Fundamentals of P&C Insurance: What You Need to Know

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Presenters

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President
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Chris Belle is President of ITS, a consulting company that helps carriers and solution providers implement new systems with a suite of services and tools for project management, business analysis, testing, and data conversion that are specific to the insurance industry. Chris has more than 20 years of experience in management & technology consulting in the property & casualty insurance industry. He completed his Project Management Professional (PMP®) certification in 2003 and is a Certified Scrum Master (CSM®). Prior to joining ITS, Chris was Chief Information Officer for a regional P&C carrier based in Texas. He is past president of the Texas IASA chapter and currently volunteers with the International IASA.
Richard Pullara

Market Specialist
Clearwater Analytics

Richard Pullara is currently the Insurance Specialist for Clearwater and joined Clearwater Analytics in early 2012. Richard is a subject matter expert in statutory accounting and investment systems and is currently Clearwater’s liaisons for the NAIC, NASVA, IASA and the Interested Parties Subgroup. In his current role, Richard predominately focuses on helping insurance clients improve the efficiency and accuracy of their investment and accounting operations and processes through the implementation of the Clearwater system. In addition to his current role, Richard assists Product Management, Client Services and Business Development in ensuring that Clearwater’s insurance product maintains best-of-breath status and is clearly communicated throughout the company and industry. Richard frequently writes white papers and presents educational content on the latest changes mandated by the NAIC on statutory investment accounting and system trends. Over his career, Richard has also had titles and served as Director of Investment Accounting and Director of Implementations for software vendors.

Richard has more than 18 years of investment accounting experience including time spent at SS&C, CIBC Oppenheimer and Rochdale Investment Management. He received his MBA in Finance from the University of Hartford and his undergraduate degree in Accounting from York College of Pennsylvania.

#IASASummit
Topics

• Terminology
• Types of Insurance Companies
• Types of Insurance Products
• Types of Insurance Markets
• Operational Functions
Definitions & Acronyms

• **Insurance** - a system of pooling and transferring funds to reduce the risk of financial loss for potential exposures

• **Risk** - Any chance of loss

• **Loss** - Unintentional decline in, or disappearance of, value arising from an accidental occurrence

• **Exposure** - The state of being subject to the possibility of loss

• **Liability** - The state of being legally obligated; responsible
Definitions & Acronyms

- **Property Insurance** - Protection against financial loss due to loss of or damage to real or personal property due to fire, windstorm, hail, etc. (perils)
- **Real Property** - Land and attached structures
- **Personal Property** - Items not attached to land or dwelling, such as clothing, jewelry, etc.
- **Casualty Insurance** - Protection against financial loss due to legal liability as a result of bodily injury (BI) or property damage (PD) resulting from an accident caused by an insured.
Definitions & Acronyms

- **NAIC** – National Association of Insurance Commissioners
- **STAT** – Statutory Accounting Treatment
- **SSAP** – Statement of Statutory Accounting Principles
- **VOS** – Valuation of Securities Task Force
- **Schedule D** – Investment Schedules of an insurance company
Who is the NAIC and why do they matter

- National Association of Insurance Commissioners
  - Consumer protection
  - Promote competitive markets
  - Common set of standards
  - Ensures insurance companies ability to pay future claims.

The NAIC originated in 1871 in an effort headed up by the New York State Insurance Department (“NYSID”) to establish uniformity of states requirements and regulation of the insurance industry.
Key groups of the NAIC

- Executive Committee
- Financial Condition (E) Committee
  - Anything with Finance and Investments
    - SAPWG
    - AICPA Working Group
    - Annual Statement Changes
    - Solvency \ Risked Based Capital
    - Compliance \ State Regulations
Type of insurance companies

- Property and Casualty
- Life
- Health
- Title
- Fraternal
- Separate Accounts

- Yellow
- Blue
- Orange
- Pink
- Brown
- Green
Other types of insurance companies

- Captives
  - Self formed insurance company.
  - Very small
  - Typically not regulated by NAIC
  - Limited Purpose establish with specific objective of financing risks from parent groups.
  - 90% of Fortune 1000 companies have captives
Other types of insurance companies

- Risk Retention Groups
  - Self owned insurance companies
  - RRGs can be captives if domiciled off shore
  - RRGs domiciled in states are regulated.

Most RRGs are regulated as captive insurance companies. However, RRGs domiciled in states without captive law are regulated as traditional insurance companies.
How are Insurance Companies Different

- **Duration**
  - P&C companies, average 1-2 years in duration
  - Life companies, average 10+ years
- **AVR \ IMR**
  - Asset Valuation Reserve – Life Only
  - Interest Maintenance Reserve – Life Only
- **Separate Accounts**
  - Schedule D at Market Value or Book Value only
The Life Insurance Industry

• Pre-Summit Overview Webinar on 1/24/2017 – Claire Burke
Types of P&C Insurance Companies

- Capital Stock
- Mutual
- Reciprocal (or Insurance Exchange)
- Lloyd’s Association
- Captive
How Insurance Companies Make Money

Premium

- Stocks
- Bonds
- Mortgages

Insurance Company

Investment Income

Losses

- Salaries
- Taxes
- Other Costs

Unallocated Expenses
P&C Insurance Product Lines

Personal

Commercial

Insurance is a Contract of Indemnity
General P&C Policy Components

• Declarations Page
• Standard Forms
  ▪ Definitions
  ▪ Insuring Agreement
  ▪ Exclusions
  ▪ Conditions
• Endorsements
Personal P&C Insurance Products

- Renters Insurance
- Homeowners / Dwelling Fire
- Automobile Insurance
- Personal Liability Umbrella
- Boat Owner’s Policy
- Personal Floater or Personal Articles
Commercial P&C Insurance Products

- Commercial Property Insurance
- Commercial General Liability Insurance
- Commercial Auto Insurance
- Commercial Liability Umbrella
- Commercial Package
- Business Owner’s Policy
- Workers’ Compensation
- Ocean Marine
- Inland Marine
- Aviation

- Fidelity Bonds
- Surety Bonds
Functional Model

- IT
- Human Resources
- Marketing & Sales
- Underwriting
- Agency Mgmt
- HR
- Policy
- Reinsurance
- All Systems
- Billing AR/AP/GL
- Claims
- Accounting
- Claims
- Reinsurance

IASA Solution Provider Summit

Processes & Systems
Functions & Staff
# Insurance Markets

<table>
<thead>
<tr>
<th>Market</th>
<th>Distribution</th>
<th>Rates</th>
<th>Forms</th>
<th>Policyholder Protection</th>
<th>State License</th>
</tr>
</thead>
<tbody>
<tr>
<td>Standard / Admitted</td>
<td>Direct or by Agent</td>
<td>State Approved</td>
<td>State Approved</td>
<td>Guaranty Fund</td>
<td>Required</td>
</tr>
<tr>
<td>Non-Standard / Non-Admitted / Surplus</td>
<td><strong>Surplus</strong> Line Broker</td>
<td>Non-regulated</td>
<td>State Approved</td>
<td>None</td>
<td>Not Required</td>
</tr>
</tbody>
</table>
Marketing/Sales vs. Underwriting

• The role of the marketing/sales is to generate insurance premium volume.

• Underwriting’s objectives are:
  ▪ Expand written premiums
  ▪ Increase market share
  ▪ Assure profitable results
Underwriting Responsibilities

• Book of Business
• Reinsurance
• Avoid Adverse Selection
• Agency Relationship
• Capacity/Surplus
Underwriting Process

1. Start
2. Submission
3. Underwriting
4. Rating
5. Quotes
6. Policy Issuance
7. Billings/Collections
8. Policy Lifecycle
9. Meets Criteria
10. Client Approval
Life of a Policy

- Policy Maintenance / Endorsement
- Cancellation
- Reinstatement
- Rewrite
- Renewal
Reinsurance
Reinsurance Function

• Reduces risk of loss
• Overcomes capacity problems
• Assists in underwriting
Types of Reinsurance

- Facultative
- Treaty
- Combination
Claims
What is a Claim?

- A claim is a request for payment of a loss.

- First Party Claim
  - Insured Loss

- Third Party Claim
  - Loss to Another
Claim Process

1. Start
2. First Notice of Loss
3. Coverage Verification
4. Claim Setup
5. Investigation
6. Reserve Adjustment
7. Payments and Settlement
8. Yes (Meets Policy Conditions)
9. NO

Flowchart:
- Start → First Notice of Loss → Coverage Verification
- Claim Setup → Investigation → Reserve Adjustment
- Payments and Settlement
- Decision point (Meets Policy Conditions)
Salvage and Subrogation
Accounting Operations

- Budget and Planning
- Premium Accounting (Accounts Receivable)
  - Agency Bill
  - Direct Bill
- 1099s
- Premium Finance
Accounting Operations, cont.

- General Accounting
- Reinsurance Accounting
- Internal Auditing
- Investment Accounting
Methods of Accounting

- Statutory Accounting
- Generally Accepted Accounting Principles (GAAP)
- Differences Between Stat and GAAP Accounting Practices
- Sarbanes-Oxley Act
How Insurance Companies Make Money

- Premium
  - Stocks
  - Bonds
  - Mortgages

Insurance Company

Loss Ratio
- Losses

Investment Income

- Premium

Unallocated Expenses
- Salaries
- Taxes
- Other Costs

How Insurance Companies Make Money

- Premium
  - Stocks
  - Bonds
  - Mortgages

Insurance Company

Loss Ratio
- Losses

Investment Income

- Premium

Unallocated Expenses
- Salaries
- Taxes
- Other Costs
What is Schedule D?

- General Term used by the insurance industry to describe the quarterly and annual statement for investment-related schedules.
- Schedule D is one of many types of investment schedules that insurance companies produce.
- Schedule D is part of the annual statement.
## Key Schedules

<table>
<thead>
<tr>
<th>Schedule Name</th>
<th>Description</th>
</tr>
</thead>
<tbody>
<tr>
<td>Schedule A</td>
<td>Real Estate owned by the insurance company</td>
</tr>
<tr>
<td>Schedule B</td>
<td>Commercial Mortgage Loans</td>
</tr>
<tr>
<td>Schedule BA</td>
<td>Other Long Term Assets</td>
</tr>
<tr>
<td>Schedule D</td>
<td>Long Term Investments</td>
</tr>
<tr>
<td>Schedule DA</td>
<td>Short Term Investments</td>
</tr>
<tr>
<td>Schedule DB</td>
<td>Derivatives</td>
</tr>
<tr>
<td>Schedule E</td>
<td>Cash &amp; Cash Equivalents</td>
</tr>
<tr>
<td>AVR</td>
<td>Asset Valuation Reserve</td>
</tr>
<tr>
<td>IMR</td>
<td>Interest Maintenance Reserve</td>
</tr>
</tbody>
</table>
What is RBC?

- Method of measuring minimum amount of capital required
- Intended to limit risk by requiring more capital for more risk
- Capital is intended to provide a cushion against insolvency
- Giant formula calculated in Excel, filed annually w/ NAIC & state
- Before RBC fixed capital standard based on state, line of business
What Are the Components?

3 main areas

- Asset risk
  - Focus is different for Life (interest rate) than P&C (credit)
  - This is a much bigger part for Life than for P&C

- Underwriting risk
  - Most of P&C RBC is here

- Other risk
  - catastrophe, fraud, etc.
What Do the Results Mean?

If you don’t meet RBC:

<table>
<thead>
<tr>
<th>Company action</th>
<th>File a report</th>
</tr>
</thead>
<tbody>
<tr>
<td>Regulatory action</td>
<td>Increased scrutiny on report</td>
</tr>
<tr>
<td>Authorized control</td>
<td>Commissioner can take over</td>
</tr>
<tr>
<td>Mandatory control</td>
<td>Commissioner must take over</td>
</tr>
</tbody>
</table>

“Tripwire system”

Confidential filings—cannot view on SNL
Information Technology
IT Responsibilities

- Hardware
- Software
- Data
- Process Flows
- Business Requirements
- Research & Planning
- Disaster Recovery
- Security
Functional Model
Conclusions

• The insurance industry is complicated and has a language all its own.

• The more you learn, the less complicated it appears.

• For success, it is critical for solution providers to:
  ▪ Understand the business model and operations of their customers
  ▪ Communicate effectively

• Recognize that each company is unique and learn how to apply your product/service to meet their unique needs.
Questions?

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