

Interpretation of the Emerging Accounting Issues Working Group

INT 02-21: Accounting for Prepaid Loss Adjustment Expenses and Claim Adjustment Expenses

ISSUE NULLIFIED BY SSAP NO. 55

INT 02-21 Dates Discussed

September 10, 2002; December 8, 2002; June 11, 2006; September 10, 2006

INT 02-21 References

SSAP No. 55—Unpaid Claims, Losses and Loss Adjustment Expenses (SSAP No. 55)

SSAP No. 84—Certain Health Care Receivables Under Government Insured Plans (SSAP No. 84)

INT 02-21 Issue

1. NAIC staff has received several inquiries relating to guidance included in Chapter 11 of the Property/Casualty Accounting Practices and Procedures Manual concerning the treatment of unpaid loss adjustment expenses (LAE). This guidance states that the liability for LAE should be established regardless of any payments made to third party administrators, management companies, etc.

2. It appears from discussion with various regulators that this guidance was a significant change upon adoption in 1988, but the guidance was not included within SSAP No. 55. However, Paragraph 17 of *Issue Paper No. 55—Unpaid Claims, Losses and Loss Adjustment Expenses* states, “the statutory principles outlined in the conclusion above are consistent with the current statutory guidance for recording a liability for unpaid claims and unpaid losses and loss/claim adjustment expenses.” These two statements appear contradictory.

3. The accounting issues are when establishing the liability for unpaid loss adjustment expenses, should the liability be established in a manner to include estimated expenses to adjust all unpaid claims, regardless of whether the reporting entity has paid an outside party for these responsibilities? Further, whether this requirement should also apply to claim adjustment expenses under accident and health contracts?

INT 02-21 Discussion

4. The working group reached a consensus that the liability for unpaid LAE should be established regardless of any payments made to third party administrators, management companies or other entities. This is consistent with the concepts of conservatism and consistency in the Statement of Concepts. The establishment of the liability for LAE gross of any amounts paid to these entities results in more meaningful financial statements in that the financial condition of the reporting entity is more appropriately stated.

5. Further, the liability for claim adjustment expenses on indemnity accident and health contracts should be established in an amount necessary to adjust all unpaid claims irrespective of payments made to third party administrators, etc. This supports the concept of consistency found in the Preamble to the *Accounting Practices and Procedures Manual*, as there is no overriding difference between unpaid LAE for property/casualty insurers and unpaid claim adjustment expenses of health entities.

6. On September 10, 2006 the Working Group reached a consensus as to the applicability of guidance to managed care contracts. The liability for claims adjustment expenses on non-capitated payments under managed care contracts should be established in an amount necessary to adjust all unpaid claims irrespective of payments made to third party administrators, etc. The working group determined that capitated payments under managed care contracts are not included within the scope of this issue. This paragraph shall become effective for reporting periods ending on or after December 31, 2006.

INT 02-21 Status

7. No further discussion is planned.