

Commissioner Order CO-03-1142

Official Order of the Commissioner of Insurance of the State of Texas

Austin, Texas

Date: November 19, 2003

Subject Considered:

PRIVATE PASSENGER AND COMMERCIAL AUTOMOBILE INSURANCE

PROVIDED THROUGH THE TEXAS AUTOMOBILE INSURANCE PLAN ASSOCIATION

DOCKET NO. 2542

General Remarks and official action taken:

On this day came on for consideration by the Commissioner of Insurance (Commissioner) the matter of the 2002 rate filing by the Texas Automobile Insurance Plan Association (TAIPA) with the Texas Department of Insurance (TDI), as required by the TEX. INS. CODE ANN. Article 21.81 (c) for private passenger and commercial automobile insurance coverage. Notice of the TAIPA rate filing was provided to the Secretary of State for posting in the Texas Register on December 2, 2002, and the date for the hearing was published in the Texas Register on December 13, 2002. On January 9, 2003, a hearing was convened before the Commissioner in Room 100 of the Hobby Building to consider the TAIPA's rate filing, allowing all interested persons to present written and oral comments relating to TAIPA's rate filing. TAIPA was present and represented by Mr. Richard S. Geiger and Mr. Michael W. Jones of Thompson, Coe, Cousins & Irons, L.L.P. and Office of Public Insurance Counsel (OPIC) was present and represented by Mr. Rod Bordelon and Ms. Erin Martens.

After considering the TAIPA's rate filing, staff's analysis, and all written and oral comments presented, the Commissioner adopts the following findings of fact and conclusions of law.

Findings of Fact

Notice

1. The TAIPA rate filing was filed with TDI on December 2, 2002. In its rate filing, the TAIPA proposed an increase of 49.9 percent for the rates to be charged for private passenger automobile insurance provided through the TAIPA.
2. On January 2, 2003, OPIC filed with TDI its calculations of its rate recommendation for private passenger automobile insurance provided through the TAIPA. OPIC's calculation indicated an increase of 7.7 percent.
3. The Commissioner shall determine and prescribe TAIPA rates that are just, reasonable, adequate, not excessive, not confiscatory, and not unfairly discriminatory for the risks to which they apply.
4. TAIPA rates shall be set in an amount sufficient to carry all claims to maturity and to meet the expenses incurred in the writing and servicing of the business.
5. The Commissioner can approve, disapprove or modify a filing made by TAIPA.
6. The TDI issued the notice of public hearing on December 13, 2002.
7. The notice of public hearing included statements of the time, place, and nature of the hearing; the legal authority and jurisdiction under which the hearing would be held; a statement of the matter to be addressed; and references to the particular statutes and rules involved.
8. A hearing was held on January 9, 2003 before the Commissioner to receive oral and written comments concerning the filing made by TAIPA.
9. Organizations providing testimony in the proceeding were TAIPA, represented by Richard S. Geiger and Michael W. Jones, attorneys; and the Office of Public Insurance Counsel (OPIC), represented by Erin C. Martens, Staff Attorney.

Actuarial Methodology

10. A loss ratio methodology is a reasonable methodology to fulfill the objectives set forth in Finding Nos. 3 and 4.
11. The loss ratio method of setting rates considers reports of aggregated premiums earned and losses and expenses incurred in the writing of insurance through TAIPA.
12. Both TAIPA and OPIC used calendar-year premium data and accident-year loss data for each of three years ending December 31, 1999, 2000, and 2001 to calculate rates.
13. 2002 calendar-year premium data and accident-year loss data became available in September of 2003.
14. It is reasonable to use the most current data available when calculating rate indications.
15. It is reasonable to use a three year loss ratio to calculate rate indications utilizing calendar-year premium data and accident-year loss data for each of three years ending December 31, 2000, 2001, and 2002.

Premiums at Current Rate Levels

16. It is reasonable to use the distribution of TAIPA premiums by driver class and territory as recommended by TAIPA in the calculation of premiums at current rate levels.

17. It is reasonable to use TAIPA's on-level factors to calculate historical premiums at current rate levels.

Loss Development

18. Because claims are not necessarily settled in the year they occur, loss development analyses are necessary to estimate their final settlement cost.

19. The TAIPA selected loss development factors from the loss development patterns from prior TAIPA experience.

20. Using TAIPA experience to calculate the loss development factors is reasonable.

21. It is reasonable to use TAIPA's loss development factors.

Loss Trend Factors

22. Loss trending accounts for expected changes in the number of claims per unit of exposure, referred to as claims frequency, and the average cost of claims, referred to as claims severity.

23. Many of the economic, social, legal, and other forces that impact the TAIPA loss trend experience and the voluntary loss trend experience are similar.

24. TAIPA provided an analysis of claim frequency, claim cost and pure premium trends for TAIPA business. However, TAIPA based its trend selections on TAIPA annual aggregate loss ratio data due to concerns about the reliability of the Quarterly Detailed Experience (QDE) database used to calculate TAIPA trends.

25. OPIC based its trend selections on an analysis of both paid and incurred trend in TAIPA, as well as the combined voluntary and involuntary Texas market experience.

26. Due to the concerns raised by TAIPA concerning the TAIPA trend data, it is reasonable to consider multiple sources such as the voluntary data and loss ratio trend data.

27. TAIPA and OPIC relied on data thru 2001.

28. 2002 TAIPA trend data became available in September of 2003.

29. A review of the QDE data reports suggests that these can be reasonably reconciled with other TAIPA data such as the annual aggregate report.

30. The most recent available QDE data suggested some moderation in loss trends during 2002.

31. It is reasonable to utilize the most current data available.

32. Due to the small volume of Uninsured Motorist (UM) and Personal Injury Protection (PIP) experience, it is reasonable to rely more heavily on the trends in the voluntary data for these coverages while still considering TAIPA trend data.

33. Based on Finding Nos. 26, 31 and 32 it is reasonable to use the following trend selections:

Bodily Injury: retrospective -5.0%, prospective 0.0%

Property Damage: 3.0%

PIP: 3.0%

UM: 1.0%

Loss Adjustment Expenses

34. Loss adjustment expenses (LAE) are costs incurred by insurers in resolving claims, such as legal fees, court costs, fees for independent claim adjusters and experts, company claim adjuster salaries, appraisals, and related rent and utilities.

35. Defense and cost containment expenses (DCCE) represent costs that can be associated with a particular claim, while adjustment and other expenses (AOE) cannot usually be associated with a particular claim.

36. No adjustment is necessary for DCCE because DCCE are included with the losses reported by insurers under the statistical plan.

37. TAIPA's AOE factor indications are based on the experience for the years 1998, 1999, 2000, and 2001. The factor for each of the years 1999, 2000, and 2001 is the two year average of that year and the prior year's experience. For example, the factor for 1999 is the two year average of the 1998 and 1999 experience.

38. The definitions used to categorize LAE changed in 1999. 1998 experience is not strictly comparable to that of subsequent years.

39. OPIC based its AOE factors on the experience for each of the years 1999, 2000 and 2001.

40 AOE experience for 2002 is not yet available.

41. It is reasonable to base AOE factors on the average of the experience of 2000 and 2001.

Fixed and Variable Expenses

42. In the present case, variable expenses are commissions and taxes, licenses, and fees, and are directly variable with premiums.

43. For variable expenses, it is reasonable to use a 10 percent provision for TAIPA commissions, consistent with the actual commissions paid on TAIPA business, and a provision of 1.7 percent for taxes, licenses, and fees consistent with the statutory premium tax rate of 1.6 percent and the present maintenance tax rate of 0.053 percent.

44. Fixed expenses represent insurers' overhead expenses, and are also known as general and other acquisition expenses.

45. TAIPA uses an expense ratio analysis to determine general and other acquisition expenses.

46. The effective assumption in such an analysis is that these expenses will be a constant ratio of premiums, regardless of the amount of premium per policy.

47. OPIC calculated general and other acquisition expenses as a dollar amount per policy, using combined voluntary and TAIPA experience.

48. TAIPA, as an insurer of last resort, has generally higher rates than the voluntary market.

49. It is reasonable to calculate general and other acquisition expense as a dollar amount per policy.

50. OPIC based its calculations of expenses on the data for 1999-2001 for bodily injury liability (BI), property damage liability (PD), and PIP. It did not include UM.

51. In the voluntary market, both liability and physical damage coverage are normally written on the same policy.

52. It is reasonable to assume that the marginal costs of including physical damage coverage on a policy are not significant.

53. It is therefore reasonable to include some portion of voluntary fixed expenses allocated to physical damage by voluntary insurers even though TAIPA does not provide physical damage coverage.

54. It is reasonable to increase the provision for fixed expenses by an amount equivalent to 50 percent of the amount allocated by voluntary insurers to physical damage coverage in determining TAIPA rates.

55. Some insurance companies in the voluntary private passenger automobile insurance market utilize their own employees to write and service their business. Such costs are normally characterized as other acquisition expense.

56. It is reasonable to assume that agents writing TAIPA business perform some of the services normally carried out by insurance company employees in the voluntary market.

57. To the extent that insurers utilize their employees to perform some of the services, other acquisition expense tends to be overstated as compared to expense needs in servicing involuntary business.

58. It is reasonable to reduce fixed expenses by 0.5 percentage points as recommended by OPIC to account for the difference in services performed by agents writing TAIPA business as compared to services performed by insurance company employees in the voluntary private passenger automobile insurance market.

59. General expense data reported by insurers contains some expenses that are disallowed expenses under Texas law.

60. TAIPA reduced fixed expenses by 0.4 percentage points to account for the disallowed expenses included in general expenses.

61. TAIPA's adjustment for disallowed expenses of 0.4 percentage points is reasonable and should be used.

62. Other acquisition expense reported by insurers includes advertising expenses.

63. Advertising expenses are not relevant to TAIPA business.

64. The TAIPA made an adjustment of 0.7 percentage points to account for the advertising expenses that are not relevant to TAIPA business.

65. TAIPA's adjustment for advertising expenses of 0.7 percentage points is reasonable and should be used.

66. TAIPA used an expense trend based on an average of the Fitted Consumer Price Index (CPI) trend and the average weekly wage of fire & casualty employees (AWW) trend. This resulted in a trend selection of 2.4 percent.

67. OPIC utilized an expense trend of 1.6 percent. This is based on an average of the CPI trend and a weekly wage trend reflecting the trend in the number of employees in Fire, Marine and Casualty Insurance.

68. Adjusting TAIPA's expense trend selection by adjusting the AWW trend for the trend in the number of employees in Fire, Marine and Casualty

Insurance results in an average trend of 2.0 percent.

69. Adjusting TAIPA's expense trend selection by adjusting the AWW trend for the trend in the number of employees in Fire, Marine and Casualty Insurance is reasonable and the resultant expense trend should be used.

70. OPIC adjusted the fixed expense ratio by a factor of 0.5 to account for the policy length difference between the voluntary market which typically sells six month policies and the TAIPA market which has annual policies.

71. While there may be some savings arising from the issuance of annual as compared to six month policies, it is unclear from the record exactly what those savings might be.

72. It is not reasonable to make the adjustment proposed by OPIC.

73. It is reasonable to make an adjustment of three dollars to account for the policy length difference.

74. In the voluntary market, an average 94.2 percent of the premium originally written is earned compared to TAIPA, where 84.3 percent of the premium originally written is earned.

75. It is reasonable to adjust the TAIPA expense ratio upward by a factor of 1.117 based upon the ratio of premiums earned in the voluntary market as compared to premiums earned in the TAIPA market.

Installment Fees

76. Installment fees paid by TAIPA insureds are a source of revenue that is not included as part of premium income.

77. It is reasonable to account for installment fees as a deduction from fixed expenses.

78. OPIC's estimate of installment fee income is based on the following assumptions:

- a. An average of 1.1 cars per policy;
- b. An average installment fee revenue per policy of \$28.00;
- c. 90 percent of TAIPA policies are purchased on an installment basis; and
- d. The average premium per policy is \$567.00.

79. Based on Finding No. 78, the average installment fee revenue as a percentage of premium is 4.4 percent.

80. TAIPA did not provide an estimate for installment fee income.

81. OPIC's installment fee income assumption is reasonable and should be used.

Underwriting Profit

82. The TAIPA used an underwriting profit provision of 0.0 percent.

83. OPIC recommended an underwriting profit provision of -4.2 percent.

84. An underwriting profit provision of -1.0 percent is reasonable and should be used.

Commercial Automobile Insurance Rates

85. TAIPA recommended that rates for commercial automobile insurance written through TAIPA be adjusted at the same time and in the same amounts as the voluntary market rates. No specific percentage change was recommended.

86. No adjustments have been made to the voluntary commercial automobile insurance benchmark rates as the benchmark statute no longer applies to commercial automobile insurance.

87. It is reasonable to keep the existing TAIPA commercial automobile rates without modification at this time.

Conclusions of Law

1. The Commissioner has jurisdiction over this matter pursuant to Tex. Ins. Code Ann . art. 21.81, § 5.

2. Proper and timely notice of the hearing was given pursuant to Tex. Ins. Code Ann . art. 21.81, § 5, 28 Tex. Admin. Code § 1.1304 and Tex. Gov't Code Ann . §§ 2001.051 and 2001.052.

3. The setting of rates in accordance with these findings of fact and conclusions of law is in compliance with the provisions of Tex. Ins. Code Ann . art. 21.81, § 5(a). This section provides that the Commissioner shall determine and prescribe TAIPA rates that are just, reasonable, adequate, not excessive, not confiscatory, and not unfairly discriminatory for the risks to which they apply. This section also provides that TAIPA rates shall be set in an amount sufficient to carry all claims to maturity and to meet the expenses incurred in the writing and servicing of the business.

IT IS THEREFORE THE ORDER of the Commissioner that the above findings of fact and conclusions of law are adopted.

IT IS FURTHER ORDERED that the rate filing for private passenger automobile rates to be written through TAIPA be modified consistent with the findings and conclusions set forth in this order.

IT IS FURTHER ORDERED that the rates for TAIPA for private passenger automobile be increased by 29.1% for bodily injury liability, 24.1% for property damage liability, 86.2% for personal injury protection, and 29.1% for uninsured/underinsured motorist coverage.

IT IS FURTHER ORDERED that the existing rates for commercial automobile continue unchanged.

IT IS FURTHER ORDERED that the TAIPA's rates as modified in this order become effective February 1, 2004 .

For more information, contact: ChiefClerk@tdi.texas.gov

Last updated: 09/06/2014