

Department of Legislative Services
Maryland General Assembly
2013 Session

FISCAL AND POLICY NOTE

Senate Bill 735
Finance

(Senator Astle)

Insurance - Premium Financing

This bill authorizes a premium finance company to enter into a premium finance agreement that includes the costs of a motor club membership. The bill also alters the method by which a finance charge in a premium finance agreement is calculated. The bill increases the amount of a cancellation charge and the ceiling of a delinquency and collection charge. The bill alters the circumstances in which a premium finance agreement may require an insured to pay a cancellation charge.

The bill takes effect June 1, 2013.

Fiscal Summary

State Effect: Approval of amended premium financing agreements and review of interest computations can be handled by the Maryland Insurance Administration with existing resources. No impact on revenues.

Local Effect: None.

Small Business Effect: Meaningful.

Analysis

Bill Summary: To authorize motor clubs to engage in the business of financing premiums, the bill amends various provisions of current law relating to premium financing, including:

- amending the definition of premium finance agreement;

- requiring a motor club to register with the Commissioner before engaging in the business of financing premiums in the State;
- requiring a premium finance agreement to include, if applicable, the name and place of business of the motor club providing motor club service and the total amount of motor club costs;
- requiring a premium finance company, at least 10 days before canceling a motor club membership, to deliver or mail a written notice of intent to cancel the membership;
- authorizing a premium finance company to cancel a motor club membership by submitting to the motor club a notice of cancellation that specifies the effective date of the cancellation; and
- determining the effective date of a cancellation for a motor club membership dependent on the date of receipt of the notice of cancellation.

The bill requires that any insured who is a party to a premium finance agreement have the ability to prepay the obligation in full at any time and receive a refund credit. If an insured receives a refund credit due to the prepayment of an obligation, the bill requires that the amount of the refund must be calculated by the actuarial method of calculating refunds. The finance charge must be computed in an amount not exceeding the sum of 1.15% for each 30 days of the loan, computed in advance. The bill also requires a premium finance company to calculate interest as earned in 30-day increments on the first day of each 30-day period. No more interest may be retained by the premium finance company than is actually earned. The bill imposes specified requirements on a managing general agent to return any gross unearned premiums that are due under an insurance contract.

The bill authorizes a premium finance agreement to pay a cancellation charge if a default in paying an installment results in the issuance of a notice of intent to cancel and the defaulted installment is received on or after the cancellation date stated in the notice. The bill increases the ceiling, from \$8 to \$15, on the amount a premium finance company may charge an insured a delinquency and collection charge on each installment that is in default. The bill also increases the amount of a possible cancellation charge by \$10. The increased amounts only apply to private passenger automobile or personal fire or liability insurance.

If a payment is dishonored for insufficient funds, the bill authorizes a premium finance company to issue a notice of intent to cancel with the same date of cancellation that would have been used if the payment had not been made in a timely manner.

The bill also requires a premium finance company to refund to the insured the amount of unearned premiums greater than any amount due under the insured's account, which may

include previous premium finance agreements if the insurer or managing general agent returns any gross unearned premiums to a premium finance company due to the cancellation of an insurance contract.

The bill alters the definition of “electronic payment” to allow payment by electronic check. The bill also repeals the requirement that a premium finance company needs *written* consent of the insured before any notice sent by a means other than personal delivery, first-class mail, or commercial delivery.

Current Law:

Premium Finance Agreement Definition: A “premium finance agreement” is an agreement (1) by which an insured or prospective insured promises to pay a premium finance company the amount advanced or to be advanced under the agreement, together with interest and a service fee, to an insurer, an insurance producer, in payment of premiums and (2) that contains an assignment of or is otherwise secured by the unearned premium or refund obtainable from the insurer on cancellation of the insurance contract. A premium finance agreement is not a premium financed in connection with a time sale of goods or services or an extension of credit without charge by an insurance producer.

Registration: A premium finance company must register with the Commissioner before engaging in business as a premium finance company in the State. An insurer or an insurance producer that finances premiums in the State must also register.

Premium Finance Agreement: A premium finance agreement must contain:

- the name and place of business or address for the insurance producer negotiating the related insurance contract, the insured, and the premium finance company to which payments may be made;
- an itemized list for each insurance contract or coverage financed under the agreement that includes specified identifying information;
- if applicable, (1) the total amount of premiums; (2) the amount of the down payment; (3) the principal balance; (4) the amount of the finance charge; (5) the balance payable by the insured; (6) the number, amount, and due date of installments required; and (7) the electronic payment fee.

Finance Charge: A premium finance company may charge a finance charge on insurance premiums that it finances through a premium loan. The finance charge must be computed (1) on the amount of the entire premium loan advanced, after subtracting any down payment on the premium loan; (2) from the inception date of the insurance contract or from the premium’s due date through the final installment’s payable date, disregarding

any grace period or credit allowed for payment of the premium; and (3) at a maximum rate of 1.15% for each 30 days, charged in advance.

Special Charges: A premium finance agreement may require the insured to pay a delinquency and collection charge on each installment that is in default for a period of not less than five days. The charge must be at least \$1 and may not exceed 5% of the installment in default or \$8 with respect to private passenger automobile or personal fire or liability insurance and \$100 for commercial automobile, fire, or liability insurance. Only one such charge may be collected on an installment, regardless of the period during which the installment remains in default.

A premium finance agreement may also require the insured to pay a cancellation charge if a default in paying an installment results in the cancellation of an insurance contract named in the agreement. The charge must be, with respect to private passenger automobile or personal fire or liability insurance, equal to the difference between the applicable delinquency and collection charge and \$15. If the charge relates to commercial automobile, fire, or liability insurance, it must be 5% of the installment but not greater than the difference between the applicable delinquency and collection charge and \$100. If a notice of cancellation is withdrawn and the insurance coverage is reinstated, the agreement may require the insured to pay a reinstatement charge in the same amount as the cancellation charge that would have been paid.

Electronic Payment: A premium finance agreement may require the insured to pay an electronic payment fee if the insured elects to pay a premium finance company by means of an electronic payment. A premium finance company may charge an electronic payment fee, up to \$8, for actual expenses incurred for the electronic payment.

Notice Requirements: Generally, an insured may direct a premium finance company to send any required notice by personal delivery, first-class mail, commercial delivery service, electronic mail, or facsimile transmission. If a premium finance company obtains an insured's written consent, it may deliver notice by a method other than personal delivery, first-class mail, or commercial delivery.

Cancellation of an Insurance Contract: At least 10 days before cancelling an insurance contract, a premium finance company must deliver or mail to the insured written notice of intent to cancel the contract unless it receives the required installment payment within the 10 days. The cancellation of a contract on the date stated in either the notice of intent to cancel or the notice of cancellation is not superseded by a premium finance company's issuance of a subsequent notice of intent to cancel or notice of cancellation. If the insurance contract relates to automobile liability, the notice of intent to cancel must include specified information.

At the end of the 10-day period, the premium finance company may cancel the insurance contract by, delivering or mailing a copy to the insured's last known address, a notice of cancellation that states the cancellation's effective date. The cancellation's effective date is dependent on whether the insurer receives the notice of cancellation within 30 days of the notice's stated effective date of cancellation.

When an insurance contract is canceled, the insurer must return any gross unearned premiums that are due under the insurance contract, computed *pro rata*, to the premium finance company for the account of the insured within 45 days after (1) receiving a notice of cancellation from the premium finance company or the insured; (2) the date that the insurer cancels the contract; or (3) completion of any payroll audit necessary to determine the amount of premium earned while the insurance contract was in force. Such an audit must be performed within 45 days after the insurer receives the notice of cancellation.

After the insurer returns to the premium finance company any gross unearned premiums that are due under the contract, the premium finance company must refund to the insured the amount of unearned premium that exceeds any amount due under the premium finance agreement. A premium finance company is not required to refund any amount that would be less than \$5.

Whenever an insurer, after receiving notice of the existence of a premium finance agreement, returns any unearned premiums to a person other than the premium finance company named in the agreement, the insurer is directly responsible to the company for all unearned premiums arising from the cancellation. If the insurer fails to return the necessary amount, interest accumulates at 1% per month on the unearned premium that has not been returned until the unearned premium is returned.

An insurer may not deduct from any returned premium any amount owed to the insurer by the insured under another insurance contract. An insurance producer must return any gross unearned commission to an insurer within a reasonable time period as required by the insurer.

Maryland Automobile Insurance Fund (MAIF): MAIF may not provide directly or indirectly for the financing of premiums or accept premiums on an installment basis.

Background: A 2011 Maryland Court of Appeals case, *MIC v. Central Acceptance Corp.* 33 A.3d 949, 424 Md. 1 (2011), held that the application of the "Rule of 78s" by eight of the State's largest premium finance companies to calculate the amount of interest due violates the requirement under current law that a premium finance company may not charge more than 1.15% for each 30-day period.

Under the bill, a premium finance company must use the actuarial method to calculate interest. The actuarial method precomputes interest, as opposed to using simple interest. An account that has precomputed interest has debt that is expressed as a sum comprising the principal and the amount of the finance charge computed in advance. A simple interest account is one in which the balance includes only the principal amount. The interest calculated from payment date to payment date is subtracted from the total amount of the payment and the remainder of the payment is subtracted from the principal balance.

As 97% of MAIF's policyholders use a premium finance company, the bill could have a significant impact on these policyholders.

Small Business Effect: The bill has a meaningful beneficial impact to premium finance companies, some of which are small businesses. For MAIF policies alone, the change in interest computation and the increase in various charges significantly increases revenue.

MAIF advises there were 64,045 *applications* for coverage under MAIF in 2012 with a 50% cancellation rate after four months. Due to the \$7 increase in late fees, if each policyholder made one late payment, premium finance companies would collect an additional \$434,866 in delinquency and collection fees from the 97% of MAIF policyholders who use premium finance companies. An additional \$310,623 is collected due to the \$10 increase in cancellation charges. A premium finance company's revenue also increases from the bill's change in interest computation and increase in reinstatement fees.

Additional Information

Prior Introductions: None.

Cross File: None.

Information Source(s): Maryland Insurance Administration, Maryland Automobile Insurance Fund, Maryland Court of Appeals, Indiana Department of Financial Institutions, Department of Legislative Services

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