

An Introduction to
Assigned Risk



Assigned Risk

What does Assigned Risk mean and how does it effect a premium finance transaction?

Assigned risk pools, as they are often referred to, are state sponsored organizations that allow people and businesses to obtain insurance who would otherwise find it difficult (or impossible) to do so. Assigned risk pools are structured around particular types of risks(i.e. auto insurance, fire insurance, workers compensation insurance, etc.)

Automobile insurance is a prime example of how assigned risk pools work. Many states require automobile insurance. Some people, due to their driving record or the car they drive or where they live or some other circumstance, cannot get insurance because no one will insure them. Well, the state cannot force an individual to comply with a law if that individual has no possible way of doing so. Therefore, the state must provide a way for a person to get insurance despite the fact that no one will insure them.

Who provides insurance under assigned risk plans?

The answer is the same insurance companies which serve the rest of the industry. In providing this insurance, the state makes a simple calculation which involves determining the total amount of, for example, automobile insurance which is written in the state. This figure is then broken down by insurance carrier. The state then knows what percentage of all the business each insurance carrier provides. Every insurance carrier is required to provide insurance to these otherwise uninsurable people in the same proportion that they provide insurance to insurable people that are not part of the assigned risk pool. For example, State Farm Property & Casualty is one of the largest writers of automobile insurance in the state of California. Therefore, State Farm provides a good share of the insurance to assigned risk people.

The state forces each insurance carrier to write assigned risk business in their respective proportion just for the pleasure of being able to sell insurance to the rest of the population in that state.

The names of some of these assigned risk pools for

automobile insurance are, the California Automobile Assigned Risk Plan (CAARP), the Texas Automobile Insurance Plan Association (TAIPA), and the Maryland Automobile Insurance Fund (MAIF).

Assigned Risk business is riskier for a premium finance company to write than non-assigned risk business. Why?

1. Assigned risk business has a higher frequency of default (the people don't pay).
2. The assigned risk business has a higher frequency of up-rates (the people lie about their driving record or are involved in accidents and as a result, the premium is increased mid-term which can leave the finance company with a greater loan balance then the available unearned premium).
3. The assigned risk plans are administered by the state and as such are not subject to all of the rules and regulations that standard businesses are. The primary example of this is the rule of pro-rate versus short-rate calculation of unearned premium (In a nutshell, short-rate return premium allows the carrier to keep more of the premium upon cancellation. Since a premium finance company collateralizes its loan with the unearned premium, if less is available, the finance company has a greater risk of a shortfall in the loan balance if the borrower stops paying. Since assigned risk business defaults more frequently, this makes this possibility of shortfall higher).

As with any situation when a premium finance company has a greater risk in making a loan, assigned risk business often times requires a higher down payment and sometimes a shorter loan term (i.e. fewer installments).

It is important to understand that not every premium finance company will take a higher down payment when financing an assigned risk policy. The reason that they may not is simply due to competition. If one takes a higher down, the next one will decrease the down payment in order to capture more business. Eventually, they all reach rock-bottom and going any further will result in losses too great for any finance company to withstand.





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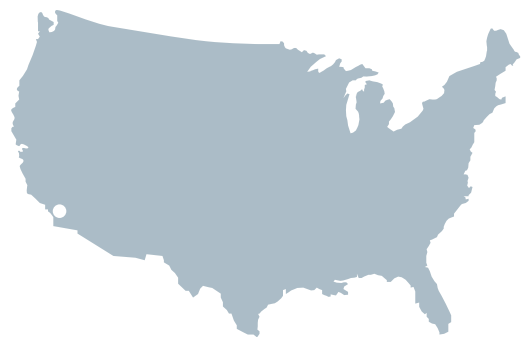
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