

**DEPARTMENT OF INSURANCE**

300 Capitol Mall, 17th Floor  
Sacramento, CA 95814

**RATE REGULATION ADVISORY NOTICE 2005-02**

**Date:** May 2, 2005

**To:** All Property and Casualty Insurers Subject to Proposition 103  
and Other Interested Persons

**Subject:** Use of Discounts in Determining Private Passenger Automobile Insurance  
Rates and Premiums

The purpose of this Advisory Notice is to remind all property and casualty insurers subject to the provisions of Proposition 103 and other interested persons about the provisions of Proposition 103 and related implementing regulations governing premium discounts.

California Insurance Code Section 1861.02(a) provides as follows:

Rates and premiums for an automobile insurance policy ... shall be determined by application of the following factors in decreasing order of importance:

- (1) The insured's driving safety record.
- (2) The number of miles he or she drives annually.
- (3) The number of years of driving experience the insured has had.
- (4) Those other factors that the commissioner may adopt by regulation and that have a substantial relationship to the risk of loss.

Title 10, California Code of Regulations, Section 2632.2(a) defines the term "rating factor" as any factor, including discounts, used by an insurer which establishes or affects the rates, premiums, or charges assessed for a policy of automobile insurance.

Title 10, California Code of Regulations, Section 2632.5(d) sets forth 16 optional rating factors which insurers may include in their class plan applications and may use if the class plan application is approved by the Commissioner.

Title 10, California Code of Regulations, Section 2632.6 authorizes insurers to offer premium discounts for completion of driver training or defensive driving courses, or any other premium discount provided by law.

These provisions thus limit the discounts which insurers may offer in connection with private passenger automobile insurance policies.

Some insurers offer both six-month and annual policy terms for private passenger automobile liability and/or physical damage policies. The Department has received rate and/or class plan applications which, for example, would result in a \$1,000.00 premium charge for an annual policy, but a \$550.00 premium charge for the same policy sold on a six-month basis. There is no legal authority supporting a proportionally higher premium charge for a six-month policy than for an annual policy or, in effect, a discount for purchasing an annual policy rather than a six-month policy. Therefore, the Department will not approve rate or class plan applications seeking to charge a higher “term factor” for a six-month policy than for an annual policy. The premium for a six-month policy shall be one-half that of the same policy sold on an annual basis.

Likewise, there is no legal authority supporting use of a “paid in full discount” and the Department will not approve or permit use of premium discounts, whether categorized as a business arrangement or otherwise, when a policy is paid in full or a greater down-payment is made at or near the inception of the policy.

“Term factors” and “paid in full discounts” are neither approved optional rating factors nor discounts provided by law, and therefore are not permissible.

No later than June 3, 2005, any insurer currently applying such discounts shall file the appropriate rate and/or class plan applications to comply with all applicable legal provisions.

Questions regarding this Advisory Notice may be directed to:

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JOHN GARAMENDI  
Insurance Commissioner