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MARKETS

State Farm Is There: As You Drive

Insurers Use Big Data to Track Drivers, Offering Discounts as Lure, But Privacy Advocates See Dangers

By LESLIE SCISM

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As soon as Ed Scharlau of Austin, Texas, pulls out of his driveway in his Ford Expedition, a computer starts keeping score. It keeps track of how fast he accelerates, how abruptly he brakes and how far he drives.

The prize if he scores high enough: a substantial discount on his car insurance.

"This is a step in the right direction," the 74-year-old former manufacturing executive said. "How I drive should affect my insurance premium."

Mr. Scharlau is on the leading edge of a revolutionary shift in how insurers price car insurance, one that has tantalized the \$167 billion industry for more than a decade.

But what many insurers see as a smart application of Big Data, some customers and privacy advocates view as a worrisome encroachment by Big Brother.



Emily Cooper

The idea is to use small telematic devices—in Mr. Scharlau's case, one that plugs into his Expedition's diagnostic port—to compile and analyze data on driver behavior.

The programs are voluntary, and better drivers qualify for discounts. In general, insurers say those who fall short aren't charged higher rates, but instead pay no more than what they already are paying, based on conventional pricing methods.

The insurers embracing telematics are gambling that the incentive of discounts and data-based feedback will produce better drivers, and thus fewer claims—and higher profits. With efforts generally in early stages, it is too early to know if this is true. For customers, this "usage-based insurance" is pitched as a can't-lose—at least for those who can stomach the privacy concerns.

Mr. Scharlau is an early customer of State Farm Mutual Automobile Insurance Co.'s "Drive Safe &

Save" program, which it plans to promote across most of the U.S. later this year.

Adoption of the technology by the country's biggest auto insurer "is going to push this to a whole other level," said Brian Sullivan, who runs Risk Information Inc., a publisher of insurance-industry newsletters.



State Farm plans to promote its 'Drive Safe & Save' program across most of the U.S. later this year. Steve Smedley/Associated Press

The pioneer in telematics, Progressive Corp. , began experimenting with the technology more than a decade ago and has tried to maintain its edge with patent-infringement lawsuits in federal court, including one against State Farm. Those are currently stayed as the U.S. Patent and Trademark Office reviews the patents. "For now, they are presumed valid," said Dave Pratt, a Progressive general manager. State Farm declined to comment on the litigation.

Allstate Corp., which resolved legal disputes with Progressive in 2011 with agreements that included licensing patents to each other, expects its "Drivewise" program to be available in most states by the end of this year. Progressive, meanwhile, in recent months has discussed licensing use of its patents with about two dozen other insurers, it told investors in May.

The conventional methods for pricing car insurance involve pooling customers on the basis of characteristics such as age, gender and history of speeding tickets and crashes, all of which actuaries have correlated with loss potential. Insurers acknowledge those methods are imprecise. "We know that 16-year-old drivers have a whole lot of accidents...but not every 16-year-old is a lousy driver," said Scott Bruns, who heads a telematics unit in State Farm's property-casualty actuarial department. Basing rates in part on actual behavior is a "big advantage in being able to price appropriately."

More than 1.4 million drivers have signed up for Progressive's "Snapshot" program since 2008, and the insurer said discounts of up to 30% have topped \$125 million. State Farm's discounts run as high as 50%.

Still, the programs have critics because of the voluminous data they collect on customers.

"It's a slippery slope," said Paul Stephens, an official with the Privacy Rights Clearinghouse, speaking generally. While insurers say they don't track routes driven, Mr. Stephens fears that as programs expand and get more commonplace, insurers may wind up with "a very detailed log of your whereabouts throughout the day."

And the data, he said, might be obtained by law-enforcement authorities for criminal probes and parties in civil litigation.

Allstate, State Farm and Progressive said they share data as required by law and that they

disclose this to customers. Allstate and Progressive said their devices don't have Global Positioning System functions. State Farm said it receives information "about the broad geographic areas" in which a vehicle is driven, measuring about 40 square miles, but not "the exact vehicle location."

Brent Allen, who is Mr. Scharlau's State Farm agent, said some clients have no interest in the program because of "the Big Brother thing," but others are eager for discounts.

Mike Hatch, a Minneapolis lawyer who is a former Minnesota attorney general, said more consumers should be wary. "People ought to be more cautious" about allowing such inroads into privacy, he said.

A positive of usage-based programs is that drivers who earn discounts effectively are reducing the role of credit-related items in the pricing process, said Mike Chaney, Mississippi's top insurance regulator who heads a committee overseeing car-insurance issues at the National Association of Insurance Commissioners. Some consumer advocates maintain that insurers' use of credit factors—common since the 1990s—is unfair to many poor people, while insurers defend them as highly correlated to claims costs.

It remains to be seen whether it is possible to offer discounts to more customers, keep rates the same for everyone else and still maintain profit margins. At its May presentation, Progressive told analysts and investors that it is an open question if usage-based programs will remain "discount-only" models.

But insurers are convinced that their feedback will lead to fewer accidents.

One day recently, Mr. Scharlau logged onto his State Farm account to learn he so far had earned "A+" grades for left-hand turns and for not topping 80 miles per hour, but only "B+" for braking, acceleration and time of day his Expedition was on the road.

Mr. Scharlau said he and his wife now find themselves chatting "about our own driving and what we see around us: 'Oops, did we just lose points?'"

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