INSURANCE INFORMATION INSTITUTE

TRIPLE-I TALKING POINTS: FAIR 2.0 & Risk-Based Pricing

Updated: July 1, 2021

Issue overview: Insurance policies are priced based on extensive evidence collection and analysis. To educate the public on the issue, the Triple-I's Future of American Insurance and Reinsurance (FAIR) campaign will focus this year on risk-based pricing.

Accurately measuring and pricing risk allows insurers to provide accessible, affordable products. Working with regulators, technologists, and academics, insurers continue to refine underwriting models using advanced analytics and artificial intelligence to improve predictive models and ensure insurance policies closely reflect customer behavior and are priced fairly and accurately. Insurers are on a constant mission to make the cost of insurance more reflective of individual risk and responsibility. This is a commitment that is also safeguarded by robust market competition protecting consumers from unfair pricing.

Key idea: Risk-based pricing is essential to making sure lower-risk policyholders pay less.

Talking Points:

- Insurers' rigorous data analysis allows them to understand the risks they are assuming on behalf of a policyholder and then price accurately the policies insurers sell. Both criteria must be met for risk-based pricing to exist.

- Given the close regulatory scrutiny insurers face, the cost of insurance policies in the U.S. are neither excessive, inadequate, or unfairly discriminatory.

- Actuarial studies indicate how a person manages his or her financial affairs, which is what an insurance score captures, is a good predictor of whether they will file a claim.
    - Insurance scores are not the same as credit scores**.** Credit scores predict credit delinquency whereas insurance scores predict insurance losses. Both are based on a person's credit report.

- Auto insurance premiums are calculated using many factors—and some insurers give more weight to some factors than others. The cost of an auto insurance policy is generally determined by the amount of coverage, types of coverage chosen and other factors such as what you drive, where you live, your driving record, sex, age and credit history.

- Decreasing accuracy can result in lower-risk policyholders paying higher premiums and higher-risk policyholders paying lower premiums. Aside from being unfair, that system could ultimately result in higher insurance prices, increased property damages, and more injuries and fatalities.

- Accurate pricing is the ultimate goal of ratemaking and underwriting. Accurate prices provide financial stability for companies; meanwhile it also places the cost of risk on those creating the most exposure. Conventional wisdom seems to indicate that when policyholders bear the cost of their own risk, they will more likely behave in less risky behavior.