July 27, 2011

Hon. Kamala D. Harris
Attorney General
1300 I Street, 17th Floor
Sacramento, California 95814

Attention: Ms. Dawn McFarland
Initiative Coordinator

Dear Attorney General Harris:

Pursuant to Elections Code Section 9005, we have reviewed a proposed statutory initiative relating to automobile insurance discounts (A.G. File No. 11-0013, Amdt. #1-S).

Background

Automobile insurance is one of the major types of insurance purchased by California residents. It accounted for about $21 billion (19 percent) of all premiums collected by California insurers in 2010.

State Regulation of Automobile Insurance. In 1988, California voters passed Proposition 103, which requires the Insurance Commissioner to review and approve rate changes for certain types of insurance, including automobile insurance, before changes to the rates can take effect. Proposition 103 also requires that rates and premiums for automobile insurance policies be set by applying the following rating factors in decreasing order of importance: (1) the insured's driving safety record, (2) the number of miles they drive each year, and (3) the number of years they have been driving.

The Insurance Commissioner may adopt additional rating factors to determine automobile rates and premiums. Currently, 16 optional rating factors may be used for these purposes. For example, insurance companies may provide discounts to individuals for maintaining coverage with them. Insurance companies are prohibited, however, from offering this kind of discount to new customers who switch to them from other insurers.

In addition, Proposition 103 contains a provision related to individuals who were previously uninsured. Specifically, Proposition 103 prohibits insurance companies from using the information that an individual did not previously have automobile insurance to: (1) determine whether the individual is eligible for coverage or (2) decide the premiums charged for coverage.

Insurance Premium Tax. Insurance companies doing business in California currently pay an insurance premium tax instead of the state corporation tax. The premium tax is based on the amount of insurance premiums earned in the state each year for automobile insurance as well as for other types of insurance coverage. In 2010, insurance companies paid about $500 million in premium tax revenues on automobile policies in California. These revenues are deposited into the state General Fund.

Proposal

This measure amends Proposition 103 to allow an insurance company to offer a "continuous coverage" discount on automobile insurance policies to insurance consumers if they have continuously followed the mandatory insurance law. Under this measure, continuous coverage means uninterrupted automobile insurance coverage. Consumers with a lapse in coverage would still be eligible for this discount, however, if the lapse was:

- Not more than 90 days in the past five years for any reason.
- For no more than 18 months in the last five years due to loss of employment resulting from layoff or furlough.
- Due to active military service.

Also, children residing with a parent could qualify for the discount based on their parent's eligibility.

If an insurance company chose to provide such a discount, it would be provided on a proportional basis. The discount would be based on the number of years in the immediate previous five years (rounded to a whole number) that the customer was insured. For example, if a customer was able to demonstrate that he or she had coverage for three of the five previous years, the customer would receive 60 percent of the total continuous coverage discount.

Fiscal Effects

This measure could result in a change in the total amount of automobile insurance premiums earned by insurance companies in California and, therefore, the amount of premium tax revenues received by the state. On the one hand, the provision of continuous coverage discounts could reduce premium tax revenues received by the state. This would depend, however, on the extent to which insurers chose to offer such discounts to their customers, and the size of the discounts provided. On the other hand, insurers offering such discounts could make up for some or all of these discounts by charging higher premiums to some of its other customers.

The net impact on state premium tax revenues from this measure would probably not be significant. This is because overall premiums are predominately determined by other factors—

such as driver safety, the number of miles driven, and years of driving experience—which are unaffected by the measure.

Summary of Fiscal Effects. Our analysis of the fiscal effects of this measure is as follows:

- Probably no significant fiscal effect on state insurance premium tax revenues.

Sincerely,

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Mac Taylor
Legislative Analyst

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Ana J. Matosantos
Director of Finance