Maryland
INSURANCE ADMINISTRATION

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

Al Redmer, Jr.

Commissioner

December 1, 2019

I. 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Effective January 1, 2018, Chapter 509, 2017 Laws of Maryland ("Chapter 509"), repealed the provision of law subjecting the Maryland Automobile Insurance Fund (the "Fund") to premium tax for a period of time and established certain reporting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 (the "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.

II. Review of the Premium Tax Exemption Report

On October 1, 2019, the Fund timely filed its 2019 Premium Tax Exemption Report (Exhibit A) with the MIA. This report contains the results of the MIA's review of the Fund's 2019 Premium Tax Exemption Report.

A. Surplus Increase or Decrease

Chapter 509 requires the MIA to evaluate whether the Fund's surplus has increased or decreased. At December 31, 2017, the Fund's surplus was $57,488,673, and at December 31, 2018, the Fund's surplus was $35,631,014. Therefore, the Fund's surplus has decreased by $21,857,656 in the 12 months since the premium tax exemption became effective.

B. 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 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 were 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.

Presented below is the trend in the ratio of surplus to assessment triggers for December 31, 2016, December 31, 2017 and December 31, 2018:

	2018	2017	2016	2015	2014
Surplus	35,631,014	57,488,673	64,085,081	69,388,760	97,255,167
Direct Premium Written	91,755,980	85,763,071	79,453,933	83,020,590	79,268,864
Average 3-Year Direct Premium Written	85,657,661	82,745,864	80,581,129		
Assessment Trigger (25% of Average Premium)	21,414,415	20,686,466	20,145,282		
Ratio of Surplus to Assessment Trigger	1.7	2.8	3.2		

There is a decreasing trend in the ratio of surplus to the assessment trigger resulting from the decrease in surplus and the increase in premiums written. The amount of surplus is nearing the assessment trigger.

Surplus as measured by RBC – The Fund is not subject to RBC requirements. However, under a 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.

[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 a sufficient method for the purpose of our analysis.

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.

Compared to the top 20 writers of automobile insurance in Maryland, as measured by direct premiums written, the Fund's premium written ranks number 14. However, the Fund's RBC ratio is the lowest of all top 20 writers of automobile insurance in Maryland.

The Fund's premium tax exemption was effective January 1, 2018. Without the premium tax exemption, the Fund would have paid a premium tax of $1,835,120 based on gross direct written premium of $91,755,980 at December 31, 2018. Payment of the $1,835,120 premium tax in 2018 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.

C. 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 2019 Premium Tax Exemption Report, "During 2018, the Fund instituted a general, private passenger overall rate increase of 8.6% for all coverages (7.3% for physical damage and 8.9% for liability). This rate was effective 6/15/18. The Fund also instituted a general rate increase for Commercial Auto policies of 0.6% effective 9/1/18 and an overall 25.3% rate increase effective 4/1/17." Therefore, the Fund has implemented an increase, not a decrease, in its overall premium rate structure in the 12 months since the premium tax exemption became effective.

D. 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 $1,835,120 if the Fund had been subject to the premium tax in 2018. It stands to reason that the amount that would have otherwise been paid in premium tax was available to subsidize premium rates. However, the Fund's total premium tax exemption of $1,835,120 was only 2.0% of the Fund's total premium revenue of $89,731,870; therefore, in the opinion of the MIA, any subsidy provided by the premium tax exemption was not material.

III. Conclusion

After reviewing the Fund's 2019 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 decreased its overall premium rate structure and that any subsidy to premium rates provided by the premium tax exemption is not material.

EXHIBIT

A

MARYLAND

AUTO INSURANCE

September 25, 2019

Mr. Al Redmer, Jr.
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 Redmer:

Pursuant to Senate Bill 910/ Chapter 509 (2017), enclosed please find the Maryland Automobile Insurance Fund's Premium Tax Exemption Report for 2019. The Report is based on year-end 2018 results. The Maryland Automobile Insurance Fund is required to annually file this report with the Insurance Commissioner on or before October 1, 2019, October 1, 2020 and 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, Maryland Auto's rates were substantially increased and its surplus declined by $21.8 million during 2018. As a result, neither of the concerns materialized.

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

Sincerely,

Mark D. McCurdy
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, 2019

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 2018, the Fund states:

(i) The Fund's gross direct written premium for 2018 was $91,755,980. As a result, in the absence of the exemption, the Fund would have paid $1,835,120 in premium taxes, under IN §6-102 and §6-103 for calendar year 2018;

(ii) The Fund's year-end 2017 surplus was $57,488,675 and the year-end surplus for 2018 was $35,631,014. Therefore, the year-over-year change in the Fund's surplus was ($21,857,661);

(iii) During 2018, the Fund instituted a general, private passenger overall rate increase of 8.6% for all coverages (7.3% for physical damage and 8.9% for liability). This rate was effective 6/15/18. The Fund also instituted a general rate increase for Commercial Auto policies of 0.6% effective 9/1/18 and an overall 25.3% rate increase effective 4/1/17;

(iv) The Fund's surplus would have been smaller by $1,835,120 if the Fund had been subject to the premium tax for calendar 2018, as the surplus would have been $33,795,894 rather than the reported $35,631,014;

(v) The Fund's assessment threshold for year-end 2018 was $21,414,415. The surplus to assessment ratio for 2018 was 1.7 ($35,631,014 / $21,414,415).

The premium tax exemption did not decrease or subsidize the Fund's rates. The exemption did contribute to the Fund's surplus.

1215 East Fort Avenue, Suite 300 · Baltimore, MD 21230 · 800 492 7120
MyMarylandAuto.com