



GarageGuys Tech Service Bulletin 02192009

Switching Insurance

Today's discussion is about expiration dates, short rate penalties and when it is OK to switch insurance carriers... and when it isn't.

We'll talk about some definitions first:

Short Rate Penalty—*This is the EXTRA cost (beyond a simple pro rata amount) of cancelling some policies before their natural expiration date. It reflects the idea that certain costs of issuing an insurance policy are fixed (such as the actual cost of printing and mailing the policy, inspecting the premises and ordering reinsurance) and are only fully amortized over the course of the entire year. This short rate has been arbitrarily fixed by the insurance industry at 10% of the remaining pro-rata amount. So a policy which costs \$365 per year and which is cancelled 165 days into the policy would generate a pro rata premium of \$200 ($\$365 - \$165 = \200). The short rate penalty would be 10% of the remainder or \$20 ($\$200 \times 10\% = \20). You can see from this example that the short rate penalty decreases steadily as the policy ages through the policy term and eventually becomes insignificant.*

Pro-Rata Cancellation—*A pro-rata cancellation reflects only the exact amount of insurance used from the start date until the day you cancel the policy. Each day that the policy is in force costs 1/365th of the full policy amount. Pro-rata cancellation is ALWAYS allowed for the following reasons: 1) The business which is insured is sold or goes out of business or 2) the cancellation is as a result of action by the CARRIER (either for non-payment of premium, an underwriting reason or some other carrier related cause.)*

Traditionally, facilities review their insurance a little less than one year from the start of their policy—usually called the “expiration” date or “ex date.” This ex-date provides a convenient reminder that a year has passed since the policy has started and also provides a “jumping off” point should you want to change carriers without any penalty. Some facility owners will not consider changing carriers except on the expiration date of their policy and while there is nothing wrong with

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this in principle, sometimes it may be better to consider the alternatives.

Here is a hypothetical example illustrating how "ex date only" is sometimes a short sighted route.

Let's say that your current package insurance premium is \$5,000 with someone besides GarageGuys and your policy will expire January 1st, 2010. Let's also say that you get a quote from GarageGuys on July 1, 2009 for \$4000.

You are an "ex date only" type of guy. You were happy to take the quote from us because of our fine reputation. But you were thinking that you would wait until January when your policy expired to put our quote in force because you don't want to cancel your current policy in the middle.

Let's analyze this in dollars and cents. If you were to cancel your \$5000 policy on July 1st, the short rate penalty would be \$250 (*here's how we figured that out—the pro rata remaining premium on a policy cancelled exactly in mid term is 50%. So 50% of the policy annual premium would be \$2500. The short rate penalty is 10% of \$2500 is \$250*)

If the penalty for cancelling your policy is \$250 then the only good reason for cancelling it is if you stand to save more than \$250 by doing so. In our example, the savings is \$1000. Your net gain is \$750 since you would subtract the short rate penalty from your savings.

Yes, you may have a reluctance to cancel your policy mid term. Still, it may be worth your while to cancel your policy mid term, take the penalty and still wind up \$750 ahead.

By the way, cancelling your policy in no way affects your credit rating personally or business.

What GarageGuys will do for you:

1. Calculate your penalty (if any) and advise you of your TRUE savings involved in our quote

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2. Handle your cancellation with your current carrier should you decide to switch to us.
3. Follow up to make sure that you receive any refund you may be due as a result of your policy cancellation.

Switching mid term may not be for everyone, however as you can see, it is not quite as complicated as you may have thought and there may well be benefits sufficient to make the process worthwhile.

Best Regards,

A handwritten signature in black ink that reads "Keith Friedlander". The signature is written in a cursive style with a horizontal line underneath the name.

Keith Friedlander
President

GarageGuys—Insurance For Your Shop

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