PCFRC – 2021 guidance to P&C actuaries

Special considerations due to COVID-19

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This article reflects the opinion of the authors and does not represent official guidance of the CIA.

As the COVID-19 situation continues to evolve, actuaries should pay close attention to all guidance and updates from the Office of the Superintendent of Financial Institutions, the Autorité des marchés financiers, and the CIA.

Beginning in March 2020, the COVID-19 pandemic-related lockdowns in Canada and across the world have affected trends and key metrics in property and casualty (P&C) insurance, and the impacts are expected to be long-term. Actuaries would continue to apply care and judgment in how the impact of this pandemic could affect their work.

In July 2020, the Property and Casualty Financial Reporting Committee (PCFRC) published an article on special considerations due to COVID-19. The considerations were not intended to be prescriptive nor comprehensive. These elements are still relevant and would continue to be considered by actuaries as they perform their work in 2021. However, some of the comments made in the article contained forward-looking statements which might not have been realized.

This is the second article that PCFRC is publishing to provide updates and additional considerations in light of the additional impacts since last year. There may be additional impacts on the valuation of policy liabilities, on the Financial Condition Testing (FCT) process or other areas relevant to actuaries, that are not included in these discussions. The considerations were drafted by the PCFRC to assist P&C actuaries.

1. Impact of COVID-19 on policy liabilities valuation

COVID-19 may continue to affect claim and premium liabilities estimated by the actuary from various perspectives. Actuaries would pay particular attention to how COVID-19 is altering trends and key metrics.

In particular, actuaries may consider the impact on the frequency of claims (for example, reduction in auto frequency due to less driving), as well as the cost of material and labour in the severity of claims. There may also be potential impacts from delays in court proceedings as well as medical treatments that may affect the cost and settlement pattern of claims. Actuaries may also consider the character of the alterations as being temporary or permanent in nature and reflect it accordingly in their work.

In selecting loss development factors, the actuary would use judgment in determining whether the patterns observed in the most recent periods are reflective of expected future patterns. The actuary may choose to include, exclude, or reflect the most recent experience only to a certain extent.

In addition, historical paid and reported development factors may need to be adjusted for the accident period related to the pandemic. With changes in claims frequency during the lockdown, the average accident date in the current accident year may vary from historical levels. The actuary would consider the impact of pandemic-related premium/exposure adjustments and their impact on the expected loss ratios/loss costs.

Business interruption (covered and alleged) claims have emerged over time either in the form of individual claims or class actions. Standard business interruption policies provide compensation for lost profit (and some expenses) due to a business being shut down as a result of a direct physical loss. Standard commercial property insurance is meant to cover physical damage from natural perils like fire, tornado, windstorm, and hail. A business interruption caused by a communicable disease or a government-imposed shut down is not intended to be covered by those policies. A number of class actions were launched against various insurers and groups of insurers, and defence costs may be incurred, regardless of whether an indemnity is paid out. However, some business interruption policies are specifically designed to cover the risk of pandemic. These policies are not widely purchased and would normally be subject to a sub-limit. The actuary could consult with the underwriting and legal teams to identify and determine whether there are special programs that the company offers that may be covering or potentially covering pandemic losses. The actuary could also closely follow the legal development on these claims.

Regular communication with claims professionals and finance and underwriting teams continues to be essential to the valuation of claim liabilities. Discussion points may include the potential effect of emerging claims that have not yet been reported, court decisions, judicial events, and political events.

2. Impact of COVID-19 on the FCT

As part of the FCT, the actuary prepares a base scenario that would normally be consistent with the business plan of the company. In light of recent developments due to COVID-19, insurers may experience unforeseen financial results due to market conditions and/or additional claim activity. Consideration could be given to adapt the base scenario to reflect the most recent financial data available, if actual financial results differ materially from the business plan. Actuaries would refer to the educational note *Guidance for the 2021 Reporting on Capital and Financial Condition Testing for Life, P&C, and Mortgage Insurers* published by the Committee on Risk Management and Capital Requirements for considerations due to COVID-19.

Any adjustments made to the base scenario due to COVID-19 would typically also affect the magnitude and likelihood of the adverse scenarios. For example, if the inflation on claim amounts assumed in the base scenario is increased due to the impact of COVID-19, the probability and quantum for the inflation assumption in an adverse scenario would also be expected to change.

This article is part of a series of practice-specific articles under the Actuarial Guidance Council.