Insurance companies use rating variables to develop premiums that better reflect the risks that consumers face.
- For example, in auto insurance, a common rating variable is make and model.
- Imagine two cars. One is an expensive sports car. The other is a family sedan.

Now imagine the cars get into a fender bender. The sports car requires expensive specialty parts. The family sedan just needs a new low-cost fender.
- That’s why insurance companies and regulators agree that make and model is a good indicator of how expensive repair work will be. That’s why the sports car pays a higher premium.

Actuaries rigorously study rating variables for their effectiveness and for making sure they keep insurance affordable. They are also closely regulated.
- In this case, insurance companies and regulators agree that make and model is a good indicator of how expensive repair work will be. That’s why the sports car pays a higher premium.

Rating variables give consumers more choice and fairness. Expensive sports cars pay more than family sedans.

Average annual premium WITH RATING VARIABLES

Average annual premium WITHOUT RATING VARIABLES

Restricting rating variables could lead to unintended consequences. If make and model isn’t allowed, then the family sedan subsidizes the expensive sports car.

For more insights on insurance rating variables, see the educational paper “Insurance Rating Variables: What They Are and Why They Matter,” published by the Casualty Actuarial Society and the Insurance Information Institute. The paper is available on the CAS and I.I.I. websites.