Article from

Small Talk

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COVID-19: Implications for Smaller Insurance Companies

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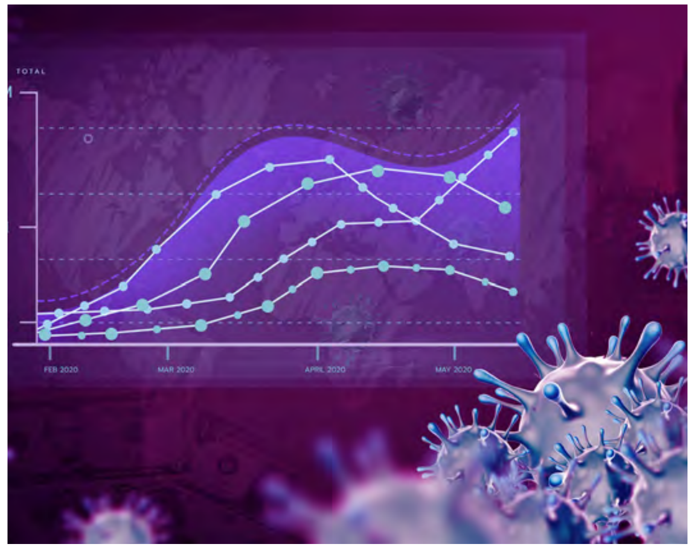

As part of the Smaller Insurance Company Section meeting, we hosted a discussion among actuaries regarding the uncertainty brought about by the COVID-19 pandemic. The more we shared our thoughts and ideas for informational resources, the more we realized that there was a benefit for further actuarial discussion. As a result, the Smaller Insurance Company Section of the Society of Actuaries hosted "COVID-19: What a Smaller Insurance Company Actuary Needs to Know Virtual Town Hall" on April 17, 2020.

The town hall featured presentations and discussions by Pete Heinrichs, Scott Wright and Jonathan Pollio, and I had the opportunity to moderate the event. This article discusses the highlights of the town hall, focusing on the initial reactions to the pandemic.

THE EARLY PANDEMIC PROGRESSION MODELS

Pete Heinrichs, a managing director with AON, presented the AON pandemic progression models, which included a variety of countries and states, highlighting the number of COVID-19 cases, deaths and transmission rates. The AON pandemic models tracked and projected transmission rates, daily deaths and cumulative daily deaths for multiple countries, and we looked at those for the United States.

When AON added the effects of the stay-at-home orders, it was apparent that this had a risk-mitigating effect. It was also apparent that there was a high degree of uncertainty about the future cases, deaths and transmission rates. Today, the actual U.S. death count has surpassed the higher projection (120,000) and is well beyond the lower projection (50,000). The Johns Hopkins COVID-19 Dashboard by the Center for Systems Science and Engineering (CSSE) counted around 30,000 deaths at the time of the town hall. As of September 2020, it stands at 189,000.

THE PANDEMIC RISKS TO INSURANCE

According to Heinrichs, claim risk is not the most important risk facing small insurance companies during the pandemic. The insurance risk includes persistency. Lapses due to unemployment and furloughs causing a decrease in worksite products are expected to be a much higher risk.

Operational risks to companies include the ability to pay claims with the stay-at-home orders. Companies are relying on their business continuity procedures, and these have been revised to address the features of this pandemic. Also, underwriting is slowed because it is difficult to get paramedical and medical exams during this period. Investment risk has been difficult for companies because the market has been volatile, and interest rates remain low. Market risk includes the willingness for policyowners to continue premiums, given the increase in unemployment. Regulatory risk includes the increases in risk due to regulatory mandates for covering COVID-19 testing, treatment and extended grace periods. Finally, reputational risk is important; views are mixed, and all eyes are focused on how the insurance industry is responding to the pandemic.

THE EARLY REGULATORY ENVIRONMENT

Next to speak was Scott Wright, a life actuary for Swiss Re. Wright discussed the regulatory environment. The World Health Organization had declared COVID-19 a pandemic one week before the town hall, and immediately, the financial markets changed. Layoffs began. States closed business offices and stores, except for essential services. The closings were not well coordinated. The CARES Act was enacted and signed into law on Friday, March 27, 2020.

States began enacting legislation for extended grace periods for premium payments, and this varied for each state. As a result, the National Association of Insurance Commissioners asked for consistency. The financial impact of these changes will be emerging over the next few months.

Wright suggested we can expect changes for property and casualty insurance: Business interruption insurance usually excludes pandemics, but we may see changes to that tradition to protect the reputation of insurance. Automobile insurance refunds have already helped the reputations of those companies.

Wright highlighted the fact that we still have many questions. How do we prepare for the next "event"? How do we deal with cash flow testing for asset adequacy in this persistent low-interest environment? Companies are interested in having discussions for relief on the asset side.

HOW CAN WE STAY INFORMED OF THE ITEMS AFFECTING OUR WORK?

The final presenter was Jonathan Pollio, who is senior vice president, chief actuary at Amalgamated Life Insurance Company in White Plains, New York. He lives at what was initially the heart of the pandemic, and he discussed the challenges of the smaller insurance company actuary. His priority was finding accurate information about COVID-19, and his son sent articles about the biological aspects of the disease and the expected epidemic growth. His resources predicted that the virus would affect 2 percent of the population. Many New York counties have already reached the 2 percent level. The Johns Hopkins dashboard provided the most useful data, Pollio said, and he learned about the impacts from consultants, reinsurers and conference calls.

DIFFICULTIES WITH THE SITUATION

Pollio's second challenge was how to project data. The businesses mentioned were group life, stop loss, a health fund, worksite products, statutory (state-run) disability and paid family leave. The major issues for projections are (1) premium persistency due to layoffs and (2) lapses. Projections could become difficult, because lapses may be delayed to the end of the extended grace period. Also, with the sales force quarantined, new business has been negatively affected, especially for credit and preneed insurance.

The regulatory issues include dealing with rapid changes in laws for 50 states. Adapting to changing laws has always been a challenge, but it has been accentuated by the pandemic.

Finally, at the time of the town hall, it was audit season for companies, and this seems to have proceeded according to the schedule set up before the COVID-19 disruptions. This may have been the only "business as usual" event, which was made more difficult due to the distractions.

TOWN HALL AUDIENCE DISCUSSIONS

The audience commented on working with remote staffs. One attendee mentioned a great article on Inc.com about managing remote teams.[1] The main tips were:

- have a daily check-in;
- communicate a lot;
- take advantage of technology;
- manage expectations;
- focus on outcomes, not activity;
- resource your team (they will need laptops, mobile devices, high-speed internet); and
- be flexible.

One question from the audience pertained to potential changes to the IRC Section 7702 interest rate from 4 percent to a lower rate that allows higher premiums. This could be combined with a change in the nonforfeiture rate. Actuaries have been looking for relief from changes to lower interest rates in both rates for a few years.

We also discussed how to model the impact of the pandemic on health care insurance. There will be changes, because of the higher claim costs from COVID-19, but many costs are initially lower because elective procedures have been postponed. That may correct itself in the coming year.

The discussion then turned to lapse rates. We can expect selective lapses, because some insurance will be less affordable, due to the recession. At the same time, it is more difficult for brokers to replace existing coverage. However, with some of the generous state changes to grace periods, we may not see lapses for some time.

With respect to insurance and reputation risk, the public was initially reactive, and now they are thinking ahead. According to the panelists, they value health and life insurance more.

For insurance companies, attendees largely agreed we may not see solvency issues; we can likely expect **surplus** issues instead. Waves of acquisitions are also expected, but this is complicated because COVID-19 is a global issue. Many acquisitions have historically been accomplished by global insurers.

Reinsurance may provide an alternative solution for surplus relief. We can expect a low volume of transactions at first, but it will peak toward the end of the pandemic crisis. Reinsurance costs are not expected to increase, but we may see pandemic exclusions in treaties where they were previously not mentioned. We also are seeing reinsurers avoiding the tail risk, which surprised the experts.

Should companies be in a position of addressing surplus issues, the panel of speakers suggested that it would be far better to start conversations with the regulators early on, as company plans are considered. They would be likely to entertain changes that remedy any short-term troubles.

Questions came in about whether there will be changes to cash flow testing and the scenarios. The three experts believed that there will be no changes to the standard scenarios, and sensitivity testing will include extra high mortality, even as high as 50 percent.

We continued the discussions about mortality and morbidity. Socioeconomic classes are not so much of a factor for extra deaths. Rural versus urban residences have a far greater effect. Occupational classes have an effect, depending on whether the employee is an "essential worker," because of the greater exposure to the COVID-19 virus. This may change some of the underwriting. The comorbidity between COVID-19 infections and older ages exists, but it is difficult to measure.

The costs for acute treatments are expected to cause a loss in premium income, but other procedures have been delayed. The speakers suggested companies will want to add a spike in treatments after the deferral. Some professionals, like teachers, may have seasonal elective surgery, and this may be different this year. Surgeries may be delayed or omitted. We will all continue to evaluate the experience as it emerges. ■

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ENDNOTE

1 Ater, Jason. 7 tips for successfully managing remote teams. *Inc.com*, March 15, 2019, *https://www.inc.com/jason-aten/7-tips-for-working-fsuccessfully-managing-remote-teams.html* (accessed August 26, 2020).