Maryland
INSURANCE ADMINISTRATION

# MSAR #12427

# 2021 Review of the Premium Tax Exemption Report filed by the Maryland Automobile Insurance Fund

Kathleen A. Birrane

Commissioner

December 1, 2021

## Report Background

Effective January 1, 2018, Chapter 509, 2017 Laws of Maryland ("Chapter 509"), repealed the provision of law subjecting the Maryland Automobile Insurance Fund ("Fund") to premium tax for a period of time and established certain reporting requirements related to the premium tax exemption. Pursuant to Chapter 509, the Fund is required to file with the Maryland Insurance Administration ("Administration" or "MIA") a premium tax exemption report on or before October 1, 2019, October 1, 2020, and October 1, 2021, that specifies, since the premium tax exemption became effective on January 1, 2018:

(i) the amount of the premium tax subject to the exemption;

(ii) the year–over–year change in the Fund's surplus;

(iii) the increase or decrease in the Fund's overall premium rate structure;

(iv) the impact of the premium tax exemption on the Fund's surplus; and

(v) the surplus-to-assessment threshold ratio.

The MIA is required to review the Fund's premium tax exemption report and determine whether, since the premium tax exemption became effective:

(i) the Fund's surplus has increased or decreased;

(ii) any additions to the Fund's surplus due to the premium tax exemption have allowed the surplus to become excessive;

(iii) the Fund has decreased its overall premium rate structure; and

(iv) the Fund's premium rates have been subsidized by the premium tax exemption.

The MIA is required to report its findings to the Senate Finance Committee and the House Economic Matters Committee on or before December 1, 2019, December 1, 2020, and December 1, 2021.

## Review of the Premium Tax Exemption Report

On September 15, 2021, the Fund timely filed its 2021 Premium Tax Exemption Report (Exhibit A) with the MIA. This report contains the results of the MIA's review of the Fund's 2021 Premium Tax Exemption Report.

### *Surplus Increase or Decrease*

Chapter 509 requires the MIA to evaluate whether the Fund's surplus has increased or decreased. Since the premium tax exemption became effective in January 1, 2018, the Fund's surplus has declined from $57,488,673 to $54,018,455, as follows:

| Date | Surplus | % Change from Prior Date |
|---|---|---|
| December 31, 2017 | $57,488,673 | |
| December 31, 2018 | $35,631,014 | -38% |
| December 31, 2019 | $46,327,425 | 30% |
| December 31, 2020 | $54,018,455 | 17% |

***Excess Surplus***

Chapter 509 requires the MIA to evaluate whether any additions to the Fund's surplus due to the premium tax exemption have allowed the Fund's surplus to become excessive.

An insurer's surplus is the amount by which its assets exceed its liabilities. An insurer must maintain a surplus that is reasonable in relation to its outstanding liabilities and that is adequate to meet its financial needs. In evaluating whether any additions to the Fund's surplus due to the premium tax exemption have allowed the Fund's surplus to become excessive, the MIA considered a) the ratio of the Fund's surplus to the assessment triggers and b) the Fund's surplus as measured by Risk-Based Capital ("RBC").

***Ratio of surplus to the assessment triggers***

Title 20, Subtitle 4, of the Insurance Article of the Annotated Code of Maryland, provides an assessment mechanism under which the Fund would obtain funds from private insurers operating in Maryland's automobile insurance market in the event that the Fund's surplus was to decrease below either or both of two assessment triggers. The first of these triggers is the private passenger auto assessment limit, which requires an assessment when the year-end surplus is less than 25% of the average of the Fund's net direct written private passenger auto premiums for the three immediately preceding calendar years. The second trigger is the commercial auto assessment limit, which requires an assessment when the year-end "commercial auto surplus"[1] is less than 25% of the average of the Fund's net direct written commercial auto premiums for the three immediately preceding calendar years.

[1] The Fund's Annual Statement does not segregate surplus between the Fund's private passenger auto business and its commercial auto business. For purposes of determining the commercial auto assessment limit, a "commercial auto surplus" is determined annually by the Fund's Board of Trustees. However, for the MIA's analysis, we used surplus as reported on the Fund's Annual Statement, and we combined premium for the Fund's private passenger auto business and its commercial auto business. We believe this is a sufficient method for the purpose of our analysis.

Presented below is the trend in the ratio of surplus to assessment triggers for December 31, 2016 through December 31, 2020:

| | 2020 | 2019 | 2018 | 2017 | 2016 |
|---|---|---|---|---|---|
| Surplus | 54,018,455 | 46,327,425 | 35,631,014 | 57,488,673 | 64,085,081 |
| Direct Premium Written | 65,095,666 | 84,629,703 | 91,755,980 | 85,763,041 | 79,453,933 |
| Average 3-Year Direct Premium Written | 80,493,783 | 87,382,908 | 85,657,651 | 82,745,855 | 80,581,129 |
| Assessment Trigger (25% of Average Premium) | 20,123,446 | 21,845,727 | 21,414,413 | 20,686,464 | 20,145,282 |
| Ratio of Surplus to Assessment Trigger | 2.7 | 2.1 | 1.7 | 2.8 | 3.2 |

Overall, the five-year ratio trend has remained fairly stable, as the five-year ratio average is 2.5.

***Surplus as measured by RBC***

The Fund is not subject to RBC requirements. However, under long-standing practice, the Fund submits an RBC report to the MIA on an annual basis. RBC is a method for establishing the minimum amount of capital an insurance company must maintain to support its business operations based upon the company's size and risk profile. Therefore, RBC is not intended to be a measure of excessive surplus. However, if the Fund's RBC ratio were an outlier when compared to other insurers, it could be indicative of either excessive or insufficient surplus.

According to a National Association Of Insurance Commissioners market share report, the Fund's premium written of $65 million ranks number 11 compared to the top 20 writers of automobile insurance in Maryland, as measured by direct premiums written in 2020. However, the Fund's RBC ratio of 502.71% is the lowest of all top 20 writers of automobile insurance in Maryland.

For the calendar year 2020, without the premium tax exemption, the Fund would have paid a premium tax of $1,301,913 based on a gross direct written premium of $65,095,666 for the year. Payment of the $1,301,913 premium tax in 2020 would have further reduced the Fund's surplus, causing the surplus amount to be closer to the assessment trigger, and would have further reduced the RBC ratio. Therefore, the additions to the Fund's surplus due to the premium tax exemption have not allowed the surplus to become excessive.

## Overall Premium Rate Structure

Chapter 509 requires the MIA to evaluate whether the Fund has decreased its overall premium rate structure. According to the Fund's 2021 Premium Tax Exemption Report, "During

2020, the Fund instituted a general, private passenger overall rate decrease of -0.3% for all coverages effective 11/1/2020. The Fund also instituted a general rate increase for commercial auto policies of 4% effective 9/1/2020."

The rate changes that took effect in 2020 reduced private passenger auto rates slightly while increasing the commercial auto rating structure. Private passenger auto makes up over 90% of the Fund's total premium revenue. Therefore, while the Fund has increased its overall premium rate percentage, the slight decrease in the private passenger auto rates likely resulted in a small overall premium revenue decrease.

## Subsidized Premium

Chapter 509 requires the MIA to evaluate whether the Fund's premium rates have been subsidized by the premium tax exemption. The Fund would have incurred an expense of $1,301,913 if the Fund had been subject to the premium tax in 2020. It stands to reason that the amount that would have otherwise been paid in premium tax was available to subsidize premium rates.

## Conclusion

After reviewing the Fund's 2021 Premium Tax Exemption Report, and considering the factors discussed in this report, the MIA concludes that since the premium tax exemption became effective on January 1, 2018, the Fund's surplus has decreased, and the additions to the Fund's surplus due to the premium tax exemption have not allowed the surplus to become excessive. In addition, the MIA concludes that the Fund has not significantly decreased its overall premium rate structure.

# Exhibit A

MARYLAND
AUTO INSURANCE

**Al Redmer, Jr.**
Executive Director
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September 15, 2021

Ms. Kathleen A. Birrane
Insurance Commissioner
Maryland Insurance Administration
200 Saint Paul Place, Suite 2700
Baltimore, MD 21202-2004

Re: Maryland Automobile Insurance Fund - Premium Tax Exemption Report

Dear Commissioner Birrane:

Pursuant to Senate Bill 910, Chapter 509 (2017), enclosed please find the Maryland Automobile Insurance Fund's Premium Tax Exemption Report for 2021. The Report is based on year-end 2020 results. The Maryland Automobile Insurance Fund is required to file this report with the Insurance Commissioner on or before October 1, 2021.

This report was required by the Legislature to address industry concerns that the premium tax exemption would lead to subsidized rates or excessive surplus. As you can see, for 2020 Maryland Auto's rates decreased nominally for private passenger, increased for commercial and surplus is not excessive.

We would appreciate a copy of the MIA's premium tax exemption report prior to its submission to the legislative committees.

Please let me know if you or your staff has any questions or if we can provide additional information.

Sincerely,

Al Redmer, Jr.
Executive Director

Attachment

cc: Michael Paddy, Director of Government Relations
Robert Baron, Associate Commissioner, Property & Casualty

MARYLAND
AUTO INSURANCE

# Premium Tax Exemption Report

October 1, 2021

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Pursuant to Senate Bill 910, Chapter 509 Laws of Maryland (2017), the Maryland Automobile Insurance Fund ("the Fund") files this Premium Tax Exempt Report.

For year-end 2020, the Fund states:

(i) The Fund's gross direct written premium for 2020 was $65,095,666. As a result, in the absence of the exemption, the Fund would have paid $1,301,913 in premium taxes, under Insurance Article §6-102 and §6-103 for calendar year 2020;

(ii) The Fund's year-end 2019 surplus was $46,327,426 and the year-end surplus for 2020 was $54,018,455. Therefore, the year-over-year change in the Fund's surplus was $7,691,029;

(iii) During 2020, the Fund instituted a general private passenger overall rate decrease of -0.3% for all coverages effective 11/1/2020. The Fund also instituted a general overall rate increase for commercial auto policies of 4.0% effective 9/1/2020;

*(iv)* The Fund's surplus would have been smaller by $1,301,913 if the Fund had been subject to the premium tax for calendar 2020, as the surplus would have been $52,716,542 rather than the reported $54,018,455.

(v) The Fund's assessment threshold for year-end 2020 was $20,123,446. The surplus to assessment ratio for 2020 was 2.7 ($54,018,455/ $20,123,446).

Rates nominally decreased for private passenger and increased for commercial. The exemption did contribute to the Fund's surplus.