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 will use rating variables like make and model. The sports car should pay more premium, since it costs a lot more to repair.

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.

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.