Pay As You Drive

Ever had to read your insurance policy for a home, seasonal home or rental property? Then you probably ran head-first into the terms "hazard," "peril," or "cause of loss." These refer to events that could damage your property and which are covered by your insurance. While you may understand some terms, you may be confused by others. This article (and part two) briefly explains some common terms which, in some cases, may not mean the same as they do in the dictionary.

California, the nation's frequent trend-setter, has thrown the switch on an idea that could affect the way the rest of the U.S. buys personal automobile insurance. In the last quarter of 2009, California's drivers will have the option to buy insurance on a "Pay As You Drive" basis.

How insurance companies charge you and I for auto insurance remained roughly the same for decades; using two levels of characteristics called rating factors. The primary set of factors usually includes:

- Territory
- Age, Gender, and Marital Status
- Vehicle Use
- Discounts

Another (secondary) set of characteristics include vehicle age and original cost, susceptibility to damage, ease/difficulty to repair and vehicle performance capability.

The primary factors had long been proven as reliable guides on what type of risk an insurer took when considering providing coverage for a certain type of driver. For instance, a driver's territory was based on a section of a state where a driver lived and operated his car for work and pleasure. Statistics are widely available about a given territory, such as traffic density, amount of city, vs. suburban and rural roads, accident and loss data, etc. Factors such as age, gender, and marital status relied on data concerning driver experience, maturity and stability with regard to likely operation of a vehicle. It also provides important information on long-term prospects, particularly the impact of becoming elderly operators.

The "Pay As You Drive" (PAYD) concept is not new. It has long been discussed as an alternative way for insurers to charge drivers according to, some say, the most important risk affecting auto insurance….how often a person actually drives a car. It is also used by insurers in other parts of the world, including the U.K and Australia. While most of the factors used to rate drivers would still be used; they would be strongly connected to actual usage.

Those who favor the idea cite the fact that, since it is tied to actual use, it gives drivers control over a major household expense. Fans of the concept's use in the U.S. usually mention the following advantages:

- Nationwide Driving would be reduced
- Pollution from cars would decrease
- The majority of households would experience lower auto insurance costs

Under the California plan, the state would have to approve all such programs and each insurer will be required to file its plan with state authorities. Insurers have two choices; they can convert to offering only PAYD plans or offer it along with traditionally rated insurance. Insurers may also offer coverage based on actual miles used, or upon low-mileage plans, based on selecting among monthly or annual mileage bands.

Other states in the U.S. do offer forms of low-mileage options, such as Texas. Further, various insurance companies have also used their own versions of PAYD in certain states. However, according to some critics, they do not offer the same level of potential savings and driving-reduction incentives as true PAYD.

PAYD does create a major privacy concern. In order to use the program, insurers must have ways to monitor and document a driver's actual mileage. Methods of making such measurements include use of GPS devices, certifying odometers (self-reporting or installed devices) or use of inspection points (such as gas stations). The privacy issue arises from the use of GPS devices that would also provide insurers with many more details about driving behavior, such as the time of day that vehicles are operated, locations driven, car operating speed, etc. Naturally insurers claim such information would permit greater accuracy in rating. Consumer advocacy and other groups counter that insurers don't have a legitimate claim for such information and they fear abuses. Under California's recently approved plan, insurers are prohibited from collecting additional information.

For the time being, both Californians and the rest of us will be watching to see if PAYD translates into PAYDAY as a viable option for buying insurance.
