

Proposition 103 Successful Or Not?

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Introduction

Proposition 103 was approved in 1988 by voters in California, which has had long-lasting and drastic effects on the state's insurance regulatory structure. The enactors of the legislation, as well as its supporters, claim that the legislation has been effective in curtailing the rising insurance rates. As a result, the people of California were able to save billions of dollars. The supporters of the legislation have lobbied extensively to thwart any attempts to either repeal or amend the legislation. They have advocated vigorously for increasing its scope. They have engaged in extensive litigation as well as participated in hot debates in the legislature to ensure that the law continues to live on. However, despite the tall claims of its supporters, Proposition 103 is not without its drawbacks.

Insurance Regulation Before Prop 103

Insurance is a way of managing risk. It has existed before the Roman Empire as well. The rise of trade leads to an increase in insurance practices as well. Vessels carrying special cargo were insured in exchange for a fee. In case any harm came to the vessel, insurers provided sailors and vessel owners with some guarantee. In the 17th century, insurance, as we know it today, was born. The 19th century marked the earliest legislation to be enacted to regulate insurance. It was done by the state of Massachusetts. The first state to appoint an independent insurance commissioner was New Hampshire, whereas New York established the first insurance department.

In 1869, the U.S. Supreme Court ruled that regulating insurance schemes was the sole prerogative of state governments and did not fall under the jurisdiction of the federal government. Later, in 1944, the Supreme Court overturned its previous decision. However, the very next year, Congress passed the McCarran-Ferguson Act. Under this Act, insurance was again decided as a subject which falls under state jurisdiction. Thus, the Act effectively closed the doors of federal regulation of insurance-related matters.

In 1868, California, for the first time, tried its hand at regulating insurance matters. However, California took considerable time to establish a separate division for the matter. It was in 1929 that the Division of Insurance established the Department of Investment. The Division was focused on regulating insurers doing business in California. In 1945, the state established the California Department of Insurance, which was an autonomous body. The State of California passed the McBride-Grunsky Insurance Regulation Act, under which all insurers were required to be registered with the Department of Insurance. It also regulated the rates and rating practices of the insurers. The law provided a platform of non-interference in which rates were determined by the insurers. It allowed

for a system where competition among insurers was supposed to flourish. Later on, Proposition 103 was approved by the voters.

Politics Involved

There was a lot of politics involved in the passage of Proposition 103. Insurance companies and law firms spent a massive \$76 million to bury the proposed legislation. This means that the insurers and supporters spent more than George Bush did during his presidential campaign at the time. On the other hand, the supporters of the legislation only spent \$4 million. It shows that people had become wary of the profit-mongers and wanted to do away with their unlimited powers. As the law took away considerable powers from the insurers, they were naturally against it. They lobbied heavily against it but still failed. It meant that the massive campaign spending only served to provide more information about the workings of the insurers, which further added to the anger of the people. Harvey Rosenfield, the author of Prop 103, was a consumer advocate and maintained that rates were increasing as a result of insurers' attempts to maximize their profits. Rosenfield reflected that:

"...insurance industry is no longer strictly a mechanism for risk sharing. Rather, it has become a financial institution devoted primarily to maximizing profit premiums...". (Rosenfield)

As a result, Proposition 103 was approved by 51% of the total vote.

Proposition 103

Prop 103 is the set of rules and regulations that deal with insurers operating in California. The Prop sets out not only the regulatory mechanism but also the functions under which the Department of Insurance operates. It is the main framework from which it derives its powers. Prop 103 did not repeal the previous statute under which the CDI operated; rather, it supplanted it. Therefore, no changes were made to the existing functions of the department. Prop 103 only added more functions to the department, making it even more powerful. Thus, although the department's power and structure have changed drastically due to Prop 103, its primary functions remain the same as before. Prop 103 added three more functions: 1) prior approval of rates, 2) establishment of a system of intervenors, and 3) an elected insurance commissioner as the final authority. (Department of Banking and Insurance)

Under the Prop, antimonopoly laws are now applicable to the insurers as well. It would also develop a system under which arbitrary price increases cannot be made, as well as a system for the election of an insurance commissioner. The impact of Prop 103 is not limited to business, home and auto insurance. In fact, it also has considerable influence upon:

- Fire
- Earthquake

- medical malpractice
- professional liability and other liability, etc.

One of the outcomes has been the reward of a “good driver discount”, notwithstanding that all drivers are accorded this discount as a result of the ‘not so strict’ conditions attached to the program. The hallmark of Prop 103 was the introduction of a new system where the rate was approved by the CDI and not the insurer. Although it seems easy, the new system is very complicated as there are no benchmarks. Approval is a subjective matter and is decided case by case. It is the duty of the insurance commissioner to decide whether the request should be approved or not. The process can take months, and there is a debate on whether or not it has protected consumers from insurers. One of the distinguishing characteristics of Prop 103 is the inclusion of outside parties in the rate-approval process. These outsiders are known as ‘intervenorors’ and can include anyone. Usually, the Consumer Watchdog is the intervenor.

Insurers claimed that the high prices were not because of their greed but because of the 1979 *Royal Globe Insurance Company v. Superior Court*. The ruling allowed for third parties, not a party to the insurance contract, to bring actions against the insurers. As a result, frivolous litigation was brought against insurers. To pay for the suits, insurers transferred the prices directly to the consumers. As a result of which, insurance rates skyrocketed in California.

Successful Or Not?

Prop 103 has attracted a lot of debate. Some have claimed that it has been a success, while others disagree. Coinciding with Prop 103 was the decision to overturn the Royal Globe decision. In *Moradi Shalal v. Fireman's Fund*, it was held that the grounds for third-party liability as laid down by the Supreme Court in its judgment in *Royal Globe* was problematic. It created problems not just for the legal fraternity but also as a matter of policy. As a result of the decision, actions by third parties more than halved the claims. Many academicians and researchers contend that Prop 103 is not a success. (A.Fields, Chinmoy Ghosh and S.Kidwell) The reason behind the rate changes is not Prop 103 but other factors, which include fewer auto lawsuits, safer and technologically advanced vehicles, [strict laws regarding drunk driving](#), stringent anti-fraud measures, decisions like the one mentioned above, etc.

One of the stances of the Prop 103 was to reduce the profit margins of the insurers. However, California insurers' profitability did not take a hit. Instead, they witnessed the same growth as in other parts of the country. David Appel concluded that holding the rates down resulted in an opportunity cost of \$10 billion to Californians. (Harrington) Brian Sullivan, a leading voice on insurance matters, contended that Prop 103 was indeed successful in curtailing rising rates. However, at the same time, it was made equally challenging to lower rates as well.

Conclusion

There is no consensus among the researchers and policy analysts over the success of Proposition 103. Similarly, I, too, find it difficult to conclude whether the changes brought about by Prop 103 have been successful. Although the premium rates declined drastically in California after the enactment of Prop 103, we cannot rule out other factors. The success of Prop 103 depends on whether or not other factors played a role in reducing insurance rates in California. Even if they were not, in my opinion, Prop 103 is not as successful as it should have been. The changes brought by it have had adverse effects as well. It has greatly increased bureaucratic red tape. Lastly, a more carefully drafted legislation would be much more successful and efficient in regulating insurance in California.

Works Cited

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