PO BOX 201706
Helena, MT 59620-1706
(406) 444-3064
FAX (406) 444-3036

Revenue and Transportation Interim Committee

61st Montana Legislature

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TO: Revenue and Transportation Committee

FROM: Jeff Martin, Legislative Research Analyst

SUBJECT: Mileage-based Motor Vehicle Insurance

As part of the Senate Joint Resolution 16 study of uninsured and underinsured motorists, the Revenue and Transportation Interim Committee has touched upon the concept of mileage-based auto insurance. At the Committee's December 3, 2009, meeting, Patrick Butler, National Organization for Women, discussed the concept. Joe Schmidt, a citizen from Billings, has testified in support of this type of insurance.

The purpose of this memo is to briefly discuss mileage-based automobile insurance and the reasons this type of insurance is promoted and to highlight state actions in Texas, California, and Oregon that encourage mileage-based insurance. The memo concludes with a brief comment on a survey of state insurance commissioners on impediments to mileage-based insurance.

MILEAGE-BASED INSURANCE

Mileage-based automobile insurance (often referred to as "pay-as-you-go" insurance) means that a vehicle's insurance premiums are based on how much the vehicle is driven.[1] The unit of exposure is the vehicle-mile rather than vehicle-year. This type of insurance would allow insurers to assign each driver to an appropriate cent-per-mile rate group based on standard insurance variables.[2] Under this type of insurance policy, insurance premiums would reflect a variable cost of driving a motor vehicle rather than a fixed cost.

Billing for this type of insurance could take a variety of forms. For example, motorists would prepay for the miles they expect to drive during the period of coverage, either in a lump sum or

[1] "Pay-As-You-Drive Vehicle Insurance: Converting Vehicle Insurance Premiums Into Use-Based Charges", Transportation Demand Management Encyclopedia, Victoria Transport Policy Institute, Updated 8 February 2010, p. 1. Retrieved from http://www.vtpi.org/tdm/tdm79.htm on April 17, 2010.

[2] Randall Guensler, et al., "Current State Regulatory Support for Pay-As-You-Drive Automobile Insurance Options", p. 4. Retrieved from http://commuteatlanta.ce.gatech.edu/Resources/PAYD%20State%20Survey%20Paper%20Final%20Version%20Sent%20to%20Journal%20Edit..pdf. Also printed in *Journal of Insurance Regulation*, National Association of Insurance Commissioners, Volume 21, No. 3, Spring, 2003.

in several payments.[3] They would receive a credit for unused miles or pay the balance due if actual miles exceeded the estimate.[4] Insurance companies could establish each year's estimate based on the total number of miles driven in the prior year. Motorists would be free to change that estimate if they anticipated driving more or less than in the prior year, but they would pay a penalty if the actual miles driven exceeded the estimate by more than a certain amount.[5] Insurance companies could also bill motorists based on their monthly or bimonthly vehicle mileage. This would probably require collecting mileage data electronically.[6]

Mileage-based insurance requires verified mileage data. Vehicle miles can be reported in a number of ways (the discussion on state activities provides some examples). In addition, an odometer audit procedure would have to be implemented. Some of the elements of the audit may include:

- check speedometer and instrument cluster for indications of tampering;
- make sure tire size is within specified range;
- attach seal to ends of odometer cable to indicate if it has been removed (unnecessary with electronic speedometers);
- check odometer accuracy and forward mileage reading to vehicle licensing agency.[7]

Mileage-based insurance is promoted for a variety of reasons including:

- economic efficiency;
- increased fairness;
- progressivity with respect to income;
- reduced uninsured driving;
- reduced need for cross-subsidies;
- reduced vehicle travel leading to reductions in:
    - traffic crashes;
    - traffic congestion;
    - road and parking facility costs;
    - energy consumption and pollution emissions;
    - consumer costs;

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[3] Jason E. Bordoff and Pascal J. Noel, "Pay-As-You-Drive Auto Insurance: A Simple Way to Reduce Diving- Related Harms and Increase Equity", Brookings Institute, July 2008, p. 13.

[4] TDM, Victoria Transport Policy Institute," Pay-As-You-Drive Vehicle Insurance: Converting Vehicle Insurance Premiums Into Use-Based Charges", p. 2.

[5] Bordoff and Noel, "Pay-As You-Drive Auto Insurance: A Simple Way to Reduce Driving-Related Harms and Increase Equity", p. 13.

[6] Ibid., p.13.

[7] TDM, Victoria Transport Policy Institute, pp 2-3.

- urban sprawl.[8]

STATE ACTIONS
Some states have encouraged mileage-based insurance on the basis of one or more of the reasons listed above. They have accomplished this either through legislation authorizing mile-based insurance (e.g. Texas), through revising insurance regulations (e.g. California), or by enacting tax credits for insurers offering mileage-based insurance (e.g., Oregon).

Texas
In 2001, Texas enacted House Bill No. 45 to allow an insurer of motor vehicles to offer the choice between a mile-based rating plan and a time-based rating plan for coverage for losses caused by collision or other driving-related accidents.[9] As introduced, the bill would have required insurers to offer such a plan. Previously Texas law required insurers to offer a time-based rating plan (one month policy for vehicle title changes[10]). The legislation also authorized an insurer to require a purchaser to use the same rating plan for all vehicles. According to the bill analysis of HB 45, certain customers such as the elderly and families with more than one motor vehicle could benefit from a mileage-based plan.

Among other things, the legislation required the commissioner of insurance to analyze the effect of mile-based rating plans on premium rates offered for motor vehicle insurance based on time-based rating plans and on the number of uninsured motorists in the state. The legislation also directed the commissioner of insurance to adopt rules on prepayment arrangements, proof of financial responsibility, and auditing of the odometer for the purpose of determining whether insurance coverage is in effect. The legislation terminated September 1, 2005.

MileMeter offers mileage-based insurance in Texas. Six-month insurance policies may be purchased for between 1,000 and 6,000 miles of coverage. The company provides all types of policies from minimum liability and uninsured and underinsured motorist coverage to full coverage.

If a policyholder inadvertently drives over the mileage coverage, the policyholder can purchase additional mileage to keep the policy in good standing. Unused mileage may be credited to a renewal policy subject to a deduction for an "earned premium of 1,000 miles". Odometer mileage is verified by digital photograph of the car's odometer with the policyholder's driver's license visible in the photograph. MileMeter may require another photograph at a random time for statistical purposes.[11]

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[8]Ibid., pp 4-5.

[9]See http://www.legis.state.tx.us/tlodocs/77R/billtext/html/HB00045F.htm.

[10]Bordoff and Noel, "Pay-As-You-Drive Auto Insurance: A Simple Way to Reduce Driving-Related Harms and Increase Equity", p. 17.

[11]See "How It Works - Introducing MileMeter 2.0!" at http://milemeter.com/milemeter2.

California
On November 8, 1988, California voters approved the Insurance Rate Reduction and Reform Act (Proposition 103). The measure made a variety of changes to California's insurance laws, including motor vehicle insurance. The measure provided that rates and premiums for automobile insurance must be based on three factors in decreasing order of importance:

- the insured's driving record;
- the number of miles the insured drives annually; and
- the number of years of driving experience the insured has had.

According to the Brookings Institution, the regulations implementing the proposition precluded insurers from offering "an insurance product to low-mileage drivers that more accurately reflects their accident risk because other low-mile drivers in traditional insurance plans would be paying a different (and higher) rate."[12]

Last September, the California Department of Insurance adopted revised regulations that allow insurers to offer insurance policies that are based on actual miles driven instead of, or in addition to, estimated miles driven. The regulations state that the [Insurance] "Commissioner finds that basing the Second Mandatary Rating Factor on verified actual miles driven, rather than on estimated miles driven, may enable policyholders to reduce their premiums by driving less and create incentives for innovation in automobile insurance rating in California with numerous attendant benefits." (California Administrative Code, Title 10, section 2632.5)

Some of the attendant benefits that the insurance commissioner had in mind included "lower-cost insurance, less air pollution, and a reduced dependence on foreign oil."[13]

The regulations contain the following provisions:

- authorizes insurers to offer an automobile insurance program to policyholders that uses verified actual mileage instead of, or in addition to, an estimated mileage program;

- allows an insurer who offers both estimation and verification methods for determining mileage to require an insured who chooses verified mileage for one vehicle to choose verified mileage for all vehicles insured under the same policy;
- allows an insurer that offers both a mileage estimation program and a verified actual mileage program to provide a discount to a policyholder who participates in a verified actual mileage program. The discount must be based on demonstrated cost savings or actuarial accuracy associated with obtaining and using actual miles driven rather than

[12] Bordoff and Noel, "Pay-As-You-Drive Auto Insurance: A Simple Way to Reduce Driving-Related Harms and Increase Equity", p. 17.

[13] Timothy F. Kirn, "California Gets Pay-As-You-Drive", *Insurance Journal*, October 19, 2009. Retrieved from http://www.insurancejournal.com/news/west/2009/10/19/104627.htm, April 19, 2010.

estimated mileage. The discount applies to all policyholders in the program, regardless of the method of verification.

- allows an insurer to retroactively or prospectively adjust premiums based on actual miles driven provided notice is given to policyholder before the effective date of the policy;

- odometer readings may be verified by the insurer or agent, an auto repair dealer, smog check stations, government agencies (such as the Department of Motor Vehicles), technological devices, or odometer readings by the insured. The insurer may not use a technological device to collect or store information about the location of the insured vehicle.[14]

Oregon

In 2003, Oregon enacted a tax credit for corporations that provide motor vehicle insurance policies that are at least 70% based on a mile-based rating plan or a time-based rating plan (Chapter 545, Oregon Laws 2003). The amount of the credit is $100 for each vehicle insured under a policy issued in Oregon, but the credit may not exceed $300 for each policy issued. The credit is nonrefundable and may not be carried forward. The credit may not be claimed for a policy for which a tax credit was claimed in a prior tax year. The credit is not allowed after the total amount of the credit claimed by all taxpayers for all tax years exceeds $1 million.

The credit was originally due to expire December 31, 2009, but the expiration date was extended to December 31, 2011 (Chapter 913, Oregon Laws 2009).

The original legislation did not state a purpose for enactment, but according to the Oregon Department of Revenue tax expenditure report, a legislative staff summary of the legislation said that the purpose was "to provide an incentive for Oregon drivers to drive less leading to a reduction in road congestion and environmental pollution."[15]

There are three insurers who offer mileage-based or time-based insurance plans. The plans are evaluated by the Department of Consumer and Business Services on the basis of actuarial soundness. No changes to the insurance laws or regulations were required to approve the plans.

A brief description of each insurer's basic plan, extracted from the website of the Oregon Department of Consumer and Business Services, is described below. According to the Department's website, the plans require a data logging device that is plugged into an automobile's onboard diagnostic port. As such, owners of automobiles made in the U.S. before 1996 might not be able to participate in the plans.

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[14] There are exceptions for devices used for emergency road service, theft service, map service, or travel service.

[15] Oregon Department of Revenue, 2009-2011 Tax Expenditure Report, Chapter 1, Income Tax (Personal and Corporation), p. 186. Retrieved from http://www.oregon.gov/DOR/STATS/ docs/ExpR09-11/Chapter1.pdf, April 14, 2010.

Companies offering discounts

National General Assurance Company: This program is available for OnStar customers and includes six, mileage-based discount levels. Discounts range from 50 percent if you drive less than 2,500 miles a year to 5 percent discount for driving 12,000-15,000 miles.

Progressive Universal Insurance Company: The company offers premium discounts of 5 percent to 25 percent, depending on when you drive and your total mileage. A base discount applies when you begin the program. After the initial period, the discount is based on the mileage and time of day data from your logging device and is reviewed and applied at each subsequent renewal.

The Travelers Home and Marine Insurance Company: This program is similar to Progressive's. You receive a 3 percent discount for participating in the program. The additional discount is based on the average weekly mileage driven. The discount can be as high as 20 percent if you drive less than six miles a week (312 miles a year) to no discount if you drive more than 196 miles a week (10,000 miles a year).[16]

STATE SURVEY

In 2002, the Georgia Institute of Technology conducted a survey of state insurance commissioners to find out whether state law or insurance regulations would allow pay-as-you-drive insurance.[17] Forty-three states responded to the survey. Sixty-three percent of the respondents (including Montana) said that existing laws and regulations would allow this type of insurance.

However, the Brookings Institution said in a discussion of the survey that certain legislative reforms might still be needed in some states because of potential conflicts with existing law. The Institute said that Michigan requires an upfront statement of the premium charge, and the policy must have an expiration date and must be renewable. Because the total premium for pay-as-you-drive is based on actual miles driven, Michigan may have to revise its regulations to allow this type of insurance.[18]

The Brookings Institution also pointed out that high startup costs and uncertainty may discourage insurance companies from offering pay-as you-drive insurance.[19]

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[16]Oregon Department of Consumer and Business Services, Insurance Division at http://www.cbs.state.or.us/ins/consumer/auto-insurance/pay-as-you-go.html.

[17]Guensler, et al., “Current State Regulatory Support for Pay-as-You-Drive Automobile Insurance Options”.

[18]Bordoff and Noel, "Pay-As-You-Drive Auto Insurance: A Simple Way to Reduce Driving-Related Harms and Increase Equity", p. 17

[19]Ibid., p. 18.

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