

**EXAM 6 – CANADA, FALL 2019**

12. (3.25 points)

a. (0.25 point)

Briefly describe the goal of the Facility Association (FA).

b. (0.5 point)

Briefly describe each of the following FA risk sharing mechanisms:

- i. Facility Association Residual Market
- ii. Risk Sharing Pool (RSP)

c. (0.75 point)

Briefly describe one difference and one similarity between the two risk sharing mechanisms in part b. above.

d. (1.25 point)

Identify the five minimum requirements that a risk must meet in order to be eligible for transfer to one of the FA RSPs.

e. (0.5 point)

An insurance company writes private passenger automobile insurance in Ontario. The company decided to cede certain exposures to the RSP at the beginning of calendar year 2019.

Type	Direct Business Earned	Incurred Losses
Policies ceded to RSP	\$50 million	\$100 million
Policies not ceded to RSP	\$950 million	\$600 million
Total	\$1,000 million	\$700 million

Calculate the company's direct loss ratio net of the RSP cession.

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**SAMPLE ANSWERS AND EXAMINER'S REPORT**

<b>QUESTION 12</b>	
<b>TOTAL POINT VALUE: 3.25</b>	<b>LEARNING OBJECTIVE(S): B1-B2</b>
<b>SAMPLE ANSWERS</b>	
<b>Part a: 0.25 point</b>	
<p><u>Sample 1</u> Every person licensed to drive has access to mandatory auto insurance coverage needed to operate a vehicle.</p> <p><u>Sample 2</u> Ensure availability of auto insurance for everyone who can legally operate an automobile.</p>	
<b>Part b: 0.5 point</b>	
<p>i. FARM <u>Sample 1</u> Residual market for drivers who can't find coverage in voluntary market, declined everywhere</p> <p><u>Sample 2</u> Provide insurance for risks that were not able to find insurance in the private market</p> <p>ii. RSP <u>Sample 1</u> Pool where private insurers can cede their unprofitable high risk business and losses shared with industry</p> <p><u>Sample 2</u> Insurers can send risks with inadequate premium to a pool where premium and losses are shared</p>	
<b>Part c: 0.75 point</b>	
<p>Differences: <u>Sample 1</u> FARM: uses FA rates. RSP: uses ceding company's rates.</p> <p><u>Sample 2</u> Insured is aware they are in FA but not aware if they are in RSP.</p> <p>Similarities: <u>Sample 1</u> Both are mechanisms where losses and premiums are shared among insurers in the industry.</p> <p><u>Sample 2</u> Results/losses are paid for by participating members.</p>	
<b>Part d: 1.25 points</b>	
<p><u>Sample</u></p> <ul style="list-style-type: none"> <li>• Must be PPA</li> </ul>	

## SAMPLE ANSWERS AND EXAMINER'S REPORT

- Must not be eligible for FARM
- Must have minimum statutory TPL limit
- Must use approved rates
- Must follow insurer's classification and rating procedures

### Part e: 0.5 point

#### Sample 1

In ON, insurer retains 15% of the exposure from risks ceded into the pool.  
 $(600 + 100 \times 0.15) / (950 + 50 \times 0.15) = 64.23\%$

#### Sample 2

$950,000 + 50,000(0.15) = 957,500$   
 $600,000 + 100,000(0.15) = 615,000$   
Net RSP Direct LR =  $615,000 / 957,500 = 64.23\%$

### EXAMINER'S REPORT

Candidates were expected to understand the objectives and operations of the residual personal insurance markets operating in Canada.

#### Part a

Candidates were expected to discuss the Facility Association's (FA) goal of ensuring the availability of automobile insurance.

Common errors included:

- Not including enough detail such that FA is concerned with automobile insurance, or other related words like "licensed driver", "vehicle owner", etc.
- Not correctly identifying the goal of FA by stating that FA is only concerned with the Risk Sharing Pool (RSP) or Facility Association Residual Market (FARM) risks instead of ensuring auto insurance is available to all owners and licensed drivers of motor vehicles who need the insurance to legally operate those vehicles.

#### Part b

Candidates were expected to briefly describe the two risk sharing mechanisms.

A common error included:

- Not including enough detail on the RSP pooling mechanism. Candidates were expected to mention some aspect of the pool being industry wide, and losses being shared.

#### Part c

Candidates were expected to provide both a meaningful difference and similarity between the FARM and RSP risk sharing mechanisms.

Common errors included:

- Not providing a meaningful comparison, for example, stating "both FA and RSP achieve the goal of FA"

## SAMPLE ANSWERS AND EXAMINER'S REPORT

- Not providing a similarity

### **Part d**

Candidates were expected to identify the five requirements to be eligible to transfer risk to the pool.

There were no common errors. Most of the responses not receiving full credit were due to providing fewer than five requirements.

### **Part e**

Candidates were expected to demonstrate knowledge of the RSP structure in Ontario including calculating the direct loss ratio net of RSP cession.

A common error included:

- Not accounting for the Ontario specific 15% of transferred risks that remain with the ceding company, for both premiums and losses