

Broker Fees vs Producer Fees



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What is the difference between a broker fee and a producer fee?

One of the reasons that these two items might be confusing is that a retail agent is often times called a broker or a producer. Therefore, one might assume that a broker fee and a producer fee are the same thing. This, however, is not the case.

1. A **Broker Fee** is a fully earned “placement fee” which the retail agency charges the client for placing (selling) the insurance policy. Whether or not a broker charges a broker fee and the amount of the fee, is completely up to the broker. It is important to understand that **broker fees are often charged whether or not a policy premium is financed**. Therefore it is fair to say that broker fees have nothing to do with premium financing. In some cases state laws prohibit a broker from charging a broker fee or limit the amount which the broker may charge.

Now that we know that broker fees have nothing to do with premium financing, we might ask, “Why do broker fees appear on the premium finance contract?” The answer is that when a broker sells one or more insurance policies and the client elects to finance them, a down payment must be made. This down payment is the amount of money that the borrower must come up with to put a deposit on the insurance and take out a loan for the balance. The borrower must pay for both the insurance policy(ies) and the broker fee. Since this fee is typically not financed by the finance company, the down payment must consist of the entire broker fee plus the deposit portion of the premium (usually 15% — 25%). The broker could keep the broker fee and the deposit portion of the premium separate, but for ease, the broker fee is listed on the premium finance contract so that the borrower only has to look at one piece of paper to know how much money is required at the onset of the purchase.

As indicated above, the broker fee is typically not financed. Sometimes the broker fee is financed (this allows the broker to require a lower down payment from his client), however this practice is limited because there is no collateral on

a financed broker fee. Therefore, if a premium finance company finances \$800 of a \$1,000 premium and \$80 of a \$100 broker fee and the borrower defaults on the loan, the premium finance company by law is entitled to the unearned portion of the full \$1,000 premium. But, no such law exists for the unearned portion of the broker fee. From a legal standpoint, there is no such thing as an *unearned broker fee*. The only way a premium finance company can protect itself when financing a broker fee is to obtain a written agreement from the broker to return a portion of the financed broker fee in the event the borrower stops making payments. In this case, if a premium finance company were to finance broker fees, it can obtain no relief from any state regulatory agency if the broker decides not to return the unearned broker fee. The only thing the finance company could do if a broker renegeed on a deal to return broker fees would be to take the broker to court. Needless to say, financing broker fees is not as clean a business as financing premiums.

2. A **Producer Fee or Referral Fee** is a fee paid to the retail agency by the premium finance company for inducing the borrower to take out a loan for the premium. State laws may prohibit or limit the amount of money which a premium finance company may pay to a broker.

The reason that premium finance companies pay brokers producer fees is that the broker is at the point of sale on the insurance contract. The broker is going to sell insurance in either the easiest or most profitable way he/she can. In many cases, if a premium finance company doesn't make it worth the broker's while, the broker might recommend the borrower use an insurance company payment plan rather than premium financing. The producer fee motivates the broker to encourage his customer to take out a loan for the insurance premium.

Producer fees can vary in how they are calculated. As described above, a broker fee is completely up to the broker in terms of when it is charged and how much it is and often times it is quite arbitrary. Producer fees, on the other hand, are usually calculated using some formula or figure which is established by the premium finance company.



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Here are some common formulas used in calculating the producer fee:

1. % of the premium
2. Dollar amount per contract
3. % of the Amount Financed
4. % of the Amount Financed but not less than \$_____ per contract
5. Spread in APR

The premium finance company usually never pays for the producer fee. Premium finance companies invariably charge the borrower a higher rate of interest for each loan in which a producer fee must be paid. In other words, the borrower pays for the producer fee.

Certain state regulatory agencies feel that allowing a premium finance company to induce the broker to sell financing is unethical and therefore it is outlawed. Almost all states which allow the charging of a producer fee require that the amount of this fee be clearly disclosed on the premium finance contract.



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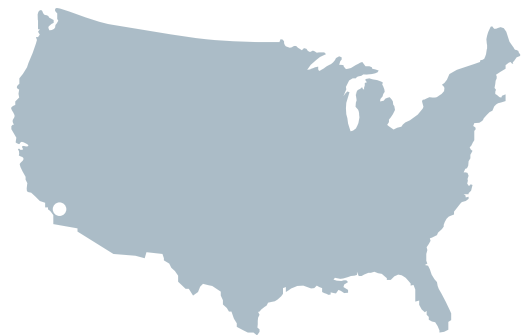
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