MINNESOTA DEPARTMENT OF
COMMERCE

85 7TH PLACE EAST, SUITE 500
SAINT PAUL, MINNESOTA 55101-2198
MN.GOV/COMMERCE
651.539.1500 FAX: 651.539.1547
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Administrative Bulletin 2015-3

Bulletin Regarding Unfair Discrimination in Rating: Price Optimization

Date: November 16, 2015

To: **Property and Casualty Insurers Doing Business in Minnesota**

This Bulletin is applicable to all property and casualty insurers issuing personal lines policies in the State of Minnesota.

While there is no universally accepted definition of price optimization, the practice, in some of its applications, involves the use of factors not specifically related to an insured's expected losses and expenses but are used to help determine or to adjust an insured's premium. For purposes of this Administrative Bulletin, "price optimization" refers to any method of taking into account an individual's or class's willingness to pay a higher premium relative to other individuals or classes. Price optimization includes the practice of varying rates or premiums in order to maximize insurer retention, profitability, written premium, market share or some combination of these. Price optimization usually includes considerations other than expected losses, expected expenses and/or expected risk. An example would be using an individual policyholder's response to previous premium increases to determine how much of a premium increase the policyholder will tolerate at renewal before engaging in comparison shopping or switching to a different insurer. This practice can result in two policyholders receiving different premium increases even though they have the same loss history and risk profile.

Property and casualty insurers doing business in Minnesota are reminded that all ratemaking must conform to the statutory requirements contained in Minnesota Statutes. Minnesota Statutes section 70A.04, subdivision 1, states that, "Rates shall not be excessive, inadequate or unfairly discriminatory, nor shall an insurer use rates to engage in unfair price competition." Further, subdivision 4 states that, "One rate is unfairly discriminatory in relation to another if it clearly fails to reflect equitably the differences in expected losses, expenses and the degree of risk."

Price optimization is not an actuarial estimate based on expected losses, expenses, and the degree of risk. Accordingly, any use of price optimization in the ratemaking or pricing process or in a rating plan is unfairly discriminatory and in violation of Minnesota law. While insurers may employ judgment in setting their rates, judgmental adjustments to a rate may not be based on non-risk related factors, such as an individual's "price elasticity of demand," which seek to predict how much of a price increase a policyholder will tolerate before switching to a different insurer.

Any insurer that uses price optimization in Minnesota shall immediately cease this practice, and within 60 days from the date of this bulletin submit revised filings to remove the rating practice as well as a corrective action plan. An insurer should include the following in the corrective action plan:

- The lines of business for which the insurer is using price optimization, a description of the manner in which the insurer is using price optimization, and the SERFF filing numbers of any rate and/or rule filings that contain price optimization;
- Any insurer that has a factor or factors based on price optimization in its rating plan shall remove the factor or factors, or make adjustments to the factor or factors so that the factor or factors are no longer based on price optimization in its rate filing and resubmit the filing to the Department; and
- A detailed description of the insurer's proposed action to address any consumer issues related to the use of price optimization factors or practices in previously issued policies.

When submitting property and casualty rate filings in the future, any insurer must include in their documentation filed in SERFF an attestation signed by an officer of the company or actuary that price optimization is not being used. Companies that fail to comply with this bulletin and are later determined to be using price optimization may be subject to disciplinary action.

Questions regarding this bulletin may be directed to Phil Vigliaturo, Property and Casualty Actuary, Minnesota Department of Commerce.

Signed

Mike Rothman

Mike Rothman
Commerce Commissioner