Statutory Issue Paper No. 21

Bills Receivable For Premiums

STATUS
Finalized March 16, 1998

Original SSAP and Current Authoritative Guidance: SSAP No. 6

Type of Issue:
Common Area

SUMMARY OF ISSUE

1. Bills receivable, which are generally interest bearing, are used by reporting entities as methods of financing premiums. The Accounting Practices and Procedures Manual for Property and Casualty Insurance Companies provides guidance on the accounting for bills receivable taken for premiums. However, the guidance for bills receivable in the Accounting Practices and Procedures Manual for Life and Accident and Health Insurance Companies relates to non-premium loans (which will be addressed in a separate issue paper). This issue paper establishes statutory accounting for bills receivable for premiums that is consistent with the Statutory Accounting Principles Statement of Concepts and Statutory Hierarchy (Statement of Concepts).

SUMMARY CONCLUSION

2. Bills receivable for premiums meet the definition of assets as set forth in *Issue Paper No. 4—Definition of Assets and Nonadmitted Assets*. First, an evaluation shall be made to determine nonadmitted amounts. Next, an evaluation shall be made of such assets in accordance with *Issue Paper No. 5—Definition of Liabilities, Loss Contingencies and Impairments of Assets* (Issue Paper No. 5) to determine whether there is an impairment. This two step process is set forth below:

1. Bills receivable shall be accounted for as a nonadmitted asset if either of the following conditions are present:

   a. Past due installment: If any installment is past due, the entire bills receivable balance from that policy is nonadmitted; or

   b. Aggregate bills receivable balance due in excess of the unearned premium on the policy for which the note was accepted: If the aggregate bills receivable balance due exceeds the policy's unearned premium, the amount in excess of the unearned premium is nonadmitted.

3. Amounts determined to be uncollectible shall be written off: If, in accordance with Issue Paper No. 5, it is probable a portion of the bills receivable is uncollectible, any uncollectible bills receivable shall be written off against operations in the period such determination is made. If it is reasonably possible a portion of the balance is uncollectible, disclosure requirements outlined in Issue Paper No. 5 shall be followed.

4. The following shall provide additional guidance in determining the nonadmitted portion of bills receivable:

a. Amounts classified as nonadmitted assets collected subsequent to the date of the statutory financial statements - Such amounts shall not be used to decrease the nonadmitted asset otherwise calculated.

b. Determination of the Due Date - The due date is governed by the contractual due date of the installment.

DISCUSSION

5. The Statement of Concepts states:

> The ability to meet policyholder obligations is predicated on the existence of readily marketable assets available when both current and future obligations are due. Assets having economic value other than those which can be used to fulfill policyholder obligations, or those assets which may be unavailable due to encumbrances or other third party interests should not be recognized on the balance sheet but rather should be charged against surplus when acquired or when availability otherwise becomes questionable.

6. Based upon the above concept, bills receivable should reflect only amounts that are available to meet both current and future policyholder obligations when the obligations are due. Therefore, amounts determined to be impaired (i.e., uncollectible), regardless of aging, should be charged to operations in the period such determination is made.

7. Under the conservatism concept of statutory accounting and consistent with current statutory accounting guidance, the entire bill receivable is nonadmitted if the related premium installment is past due. In addition, any excess of the aggregate bill receivable over the unearned premium amount on the policy of any performing bill receivable is nonadmitted. In accordance with the concept of conservatism, subsequent collection of nonadmitted assets should not be considered in the determining period-end nonadmitted assets. These recoveries should be accounted for in the period received.

Drafting Notes/Comments

- Accounting/aging of retrospective premiums currently reported on line 9.2 or line 9.3 is addressed in a separate issue paper.
- Accounting for uncollected agents' balances is addressed in *Issue Paper No 6—Amounts Due From Agents and Brokers.*
- A separate issue paper addresses unearned and unbilled premiums.
- Accounting for uncollected premium balances is addressed in *Issue Paper No. 10—Uncollected Premium Balances*.

RELEVANT STATUTORY ACCOUNTING AND GAAP GUIDANCE

Statutory Accounting

8. Chapter 8, *Other Admitted Assets*, of the Accounting Practices and Procedures Manual for Property and Casualty Insurance Companies discusses bills receivable as follows:

> (g) Bills receivable taken for premiums are admitted assets provided that the current installment is not past due, and the balance due does not exceed the unearned premium on the policy for which the note was accepted.

9. Chapter 9, *Nonadmitted Assets,* of the Accounting Practices and Procedures Manual for Property and Casualty Insurance Companies discusses bills receivable as follows:

> 6. Bills Receivable, Taken for Premiums: Bills or notes receivable are used as methods of financing premiums usually in states where installment premiums are not permitted or customary. If any portion of a bill or note receivable is unpaid past the due date of an installment, the entire bill or note is classified as nonadmitted. Also, on bills or notes not past due, the excess of the balance due over the unearned premium on the underlying policy or policies is classified as a nonadmitted asset. To the extent bills receivable are taken for premium for retrospectively rated policies, such bills must meet the same criteria required of accrued retrospective premiums to be reported as an admitted asset.

Generally Accepted Accounting Principles

10. GAAP addresses collectibility issues related to bills receivable in FASB Statement No. 5, *Accounting for Contingencies* (FAS 5), paragraphs 1, 3 and 8:

> 1. For the purpose of this Statement (FAS 5), a contingency is defined as an existing condition, situation, or set of circumstances involving uncertainty as to possible gain (hereinafter a "gain contingency") or loss[1] (hereinafter a "loss contingency") to an enterprise that will ultimately be resolved when one or more future events occur or fail to occur. Resolution of the uncertainty may confirm the acquisition of an asset or the reduction of a liability or the loss or impairment of an asset or the incurrence of a liability.
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> [1] The term loss is used for convenience to include many charges against income that are commonly referred to as expenses and others that are commonly referred to as losses.
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> 3. When a loss contingency exists, the likelihood that the future event or events will confirm the loss or impairment of an asset or the incurrence of a liability can range from probable to remote. This Statement uses the terms probable, reasonably possible, and remote to identify three areas within that range, as follows:
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>   a) Probable. The future event or events are likely to occur.
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>   b) Reasonably possible. The chance of the future event or events occurring is more than remote but less than likely.
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>   c) Remote. The chance of the future event or events occurring is slight.
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> 8. An estimated loss from a loss contingency (as defined in paragraph 1) shall be accrued by a charge to income[3] if both of the following conditions are met:
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>   a) Information available prior to issuance of the financial statements indicates that it is probable that an asset had been impaired or a liability had been incurred at the date of the financial statements.[4] It is implicit in this condition that it must be probable that one or more future events will occur confirming the fact of the loss.
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>   b) The amount of loss can be reasonably estimated.
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> [3] Paragraphs 23-24 of APB Opinion No. 9, Reporting the Results of Operations, describe the rare circumstances in which a prior period adjustment is appropriate. Those paragraphs are not amended by this Statement.
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> [4] Date of the financial statements means the end of the most recent accounting period for which financial statements are being presented.

11. The FAS 5 criteria above is used in interpreting information such as historical trending and general information about the financial condition of the insureds in an effort to evaluate the collectibility of a receivable balance. Accounting for contingencies is discussed in more detail in Issue Paper No. 5.

RELEVANT LITERATURE

Statutory Accounting

- Statutory Accounting Principles Statement of Concepts and Statutory Hierarchy
- Accounting Practices and Procedures Manual for Property and Casualty Insurance Companies, Chapters 8 and 9
- *Issue Paper No. 4—Definition of Assets and Nonadmitted Assets*
- *Issue Paper No. 5—Definition of Liabilities, Loss Contingencies and Impairments of Assets*

Generally Accepted Accounting Principles

- *FASB Statement No. 5, Accounting for Contingencies*

State Regulations

- No additional guidance obtained from state statutes or regulations.

