HELPING INSUREDS LEVERAGE THEIR CAPITAL

How premium financing can help your clients' cash flow

By Pattie Matos

Many Florida business owners have become optimistic about improved economic conditions, lower taxes, and fewer regulations. They anticipate a better overall economic environment that will stimulate cash flow and provide flexibility to invest in their business.

As the economy picks up, it pays agents to help insureds understand another option that can improve cash flow—leveraging premium financing. Premium financing is a simple way to free up capital that would otherwise have been spent on up-front, lump-sum payments for property and casualty insurance.

No collateral is required for a premium finance loan, as it is secured by unearned premium in the underlying insurance policy. A typical premium finance transaction involves a 20% down payment with the remaining 80% financed over nine or 10 months.

Understanding cash flow improvements

Let's compare the cost of financing to the return that can be generated on the working capital the insured retains by financing their premiums. Without financing, of course, insureds would pay the entire premium within 30 days of policy inception, thus losing the ability to leverage the money it would pay out as a lump sum.

The table at the top of the next page shows how an insured can retain cash each month with monthly premium financing vs. using an up-front lump-sum cash payment over the span of nine monthly payments.

Column C reflects cumulative payments made under a premium financing loan. Column D lists working capital

FINANCING—HOW IT BREAKS DOWN

Total Premium	**$250,000.00**
Down Payment	$50,000.00
Amount Financed	$200,000.00
Finance Charge (4.35% in this example)	$3,642.10
Total of Payments **(9 payments @ $22,626.90)**	**$203,642.10**

DETAILED ANALYSIS OF CASH RETAINED EACH MONTH			
Column A	Column B	Column C	Column D
Month	**Cash Payment** (Loss of use of cash each month is equal to the full premium amount)	**Financing** (Loss of use of cash each month is equal to the down payment plus each monthly installment)	**Working Capital** (Cash Payment minus Financing; Column B minus Column C)
1	$250,000	$50,000.00	$200,000.00
2	250,000	72,626.90	177,373.10
3	250,000	95,253.80	154,746.20
4	250,000	117,880.70	132,119.30
5	250,000	140,507.60	109,492.40
6	250,000	163,134.50	86,865.50
7	250,000	185,761.40	64,238.60
8	250,000	208,388.30	41,611.70
9	250,000	231,015.20	18,984.80
Total for all months			**$985,431.60**

freed up for each 30-day period (*i.e.,* the amount in Column B minus the amount shown in Column C equals the amount shown in Column D).

The total of **$985,431.60**, as shown in the bottom line of the table is divided by nine months to arrive at a figure for average working capital; in this example, it's **$109,492.40**.

Next, as shown below, let's look at the amount of additional income available to the insured that would not have otherwise been available without using premium finance. In addition to the income, which is more than **$926.51**, the insured can use the retained amount—averaging more than $100,000—for other purposes, once the down payment is made.

When discussing insurance plan options with their commercial clients, Florida agents can help them by reminding insureds that premium finance presents a pragmatic option that may well improve their cash position and flexibility—especially with respect to leveraging operational capital for investments in their business.

With an improving economy, the timing for leveraging premium finance to make best use of cash is right on the money. ■

The author

Pattie Matos is the Miami marketing office manager for AFCO Credit Corporation and Prime Rate Premium Finance Corporation, affiliated companies offering agents and brokers customized premium finance solutions for their insureds' property and casualty insurance.

ADVANTAGES OF FINANCING

Average Working Capital Retained by financing: $109,492.40

After-Tax Return of 4.00% for the nine-months finance term on the Average Working Capital Retained (added revenue to insured borrower): $3,284.77

Finance charge of 4.35%: $3,642.10

Less 35.25% tax liability reduction
(i.e., tax deductible amount):.. -1,283.84

After-Tax Cost of Finance Charge (added cost to insured borrower)..$2,358.26

Additional income to the Insured:...$926.51