Insurance Premium Financing

Frank A. Valenti

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INSURANCE PREMIUM FINANCING

I. INTRODUCTION

As consumer protection has come into fashion, its legal aspects have become a favorite topic for analysis. One area of potential concern, insurance premium financing, has not been legally explored. This lack of attention is probably due to the emergence of premium financing and its gradual acceptance by the consuming public only over the past decade.

This comment will consider the origin, mechanics, function, and legality of various aspects of premium financing. For analytical purposes, it will be divided into four basic sections. In the first two sections some fundamental elements of insurance premium financing will be discussed. Consideration of the evolution and validity of regulation will be set forth in the next section. Finally, the comment will conclude with an analysis of some current controversies, particularly the "cancellation tort-victim controversy."

II. SOME FUNDAMENTALS OF INSURANCE PREMIUM FINANCING

A. Origin

The contemporary era can be characterized as an age of credit. Installment credit is extensively used in purchasing durable consumer goods, and services, and has become an integral part of the American economy. This general acceptance of installment buying is not new. The time-sale of automobiles and television sets, and the revolving credit plans of most department stores were the forerunners of the credit revolution. Today such diverse uses as church donations, doctors' visits, bail, and city fees ranging from business licenses to civic theater tickets can be made of credit cards. In some areas, even federal income taxes can now be charged on bank credit cards.¹

It is hardly surprising that the payment of insurance premiums has also been engulfed by the credit revolution. Insurance companies inaugurated this development with their time honored policy of granting a discount if a term policy premium was paid in advance. Under such a plan, five-year coverage for four annual premiums, or three year coverage for two-and-a-half annual premiums, was offered for full payment for the entire term made at the policy's inception. This practice resulted in a benefit to the insurance company as well as the insured since in addition to saving money by not having to issue a new

¹ TIME, Jan. 26, 1970, at 70.
policy each year, the company obtained the benefit of increased investment income. In the 1940's, a new plan, which still offered the discount but provided for annual installments, was introduced. This development was the beginning of what are known as deferred payment plans. Presently, insurance companies provide for the payment of annual premiums on an installment basis for most customers. Typically, the insured pays 40% of the annual premium at the outset and two subsequent 30% installments.

Even with these plans, the payment of insurance premiums may still impose a heavy financial burden on the insured. Compulsory automobile liability insurance or financial responsibility statutes virtually make insurance a requisite to earning a living. This is true not only for those who must drive as part of their business, but also for those who rely on their automobiles for transportation to and from their place of employment. Ever increasing automobile insurance rates, which reflect the radically rising costs of medical expenses and automobile collision repairs compound the financial burden caused by compulsory insurance. Moreover, the adverse experience of insurance companies in underwriting automobile insurance forces many drivers to pay the higher premiums of assigned risk plans. Under many of these plans the full annual premium is due in a lump sum at, or shortly after, the inception of the policy.

A number of insureds do not enjoy the best of credit, thus lending facilities are not immediately available to help them meet their premium payments. American business ingenuity, sensing the need inherent in this situation, set out in search of a workable, and profitable, solution. As a result, premium financing came into existence and has become a natural vehicle for insurance premium payment.

Use of premium financing services is steadily increasing. Since 1962 the amount of premiums financed in New York has doubled to over $100 million per year. In 1966 more than 286,000 premium finance agreements were entered into in New York state alone.

B. Nature of Premium Financing

Financing insurance premiums necessarily differs from ordinary security interest credit transactions. In ordinary security interest transactions, the

3. E.g., N.Y. INS. LAW § 63 (McKinney 1966).
4. 1967 N.Y. SUP'T OF BANKS ANN. REP. 136. Similarly, Virginia has seen a yearly increase in financed premiums. There, in 1967, more than $12 million in premiums were financed. Johnson, Problems in Premium Financing, BEST'S INSURANCE NEWS, Oct. 1968, at 47. In North Carolina, premiums of $18 million or 5.3% of all the premiums written in that state in 1965, were financed. Address by Edward L. Denton, Jr., Third Annual Insurance Premium Finance Seminar sponsored by the North Carolina Department of Insurance, May 10-11, 1967 [hereinafter referred to as Denton speech]. Mr. Denton's speech has served as a background for much of the material in this comment.
chattel to be purchased with the loan in question usually serves as collateral to protect the lender’s interest. If the borrower defaults in his installment payments, the lender can foreclose on the chattel to protect his interest. This kind of creditor protection, however, is not possible in insurance premium financing transactions. When an insurance contract is financed, owing to the purpose for which the loan is given, no tangible security is involved which may be subject to foreclosure upon default. What is actually financed is an intangible—protection. As a result, a modified form of the standard security interest used in ordinary credit transactions is required to protect the interest of the financing agency. To accomplish this, the premium finance agency obtains a power of attorney from the insured permitting it to effect cancellation of the financed insurance contract in the event the insured defaults in his installment payments. Coupled with this cancellation power, the finance agency receives an assignment from the insured, of the unearned premium payable under the insurance contract. In this manner, the finance agency protects its investment in the event of the borrower’s default.

The effectiveness of this technique requires that the financed insurance contract be cancellable. Examples of such cancellable policies which are ordinarily financed today are auto, fire, theft, homeowners’, workman’s compensation, and inland marine. In addition larger premium finance agencies will finance the expensive commercial package policies of a business concern. Such policies often include all of the various types of insurance that the concern requires for its successful operation.

Before a more detailed examination of premium financing is pursued, an illustration of the ordinary premium finance transaction would be helpful. Suppose a hypothetical driver, reviewing his financial situation, concludes that even under a 40-30-30 payment plan his automobile insurance premiums totaling $300 annually have become an excessive financial strain. Assume further, that this driver lives in a state where automobile liability insurance is compulsory. Thus, if the driver sees his driving privilege as an absolute necessity, his alternatives are automatically limited. Hence, he may decide to have his insurance contract financed. He contacts his insurance broker (or agent) and enters into a premium finance agreement7 with him. Normally a down payment of about 30% is required; say $100 in our hypothetical. According to the standard agreement form, the hypothetical driver agrees to pay the broker (the payee) six $36 monthly installments in consideration for the payment of the amount financed, here $200, to the insurance company. Included in these $36 payments is a total finance charge of $16. As security for repayment, the

7. “Premium finance agreement” means a promissory note or other written agreement by which an insured promises or agrees to pay to, or to the order of, either a premium finance agency or an insurance agent or broker the amount advanced or to be advanced under the agreement to an authorized insurer or to an insurance agent or broker in payment of premiums on an insurance contract, together with a service charge as authorized and limited by law. N.Y. Banking Law § 554(8) (McKinney Supp. 1969-70).

8. Installments are normally spread over periods ranging from four to nine months.
insured assigns to the broker any unearned premium to which he may become entitled under the policy. In addition, he agrees to pay a late charge of 5% of any installment in default. If default results in cancellation of the insurance contract, there will be an additional charge equal to the difference between any late charge and $5. More importantly, the driver agrees that if default occurs, he irrevocably appoints the broker his attorney-in-fact, authorized to cancel the insurance contract. He also agrees that should the agreement be referred to an attorney for collection, he will pay as attorney's fees 20% of the amount due.

After this transaction has been completed, the broker will frequently assign the agreement to a premium finance agency and the agency in turn will forward to him the $200 that is being financed. The broker then remits the total premium to the insurance company. Meanwhile, the insured driver receives a payment book from the finance agency and proceeds to make his $36 monthly payments.

Suppose that after making two such monthly payments the insured driver defaults on his next monthly payment. Five days after the due date, the insured will receive from the agency a notice of default and intent to cancel which states that his insurance contract is to be cancelled in 13 days unless the default is cured by payment. If the driver ignores this notice and 13 days elapse, the agency will effect cancellation by notifying the insurance company. Shortly thereafter the insurance company sends the agency the unearned premium on the policy. From this sum the agency satisfies the insured's obligation to it. The insured, however, remains liable to the agency for any deficiency in his account balance in the event the unearned premium is not sufficient to satisfy the outstanding claim. As would logically be expected, the insured is entitled to any unearned premium in excess of his account balance.9

III. FURTHER CONSIDERATIONS

Whether any particular feature of premium financing is favorable depends on the interests of the party. Without question, premium financing is a headache for insurance companies because of the extra paper work that it entails. Moreover, a fourth party has been brought into the picture meaning that another opportunity exists for error in handling the account. For the finance agency, however, premium financing represents a profitable enterprise. Perhaps

9. Upon the insured's default, premium finance agencies in the past have attempted to bring suit against assigning brokers on the assigned note. Under the Uniform Commercial Code such an action appears possible. N.Y. U.C.C. § 3-202(4) (McKinney 1964). In New York, however, there is judicial authority to the effect that under its premium finance statute such an assignment is implied to be without recourse unless the finance agency and the broker mutually agree that the agreement is with recourse. Standard Premium Plan Corp. v. Hirschorn, 56 Misc. 2d 687, 290 N.Y.S.2d 226 (Civ. Ct. of City of N.Y. 1968); Standard Premium Plan Corp. v. Wolf, 56 Misc. 2d 522, 288 N.Y.S.2d 987 (Civ. Ct. of City of N.Y. 1968). In both of these cases the statutory provision in issue was N.Y. BANKING LAW § 566(2) (McKinney Supp. 1969-70).
most importantly, premium financing allows many people to purchase insurance which otherwise would be beyond their means.

All kinds of people avail themselves of premium financing. Most obvious are those to whom it is a sheer economic necessity. Especially likely to be included in this category is the driver under 25 who because of his age faces high insurance rates, or the driver subject to the higher rates of an assigned risk plan. The businessman who has the large premiums of a commercial package policy is another prospect likely to prefer spreading his payment over the term of the policy; he too will often make use of a premium finance agency's services.

The premium finance agency, existing as an independent enterprise, is not the only available institution which finances insurance premiums. In some communities, local banks provide premium financing. Many insurance agents and brokers, licensed under state law likewise finance the premiums they handle. Several insurance companies also have set up installment payment plans for premiums.

IV. STATE REGULATION

A. The History of Regulation

Relatively insignificant a decade ago, premium financing has become a billion dollar business. Both the great number of people and the enormous sums of money involved in premium financing point to the need for regulation.

As recently as ten years ago, there were no laws which regulated premium finance agencies. As a result, obviously usurious plans were all too common. In 1960, a New York legislative committee studying insurance premium financing reported that some finance agencies, without any statutory authority, were charging insureds a simple interest equivalent of more than 26% per annum, rates far in excess of those which other premium finance agencies were currently charging. Prior to the enactment of the Virginia premium finance law, an agent is reported to have been collecting $6 per week from an insured, of which more than $3 was an interest charge.

The oppressed insured, in demanding regulation of this unscrupulous practice, was not alone in instigating state action. Many legitimate premium

10. A reduced license fee is often provided for insurance agents or brokers who finance premiums the aggregate unpaid balance of which does not exceed a specified dollar amount. E.g., N.Y. BANKING LAW § 566(1) (McKinney Supp. 1969-70).
11. While insurance company plans usually have much lower rates than those currently charged by premium finance agencies, many agents and brokers, in spite of this price advantage prefer not to use company plans because most often these plans are restricted to premiums of the particular company offering the service. If an agent has more than one company in his agency which have installment plans, this may mean many different forms and procedures, all of which can be quite confusing as well as costly.
12. MEMORANDUM OF JOINT LEGISLATIVE COMMITTEE ON COMMERCE AND ECONOMIC DEVELOPMENT, N.Y. LEGISLATIVE ANNUAL, at 46.
finance agencies also sought permissive legislation because a state's general usury statute, when applied to the premium finance industry, was often unduly restrictive. The nature of the premium finance business dictates that most of the accounts handled are relatively small.\(^{14}\) When a general usury rate of 6%, for example, is applied to the small accounts of a premium finance agency, profit ratios often will not match those of other legitimate businesses. Hence, there evolved a movement from within the industry for authorization of a rate which would yield a return more in line with that of other businesses.

Few states have responded to the call for legislation to specifically regulate premium financing.\(^{15}\) The first state to pass such legislation was New York.\(^{16}\) A primary reason for the New York Legislature's action was "the increasing need for facilities for installment financing of insurance premiums occasioned, in part, by the inability of many insureds to pay in one lump sum annual premiums as high as $500 for compulsory automobile liability insurance."\(^{17}\) It was the Legislative Committee's belief that premium finance regulation would "fill a vacuum in the existing statutes and [would] further the interests of the consumer, the public and both the underwriting and producing segments of the insurance industry; and it would make insurance premium financing more readily available to the consumer at fair rates and create a sound legal basis for insurance premium financing in place of . . . unregulated practices of doubtful legality."\(^{18}\) The Legislative Committee was informed that its proposed legislation had the endorsement of the major segments of the premium finance industry.\(^{19}\)

Following the New York example, several other states enacted specific premium finance legislation.\(^{20}\) As in New York, the proximate cause in North Carolina was a compulsory automobile liability statute. In Maryland, which has an Unsatisfied Judgment Fund contributed to by uninsured drivers, the need for premium financing was caused by the fact that the uninsured motorist's fee had reached about $80, which in some instances was higher than the cost of automobile liability insurance. Under these circumstances, many vehicle owners purchased insurance to avoid the uninsured motorist fee, made a small

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14. The average size premium finance account in North Carolina in 1966 for example was $106.09. Denton speech supra note 4. In New York, statistics reveal that a few years ago 78.3% of all premium finance accounts were under $200. Id.


18. Id. at 46-47.

19. Id. at 47.

20. See note 15 supra.
down payment, and, after obtaining their registration plates, permitted the insurance to be cancelled. In light of such developments, the Maryland General Assembly decided that premium finance agencies should be regulated; in 1964, a law was passed.  

As various states have considered premium finance statutes, premium finance agencies, especially those that operate in more than one state, have endeavored to minimize the difference between state laws. For these agencies, a minimum of difference and variation among jurisdictions results in more economical operations.  

The National Conference of Commissioners on Uniform State Laws has recently considered premium finance regulation in the preparation of the Uniform Consumers Credit Code.\(^2\) The overall philosophy of the UCCC is that "'credit transactions' is a single subject of law notwithstanding its many facets."\(^2\) In keeping with this philosophy, the Conference decided that the UCCC would contain no distinctive rules for insurance premium loans as opposed to ordinary consumer loans. It concluded "that the [general] provisions of the Act may appropriately be applied to insurance premium loans."\(^2\)

That the Conference reached this decision seems unfortunate, for the differences between insurance premium loans and other consumer loans appears to warrant distinctive rules for premium financing. In addition to the fundamental difference between the two in terms of the lender's security protection device,\(^4\) there are other more subtle variances that appear to require specific statutory attention. Primary among these is the inclusion in premium finance transactions of a third party, the broker or agent, not generally found in other types of consumer loans. Regulation of the relationship of this third party to both the borrower (the insured) and the lender (the finance company) is desirable. In addition, specific rules governing cancellation charges would be beneficial to all parties. Moreover, if the interests of potential third party automobile accident victims are to be considered, detailed regulation of cancellation procedures appears crucial.\(^5\)

Little difference in substance exists among the limited number of premium finance statutes presently in effect. New York's well drafted statute, has served as a basis for the statutes of several other states. Fundamental to any understanding of premium finance regulation is an awareness of the typical substantive provisions in premium finance statutes. The New York statute will serve as a suitable model here.\(^6\)

All premium finance statutes include a licensing provision. The New York

\(^{21}\) 1 P-H 1969 Consumer and Commercial Credit—Installment Sales ¶ 12,103 et seq. [hereinafter referred to as UCCC].

\(^{22}\) Id. ¶ 12,103 (official comment).

\(^{23}\) Id. ¶ 12,523 (official comment 4).

\(^{24}\) See text accompanying note 6 supra.

\(^{25}\) See text accompanying notes 60-72 infra.

statute provides that no person shall engage in the business of premium financing without a license obtained from the superintendent of banks. Among the states that have premium finance statutes, similar criteria have been established as prerequisites to the acquisition of a license. The New York statute typically maintains that “the financial responsibility, experience, character, and general fitness of the applicant or any person associated with the applicant must command the confidence of the community and warrant the belief that the business will be conducted honestly, fairly, and efficiently within the purpose and intent” of the statute. An insurance agent or broker may be licensed as a premium finance agency, and a reduced license fee is permitted where the license application states that the aggregate unpaid balance of all premium finance agreements to be held by such applicant will not exceed a stated sum. The superintendent of banks is authorized to revoke or suspend any license upon a finding of certain specific statutory violations.

To reinforce the licensing provision in New York, a distinct statute directed at the insurer dictates that an insurer or its agent may not knowingly accept payment of premiums for an insurance contract financed under a premium finance agreement from any person, firm, or corporation not authorized to engage in premium financing in accordance with the Banking Law. It further states that an insurer cannot honor a power of attorney to cancel an insurance contract except in accordance with the cancellation provisions of the premium finance statute.

The superintendent is authorized by statute to make rules and regulations, conduct hearings, and make such orders and findings as may be necessary for the proper conduct of business by insurance premium finance companies, and for the enforcement of the statutory provisions regulating premium financing. In addition, he has authority to make such investigations as he deems necessary to determine whether any licensee has violated the statute, and to make examinations of books, records, and accounts used in the business of any licensee to determine whether any statutory violations have taken place. Pursuant to his investigative power, the superintendent, or any person designated

27. Excepted from the requirements of this provision are banks and authorized insurers. N.Y. BANKING LAW § 555(1) (McKinney Supp. 1969-70).
31. Id. § 559. Among these violations are: failure to pay the annual license fee; failure to comply with any lawful demand, ruling, or requirement of the superintendent; violation of the Federal “Truth-in-Lending Act.” Cf. ILL. ANN. STAT. § 1065.65 (Smith-Hurd Supp. 1970); N.J. STAT. ANN. § 17:16D-6 (Supp. 1969-70).
32. N.Y. INS. LAW § 153(2) (McKinney 1966).
33. Id. § 153(3).
36. Id. § 560(2).
by him, may subpoena witnesses, administer oaths, and compel by order or subpoena the production of books, records, and accounts.\textsuperscript{37}

In addition to close administrative control of licensees, almost all of the various regulatory statutes presently in effect govern the form and content of premium finance contracts. A premium finance agreement must be in writing with a minimum print-size required.\textsuperscript{38} The writing must contain the entire agreement\textsuperscript{39} as well as certain wording set forth in the statute.\textsuperscript{40} Moreover, the New York statute incorporates by reference the Federal "Truth in Lending Act".\textsuperscript{41} No premium finance agreement can be signed by an insured when it contains any blank space to be filled in after it has been signed.\textsuperscript{42}

A maximum service charge of "ten dollars per one hundred dollars per annum" and a minimum service charge, varying from $8 to $15 depending on the number of monthly installments, is provided for.\textsuperscript{43} In the event of default on an installment for a period of not less than five days, a delinquency charge not in excess of five per cent of the installment or five dollars is allowed on each installment in default.\textsuperscript{44} Further, if the default results in cancellation of a financed insurance contract, a cancellation charge "equal to the difference between any delinquency and collection charge imposed in respect to the installment in default and five dollars" is permitted.\textsuperscript{45} A premium finance agreement may also provide for the payment of attorney's fees not exceeding 20 per cent of the amount due if the agreement is referred to an attorney for collection.\textsuperscript{46}

Many financed insurance contracts are for automobile liability insurance. Due to the possible adverse ramifications of cancellation of this type of insurance both to the insured and to potential innocent tort victims of the insured, premium finance statutes generally require strict procedures for cancellation of insurance contracts. When a premium finance agreement contains a provision permitting cancellation by a power of attorney, the insurance contract cannot be cancelled unless effected in the statutory manner.\textsuperscript{47} Among the statutory requirements that must be complied with to effect cancellation are: (1) that

\textsuperscript{37} Id. § 562.
\textsuperscript{39} N.Y. Banking Law § 567(2) (McKinney Supp. 1969-70).
\textsuperscript{40} Id. § 567(2). The wording is as follows: "NOTICE: 1. Do not sign this agreement before you read it or if it contains any blank space. 2. You are entitled to a completely filled in copy of this agreement. 3. Under the law, you have a right to pay off in advance the full amount due and under certain conditions to obtain a partial refund of the service charge."
\textsuperscript{41} Id. § 567(3)(b). The "Truth-in-Lending Act" is basically a disclosure statute.
\textsuperscript{42} Id. § 567(4).
\textsuperscript{44} N.Y. Banking Law § 569(1) (McKinney Supp. 1969-70).
\textsuperscript{45} Id.
\textsuperscript{46} Id. § 569(2).
ten days unconditional notice be served upon the insured before his insurance be cancelled; (2) that if this notice is served by mail an additional three days be allowed; (3) that the notice of cancellation include in type or print of at least twelve points, a statement that if the insurance involved is motor vehicle liability insurance, proof of financial security is required to be maintained continuously throughout the registration period, and that failure to maintain proof of such financial security requires revocation of the registration of the motor vehicle, unless the registration certificate and number plate of such vehicle have been surrendered to the commissioner of motor vehicles prior to the time at which cancellation becomes effective; (4) that all statutory, regulatory, and contractual restrictions providing that the insured may not cancel his insurance contract unless he or the insurer first satisfy such restrictions by giving a prescribed notice to a governmental agency, or an individual designated to receive such notice for said governmental agency, shall apply; (5) that the insurer within a reasonable time after cancellation returns whatever gross unearned premiums are due under the contract to the premium finance agency for the benefit of the insured; (6) that, subject to exception, upon the cancellation of motor vehicle liability insurance by a premium finance agency, notice of the cancellation must be filed by the insurer with the commissioner of motor vehicles not later than thirty days following the effective date of such cancellation.49

For violation of any provision of the premium finance statute misdemeanor criminal sanctions are authorized.50 Moreover, a premium finance agency which knowingly charges more than authorized, forfeits all charges which the premium finance agreement carries; if a greater charge is in fact paid by an insured, he is entitled to double damages from the premium finance agency.51

B. The Validity of Regulation

That a state may in the exercise of its police power regulate interest rates52 and require money lenders to obtain a license as a condition to carrying on business53 is firmly established. Further, reasonable state regulation of the

48. An insurer is not required to file a notice of cancellation where the insurer has been advised by the commissioner that such insurance has been superseded by another insurance contract which took effect at or prior to the time at which termination became effective, or where the insured has surrendered his registration certificate and number plates to the commissioner and has delivered to the insurer a copy of the notice indicating surrender at or prior to the time at which the termination became effective. N.Y. Veh. & Traf. Law § 313 (McKinney Supp. 1969-70).
51. Id. § 563(2).
53. Ex parte Fuller, 15 Cal. 2d 425, 102 P.2d 321 (1940); Berry v. Fort Worth, 110 S.W.2d 95 (Ct. of Civ. App. of Tex. 1937); Dunn v. City of Hoboken, 85 N.J. Law. 79, 88 A. 1053 (1913); Dewy v. Richardson, 206 Mass. 430, 92 N.E. 708 (1910).
small loan business in the public interest is not violative of due process of law.\textsuperscript{54}

Because the development of premium financing and the limited legislation that has slowly evolved with it are recent phenomena, there is very little specific authority directly concerned with the validity of premium financing. On principle, it would seem that a premium payment service plan entered into between an insured and a finance company not so connected with the insurer as to create conflicting interests would be valid and enforceable, providing the contract was fairly made and contained no provisions in conflict with statutory regulations governing insurance contracts.\textsuperscript{56}

Of the limited number of cases dealing with premium financing, the leading case directly concerned with its validity indicates that where a premium finance company is a third party, disinterested in the substance of the insurance contract, a premium finance agreement may be valid.\textsuperscript{66} Similarly, another case intimates that premium finance agreements might validly be made, provided the insured's statutory rights with respect to notice of cancellation are not violated.\textsuperscript{67}

Further authority dealing directly with the validity of premium financing agreements is wanting. Yet, because premium financing is in many respects similar to ordinary small loan transactions, case law on the latter, by analogy, seems applicable to premium financing.

In New York, while the Court of Appeals has not passed directly on the constitutionality of the Small Loans Act,\textsuperscript{58} it has approved the principle involved.\textsuperscript{59} This approval may indicate that the constitutionality of Article XII-B, the New York premium finance statute, is not in jeopardy. In fact, no statute regulating premium financing has yet been declared unconstitutional in any jurisdiction.

V. CURRENT CONTROVERSIES

A. Cancellation

Of the many ramifications of premium financing the cancellation feature is probably most debatable. As previously mentioned, due to the potential adverse consequence to third party accident victims, premium finance statutes generally mandate compliance with strict procedures to effectively cancel a financed insurance contract.\textsuperscript{60} Nonetheless, some critics contend that these statutory procedures are not adequate to protect the interests of potential tort victims.


\textsuperscript{55} See generally Annot., 115 A.L.R. 1212 (1938).


\textsuperscript{57} Clark v. Employers Mut. Cas. Co., 90 F.2d 667 (8th Cir. 1937).

\textsuperscript{58} N.Y. Banking Law art. 9 (§§ 340-65) (McKinney 1950).

\textsuperscript{59} London Realty Co. v. Riordan, 207 N.Y. 264, 100 N.E. 800 (1913); Lowry v. Collateral Loan Ass'n, 172 N.Y. 394, 65 N.E. 206 (1902).

\textsuperscript{60} See text accompanying note 47 supra.
Those proponents who seek additional protection of such interests cite statistics which indicate that there are a significant number of uninsured motorists. Even in those states where liability insurance is compulsory the illegal presence of an uninsured motorist is not all too infrequent. Thus, it is argued that the public should not be subjected to the additional risk of uninsured injury inflicted by the driver who, because of a premium finance agency's cancellation of his insurance contract, is uninsured.

In New York, where the Motor Vehicle Accident Indemnification Corporation has been established by the state to compensate the victims of uninsured motorists, this problem appears nonexistent. In all other jurisdictions, those who are insured under "Uninsured Motorist Endorsement" will be similarly protected. This protection, however, does not accrue to pedestrians, for instance, who are not within the reach of the uninsured motorist coverage. With respect to them the argument against cancellation remains relevant.

It seems apparent that the strict cancellation provisions in premium finance statutes are, in part at least, a response to the problems that underlie this argument. The courts, by strictly construing cancellation provisions, have shared the legislature's concern in this regard. Statutory provisions dealing with such aspects as the service of notice of cancellation upon the insured, the timing of cancellation after notice, the creation of a power of attorney to cancel, and notification of the commissioner of motor vehicles of cancellation, all have strictly been construed in favor of continuing the insurance contract in effect. Yet, notwithstanding the rigid statutory cancellation provisions and their strict judicial interpretation, the proponents of the non-cancellation argument would go still further. Their goal is the total elimination of the premium finance agency's power of cancellation.

Any attempt in this direction by means of a direct attack on the power of attorney cancellation clause would prove fruitless. In addition to case law holding that premium finance agreements are basically valid, nothing in agency or insurance principles prevents the insured from authorizing an agent to cancel his insurance contract. This is so because cancellation is not an act

62. This is a special policy which is sold almost automatically to holders of automobile liability insurance policies. It protects the insured against the risk of being hit by a negligent uninsured driver. See Laufer, Insurance against Lack of Insurance? A Dissent from the Uninsured Motorist Endorsement, 1969 DUKE L.J. 227 (1969).
68. Western Cas. & Sur. Co. v. Lund, 234 F.2d 916 (10th Cir. 1956); Sweers v. Malloy,
so personal in nature as to preclude delegation in the absence of statutory provision to the contrary.\textsuperscript{69} Hence, cancellation effected by an agent of the insured is valid if he acts within the scope of his express or implied authority.\textsuperscript{70} Moreover, the extension of credit and an agreement that the insured may pay a premium finance agency in installments are sufficient consideration to support a power of attorney to effect cancellation.\textsuperscript{71} Most directly in point is a North Carolina court's holding that the state's Vehicle Financial Responsibility Act does not forbid cancellation of an insurance contract by an insured through an agent.\textsuperscript{72}

Thus, the limited number of cases in point indicate that the only possible means of eliminating the cancellation power is by legislative fiat predicated on the state police power. Ideally, a consideration of the consequences of such legislative action should be determinative of whether it will be in the public interest. Without the cancellation power the premium finance industry could not function since this is its sole means of security. In a state where automobile liability insurance is compulsory, the demise of the premium finance industry would result in a curtailment of driving privileges for those drivers who, due to economic necessity, must necessarily rely on premium financing. It is conceivable that such a development might prompt insurance companies to offer installment payment facilities on a large scale. The public, however, would bear the cost of such a service in the form of higher rates. Most importantly of all, the innocent victim of an uninsured driver should be considered.

The issue of cancellation versus non-cancellation is one of conflicting interests. It is obvious that in considering such alternatives as the continuation or elimination of the cancellation power these conflicting interests must be balanced by the state legislature. The probabilities of the loss of driving privileges, higher insurance rates, and injury to innocent parties by the uninsured must be contemplated. Then, the societal value placed on each of these interests must be considered. A rational decision can be based only upon this type of analysis. But in weighing competing interests in such a fashion a very difficult process is involved, for what actually are being balanced are complex, diverse intangibles. The key to any ultimate resolution will eventually lie in a value judgment that must come from the state legislature.

\textsuperscript{72} Id., Dawson v. Concordia Fire Ins. Co., 192 N.C. 312, 135 S.E. 34 (1926).
Without doubt premium financing has filled a public need, but in so doing it has also created certain problems. In addition to the cancellation power controversy discussed above, other lively issues exist.

"The purpose of regulating any financial institution is to permit a just return, which will be adequate to insure the participation of legitimate business concerns in the field and to provide assurance that the loan shark and other illegitimate lenders will have no place in the lending picture." In permitting small loan companies to charge interest rates in excess of the general usury rate, the legislature has imposed a duty upon them to deal fairly with borrowers. Loans must be made with scrupulous adherence to the statute authorizing them. For obvious reasons the degree of such scrupulousness is closely guarded by both regulatory administrative agencies as well as the courts. Moreover, because premium finance agreements are to be considered adhesion contracts, they should be strongly construed against the dominant party who has prepared and offered them.

The state's watchful supervision of premium finance agencies, if not prudently exercised, however, can become detrimental to the very party for whose benefit it is being implemented, since it is the consumer, the man who finances his premiums, who ultimately pays the costs of over regulation.

At the inception of premium finance regulation, the unscrupulous practices of many agencies left much to be desired. The remedial legislation enacted to rectify this situation was often justifiably stringent. What may have been laudatory regulation then, however, may not continue to be best in light of the present state of the industry. For example, some states require that all forms used by premium finance agencies must be filed and approved before they can be used. This requirement applies even to form letters. While it may not be unreasonable to require the approval of agreement forms by which an insured makes certain agreements or commitments, the requirement of approval of all forms, including form letters, is unduly burdensome to the industry, and in the long run penalizes the public in the form of higher costs.

Another significant issue relevant to contemporary premium financing is concerned with delinquency and cancellation charges. Unfortunately, not all insureds pay their obligations promptly. Upon default, it is standard practice among premium finance agencies to send out delinquency and intent-to-cancel

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76. The adhesion contract is a standardized form agreement that is drafted by a dominant party and then presented to a weaker party as the only acceptable instrument. RESTATEMENT (SECOND) CONTRACTS § 322(a) (Tent. Draft No. 6, 1960).
notices. Because this practice adds to the operational costs of premium financing, most regulatory statutes permit agencies to impose a delinquency charge. Some states, however, do not. In addition, some states permit a cancellation charge if a default actually results in cancellation. Again, other states do not.

It is submitted that delinquency and cancellation charges should be permitted in all jurisdictions. In states where premium finance agencies are not permitted a delinquency or cancellation charge, overall rates are higher in order to offset the additional costs incurred due to delinquent insureds. The insured who lives up to his financial commitments under a premium finance agreement should not be obliged to pay the additional costs incurred by the premium finance agency due to delinquent insureds. This can only be accomplished by allowing delinquency and cancellation charges.

Finally, there is one problem that from a public relations standpoint is most objectionable to the agent who finances insurance premiums himself. This is the Federal “Truth in Lending Law,” which requires in addition to the expression of finance charges, in terms of dollar amounts, that finance charges be expressed in bold print on the contract in terms of simple interest at an annual rate.

The nature of premium financing dictates that accounts handled be relatively small. To handle small accounts at a profit a minimum income is necessary to cover costs. Such income in effect, is really a service charge. To have it expressed in terms of an annual interest rate is very deceptive. This point is illustrated by one writer:

When the amount involved is small and the payment terms are short, time rate disclosure is meaningless and only dollar disclosure should be required. For a merchant to tell his customer, who wishes to buy a $60 vacuum cleaner on time, that it will cost him a minimum $10 credit service charge and a total time price of $70 payable in 8 monthly installments of $8.75 each, enables the customer to make a value judgment as to whether or not he wishes to buy the cleaner on those terms; for the merchant to tell him that the credit service charge is at an annual rate of 29.63% does not help the customer in making that judgment.

A similar example will forcefully illustrate this point. Where, for example, $34 is financed and is to be repaid in four monthly installments along with an $8 finance charge, in order to comply with the “Truth in Lending Law,” a premium finance agency is required to indicate in bold print on the premium finance agreement that the annual percentage rate charges is 110.5. Since annual percentage rates are not always meaningful, maybe premium finance agencies should not be required to display the effective rate on smaller size loans but rather only the total dollar cost.

79. See note 14 supra.
COMMENTS

VI. CONCLUSION

Premium financing has developed as a distinct form of consumer credit to meet a specific public need, but in many jurisdictions the law governing it has sorely lagged behind. The diverse interests in need of protection, as well as the sheer volume of capital involved, call for reasonable state regulation. With such regulation this new industry can effectively function to the benefit of all parties involved. Yet to accomplish this end there must first be an awareness within the legal community of the nature of premium financing and the legal ramifications that it entails.

FRANK A. VALENTI