Interpretation of the Statutory Accounting Principles Working Group

INT 20-08: COVID-19 Premium Refunds, Limited-Time Exception, Rate Reductions and Policyholder Dividends

GUIDANCE NULLIFIED JANUARY 1, 2021

INT 20-08 Dates Discussed

Expose May 5, 2020; May 20, 2020; June 15, 2020; July 22, 2020

INT 20-08 References

SSAP *No. 5R—Liabilities, Contingencies and Impairments of Assets*
SSAP No. 24—Discontinued Operations and Unusual or Infrequent Items
SSAP No. 53—Property Casualty Contracts—Premiums
SSAP No. 54R—Individual and Group Accident and Health Contracts
SSAP No. 65—Property and Casualty Contracts
SSAP No. 66—Retrospectively Rated Contracts

INT 20-08 Issue

COVID-19

1. A previously unknown virus began transmitting between October 2019 and March 2020, with the first deaths in the U.S. reported in early March 2020. The disease caused by the virus is known as Coronavirus Disease 2019 (COVID-19). Several states and cities have issued "stay home" orders and forced all non-essential businesses to temporarily close. This led to a significant increase in unemployment and the potential permanent closure of many businesses. Total economic damage is still being assessed however the total impact is likely to exceed $1 trillion in the U.S. alone.

Refunds, Rate Reductions and Policyholder Dividends

2. The federal, state or local government orders requiring non-essential workers to "stay home" caused a significant reduction in commercial and non-commercial activity, including automotive usage. Some consumer groups wrote letters and issued press releases calling for insurance premium refunds or pricing decreases, which included specific comments directed toward consumer automotive lines. The comments presumed that the decrease in activity would result in fewer losses.

3. Many insurers began issuing voluntary premium refunds, future rate reductions or policyholder dividends because of the decreased activity. The majority of the refunds were related to automotive lines of business however, some accident and health products also provided payments. Insurers have provided the reductions in a variety of ways. Some of the rate reductions were specific for in-force policies, whereas some of the rate reductions would apply to future policy renewals. Insurers provided unprecedentedly large payments to policyholders in an expedited fashion. These payments were viewed by regulators and insurers as being in the best interests of policyholders.

Voluntary

4. The majority of the refunds or rate reductions are being offered voluntarily and are not amounts required under the policy terms. The aggregate monetary amount of the return of funds is considered materially significant.

Jurisdiction Directed

5. In addition, a few jurisdictions have issued bulletins directing refunds and rate reductions on accident and health insurance and varying lines of prop

b. SSAP No. 54R provides guidance for policies subject to redetermination in which the premium is subject to adjustments by contract terms. This is commonly seen in federal and state groups. The guidance notes that estimates are based on experience to date and premium adjustments are estimated for the portion of the policy that has expired. Accrued return premiums are recorded as a liability with a corresponding entry to written premium. Refunds required under the policy terms would continue to be reported as retrospective or redetermination premium liabilities if applicable.

c. SSAP No. 66 provides guidance for policies whose terms or legal formulas determine premium based on losses. SSAP No. 66 references other applicable statements based on contract type for the initial accrual of premium. Estimates of premium adjustments are accrued based on activity to date and result in immediate adjustments to premium. SSAP No. 66 guidance specifies the corresponding annual statement reporting lines for different entity types.

Issue 3: How to Account for Rate Reductions

15. Some reporting entities are offering rate reductions instead of premium refunds. Some of these rate reductions provide one-time price decreases to future payments on in-force policies. Other reporting entities have provided offers of rate reductions on future renewals. Some of the offers for future rate reductions are only applicable to inforce policyholders as of a specified date. Some reporting entities have offered one-time rate reductions for future renewals for both existing and new policyholders for 2020.

a. Rate reductions on in-force business, shall be recognized as immediate adjustments to premium.

b. Rate reductions on future renewals shall be reflected in the premium rate charged on renewal. This is because it is outside of the policy boundary to require the accrual before contract inception. While the amount of future rate reduction can be estimated, it is not a change to existing policy terms and policyholders are not obligated to renew at the reduced rate, therefore, payment of the amount is avoidable. Such amounts shall be disclosed as discussed in Issue No. 5.

Issue 4: How to Account for Policyholder Dividends

16. *SSAP No. 65—Property and Casualty Contracts,* paragraph 46 requires that dividends to policyholders immediately become liabilities of the reporting entity when they are declared by the board of directors and shall be recorded as a liability.

17. The Working Group noted that policyholder dividends are typically only provided on participating policies or policies issued by non-stock companies, such as mutual entities and other corporate entity types in which profits are shared with policyholders.

18. Research during the development of this item identified that a small number of jurisdictions have legal restrictions which only allow policyholder dividends to be provided after the expiration of the policy period for which the dividend was earned. This interpretation only addresses policyholder dividends which are permitted by the applicable jurisdiction.

19. The property and casualty annual statement blank provides specific reporting lines for policyholder dividends including, but not limited to a liability line and a line in the income statement and statement of cash flow. For those entities whose policies are participating or whose corporate shell type and/or membership structure allow for policyholder dividends, the accounting for policyholder dividends is unchanged by this interpretation

20. This interpretation does not change the policyholder dividend disclosure or reporting but provides additional guidance that such policyholder dividends issued in response to COVID-19 decreases in activity shall also be disclosed as discussed in Issue 5.

Issue 5: Where to Disclose Refunds, Rate Reductions and Policyholder Dividends Related to COVID-19 Decreases in Activity

21. There are various places in the notes to the statutory annual statement where disclosures of various aspects of premium refunds, premium reductions or policyholder dividends are required. This interpretation does not recommend changes to those existing disclosures. This interpretation does, however, provides consistent annual statement disclosure for all such amounts to allow for comparable disclosures.

22. *SSAP No. 24—Discontinued Operations and Unusual or Infrequent Items* requires disclosure of the nature and financial effects of each unusual or infrequent event or transaction. Gains or losses of a similar nature that are not individually material sha

disclosure shall include the financial statement reporting line(s) predominantly impacted by the limited-time exception. (Although most practices impact net income or surplus, direct reference to those lines should be avoided. The intent is to capture the financial statement line(s) reflecting the practice which ultimately impacts net income or statutory surplus.) Additionally, a reference to Note 1 shall be included in the individual notes to financial statements impacted by the limited-time exception as applicable.

b. The monetary effect on revenue and expense.

c. If a reporting entity's risk-based capital would have triggered a regulatory event had it not used the limited-time exception, that fact should be disclosed.

d. The reasons the reporting entity elected to use the limited-time exception rather than as a return of premium.

e. Note 1 shall also identify the impact of not reporting such amounts as a return of premium on the operating percentages and other percentages reported in the Five Year Historical Data Exhibit and disclose the percentages/ratios as reported and as adjusted to report payments to policyholders as a return of premium.

i. The operating ratios to be reported include:

1. Premium earned,

2. Losses incurred,

3. Loss expenses incurred,

4. Other underwriting expenses incurred, and

5. Net underwriting gain or loss.

ii. The other ratios to be reported include:

1. Other underwriting expenses to net premiums written,

2. Losses and loss expenses incurred to premiums earned, and

3. Net premiums written to policyholder's surplus.

26. If a domiciliary jurisdiction's prescribed or permitted practices allow voluntary COVID-19 payments which are either consistent with the limited-time exception or different from a reduction in premium, the reporting entity shall complete the disclosures in Note 1 which identify that a permitted or prescribed practice was applied and in paragraphs 24 and 25 of this Interpretation. The disclosure in paragraph 25 in such instances shall reflect the impact on the ratios in paragraph 25 compared to the default premium treatment.

Does Not Address Premium Taxation

27. The Working Group noted that premium taxation requirements vary by jurisdiction and this interpretation is not intended to address premium taxation in any jurisdiction. Taxation is determined by the jurisdiction where the premium is written/returned to the policyholder according to the laws, regulations and general administrative rules applicable to all insurance enterprises licensed in a that jurisdiction. This

interpretation defers to each jurisdiction's premium tax requirements for purposes of determining taxable amounts.

Effective Date

28. The limited-time exception allowance for expense reporting for endorsements and rate filings prior to June 15, 2020, applies only to these specific issues arising from COVID-19, is effective for second