



Southwestern Insurance Information Service

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FACT SHEET

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UNDERWRITING GUIDELINES BENEFIT INSURANCE BUYERS

Insurance underwriting guidelines help an insurance company determine the risk that an applicant represents and the appropriate premium which reflects that risk, or whether to accept the risk at all. The guidelines seek to evaluate the likelihood that an applicant would subsequently have an accident, particularly a costly accident, covered by his or her insurance company.

Having the option to turn away or charge a higher premium for bad risks is advantageous to the vast majority of a company's policyholders who have good driving records. The cost of paying more claims, filed by poor drivers, would otherwise be borne by everyone which would result in higher rates for average and above average drivers. Or, if a company insured too many poor drivers, and had inadequate rates to cover their losses, the firm might become insolvent and not able to meet its obligations to pay claims. Without the guidelines, a driver who has not had any accidents, for example, could not be distinguished from one who, with five accidents, represents a higher risk.

The only way that insurance rates can be fair to all drivers is for everyone to pay a premium that most accurately reflects their underwriting risk, meaning, that they will be involved in an accident. Middle-age drivers should not subsidize teenagers who, statistics show, have more accidents. People who live in the suburbs, or the country, should not pay higher rates to cover the higher and more frequent claims filed by people who live in congested areas.

Applying underwriting guidelines for insurance applications is similar to a bank loan officer's analysis of a loan application. Loans for customers are granted if the bank loan officer feels the applicant will be able to repay the loan. This keeps the bank solvent and serves all of the bank's customers. Similarly, underwriting guidelines attempt to establish which applicants for insurance are more, or

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less, likely to have costly claims. This keeps the insurance company solvent and helps hold rates down for all insureds with that company.

A recent industry survey revealed that almost two-thirds of Americans feel an auto insurer should be able to reject a potential new customer who has poor driving record.

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