



Consumer Federation of America

June 12, 2015

Dear Commissioner:

Your colleague, Mike Kreidler, has a problem. He is looking for price optimization in insurer rate filings in Washington, because he sees it as “a loyalty penalty.” But his office is having difficulty determining which filings include price optimization, viz.:

“Kreidler said he suspects personal lines insurers in his state are using price optimization techniques, but department actuaries are having difficulty in pinning down how to identify price optimization use in filings. Kreidler said he is stopping short of issuing a bulletin prohibiting its use partly because of the difficulties in determining how price optimization is being used in the massive filing documents. ‘It’s tough to be able to identify where it’s taking place,’ he said.”¹

In all likelihood, your staff faces the same conundrum. How do you block the use of techniques that you can’t see and can’t test? Our discussions with several insurance departments confirm that the department rate analysts and actuaries are finding it difficult, if not impossible, to determine which filings incorporate price optimization and which do not.

We know that price optimization is in wide use. Earnix research shows that, in 2013 “Of the companies with over \$1B GWP, 45% currently optimize their prices and additional 29% are planning to optimize in the near future.”² Certainly, the use of price optimization has increased since then. Yet it remains hidden behind the curtain like the Wizard of Oz, impacting pricing in undisclosed ways. If insurers were so confident about the propriety of price optimization, one would imagine they would be more forthcoming about its presence in their filings.

CFA actuarial review of auto insurance filings in several states concludes that some filings are likely using price optimization and some are likely not, but we cannot, with 100 percent certainty, be sure of any filings (except for the Allstate Complementary Rating Group filings made in over 30 states about which we have previously written). We would be happy to share a review of our research

¹ “Washington Commissioner Probing to Find Price Optimization in Filings,” Best’s Insurance News & Analysis, June 3, 2015

² “2013 North American Auto Insurance Pricing Benchmark Survey,” Earnix, 2013

concerning the search for price optimization with any interested regulator who would like to discuss it.

As with Commissioner Kreidler, we believe that you, too, have a problem with Price Optimization that needs to be addressed directly. As we see it there are two reasonable options you have:

1. Ban the practice as several states have already done; or
2. Accept no filings that do not clearly disclose whether price optimization is being used or not. We suggest that such a certification be required under penalty of perjury. For those filings where the certification indicates use of price optimization, there should be a requirement of full disclosure of how price optimization was used in underwriting, rating or other processes; information sufficient to assess whether the technique leads to unfair discrimination and to determine exactly the impact of its use (e.g., which factors were impacted by price optimization and by how much); and a calculation of the range of the cumulative impact of its use on individual policyholders.

To repair existing filings that may have used price optimization but are already in effect in your state, you should also require insurers to refile any such filings with the same certification and disclosure.

Please contact us if you have any questions or if you would like to discuss the findings from our own investigations into the use of price optimization in rate filings.

Sincerely,



J. Robert Hunter
Director of Insurance