

**TESTIMONY OF PAMELA PRESSLEY
THE FOUNDATION FOR TAXPAYER AND CONSUMER RIGHTS
BEFORE THE CALIFORNIA DEPARTMENT OF INSURANCE**

**In the Matter of RH-402
Hearing Regarding Proposed Changes to the
Persistency Optional Automobile Rating Factor at CCR 2632.5(d)(11)
February 28, 2002**

I. INTRODUCTION

A. Opening Remarks

My name is Pamela Pressley, and I am a staff attorney for The Foundation for Taxpayer and Consumer Rights (FTCR), a non-profit, non-partisan public interest corporation organized to represent the interests of taxpayers and consumers. One of FTCR's chief programs is the Proposition 103 Enforcement Project, which was formed in 1993 to represent the interests of insurance policyholders, particularly as they relate to the implementation and enforcement of Proposition 103 in matters before the Legislature, the courts, and the CDI. FTCR appreciates Commissioner Low's granting of its rulemaking request and having the opportunity to testify today on this important issue affecting all Californians who are required by law to maintain automobile insurance coverage.

B. Scope of Problem and Procedural Background

FTCR initiated this proceeding, RH-402, by petitioning the Commissioner for a rulemaking hearing, by letter dated May 4, 2001, to address the abuses of certain insurers

it found to be illegally using automobile insurance rating factors to charge previously uninsured drivers higher premiums, in violation of the mandates of Insurance Code § 1861.02(c). (“§ 1861.02(c)”) According to the latest CDI statistics, approximately one in four California motorists are uninsured. (Bernstein, CDI, *California Uninsured Vehicles as of June 1, 1997*, February 1999, p. iii [5.3 million of 23.5 million potentially insurable vehicles].) Of course, the uninsured motorist rate ranges much higher in low-income and minority communities—up to 51% in underserved communities¹ overall and up to 75-80% in certain low-income Los Angeles County communities. (1998 Commissioner’s Report on Underserved Communities.) Affordability remains a key reason why such a high number of drivers are uninsured. According to a 1999 CDI study, the majority of uninsured motorists surveyed indicated that they would probably purchase insurance if premiums were even 10% lower than the current level. (Lyn Hunstad, CDI, *Characteristics of Uninsured Motorist*, February 1999, p.1.) The uninsured motorist rate is closely linked to higher premiums in that “each \$22 increase in annual premiums increases the average uninsured rate by 1 percent.” (Berstein, p. iv.)

¹ Per Cal. Code Regs. § 2646.6, a community shall be deemed to be underserved by the insurance industry if the Commissioner finds:

- a) the proportion of uninsured motorists is ten percentage points above the statewide average as reflected in the most recent Department of Insurance statistics regarding the statewide average of uninsured motorists; and
- b) the per capita income of the community, as measured in the most recent U.S. Census, is below the fiftieth (50th) percentile for California; and
- c) the community, as measured in the most recent U.S. Census, is predominantly minority. Predominantly minority community can be qualified as any community that is composed of two-thirds or more minorities as those groups are defined in subsection (b)(6)(A) through (D) of CCR Code 2646.6.

Particularly in light of the recent flurry of requested rate increases,² and the expectation of further applications, what these statistics show is that even a 10-15% surcharge on previously uninsured motorists will hugely impact the number of drivers who are unable to afford auto insurance. The uninsured are in a perpetual “Catch-22” situation. These higher initial rates will in many cases be enough to prevent the uninsured from being able to afford a policy. The door to insured status remains closed to these drivers.

Of course, the over 20 million drivers who are currently insured are also negatively impacted by the inability of uninsured motorists to obtain affordable coverage. Just as implementing the Lifeline Auto Insurance Program will result in hundreds of millions of dollars in reduced uninsured motorist coverage premiums to the currently insured, so too will eliminating illegal surcharges to the previously uninsured.

On June 4, 2001, the Insurance Commissioner issued his decision granting FTCR’s rulemaking petition, wherein he agreed that insurers’ use of certain “discounts” or “surcharges”, such as “persistency” discounts, “has the potential to conflict with the provisions of California Insurance Code § 1861.02(c).” (Decision on Petition for Rulemaking, File No. RH-402 (June 4, 2001).)

FTCR, jointly with Consumers Union, then petitioned on July 18, 2001 for emergency regulations and proposed regulatory language, which it urged the Commissioner to enact pending his adoption of final regulations in RH-402. This

² See *Los Angeles Times*, “Auto Insurance Seen Returning to Era of Annual Rate Increases; Premiums: Major insurers, looking to increase profits and citing higher claim costs, seek to raise fees, executive says,” by Jerry Hirsch, May 1, 2001, Business section, page 1.

petition for emergency regulations was denied by the Commissioner by decision dated August 17, 2001, File No. ER-01-01-5986.

On September 6, 2001, the Commissioner issued a “Request for Public Input” on proposed regulatory language addressing the use of persistency as an automobile rating factor, which included the regulatory language proposed by FTCR and Consumers Union as set forth in their petition for emergency regulation, as well as draft regulatory language proposed by the Commissioner. FTCR submitted comments in response to the Commissioner’s Request for Public Input on September 21, 2001 (RPI). Subsequently, by letter to the CDI dated November 5, 2001, FTCR responded to insurers’ comments on the RPI’s proposed language.

C. Overview of FTCR’s Testimony

FTCR’s testimony today will focus on the following two points:

- 1) The Commissioner should use this proceeding, RH-402, as initially requested by FTCR, to adopt a regulation within the context of the rating factor regulations which clarifies that the use by insurers of the absence of prior insurance, alone or in combination with any other rating factor, violates Insurance Code § 1861.02 (c).
- 2) The Commissioner must adopt a consistent definition of persistency, as currently listed but undefined in Cal. Code Regs., tit. 10, § 2632.5(d)(11) (“§2632.5(d)(11)”), which has a substantial relationship to risk of loss as required by Ins. Code § 1861.02(a)(4) (“§ 1861.02(a)(4)”) and which does not violate § 1861.02(c) by unfairly discriminating against drivers who were previously uninsured. FTCR believes that the Commissioner’s proposed

language has substantially met these dual goals by defining persistency in the traditional sense as years with the company issuing the policy, although some fine-tuning of the language may be required.

II. ARGUMENT

A. The Scope of this Proceeding Should Include the Commissioner's Adoption of a Regulation to Prohibit the Use of the Presence of Absence of Prior Insurance in Automobile Insurance Premium Determinations.

While FTCR's request for a rulemaking proceeding was triggered by certain insurers' use of persistency discounts to evade the mandates of § 1861.02(c), which prohibits the use of prior insurance as a rating factor, the primary objective sought by FTCR in initiating this proceeding was and remains to ensure, as § 1861.02(c) requires, that uninsured motorists are not prevented from entering the insurance marketplace due to prohibitively high premiums. Section 1861.02(c) provides:

the absence of prior automobile insurance coverage, in and of itself, shall not be a criterion for determining eligibility for a Good Driver Discount policy, or generally for automobile rates, premiums or insurability.

(Cal. Ins. Code § 1861.02(c).)

Any "discount" or "surcharge" applied in the determination of automobile insurance rates that results in higher rates for consumers solely because of their no prior insurance status, therefore, necessarily violates § 1861.02(c). The statute acts to prevent two consumers – otherwise identical – from being charged different rates solely because one had prior insurance and one did not. The public policy behind § 1861.02(c) is that consumers trying to enter the insurance market should not be penalized for being previously uninsured, regardless of actuarial studies. The policy is one that facilitates consumers purchasing insurance and recognizes that consumers may have not had prior

insurance for a number of reasons unrelated to risk, such as redlining by insurance companies.

As set forth in FTCR's initial May 4, 2001 request for rulemaking to Commissioner Low on this issue, insurers have used various labels to charge previously uninsured motorists higher premiums in violation of the law—from proof of compliance with the state's financial responsibility law, to verification of driving safety, to "persistence." In its letter dated May 19, 2001 to the Commissioner submitting further information in support of its rulemaking request, FTCR again framed its request to encompass *any* illegal use of prior insurance as a rating factor when it urged the Commissioner "to address the issues of how insurance companies are evading the mandates of §1861.02(c) through their use of persistence and *other so-called surcharges and discounts.*" FTCR and Intervenors, Consumers Union and Southern Christian Leadership Conference, by their motion to adopt emergency regulations, then proposed language that is intended to ensure that no approved optional rating factors or other proposed factors may be used by insurers in any way to avoid compliance with §1861.02(c) as follows:

No insurer may use the absence of prior automobile insurance coverage (including but not limited to the absence of evidence of prior automobile insurance coverage and the absence of verification of any underwriting or rating characteristic by a prior insurance carrier) to determine or vary any rate or premium by surcharge, discount, or otherwise; nor to determine eligibility for coverage with the insurer or to shift eligibility from a standard to a substandard insurer, nor generally for the insurer's automobile rates, premiums, underwriting criteria, or determination of insurability. This prohibition applies to such use alone and to such use in conjunction with any other rating factor.

(Petition To Adopt Emergency Regulations Pending Determination of Rulemaking Hearing, File No. RH-402, July 18, 2001, p. 4.)

The intent of this proposed regulatory language is to enforce the statutory mandate of §1861.02(c), in the context of determining automobile insurance premiums by preventing insurers from using any approved (or non-approved) optional rating factor as a surrogate for the absence of prior insurance. Given the documented history of insurers finding new ways to discriminate against the previously uninsured, this general prohibition is necessary to prevent the use of prior insurance, no matter how it may be cloaked in an insurer's rating plan, and to ensure that automobile insurance is made affordable to the almost 25% of California motorists who remain uninsured and the over 20 million insured motorists negatively impacted by the inability of uninsured motorists to obtain affordable coverage.

The Commissioner's Request for Public Input in this proceeding, issued on September 6, 2001, sought and obtained comments from interested parties on FTCR's proposed language, giving proper public notice of the scope of the proposed regulations. Accordingly, this language should have been included in the final public notice of this hearing in order to give the opportunity for further oral testimony to be presented. FTCR believes that the Commissioner should therefore use the present proceeding, perhaps by noticing another public hearing, to address the broader issue of the discriminatory use of no prior insurance as originally encompassed in its rulemaking request. The remainder of FTCR's testimony today, nevertheless, will address the Commissioner's proposed language aimed at defining the optional "persistence" rating factor.

B. The Optional Automobile Insurance Rating Factor of “Persistence” Must Be Defined in a Consistent Manner That Does Not Unfairly Discriminate Against Drivers Who Were Previously Uninsured.

To illustrate the blatant illegal surcharging of previously uninsured motorists, FTCR cited, in its rulemaking request, to the example of the misuse of the “persistence” optional rating factor. In reviewing the rating rules of several insurers, it became clear to FTCR that there is no consistent definition of persistence. As a result, insurers seized upon that undefined rating factor as a justification for using the absence of prior insurance in premium determinations. For example, one insurer has a “persistence” rating rule that says if you can show you had prior insurance with any one company for three years, you receive a discount. Clearly this insurer merely replaced the absence of prior insurance with the label of “persistence” and claimed that it was legal under § 2632.5(d)(11)—the undefined persistence rating factor. Whatever “persistence” means, however, it must be demonstrated to have a “substantial relationship to risk of loss” as required by § 1861.02(a)(4), and it cannot be allowed to trump the specific statutory mandate of Prop 103 prohibiting the use of the absence of prior insurance in premium determinations contained in § 1861.02(c).

The Commissioner should note that at least three of the insurers submitting comments in response to his RPI—State Farm, CSAA Inter-Insurance Bureau, and Automobile Club of Southern California—agreed that persistence needs to be defined in a consistent manner and proposed definitions based on length of time with the carrier issuing the policy. CSAA, for example, commented that it currently applies persistence “based only upon the length of time a person has previously been insured with the Bureau or one of its affiliates” and that “if that is the maximum extent to which persistence is

permitted by the language of Proposition 103, *all insurers should be held to that standard.*” AAA and State Farm should also agree with the Commissioner’s latest proposed definition, as he has now incorporated their recommendation made in response to the RPI that new policies (and not just renewals) written for existing policyholders be allowed to receive a persistency discount.

While some insurers agree that persistency should be defined as in the Commissioner’s proposal—length of time with the company issuing the policy—other insurers insist that actuarial evidence supports the use of persistency defined as maintaining insurance with any company over a period of time. Yet, just how and when (if at all) that justification has been demonstrated is open to question. PIFC claimed in its written comments submitted in response to the Commissioner’s RPI that the actuarial relationship has been “demonstrated by insurers in their rate filings with the Department.” Mercury Insurance claimed that the Insurance Commissioner has “necessarily determined that persistency of coverage, as presently listed in § 2632.5(d)(11), is a rating factor with ‘a substantial relationship to risk of loss.’” Presumably, most insurers follow the logic of Mercury and do not provide any actuarial justification for their persistency discounts with their rating plans because, they reason, “persistency” is an approved rating factor. But what kind of “persistency” has been approved? It is this ever-expanding, “anything goes” approach by insurers to applying a “persistency” rating factor that led to the initiation of this rulemaking proceeding in the first place.

FTCR believes that the Commissioner’s proposed rule places appropriate parameters on the persistency rating factor; under the Commissioner’s proposed language

providing that “no insurer shall base persistency upon the length of time an insured has been previously insured by a non-affiliated insurer,” new applicants who have not been previously insured should be treated like all other similar drivers coming to that particular insurer for the first time.

There may be a need however, to add further clarification to the rule. For example, under the proposed rule, we know *who* will be eligible for a “persistency credit,” but exactly *what is* a “persistency credit”? Is it a discount based on having maintained coverage with that particular company for a set length of time? Or could insurers still circumvent the prohibition of §1861.02(c) and say that upon an insured’s policy renewal, they will offer a “persistency credit” to anyone who maintained insurance with any company prior to first applying with that particular company? FTCR believes that such a loophole would be foreclosed under the language proposed by the Commissioner which states: “Nor shall any insurer apply persistency, *at any time, when based in whole or in part upon automobile insurance coverage provided by a non-affiliated insurer.*” (emphasis added.) However, insurers must still justify that any variant of a “persistency credit” they apply, within the parameters of the Commissioner’s proposed regulation, has a substantial relationship to risk of loss.

In this regard, the Commissioner should make available to FTCR and the public any data used in its approval process of any persistency factors proposed in insurers’ class plans. If the Commissioner does not already have such data available to it showing the relationship to risk of loss of a “persistency” rating factor, then it should issue a data call to obtain that information from insurers and make it available to FTCR and the public.

With these caveats, FTCR would approve the Commissioner's language defining persistency as it has traditionally been defined in the industry as the length of time the current named insured has been insured by the insurer renewing an existing automobile insurance policy.

III. CONCLUSION

In closing, FTCR again wishes to thank Commissioner Low for opening this rulemaking proceeding. We are pleased with his effort to place clear parameters in regulation to define the optional "persistency" rating factor in a way which will not be unfairly discriminatory to previously uninsured motorists. As set forth above, however, the Commissioner's specific language defining persistency should be considered not as a substitute for, but in addition to, the language proposed by FTCR and Intervenors, Consumers Union and Southern Christian Leadership Conference prohibiting rating factors that use the presence or absence of prior insurance in violation of §1861.02(c). It is only by the adoption of this general prohibition in the rating regulations, implementing the statutory mandate of Prop 103, that the abuses we have historically seen by insurers who continue to seek out new ways to discourage the sale of their policies to the previously uninsured will be stopped.

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Respectfully Submitted,

**THE FOUNDATION FOR TAXPAYER
AND CONSUMER RIGHTS**

BY: _____
Pamela Pressley