Comments of the Center for Economic Justice to the

NAIC Committee on Race and Insurance

December 16, 2020

CEJ submits these comments to the Committee on Race and Insurance to provide a comprehensive set of recommendations addressing all of the work streams. Our recommendations are most detailed for the line of business and regulatory diversity work streams. We have limited comments on the insurance industry diversity work stream.

As mentioned in earlier comments and presentations, it is relevant and necessary to determine why, despite CEJ or other consumer and civil rights advocates raising issues of racial discrimination in insurance for decades, it took the murder of George Floyd for the NAIC and industry to acknowledge the problem and commit to actions to address systemic racism in insurance.

We offered our analysis of the structural impediments to regulatory action to address systemic racism in insurance in the past in our August 14, 2020 presentation, attached:

- Lack of Minority Voices and Experience in Insurer and Regulator Leadership
- Imbalance Between Consumer and Insurer/Producer Access to Critical Regulatory and Legislative Processes
- Trade Associations Fighting to Protect Practices that Reflect and Perpetuate Systemic Racism in Insurance
- Regulatory Authorities and Infrastructure Failing to Keep Up With Seismic Changes in Insurer Practices.

We all know that the lack of diversity among insurers and regulators is a problem. But, what has led to this lack of minority participation? Improving diversity is a strategy and not the goal. It is a strategy to cause insurers and regulators to better consider the impacts of their practices on communities of color by having people making decisions better reflecting the people who are affected by those decisions. The goal is racial justice and improved diversity is one part of the strategy to attain that goal.

Our recommendations are informed by our 30 years of working on racial and economic justice in insurance at the NAIC, in the states and before Congress and the lessons we've learned about what's necessary to create the changes to lead to racial justice.

Our recommendations are presented as follows:

- Recommendations Common to All Line of Business Work Streams
  - Recommendations for Actions by the Committee on Race and Insurance
  - Recommendations for Actions by Other NAIC Committees, Task Forces and Working Groups
- Recommendations for Improving Regulatory Diversity
- Recommendations for Improving Insurer and Producer Diversity

Recommendations Common to All Line of Business Work Streams

Recommendations for Committee on Race and Insurance

1 Explicit recognition of disparate impact / proxy discrimination against protected classes as unfair discrimination in insurance

2 Develop guidance to require insurers to test for and minimize disparate impact in all aspects of their consumer-facing operations – marketing, underwriting, pricing, claims settlement, antifraud, payment plan eligibility, investments

3 Develop guidance for regulators and insurers for acceptable methods of testing and reporting results of testing for disparate impact to regulators and the public

4 Develop a data reporting framework to permit meaningful and timely analysis of availability and affordability of insurance, generally, and in communities of color, specifically – sales data showing products sold with price by specific type by granular geography area.

Discussion

1 Explicit recognition of disparate impact / proxy discrimination against protected classes as unfair discrimination in insurance

Regulators have made clear in a variety of discussions that you believe you have authority to stop proxy discrimination against protected classes or disparate impact as unfair discrimination in insurance. You memorialized this in the principles for Artificial Intelligence which included a requirement for insurers to pro-actively avoid proxy discrimination against protected classes.

Yet, industry has fought and continues to oppose the proposition that unfair discrimination on the basis of race means anything other than intentional discrimination. Industry has reiterated this position several times including most recently at the NCOIL annual conference in which they argued against and opposed any regulatory authority or insurer responsibility to address unintentional, unneeded proxy discrimination on the basis of race.

Clearly, any serious effort to address systemic racism in insurance must address practices that intentionally or unintentionally, reflect and perpetuate historic discrimination against protected classes. If the NAIC is to make any progress, it must avoid endless debates with industry about legislative intent or regulatory authority and start with the proposition that, whatever one thinks the current legislative intent or regulatory authority may be, the NAIC starts from the foundational premise that disparate impact is unfair discrimination in insurance. If changes are needed in legislative intent or regulatory authority, the NAIC will develop the model guidance necessary, but there should not be debate about the principle that is the foundation of racial justice.

2. Develop guidance to require insurers to test for and minimize disparate impact in all aspects of their consumer-facing operations – marketing, underwriting, pricing, claims settlement, antifraud, payment plan eligibility, investments

Simply stated, it should be part of the DNA of insurers to test all their practices, operations and algorithms for disparate impact and take steps to minimize that impact within the risk-based framework of insurance. The burden must be on insurers to employ practices that do not unnecessarily and unintentionally reflect and perpetuate systemic racism. It is unreasonable to place the burden on consumers or regulators to identify such practices and then challenge insurers, particularly when the vast majority of the practices are opaque to regulators or consumers and incorporated into black-box big data algorithms.

Lenders have had such a responsibility for decades and testing for and minimizing disparate impact is simply part of the development of lender underwriting, pricing and other practices.[1]

It is also essential that insurers test for racial inequities in all aspects of their consumer-facing operations. It is far from sufficient to examine only underwriting and pricing. In an era of big data micro-targeting, insurers, like other businesses, have the ability to micro-target particular product marketing to individuals with the result that the underwriting process is effectively moved to the marketing program.

Slides 25 to 27 of the attached CEJ presentation to NCOIL cite insurer CEO statements to investment analysts in which the CEO explain not just their intent to attract “high-value” customers and repel low-value customers – labels which reflect racial bias – but the ability to use marketing tools and big data to micro-target those high-value customers. It is specifically the big data tools like price optimization, customer lifetime value and propensity for fraud that are use and which rely on data and algorithms that reflect and perpetuate systemic discrimination. The

[1] See for example, chapter 10 of *Credit Scoring for Risk Managers: The Handbook for Lenders*.

amount of personal consumer information available for micro-targeting is incomprehensibly large – just look at the websites of data brokers or vendors specializing in assisting insurers like Carpe Data or Journaya.

We've repeatedly raised the concern about claim settlement and antifraud algorithms that rely on biased data and biased modelers. In the case of antifraud, biased algorithms become self-fulfilling because an insurer will not find fraud if the claim isn't investigated. So bias in deciding which claims are suspicious will lead to bias in the claims labeled as fraudulent.

Insurers should also examine their investments and investment practices for climate and environmental justice. Numerous studies have shown that historical racism in housing has led to more severe impacts of climate change on communities of color as well as more severe impacts of the pandemic. Further, racial justice must consider and incorporate environmental and economic justice. Insurers should be examining their investments and investment practices to ensure they are not, for example, supporting predatory lenders or racist housing and environmental policies.

It is essential that the approach taken to address racism in insurance be holistic and comprehensive. Attempting to prohibit one offensive rating factor or data source or algorithm is a fool's errand. The same racial bias from that one prohibited factor will likely be replicated by another new data source or algorithm. Further, the goal should not be to eliminate data sources for insurers, but require the use of any data source in a manner that eliminates or minimizes the disparate impact.

The action needed here is for the Committee on Race and Insurance to develop the guidance for the requirement that insurers test for and minimize disparate impact in their practices. This will be universal guidance – and the guidance sought by many of the NAIC working groups – like the Casualty Actuarial and Statistical Task Force and the Anti-Fraud Task Force – who have punted on addressing issues of racial equity in algorithms.

3. Develop guidance for regulators and insurers for acceptable methods of testing and reporting results of testing for disparate impact to regulators and the public

Once the requirement for insurers to test for and minimize disparate impact is established, the next step is for the Committee on Race and Insurance to develop the guidance for how insurers should test, minimize and report the results of such disparate impact testing. This guidance should include data sources for protected class characteristics if the insurers does not collect those data, acceptable and unacceptable methods of testing, safe harbors for insurers who test for and minimize disparate impact and how and how often to test and report results to regulators and the public.

It is important to note that insurance regulators do not have to reinvent the wheel here. There is a rich history of disparate impact testing methodologies not just from here in the U.S. related to federal employment, lending and housing laws – and applications of disparate impact analysis to insurance under the Fair Housing Act – but experience from other nations about how to address disparate impact in insurance.

4. Develop a data reporting framework to permit meaningful and timely analysis of availability and affordability of insurance, generally, and in communities of color, specifically – sales data showing products sold with price by specific type by granular geography area.

The Committee on Race and Insurance must address another key structural impediment to racial justice in insurance – the absence of routine data reporting by insurers of granular consumer market outcomes sufficient to analyze the impact of insurer marketing, sales, claims and antifraud practices on communities of color.

The contrast between the lack of market outcome data in insurance and other financial services is stark. While public and private sources have reported the impact of the pandemic and federal relief (e.g. CARES Act) on all types of borrowers on a weekly and monthly basis – including changes in delinquencies, late payments, use of forbearance and much more – insurance regulators have had no information on consumers' use of premium relief or real-time changes in claims during the pandemic.

More important, insurers have steadfastly opposed the publication of data by individual insurers by ZIP Code or Census Block that permits regulators, academics, consumer and civil rights groups from analyzing racial disparities in insurance. Regulators must overcome this opposition and develop a market regulation data reporting regime that matches the financial regulation data reporting regime in breadth and intensity.

Taken together, these four common-to-all-work stream actions should be memorialized in two charges to the Committee on Race and Insurance – one regarding disparate impact and one regarding data collection.

Recommendation for Specific to Lines of Business

In addition to certain racial justice actions that should be centralized at the Committee on Race and Insurance, there are also activities that should be assigned to other NAIC committees, task force and working groups. We mentioned above that some NAIC working groups have specifically rejected requests to examine racial bias in insurer practices that fall under that working group activity. For example, the CASTF white paper on predictive modeling explicitly rejected addressing racial bias in regulatory review of algorithms. The Antifraud Task Force explicitly rejected including a requirement for insurers to test for racial bias in antifraud practices and algorithms in the recent update the antifraud policy guideline. Both groups based their decision on the claim that other groups at the NAIC were working on the issue.

While the development the guidance on how to test for, minimize and reporting the findings of disparate impact analysis should be centralized at the Committee on Race and Insurance, there are several actions that individual committees, task forces and working groups can and should take to help achieve racial justice in insurance.

1. Add a charge to identify potential **insurer practices** that disadvantage or disproportionately discriminate against communities of color.

Each committee, task force and working group should receive a charge for 2021 to identify insurer practices that may disadvantage or disproportionately discriminate against communities of color. Such a charge is vital for each of the subject matter groups to have ownership of the issue and to educate themselves about race and insurance. The outcome from this charge – a list of practices that insurers should prioritize for disparate impact testing – will complement the work of the Committee on Race and Insurance.

2. Add a charge examine **public policies** that disadvantage or disproportionately discrimination against communities of color.

This second charge to all committees, task forces and working groups is directed at public policies that unfairly harm communities of color. This charge focuses more on laws and regulatory guidance, as opposed to practices under the discretion of insurers. The outcome form tis charge – a list of public policies, laws, regulations and regulatory guidance that unfairly discriminate against communities of color – will also complement the work of the Committee on Race and Insurance. To illustrate, we list some public policies related to private passenger auto that disproportionately and unfairly impact communities of color.

a. Property Casualty / PPA
    i. Pay to Play Laws Punishing Uninsured Drivers
    ii. Territorial Rating for Uninsured Motorists
    iii. High Minimum Limits
    iv. Criminal Penalties / Debtors Prison for Uninsured Motorists
    v. Oversight of Advisory Organizations / Data Brokers

3. Add a charge to **identify low-value products targeted to communities of color and new high-value products opportunities that better meet the needs of communities of color.**

A third charge to all committees, task forces and working groups is directed at identifying current products that, because of their low-value, strip consumers of assets instead of protecting those assets. In our experience, these low-value products are disproportionately marketed to and sold in and to communities of color. In addition, some lines of business simply have no products designed for the needs of communities of color and there are opportunities to identify the unique needs of these communities and then develop high-value products targeted to meet those needs. As discussed below, this charge is also relevant for addressing diversity in insurers and producers.

Recommendations for Regulatory Diversity

We have a series of recommendation to improve diversity within the regulatory community. As set out in our earlier comments and presentations to the Committee, the lack of diversity among the regulatory community and the regulatory decisions which codify disparate impact are a result of a lack of consumer stakeholder participation, generally, and an even greater absence of stakeholders from communities of color, specifically. Our recommendations are:

1. Develop guidance for establishing a public agency dedicated to representing consumer before the Department of Insurance and the Legislature – a Bureau of the Insurance Consumer Advocate.

2. Measure consumer participation, generally, and minority participation, specifically in NAIC meetings and conferences and events

3. Allocate speaking time, when there are time constraints, based on industry / consumer, not based on number of speakers

4. Increase funding for NAIC consumer participation to permit consumer reps to retain experts for priority projects.

Discussion

1. Develop guidance for establishing a public agency dedicated to representing consumer before the Department of Insurance and the Legislature – a Bureau of the Insurance Consumer Advocate.

There is a great need to establish institutions to advocate on behalf of consumers before insurance departments and state legislatures to level the playing field versus the hundreds of millions of dollars of policyholder-supplied funds spent by insurers and trade associations to press their views.

The establishment of a Bureau of Insurance Consumer Advocate in each state would have an impact far beyond the advocacy for consumers performed by that agency. These BICAs create opportunities for employment, including minority employment, in insurance other than working for insurers or regulators. And they create employment opportunities outside of industry for regulators who want to leave the insurance department. BICAs are a strategy to increase diversity in insurance as well as addressing a core barrier to ending systemic racism in insurance.

2. Measure consumer participation, generally, and minority participation, specifically in NAIC meetings and conferences and events.

3. Allocate speaking time, when there are time constraints, based on industry / consumer, not based on number of speakers

If you can't measure it, you can't fix it. Speaking about diversity in abstract terms cannot lead to assessment of failure or success of the strategies to improve diversity. Further, a requirement to measure diversity in NAIC events will raise awareness of the need to improve diversity.

The need for such improvement is huge. We've pointed out that the CIPR events at the NAIC Summit not only failed to include any minority voices, but included one overtly racist presentation. We've pointed out that this year's Insurance Regulatory Examiners' Society Career Development Seminar failed to include any minority or consumer presenters. And these results occurred after the NAIC declared its commitment to racial justice. It gets worse. At the recent Fall National Meeting, the CIPR event on pandemic insurance featured eight white men. No members of the communities of color most impacted by the lack of pandemic insurance. No small businesses from communities of color. No consumer stakeholders who have been active in these debates from day 1.

The two actions will help ensure that NAIC event planners, committees, task forces and working groups better understand the importance of consumer stakeholder participation, generally, and minority participation, specifically.

As someone who is often the only consumer stakeholder among many industry stakeholders in NAIC meetings, I'm keenly aware of situations in which a half dozen industry trades each have the same amount of time as me – to repeat and agree with each other trade's comments. To be clear, this is not always the case, but the larger point is that, when speakers' time is limited, the allocation of that time should be based on the major positons/views and not on the sheer number of speakers.

4. Increase funding for NAIC consumer participation to permit consumer reps to retain experts for priority projects and engage with stakeholders from communities of color impacted by NAIC deliberations.

As someone who has been involved in the NAIC Consumer Participation program from its beginning 30 years ago, I'm grateful for the NAIC's commitment to consumer participation. The NAIC program stands in contrast to the absence of such a formal consumer participation program in most states and other organizations, like NCOIL.

The NAIC consumer participation budget is about 0.1% of the total NAIC budget. It covers reimbursement of travel expenses for funded consumer representatives to attend NAIC national and interim meetings and some IAIS events. It also covers registration fees, publication costs and conference call costs for funded and unfunded consumer representatives. No consumer

representative is paid for their time out of NAIC funds. Most funded and unfunded consumer representatives volunteer their time – beyond their regulator work commitments – to advocate for consumers at the NAIC.

We are not asking for NAIC consumer representatives to be compensated for our time at NAIC events. Rather, we're asking for additional funding to leverage our individual contributions to retain subject-matter experts or consultants or to fund participation from key stakeholders from communities of color to assist the consumer representatives on key issues. This assistance is particularly important in areas like consumer testing of information and disclosures and analyzing actuarial, reserving, accounting, investment or capital-related proposals.

The NAIC consumer representatives took responsibility for the lack of minority voices among our group in 2020 by recruiting heavily for applicants representing communities of color. We were successful in encouraging many new, exceptionally-qualified applicants of color and hope they will be accepted as NAIC consumer representatives. But, we want these new consumer representatives – if accepted by the Consumer Board of Trustees – to feel their time is well spent and to continue to participate for years to come while helping recruit new consumer stakeholders of color. For that to happen, the Consumer Participation program must be strengthened and one way is to increase NAIC funding for the consumer reps to use to retain experts and consultants and reach out to communities and stakeholders impacted by NAIC discussions.

Recommendations for Insurer Diversity

1. Identify products providing low-value to communities of color and develop new high-value products that better meet the needs of communities of color

We offer this action to improve insurer diversity based on the belief that someone will want to work for companies who provide products and services that that person and that person's community values and likes. Why would members of community color want to work for an industry that the community perceives as ripping them off? We suggest that if communities of color value the products sold by insurers, members of those communities are more likely to seek out work with those insurers.

This recommendation is essentially the opposite of suggestions to improve financial or other education in communities of color. In our view, the improve-education argument blames the victim. Our approach suggests that people are not uneducated, but want to work for companies providing products that they and their community like and value.

2. Examine impact of criminal history in producer licensing qualifications

We raise this specific issue because of documented disparity and racial discrimination.in policing and criminal complaints against members of communities of color.

A Model Law to Address Systemic Racism in Insurance

Presentation to the NAIC Consumer Liaison Committee

August 14, 2020

Birny Birnbaum
Center for Economic Justice

The Center for Economic Justice

CEJ is a non-profit consumer advocacy organization dedicated to representing the interests of low-income and minority consumers as a class on economic justice issues. Most of our work is before administrative agencies on insurance, financial services and utility issues.

On the Web: www.cej-online.org

About Birny Birnbaum

Birny Birnbaum is the Director of the Center for Economic Justice, a non-profit organization whose mission is to advocate on behalf of low-income consumers on issues of availability, affordability, accessibility of basic goods and services, such as utilities, credit and insurance.

Birny, an economist and former insurance regulator, has worked on racial justice issues for 30 years. He performed the first insurance redlining studies in Texas in 1991 and since then has conducted numerous studies and analyses of racial bias in insurance for consumer and public organizations. He has served for many years as a designated Consumer Representative at the National Association of Insurance Commissioners and is a member of the U.S. Department of Treasury's Federal Advisory Committee on Insurance, where he co-chairs the subcommittee on insurance availability. Birny is also a member of the U.S. Federal Reserve Board's Insurance Policy Advisory Committee.

Birny served as Associate Commissioner for Policy and Research and the Chief Economist at the Texas Department of Insurance. At the Department, Birny developed and implemented a robust data collection program for market monitoring and surveillance.

Birny was educated at Bowdoin College and the Massachusetts Institute of Technology. He holds Master's Degrees from MIT in Management and in Urban Planning with concentrations is finance and applied economics. He holds the AMCM certification.

Why CEJ Works on Insurance Issues

Insurance Products Are Financial Security Tools Essential for Individual and Community Economic Development:

CEJ works to ensure ***fair access*** and ***fair treatment*** for insurance consumers, particularly for low- and moderate-income consumers.

Insurance is the Primary Institution to Promote Loss Prevention and Mitigation, Resiliency and Sustainability:

CEJ works to ensure insurance institutions maximize their role in efforts to reduce loss of life and property from catastrophic events and to ***promote resiliency and sustainability*** of individuals, businesses and communities.

Race and Diversity in Insurance:

Following the Murder of George Floyd, Insurer CEOs and Insurance Regulators Have Pledged to Fight Systemic Racism and Inherent Bias in Insurance.

Consumer Advocates Have Been Raising the Issue of Systemic Racism in Insurance for Many Years. Why Has the Issue Not Been Addressed, or Addressed With This Level of Commitment, by the NAIC Before Now?

Understanding This History Will Help Identify Actions Needed to Address Systemic Racism in Insurance Now.

Our Perspective on Why Systemic Racism in Insurance Has Not Been Addressed to Date

- Lack of Minority Voices and Experience in Insurer and Regulator Leadership
- Imbalance Between Consumer and Insurer/Producer Access to Critical Regulatory and Legislative Processes
- Trade Associations Fighting to Protect Practices that Reflect and Perpetuate Systemic Racism in Insurance
- Regulatory Authorities and Infrastructure Failing to Keep Up With Seismic Changes in Insurer Practices.

What Should a Model Law Include to Address Systemic Racism and Modernize Insurance Market Regulation?

- Reinforce Risk Pooling and Cost-Based Practices as the Foundation of Insurance;
- Ensure That Consumers, generally, and Minority Consumers, particularly, Have a Strong Voice in Regulatory Processes;
- Define Fair and Unfair Discrimination in Insurance, including Proxy Discrimination Against Protected Classes;
- Require Insurers and Regulators to Pro-Actively Identify and Minimize Proxy Discrimination Against Protected Classes and Provide Safe Harbors for Insurers For Such Actions
- Provide Meaning Oversight by Regulators of Insurers' Use of Data, Algorithms and Artificial Intelligence, Including Modernizing the Definition and Oversight of Advisory Organizations and Statistical Agents.
- Improve Consumer Control over Their Data, including Fair Credit Reporting Act-type protections for All Personal Consumer Information Used by Insurers
- Improve Competition in Insurance Markets with More Accessible and Actionable Information to Consumers

Systemic Racism in Insurance

1. Intentional Discrimination / Disparate Treatment
2. Proxy Discrimination / Disparate Impact
3. Systemic Injustice

Intentional Discrimination and Proxy Discrimination Can Be Addressed by Regulatory Oversight and Statistical / Technical Treatment within the Cost-Based Framework of Insurance.

Systemic Injustice Means That Systemic Racism and Inherent Bias Have So Pervaded a Particular Community That Insurance Costs are Inseparable from the Class Characteristic. Addressing This Type of Unfair Discrimination is a Legislative Role, such as, Prohibiting Discrimination on the Basis of Race.

Define Fair and Unfair Discrimination

Fair discrimination means adherence to cost-based practices for pricing, claims settlement and other aspects of insurer operations. Fair discrimination means treating similarly-situated consumers in a like manner.

For pricing, including underwriting, rating and payment plan eligibility, means charging the same rates and payment options to consumers posing similar expected costs for the period of coverage.

Rate shall not be excessive, inadequate or unfairly discriminatory

For claim settlement, fair discrimination means similar claims outcomes for similar claims.

Unfair Discrimination

Unfair discrimination means

1. Treating similarly situated consumers differently without a justification based on expected claim costs or expenses associated with the transfer of risk for the period of coverage provided or claim presented to the insurer;

2. For all lines of insurance, discriminating on the basis of a protected class; or

3. For [personal automobile insurance, residential property insurance, life insurance and annuities], discriminating on the basis of [insert]

4. Use of any data or characteristic of the consumer, vehicle, property or natural or built environment unless approved by the Commissioner.

Unfair Discrimination

"Protected Class" means a group of consumers based on one or more of the following characteristics:

Race
Religion
National origin
[Other]

"Discriminating on the basis of" means disparate treatment or disparate impact.

"Disparate treatment" means outcomes determined by explicit application of a protected class characteristic.

"Disparate impact" or "proxy discrimination" mean outcomes that have a disproportionate impact on a protected class or practices that serve as a proxy for disparate treatment.

Unfair Discrimination

Disparate impact is not unfair discrimination if:

1. The insurer has taken reasonable actions to identify and minimize disparate impact; and

2. There is no alternative to the practice resulting in disparate impact that permits the insurer from achieving substantially similar legitimate business outcomes.

The Commissioner shall promulgate rules to identify a non-exclusive list of reasonable actions an insurer may take to meet the requirements of this section.

Strengthen Consumer Voices in Regulatory Processes

Establish a public agency dedicated to representing insurance consumers before the Department of Insurance and Legislature.

Fund the Bureau of the Insurance Consumer Advocate (BICA) through a $0.10 to $0.25 (depending on size of the state) assessment on every individual policy and certificate under a group or master policy issued in the state.

BICA has standing to intervene on behalf of consumers in any insurance regulatory proceeding, including rulemaking and review of rate and form filings.

BICA has access to non-public information received by the Department of Insurance subject to same confidentiality as the Department of Insurance and related to the purposes of the Bureau.

Director of BICA selected by the Governor from a list of recommended candidates prepared by an advisory committee of individuals engaged in consumer advocacy. Director has a 5 year term.

Oversight of Data, Algorithms and Advisory Organizations

Routine reporting by insurers of sources and uses of data and data vendors and providers of algorithms

Modernize definition of advisory organization to create a level playing field for providers of algorithms used by insurers for marketing, pricing, claims settlement and anti-fraud.

Filing of algorithms by advisory organizations.

Modernize definition of statistical agent and statistical plans.

Commissioner authority to permit use of new data sources / algorithms / AI in controlled environment for purposes of data creation, data collection and evaluation.

Fair Credit Reporting Act-Type Consumer Protections for All Consumer Data Used by Insurers

Disclosure of Data to be Used, Source of Data and Uses of Data

Permission / Consent by Consumer

Adverse Action Notice

Consumer Access to Consumer's Own Data

Ability to Dispute and Correct Incorrect Data

Ability to Request Reconsideration Based on Corrected Data

Plus

Destruction of Consumer Data by Insurer When No Longer Needed for Business Purpose by the Insurer

Limited Use of Consumer Data to Stated and Disclosed Purposes. Opt-In / Consent for Any Purpose, with Particular Attention to Consumer-Generated Data from Devices Used for Insurance Exposure and Loss Assessment and Loss Prevention.

Addressing Systemic Racism in Insurance

Presentation to the NCOIL Special Committee on Race

December 9, 2020

Birny Birnbaum
Center for Economic Justice

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Why CEJ Works on Insurance Issues

Insurance Products Are Financial Security Tools Essential for Individual and Community Economic Development:

CEJ works to ensure ***fair access*** and ***fair treatment*** for insurance consumers, particularly for low- and moderate-income consumers.

Insurance is the Primary Institution to Promote Loss Prevention and Mitigation, Resiliency and Sustainability:

CEJ works to ensure insurance institutions maximize their role in efforts to reduce loss of life and property from catastrophic events and to ***promote resiliency and sustainability*** of individuals, businesses and communities.

Fair and Unfair Discrimination in Insurance

Provisions regarding unfair discrimination generally found in two places: statutes for rating and for unfair and deceptive practices.

Rating Statutes define two types of unfair discrimination:

- Actuarial – there must be an actuarial basis for distinction among groups of consumers; and
- Protected Classes – distinctions among groups defined by certain characteristics – race, religion, national origin – prohibited regardless of actuarial basis.

Unfair and Deceptive Trade Practices Statutes typically define unfair discrimination as distinction among groups based on a protected class characteristic.

NCOIL Model Act Language

NCOIL P/C Insurance Modernization Act

Section 6.A.3.a. For the purpose of this Act, “Unfairly discriminatory” refers to rates that cannot be actuarially justified. It does not refer to rates that produce differences in premiums for policyholders with like loss exposures, so long as the rate reflects such differences with reasonable accuracy.

Section 6.A.3.b. No rate in a competitive market shall be considered unfairly discriminatory unless it violates the provisions of section 6(B) in that it classifies risk, on the basis of race, color creed, or national origin. Risks may be classified in any way except that no risk may be classified on the basis of race, color, creed, or national origin.

NAIC Model Act Language

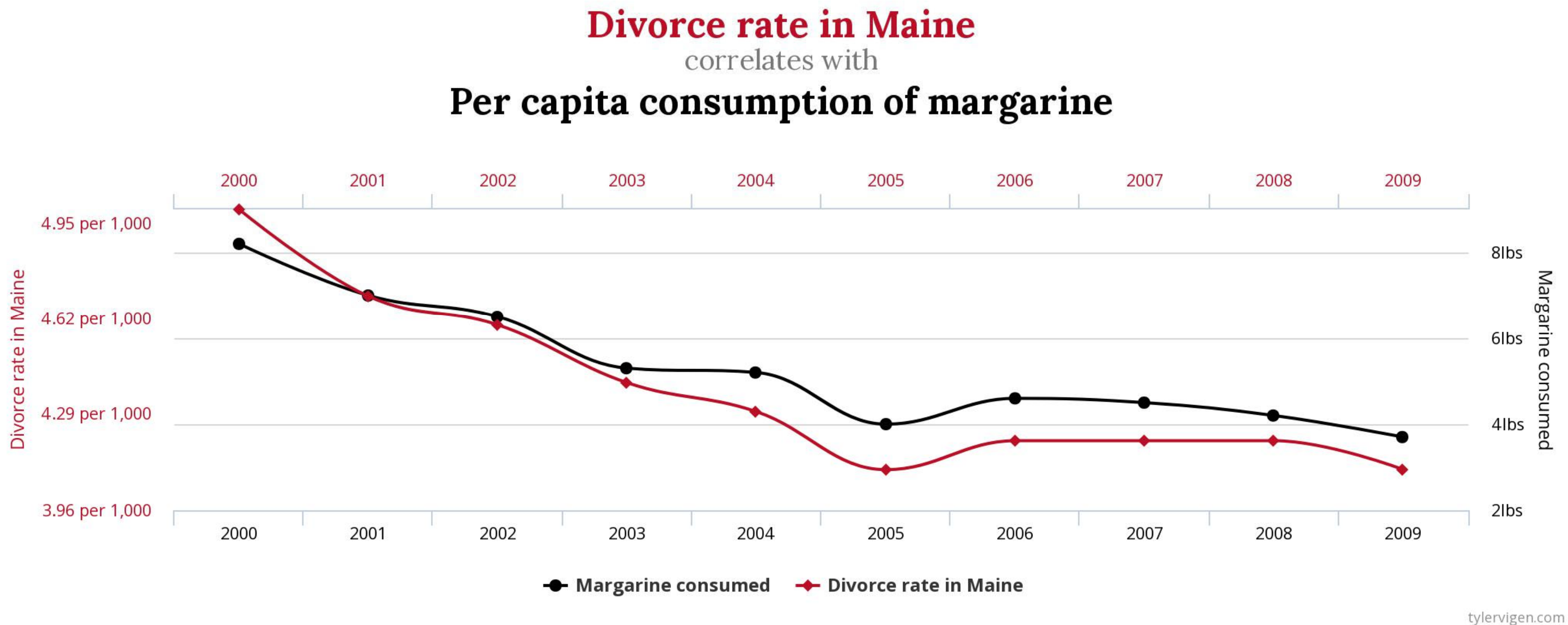
NAIC Property Casualty Model Rating Law, Model 1775

Section 5.A.3. Unfairly Discriminatory Rates. Unfair discrimination exists if, after allowing for practical limitations, price differentials fail to reflect equitably the differences in expected losses and expenses.

Section 5.A.4. Classification. Risks may be grouped by classifications for the establishment of rates and minimum premiums. Classification rates may be modified to produce rates for individual risks in accordance with rating plans which establish standards for measuring variations in hazards or expense provisions, or both. Such standards may measure any differences among risks that can be demonstrated to have a probable effect upon losses or expenses. No risk classification, however, may be based upon race, creed, national origin or the religion of the insured.

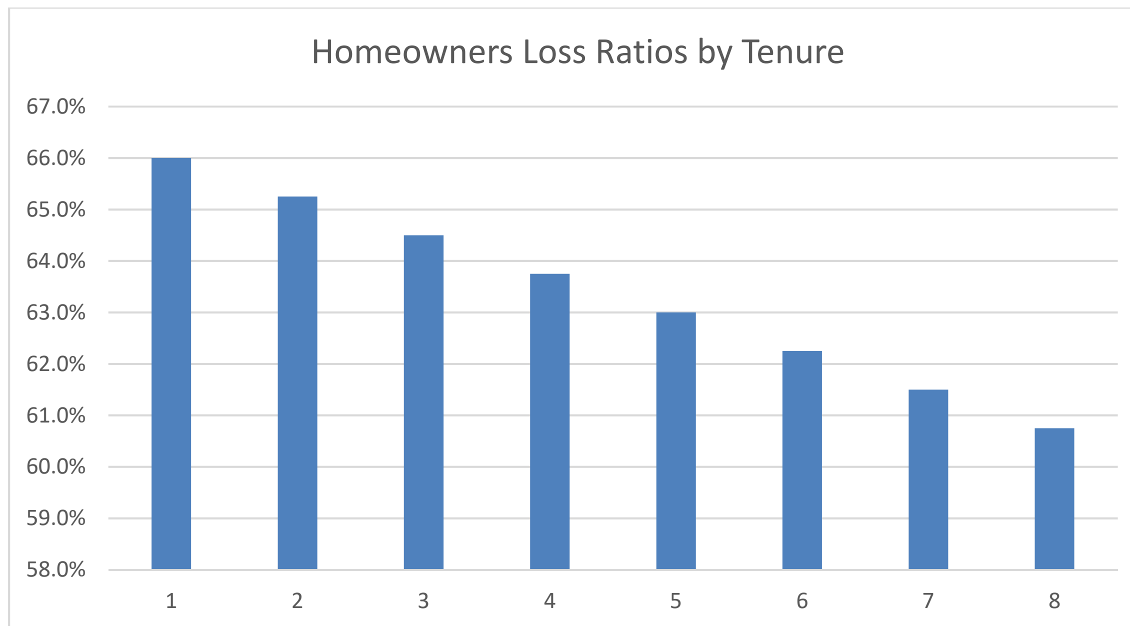
Correlation is Not the Standard for Fair Actuarial Discrimination

Statutes and actuarial standards don't refer to correlation, but demand a more robust relationship. Why? Here's an example of an almost perfect correlation – over 99%.



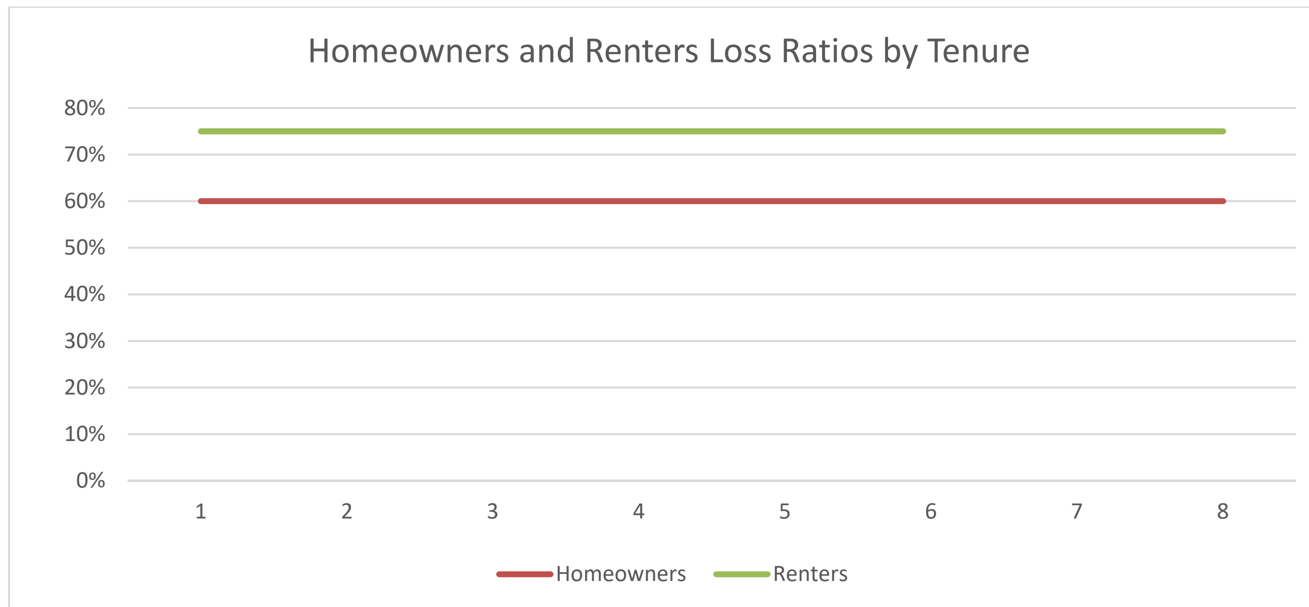
Spurious Correlation in Insurance

In the early 1990's, a company filed for a homeowners discount based on tenure with the company. The initial data presented show declining loss ratios with each additional year the consumer had a policy with the company. If a simple correlation was the only justification needed, this would have been the end of inquiry.



Spurious Correlation

But, we asked to see a break out of loss ratios by tenure for homeowners policies versus renters policies. Here's what we found – loss ratios did not change by tenure. The original chart was a spurious correlation that failed to reflect that with each year of tenure, the share of low-loss ratio homeowners policies increased, producing a lower overall loss ratio.



Why isn't a simple correlation relied upon or sufficient?

Because a predictive characteristic (or variable) may not be correlated in whole or in part to the outcome, but may also be correlated to other predictive variables.

Consider the difference between an outcome – say, claim frequency – and one predictive variable versus an outcome and multiple predictive variables.

There may be correlations between:

Driver Age and Auto Claim Frequency

Marital Status and Auto Claim Frequency

Vehicle Age and Auto Claim Frequency

Each of these represents a one-to-one – or univariate – relationship. But each predictive variable may be replicating part of another variable because of correlation between the predictive variables.

Eliminating Correlation among Predictive Variables: Multi-variate Analysis

Over the last 30 years, insurers and actuaries have developed new techniques to address the problems with univariate analysis. In our example, if we analyzed age vs. claims and marital status vs. claim separately and then used the results, we would likely be double-counting some effects because of the high correlation between age and marital status.

Insurers use a variety of techniques to eliminate correlations among predictive variables in order to isolate each individual predictive variable's unique contribution to explaining the outcome.

What Techniques Are Insurers Using?

Each month, the NAIC Casualty and Actuarial Task Force holds a “book club” with a presentation on new techniques insurers are using for pricing. Here are some recent techniques presented:

Families of Generalized Linear Models (Variations on Multiple Regression)

Gradient Boosting Models

Machine Learning

Hyperparameter Tuning

Neural Networks

Generative Adversarial Networks

Simple Correlation is to Today’s Insurance Big Data Algorithms as a Paper Plane is to a Boeing 787

How Does Multi-Variate Analysis Work?

Here's a simple illustration of a multivariate model. Let's create a simple model to predict the likelihood of an auto claim:

$$b_0 + b_1X_1 + b_2X_2 + b_3X_3 + e = y$$

$X_{1,}$ X_2 + X_3 are the predictive variables trying to predict y.

Say that $X_{1,}$ X_2 + X_3 are age, marital status and credit score and we are trying to predict y – the frequency of an auto claim.

Let's assume that all three Xs are statistically significant predictors of the likelihood of a claim and the b values are how much each X contributes to the explanation of claim. The b values can be tested for statistical significance – how reliable are these estimates of the contribution of each X?

By analyzing these predictive variable simultaneously, the model removes the correlation among the predictive variables.

Use of Control Variables in Multivariate Insurance Models

Suppose an insurer want to control for certain factors that might distort the analysis? For example, an insurer developing a national auto insurance pricing model would want to control for different state effects like different age distributions, different minimum limits requirements and differences in jurisprudence. An insurer would add one or more control variables.

$$b_0 + b_1X_1 + b_2X_2 + b_3X_3 + \mathbf{b_4C_1} + e = y$$

C_1 is a control variable – let's say for State. By including State as a control variable, the correlation of the Xs to State is statistically removed and the new b values are now the contribution of the Xs, independent of their correlation to State, to explaining the likelihood of a claim. When the insurer deploys the model, it still only uses the X variables, but now with more accurate b values.

Legislators Are Familiar with Proxy Discrimination

Whether you call it proxy discrimination or not, you are familiar with the use of proxies to identify how people will vote. When state legislatures develop legislative districts – for state and federal legislators – the party in power seeks to maximize the number of districts whose voters will likely vote for members of their party. You know what voter characteristics are more likely to vote for one party or the other and you create districts based on these characteristics to either pack as many voters likely to vote for the opposing party in as few districts as possible or spread as many voters likely to vote for your party over as many districts as possible to gain a majority in as many districts as possible.

Proxy Discrimination Against a Protected Class in Insurance

The terms “proxy discrimination against a protected class” and “disparate impact” mean the same – discriminating on the basis of a protected class characteristic using a proxy for the protected class characteristic.

I hope we agree that denying coverage or otherwise discriminating against consumers because they are Black Americans or Evangelical Christians is unfair discrimination in insurance.

Suppose, now that we are in an era of Big Data where insurers have access to massive amounts of personal consumer information, that I found a perfect proxy for either of these protected class characteristics and the effect is identical to discriminating directly on the basis of the protected class characteristics. Should a regulator stop the use of these proxy variables on the basis of discriminating against a protected class?

The industry trades say no – the regulator has no such authority.

What is Systemic Racism and Inherent Bias?

"In the coming days, I encourage each of us to step outside of our comfort zones, seek to understand, engage in productive conversations and hold ourselves accountable for being part of the solution. We must forever stamp out racism and discrimination." Those are the words of Kirt Walker, Chief Executive Officer of Nationwide.

Floyd's death in Minneapolis is the latest example of "a broken society, fueled by a variety of factors but all connected by inherent bias and systemic racism. Society must take action on multiple levels and in new ways. It also requires people of privilege—white people—to stand up for and stand with our communities like we never have before," Those are the words of Jack Salzwedel, the CEO of American Family.

Why Do State and Federal Laws Prohibition Discrimination on the Basis of Race?

Justice Kennedy for the Majority in the U.S. Supreme Court's 2015 *Inclusive Communities* Opinion upholding disparate impact as unfair discrimination under the Fair Housing Act.

Recognition of disparate-impact claims is also consistent with the central purpose of the FHA, which, like Title VII and the ADEA, was enacted to eradicate discriminatory practices within a sector of the Nation's economy.

Recognition of disparate-impact liability under the FHA plays an important role in uncovering discriminatory intent: it permits plaintiffs to counteract unconscious prejudices and disguised animus that escape easy classification as disparate treatment.

Why Are Race and Other Protected Class Characteristics Carved Out of Fair Actuarial Discrimination?

The existence of historical, intentional discrimination based on these characteristics – discrimination that violates state and federal constitutions. But, also, the recognition that the historical discrimination has long-lasting effects that disadvantage those groups. Stated differently, you can't enslave a population for two hundred years and then expect the legacy of that enslavement will disappear overnight.

We continue to see those legacies of historical discrimination – systemic racism -- today both directly and indirectly in policing and criminal justice, housing, and the impacts of the Covid-19 pandemic.

Insurance Not Immune to Systemic Racism

There are numerous examples of insurer practices that have a disproportionate impact on the basis of race throughout the insurers' operations – marketing, pricing, claims settlement, anti-fraud.

Examples of practices that have disparate racial impact include:

- Credit-based insurance scores
- Consumer lifetime value scores
- Criminal history scores

The data used to develop these scores reflect historical discrimination in housing, credit and criminal justice. The scores reflect and perpetuate historic discrimination.

Disparate Impact as Both a Standard and a Methodology

Let's go back to multi-variate model, but now use Race as a control variable:

$$b_0 + b_1X_1 + b_2X_2 + b_3X_3 + \mathbf{b_4R_1} + e = y$$

R_1 is a control variable – by including race in the model development, the correlation of the Xs to race is statistically removed and the new b values are now the contribution of the Xs, independent of their correlation to race, to explaining the likelihood of a claim

What if X1 is a perfect proxy for Race?

Then once we add the control variable for Race, X1 no longer has any predictive value because all it was doing was predicting race, not the outcome y.

Disparate Impact Analysis Improves Cost-Based Pricing

There is a long history and many approaches to identifying and minimizing disparate impact in employment, credit and insurance. But, the general principle is to identify and remove the correlations between the protected class characteristic and the predictive variables.

$$b_0 + b_1X_1 + b_2X_2 + b_3X_3 + \mathbf{b_4R_1} + e = y$$

What if X1, X2 and X3 are not perfect proxies for Race, but still have high correlation? Then, the disparate impact analysis – and our simple model – removes that correlation and the remaining values for b1, b2 and b3 are the unique contributions of each predictive variable to explaining the outcome. The result is more – not less – accurate cost-based or risk-based analysis.

Why is it Reasonable and Necessary to Recognize Disparate Impact as Unfair Discrimination in Insurance?

1. It makes no sense to permit insurers to do indirectly what they are prohibited from doing directly. If we don't want insurers to discriminate on the basis of race, why would we ignore practices that have the same effect?
2. It improves risk-based and cost-based practices.
3. In an era of Big Data, systemic racism means that there are no "facially-neutral" factors. From Barocas and Selbst:

Advocates of algorithmic techniques like data mining argue that they eliminate human biases from the decision-making process. ***But an algorithm is only as good as the data it works with.*** *Data mining can inherit the prejudices of prior decision-makers or reflect the widespread biases that persist in society at large.* ***Often, the "patterns" it discovers are simply preexisting societal patterns of inequality and exclusion. Unthinking reliance on data mining can deny members of vulnerable groups full participation in society.***

Why is it Reasonable and Necessary to Require Insurers to Test for and Minimize Disparate Impact?

Insurer practices and algorithms do not necessarily use expected claims as the outcome variable. Sometimes the desired outcome is based on non-cost factors and these non-cost factors has disproportionate impact on communities of color.

In 2005, then CEO of Allstate, Ed Liddy told investment analysts about how credit scoring was helping Allstate avoid the wrong customers:[1]

> Tiered pricing helps us attract higher lifetime value customers who buy more products and stay with us for a longer period of time. That's Nirvana for an insurance company. That drives growth on both the top and bottom line.
>
> This year, we've expanded from 7 basic price levels to 384 potential price levels in our auto business.

[1] Transcript of Presentation to Edward M. Liddy, Chairman and CEO, The Allstate Corporation Twenty-First Annual Strategic Decisions Conference, Sanford C. Bernstein & Co., June 2, 2005.

Tiered pricing has several very good, very positive effects on our business. It enables us to attract really high quality customers to our book of business.

The key, of course, is if 23% or 20% of the American public shops, some will shop every six months in order to save a buck on a six-month auto policy. ***That's not exactly the kind of customer that we want.*** So, the key is to use our drawing mechanisms and our tiered pricing to find out of that 20% or 23%, to find those that are unhappy with their current carrier, are likely to stay with us longer, likely to buy multiple products and that's where tiered pricing and a good advertising campaign comes in.

These statements were made in the Stone Age of Big Data – 2005. Since then insurers' use of new, bigger and more granular personal consumer data has exploded.

Allstate CEO to Investment Analysts, May 2017[2]

The insurer's "universal consumer view" keeps track of information on 125 million households, or 300 million-plus people, Wilson said.

"When you call now they'll know you and know you in some ways that they will surprise you, and give them the ability to provide more value added, so we call it the trusted adviser initiative," said Wilson.

Progressives CEO to Investment Analysts, November, 2020[3]

[Analyst] Gary Ransom
Usually that just means your price is lowest on the comparative raters there. But is there more to it than that as well? Are they – are you seeing more coming into the agents? Is there -- are there agents' incentives or other things going on there?

[CEO Tricia Griffith]
But, yes, we have -- we do incentives and we have different commissions based on the type of customer that we get in namely preferred.

[2] "Allstate CEO: Agents Will Have Access to Data on 125 Million Households," Best's New Service, May 30, 2017
[3] https://seekingalpha.com/article/4385047-progressive-corporation-pgr-ceo-tricia-griffith-on-q3-2020-results-earnings-call-transcript

Practices That Raise Concerns About Proxy Discrimination on the Basis of Race

Price Optimization and Consumer Lifetime Value Scores

By definition, these algorithms used by insurers utilize non-cost factors to differentiate among consumers and the factors and data reflect bias against communities of color.

Credit-Based Insurance Scores

The consumer credit information factors used in CBIS are highly correlated with race. The Missouri Department of Insurance found that the single best predictor of the average CBIS in a ZIP Code was minority population.

Criminal History Scores

Here, the problem is not just the legacy of historical discrimination, but ongoing discrimination in policing and criminal justice.

What are the Benefits and Costs of Requiring Insurers to Test For and Minimize Disparate Impact?

If racial and economic justice are a priority, if cost-based insurer practices are a priority, if closing the protection gap and making insurance more affordable and available in traditionally underserved communities, then the benefits of requiring insurers to test for and minimize disparate impact far, far outweigh the costs.

While there are examples of disparate impact claims brought against insurers under the federal Fair Housing Act that have resulted in improved risk-based pricing and improved insurance availability in communities of color – e.g., challenges against underwriting based on age and value of the home – industry has not been able to cite a single example of a successful disparate impact claim that has harmed risk-based pricing.

Why is it Reasonable and Necessary to Test for and Minimize Disparate Impact in Every Aspect of Insurers' Operations?

Marketing – Today's Big Data algorithms and variety of marketing channels give insurers – like other businesses – the ability to micro-target consumers. This ability to micro-target gives insurers the ability to attract or discourage customers even before the pricing stage.

Claims Settlement and Anti-fraud – Just as insurers use non-cost factors for price optimization in rating, so do they use non-cost factors for claims optimization. Antifraud algorithms – including those use at underwriting for "propensity for fraud" – are most vulnerable to racial bias. Historical bias in what claims to examine for fraud results in bias in the claims identified as fraudulent. Biased antifraud algorithms become self-fulling – if there is racial bias in the claims you identify as potential fraudulent and investigate, there will be racial bias in the claims identified as fraudulent. You can't find fraud in a claim you don't investigate.