

**STATE OF CALIFORNIA  
DEPARTMENT OF INSURANCE  
45 Fremont Street, 21<sup>st</sup> Floor  
San Francisco, California 94105**

**Proposed Amendments to Title 10, California Code of  
Regulations, Chapter 5, Subchapter 4.7, Section 2632.5  
[Pay-Drive (Usage Based Auto Insurance)]**

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**File No. REG-2008-00020**

**INITIAL STATEMENT OF REASONS**

**INTRODUCTION**

Pursuant to Insurance Code section 1861.02(e), Insurance Commissioner Steve Poizner (“Commissioner”) proposes to amend California Code of Regulations (CCR), Title 10, Chapter 5, Subchapter 4.7, Article 3, section 2632.5 (hereafter “Section 2632.5”). California Insurance Code (“CIC”) section 1861.02(e) requires the Commissioner to adopt regulations to implement CIC section 1861.02, including the auto rating factor provisions of that section.

CIC section 1861.02(a), added by Proposition 103, provides in relevant part:

Rates and premiums for an automobile insurance policy . . . shall be determined by application of the following factors in decreasing order of importance:

- (1) The insured's driving safety record.
- (2) The number of miles he or she drives annually.
- (3) The number of years of driving experience the insured has had.
- (4) Those other factors that the commissioner may adopt by regulation and that have a substantial relationship to the risk of loss.

These proposed amendments are also authorized by *CalFarm v. Deukmejian* (1989) 48 Cal.3d 805, 825 [258 Cal.Rptr. 161], *20th Century v. Garamendi* (1994) 8 Cal. 4th 216, 280 [32 Cal.Rptr.2d 807], *State Farm Mutual Auto. Ins. Co. v. Garamendi* (2004) 32 Cal.4th 1029, 1041 [12 Cal.Rptr. 3d 343], and *Spanish Speaking Citizens Foundation, Inc. v. Low* (2000) 85 Cal.App.4<sup>th</sup> 1179, 1214-17 [103 Cal.Rptr.2d 75] which recognize the Commissioner’s broad authority over insurance ratemaking.

**PURPOSE AND REASONABLE NECESSITY OF THE REGULATION**

The Commissioner has determined that the proposed amendments are reasonably necessary to carry out the requirements articulated in Insurance Code section 1861.02(a). The bases for this determination and the specific purpose of the proposed amendments are set forth below.

**Section 2632.5(c)(2).** The addition of the words “Except as provided in subdivision (E)” to Section 2632.5(c)(2) is necessary to make it clearer that the newly added subdivision 2632.5(c)(E) is an alternative to using estimated miles for the second mandatory rating factor.

**Section 2632.5(c)(E).** The existing subdivision “E” has been relabeled “F” and a new subdivision “E” is added. Subsequent paragraphs have been relabeled accordingly and references to the current subdivision “E” have been relabeled to reference “F.” The purpose of the newly added subdivision 2632.5(c)(E) is to clarify and make specific the following:

- That an insurer may employ verified actual mileage rather than estimated mileage as the second mandatory factor.
- That if an insurer employs verified actual mileage rather than estimated mileage, the insurer must verify the mileage using one of three methods. The three methods are (1) odometer readings by an employee or agent of the insurer; (2) service records obtained from an automotive repair dealer as defined in the California Business and Professions Code section 9880.1; (3) through the use of a technological device.
- That if an insurer employs verified actual mileage rather than estimated mileage, the insurer may retroactively adjust premiums based on actual miles driven provided the policy holder is notified before the effective date of the policy.
- That if an insurer employs verified actual mileage rather than estimated mileage, the insurer may provide a discount to reflect any cost savings or increased actuarial accuracy associated with the use of verified actual mileage, provided the discount has been filed with and approved by the Commissioner.
- That the insurers can only use verified actual mileage at the option of the insured and the insurer cannot require it as a condition to purchase insurance.

As indicated in the introduction above, the three mandatory rating factors in Proposition 103 are, in decreasing order of importance, driving safety record, miles driven annually, and years licensed. Of the three, the number of miles driven annually is the only one that may be based on a future estimate. This makes it relatively difficult to determine the second mandatory rating factor.

**Verified Actual Mileage -- Obtaining More Accurate Figures for Miles Driven Annually:** Insurers frequently rely on consumers to provide their own estimates of the number of miles they drive annually. One problem with self-estimated mileage is that there is no reliable way for consumers to estimate miles to be driven and estimates may vary considerably from the actual number of miles driven. In addition, while insurers are required to request insureds to re-estimate the number of miles to be driven annually at least every 3 years, insureds do not always respond to the request. As a result, insurers often either continue to use the previous estimate of miles to be driven annually or place the insured into a default mileage band. By making it possible to determine mileage more accurately, this regulation will advance more accurate and fair pricing of insurance for individual consumers, as contemplated by Proposition 103.

This, in turn, may reduce premiums for some drivers and increase competition in the automobile insurance marketplace.

**Necessity to Standardize and Limit Methods for Verifying Actual Miles Driven:** These amendments specify how an insurer may verify actual miles driven. This is necessary to achieve uniform results and protect consumers from arbitrary and/or unnecessarily burdensome or invasive mileage verification techniques.

**Necessity to Clarify When Insurers May Retroactively Adjust Premiums Based on Actual Miles Driven:** One way for an insurer to apply actual miles driven is to adjust the premium after the actual miles driven are verified and known. These amendments are necessary to make clear the permissibility of using verified actual miles driven for retroactive premium adjustment. This is only permissible provided the insurer has also given advance notification to the consumer that the premium may be adjusted based on the number of miles actually driven.

Further, these amendments are necessary to allow insurers to provide discounts to consumers who agree to use verified actual mileage as opposed to estimated mileage. This would allow policyholders who choose this option the opportunity to reduce their premium costs if they drive fewer miles.

**Necessity to Make the Use of Verified Actual Miles Driven Optional to the Insured:** The use of verified miles driven must be optional in order to prevent insurers from unfairly discriminating against certain insureds and to protect the privacy of insureds. These amendments are necessary to make the use of verified actual Miles driven optional to the insured.

#### **IDENTIFICATION OF STUDIES**

The Department has not relied upon any studies in connection with this rulemaking proceeding.

#### **SPECIFIC ACTIONS, PROCEDURES, TECHNOLOGIES OR EQUIPMENT**

Adoption of the proposed changes would not mandate the use of specific technologies or equipment.

#### **REASONABLE ALTERNATIVES**

Verification of the actual number of miles driven, as opposed to estimating the number of miles driven is optional under this regulation. However, performance standards were considered but were rejected as an unreasonable and impracticable alternative for determining the actual number of miles driven for the second mandatory rating factor. The Commissioner invites public comments on the proposed changes and reasonable alternatives which would be as effective to carry out the proposed changes.

#### **ECONOMIC IMPACT ON SMALL BUSINESS**

The Commissioner has initially determined that adoption of the proposed regulation will not have a significant, statewide adverse economic impact directly affecting small businesses. The Commissioner has identified no reasonable alternatives to the proposed regulations, nor have any such alternatives been brought to the attention of the Department, that would lessen any impact on small business. However, the Department invites public comments on the question of the economic impact on small businesses.

## **PRENOTICE PUBLIC DISCUSSIONS**

Pursuant to Government Code Section 11346.45, and California Code of Regulations, title 10, section 2646.3, the California Department of Insurance held a publicly noticed workshop on the topic of this regulation on June 23, 2008. Insurers and other parties who would likely be interested in or subject to the proposed regulation were invited and many attended the workshop.