2008 SNA- FINANCIAL SECTOR

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Outline of Presentation

- Insurance
- Social security
- Standardized guarantees

Insurance policy

Agreement between insurance corporation and another institutional unit (policyholder)

Policyholder makes payment (premium) to insurance corporation for protection against certain risks

In this way the policyholders protects itself against certain forms of risks, by pooling the risks the insurance corporation aims to receive more from the receipt of premiums than it has to pay out as claims.

Insurance corporation makes payment (claim/benefit) to policyholder when specified insured event occurs

Actual transactions to be partitioned and other transactions imputed to bring out underlying economic process

Insurance

Types of insurance

Non-life insurance

Life insurance

Direct insurance

Reinsurance

Insurance

Life insurance

Is an activity whereby a policyholder makes regular payments to an insurer in return for which the insurer guarantees to provide the policyholders (or in some cases another nominated person) with an agreed sum, or an annuity, at a given date or earlier if the policyholders dies beforehand.

The sum payable under the policy (benefit) may be fixed or may vary to reflect the income earned from the investment of premiums during the period for which the policy operates.

Policy with varying returns, the term “with-profits” life insurance is used.

Insurance

Non-life insurance

Is an activity similar to life insurance except that it covers all other risks, accidents, sickness, fire, etc.

With non-life insurance, a claim is payable only if a specified contingency occurs.

What life and non-life insurance have in common is that

They both involve spreading risk. Insurer receive many small regular payment of premiums from policyholders and pay much larger sums to claimants.

For non-life insurance, the risk are spread over the whole population that takes out the insurance policy.

Insurance

Key difference between non-life and life insurance

Despite the similarity of the activity of them, they are significant differences between them.

Non-life insurance

- Redistribution in current period between all policyholders and a few claimants

Life insurance

- Redistribute premiums paid over a period of time as benefits paid later to same policyholder
- Premiums and claims are Financial transactions

Reinsurance

Just as an individual, institutional unit protects itself against the financial consequences of loss or damage, so an insurance corporation may also protect itself against an unexpectedly large number of claims, or exceptionally heavy claims, by taking out a reinsurance policy with another insurance corporation.

The number of corporations that take out reinsurance are too much but there are a few corporation that specialize in issuing reinsurance policies.

sometimes reinsurance involve transactions with the rest of the world.

Reinsurance

Reinsurance policies are most common for non-life insurance.

two types of reinsurance:

Proportionate reinsurance

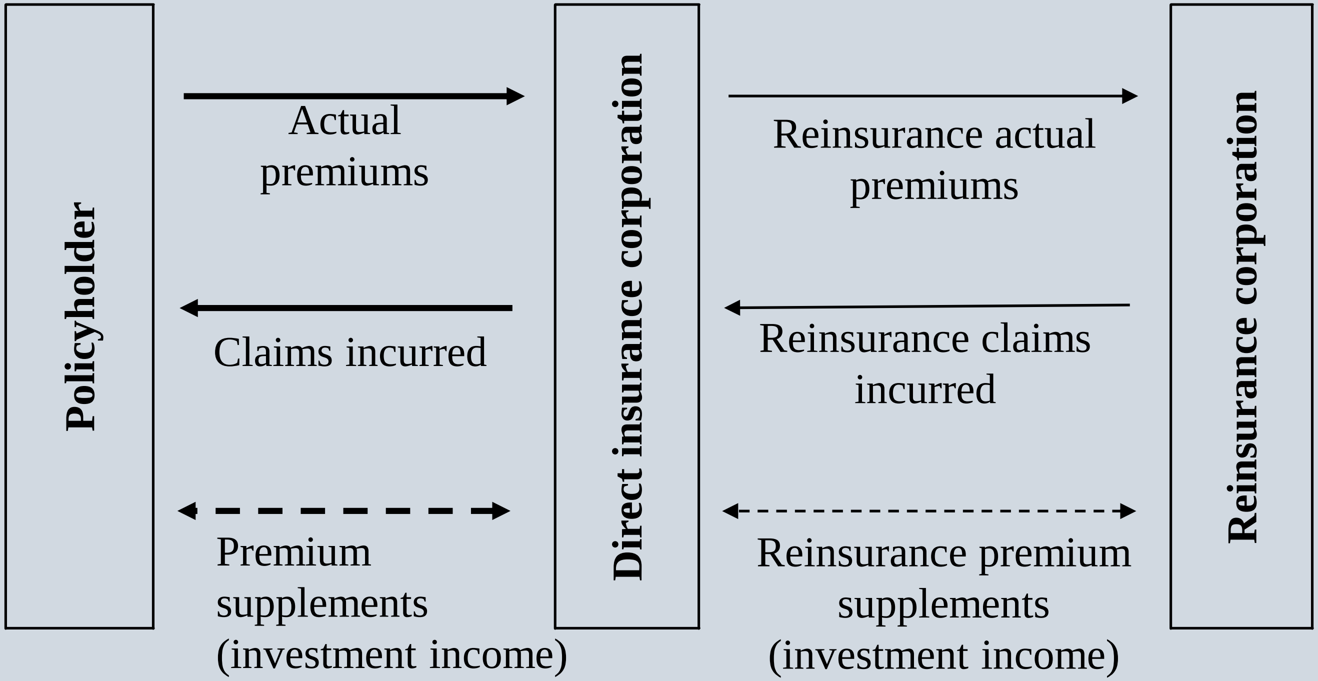
the reinsurer accept an agreed proportionate of the risks

Excess of loss reinsurance

The reinsurer undertakes to pay all losses over a given threshold. If there are no or few claims above the threshold, the reinsurer may pass a share of his profits to the direct insurer.

Insurance

Insurance – transactions involved



Insurance

Terms

Actual premium

- Amount payable to the insurer (or re-insurer) after deduction of all allowances, discounts or bonuses

Premium earned

- The part of the actual premium that relates to cover provided in the accounting period

Unearned premium

- The amount of the actual premium received that relates to the period past the accounting point

Claim (benefit)

- The amount payable to the policyholder by the direct insurer or reinsurer in respect of an event covered by the policy occurring in the period for which the policy is valid

- Claims outstanding
  - Cover claims that have not been reported, have been reported but are not yet settled or have been both reported and settled but not yet paid

Insurance

Terms

- Technical Reserve
    - Amount at disposal of insurance corporations for investment

  Investment income
    - Income from the investment of reserves (usually financial assets)
    - Sometimes in a separate establishment or as a secondary activity(most common example is real estate)
    - Attributable to policyholders

Insurance

Premium supplements

- Investment income attributable to policyholders retained by insurance corporations.

Net premiums

- Premiums earned
- Plus premium supplements
- Minus insurance service consumed by policyholders

Non-life insurance

3 methods to compute non-life insurance output

- Expectations approach
- Accounting approach
- Cost approach

2008 SNA’s methods are an improvement over 1993 SNA’s

- 1993 SNA
- Output of insurance activity estimated using the basic algorithm anchored on the balance of premiums and claims (on accrual basis)
- Could be extremely volatile (even negative) due to massive claims on non-life insurance corporations arising from catastrophic events
- 2008 SNA
- Recommends that output of non-life insurance activity should be calculated using adjusted claims and adjusted premiums supplements

Non-life insurance

Expectations approach

- Ex-ante model
- Insurers consider expectation of claims and premium supplements in setting premiums
- Output
- Premiums earned
- Plus expected premium supplements
- Minus expected claims

Non-life insurance

Accounting approach

- Output
- Premiums earned
- Plus premium supplements
- Minus adjusted claims incurred
- Adjusted claims incurred determined by using claims incurred plus changes in equalization provisions and, if necessary, changes to own funds

Cost approach

- Use if data are not available to apply the expectations and accounting approaches
- Output is estimated as sum of costs (including intermediate costs, labour and capital inputs) plus allowance for "normal profit"

Non-life insurance

Recording of transactions

Value of output

- Production account of insurance corporations
- Intermediate consumption in production account of resident corporations, general government and NPISHs
- Final consumption of households in use of income account
- Exports of goods and services in rest of the world account

Recording of transactions

Insurance services are consumed by those sectors(and the rest of the world) that pay premiums. Estimates of the value of consumption by sector are usually made by allocating the total value of the service in proportion to the actual premiums payable.

Recording claims

The time of recording claims incurred is generally in the period in which the event to which the claim relates took place. This principle is applied even when, in the case of disputed claims, the settlement may take place years after the event concerned.

Non-life insurance

Exception

Where the possibility of making a claim is recognized only long after the event has happened.

- The claim is recorded at the time that the insurance company accepts the liability.

Recording claims

- Normally recorded as current transfers payable by the insurance corporation to policyholders.
- In some circumstances, an insurer corporation may set the level of premiums so low that are not accepted to cover costs and predicted level of claims.
- Happen when the surplus from one line of business is being used to cross-subsidies another line of business.

Note

Catastrophes

- Record claims incurred as capital transfers in capital account
- Criteria: according to the national circumstances(may involve the number of policyholders affected and the amount of damage done)
- Rational: many of the claims relate to serious damage to assets such as dwelling, building and structures.

Life insurance

Output

- Premiums earned
- Plus premium supplements
- Minus benefits due
- Minus increases (plus decreases) in actuarial reserves and reserves for with-profits insurance

If adequate data are not available for the calculation of life insurance according to this formula, an approach base on the sum of costs, similar to that described for non-life insurance, may be used.

As for non-life insurance, an allowance for normal profits must be included.

Life insurance

Recording of transactions

Value of output

- Production account of insurance corporations
- Final consumption of households in use of income account

Reinsurance

Entries in the accounts are similar to those for non-life insurance

- All policy holders are insurance corporations
- Some payment peculiar to reinsurances.

Output=

- Premiums earned less commissions payable
- Plus premium supplements
- Minus benefits due
- Minus both adjusted claims incurred and profit sharing

Social security

Social insurance scheme covering the entire community, or large sections of the community, that are imposed, controlled and financed by government units

Individual must participate in the scheme to receive social security benefits

Two types

- Pension
- Non-pension

Social security

Terms

Social contributions

- Payments to social insurance schemes to make provision for social insurance benefits to be paid
  - Employers
  - Employees
  - Self employed and unemployed

Social insurance benefits

- Social benefit payable because the beneficiary participates in a social insurance scheme and the social risk insured against has occurred

Social security

Output

Separate unit

- Sum of costs of non-market output

No separate unit

- Output is included with the output of the level of government at which it operates

Social security

Recording of transactions

Value of output

- Production account of social security fund
- Final consumption of households in use of income account
- Exports of goods and services in rest of the world account

Employers’ and employees’ social contributions

- Generation of income account
- “Uses” of employers
- Allocation of primary income account
- “Resources” of households
- Secondary distribution of income account
- “Uses” of households
- “Resources” of social security fund

Social insurance benefits (pension and non-pension)

- Secondary distribution of income account

Standardized guarantees

Standardized guarantees have much in common with non-life insurances.

There are three parties involved in these arrangements:

- Debtor
- Creditor
- Guarantor

Either the debtor or creditor may contract with the guarantor to repay the creditor if the debtor defaults

Examples

- Export credit guarantees
- Student loan guarantees

The guarantor expects all the fees paid, plus the investment income earned on the fees and any reserves, to cover the expected defaults along with the costs and leave a profit

Standardized guarantees may be provided by a financial institution, including but not confined to insurance corporations. They may also be provided by government units.

Similar recording as non-life insurance

Thank You