# INSURANCE RATES REGULATION IN COMPARISON WITH OPEN COMPETITION

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*This article examines rate regulation in the property and casualty insurance market in the United States. While rate regulation serves, in particular, the purpose of promoting insurer solvency and preventing oligopolistic pricing, it can also lead to market inefficiencies. The article argues for rate deregulation as a superior alternative to the current regulation model.*

*During the nineteenth century the property and casualty insurance market was highly competitive, featuring periods of low losses and large profits that attracted new market entrants. This competition caused insurance companies to set rates that were inadequate, thus leading to thousands of insolvencies. One method to solve the problem was the compact, an agreement among insurers to have a manager set rates. This solution often failed because members of the compact often cheated and there was no way to make every insurer in the market join. By the end of the nineteenth century several states had passed anti-compact law prohibiting the practice.*

*States in the early twentieth century started passing rate regulation laws in the fire insurance market. These laws subjected rate setting to state control. These laws were prevalent in the fire insurance market by the 1940's, but were not widespread in the casualty insurance market. With the passage of the McCarran-Ferguson Act in 1945, insurance regulation was made the primary purview of the several states, with federal intervention allowable only where states failed to legislate. Soon after, the AIC and NAIC crafted model laws that became the basis for much state legislation. While state laws started out with an emphasis on cooperative rate setting by rate bureaus, gradually the laws were changed to facilitate independent rate filing by insurers directly to state insurance regulators, thus increasing rate competition. Today, the trend is toward less restrictive systems of rate regulation in most property lines: gradually away from "prior approval" towards "file and use," "use and file," "flex rating," "modified prior approval," or no file systems.*

*The rationales for rate regulation include consumer protection, the prevention of insurer insolvency and unfair pricing, and the promotion of actuarial accuracy. The rationales against rate regulation are mainly that cartel pricing and destructive competition are not a threat today, that the market is the appropriate price setting mechanism in insurance markets, deregulation promotes competition, and that rate deregulation would take the politics out of rate setting.*

*Examining the structure of the American property and casualty insurance market is necessary to determine how successful a policy of deregulation will be. The U.S. property and casualty insurance market*

*presents the structural features of a competitive market because it is characterized by a large number of firms selling products with identical features. Evaluation of the Herfindahl-Hirschman Index for industry concentration in conjunction with the Department of Justice's Merger Guidelines indicates that the property and casualty insurance market is not concentrated. Furthermore, the trend toward an increase in the level of market concentration is oftentimes the result of market competition since it leads to low-cost, efficient firms replacing high-cost firms. The property and casualty insurance market is also widely regarded as having low barriers to entry for new firms. Thus the market does not have monopolistic or oligopolistic characteristics that would justify rate regulation. Nevertheless, purely competitive rate setting systems are seldom used throughout the United States.*

*The European Union can provide a helpful case study in considering rate setting deregulation because EU member states do not have the right to regulate insurance prices, after the European Parliament passed the third non-life insurance Directive in 1992. Previously, EU member states exercised considerable rate setting power. The experience has been a positive one. Competition increased, especially in heavily regulated markets, and premium rates decreased. Market concentration, however, did not decrease, though this could be attributed to an increase in mergers and acquisitions. The number of insolvencies decreased as prices were better aligned with costs.*

*Rate regulation in the United States may be adversely impacting insurer profitably, as rate changes are impeded as market conditions change. There is empirical evidence that property and casualty insurance companies have experienced a lower rate of return than other industries. These artificially low returns may have led to many insurers' exits from the market. In particular, with regard to some lines, over the 2000-2009 period, more insurers exited the market than entered it. Deregulation would eliminate compliance costs and allow rate changes. Even if rate deregulation lead to higher rates, in the long run this would be offset by greater market availability and consumer choice. Rate regulation has the tendency to force stricter underwriting that limits market availability. Additionally, there is no evidence that rate regulation has eliminated the possibility of insurer insolvency. It is more likely that allowing insurance companies to set rates commensurate with their costs will enhance their financial strength. Therefore policy makers should seriously consider greater insurance rate deregulation.*

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## INTRODUCTION

The traditional justification for economic regulation is to protect the public interest by correcting market failures and improving economic efficiency and equity.[1] In particular, with regard to insurance, regulation aims to protect policyholders by ensuring the solvency of the insurance companies. In light of the peculiar nature of an insurance contract, in which the policyholder pays an upfront premium in exchange for the insurer's promise to pay in case a loss occurs, the need is clear to assure the financial solidity of the insurance companies and their ability to pay possible future claims.

In this context, by the first half of the twentieth century individual states within the United States enacted rate regulatory laws to ensure that rates were "adequate, not excessive and not unfairly discriminatory." One objective of rate regulation is to prevent insolvencies by avoiding a sort of ruinous competition in which insurers, in order to strengthen their market position, charge rates not sufficient to cover their costs. Another is to avoid oligopolistic pricing.

This study will focus on the regulation of rates in the U.S. property and casualty insurance market, highlighting the inefficiencies caused by the system. The aim of the paper is to examine the advisability of replacing rate regulation with rate deregulation. In this regard, although some states have rating methods less restrictive than prior approval, like file and use, use and file, flex rating and modified prior approval, it must be emphasized that none of these methods fully rely on competition since the insurance commissioner basically still retains the right to direct the insurers' setting of rates. The analysis supports the conclusion that rate deregulation should be introduced.

Part I will provide the historical background of rate regulation, discussing the developments from the nineteenth century, when rate regulation was introduced in order to prevent insurers' insolvencies, to the more recent trend toward less restrictive rating laws.

Part II will set out the purposes of rate regulation to ensure, as stated above, that insurance rates are "adequate, not excessive and not

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[1] STEPHEN BREYER, REGULATION AND ITS REFORM 15-16 (1982); SCOTT E. HARRINGTON, INSURANCE DEREGULATION AND THE PUBLIC INTEREST 15 (2000); 2 ALFRED E. KAHN, THE ECONOMICS OF REGULATION, INSTITUTIONAL ISSUES 11 (1988).

unfairly discriminatory." Further, the arguments adduced for and against rate regulation will be presented.

Part III will make the case for rate deregulation. In particular, the analysis will consider the U.S. property and casualty insurance market structure, the performance of the industry, market growth, market entries and exits and the effects of rate regulation on insurance availability. The analysis also considers the experience of the European Union, where state supervisory authorities have been prevented from exerting control over insurance premiums prices.

## I. HISTORICAL DEVELOPMENT OF RATE REGULATION

### A. PRIVATE CONTROLS OVER INSURANCE RATES AND THE ENACTMENT OF ANTI-COMPACT LAWS

During the nineteenth century, the property and casualty insurance market was distinguished by a high level of competition. Indeed, since historically the fire insurance business was highly cyclical, in periods when losses were low and profits high new insurance companies entered the market aiming to make large profits.[2] Neither barriers to entry nor significant economies of scale hindered the entrance into the market.[3] The strong competition in the market in the 1800's led insurers to set inadequate rates and thus, by 1877, around 3000 companies had become insolvent.[4]

In response, in 1866 insurers instituted a national organization, the National Board of Fire Underwriters, in order to "establish and maintain, as far as practicable, a system of uniform rates of premium."[5] However, the fact that, in profitable periods, insurance companies violated the agreements concerning the rates established by the Board, made the Board

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[2] 1 JON S. HANSON ET AL., NATIONAL ASSOCIATION OF INSURANCE COMMISSIONERS, MONITORING COMPETITION: A MEANS OF REGULATING THE PROPERTY AND LIABILITY INSURANCE BUSINESS 9 (1974); Spencer L. Kimball & Ronald N. Boyce, *The Adequacy of State Insurance Rate Regulation: The McCarran-Ferguson Act in Historical Perspective*, 56 MICH. L. REV. 545, 547 (1958); Michael D. Rose, *State Regulation of Property and Casualty Insurance Rates*, 28 OHIO ST. L.J. 669, 677 (1967).

[3] Rose, *supra* note 2, at 677.

[4] HANSON ET AL., *supra* note 2, at 9; Kimball & Boyce, *supra* note 2, at 547-48; Rose, *supra* note 2, at 677.

[5] Rose, *supra* note 2, at 677 (quoting Kimball & Boyce, *supra* note 2, at 548).

ineffective in controlling rates.[6] Nevertheless, after the fire losses that occurred in Chicago and Boston respectively in 1871 and 1872, it appeared inevitable that insurance companies had to cooperate in order to set adequate rates.[7] In 1877, the National Board of Fire Underwriters abandoned its function of rate control – addressing itself only to fire prevention and the maintenance of statistics – and in the 1880s, regional associations of companies assumed the task of rate stabilization.[8] Among the techniques implemented by the regional associations in order to control rates was the compact, an agreement according to which the compact manager set the rates and usually enforced them in compliance with the compact's conditions.[9]

However, the problem any cartel faces is that each cartel member has incentives to raise its profits by cheating the cartel: bringing down the cartel's price and increasing its output.[10] In the same way, these regional associations did not effectively stabilize insurance rates.[11] Indeed, the insurer members of the association did not always honor the agreements made in good faith since they used to cut rates.[12] Further, the agreements were often undermined by insurers that were not members of the association.[13]

Toward the end of the 1800's, many states responded to the insurers' efforts to fix rates by passing anti-compact laws.[14] The first anti-compact laws were passed by Ohio and New Hampshire in 1885[15] and by 1912 twenty-three states had passed such type of legislation.[16]

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[6] HANSON ET AL., *supra* note 2, at 10-11; Kimball & Boyce, *supra* note 2, at 548; Rose, *supra* note 2, at 677.

[7] Kimball & Boyce, *supra* note 2, at 548.

[8] HANSON ET AL., *supra* note 2, at 11; Kimball & Boyce, *supra* note 2, at 549; Kent H, Parker, *Ratemaking in Fire Insurance*, *in* PROPERTY AND LIABILITY INSURANCE HANDBOOK 169, 170 (John D. Long & Davis W. Gregg eds., 1965); Rose, *supra* note 2, at 677-78.

[9] HANSON ET AL., *supra* note 2, at 11; Kimball & Boyce, *supra* note 2, at 549. The first compact was the St. Louis Compact, concluded in 1879.

[10] LEE S. FRIEDMAN, THE MICROECONOMICS OF PUBLIC POLICY ANALYSIS 668 (2002); DAVID A. BESANKO & RONALD R. BRAEUTIGAM, MICROECONOMICS 495 (2002); *see generally* D. K. Osborne, *Cartel Problems*, 66 AM. ECON. REV. 835-44 (1976).

[11] HANSON ET AL., *supra* note 2, at 12-13.

[12] *Id*. at 12.

[13] *Id*.

[14] Kimball & Boyce, *supra* note 2, at 549; Rose, *supra* note 2, at 678.

[15] HANSON ET AL., *supra* note 2, at 14.

[16] Kimball & Boyce, *supra* note 2, at 550.

Nevertheless, the anti-compact laws were often evaded. In cases where the law expressly prohibited agreements between insurance companies, like in Ohio and Wisconsin, insurers concluded that agreements between agents were not prohibited. So, the insurance companies relied on their agents to fix rates.[17] Elsewhere, where the law prohibited all agreements relating to the establishment of rates, insurance companies formed "independent" bureaus to make advisory rates.[18]

### B. BEGINNING OF RATE REGULATION

During the first half of the twentieth century, states became aware of the risks that ruinous competition posed to policyholders and began to enact legislation to regulate fire insurance rates.[19] The first rate regulatory law, passed in Kansas in 1909, required fire insurers to file their rates and their rating plans with the superintendent of insurance and prohibited rate discrimination among insureds.[20] It also required insurance companies to give the insurance commissioner ten days' notice in order to change rates and authorized the commissioner to adjust rates that were excessive or inadequate.[21] In 1914, the German Alliance Insurance Company challenged the Kansas law as unconstitutional.[22] The company argued that insurance is a private contract and that the state has no power to interfere by regulating insurance rates; otherwise, such regulation would be a deprivation of the insurer's property without due process of law, in violation of the Fourteenth Amendment to the Constitution.[23] The Supreme Court rejected the complaint, stating that insurance was affected with a public interest and, for this reason, the insurance premium could be fixed by law.[24]

After the San Francisco fire of 1909, the New York legislature conducted an investigation on fire insurance rating practices.[25] To this end a Joint Legislative Committee, known as the Merritt Committee, was

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[17] Rose, *supra* note 2, at 678.

[18] Rose, *supra* note 2, at 678; Richard A. Wiley, *Pups, Plants and Package Policies – or the Insurance Antitrust Exemption Re-Examined*, 6 VILL. L. REV. 281, 312-14 (1961).

[19] Kimball & Boyce, *supra* note 2, at 551; Rose, *supra* note 2, at 679.

[20] Kimball & Boyce, *supra* note 2, at 551; Rose, *supra* note 2, at 679.

[21] Kimball & Boyce, *supra* note 2, at 551; Rose, *supra* note 2, at 679.

[22] German Alliance Ins. Co. v. Lewis, 233 U.S. 389, 389 (1914).

[23] *Id.* at 397.

[24] *Id.* at 414-18. *See also* Nat'l Union Fire Ins. Co. v. Wanberg, 260 U.S. 71, 75 (1922) (holding that insurance is a business affected with a public interest).

[25] HANSON ET AL., *supra* note 2, at 17; Rose, *supra* note 2, at 679-80.

established.[26] The Committee did not view the results of the anti-compact laws positively since they led to destructive competition and rate discrimination.[27] It instead recommended the passage of a statute providing for the filing by rate bureaus of fire insurance rates with the Insurance Department and subjecting those bureaus to the Insurance Department's control.[28] In accordance with these recommendations, the New York legislature enacted a law allowing fire insurers to fix rates in concert.[29] Rate bureaus were authorized and had to set the rates; the rates had to be filed with the insurance superintendent, who had to approve them before they could be used.[30]

Afterwards other states, acknowledging the inefficiency of the anti-compact laws, passed similar rate regulatory laws.[31] States no longer relied on competition as a means for rate-setting; instead, they authorized rating bureaus to set fire insurance rates. Rate bureaus evolved from both the public and the industry interest in rate setting; they were privately operated except in Texas.[32] Some states required companies "to become a member of or subscriber to a rating organization."[33] Rates were, however, subject to the public control by state insurance departments, which usually had to approve them. By 1944, there were only three states with no public control of rate-setting.[34]

Up to 1945 states did not regulate rates for the casualty insurance industry to the same extent as in fire insurance.[35] Except for workmen's compensation insurance, most regulation aimed at avoiding rate discrimination.[36] Further, only a small number of states required filing and approval of automobile insurance rates.[37] In general, rate competition was prevalent in the casualty insurance market.[38]

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[26] HANSON ET AL., *supra* note 2, at 17; Rose, *supra* note 2, at 679-80.

[27] HANSON ET AL., *supra* note 2, at 17; Rose, *supra* note 2, at 679-80.

[28] HANSON ET AL., *supra* note 2, at 19; Rose, *supra* note 2, at 680.

[29] HANSON ET AL., *supra* note 2, at 19; Rose, *supra* note 2, at 680.

[30] Rose, *supra* note 2, at 680.

[31] HANSON ET AL., *supra* note 2, at 19.

[32] HANSON ET AL., *supra* note 2, at 20; Kimball & Boyce, *supra* note 2, at 552; Wiley, *supra* note 18, at 314.

[33] HANSON ET AL., *supra* note 2, at 20.

[34] Kimball & Boyce, *supra* note 2, at 551.

[35] HANSON ET AL., *supra* note 2, at 20; Rose, *supra* note 2, at 682.

[36] HANSON ET AL., *supra* note 2, at 20-21; Rose, *supra* note 2, at 682.

[37] HANSON ET AL., *supra* note 2, at 21; Rose, *supra* note 2, at 682.

[38] Rose, *supra* note 2, at 682.

### C. *U.S. v. South-Eastern Underwriters Association* and the McCarran-Ferguson Act

Until 1944, the U.S. Supreme Court's 1868 holding in *Paul v. Virginia* exempted rate-setting agreements from federal antitrust law.[39] The case involved an 1866 Virginia statute that prohibited insurers who were not incorporated in Virginia and their local agents from doing business in the state without first obtaining a license. The statute was challenged on the ground, *inter alia*, that it conflicted with the Commerce Clause of the U.S. Constitution,[40] which gives Congress the power "to regulate commerce with foreign nations, and among the several States."[41] The Court, upholding the Virginia statute, held that insurance was not commerce, interstate or otherwise.[42] From then on, insurance contracts were not subject to federal antitrust law.[43]

In 1944, however, in *U.S. v. South-Eastern Underwriters Association*,[44] the Supreme Court reversed *Paul v. Virginia*. In that case, 198 member companies of the South-Eastern Underwriters Association and twenty-seven individuals were indicted in the U.S. District Court for the Northern District of Georgia.[45] The indictment alleged two conspiracies in violation of the Sherman Act.[46] The first was a conspiracy to restrain interstate commerce by fixing insurance premiums.[47] The second was a conspiracy to monopolize trade and commerce in the fire insurance sector and in allied lines in the states of Alabama, Florida, Georgia, North Carolina, South Carolina and Virginia.[48] The District Court dismissed the indictment and, relying on *Paul v. Virginia*, held that insurance was not commerce and therefore price-fixing in the business of insurance did not violate the Sherman Act.[49] On appeal, the Supreme Court ruled that the Sherman Act did apply to the fire insurance business since any business conducted across state lines was "commerce among the several States."[50] In

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39 Paul v. Virginia, 75 U.S. 168, 183 (1868).
40 *Id*. at 177.
41 U.S. CONST. art. I, § 8, cl. 3.
42 *Paul*, 75 U.S. at 183.
43 *Id*.
44 U.S. v. Se. Underwriters Ass'n, 51 F. Supp. 712, 713 (N.D. Ga. 1943).
45 *Id.*
46 *Id*.
47 *Id*.
48 *Id*.
49 *Id*. at 713-15.
50 U.S. v. Se. Underwriters Ass'n, 322 U.S. 533, 538-41 (1944).

that regard, the Court specified that all commercial activities conducted across state lines fell within Congress' regulatory power under the Commerce Clause and no exception could be made for the business of insurance.[51]

Following this decision, insurance companies and states lobbied Congress to avoid federal regulation of the insurance sector.[52] In particular, states were afraid to lose their regulatory power and the power to tax insurance companies.[53] In 1945 Congress passed the McCarran-Ferguson Act to preserve the states' control over insurance regulation.[54] Congress was concerned about the uncertainty that might ensue from a change in regulatory authority and also believed that states could regulate insurance better than the federal government, because of their relationship with the insurance companies and their experience with regulating insurance.[55]

In the preamble McCarran-Ferguson states that "the continued regulation and taxation by the several States of the business of insurance is in the public interest."[56] To that end, Section 1012(b) of McCarran-Ferguson provides that no "Act of Congress shall be construed to invalidate, impair or supersede" any state law enacted in order to regulate or tax the business of insurance.[57] By virtue of this provision, state law supplanted federal antitrust regulation of the insurance industry. Conversely, the Act provides that the Sherman, Clayton and Federal Trade Commission Acts apply to "the business of insurance to the extent that such business is not regulated by State law,"[58] except for agreements or acts of boycott, coercion, or intimidation.[59] This aspect of the act was considered a compromise between those in Congress who favored an antitrust exemption and those who favored federal supervision of the insurance industry.[60] In this way the act permits states the opportunity to continue to regulate insurance, while retaining the right for federal intervention in case the states failed to intervene.[61] As a consequence of

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[51] *Id.* at 553.
[52] Kimball & Boyce, *supra* note 2, at 553-54.
[53] *Id*. at 554.
[54] 15 U.S.C.A. §§ 1011-1015 (West 2009).
[55] Rose, *supra* note 2, at 694.
[56] 15 U.S.C.A. § 1011 (West 2009).
[57] *Id.* § 1012(b).
[58] *Id*.
[59] *Id.* § 1013(b).
[60] Kimball & Boyce, *supra* note 2, at 555.
[61] *Id*.

McCarran-Ferguson most states enacted laws regulating insurance and, in particular, rate-setting.[62]

### D. THE NAIC-AIC MODEL RATE REGULATORY BILLS AND THE SUBSEQUENT STATE LEGISLATIVE ACTION

Section 1012(b) of McCarran-Ferguson encouraged the states to regulate insurance in order to avoid federal intervention.[63] Soon, uniform legislation was introduced in the states under the auspices of the NAIC and the All-Industry Committee (AIC).[64] The AIC, representing nineteen insurer associations, was formed to cooperate with the NAIC to develop model legislation designed to reinforce state control of insurance in accordance with section 1012(b).[65] In 1946, two model laws, one for fire, marine and inland marine insurance and the other for casualty and surety insurance, were submitted to individual states for passage.[66]

The two model laws, which were similar in content, proposed proscriptions on excessive, inadequate or unfairly discriminatory rates and advocated supervision of rate-setting among insurers.[67] The bills provided that in setting rates, consideration should be given, *inter alia*, to past and prospective loss experience in the state and elsewhere.[68] Further, insurers had to file any rating plan and any modification to that plan with state insurance commissioners.[69] Under the model laws, such information would become public after the filing became effective.[70]

The model laws also addressed rate-setting by insurers. Insurers were allowed to benefit from the services of rating organizations or of advisory organizations.[71] Rating organizations made rates for their members and subscribers, while advisory organizations assisted insurers which filed their own rates or rating organizations in rate making by

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[62] Rose, *supra* note 2, at 696.

[63] *Id*. (quoting Patrick A. McCarran, *Federal Control of Insurance: Moratorium under Public Law 15 Expired July 1*, 34 A.B.A. J. 539, 540 (1948)).

[64] Kimball & Boyce, *supra* note 2, at 555; Rose, *supra* note 2, at 696-97.

[65] Rose, *supra* note 2, at 697.

[66] Kimball & Boyce, *supra* note 2, at 555; Rose, *supra* note 2, at 698-99.

[67] HANSON ET AL., *supra* note 2, at 29-33 (reproducing the draft of the casualty and surety insurance bill); Rose, *supra* note 2, at 699-701 (reproducing the draft of the fire, marine and inland marine insurance bill).

[68] HANSON ET AL., *supra* note 2, at 30; Rose, *supra* note 2, at 699.

[69] HANSON ET AL., *supra* note 2, at 30; Rose, *supra* note 2, at 699.

[70] HANSON ET AL., *supra* note 2, at 30; Rose, *supra* note 2, at 699.

[71] HANSON ET AL., *supra* note 2, at 31-32; Rose, *supra* note 2, at 699-700.

collecting and furnishing loss and expense data or by providing recommendations concerning rates.[72] Both rating organizations and advisory organizations were subject to state requirements.[73] Insurers could file independent rates or those made by a licensed rating organization. Insurers were also allowed to seek permission from commissioners to file deviations from rates set by a rating organization.[74] Lastly, under the so-called "deemer clause", rate filings were considered approved unless disapproved within fifteen days, or thirty days if the commissioner decided to extend the period for approval.[75]

The model bills, which favored the interests of the rate bureaus,[76] were introduced with amendments in some states.[77] In particular, the amendments concerned the deemer clause since states had different interpretations about how rates should be filed with commissioners in order to meet the state regulation requirement of section 1012(b) of the McCarran-Ferguson Act.[78] Some states, like California, Missouri and Idaho, did not require rate filings for fire or casualty lines (although the insurance commissioner had discretionary authority to request such filings), while other states, like Delaware, Maine, Massachusetts, Wyoming, Ohio and District of Columbia, provided that the rates once filed became effective, subject to subsequent disapproval.[79] The model laws assumed that the requirements for reverse preemption found in section 1012(b) of McCarran-Ferguson were met by the mere existence of state legislation.[80]

### E. THE AFTERMATH OF THE ENACTMENT OF THE RATE REGULATORY BILLS

With the enactment of state rate regulatory laws based on the NAIC-AIC model bills, several controversies about competitive versus cooperative rate making arose.[81] Between 1947 and 1957 the rate bureaus

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[72] HANSON ET AL., *supra* note 2, at 31-32; Rose, *supra* note 2, at 700.
[73] HANSON ET AL., *supra* note 2, at 31-32; Rose, *supra* note 2, at 700.
[74] HANSON ET AL., *supra* note 2, at 30-31; Rose, *supra* note 2, at 700.
[75] HANSON ET AL., *supra* note 2, at 30; Rose, *supra* note 2, at 701.
[76] Rose, *supra* note 2, at 698, 703.
[77] Kimball & Boyce, *supra* note 2, at 555.
[78] Rose, *supra* note 2, at 704.
[79] *Id*. at 704 & nn.176-77.
[80] *See id*. at 705-06 (describing the legislative history of the McCarran-Ferguson Act).
[81] *Id.* at 716-17.

put up strong resistance to rate deviations.[82] Insurers seeking to file deviations experienced obstacles because the NAIC-AIC model laws required commissioners to notify the rate bureaus before approving a rate deviation.[83] The rate bureaus could then testify in opposition to the deviation.[84] Further, since the deviation filing was valid for only one year, insurers had to, at considerable cost, justify their request annually.[85] This led many insurers to resign from the bureaus in order to make independent filings.[86] For example, in 1954 the Insurance Company of North America (INA) resigned from the New York Fire Insurance Rating Organization (NYFIRO) and made independent rate filings for most dwelling classes while remaining a subscriber for other dwelling classes and commercial lines.[87] The NYFIRO challenged the New York department's approval, arguing that INA could not independently file for some risks and subscribe to the bureau for others and that INA violated NYFIRO's property rights by using bureau data in its filings.[88] The New York Insurance Department rejected the NYFIRO's petition and authorized independent filing and the right of partial subscribership.[89]

In 1955 the Pacific Fire Rate Bureau adopted a rule that companies that made independent filings could no longer benefit from bureau scheduled-rating services.[90] The rule was challenged in several states since insurers valued the scheduled-rating services and did not want to lose their right to subscribe to them.[91] The Arizona Supreme Court held the rule invalid in 1958.[92]

The partial subscribership system that resulted permitted the setting of more independent rates since insurance companies with sufficient loss experience in certain lines of insurance could make independent filings.[93] In doing so, insurers had to confront the attempts by the bureaus to

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[82] *See id*. at 718.
[83] *Id*.
[84] Rose, *supra* note 2, at 718.
[85] *Id*.
[86] *Id*. at 720.
[87] *Id*.
[88] *Id*. at 720-21.
[89] *Id*. at 721.
[90] Rose, *supra* note 2, at 721.
[91] *Id*.
[92] Pac. Fire Rating Bureau v. Ins. Co. of N. Am., 321 P.2d 1030, 1034-35 (Ariz. 1958).
[93] Joel B. Dirlam & Irwin M. Stelzer, *The Insurance Industry: A Case Study in the Workability of Regulated Competition*, 107 U. PA. L. REV. 199, 208 (1959).

intervene in the hearings and oppose the deviations as aggrieved parties, subjecting insurers to delays and expenses.[94] To remedy this situation, insurance commissioners and courts[95] ruled that rate bureaus could not appear as aggrieved parties because they acted not to benefit the public but rather to protect their own interests.[96] In the process, a more flexible rate setting system emerged that permitted price competition to a certain extent through deviations from the bureau rates, aided by provisions in the NAIC-AIC model laws that did not make membership in rate bureaus mandatory, allowing insurers to make independent filings.

### F. Revision of the Rating Laws

The trend toward less regulated rates was also reflected in a study conducted by the Senate Antitrust and Monopoly Subcommittee in 1958. The Senate appointed the Subcommittee to conduct a study on insurance and antitrust laws. The Subcommittee recommended denying rate bureaus the status of aggrieved parties, eliminating the requirement of the annual filings of deviations and, lastly, adopting file-and-use rating systems.[97]

Similar recommendations were also provided by the subcommittee appointed by the NAIC Rates and Rating Organization Committee in 1960 in order to review the insurance state regulation system.[98] The subcommittee recommended that no rate bureau should have the status of aggrieved party because the bureaus had no interest in decisions on rate filings. Rate bureaus, according to the subcommittee, should have been denied status to apply for a hearing on insurers' independent filings and the one-year limitation on deviation should have been eliminated. The subcommittee also recommended continuing the deemer clause and the right of partial subscribership to bureaus and to consolidate the fire and casualty rating bills in order to permit the development of multi-line package policies.[99]

In 1962 the NAIC approved amendments to the model rating laws, adopting the recommendations of its subcommittee.[100] In 1964 the NAIC

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[94] *See* Rose, *supra* note 2, at 723-24.

[95] *See, e.g.*, Va. Ass'n of Ins. Agents v. Commonwealth, 110 S.E.2d 223, 228 (Va. 1959) (holding that rate bureaus could not be granted the status of aggrieved party since orders concerning rates were not addressed to them).

[96] Rose, *supra* note 2, at 725.

[97] *Id*. at 725-26.

[98] Hanson et al., *supra* note 2, at 46-47.

[99] *Id*. at 46-47.

[100] Hanson et al., *supra* note 2, at 48; Rose, *supra* note 2, at 726.

Rates and Rating Organizations Committee appointed another subcommittee to inquire into the rate regulation system.[101] The subcommittee found that competition had increased in the insurance market since the 1940s.[102] In particular, it noted that price competition had become more widespread due to independent rate filings and decreased influence by rate bureaus in setting rates.[103] The Subcommittee recommended placing more reliance on fair competition to set insurance prices[104] and suggested the suspension where possible of the prior approval system and its replacement with no prior approval rate regulation.[105] In states where local market characteristics did not permit such a change, the subcommittee recommended continuing the deemer provision to assure prompt responses to rate filings.[106]

In a file and use system a rate filing becomes effective once the rate is filed with the insurance commissioner. Soon, the insurance industry embraced no prior rate approval and file and use provisions to permit insurers to respond immediately to market changes.[107] By 1985, 24 states adopted such changes in their rating laws.[108]

California, for example, adopted a competitive rate setting system that incorporated a no filing provision and abolished any requirement to belong to a rate bureau.[109] Under California law, rates could be used immediately without having to be filed or approved by the commissioner. Illinois, which had originally enacted a prior approval law, enacted an open competition law in 1970.[110] The open competition rating law was distinguished by the lack of advance approval or disapproval by the

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[101] HANSON ET AL., *supra* note 2, at 48.
[102] *Id*. at 51.
[103] *Id*.
[104] *Id*.
[105] *Id*.
[106] *Id*. at 53.
[107] Rose, *supra* note 2, at 726-28.
[108] Paul L. Joskow & Linda McLaughlin, *McCarran-Ferguson Act Reform: More Competition or More Regulation?*, 4 J. RISK & UNCERTAINTY 373, 380 (1991).
[109] CAL. INS. CODE §§ 1850-1850.3 (1947) (repealed 1988); HANSON ET AL., *supra* note 2, at 56, 395-419.
[110] HANSON ET AL., *supra* note 2, at 57, 420; Stephen P. D'Arcy, *Insurance Price Deregulation: The Illinois Experience*, *in* DEREGULATING PROPERTY-LIABILITY INSURANCE: RESTORING COMPETITION AND INCREASING MARKET EFFICIENCY 248, 256 (David J. Cummins ed., 2002).

regulator and the prohibition of any agreement to adhere to bureau rates.[111] In August 1971[112] the law was allowed to sunset and Illinois became the only state without a rating law for property and casualty insurance.[113] However, there has been no attempt at federal antitrust enforcement in Illinois since the two largest personal lines insurers domiciled there, State Farm and Allstate, make their rates independently.[114] In June 1972 the state enacted a law limited to regulating advisory organizations which were defined to mean every person, other than an insurer, who compiles insurance statistics, prepares insurance policies and underwriting rules, makes surveys and insurance research and furnishes that material to insurance companies.[115] Insurers were prohibited from agreeing with each other or the advisory organization to adhere to the use of any statistics, policy forms or underwriting rules.[116]

### G. RECENT DEVELOPMENTS

Between 1985 and 1988 several states adopted flex-rating systems, seeking to establish caps on price increases.[117] Indeed, especially in the area of auto insurance, regulators started focusing on affordability of coverage and suppression of rates despite increasing claim costs.[118] In this connection, an important regulatory development occurred in California on November 8, 1988 with the passage of Proposition 103.[119] Proposition 103 required a rollback of rates for automobile insurance to 20 percent below the rates in effect on November 8, 1987[120] unless the downturn in rates would have led to the insolvency of the insurer.[121] In addition, a prior

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[111] HANSON ET AL., *supra* note 2, at 395.
[112] HANSON ET AL., *supra* note 2, at 57, 420; D'Arcy, *supra* note 110, at 257.
[113] D'Arcy, *supra* note 110, at 257.
[114] *Id.*
[115] HANSON ET AL., *supra* note 2, at 57, 420-21.
[116] *Id*. at 57, 421.
[117] Joskow & McLaughlin, *supra* note 108, at 380.
[118] Scott E. Harrington, *Rate Suppression*, 59 J. RISK & INS. 185, 187 (1992) (defining "rate suppression" as government suppression of insurance rates below the level that would exist in the absence of price regulation).
[119] CAL. INS. CODE §§ 1861.01-1861.02 (2008).
[120] *Id.* § 1861.01(a).
[121] *Id.* § 1861.01(b). Subdivision (b) of § 1861.01 has been held unconstitutional on May 4, 1989 in the case of *Califarm Ins. Co. v. Deukmejian*, 771 P.2d 1247, 1255 (Cal. 1989) (reaffirming the constitutional standard of a fair

approval system was introduced for most casualty insurance rates. Beginning on November 8, 1989, property and casualty insurance rates in California had to be approved by the commissioner prior to use.[122] Finally, Proposition 103 provided that personal automobile insurance rates must be determined taking into account, in decreasing order of importance, the insured's driving safety record, the number of miles driven annually by the insured, the number of years of driving experience of the insured and any other rating factors that the commissioner specified had a substantial relationship to the risk of loss.[123] A mandatory 20 percent discount for good drivers was also established.[124] Thus, Proposition 103 replaced the open competition system in force until then in California.

In 1994, in *20th Century Ins. Co. v. Garamendi*, the California Supreme Court affirmed the Insurance Commissioner's authority to adopt a ratemaking formula implementing the rate rollback provision of Proposition 103.[125] The court held that the rate making formula was not confiscatory since it did not preclude the setting of a just and reasonable rate.[126] According to the court, the rates set under the formula did not inflict "deep financial hardship" on insurers and therefore did not prevent them from operating successfully.[127] Going forward, California's system of rate regulation mainly aimed to avoid excessive rates by determining maximum rate levels.[128]

In 1980 the NAIC adopted model laws for less restrictive rating systems introducing the "file and use" and "use and file" types of rate regulation.[129] In the 1990s, catastrophic losses increased the level of state intervention in the pricing and underwriting of homeowners' insurance.[130] A tendency towards less restrictive rate regulation emerged with regard to other property lines, in particular automobile insurance.[131] Favorable loss

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and reasonable return according to the due process clause of the state and federal Constitution).

[122] CAL. INS. CODE § 1861.01(c) (2008).

[123] *Id.* § 1861.02(a).

[124] *Id.* § 1861.02(b)(2).

[125] 20th Century Ins. Co. v. Garamendi, 878 P.2d 566 (Cal. 1994).

[126] *Id*. at 617-18.

[127] *Id*.

[128] Harrington, *supra* note 118; Joskow & McLaughlin, *supra* note 108.

[129] NAIC, PERSONAL LINES REGULATORY FRAMEWORK 2 (draft white paper) (Apr. 16, 2009), www.naic.org/documents/committees_papers_framework_02.doc.

[130] HARRINGTON, *supra* note 1, at 9-10.

[131] *Id*. at 10.

trends led insurers to reduce their rates and consequently the need to use regulation to suppress rates declined.[132]

Toward the end of the 1990s, many states passed laws deregulating the price and policy forms of commercial insurance.[133] Commercial deregulation laws were enacted in 1998 in Arizona, Georgia, Illinois and New Hampshire and in 1999 in Arkansas, Colorado, Kansas, Montana, Missouri, Oklahoma, Indiana, Maine, Louisiana, Virginia and Rhode Island.[134] New York, Connecticut and Massachusetts have also adopted similar legislation.[135] These laws exempt insurance companies that sell their products to large specialized commercial insurance buyers from rate and policy form requirements.[136] The hope was that if insurers did not have to comply with state control, they would be able to diversify both their rates and types of policies, thereby expanding the range of products they could offer.[137]

Currently, there are six different types of rate regulation systems.[138] Rate regulation varies from the most restrictive type, the prior approval method, to the no-filing method, the least restrictive. The six systems are the prior approval, file and use, use and file, flex rating, modified prior approval, and no file methods.[139] The prior approval system requires insurers to file the rates and wait for the approval by the insurance commissioner before using them. Approval is presumed if rates are not denied within a specified number of days, in case there is a deemer clause. In the file and use system, rates become effective immediately upon filing. The insurance commissioner, however, may subsequently disapprove the rates. A use and file system provides that rates must be filed with the insurance commissioner within a specified period of time after their first use. In the flex rating system insurers may increase or decrease rates within a certain percentage range. Prior approval is required only if the rate

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[132] *Id*.

[133] *Id.*; Robert M. Ferm & Amy C. Palmerlee, *Recent Developments in Public Regulation of Insurance*, 35 TORT & INS. L. J. 603, 607 (2000).

[134] Ferm & Palmerlee, *supra* note 133, at 607.

[135] *Id*.

[136] HARRINGTON, *supra* note 1, at 10; Ferm & Palmerlee, *supra* note 133, at 607.

[137] Ferm & Palmerlee, *supra* note 133, at 607; *see also* HARRINGTON, *supra* note 1, at 10 (stating that the deregulation trend reflected recognition that rate and form regulation serve no useful purpose and are instead counterproductive).

[138] NAIC, 2 COMPENDIUM OF STATE LAWS ON INSURANCE TOPICS, HEALTH/LIFE/PROPERTY/CASUALTY II-PA-10-21 (2011).

[139] *Id*.

change is larger than the specified percentage. The modified prior approval system provides that rate revisions based only on a change in loss experience are subject to file and use regulation. However, rate revisions based on a change in expense ratio or rate classifications are subject to prior approval. Lastly, under the no-filing system rates do not need to be filed with or approved by the state insurance commissioner. The table in Appendix 1 identifies the types of rate regulation systems according to state.

Recent changes in state rating laws confirm the trend towards less restrictive systems of rate regulation. As of April 2008 rates in Massachusetts were determined according to what the insurance commissioner at the time, Nonnie Burns, called "managed competition".[140] Previously Massachusetts had been the only state where the insurance commissioner set rates for auto insurance. Now, insurance companies submit their rates to the state insurance commissioner, who has power to disapprove them if they are excessive or unfairly discriminatory.[141] In May 2008 the Georgia legislature passed legislation[142] permitting auto insurance companies to set rates above the mandatory minimum limits without prior approval from the insurance commissioner.[143] Finally, in June 2008 the New York legislature approved an auto insurance flex rating bill[144] that allows auto insurance companies to adjust their rates twice annually within a 5 percent band without seeking prior regulatory approval.[145]

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[140] Robert P. Spellane, *Managed Competition Good News for Auto Insurance Buyers*, http://www.thefreelibrary.com/Managed+competition+good+news+for+auto+insurance+buyers.-a0168869015.

[141] Press Release, Mass. Gov't. Office of Consumer Affairs & Bus. Regulation, Mass. Gov't, Insurance Commissioner Issues Final Managed Competition Regulation (Oct. 5, 2007), http://www.mass.gov/?pageID=ocapressrelease&L=1&L0=Home&sid=Eoca&b=pressrelease&f=07_10_05_autoinsurance&csid=Eoca.

[142] S.B. 276, 2008 Gen. Assemb. Sess. (Ga. 2009) (codified as amended at GA. CODE ANN. § 33-9-21(b)(21) (West 2011).

[143] GA. CODE ANN. § 33-9-21(b)(2) (West 2011).

[144] N.Y. INS. LAW § 2350 (McKinney 2011).

[145] *Id.*

## II. RATIONALES FOR AND AGAINST RATE REGULATION

### A. PURPOSES OF RATE REGULATION

In the 1914 landmark case, *German Alliance Ins. Co. v. Lewis*, the U.S. Supreme Court upheld the power of the states to regulate rates on grounds that insurance is affected by the public interest.[146] According to the public interest theory and normative economic theory, insurance rate regulation is intended to correct market failures that would otherwise cause inefficiency and inequity in the insurance market and harm the interest of the general public.[147]

In particular, rate regulation primarily aims to remedy two opposite problems: one, the tendency of insurance companies to engage in destructive competition and two, the formation of price cartels by insurance companies that could set excessive rates.[148] These aims were clearly defined by the subcommittee appointed by the NAIC Rates and Rating Organization Committee in 1960 to review the status of insurance rate regulation.[149] In a report dated November 28, 1960, the subcommittee stated that rate regulation is intended to assure that insurance coverages desired by the public are offered to the public by licensed insurers, that the cost of these coverages is reasonable and not excessive, that insureds bear a fair share of the cost of insurance and that insurers remain solvent to protect their policyholders.[150] In accordance with those objectives, states seek to promote the public welfare by ensuring that premiums are "adequate, not excessive and not unfairly discriminatory." Although these three rate standards are interpreted differently in the different states, they have basic common features that the following analysis will describe.

The first aim of insurance rate regulation, to ensure adequate rates, stems from past experience with unregulated rates and the consequent destructive competition that led to several insurers' insolvencies.[151] One of the principal aims of rate regulation is to maintain the solvency of

[146] German Alliance Ins. Co. v. Lewis, 233 U.S. 389, 414-18 (1914).

[147] David J. Cummins, *Property-Liability Insurance Price Deregulation: The Last Bastion?*, *in* DEREGULATING PROPERTY-LIABILITY INSURANCE: RESTORING COMPETITION AND INCREASING MARKET EFFICIENCY 6 (Cummins ed., 2002).

[148] *Id*.

[149] *See supra* p. 122.

[150] HANSON ET AL., *supra* note 2, at 46-47.

[151] *See supra* pp. 113-16.

insurance companies and to prevent rates from being set too low.[152] The importance of this goal results from the unique nature of the insurance contract. An insurance contract, indeed, is an aleatory contract in which the policyholder pays up-front premiums in exchange for the insurer's promise to indemnify in case a future loss occurs. This gives policyholders an interest in the financial solidity of their insurance companies and in the companies' ability to pay future claims. Given the function of insurance in satisfying society's need for security, the financial solvency of insurance companies is the principal purpose of insurance regulation.[153] For this reason, "the principle of *solidity* is pervasive" in insurance regulation.[154] Rate regulation, like capital adequacy, is considered a means to ensure the solidity of the insurance industry.[155] The self-interest of insurance companies in remaining solvent has not always been reckoned sufficient.[156] Rate regulation, instead, is believed to assure insurers' solvency by keeping rates above a certain minimum level of adequacy so that adequate reserves can be maintained.[157]

As for the second purpose of insurance rate regulation, the concern for making rates not excessive was not one of the original reasons for regulating prices. Initially, regulators and insurance companies were concerned about ruinous competition that could threaten solvency.[158] The NAIC-AIC model laws introduced the "not excessive" standard due to the drafters' belief that cooperation among insurers in setting rates created a need to prevent excessive rates.[159]

The "not excessive" standard seeks to make the cost of insurance affordable.[160] In the process, the standard promotes the availability of insurance.[161] At the same time, this standard may be in tension with the first

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[152] BANKS MCDOWELL, DEREGULATION AND COMPETITION IN THE INSURANCE INDUSTRY 36 (Greenwood Press 1989); Irwin M. Stelzer & Geraldine Alpert, *Benefits and Costs of Insurance Deregulation*, *in* INSURANCE DEREGULATION: ISSUES AND PERSPECTIVES 6, 8 (Nathan Weber ed., The Conference Board 1982).

[153] Spencer L. Kimball, *The Purpose of Insurance Regulation: A Preliminary Inquiry in the Theory of Insurance Law*, 45 MINN. L. REV. 471, 478-80 (1961).

[154] *Id*. at 480.

[155] *Id*. at 481-83.

[156] *Id*. at 482-83.

[157] MCDOWELL, *supra* note 152, at 36.

[158] *Id*. at 37.

[159] *Id*.

[160] Kimball, *supra* note 153, at 491.

[161] Stelzer & Alpert, *supra* note 152, at 8.

standard, which requires insurance rates to be adequate in order to assure the solvency of the insurance companies.[162]

Finally, rate insurance regulation seeks to avoid rates that unfairly discriminate among insureds. This third goal reflects regulators' concerns about price discrimination among consumers when such discrimination is not related to differences in the risks underwritten.[163] Objectionable forms of discrimination include: (i) unfair individual discrimination, such as rebates, credits and misclassifications that favor one insured over another when the risk underwritten is the same,[164] (ii) unfair group rate discrimination that usually involves rating plans that arbitrarily differentiate among the insureds without taking into account their risk[165] and (iii) unfair product discrimination that results in unreasonable overpricing or under pricing of one product compared to another.[166] In this regard, insurance regulators aim to ensure that rates are fair for every class of insured and that the classes are fair and nondiscriminatory.[167] Therefore, while the standard of "not excessive" rates seeks to accomplish reasonableness between insurance companies and policyholders, the standard of "not unfairly discriminatory" rates seeks to accomplish "equity" by ensuring that policyholders are not unfairly discriminated against.[168] In order to achieve this objective, fair classifications of policyholders for premium calculation are necessary so that every insured will bear the cost of his or her own insurance.[169] It is difficult to make fair classifications, however, since every risk is unique and theoretically could be uniquely rated.[170]

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[162] *Id*.

[163] MCDOWELL, *supra* note 152, at 39; SHARON TENNYSON, EFFICIENCY CONSEQUENCES OF RATE REGULATION IN INSURANCE MARKETS, Networks Financial Institute 6 (2007), http://www.networksfinancialinstitute.org/Lists/Publication%20Library/Attachments/15/2007-PB-03_Tennyson.pdf.

[164] HANSON ET AL., *supra* note 2, at 432-33.

[165] *Id*. at 433.

[166] *Id*.

[167] MCDOWELL, *supra* note 152, at 39.

[168] Kimball, *supra* note 153, at 495.

[169] HANSON ET AL., *supra* note 2, at 93; Kimball, *supra* note 153, at 495; Jason C. Blackford, *Competition as a Means of Regulating Insurance*, 18 CLEV.-MARSHALL L. REV. 116, 128 (1969).

[170] Kimball, *supra* note 153, at 495.

## B. ARGUMENTS FOR RATE REGULATION

Having analyzed the goals of rate regulation, now the article turns to the arguments in favor of state regulation of insurance rates.

According to the traditional rationale for regulation of insurance rates, states can protect policyholders by controlling rates.[171] The argument is based on the fact that policyholders and insurance companies do not deal at arm's length and that insurance companies are likely to overcharge policyholders in the absence of rate regulation.[172] When competition results in a variety of rates, some argue that policyholders do not benefit from that variety because they may not have the ability to compare the rates.[173] Policyholders have difficulty in fully understanding the insurance contract and in establishing a connection between the price and the quality of the coverage. In these circumstances, rate regulation and standardization are said to be appropriate.[174] In an un-regulated system, some insurers may cut rates by providing low-quality insurance products that policyholders might not recognize as poor quality due to imperfect information about the characteristics of the coverage offered and the financial solidity of the insurer.[175] Rate regulation would counteract deception by insurers and assist consumers in comparing different insurance policies.[176]

Rate regulation also helps to prevent ruinous price competition with a subsequent increase in insurers' insolvencies.[177] Advocates for rate regulation argue that insurance companies will respond to the danger of destructive competition, by conspiring to set rates.[178] This raises concerns

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[171] JONATHAN R. MACEY & GEOFFREY P. MILLER, COSTLY POLICIES: STATE REGULATION AND ANTITRUST EXEMPTION IN INSURANCE MARKETS 106 (Christopher C. DeMuth & Jonathan R. Macey eds., American Enterprise Institute Press 1993).

[172] *Id*.

[173] FREDERICK G. CRANE, AUTOMOBILE INSURANCE RATE REGULATION 84-85 (Ohio State University 1962); ROBERT E. DINEEN ET AL., INSURANCE AND GOVERNMENT: THE ECONOMICS AND PRINCIPLE OF INSURANCE SUPERVISION 14 (Charles C. Center & Richard M. Heins eds., University of Wisconsin 1960); HANSON ET AL., *supra* note 2, at 529-30; MACEY & MILLER, *supra* note 187, at 106.

[174] HANSON ET AL., *supra* note 2, at 529-30.

[175] *Id*.

[176] *Id*. at 530.

[177] Blackford, *supra* note 169, at 129.

[178] *Id*. at 130.

about anti-competitive conduct and the converse danger of excessive rates.[179]

Predatory pricing concerns are another reason to favor of rate regulation. The concern is that rate deregulation might induce stronger insurers to use their greater financial resources to temporarily cut rates to increase their market share and force weaker insurers out of the insurance market.[180]

Rate regulation is also urged in the interest of actuarial accuracy, because regulators must rely on wide loss experience in setting rates that even larger insurance companies may lack.[181] Moreover, unregulated rates might lead to underwriting restrictions because some insurers might decide to write only low-risk insureds in order to minimize their costs and charge lower premiums.[182] Insurers that continued to write higher-risk insureds would bear a greater proportion of such risks and be forced to increase their rates in order to cover possible losses.[183] This would create problems of insurance affordability and has the potential to result in insolvency of the higher-risk insurers.[184]

### C. ARGUMENTS AGAINST RATE REGULATION

This article will now examine the arguments in favor of deregulating rates. The principal rationale for insurance rate regulation is that it is needed to correct market failures.[185] Opponents of rate regulation, however, argue that the insurance market is competitive[186] since it is characterized by a large number of firms doing business with a low level of concentration and selling similar products.[187] They agree that there are modest barriers to entry and that profits are not excessive compared with

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[179] *Id*.

[180] HANSON ET AL., *supra* note 2, at 528; Blackford, *supra* note 169, at 130.

[181] HANSON ET AL., *supra* note 2, at 528.

[182] CRANE, *supra* note 173, at 78-79; HANSON ET AL., *supra* note 2, at 529.

[183] CRANE, *supra* note 173, at 78-79; HANSON ET AL., *supra* note 2, at 529.

[184] CRANE, *supra* note 173, at 78-79; HANSON ET AL., *supra* note 2, at 529.

[185] *See supra* p. 127; HARRINGTON, *supra* note 1, at 15; Cummins, *supra* note 147, at 6; Tennyson, *supra* note 163, at 8; D'Arcy, *supra* note 110, at 262.

[186] *See infra* pp. 136-41, 150-52.

[187] HARRINGTON, *supra* note 1, at 15-18; Cummins, *supra* note 147, at 7; Tennyson, *supra* note 163, at 8; Paul L. Joskow, *Cartels, Competition and Regulation in the Property-Liability Insurance Industry*, 4 BELL J. OF ECON. AND MGMT. SCI. 375, 379-82, 391 (1973); Joskow & McLaughlin, *supra* note 108, at 378-79.

other industries.[188] Thus, they conclude there is no evidence of market failure that may justify insurance rate regulation.[189]

Further, with regard to the two opposite concerns that, in the absence of rate regulation, insurers would engage in destructive competition or form cartels that would lead to excessive rates,[190] proponents of rate deregulation note that these concerns are outdated.[191]

The concept of destructive competition dates back to the nineteenth century[192] and is no longer well founded since more recently there has been no evidence of dangerous price cutting; rather prices in insurance markets reflect expected claim costs and reasonable profits for insurance companies.[193] Those who favor deregulated rates stress that insurance companies, like all other enterprises, aim to conduct a financially successful business and to avoid charging rates that are too low to cover their costs.[194] Under this view, rate deregulation is not likely to cause ruinous competition because, even assuming that a big insurer reduces its rates in order to eliminate possible competitors, in the long run it will have to raise its rates to cover its costs.[195] In that event, new competitors, attracted by the possibility of making profit, will enter the market.[196]

The cartel pricing concern originated from the initial bureau rate-making activities and the regulatory restrictions on deviations from the bureau rates in the 1950s and early 1960s.[197] Effective cartel pricing is now unlikely given the large number of insurers, ease of entry into the market and the decreased influence by rate bureaus in setting rates.[198]

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[188] HARRINGTON, *supra* note 1, at 15-18; Cummins, *supra* note 147, at 7; Tennyson, *supra* note 163, at 8; Joskow, *supra* note 187, at 388-91; Joskow & McLaughlin, *supra* note 108, at 379.

[189] HARRINGTON, *supra* note 1, at 18; Cummins, *supra* note 147, at 7; Tennyson, *supra* note 163, at 8; Joskow, *supra* note 187, at 403; Joskow & McLaughlin, *supra* note 108, at 379.

[190] *See supra* pp. 111-23.

[191] Cummins, *supra* note 147, at 6.

[192] *Id*.

[193] CRANE, *supra* note 173, at 87-88; Cummins, *supra* note 147, at 6.

[194] CRANE, *supra* note 173, at 88.

[195] *Id*.

[196] *Id*.

[197] Joskow & McLaughlin, *supra* note 108, at 379-80; Cummins, *supra* note 147, at 7.

[198] Joskow & McLaughlin, *supra* note 108, at 379-80; Cummins, *supra* note 147, at 7; HANSON ET AL., *supra* note 2, at 447-53.

Advocates of rate deregulation maintain that the free market is just as appropriate for the insurance sector as it is for other businesses.[199] Although insurance regulation is considered important to ensure the protection of policyholders, proponents of deregulation agree that state control of the insurance market impedes competition.[200] In this connection, rate regulation may lead to both inadequate and excessive rates.[201] In the latter case, rate regulation might cause levels of premiums so high that even the most inefficient insurance companies would make profits.[202] Regulators should not intervene in rate setting and insurance companies should be permitted to make rates so that policyholders can benefit from lower-cost insurance.[203]

Further, advocates point out that determining a proper rate is not feasible since rate setting is "not an inevitably accurate and scientific calculation."[204] They observe that rate-setting is a subjective activity and because there can be more than one reasonable decision in making rates, there is no reason to regard a commissioner's decision as the most reasonable.[205] Indeed, the setting of rates by competently managed insurance companies is arguably as reasonable as the setting of rates by the commissioners.[206] It is also emphasized that a rate proper for one insurer might not be proper for another one.[207]

In addition, proponents argue that unregulated rates will avoid commission wars.[208] When price uniformity prevails, insurers are more likely to have to pay agents higher commissions in order to obtain business.[209] Conversely, they say, the problem of commission wars can be overcome when rates are deregulated since insurers can obtain business by competing on the price of the products offered.[210] Another disadvantage is that restrictions on price competition limit product differentiation because

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[199] CRANE, *supra* note 173, at 84; HANSON ET AL., *supra* note 2, at 530.

[200] CRANE, *supra* note 173, at 84; HANSON ET AL., *supra* note 2, at 530.

[201] HANSON ET AL., *supra* note 2, at 535-36.

[202] HANSON ET AL., *supra* note 2, at 530.

[203] *Id*.

[204] CRANE, *supra* note 173, at 86 (citing Thomas O. Carlson, President, "Statistics for the Ratemaker," *Proceedings of the Casualty Actuarial Society* 1 (May 1953)).

[205] *Id*.

[206] *Id*.

[207] *Id*.

[208] HANSON ET AL., *supra* note 2, at 532.

[209] *Id*.

[210] *Id*.

comparable rates must be charged for comparable products in order to implement a uniform pricing system.[211] Moreover, rate regulation requires even more resources and efforts by the insurance departments in order to examine insurance rates. Deregulation of rates would permit regulators to fully devote themselves to other more important supervisory activities such as solvency supervision.[212]

Another reason advanced in favor of rate deregulation is that it would take politics out of rate-setting.[213] Rate regulation often involves political pressure on insurance commissioners by insurers demanding rate increases and consumers that look unfavorably on those increases.[214] In particular, advocates of rate deregulation observe that the political pressure by policyholders may lead to inadequate rates since regulators will be influenced to approve rate increases that "may be either too little and/or too late."[215] Ironically, even though rate regulation is aimed at avoiding inadequate rates, it may actually lead to inadequate rates.[216] This is especially true in prior-approval systems, because of delays in obtaining approval cost insurers, especially after taking inflation into account.[217] Insurance companies react to inadequate rates by restricting underwriting or by cancelling and refusing to renew insurance policies creating subsequent possible problems of unavailable coverage.[218] This result undermines one of the purposes of insurance rate regulation, to promote insurance availability. Consequently, reduced rate regulation will give

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[211] CRANE, *supra* note 173, at 96; HANSON ET AL., *supra* note 2, at 533.

[212] *See* CRANE, *supra* note 173, at 97-99; HANSON ET AL., *supra* note 2, at 533; HARRINGTON, *supra* note 1, at 33.

[213] CRANE, *supra* note 173, at 100; HANSON ET AL., *supra* note 2, at 62-64, 535.

[214] CRANE, *supra* note 173, at 99-100; HANSON ET AL., *supra* note 2, at 62-64, 535.

[215] HANSON ET AL., *supra* note 2, at 64; David J. Cummins, Richard D. Phillips & Sharon Tennyson, *Regulation, Political Influence and the Price of Automobile Insurance*, 20 J. INS. REG. 9, 42-44 (2001) (showing by statistical regression analysis that insurance prices in regulated states are affected by political influence activities of consumer groups); David J. Cummins & Scott E. Harrington, *The Impact of Rate Regulation in U.S. Property-Liability Insurance Markets: A Cross-Sectional Analysis of Individual Firm Loss Ratios*, 12 GENEVA PAPERS ON RISK & INS. 50, 60 (1987) (suggesting that regulators responded to consumer pressure by holding rates below levels that would have occurred under pricing freedom); Harrington, *supra* note 118, at 189.

[216] HANSON ET AL., *supra* note 2, at 64-65, 535.

[217] *Id*. at 64.

[218] *Id*. at 535-36; Harrington, *supra* note 118, at 189.

insurers the flexibility to adjust rates, ensure adequate rates and make insurance available.[219]

Finally, advocates of deregulation note that the prior approval system can cause rates to remain at a higher level than appropriate.[220] Due to the time necessary to approve a new rate, a cost decline does not automatically translate into a lower rate.[221] Moreover, insurers may not apply for lower rates based on improvement in their underwriting experience if they expect to have difficulty in later obtaining a needed increase.[222]

## III. THE EFFECTS OF OPEN COMPETITION

### A. THE STRUCTURE OF THE U.S. PROPERTY AND CASUALTY INSURANCE MARKET

The economic justification for rate regulation is that it protects the public interest by avoiding inefficiency that would otherwise result from monopolistic or oligopolistic conduct. Under this logic, in order to assess whether the property and casualty industry is likely to achieve benefits from rate deregulation, market structure and easy of entry should be examined.[223] The principal characteristic of monopoly is the presence of a single seller of a product for which there are no alternatives.[224] However, economists have demonstrated that oligopoly power may also exist if there are few sellers and they act in concert.[225] Entry by competitors is the main limitation on monopoly power in a market economy.[226]

The U.S. property and casualty insurance market has the structural characteristics of a competitive market.[227] The market is characterized by a large number of firms operating with low levels of concentration and selling products with identical features.[228] The competitive structure of the market is apparent from the fact that in 2009 there were 2,737 property and

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[219] HANSON ET AL., *supra* note 2, at 536.
[220] *Id*. at 71.
[221] *Id*.
[222] *Id*.
[223] HARRINGTON, *supra* note 1, at 15.
[224] KAHN, *supra* note 1, at 116.
[225] *Id.*
[226] *Id.*
[227] HARRINGTON, *supra* note 1, at 16; Joskow, *supra* note 187, at 391.
[228] Joskow, *supra* note 187, at 390.

casualty insurance companies operating in the United States.[229] This number has increased since 1971, when there were 1,206 companies operating in the U.S. property and casualty insurance market.[230]

That said, the presence of a large number of insurers offering basically the same product is not by itself indicative of competition since a small number of companies could write a majority of the premiums and by virtue of their market share be able to fix prices.[231] It is necessary, therefore, to consider the relative market share of insurance companies in order to determine whether the market is competitive. The following table presents the 2009 nationwide market share of the top twenty-five U.S. property and casualty insurance groups. The market share of different corporate groups as a whole is a more accurate indicator than market share of their individual insurance subsidiaries. While individual subsidiaries are separate legal entities, they are not economically independent and are subject to the group's management decisions.

**Table 1 – Property and Casualty Insurance Industry 2009 Market Share Nationwide by Group**

| | GROUP NAME | DIRECT PREMIUMS WRITTEN | MARKET SHARE percent | CUMULATIVE MARKET SHARE percent |
|---|---|---|---|---|
| 1 | State Farm Grp | 51,063,110,761 | 10.50 | 10.50 |
| 2 | Zurich Ins Grp | 28,979,691,684 | 5.96 | 16.46 |
| 3 | Allstate Ins Grp | 26,153,440,231 | 5.38 | 21.84 |
| 4 | American Intl Grp | 26,140,201,178 | 5.38 | 27.22 |
| 5 | Liberty Mut Grp | 24,772,894,328 | 5.10 | 32.32 |
| 6 | Travelers Grp | 21,409,548,242 | 4.40 | 36.72 |
| 7 | Berkshire Hathaway Grp | 16,054,658,656 | 3.30 | 40.02 |
| 8 | Nationwide Corp Grp | 15,405,561,636 | 3.17 | 43.19 |
| 9 | Progressive Grp | 14,200,294,349 | 2.92 | 46.11 |
| 10 | Hartford Fire & Cas Grp | 10,473,026,375 | 2.15 | 48.26 |
| 11 | United Serv Automobile Ass'n Grp | 10,439,501,509 | 2.15 | 50.41 |

[229] INSURANCE INFORMATION INSTITUTE, THE INSURANCE FACT BOOK 2011 V (2011) [hereinafter THE INSURANCE FACT BOOK 2011].
[230] Joskow, *supra* note 187, at 379.
[231] *Id*. at 380.

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|---|---|---|---|---|
| 12 | Chubb & Son Ins Grp | 9,419,255,363 | 1.94 | 52.35 |
| 13 | Cna Ins Grp | 8,131,205,861 | 1.67 | 54.02 |
| 14 | Ace Ltd Grp | 7,780,534,083 | 1.60 | 55.62 |
| 15 | Allianz Ins Grp | 5,764,589,841 | 1.19 | 56.81 |
| 16 | American Family Ins Grp | 5,681,564,588 | 1.17 | 57.98 |
| 17 | Auto Owners Grp | 4,451,729,312 | 0.92 | 58.90 |
| 18 | Erie Ins Grp | 3,860,839,234 | 0.79 | 59.69 |
| 19 | Assurant Inc Grp | 3,735,278,486 | 0.77 | 60.46 |
| 20 | American Financial Grp | 3,565,868,308 | 0.73 | 61.19 |
| 21 | Wr Berkley Corp Grp | 3,255,838,299 | 0.67 | 61.86 |
| 22 | Fm Global Grp | 3,199,857,312 | 0.66 | 62.52 |
| 23 | Qbe Ins Grp | 3,128,630,118 | 0.64 | 63.16 |
| 24 | Cincinnati Fin Grp | 3,071,344,125 | 0.63 | 63.79 |
| 25 | Metropolitan Grp | 2,984,332,558 | 0.61 | 64.40 |

Source: NAIC, 2009 Market Share Reports for the Top 25 Property/Casualty Insurers Over 25 Years 39 (2010), reprinted with permission. The NAIC does not endorse any analysis or conclusions based on use of its data.

Although table 1 suggests that the market is concentrated since twenty-five insurance groups control 64.40 percent of the market, with State Farm Group controlling a market share of 10.50 percent,[232] evaluation of the Herfindahl-Hirschman Index (HHI) leads to a different conclusion. The HHI is a commonly used measure of industry concentration and is calculated by summing the squares of the market share percentage of all companies in the market. For example, if a market had only one seller, its market share would be 100 percent and its HHI would be 10,000. If a market had five sellers, each with an equal 20 percent of the market, the HHI would be 2000. The HHI tends to zero when a market consists of a large number of firms of relatively equal size. Increases in the value of the HHI indicate higher concentration in the market, either due to a decrease in the number of firms or an increase in the disparity in size between these firms. Although there is no precise point at which the HHI indicates market concentration sufficient to restrict competition, the Department of Justice

[232] *See* James Barrese, Gene Lai & Nicos Scordis, *Ownership Concentration and Governance in the U.S. Insurance Industry*, 30 J. INS. ISSUES 1 (2007).

has developed Merger Guidelines under which an HHI of less than 1000 means the market is not concentrated, an HHI between 1,000 and 1,800 points means the market is moderately concentrated and an HHI over 1,800 points means the market is concentrated.[233] According to the ISO, the HHI for the property and casualty insurance market in 2009 was 351 points.[234] This indicates that the market was not concentrated. Further, the trend toward an increase in the level of market concentration indicates a decline in high-cost companies in favor of more efficient and lower-cost companies.[235] Therefore, higher market concentration may be the result of increased market competition and a subsequent improvement in policyholders' welfare.[236]

With respect to possible barriers to entry, it is generally acknowledged that insurers can easily enter the property and casualty insurance market.[237] The ability of new insurers to enter into the business assures efficiency and competition. When there are excessive profits in the market, new firms are induced to enter and the quantity of products offered is increased. Consequently, excess profits decrease until reaching a price level where zero excess profits exist. In this way a competitive market is achieved. The following table shows, *inter alia*, the number of entries in the markets for commercial property and casualty insurance products from 2004 to 2009.

**Table 2 – 2009 Commercial Lines Data – Nationwide**

| LINE OF BUSINESS | PREMIUMS WRITTEN | MARKET SHARES FOUR LARGEST GROUPS | HHI BASED ON PREMIUM | NUMBER OF SELLERS (GROUPS) | NUMBER OF ENTRIES LAST 5 YEARS | NUMBER OF EXITS LAST 5 YEARS | MARKET GROWTH LAST 3 YEARS | MARKET GROWTH LAST 10 YEARS | RETURN ON NET WORTH 10-YEAR MEAN |
|---|---|---|---|---|---|---|---|---|---|
| Commercial Auto Liability | 18,988,326,402 | 28.55 percent | 320 | 105 | 30 | 29 | -13.97 percent | 25.05 percent | 7.43 percent |

[233] U.S. Department of Justice and the Federal Trade Commission, Horizontal Merger Guidelines § 1.51 (1997), *available at* http://www.usdoj.gov/atr/public/guidelines/hmg.htm.

[234] THE INSURANCE FACT BOOK 2011, *supra* note 229, at 47.

[235] Joskow, *supra* note 187, at 382.

[236] *Id.*

[237] HARRINGTON, *supra* note 1, at 16; Joskow, *supra* note 187, at 388-91; Joskow & McLaughlin, *supra* note 108, 379.

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|---|---|---|---|---|---|---|---|---|---|
| Commercial Auto Physical | 5,792,918,385 | 25.21 percent | 266 | 119 | 32 | 24 | -20.16 percent | -4.67 percent | 13.36 percent |
| Commercial Auto Total | 24,781,244,787 | 27.77 percent | 297 | 115 | 33 | 25 | -15.50 percent | 16.56 percent | 8.49 percent |
| Commercial Multiple Peril | 34,034,902,544 | 27.80 percent | 338 | 104 | 25 | 27 | -5.82 percent | 50.34 percent | 8.03 percent |
| Fire | 12,861,192,843 | 38.65 percent | 554 | 99 | 33 | 33 | 5.11 percent | 138.66 percent | 19.77 percent |
| Allied Lines | 11,249,248,316 | 38.47 percent | 499 | 84 | 28 | 43 | -1.31 percent | 186.42 percent | -3.92 percent |
| Inland Marine | 13,434,863,829 | 35.08 percent | 495 | 76 | 25 | 32 | -12.81 percent | 61.49 percent | 19.07 percent |
| Mortgage Guaranty | 5,449,184,963 | 69.45 percent | 1,594 | 8 | 1 | 1 | -11.43 percent | 46.31 percent | -33.39 percent* |
| Financial Guaranty | 1,922,896,601 | 89.54 percent | 2,985 | 9 | 5 | 5 | -45.91 percent | 22.40 percent | -15.44 percent* |
| Medical Professional Liability | 10,817,257,976 | 24.28 percent | 288 | 98 | 27 | 25 | -7.42 percent | 67.72 percent | 7.40 percent |
| Other Liability | 47,489,981,386 | 33.13 percent | 451 | 88 | 23 | 21 | -13.41 percent | 82.38 percent | 4.66 percent |
| Workers Compensation | 41,287,350,051 | 33.34 percent | 395 | 110 | 39 | 31 | -20.98 percent | 19.64 percent | 6.35 percent |
| Products Liability | 2,895,299,149 | 30.42 percent | 404 | 66 | 19 | 16 | -28.72 percent | 47.40 percent | 0.43 percent* |

* Denotes Return on Net Worth for 2009 data year only.

Source: NAIC, 2009 Competition Database Report 10 (2010), reprinted with permission. The NAIC does not endorse any analysis or conclusions based on use of its data.

In particular, it can be seen that the number of insurance groups with affiliated insurers which have entered the markets for commercial property and casualty insurance products between 2004 and 2009 is substantial. For example, thirty-nine insurers entered the workers compensation market, thirty entered the commercial auto insurance market, twenty-seven entered the medical professional liability market and twenty-five entered the commercial multiple peril market. This, along with the fact that the level of concentration in the U.S. property and casualty insurance market is low, leads to the conclusion that insurance companies are unable to charge excessive prices by attempting to act in concert since, in the absence of substantial barriers to entry, new insurers will prevent existing companies from fixing prices.

As this shows, the U.S. property and casualty insurance market is competitive because it is characterized by a large number of insurance companies operating with low concentration levels. Prof. Paul Joskow called the insurance market one of the markets that conform more closely to the ideal model of perfect competition.[238] The insurance market, therefore, does not present characteristics of a monopoly or an oligopoly that may justify rate regulation.

In recognition of the wisdom of rate deregulation, there has been a gradual movement away from prior-approval systems toward less restrictive systems such as: file and use, use and file, flex rating, modified prior approval and, in particular, no file systems.[239] Further, the NAIC File and Use Model Act introduced a presumption in favor of the existence of a competitive market unless the commissioner, after a hearing, determines that the market is not competitive.[240] The Model Act also established a standard which provides that a rate in a competitive market is not excessive.[241]

Nevertheless, prior-approval laws are still enforced in many states.[242] For example, prior approval systems are used in Mississippi with regard to all insurance lines, in California with regard to all lines except title insurance, in Alabama for medical malpractice, property and inland marine, workers' compensation and personal lines, in Alaska with regard to medical malpractice, workers' compensation and assigned risk rates, in Connecticut with regard to medical malpractice (for rate increases of 7.5

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[238] Joskow, *supra* note 187, at 391.

[239] *See supra* pp. 125-26.

[240] *E.g.*, PROPERTY AND CASUALTY MODEL RATING LAW (FILE AND USE VERSION) § 4 (NAIC 2010) [hereinafter FILE AND USE MODEL LAW] (providing that the insurance commissioner in determining whether a reasonable degree of competition exists in the market shall consider market structure, market performance, market conduct, the consumers' practical opportunities to acquire pricing and other information and to compare and purchase insurance from competing insurers).

[241] *See, e.g.*, FILE AND USE MODEL LAW, *supra* note 240, at § 5(A)(1)(a).

[242] *See* Appendix 1.

percent or more over the last rates filed) and title insurance.[243] It is also worth mentioning that, except for the no-file systems, all the other systems mentioned above retain some form of regulatory control over insurance rates. Although rating laws in the different states vary to some extent, insurance commissioners retain the right to disapprove rates in file and use and use and file systems, while in flex rating and in modified prior approval systems insurers may be required to obtain prior approval from a commissioner if an increase is larger than the percentage rate established or the rate revision is based on a change in expense ratio or rate classifications.[244] With a few rare exceptions, purely competitive rating models are not used in the United States. No-file systems are limited to just a few lines in some states.[245] This stands in contrast with the fact that the competitive structure of the property and casualty insurance market in the U.S. does not justify the regulation of rates.

### B. The European Experience with Regard to Regulation of Insurance Tariffs

European Member States' regulators do not have the right to regulate insurance prices. It is worthwhile, therefore, to analyze the EU experience in order to draw possible conclusions that could be valuable in considering rate deregulation.

Insurance regulation in Europe aims to create an integrated insurance market so that insurers can better diversify their risks and attain more economies of scale, while allowing policyholders to benefit from increased competition and a wider choice of insurance products.

To this end, the EU legislature has attempted to remove regulatory barriers between Member States by introducing the principles of freedom of establishment and freedom to provide services.[246] In order to foster

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[243] *See* Appendix 1.

[244] *See supra* p. 126.

[245] *See* Appendix 1.

[246] The third non-life Council Directive 92/49/EEC, 1992 O.J. (L 228) and the third life Council Directive 92/96/EEC, 1992 O.J. (L 360) established a single system for the authorization and financial supervision of insurance companies by the Member State in which an insurer has its head office (the home Member State). The authorization issued by the home Member State allows an insurance company to conduct its business in the other European Member States, either by opening agencies or branches (freedom of establishment) or by offering services on a temporary basis (freedom to provide services). In general, the principle of freedom

competition in the single insurance market, the third non-life insurance Directive prevented insurance supervisory authorities from regulating insurance premium prices and policy conditions.[247]

Previously, most EU Member States had exercised considerable control over premiums by setting minimum or maximum prices or fixing price scales for some lines of insurance or even for all insurance lines.[248] In the Italian insurance market, for example, before the enactment of the "third generation" of Directives the principles of "authorization of admission" and of "control on tariffs" were well established in the industry.[249] Before deregulation, potential competition in the European insurance market was impeded by regulated tariffs that hampered insurance companies from competing on price.[250]

With the removal of national control over insurance tariffs, new insurance products can be introduced into the market without prior regulatory approval. In this way, insurers' efficiency increased and consumers benefited from lower prices.[251] Article 29 of the third non-life insurance Directive of 1992 provides that Member States cannot maintain or introduce systems of prior notification or approval of insurers' proposed increases in premium rates except as a part of general systems aimed at controlling prices.[252] Insurance companies in Europe are now free to set their rates without any state interference and to write insurance contracts on any terms they agree to with their policyholders. Efforts by Member States to control insurance prices have been censured by the European Commission. In 2000 the Italian government, due to the effects of motor insurance prices on inflation, imposed a one-year ban on any increase in premiums for certain policyholders whose rates were calculated on the

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of establishment and freedom to provide services are set out, respectively, in article 49 and article 56 of the Treaty on the Functioning of the European Union.

[247] Council Directive 92/49/EEC, art. 29, 1992 O.J. (L 228).

[248] European Commission, *Business Insurance Sector Inquiry* 20 (2007), http://ec.europa.eu/competition/sectors/financial_services/inquiries/interim_report_24012007.pdf.

[249] Giuseppe Turchetti & Cinzia Daraio, *How Deregulation Shapes Market Structure and Industry Efficiency: The Case of the Italian Motor Insurance Industry*, 29 GENEVA PAPERS ON RISK AND INS. 202 (2004).

[250] European Commission, *supra* note 248, at 36.

[251] *Id*. at 45.

[252] *See also* Council Directive 92/49/EEC, art. 29, 1992 O.J. (L 228) 16-17.

basis of accidents.[253] Additionally, the Italian government imposed a one-year freezing on all new policies that were calculated on the same basis.[254] The European Commission censured the measure.[255] According to the Commission, the price freeze was incompatible with the freedom to market insurance products within the European Union under the third non-life insurance Directive and was neither part of a general price-control system nor was it justified by the public interest.[256]

There is a legitimate concern that deregulation will obstruct setting accurate rates in the short run because insurers may not have sufficient loss experience on which to rely.[257] The European Union addressed this problem within the framework of the insurance Block Exemption Regulations. The first Block Exemption Regulation, Regulation 3932/92, was adopted by the Commission in 1992.[258] When this Regulation expired on March 31, 2003, the Commission replaced it with Regulation 358/2003.[259] Afterwards, when also this second Regulation expired, on March 31, 2010, the Commission adopted a new insurance block exemption Regulation, Regulation 267/2010.[260] The first Block Exemption Regulation was introduced following the *Verband der Sachversicherer* case, in which the European Court of Justice rejected arguments that full competition would cause more insurers' insolvencies and that, since cooperation between insurance companies was necessary to avoid such a risk, the applicability of Article 101 of the Treaty on the Functioning of the European Union (formerly Article 81 of the Treaty establishing the European Community)[261] should be limited.[262] Article 101(1) of the Treaty

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[253] If no accidents caused by the policyholders had occurred during a recent observation period. *See* art. 2, Legge 26 maggio 2000, n. 137, in G.U. 27 maggio 2000, n. 122 (It.).

[254] *Id*.

[255] *See* Press Release, Motor Insurance: The Commission Decides to Ask Italy to End Its Price Freeze (Oct. 25, 2000), http://europa.eu/rapid/pressReleasesAction.do?reference=IP/00/1210&format=HTML&aged=1&language=EN&guiLanguage=en.

[256] *Id*.

[257] *See supra* p. 132.

[258] *See* Commission Regulation 3932/92, art. 1, 1992 O.J. (L 398) 9 (EC).

[259] *See* Commission Regulation 358/2003, art. 1, 2003 O.J. (L 53) 11-12 (EC).

[260] *See* Commission Regulation 267/2010 2010, art. 2, 2010 O.J. (L 83) 5 (EU). This Regulation will expire on 31 March 2017. *See* Commission Regulation 267/2010 2010, art. 9, 2010 O.J. (L 83) 7 (EU).

[261] With effect from 1 December 2009, Article 81 of the EC Treaty has become Article 101 of the Treaty on the Functioning of the European Union. The

prohibits, *inter alia*, agreements between undertakings that prevent, restrict or distort competition within the EU common market by fixing prices and other trading conditions either directly or indirectly prices.[263]

The Commission, recognizing the importance of cooperation among insurance companies to produce pool data concerning the calculation of the average cost of covering a specified risk in the past, the frequency and the size of past insurance claims, exempted the joint compilation and distribution of calculations and studies from the application of article 101(1) of the Treaty.[264] The Commission also exempted other agreements in the insurance sector concerning the setting up and operation of industry (re)insurance pools for the common coverage of certain risks in the form of co-(re)insurance.[265]

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two articles are substantially the same. *See* Commission Regulation 267/2010, art. 1, fn. 2, 2010 O.J. (L 83) 1 (EU). Article 101(1) prohibits "all agreements between undertakings, decisions by associations of undertakings and concerted practices which may affect trade between Member States and which have as their object or effect the prevention, restriction or distortion of competition." *See* Consolidated Version of the Treaty on the Functioning of the European Union art. 101(1), Mar. 30, 2010, 2010 O.J. (C 83), 88. As an exception to this rule, Article 101(3) provides that the provisions contained in Article 101(1) may be declared inapplicable in case of agreements "which contribut[e] to improving the production or distribution of goods or to promoting technical or economic progress, while allowing consumers a fair share of the resulting benefit[s]", and which do not impose restrictions which are not indispensable to the attainment of these objectives and do not afford such undertakings the possibility of eliminating competition in respect of a substantial part of the products concerned. *See* Consolidated Version of the Treaty on the Functioning of the European Union art. 101(3), Mar. 30, 2010, 2010 O.J. (C 83), 88-89.

[262] *See* Case 45/85, Verband der Sachversicherer e.V. v. Comm'n of the European Communities, 1987 E.C.R. 405.

[263] *See* Consolidated Version of the Treaty on the Functioning of the European Union art. 101(1), Mar. 30, 2010, 2010 O.J. (C 83) 88.

[264] *See* Commission Regulation 267/2010, art. 2, 2010 O.J. (L 83) 5 (EU). According to paragraph 9 of the Preamble, access to past statistical data is essential in order to facilitate the pricing of risks and therefore the Commission considered cooperation in this area necessary. This can in turn facilitate market entry and benefit consumers. It is specified, however, that agreements on commercial premiums are not exempted. *See also* Commission Regulation 267/2010, pmbl. ¶ 9, 2010 O.J. (L 83) 2 (EU).

[265] *See* Commission Regulation 267/2010, art. 5, 2010 O.J. (L 83) 6 (EU). Commission Regulation 267/2010 did not renew the exemption granted by the previous Block Exemption Regulation for agreements on standard policy conditions and security devices. In particular, according to paragraph 3 of the

Unlike the old system where regulated tariffs prevented price competition, liberalization following the third non-life insurance Directive led to increased competition, particularly in formerly heavily-regulated markets such as Italy, Germany, Belgium and Portugal.[266] After price controls were abolished, premium rates decreased.[267] In particular, in countries such as Germany, Austria and Spain that used to have minimum premium regulation, price competition increased considerably.[268] In Germany, due to discounts and price reductions, premium income from motor insurance decreased from DEM 44 billion in 1995 to DEM 39 billion in 1998.[269] On the other hand, in countries such as Italy, Portugal and Greece, deregulation led to tariff increases in the motor liability sector in order to cover actual claim costs.[270] Deregulation permitted insurance companies in those countries to reach a balance between the risks underwritten and the premiums charged to cover potential losses. Previously, in those countries premiums had been artificially low in order to prevent inflationary pressure.[271]

The experience in countries like the United Kingdom and France, countries that had not regulated insurance prices and contractual terms before the Third Non-Life Insurance Directive confirms the benefits of rate deregulation.[272] In the United Kingdom, for example, market concentration has decreased as an immediate effect of deregulation. In 1981, the fifteen largest insurers operating in that country underwrote almost 80 percent of

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Preamble, the new Regulation does not grant an exemption for the establishment of standard policy conditions and the testing and acceptance of security devices because the Commission's review of the functioning of Regulation 358/2003 revealed that it was no longer necessary to include such agreements in a sector specific block exemption regulation. The Commission considered more appropriate that they be subject to self-assessment. *See also* Commission Regulation 267/2010, pmbl. ¶ 3, 2010 O.J. (L 83) 1 (EU).

[266] Autorità Garante della Concorrenza e del Mercato, *Gli Effetti Attesi della Liberalizzazione* 15-16 (2001), http://www.agcm.it/trasp-statistiche/doc_download/163-parte-i.html.

[267] Swiss Re, Sigma: Europe in Focus: Non-Life Markets Undergoing Structure Change, 3 (2000).

[268] *Id.*

[269] *Id.*

[270] *Id.*

[271] *Id.*

[272] Autorità Garante della Concorrenza e del Mercato, *Il Mercato*, 17 (2001), www.agcm.it/trasp-statistiche/doc_download/164-parte-ii.html (also stating that more recently the concentration ratios has increased due to insurance companies' reorganizations that have occurred recently).

the total premiums while in 1994, they underwrote about 65 percent of the total premiums.[273] Moreover, as a consequence of market liberalization, even more foreign insurance companies set up business in the United Kingdom.[274]

Following the deregulation of insurance prices and conditions, concentration, however, did not decrease. After deregulation in 1992, the largest insurers consolidated their positions in their national markets. Between 1990 and 1998 the combined market share of European multinational insurers (Allianz, Axa, Cgu, Generali, Royal & Sun Alliance, Winterthur and Zurich) in the six largest national markets (United Kingdom, Germany, France, Italy, Netherlands, Spain) increased from 18 to 39 percent.[275] In France in 1990, the combined market share of the five biggest insurance companies was about 40 percent, while in the second half of the nineties their market share increased to 57 percent.[276] The same trend appeared in Italy. In 1990, the top five insurers controlled almost half of the Italian market, while in 1999 they had a market share of 60 percent.[277] In Germany, the top five insurers had a market share of almost 32 percent in 1990 and 40 percent in 1999.[278] In the United Kingdom, the top five insurers controlled 32 percent of the market in 1994 and 55 percent in 1999.[279]

It is difficult to know whether deregulation accounts for that higher concentration. More likely, the reduction in the number of insurers in the European market resulted from the increasing number of mergers and acquisitions at the end of the 1990s.[280] For example, higher concentration ratios in Italy were due to the fact that Generali bought out INA in 1999, while in Germany they ensued from Generali's acquisition of AMB and AXA's takeover of Albingia.[281] Thus, it is unlikely that the increase in concentration ratios of the non-life European market resulted from deregulation. A case history of the motor insurance industry in Italy

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[273] *Id.*
[274] *Id.*
[275] Swiss Re, *supra* note 267, at 17.
[276] *Id.* at 22.
[277] *Id.* at 23-24.
[278] *Id.*
[279] *Id.* at 24.
[280] *See* European Insurance in Figures, CEA STATISTICS N° 36 (CEA Insurers of Europe, Brussels, Belgium available at http://www.cea.eu/uploads/Modules/Publications/1224519688_eif.pdf), Oct. 2008, at 25 [hereinafter 2008 CEA Statistics].
[281] Swiss Re, *supra* note 267, at 23-24.

following deregulation is also illustrative. The Italian auto insurance sector, which had been highly regulated by the government, was considerably affected by the change introduced by the third non-life Directive.[282] The same trend seen in the general European non-life insurance market appeared in the Italian auto insurance market. Between 1982 and 1991, the number of insurance companies grew from 97 to 113, but then dropped to 80 between 1991 and 2000.[283] The peak of the reduction occurred in the period after 1994, when the number of insurers declined from 105 to 80.[284] Entries in the market rose in the second half of the 1980s and decreased in the 1990s.[285] Conversely, the number of exits from the market decreased in the second half of the 1980s and increased in the 1990s.[286] The net entry in the market between 1994 and 2002 was -28.[287] The combined market share of the top 20 insurers also increased from 63.63 percent in 1982 to 79.87 percent in 2000.[288] From this, one might infer that deregulation in the Italian auto insurance market had a negative effect on competition. However, in a study conducted in 2001, the Italian Antitrust Authority concluded that net exits from the market were not due to deregulation because only some of the insurance companies that exited the market had financial problems.[289] Rather, the exits occurred because insurance companies were acquired by other companies and some insurers voluntarily ceased trading.[290] The number of insurers' insolvencies decreased with the deregulation of insurance tariffs. In 1993-1994 around ten companies were insolvent, but in 1995 that number dropped to six.[291] The reduction in the number of insurers' insolvencies might be a result of the fact that insurers were free to set the price of premiums at an adequate level to cover their costs. Indeed, one adverse effect of rate regulation is to weaken the relationship between premiums and expected loss costs;[292] deregulation, on the contrary, permits a better alignment of prices with costs.[293] Premiums rates went up and down until the first half of 1990s, while after tariffs

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[282] *See* Turchetti & Daraio, *supra* note 249, at 202.
[283] *Id.* at 203-04.
[284] *Id.* at 204.
[285] *Id.*
[286] *Id*. at 205.
[287] Autorità Garante della Concorrenza e del Mercato, *supra* note 272, at 35.
[288] *Id.* at 26.
[289] *Id*. at 36.
[290] *Id.* at 36-37.
[291] *Id.* at 36.
[292] Cummins, *supra* note 147, at 12; *see* Tennyson, *supra* note 177, at 14.
[293] *See* Cummins, *supra* note 147, at 2, 11.

deregulation they tended to increase.[294] Among the causes adduced to explain rates increase are (1) the rise in the average cost of compensation for damage that changed from € 1,923 to € 3,830 between 1994 and 2001; (2) the increase in cost of repairs; (3) the frequency of fraud and the considerable frequency of cervical spine lesions reported in around 66 percent of the claims.[295] Moreover, an efficiency analysis of forty-five Italian insurers in the motor insurance sector showed that the cost efficiency and the total productivity of these companies increased between 1982 and 2000, particularly in the second half of the 1990s after adoption of the third non-life Directive.[296]

Motor insurance aside, the other non-life lines in Italy experienced a decrease in rates from 1993 to 1996.[297] This trend toward lower rates was common throughout Europe as a consequence of increased competition.[298] For example, in Germany in 1997, strong competition among insurance companies resulted in falling rates.[299]

As for more general European insurance rate trends, total premiums for the overall countries represented by the European insurance and reinsurance federation (CEA)[300] grew in real terms by 1.2 percent in 2007, compared to an annual increase of 6.5 percent in the two previous years.[301] The slowdown in the rate of total premium increase was due to

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[294] Turchetti & Daraio, *supra* note 249, at 205.

[295] *Id.* at 207-08.

[296] *Id.* at 217.

[297] 5 SWISS RE, Sigma, *Upheaval in Insurance Markets – Results Still Good Despite Increased Competition, Forecast for the Biggest non-Life Markets in 1998 and 1999*, at 19 (1998), media.swissre.com/documents/1b477a804659d8e893f8df 4ba16c05ab-17 Aug 1998_Upheaval in insurance.pdf.

[298] *Id.* at 4.

[299] *Id.* at 14.

[300] The CEA (Comité Européen des Assurances) is the European insurance and reinsurance federation; its members are the national insurance associations in 32 European countries (Austria, Belgium, Bulgaria, Croatia, Cyprus, Czech Republic, Denmark, Estonia, Finland, France, Germany, Greece, Hungary, Iceland, Ireland, Italy, Latvia, Liechtenstein, Luxembourg, Malta, Netherlands, Norway, Poland, Portugal, Romania, Slovakia, Slovenia, Spain, Sweden, Switzerland, Turkey and United Kingdom). The statistical data presented in the text refer to the above-mentioned 32 countries beside Lithuania. COMITÉ EUROPÉEN DES ASSURANCES, http://www.cea.eu/.

[301] 2008 CEA Statistics, *supra* note 280, at 11. This part of the article considers 2007 data since 2008 and 2009 insurance premium data are affected by the impact of the financial crisis. Due to the financial crisis, gross written premiums declined by 6% in 2008. *See CEA Statistics No. 37: European Insurance*

strong competition between insurance companies in the non-life sector.[302] In the non-life sector premium growth in 2007 slowed down to 0.4 percent in real terms.[303] In Western Europe, eight out of fifteen markets experienced a decrease in premium volumes.[304] For example, in Germany and in the United Kingdom, which are the two largest European non-life markets, premium volume fell respectively 1.4 percent and 0.7 percent respectively.[305] The link between the general slowdown in total European non-life premiums and lower insurance rates could also be seen in the motor vehicle insurance line, which is the biggest line of non-life insurance in Europe, accounting for 31 percent of total premiums in 2007.[306] Motor insurance premiums declined by 0.4 percent in real terms in 2007 and by 2 percent in 2006.[307] This reduction was caused by lower rates due to strong competition between insurance companies.[308]

Thus, deregulation and the establishment of a single insurance market in Europe had positive effects by intensifying competition among

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*in Figures*, COMITÉ EUROPÉEN DES ASSURANCES 9 (Oct., 2009), http://www.cea.eu/upl oads/Modules/Publications/eif-2009.pdf [hereinafter 2009 CEA Statistics]. In 2009 the European insurance industry weathered the crisis better as to premium growth and total European premiums increased by 2.9%. *See CEA Statistics No. 42: European Insurance in Figures*, COMITÉ EUROPÉEN DES ASSURANCES 10 (Nov., 2010), http://www.cea.eu/uploads/Modules/Publications/1290503264_european-nsurance-in-figures.pdf [hereinafter 2010 CEA Statistics].

[302] 2008 CEA Statistics, *supra* note 302, at 11.

[303] *Id*. at 14.

[304] *Id*.

[305] *Id*.

[306] *See id*. at 15. *See also* 2009 CEA Statistics, *supra* note 301, at 14 (showing a decline in European motor insurance premiums in 2008 due to insurers' efforts to improve the value for money of products sold, the strong competition in the market and the decline in new car sales because of the economic crisis); 2010 CEA Statistics, *supra* note 301, at 15 (showing a decline in European motor insurance premiums in 2009 mainly due to the competitiveness of the market and the economic crisis); *Retail Insurance Market Study*, EUROPE ECONOMICS 100, 104-05 (Nov. 26, 2009), http://ec.europa.eu/internal_market/insurance/docs/motor/20100302rim_en.pdf (stating that Europe has the largest motor insurance market in the world, with almost € 119 billion motor insurance premiums in the EU27 in 2008) [hereinafter *Retail Insurance Market Study*].

[307] 2008 CEA Statistics, *supra* note 280, at 15.

[308] *Id*.

insurers.[309] Insurance companies were able to adjust their rates following deregulation, and there were not substantial rate increases.[310]

C. THE CASE FOR RATE DEREGULATION

The concern that deregulation could lead to monopolistic or oligopolistic pricing is controverted by the fact that the U.S. insurance market is competitive and does not require regulation of insurance rates.[311] Table 2 above, for example, shows no evidence of excessive profits by insurers.

Indeed, rate regulation in the U.S. may result in artificially low returns. According to an ISO analysis, the profitability of property and casualty insurers measured under generally accepted accounting principles (GAAP)[312] is lower than other industries.[313] The return on net worth of both large property and casualty insurance companies and the entire property and casualty insurance industry for the period 1983 to 2009 was lower than the return on net worth for the Fortune 500 combined companies except in 1986 and in 1987.[314] Other industries also had higher rates of return compared to the property and casualty insurance industry over that period.

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[309] *See Retail Insurance Market Study*, *supra* note 306, at xxi, 89-90 (analyzing the European motor insurance market).

[310] *See Id*.

[311] *See supra* pp. 134-39.

[312] The data reported in the annual statement filed by insurance companies with state Insurance Departments and the Internal Revenue Service are on a statutory accounting principles (SAP) basis, that tends to be more conservative than GAAP. Therefore, in order to make comparisons with other industries it is appropriate to consider the adjustment of the insurers' profitability on a GAAP basis. *See* THE INSURANCE FACT BOOK 2011, *supra* note 229, at 39.

[313] THE INSURANCE FACT BOOK 2011, *supra* note 229, at 39.

[314] *See* INSURANCE INFORMATION INSTITUTE, THE INSURANCE FACT BOOK 2009 33 (2009); THE INSURANCE FACT BOOK 2011, *supra* note 229, at 39.

**Table 3 – 2000-2009 Annual Rate of Return: Net Income After Taxes as a Percent of Equity**

| | Property and Casualty Insurance | | Selected Other Industries | | |
|---|---|---|---|---|---|
| Year | Statutory Accounting | GAAP Accounting | Commercial banks | Electric and gas utilities | Fortune 500 combined industrials and service |
| 2000 | 6.2 percent | 5.9 percent | 16.7 percent | 11.8 percent | 14.6 percent |
| 2001 | -2.0 percent | -1.2 percent | 14.0 percent | 10.5 percent | 10.4 percent |
| 2002 | 3.0 percent | 2.1 percent | 17.3 percent | 7.9 percent | 10.2 percent |
| 2003 | 8.3 percent | 8.8 percent | 14.9 percent | 10.5 percent | 12.6 percent |
| 2004 | 9.7 percent | 9.4 percent | 15.5 percent | 10.5 percent | 13.9 percent |
| 2005 | 10.9 percent | 9.6 percent | 16.0 percent | 10.0 percent | 14.9 percent |
| 2006 | 14.2 percent | 12.7 percent | 15.0 percent | 11.0 percent | 15.4 percent |
| 2007 | 12.0 percent | 10.9 percent | 11.0 percent | 11.0 percent | 15.2 percent |
| 2008 | 0.8 percent | 0.1 percent | 3.0 percent | 13.0 percent | 13.1 percent |
| 2009 | 6.2 percent | 4.7 percent | 4.0 percent | 9.0 percent | 10.5 percent |

Source: INSURANCE INFORMATION INSTITUTE, THE INSURANCE FACT BOOK 2011 39 (2011), reprinted with permission. (Source: SNL Financial LC; ISO; Fortune).

Calculating, from data in Table 3, the average rate of return on a GAAP basis for the property casualty insurance industry and the average rate of return for the Fortune 500 combined companies for the period 2000-2009, the return on average for the property and casualty insurers was 6.3 percent and 13.08 percent for the Fortune 500 combined companies.

Table 2 also raises questions about insurers' low profitability.[315] Although the market growth for commercial lines over the 2000-2009 period indicated that new insurers had incentives to enter the business,[316] nevertheless many insurers exited the market.[317] For example, 29 insurers exited the commercial auto liability market, 31 exited the workers'

[315] *See supra* Table 2.

[316] It is more appropriate to consider the market growth over the period 2000-2009 than just over the period 2007-2009 since 2007-2009 data may be affected by the impact of the 2008 financial crisis. As to the data for commercial property and casualty insurance before the financial crisis, *see infra* Appendix 2.

[317] *See supra* Table 2.

compensation market, 32 left the market for inland marine and 43 exited the allied lines market.[318] The fact that those insurers exited the market may suggest that they did not consider the market profitable enough to remain in business.[319]

It is difficult to establish for certain a direct causal link between this data and insurance rate regulation. At a minimum, rate regulation could be one of the causes depressing insurers' profitability.[320]

Rate regulation may affect insurers' profitability since it may limit insurers' ability to adjust their rates according to changes in market conditions. Insurers might need to raise rates when investment income dips or premiums are too low to absorb losses. Yet in prior approval systems insurers may experience delays or denials in getting approval for rate increases. There could also be political pressure on insurance commissioners to keep rates low.[321] A commissioner might grant approval for a rate increase lower than that requested by the insurer, either to attain the rate increase over a longer period of time or not at all. This can have adverse effects on insurance companies. Similar concerns surround file and use, use and file, flex rating and modified prior approval systems. With regard to the first two systems, the commissioner retains the right to disapprove the rates filed, while, with regard to the flex rating and modified prior approval system, both require prior approval if the rate change is larger than the specified percentage rate, or if the rate revision is based on a change in expense ratio or rate classifications. Because of the time and expense to meet the rate-filing requirements, insurance companies may have less-than-optimal opportunity to adjust their rates to changes in the

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[318] *See id.*

[319] In particular, with regard to commercial multiple peril insurance, inland marine and allied lines, more insurers exited the market than entered it (a net loss of 2 in the commercial multiple peril market, of 7 in the inland marine market and of 15 in the market for allied lines). *See supra* Table 2.

[320] *See* Cummins et al., *supra* note 215, at 42-44 (demonstrating by statistical regression analysis that insurance regulation led to significantly lower prices in the majority of states that were regulated during the sample period 1980-1996); Cummins & Harrington, *supra* note 215, at 60 (showing by multiple regression analysis that in competitive rating states loss ratios are significantly lower and average prices significantly higher); Scott E. Harrington, *A Note on the Impact of Auto Insurance Rate Regulation*, 69 REV. ECON. & STAT. 166, 169 (1987) (finding that auto insurance rate regulation increased average loss ratios during the sample period 1976-1981).

[321] *See supra* p. 135.

market.[322] While deregulating might result in higher rate volatility, it would permit insurance companies to set appropriate rates in response to changes in market conditions.

Deregulation would also allow insurers to eliminate the costs of complying with rate regulation and prior approval systems. Under the NAIC Property and Casualty Model Law, an insurer has to file with the insurance commissioners "every manual, minimum premium, class rate, rating schedule or rating plan and every other rating rule, and every modification of any of the foregoing which it proposes to use."[323] Further, insurers have to submit or incorporate by reference "all supplementary rating and supporting information to be used in support of or in conjunction with a rate," such as the insurers' interpretation of statistical data on which they relied, the experience of other insurance companies, and any other relevant information.[324] The commissioner, after reviewing the insurer's filing, may require that "the insurer's rates be based upon the insurer's own loss, special assessment and expense information," where the insurer's loss is not actuarially credible, the insurer "may use or supplement its experience with information filed with the commissioner by an advisory organization or statistical agent."[325] For insurers using the services of an advisory organization, the commissioner may require them to provide "a description of the rationale for such use, including its own information and method of utilization of the advisory organization's information."[326]

Rate filings, therefore, are a drain on insurers' time and resources. The process to approve rates can be invasive, lengthy, inaccurate and disputed.[327] Further, a commissioner's analysis of whether the rates are "excessive, inadequate or unfairly discriminatory" requires a considerable outlay of effort and resources by insurance department staff in order to consider past and prospective loss experience and expenses.[328] The same is

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[322] HARRINGTON, *supra* note 1, at 33.

[323] PROPERTY AND CASUALTY MODEL RATING LAW (PRIOR APPROVAL VERSION) § 5(A)(1) (2009) [hereinafter PRIOR APPROVAL MODEL LAW]; FILE AND USE MODEL LAW, *supra* note 240, at § 6(A)(1).

[324] PRIOR APPROVAL MODEL LAW, *supra* note 323, at § 5(A)(2); FILE AND USE MODEL LAW, *supra* note 240, at § 6(A)(2).

[325] *Prior Approval Model Law*, *supra* note 323, at § 5(A)(4); FILE AND USE MODEL LAW, *supra* note 240, at § 6(A)(4).

[326] *Prior Approval Model Law*, *supra* note 323, at § 5(A)(5); FILE AND USE MODEL LAW, *supra* note 240, at § 6(A)(5).

[327] HARRINGTON, *supra* note 1, at 31.

[328] *Prior Approval Model Law*, *supra* note 323, at § 4(B); FILE AND USE MODEL LAW, *supra* note 240, at § 5(A)(4).

true for a commissioner's determination of whether there is competition in the market.[329] Rate deregulation could allow insurance departments to fully devote themselves to other more important supervisory activities such as solvency supervision.[330]

In addition, the effect of rate regulation on the availability of insurance can be seen by analyzing the residual market. Generally, a declining residual market means that insurance is relatively more available in the voluntary market, and vice versa. Thus, it is of concern that residual market shares increase along with the degree of rate regulation. Table 4 compares the size of the voluntary market and the residual market by state for private passenger car insurance for the year 2008.

**Table 4 – Private Passenger Cars Insured in the Voluntary and Residual Market, 2008**

| State | Voluntary Market | Residual Market | Total | Residual market as a percentage of total |
|---|---|---|---|---|
| Alabama | 3,384,021 | 6 | 3,384,027 | < 0.001 percent |
| Alaska | 437,274 | 122 | 437,396 | 0.028 percent |
| Arizona | 4,130,900 | 20 | 4,130,920 | < 0.001 percent |
| Arkansas | 2,069,310 | 0 | 2,069,310 | < 0.001 percent |
| California | 24,127,758 | 5,941 | 24,133,699 | 0.025 percent |
| Colorado | 3,667,061 | 0 | 3,667,061 | < 0.001 percent |
| Connecticut | 2,442,996 | 487 | 2,443,483 | 0.020 percent |
| Delaware | 608,459 | 25 | 608,484 | 0.004 percent |
| D.C. | 221,678 | 457 | 222,135 | 0.206 percent |
| Florida | 11,288,408 | 6 | 11,288,414 | < 0.001 percent |
| Georgia | 6,789,526 | 3 | 6,789,529 | < 0.001 percent |
| Hawaii | 796,742 | 5,188 | 801,930 | 0.647 percent |
| Idaho | 1,068,562 | 38 | 1,068,600 | 0.004 percent |
| Illinois | 7,936,919 | 1,153 | 7,938,072 | 0.015 percent |
| Indiana | 4,578,960 | 6 | 4,578,966 | < 0.001 percent |
| Iowa | 2,398,138 | 9 | 2,398,147 | < 0.001 percent |

[329] FILE AND USE MODEL LAW, *supra* note 240, at § 4, 8.
[330] *See supra* p. 135.

| | | | | |
|---|---|---|---|---|
| Kansas | 2,349,365 | 1,327 | 2,350,692 | 0.056 percent |
| Kentucky | 3,013,470 | 64 | 3,013,534 | 0.002 percent |
| Louisiana | 2,834,988 | 7 | 2,834,995 | < 0.001 percent |
| Maine | 1,022,278 | 28 | 1,022,306 | 0.003 percent |
| Maryland | 3,792,401 | 73,328 | 3,865,729 | 1.897 percent |
| Massachusetts | 3,955,971 | 112,891 | 4,068,862 | 2.775 percent |
| Michigan | 6,164,846 | 1,297 | 6,166,143 | 0.021 percent |
| Minnesota | 3,746,861 | 5 | 3,746,866 | < 0.001 percent |
| Mississippi | 2,076,581 | 76 | 2,076,657 | 0.004 percent |
| Missouri | 4,195,783 | 41 | 4,195,824 | 0.001 percent |
| Montana | 775,934 | 230 | 776,164 | 0.030 percent |
| Nebraska | 1,501,473 | 4 | 1,501,477 | < 0.001 percent |
| Nevada | 1,793,132 | 23 | 1,793,155 | 0.001 percent |
| New Hampshire | 904,727 | 710 | 905,437 | 0.078 percent |
| New Jersey | 5,290,260 | 15,048 | 5,305,308 | 0.284 percent |
| New Mexico | 1,455,016 | 24 | 1,455,040 | 0.002 percent |
| New York | 9,233,103 | 92,283 | 9,325,386 | 0.990 percent |
| North Carolina | 5,607,617 | 1,442,470 | 7,050,087 | 20.460 percent |
| North Dakota | 592,814 | 4 | 592,818 | 0.001 percent |
| Ohio | 8,029,756 | 0 | 8,029,756 | < 0.001 percent |
| Oklahoma | 2,719,636 | 52 | 2,719,688 | 0.002 percent |
| Oregon | 2,724,683 | 9 | 2,724,692 | < 0.001 percent |
| Pennsylvania | 8,483,438 | 19,151 | 8,502,589 | 0.225 percent |
| Rhode Island | 663,890 | 9,335 | 673,225 | 1.387 percent |
| South Carolina | 3,294,512 | 1 | 3,294,513 | < 0.001 percent |
| South Dakota | 681,839 | 0 | 681,839 | < 0.001 percent |
| Tennessee | 4,187,461 | 24 | 4,187,485 | 0.001 percent |
| Texas | Data not available | Data not available | Data not available | Data not available |
| Utah | 1,808,234 | 2 | 1,808,236 | < 0.001 percent |
| Vermont | 474,881 | 450 | 475,331 | 0.095 percent |
| Virginia | 6,023,910 | 1,460 | 6,025,370 | 0.024 percent |
| Washington | 4,513,296 | 0 | 4,513,296 | < 0.001 percent |

| | | | | |
|---|---|---|---|---|
| West Virginia | 1,305,657 | 39 | 1,305,696 | 0.003 percent |
| Wisconsin | 3,674,130 | 0 | 3,674,130 | < 0.001 percent |
| Wyoming | 503,741 | 1 | 503,742 | < 0.001 percent |
| **Nationwide** | 185,342,396 | 1,783,845 | 187,126,241 | 0.953 percent |

Source: INSURANCE INFORMATION INSTITUTE, THE INSURANCE FACT BOOK 2011 71-72 (2011), reprinted with permission. (Source: Automobile Insurance Plans Service Office).

Of the states with a higher residual market share relative to the total private passenger cars insured in 2008, North Carolina (20.460 percent), Massachusetts (2.775 percent), and New York (0.990 percent) had strict rate regulation systems for automobile insurance.[331] North Carolina and New York had prior-approval rating laws with regard to auto-insurance,[332] while in Massachusetts until April 2008 auto insurance rates were set by the commissioner.[333] Conversely, some of the states with a lower residual market share were states with less restrictive rating systems like file and use or use and file: Arizona, Arkansas, Colorado, Indiana, Iowa, Minnesota, Nebraska (less than 0.001 percent), Delaware (0.004 percent), Idaho (0.004 percent), Illinois (0.015 percent).[334]

This suggests that rate regulation may have negative effects on insurance availability. Rate suppression, especially, may force insurers to tighten underwriting, forcing consumers to turn to the residual markets for coverage.[335] Understandably, insurers will not underwrite higher risk consumers if rates are too low to cover their possible costs. In the worst

[331] *But see* the cases of Maryland and Rhode Island having a quite high residual market share (1.897 percent and 1.387 percent respectively) even though they adopt less restrictive rating systems: file-and-use the former and flex-rating the latter.

[332] *See* NAIC, *Auto Insurance Database Report 2005/2006* 231, (2008) [hereinafter *Auto Insurance Database Report*]. In June 2008 the New York legislature approved flex-rating legislation for auto insurance providing that, subject to some conditions, overall average rate level increases or decreases of 5 percent above or below the previously filed rates may take effect without obtaining prior regulatory approval.

[333] *See supra* pp. 126-27.

[334] With regard to the rating systems for auto insurance adopted in the states, *see Auto Insurance Database Report*, *supra* note 332, at 231.

[335] Residual market mechanisms are statutory arrangements that permit to provide insurance to people considered ineligible for coverage in the voluntary market.

case rate suppression could cause insurers who cannot offset low rates with decreased costs to exit the market.[336] Consider, for example, the number of insurers who exited California following the introduction of Proposition 103[337] and Massachusetts, New Jersey and South Carolina because of strict rate regulation in the auto insurance market.[338] In particular, New Jersey, before 2003, had had a highly regulated automobile insurance market that prompted over 20 insurers to exit over a period of 10 years.[339] After the state enacted reforms in 2003 increasing competition in the market,[340] the number of insurance companies changed from 17 to 39, the availability of insurance increased, and insurance prices fell for most policyholders.[341] The same occurred in South Carolina where a less restrictive rating law was passed in 1999. Afterwards, the number of insurers offering automobile insurance almost doubled and the residual market share and rate levels fell.[342]

Deregulation of rates, therefore, would avoid problems with the availability of insurance by allowing insurers to charge an appropriate price to cover their costs and earn a reasonable profit. Although deregulation might lead to higher rates, the benefits of rate suppression are not worth the cost of restricted availability. While rate suppression may make insurance affordable in the short run, in the long run it will cause insurers to exit from the market with consequent problems for consumers and the social welfare. Instead, rate deregulation will result in appropriate prices for insurance

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[336] Harrington, *supra* note 118, at 189.

[337] Editorial, *California Smashup*, WALL ST. J., Nov. 15, 1988, at A22 (discussing the exit of forty insurance companies from California due to the enforcement of Proposition 103 rate rollback).

[338] Harrington, *supra* note 118, at 189.

[339] Tennyson, *supra* note 179, at 16.

[340] The Auto Insurance Reform Act approved in June 2003 (P.L. 2003, c. 89), introduced *inter alia* (i) the phase-out and final elimination of the "take-all-comers" provisions of the Fair Automobile Insurance Reform Act of 1990 (P.L. 1990, c. 8); (ii) amendments to the prior approval rate filing provision to establish a time-line for regulatory action; (iii) changes in the expedited rate filing procedure by raising the ceiling for rate increases; (iv) provisions that simplify the procedures to be used by insurers to withdraw from selling a particular type of insurance or to withdraw from the state; (v) measures to combat insurance fraud and provide for consumer protection and education. Further, the 2003 Act also amended the New Jersey's excess profits law, according to which insurers were prohibited from earning more than 6 percent in profits from the sales of auto insurance policies over a three-year period. The Act extended that period from three to seven years.

[341] Tenyson, *supra* note 179, at 16.

[342] HARRINGTON, *supra* note 1, at 22; Tenyson, *supra* note 179, at 16.

because insurance companies in a competitive market will supply products in the long run at prices equaling their average costs plus a reasonable profit.

Rate deregulation will also lead to more consumer choices because, by increasing the range of prices that insurers can charge, the range of products offered to policyholders should increase as well. Rate regulation limits consumer choice since, to implement a uniform price system, comparable rates must be charged for comparable products. Any effects on the ability of consumers to compare insurance rates can be addressed by increasing disclosure and enhancing regulation of insurance advertising and marketing.[343] In addition, standard policy conditions may also facilitate consumers in comparing insurance policies offered by different insurers.[344] This way, policyholders may acquire the knowledge they need to properly compare rates and make informed decisions, taking into account the price, the quality of the policy and the insurer's financial strength. Comparison shopping can be enhanced by the on-line availability of insurance quotations[345] and help of independent agents and brokers in assisting policyholders with price comparisons.[346]

One of the main objectives of rate regulation is to prevent insurance insolvencies that could result from ruinous competition. In the long term a competitive market should reach equilibrium where insurers charge premiums that equal their average costs. Insurance companies like all other enterprises strive to conduct a financially successful business so that they are most unlikely to charge rates not sufficient to cover incurred losses and expenses.

Even if that is not always the case, rate regulation has not avoided insurers' insolvencies. In the United States, around 340 property and

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[343] HARRINGTON, *supra* note 1, at 26.

[344] *Id*. at 44-45.

[345] *See, e.g.*, the Massachusetts Division of Insurance's website on auto insurance premium comparison, http://www.mass.gov/?pageID=ocaterminal&L=4&L0=Home&L1=Consumer&L2=Insurance&L3=Automobile+Insurance&sid=Eoca&b=terminalcontent&f=doi_AutorateCompare_autoratecompare&csid=Eoca. The website gives information on how to contact insurance companies and agents directly for quotes and allows consumers to compare premiums for new private passenger auto insurance across companies for seven policy examples by showing the range of prices and discounts they may qualify for.

[346] HARRINGTON, *supra* note 1, at 26-27.

casualty insurance companies became insolvent from 1986 to 2006.[347] Furthermore, there have been relatively fewer insolvencies in states with less restrictive rating laws than in those that highly regulate rates.[348] Of 79 insolvent insurance companies subject to rate regulation in the period 1946 to 1959, 26 were based in Texas, a state which used to have rate uniformity enforced by law.[349] California and Missouri that did not then regulate rates at all had only 3 insolvencies each.[350] Similar considerations can be inferred from the data concerning the number of insolvencies in the Italian auto insurance market for the period immediately following deregulation of tariffs.[351] Rate deregulation, therefore, is consistent with a financially healthy insurance industry. It permits flexibility in the price of insurance and allows insurers to charge appropriate rates in connection with possible market changes and, ultimately, to set rates more aligned with costs, thereby enhancing insurers' financial strength.

## CONCLUSION

Rate regulation seems to be based more on an historical tradition than on solid economic arguments. Although deregulation might seem bold in the current financial crisis, it is important to distinguish between the need for rate regulation and the desirability of more effective solvency regulation. Solvency concerns can be addressed by focusing on insurers' reserves and increasing the monitoring of the financial conditions of insurers. For these reasons rate freedom should replace regulation of rates.

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[347] American Academy of Actuaries, *Risk Focused Surveillance Framework* 14 (2006), http://www.naic.org/documents/committees_c_catf_aaa_risk_focused_surveillance.doc.

[348] CRANE, *supra* note 189, at 95.

[349] *Id*.

[350] *Id*.

[351] *See supra* p. 148.

## Appendix 1

### Rate Filing Methods

| STATE | FILING METHOD | LINES |
|---|---|---|
| Alabama | file and use<br><br>prior approval | commercial lines, title<br>medical malpractice,<br><br>personal lines, property and inland marine, casualty and surety, workers' compensation |
| Alaska | prior approval<br><br>flex rating on rate changes<br><br><br><br>file and use rate changes | medical malpractice, title workers' compensation, assigned risk rates<br><br>all property and casualty lines except workers' compensation, medical malpractice, assigned risk<br><br>all property and casualty lines except workers' compensation, medical malpractice, assigned risk |
| Arizona | file and use<br><br>use and file | workers' compensation, title<br><br>other property and casualty lines |
| Arkansas | file and use (competitive market); prior approval (non-competitive market)<br><br>no filing<br><br>prior approval | personal lines and small commercial risks<br><br>large commercial risks<br><br>workers' compensation |
| California | prior approval<br><br>file and use | all property and casualty lines<br><br>Title |
| Colorado | prior approval<br><br>file and use<br><br>no file; must maintain documentation | workers' compensation loss cost filing by a rating organization; auto assigned risk<br><br>all other property and casualty lines, except exempt commercial policyholders, title<br><br>exempt commercial policyholders |

| | | |
|---|---|---|
| Connecticut | file and use<br><br>prior approval | commercial lines (exception), personal lines<br><br>medical malpractice (for rate increasing 7.5 percent or more over last rates filed), title |
| Delaware | file and use | all lines except title |
| District of Columbia | file and use<br>prior approval | all lines<br>workers' compensation and medical malpractice |
| Florida | file and use or use and file<br><br>prior approval<br><br>rate set by the Commissioner | all lines except title and workers' compensation<br><br>workers' compensation<br><br>title |
| Georgia | prior approval<br>file and use<br>no file | personal private passenger auto<br>other property and casualty lines<br>large commercial risks |
| Hawaii | prior approval | property and casualty lines |
| Idaho | prior approval<br><br>use and file | workers' compensation, title<br><br>other property and casualty lines |
| Illinois | use and file<br><br>file and use | private passenger auto, taxicabs,motorcycles, homeowners,allied lines, dwelling fire, liquor liability, workers' compensation<br><br>medical malpractice, group inland marine |
| Indiana | file and use<br><br>modified file and use | property and casualty lines<br><br>workers' compensation |
| Iowa | prior approval<br><br>use and file | workers' compensation, other property and casualty lines, title<br><br>homeowners, private passenger auto |
| Kansas | prior approval<br><br>file and use<br><br>no file | workers' compensation<br><br>personal and commercial lines<br><br>large commercial insured, medical malpractice |

| | | |
|---|---|---|
| Kentucky | use and file (competitive market); prior approval (non-competitive market); prior approval of any rates which when combined with any rating factors effectively change pre-tax premium of any particular policy by more than +/- 25 percent in any 12-month period of time<br><br>no file<br><br>file and use | personal lines, auto guaranty, credit, medical malpractice, workers' compensation<br><br>other commercial lines<br><br>title |
| Louisiana | prior approval<br><br>no file | all property and casualty lines<br><br>workers' compensation (competitive market) |
| Maine * | modified file and use<br><br>no filing<br><br>prior approval | property and casualty lines, title<br><br>large commercial risks<br><br>workers' compensation |
| Maryland | file and use<br><br>prior approval | lines designated by the commissioner as competitive<br><br>property and casualty lines, title |
| Massachusetts | file and use or set by the commissioner<br><br>file and use | motor vehicle (filing method based on finding of existence of competitive market by commissioner)<br>all other lines |
| Michigan | file and use<br><br>prior approval | auto, homeowners, workers' compensation, inland marine, title<br><br>property excluding auto and homeowners |
| Minnesota | file and use<br><br>prior approval | all lines except workers' compensation<br><br>workers' compensation |
| Mississippi | prior approval | property and casualty lines |
| Missouri | informational filing only<br><br>use and file | commercial property and casualty lines<br><br>other property and casualty lines, workers' compensation |

| | | |
|---|---|---|
| Montana | file and use | property and casualty lines, title |
| Nebraska | file and use<br><br><br><br>prior approval | personal lines, workers' compensation, most commercial lines,<br>crop, professional liability, excess and large deductible workers' compensation<br><br>medical professional liability, title |
| Nevada | prior approval<br><br>prior approval<br><br>file and use<br><br>file and use | all personal lines, medical professional liability rates, except surety<br><br>workers' compensation loss costs and assigned risk rates<br><br>workers' compensation loss cost multipliers and supplementary rate information<br>title |
| New Hampshire | file and use (competitive market); prior approval (non-competitive market)<br>use and file<br><br>prior approval<br><br>no filing<br><br>use and file<br><br>prior approval<br><br>no filing required | personal lines (competitive market)<br><br>commercial lines (competitive market), workers' compensation<br><br>commercial lines (non-competitive market)<br><br>ocean marine, aircraft, financial guaranty, boiler and machinery<br>title<br><br>workers' compensation<br><br>ocean marine, aircraft, financial guaranty, boiler and machinery |
| New Jersey | use and file<br><br>prior approval | commercial lines<br><br>other property and casualty lines, workers' compensation, title |
| New Mexico | prior approval<br><br><br><br>no file<br><br><br>commissioner-set rates | property and casualty lines (non-competitive markets, reverse competitive and residual markets), workers' compensation<br>property and casualty lines ( competitive markets except workers' compensation and medical professional liability)<br>title |

| | | |
|---|---|---|
| New York | prior approval | workers' compensation, title, medical malpractice, personal and commercial lines |
| | flex rating | auto |
| | file and use | other property and casualty lines |
| North Carolina | prior approval | personal auto, homeowners |
| | modified file and use | commercial property and casualty lines |
| | file and use | workers' compensation, title |
| North Dakota | prior approval | all lines except workers' compensation and aircraft |
| Ohio | file and use | all other lines |
| | file and use (competitive market) prior approval (non-competitive market) | commercial casualty |
| | file and use | medical malpractice |
| Oklahoma | use and file | property and casualty lines (competitive market) |
| | file and use | property and casualty lines (non-competitive market), medical malpractice |
| Oregon | flex rating | commercial casualty |
| | prior approval | workers' compensation, title |
| | file and use | other property and casualty lines |
| Pennsylvania | prior approval | property and casualty lines |
| | exempt from filing | large commercial risks |
| | file and use | small commercial risks |
| Rhode Island | file and use | casualty, property, title |
| | prior approval | workers' compensation |
| | no file | large commercial risks |
| | flex rating | casualty insurance, fire and marine |
| South Carolina | prior approval | all lines |
| | prior approval or file and use | commercial auto rate changes of 7 percent or less |

| | | |
|---|---|---|
| South Dakota | no file<br><br>file and use<br><br>prior approval | large commercial risks<br><br>all lines except title<br><br>title |
| Tennessee | prior approval<br><br>use and file<br><br><br><br>file and use | personal lines, workers compensation<br><br>commercial lines, workers compensation loss cost multipliers<br><br>title |
| Texas | file and use<br><br>commissioner sets rates | all lines<br><br>title |
| Utah | use and file<br><br>file and use | property and casualty lines<br><br>title, workers' compensation |
| Vermont | prior approval<br><br>use and file | workers' compensation, auto (assigned risk), property and casualty lines ( non-competitive market)<br>property and casualty lines (except claims made and assigned risk), title and other types of workers' compensation (voluntary market) |
| Virginia | prior approval<br><br>no file<br><br>file and use (competitive market)<br><br>60 days prior filing requirement for non-competitive lines | residual market for workers' compensation and automobile; home protection, credit property, credit involuntary unemployment<br><br>large commercial risks, title<br><br>general liability, homeowners, fire, miscellaneous property and casualty, boiler and machinery, surety, credit, inland marine, farm owners', mortgage guaranty<br>commercial multi-peril;<br>professional liability and legal services<br>property and casualty lines identified by commissioner after hearing |

| | | |
|---|---|---|
| Washington | prior approval<br><br><br><br>use and file<br><br><br><br><br>file and use | property and casualty (except commercial lines),<br>medical malpractice,<br>workers' compensation<br>commercial lines<br><br><br><br><br>title |
| West Virginia | prior approval<br><br>file and use | other property and casualy lines, excluding workers' compensation<br>commercial lines |
| Wisconsin | use and file<br><br>prior approval | property and casualty, title<br><br>workers' compensation |
| Wyoming | prior approval<br><br>no filing (competitive market); prior approval (non-competitive market) | title, medical malpractice<br><br>property and casualty |

SOURCE: NAIC, 2 COMPENDIUM OF STATE LAWS ON INSURANCE TOPICS, HEALTH/LIFE/PROPERTY/CASUALTY II-PA-10-1–II-PA-10-20 (2010), reprinted with permission. The NAIC does not endorse any analysis or conclusions based on use of its data; NAIC, 2 COMPENDIUM OF STATE LAWS ON INSURANCE TOPICS, HEALTH/LIFE/PROPERTY/CASUALTY II-PA-10-9 (2008), reprinted with permission. The NAIC does not endorse any analysis or conclusions based on use of its data.

## Appendix 2

### 2007 Commercial Lines Data – Countrywide

| LINE OF BUSINESS | PREMIUMS WRITTEN | MARKET SHARES FOUR LARGEST GROUPS | HHI BASED ON PREMIUM | NUMBER OF SELLERS (GROUPS) | NUMBER OF ENTRIES LAST 5 YEARS | NUMBER OF EXITS LAST 5 YEARS | MARKET GROWTH LAST 3 YEARS | MARKET GROWTH LAST 10 YEARS | RETURN ON NET WORTH 10-YEAR MEAN |
|---|---|---|---|---|---|---|---|---|---|
| Commercial Auto Liability | 22,071,577,526 | 27.64 percent | 308.6 | 103 | 28 | 35 | 3.50 percent | 62.76 percent | 6.45 percent |
| Commercial Auto Physical | 7,255,767,155 | 24.45 percent | 260 | 114 | 24 | 29 | 6.44 percent | 34.54 percent | 11.72 percent |
| Commercial Auto Total | 29,327,344,681 | 25.89 percent | 281.5 | 109 | 27 | 33 | 4.24 percent | 54.73 percent | 7.39 percent |
| Commercial Multiple Peril | 36,138,799,711 | 26.75 percent | 327.8 | 105 | 36 | 34 | 4.52 percent | 68.36 percent | 7.00 percent |
| Fire | 12,235,775,465 | 38.74 percent | 579.2 | 95 | 32 | 29 | 26.33 percent | 152.40 percent | 17.39 percent |
| Allied Lines | 11,399,110,261 | 42.38 percent | 621.6 | 85 | 29 | 37 | 48.72 percent | 242.60 percent | 8.41 percent |
| Inland Marine | 15,408,763,035 | 33.44 percent | 450 | 78 | 25 | 30 | 21.02 percent | 111.90 percent | 18.46 percent |
| Medical Malpractice | 11,684,425,721 | 25.27 percent | 289.9 | 99 | 41 | 25 | 4.24 percent | 87.39 percent | 6.15 percent |
| Other Liability | 54,845,528,333 | 38.39 percent | 627.9 | 88 | 36 | 25 | 1.28 percent | 126.30 percent | 5.28 percent |
| Workers Compensation | 52,247,498,240 | 34.20 percent | 425.5 | 104 | 35 | 37 | 5.77 percent | 71.94 percent | 6.76 percent |

SOURCE: NAIC, 2007 Commercial Lines Competition Database Report 13 (2008), reprinted with permission. The NAIC does not endorse any analysis or conclusions based on use of its data.