

How Auto Rates Are Calculated

Like all businesses, an insurance company must cover its costs to stay viable. The difference with an insurance company is they will not know how much the product costs at the point of sale. An auto insurance company collects premiums to pay

for insurance claims, administration, and taxes.

“Claims are the largest expense for an insurance company & the hardest to predict.”

Claims pay for bodily injury and vehicle repair or replacement. They are also the most unknown expense at the time of purchase,

making them difficult to predict and pose a big risk to the insurance company.

To cover the high risk and expense of claims, an insurance company:

- ▶ Considers the number of past claims when setting their base rate.
- ▶ Uses premiums collected from policyholders to pay for the few who make a claim.
- ▶ Invests the money collected from policyholders to reduce financial risk.

The Calculation

To determine the cost of your auto insurance policy, a formula based on a number of identified risks is used to come up with a price. These risks include where you live, your age, vehicle type, how much you drive, and any past insurance claims. In short, this formula is used to calculate your auto insurance rate:

Base Rate × **Rating Factors** × **Surcharge & Discounts**

Base Rate

The base rate covers an insurance company's expected claim and operating expenses, and a reasonable profit to ensure the company's viability (insurers may only allow for a 6% return-on-premium).

Rating Factors

Insurance companies have access to significant amounts of data. They use it to predict the risk of you making a claim. For each data point, they will assign different weights or percentages. Insurance companies use your personal characteristics such as age, gender, and marital status to predict risk. For more details see the following page.



Surcharges & Discounts

An insurance company may apply a surcharge based on any accidents or convictions you have. You may also be eligible for several discounts or preferred rates such as:

- ▶ Bundling your home and vehicle insurance.
- ▶ Having an anti-theft system.
- ▶ Using winter tires.
- ▶ Having a membership in a professional association.
- ▶ Being an alumnus of a university or college.



Ask your insurance agent, broker, or direct writer about surcharges or discounts when seeking a quote.

4 Types of Rating Factors

Your Driving Record



Insurance companies use your driving record to determine how much of a risk you pose on the road. Generally, the better your driving record, the lower your insurance rate. For example, a driver with at-

fault accidents poses a higher risk to an insurance company. Your rate may also increase if you have more than one traffic conviction in the last three years, such as speeding or careless driving.

When looking at your driving record, insurance companies consider:

- ▶ The number of years licensed.
- ▶ The number of traffic convictions, such as speeding tickets.
- ▶ The number of at-fault accidents.
- ▶ If you have taken driver training.

How Much & Where You Drive



If you live or drive in a city, your rate will likely be higher due to the higher risk of vehicle theft or accidents. Also, insurance companies determine risk by examining the number of km driven.

Driving more increases your risk of being in an accident, which raises your insurance rate.

Type & Amount of Coverage

The more coverage you have, the higher your insurance rate. You can customize your insurance to meet your needs by adding or removing specific types of coverage such as collision or comprehensive. If you drive an older vehicle, you may remove collision coverage, or if you are leasing/financing you may be required to carry collision.



Your Vehicle

Your vehicle's make, model, and year affect your insurance rate. Insurance companies consider the cost of replacing your vehicle if it was stolen or damaged in an accident. Your

insurance rate might be statistically proven less likely to be stolen or involved in an accident. It also might be lower if the vehicle has better safety and handling features or is less costly to repair. Generally, insurance rates are higher for new vehicles and sports cars, but a vehicle's safety features may help lower the price.

