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CONSUMER GROUPS APPLAUD MARYLAND INSURANCE COMMISSIONER GOLDSMITH FOR STOPPING UNFAIR DISCRIMINATION AND GOUGING IN INSURANCE PRICING

Commissioner Declares "Price Optimization" Contrary to Statutory Requirements That Insurance Rates Reflect Actual Cost Differences

Washington, D.C. – Maryland Insurance Commissioner Therese Goldsmith, in a bulletin issued last Friday, ordered all insurers that use "price optimization" techniques in Maryland to file a plan for ending this pricing strategy.

Over the past several years there has been a growing trend in the insurance industry to use personal consumer data and statistical models to measure how likely each customer is to shop around and how much of a price increase he or she will tolerate. After determining what economists call the "price elasticity of demand," insurers push up premiums based on how unlikely it is that a customer will shop around for a better price, even if the policyholder has never caused an accident, been issued a ticket or filed a claim.

In a series of letters to state insurance commissioners and in presentations to the National Association of Insurance Commissioners, Consumer Federation of America and the Center for Economic Justice have called for pro-active and pre-emptive efforts by insurance departments to block the use of price optimization, which the groups consider an illegal rating practice. Maryland is the first state to issue a formal bulletin prohibiting price optimization, though other state agencies and commissioners have indicated that the pricing technique would be deemed unfair discrimination in their state.

"Most Americans are required by law to buy auto insurance and by their mortgage company to buy homeowners insurance, and it is terribly unfair and entirely illegal for insurance companies to vary premiums based on whether or not they are statistically like to shop around," said J. Robert Hunter, Director of Insurance for Consumer Federation of America and former Texas Insurance Commissioner. "It is the obligation of Insurance Commissioners to protect consumers from this kind of price gouging, and we applaud Commissioner Goldsmith for her action."

The bulletin issued by the Maryland Insurance Administration notes that one price optimizing factor insurers use is whether or not a customer has complained about their insurance in the past. "This means," the bulletin explains, "that policyholders would be charged higher premiums simply because they have not complained to the insurer, regardless of whether these policyholders pose any more risk of loss than policyholders who have complained." The bulletin is available at http://bit.ly/1uqGcXY.

The bulletin also quoted one firm that sells insurance price optimization tools as saying that if "insurers adopt advanced pricing strategies that consider customer elasticity differences, they can boost their revenue by roughly 3 percent and returns-on-equity by 1 percent, on average."

According to the consumer groups, price optimization marks a radical departure from the actuarial practice of pricing insurance premiums according to the risk of loss posed by the policyholder. The purpose of price optimization is to extract as much profit as possible from policyholders who are often required to purchase insurance policies. CFA and CEJ are calling on all state insurance departments to follow Maryland's lead and ban the use of price optimization in the insurance market.

It is not clear exactly how many insurers currently use price optimization or similar non-actuarial pricing strategies in the United States. One company that provides price optimization tools, Earnix, has claimed that approximately half of the nation's large property-casualty insurers use price optimization for auto insurance and over one-quarter of large insurers use it for homeowners insurance.

"Commissioner Goldsmith's action is a needed counterbalance to the penalties imposed on drivers unable to afford auto insurance. By requiring that auto insurance rates be based on insurance-related costs, the Commissioner's action ends a discriminatory practice and will help make insurance more affordable," said Birny Birnbaum, Director of the Center for Economic Justice.

The Consumer Federation of America (CFA) is an association of non-profit consumer organizations that was established in 1968 to advance the consumer interest through research, advocacy, and education. Today, more than 250 of these groups participate in the federation and govern it through their representatives on the organization's Board of Directors.

CEJ is a non-profit organization that works to increase the availability, affordability and accessibility of insurance, credit, utilities, and other economic goods and services for low-income and minority consumers.