

AN ALTERNATIVE RECOMMENDATION
FOR A PILOT PROJECT TESTING PRICING FREEDOM

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Recently it was announced by the Council of Insurance Agents and Brokers¹ that an electronic insurance exchange has been developed to streamline the underwriting process. The insurance exchange allows an insurance producer to complete a single application for a variety of insurance products and to submit that single application to multiple insurers. The insurers respond with a quote if they are interested in the risk. The insurance producer informs the applicant of the quotes received and advises the applicant with regard to price, coverage limits, comparisons of contract provisions, claims payment history and other quality measures such as providing information regarding the financial standing of the insurer. Once the applicant selects the insurer, the producer uses the insurance exchange to inform the insurer and the insurer issues the policy to the applicant.

This process offers an opportunity for the insurance industry and regulators to address several market failures for personal lines insurance products. Applicants tend not to search the marketplace because of lack of transparency and the time consuming process that must be endured if one is to seek multiple quotes. Thus, from an economic perspective the market failure is lack of price and eligibility transparency. In today's marketplace, each insurer has its own application form that an individual or the insurance producer must complete. A person generally is only willing to complete one or a small number of application forms to receive quotes from insurers. Sometimes employees of the insurance producer complete multiple insurer forms on behalf of the applicant. Going beyond that is very tedious and time-consuming. This process limits the individual's access to potentially willing insurers. Insurer proprietary systems require multiple data entry by insurance producers or the applicant. The ability to complete a single application form and receive multiple prices quotations would be considered a plus by consumers and insurance producers. The marginal cost for that part of the underwriting process should be reduced for those that use the system.

Insurers have long been advocates of pricing freedom. It would seem that the operation of an insurance exchange would offer the possibility of a win-win-win situation developing. In exchange for providing easy access to multiple quotations the insurers could be offered pricing freedom through a pilot project that is enabled by interested insurance regulators. It would benefit consumers by providing greater choice and transparency and ease of access to a system that today is overly complex and confusing. It would provide expense reductions, improved efficiency and greater access to markets for insurance producers.

¹ Arvidson, Cheryl, In Search of Brokers' Holy Grail, Leader's Edge Magazine, December 2006.

What is proposed is to have participating states use discretionary authority contained in current rating laws to enable a pilot project that does the following:

- Applies to personal auto insurance and homeowners insurance coverages (other products could be added);
- Authorizes insurers to ignore current filed rates and competitively bid on applicants seeking coverage through the electronic insurance exchange system;
- Allows an insurance producer selected by the applicant to assist the applicant with completion of a single application that is submitted through the system to all interested insurers;
- Requires insurers to disclose coverage terms and conditions to the applicant, through the insurance producer, along with the competitive bid detailing the cost for the coverages requested by the applicant;
- Provides insurance regulators with statistical information needed to evaluate whether the pricing freedom is providing applicants with sufficient information and broad selection among a variety of insurers and insurance products; and
- Leads to a formal evaluation of the success or failure of the pilot project by participating states.

Most insurance laws that provide for prior approval of rates and rating systems have a provision that is substantially similar to the following provision that is taken from the NAIC's Model Law #780:

“Under such rules and regulations as may be adopted, the commissioner may, by written order, suspend or modify the requirement of filing as to any kind of insurance, subdivision or combination thereof, or as to classes of risks, for which the rates cannot practicably be filed before they are used. The commissioner may make such examination as deemed advisable to ascertain whether any rates affected by such order meet the standards set forth in Section 4.”

It is envisioned that, for purposes of the pilot project, the insurance commissioner would issue an order granting pricing freedom to those insurers that notify the commissioner and make arrangements to participate in the pilot project. The order would specify the disclosures that would be required and the statistical information that would be collected from the participating insurers and the electronic insurance exchange. Each order would be consistent with the orders issued by other states participating in the pilot project. Interested state regulators would draft a uniform order that all interested states would agree to use. Before it is adopted, the model order would be distributed to all interested parties for comment.