CASUALTY INSURANCE ACCOUNTING AND THE ANNUAL STATEMENT BLANK

BY

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Methods of casualty insurance accounting are not and probably never will become standardized. Opinions differ as to the most efficient methods of compiling accounting data. The annual statement blank, however, is, with a few unimportant exceptions, uniform for all states and, accordingly, whatever accounting methods are adopted must be designed to permit the assembling of the results to conform with prescribed uniform annual statement requirements.

Insurance accounting is a highly specialized branch of accounting and because of this fact text-books on general or commercial bookkeeping and accounting are not of material benefit to the student of insurance accounting other than to ground him in fundamental principles.

The purpose of this paper is to show briefly the application of general bookkeeping and accounting principles to casualty insurance with particular reference to the requirements of the annual statement blank as respects Income, Disbursements and Ledger Assets.

The principles of double entry bookkeeping debit and credit are necessarily the same for all kinds of business enterprises. A debit represents either expense (decrease of proprietorship), an increase in an asset or a decrease in a liability; a credit represents either income (increase of proprietorship), a decrease in an asset or an increase in a liability. It is fundamental, of course, that for each debit there is a corresponding offsetting credit and vice versa. These principles as applied to casualty insurance will be illustrated in connection with consideration of various annual statement items.

The books of account used by insurance companies are basically the same as those used by other business enterprises and consist of Journal, Cash Book and Ledger. In practice, however, various journals are generally used, each for a specific purpose, and the general ledger is used for controlling or summary accounts only and various subsidiary ledgers maintained for recording details. As examples, most companies maintain separate journals for:—

Premiums written
Premiums paid
Losses paid
Expenses paid

The premium and loss journals are in turn further subdivided to show transactions by line of insurance, and in case of premiums written according to kind of premium transaction (Gross written, Not taken, Return and Reinsurance); in case of losses paid according to kind of loss transaction (Gross paid, Salvage received, Reinsurance received).

The distinction between cash book and journal in insurance accounting as well as in the accounting of most large enterprises is not clearly drawn. As a rule, the cash book is in summary or condensed form, the supporting details being carried in various so-called journals. An illustration in connection with accounting for paid premiums is given at a later point.

A simple illustration of a general ledger controlling account supplemented by subsidiary ledger accounts is the collateral loan account. The general ledger would show only the transactions affecting the general account and a subsidiary ledger would carry the details of the accounts with the individual borrowers.

The most important divisions of the annual statement blank from the financial standpoint are as follows:

1. Income and Disbursements
2. Assets and Liabilities
3. Underwriting and Investment Exhibit

In addition, the statement contains various general interrogatories regarding the conduct of the business and numerous exhibits and supporting schedules, which have no effect upon the financial results but are designed chiefly to enable insurance departments to partially audit the statement results and provide information and publicity considered desirable from a supervisory standpoint.

Statements of most commercial enterprises are prepared upon the so-called "revenue" or "accrual" basis. The books of account show earned income and incurred expenses. Insurance companies' statements of income and disbursements are prepared upon the "cash" basis and the books of account show only cash income (or the equivalent thereof) and paid expenses, subject to a few minor exceptions hereinafter referred to. While the Underwriting and Investment Exhibit of the casualty annual statement blank assembles the year's results on a revenue basis, the difference mentioned above makes it rather difficult for one whose knowledge of accounting and statements has been confined to general commercial accounting or the study of standard accounting textbooks to clearly comprehend the insurance blank.

The principle underlying the casualty annual statement blank is, in fact, rather simple. Expressed as a formula it is as follows:

To:	Ledger assets at the beginning of the year
Add or Deduct:	Increase or decrease in capital during the year
Add:	Cash received during the year
Add:	Profit and loss adjustments in ledger assets—Increases
Deduct:	Cash disbursed during the year
Deduct:	Profit and loss adjustments in ledger assets—Decreases
Balance =	Ledger assets at the end of the year

The term cash as used in the above formula means cash or the equivalent thereof and in many instances "net" cash as will be brought out more fully upon consideration of certain specific income and disbursement items.

The annual statement blank to which all subsequent references are made is that prescribed by the National Convention of Insurance Commissioners known as the "Convention Edition" and supplied to the companies for their returns as of December 31, 1928. It should be pointed out that changes in the blank are made yearly and, accordingly, item number references and descriptions of items may change in future editions. The various sections to be considered will be taken up in the order in which they appear in the statement.

Section I—Capital Stock (Page 2)

(See Exhibit 1, page 143)

Item 1—"Amount of Capital Paid Up."

This item is merely a memorandum statement of the amount of capital paid up at the end (not the beginning) of the year of statement.

EXHIBIT 1

2 ANNUAL STATEMENT FOR THE YEAR 1928 OF THE.. (Write or stamp name of Company) Form 3

I—CAPITAL STOCK

1. Amount of capital paid up . . . . $..............................
2. Amount of ledger assets (as per balance), December 31 of previous year . . . . $..............................
3. ....crease of paid up capital during the year . . . .

Extended at . . . . $..............................

II—INCOME

	(1)	(2)	(3)	(4)	(5)	(6)
		DEDUCT				
	*Gross premiums, including policy fees, written and renewed during the year per Col. 2, VI page 7	Premiums on policies not taken	Return premiums on policies cancelled	Reinsurance	Total deductions	Net premiums
4. Accident						
5. Health						
6. Non-cancellable accident and health						
7. Auto liability *(a)* .						
8. Liability other than auto *(a)*						
9. Workmen's compensation *(b)*						
10. Fidelity						
11. Surety						
12. Plate glass						
13. Burglary and theft						
14. Steam boiler . . .						
15. Machinery						
16. Auto property damage						
17. Auto collision . . .						
18. Property damage and collision other than auto						
10. *(c)*						
20. Totals						

20. $..............................

21. Inspections . . . .
22. Gross interest on mortgage loans, per Schedule B, less $..............................accrued interest on mortgages acquired during the year . . . . $..............................
23. Gross interest on collateral loans, per Schedule C . . . .
24. Gross interest on bonds and dividends on stocks, less $..............................accrued interest on bonds acquired during the year, per Schedule D . . . .
25. Gross interest on deposits in trust companies and banks, per Schedule N . . . .
26. Gross interest from all other sources (give items and amounts):
27. ....
28. ....
29. Gross rents from company's property, including $..............................for company's occupancy of its own building, less $..............................interest on incumbrances, per Schedule A . . . .
30. Total Interest and Rents . . . .
31. From other sources (give items and amounts):
32. .... $..............................
33. ....
34. ....
35. Remittances from Home Office to United States Branch (gross) . . . .
36. Borrowed money (gross)† . . . .
37. From agents' balances previously charged off . . . .
38. Gross profit on sale or maturity of ledger assets, viz:
    (a) Real estate, per Schedule A . . . . $..............................
    (b) Bonds, per Schedule D . . . .
    (c) Stocks, per Schedule D . . . .
39. Gross increase by adjustment in book value of ledger assets, viz:
    (a) Real estate, per Schedule A . . . . $..............................
    (b) Bonds, per Schedule D . . . .
    (c) Stocks, per Schedule D . . . .
40. **Total Income** . . . . $..............................
41. .... Amount carried forward $..............................

*By gross premiums is meant the aggregate of all the premiums written in the policies or renewals issued during the year. Are they so returned in this statement? Answer: ....

†Company is at liberty to briefly state transaction, so that explanation can be carried as footnote in department report.

(a) Including net premiums on policies issued in previous years. Indicate refunds by minus sign.

1927, $..............; 1926, $..............; 1925, $..............

1924, $..............; 1923, $..............; prior to 1923, $..............

(b) Including net premiums on policies issued in previous years. Indicate refunds by minus sign.

1927, $..............; 1926, $..............; 1925, $..............

1924, $..............; 1923, $..............; prior to 1923, $..............

(c) Enter "Credit," "Live Stock," or "Sprinkler."

Item 2—"Amount of Ledger Assets (as per balance) December 31 of previous year."

This item, which must agree with Item 31, page 4, of the previous year's statement, is the starting point of the basic formula as set out on page 144 hereof.

Item 3—"—crease of Paid-Up Capital during the Year."

This item is not an income item as it is merely an addition to or decrease of capital account. It does, however, represent cash received during the year where an increase is made and, accordingly, enters into the accounting formula. Where capital is increased the bookkeeping entries are:

Debit: Cash
Credit: Capital stock

SECTION II—INCOME (Page 2)
(See Exhibit 1, Page 143)

Items 4-20—Premium Income.

The annual statement blank requires that premiums be reported on a "written" instead of a "paid" basis. Hence, written premiums for statement purposes are considered as the equivalent of cash. Premiums are reported by line of insurance and according to kind of premium transaction. The "net" credit balances of the various premium accounts are shown on the income page.

Since written premiums are credited but the cash not necessarily received until sometime subsequently, it is necessary to set up ledger asset accounts in which to carry the premiums receivable until they are collected. These accounts are known as "Premiums in course of Collection" (Items 9-25, Page 4).

The bookkeeping entries involved in the various kinds of premium transactions for each line of insurance are as follows:

(1) Gross premiums, etc.
Debit: Premiums in course of collection
Credit: Gross premiums written

(2) Premiums on policies not taken
Debit: Not taken premiums
Credit: Premiums in course of collection

(3) Return premiums on policies canceled
Debit: Cancelation (or return) premiums
Credit: Premiums in course of collection

(4) Reinsurance

Gross written

Debit: Reinsurance premiums written
Credit: Reinsurance premiums payable

Not taken and canceled (or return)

Debit: Reinsurance premiums payable
Credit: Reinsurance premiums written

Note that it is not necessary to keep reinsurance premium accounts subdivided according to gross, not taken and canceled.

Premiums in course of collection and reinsurance premiums payable receive further consideration in connection with SECTION IV—LEDGER ASSETS (Page 4 of statement).

Item 21—"Inspections."

This item represents income received by a company for inspecting mechanical equipment, usually steam boilers, where a regular inspection and indemnity contract is not carried in the company.

The bookkeeping entries are:

Debit: Cash
Credit: Inspections

Items 22-28—Interest Received on Various Forms of Ledger Assets.

These items represent net cash received—gross cash less amount paid for accrued interest, if any. The bookkeeping entries can be best illustrated by an example: Assume a 5% bond for $1000 with interest payable semi-annually acquired at par value plus three months accrued interest. The bookkeeping entries at purchase for the interest part of the transaction would be:

Debit: Bond interest (or bond interest accrued) $12.50
Credit: Cash $12.50

When the next coupon due was collected the entries would be:

Debit: Cash $25
Credit: Bond interest $25

The net interest received would be $12.50.

Item 29—"Gross Rents from Company's Property, including $——— for company's occupancy, less $——— interest on incumbrances, per Schedule A."

This item may involve three accounts—Rents received, Rents paid and Interest on mortgages payable.

The bookkeeping entries for space leased or rented to tenants would be:

Debit: Cash
Credit: Rents received

The bookkeeping entries for rent charged the company by itself for its own occupancy would be:

Debit: Rents paid
Credit: Rents received

The bookkeeping entries in connection with interest paid on incumbrances (mortgages) would be:

Debit: Interest on mortgages payable
Credit: Cash

Items 31-34—"From other Sources (give items and amounts)."

These lines are intended to provide miscellaneous and unusual income or cash received transactions and profit and loss adjustments not otherwise provided for. As an example, surplus paid in by stockholders would be reported in one of these lines. Such surplus is not income but merely an addition to surplus account. The bookkeeping entries would be:

Debit: Cash
Credit: Profit and loss (surplus paid in)

In rare cases companies, in order to provide additional surplus, reduce the par value of their stock and transfer the difference between the amounts at the old and new par values to surplus. In such cases the decrease in capital would be reported in Item 3 and the corresponding surplus gain in one of the Items 32-34 under some such description as "Surplus transferred from capital account." The bookkeeping entries would be as follows:

Debit: Capital
Credit: Profit and loss (capital transferred to surplus)

Item 35—"Remittances from Home Office to United States Branch (gross)."

This item applies only to the United States Branches of Foreign Companies. It represents funds supplied by the Home Office for capital and surplus purposes and is not income. The bookkeeping entries are:

Debit: Cash
Credit: Remittances from home office

Item 36—"Borrowed Money (gross)."

This item is self-explanatory. The bookkeeping entries are:

Debit: Cash
Credit: Borrowed money

It is noted that the foregoing item is not income. An asset (cash) is created but a corresponding liability (borrowed money payable) is also created co-incident therewith. As a matter of fact, if the borrowed money were repaid in full during the calendar year of statement it could be—and from a pure accounting standpoint should be—entirely omitted from the statement. It is obvious that the subtracting (or dropping) of equal amounts from both sides of the basic equation (or from both "Income" and "Disbursements") will not affect the balance of the equation (or the statement balance). However, the statement requires that borrowed money received and borrowed money repaid (see Item 53, EXHIBIT 2—DISBURSEMENTS, Page 3 of statement) be reported gross.

Item 37—"From Agents' Balances Previously Charged Off."

This item arises when a balance due from an agent and charged off as uncollectible is subsequently recovered. The bookkeeping entries are as follows:

Debit: Cash
Credit: Profit and loss (Agents' balances)

Item 38—"Gross Profit on Sale or Maturity of Ledger Assets"—Real Estate, Bonds and Stocks.

The profit (or loss) on sale of ledger assets is the difference between the book value (not the actual cost) at date of sale and the sale price. The bookkeeping entries for the profit portion are:

Debit: Cash
Credit: Profit and loss—profit on sale of (real estate, bonds or stocks)

There are two methods of accounting for profit and loss items in general use. One method (that followed in this paper) is to charge or credit such items as profit or loss on sale direct to a single controlling Profit and Loss ledger account and maintain subsidiary accounts for the details required by the annual statement. The second method is to carry separate profit and loss ledger accounts for each such annual statement item. Where the second method is followed the account credited in the above example would be "Profit on sale of (real estate, bonds or stocks)."

Item 39—"Gross Increase by Adjustment in Book Value of Ledger Assets"—Real Estate, Bonds and Stocks.

This item does not represent cash income or profit but is in the nature of accrued income or profit. Some companies follow the practice of maintaining the book values of real estate, bonds and stocks at approximately the market values. Profit and loss entries are made at the end of the year to bring the book values up to the approximate market values. The bookkeeping entries are:

Debit: Real estate, bonds or stocks (book value)
Credit: Profit and loss—Increase by adjustment in book value of (real estate, bonds or stocks)

In case of bonds a further use is made of this item by companies which value their bond holdings on the amortization basis. If a bond is acquired at a discount, the effective rate of interest will be in excess of the nominal rate. Assume that the nominal (coupon) rate is 4%, the purchase price 90 and the term to maturity 14 years. The effective rate of interest, as determined by reference to any standard table of bond values is 5%. If the bond were carried upon the books at $900 until maturity, a false profit on maturity of $100 would be shown and the interest income during the period would be too small, since it is reasonable to assume that the effective rate of 5% represents a fair interest return on funds invested at the time of purchase of the bond. The company would, however, receive only the nominal interest of 4% during the term of the bond, the additional interest being deferred and accumulated at the effective rate until maturity. Such deferred interest would be taken credit for by adding the yearly accrual to the book value of the bond. The bookkeeping entries would be:

Debit: Bonds (book value)
Credit: Profit and loss—accrual of bond discount

The foregoing is an exception to the general rule that the statement is based upon cash income or receipts.

It will be shown upon consideration of SECTION IV—ASSETS (Page 4 of statement) that increases (or decreases) by adjustment are unnecessary so far as the effects of changes in security values upon surplus and total admitted assets are concerned. They do, however, affect the amount of ledger assets.

Item 40—"Total Income."

This is the sum of the extended amounts of Items 20, 21, 30 and 34-39.

Item 41—"Amount Carried Forward."

This is the sum of the ledger assets at beginning of year, plus or minus the increase or decrease in capital during the year, and total income (Item 40).

Section III—Disbursements (Page 3)

(See Exhibit 2, Page 151)

Items 1-17—Losses Paid.

Accounting procedure in connection with losses paid is comparatively simple so far as meeting annual statement requirements are concerned. The bookkeeping entries for each of the various kinds of loss transactions for each line of business are as follows:

(1) Gross amount paid for losses
  Debit: Losses
  Credit: Cash

(2) Gross salvage
  Debit: Cash
  Credit: Salvage recovered

(3) Reinsurance
  Debit: Cash
  Credit: Reinsurance recovered

In cases where salvage has been recovered on a paid loss under which there was reinsurance the original company would refund to the reinsuring company its proportion of the salvage recovery. The bookkeeping entries on payment to the reinsuring company would be:

  Debit: Reinsurance recovered
  Credit: Cash

At first glance it would appear that this method of accounting is incorrect and that the bookkeeping entries should be:

  Debit: Salvage
  Credit: Cash

It will be noted that the heading "Gross" precludes any debit entries to the salvage account and an example will show that the prescribed method is correct.

Assume that a company pays a gross loss of $1000 and that the

EXHIBIT 2

Form 3 ANNUAL STATEMENT FOR THE YEAR 1928 OF THE 3
(Write or stamp name of Company)

Amount brought forward, $

III—DISBURSEMENTS

	(1) Gross amount paid for losses	(2) DEDUCT Gross Salvage (Sched. H)	(3) Reinsurance	(4) Total deduction	(5) Net amount paid policyholders for losses
1. Accident					
2. Health					
3. Non-cancellable accident and health					
4. Auto liability					
5. Liability other than auto					
6. Workmen's compensation					
7. Fidelity					
8. Surety					
9. Plate glass					
10. Burglary and theft					
11. Steam boiler					
12. Machinery					
13. Auto property damage					
14. Auto collision					
15. Property damage and collision other than auto					
16. (a)........					
17. TOTALS					$

18. Investigation and adjustment of claims, viz:
19. Accident $........; Health $........; Non-cancellable accident and health $........; Auto liability $........;
20. Liability other than auto $........; Workmen's compensation $........; Fidelity $........; Surety $........;
21. Plate glass $........; Burglary and theft $........; Steam boiler $........; Machinery $........;
22. Auto property damage $........; Auto collision $........; Property damage and collision other than auto $........; (a) .... $........;
23. Policy fees retained by agents
24. Commissions or brokerage, less amount received on return premiums and reinsurance for the following classes:
25. Accident $........; Health $........; Non-cancellable accident and health $........; Auto liability $........;
26. Liability other than auto $........; Workmen's compensation, $........; Fidelity $........; Surety $........;
27. Plate glass $........; Burglary and theft $........; Steam boiler $........; Machinery $........;
28. Auto property damage $........; Auto collision $........; Property damage and collision other than auto $........; (a) .... $........;
29. Salaries, fees, other compensation and traveling expenses of officers, directors, trustees and home office employees
30. Salaries, traveling and all other expenses of branch office employees and agents not paid by commissions
31. Medical examiners' fees and salaries
32. Inspections, including accident prevention
33. Rents, including $........ for company's occupancy of its own buildings
34. General office maintenance and expense
35. Repairs and expenses (other than taxes) on real estate
36. Taxes on real estate
37. State taxes on premiums $........
38. Insurance department licenses and fees
39. Federal taxes
40. All other licenses, fees and taxes (give items and amounts):
41. ....
42. ....
43. ....
44. Legal expenses $........; advertising $........; printing and stationery $........
45. Postage, telegraph, telephone, exchange and express $........; insurance $........
46. Furniture and fixtures $........; books, newspapers and periodicals $........
47. Bureau and Association dues and assessments
48. Stockholders for dividends (amount declared during the year, cash $........; stock $........)
48A. Policyholders for dividends, less $........ dividends received from reinsuring companies
49. Other disbursements (give items and amounts):
50. .... $........
51. ....
52. Remittances to Home Office from United States Branch (gross)
53. Borrowed money repaid (gross)
54. Interest on borrowed money
55. Agents' balances charged off
56. Gross loss on sale or maturity of ledger assets, viz:
    (a) Real estate, per Schedule A $........
    (b) Bonds, per Schedule D
    (c) Stocks, per Schedule D
57. Gross decrease, by adjustment, in book value of ledger assets, viz:
    (a) Real estate, per Schedule A $........
    (b) Bonds, per Schedule D
    (c) Stocks, per Schedule D
58. Total Disbursements $
59. BALANCE $

(a) Enter "Credit," "Live Stock," or "Sprinkler."

risk is one-half reinsured. The statement as respects this item would appear as follows:

Gross Amount Paid	Salvage	Reinsurance	Total Deduction	Net Amount Paid
$1,000.00	....	$500.00	$500.00	$500.00

If $500 salvage were subsequently received the statement under the prescribed method would show:

(a) Gross Amount Paid	Salvage	Reinsurance	Total Deduction	Net Amount Paid
$1,000.00	$500.00	$250.00	$750.00	$250.00

and under the incorrect method:

(b) Gross Amount Paid	Salvage	Reinsurance	Total Deduction	Net Amount Paid
$1,000.00	$250.00	$500.00	$750.00	$250.00

Since reinsurance applies to the net loss sustained by a company, method (a) is obviously correct as it shows reinsurance equal to 50% of the net loss — $250.00 ÷ ($1000.00 — $500) and method (b) incorrect since it shows reinsurance equal to 66 2/3% of the net loss—$500.00 ÷ ($1000.00 — $250.00).

Reinsurance is usually collected sometime after the gross loss is paid. This results in reinsurance recoverable and most companies prefer to credit this to loss account immediately. This procedure is similar in theory to the crediting of written premiums. To accomplish this result a ledger asset account "Reinsurance recoverable on paid losses" is set up and the bookkeeping entries become:

Debit: Reinsurance recoverable (on paid losses)
Credit: Reinsurance recovered

Items 18-47 and 49-51—Expenses.

These items cover various underwriting (claim, acquisition, administration, inspection, tax and bureau) and investment (real estate and other) expenses. No special accounting procedure is involved except in connection with claim and inspection expense and the usual bookkeeping entries are:

Debit: Expense (by item)
Credit: Cash

Claim expense is divided into two parts—allocated and unallocated. Allocated expense is that chargeable to specific claims, such as attorneys' and court fees, cost of medical examinations (in public liability claims) and cost of appraisals (in case of property damage losses). Unallocated claim expense consists of the general overhead cost of maintaining claim service, both in the field and at the Home Office, comprising such items as salaries, traveling expense, rent, heat, light, printing and stationery, furniture and fixtures, etc. Separate ledger accounts are maintained for assigned loss expense by line the same as in the case of losses. Separate ledger accounts are also usually maintained for claim salaries and claim traveling expense, but not by line of insurance. The problem of determining what proportion of field and Home Office rent, heat, light, printing and stationery, furniture and fixtures, should be charged to claim expense and the further distribution of such proportions plus claim salaries and claim traveling expenses to the various lines of insurance involves the application of advanced cost accounting principles and the treatment of this phase of accounting, even briefly, is beyond the scope of this paper.

Problems similar to those involved in determining unallocated claim expense are encountered in determining inspection expense, since this expense is also made up of salaries, traveling expense, rent, heat, light, printing and stationery, furniture and fixtures, etc.

It is obvious from the foregoing that the disbursements as shown on Page 3 of the statement will not check with the Trial Balance as respects many items—salaries, traveling expense, rents, printing and stationery, furniture and fixtures, etc.

Item 48—"Stockholders for Dividends (Amount declared during the year, cash $———; Stock $———)."

This item requires no special comment. The provision for showing in parenthesis dividends declared during the year is to provide a check on the liability for unpaid dividends, Page 5 of statement. The bookkeeping entries involved in the dividend account are as follows:

Debit: Dividends paid
Credit: Cash

Item 48A—"Policyholders for Dividends, less $——— Dividends received from Reinsuring Companies."

This item is peculiar to mutual companies or stock companies writing participating contracts. It involves no unusual accounting principles. Note, however, that dividends paid are net—gross paid less dividends received from reinsuring companies. Separate accounts are maintained—one for gross dividends and the other for reinsurance dividends. The bookkeeping entries are as follows:

Gross dividends paid

Debit: Dividends to policyholders
Credit: Cash

Reinsurance dividends received

Debit: Cash
Credit: Reinsurance dividends

Item 52—"Remittances to Home Office from United States Branch (gross.)"

This item is the opposite of Item 35, Page 2, and represents surplus funds returned to Home Office. The bookkeeping entries are:

Debit: Remittances to Home Office
Credit: Cash

Item 53—"Borrowed Money Repaid (gross)."

This item is the opposite of Item 36, Page 2. The bookkeeping entries are:

Debit: Borrowed money
Credit: Cash

Item 54—"Interest on Borrowed Money."

This item is self-explanatory. The bookkeeping entries are, of course:

Debit: Interest on borrowed money
Credit: Cash

Item 55—"Agents' Balances Charged Off."

This is a profit and loss item representing the charge off of a balance considered as uncollectible. The bookkeeping entries are as follows:

Debit: Profit and loss (Agents' balances)
Credit: Agents' balances

Item 56—"Gross Loss on Sale or Maturity of Ledger Assets"—Real Estate, Bonds and Stocks.

This is the opposite of Item 38, Page 2. The bookkeeping entries, so far as the loss on sale is concerned, are:

Debit: Profit and loss—loss on sale of (real estate, bonds or stocks)
Credit: Real estate, bonds or stocks (book value)

The bookkeeping entries for both Items 38, Page 2, and 56, Page 3, are further illustrated in the consideration of SECTION IV—LEDGER ASSETS (Page 4 of statement), Item 4—"Book Value of Bonds."

Item 57—"Gross Decrease by Adjustment in Book Value of Ledger Assets"—Real Estate, Bonds and Stocks.

This item is the reverse of Item 39, Page 2. For ordinary adjustments to bring the book value down to the market value the bookkeeping entries are:

Debit: Profit and loss—increase by adjustment in book value of (real estate, bonds or stocks)
Credit: Real estate, bonds or stocks (book value)

In case of companies valuing their bonds on the amortization basis the process is the reverse of that illustrated in connection with Item 39, Page 2. If a bond is acquired at a premium the effective rate of interest will be less than the nominal rate. Assume that the nominal (coupon) rate is 6%, the purchase price 115 and the term to maturity 28 years. The effective rate of interest would be 5%. Under these circumstances the excess of the nominal interest over the effective interest would be used to amortize the premium over the term of the bond so that at maturity the bond would stand on the books at its par value. The bookkeeping entries would be:

Debit: Profit and loss—amortization of bond premiums
Credit: Bonds (book value)

Item 58—"Total Disbursements."

This item is the sum of the extended amounts of Items 17, 22, 23, 28-36, 43-48A, 51-55, 56 and 57.

Item 59—"Balance."

This item is the difference between the item "Amount brought forward" at the top of the page and Item 58. It balances with Item 31, Page 4 of statement (see Exhibit 3, Page 157).

SECTION IV—ASSETS (Page 4)

(See Exhibit 3, Page 157)

This section is divided into three subsections:

(1) Ledger Assets
(2) Non-Ledger Assets
(3) Assets Not Admitted

(1) LEDGER ASSETS

Items 1-4—Investments—Real Estate, Mortgage Loans, Collateral Loans, Bonds and Stocks.

These items call for the book values of the various forms of investments. It should be noted that Item 1 provides for the deduction of incumbrances from the book value of real estate and the showing of only the net value as a ledger asset. This is not in accordance with the usual accounting practice of showing the gross value as an asset and mortgage incumbrances as a liability.

When an investment is made the bookkeeping entries are:

Debit: Real estate, mortgage loans, etc.
Credit: Cash

When an investment matures or is disposed of the bookkeeping entries are:

Debit: Cash
Credit: Real estate, mortgage loans, etc.

Where there is a profit or loss on sale or maturity at least three and in some instances four accounts are affected. Examples using th esale of a bond at a profit and a loss will illustrate. Assume that a bond carried at a book value of $980 is sold for par ($1000) and accrued interest of $25. The bookkeeping entries would be as follows:

	Debit	Credit
Cash	$1,025.00	....
Bonds (book value)	....	$980.00
Profit and loss—profit on sale of bonds	....	20.00
Bond interest	....	25.00
	$1,025.00	$1,025.00

If the book value and sale amounts were reversed, i.e., book value $1000 and sale price $980 plus accrued interest of $25, the bookkeeping entries would be as follows:

	Debit	Credit
Cash	$1,005.00	....
Bonds (book value)	....	$1,000.00
Profit and loss—loss on sale of bonds	20.00	....
Bond interest	....	25.00
	$1,025.00	$1,025.00

EXHIBIT 3

IV—LEDGER ASSETS

1. Book value of real estate (less $..........incumbrances), per Schedule A . . . . . . $
2. Mortgage loans on real estate per Schedule B, first liens $..........
   other than first ....
3. Loans secured by pledge of bonds, stocks or other collateral, per Schedule C . . . .
4. Book value of bonds, $..........; and
   stocks, $..........; per Schedule D . . . .
5. Cash in company's office . . . . $
6. Deposits in trust companies and banks not on interest, per Schedule N .
7. Deposits in trust companies and banks on interest, per Schedule N . .
8. Gross premiums in course of collection, viz:

		(1) On policies or renewals effective on or after October 1 of Current Year	(2) On policies or renewals effective prior to October 1 of Current Year
9.	Accident	$	$
10.	Health		
11.	Non-cancellable accident and health		
12.	Auto liability		
13.	Liability other than auto		
14.	Workmen's compensation		
15.	Fidelity		
16.	Surety		
17.	Plate glass		
18.	Burglary and theft		
19.	Steam boiler		
20.	Machinery		
21.	Auto property damage		
22.	Auto collision		
23.	Property damage and collision other than auto		
24.	(a)..........		
25.	TOTALS	$	$

26. Bills receivable . . . .
27. Other ledger assets, viz:
28. .... $
29. ....
30. ....
31. Ledger Assets, as per Balance on page 3 . . . . $

NON-LEDGER ASSETS

32. Interest due, $..........and accrued, $..........on mortgages, per Schedule B . . $
33. Interest due, $..........and accrued, $..........on collateral loans, per Schedule C, Part 1 .
34. Interest due, $..........and accrued, $..........on bonds, not in default, per Schedule D, Part 1
35. Interest due, $..........and accrued, $..........on other assets (give items and amounts): .
36. ....
37. ....
38. Rents due, $..........and accrued, $..........on company's property or lease . .
39. Market value of real estate over book value, per Schedule A . . . .
40. Market value (not including interest in Item 34) of bonds and stocks over book value, per Schedule D . . . . . .
41. Other non-ledger assets, viz:
42. .... $
43. ....
44. Gross Assets . . . . $

DEDUCT ASSETS NOT ADMITTED

45. Company's stock owned, $..........; loans on, $.......... $
46. Supplies, printed matter and stationery . . . .
47. Furniture, fixtures and safes . . . .
48. Gross premiums in course of collection effective prior to October 1 of current year . . . .
49. Bills receivable . . . .
50. Loans on personal security, endorsed or not . . . .
51. ....
52. Book value of real estate over market value, per Schedule A . . . . . . $
53. Book value of bonds and stocks over market value, per Schedule D . . . .
54. Book value of other ledger assets over market value, viz:
55. ....
56. ....
57. ....
58. Total Admitted Assets . . . . $

(a) Enter "Credit," "Live Stock," or "Sprinkler."

In order to conveniently record the various bookkeeping entries arising from either of the above transactions, a voucher would be prepared showing the four debits and credits. The cash would be posted in the cash book and the other entries in a journal designed to provide for entries such as the foregoing. Many companies maintain what is known as a cash-journal, a combination of cash book and journal, and in such cases all four entries would be posted in this book.

Items 6 and 7—Deposits in Trust Companies and Banks.

Heretofore in all examples of bookkeeping entries involving actual receipts and disbursements, it has been assumed that such receipts and disbursements have been in the form of cash and for simplicity of illustration "Cash" has been used as the account involved. In practice, however, only a small part of the actual business transactions of an insurance company involve actual cash but are represented by check receipts and disbursements. Accordingly, companies maintain, in addition to a pure cash account, separate ledger accounts with various banks. Checks received are usually charged to cash through the medium of the cash book and subsequently credited to cash and charged to the bank of deposit. Debit may be, and frequently is, made direct to the bank without the intermediate step of passing through the cash book. Under the latter conditions the bookkeeping debit would be to "Bank" instead of to "Cash." As an example the bookkeeping entries in connection with rents received (see page 147) would be:

Debit: Bank (by name)
Credit: Rents received

Disbursements, except for petty cash items, are almost invariably made by check and charged direct to the bank upon which they are drawn. Using gross losses paid, for example, the bookkeeping entries in actual practice (see page 150) would be:

Debit: Losses
Credit: Bank (by name)

Items 8-25—"Gross Premiums in Course of Collection"—(by line of insurance).

The function of these items has been explained in connection with the consideration of Items 4-20, Page 2 of statement. The significance of the word "Gross" is usually interpreted as meaning "without deduction of commissions." These accounts consist of the net amount of unpaid direct premiums (gross, less not taken and return) minus the net amount of reinsurance premiums payable.

When premiums are collected two asset and one disbursement accounts are affected, since premiums are remitted "net" (less commissions) by agents. Cash is debited, premiums in course of collection are credited and commissions are debited. If premiums to the gross amount of $1000, with a commission rate of 25% were remitted, the bookkeeping entries would be:

	Debit	Credit
Cash (or bank)	$750.00	....
Premiums in course of collection	....	$1,000.00
Commissions paid	250.00	....
	$1,000.00	$1,000.00

On payment of reinsurance premiums by the company the bookkeeping entries, assuming gross reinsurance premiums of $1000 and a commission rate of 35%, would be:

	Debit	Credit
Cash (or bank)	....	$650.00
Reinsurance premiums payable	$1,000.00	....
Commissions paid	....	350.00
	$1,000.00	$1,000.00

In actual practice the bookkeeping is handled somewhat differently from the simple illustrations above. In case of direct business a summary of the premium, commission and any other charges or credits and the net cash remitted, usually referred to as a "Paid Premium Report" or "Account Current," would accompany the remittance. Using this as a voucher the net cash would be debited on the cash book or to the bank and the remaining items posted to the paid premium journal. At the end of the month the total debits and credits would be posted therefrom to the appropriate ledger accounts—premiums in course of collection, commissions and expense (by account), if any.

Item 26—"Bills Receivable."

This item is of slight consequence in the accounts of insurance companies and involves no special accounting consideration. If a note were accepted from an agent for a balance due for premiums, the bookkeeping entries would be the same except that bills receivable would be debited instead of cash or bank. When the note was paid, the bookkeeping entries would be:

Debit: Cash (or bank)
Credit: Bills receivable

Items 27-30—"Other Ledger Assets, viz.:"

The more important items usually found in these lines are "Reinsurance recoverable on paid losses," referred to in connection with the consideration of paid losses, Items 1-17, Page 3 of statement, and "Agents' sundry balances."

When the reinsurance recoverable mentioned on page 152 is actually paid by the reinsuring company, the bookkeeping entries are:

Debit: Cash (or bank)
Credit: Reinsurance recoverable on paid losses

Agents' sundry balances generally arise from errors made in agents' accounts which are discovered upon audit at the Home Office. If, for example, an agent made an error of $10 in computing a commission, his account would be short or over by such amount and this would require a debit or credit to "Agents' sundry balances."

For example, assuming premiums of $1000, commissions of $250 (incorrectly computed by the agent at $260), the complete bookkeeping entries would be:

	Debit	Credit
Cash (or bank)	$740.00	....
Agents' sundry balances	10.00	....
Premiums in course of collection	....	$1,000.00
Commissions paid	250.00	....
	$1,000.00	$1,000.00

These sundry balances are cleared in subsequent reports.

Item 31—"Ledger Assets, as per Balance on Page 3."

This item is the sum of Items 1, 2, 3, 4, 7, 25, 26 and 30, and, as indicated and also previously pointed out, must agree with Item 59, Page 3.

With the exception of capital and a few ledger liability items of rather infrequent occurrence and which involve somewhat advanced and unusual accounting theory and practice, all items which are derived from the Trial Balance of a company have now been considered and the main purpose of the paper accomplished. Accordingly, consideration of the balance of the financial statement will be made as brief as possible.

(2) Non-ledger Assets

Items 32-37—Interest Due and Accrued on Various Ledger Assets.

These items are necessary to compute the actual interest earned during the year. Their determination is mainly a matter of the arithmetical computation and summarization of detail items.

Item 38—Rents Due and Accrued.

This item is similar to Items 32-37 and requires no particular explanation.

Item 39—"Market Value of Real Estate over Book Value, per Schedule A".

Insurance companies are required to compile their statements upon market values of assets. If the market value exceeds the book value, the excess is treated as a non-ledger asset.

Item 40—"Market Value (not including interest in Item 34) of Bonds and Stocks over Book Value, per Schedule D".

This item is similar to Item 39 and requires no particular comment. It should be noted that the market values of stocks include accrued dividends and, accordingly, no credit for accrued dividends should be taken in Items 35-37.

Items 41-43—"Other Non-ledger Assets, Viz:"

These items are to provide for unusual or infrequent non-ledger assets. In the case of a company which does not credit losses for reinsurance recoverable at the time of paying the gross loss (see comments on reinsurance losses, page 152) but only upon collection of the reinsurance the "Reinsurance recoverable on paid losses" would be carried as a non-ledger asset.

Item 44—"Gross Assets".

This item which is self-explanatory is the sum of Items 31, 38-40 and 43.

(3) Assets Not Admitted

From the "Gross Assets" certain deductions are made to arrive at the "Admitted Assets". These deductions consist of (1) assets of doubtful value in fact or arbitrarily so classified by law or rulings of insurance departments and (2) excesses of book values of investments over market values.

Item 45—"Company's Stock Owned, $———, Loans on $———."

Such items are of rare occurrence. Their treatment as non-admitted assets is, of course, logical.

Items 46 and 47—"Supplies, Printed Matter and Stationery" and "Furniture, Fixtures and Safes".

The treatment of the above items as non-admitted assets is open to question. Supplies, printed matter and stationery have a certain asset value, especially to a going concern, and furniture and fixtures unquestionably have an asset value, both on the basis of a going concern and because of their resale value. The fact that no asset value is permitted for these items is probably due to difficulties incident to a proper appraisal of their worth.

In view of the fact that no asset value is permitted for the above items, most companies carry no asset accounts for the same but treat all purchases as expense.

Item 48—"Gross Premiums in course of collection effective prior to October 1 of Current Year".

This item is similar to the item frequently found in the statements of manufacturing and merchandising corporations under the caption "Reserve for bad debts". It should be noted, however, that insurance companies are not permitted to exercise any judgment in determining the amount of the item but are required to consider all premiums outstanding more than three months as uncollectible or of no value. Experience shows that as a matter of fact only a small proportion of such items are eventually charged off as uncollectible.

Items 49 and 50—"Bills Receivable" and "Loans on Personal Security, endorsed or not".

The treatment of these items in their entirety as non-admitted assets is open to debate. Notes may be taken from agents as a last resort to effect collection of premium balances. On the other hand, notes or interest bearing warrants sometimes issued by municipalities in payment of premiums and assumed by a company from its agents are usually perfectly good assets. Loans on personal security are of rare occurrence in the statements of insurance companies and their treatment of non-admitted assets works no great hardship. Banks loan considerable amounts on personal security and such loans, if not in default, are considered as good assets. However, it is a part of a bank's business to make loans to individuals whereas this function is not necessary to the operation of an insurance company.

Items 52 and 53—Book Value of Ledger Assets over Market Value —Real Estate, Bonds and Stocks.

These items are the reverse of Items 39 and 40. If the book value exceeds the market value the excess is treated as a non-admitted asset.

In computing the excess of market values of the various ledger assets over the corresponding book values the excesses are "net" and not "gross". If a company owned five pieces of real estate, on three of which the market value exceeded the book value and on the other two the book value exceeded the market value, the net excess would be entered in either Item 39 or Item 52. In case of bonds and stocks the net excess would be determined for both bonds and stocks combined and the net amount entered in either Item 40 or Item 53.

As pointed out on page 149, increases (or decreases) by adjustment of ledger assets are unnecessary so far as the effects of changes in security values upon surplus are concerned, since such changes in surplus are automatically reflected in Items 40 or 53, Page 4. A simple example will illustrate. Assume that a bond carried upon the books at $990 has a market value of $1,000. If an increase by adjustment is made, the effect upon the statement is as follows:

Increase by adjustment	$10.00	(Increase in surplus)
Increase in ledger assets	10.00	
Market value of bonds over book value	0	
Increase in gross assets	10.00	
Increase in admitted assets	10.00	

If the increase by adjustment is not made, the effect upon the statement is as follows:

Increase by adjustment	0	
Increase in ledger assets	0	
Market value of bonds over book value	$10.00	(Increase in surplus)
Increase in gross assets	10.00	
Increase in admitted assets	10.00	

Items 54-57—"Book Value of Other Ledger Assets over Market Value, Viz:"

These lines are to provide for the excesses of book over market values of any ledger assets not specifically provided for.

Item 58—"Total Admitted Assets".

This item is the difference between Item 44 and the extended amount of Item 57.

Section V—Liabilities (Page 5)

(See Exhibit 4, Page 165)

With the exception of capital and a few unimportant ledger liabilities the various items of liabilities are not taken from the books of account but are determined by inventory and formula methods.* The most important items are the claim and unearned premium reserves, which usually account for from 85% to 90% of the total liabilities excluding capital. In addition to the claim and unearned premium reserves specific provision is made for liabilities or reserves for claim expense, commissions due or to become due, salaries and other expenses due or accrued, taxes due or accrued, declared and unpaid dividends, borrowed money and interest due or accrued thereon and return and reinsurance premiums payable which have not been entered on the accounting records or which are not handled through the accounts under the usual methods of premium accounting described in this paper.

It seems unnecessary to comment upon each individual item of this section and to attempt to describe the methods, formulae and accounting practices prescribed for or adopted by the companies is beyond the scope of this paper.

The difference between the "Total Admitted Assets", Item 58, Page 4, and the sum of "Total amount of all liabilities, except capital", Item 47, and "Capital paid up", Item 48, produces the "Surplus over all liabilities", or company surplus, Item 49.

Item 50, the sum of Items 48 and 49, is designated as the "Surplus as regards policyholders".

Item 51, "Total," is the sum of Items 47 and 50 and, as indicated, balances with Item 58, Page 4.

*Page 5 of the annual statement blank does not, in theory, contemplate ledger liabilities, other than capital, but these sometimes occur in practice.

EXHIBIT 4

Form 3 ANNUAL STATEMENT FOR THE YEAR 1928 OF THE 5
(Write or stamp name of Company)

V—LIABILITIES

1. Losses and claims:	(1) Adjusted or in process of adjustment	(2) Resisted	(3) Deduct reinsurance per schedule E column (2)	(4) Net unpaid claims excluding incurred but not reported	(5) Incurred but not reported	(6) Total net unpaid claims except liability and workmen's compensation claims (excluding expenses of investigation and adjustment)
2. Accident						(d)
3. Health						(d)
4. (c) Non-cancellable accident and health						(d)
5. Fidelity						
6. Surety						
7. Plate glass						
8. Burglary and theft						
9. Steam boiler						
10. Machinery						
11. Auto property damage						
12. Auto collision						
13. Property damage and coll. other than auto						
14. (a)						
15. TOTALS						

16. Special reserve for unpaid liability losses .... $..........
and Workmen's Compensation losses .... $..........

17. Special reserve for credit losses on policies expiring in October, November and December of current year, being fifty per cent of $.........., gross premiums received on said policies, less $..........paid on losses under said policies ....

18. Special reserve for accrued losses on credit policies in force December 31 of current year, being fifty per cent of $.......... earned premiums on said policies, less $..........paid on losses under said policies ....

19. Total unpaid claims .... $..........

20. Estimated expenses of investigation and adjustment of unpaid claims:

21. Accident $..........; Health $..........; Non-cancellable accident and health $..........; Fidelity $..........;

22. Surety $..........; Plate glass $..........; Burglary and theft $..........; Steam boiler $..........;

23. Machinery $..........; Auto prop. damage $..........; Auto collision $..........; Property damage and collision other than auto $..........;

24. (b).......... $..........; ....$..........; ....$..........; ....$..........;

25. Total unearned premiums as shown by recapitulation, page 7 ....

25½ (c) Additional reserve on non-cancellable accident and health policies $.........., less $.......... reserve on policies reinsured

26. Commissions, brokerage and other charges due or to become due to agents or brokers on policies effective on or after October 1 of current year, viz:

27. Accident $..........; Health $..........; Non-cancellable accident and health $..........; Auto liability $..........;

28. Liability other than auto $..........; Workmen's compensation $..........; Fidelity $..........; Surety $..........;

29. Plate glass $..........; Burglary and theft $..........; Steam boiler $..........; Machinery $..........;

30. Auto prop. damage $..........; Auto collision $..........; Property damage and collision other than auto $..........; (b) ....$..........;

31. Salaries, rents, expenses, bills, accounts, fees, etc., due or accrued ....

32. Estimated amount hereafter payable for federal, state and other taxes based upon the business of the year of this statement ....

33. Dividends declared and unpaid to stockholders, $.........., to policyholders, $.......... ....

34. Due and to become due for borrowed money ....

35. Interest due or accrued ....

36. Return premiums, gross as to commissions ....

37. Reinsurance ....

38. Other liabilities, viz:

39. .... $..........

40. ....

41. ....

42. ....

43. ....

44. ....

45. ....

46. ....

47. Total amount of all liabilities, except capital .... $..........

48. Capital paid up .... $..........

49. Surplus over all liabilities ....

50. Surplus as regards policyholders ....

51. Total .... $..........

(a) Enter "Credit (on policies expiring prior to October of current year)," "Live Stock," or "Sprinkler."
(b) Enter "Credit," "Live Stock," or "Sprinkler."
(c) State reserve basis and describe methods used.
(d) Including $..........for present value of life indemnity claims.

Underwriting and Investment Exhibit
(See Exhibit 5, Pages 167 and 168)

The underwriting and investment exhibit corresponds to what is designated in general commercial accounting as the "Profit and Loss" account. In this exhibit the statement is transformed (in summary form) from a "cash" to a "revenue" basis and, in addition, shows the gains or losses from various sources and the disposition thereof. The exhibit is divided into three main partsas follows:

(1) Underwriting exhibit
(2) Investment exhibit
(3) Miscellaneous exhibit

The various subdivisions of Part (1) arranged in debit and credit order are:

	Debit		Credit
Premiums earned	..		X
Losses incurred	X		..
Underwriting expenses incurred	X		..
Underwriting profit or loss items	X	or	X

The net balance (Item 40) of the foregoing produces the net gain or loss from underwriting, including underwriting profit and loss.

The various subdivisions of Part (2) arranged in debit and credit order are:

	Debit	Credit
Interest and rents earned	..	X
Investment expenses incurred	X	..
Profit on investments	..	X
Loss on investments	X	..

The net balance (Item 68)of the foregoing produces the net gain or loss on investments, including investment profit and loss.

The various subdivisions of Part (3) arranged in debit and credit order are:

	Debit		Credit
Dividends declared to stockholders	X		..
Dividends declared to policyholders	X		..
Remittances from home office	..		X
Remittances to home office	X		..
Increase (or decrease) in special reserves	X	or	X
(Gain or loss) from other sources	X	or	X

The net balance (Item 78) of the foregoing produces the net gain or loss in surplus from miscellaneous sources after deduction of dividends to stockholders (and/or policyholders) and special reserve adjustments.

The algebraic sum (+ = credit balance or gain; − = debit bal-

EXHIBIT 5

8 ANNUAL STATEMENT FOR THE YEAR 1928 OF THE .... (Write or stamp name of Company) FORM 3

UNDERWRITING AND INVESTMENT EXHIBIT

Showing the Sources of the Increase and Decrease in Surplus During the Year

					Gain in Surplus	Loss in Surplus
	UNDERWRITING EXHIBIT					
	PREMIUMS					
1.	Total premiums, per item 20, page 2					
2.	Add unpaid return and reinsurance premiums December 31 of previous year, per item 4 of last year's exhibit					
3.	Total					
4.	Deduct unpaid return and reinsurance premiums December 31 of current year, per items 36 and 37, page 5					
5.	Balance					
6.	Add unearned premiums and additional reserve December 31 of previous year, per item 8 of last year's exhibit					
7.	Total					
8.	Deduct unearned premiums and additional reserve Dec. 31 of current year, per items 25 and 25½ page 5					
9.	**Premiums earned during the year**					
	LOSSES					
10.	Losses paid, per item 17, page 3					
11.	Add salvage and reinsurance recoverable December 31 of previous year, per item 13 of last year's exhibit					
12.	Total					
13.	Deduct salvage and reinsurance recoverable December 31 of current year, per items (a) ...., page 4					
14.	Balance					
15.	Add unpaid losses December 31 of current year, per item 19, page 5					
16.	Total					
17.	Deduct unpaid losses December 31 of previous year, per item 15 of last year's exhibit					
18.	**Losses incurred during the year**					
	UNDERWRITING EXPENSES					
19.	(c) Underwriting expenses paid during the year, per disbursement exhibit, page 3					
20.	(a) Add underwriting expenses unpaid December 31 of current year, per liabilities exhibit, page 5, viz:—...					
21.	Total					
22.	(a) Deduct underwriting expenses unpaid December 31 of previous year, per item 20 of last year's exhibit					
23.	**Underwriting expenses incurred during the year**					
24.	**Underwriting losses and expenses**					
25.	(b)........**from underwriting during the year**					
	UNDERWRITING PROFIT AND LOSS ITEMS					
26.	Gain from:					
27.	Inspections, per item 21, page 2					
28.	Agents' balances previously charged off, per item 37, page 2					
29.	Other underwriting income, per income exhibit, page 2(a)					
30.	Total					
31.	Loss from:					
32.	Agents' balances charged off, per item 55, page 3					
33.	Other underwriting disbursements, per disbursement exhibit, page 3, other than losses and expenses, per items 10 and 19 of this exhibit (a)........					
34.	Total					
35.	(b)........ from items 26 to 34					
36.	Bills receivable and premiums in course of collection not admitted December 31 of previous year, per item 39 of last year's exhibit . . . $........					
37.	Bills receivable and premiums in course of collection not admitted December 31 of current year, per items 48 and 49, page 4 . . . $........					
38.	(b)........from items 36 and 37					
39.	(b)........**from profit and loss items**					
40.	(b)........**from underwriting and profit and loss items during the year**					
41.	Carried forward					

(a) Give statement number of each item or portion thereof included herein.
(b) Write "Gain" or "Loss".
(c) In order to secure uniformity in the reports of the various companies, all companies are directed to include in this item all disbursements, except payments to policyholders, per item 17, page 3; agents' balances charged off, in item 55, page 3; repairs, expenses and taxes on real estate; such other taxes and fees as apply to investments and personal property only; dividends to stockholders; loss on sale or maturity and decrease in book value of ledger assets, and such other items, if any, as are known to apply exclusively to the assets of the company, and to deduct from the total of said items as investment expenses one-eighth of one per cent. of the mean invested assets, viz: Real estate owned, mortgage loans, collateral loans and stocks and bonds owned.

EXHIBIT 5 (Cont'd)

Form 3 ANNUAL STATEMENT FOR THE YEAR 1928 OF THE.. 9

(Write or stamp name of Company)

INVESTMENT EXHIBIT

GAIN IN SURPLUS | LOSS IN SURPLUS

42. Brought forward

INTEREST AND RENTS

43. Interest, dividends and rents received during the year, per item 30, page 2, less item 54, page 3
44. Deduct interest, dividends and rents due and accrued December 31 of previous year, per item 48 of last year's exhibit
45. Balance
46. Add interest, dividends and rents due and accrued December 31 of current year, per item 38, page 4, less item 35, page 5
47. Add interest and rents paid in advance December 31 of previous year, per item 51 of last year's exhibit
48. Total
49. Deduct interest and rents paid in advance December 31 of current year, per liability exhibit, page 5
50. **Gross interest and rents earned during the year**

INVESTMENT EXPENSES

51. (d) Investment expenses paid during the year, per disbursement exhibit, page 3. (Attach exhibit)..........
52. Deduct investment expenses unpaid December 31 of previous year, per item 56 of last year's exhibit
53. **Balance**
54. (a) Add investment expenses unpaid December 31 of current year, per liabilities exhibit, page 5, viz:—..........
55. **Investment expenses incurred during the year**
56. **Net interest and rents earned during the year**

PROFIT ON INVESTMENTS

57. Gain from sale of ledger assets, per item 38, page 2
58. Gain from increase in book value of ledger assets, per item 39, page 2
59. Gain from change in difference between book and market value during the year
60. Gain from other investments, viz:—(Give items and amounts)..........
61. **Profit on investments during the year**

LOSS ON INVESTMENTS

62. Loss from sale of ledger assets, per item 56, page 3
63. Loss from decrease in book value of ledger assets, per item 57, page 3
64. Loss from change in difference between book and market value during the year
65. Loss from other investments, viz:—(Give items and amounts)..........
66. **Loss on investments during the year**
67. (b)..........**from investment profit and loss items**
68. (b)..........**from investments during the year**
69. Total gains and losses from Underwriting and investments

MISCELLANEOUS EXHIBIT

GAIN IN SURPLUS | LOSS IN SURPLUS

70. Dividends declared to stockholders during the year
71. Dividends declared to policyholders during the year
72. Remittances from Home Office (gross)
73. Remittances to Home Office (gross)
74. ....crease in special reserves
75. (a,) (b)..........from other sources:
76. ....
77. ....
78. Net (b)..........from items 70-77
79. Total gains and losses in surplus during the year
80. Surplus December 31 of previous year, per item 83 of last year's exhibit
81. Surplus December 31 of current year, per item 49, page 5
82. ....**crease in surplus during the year** (enter in column to balance)
83. Totals
84. Per cent. of losses incurred to premiums earned..........
85. Per cent. of underwriting expenses incurred to premiums earned..........
86. Per cent. of investment expenses incurred to gross interest and rents earned..........
87. Per cent. of total losses and expenses incurred and dividends declared to total income earned (sum of lines 24, 55, 66, 70 and 71 divided by the sum of lines 9, 39, 50 and 61)..........

(a) Give statement number of each item or portion thereof included herein.
(b) Write "Gain" or "Loss".
(d) Include in this item one-eighth of one per cent. of the mean invested assets; repairs, expenses and taxes on real estate; such other taxes and fees as apply to investments and personal property only; and such other items, if any, as are known to apply exclusively to the assets of the company.

ance or loss) of the net balances of the three subdivisions produces the net increase or decrease in surplus during the year—Item 82.

The various items of the underwriting and investment exhibit are all obtainable from Sections I-V of the current year's annual statement and Sections IV, V and the underwriting and investment exhibit of the previous year's statement. It should be pointed out that in arriving at the investment expenses paid during the year it is arbitrarily assumed—see footnote (d), Page 9 of statement—that a portion of general expense equal to ⅛ of 1% of mean invested assets (Items 1-4, Page 4 of statement) is chargeable to investments in addition to all specific investment expense. In order to preserve the statement balance, this arbitrary amount is deducted from underwriting expenses paid (Item 19, Page 8 of statement).

The earned income and incurred losses and expenses are determined from the cash income, cash disbursements, non-ledger assets, non-admitted assets and non-ledger liabilities by means of the following basic formulae:

Earned Income

(1) To: Cash income (net)
(2) Add: The current year's non-ledger asset
(3) Add: The previous year's non-ledger liability (or liabilities)
(4) Deduct: The previous year's non-ledger asset
(5) Deduct: The current year's non-ledger liability (or liabilities)
(6) Balance = Earned income

The foregoing formula applies to the subsections headed Premiums and Interest and Rents.

Incurred Losses and Expenses

(1) To: Cash disbursements
(2) Add: The current year's non-ledger liability (or liabilities)
(3) Add: The previous year's non-ledger asset
(4) Deduct: The previous year's non-ledger liability (or liabilities)
(5) Deduct: The current year's non-ledger asset
(6) Balance = Incurred losses (or expenses)

The foregoing formula applies to the subsections headed Losses, Underwriting Expenses and Investment Expenses.

The above formulae are inclusive so to speak. For example, in determining earned premiums (first formula) only Items (1), (3) and (5) are used in most instances as Items (2) and (4) are usually "O". Similarly, in determining incurred expenses (second formula) only Items (1), (2) and (4) are used in most instances as Items (3) and (5) are usually "O".

The items included in Lines 27-35, Page 8 of statement and Lines 57, 58, 62, 63, 70, 71, 72 and 73, Page 9 of statement, do not involve non-ledger items but are taken direct from the income or disbursement pages.

Gains or losses involving only non-ledger assets, non-admitted assets, or non-ledger liabilities and not income and disbursements are determined by taking the differences between such items in the current and previous year's statements. These include the following:—Item 38, Page 8 of statement, and Items 59 or 64, 60 or 65 and 74, Page 9 of statement.

In case of companies which value their bonds on the amortization basis, the net amount of the increases for accrual of discount and the decreases for amortization of premiums is reported as interest in Item 43, Page 9 of statement instead of in Items 58 and 63 respectively. This procedure is in harmony with the theory of valuation on the amortized basis, since the effective interest and not the nominal interest should be credited to interest account.

Conclusion

The foregoing is intended merely as an introduction to the subject of casualty insurance bookkeeping and accounting and a necessarily limited exposition of the requirements of the financial sections and the underwriting and investment exhibit of the casualty annual statement blank. References to other exhibits and the various supporting schedules have purposely been omitted as a consideration of these features would have extended the paper to an undesirable length. It is the intention of the writer to present a paper upon these features at some subsequent meeting, provided the need for the same has not been met in the meantime by some suitable paper or other text.