



COMMONWEALTH OF PUERTO RICO
OFFICE OF THE COMMISSIONER OF INSURANCE

March 10, 1995

Ruling Letter N-E-2-68-95

**TO ALL DOMESTIC INSURERS AUTHORIZED TO DO PROPERTY
INSURANCE BUSINESS**

**Re: Accounting Treatment and Presentation in the Annual Report of
the Insurance Catastrophe Loss Reserve**

Dear Sirs:

In our Circular Letter Number AC-11-9-1360-94, dated October 14, 1994, domestic insurers were notified of the approval of Public Law No. 73, enacted on August 12, 1994, which added Chapter 25 to the Puerto Rico Insurance Code, among other purposes, to require all domestic insurers to establish a reserve for the payment of catastrophe insurance losses ("the catastrophe loss reserve") and to establish a trust ("the trust") to manage the funds of the reserve.

Section 25.030(6) of said legal code provides that the catastrophe loss reserve will be included in the insurer's liabilities, will be counted as an unpaid loss, and will be charged against the assets of the domestic insurer for the financial statements of the insurer. Furthermore, the Commissioner of Insurance is charged with determining the manner in which said reserve will be reported in the insurer's annual statement, provided that such determination will not have any adverse effect on the evaluation parameters used by the National Association of Insurance Commissioners ("NAIC") or other evaluating entities.

Pursuant to the powers granted us by this legal provision, we are hereby stating the guidelines to be followed in the accounting treatment and the presentation of the catastrophe loss reserve in the insurer's records and annual statement¹:

1. The catastrophe loss reserve will be recorded on an accrual basis. Therefore, at the close of each year, insurers will segregate from the unassigned surplus the amount of the catastrophe loss reserve as determined according to Section 25.030 of the Puerto Rico Insurance Code. For the first year, as of December 31, 1994, the reserve determined for 1993 and 1994 will be segregated from the surplus.

2. The presentation on the annual statement will be as follows:

(a) "Assets, Liabilities, Surplus and Other Funds" (Pages 2 and 3 of the annual statement):

(i) As of December 31 of every year, assets subject to the trust will be included in the different lines on page 2 of the annual statement for that year, according to the asset type as of that date.

(ii) Each year the following amounts will be segregated from the unassigned surplus, Line 24C, page 3, "Unassigned funds (surplus)":

(1) The reserve amount for the year being reported in the statement, determined according to said Chapter 25 (see paragraph 1 of this letter for the first year accrual).

(2) The amount of investment income generated by assets subject the trust the year being reported in the statement.

(3) The balance of amounts so segregated from previous periods.

¹For the purposes of this ruling letter all allusions to the annual statement refer to the official form published by the National Association of Insurance Commissioners (NAIC), 1994 edition.

- (iii) This segregated amount will be included in the item shown on Line 22 on page 3 of the annual statement, "Aggregate write-ins for special surplus funds." This segregated amount will be shown on Line 2201, on the same page, using the following description: "Reserve for Catastrophe Insurance Losses pursuant to Chapter 25 of the Insurance Code of Puerto Rico." These amounts will be maintained in these items, and will only be decreased as provided in Section 25.060 of the Puerto Rico Insurance Code.
 - (iv) The amount on line 22, "Aggregate write-ins for special surplus funds," page 3 of the annual statement, will be transferred to line 24C, "Unassigned funds (surplus)," during the accounting period in which the catastrophe losses covered in Chapter 25 of the Puerto Rico Insurance Code occurred, and the amount will be reduced from line 2201, on the same page. The amount to be transferred will be determined according to the provisions of said Chapter 25 and the deed of trust executed by the insurer.
- (b) "Underwriting and Investment Exhibit - Statement of Income" (Page 4 of the annual statement)
- (i) No charge will be made against the year's operations shown on page 4 of the annual statement, for the catastrophe loss reserve determined each year, nor for the transfer as of January 31 of each year of the funds subject to the trust.
 - (ii) The charge to operations will be made in the accounting period during which the catastrophic losses occur, according to the usual procedures established by the NAIC for preparing annual statements. Refer to subparagraphs 2(a)(iii) and (iv), above, for the treatment of surplus accounts.
 - (iii) The following will be recognized as investment income during each year shown in the annual statement:
 - (1) Investment income generated by the funds subject to the trust. This income will be shown on line 8, page 4, "Net investment income earned."
 - (2) Realized capital gains and losses resulting from transactions with the funds

subject to the trust. The gains and losses will be shown on line 9, on page 4, "Net realized capital gains or (losses)."

(3) Unrealized capital gains and losses for funds subject to the trust. These gains and losses will be reported on line 19, page 4, "Net unrealized capital gains or (losses)."

- (c) "Underwriting Land Investment Exhibit - Part 1 - Interest, Dividends and Real Estate Income" (page 6 of the annual statement)

Investment income generated by assets subject to the trust will be included in the different Lines of Part 1, page 6 of the annual statement, according to the type of investment made.

- (d) "Underwriting and Investment Exhibit - Part 1A - Capital Gains and (Losses) on Investments" (page 6 of the annual statement)

Realized capital gains and losses resulting from transactions with assets subject to the trust will be shown on the different Lines of Part 1A, page 6 of the annual statement, according to the type of investment made.

- (e) "Notes to Financial Statements"' (page 18 of the annual statement)

Notes to the financial statements will be included to explain the details of the catastrophe loss reserve and the presentation of the reserve in the annual statement.

- (f) "Schedule of Special Deposits" (page 19 of the annual statement)

Assets subject to the trust will be included on page 19, "Schedule of Special Deposits", of the annual statement, according to the usual procedures established by the NAIC for the preparation of this statement.

- (g) "Schedule D" and "Schedule DA" of the annual statement

Transactions with the assets subject to the trust will be included in "Schedules D" and "DA" of the annual statement, according to the usual procedures established by the NAIC for the preparation of this statement.

All domestic insurers are required to comply strictly with the guidelines set forth in this Ruling Letter,

beginning with the annual statement for 1994. Any violation of these guidelines will be interpreted by our Office as a violation of an order issued by the Commissioner of Insurance.

Very truly yours,

Juan Antonio Garcia
Commissioner of Insurance