

amined the monthly reports from Old Republic, deposited its monthly receipts, and prepared its annual statements to the Indiana Insurance Department with the help of information furnished him by Old Republic and Alinco's consulting actuary. On the average he was able to perform these duties in the space of approximately one day each month.

"Despite the simplicity of this operation, Alinco's financial success during the period 1953 through 1959 was striking. Its net gain from operations during that period, before Federal income taxes but after paying its expenses and share of death benefits, was in excess of \$28,500,000."

The process by which a credit life company operating in many states in effect stands in place of the creditor's captive reinsurer can be described as a "fronting" arrangement. The primary insurer's cut of the business is sometimes known as a "fronting fee". Its size depends on the relative strengths of the creditor and the insurer. Earlier we described how competition tends to keep premiums high in credit insurance. The real competition is between the creditor, on behalf of his captive reinsurer, and the insurer as to who gets what share of the action.

As time passes, the alert creditor will demand "more and more of the pot", as the expression goes, by threatening to move his insurance to a carrier who will provide the desired arrangement.

This squeeze play by the creditor often reduces the insurer's net profit nearly to the vanishing point. For example, one "pot" I am aware of is split 39 parts to the creditor's captive company and one part to the "fronting" insurer.

I have heard of deals where the fronting company writes the business for no profit at all save the investment income it can generate from the premium income. Some insurers, I am told, will write the business at no profit for the volume of insurance tends to inflate the annual financial statement, making it much easier to run up the company's stock.

Further, without going into detail, there are important tax advantages to having the creditor's share of the pot flow to a subsidiary life company rather than be received directly as commissions or dividends. The advantages, however, are much less significant than they were prior to 1959 when the method of taxing life insurance was changed.

The villain of the piece begins to emerge then. The big profits are not going to the life insurance companies who provide the service (except where the insurer is owned by the creditor) but rather to the creditors—small loan companies, finance companies, banks, merchants who sell on time, anyone in the business of extending credit for profit.

WHAT ARE SOME OF THE OTHER ABUSES PREVALENT IN CREDIT INSURANCE?

The big money in credit insurance is made by the creditor by capturing a large share of an excessive premium, as we have just described. Among other schemes by which the creditor profits at the expense of the debtor are the following:

(1) *Failure to Refund the Unearned Insurance Premium on Refinancing or Repayment of the Debt*—State laws require refund of unearned finance charges on prepayment by the debtor. Since the insurance premium is paid in advance as well, the unearned portion of it should be refunded on prepayment. But many states have no law on this and the creditor often pockets the insurance refund himself.

(2) *Pyramiding of Policies*—Often debts are refinanced or renewed. If so, a new insurance policy is issued and paid for. The proper procedure is to cancel the old policy and make a refund but some lenders leave the old policy in force. Thus the debtor ends up with two or more expensive policies for amounts in excess of his debt.

(3) *Excessive Coverage Sold at the Inception of the Credit Transaction*—Level term policies may be sold to cover a loan repayable in installments rather than decreasing term insurance. The debtor ends up paying too high a price for more coverage than is necessary.

(Those states with credit insurance legislation or effective regulations have pretty well put a stop to the three practices above, but, as we will see, many states have no control over the business.)

(4) *Profit from Finance Charges Added to the Insurance Premium*—The normal method for calculating the finance charge is to add the single premium for the insurance to the principal amount borrowed *before making the calculation*. Thus, the creditor's interest income is increased over what it would be had there