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Comments of the Center or Economic Justice

To the NAIC Property Casualty (C) Committee

Personal Auto Pandemic Windfall Profits and Premium Relief

December 14, 2021

I'd like to make four points today based upon CFA and CEJ's 21 months of research and analysis since the beginning of the pandemic and nearly 100 years of combined experience in insurance ratemaking. In doing so, I respond to the insurer trades' public relations effort on behalf of insurers.

First, the bulk of the industry arguments are extreme efforts to distract from basic fact that the pandemic led to such reduced driving that auto insurance claims and claim payments declined by 20% from expected levels and that rates became excessive by over 40 billion in 2020 annually nearly overnight. The remainder of the arguments are fabrications. We should add that insurers padded their reserves and the actual amount of claim reduction was even greater than reported.

Second, it was completely foreseeable that insurers would realize windfall profits absent regulatory guidance. Our projections of reduced claim costs in March and April, without even having access to the granular data of insurers, were remarkably accurate. And we accounted for potential increased costs resulting from payment grace periods.

Third, it was also clear that traditional actuarial ratemaking methods and traditional regulatory rate filing approaches were not suited to the problem. I'd note that the CFA CEJ analyses are consistent with the principles offered by Mr. Gibson.

Fourth, in addition to attempting to recoup some of the 2020 windfall profits for consumers, we hope you will address the limitations in regulatory resources and authority to address a situation like this in the future.

Doug Heller has shown you the actual premium and claim results for 2016 to 2020 for personal auto insurance. The rates in effect at the beginning of March 2020 anticipated $175 billion of claims out of an expected $260 billion in premium. The reported incurred claims for 2020 by insurers were about 35 billion, or 20%, less than expected.

A significant portion of insurer expenses are variable – meaning the expenses increase with higher claim payments and decrease with lower claim payments. So a reduction in claims costs of 35 Billion means a reduction in premium of even higher amount.

Again, analyzing annual statement data reported by insurers, rates and premiums for personal auto in 2020 were excessive by over $40 billion before insurer premium relief and by about $30 billion after premium relief. That $30 billion windfall profit represents over $125 per insured vehicle or over 10% of total premium. I should add that public insurers' quarterly and annual reports to investors are consistent with our analysis.

APCIA asks you to look at the trees and avert your gaze from the forest. They cite the tragic increase in traffic fatalities. Yes, with fewer cars on the road, those driving drove faster and traffic fatalities increased. But any increase in claim severity was dwarfed by the reduction in claim frequency.

APCIA argues that claim severity increased dramatically in late 2020 and into 2021, falsely suggesting that insurers were somehow losing money in later 2020 and into 2021. But APCIA itself provides the data disproving the assertion – their chart showing personal auto loss ratios over time shows that after the massive drop in 2020 from long term results, insurers' 2021 results to date are simply returning to the long term – and reasonable rate – average.

APCIA argues that late 2020 and 2021 results offset early 2020 declines in claims. Again, the actual data refute this preposterous claim. Insurers haven't lost 40 billion in 2021. Indeed, Progressive today reported 11 month results with healthy $3 billion in profit for the year to date.

APCIA's argument about instability and short term fluctuations is also ridiculous. Insurers haven't acted with the long-term approach espoused by APCIA – they pocketed the windfall profits in 2020 and are not using those windfall profits to offset increasing claim costs in 2021 – they're seeking rate increases. APCIA is false equating a 20% reduction in claims in 2020 with a few percentage point increase in 2021.

More important, insurers' actions show why regulatory guidance was and is needed. There is no factual dispute that insurers received massive windfall profits in 2020. Did they hold on to these excess profits in anticipation of increasing claim costs? No, they gave the windfall profits to investors or management. Market forces did not compel insurers to give up all the windfall profits back to policyholders. But, now in 2021, insurers are aggressively seeking and obtaining rate increases based on the current situation with no reference to the 2020 windfall profits. In fact, insurers' rate filing tell regulators that 2020 was an anomaly and that experience should be ignored.

NAMIC also seeks to divert attention from the fact of windfall profits. NAMIC claims, without a bit of irony, that CFA and CEJ ignore key facts. Yet nowhere in the NAMIC presentation is any mention of the fact that the actual reported 2020 personal auto loss ratio was over ten points lower than historical and expected results – in a market that, as Mr. Gibson points out, loss ratios are typically a couple of points above or below a long-term average.

Of course, neither NAMIC or APCIA mention expense savings realized by insurers from having employees work from home, the virtual elimination of business travel costs and the efficiencies from rapid increases in digital claims settlement.

The 2020 windfall profits were clearly foreseeable by mid-March 2020. We saw Warrant Buffet talk about the reduced claim counts in a television interview in mid-March. Of course insurers could see, in real time, how the number of new claims filed was far lower than historical levels and far lower than expected. Insurers know how many claims they receive on any day of the year and how that compares with the prior week, month or year. If insurers can rely on limited inflation experience to justify rate increases, surely they could have relied upon limited claims reduction experience and other data to offer meaningful premium relief.

Insurers can quickly file for rate increases whenever they anticipate any increase in costs, but there is no mechanism for regulators to quickly order premium relief or rate reductions when a rare event occurs that dramatically reduces claim costs from levels anticipated in rates.

As we pointed out in March 2020, traditional actuarial methods were not suited to the situation caused by the pandemic. When insurers establish rates, they seek to predict expected costs during the period the rates will be in effect and they do this generally by extrapolating historical experience into the future. Ratemaking is premised on slow changes from historical to future, absent some major policy change like major changes in the civil justice system. As the pandemic unfolded, it was obvious that the historical data insurers relied upon to set prospective rates was no longer a guide. Again, we see the irony of the situation as today insurers urge regulators to ignore 2020 experience as they seek approval of rate increases. APCIA's call for a long-term perspective rings hollow given insurers actions.

The fact that traditional actuarial approaches did not and could address the situation raised by the pandemic meant a new approach was needed. CFA and CEJ recommended that rates in effect as of March 1, 2020 be frozen and that insurers provide premium relief based on monthly assessments of claims experience relative to historical periods. And, many insurers followed this approach, but most for only a couple of months. Critically, some insurers provided no premium relief and those insurers were generally non-standard insurers serving communities of color.

We urged regulators to start collecting data from insurers not just so regulators could track changes in new claims arising from historical periods as the pandemic unfolded, but to aggregate these data to help small and medium-sized insurers whose experience might be limited. While the NAIC did decide to collect data – it was on business interruption claims – and not on personal auto.

We also identified the limitations of traditional rate regulation – it was impractical and unreliable for regulators to declare all insurers' rates excessive and require immediate rate filings. So we urged you to use the approach of monthly premium relief until traditional ratemaking approaches could be employed.

So going forward, we suggest the lessons learned from the pandemic include the need for new regulatory tools – more timely data collection to better monitor the market and clear statutory authority to freeze rates and move to a monthly premium relief program during an emergency. Surely, if regulators can direct insurers not to cancel or non-renew a policyholder for a limited time for failing to pay premium, you should be able to require premium relief if a pandemic or other event causes a radical and sudden change to expected claim activity.