Statutory Issue Paper No. 59

Credit Life and Accident and Health Insurance Contracts

STATUS
Finalized March 16, 1998

Original SSAP and Current Authoritative Guidance: SSAP No. 59

Type of Issue:
Common Area

SUMMARY OF ISSUE

1. Current statutory accounting guidance on policy reserves for credit life and accident and health insurance contracts, as defined in *Issue Paper No. 50—Classifications and Definitions of Insurance or Managed Care Contracts In Force* (Issue Paper No. 50), is addressed in Chapter 10, Aggregate Reserves for Life and Annuity Contracts and Chapter 13, Aggregate Reserves for Accident and Health Policies of the Accounting Practices and Procedures Manual for Life

5. Credit life insurance, generally in the form of decreasing term insurance, is issued on the lives of

guidance does not specifically address premium deficiency reserves. These changes were made to improve consistency in accounting and reporting for credit insurance contracts.

GAAP Literature

14. Consistent with Issue Papers Nos. 50, 51 and *Issue Paper No. 54 - Individual and Group Accident and Health Contracts* (Issue Paper No. 54), *FASB Statement No. 60*, *Accounting and Reporting by Insurance Enterprises* (FAS 60), *FASB Statement No. 97*, *Accounting and Reporting by Insurance Enterprises for Certain Long-Duration Contracts and for Realized Gains and Losses from the Sale of*

RELEVANT STATUTORY ACCOUNTING AND GAAP GUIDANCE (only pertinent excerpts are included below)

Statutory Accounting

24. The Life/A&H Accounting Practices and Procedures Manual provides the following guidance with respect to credit life insurance policies:

> CHAPTER 10
> AGGREGATE RESERVES FOR LIFE AND ANNUITY CONTRACTS
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> Life Insurance
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> The fourth line of life insurance is credit. Credit insurance may be either individual or group. All life and all accident and health insurance that is sold in connection with loans or other credit transactions not exceeding a stated duration is to be reported as credit insurance.
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> Types of Reserves
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> Reserves for credit insurance to a great extent depend on the premium payment plan which may be either a single premium or a monthly premium based on the outstanding loan balance. If the premium is included as part of the finance charge, and included with the total principal and interest to be paid, it is single premium credit insurance. The single premium is remitted to the insurer at the time the loan is made. State regulations may prohibit remittance of a single premium on a monthly basis by a creditor.
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> If the premium is collected monthly for the amount of indemnity, the indemnity generally is the outstanding balance type. Reserves for credit life insurance on which premiums are remitted monthly are, in most cases, pro rata unearned premium.
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> Reserves for single premium credit life may be computed by any of several methods. One method is unearned premium reserves based on the refund formula, usually called Sum of the Digits method or the "Rule of 78's" method. The "Rule of 78's" method assumes that refunds may be made to all insureds. Another method of computation establishes reserves in accordance with the assumed risks. This assumes that refunds will be made as they are experienced in the normal course of business, but not necessarily for all policies. Based on this method, reserves for single premium credit life insurance are established using mortality factors.

25. The Life/A&H Accounting Practices and Procedures Manual provides the following guidance with respect to credit accident and health insurance policies:

> CHAPTER 13
> AGGREGATE RESERVES FOR ACCIDENT AND HEALTH POLICIES
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> Credit Insurance
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> Credit accident and health insurance is insurance on a debtor to provide indemnity for payments becoming due on a specific loan or other credit transaction while the debtor is disabled as defined in the policy. Credit policies are limited to issues of 120 months or less in most states. Some states limit such policies to 60 months.
>
> Credit accident and health insurance is sold as either individual or group coverage, and the reserves are included in the annual statement. Because of the significant growth in recent years of credit insurance coverages of 120 months or less are now reported as a separate line of business in the annual statement.
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> The premium payment methods of credit insurance may be single premium or monthly premium on the outstanding balance. Outstanding balance rates, used only for group coverage, are determined by multiplying a monthly rate times the amount of outstanding insured indebtedness.

The premium so determined is remitted on each monthly due date to the insurer by the group creditor. Under single premium credit insurance, the premium rate is applied to the initial amount of insurance and generally is included in the debt. Creditors usually remit the single premium for each new insured once a month.

Although credit insurance may be written on an individual or a group basis, the major portion of credit insurance that is written today is group. The two types differ only in form, not in substance. Consequently, they are treated here as one, unless otherwise noted.

STANDARDS OF FINANCIAL ACCOUNTING AND REPORTING

General Principles

7. Insurance contracts, for purposes of this Statement, shall be classified as short-duration or long-duration contracts depending on whether the contracts are expected to remain in force[3] for an extended period. The factors that shall be considered in determining whether a particular contract can be expected to remain in force for an extended period are:

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[3] *In force* refers to the period of coverage, that is, the period during which the occurrence of insured events can result in liabilities of the insurance enterprise.

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a. Short-duration contract. The contract provides insurance protection for a fixed period of short duration and enables the insurer to cancel the contract or to adjust the provisions of the contract at the end of any contract period, such as adjusting the amount of premiums charged or coverage provided.

b. Long-duration contract. The contract generally is not subject to unilateral changes in its provisions, such as a noncancelable or guaranteed renewable contract, and requires the performance of various functions and services (including insurance protection) for an extended period.

8. Examples of short-duration contracts include most property and liability insurance contracts and certain term life insurance contracts, such as credit life insurance. Examples of long-duration contracts include w

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