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STUDY RATES CALIFORNIA AUTO INSURANCE REGULATION MOST PRO-CONSUMER (AND VERY PRO-INDUSTRY)

Washington, D.C. -- A 90-page Consumer Federation of America study, released this morning, concludes that California has the most pro-consumer auto insurance regulation in the nation. The report found that the provisions of Proposition 103 -- passed by California voters in 1988 -- led to the creation of a regulatory system that benefitted both consumers and insurers alike.

"Prop. 103 created a system with higher profits, lower rate increases, and more rapid declines in assigned rate drivers than in any other state," said J. Robert Hunter, CFA's Director of Insurance and former Texas Insurance Commissioner, who prepared the study. "Instead of eagerly embracing industry deregulation proposals, state insurance commissioners should look to California for guidance about how to effectively regulate personal lines of insurance," he added.

Consumers spend, on average, more on auto insurance than on any other type of insurance -- annually, an average of more than $700 per car and more than $1,500 per household -- well over $100 billion nationwide. Their concern about rising auto insurance rates, more than any other factor, led to voter approval of the California initiative which insurers spent tens of millions of dollars trying to defeat.

California Drivers Gain Lower Rates While Insurers Profit

After passage of Prop. 103, California drivers received rate rollbacks totaling $1.3 billion. But their greatest gain was rates that declined over the next decade. From 1989 to 1998, auto insurance rates declined by 4 percent in California while they were rising by more than 25 percent in the rest of the country. That decline represents the lowest rate of change of any state in the nation.

During the same period, California auto insurers were enjoying healthy profits. A calculation of annual return on net worth from 1990 to 1999 reveals that these insurers received 16.0 percent compared to only 10.9 percent received by auto insurers nationally.

More Competition and Smarter Regulation Explain Lower Rates

Despite industry opposition, Prop. 103 created a system mixing greater competition with smarter regulation and greater consumer participation. The result was lower consumer rates and higher industry profits.

Greater Competition: To promote competition, the initiative eliminated the state antitrust exemption, allowed banks to sell insurance, allowed groups to make purchases collectively, enabled insurance agents to rebate part of their commissions, and greatly improved consumer information. In regard to the latter, Prop. 103 required the California Commissioner to provide consumers with a current rate comparison survey for all personal lines of insurance.

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Smarter Regulation: Prop. 103 required insurers to open their books to justify rate increases or decreases. For the first time in the state, insurers were provided with financial incentives for efficient performance. Most importantly, this "prior approval" regulatory system effectively ended the traditional "cost-plus" method of insurer pricing in which there was little incentive for insurers to restrain losses and operate efficiently. Insurers began to actively hold down costs.

Prop. 103 also provided consumers with "good driver" incentives while reducing the discriminatory impact of risk factors over which drivers had little or no control. "Clean" drivers received a 20 percent discount and also the right to purchase insurance from the company of their choice through the initiative's "good driver protections." This was an important reason that the proportion of those who were uninsured or insured in the California Automobile Assigned Risk Plan dropped from by more than 50% from 1989 to 1999.

Greater Consumer Participation: Prop. 103 also allowed greater consumer participation by providing funding for consumer intervention if the intervenors make a "substantial contribution" to the case. This provision not only helped empower California consumers; it also helped keep insurance regulators honest.

Insurer Criticism of Prop. 103 Is Weak

The insurance industry and its partisans offer weak criticism of Prop. 103. That criticism includes the claim that the initiative allowed them to gain excessive profits. They argue that, had insurers been free to increase rates without regulatory approval, they would have lowered their prices even more than they did, knowing that they could later increase rates freely if conditions changed.

However, insurer profits were high not only because Prop. 103 rationalized the regulatory system but also because of the generosity of Insurance Commissioner Quackenbush to the industry. Quackenbush, commissioner from 1995 to 2000, refused to investigate, let alone limit, insurer profits. Later, it became clear that some of the same companies who benefited from the Commissioner's refusal to use his regulatory powers under 103 were companies that provided money to various slush funds he was amassing outside of government in exchange for favors.

Insurers also argue that greater use of seat belts in California was largely responsible for lower rates in that state. However, data show that, from 1989 to 1998, seatbelt use in California rose by only 34 percent while it was rising by 54 percent in the rest of the country.

CFA Calls On Insurance Regulators to Consider California System

"As the NAIC studies personal lines regulation, it should not simply deregulate the current non-competitive systems," said Hunter. "Instead, NAIC should adopt the sort of full competition and excellent regulatory backup that Prop. 103 has provided for California's consumers. Why not the best for all the people of America?" Hunter asked.

CFA will be distributing copies of the report at the upcoming National Association of Insurance Commissioners' meeting in New Orleans this weekend. It also will be mailing copies to each state regulator. Finally, it will be distributing copies to national policymakers and other experts concerned about insurance regulation.

CFA is a non-profit association of 285 consumer groups that, since 1968, has sought to advance the consumer interest through advocacy and education.

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