

STATE OF ALASKA

DEPARTMENT OF COMMERCE AND
ECONOMIC DEVELOPMENT

DIVISION OF INSURANCE

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BULLETIN 94-09

TO: ALL ALASKA LICENSED PRODUCERS

RE: PREMIUM TRUST MONEY ACCOUNT REGULATIONS

Regulations for premium trust money accounts were initially adopted in August of 1990. Revisions of the regulations were adopted in June 1994. Following are several items of clarification regarding use of trust money accounts in compliance with Alaska statute and regulations. These comments are in response to questions and concerns raised as to the proper use of premium trust accounts.

Commingling of Funds in the Trust Money Account

A producer may leave a fund in the trust money account for purposes listed in AS 21.27.360(d):

A licensee may only commingle premium taxes and fees, premiums, and return premiums with additional money for the purpose of advancing premiums, establishing reserves for the payment of return premiums or reserves for receiving and transmitting premium or return premium money. Money collected for the payment of premium taxes, policy or filing fees, late payment charges, and interest from fiduciary money on deposit may be commingled in a fiduciary account, but shall be separately accounted for and periodically removed from the fiduciary account.

It is not required that earned commission be removed from the trust money account. Commissions retained in the account are considered additions to reserve funds. The monies left in the account, however, can only be used for advancing premium or payment of return premium or service charges deducted directly from the account and any other use of the reserve funds is not allowed. If the producer chooses to maintain reserves in the account, the aggregate reserve would be a category listed on a reconciliation of the total of the trust account to make it clear reserve monies belong to the producer and not to insurers or insureds. See Record Keeping and Reconciliation of Trust Money Account later in this Bulletin.

AS 21.27.360(d).requires the periodic removal of interest and late payment charges remaining in the account. This is to avoid the accumulation of large reserve funds in the trust money account. Because the purpose of the trust money account is to hold premium or return premium until forwarded to the insurer or insured, the reserve funds should not become so large as to be a

major portion of the money held in the account. In addition, it is not appropriate to hide income (commissions earned or other income) in the trust account to avoid attachment by others under the exemption of 3 AAC 23.720.

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Earned Commission

When the contract between a producer and an insurer specifies when commission is earned by the producer (transferred to the producer's use), contract language shall supersede the requirements of 3 AAC 23.620.

If there is no contract language stating when commission is earned, the regulations require that commissions can be earned no earlier than the date on which both

- 1) funds are received by the producer, and
- 2) insurance coverage is bound.

For example, if the contract between the producer and the insurer stated that commissions can be transferred to the producer at the time funds are received, the commissions for policies with that insurer may be removed from the trust money account at that time. If the contract between the producer and the insurer is silent as to when commissions are earned or transferred, the requirements of 3 AAC 23.620 would apply such that commissions are earned after the premiums are received and the coverage is bound. This, however, does not change the requirement that on cancellation of an unexpired policy appropriate unearned commission must be added to unearned premium and returned to the client. This returned commission must come from the producer's funds.

With these changes in 3 AAC 23.620, the producer may take commission any time after the two conditions are met. The producer may find, however, that the agency accounting system provides better internal control and record keeping if commissions are not taken or "earned" until the settlement date of the account current. In any case, the producer must be able to show a division examiner the system for determining when commissions are earned and provide documentation to show that only proper amounts of commission have been removed from the premium trust account or transferred to reserves in the account.

The last sentence of 3 AAC 23.620 clarifies that if the producer's funds are in the premium trust account for advance payment of a specific premium to the insurer (prior to receipt of payment from the client), any amount appropriately considered commission could be removed from the premium trust account immediately. This is allowed because the funds representing commission in the transaction are considered funds of the producer at all times.

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Record Keeping and Reconciliation of Trust Money Account

3 AAC 23.520 and 3 AAC 23.530 discuss record keeping requirements of Alaska producers. 3 AAC 23.520 specifies that a system of control accounts and subsidiary ledgers is required for accounts receivable, accounts payable, and the trust money account. The level of detail required in the accounting system for the trust money account is stated in 3 AAC 23.520(b)(1) so as to allow:

"the ready identification of the dollar amount, by category, of the money comprising the balance of a control account."

The reference to category in this phrase can be no more detailed than those categories required in Alaska Statute (AS). Specifically AS 21.27.360 refers to premiums, return premiums, premium taxes and fees, and money for the purpose of advancing premium or payment of return premiums or service charges, policy or filing fees, late payment charges, or interest. The broad categories are 1) money for the payment of premium to insurers, 2) money for the payment of return premium to insureds, 3) money for the payment of taxes or fees to third parties, and 4) money owned by the producer held in the trust account as reserves.

3 AAC 23.520 requires reconciliation of the amounts by category with the total balance in the account (bank statement account balance and general ledger account balance). The method by which the producer determines the amount by category is a business decision made by the producer after considering business volume and the accounting system. The amounts by category must have support in the accounting records. To complete the reconciliation, it is not required that the licensee use the "specific item method" of accounting (the accumulation of separate trust money receipts in a separate tracking system). Any other procedure which is reliable and accurate for determining the amounts by category on a periodic basis is acceptable. 3 AAC 23.520(c)(2), however, does require that each receipt of premium trust funds be entered into the accounting system as a separate transaction.

To show compliance with 3 AAC 23.520, the producer must be able to explain the movement of trust fund transactions through the accounting system. The explanation must go from documents in the insured file to accounts receivable (if applicable) to payment of premium to the insurer, and include the flow of any other items which may affect the balance of the trust account. The producer must also be able to explain the calculation of the amounts by category on the reconciliation. The reconciliation of the trust account must be completed periodically which is defined in 3 AAC 23.730 as a frequency occurring as often as internal financial statements are prepared. We recommend preparation of reconciliations monthly so that errors discovered in the records are corrected on a timely basis.

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Advancing of Funds to Pay Premium

Changes to 3 AAC 23.250 and 3 AAC 23.650 will allow the advancing of premium by the producer without a signed premium finance agreement only if:

(1) the extension of credit to pay premium is on a zero interest cost to the insured, with no service charge representing income to the licensee or expense to the insured, however, a late fee in keeping with the standard late fee charged by the licensee may be collected; and

(2) the insured is notified within 30 days after the extension of credit of the amount of credit extended and for what purpose.

If the licensee chooses to forward premium without a premium finance agreement, the licensee must take the risk of extending credit or loaning funds. If notified by the insured that the insurance was not desired, the producer must reverse the extension of credit from the insured's records effective to the date the credit was extended.

The notice to the insured of the extension of credit must clearly state the amount of premium when the loan or extension of credit was made and for what specific policies. The amount should be broken down by policy if more than one policy was involved. The notice may be made on a monthly statement to the client or by separate notification as long as it is done within 30 days after the advance of premium through a loan or extension of credit.

The category of reserve funds held in the trust money account for the purpose of forwarding premium may be used for the payment of premiums to the insurer when the insured has not yet paid. Funds held in the account belonging to insureds cannot be used to forward premium for a different insured who has not paid regardless of the size of the trust money account.

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Application of Refunds to Amounts Due

Changes in 3 AAC 23.680 will allow the use of refunds to offset other amounts due from the same insured. However, the insured must be notified of the application of refund within the 45-day period for processing of refunds in 3 AAC 23.600. This does not allow the holding of refunds beyond the 45-day period without returning the money to the insured or sending written notice specifying how the refund was used.

This bulletin has been issued to answer questions regarding the use of fiduciary accounts to hold premium as required in Alaska statute. This is not a restatement of all of the regulations on this subject and all producers are encouraged to become familiar with the regulations as published. The program of examination of trust money accounts conducted by the Division of Insurance will continue in the future to evaluate compliance with AS 21.27.350, AS 21.27.360, and 3 AAC 23.500 to 3 AAC 23.730.

Signed this 9th day of September, 1994


David J. Walsh, Director

