A REPORT ON CREDIT INSURANCE IN MASSACHUSETTS 2009

A report to the Joint Committee on Financial Services,
the Senate Committee on Ways and Means, and
House Committee on Ways and Means
of the Massachusetts General Court,
the Attorney General,
and the Secretary of the Commonwealth

JOSEPH G. MURPHY
COMMISSIONER OF INSURANCE

Acknowledgements

The enclosed report was prepared by the State Rating Bureau staff of the Massachusetts Division of Insurance ("Division"). Chet Lewandowski and Kevin Beagan prepared the report and provided the analysis. The report is based primarily on responses from companies offering credit insurance in Massachusetts reflecting their experience. Unless otherwise noted in the report, references to credit insurance include credit life insurance, credit disability insurance and credit involuntary unemployment insurance.

The Division makes all appropriate efforts to check the completeness and consistency of data reported by insurance companies and their statistical agents, but does rely on the insurance companies for the accuracy of all reported information.

Annual Reports

The Division produces an annual report on credit insurance pursuant to M.G.L. c. 175, §117C. .

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Section 1 Overview of Credit Insurance

Credit insurance is a type of insurance coverage that may be offered to debtors of a lending organization for lines of credit other than a residential first mortgage (also known as "first lien on a residential property")[1]. Depending on what coverage is purchased, credit insurance may pay all of a debt or required minimum periodic payments. Under Massachusetts law[2], it is illegal for a lender to require a person to buy credit insurance as a condition of obtaining a loan. Potential insureds are required, by regulation[3], to receive certain disclosure materials prior to any such coverage becoming effective.

This report describes credit insurance offered by licensed or authorized insurers and does not address non-insurance banking products - such as debt cancellation or debt suspension products - considered to be bank services. These products are not subject to state insurance laws or regulations.

Types of Credit Insurance

Credit life insurance is designed to pay off a specific debt in the event of the death of the insured debtor. Unlike traditional life insurance, the beneficiary on the credit life insurance policy is the entity who offers the credit (the "creditor"), and not a friend or family member of the insured. Credit life insurance in Massachusetts is governed by the standards in M.G.L. c. 175, §117C which are as follows:

(1) the death benefit may not be for more than $125,000;
(2) the insurance may not be for more than a 15-year period;
(3) the insurance may only be for the remaining outstanding balance of a debt; and
(4) the coverage ends when the debt is discharged.

By statute, an insurance company's credit life losses in relation to its earned premium – called the loss ratio - must be at least 50%. Per M.G.L. c. 175, §117C, a company is required to report its credit life insurance premium and loss experience annually. Companies whose loss experience is credible and which did not meet the required loss ratio standard are required to file revised rates which meet the statutorily required loss ratio standard.

Credit disability insurance, also known as credit accident and sickness insurance, is designed to pay a monthly amount that is never less than the minimum monthly payment required under the debt agreement. Unlike traditional disability insurance, the beneficiary is the creditor and payments are made to the creditor instead of to the insured person. Credit disability insurance may only be offered in Massachusetts in accordance with to the standards set forth under M.G.L. c. 175, §117C that include the following:

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[1] As authorized under Chapter 303 of the Acts of 1988, credit insurance is to be used with a "loan for personal, family or household purposes, except in the case of a loan secured by a first lien on real property" (M.G.L. c. 255, §12G); "retail installment contract" (M.G.L. c. 255B § 10); "premium finance agreement" (M.G.L. c. 255C, §14A); or "retail installment sale agreement or revolving credit agreement (M.G.L. c. 255D, §26C).
[2] Chapter 303 of the Acts of 1988.
[3] 211 CMR 143.00.

(1) the monthly benefit is equal to the loan's minimum monthly payment;
(2) there may be an elimination period before a benefit is paid; and
(3) the benefit may or may not be retroactive.

By statute, an insurance company's loss ratio for credit disability insurance must be at least 55%. Per M.G.L. c. 175, §117C, a company is required to report its credit disability insurance premiums and claims annually. Companies whose claims experience is credible and which did not meet the required loss ratio standard must file revised rates which meet the statutorily required loss ratio standard.

Credit involuntary unemployment insurance is designed to pay a monthly amount that is never less than the minimum monthly payment under the debt agreement. Unlike traditional involuntary unemployment insurance, the beneficiary is the creditor and payments are made to the creditor instead of the insured person. Credit involuntary unemployment insurance may only be offered in Massachusetts in accordance with the standards set forth under M.G.L. c. 175, §117D that include the following:

(1) the monthly benefit is equal to the loan's minimum monthly payment;
(2) there may be an elimination period before a benefit is paid; and
(3) the benefit may or may not be retroactive.

By statute, an insurance company's loss ratio for credit involuntary unemployment insurance must be at least 60%. Per M.G.L. c. 175, §117D, a company is required to report its credit involuntary unemployment insurance premiums and claims annually. Companies whose claims experience is credible and which did not meet the required loss ratio standard must file revised rates which meet the statutorily required loss ratio standard.

Credit property insurance is designed to pay the outstanding balance under a debt agreement in case the covered property is destroyed by specific named perils such as an accident or theft. Usually this product does not have any upfront deductible.

Although the rates used for credit property insurance are to be actuarially supportable when filed with the Division, there is no statutorily required loss ratio for this product and this product is not referenced in the data collected for this report.

Reporting by Classes of Business

The rates to be used for credit life and credit disability insurance offered through the Motor Vehicle Dealers ("MVD") class of business – for auto-related loans – are set by the Division triennially using the last three available years of experience. (Bulletin 2010-09 identifies the rates applying to 2011, 2012 and 2013, based on 2007-2009 experience.) For all other classes of business, insurers are to submit rate filings for a specific line that comply with the statutorily defined standards[4]. In order to differentiate MVD credit insurance from all other credit insurance, the Division expects companies to maintain and report the experience of these lines separately.

[4] As defined in M.G.L. c. 175, §117C.

Section 2 Data and Reporting Requirements

Data Requirements

Insurers offering credit insurance are required to file claims experience and loss ratio data annually. The Commissioner of Insurance, by September 30th of each year, provides a summary of the information reported by companies. When submitting information, insurers are to report claims and premium data and calculate a loss ratio in the following manner:

Incurred Claims = Total credit insurance claims paid during the experience period adjusted for changes to the credit insurance claim reserve.

Earned Premiums = Actual earned premiums

$$\text{Loss Ratio} = \frac{\text{Incurred Claims}}{\text{Earned Premiums}}$$

Reporting Requirements

When submitting credit insurance information, the Division requires companies to report separately for credit life, credit disability and credit involuntary unemployment insurance. Within the Credit Life and Credit Disability reports, the Division has requires information to be reported separately for the MVD and non-MVD classes of business. (Information on the credit involuntary unemployment insurance need not be broken out in that way because the Division does not set credit involuntary unemployment rates for any class of business.) The Division requires data to be reported for each individual product offered within a line of coverage so that the loss ratio of the individual product may be compared to the statutory loss ratio requirements.

Section 3 Credit Life Insurance

The following charts represent the experience reported by the 29 companies submitting reports for credit life insurance business in force between 2007 and 2009:

Motor Vehicle Dealer Class of Business

	2007	*2008*	*2009*	*Total 2007-2009*
Direct Premium Earned	3,949,087	3,080,259	2,132,850	9,162,196
Direct Losses Incurred	644,844	639,174	548,576	1,832,594
Loss Ratio	16.33%	20.75%	25.72%	20.00%

All Other Classes of Business

	2007	*2008*	*2009*	*Total 2007-2009*
Direct Premium Earned	7,223,736	6,238,484	5,237,250	18,699,470
Direct Losses Incurred	3,347,956	2,796,656	2,094,400	8,239,012
Loss Ratio	46.35%	44.83%	39.99%	44.06%

Motor Vehicle Dealer Class and All Other Classes Combined

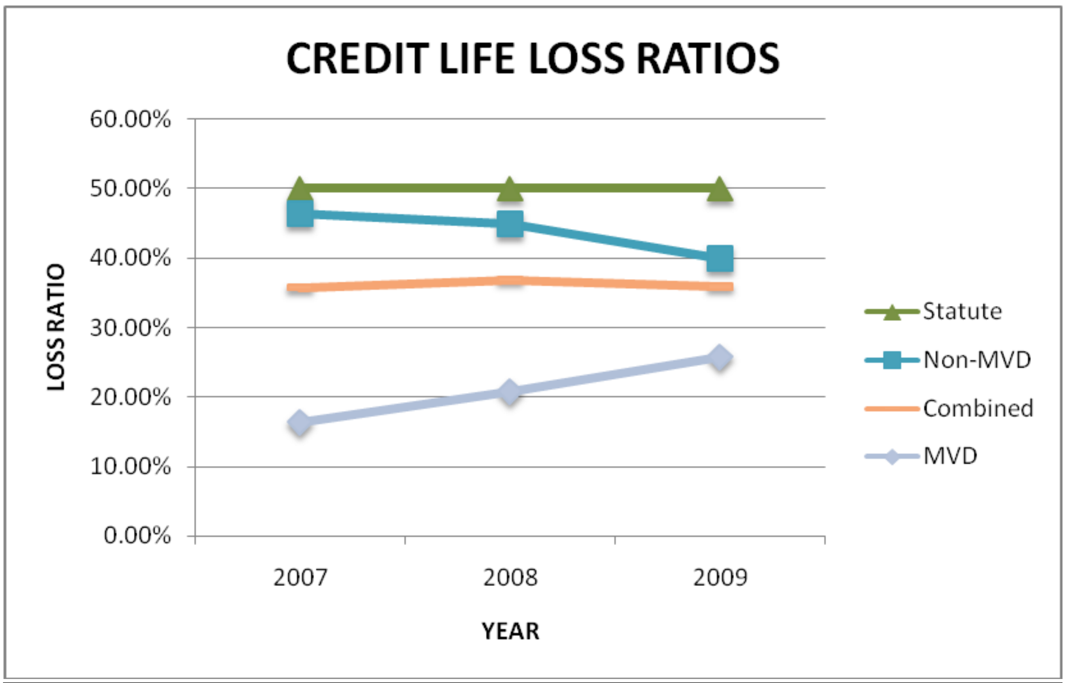
	2007	*2008*	*2009*	*Total 2007-2009*
Direct Premium Earned	11,172,823	9,318,743	7,370,100	27,861,666
Direct Losses Incurred	3,992,800	3,435,830	2,642,976	10,071,606
Loss Ratio	35.74%	36.87%	35.86%	36.15%

Analysis of Data

Credit life insurance earned premiums decreased by $1,948,643, or 21%, from 2008 to 2009. Premiums for the MVD class of business decreased by slightly over $947,000, and premiums for other credit life insurance business decreased by slightly over $1,000,000. Incurred claims decreased by $792,854 from 2008 to 2009.

Comparison to Statutory Standards

As shown in the following graph, the reported loss ratios for credit life insurance in the aggregate are below the statutory required loss ratio standards. Credit life insurance products are required to be written at the 50% loss ratio. The 2009 aggregate loss ratio was 25.72% for the MVD line of business and 39.99% for all non-MVD lines of business.



Evaluation of the Loss Ratio Results

As noted previously, the Division develops the deviated rates for the MVD line of business every three years based on the previous three-year period's experience and these time lags can affect the loss ratios of this business. Bulletin 2010-09, issued in October, sets the credit life rates for the years 2011 through 2013 based on reported information from the period between 2007 and 2009. The premium and claims reported for 2009 have been factored into the rates set in 2010 to be effective between 2011 and 2013.

For the non-MVD line of business, each of the companies submitted earned premium and claims information which was individually reviewed for the credibility of the reported information. Seven companies were required to submit amended rate filings because their reported loss ratios fell below the statutorily required limits.

Section 4 Credit Accident and Sickness Insurance

The following charts represent the experience reported by the 27 companies submitting reports for credit accident and sickness insurance business in force between 2007 and 2009:

Motor Vehicle Dealer Class of Business

	2007	***2008***	***2009***	***Total 2007-2009***
Direct Premium Earned	8,400,899	5,173,085	3,675,144	17,249,128
Direct Losses Incurred	1,634,008	1,516,490	999,762	4,150,260
Loss Ratio	19.45%	29.32%	27.20%	24.06%

All Other Classes of Business

	2007	***2008***	***2009***	***Total 2007-2009***
Direct Premium Earned	12,043,183	10,721,851	8,979,073	31,744,107
Direct Losses Incurred	4,795,548	5,323,589	4,326,765	14,445,902
Loss Ratio	39.82%	49.65%	48.19%	45.51%

Motor Vehicle Dealer Class and All Other Classes Combined

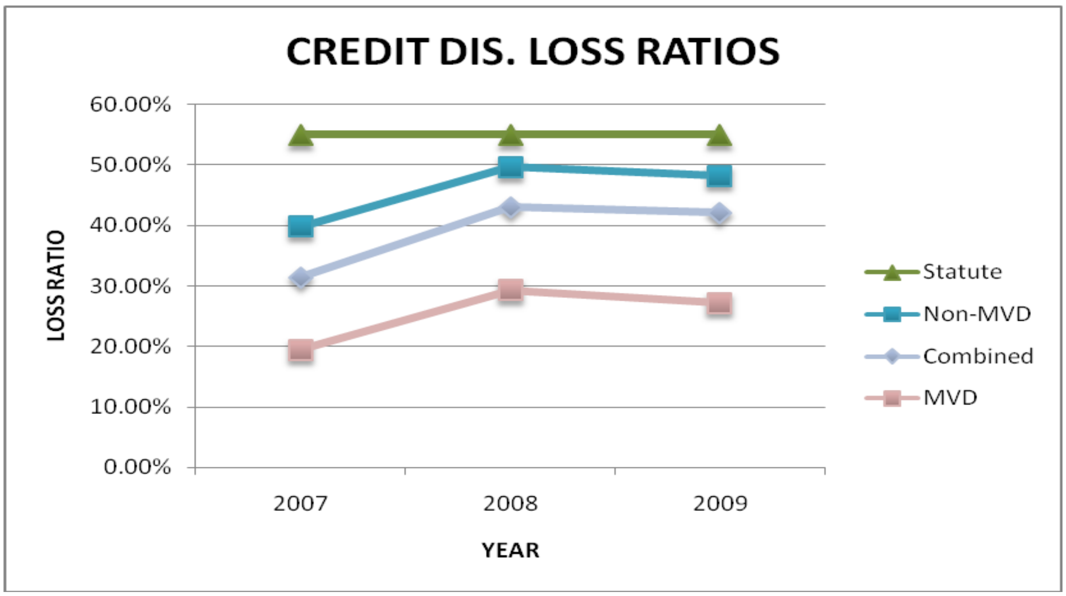
	2007	***2008***	***2009***	***Total 2007-2009***
Direct Premium Earned	20,444,082	15,894,936	12,654,217	48,993,235
Direct Losses Incurred	6,429,556	6,840,079	5,326,527	18,596,162
Loss Ratio	31.45%	43.03%	42.09%	37.96%

Analysis of Data

Credit disability insurance earned premiums declined by $3,240, 719 or 20% from 2008 to 2009. MVD premiums decreased by $1,497,941. The other credit disability insurance decreased $1,742,778. Incurred claims decreased by $1,513,552 or 22%. Incurred claims on the MVD class of business decreased by $516,728 while the incurred claims on the other credit disability insurance decreased by $996,824.

Comparison to Statutory Standards

As presented in the following graph, the reported loss ratios for credit disability insurance in the aggregate are below the statutory required loss ratio standards. Credit disability insurance products are required to be written at a 55% loss ratio. The 2009 aggregate loss ratio was 27.20% for the MVD line of business and 48.19% for all non-MVD lines of business. While the non-MVD class of business is close to the statutory standard, the MVD class of business is significantly below the required level.



Evaluation of the Loss Ratio Results

As noted previously, the Division develops the deviated rates for the MVD line of business every three years based on the previous three-year period's experience. These time lags can affect the loss ratios of this business. Division Bulletin 2010-09 sets the credit disability insurance rates for the years 2011 through 2013 based on reported information from the period between 2007 and 2009. The premium and claims reported for 2009 have been factored into the rates set in 2010 to be effective between 2011 and 2013.

For the non-MVD line of business, each of the companies' submitted earned premium and claims information was individually reviewed for the credibility of the reported information. Six companies were required to submit amended filings to reduce their credit disability rates, because their reported loss ratios fell below the statutorily required loss ratios.

Section 5 Credit Involuntary Unemployment Insurance

The following chart represents the experience reported by the nine companies submitting reports for credit involuntary unemployment insurance business in force between 2007 and 2009. (For this line, companies do not rate or report the MVD class of business separately.)

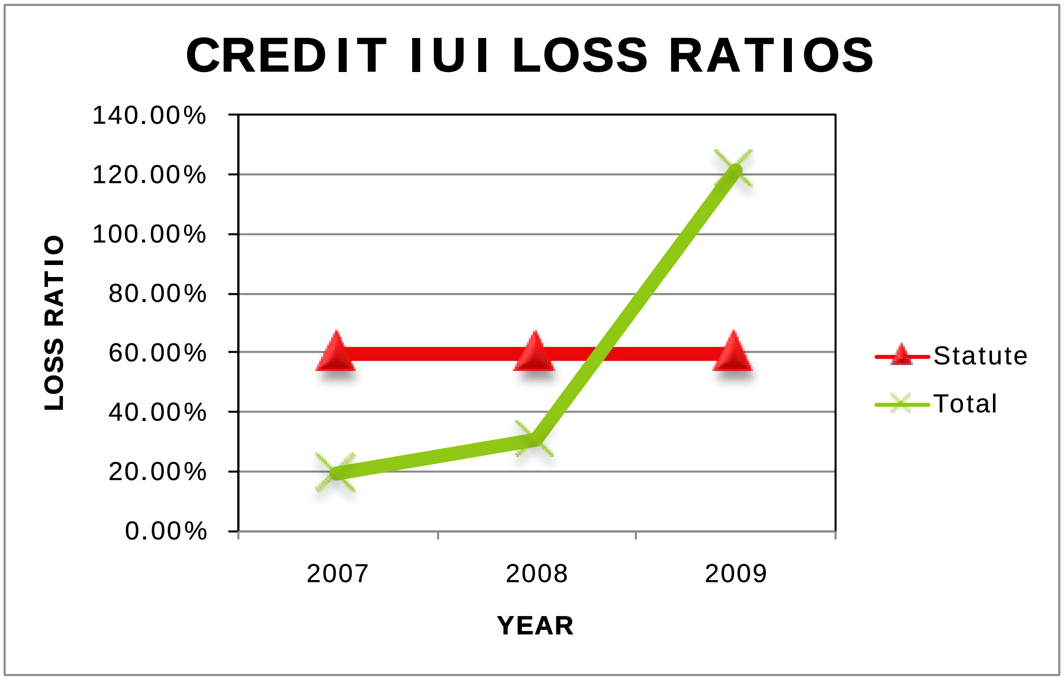
	2007	***2008***	***2009***	***Total 2007-2009***
Direct Premiums Earned	3,308,849	2,641,613	1,647,243	7,597,705
Direct Losses Incurred	636,714	814,278	2,006,116	3,457,108
Loss Ratio	19.24%	30.83%	121.79%	45.50%

Analysis of Data

Credit involuntary unemployment insurance earned premiums declined by $994,370, or by 38%, from 2008 to 2009. Incurred claim losses increased by $1,191,838 from 2008 to 2009. The loss ratio for credit involuntary unemployment insurance increased significantly, from 30.83% to 121.79%, and is well above the statutory requirement of 60%.

Comparison to Statutory Standards

In past years, the reported involuntary unemployment insurance loss ratio has been significantly less than the statutory minimum loss ratio of 60%. In 2009, the pattern reversed as the actual loss ratio of 122% is well in excess of the statutory loss ratio of 60%. Over the past three years the credit involuntary unemployment insurance block of business has declined significantly. In 2009, the line's earned premiums were $1,647, 243, compared to $3,308,849 in 2007. If this block continues to decline its reported loss ratio will be volatile. One major writer of this line, Triton Insurance Company, had a 2009 loss ratio of 262%. The Triton actuary cited two reasons for Triton's large reported loss ratio: 1) the December 31, 2008 claim reserves were understated as the company underestimated the number of 2008 incurred claims; and 2) because of economic conditions the incidence of claims has been significantly higher than in past years. Eliminating Triton, the reported loss ratio for the remaining writers would decline to 81%, a value that still exceeds the statutory loss ratio.



Evaluation of the Loss Ratio Results

Each of the companies submitting earned premium and claims information was individually reviewed for the credibility of the reported information. No companies were required to submit amended filings to reduce their credit involuntary unemployment insurance rates.