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STATE OF CALIFORNIA  
DEPARTMENT OF INSURANCE  
45 Fremont Street, 21st Floor  
San Francisco, California 94105

File No. RH05044654

Date: September 8, 2006

## **INITIAL STATEMENT OF REASONS**

### **PROPOSED AMENDMENTS TO THE AUTO BODY REPAIR LABOR RATE SURVEYS REGULATIONS**

#### **INTRODUCTION:**

California Insurance Commissioner John Garamendi ("Commissioner") will consider the amendment of Title 10, California Code of Regulations, Chapter 5, Subchapter 9, Article 7, Section 2698.91, entitled "Auto Body Repair Labor Rate Surveys". The original regulations became effective October 25, 2002. After working with the regulations, it has become apparent that additional clarification is necessary for the proper interpretation and implementation of the statute.

The purpose of the proposed amendment is to further interpret, clarify, and make specific the provisions of California Insurance Code ("Ins. Code") section 758(c) and to provide insurers with a mechanism to support the use of labor rate surveys when settling automobile insurance repair claims in a fair, equitable and reasonable manner, as required by California Insurance Code ("Ins. Code") section 790.03(h).

#### **DESCRIPTION OF THE PUBLIC PROBLEM ADDRESSED BY EACH SUBDIVISION / THE SPECIFIC PURPOSE AND NECESSITY OF EACH SUBDIVISION**

Auto insurance fraud and theft in California costs upwards of \$9 billion annually. The Legislative Branch determined that more was needed to be done to curtail these fraudulent activities.

Ins. Code section 758 (c) provides that if an insurer conducts an auto body repair labor rate survey to determine and set a specified prevailing rate in a specific geographic area, the insurers must report the results of the survey to the Department of Insurance. The Department of Insurance is required to make the information available upon request.

The current regulations provide some broad definitions, outline what information should be included in the surveys, and provide a procedure for submitting the surveys to the Department of Insurance. However, based on the information, reports, and complaints we have received from consumers, insurers, and the auto body industry, there are several areas that require further clarification. For example, because there is no standard methodology specifically outlined in the statute (i.e. should insurers use the average rate of the shops surveyed or the median of rates obtained by survey), the surveys tend to produce inconsistent results, creating confusion when the insurers rely on the results to support their adjustment of the body shop estimate as reasonable within the meaning of CCR 2695.8(f) of the Fair Claims Settlement Practices regulations. As a result of the labor rates disputes that arise, the consumer is often placed in a position where they have to pay the difference between the shops labor rate and the rate the insurer will pay before the body shop releases the car.

The proposed amendments will further define specific terms and more clearly set out the purpose and use of surveys conducted pursuant to Insurance Code Section 758(c). Further, since surveys conducted pursuant to Insurance Code Section 758(c) contain only minimal standards, the Commissioner has deemed them unreliable for use by insurers in settling claims. Therefore, in addition to clarifying the standards and use of Insurance Code Section 758(c) surveys, the Commissioner proposes amendments, which would permit insurers to conduct a more reliable labor rate survey, using additional standards set forth in these regulations.

The specific purpose of each amendment or adoption, and the rationale for the determination that each amendment or adoption is reasonably necessary to carry out the purpose for which it is proposed, together with a description of the public problem, administrative requirement, or other condition or circumstance that each adoption is intended to address, is set forth below.

Proposed section 2698.91(a): (Amend)

Existing 2698.91(a) defines the term "auto body repair labor rate survey" as used in Ins. Code section 758(c). The proposed amendment would make the definition apply to the term "survey" as well. Additional language and punctuation changes have been made for clarification and consistency purposes. The change to this section is necessary to further define and clarify these terms in order to assist the reader in understanding the statute and regulations.

Proposed section 2698.91(b): (Amend)

Existing 2698.91(b) defines "prevailing auto body rate" as employed in Ins. Code section 758(c). Confusion has arisen regarding the current definition. The proposed amendment clarifies the definition by more specifically describing the term. Webster's New World Dictionary, Third College Edition (1991), defines "prevailing" as "predominant....widely existing....prevalent". The proposed definition clarifies that "prevailing auto body rate" means the rate at or below which, the majority of surveyed shops charge in a geographic area. Further, in order that the rate described above does not fall below the average of rates in an area, the prevailing rate must be at least equal to or greater than the average rate. Additional language and punctuation changes have been made for clarification and consistency purposes. The change to this section is necessary to further define and clarify these terms in order to assist the reader in understanding the statute and regulations.

Proposed section 2698.91(c): (Amend)

Existing 2698.91(c) requires the insurer to provide a description of what geographic areas were surveyed, a description of the methodology used to reach the prevailing rate, and the prevailing rate established for each geographic area surveyed. This information provides a context for the information specifically outlined in the statute. The proposed amendment further requires that the submitting insurer provide the labor rate charged by each particular shop surveyed the total number of shops that responded to their survey, and the date the survey was completed.

Additional language and punctuation changes have been made for clarification and consistency purposes. The change to this section is necessary to further clarify the statutory provisions and for organizational purposes and consistency.

Current section 2698.91(d): (Repeal)

This section is repealed, as the submission requirements to the Department have been clarified in the adoption of proposed section 2698.91(f).

Proposed section 2698.91(d): (Adopt)

The proposed adoption of 2698.91(d) is intended to clarify the distinction between public information, as described in section 2698.91(c) and non-public information. The non-public information required to be submitted to the Department includes the (1) the labor rate reported by each shop that responded to the survey; (2) the name and address of each shop sent a survey, but that did not respond to the survey, reported for each geographic area surveyed; and (3) a copy of the survey questionnaire used to survey the auto body repair shops.

Proposed section 2698.91(e): (Adopt)

This adoption clarifies the requirement that the survey must be conducted in writing or the insurer must maintain written records of the information gathered by any method other than writing. Upon request, the department shall have access to all records, data, computer programs, or any other information used by the insurer or any other source to determine geographic area labor rate information. This adoption is necessary to ensure that the Commissioner is able to obtain and review the documentation to ensure that the surveys were conducted in compliance with the standards set forth in these regulations.

Proposed section 2698.91(f): (Adopt)

This proposed section sets forth the submission requirements that insurer must adhere to when submitting the surveys to the department. The change to this section is necessary to better implement the statutory provisions and simplify the submission and publication of the statutory requirements.

Proposed section 2698.91(g): (Re-letter and Amend)

Existing 2698.91(e) sets out the procedure for making copies of the surveys available to the public. Minor changes have also been made to complete the citation to the California Public Records Act. This section is re-lettered to section 2698.91(g) and amended to further clarify what information will be made public and what information will not be made public.

Proposed section 2698.91(h): (Adopt)

This new section declares that an insurer shall not use any discounted rates, obtained from Direct Repair Program (DRP) shops, in its surveys. This adopted section clarifies the Department's position that a survey is not reliable if it contains labor rates that are artificially low and that do not reflect the retail market for auto body repairs that consumers, who do not have DRP arrangements, must pay for repairs.

Proposed section 2698.91(i): (Adopt)

The proposed section clarifies the primary purpose of a survey submitted pursuant to Insurance Code section 758, which is to inform the public about the prevailing labor rates charged in a specific geographic area and to provide insurers with a starting point in negotiating labor rates with auto body repair shops. It further clarifies that a survey shall not be used to cap or reduce the labor rate charged on an estimate or repair order prepared by the claimant's chosen auto body repair shop or to support the reasonableness of an insurers' adjustment of a written estimate provided by a claimant pursuant to section 2695.8(f)(3) of California Code of Regulations, Title 10, Chapter 5, Subchapter 7.5, except as provided in Section 2698.92 of these regulations. This amendment is necessary to describe the limited purpose of a survey submitted pursuant to Insurance Code section 758 in order to distinguish it from the purpose and scope of a survey conducted pursuant to proposed section 2696.92.

Proposed section 2698.91(j): (Adopt)

This proposed section is intended to clarify that nothing in these regulations shall be construed to require an insurer to pay more than the amount necessary to perform workmanlike repairs.

Proposed section 2698.91(k): (Adopt)

The proposed amendment clarifies that nothing in these regulations prohibits an insurer from voluntarily negotiating or contracting with an auto body repair shop for a specific labor rate. The change to this section is necessary to clarify the statutory provisions.

Proposed section 2698.91(l): (Adopt)

Insurance Code Section 758(c) does not require an insurer to conduct a labor rate survey. The proposed amendment clarifies this legislative intent in stating that nothing in these regulations shall require an insurer to conduct an auto body labor rate survey.

Proposed section 2698.91(m): (Adopt)

The Bureau of Automotive Repair does not require auto body repair shops to post the labor rates they charge to customers. Also, in some cases, where auto body repair shops do post a labor rate, these shops do not charge this posted rate on any consistent basis. The purpose of this amendment is to recognize this reality and clarify that insurers are not required to use a shop's posted labor rate, unless that shop charges its posted labor rate on a consistent basis.

Section 2698.91 (Note):

The "Note" for this section is amended to add the reference cite for Insurance Code section 790.03, as the Unfair Practices Act is the basis for the department's regulation of how surveys are conducted is based upon the premise that these surveys should be reliable, fair and reasonable. Also, Section 2695.8 (f)(3) of California Code of Regulations, Title 10, Chapter 5, Subchapter 7.5. (Fair Claims Settlement Practices Regulations) was added as this section was referenced in our proposed section 2698.91(i).

Proposed section 2698.92(a): (Adopt)

This section is adopted in order to set forth additional standards and processes that would result in a more reliable survey, than a survey conducted pursuant to the minimal standards of a survey conducted pursuant to Insurance Code Section 758(c). The additional standards set forth in this new section (2698.92), are based upon the authority granted under Insurance Code Section 790.10. This proposed amendment seeks to set forth the method by which an insurer may support its compliance with Insurance Code section 790.03(h)(5) and the associated Fair Claims Settlement Practices Regulations section 2695.8(f)(3), which requires insurers to reasonably adjust an estimate prepared by the claimant's shop. If an insurer chooses to conduct a survey pursuant to this newly adopted section, the Department may consider this survey in determining whether an insurer has offered a fair and reasonable claims settlement. As these may be some differences in the standards or requirements of a survey conducted pursuant to section 2698.91 and section 2698.92, additional language is adopted to clarify that in instances where the standards in this section and Section 2698.91 conflict, the provisions of this section shall supersede the provisions of Section 2698.91.

Proposed section 2698.92(b): (Adopt)

The Department recognizes that overhead and other costs that determine a labor rate may change over time. Survey data may become stale and not properly represent the going market rate for repairs. This subsection is proposed to set forth the standard that, unless otherwise authorized by the Department, a survey compliant with this section must be submitted to the Department no less than annually.

Proposed section 2698.92(c): (Adopt)

According to the Bureau of Automotive Repair, there are approximately 5,000 automotive repair dealers licensed to perform automobile collision repair services in this state. Given this relatively low number of shops, especially when broken down into smaller geographic areas, surveying too few shops would result in an unreliable prevailing rate for any given area. This subsection is adopted to ensure that all qualified shops be surveyed to ensure the most accurate and reliable results. This language also reduces the possibility that the shops with known lower labor rates are used in a survey to the detriment of higher (but still reasonably) priced shops. To be a statistically valid survey, the insurer must survey, or send a survey questionnaire to, all known auto body repair shops licensed by the Bureau of Automotive Repair in a specific geographic area. All shops that respond to the survey, and which meet the standards set forth in subsection 2698.92(f) of these regulations, shall be used to determine the prevailing auto body rate in that geographic area.

Proposed section 2698.92(d): (Adopt)

This subsection is proposed to ensure that repair facilities, which may not be duly licensed by the Bureau of Automotive Repair, should not be used in the survey. Also, this subsection shall not require an insurer to verify the licenses status of surveyed shops with the Bureau of Automotive Repair, in cases where the survey questionnaire or survey format asks the repair shop to respond as to whether it is duly licensed to perform auto body collision repairs in this state.

Proposed section 2698.92(e): (Adopt)

The general premise is that shops that do not have all the standard equipment necessary to effect proper repairs may charge rates below the market rate due to cheaper operating costs. This subsection is

intended to ensure that shops that do not meet certain standards shall not be used in a labor rate survey. An insurer may only use labor rates in a survey reported by shops that meet the enumerated specific standards. These standards were obtained from (1) the equipment requirements for auto body repair shops, as required by the Bureau of Automotive Repair and as described in California Code of Regulations, Title 16, Division 33, Chapter 1, Article 6, Section 3351.5, Equipment Requirements for Auto Body Repair Shops; and (2) the "Minimum Recommended Requirements for a `Class A" Collision Center", as published by the Collision Industry Conference (CIC) in 2005. This subsection also recognizes that it would be burdensome on insurers if required to inspect each surveyed shop to determine if it meets these specific criteria. Therefore, additional language permits an insurer to ask the repair shop in the survey whether it meets the specifically identified standards. Lastly, language is added to clarify that these standards are only to be used to determine which shops' labor rates may be included in a survey and it must not be used to prohibit a shop from performing repairs on a vehicle. Insurance Code Section 758.5 provides that all claimants have a right to have their vehicle repaired in the shop of their choice. The fact that a shop does not meet these standards should not be construed as permission for insurers to imply that the shop is inferior or should not be used by the claimant to perform repairs.

Proposed section 2698.92(f): (Adopt)

This subsection adds the additional standard that the survey results shall contain the labor rate amount charged by each particular shop that responded to the survey. The purpose of this subsection is to provide the Department with sufficient information it needs to verify the accuracy of the survey conducted by the insurer. This information will be considered non-public information and will not be subject to public disclosure, as described by these regulations in section 2698.91(g).

Proposed section 2698.92(g): (Adopt)

The purpose of this subsection is to clarify that the "prevailing auto body rate", as defined in Section 2698.91(b), of these regulations, is the same standard that shall apply for a survey conducted pursuant to this section. Further, the department recognizes that other methods may result in fair and reasonable settlement offers. Therefore, this subsection also permits other methods, but only after review and approval by the Commissioner.

Proposed section 2698.92(h): (Adopt)

This subsection clarifies that the additional data and survey information provided in accordance with this section shall not be the subject of a Public Records Act request, pursuant to the California Public Records Act, Government Code section 6250 et seq. The additional intent of this subsection is to provide a mechanism for compliance with Insurance Code section 758(c), on making a survey public, while acknowledging that the additional information is not subject to public disclosure.

Proposed section 2698.92(i): (Adopt)

This subsection clarifies that the geographic area must be based upon the specific description of each area as cited in subsection 2698.92(j).

Proposed section 2698.92(j): (Adopt)

This subsection defines each geographic area zone. The purpose is to ensure consistency and reliability among insurers in their surveys.

Proposed section 2698.92 (Note): (Adopt)

The Note is proposed to add the Authority cites for Sections 758, 790.03, 12921, and 12926, Insurance Code and Reference: Sections 758 and 790.03, Insurance Code; Section 6250-6276.48, Government Code; and Section 2695.8(f)(3) of California Code of Regulations, Title 10, Chapter 5, Subchapter 7.5.

## **IDENTIFICATION OF STUDIES AND REPORTS**

The Department of Insurance did not rely upon any technical, theoretical and/or empirical study, report or similar document in proposing this regulation. Rather, it relied on the extensive data and experience of the Department's Consumer Services Bureau, its Enforcement Division, its Legal Division, and extensive input from various trade organizations.

## **SPECIFIC TECHNOLOGIES OR EQUIPMENT**

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

#### CONSIDERATION OF ALTERNATIVES

The Commissioner has not identified alternatives to any of the sections or subdivisions thereof which would lessen any adverse impact on small businesses, yet still achieve the desired regulatory objective.

#### IMPACT ON SMALL BUSINESS

The Commissioner has determined that the proposed regulations do not affect small businesses. The regulations do not require any action on the part of any business or individual. Instead, it mandates that the Department of Insurance maintain information submitted to it and make the information available to the public if requested.

#### PRE-NOTICE DISCUSSIONS

The Commissioner conducted pre-notice public discussions pursuant to Government Code Section 11346.45(a) on June 8, 2005. Interested and affected parties were given an opportunity to present statements or comments with respect to the proposed amendments. The Commissioner considered these statements and comments in drafting the proposed amendments.

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