rate will generally be on either a flat rate or a sliding scale basis.
 - (D) The reinsurer will want to consider past changes in the insurer's operations during the same period.
31. The tendency of courts over time to award larger amounts in claims settlements is an example of
- (A) economic inflation.
 - (B) late reporting of claims.
 - (C) social inflation.
 - (D) under-reserving of larger claims.

32. Using a wage index rather than a cost of living index is a way to partially offset
- (A) economic inflation.
 - (B) late reporting of claims.
 - (C) social inflation.
 - (D) under-reserving of larger claims.
33. Which of the following is NOT a consideration of the intermediary in the reinsurance relationship?
- (A) Sign satisfactory reinsurance agreements with the insurer and the reinsurer
 - (B) Assist the insurer in selecting a reinsurance company that combines the protection sought by the insurer at a reasonable price and with quality, financially secure reinsurers
 - (C) Monitor activities in the insurance or reinsurance market
 - (D) Maintain confidentiality of the insurer/reinsurer guidelines
34. Which of the following is the best indicator of the financial strength of a reinsurer?
- (A) Past financial statements
 - (B) National profit of a multi-national reinsurer
 - (C) The reports of the financial analysis services
 - (D) The percentage of the reinsurer's business that it retrocedes
35. The most important consideration that an insurer should weigh when negotiating with a treaty or facultative reinsurer is the
- (A) short term basis of the relationship.
 - (B) willingness of the reinsurer to pay the losses at the time of the negotiations.
 - (C) ability of the reinsurer to pay the losses at the time of the loss.
 - (D) cheapest price at the time of the negotiations.
36. One of the two basic areas that an insurer will examine in selecting its reinsurance market is
- (A) accounting.
 - (B) management.
 - (C) underwriting.
 - (D) financial strength.
37. The largest single values of any objects insured in the marine reinsurance market are represented by
- (A) oil risks.
 - (B) cargo.
 - (C) war risks.
 - (D) hulls.

38. In marine reinsurance, the disadvantage of rigidity found in proportional treaty reinsurance may be eased slightly by using
- (A) variable quota share treaties.
 - (B) excess line treaties.
 - (C) excess of line treaties.
 - (D) catastrophic loss treaties.
39. Which of the following is FALSE 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 long-term and are generally non-cancellable.
 - (C) Some types of life policy offer both protection and a form of savings.
 - (D) The annual premium for most life policies varies throughout the period.
40. Which of the following is FALSE of hail insurance or reinsurance?
- (A) Facultative reinsurance cannot be used if the number of cases of unacceptably heavy concentration of risk for the insurer is relatively small.
 - (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. (a) Define **insurance** and **reinsurance**. (5 marks)
- (b) Briefly describe the nature and operation of each of the following reinsurance markets:
- (i) Insurance company
 - (ii) Professional reinsurer
 - (iii) Exchange
 - (iv) Captive insurance company
 - (v) State reinsurance company (15 marks)
- Question 3. Compare and contrast facultative and treaty reinsurance. (20 marks)

- Question 4. Briefly explain the following Articles as they apply to non-proportional treaty wordings:
- (a) Net Retained Lines
 - (b) Ultimate Net Loss
 - (c) Loss Occurrence
 - (d) Gross Net Premium Income (5 marks each = 20)
- Question 5. (a) When a new surplus treaty replaces a similar surplus treaty, explain how the premium portfolio is calculated and how the loss portfolio is handled. Include in your answer any special provisions that may apply later. (10 marks)
- (b) Identify FIVE (5) reasons why some types of business are excluded from reinsurance treaty coverages. (10 marks)
- Question 6. Identify and describe the services that an insurer might expect to receive from a reinsurer, in addition to the four basic functions of reinsurance. (20 marks)

Section C: Application Question

- Question 7. (a) You are a reinsurance broker. One of your clients (an insurer) feels that the retention under its quota share treaty is too high and that a per risk excess of loss cover might be arranged to bring the maximum exposure down to a more satisfactory level. How would you explain to your client the advantages of the "gross account" approach as contrasted to the "net account" approach? (10 marks)
- (b) (i) You are an insurer calculating your profit commission for the year 2002 based on your treaty proportional reinsurance portfolio with the Reliable Reinsurance Corporation. Your contract is written on a 20% profit commission basis. Calculate the amount of your cheque based on the following information. Show your calculations.
- | | |
|-----------------------------|--------------|
| Reinsurance commission | \$ 1,250,000 |
| Reinsurance premium earned | \$ 5,000,000 |
| Paid and outstanding losses | \$ 2,500,000 |
| Reinsurer's expenses | \$ 250,000 |
- (5 marks)
- (ii) If your contract provided for the carrying forward of deficits from previous years and in 2001 you had a loss of \$600,000, how much would you receive as a profit commission? Show your calculations. (5 marks)

