Principles of reinsurance

Objective: To develop in the candidate:
- a knowledge and understanding of the principles of reinsurance and their general application to the different methods of reinsurance;
- a knowledge of the law and regulation relating to reinsurance;
- a knowledge of the basic contract wordings;
- a knowledge of the basic accounting considerations;
- the ability to apply knowledge and skills to practical situations;
- the ability to synthesise different aspects of the syllabus and apply them to given scenarios.

Assumed knowledge and application skills:
It is assumed that the candidate already has knowledge of the basic legal principles and how they apply to insurance. These can be gained from a study of the CII unit P05 Insurance law, or equivalent qualification.

Notes:
- The syllabus will be based on English law and practice.
- The April session will test the legal position as of 31st August of the preceding year.
- The October session will test the legal position as of 28th February of the same year.
- The final exam sitting for this unit is October 2010.
1. The purposes of and parties to reinsurance

1.1 The purpose of reinsurance
Candidates should be able to:
- explain the purpose of reinsurance;
- explain how reinsurance enables the spreading of risk;
- discuss how reinsurance provides risk capacity;
- discuss how reinsurance can provide financial security.

1.2 The parties to reinsurance
Candidates should be able to:
- identify different types of reinsurance buyers and explain their different motivations for purchasing reinsurance;
- identify the different types of reinsurance sellers and explain their different motivations;
- explain the contractual relationship between the parties;
- describe the role of the retrocedant and retrocessionaire;
- describe the role and purpose of the broker/intermediary in the reinsurance buying process.

2. Reinsurance issues

2.1 Methods
Candidates should be able to:
- describe the main features and characteristics of:
  - proportional reinsurance;
  - non-proportional reinsurance;
  - facultative reinsurance;
  - treaty reinsurance;
- explain the differences between these methods of reinsurance.

2.2 Reinsurance premiums
Candidates should be able to:
- outline the definitions of premium income used in reinsurance;
- explain how definitions of premium income apply to reinsurance programmes.

2.3 Retrocession
Candidates should be able to:
- describe how the methods in 2.1 apply to retrocession.

3. Operation of facultative reinsurance

3.1 Facultative reinsurance
Candidates should be able to:
- discuss how the different methods of facultative reinsurance operate.

3.2 Premium calculation
Candidates should be able to:
- differentiate between the premium and claim calculations for proportional reinsurance and excess of loss reinsurance.

4. Operation of proportional reinsurance treaties

4.1 Treaties
Candidates should be able to:
- explain the operation of and differences between the following treaties:
  - quota share;
  - surplus;
  - facultative obligatory.

4.2 Bases of cover
Candidates should be able to:
- discuss the reasons for alternative bases of cover, including:
  - underwriting year;
  - portfolio transfer (clean cut).

4.3 Commissions
Candidates should be able to:
- discuss the following types of ceding commissions:
  - flat rate;
  - sliding;
- discuss the following bases of profit commission:
  - no loss carry forward;
  - loss carry forward;
  - average basis.

4.4 Reserves
Candidates should be able to:
- explain the use of and distinguish between:
  - premium reserves;
  - claims reserves.

4.5 Cession and event limits
Candidates should be able to:
- explain the use of cession and event limits in proportional treaties.

4.6 Loss participation clause
Candidates should be able to:
- explain the use of the loss participation clause in proportional treaties.

5. Operation of non-proportional reinsurance treaties

5.1 Operation
Candidates should be able to:
- explain the operation of the following treaties, including calculation of premium and claims:
  - excess of loss;
  - stop loss;
  - aggregate excess of loss;
- explain the operation of excess of loss for common account.

5.2 Bases of cover
Candidates should be able to:
- discuss the following bases of cover:
  - risks attaching;
  - losses occurring;
  - claims made/losses discovered.
5.3 Risk and catastrophe
Candidates should be able to:
- explain the use of risk excess, including
  • working covers;
  • application to any one risk;
- explain the use of catastrophe excess of loss, including
  application to any one event;
- differentiate between risk excess and catastrophe excess of loss.

5.4 Event limits
Candidates should be able to:
- describe event limits;
- explain their use in non-proportional treaties.

5.5 Reinstatements
Candidates should be able to:
- describe reinstatements;
- describe their use in non-proportional treaties.

6. Legal issues relating to reinsurance
6.1 Legal principles
Candidates should be able to:
- describe the general legal principles applicable to reinsurance.

6.2 Policy terms
Candidates should be able to:
- explain the importance of incorporating the terms of the original policy.

6.3 Construction (interpretation)
Candidates should be able to:
- explain the principles of construction (interpretation) of reinsurance contracts.

6.4 Disputes
Candidates should be able to:
- explain the methods used to resolve reinsurance disputes, including:
  • arbitration;
  • alternative dispute resolution.

6.5 Insolvency and winding-up
Candidates should be able to:
- explain the rights of parties in the event of insolvency and/or winding up of companies as applicable to reinsurance contracts.

6.6 Jurisdiction
Candidates should be able to:
- explain the implications of jurisdiction and applicable law, in relation to reinsurance contracts.

7. Contract wordings
7.1 Formation
Candidates should be able to:
- explain the basis of formation of contract wordings.

7.2 Typical clauses
Candidates should be able to:
- describe the typical clauses found within:
  • proportional property wordings;
  • proportional casualty wordings;
  • proportional marine wordings;
  • proportional aviation wordings;
  • non-proportional property wordings;
  • non-proportional casualty wordings;
  • non-proportional marine wordings;
  • non-proportional aviation wordings.

7.3 Treaty exclusions
Candidates should be able to:
- explain the importance of treaty exclusions and contract specific exclusions; both general and market specific.

8. Placing of reinsurance
8.1 The use of the slip
Candidates should be able to:
- describe the use of the slip in placing facultative and treaty reinsurance;
- describe the structure and content of the slip for proportional and non-proportional reinsurance;
- describe the structure and content of the Market Reform Contract.

8.2 Statistics
Candidates should be able to:
- identify the types of information and statistics used in the placing of reinsurance;
- explain how and why this information would be used.

8.3 Cover notes
Candidates should be able to:
- explain the use and importance of cover notes and closing instructions.

9. Reinsurance markets
9.1 Markets
Candidates should be able to:
- discuss the composition, operation and regulation of the following reinsurance markets in relation to the placing of reinsurance:
  • the London market;
  • other European markets;
  • the North American markets;
  • Asia markets;
  • Bermuda and other major accepting markets.

9.2 Main characteristics
Candidates should be able to:
- explain the main characteristics and operation of the following:
  • captives;
  • retrocessional markets;
  • capital markets;
  • hard/soft markets;
  • terrorism reinsurance markets.
9.3 Market associations
Candidates should be able to:
- describe the role and operation of the principal reinsurance market associations.

9.4 Security
Candidates should be able to:
- explain why the security offered by reinsurers is an important factor for reinsurer selection.

10. Accounting
10.1 Accounting methods for proportional reinsurance
Candidates should be able to:
- describe the accounting methods for facultative and proportional reinsurance, including:
  - calculations of commissions;
  - profit commissions;
  - release of reserves.

10.2 Earned and unearned premiums
Candidates should be able to:
- explain the common methods of calculating earned and unearned premiums.

10.3 Accounting methods for non-proportional reinsurance
Candidates should be able to:
- describe the accounting methods for non-proportional reinsurance, including:
  - deposit or minimum and deposit premiums;
  - adjustment premiums;
  - reinstatement premiums.

10.4 Financial considerations
Candidates should be able to:
- explain the financial considerations regarding reserve deposits, including the payment of interest and alternatives to cash deposits.

10.5 Discounts and deductions
Candidates should be able to:
- explain the operation and effect of discounts, and deductions from premiums, including taxes and brokerage.

11. Property reinsurance
11.1 Underwriting characteristics
Candidates should be able to:
- discuss the underwriting characteristics, including principles of rating, for property reinsurance.

11.2 Methods
Candidates should be able to:
- explain the use of different methods of reinsurance as they apply to property reinsurance.

11.3 Terms and conditions
Candidates should be able to:
- explain the following terms and conditions specific to property reinsurance, including:
  - hours clause;
  - estimated maximum loss;
  - accumulation;
  - loss event definition;
  - cession;
  - event limitation.

12. Casualty reinsurance
12.1 Underwriting characteristics
Candidates should be able to:
- discuss the underwriting characteristics, including principles of rating, for casualty reinsurance, including:
  - long-tail features: IBNR and claims inflation;
  - occupational disease risks;
  - product liability;
  - professional indemnity;
  - North American exposures.

12.2 Methods
Candidates should be able to:
- explain the use of different methods of reinsurance as they apply to casualty reinsurance.

12.3 Terms and conditions
Candidates should be able to:
- explain the following terms and conditions specific to casualty reinsurance, including:
  - key clauses within motor, liability, professional indemnity and workers’ compensation treaties;
  - definition of the loss event in casualty excess of loss cover.

13. Marine reinsurance
13.1 Underwriting characteristics
Candidates should be able to:
- discuss the underwriting characteristics, including principles of rating, for marine reinsurance, including war risks.

13.2 Terms and conditions
Candidates should be able to:
- explain the following terms and conditions specific to marine reinsurance, including:
  - clauses additional to the MAREXEL form;
  - accumulation of interests;
  - war coverage;
  - terms and conditions specific to hull, cargo and energy.

14. Aviation reinsurance
14.1 Underwriting characteristics
Candidates should be able to:
- discuss the underwriting characteristics, including principles of rating, for aviation reinsurance, including:
  - war;
  - hi-jacking and terrorist risks;
  - aviation liabilities.
Reading list
The following list provides details of various publications which may assist with your studies. Periodicals and publications listed will be of value in ensuring candidates keep up to date with developments and in providing a wider coverage of syllabus topics. Any reference materials cited are authoritative, detailed works which should be used selectively as and when required.

Note: The examination will test the syllabus alone. The reading list is provided for guidance only and is not in itself the subject of the examination.

CII/Personal Finance Society members can borrow most of these additional study materials from CII Knowledge Services and may be able to purchase some at a special discount. For further information on lending and discounts go to www.cii.co.uk/knowledge.


Reference materials

Periodicals

Websites
CII Knowledge Services, www.cii.co.uk/knowledge.

Examination guides
Guides are produced for each sitting of written answer examinations. These include the exam questions, examiners' comments on candidates' performance and key points for inclusion in answers. You are strongly advised to study guides for the last two sittings. Please visit www.cii.co.uk to buy online or contact CII Customer Service for further information on 020 8989 8466. Older examination guides are available (for members only) at www.cii.co.uk/knowledge/examguides.