What Works:

A Review of Auto Insurance Rate Regulation in America and How Best Practices Save Billions of Dollars

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Executive Summary

Over the past quarter century, auto insurance expenditures in America have risen by more than 40 percent. Consumers in some states are paying 80 percent, 90 percent, and even 100 percent more for auto insurance than they paid in 1989. These increases have accrued despite substantial gains in automobile safety and the arrival of several new players in the insurance markets. Only in California, where a 1988 ballot initiative transformed oversight of the industry and curtailed some of its most anti-consumer practices, has the amount that drivers spend on auto insurance declined.

This report follows prior reports in 2008 and 2001; it is part of Consumer Federation of America's ongoing effort to evaluate the various types of insurance regulatory regimes found across the country and identify best practices from a consumer protection perspective. The data sets we have reviewed allow us to conduct a rigorous comparative analysis of both state markets and regulatory systems.

The data provides several important findings about the insurance marketplaces in each state and the efficacy of different approaches to insurance regulation. We found,

On insurance prices:

1. The average expenditure on auto insurance since 1989 has increased by 43.3 percent;
2. The states with the highest increases are Nebraska, Louisiana, Montana, Wyoming and Kentucky;
3. The states with the lowest increases are Hawaii, New Hampshire, New Jersey, Massachusetts, and Pennsylvania; and
4. Only California has seen average expenditures decrease since 1989.

On regulatory systems:

1. The prior approval system of regulation, in which insurers must apply for rate changes before they can be imposed in the market, is most effective at keeping rates low;
2. Markets that are less or not regulated tend to have the most substantial increases;
3. While mildly and strongly regulated states tend to have very or somewhat competitive markets for auto insurance, deregulated and flexible rating states have the least competitive markets; and
4. Insurance companies are generally able to adapt to any regulatory system and consistently maintain reasonable profitability.

On California's unique success:

1. Over $100 billion in savings for motorists as a result of lower auto insurance rates driven by the strong regulatory oversight and more competitive market fostered by the 1988 insurance reform measure known as Proposition 103;
2. Between 1989 and 2002, insurance companies operating in California issued over $1.43 billion in premium refunds to more than seven million policyholders under Proposition 103's rollback mandate;
3. State rules prohibit many of the discriminatory elements that plague low-income and minority consumers in other states, especially prohibitions on use of credit scoring and prior insurance coverage as rating factors;
4. State rules temper the impact on consumers of other non-driving related classifications, such as territory and occupation by requiring that the most weight in the pricing for a consumer be given to driving record;
5. The intervenor system, allowing systemically-funded public challenges to rate hikes, improves both industry and government accountability; and
6. The state has innovated in the marketplace with the implementation of an unsubsidized alternative policy for low-income consumers.

The research conducted for this paper, building on prior research, clearly indicates that consumers across the country would be better served with a more robust, prior-approval system of auto insurance regulation than the system currently in place in most states. Policymakers and regulators should consider these findings as they look for ways to better protect consumers from marketplace abuses and from unnecessary increases in insurance premiums.

If every state in the nation were to implement and enforce a regulatory agenda as demonstrably pro-consumer as that in California, the research indicates that Americans could save over $350 billion over the next decade, even as insurance companies realize reasonable profitability. In order to achieve the most effective form of a prior approval system, states should construct an intervenor system that provides resources for citizen and organizational watchdogs who can serve as both a resource for and check on state Departments of Insurance and who will help hold insurance rates down to appropriate levels. Further, states should proscribe the egregious non-driving related premium factors that lead to higher premiums for low- and moderate-income drivers.