**Section 205.60 Financial Statements**

a) A municipal bond insurer shall maintain an unearned premium reserve computed to show gross premiums, without any deductions, received and receivable upon all unexpired risks, net of reinsurance, on a monthly pro rata basis, except that in the case of premiums paid more than one (1) year in advance, the premiums shall be earned proportionally with the expiration of exposure, or by such other method which will correlate the expiration of exposure with the premium earned as the Director may prescribe or approve when the company's exposure to loss does not correlate with the passage of time.

b) In addition to the contingency reserve, a municipal bond insurer shall compute and maintain reserves for losses and loss adjustment expenses for claims reported and unpaid determined by use of the case basis method or, when the requirements of Section 378 of the Insurance Code will not be met by the case basis method, such other methods as the Director may prescribe or approve which produces the reserves required by Section 378 of the Insurance Code. (Ill. Rev. Stat. 1985, ch. 73, par. 990).

1) Except as otherwise permitted by the Director, no deduction shall be made for anticipated salvage in computing case basis loss reserves unless such salvage is held by or under the control of the insurer and would qualify as an admitted asset under Section 3.1 of the Illinois Insurance Code (Ill. Rev. Stat. 1985, ch. 73, par. 615.1) or unless such salvage constitutes or is secured by a clean, irrevocable letter of credit.

2) A deduction from reserves for losses shall be allowed for the time value of money by application of a discount rate equal to the average rate of return on the admitted assets of the insurer as of the date of the computation of any such reserve. The discount rate shall be adjusted annually on the last day of each year. No deduction from reserves for losses shall be otherwise allowed for the time value of money unless the insurer can satisfy the Director that bonds, notes and other fixed income investment, as authorized under Sections 124 through 125.24a of the Illinois Insurance Code (Ill. Rev. Stat. 1985, ch. 73, pars. 736 through 737.24a inclusive) sufficient to meet obligations for insured unpaid principal and insured unpaid interest calculated to the redemption of the defaulted issue have been deposited in trust for the purpose of meeting such obligations.

3) If the insured principal and interest on a defaulted issue of bonds due and payable over the period of the next three years exceeds ten percent (10%) of the insurer's policyholders' surplus plus its contingency reserve, and such default is a default in payment of sums due, the insurer's reserve shall be supported by a report from a qualified independent source if the reserve is set up for less than the entire unpaid insured principal and unpaid insured interest to redemption.

c) Treatment of Contingency Reserve on Financial Statements

1) The contingency reserve required by subsection 205.40(b) shall be reported as a separate liability in all statutory financial statements. Any increase or decrease in the contingency reserve for the period shall be reported as a direct adjustment to surplus and shown separately in the Capital and Surplus Account of the Underwriting and Investment Exhibit.

2) For purposes of determining whether a dividend or distribution is extraordinary pursuant to Section 131.20 of the Illinois Insurance Code (Ill. Rev. Stat. 1985, ch. 73, par. 743.20(3)), the change in the contingency reserve shall be included as net income (loss) for the period.