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PUBLIC HEARING

before

SENATE SPECIAL COMMITTEE ON AUTOMOBILE INSURANCE REFORM

on

AUTOMOBILE INSURANCE REFORM

May 5, 1986
Room 334
State House Annex
Trenton, New Jersey

MEMBERS OF COMMITTEE PRESENT:

- Senator Daniel J. Dalton, Chairman
- Senator Carmen A. Orechio
- Senator Christopher J. Jackman
- Senator Lee B. Laskin
- Senator Leonard T. Connors, Jr.
- Senator Raymond J. Zane

New Jersey State Library

ALSO PRESENT:

Laurine Purola
Office of Legislative Services
Aide, Senate Special Committee
on Automobile Insurance Reform

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M E M O R A N D U M

April 30, 1986

TO: Members of the Senate Special Committee on
Automobile Insurance Reform

FROM: Laurine Purola

SUBJECT: Committee Meeting

The Senate Special Committee on Automobile Insurance Reform will meet on Monday, May 5, 1986 from 9:30 A.M. to 11:30 A.M. in Room 334 of the State House Annex. The topic will be a continuation of the discussion on the Joint Underwriting Association with Mr. Willard Young, Chairman of the Joint Underwriting Association. After the presentation, the members of the Committee will meet in executive session.

TABLE OF CONTENTS

	<u>Page</u>
William Young Joint Underwriting Association	1
Jasper J. Jackson Deputy Commissioner New Jersey Department of Insurance	26

* * * * *

mjz: 1-20
tdm: 21-39
mjz: 40-47

SENATOR DANIEL J. DALTON, (Chairman): I want to get the meeting started. The meeting today is going to be divided up into two sections. The first section will conclude hearing from Bill Young, of the Joint Underwriting Association. When Bill concludes at that time, the Committee will go into Executive Session. The purpose of the Executive Session will be to hear from the Department of Insurance with regard to the JUA situation. It is my understanding that the Department of Insurance is involved in some litigation with regard to the whole JUA issue and, as a result, has requested that if, in fact, they do participate -- and we certainly wanted them to -- that we would have to go into Executive Session to hear from them.

So, after Mr. Young, we are going to ask everyone but staff to leave, and then we will be able to hear from the Department of Insurance.

Bill, I know you don't have a prepared statement, and certainly this is just an extension of your last appearance here, but I think probably it would be worthwhile for the Committee members to hear a summarization from you of the deficit situation, how we got into this deficit, and perhaps even hear some of your thoughts as to how you hope to extricate yourself from the deficit. I know you will be Houdini if, in fact, we can extricate ourselves from this deficit problem painlessly, but the floor is yours.

W I L L I A M Y O U N G: Okay, thank you, Senator. The JUA deficit problem is a creation of a number of factors. I think to get a basic understanding you need to go back and understand that the JUA, when it was created, was given a rate level -- a premium level -- to charge its customers, which had no basis or relationship to the loss history or loss experience of those people insured in the JUA. In a voluntary market company, theoretically, the rates charged should be able to match the claims payment and the expenses of the insurance company. With

the JUA, there was really no attempt to make that kind of a connection. The JUA charges a rate level which is equal to the ISO rate level, and the ISO rate level is based on the experience of voluntary market insurance companies which use ISO rates and contribute their data to the ISO rating formula.

So, the population of the JUA is not, in any way, tied to the ISO rate base. If the JUA population were better drivers than the voluntary market, then we would have rates which were higher, but as a practical matter, the JUA driving public has a higher accident rate and a higher claims cost in many respects than does the voluntary market that is used for setting the rates.

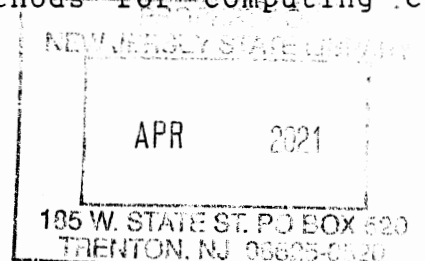
There are many, many reasons for this. One of the most obvious is, anyone who can't get insurance in the voluntary market must be insured through the JUA. So, we get a greater proportion of bad drivers. We also get a high proportion of questionable claims situations, where the claims -- ah, payments, the reasons, the causes of the claims may not necessarily be as clear-cut as they would be in the voluntary market. We have a high turnover rate in our policyholders, much higher than the voluntary market, which, of course, pushes the cost up because people will take out a policy, let it lapse, and then go back and get a new one with a much higher frequency than in the voluntary market, thereby pushing our costs up.

There are many reasons for the deficit which are based in the statute. There are other matters as well. I spoke at the last session about the lack of an appropriate DMV collection rate and the feeling that the DMV surcharge level had been initially set too low. Another change which occurred at the time of the initial legislation, which has only very recently been corrected, is the issue of chargeable accidents. In the legislation setting up the JUA, the only accidents which could be surcharged for had to involve property damage

liability, which is where your insurance company pays out money for damage you cause, or for bodily injury involving pedestrians. I think that was perhaps an error, in retrospect, because we eliminated many accidents which should be surcharged for. For example, if you were driving your car, ran into a telephone pole, and did \$1000 worth of damage, it was your fault, and there was no way to surcharge for that accident unless you caused over \$300 in property damage to that telephone pole, which rarely occurred. So there were many cases where accident surcharges would have been levied in the past, but weren't being levied under the new system. So there was income loss there.

There are also problems on the physical damage, which is the collision and comprehensive side of the business. Again, we were required to use ISO rates, and those ISO rates were lower than were being collected in the previous assigned risk claim, the AIP. So, we started with lower rates. We have a high frequency of physical damage losses, and because in many cases we insure drivers who have higher than average claim frequency, we are getting drivers who have repeat collision and comprehensive claims with no way to go back and charge them for the excessive losses. Again, recent legislation has corrected that particular problem, but we have not yet seen new rules established which would allow us to collect that money.

The base rates, we believe, for our driving population are probably lower than their actual loss potential, so we have a disparity there. All these things taken together combine to create the deficit we have. There are many ways to attack it. There are things which I mentioned we were doing. For example, we have started to reduce the payments we're making to service carriers. We have reduced the administrative fee they received just for the process of issuing insurance policies. We are reviewing, at the present time, further changes in that fee. We are also reviewing different methods for computing claims



payment fees to service carriers, and there are several different ways that that can be done. Unless it is of interest, I won't go into it because it can be kind of mind-numbing to hear that discussion.

We are reviewing the claims payment procedures more thoroughly to make sure that fraudulent claims are found, to make sure that only valid claims payments are made. In fact, we have had a number of instances where claims have occurred which perhaps under the old system might have been paid, but we have denied them because they involved ineligible vehicles or ineligible drivers. So we're trying to tighten up our own standards, but there are only certain things that are within our capability to do because we have no control over the income we receive. As long as the JUA continues to grow and we have a greater and greater share of the driving public, these problems are going to continue to get bigger and bigger and bigger in the total. It's only if we can change the direction of the JUA, start to shrink it back to the point where we are actually insuring only the people who belong there -- who are the people with difficult driving records or difficult personal situations-- When we get to that point, then we will be able, I think, to bring some control to this deficit problem. But, as long as we have the limited income resources on the one side and the continued growth on the other side, we are going to continue to have large deficits which are going to keep piling up into the future.

I think that is sort of a quick summary of our deficit problem. In 1984, we estimated our deficit-- I believe the figure was \$430 million on what we call a "statutory basis" -- I'm sorry, \$260 million on a statutory basis, and that number is continuing to rise. We expect it will be equaled in 1985, and that information should be available within the next few weeks if we complete our annual statement.

So, we're estimating that on a statutory basis we have somewhere between a five and six hundred million dollar deficit, and I think that various State agencies, while they may disagree with our methodology, are in general agreement that, in fact, the deficits are there, that they will come due. I think our major disputes are on how we are going to collect that money. Do we start at this point in time? Do we wait until a serious crisis exists? Can we find other sources of income, such as the DMV collections, such as the accident surcharges that I mentioned earlier? Where can we find other sources of income to help delay the inevitable date when we will run out of money or to minimize the need for a RMEC or any other surcharge procedure?

SENATOR DALTON: Bill, let me start off, if I may. One of the things I want to ask you about is the whole issue of fraud. What experience, as Chairperson of the JUA, have you seen as far as fraudulent claims, and what is the origin of those fraudulent claims?

MR. YOUNG: Well, we have seen a number. Our General Manager, Nelson Ealey, who is here today with me, has operational oversight in that area. I can talk in general terms, but if you would like some specifics of the kinds of things that we have been involved in, I would defer to him. We have found cases where medical bills were inflated, where information with regard to the seriousness of a claim was either misrepresented or overstated. We have found cases where rings have been set up to steal cars, particularly late model cars. They end up burned, they disappear, you know, they could end up in another country, as far as we can determine.

We know that these situations exist. We have limited resources to do anything about them. What we have done in a couple of cases is work closely with the Insurance Department's Fraud Bureau. We have been involved with several county prosecutors in matters that they have uncovered, including some

where they asked our assistance in helping to catch the people involved. Our resources are limited, as an Association. The existence of the Fraud Bureau puts a great deal of the investigation in their bailiwick. We don't have a lot of authority to investigate fraud, but we do turn over everything we find to either them or to prosecutors, depending upon the circumstances.

SENATOR DALTON: Is it significant -- the amount of fraud we're seeing, as far as claims submitted?

MR. YOUNG: Yes, it is.

SENATOR DALTON: Okay. The next issue that I want to get involved in was a very controversial issue when the JUA was formulated; it deals with the whole issue of agents' commissions. .

What is the status of agents' commissions via the JUA presently?

MR. YOUNG: Initially, going back to the old assigned risk plan, the agents' commission was set at 10% of the total policy premium. When the JUA was set up, several changes occurred. First, certain portions of the insurance premium were excluded from commissions. So, instead of receiving commissions on the full 100% of the premium, the commissions were paid on something less. In addition, there were no accident surcharges, no driver surcharges, so that in balance, the dollars upon which the commissions were paid shrunk a little bit.

Initially, the commission rate was set at 13% in recognition that every single policyholder -- over a million of them -- was going to have to have new policies issued within a 12-month period. It was a massive undertaking for the insurance industry. Following that first year, the commission rates were lowered to 11%, which was believed to approximate the old 10% because of the differences in the base upon which it was computed.

In recent times, it has been determined that a portion of a statute which was felt not to apply, does in fact apply, and that is called the "fully earned commission statute." What that means is that when a policyholder cancels his policy, at his request, including for nonpayment of the premium, the agent, or broker, receives the full annual commission on that policy, instead of only the proportionate amount of commission for the time period during which that policy was in force. It had been the Association's position that that statute did not apply because we did not feel that the Association was a direct descendent of the assigned risk plan. The Insurance Department advised us, through the Attorney General, that they determined that the statute did apply, so we have been paying those commissions since January 1, on those types of cancelled policies. So that has increased commissions somewhat. We don't yet know how much because we only have a few months of this statute behind us, or this interpretation, so we really don't know its dollar impact. By the end of this year we will be able to determine. This was, in effect, an increase in the commission rate to producers.

SENATOR DALTON: Let me ask you one more question before I look to the other Committee members. As far as extricating ourselves from this JUA, do you believe that some sort of a two-tiered system, or two-tiered rating provision within the context of the JUA is something that we ought to be doing?

MR. YOUNG: Yes, I do. I believe the two-tier system will be necessary if we are ever to depopulate or to force the JUA drivers to look for alternatives. It is very easy to be insured in the JUA. It is probably the easiest place to be insured in New Jersey. Our rates are very competitive. Our procedures are such so that the public does not feel any pressure or any stigma from being in a second-class market. They receive first-class service. So, there is no incentive

for the public to seek alternatives. There may be alternative markets available, but there is really no impetus for them to go look. The only way we are really going to get their attention is if we are able to charge a higher rate.

Now, I mentioned to you earlier the problem in using the ISO rate base, which is that it does not reflect the driving experience of our drivers in the JUA. If we were allowed to gradually start increasing our rates -- whether on a limited or full basis -- we would start to create that impetus towards forcing people out of the JUA, to look for what alternatives are available, as well as to raise additional income for the JUA. This has been done successfully in other JUAs, notably the Florida one, which is self-rating -- which is what we would call this -- and their JUA has shrunk.

Now, keep in mind that the voluntary market has created the capacity to write new business in Florida. I don't necessarily see that happening in New Jersey, given the present set of circumstances and the status of the insurance industry -- things that we talked about at the last meeting.

SENATOR DALTON: Just to, I guess, underline what you're saying -- I'll pass this around to the Committee members -- this is, I guess, a marketing brochure that was put out by an agent, which really-- It says, you know, "Hey, we can give you lower rates through the New Jersey Joint Underwriting Association." It has a form for you to fill out and everything like that, but I think it sort of underscores what you're saying, you know, "There is no incentive to move out of the JUA," in effect.

MR. YOUNG: That's right. I might make an interesting -- just a side comment with regard to that. The agency which is doing that advertising had an earlier ad which had testimonials from individuals on savings, and the Association did some investigation because they were talking about Association policies. Of the ones we could check out, we found

that the claims were not true, that, in fact, the people were not paying less. But, nonetheless, it is that kind of advertising which makes the Association grow.

SENATOR DALTON: There are a tremendous amount of agents-- I shouldn't say tremendous, but there are agents out there who just do JUA business and nothing else. Right?

MR. YOUNG: That is correct.

SENATOR DALTON: That's their whole purpose and their livelihood, doing JUA business.

MR. YOUNG: That is correct.

SENATOR DALTON: Ray, any questions? Len?

SENATOR CONNORS: On that score, just to better understand it, as I understand what is going on, if a person who has a policy in a voluntary market has an accident, and the people who are the insurers raise his rates because he has had an accident, it would be much easier for him to go into the JUA and pay no raise in the fee, right? Is that what you're saying?

MR. YOUNG: Not precisely, Senator. If that same individual came into the JUA, we would do an investigation of his driving background. If we uncovered the fact that he had that accident, we would charge him the same rate as a voluntary market company would have, but keep in mind that for accidents which occurred prior to the signing of 3913, there were very limited circumstances for charging a surcharge for that accident.

SENATOR CONNORS: The chances of you finding that, though, would be relatively nil with the amount of people who are coming into the JUA on a daily basis. Is that a fair assumption?

MR. YOUNG: It is difficult, yes; that is correct.

SENATOR CONNORS: The question that I just jotted down here is, as I understand -- and you have answered it perhaps, but I will just go a little further-- The ISO rates are not based on JUA rates, on JUA accidents, etc.

MR. YOUNG: That is correct. Our rates are based on the ISO accident history.

SENATOR CONNORS: In the voluntary market?

MR. YOUNG: In the voluntary market only.

SENATOR CONNORS: And last session, you put down four points about where the money came from to fund the JUA. They were the premium rate surcharges, policy constant, RMEC, and driving record surcharges -- and then investment, I think, was the fifth one you added later. Would you go over the policy constant with me again, please?

MR. YOUNG: Certainly. The policy constant is a fee which was imposed about six years ago to offset the losses in the old assigned risk plan. The money was collected by and kept by the insurance companies because at that time they were the ones who were paying the assigned risk losses. When the JUA was created, that surcharge, which was designed to offset the old assigned risk losses, was then transferred to the JUA. So, the moneys that used to stay with the insurance companies no longer did. They now come to the JUA. There is a surcharge for liability; there is a surcharge for collision; and, there is a surcharge for comprehensive. That is levied on a per-car basis.

SENATOR CONNORS: So, people who buy their automobile policies in the voluntary market are also paying for the people in the JUA--

MR. YOUNG: That is correct.

SENATOR CONNORS: --through a policy constant. Then we also have the double-whammy, the RMEC, the possibility of utilizing the RMEC to even get some more money out of those people who buy in the voluntary.

MR. YOUNG: That is correct.

SENATOR CONNORS: You referred to collision. It was my impression that collision was a non-mandatory form of insurance. How does that fit into the JUA, its rates and surcharges?

MR. YOUNG: Collision insurance is not mandatory coverage. When the JUA was set up, it was told that it had to provide, in addition to the very limited mandatory coverage of liability insurance of \$35,000--

SENATOR CONNORS: Who told them that?

MR. YOUNG: The statute says that.

SENATOR CONNORS: The statute says that.

MR. YOUNG: The statute says that the JUA -- this is the original statute -- must offer liability limits of up to \$500,000 for liability, or some combination which equals that; the same limit for uninsured motorists and underinsured motorists; must provide physical damage coverages, which are collision and comprehensive, with a range of deductibles; and, in addition, all the various no-fault coverages. These are contained in the statute and we are mandated by law to offer these.

SENATOR CONNORS: Was that under A-1695, do you recall?

MR. YOUNG: Yes, it was.

SENATOR CONNORS: It was. So, the collision-- Again, the policyholder, out of the constant, would be paying to subsidize those rates in the JUA for people who might not ordinarily be able to buy insurance -- collision insurance -- in a totally voluntary -- supposedly totally voluntary market.

MR. YOUNG: That is correct.

SENATOR CONNORS: That is correct, is it? You know, just as a side note, a personal experience, we have a young fellow who lives in my area, and he makes a lot of money. He is a first mate on a fishing vessel and he makes a considerable amount of money. He has gone through four 1985 -- those great big wheel jobs -- pick-up trucks, because he rolled them over. You know, I kind of -- I am just telling you my personal opinion, not knowing this until you told me and cleared it up -- I kind of resented that my policy dollars were being utilized to subsidize him going out and buying automobiles and

putting collision insurance on them. I don't think it's fair. I think the-- Of course, it's not up to you, it's up to us, to do something about this. But I really think it is totally objectionable, as far as I am concerned.

MR. YOUNG: Senator, there is something that we have discovered since we have been in operation, and that is that we probably insure the highest proportion of Rolls-Royces of any insurance company in the country because our rates, which are established by ISO, are in the three to four to five thousand dollars per year range for collision and comprehensive for a Rolls-Royce costing in excess of \$100,000. If the individual had to go and buy that coverage in the voluntary market, he would probably be paying somewhere around eight to ten to twelve thousand dollars. So, we are extremely competitive in those very high value vehicles, and there is actually nothing we can do about it because we must provide that insurance.

SENATOR CONNORS: Well, I'm glad you brought that to my attention. That certainly is another good reason why we should be doing something about it.

I have another question I jotted down here. If the companies administer the claims for the JUA, why should they care how much the claims are?

MR. YOUNG: That is a very good question. Just looking at it from the surface, that is a potential problem. They are paid a fee based on the claims that they process and the dollar value of those claims. The only way we can determine that they are, in fact, doing things correctly, is through a very extensive auditing procedure, which we utilize. We conduct audits of the service carriers, of their claims, on a random basis, so that we can try to determine whether the claims payments are fair, whether they are being made promptly, and whether they are in the right amount. That then helps to control the fees that the service carriers receive.

We are in the process of creating, within our Association staff, an expanded capability to do the same thing, by hiring claims examiners. We now have a full-time claims manager, and we are going to be doing more scrutiny of this whole process in future months to make sure that only those valid claims are being paid or reserved, and that the payments that are computed against those numbers are, in fact, accurate.

SENATOR CONNORS: And my last question, in your presentation this morning and going back, it seemed to me that you said you are looking to surcharge the insured motorists who have accidents. Is that true?

MR. YOUNG: That's correct, only those drivers who have insurance policies pay surcharges.

SENATOR CONNORS: In the voluntary market?

MR. YOUNG: In the voluntary market and in the JUA. A driver who does not carry insurance -- which is, of course, illegal -- is, of course, not going to pay a surcharge.

SENATOR CONNORS: He doesn't pay anything.

MR. YOUNG: That is correct.

SENATOR CONNORS: He doesn't pay the policy constant.

MR. YOUNG: He doesn't pay anything.

SENATOR CONNORS: He doesn't pay the residual market equalization charges, if there are any. He doesn't pay anything.

MR. YOUNG: Sure.

SENATOR CONNORS: The plain fact of the matter is, are you suggesting then that motorists be surcharged to the JUA for accidents they have while they are insured in the voluntary market?

MR. YOUNG: No.

SENATOR CONNORS: No?

MR. YOUNG: Drivers who are insured in the voluntary market who have accidents-- The surcharges that would be collected for them would stay with their insurance company.

What I'm saying is, the drivers who we insure in the JUA, who have accidents, the surcharges collected from them would come to and stay with the JUA.

SENATOR CONNORS: Are you presently surcharging motorists who have accidents?

MR. YOUNG: No, we're not. We do not have the authority, we believe, to impose a surcharge system for accidents. Now, the Insurance Department has just -- in the last week -- indicated that they perhaps feel that maybe authority does exist, and we are going to explore this in detail with them.

In any event, that authority did not really exist prior to the signing of 3913 because of the very limited nature of chargeable accidents.

SENATOR CONNORS: So, making a comparison then, a person in the voluntary market who has an accident, and who remains in a voluntary market, the insurance company can surcharge, but a person then who presently -- up to this day, this hour -- is in the JUA, can have an accident and he doesn't get surcharged.

MR. YOUNG: You're correct, except for one point which might need to be clarified. In the voluntary market, the surcharges for chargeable accidents could not be made either, because the definition of what was a chargeable accident was contained in the original statute. Until that was just recently modified, no policyholder could be surcharged for an accident unless it fell into that narrow definition.

SENATOR CONNORS: Okay. Now it falls into the definition, and the person in the voluntary market can be surcharged, and a person who is in the JUA cannot be surcharged.

MR. YOUNG: I believe that is a temporary problem because we're--

SENATOR CONNORS: Pending some form of legislation. Well, it was temporary-- You might say then it was temporary since we enacted the law. It's been temporary for over a year.

MR. YOUNG: The law which allows the broader definitions sets up certain procedures which must be followed for setting up the surcharge process, and the Insurance Department is currently going through that process. We have to wait until they complete it before we have the rules with which we can charge for those accidents. I believe that that issue is in the process of being resolved by the Department right now. It's just that they have not had a chance to complete the background work they need to do.

SENATOR CONNORS: Thank you.

SENATOR DALTON: Senator Orechio?

SENATOR ORECHIO: Yeah. Mr. Young, you indicated that a claims manager has just come aboard, and you also said earlier that you don't really have a fraud department per se. With these deficits at the half billion dollar mark, aren't there some other things you can do, for example, to minimize some of your losses? Wouldn't it be a good idea to maybe have a fraud department to monitor what happens at the adjuster shops, etc., etc., as the carriers do in the voluntary market?

MR. YOUNG: The procedure we follow-- Of course, the Department of Insurance has its Fraud Bureau which handles all complaints involving fraud. We require of our service carriers that they have fraud investigation units within their companies. These investigation units provide internal analyses of all those claims, and most of the questionable claims that the companies encounter-- As an agent, I have had some contact with these internal fraud investigation units, and they do a good job. They are extremely thorough. Most are staffed by ex-law enforcement personnel, so they have the background to do the work.

For us to establish in the JUA a separate fraud unit might be redundant because we believe that the service carriers are doing a good job of uncovering this. By law, they are required to do it.

SENATOR ORECHIO: They do it as part of the fee they get, right?

MR. YOUNG: They are doing that as a part of their fee. This is one of the things we look for when we do our claims audits. The Insurance Department receives these complaints directly because that is the way in which the Fraud Bureau was set up. We try to monitor, as best we can at the JUA office, those claims which involve fraud. Sometimes there are confidential things going on that we can't necessarily have access to, but we have good communications with the Insurance Department's Fraud Bureau, and we have, I think, done a reasonably good job at uncovering this.

I'm sure there are cases of fraud which have occurred that we have not been able to uncover. That, I think, is an ongoing problem.

SENATOR ORECHIO: How does car thievery -- the incidence of car thievery among those involved in the JUA -- compare with those in the voluntary market?

MR. YOUNG: I'm not sure we really have statistics which would give you a clear-cut answer. I have to give you what my feeling is, and my feeling is that the rate of thievery among JUA policyholders is probably higher than the voluntary market, but I can't prove that. That is only a feeling I have.

SENATOR ORECHIO: To follow up a question Lenny alluded to earlier, is there any recommendation you can make as to how we can zero in on the uninsured driver who goes off scot-free? I remember years ago when people's licenses were suspended, the local daily papers would publish a list of those suspended, for example. Secondly, when you apply for a renewal registration, you just put down the insurance company's policy number, and that generally gets you by. Somehow if there was a submission of a copy of the policy, or something else maybe that wouldn't be tedious-- Shouldn't there be some way-- Can you recommend any way that maybe we can do a better job and

focus in on the uninsured driver and try to get him on our rolls?

MR. YOUNG: I think the capacity of the insurance industry to do as you are suggesting is relatively limited. At the present time, we do notify the DMV of policy cancellations, which should be the trigger for determining whether or not a driver is insured. But I know that the quantity of these notifications is extremely high. I know that the DMV has some difficulty in just keeping up with the paperwork.

I think the matter is really a law enforcement question more than it is an insurance question, but that is just an opinion of mine.

SENATOR ORECHIO: No more questions.

SENATOR DALTON: Senator Zane?

SENATOR ZANE: Yeah. I would like to ask just a couple. The deficit you speak of, what are the elements that go into it? Is it a matter of the claims you have versus the revenues that you anticipate, and the difference is the deficit?

MR. YOUNG: That's a pretty correct statement, Senator. We base our estimates on what we call accident years, or policy years, which means that all the income derived from policies issued in a particular year are matched against the claims on those very policies, and the difference is the deficit. So, for example, when I say we lost \$260 million in 1984, on all the policies issued in 1984 -- which would be from January 1 through December 31 -- when those policies run their full cycle, which means they could run into almost the end of 1985, and the accidents that occurred on those policies are all matched up, the claims payments will exceed the premium income by about \$260 million.

SENATOR ZANE: Okay. Didn't you indicate-- By when did you indicate that you anticipate this deficit to be half a billion dollars?

MR. YOUNG: We anticipate, adding the 1984 deficit and the expected 1985 deficit, we will be at the \$500 million level.

SENATOR ZANE: Let me ask you this. Those drivers -- the other 50% of the motorists, or roughly that -- who aren't in the JUA, are, in fact, to some extent, subsidizing JUA. Correct?

MR. YOUNG: That is correct.

SENATOR ZANE: If you remove the subsidy from the other drivers, do you have any idea what the deficit would be? In other words, how much greater?

MR. YOUNG: My recollection of the subsidy is that the surcharge collections from the voluntary market were about \$80 million in 1984. Is that about the right number? (addressing someone in the audience)

FROM AUDIENCE: In '84, it was about \$135 million.

MR. YOUNG: I'm sorry -- \$135 million. So that would increase the deficit by that amount.

SENATOR ZANE: So, to match the numbers up, when you are projecting the half a billion dollars, by then the additional moneys paid in by other insured motorists would be an additional \$135, or would it be more than that by that time, when the half a billion dollar deficit comes up?

MR. YOUNG: The half a billion dollars is already offset by the moneys paid in by the voluntary market.

SENATOR ZANE: Okay. So, would it still be \$135 million by that point, or would there be more moneys than that paid in by the time you reach the half a billion dollars?

MR. YOUNG: Well, it would be that amount for each year.

SENATOR ZANE: In other words, it would have been \$635 million, but for the underwriting by the other motorists?

MR. YOUNG: No, I think the number would be closer to \$700 million.

SENATOR ZANE: Okay. It would seem to me if that is the case that the JUA then would not have any investments. Is that correct?

MR. YOUNG: We have investments because of the time lag in paying claims, particularly liability claims. An accident occurs and, depending upon its seriousness, it could take several, even three or four years to run the process, particularly if it is being litigated to settlement. During that period of time, we have the funds on investment. We keep the moneys there. We invest them and use that investment income to offset or reduce the ultimate net loss.

SENATOR ZANE: And, again, to match up with the same period of time, what is that investment income that you realized, or what will it be?

MR. YOUNG: The dollar amount?

SENATOR ZANE: Yeah.

MR. YOUNG: I'm not sure that I have the specific answer to that. The investment income in 1984 was--

FROM AUDIENCE: Thirty-eight million.

MR. YOUNG: Approximately \$38 million in 1984. That amount will be higher in 1985. Again, we will know in a few weeks the exact amount.

SENATOR ZANE: Okay. Let me ask you one other. I guess from Motor Vehicle, are there -- what, I guess we could call it accounts receivable, that you know exactly what those amounts are that you should be getting on the surcharge?

MR. YOUNG: What we do know from the DMV is what they have billed.

SENATOR ZANE: Let me ask it very directly. What does the Division of Motor Vehicles owe your department?

MR. YOUNG: What was the billing for 1984?

FROM AUDIENCE: I don't have that.

MR. YOUNG: We can go back and get that information for you. I hesitate to give you a ball park--

SENATOR ZANE: I'm sorry?

MR. YOUNG: I hesitate to give you a ball park guess at this point as to what they have uncollected. We don't know what is uncollectable. We can only tell you the difference between what they have billed and what they have paid us. Those are the only figures we get, so we don't know if a driver has subsequently moved out of the State, is deceased, things like that.

SENATOR ZANE: I'm told that the numbers are probably somewhere in the area of \$125 million. Does that seem reasonable to you -- that is presently owed to the JUA?

MR. YOUNG: I would have to say that is probably not too far from the truth.

SENATOR ZANE: Okay. Now the effect of that on the deficit would be what -- to reduce it, or is it so ongoing that it--

MR. YOUNG: If we had that money, it would reduce the deficit by that amount, plus whatever investment income we could generate on that money between the time we received it and the time we had to pay it out.

SENATOR ZANE: And one other question, and then that's it. From the time the Division of Motor Vehicles collects it, is there a lag period before you get it?

MR. YOUNG: Yes, there is.

SENATOR ZANE: How much time?

MR. YOUNG: We don't know because we don't receive any information which would tell us when moneys are collected and when they are transmitted to us.

SENATOR ZANE: Do you know what the Division of Motor Vehicles does with that money during that lag period, whatever it is?

MR. YOUNG: No, we don't.

SENATOR ZANE: Don't take this in the form of being chastised, I don't mean it that way, but don't you feel that

you should have a handle on that? Isn't that really money that if there was a long lag period would be available to you in the form of investments to further reduce--

MR. YOUNG: We have asked questions of both the Department of Insurance and DMV hoping to find out some of that information -- not all of it, but some of it. We have not received a response to that.

SENATOR DALTON: We'd like to wrap this up, if we can. Do you have a question, Chris?

SENATOR JACKMAN: Yes.

SENATOR DALTON: And Senator Laskin does also. We have the Department out there too, and we only have another hour to spend with the Department. So, Chris? -- and then Senator Laskin.

SENATOR JACKMAN: I'm just interested in the uninsured motorist today. What figure would you think was uninsured today in our State?

MR. YOUNG: Based on information I've seen, Senator, I'd have to guess 10% to 15% of the drivers are currently driving without insurance.

SENATOR JACKMAN: Half a million? Is that it?

MR. YOUNG: I believe there's somewhere around five million drivers or so, yes.

SENATOR JACKMAN: Half a million? An accident happens -- uninsured driver. The other insurance pays, JUA pays. How do you collect from the uninsured motorist?

MR. YOUNG: We don't.

SENATOR JACKMAN: You don't?

MR. YOUNG: Because most of these drivers don't have any assets or any money that we can go after, so they're-- They cause the accident, or they receive benefits from our policyholders, and there's very little we can do.

SENATOR JACKMAN: Well what have we done to ensure getting the uninsured motorist insured? I mean, not you -- not

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you per se, JUA -- but the the DMV, but what has anybody done with these people? Wouldn't you agree that a lot of your money would be going to the uninsured motorist -- is being paid out because of an uninsured motorist having an accident and not being responsible for anything?

MR. YOUNG: Yes, sir. We are paying out considerable amounts of money in that area.

SENATOR JACKMAN: All right. Now, go back again. The uninsured insures himself for one month. The agent gets-- Let's hypothetically use figures again. Insurance costs \$600. The insurance agent would get \$60.

MR. YOUNG: Correct.

SENATOR JACKMAN: Right -- 10%? He's insured for one month. He only paid \$56. We lose \$4 for the guy being insured for only one month. He quits. That's possible, isn't it?

MR. YOUNG: Theoretically, but as a practical matter, he'd collect more money.

SENATOR JACKMAN: How much do you collect the first-- Well, for example, if I want to be insured. Do you have to pay one month? Do you have to pay three months for insurance?

SENATOR LASKIN: Three months.

MR. YOUNG: Approximately three months.

SENATOR JACKMAN: Approximately three months?

MR. YOUNG: A little more than that.

SENATOR JACKMAN: Yeah.

MR. YOUNG: Now, billing is such that the amount of money we collect, less the commission -- the next bill is due at that point in time. So, there should be a zero on that.

SENATOR JACKMAN: DMV doesn't do anything with the uninsured motorist as far as -- to your knowledge? The accident occurs. You pay out. JUA pays out. The sum total could be \$5000, or whatever it may be. You pay it out. This guy paid \$180 worth of insurance, quits, and now he rides free for nine months. He has this accident. Is there anything happens to this individual?

MR. YOUNG: I know that the DMV has certain procedures that they can follow to suspend his driving privileges, but if they suspend, he can still continue.

SENATOR JACKMAN: By the time he gets through that phase, I guess five years will go by because the computers are backed up, they tell me. I mean, I'm not kidding you when I say that, because I call up and they tell me the computers are backed up. I mean, the guy goes five years without--

If every one of those people were in your JUA today, and there's a half million of them, and they said "just average," and they paid \$500, you've got yourself \$250 million bananas.

MR. YOUNG: Well, we would have to pay some claims out of that.

SENATOR JACKMAN: Yeah, but there's money there. That's why I get a little annoyed with the JUA -- not you now. I think the DMV is responsible here, a little bit more than your area. That's enough questions. Go ahead.

SENATOR DALTON: Senator Laskin?

SENATOR LASKIN: Mr. Young, I'm going to ask some questions pertaining to what I see as the reason why we're here. It's nice that we get all these technical disclosures about all these agencies, and I'm sure they're very worthwhile and helpful to us in making decisions, but I'm somewhat impatient. I think that we know how to solve the problem. I get annoyed that we haven't done it yet.

You point out about insurance. If you didn't have mandatory insurance, we wouldn't have the problem that you and Senator Jackman were just talking about; we could save a lot of money. That's a more basic issue. If you didn't have mandatory insurance, then you wouldn't have to strike premiums based upon the possibility that everybody gets insured -- the good drivers, the bad drivers, etc. That's sort of a deeper issue that I don't think we can handle so superficially here.

Relating to the area where I think we could save some money under this system or any system, the inflated over treatment that you discussed earlier, the inflated medical bills, the over treatment of an injured person -- apparently nothing is really done about it, except that you indicated that some of the insurance companies who you call your servicers -- because you don't do this yourself -- are charged with the responsibility of making sure that there's no fraud, or an absence of fraud, or as little fraud as possible.

Now, here's the problem: A servicer, an insurance company, who does your work, and who apparently has to because there's not enough money to fund the JUA Fraud Bureau -- Investigation Bureau -- and all these other things that we need, gets paid a fee. They get paid that fee whether they do a good job or a bad job. They get paid a fee for handling the claim. Am I right?

MR. YOUNG: That's correct.

SENATOR LASKIN: Okay. Now, if they save you money that's wonderful. If they spend more money than the case is worth, that's terrible. But, there's nothing you can do about it. They get paid a fee for handling the claim. There's absolutely no incentive on behalf of, or on the part of that insurance company adjuster to save JUA money because they're going to get paid the same fee whether they do a good job or a bad job, isn't that true?

MR. YOUNG: Ah-- That's probably a good general statement, yes.

SENATOR LASKIN: Now, however, if the insurance company is investigating its own claim, the insurance adjuster who works for that company is under a lot of pressure to make sure he checks into these things and settles the cases as cheaply as possible because that's going to affect his job. Isn't that right?

MR. YOUNG: That's correct.

SENATOR LASKIN: Okay. So, this goofy system that we have -- and I call it goofy, and I'm as courteous as I can be -- only gives incentive to cost more money, not to save money. Isn't that really true?

MR. YOUNG: As it currently exists, that's a fair statement.

SENATOR LASKIN: That's what bothers me. There are so many basic problems, and here we are worrying about the insurance agent's commission and this and that, when we have enough information, in my opinion -- and, of course, everyone has their own opinion -- we've got enough information now to solve this problem, in my opinion. And we just seem to be going around, and around, and around over these little points that really don't go to the heart of this problem that we face. That's a basic wrong with the system, and we could correct that.

Sorry, Mr. Chairman.

SENATOR JACKMAN: Give us the answer.

SENATOR LASKIN: I gave you the answer.

SENATOR DALTON: Mr. Young, first of all, on behalf of the Committee, I want to thank you very much. This is your second time here, and we've put you through the mill here a little bit, and we really appreciate the amount of time that you've spent with us and the detail of your answers, and the insight that you've provided us.

Several months ago, Commissioner Gluck indicated that she would like to -- she wanted to testify in this whole area of the JUA. However, she also advised the Committee that because of certain litigation between the JUA and the Department, that those questions and that testimony would have to be taken in executive session. So, what we'd like to do now is, the Committee will go into executive session to hear from the Department. The only people who will be allowed in the room are either OLS staff or partisan staff, to hear from the

Department of Insurance.

So, thank you very much, Mr. Young.

(EXECUTIVE SESSION)

AFTER EXECUTIVE SESSION:

SENATOR DALTON: Sir, you're from--

DEPUTY COMM. JASPER JACKSON: The Department of Insurance.

SENATOR DALTON: The Department, okay. Jasper, we have 45 minutes to spend with you on this whole issue of the JUA and the JUA deficit. I think what I'd like to do -- and the members of the Committee agree -- is, we'd like to start out with your feelings on the deficit, a description of the deficit, how we came to the deficit, and how we can extricate ourselves from this situation. I think they're the-- You've got 45 minutes. It's an essay question. You'll be graded. (laughter) But I think those three questions are the heart of what we've been trying to get at with Mr. Young, and, obviously, we wanted your perspective on it, since Commissioner Gluck was very -- she wanted to come here and to testify on this specific issue. She wanted the Department to here here.

MR. JACKSON: Okay. Well at the outset, let me say that before I leave I should be able to leave with every member of the Committee the Commissioner's recent decision on the JUA's application for a RMEC to fund what they contend the deficit is. We were under the impression that document had been delivered to you all last week, and I just discovered through our Legislative Affairs Unit that it had not been, and they are in the process of putting it together. I think that document, once you review it, will answer a lot of your questions and it will crystallize a lot of the issues.

You asked me to identify the deficit. I hate to say it, but I cannot do that. But I'd also like to say that neither can the JUA. The JUA right now contends that it is operating at a \$200 million deficit on an annual basis, for 1984 and 1985. Now, the way they get there is, on the basis of the old assigned risk data, they take -- they've taken the three most recent year's experience, meaning the last three years's experience -- operating experience -- of the old Assigned Risk Plan, and they've projected that into the future as if that experience will be more or less the same type of experience that they can expect in the JUA. We do not believe that to be true for a number of reasons.

One, when the Assigned Risk Plan went out of existence, there were not a lot of laws on line, that are currently on line now, that were designed to reduce the cost of automobile insurance across the board, whether it's for a voluntary market carrier or a residual market carrier, like the JUA, or the old Assigned Risk Plan.

For instance, the AIP data does not reflect the impact of the law that was enacted in 1981, that would require child restraints in all passenger vehicles for children. It does not reflect the data that has been produced by the law that mandates seat belts. It does not reflect the cost containment options. It does not reflect the tort threshold option. It does not reflect a number of laws that have been brought on line to either contain cost or reduce cost.

So, we don't believe that the JUA will have experience upon which credible rates or predictions can be made until at least the end of this year, which would be 12/31/86. That would give us three years of operational data for the JUA itself: 1984, 1985, and 1986. Even then, a lot of these cost containment laws, or the experience produced by them, will not be fully reflected in the JUA data base.

Another problem we have is that when the JUA came into

operation, the Legislature also created a funding mechanism for it. The centerpiece for the funding mechanism was the driver record surcharge system under the-- But the legislation contained instructions as to how that system was supposed to be set up.

I cannot speak to the type of review that was undertaken by Commissioner Murphy and the actuaries in the Department at the time that Commissioner Murphy was there. But, we suspect that the driver record surcharge system was never set up correctly, pursuant to the legislation. It had two instructions as to how it should have been established. One is what I will call a minimal instruction, and that is that if someone had driver record points of six or more, there was supposed to be a \$100 minimum surcharge, and \$25 per point for every point after six. But, another section of the legislation instructed that in the first year of the JUA's operation, the driver record surcharge system should produce the same amount of money that the old Assigned Risk Plan had produced, once you deducted what would be collected from compelling the JUA to utilize the rates of ISO, which is the largest rating organization in the voluntary market.

It appears to us that that was never done. As a consequence, we believe that the JUA may be out of about \$50 to -- somewhere between \$50 and \$100 million that should have been assessed against drivers accumulating points that were never assessed.

Another problem seems to have been created in the JUA surcharge system by itself. Although the law instructs the JUA to utilize the ISO standard market rates, it gave the JUA the ability to fix and assess -- to establish its own accident surcharge system. For some reason, when the JUA established its rating system, it copied the entire ISO rating system, not only the basic premium rates but also the accident surcharge system. By doing so, it utilizes an accident surcharge system

that is based upon the experience of ISO insureds and not upon the experience of JUA insureds. So, we're in the process of helping them straighten that mess out.

Another problem -- another reason why we have difficulty in coming to what a deficit is right now is also due to the policy constants. As you know, when the Assigned Risk Plan went out of existence, all the carriers were collecting approximately \$70 per car in both markets for motorists who have a full complement of coverages, meaning both liability and physical damage coverages. Well, there appear to be two problems. When the Commercial Insurance Deregulation Act of 1982 went into effect, or when the legislation establishing the JUA became operative, a number of carriers -- most notably, ISO -- removed policy constants from the private passenger type cars that are being written in the commercial market. We did not believe that to be proper.

Now, we permit the companies, because of the various market strategies that they have, to write private passenger types in the commercial market if it helps them with their marketing strategies, but because it's a private passenger type car, regardless of what market it's in, the policy constants should have been attached. We estimate that the JUA is losing something like \$15 million a year just on that basis.

Another problem that we appear to have is that when the Legislature passed the legislation ordering that the policy constants income be turned over to the JUA, all the data before the Department, demonstrated that at least \$225 million a year should have been transferred to the JUA just off the policy constant.

The numbers that we have before us about policy constant collection-- In 1984, the JUA collected only \$85 million in policy constant income. In 1985, they collected approximately \$139-1/2 million. In the first three months of this year, they've collected approximately \$35 million. Well,

looking at the annualized figures in 1984 and 1985, if we believe that they should have been collecting \$225 million a year, and, in fact, in 1984 they collected significantly less than half of that amount, and in 1985 they collected approximately half of that amount, then somewhere in the pipeline there's still \$100 million in both years that is owed to the JUA.

The Department is currently in the process of putting together a survey -- a company survey which is designed to find out from each company the number of cars they have, the number of policyholders they have, the number of policyholders per car, and the amount of coverages that they wrote in both years, and the amount of money that they actually transferred to the JUA. But, once we get the basic raw data, we can compute what the amount of policy constant income they collected, and what should have been transferred to the JUA.

So, I guess in my mind -- even assuming that the JUA was running at a \$200 million annual deficit -- there appears to be money in the pipeline somewhere that should have been transferred to the JUA that has not yet been transferred to the JUA. It appears that the accident surcharge system was not -- that they have never established an accident surcharge system based on their own experience, as they should. They're losing money there. And, it also appears that the driver record surcharge system was never set up properly, and we're taking steps to see that that occurs. But, there are other problems in a driver record surcharge system.

When the system first came on line, everyone made predictions as if once a surcharge was assessed, the money would be collected immediately up-front, and that's simply not the case. First of all, the surcharge is a function of licensure. The surcharge is not assessed against the license until the license comes up for renewal. In New Jersey now, they renew some licenses for a two-year period. So, even if in

1984 you have a licensee who should have been surcharged, if the license was gotten, let's say, January 1, 1984, we cannot surcharge that person until-- Pursuant to the current procedures of the DMV, that person would not be surcharged until January 1, 1986.

Another problem is that everyone's predictions also did not take into account that a lot of motorists would be permitted to pay the surcharge income on an installment basis.

Another thing that was not taken into account was that some of -- a large number of drivers, for various reasons, would have their licenses suspended, and even though they were assessed a surcharge, they would not pay those surcharges until they actually returned to the marketplace.

Now in 1984, the figures on DMV surcharge collection showed that they only collected about 30% to 35% of all the driver record surcharge moneys that were levied against different motorists. But, at this date, in 1985, they have now collected approximately 85% of all the surcharges that were assessed in 1984.

In 1985 the collection rate is running slightly higher than what that 1984 rate was, but based upon the way the system actually operates, and the collection rates, we don't believe that the driver record surcharge system itself will mature for about a three-year period; only, it appears that because the way it's set up, and because of the various installment plans and license suspensions, and everything like that, that in any particular year-- Let's say if DMV was to assess \$200 million in surcharge income in 1985, you really could not expect to have 100% collection until over a three year period. And, that being the case, rather than making the predictions as to getting all the money in now, you'd have to spread it over a three-year period.

One of the problems with the JUA projections about the \$200 million deficit is that they project a deficit of \$200

million in 1984, but what they've done is, they did not take into account the \$225 million that they're supposed to get on an annual basis on a policy constant income. If they looked at their books of a town, and they had only collected \$35 million, then they said, "Well, we only got \$35 million worth of policy constant income." They didn't take into account the other \$100-plus million that was missing.

When they looked at the -- once again in projecting the deficit -- driving record surcharge system, they did not look at the amount of surcharges that were assessed and what the collection rate was, and how long it would take for the system to mature. They simply said, "If we have \$20 million in surcharge income, that's what we collected." Then that's what they reflect in the book, and then they projected the deficit, and they projected the deficit into the future. We don't believe that's correct because if we permitted them to fund the system that way and then we brought a RMEC on line to, say, raise the \$200 million that way, assuming that all the predictions were correct, well into the future when this other money began to come in over time, there would be a lot of excess money in the system. So, we would then have the problem of reducing the rate.

Another thing that makes it difficult to assess what the deficit now, and what it probably will be, is that the JUA, when it first came on line, was supposed to establish a uniform reserving system for its loss reserves. It never did. It has 15 separate and distinct servicing carriers, and it has permitted each servicing carrier to utilize whatever its reserving philosophy was with respect to its own voluntary market business, and it never reviewed what the various reserving philosophies of each company was.

As a result, we've had to order a financial audit of the loss reserves so we can establish-- One, we feel there are a number of things going on. Different companies at different

points in the year, depending upon what's happening with their book of business, change their reserving philosophy, and when they change their reserving philosophy it has an impact on the bottom line. It changes what the projections are. So, we have a feeling that because there's no uniform reserving philosophy, that some companies' reserves may be overstated and some companies' reserves may be understated. We don't know. But one thing we do know, when we initiated the financial audit we found out that the companies had established -- whatever philosophy they were operating by -- bulk loss reserves, and they did not discount those loss reserves for the investment income that would be earned on them.

So, just in terms of looking at their annual deficit projections of \$200 million, we found that the reserve should have been discounted by something like 8% to 10%. Had that been done, that -- in and of itself -- removes about \$80 million from the \$200 million deficit that they make.

Another problem is that when the system was established and they worked out the remunerative system for the servicing carriers, the reigning commissioner then -- once again Commissioner Murphy -- accepted a formula which believe fosters a lot of problems.

One, we think it may foster over reserving because on the liability portion of the coverages, the claims reimbursement fee is a function of whatever the law says. Let's say for every \$100 in loss reserves that they have on the liability side, they get reimbursed at a rate of 16%, or \$16. It doesn't take a mental giant to see that if a company wanted to enhance its expense reimbursement, then all it would have to do is initially overstate the reserve, and by overstating the reserve, it can enhance its recoupment on expenses.

Another problem with that reimbursement mechanism is that it does not take into account the various differences between the servicing carriers. Some servicing carriers are

direct writers and some are stock agency companies. The direct writers have significantly lower expenses than stock companies do. But the reimbursement fees now reimburse all companies pursuant to the same formula, as if they're all on an equal footing basis with the same level of expenses, and they are not. So, once again, our concern is that some companies are being over-compensated and some may be slightly under-compensated.

We believe that there should be a service carrier reimbursement on a structure that works on a graduated basis. But, once we straighten it out, that will return additional moneys to offset losses.

But, another problem with the system-- And, once again, you have to look at the types of servicing carriers. Some are stock companies and some are direct writers. Direct writers mean that they do not employ independent agents to produce their business; they use company employees.

The way the JUA law is structured now, regardless of whether it's a direct writer or a stock company, an agent producing the business, or an employee producing the business, is entitled to an 11%, or 10% agent's commission. The direct writers, notably Allstate -- I know Allstate and Prudential does this, although Prudential is a stock company; it operates only through a direct writer -- has branch offices out of which its employees operate. Prudential has offices out of which its employees operate. State Farm has branch offices out of which its employees operate.

What they're doing-- Although they're supposedly being fully compensated for whatever their expenses are, pursuant to these claim expense and administrative service expense formulas that were approved by Commissioner Murphy, what Allstate has said to its agency force, and what Liberty Mutual has said to its agency force is, "Well, for the JUA business, you're utilizing our office space, so we're going to

charge you a fee for that; we're going to deduct from your-- First of all, since you're not an agent and you're a company employee, we're not going to give you the agent's commission. Second of all, whatever fee we give you we're going to deduct from that fee the cost of your utilizing our office space."

The problem that presents for us is, once again -- to the extent that they are supposedly being fully compensated for whatever their expenses are through these fees, once they extract these moneys out of their employee force, then rather than permitting that money to flow into their own coffers, that money should come back to the JUA.

SENATOR DALTON: Jasper, aren't all these problems that your're outlining -- aren't they all under the control of the Department?

DEPUTY COMM. JACKSON: Yes, they are.

SENATOR DALTON: Yeah, I was going to say this sounds like an indictment of the Department as opposed to the JUA.

DEPUTY COMM. JACKSON: Well, if it sounds like an indictment of the Department, let me say this: I'd say I can't speak for Commissioner Murphy because I don't know what was in his mind when he approved these things.

I do know that there was a short time frame. I know he was operating in a short time frame in terms of getting the JUA set up and established and maybe that accounts for some of the problems that we have.

As lot of the other problems, they're functions of the Department, but it takes time to uncover what the facts are. We have a financial examination going on to test the loss reserves and servicing carrier fees, and a lot of the other problems that are there. We've been involved in that process now for various phases of it, also including investigation of the DMV surcharge system and the problems with it. We've been involved in the various elements of it now for about a year, and I project that it's going to take us another three to six

months before we can come to a bottom line on that whole mess. A financial examination just takes time, particularly when--

You know, let me put it this way: We have about 260 employees within the Department. If we could take those 200 people and assign them all to the various types of problems that we perceive to be in the JUA operation, we probably could have had it done in three months, but we can't do that because we have a multitude of other duties and responsibilities, so it just couldn't be done on that basis.

Also, when I came into the Department, along with Ken Merin, we were told that there was a justifiable basis for just about everything that had been approved. It took us some time to discover all the documents upon which the system is predicated, and to review and have those documents analyzed before we could identify exactly where the problems were and what the nature and the magnitude of the problems may be.

SENATOR DALTON: Okay. Are there questions from the members? Senator Connors?

SENATOR CONNORS: After all of this study that you've been working on, I notice you were either very careful, or you were just talking that you were promised that there wasn't going to be a deficit.

DEPUTY COMM. JACKSON: I acknowledged, what?

SENATOR CONNORS: That there is going to be a deficit.

DEPUTY COMM. JACKSON: I don't acknowledge that. I-- Let me explain to you.

SENATOR CONNORS: You said there was going to be a surplus?

DEPUTY COMM. JACKSON: Let me express it in this way: If you look at-- If you can take the Assigned Risk Plan level of losses at the time that the Assigned Risk Plan ceased operation, and then you take the JUA and project the income that the ISO rates produced, and the income that the driver record surcharge system produced -- based upon the way that it

was established -- then one would be able to say that there is going to be a deficit. But even then you would be hard pressed to fix exactly what the deficit is going to be because you have to be able to predict inflation.

Now, the way the actuaries do it, if they predicted inflation off of the old AIP -- of the old assigned risk data base -- they would come up with double digit inflationary numbers which would not be reality with respect to what actually transpired from '84 to this period in time.

SENATOR CONNORS: Thank you for taking me by way of left field. All I'm saying is, you've been studying it for a year -- okay? Do you intend to study it for another year?

DEPUTY COMM. JACKSON: We intend to have an ongoing study of the JUA.

SENATOR CONNORS: Do you think it will take another year before you'll be able to arrive at some kind of a decision?

DEPUTY COMM. JACKSON: No, I think that we are no more than three to six months away from what the bottom line is with respect to certain parts of the problem. We will not be able to project, we feel, within a zone of reasonableness, what the actual deficit may be until--

SENATOR CONNORS: There you go again: "What the actual deficit may be." You are talking in terms of a positive deficit.

DEPUTY COMM. JACKSON: Well, deficit if there is one. Right now, I guess I'm talking from the vantage point of the JUA contending that there is a \$200 million deficit.

What I'm saying is, assuming that there is a deficit, I know it's not \$200 million.

SENATOR CONNORS: You know it's not going to be that loss?

DEPUTY COMM. JACKSON: I know it's not that loss. I know it's not that loss, just from looking at what they presented to produce the \$200 million.

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SENATOR CONNORS: But you think there very well may be?

DEPUTY COMM. JACKSON: Based on the way the system is going now, somewhere in the area of \$50 to \$100 million, if that much.

SENATOR LASKIN: Wait a minute. I don't want to leave this. I only want to ask one question.

SENATOR CONNORS: Go ahead.

SENATOR LASKIN: We've had so-called responsible, reasonable leaders of the JUA appear before this Committee-- And I'm not talking about anybody being a liar or unethical or dishonest; these are figures and anybody can misinterpret them. But we've had statements here which shocked us to death, that in 1989 there would be a \$1 billion deficit.

DEPUTY COMM. JACKSON: That's if you can believe their numbers. I don't believe those.

SENATOR LASKIN: All right, let's assume they're off a little bit, and you're off a little bit. Are we at \$800 million? I mean, you're talking about a \$1 billion estimate, not a \$100 million estimate.

DEPUTY COMM. JACKSON: First of all, I don't believe the numbers. I don't believe it's going to be \$1 billion, but even if it is \$1 billion-- Let's assume it is \$1 billion. In 1989, let's say they're operating at an annual deficit of \$200 million, as they contend, and, come January, sometime in 1989, there's a \$1 billion deficit. Well, even if there is, that deficit will not have to be paid out at that time. That deficit will run off in the same manner that it was built.

SENATOR LASKIN: We know it won't have to be paid in January, but it keeps getting bigger, and bigger, and bigger.

DEPUTY COMM. JACKSON: But the point is, it will run off over time, almost in the same way in which it accumulated. So, even assuming that there's a \$200 billion deficit that's going to build to \$1 billion in 1989, do you extract now from policyholders \$200 billion every year -- \$200 million every

year -- just so they can throw it in a bank and it can remain there for a number of years?

SENATOR LASKIN: We don't know that answer, that's why the Chairman's getting all these witnesses here. We need help. I mean, we all get scared to death when somebody comes up here and says, "You're going to have a \$1 billion deficit in two years." That's scary. We don't know what to do with it.

DEPUTY COMM. JACKSON: Well, we don't believe it's going to be \$1 billion for a host of reasons. Whatever the cumulative deficit is, it will not have to be paid off at one time. It will run off over a number of years almost in the same manner in which it accumulated.

But, one thing I do know is, once the Department feels it can make a reasonable estimate with respect to whatever deficit it may be, the Department will take steps to raise the revenues to match the runoff period.

SENATOR LASKIN: That means increased premiums.

DEPUTY COMM. JACKSON: Well, not necessarily. We may make adjustments in the surcharge system. You see, the way we interpret the current law is that the Legislature, by enacting it, intended to provide, essentially, a fair market rate to every insured in the marketplace with a clean record, regardless of what market they were insured in. And, to the extent it was possible to do so, shift the cost of actual accidents to those who were actually involved in accidents, or had a certain driver record profile.

The mechanism is there to do that. It's there in the driver record surcharge system, it's there in the accident surcharge system, and it's there in a category that was created by the enactment of A-3913, something called the "dangerous driver," which will permit the Department to take into account the total record -- the total driving record -- of all motorists in the market, meaning both their moving vehicle violation record and their accident involvement record.

SENATOR DALTON: Carmen?

SENATOR ORECHIO: Yes. Jasper, are you supporting your position in terms of this deficit not being as large as what was said in testimony by the Chairman of the JUA, on a number of things -- number one, the money that should be in the system and isn't because of the collections? Secondly, you pointed out before that the old assigned risk projected losses cannot be used as a standard with JUA projected losses because of what we have done with cost containment, the seat belt law, and the alternate threshold in terms of separate pain and suffering.

DEPUTY COMM. JACKSON: Yes.

SENATOR ORECHIO: Those factors?

DEPUTY COMM. JACKSON: Yes. See, what we believe is that they-- See, without getting into technical arguments that actuaries, economists, and accountants would get into, one thing we are certain of is that the assigned risk plan data base is not a credible data base for the JUA upon which to predict their loss future costs, and that is what they have done.

Aside from the fact of it appearing-- Let's say once again that they are running a \$200 million deficit. Well, they have tens of millions of dollars of policy constant money still in the company coffers somewhere, that should be transferred to the JUA. If the driver record surcharge system was never set up properly and you make adjustments there, if they haven't discounted their loss reserves and the time value of the money that that money sits in an account, and you compel them to do that, if you establish a reimbursement schedule that makes sense, given the type of servicing carrier, even assuming that there is a \$200 million deficit, all of those adjustments are going to have a dramatic impact on it -- are going to have a dramatic impact on reducing it.

That is what I am saying, even assuming -- and I am willing to assume for the sake of this discussion that their figures are right-- Until other adjustments are made, we would not dare predict what the accumulative deficit is going to be, in 1989, as they contend, nor would we dare predict what a RMEC would be, if one has to come on line. But in our mind, the way we interpret the law, there are a host of things that we have to do before RMEC can come on line. The way we interpret the law, the RMEC is a measure of last resort, only to be utilized when the funding mechanism set up for the JUA -- when all of the moneys have either been fully incorporated into JUA's operation, or we can reasonably forecast what the incorporation of that money will mean. Only then can we consider a RMEC, or the assessment of a RMEC. We simply are not in a position to be able to do that yet; one, because we don't have a credible experience base from the JUA in terms of the actual operations of the JUA itself; and also, there appear to be all sorts of problems in the funding mechanisms, some under the control of DMV, but some, quite frankly, under the control of the companies.

Then also, I think, Senator Laskin hit upon an issue when he was speaking with Mr. Young. We are also interested, and we are auditing all the servicing carriers also. We're auditing not only how they treat their JUA business, we are also auditing how they treat their voluntary market business because whatever their philosophy was with respect to settling an automobile claim, it should have been the same in both markets. If we find that they have effected a different standard in both markets, then we are going to penalize them for it, and we are going to assess the companies for it.

SENATOR DALTON: You know, I agree with that. Lee brought up a good point. We are all concerned about the fundamentals here. Let me ask you a fundamental question. You've got the largest insurance entity in the State, the JUA,

insuring 50% of the cars in this State -- 50% of the cars. Nobody even comes close to that, as far as a market share. Okay? But the JUA is utilizing non-JUA rates to come up with a premium. Isn't that fundamentally a problem?

DEPUTY COMM. JACKSON: No.

SENATOR DALTON: It's not a problem?

DEPUTY COMM. JACKSON: As a matter of fact, I think it is the most equitable system in the country. Do you want to know why?

SENATOR DALTON: Tell me why.

DEPUTY COMM. JACKSON: Because you, as legislators, have chosen not to feather the underwriting judgment of an insurer at all. What that means is, an insurance company operates on the basis of spreading its risk over the broadest possible base, and the way rates are made-- The rates are made-- A company files for a rating manual, and the rating manual is approved and produces rates by class and by territory on an average rating basis. If a company-- Whatever high risk insureds they have, whatever average risk insureds they have, whatever low risk insureds they have, the rating manual is supposed to produce a rate on average that will permit them, after they pay for anticipated losses, after they pay for expenses, a reasonable profit.

But that assumes that a company is out there, if someone comes in the door, that as long as they have a rate on the books from which they can charge that individual insurer, that on average they will make a profit, then they should write them. But the companies don't do that. What the companies are trying to do-- Each company is out there trying to do better than the average statistics. What they want-- They don't want to write any risk that may come through the door. I may come to the door and I may live in Newark. I may have been driving for 20 years. I may have never had an accident. I may never have had a driver record incident, but there is one thing that

is true about my living in the City of Newark. It is the most densely populated automobile territory in the State, and all other things being equal, whether I had an accident or not, the likelihood that I will have an accident is greater than, say, with a person living in Princeton Township, or even Trenton.

So, a company underwriter looks at it and he says, "Well, this guy has never had an accident. He has a clean record, but he is living in Newark, a higher than average territory, and there is a higher than average likelihood of him having an accident. I don't want him." So, what they are seeking is a better than average risk. If you look at State Farm, State Farm's whole book of business is almost a preferred book of business. Almost everyone who they write voluntarily is someone who comes out of a lower than average rating territory or lower than average class. The question you have to ask is, is that really insurance, and is that fair to those motorists in the market who, although they never had a driver record incident or an accident-- Is it fair to permit a company to reject them simply because they are in a classification that has a higher than average loss ratio, or because they live in a territory that has a higher than average loss ratio?

If you look at the JUA--

SENATOR DALTON: But the thing is-- Let's take your Newark example, okay? You have the person who comes into the agent from Newark looking for a personal auto policy who is placed in the JUA, okay?

DEPUTY COMM. JACKSON: Yes?

SENATOR DALTON: Nine times out of ten, if there is anybody in Newark who is not written in the JUA -- I suspect there aren't that many people -- his rate is based upon ISO, an ISO rating system. What I'm saying is, what is the correlation between an ISO rating system and the people in the JUA?

DEPUTY COMM. JACKSON: There is none.

SENATOR DALTON: That's what I'm saying.

DEPUTY COMM. JACKSON: Yeah, but what I'm saying is, why should the poor slobs with the clean records who, for no reason of their own, are compelled to purchase insurance, when you have chosen to exercise no control at all over companies' underwriting judgment-- The one thing I do know is true about the residual market is that most of the really bad-apple drivers, hazardous drivers, dangerous drivers in that market -- whatever percentage of the market they may be-- The problem for the clean-record driver, if he is thrown into that market, and that market is then rated on the basis of that market, is that that poor slob with the clean driving record is going to bear, totally, the burden -- is going to bear the total burden of the bad apple in the marketplace by himself. That is the problem, in my mind.

SENATOR DALTON: Senator Orechio, I interrupted you; I'm sorry. Do you have any more questions?

SENATOR ORECHIO: No, thanks.

DEPUTY COMM. JACKSON: You know, you can go to other rating regimes, you can make that market self-supporting, but if that market becomes self-supporting and the experience is anything like the AIP experience, the rates will be so humongous that the drivers won't be able to afford them, and you will have a tremendous uninsured motorist population on your hands. People are going to drive -- well, you can shake your head--

SENATOR DALTON: No, I'm not shaking my head. Some of the people on this Committee say, "Let there be a significant uninsured motorist public out there. Let liability be voluntary."

DEPUTY COMM. JACKSON: Well, what will happen is, the course will still be there. The people who are injured in accidents by uninsured motorist drivers will be made whole by someone. If they are not made whole out of the automobile insurance regime itself, then they will simply become wards of the State. Taxpayers will pay for it in one way or another.

SENATOR CONNORS: No -- excuse me. It is my understanding that the law we presently have on the books-- The reason why most people are being thrown into the assigned risk -- and 50% of the insured motorists are now in the assigned risk -- is because we said you can't cancel it. A company has no-- You can't cancel their insurance except for revocation of license or nonpayment of the bill. Is that true?

DEPUTY COMM. JACKSON: That's not true.

SENATOR CONNORS: It's not true?

DEPUTY COMM. JACKSON: It's not true. The Department has a regulation--

SENATOR CONNORS: Well, some of the documents we have here, if it's not true--

DEPUTY COMM. JACKSON: It's not true. The Department has a regulation that has been on the books for a number of years, and it enumerates the factors by which automobile insurers are permitted to either cancel or non-renew an insured. If you look at the list -- and I have done this because they came to the Department when I first came there with Ken Merin and made that complaint-- We looked at the enumerated factors, and it was difficult for us to find a reason other than those enumerated by which an automobile insurer should be permitted to cancel or non-renew someone. It covered a whole range of incidents. What they wanted was simply the ability to be able to cancel or non-renew someone for whatever reason, whatever business perception, whatever reason they had. They just offered no reason at all. They just wanted to have the ability to cancel a certain percentage of their book in any particular year.

SENATOR CONNORS: It's got to be one or the other. If there are good drivers who have had no accidents and no tickets, just little old ladies who buy insurance -- and there are a handful of those -- there is no incentive for them to be pulled out of the JUA and placed in the voluntary market by the

insurance companies. They make out better by having their agents get the commission, under the law, and handling the administration of the claims, and then when there is a claim, JUA pays the bill. If there is not enough money, REMEC, constant--

SENATOR DALTON: Len -- and it's not because it isn't a good question -- I am going to have to cut you off now. We have an 11:30--

DEPUTY COMM. JACKSON: May I just answer that one question?

SENATOR DALTON: You can answer it to him individually. You know, I'm sure he is interested in your answer, but the rest of us have to go for a quorum call.

The next meeting is May 22. At that meeting we are going to have people from four states come in and discuss no-fault, some of them no-fault states, some of them not no-fault states.

SENATOR LASKIN: Anybody from California?

SENATOR DALTON: Is there going to be anybody from California?

MS. PUROLA: Well, the list is still being put together, but there is not, so far.

SENATOR DALTON: Right now what we have are Michigan, Ohio, Florida, Delaware, and we might bring somebody in from California. The question about California -- to put it quite bluntly -- is cost, the cost of flying him or her in. We've had somebody from Illinois and Indiana. Indiana, I believe, is a totally non-regulated state.

SENATOR LASKIN: Illinois.

SENATOR DALTON: Illinois -- excuse me -- is a non-regulated state. They were in, like, a month ago when we had a hearing.

SENATOR LASKIN: Except, Dan, California is really the leader in major changes.

DEPUTY COMM. JACKSON: All of the states are changing their systems. I think you should look at the laws as proposed. They have the Governor's support and they have the whole party's support. Illinois is in the process of going to a modified prior approval system and California is designing one.

SENATOR DALTON: California is designing a prior approval system?

DEPUTY COMM. JACKSON: Yes. (At this point everyone is speaking at once, and transcriber is unable to pick up the remainder of Deputy Commissioner Jackson's statement.)

(HEARING CONCLUDED)

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