



For Immediate Release...

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OAKLAND, (December 4, 2003) -- More than 60 percent of California drivers -- 13.5 million motorists -- would see their auto insurance rates arbitrarily increased if a proposal under review by the Department of Insurance is adopted. That is the conclusion found in a study conducted by one of the nation's leading auto insurance actuaries.

Robert Downer, an independent insurance actuary, conducted a study that found that if the changes proposed in the petition are approved, drivers in 52 counties would be affected by suffering higher auto insurance rates. "Suburban and rural drivers and drivers in small to moderate size cities would pay more to subsidize urban drivers in a few larger cities. In addition, experienced drivers would pay more to subsidize inexperienced drivers, and good drivers would pay more to subsidize bad drivers," Downer said.

"Fifty-six percent of "bad" drivers (with at-fault accidents, traffic citations and/or very limited driving experience) would receive rate decreases, while 63 percent of California's good drivers (without at-fault accidents and/or traffic citations) would receive rate hikes. Also, 73 percent of California drivers with 34 or more years of driving experience would receive rate increases ranging up to 40% and more," said Downer, president of ARM Consultants.

A number of consumer groups have petitioned the Insurance Commissioner to modify and limit the opportunity for insurers in California to use optional rating factors in setting private passenger automobile rates. The Downer study was conducted at the request of three insurance trade associations -- the Personal Insurance Federation of California (PIFC), the Association of California Insurance Companies (ACIC) and the American Insurance Association (AIA). In order to perform this study, data was collected from four of the largest insurance companies in California. These insurers write private passenger auto insurance throughout the state. The impact for all California drivers is expected to be consistent with the findings from the business of these four companies.

At the first of several public discussions conducted today by the Department of Insurance, Sam Sorich, president of ACIC, noted the California Court of Appeals in *Spanish Speaking Citizens v. Low* upheld the current auto rating factor regulations. Proposition 103 requires auto insurers to base their rates on three mandatory factors-- driving record, miles driven and years of driving experience--and other optional factors approved by the insurance commissioner. The existing regulations upheld by the court allow insurers to give due consideration to factors related to where a car is garaged and driven.

Diane Colborn, vice president of PIFC, testified that auto rates be based on the cost of insuring the risk. Basing rates on the actual costs of providing insurance is necessary to avoid arbitrary rates or unfair subsidies. Both the courts and the Legislature have recognized that territorial factors that differ by region such as claim frequency, are important factors in determining future risk and cost-based rates. The Legislature recognized that auto insurance risks and costs differ by geographic area when it passed the Low-Cost Auto Insurance Program. "The program is available in Los Angeles and San Francisco Counties, however, the rates established by the Legislature for the low-cost policy in Los Angeles are higher than the rates set for San Francisco," she said. "The Downer study also concludes that location of the insured is very important in determining the risk and cost of losses. The cost and

the likelihood of being in an accident does vary significantly by region, and the price of insurance should reflect these cost-based differences,” stated Colborn.

Bill Gausewitz, assistant vice president of AIA, stated that “the California Supreme Court has made it clear that the current regulations comply fully with Proposition 103. The changes being reviewed are not required by law and would simply disrupt California’s auto insurance market.”

Sorich said if restrictions were placed on territory as a rating factor, policyholders living in higher-cost areas would have a decrease in their premiums, while drivers in lower-cost areas would have an increase. “According to public opinion polls almost 7 out of 10 persons feel it is unfair to make suburban and rural residents pay higher auto insurance premiums to subsidize those living in urban areas,” concluded Sorich.

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Impact of petition to modify use of Optional Rating Factors

Executive Summary

**Prepared by Robert Downer, Fellow of the Casualty Actuarial Society,
President, ARM Consultants, Inc.**

OVERVIEW

A number of consumer groups have petitioned the Commissioner of Insurance to modify and limit the opportunity for insurers in California to use optional rating factors in setting private passenger automobile rates. Optional rating factors are those other than the three mandatory factors – driving safety record, annual mileage and years of driving experience – that are substantially related to loss. The Personal Insurance Federation of California (“PIFC”) and the Association of California Insurance Companies (“ACIC”) commissioned a study of the impact of the proposals made by the petitioners.

Using comprehensive data from four large California private passenger automobile insurance companies, the impact of the proposal was assessed relative to (1) all drivers, (2) experienced drivers, (3) California good drivers, and (4) “bad” drivers (i.e., drivers not meeting California good driver criteria). The results of the study show:

- More than 60% of all California drivers would experience rate increases.
- Nearly three quarters (73%) of California drivers with 34 or more years experience – generally drivers age 50 and older – would receive rate increases.
- 63% of California good drivers would receive rate increases.
- 56% of “bad” drivers – drivers not meeting the California good driver criteria – would receive rate *decreases*.

None of these effects are related to risk of loss. To the contrary, they result from “tempering”, which in purpose and effect disassociates rates and premiums from risk of loss.

In order to perform this study, data was collected from four large insurance companies: State Farm Mutual Automobile Insurance Company, Zurich/Farmers, Allstate, and USAA. Together, these insurers comprise 37.8% of the California private passenger liability market (per 2002 DOI market share statistics). These insurers write private passenger auto insurance throughout the state; the impact for all California drivers is expected to be consistent with the findings from the business of these four companies.

FINDINGS OF THE STUDY

The petitioners' proposal creates increases in rates for some and decreases for others. Many of the rate changes are substantial (>10%). None of the changes are related to risk of loss, or the cost of providing the insurance. Some of the specific changes observed include:

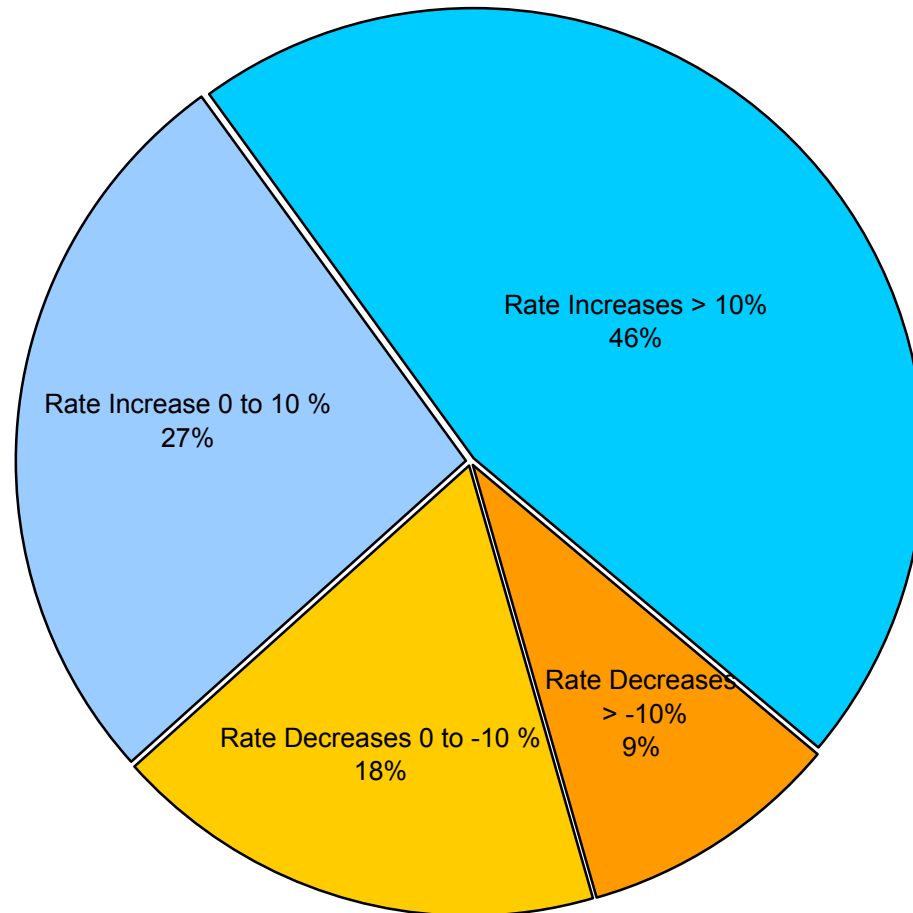
1. All Drivers - 61% of California drivers – thirteen and a half million drivers – would receive a rate increase. Nearly one-third of all California drivers (32%) – seven million drivers – would receive a substantial rate increase of greater than 10%. There is no change in risk of loss, just a rate increase unrelated to risk of loss. The rate changes are illustrated in Exhibit 1, attached hereto.
2. Experienced Drivers - Nearly three-quarters of experienced drivers (those with 34+ years of driving experience) would receive rate increases. Almost one-half (46%) of experienced drivers would receive a substantial rate increase of greater than 10%. These drivers, who are usually age 50 and up, are generally better drivers because of experience and maturity. Insurers generally see lower losses for the experienced drivers in this category. But, under petitioners' proposal, this group would unfairly receive rate increases entirely unrelated to their risk of loss. The rate changes are illustrated in Exhibit 2.
3. California Good Drivers - 63% of California good drivers would receive rate increases. That is, petitioners' proposal harms the majority of good drivers, by forcing them to pay higher rates without regard to risk of loss. The rate changes are illustrated in Exhibit 3.
4. Bad Drivers - 56% of "bad" drivers – drivers not meeting the California good driver criteria – would, conversely, receive rate *decreases*, favorably affecting poor drivers without basis in their risk or driving record. That is, petitioners' proposal benefits the majority of bad drivers while harming the majority of good drivers. This result is also illustrated in Exhibit 3.
5. Towns & Communities - Most communities in California will experience average rate increases; 973 of 1193 California towns and cities will receive average rate increases.
6. Counties – Fifty-two of California's fifty-eight counties would experience average rate increases under petitioners' Alternative 2. The rate changes by county are illustrated on Exhibit 4.

IMPLICATIONS AND RAMIFICATIONS

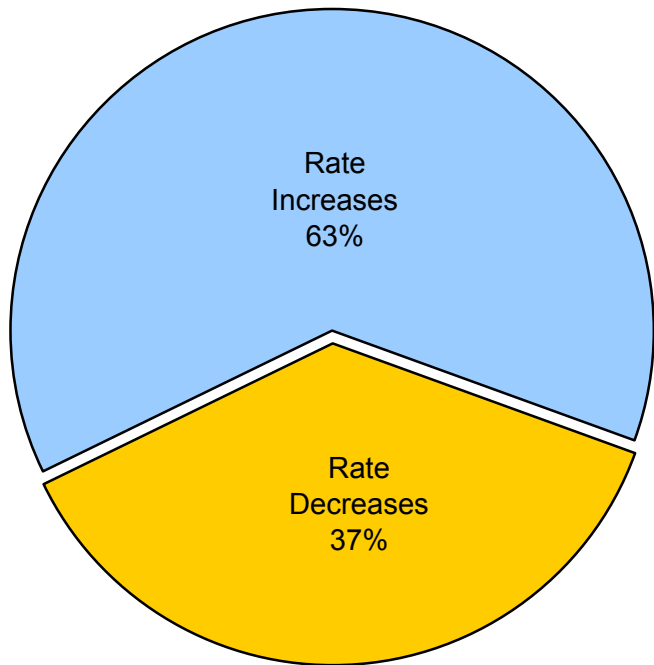
There are a number of negative implications from implementation of petitioners' proposal, most importantly:

- I. Financial disruption to individuals and households – Huge numbers of drivers would get unexpected, unjustified and substantial auto rate increases – unfairly and adversely impacting their family finances.
- II. Rates that are not risk-based – The changes requested in the petition will impose rate changes that are not cost or risk-based. Limiting the weight applied to optional rating factors limits the chance to use rating variables that are related to and actuarially predictive of losses.
- III. Rate subsidies – Subsidies will be produced all through the California automobile insurance market: suburban and rural communities will subsidize urban communities, experienced drivers will subsidize inexperienced drivers, and good drivers will subsidize bad drivers. All these subsidies are unrelated to risk of loss resulting in rates that are unfair and arbitrary.
- IV. Constraints on competition – If subsidies in rates are allowed to prosper and flourish, competition will be diminished. Subsidies arise when rates are not cost-based – lower risk drivers paying a portion of premium for higher risk drivers. Where this exists, there is reduced financial incentive by companies to write those drivers being subsidized, i.e. the higher risk drivers. There is no financial incentive; in fact, there is dis-incentive to write drivers having expected losses which exceed premiums. These conditions are not only actuarially inappropriate but also unhealthy to an active and competitive insurance marketplace

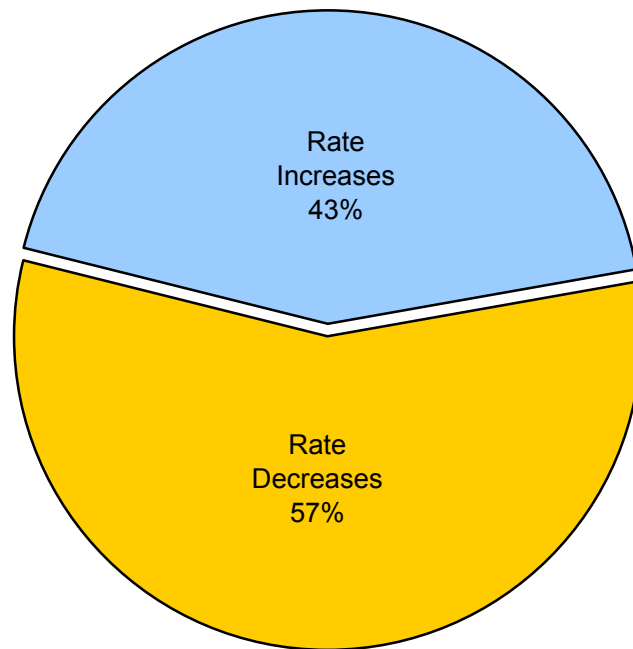
**Rate Increases/Decreases - Experienced Drivers
(34+ years driving experience)**



Rate Increases/Decreases - Good Drivers



Rate Increases/Decreases - Bad Drivers



Average Rate Increase/Decrease - By County

