



*“Serving the Insurance Industry”*

October 2, 2000

Mr. John W. Watkins, General Manager  
North Carolina Reinsurance Facility  
PO Box 176010  
Raleigh, NC 27619-6010

**RE: North Carolina Reinsurance Facility Standard Practice Manual  
Section 4., Accounting and Statistical Requirements  
Proposed Revisions - Codification**

Dear Mr. Watkins:

At its July 19, 2000 meeting, the NCRF Board of Governors unanimously approved, in concept, revising NCRF accounting and statistical requirements to comply with codification. This correspondence provides the resulting manual revisions for the Board's formal review and approval.

**BACKGROUND**

The Codification of Statutory Accounting Principles (codification) was a joint effort of the NAIC and regulators to develop a comprehensive guide to statutory accounting principles (SAP) for use by insurance companies, insurers and auditors. The NAIC mandated reporting changes related to this process effective with the first reporting period in 2001. The AIPSO Accounting & Statistical Committee identified three areas which are impacted by codification, and recommended the attached manual revisions, outlined below.

**PROPOSAL**

**Chapter 12 and Exhibit Y**

**Advance Premium Reporting** - As of January 1, 2001, written premium must not be reported until the effective date of the policy. This new requirement should be communicated to the ceding companies to ensure that ceded premium is reported accordingly. Should a ceding company report “advance premium,” it will be identified by AIPSO and *excluded* from the fiscal quarter written premium on the Members Participation (MP) Report. The excluded amount will be displayed as a separate line item on the MP Report for informational purposes only. This allows ceding companies to continue reporting ceded premium using existing procedures, if they so choose. Any reported advance premium will **not** be rejected as an erroneous submission by AIPSO; it will merely be reflected differently on the MP Reports (i.e. excluded from the written premium amount).

## **Chapter 1, Exhibits W, X, and Y,**

**Premium Deficiency Reserve** - Codification requires that a premium deficiency reserve be established when the sum of anticipated losses, LAE, commissions and other acquisition and maintenance costs exceed the recorded unearned premium reserve. This change establishes a reserve which will be calculated by AIPSO and will effect the net results of operation on the MP reports.

## **Chapter 1, Exhibits W, X, and Y**

**Earned But Unbilled Premium (EBUB)** - Adjustments to the premium charged for changes in the level of exposure are generally determined based upon the audits conducted after the policy year has expired. The new NAIC guidelines require companies to estimate the audit premium, the amount generally referred to as earned but unbilled premium (EBUB), and record it as an adjustment to premium. The effect of this entry is an increase to earned premium with a related impact to the net results of operation on the MP report. AIPSO will calculate the EBUB amount on an all companies combined basis, based upon the amount of audit premium reported under premium transaction code 5.

"Attachment 1" outlines AIPSO's treatment of codification for accounting purposes in other residual market mechanisms. These principles were used in developing the accounting-related exhibits for the NCRF manual.

### **IMPACT/EFFECTIVE DATE**

These recommendations are intended to bring the NCRF Members Participation Reports in compliance with the new NAIC guidelines. The NAIC requirements are effective with 2001 reporting; therefore, it is recommended that the changes be implemented with the quarter ending March, 2001 MP Reports.

### **CONTACT**

Should you have any questions concerning codification, please contact Jessie Gale, Manager of Accounting. Please contact me should you have any questions relative to company reporting of ceded business or the Members Participation Reports.

Please keep me advised of the Board's action with respect to this proposal. Thank you.

Sincerely,

David R. Amaral  
Insurance Specialist, Plan Services

pc: M. Bianco, AIPSO  
D. Clark, AIPSO  
E. Davis, NCRF  
J. Gale, AIPSO  
R. Greer, NCRF  
G. Fresch, AIPSO  
C. Kwolek, AIPSO

## ACCOUNTING CHANGES RELATED TO CODIFICATION

The following are the entries that AIPSO will be recording on the Plans' books to account for the changes required by codification:

Advance Premium - At the end of the quarter, AIPSO will reclassify any premium reported with an effective date in a subsequent period to a liability account - Advanced Premium - Liability. This entry will be reversed at the beginning of the next period. If the member companies have already submitted the funds for this premium to the Plan via the settlement of balances, the offset to this entry will be the cash received.

Earned but Unbilled Premium Reserve - In order to be consistent with the presentation of unearned premium on the income statement, lines for earned but unbilled premium prior and current will be established. The change in this reserve will be factored into the earned premium for the period. This reserve will also be shown on the balance sheet.

Premium Deficiency Reserve - The change in the premium deficiency reserve will be treated like the change in loss reserves on the income statement and the reserve will be shown as a liability on the balance sheet.