SECTION IV

Facility, Facility Association (FA), FA Risk Sharing Pool (FARSP)
and *Plan de répartition des risques* (P.R.R.)

The Facility, the FA, the FARSP and the P.R.R. of the *Groupement des assureurs automobiles* are distinct organizations with similar functions.

Premiums, commissions and losses relating to automobile insurance policies transferred to the Facility or to the P.R.R. are to be treated in the insurer's books as negative direct business. Premiums and commissions that have not actually been accepted by the Facility or the P.R.R. at its closing date must be entered into each insurer's books as direct premiums and commissions.

Premiums, commissions and losses transferred to the insurer, according to the allocation made by the Facility or the P.R.R., must be entered as direct business in the insurer's books.

Similarly, premiums and losses received from the FA must also be reported as direct business.

Insurers participating in the P.R.R. are required to make the following adjustments in their books:

(i) Set up a provision for the insurer's portion of the total unearned premiums as at year end on automobile insurance policies transferred to the P.R.R. and accepted as at November 30.

(ii) Set up a provision for the insurer's portion of the total losses reported or unreported and incurred in the last month of the statement year on policies transferred to the P.R.R. as at year end.

(iii) Set up, as receivable from the P.R.R., losses paid on policies that the insurer has transferred to the P.R.R. whether they have been accepted or not as at year end.

Insurers participating in the Facility, the FA and the FARSP should enter into their books an estimate of the premiums written and the losses paid after the organizations' closing dates.

Facility, FA, FARSP and P.R.R. (cont'd)

The following table outlines the details for each entity:

ORGANIZATION	YEAR END	# MONTHS ACCRUAL
Facility	Oct. 31	2
Facility Association	Oct. 31	2
FA Risk Sharing Pool	Oct. 31	2
Plan de répartition des risques	Nov. 30	None required
Unsatisfied Judgement Recovery Fund	Cash basis	None required

The organizations provide the calculations of various provisions and estimates needed to make the above-noted adjustments.

The Facility, the FA, the FARSP, the P.R.R. and the Unsatisfied Judgement Recovery Fund amounts must be included under automobile statistics. At the end of each year, the fund managers will provide insurers with the automobile liability figures representing:

(i) the unpaid assessments for claims paid by the Unsatisfied Judgement Recovery Fund in the year of account; and

(ii) an estimate of the claims awaiting settlement by the funds.

These figures must be included in a worksheet supporting line 19 of page 60.30 for the examiner's review. The Unsatisfied Judgement Recovery Fund has been replaced in Quebec by the *Régie de l'assurance automobile du Québec*.

Letters of Credit / Deposits of Reinsurers

Letters of Credit

For Canadian insurers, to a limited extent, regulators are prepared to recognize approved letters of credit as security maintained in Canada for purposes of reducing the capital otherwise required for unregistered reinsurance.

For Foreign insurers, to a limited extent, regulators are prepared to recognize approved letters of credit as security maintained in Canada for purposes of reducing the assets and margin otherwise required for unregistered reinsurance or a self-insured retention and the total value of assets otherwise required to be maintained in Canada.

Refer to "Section V - Jurisdictional Requirements" for more information on federal requirements and the provincial requirements of Quebec and Ontario. Please also refer to "Section VI - Detailed Instructions" for assistance in completing page 70.38/70.39 and to obtain additional guidance with respect to letters of credit.

Deposits of Reinsurers

Deposits provided by unregistered reinsurers may also be used to reduce the capital/margin otherwise required for unregistered reinsurance, provided that such deposits materially reduce the risk associated with the reinsurer's credit quality.

For additional information on how to complete page 70.38/70.39, refer to "Section VI - Detailed Instructions."

Role of the Chief Agent and Record Keeping Requirements

Please refer to OSFI's Guideline E-4A.

Self-Insured Retention

Self-insured retention (SIR) represents the portion of a loss that is payable by the policyholder, either to the insurer directly or to an intermediary. In some cases, SIRs may be included in the policy declaration or in an endorsement to the policy, stipulating that the policy limit applies in excess of the SIR. When policy wordings are controlled by provincial statute, the SIR arrangement is usually the subject of a separate agreement between the insurer and the policyholder.

Whether the insurer has to pay the entire claim to the policyholder or to a third party (either in accordance with the terms of the policy or the separate agreement), the amount of the SIR portion of the unpaid claim must be reported on page 20.20, line 22 as "Self-Insured Retention (SIR) portion of unpaid claims" with the equivalent amount recoverable reported as an "Other Recoverables" on page 20.10, line 37.

To admit SIR recoverables for statutory test purposes, regulators must be satisfied with the collectibility of the recoverables. Regulators may require acceptable collateral to ensure the collectibility of the recoverables. Any acceptable collateral, for example letters of credit, is subject to a capital charge based on the credit rating of the issuing/confirming bank and the term to maturity of the letter of credit on page 30.77. The total capital requirement from page 30.77 is to be reported on page 30.70, line 50.

Appropriate reserves, including a reasonable IBNR provision, must be maintained with respect to SIR accounts. The adequacy of these reserves should be addressed in the insurer's actuarial report.

Structured Settlements

A structured settlement refers to a contractual arrangement whereby a third party makes periodic payments to a claimant of an insurer.

The periodic payments are normally funded through the purchase by the insurer of an annuity from a life insurance enterprise and are usually arranged so that the payments are tax free in the hands of the claimant.

The insurer may have to report a financial liability and a financial asset on its balance sheet, depending on the type of contractual arrangement, and must disclose the information required in its notes to the financial statements.

There are essentially two types of structured settlements.

Type 1

Type 1 structured settlements have the following characteristics:

a) An annuity is purchased by an insurer who is named as the owner. There is an irrevocable direction from the insurer to the annuity underwriter to make all payments directly to the claimant.

b) Since the annuity is non-commutable, non-assignable and non-transferable, the insurer is not entitled to any annuity payments, and there are no rights under the contractual arrangement that would provide any current or future benefit to the insurer.

c) The insurer is released by the claimant to evidence settlement of the claim amount.

d) The insurer remains liable to make payments to the claimant in the event and to the extent the annuity underwriter fails to make payments under the terms and conditions of the annuity and the irrevocable direction given.

Under this type of structured settlement arrangement, the insurer does not have to recognize a liability to the claimant, nor does it have to recognize the annuity as a financial asset. However, the insurer is exposed to credit risk by guaranteeing the obligation of the annuity underwriter to the claimant.

The insurer should disclose in its notes to the financial statements the terms and conditions, the credit risk and the fair value of this financial guarantee.

Structured Settlements (cont'd)

Any gain or loss should be recorded as an adjustment of incurred claims expense.

The insurer also should not recognize a financial asset at the time of purchase where the terms of the annuity make it commutable in the event the liability to the claimant becomes fully settled or otherwise discharged. In these circumstances, the insurer could record a gain amounting to the residual value after the liability is fully settled.

In this case, the contingent gain should be assessed for disclosure in the notes with respect to its amount, nature and terms and conditions.

Type 2

Type 2 structured settlements differ from Type 1 in that:

a) the annuity is commutable, assignable or transferable; that is to say, there is some form of reversionary interest or continuing right to a benefit for the insurer; and

b) a legal release is not necessarily obtained from the claimant.

The commutation rights of the insurer have the potential for terminating the claimant's right to future payments in advance of the annuity being exhausted.

The extent of the rights held by the insurer sometimes indicates that the insurer has contracted with the annuity underwriter to provide only administrative services with respect to the periodic payments.

Under this type of arrangement, the financial liability must be recognized on the insurer's balance sheet, and the annuity must be recognized as a financial asset.

The annuity should be carried initially at its cost to the insurer, and the liability should be measured in the same manner as other outstanding claim liabilities of similar type.

The insurer should disclose in its notes to the financial statements the terms and conditions, the credit risk and the fair value of the annuities recognized as assets on the balance sheet.

Refer to the section on federal guidelines and bulletins in "Section V - Jurisdictional Requirements."