Long Time Policyholders – Price Optimization

by Yvonne R. Hunter | Jun 7, 2017

The best reason to regularly check and compare property and casualty insurance policies is a concept that you have probably experienced in other consumer purchase experiences: price optimization.

How does this work? Consider the price of a Las Vegas hotel room on New Year's Eve, compared to a Tuesday night in July. Another example is the street price of a sports ticket when the home team is on a winning streak compared to when it's on a losing streak. In each case, market conditions set the price rather than the cost of the product. You take advantage of the bargain when demand seems low for the product or service.

For insurance policy costs, price optimization causes you to pay a higher price for a policy because of years of loyalty or simply convenience. Over time, the insurance company may seem to "sweeten" the deal by offering a discount on a new product or to bundle home and auto policies. Price optimization makes loyalty a penalty for you when fees or other charges added to the cost of insurance results in higher costs to you. You may be wise to treat the offer to bundle or to pay an additional fee as a good reason to start some comparison shopping.

The National Association of Insurance Commissioners (NAIC) has been studying the issue of price optimization because consumer insurance advocacy groups believe that the use of price optimization in insurance policy prices may be unfairly discriminatory. For the technical definition, price optimization relies on consumers' price sensitivity in determining the price paid for an insurance policy or the insurance rate for insurance coverage.

Translation: price optimization means that the insurance company has determined that you as the consumer will stay with the insurance company only if the price is at X, which may be significantly higher than what a similar new insurance policyholder with similar insurance coverage would pay. In simpler terms, your loyalty may not result in a bargain.

Insurance companies have their insurance rates approved by the respective state regulator where the company is doing business and have to use actuary calculations to support the rates. The rates are traditionally analyzed based on projected costs, i.e., what is being insured and what can happen to cause the insurance company to pay. Price optimization comes under scrutiny because the traditional calculations should result in all similar customers paying the same rate, rather than long term customers paying a higher rate.

The insurance industry believes that as long as rates meet the state requirements and the actuary models show the rates are sound, the discussion should end. Consumers may innocently believe that they are being rewarded for loyalty when just the opposite may be happening.

Some states have issued bulletins, policy statements and letters to put insurance companies on notice that price optimization practices will be closely monitored to see if consumers are being economically harmed. These states may seek corrective actions with those insurance companies found to be in violation of the identified practices.

The consumer response in reviewing insurance products should be more proactive and include a "shop around" experience. Once you have gathered the relevant information on insurance products, you can do some comparative shopping with your own insurance company. You may want to check with your state Insurance Department or Insurance Commissioner to determine how the insurance company handles claims and complaints, and whether the insurance company meets the state requirements for rates. All insurance consumers should take advantage of any price optimization so that it works to their benefit.