STATE FARM INSURANCE COMPANIES

OPPOSITION TO SB 816 (MOTOR VEHICLE INSURANCE – RATE FILINGS -TRADE SECRETS AND FACTORS USED TO ESTABLISH RATES

Trade Secret Protection

SB 816 would eliminate the trade secret protection from public disclosure provided under current law for State Farm's proprietary rating models filed with the Maryland Insurance Administration in connection with a rate filing. Proprietary rating models are critical to a company's competitive position in a robust, open market. While the Maryland Insurance Administration has unrestricted access to these models in reviewing a company's rate filings, it is vitally important that these models not be available to the public at large because that would allow competitors to see and utilize each other's proprietary information.

State Farm's size allows it to amass large volumes of insurance premium and loss data, making its models more precise and predictive than those of many competitors. As a result, competitors with less credible data would like to obtain information about our models and exploit our data.

The elimination of proprietary trade secret protection in current Maryland is likely to result in the use of more generic rating models that are available publicly, which limits price competition, compresses risk segmentation and provides fewer choices to customers in pricing as well as between carriers.

As trade secrets, these models should continue to be considered confidential under the Public Information Act, which has always protected trade secrets and competitively sensitive proprietary information obtained by a state agency from public disclosure. State Farm has committed significant resources to the development of pricing and underwriting sophistication through its pricing models. These are precisely the type of business innovation which should be protected as trade secrets in a competitive market.

Rating Territories

SB 816 would limit the number of territories that an insurer can use to establish rates to five territories. Consistent experience has shown the residence address has a clearly demonstrable effect upon the probability of loss. Legislation attempting to regulate an insurer's use of territories or geographical location, including the establishment of uniform territories, would be detrimental to matching price to risk.

Critics of the current system of basing premiums on geographical territories do not dispute the fact that accident rates vary from one area to another. However, some maintain that basing premiums on geography is socially undesirable and unfair, even though it can be justified by accident statistics. It is argued those who live in large cities are not individually responsible for the high loss costs, and, therefore, should not be penalized for something they cannot control. These critics would like to see the same premiums charged throughout a state so the impact of high loss costs in larger cities would be distributed among policyholders statewide in order to “spread the risk.” Private insurance does not "spread the risk;" it is a transfer of individual risk. The effect of "spreading the risk" using methods advocated by critics would be that insurance premiums in large cities would drop while those in smaller towns and rural areas would increase. Any such departure from cost-based pricing causes unjustified rate increases and adversely affects the competitive market.

The purpose of establishing separate rates by geographic location is to create equity among the individual policyholders of the company. State Farm develops rates based on the loss experience of the particular area. The environment in which a consumer resides exerts a powerful influence on the probable loss experience of policyholders in that area. Loss frequency combines with factors such as the cost of repairs, medical and hospital costs, attorney involvement, the size of jury awards, and other factors to produce the total costs which are reflected in insurance premiums charged in the area.

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