



June 18, 2008

Ms. Sara Urakawa
California Department of Insurance
Rate Enforcement Bureau
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Dear Ms. Urakawa:

Thank you for the opportunity to submit written comments to the California Department of Insurance (CDI) in advance of the June 23, 2008 workshop regarding "Pay-As-You-Drive" automobile insurance (PAYD).

We greatly appreciate the CDI's interest in improving the auto insurance rating system. The concept of rating upon the exact number of miles actually driven, instead of estimated annual mileage, represents an important next step in auto rating. We look forward to working with the CDI to explore how to make PAYD a reality in California.

While a PAYD program could include some exciting, new developments in auto rating, we believe, at its core, the concept is nothing more than improved verification of a driver's annual mileage. As such, the main outcome of a PAYD discussion will hopefully be improvement of the existing auto rating rules.

We hope the CDI finds the following comments constructive and responsive to your workshop notice.

Rating Issues

- *CDI Rules Should Promote Innovation in Auto Rating*

Current CDI auto rating rules could be improved in significant ways before implementation of a formal PAYD system (and without triggering the "hot button" issues involving rating by garaging address). Under full implementation of the new auto rating factor (ARF) regulations, many carriers will likely be forced to require certain classes of drivers to subsidize other classes of drivers. This will happen in more than just the rural-to-urban cases that have generated so much media attention. It is highly likely that carriers will need to "pump" annual mileage beyond its predictive value to ensure it has more rating "weight" than the third mandatory factor (years of driving experience). Such pumping will lead to unfair subsidies among drivers.

A first step in any auto rating reform package should be to allow insurer innovation in rating factors, including the annual mileage factor. Current CDI rules recognize, in a limited way, that combining data for different rating factors reveals important trends. We respectfully request that the CDI allow more rating factor interactions. *We would not propose to include the optional territorial rating factors in this discussion.*

Specifically, we request the CDI to modify 10 CCR 2632.5(e) to read, in its entirety, as follows:

“2632.5 (e) The three mandatory factors may be combined with any other factor, except Claims Frequency and Claims Severity.”

With such a change, the CDI would still maintain complete control of the auto rating process. CDI rate analysts would still require a carrier to justify its actuarial analysis and use of rating factor interactions.

- *The Number of Mileage Brackets Is a Competitive Issue Not Appropriate for a “One Size Fits All” Approach*

The CDI PAYD workshop notice dated May 23, 2008 requested feedback on “appropriate mileage brackets.” We do not believe it necessary to create mandatory brackets. The experience of each carrier with the annual mileage rating factor is different; one set of brackets would be arbitrary and could affect carriers’ competitive positions.

As carriers obtain more accurate information about a driver’s actual annual mileage, they would likely find greater utility in increased numbers of mileage brackets. They should be empowered to innovate and compete without mandated segmentation of drivers into arbitrary mileage brackets.

Of particular importance is for the CDI to end its current reliance upon a driver’s “estimated mileage” without providing carriers adequate tools to verify actual mileage. Nothing in Proposition 103 requires the use of “estimated mileage” for the second mandatory factor; companies should be able to construct verification programs which allow consumer choice and potential for various rating options. Companies that insist upon overly-rigorous verification would certainly suffer in the marketplace; but, drivers who desire truthful mileage classification (and who do not want to subsidize drivers who underreport mileage) may enjoy the benefits of a rigorous verification process.

- *PAYD Programs Can be Incorporated Into Existing Rating Plans and Do Not Need to Exist Separately*

The CDI PAYD workshop asks for feedback on whether a PAYD program would need to be a separate program. We believe a PAYD program can be integrated into existing class plans.

The CDI has a few options for allowing PAYD programs into carriers’ class plans. One option is the approach in AB 2800 (Huffman). AB 2800 would permit rating discounts using the second mandatory factor for insurer-verified mileage. Allowing carriers to provide a discount to consumers willing to satisfy verification standards is a good starting point.

We understand some critics question the Legislature’s power to amend Proposition 103 in such a fashion and argue that this approach is a subterfuge to allow the Legislature to create an optional rating factor. We disagree with this contention, but the CDI could unquestionably end the debate by issuing regulations to allow insurer-verified mileage discounts (whether through the second

mandatory factor or an additional optional rating factor). We are indifferent as to the CDI's approach; we only desire the ability to offer discounts based upon insurer-verified mileage.

- *Insurer Group Issues Should Be Treated No Differently for PAYD as They are Treated Under Current Rules*

PAYD does not require new rules for insurer groups. PAYD is nothing more than a concept for rating based upon actual mileage driven. It should be, in the end, nothing more than a change from "estimated mileage" to using actual mileage for insurance rating.

The current rule which allows a consumer to obtain the lowest rate in a group for which you qualify should continue to govern after implementation of any PAYD system.

- *It is Critical to Allow Maximum Flexibility for Mileage Verification*

The CDI PAYD workshop notice requests feedback on appropriate technology for mileage verification. While technology could play a part in a PAYD program, it is not the only approach possible. CDI rules should promote a diversity of approaches that will lead to product innovation and consumer benefit.

For companies that do not plan to use new technology for a PAYD program, they should be free to establish verification programs beyond the current limited mileage verification regulations. If they believe manual collection of odometer readings would be feasible and relevant to rating, CDI rules should permit such an approach under CDI supervision without the current "estimated mileage" restrictions. For companies that do plan to use new technology for a PAYD program, such as wireless transmission of odometer information, they should likewise be free to establish a verification program under the supervision of the CDI.

A key element of PAYD mileage verification is for the CDI to promote flexibility without stifling innovation or requiring any particular approach. There is no need for the CDI to pick a certain verification approach. When considering next steps, the CDI may also want to consider whether readily available, cost effective technology will be feasible and readily available in the marketplace.

- *Privacy and Security Issues Raised by Technological Approaches Are Surmountable*

The CDI PAYD workshop notice requested feedback on privacy and security issues. We think it is very important to pursue PAYD concepts while respecting consumers' privacy concerns. The privacy concerns are less in the context of mileage verification issues, because privacy concerns should not shield dishonest reporting of mileage verification.

But the privacy concerns loom large when tracking devices are attached to vehicles. At this point, we prefer an opt-in approach for use of technology on cars. Consumers should know exactly what information will be tracked when they voluntarily attach devices to their cars; further, the CDI would rightly control what information can be used in the insurance rating process.

We do believe that carriers should be able to collect more information than what is actually used for rating purposes in hopes of learning, over time, what other variables could be predictive of the risk of loss. Such research could lead to product innovation and new discounts, and ultimately requests for either amending current rating factors or adding new ones.

We do not believe that a PAYD system presents novel security issues. Current standards for transmission of customer data to third parties or through the Internet apply with equal force to PAYD approaches.

- *Insurers Will Embrace PAYD Programs If Innovation and Flexibility Are Possible*

Carriers will embrace PAYD programs if CDI rules allow sufficient flexibility for innovation and market differentiation. If the CDI makes PAYD rules too restrictive or "one size fits all," then it is less likely for PAYD concepts to take hold in the marketplace and very unlikely to take hold broadly in the marketplace.

- *Consumers Will Participate in PAYD Programs In Which They See Value*

We do not believe any state incentives are necessary to encourage consumers to participate in PAYD programs. Each carrier will promote its PAYD programs in ways to encourage consumer participation. Presumably the biggest incentive that carriers will provide will be rating incentives; that should be sufficient.

- *Disclosure of Mileage Brackets and Mileage Factors Should Be Voluntary*

We question whether it is necessary to require disclosure of a carrier's mileage brackets or mileage factors, whether on a web site or otherwise. The average (or even extraordinary) consumer is not likely to analyze such technical details as part of his or her purchase decision. If a carrier would like to market such information or attempt to create public awareness for its own competitive advantage, it should be fully able to do so. Other carriers should be free to spend their time on what they perceive to be more productive, and less costly, activities that are more relevant to their marketplace competition.

- *There Is a Lack of Consensus Upon Optional Versus Mandatory Participation in PAYD Programs*

Our member companies have not reached consensus on the issue of whether PAYD programs should be optional or mandatory for insureds. Of the variety of opinions, there is a view that a carrier should be free to choose its PAYD/verification/rating approach – reaping the benefits or suffering the detriments of a mandatory program as dictated by customer reaction. This could include requiring reasonable disclosure of service records and other materials to enable mileage verification. Another view provides that carriers can offer incentives for consumers to opt-in to PAYD/verification/rating approaches on a voluntary basis.

Because of this divergence of opinion among our member companies, we express no opinion as a federation.

We hope the above feedback is helpful. Please call with questions. We look forward to discussing these issues with CDI staff on June 23, 2008.

Sincerely,



Rex D. Frazier
President