Introduction to the P&C Statutory Annual Statement

The Basics
Overview Objective

- To provide a high-level walkthrough of the Property & Casualty (P&C) Annual Statement blank
  - Basic information
  - High-level Statement overview with helpful tips for completion
  - Cross-checks & Validations
  - Key ratios derived from the statement
Basic Information

► Annual Statements
  ► Primary financial reports that State Insurance Departments require of all insurers operating in their jurisdictions

► Regulatory Usage
  ► Critical financial information to assist regulators in monitoring financial solvency
  ► Solvency = adequacy of an insurer’s net financial resources (capital and surplus) to support the nature and volume of business written
  ► Continually evolving to ensure regulators have pertinent information
  ► Provides audit trail of significant transactions – helps with regulatory examinations and desk audits
  ► Serves as data input into IRIS (Insurance Regulatory Information System) and FAST (Financial Analysis & Solvency Tracking) systems (used for monitoring)
Basic Information (cont.)

- Non-Regulatory Usage
  - Rating Agencies – financial condition analysis
  - Bureaus & Statistical Organizations
  - Security Analysts
  - Reinsurers
  - Competitive analysis – mergers / acquisition candidates
  - Income Tax Reporting
  - Rating Agencies / Statistical Organizations (non-regulatory use)
  - Internal financial reporting
Basic Information (cont.)

- NAIC – National Association of Insurance Commissioners
- Annual Statement submission date – March 1st
- State Checklist determines how you must file – individual states may vary from NAIC requirements
- Different guidelines for domiciled and foreign companies
- Insurers submit Annual Statement Information to the NAIC electronically through the internet only – no paper to NAIC
- Some States still require paper only, others paper and electronic
- Page numbers and content are standard
- Page values are presented in dollars (unless otherwise noted)
- Statements are generally built using insurance specific software
Basic Information (cont.)

- Insurance specific software generally creates crosschecks between your pages for data integrity.
- Some Statement pages also list crosschecks on various lines.
Statements are prepared in accordance with SAP (Statutory Accounting Principles)

- More conservative accounting perspective as compared to GAAP (Generally Accepted Accounting Principles)

Statutory accounting objectives differ from GAAP in these ways:

- Balance Sheet – SAP focuses on asset valuation and liability measurement while GAAP addresses performance measurement and matching revenue and expense
- Time Measurement – SAP is point in time solvency measurement while GAAP takes a going concern assumption
- End Users - Statutory statements are designed for Regulators while GAAP statements are intended for investors and management
Basic Information (cont.)

- Annual Statement Preparation requires adherence to:
  - NAIC Accounting Practice and Procedures Manual (SAP guidelines)
  - NAIC Annual Statement Instructions – P&C (preparation guidelines)
  - The Domiciliary State’s prescribed differences from the NAIC SAP
    - Purposes and Procedures Manual of the NAIC Securities Valuation Office
  - Filings to the Regulatory agencies are required Quarterly and Annually (each are a bit different)
Statement Overview

w/ Helpful Tips for Completion
Helpful Tips for Completion

► Annual Statement consists of a number of interwoven financial statements, schedules and exhibits
► Typically more advantageous to complete the supporting exhibits before completing the financial statements
► Suggested order of completion is not intuitive
► Have available: prior year annual statement, general ledger trial balance (supporting accounting records also helpful); Practice & Procedure Manual
► Be sure to contact your partner groups early (Investments, Actuaries, Reinsurance Team) if you are going to need information from them to complete your statement.
Jurat Page

- Provides basic company information. Includes:
  - NAIC Company Code (Group Code if part of group)
  - Contact Information

- Directors and Officers
- Signatures
Balance Sheet – Assets – Page 2

- Contains 4 columns – 3 for current year, 1 for prior
- Current year provides:
  - Gross assets
  - Nonadmitted assets
  - Net admitted assets
- Prior year provides only Net Admitted Assets
- Summarizes investment assets into several high-level groupings – can provide a quick investment portfolio view
- Displays insets for some categories
- Allows for two write-in sections
Exhibit of Nonadmitted Assets – Page 13

- Defined: assets not permitted; reflect assets capturing regulatory skepticism as to availability to pay claims
- Identifies surplus impact arising from changes in the amount of nonadmitted assets
- Contains all non-admitted asset balances as of current year and prior year
- Contains an area of write-ins to list all write-ins that have a non-admitted portion
- Will need to tie to the asset page and the income statement page
Provides for the other half of the balance sheet
Also includes insets
Allows for three sections of write-ins:
  - Liabilities
  - Special surplus funds
  - Other than special surplus funds
Comparative of current year and prior year
Just as the Asset page, it provides totals - has an imbedded crosscheck to the Asset page
Statement of Income – Page 4

- Reports operational results for the year
- Contains different lines as compared to the quarterly statement
- Combines an Income Statement with Capital and Surplus details
- Displays total surplus and a guide to help crosscheck the data
- Contains insets, write-ins and prior year data
- These three pages: Assets, Liabilities and Statement of Income tie to and, depending on how you look at it, they either form the basis for all other pages or are the summarization (roll-up) of the Schedules in the Annual Statement
Cash Flow – Page 5

- Summary of insurer’s cash flow from operations plus an overview of investing and financing activities for the year
- Displays three major sections of a cash flow page
  - Cash from Operations
  - Cash from Investments
  - Cash from Financing and Miscellaneous Sources (surplus notes, borrowed money, issue or retire stock)
- There is only one inset (for taxes) and this Schedule has no write-ins
- Rather than write-ins, it uses ‘Miscellaneous’ and ‘Other’ instead
- Provides prior year data
- Displays changes in cash and cash balances
- There is a supplemental disclosure for non-cash transactions
Underwriting and Investment Exhibits

- Pages 6 through 10 – covers all core underwriting data by line of business (also referred to as Annual Statement Line – ASL)
  - Premium, Losses
- Begin to see generic footnotes
- High level reinsurance activity on the underwriting data
- Displays some prior year data
Underwriting and Investment Exhibit: Expenses – Page 11

- Shows 3 categories of major expense functions:
  - Loss Adjustment
  - Other Underwriting
  - Investment
- Loss adjustment and Commission expense detailed by direct, assumed and ceded business
- Management Fee footnote here
- One inset for Guaranty association credits under Taxes, licenses and fees line item
- Data crosschecks with State Pages and Insurance Expense Exhibit
Exhibit of Net Investment Income
Exhibit of Capital Gains (Losses)

- Both are on Page 12
- Breaks out investments into certain asset classes – more detailed than the balance sheet
- Shows where income and gains are occurring
- Expenses are captured at a high-level
- Contains write-ins if necessary
- Contains a more detailed footnote section
Presentation is unique for every company – but most companies choose to follow NAIC examples.

Content and order are regulated.

Provides a narrative outline of major/unusual transactions and events that have occurred in the past year – to prevent misunderstandings.

Provides space to discuss Subsequent Events (Note 22).

Goal to provide written information not otherwise captured or obviously identified through the financial details.

Prescribed examples of required tables provided in Annual Statement Instructions.
Common and standardized questions unique to property and casualty insurers,

Information supplements the financial data within the Statement; focuses attention on other critical areas within the industry,

Mainly ‘Yes’ and ‘No’ questions or investment numbers,

Much of the information is provided by other areas of the company; good to plan ahead for this one,

Pretty self-explanatory
General Interrogatories – Part 2 – Page 16

- Specific to Property and Casualty companies
- Involves information on Accident & Health insurance and reinsurance
- Mainly ‘Yes’ and ‘No’ questions with limited requests for financial numbers
Summary of key performance indicators shown in a comparative format

Some Annual Statement software automatically fills this Form from other Schedules

Risk Based Capital numbers are populated by the company’s RBC statement

Contains a footnote at the bottom
Exhibit of Premiums and Losses – Page 19

- Affectionately known as “The State Page”
- Also commonly referred to as “Statutory Page 14” even though it’s now page 19 in the Statement
- One of the most important schedules in the Annual Statement
- Displays direct underwriting data by line of business
- Contains two footnotes
- Many other Supplemental Reporting Requirements use the State Page as it’s support
- Due to large amount of data, it's good to begin to review this prior to year end
Schedule F – Pages 20-29

- Core reinsurance exhibits
- Contains underwriting and cash balance details by reinsurer
- Reinsurers are separated into multiple categories
- Part 8 determines the Provision for Overdue Reinsurance (Schedule F Penalty) – penalty can arise from: amounts recoverable over 90 days past due, amounts in dispute and certain unsecured exposures.
- Schedule F Penalty varies depending on whether reinsurer is unauthorized, certified or authorized.
Schedule H – Pages 30-32

► Most detailed breakdown of Accident & Health lines of business than seen in other schedules or reports
► Contains requirements for details around direct, assumed and ceded business
Schedule P – Pages 33-93

- Everyone’s favorite
- Extremely detailed underwriting information by line of business and by accident year
- Most detailed way to exhibit loss development and identify relationships between data sets
- Contains direct, assumed and ceded data
- Interrogatories ask for very specific details on sometimes more obscure transactions
Schedule T – Page 94-95

- Displays premiums and losses by state
- Only Schedule to indicate which states your company is licensed/registered to do business in
- Footnote at the bottom indicates how you allocate premiums to the states
- Part 2 of Schedule T relates to specific lines of business and coverages
- Can help Regulators to verify amounts reported in state premium tax returns
Schedule Y – Page 96-98

- Displays company’s organizational chart as well as the same information in “list” form
- Provides insight into intercompany relationships
- Identifies specific transactions occurring between companies
- Displays pooling distribution percentages if companies are part of a pool group
- Schedule provides that the total of all transactions must equal zero
Supplemental Exhibits and Schedules Interrogatory – Page 99

- Simply asks whether various filings will be completed and delivered by designated due dates
- Unless you write a very wide-range of business, will not be answering yes to all filings
- Must provide explanation for required filings responded to with a ‘No’
Each page allowing write-ins only contain three lines.

If you have more than three, the fourth line should read ‘Summary of Remaining Write-ins’.

This Schedule provides the detail for the summary line for all pages.
Summary Investment Schedules – SI01

- Details out the investment groupings
- Quick way to perform risk-assessment of a company’s invested assets
Verification – Investment Schedules – SI02 thru SI15

- Verifications for each of the Investment Asset types
- Identifies the beginning balance of invested assets
- Provides for additions, unrealized gain/loss and other miscellaneous additions/subtractions made
- Can identify impairments, foreign exchange changes, sales and non-admitted amounts
- Shows the ending balance of each invested asset group
Investment Schedules – Pages E

- Schedule A – Real Estate
- Schedule B – Mortgage Loans
- Schedule BA – Other Invested Assets
- Schedule D – Bonds and Stocks
- Schedule DA – Short-term Investments
- Schedule DB – Options, Futures and Other Derivative Instruments
- Schedule DL – Securities Lending Collateral Assets
- Schedule E – Cash Equivalents

Various parts to each schedule detail ‘by investment’ all purchases, sales, proceeds, etc.
Major Crosschecks

- Total Assets = Total Liabilities & Surplus
- Prior year data in current year statement = prior year reported data
- Same schedules and notes completed in current year as was in the prior year
- Non-admitted assets on Asset page = data in Change in Non-admitted Asset page
- Income Statement page surplus = Liabilities & Surplus page surplus
Major Crosschecks (cont.)

- Cash Flow page cash balances and changes = Asset page cash balances and changes
- All insets, write-ins and footnotes are completed
- All General Interrogatory page questions are answered
- All electronic notes are completed
- Verify Reinsurance and Investment schedule totals tie back to the core financial statements
- Jurat page should be complete with signatures
- Crosschecks provided by your statement software complete
IRIS Ratios

- Insurance Regulatory Information System
- Assists oversight of financial condition
- Identifies companies review prioritization
- 13 ratios
- Annual statement software packages calculate
- Unusual values not necessarily indication of financial problems
- 4 or more unusual values likely target company for regulatory review
<table>
<thead>
<tr>
<th>IRIS Ratios</th>
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</thead>
<tbody>
<tr>
<td>1. Ratio 1 – Gross premium written to surplus</td>
</tr>
<tr>
<td>2. Ratio 2 – Net premium written to surplus</td>
</tr>
<tr>
<td>3. Ratio 3 – Change in net premium written</td>
</tr>
<tr>
<td>4. Ratio 4 – Surplus aid to surplus</td>
</tr>
<tr>
<td>5. Ratio 5 – Two year overall operating</td>
</tr>
<tr>
<td>6. Ratio 6 – Investment yield</td>
</tr>
<tr>
<td>7. Ratio 7 – Gross change in surplus</td>
</tr>
<tr>
<td>8. Ratio 8 – Change in adjusted surplus</td>
</tr>
<tr>
<td>9. Ratio 9 – Adjusted liabilities to liquid assets</td>
</tr>
<tr>
<td>10. Ratio 10 – Gross agent’s balances to surplus</td>
</tr>
<tr>
<td>11. Ratio 11 – One-year reserve development</td>
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<tr>
<td>12. Ratio 12 – Two-year reserve development</td>
</tr>
<tr>
<td>13. Ratio 13 – Estimated current reserve deficiency</td>
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</tbody>
</table>
Helpful Hints

► If any odd transaction were to occur, speak to your external auditors early to avoid disruption in your production
► Set a timeline calendar for when you expect to have certain items/schedules complete
► Include early notice to other groups for when you expect to have their items finished and delivered to you
► Let your printing company know ahead of time when you expect to submit statements to them
Insurance Expense Exhibit

- Used to evaluate the profitability of operations by line of business
- Required of all property/casualty insurers
- Must be filed no later than April 1
- Three major parts:
  - Part I – Allocation to Expense Groups
  - Part II – Allocation to Lines of Business Net of Reinsurance
  - Part III – Allocation to Lines of Business of Direct Business Written
Questions?

Remember, this is a major undertaking and requires a number of different groups to complete – strong collaborative efforts and great partnership will help.

Feel free to contact our Group:

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