Opinion No. 71-52

April 13, 1971

BY: OPINION OF DAVID L. NORVELL, Attorney General

TO: Mr. T.L. Thomas Consumer Credit Supervisor Department of Banking Lew Wallace Building Santa Fe, N.M. 87501

QUESTIONS

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Is there a limitation on the finance charge which is imposed for financing insurance premiums when the insurance is **not** written in connection with loans or financing?

CONCLUSION

Yes.

OPINION

*{*73}* **ANALYSIS**

A typical transaction in which an insurance premium is financed involves four parties -- the buyer, the insurance agent, a finance company, and the insurance company. The insurance agent writes the policy. If the buyer wishes to pay his premium in installments, the insurance agent obtains all the necessary papers from the finance company, which usually specializes in insurance contracts. The finance company instructs the agent on completing the forms and fixes the downpayment and the terms of payment, including the finance charge. The insurance agent collects the downpayment from the buyer, delivers the policy to him, and gives the downpayment and all the financing papers to the finance company. The finance company pays the full amount of the premium to the insurance company. The buyer makes his payments to the finance company. The insurance company give the finance company the authority to cancel the insurance policy if the buyer defaults on his payments.

This transaction appears to be an installment sale, but the courts have characterized it as a loan. In **Ehrlich v. McConnell,** 214 Cal. App. 2d 280, 29 Cal. Rptr. 283 P.2d (1963), the California Court of Appeals upheld the suspension of an insurance agent's license on the grounds that the agent had charged usurious interest for financing insurance premiums. The agent paid the premium to the insurance company for the buyer and allowed the buyer to pay him in installments. The charge for this service exceeded 40% per year. The agent argued that the usury law did not apply to the transaction because it was an installment sales contract and not a loan or forbearance of money. Saying that it would look to the substance not the form of the transaction to

determine its nature, the court held the transaction was a loan. The court said that the Insurance Commissioner correctly "contended that no actual delivery of money is required to be made to the prospective insured; and that delivery thereof to a third person on behalf of the borrower is sufficient" to make the transation a loan. **Ehrlich v. McConnell, supra;** see also **Harris v. Gallant,** 183 Ca. 2d, 6 Cal. Rptr. 630.

The financing transaction in question is almost identical to the transaction in the **Ehrlich** case. The only difference is that in our case the insurance agent acts as an agent of the finance company *{*74}* in arranging the loan rather than lending the money himself. The insurance agent uses finance company forms and acts under finance company instructions in arranging the financing. The finance company pays the insurance company on behalf of the buyer. In both the **Ehrlich** case and in the financing transaction here, a third party pays the premium on behalf of the buyer.

We conclude that the premium financing arrangement practiced in New Mexico is a loan. As a loan it is governed by the New Mexico Statutes on usury, Sections 50-6-15 to 50-6-19, N.M.S.A., 1953 Comp. Section 50-6-15 provides:

"Excessive charges prohibited. -- No person, corporation or association, directly or indirectly, shall take, reserve, receive or charge any interest, discount or other advantage for the loan of money or credit or the forbearance or postponement of the right to receive money or credit except at the rates permitted in this act [50-6-15 to 50-6-19.]."

The maximum interest rates are set forth in Section 50-6-16, N.M.S.A., 1953 Comp.:

"Rates of interest allowed -- Minimum charge. -- The interest rate shall be the rate agreed to by the parties, except that no interest rate shall be higher than twelve per cent (12%) per annum computed upon unpaid balances for the actual elapsed time during which such balances respectively are unpaid where the evidence of indebtedness of the loan is not secured by collateral security, and shall not exceed ten per cent (10%) per annum computed upon unpaid balances for the actual elapsed time during which such balances respectively are unpaid where the evidence of indebtedness is secured by collateral security; Provided that a minimum charge of two ($ 2) dollars may be made for interest where the above authorized rates fail to aggregate said sum; Provided, however, that if more than one [1] loan is outstanding to the same borrower at the same time, such minimum charge may be charged on only one [1] such loan."

In certain instances the interest rate may be higher than 12%. If the loan is $ 1000 or less and if the finance company is licensed under the Small Loan Business Act, the finance charge may exceed the 12% general limit. Section 48-17-32 of the Small Loan Business Act provides:

"Applicability of act -- Exemptions -- Evasions -- Penalty. -- (a) Scope. No person shall engage in the business of lending in amounts of one thousand ($ 1,000) dollars or less, and contract for, exact, or receive, directly or indirectly on or in connection with any

such loan any charges whether for interest compensation, consideration, or expense, which in the aggregate are greater than the maximums as elsewhere provided by the laws of the state of New Mexico, except this act [48-17-30 to 48-17-58] and without first having obtained a license from the examiner."

The section allows those firms which have obtained a license from the State Bank Examiner and have otherwise complied with the Small Loan Business Act to charge interest rates higher than those allowed by the usury laws on loans of $ 1000 or less. Section 48-17-43 sets the maximum interest rates which may be charged by a firm licensed under the Small Business Act.

In summary, we conclude that charges for financing insurance premiums under the arrangement described above are limited by the usury law, unless the financing firm is qualified to charge higher rates pursuant to the Small Loan Business Act.

By: Thomas Patrick Whelan, Jr.

Assistant Attorney General