BC FINANCIAL SERVICES AUTHORITY

April 30, 2020

VIA EMAIL

File No.: 78000-01
Ref. No.: 0506

To: CFOs, BC Incorporated Property and Casualty and Life Insurance Companies

RE: COVID-19 – Temporary Changes to Capital Requirements

The BC Financial Services Authority (BCFSA) is applying temporary easing measures to capital adequacy requirements announced on April 9, 2020, by the Office of the Superintendent of Financial Institutions (OSFI). These measures will immediately apply to BC incorporated property and casualty and life insurance companies to provide relief during the current COVID-19 pandemic. OSFI's announcement of these measures and the timing can be found in Appendix A. OSFI has also compiled a list of frequently asked questions for COVID-19 measures. Refer to the FAQs.

Under the *Financial Institutions Act* and the Capital Requirements Regulation, BC incorporated insurance companies are required to apply OSFI's guidelines for the Minimum Capital Test (MCT) and the Life Insurance Capital Adequacy Test (LICAT).

BCFSA will continue to communicate with insurance companies on further developments. Insurance companies should continue to inform their BCFSA Relationship Manager of any financial or operational challenges they may encounter as a result of the COVID-19 pandemic.

If you have any immediate questions or concerns about these easing measures, please contact Sandra Vogt, Acting Director, Financial Reporting and Standards at sandra.vogt@bcfsa.ca or 604-218-6548, or your BCFSA Relationship Manager.

Regards,

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Sandra Vogt
Acting Director, Financial Reporting and Standards

Enclosure: Appendix A – Temporary Changes to MCT and LICAT

cc: CEOs, BC Incorporated Property and Casualty and Life Insurance Companies

Appendix A – Temporary Changes to MCT and LICAT

Reference: https://www.osfi-bsif.gc.ca/Eng/fi-if/in-ai/Pages/20200409_fri_let.aspx

The following is an excerpt from OSFI's announcement.

Additional Actions to Address Issues Stemming from COVID-19

Type of Publication: Letter
Date: April 9, 2020
To: Federally Regulated Insurers[1] (FRIs)

OSFI continues to actively monitor the evolving situation with COVID-19 and has been in frequent contact with federally regulated insurers (FRIs) to assess their operational capacity and actions to address the current environment. As a result of these ongoing discussions, and further to the actions communicated in its March 27 letter, OSFI is announcing continued regulatory flexibility measures to support COVID-19 efforts while promoting financial resilience and stability.

Today, OSFI is announcing additional actions in response to the current extraordinary circumstances, including setting expectations related to:

- The capital treatment of payment deferrals granted due to COVID-19 for:
    - Mortgages, leases and other loans, and
    - Insurance premiums; and
- The approach to determining interest rate risk requirements for participating products (par) in the *Life Insurance Capital Adequacy Test* (LICAT).

Loan payment deferrals will not increase capital charges on mortgages, leases or other loans

In situations where payment deferrals for mortgage loans, leases or other loans (for example, private debt, small business loans, and mid-market commercial loans) are granted by insurers because of the impact of COVID-19, these loans and leases will continue to be treated as performing assets under the LICAT guideline. This means that these assets will not fall into the impaired and restructured category and, therefore, will not be subject to a higher credit risk factor as a result of these payment deferrals. Insurers should continue to assess the credit quality of these borrowers and follow sound credit risk management practices.

This capital treatment of loans and leases will remain in place for the duration of the payment deferral, up to a maximum of six months. Insurers may apply these measures when calculating their capital position for all cases related to COVID-19, even if they precede the date of this letter. This treatment will be revisited in the future as needed. FRIs granting payment deferrals may be subject

[1] Includes life, property & casualty and mortgage insurers; collectively referred to as FRIs or insurers.

to additional reporting requirements surrounding these loans and leases. Details on additional reporting requirements, if any, will be communicated to FRIs in the coming weeks.

Premium payment deferrals will not increase capital charges on outstanding premiums

In situations where payment deferrals for insurance premiums are approved by FRIs because of the impact of COVID-19, the related assets will not be subject to higher credit risk factors per the LICAT, *Minimum Capital Test* (MCT) and *Mortgage Insurer Capital Adequacy Test* (MICAT) guidelines. This is applicable to installment premiums receivable (not yet due), receivables outstanding less than 60 days, and receivables outstanding 60 days or more, provided that the receipt of payment is in accordance with the deferral terms and conditions. For clarity, this capital treatment applies to receivables from agents and brokers to the extent premiums flow through them. FRIs should continue to follow sound risk management practices and assess the ability of these parties to make contractual payments.

This capital treatment of receivables applies for the duration of the premium payment deferral, up to a maximum of six months. Insurers may apply these measures when calculating their capital position for all cases related to COVID-19, even if they precede the date of this letter. This treatment will be revisited in the future as needed. FRIs granting payment deferrals may be subject to additional reporting requirements surrounding these premium payment deferrals. Details on additional reporting requirements, if any, will be communicated to FRIs in the coming weeks.

LICAT interest rate risk requirements for par to be smoothed over six quarters

Earlier this year, OSFI launched a public consultation on an updated version of the LICAT guideline. Included in that consultation were adjustments to the framework aimed at correcting an aspect of the test that, due to the methodology, results in increased volatility in interest rate risk requirements for par. In order to allow insurers to focus on the current environment, that consultation is on hold.

Recognizing that there is an aspect of the LICAT that, due to the methodology, causes some increased and unwarranted volatility in interest rate risk requirements for par, and in consideration of the current environment, we are introducing a change to this aspect of the test. Specifically, the interest rate risk requirement for a par block in any given quarter will be equal to the average of the current requirement for the block, and the requirements over the five previous quarters (i.e. the rolling average over six quarters).

Insurers may determine interest rate risk requirements for par at Q1 2020 using either the current LICAT requirements or the rolling averages. Beginning in Q2 2020, the rolling average approach will become mandatory, and will remain in place until OSFI communicates otherwise.

Other considerations and next steps

OSFI will continue to engage FRIs on further developments. Insurers should continue to be proactive in informing their OSFI Lead Supervisors of any financial or operational challenges they may encounter as a result of COVID-19. If OSFI decides to further modify or clarify supervisory, regulatory or capital expectations, insurers and other stakeholders will be notified in a timely manner.