Department of Legislative Services

Maryland General Assembly
2013 Session

FISCAL AND POLICY NOTE
Revised

Senate Bill 930 (Senator Pugh, *et al.*)

Finance Economic Matters

Property and Casualty Insurance - Premium Payments - Acceptance on Installment Payment Basis and Premium Finance Agreements

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This bill authorizes the Maryland Automobile Insurance Fund (MAIF) to accept premiums on an installment payment basis on 12-month personal lines policies if specified requirements are met and the Insurance Commissioner provides approval. The bill also authorizes MAIF add-on coverage to include motor club services. Likewise, it authorizes a premium finance company to enter into a premium finance agreement that includes the costs of a motor club service contract. The bill also alters (1) the amount of a cancellation charge in years subsequent to calendar 2014 and (2) the circumstances in which a premium finance agreement may require an insured to pay a cancellation charge and a reinstatement charge. The bill requires premium finance companies to make specified disclosures, including that the actuarial method will be used to calculate an earned finance charge when applicable. The bill authorizes premium finance companies to assign all rights and obligations under a premium finance agreement to another premium finance company or pledge a premium finance agreement as collateral for a loan.

The bill also requires specified studies from MAIF and the Maryland Insurance Administration (MIA) with various reporting dates.

The bill takes effect July 1, 2013. The provisions related to premium finance companies assigning rights or obligations under, or pledging as collateral, a premium finance agreement abrogate after June 30, 2015.

Fiscal Summary

State Effect: General fund revenues decrease minimally if MAIF lowers its premiums due to the bill. Special fund revenues increase by $125 for the one-time form filing fee charged to MAIF. MIA can handle review of the installment payment plan and the evaluation report and the report to the General Assembly with existing resources.

MAIF Effect: MAIF's nonbudgeted expenditures increase minimally due to processing monthly installment payments. MAIF's nonbudgeted revenues from installment fees increase correspondingly to cover additional expenditures; the magnitude of the increase depends on the number of MAIF policyholders who choose to pay on an installment basis. MAIF is unable to predict the number of policyholders who will choose to pay on an installment basis. Increases in fee revenues may be offset by decreases in premium revenues to the extent that MAIF is able to lower its premiums as a result of the bill.

Local Effect: None.

Small Business Effect: Meaningful.

Analysis

Bill Summary:

MAIF and Installment Payment Plans: When considering whether to accept MAIF's plan to accept premiums on an installment payment basis, the Commissioner must ensure that MAIF's installment payment plan:

- requires an insured's initial premium payment to be at least 25% of the total premium if the total annual premium is less than $3,000;
- requires an insured's initial premium payment to be at least 20% of the total premium if the total annual premium is $3,000 or more;
- adjusts the amount of the total annual premium used to determine the initial premium payment on October 1 of each year using specified data from the U.S. Government Bureau of Labor Statistics;
- is structured and administered to ensure that MAIF at no time provides insurance coverage to an insured for a period during which MAIF has not received the actuarially justified premium payment;
- offers no more than six installment payments on the 12-month policy if the total annual premium is less than $3,000;
- offers no more than eight installment payments on the 12-month policy if the total annual premium is $3,000 or more;
- allows insureds to make an initial premium payment and installment payments in any commercially acceptable form; and
- allows MAIF to impose an administrative processing fee on insureds participating in the installment plan of up to $8 per installment payment.

The bill prohibits MAIF from (1) discriminating among insureds by charging different premium based on the payment option selected by an insured and (2) determining commissions paid to a MAIF producer based on whether the producer places an insured in an installment payment plan.

Disclosure Requirements: The bill requires that any written and electronic communications, including MAIF's website, affecting the placement of coverage by MAIF or a MAIF producer must include a statement, on a Commissioner-approved form, advising an applicant or an insured of the payment options available to the applicant or insured. The statement must state that the applicant or insured (1) may make payments through MAIF's installment plan, a premium finance agreement, or payment of the policy in full and (2) should consult a MAIF producer who will fully describe the terms of each payment option.

The bill requires that the statement be included on written or electronic communications when the applicant or insured (1) is issued a new policy or (2) is issued a reissuance, rewrite, or renewal of an existing policy.

Computation and Implementation of Various Charges: Any finance charge by a premium finance company 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 requires a premium finance company to calculate the finance charge as earned in 30-day increments and authorizes the company to earn the finance charge on the first day of each 30-day period. If the finance charge is earned on the first day, the premium finance agreement must contain a notice detailing this fact. A premium finance company may not retain more of the finance charge than is earned. The bill imposes additional restrictions on the imposition of a finance charge in connection with a commercial automobile, fire, or liability insurance policy. The bill prohibits a premium finance company from using the Rule of 78s to compute a finance charge.

The bill requires the premium finance company to refund to an insured a finance charge that exceeds any amount due under the premium finance agreement if the insurance contract is cancelled or the insured prepays the loan in full at any time. If the insured receives a refund, the bill specifies that the amount of the refund may be calculated using the actuarial method. The bill also alters the amount of time an insurer has to return any gross unearned premiums after the cancellation of an insurance contract.

The bill authorizes a premium finance agreement to impose a cancellation charge on or after the effective date stated in the notice of cancellation or on or after the cancellation effective date stated in the notice of intent to cancel. If the cancellation charge is imposed on or after the cancellation effective date, the premium finance company must provide a specified disclosure in the notice of intent to cancel. The bill increases the amount of a possible cancellation charge for private passenger automobile or personal fire or liability insurance by an additional dollar for each calendar year after 2014. Thus, a possible cancellation charge is the difference between a delinquency and collection charge and $15 in calendar 2014, escalating to $20 in calendar 2019 and any subsequent year.

The bill authorizes a premium finance company to charge an electronic payment fee if the insured elects to pay by electronic check, as defined by the bill. Additionally, a premium finance company may send any required notice through electronic means if the premium finance company meets specified requirements.

Motor Club: A premium finance company may not impose any finance charge or other charge on any payment for the purchase price of a motor club service contract. Additionally, the bill prohibits a premium finance company from canceling an insurance contract if any payment under the premium finance agreement (1) is sufficient to pay the installment due under the agreement that is related to the insurance contract obligation but (2) is not sufficient to cover the amount of the monthly payment for the motor club service contract.

The bill requires an insurance producer, or an employee or agent of the insurance producer, who directly or indirectly has an ownership interest in a motor club to provide a disclosure to be signed by the insured informing the insured of any interest in the motor club of the insurance producer or the producer's employee or agent.

Assignment of Rights and Obligations: If a premium finance agreement is for the payment of private passenger motor vehicle insurance and/or personal insurance, the bill authorizes a premium finance company to (1) assign all rights and obligations under a premium finance agreement to another State-registered premium finance company or (2) pledge a premium finance agreement as collateral for a loan.

The bill also authorizes a premium finance company that is a party to a premium finance agreement for commercial automobile, fire, or liability insurance to assign all rights and obligations under a premium finance agreement to another person if the premium finance agreement expressly confers the right to assign all rights and obligations under the premium finance agreement. The premium finance company may also pledge a premium finance agreement as collateral for a loan. If the premium finance company assigns rights and obligations, it must retain the obligation to service the premium finance agreement or assign the obligation to another State-registered premium finance company.

Regardless of the type of insurance, in the event the premium finance company assigns the obligation to service a premium finance agreement to another premium finance company, it must provide the insured with notice of the assignment and the third-party premium finance company's contact information. Any such notice must be by (1) first-class mail or (2) if specified requirements are met, electronic means.

These provisions remain in effect for two years and terminate after June 30, 2015.

The bill requires MIA to keep track of complaints received from consumers who have had all rights and obligations under premium finance agreements for commercial automobile, fire, or liability insurance assigned. MIA must report any findings and recommendations to the Senate Finance Committee and the House Economic Matters Committee by December 31, 2014.

Other Evaluations and Reports: The bill requires that MAIF's Executive Director, in consultation with the Commissioner and appropriate State agencies, develop criteria for evaluating the impact and effectiveness of MAIF's installment payment plan. The evaluation must consider the plan's impact on the (1) cost of automobile insurance for MAIF insureds; (2) the number of insured and uninsured motorists in the State; (3) the number of MAIF policies in force by geographic area; (4) the duration of MAIF policies in force; and (5) the frequency of payment methods used by MAIF insureds, including MAIF's installment payment plan, premium finance agreements, and cash and credit card payments.

By October 1, 2015, MAIF must prepare a report on the impact and effectiveness of the installment payment plan for the prior year and submit it to the Commissioner. The report must be based on the aforementioned evaluation criteria and limitations associated with the terms of the installment payment plan established by the bill. Once the Commissioner receives the report, the Commissioner must make a determination of the impact and effectiveness of MAIF's installment payment plan, including a review of complaints received by the Commissioner relating to MAIF's installment payment plan and premium finance agreements. Based on this determination, the Commissioner must submit a report to the Senate Finance Committee and the House Economic Matters Committee by December 31, 2015.

Current Law:

MAIF: Created by the General Assembly in 1972, MAIF provides automobile liability insurance to residents of the State who are unable to obtain policies in the private insurance market. MAIF is authorized to insure a person who owns or leases a vehicle registered in the State, has a valid State driver's license, and has made good faith attempts to obtain a policy from at least two private insurers and has been rejected or refused for any reason other than nonpayment of premiums. In other states, private insurance companies share in insuring those unable to obtain insurance (known as the residual market) through an assigned risk plan in their respective state.

MAIF may not provide directly or indirectly for the financing of premiums or accept premiums on an installment basis. A premium owed to MAIF may be financed by a premium finance company registered with the Insurance Commissioner. Thus, policyholders who are unable to pay their total insurance premium in advance must use the services of a premium finance company. The policyholder enters into a premium finance agreement, where the premium finance company pays the policyholder's total premium to MAIF and the policyholder agrees to repay the loan with finance charges and service fees in installments.

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 or 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 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 commissions to an insurer within a reasonable time period as required by the insurer.

Background: MAIF is the only state fund mechanism established to provide automobile insurance to applicants who cannot obtain coverage in the voluntary market. Neighboring jurisdictions such as District of Columbia, Delaware, Virginia, and Pennsylvania each have a direct assignment system in which applicants who cannot obtain insurance in the voluntary market are shared equitably among all insurers licensed to write automobile insurance. Each of these jurisdictions allows the payment of premiums on an installment basis.

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 may 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.

State Revenues: MAIF is subject to the 2% premium tax administered by MIA. General fund revenues from the premium tax decrease to the extent MAIF is able to lower its premiums because of the bill. Any such decrease in revenues cannot be accurately estimated but is assumed to be minimal. Based on information attained for prior introductions with similar provisions, MIA anticipates that MAIF will make one filing subject to the $125 filing fee as a result of the bill.

MIA can handle review and approval of the installment payment plan, review of the evaluation report, tracking of complaints, and the reports to the General Assembly with existing resources.

MAIF Effect: MAIF's nonbudgeted revenues increase to the extent its policyholders choose to pay premiums on an installment basis. MAIF advises that it has approximately 40,931 private passenger policies *in force* and that most policyholders currently finance their premiums through a premium finance company. Some installment payments may be submitted by electronic fund transfer, but the majority are likely to be paid by check.

The bill authorizes MAIF to impose an administrative processing fee of up to $8 per installment payment. The bill also prohibits MAIF from instituting an installment plan that requires more than six or eight payments per year, depending on the amount of the annual premium. For the purposes of this estimate, it is assumed that MAIF charges the maximum fee allowed under the bill for each payment; however, any processing fee must be approved by the Insurance Commissioner. *For illustrative purposes only*, if MAIF charges an $8 bimonthly fee to 15,200 policyholders, its revenues increase by $729,600 on an annual basis.

To the extent MAIF's fee revenues exceed its additional expenditures, MAIF can lower its premium rates. MAIF advises that the bill may save MAIF policyholders between $200 and $400 per year.

MAIF can report on the impact and effectiveness of its installment payment plan with existing resources.

Small Business Effect: Small premium finance companies that finance MAIF insurance premiums may experience a significant loss of business to the extent MAIF policyholders choose to pay premiums on an installment basis through MAIF. Currently 97% of MAIF's policyholders use a premium finance company to pay their premiums. It is assumed that the vast majority of these policyholders will participate in MAIF's installment plan rather than use a premium finance company. Thus, these companies will experience a significant loss of revenue.

Small businesses that purchase insurance through MAIF and currently use premium finance companies may experience savings to the extent MAIF's fees are lower than the fees and interest charged by their premium finance companies. Any such impact is assumed to be minimal.

The bill also has a meaningful beneficial impact to premium finance companies, some of which are small businesses, due to the bill's provisions relating to the finance charge computation and increase in various charges.

Additional Information

Prior Introductions: A similar bill, SB 394 of 2011, was heard by the Senate Finance Committee, but no further action was taken. SB 603 of 2008, another similar bill, received a favorable report from the Senate Finance Committee and passed second reading, but no further action was taken. Its cross file, HB 32, received a favorable report from the House Economic Matters Committee, but no further action was taken. Similar bills were introduced in the 2005 through 2007 sessions.

Cross File: None.

Information Source(s): Maryland Insurance Administration, Maryland Automobile Insurance Fund, Maryland Department of Transportation, AlPSO, Department of Legislative Services

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