



Comments from the Center for Economic Justice

To the NAIC Committee on Race and Insurance

November 10, 2020

The Center for Economic Justice (CEJ) is part of the broad group of civil rights, consumer and community organizations {"groups"} who submitted a comment letter to the NAIC's Committee on Race and Insurance. With these comments, CEJ offers some additional information in support of the groups' recommendations for the Committee's efforts. Like the groups' letter, these CEJ comments are directed to all line of business workstreams of the Committee.

1. Require insurers to examine every aspect of their operations – marketing, underwriting, pricing, claims settlement, and antifraud – for proxy discrimination on the basis of race.

There is no reason for the Committee to discuss whether systemic racism affects insurance consumers, anymore that there is a need to question whether there is systemic racism in our society at large. Rather, the Committee should focus on guidance for insurers for testing for proxy discrimination on the basis of race ("disparate impact") in all aspects of their operations – investments, marketing, underwriting, pricing, claims settlement and antifraud.

As noted in the groups' comment letter, there are some high priority areas to start such testing, but the Committee's priority work effort should be to develop the guidance for insurers and regulators for such testing and reporting test results. There is a rich academic and practice literature on identifying and minimizing disparate impact. The NAIC need not reinvent the wheel, but should curate the materials for the most relevance and application for insurance. We attach CEJ's earlier comments to the NAIC in which we presented one approach for disparate impact testing and explained why such testing improves risk-based practices.

There is another powerful reason why a universal requirement for insurers to test for and minimize disparate impact in insurance operations – the increasing use of new data sources by insurers that can serve as proxies for race. It makes no sense to, say, prohibit credit scoring, if the insurer has several other data sources that replicate the outcomes and disparate impact of credit scoring. ***Instead of an after-the-damage-has-occurred whack-a-mole approach, regulators and insurers should take a holistic approach that places the onus on insurers to test for and minimize disparate impact instead of incentivizing insurers to simply seek out new data sources to replicate the same racially-biased outcomes.***

The simple fact is that insurers have not been concerned about proxy discrimination on the basis of race because they haven't been required to do so. Rather, the insurers – and particularly the trade associations – have hidden behind the false claim that they cannot be discriminating on the basis of race if they don't consider race. The insurers and trades have also hidden behind their total control over the data needed to analyze whether disparate impact exists in insurance. We saw this with credit scoring in the late 1990s and early 2000s and we saw it again with the NAIC's auto insurance study from about 2012 through 2018 in which statistical agents – agents designated by regulators to collect data on behalf of regulators – refused to provide company-specific data to the regulators.

Consider the comments of insurer CEOs to investment analysts, regarding the customers they want and don't want. 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.

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.

Make no mistake about it, the economics of insurance are driven largely by retention levels. It is a huge advantage. And our retentions are as high as they have ever been.

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.

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.

Flash forward 15 years – an eternity in an era of Big Data – and last week we have Progressive – whose rating plans include millions of price levels – responding to investment analyst questions.²

[Analyst] Michael Phillips

What's the lifeline of credit score specifically as a rating variable on personal auto? Are we looking at a couple of years? Do you think that thing dries up or decades?

[CEO] Tricia Griffith

You know what? That's -- I'm glad you brought that up, because I -- we've been thinking about that a lot. And I know there's been -- there will be challenges because of the pandemic on regulatory issues.

So I'm glad you brought it up. I think that credit is a powerful variable. It is [sic] it is not race related. We do not believe it's race related and we'll continue to hold firm on them.

[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.

After examining the racial bias in some of the data used by insurers and the focus on profitability and customer lifetime value measures – as opposed to risk – as well as the cavalier attitudes of some insurers and trades about even the possibility of systemic racism in insurance, it is clear that the crucial step for regulators is to develop the guidance and requirements for insurers to test for proxy discrimination on the basis of race.

We also ask the Committee to avoid haggling with industry over special data calls. We participated in the data collection effort for the auto insurance market study by the NAIC and witnessed multi-year debacle in which industry first opposed providing any data to analyze availability and agreed to provide only those data industry wanted to provide. The result was forced acceptance by regulators of only those data hand-picked by insurers that failed to support the relevant analyses. The issue of robust and routine insurer data reporting should be addressed as a separate track from a work track to develop the guidance for disparate impact testing.

² <https://seekingalpha.com/article/4385047-progressive-corporation-pgr-ceo-tricia-griffith-on-q3-2020-results-earnings-call-transcript>

Finally, on the issue of disparate impact testing, it is crucially important to test data and algorithms used for marketing. And when examining data and algorithms used for underwriting and pricing, outcomes for all insurance applicants should be tested, not just those who purchased a policy. For example, it makes no sense to test for disparate impact based on consumer credit or criminal history if the data are limited to only those consumers who passed underwriting, were offered an affordable premium and purchased a policy. In such a situation, the data set used for testing is biased.

2. Develop a more robust and granular program of data collection for market regulation.

The groups' letter sets out the need and rationale for regulators to develop a far more robust market regulation data collection regime. The contrast between data available for regulators, academics and stakeholders for credit/lending products and insurance is stark. While granular market outcomes for other types of financial services have been available with short lag times, insurance regulators had no data to monitor the impact of the pandemic on insurers and consumers in real time. For mortgage loans, granular data on forbearance and delinquencies (by length of delinquencies) by type of lender by granular geographic area have been timely available from public and private entities, including the Federal Housing Finance Authority, Black Knight and CoreLogic. In contrast, state departments of insurance – with the exception of Texas – do not routinely publish, let alone collect, even quarterly data on insurance market outcomes.

In insurance, there is a vivid disparity between the granular and frequent collection of data for financial analysis of insurers versus data collected for market analysis. For financial regulation, regulators collect massive amounts of data on an annual basis through the statutory annual statement and supplement that with substantial quarterly financial reports. In contrast, for those lines of business for which market outcome data are collected through the Market Conduct Annual Statement (MCAS), there are a handful of data elements collected annually and summarized at the state level. The quarterly financial statements data dwarf the annual MCAS data in volume and granularity.

The problem goes far deeper than simply timely data to respond to the pandemic. Again, in contrast to other financial services, insurance regulators do not routinely collect or publish granular data on market outcomes that can be analyzed for systemic racism. For mortgage and small business lending, federal regulators collect and publish transaction data through the Home Mortgage Disclosure Act. These data have enabled lenders, regulators, academics, fair housing, civil rights and consumer organization to analyze the impact of race on various types of lending. In contrast, insurers have sued to keep even data aggregated at the ZIP Code level confidential and hidden from public view.

In 1997, CEJ published the two attached studies of auto insurance redlining in Texas. The studies prompted actions by the Department of Insurance against some insurers. Instead of responding to these findings with efforts to address the problems, insurers sued to make the information confidential, claiming trade secret.

Any serious effort by insurance regulators to address systemic racism in insurance should include dramatic improvements in reporting by insurers of consumer market outcomes at a granular detail sufficient to analyze the impact of race on insurance outcomes – whether those outcomes are marketing, underwriting, pricing, claims settlement or antifraud. The current MCAS is not up that task.

The MCAS was created 15 years ago and while there has been a revolution in the volume, types and analytics of data used by insurers, there has been no meaningful change or expansion of the handful of highly summarized, state-level MCAS data. There is a great need for the Committee to urge the market regulation committee and working groups to improve the frequency and content of market regulation data.

Thank you for your consideration.



**The Center for Economic Justice’s Call to
Insurers and Insurance Regulators**

**To Address Societal Systemic Bias and Inherent Racism in Insurance
By Explicit Recognition of Disparate Impact as Unfair Discrimination in
Insurance**

**Submitted to the National Association of Insurance Commissioners’
Big Data Working Group
Artificial Intelligence Working Group
Market Regulation and Consumer Affairs Committee
Casualty Actuarial and Statistical Task Force
Accelerated Underwriting Working Group**

June 18, 2020

Action, Not Just Words, Needed

The murder of George Floyd has led to widespread corporate recognition of and opposition to systemic bias and inherent racism in America. Corporate CEOs have spoken out, including major insurer CEOs.

“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.

Perhaps this will be a turning point in insurer and regulatory practices, **but insurers have consistently opposed proposals to address systemic bias and inherent racism in insurance.** This opposition has come in two general themes – opposition to any responsibility by insurers or regulators to identify and minimize **disparate impact**¹ in insurance and opposition to any form of regulatory data collection to allow regulators and the public to assess market outcomes and thereby hold insurers accountable for their practices.

While insurers have been constant in opposing any responsibility to address systemic bias and inherent racism – in contrast to the recent public statements of insurer CEOs – most state insurance regulators believe they have the authority to stop proxy discrimination against protected classes. This belief, however, has never manifested itself, in regulatory standards, model laws or consistent approaches across states.

If insurers and insurance regulators truly want to address systemic bias and inherent racism in insurance, two long-overdue actions are needed.

1. Explicit recognition of disparate impact as unfair discrimination against protected classes in insurance coupled with responsibility for insurers and insurance regulators to identify such disparate impact and take steps to minimize this proxy discrimination within the overall regulatory framework of cost-based pricing.
2. Development of regulatory data collection and analysis infrastructure and capabilities for insurance regulators and the public to meaningfully monitor market outcomes for all consumers, to identify discriminatory outcomes and trace disparate impact to the causes.

¹ Disparate impact refers to practices that have the same effect as disparate treatment or intentional discrimination against protected classes. Protected classes refer to those consumer characteristics which may not be the basis for discrimination and include, in most states, race, religion and national origin. Disparate impact is also known as disparate effect or proxy discrimination – discrimination against the protected class through a proxy for the protected class characteristic. Disparate impact as unfair discrimination has long been recognized under federal employment and housing laws. In 2015, the U.S. Supreme Court affirmed disparate impact as unfair discrimination under the Fair Housing Act which covers a variety of housing-related issues, including insurance, with Justice Kennedy writing, “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.”

The mechanisms to accomplish these actions are straightforward.

1. Development of, and implementation by the states, through the National Association of Insurance Commissioners (NAIC)² of a model law addressing algorithmic bias including recognition of disparate impact as unfair discrimination against protected classes in insurance with guidance and safe harbors for insurers to identify and minimize disparate impact in marketing, pricing, claims settlement and anti-fraud efforts.
2. Development of, and implementation by the states, through the NAIC, of a market regulation data collection and analysis infrastructure to timely and meaningfully monitor consumer insurance outcomes – similar in scope and capability to what state insurance regulators and the NAIC currently have for monitoring the financial condition of insurers.

In the absence of the necessary actions by insurers and the states, Congress and federal agencies will eventually address these problems through civil rights legislation and enforcement.

In An Era of Big Data Analytics and Insurers' Rapidly Growing Use of Third-Party Data and Complex Algorithms, the Potential For Algorithmic Bias and Proxy Discrimination Has Grown Dramatically.

The potential for big data, artificial intelligence, machine learning – implemented through rapid deployment of complex algorithms – has increased the potential for intentional or unintentional proxy discrimination through algorithmic bias. This potential is well recognized. Barocas and Selbst state the issue succinctly:³

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.

Most data sets of personal consumer information as well data sets of the built environment reflect historical discrimination against protected classes. For example, TransUnion has an insurance score used for pricing based on criminal violations filed with the courts – not just convictions, but all criminal filings regardless of the eventual outcome. TransUnion's marketing materials state:

² https://content.naic.org/index_about.htm

³ <http://www.californialawreview.org/wp-content/uploads/2016/06/2Barocas-Selbst.pdf>

“TransUnion recently evaluated the predictive power of court record violation data (including criminal and traffic violations)

“Also, as court records are created when the initial citation is issued, they provide insight into violations beyond those that ultimately end up on the MVR—such as violation dismissals, violation downgrades, and pre-adjudicated or open tickets.”

It did not take the recent murders of Black Americans by police to recognize that this “criminal history score” will reflect historic discrimination in policing against Black Americans and perpetuate that discrimination in insurance. Consider policing records in Ferguson, Missouri.

US DOJ Investigation of the Ferguson Police Department

Ferguson’s approach to law enforcement both reflects and reinforces racial bias, including stereotyping. The harms of Ferguson’s police and court practices are borne disproportionately by African Americans, and there is evidence that this is due in part to intentional discrimination on the basis of race.

Ferguson’s law enforcement practices overwhelmingly impact African Americans. Data collected by the Ferguson Police Department from 2012 to 2014 shows that African Americans account for 85% of vehicle stops, 90% of citations, and 93% of arrests made by FPD officers, despite comprising only 67% of Ferguson’s population.

FPD appears to bring certain offenses almost exclusively against African Americans. For example, from 2011 to 2013, African Americans accounted for 95% of Manner of Walking in Roadway charges, and 94% of all Failure to Comply charges.

Our investigation indicates that this disproportionate burden on African Americans cannot be explained by any difference in the rate at which people of different races violate the law. Rather, our investigation has revealed that these disparities occur, at least in part, because of unlawful bias against and stereotypes about African Americans.

One of the oft-cited benefits of big data analytics in insurance is greater personalization – the ability of insurers to develop products and pricing tailored to individual needs and characteristics. But the other side of personalization is exclusion. Insurers’ use of algorithmic techniques called price optimization, claim optimization and customer lifetime value are examples of the flip side of big data personalization – differential treatment of groups of consumers that reflect and perpetuate inherent bias and systemic racism.

The TransUnion Criminal History Score is just one example – egregious and obvious – of algorithms that reflect and perpetuate historic discrimination against protected classes in insurance – algorithms that reinforce inherent bias and systemic discrimination. Others include:

- Employment categories and education levels for marketing, underwriting and pricing
- Price Optimization and Customer Lifetime Value Algorithms used for marketing, underwriting, pricing and claims settlement
- Facial analytics used in life insurance underwriting
- Household composition used for underwriting and pricing
- Credit scores for marketing, underwriting, pricing, claims settlement and anti-fraud efforts
- Fraud detection models based on biased learning data

Many of these practices have shown to discriminate unfairly against protected classes, generally, and Black Americans, specifically. A number of cities – as well as Google and IBM – have stopped using facial recognition technology because of the biases against Black Americans. After the New York Department of Financial Services developed a regulation permitting the use of employment and education characteristics in auto insurance pricing only if the insurer could demonstrate the practice did not unfairly discriminate against protected classes, insurers' use of the "risk" characteristics disappeared.

The Consumer Federation of America has produced a number of extraordinary studies of discriminatory market outcomes resulting from rating factors that reflect systemic racism.⁴ Insurance industry trade associations have dismissed the CFA's discriminatory findings with the claim that insurers engage in cost-based, race-neutral practices – while refusing to both provide the data to back up these claims and refusing to recognize that systemic racism will show up as disparate impact.

If insurers and insurance regulators are serious about addressing inherent bias and systemic racism in insurance, then action is needed. Fortunately, the insurance industry has the precise skill set needed to identify and minimize disparate impact and insurance regulators have the resources to develop the necessary guidance and infrastructure.

Disparate Impact Analysis is Straightforward and Particularly Suited to Insurance.

The mechanics of a disparate impact analysis in insurance are straightforward and use well-accepted statistical and actuarial methods. Any algorithm – whether for pricing, anti-fraud, claims settlement, lifetime customer value, price optimization or other – takes the basic form of an equation in which certain variables or factors – the explanatory factors – seek to explain or predict a particular outcome.

⁴ <https://consumerfed.org/cfa-studies-on-the-plight-of-low-and-moderate-income-good-drivers-in-affording-state-required-auto-insurance/>

Consider the following general model.

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

Say that $X_1, X_2 + X_3$ are explanatory variables used to predict y – the frequency of an auto claim, for example.

Let's assume that all three X s are statistically significant predictors of the likelihood of a claim and the b values associate with each X are how much each X contributes to the explanation of claim.

b_0 is the “intercept” – a base amount and e is the error term – the portion of the explanation of the claim not provided by the independent variables.

When the algorithm or model is developed, the modeler will typically data mine some database of personal consumer information, built environment or natural environment for characteristics that are correlated with the desired outcome. These variables are combined into a model, but a variable that might be predictive on its own can lose its predictive capability when combined with other variables because the variables might be correlated with one another. In that event, the variable serving as the proxy for the other variable loses its individual explanatory power. In our example, above, if, say, $X_1 + X_2$ are highly correlated, when the two variables are used in the same algorithm, one of the variables will lose its predictive power.

From a statistical and actuarial perspective, a disparate impact analysis does two things. First, it examines the amount of correlation between explanatory variables or factors and protected class characteristics to determine if any of the explanatory variables have significant correlation with, and thereby serve as proxies – in whole or in part – for protected class characteristics.

The second function of a disparate impact analysis is to remove the correlation between the explanatory variables and protected class characteristics with the result that the remaining explanatory power of the explanatory variables is the independent contribution – independent of correlation to protected class characteristics – of the explanatory variables relationship to the outcome.

Consider the following example. Suppose an explanatory factor was perfectly correlated with being a Black American. In statistical terms, this means a perfect or 100% correlation and the explanatory factor is a perfect proxy for being African-American. Assume that when used in an algorithm, this perfect proxy for being a Black American shows us as predictive of some outcome variable. Assume variable X_1 in our simple model above is the perfect proxy characteristic and further assume that the proxy variable shows a correlation to / is predictive of the outcome variable. Given our assumption that variable X_1 is a perfect proxy for being Black American, then the results of the model would be identical whether we used the proxy variable or used Black American explicitly. If the proxy variable is used, this would not be intentional discrimination – defined as explicit use of a protected class characteristic – even though it has

precisely the same effect. While most regulators believe they have the authority and obligation to stop the use of such proxies for protected class characteristics, the insurance industry view, as espoused by the American Property Casualty Insurance Association, is that even in this extreme case, there is no unfair discrimination against a protected class.

When the data are run through the model, variable X_1 shows some correlation to the outcome variable and is, therefore, “predictive.” But, what it is really doing is simply standing in for being Black American and indirectly discriminating on the basis of race. This proxy factor is, in fact, simply reflecting and perpetuating discrimination against Black Americans.

One approach to disparate impact analysis – among many which generally try to remove the correlation between predictive variables and protected class characteristics – is to include a control explanatory variable for being Black American in the algorithm. Let’s now add a new variable to algorithm – a specific variable for being Black American.

$$b_0 + b_1X_1 + b_2X_2 + b_3X_3 + b_4R_1 + e = y$$

In statistical and actuarial terms, this is known as adding a control variable. The purpose of the control variable is to remove known correlations and biases in the other explanatory variables in order to better assess the independent and unique explanatory power of these other explanatory variables. For example, in personal auto pricing models, an insurer developing a national pricing model will utilize a control variable for State to remove the effects of / correlations with other explanatory variables of State-specific characteristics, such as different minimum liability limits, different tort and no-fault systems and different population distributions by age or other factors, among other things. In our example, our control variable R_1 is being Black American.

Now, when the data are run through the model, explanatory variable X_1 – the perfect proxy for being Black American – shows no explanatory power and the control variable now shows the explanatory power that explanatory variable X_1 had in the original model. This is statistical evidence that explanatory variable X_1 was discriminating on the basis of race.

Let’s consider two other examples – one in which there is a 50% correlation between variable X_1 and being Black American and a second in which there is a 0% correlation. In the 50% correlation, the variable X_1 may still show up as predictive of the outcome, but that predictive power will be different than from our first model without the control variable for being Black American. X_1 ’s new contribution to explaining or predicting the outcome will now be its contribution independent of any correlation to being Black American. Consequently, disparate impact is recognized and minimized. Again, this is a common statistical and actuarial technique.⁵

⁵ For example, the technique is explained in the chapter, “Credit Scoring and the Fair Lending Issue of Disparate Impact,” in *Credit Scoring for Risk Managers*, Elizabeth May, editor, 2004.

In our third example there is 0% correlation between the variables X_1 and R_1 . In this situation, the predictive power of X_1 remains the same as in the original model because there is no disparate impact.

As noted above, disparate impact analysis is particularly suited to insurance because the actuarial justification required for insurance risk classifications is a statistical test – is the characteristic correlated with risk of loss? The same statistical test can be used to evaluate and minimize disparate impact. Stated differently – if a particular correlation and statistical significance is used to justify, say, insurance credit scoring, those same standards of correlation and statistical significance are reasonable evidence of disparate impact and unfair discrimination on the basis of prohibited factors.

In addition, the ability of insurers to identify and minimize disparate impact can be easily built into the development of pricing, marketing or claim settlement models by including consideration of prohibited characteristics as control variables in the development of the model and then omitting these prohibited characteristics when the model is deployed. Again, this is one of many ways to remove the correlations between explanatory variables in algorithms and the protected class characteristics that result in reflection of and perpetuation of historic discrimination or disparate impact.

Recognition by regulators and insurers of disparate impact as unfair discrimination in insurance against protected classes and requirements to identify and

- Minimizes Disparate Impact – Stop the Cycle of Perpetuating Historical Discrimination.
- Promotes Availability and Affordability for Underserved Groups
- Improves Cost-Based Insurance Pricing Models
- Improve Price Signals to Insureds for Loss Mitigation Investments
- Help Identify Biases in Data and Modelers / Improve Data Insights
- Improve Consumer Confidence of Fair Treatment by Insurers

What NAIC Committees and Working Groups Should Be Doing

The NAIC has spread work streams related to Big Data Analytics over a number of groups. With the exception of the Artificial Intelligence Working Group, none of these groups' work efforts address systemic bias in insurance.

Artificial Intelligence Working Group

The NAIC Artificial Intelligence (AI) Working Group is developing insurance-specific principles for the governance and use of AI in insurance. While there are a number of consumer protection issues associated with insurers' use of AI (or Big Data Analytics, generally), such as protection of personal data and transparency and accountability to consumers and regulators, the most important consumer protection is establishing a responsibility for insurers and regulators to identify and minimize algorithmic bias and proxy discrimination. Recognition of disparate impact and responsibility of insurers and regulators to minimize such systemic bias must be a core AI insurance principle.

Big Data Working Group

The NAIC Big Data Working Group is examining big data analytics issues across a variety of insurance operations and lines of business. The two actions called for by CEJ regarding disparate impact and data collection should be at the core of all the working group's inquiries and activities. The Big Data Working Group should be developing the model law or revisions to existing model laws regarding explicit recognition of disparate impact, guidelines for identify and minimizing proxy discrimination and safe harbors for insurers.

Market Regulation and Consumer Affairs Committee

The NAIC Market Regulation and Consumer Affairs Committee is the parent committee for a number of working groups related to insurance market regulation, including data collection for market regulation, market surveillance, market conduct examinations and antifraud efforts. The Committee should be a contributor to the development of model laws regarding disparate impact, but must take the lead on market regulation data collection – both to identify the types of data and algorithms used by insurers and what these data are used for and to re-engineer market regulation data collection to match the granularity and frequency of financial regulation data collection.

Casualty Actuarial and Statistical Task Force

The NAIC Casualty Actuarial and Statistical Task Force deals generally with actuarial issues in property casualty lines of insurance. The Task Force is currently developing a white paper to provide best practices for regulatory review of complex pricing models used by insurers to justify rates. The current draft does not incorporate identification and minimization of systemic bias or disparate impact, but simply lists it as another consideration. Insurance rate standards include rates not being excessive, not being inadequate and not being unfairly discriminatory.

The use of complex predictive models for pricing by insurers is focused on risk segmentation and the development of risk classifications and rating factors. Traditional actuarial techniques – not complex predictive models – are generally used for overall rate level indications – the metric for assessing whether rates are excessive or inadequate. The overwhelming reason

for close scrutiny of complex predictive models by regulators is to assess whether the risk classifications are fair or unfairly discriminatory. It is an understatement to say that the current draft white paper has a massive whole because of the failure to address proxy discrimination and disparate impact. Guidance to insurance regulators for regulatory review of complex insurance predictive models should prioritize the identifications and minimization of systemic bias and disparate impact.

Accelerated Underwriting Working Group

The NAIC Accelerated Underwriting Working Group continues the NAIC's multi-year examination of life insurers' use of Big Data analytics and predictive models in place of traditional actuarial practices for underwriting and pricing life insurance. While the predictive models now used by life insurers have the same function as those used in auto, home and other property casualty lines of insurance – namely, using non-traditional data and an algorithm to predict claims (or other outcomes of value to the insurer). While there are requirements for property casualty insurers to file these predictive models for regulatory review for some purposes – justifying rates – and special laws and provisions governing property casualty insurers' use of consumer credit information, there are no similar regulatory requirements for life insurers. The time is long overdue for this working group to develop the model laws for regulatory guidance and consumer protections to ensure consumer protections in the face of life insurers' growing use of non-traditional, non-insurance data and complex algorithms. And the core of such models laws and regulatory guidance must be identification and minimization of disparate impact and systemic racism.

Conclusion

Recent events have highlighted a long-standing gaps in insurer and insurance regulatory practices – the failure to monitor consumer market outcomes for discriminatory impacts against protected classes and the failure to incorporate identification and minimization of proxy discrimination in insurers' development of predictive models for all aspects of their operations and regulators' review of these algorithms. The tools are available to address these problems – analysis of disparate impact and improved data collection. CEJ calls on insurers and regulators to match their statements of outrage over systemic racism with the actions needed to identify and minimize such unfair discrimination in insurance.

THE CENTER FOR ECONOMIC JUSTICE

**Worst Redliners Identified:
Department of Insurance
Fails to Act**

May, 1997

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THE CENTER FOR ECONOMIC JUSTICE

Executive Summary

Nationwide is not on your side--if you live on the wrong side of town. Neither is **USAA, Farm Bureau, State Farm** or **Safeco**. Analysis of individual company market data supplied by the Texas Department of Insurance shows these companies are among the state's worst redliners.

Yet, despite the clear evidence of redlining from the Department's own data, the **Texas Department of Insurance (TDI) has done little to address the problem.**

This analysis **complements the Center for Economic Justice's recent study** of urban drivers placed in sub-standard companies (usually county mutual companies) or assigned to the Texas Auto Insurance Plan Association (TAIPA), which showed that drivers in poor and minority communities were disproportionately rejected by standard (lower priced) insurers.

Now, CEJ examines the market share in Anglo and non-Anglo areas of the largest auto insurers in Texas. The study shows that five of those insurers--**Nationwide, USAA, Farm Bureau, State Farm** and **Safeco**--have a substantially smaller market share of *insured* drivers in minority communities than they do in Anglo communities.

Although the **Texas Department of Insurance** provided the data that establishes these companies as among the state's worst redliners, the Department itself has done little to address unfair discrimination in the sale of auto insurance in Texas.

The Center for Economic Justice recommends the Commissioner:

- exercise his regulatory responsibility and **immediately investigate the underwriting, marketing and sales practices of Nationwide, USAA, Farm Bureau, State Farm and Safeco;**
- **agressively investigate redlining and unfair discrimination** by using "testers";
- take **prompt and decisive action to stop illegal and unfair discrimination** by insurers;
- **follow-up on the Houston redlining task force;** and
- **bar the use of credit history, prior insurance carrier, employment and residential stability and occupation as underwriting guidelines.**

Findings

Analysis of individual company market data supplied by the Texas Department of Insurance shows that **Nationwide, USAA, Farm Bureau, State Farm and Safeco** are among the state's worst redliners. Yet, despite the clear evidence of redlining from the Department's own data, the **Texas Department of Insurance (TDI) has done little to address the problem.**

CEJ examines the market share in Anglo and non-Anglo areas of the largest auto insurers in Texas. The study shows that five of those insurers --Nationwide, USAA, Farm Bureau, State Farm and Safeco-- have a substantially smaller market share of *insured* drivers in minority communities that they do in Anglo communities.

USAA writes far more than its statewide average in predominantly Anglo areas. The results are particularly striking in San Antonio where the company writes more than 25% of the insured vehicles in Anglo areas but less than 5% in minority areas.

The **Farm Bureau's** statewide results may be partially explained by their large rural market, where the non-Anglo population is lower. However, this company also controls a substantial urban market, and **in urban areas Farm Bureau's market share also drops dramatically in minority zip codes.**

Nationwide's homeowners insurance sales practices have been the subject of consumer complaints and federal redlining investigations for years. **In predominantly Anglo areas of the state's largest cities Nationwide controls 3 to 6% of the market. In minority areas it covers less than 1.5% of the insured vehicles.**

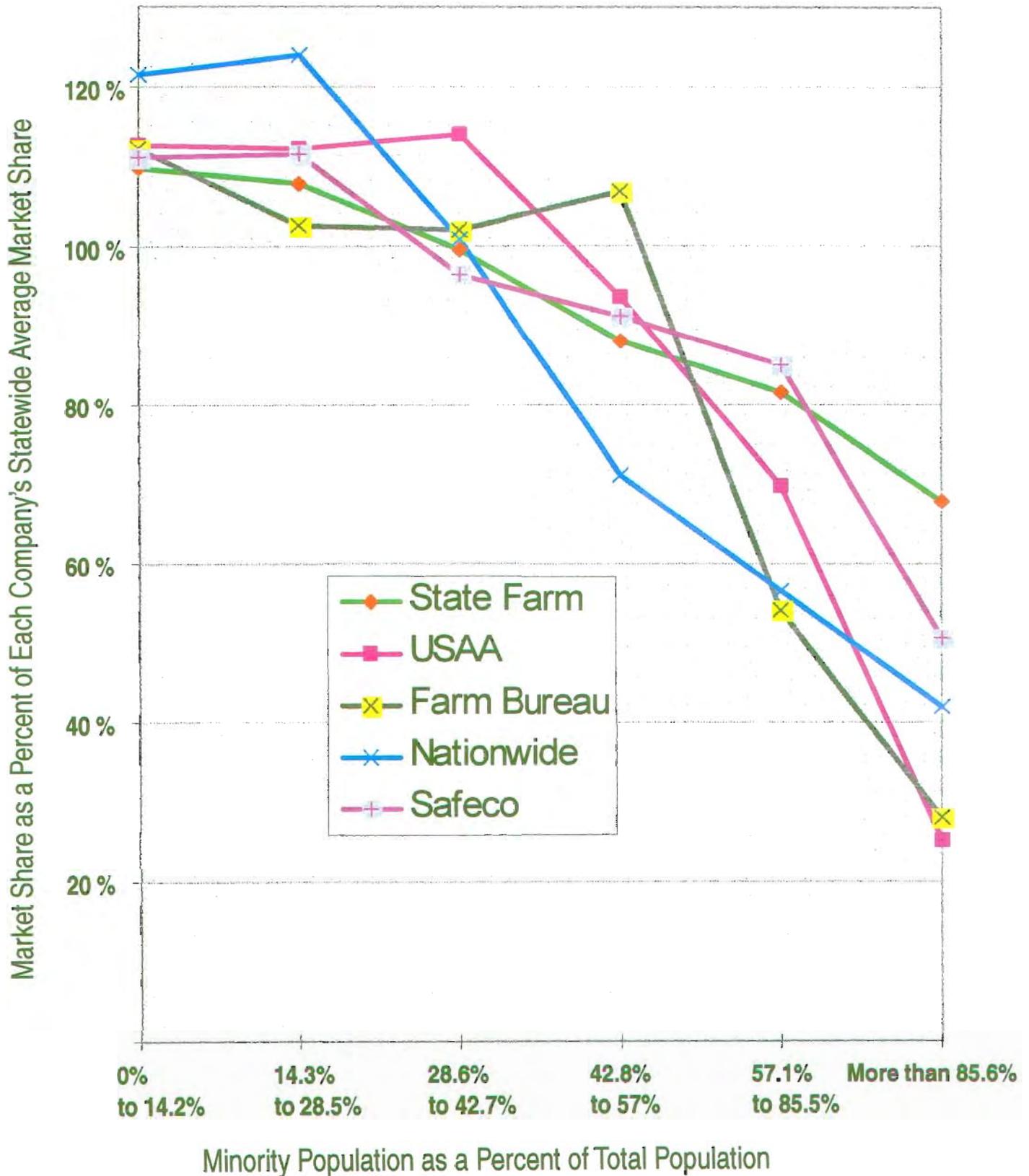
State Farm and Safeco also show significant marketshare declines in minority areas. On a statewide basis, State Farm's market share drops from 31% in Anglo areas to only 19% in non-Anglo areas. Safeco, with a far smaller share of the market as a whole, also drops to about half its Anglo area market strength in non-Anglo areas.

The significant reduction in market share in minority neighborhoods for these five insurers contrasts with that of Geico. **Geico's market share is as great or greater in minority communities as in Anglo areas.**

Farmers' market share in high-minority communities is less than its market share in low-minority communities, but to a lesser extent than Nationwide, USAA, Farm Bureau, State Farm and Safeco. While **Allstate** shows strong standard market presence in minority communities, the company places more consumers in these areas in its higher-priced county mutual company. Statewide, Allstate markets and writes far more high-cost, non-standard insurance in high minority ZIP Codes than in low-minority ZIP Codes.

Auto Insurance Redlining in Texas:

Minority Communities Do Not Have Equal Opportunity to Purchase Affordable Insurance



Recommendations

CEJ recommends the Department exercise its regulatory responsibility and immediately investigate the underwriting, marketing and sales practices of Nationwide, USAA, Farm Bureau, State Farm and Safeco. It should then take swift and decisive action to end the practices that result in redlining. The state requires all drivers to carry auto insurance, so it has a duty to protect consumers from unfair discrimination by insurers.

Second, the Department should more aggressively **investigate redlining and unfair discrimination by using “testers.”** In testing, paired “shoppers” of insurance are matched on all characteristics except their race or the racial composition of their neighborhood. Consumer advocates and regulators throughout the country have successfully used testers to identify and ultimately reduce insurance redlining.

Third, the Department should take **prompt and decisive action to stop illegal and unfair discrimination** by insurers. In September 1996, CEJ identified a new and illegal underwriting guideline by one of Texas’ largest auto insurers. This illegal guideline made it more difficult for low income consumers to comply with financial responsibility laws. The Department agreed that the guideline is illegal, but took months to even begin an investigation and to date has not issued a cease and desist order or initiated disciplinary action.

Fourth, the Department should **follow-up on the Houston redlining task force** created in 1994. That task force included the Department, insurers, and community leaders who all agreed that there is an availability problem and worked together to solve the problem. Although several insurers made commitments to increase their writings or take other steps in those underserved areas, the Department has done nothing to ensure that insurers have kept those promises.

Fifth, the Department should **pass rules to prohibit unfair underwriting guidelines that are not risk-related.** Underwriting guidelines are the rules used by insurers to determine if they will offer coverage to a consumer, and if so, at what price. Although the Department has the authority to prohibit the use of unfair underwriting guidelines, it has failed to do so. Consumers Union, for instance, petitioned the Department to adopt rules in July of 1996, one of which would prohibit the blacklisting underwriting guideline described below. Although state law required the Department to act on the petition within 60 days, the Department has failed to take any action on it.

The Commissioner should bar the use of the following underwriting guidelines:

Credit History--Many insurance companies subscribe to the credit history scoring service of Fair, Isaac. The Fair Isaac product takes information in a consumer’s credit report and creates a score--the higher the score the more attractive the risk to insurers. Fair, Isaac refuses to show regulators the inner workings of its credit scoring model, which may penalize lower income consumers.

Prior Insurance Carrier/Blacklisting--Companies have used underwriting guidelines which deny coverage to consumers who have already been turned down by other insurers or covered by non-standard companies (like County Mutuals). Consumers who are already the victims of redlining continue to face discrimination because insurance companies rely upon actions of other insurers instead of making their own independent business decisions. This underwriting practice is profoundly anti-competitive.

Employment and Residencial Stability--Underwriting guidelines which deny auto insurance to people who have recently changed jobs, been unemployed, moved or do not own their own home also punish poor and minority communities where employment is scarce. These guidelines also have an unfair impact on people who rent.

Occupation--Some insurers deny coverage to consumers in low-wage jobs. For instance, they insure attorneys but refuse to insure clerical workers. Occupation related guidelines have a disproportionate impact on poor and minority communities.

The Commissioner has ample authority to investigate and halt illegal redlining and eliminate underwriting and marketing practices that disproportionately effect minority areas. Auto insurance should be equally available to every good driver and available at the same affordable rates.

Individual Company Results

Urban Area Results

Although Safeco and Farm Bureau have a lower overall share of the auto insurance market in each of the following urban areas (relative to State Farm, for example), they typically write a much larger share of their urban area business in predominantly Anglo areas, as the following pages show.

The first page of charts to follow describes State Farm, USAA, Farm Bureau, Nationwide and Safeco's overall marketshare in each urban area. State Farm, because it controls a larger share of the market, stands out. The second page, however, compares each company's market share in each zip code grouping to *its own statewide average*. The results are striking. **Nationwide, Safeco and USAA write far more than their own statewide average in Anglo areas and far less in minority areas.**

Appendix

Automobile Insurance Redlining in Texas: Minority Communities Do Not Have Equal Opportunity to Purchase Affordable Insurance

Minority Population	Number of ZIP Codes	1990 Population	Vehicles Insured in Standard and Preferred Companies as a Percentage of Total Vehicles Insured								
			State Farm	Allstate	Allstate CM	Farmers	USAA	Farm Bureau	Geico	Nationwide	Safeco
0.0% to 14.2%	552	2378800	31.5%	13.1%	2.4%	13.7%	6.4%	4.6%	1.9%	2.3%	1.0%
14.3% to 28.5%	412	2781613	30.9%	12.4%	2.9%	13.3%	6.4%	4.2%	2.2%	2.3%	1.0%
28.6% to 42.7%	262	1713472	28.5%	11.4%	3.4%	13.1%	6.5%	4.1%	2.6%	1.9%	0.9%
42.8% to 57.0%	150	864405	25.2%	11.1%	4.1%	12.9%	5.3%	4.3%	3.2%	1.3%	0.8%
57.1% to 85.5%	165	978905	23.3%	12.3%	4.5%	13.4%	4.0%	2.2%	2.9%	1.1%	0.8%
85.6% or more	93	446935	19.4%	13.2%	4.9%	12.1%	1.4%	1.1%	2.3%	0.8%	0.5%

Statewide Market Share 28.6% 12.3% 3.3% 13.5% 5.7% 4.1% 2.3% 1.9% 0.9%

Minority Population	Market Share in ZIP Code Groupings Compared to Statewide Market Share								
	State Farm	Allstate	Allstate CM	Farmers	USAA	Farm Bureau	Geico	Nationwide	Safeco
0.0% to 14.2%	110.0%	106.1%	72.8%	101.0%	112.9%	112.4%	82.6%	121.6%	111.3%
14.3% to 28.5%	108.0%	100.5%	89.0%	98.7%	112.5%	102.7%	95.0%	124.1%	111.7%
28.6% to 42.7%	99.7%	92.4%	105.4%	97.1%	114.1%	102.1%	113.0%	101.0%	96.5%
42.8% to 57.0%	88.3%	90.1%	127.2%	95.5%	93.8%	107.0%	137.3%	71.2%	91.3%
57.1% to 85.5%	81.6%	100.3%	138.2%	99.5%	69.9%	54.1%	124.6%	56.5%	85.2%
85.6% or more	67.9%	107.5%	150.3%	89.4%	25.1%	28.0%	98.3%	42.0%	50.5%

Notes:
 All data supplied by the Texas Department of Insurance.
 Insured Vehicle Counts as of September 30, 1996
 Minority (Non-Anglo) Population from 1990 Census
 Companies Included are State Farm Mutual, Allstate Indemnity, Allstate Insurance, Allstate Property & Casualty, Allstate County Mutual, Mid-Century, Texas Farmers, USAA, USAA CIC, USAA County Mutual, Southern Farm Bureau Mutual, Texas Farm Bureau Mutual, Geico General, Geico Indemnity, Government Employees, Nationwide General, Nationwide Mutual Fire, Nationwide Mutual, Nationwide Property & Casualty, Safeco Lloyds, and Safeco of Illinois.

**Auto Insurance Redlining in Texas:
County Results**

Dallas County

Vehicles Insured in Standard and Preferred Companies as a % of Total Vehicles Insured

Minority Population	<u>State Farm</u>	<u>Allstate</u>	<u>Farmers</u>	<u>USAA</u>	<u>Farm Bureau</u>	<u>Geico</u>	<u>Nationwide</u>	<u>Safeco</u>
0-14.2%	31.1%	11.5%	12.6%	9.7%	0.7%	2.7%	5.0%	2.2%
14.3-28.5%	32.9%	12.7%	15.6%	5.4%	0.8%	2.5%	3.9%	1.5%
28.6-42.7%	29.8%	11.4%	15.9%	5.3%	0.6%	3.0%	3.1%	1.3%
42.8-57%	26.1%	13.0%	14.7%	4.8%	0.7%	2.8%	2.3%	1.4%
57.1-85.5%	24.3%	13.0%	15.4%	2.9%	0.5%	2.5%	1.6%	1.3%
85% and higher	19.1%	17.1%	14.1%	0.4%	0.2%	1.7%	1.2%	0.8%
statewide marketshare	28.6%	12.3%	13.5%	5.7%	4.1%	2.3%	1.9%	0.9%

Market Share in ZIP Code Groupings as a Percent of Statewide Market Share

Minority Population	<u>State Farm</u>	<u>Allstate</u>	<u>Farmers</u>	<u>USAA</u>	<u>Farm Bureau</u>	<u>Geico</u>	<u>Nationwide</u>	<u>Safeco</u>
0-14.2%	108.9%	93.4%	93.0%	171.0%	17.7%	118.3%	264.2%	239.6%
14.3-28.5%	115.3%	103.2%	115.4%	95.5%	19.1%	110.3%	206.8%	164.6%
28.6-42.7%	104.3%	92.2%	118.0%	93.4%	15.9%	131.6%	163.4%	141.5%
42.8-57%	91.5%	105.1%	108.9%	83.9%	16.2%	122.8%	122.2%	160.0%
57.1-85.5%	84.9%	105.9%	113.8%	51.0%	12.1%	107.0%	84.0%	140.7%
85% and higher	66.8%	138.4%	104.1%	6.9%	5.1%	73.2%	62.6%	86.7%

Harris County

Vehicles Insured in Standard and Preferred Companies as a % of Total Vehicles Insured

Minority concentration	<u>State Farm</u>	<u>Allstate</u>	<u>Farmers</u>	<u>USAA</u>	<u>Farm Bureau</u>	<u>Geico</u>	<u>Nationwide</u>	<u>Safeco</u>
0-14.2%	30.5%	13.7%	15.2%	8.5%	0.8%	2.4%	4.0%	1.0%
14.3-28.5%	31.1%	13.1%	15.9%	6.2%	0.8%	2.5%	3.5%	0.9%
28.6-42.7%	27.9%	12.4%	16.8%	4.6%	0.7%	2.8%	2.0%	0.8%
42.8-57%	24.6%	12.8%	18.4%	3.7%	0.6%	3.2%	2.2%	0.9%
57.1-85.5%	19.1%	14.9%	16.6%	2.0%	0.6%	2.3%	1.4%	0.7%
85.6% or more	13.5%	18.0%	14.2%	0.9%	0.4%	2.7%	1.4%	0.7%
statewide marketshare	28.6%	12.3%	13.5%	5.7%	4.1%	2.3%	1.9%	0.9%

Market Share in ZIP Code Groupings as a Percent of Statewide Market Share

Minority concentration	<u>State Farm</u>	<u>Allstate</u>	<u>Farmers</u>	<u>USAA</u>	<u>Farm Bureau</u>	<u>Geico</u>	<u>Nationwide</u>	<u>Safeco</u>
0-14.2%	106.7%	110.9%	112.4%	149.0%	18.6%	105.6%	212.2%	112.5%
14.3-28.5%	108.6%	106.1%	117.5%	108.5%	18.9%	109.6%	187.6%	104.7%
28.6-42.7%	97.5%	100.5%	124.0%	81.4%	17.6%	122.1%	108.2%	93.7%
42.8-57%	86.0%	103.9%	136.4%	64.3%	15.0%	137.7%	116.9%	104.0%
57.1-85.5%	66.7%	121.3%	122.9%	34.9%	14.5%	100.7%	72.9%	74.2%
85.6% or more	47.4%	145.8%	105.4%	15.0%	8.7%	115.6%	74.9%	74.1%

Tarrant County

Vehicles Insured in Standard and Preferred Companies as a % of Total Vehicles Insured

Minority concentration	<u>State Farm</u>	<u>Allstate</u>	<u>Farmers</u>	<u>USAA</u>	<u>Farm Bureau</u>	<u>Geico</u>	<u>Nationwide</u>	<u>Safeco</u>
0-14.2%	33.8%	16.1%	14.5%	7.6%	0.8%	2.6%	3.2%	1.1%
14.3-28.5%	32.7%	14.0%	15.4%	7.4%	0.7%	3.2%	2.7%	1.1%
28.6-42.7%	27.3%	13.5%	17.1%	4.8%	0.7%	3.1%	1.2%	1.7%
42.8-57%	22.3%	13.5%	16.8%	4.0%	0.6%	2.3%	1.2%	1.3%
57.1-85.5%	18.3%	14.7%	17.1%	1.1%	0.3%	2.1%	0.8%	1.2%
85.6% and up	14.3%	15.3%	13.6%	0.5%	0.2%	1.9%	0.7%	0.8%
statewide mkshare	28.6%	12.3%	13.5%	5.7%	4.1%	2.3%	1.9%	0.9%

Market Share in ZIP Code Groupings as a Percent of Statewide Market Share

Minority concentration	<u>State Farm</u>	<u>Allstate</u>	<u>Farmers</u>	<u>USAA</u>	<u>Farm Bureau</u>	<u>Geico</u>	<u>Nationwide</u>	<u>Safeco</u>
0-14.2%	118.3%	130.7%	107.3%	133.1%	20.9%	111.8%	168.2%	116.8%
14.3-28.5%	114.6%	113.8%	114.2%	129.7%	17.3%	137.1%	144.5%	127.0%
28.6-42.7%	95.5%	109.2%	126.8%	83.5%	16.2%	133.7%	66.2%	184.2%
42.8-57%	78.1%	109.7%	124.4%	70.9%	15.8%	101.3%	65.1%	143.2%
57.1-85.5%	64.1%	119.1%	126.6%	19.4%	7.8%	91.3%	42.4%	136.7%
85.6% and up	50.2%	124.3%	100.3%	8.1%	3.8%	82.6%	36.2%	90.2%

Bexar County

Vehicles Insured in Standard and Preferred Companies as a % of Total Vehicles Insured

Minority concentration	<u>State Farm</u>	<u>Allstate</u>	<u>Farmers</u>	<u>USAA</u>	<u>Farm Bureau</u>	<u>Geico</u>	<u>Nationwide</u>	<u>Safeco</u>
0-14.2%	26.1%	8.7%	7.2%	31.3%	1.9%	2.1%	6.0%	2.0%
14.3-28.5%	24.2%	7.3%	7.3%	26.9%	1.4%	3.2%	6.7%	2.4%
28.6-42.7%	26.1%	8.7%	8.4%	21.7%	0.9%	4.2%	5.6%	1.9%
42.8-57%	26.3%	9.6%	9.0%	14.5%	1.0%	5.6%	3.5%	1.8%
57.1-85.5%	24.8%	10.9%	9.7%	7.0%	1.0%	4.1%	2.2%	1.8%
85.6% or more	20.6%	7.7%	2.9%	2.9%	0.3%	3.1%	1.2%	1.2%
statewide mkshare	28.6%	12.3%	13.5%	5.7%	4.1%	2.3%	1.9%	0.9%

Market Share in ZIP Code Groupings as a Percent of Statewide Market Share

Minority concentration	<u>State Farm</u>	<u>Allstate</u>	<u>Farmers</u>	<u>USAA</u>	<u>Farm Bureau</u>	<u>Geico</u>	<u>Nationwide</u>	<u>Safeco</u>
0-14.2%	91.2%	70.3%	53.5%	550.0%	46.3%	89.2%	318.8%	225.5%
14.3-28.5%	84.6%	59.1%	54.0%	471.7%	34.4%	139.5%	355.1%	267.1%
28.6-42.7%	91.3%	71.0%	62.3%	380.1%	21.0%	181.3%	298.9%	211.0%
42.8-57%	92.0%	77.7%	66.7%	253.9%	25.6%	240.7%	187.0%	195.6%
57.1-85.5%	86.6%	88.3%	72.0%	123.6%	24.0%	175.9%	115.2%	197.6%
85.6% or more	72.1%	62.3%	21.6%	51.3%	7.6%	134.0%	61.5%	135.8%

Travis County

Vehicles Insured in Standard and Preferred Companies as a % of Total Vehicles Insured

Minority concentration	<u>State Farm</u>	<u>Allstate</u>	<u>Farmers</u>	<u>USAA</u>	<u>Farm Bureau</u>	<u>Geico</u>	<u>Nationwide</u>	<u>Safeco</u>
0-14.2%	33.0%	8.5%	10.0%	14.3%	0.8%	2.9%	4.1%	1.8%
14.3-28.5%	31.9%	10.6%	10.4%	12.1%	1.0%	3.7%	2.9%	1.5%
28.6-42.7%	30.5%	10.0%	11.3%	8.3%	1.1%	3.8%	2.7%	1.4%
42.8-57%	23.4%	12.3%	10.4%	6.3%	1.9%	4.3%	1.3%	1.2%
57.1-85.5%	24.8%	11.0%	11.4%	6.1%	0.8%	4.0%	1.4%	1.0%
85.6% or more	18.3%	15.6%	12.0%	1.2%	0.3%	2.0%	0.8%	0.8%
statewide mkshare	28.6%	12.3%	13.5%	5.7%	4.1%	2.3%	1.9%	0.9%

Market Share in ZIP Code Groupings as a Percent of Statewide Market Share

Minority concentration	<u>State Farm</u>	<u>Allstate</u>	<u>Farmers</u>	<u>USAA</u>	<u>Farm Bureau</u>	<u>Geico</u>	<u>Nationwide</u>	<u>Safeco</u>
0-14.2%	115.3%	68.8%	73.8%	250.4%	18.9%	125.3%	216.2%	203.4%
14.3-28.5%	111.7%	86.2%	76.8%	212.8%	24.9%	161.0%	156.2%	164.6%
28.6-42.7%	106.6%	81.0%	83.6%	145.0%	27.2%	163.4%	143.8%	157.1%
42.8-57%	81.8%	100.0%	77.0%	110.8%	45.8%	186.2%	68.4%	136.0%
57.1-85.5%	86.8%	89.5%	84.7%	107.0%	20.5%	173.0%	72.8%	109.6%
85.6% or more	63.9%	126.6%	88.5%	20.6%	6.7%	88.5%	40.4%	91.2%

THE CENTER FOR ECONOMIC JUSTICE

Auto Insurance Redlining In Texas:

**Availability Worsens While
Consumers Lose
Affordable Coverage Options**

April, 1997

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THE CENTER FOR ECONOMIC JUSTICE

Executive Summary

Texas auto insurers continue to redline drivers who live in low-income and minority communities, according to data provided by the Texas Department of Insurance.

This new analysis of urban drivers placed in sub-standard companies (usually county mutual companies) or assigned to the Texas Auto Insurance Plan Association (TAIPA) shows that **drivers in poor and minority communities were disproportionately rejected by standard insurers and forced into the higher cost non-standard and assigned risk markets.**

Despite several studies, acknowledgement of the problem and "commitments" by insurers to make affordable insurance more available in low-income and minority communities, **the overall rejection rate increased and insurance availability worsened** over the past five years.

The new analysis **confirms several earlier studies** of insurance availability in Texas cities, including 1993 studies by the Office of Public Insurance Counsel (OPIC) and the Texas Department of Insurance (TDI), 1994 studies by TDI and the Austin American-Statesman, and a new study by the Fort Worth Star-Telegram.

While redlining continues, consumers no longer have an affordable alternative to non-standard coverage. In 1992, the TAIPA offered coverage at reasonable rates to those rejected by the standard market. In the past two years, however, TAIPA rates increased to unaffordable levels--almost twice the state benchmark rate. Because of the excessive rates, TAIPA is no longer a safety valve for consumers in redlined communities. Instead, many consumers who want to buy insurance and comply with financial responsibility laws simply cannot afford to and become criminals.

In essence, county mutuals and the TAIPA have become a **high priced dumping ground** for low income and minority drivers who do not pose a higher risk for auto collisions but who have fewer options when they shop for a better deal. These practices **undermine the financial responsibility laws, criminalize poverty and deny low-income and minority communities equal opportunity** in the insurance market.

Recommendations

In light of these and previous similar findings, **the Center for Economic Justice recommends** the following:

- implement regulations to ensure that insurers offer drivers with no moving violations or at-fault accidents a policy in their standard or preferred company;
- cap the cost of a policy offered through the TAIPA at 145 percent of the standard market benchmark rate;
- enforce existing anti-redlining statutes and regulations;
- prohibit the use of unfair underwriting and rating factors, including credit history and prior insurance carriers.

A Divided Market

State Farm, Farmers, Allstate and many other large auto insurers sell coverage through a group of subsidiary companies that each sell the standardized Texas auto policy at a different price. Coverage through the county mutual costs two to four times more than coverage through a preferred or standard company. Independent county mutual insurers also market expensive policies to Texas drivers.

Consumers pay different rates for auto insurance depending on the type of company into which the insurer or agent places them. A Farmers County Mutual policy may cost hundreds of dollars more than a Midcentury policy (Farmers' preferred company).

Consumers qualify for coverage in either a preferred, standard or county mutual company depending on each company's underwriting practices.

Preferred consumers are those perceived by insurers as the least risky. They meet the most restrictive underwriting guidelines and qualify for the lowest rates. Preferred rates are about 10 percent to 15 percent above the benchmark rate.

Standard consumers are those insurers believe to be a little, but not much, more risky. They qualify for coverage by the company with slightly less restrictive underwriting guidelines and somewhat higher rates--generally about 25 percent to 30 percent above benchmark rates.

Rates for standard and preferred customers are regulated under *Texas Insurance Code* 5.101--benchmark rating with flexibility bands. The standard/preferred market represents about 75 to 80 percent of the total private passenger automobile insurance market in Texas.

Drivers who do not qualify for standard or preferred coverage are written in the **non-standard** market by companies with the least restrictive underwriting guidelines and the highest prices--mostly non-rate regulated **county mutual companies**. County mutuals are not subject to Article 5.101 and are not governed by the rating rules of the *Texas Automobile Rules and Rating Manual*. In the second quarter of 1996, about 20 county mutual insurers wrote private passenger automobile policies.

When an auto insurer does not want to insure a particular consumer in its standard or preferred company, the insurer's agent may assign the applicant to the **Texas Automobile Insurance Plan Association (TAIPA)**. In recent years, rates for TAIPA have risen dramatically to levels at or above county mutual rate levels.

Study Method

This study of private passenger insurance availability is based upon data supplied by the Texas Department of Insurance (TDI). The measure of insurance availability used is the share of vehicles insured by non-standard insurers and the TAIPA (assigned risk) as a percentage of all vehicles insured. Because people insured by non-standard insurers and TAIPA have been rejected by the standard market, we call this measure the auto insurance rejection rate.

This ratio of TAIPA plus nonstandard to total exposures is

an excellent measure of private passenger automobile insurance availability because the measure identifies the share of all consumers who sought automobile insurance, could afford it, paid for it, and yet, were rejected by standard and preferred companies. Because substandard company rates are typically very high and consumers are not eligible for coverage through TAIPA unless they are unable to obtain standard coverage, the class of consumers insured through TAIPA or by substandard companies constitutes a class of consumers for whom coverage in the standard and preferred market was not available.

Statewide Results

Table 1 groups Zip Codes by the auto insurance rejection rate. As the rejection rate increases, and availability decreases, the share of minority population increases and the median household income decreases. Between 1992 and 1996, little has changed for low-income and minority consumers. Both income and race are statistically significant predictors of availability.

On a statewide basis in 1996, 22.6 percent of insured drivers had non-standard or TAIPA coverage. But, in ZIP Codes with **high** minority populations and **low** median household income, the percentage of drivers who had non-standard or TAIPA coverage was substantially **higher than the statewide average**. Conversely, in Zip Codes with low minority populations and high median household income, the percentage of drivers who had non-standard or TAIPA coverage was substantially lower than the statewide average.

For instance, there were 38 Zip Codes with an average non-anglo population of 83.7 percent and an average median household income of \$16,441. The automobile insurance rejection rate in these Zip Codes was 46.8 percent to 51.9

CEJ utilized a regression analysis to determine the impact of race alone on insurance availability. The analysis shows that, even holding income constant, consumers in Zip Codes with high minority population (at least 80%) were two to three times more likely to be insured in non-standard insurers or TAIPA than consumers in low (no more than 10%) minority communities.

Summary of Insurance Availability Problems Statewide in 1992 and 1996

	1992 Average of Non-Anglo Population Percentage	1992 Average of Median Household Income	1992 Number of ZIP Codes	1996 Average of Non-Anglo Population Percentage	1996 Average of Median Household Income	1996 Number of ZIP Codes
Over 51.9%	95.2%	\$12,858	11	92.3%	\$14,015	26
46.8% to 51.9%	93.9%	\$13,173	16	83.7%	\$16,441	38
41.6% to 46.7%	88.1%	\$15,849	29	82.7%	\$17,682	45
36.4% to 41.5%	83.1%	\$18,783	41	68.5%	\$19,954	65
31.2% to 36.3%	68.5%	\$20,136	73	54.6%	\$21,549	79
26.1% to 31.1%	50.4%	\$21,771	97	43.0%	\$23,456	142
20.9% to 26.0%	34.2%	\$22,658	250	29.4%	\$24,523	280
15.7% to 20.8%	24.7%	\$24,869	484	20.7%	\$24,871	413
10.5% to 15.6%	16.1%	\$29,675	391	13.6%	\$30,565	317
5.3% to 10.4%	10.9%	\$42,097	85	12.1%	\$44,042	74
0.0% to 5.2%	10.8%	\$53,374	3	4.7%	\$22,414	1

* Groupings for comparison are based on statewide rejection rate in 1992, which was 20.8%.

percent, meaning that drivers in these poor and minority communities received non-standard or TAIPA coverage twice as often as the statewide average. But drivers in Zip Codes with low non-Anglo populations and high income levels did much better. In 317 Zip Codes with an average non-Anglo population of 13.6 percent and an average median household income of \$30,565, the automobile rejection rate was only 10.5 percent to 15.6 percent, substantially less than the statewide average.

CEJ utilized a regression analysis to determine the impact of race alone on insurance availability. The analysis shows that, even holding income constant, consumers in Zip Codes with high minority population (at least 80%) were two to three times more likely to be insured in non-standard insurers or TAIPA than consumers in low (no more than 10%) minority communities.

Major Metropolitan Area Results

Maps for several urban counties in Texas present the 1996 ZIP Code level data more graphically. The final pages of this report display these maps for Harris, Bexar, Travis, Dallas and Tarrant counties. For each county the maps show insurance availability by ZIP Code followed by the average percentage of non-Anglo population. Those ZIP Codes with poor insurance availability are, in most cases, the same ZIP Codes with high minority populations.

The Commissioner of Insurance sets the benchmark rate for

Summary of Insurance Availability Problems Harris County

Automobile rejection rate	Number Zip Codes	Non-Anglo population	Average income
Under 11.3 percent	11	12.19%	\$59,447
11.3 to 22.6 percent	41	23.45%	\$41,322
22.7 to 33.9 percent	33	40.77%	\$30,510
34 to 45.2 percent	31	69.39%	\$23,119
over 45.2 percent	13	85.29%	\$17,403

Summary of Insurance Availability Problems Travis County

Automobile rejection rate	Number Zip Codes	Non-Anglo population	Average income
Under 11.3 percent	8	8.92%	\$53,954
11.3 to 22.6 percent	21	19.22%	\$34,169
22.7 to 33.9 percent	10	40.02%	\$24,600
34 to 45.2 percent	6	58.05%	\$21,542
over 45.2 percent	7	69.80%	\$19,099

Summary of Insurance Availability Problems Bexar County

Automobile rejection rate	Number Zip Codes	Non-Anglo population	Average income
Under 11.3 percent	8	15.58%	\$49,924
11.3 to 22.6 percent	23	32.23%	\$35,061
22.7 to 33.9 percent	14	52.63%	\$25,625
34 to 45.2 percent	18	78.19%	\$20,321
over 45.2 percent	7	94.69%	\$13,541

Summary of Insurance Availability Problems Dallas County

Automobile rejection rate	Number Zip Codes	Non-Anglo population	Average income
Under 11.3 percent	8	11.64%	\$49,036
11.3 to 22.6 percent	21	24.42%	\$38,062
22.7 to 33.9 percent	10	29.79%	\$32,752
34 to 45.2 percent	6	68.52%	\$23,928
over 45.2 percent	7	96.06%	\$15,024

Summary of Insurance Availability Problems Tarrant County

Automobile rejection rate	Number Zip Codes	Non-Anglo population	Average income
Under 11.3 percent	8	8.88%	\$52,980
11.3 to 22.6 percent	32	15.93%	\$35,981
22.7 to 33.9 percent	12	32.34%	\$25,979
34 to 45.2 percent	4	65.82%	\$19,871
over 45.2 percent	2	78.90%	\$17,532

* Urban county groupings are based on the overall statewide rejection rate in 1996, which was 22.6%.

standard and preferred companies by "rating territory." Because a rating territory represents an area of relatively homogeneous geographic risk, we would not expect dramatic differences in the writings of insurers by smaller geographic areas within the rating territory. Yet, the evidence shows that ZIP Codes with poor and minority consumers are much less likely to obtain insurance through standard and preferred insurers. Put another way, standard and preferred insurers do not make their insurance equally available throughout the rating territory. The practice of denying a consumer insurance because of where they live is called *redlining*.

The Poor Pay More

Although insurers claim that the higher rates charged to consumers in county mutuals are based on risk, insurance department data shows that non-standard business at current rates is now more profitable than standard/preferred business in Texas. The investment guide *Retire with Money* recommends investing in Allstate stock because of the company's expanding sales of "extremely profitable policies to high risk drivers."

The consequences of redlining on consumers from poor and minority areas are profound. From the start, the requirement to purchase automobile insurance places a significantly higher financial burden on poor consumers than on middle- and upper-income consumers because the cost of automobile insurance represents a greater share of the poor family's income – an income that has much less available after purchase of basic food, shelter, transportation and medical care.

When consumers are denied coverage in the standard / preferred market, the costs of insurance skyrocket. Currently, minimum liability insurance through the TAIPA may cost nearly twice as much as the same policy purchased through a standard or preferred company. Premiums for county mutuals range from twice to four times the current benchmark rate set by the Commissioner of Insurance for standard and preferred companies.

In addition to significantly higher rates, county mutuals generally charge policy fees, ranging from \$60 to \$125 for an annual policy. The policy fee is fully earned, meaning that the insurer gets to keep the full policy fee even if the consumer or the insurer cancels the policy in the first month. There are no policy fees in the standard/preferred market.

Finally, county mutuals frequently direct consumers to take out a high interest loan (called a premium finance loan) in lieu of a monthly payment plan if the consumer wants to pay for an auto policy over time. The typical interest rate for a premium finance loan is over 30 percent APR.

The Price Is Not Related to Risk

Although insurers claim that the higher rates charged to consumers in county mutuals are based on risk, insurance department data shows that non-standard business at current rates is now more profitable than standard/preferred business in Texas. While rate regulated companies pay out about 73 cents in claims for every premium dollar, county mutuals pay out only 63 cents in claims. The investment guide *Retire with Money* recommends investing in Allstate stock because of the company's expanding sales of "extremely profitable policies to high risk drivers."

While minority consumers are disproportionately rejected by the standard market and placed in "high risk" insurers, 1994 data from the Texas Department of Public Safety showed that minorities are no more likely than whites to have been involved in traffic accidents.

Many consumers are denied coverage in the standard market for reasons unrelated to their driving record. Insurer underwriting practices are shrouded in secrecy, but state law allows the Office of Public Insurance Counsel to review and report on these guidelines as long as no individual companies are named.

According to a 1994 OPIC study of auto underwriting guidelines, insurers writing 56 percent of the auto market have occupation restrictions, and insurers writing 51 percent of the market have employment stability restrictions. Other automobile insurance guidelines include home ownership and length at residence requirements. One Texas automobile insurer's underwriting guideline discriminates against persons with disabilities, regardless of the disability or whether it affects driving skills: "Risks which show no apparent means of support or show disability as the occupation."

The most recent data from July, 1993 to June, 1994 show that over 75 percent of drivers insured through the TAIPA have *no* at-fault accidents or violations. At the same time, drivers insured through TAIPA are disproportionately from poor and minority neighborhoods. Yet, because of the high TAIPA rates, these good drivers without at-fault accidents or violations pay as much for insurance as high-risk drivers.

High Rates Drive Up the Number of Uninsured Motorists

The high costs of insurance through county mutuals and TAIPA force many consumers who are denied coverage in the standard/preferred market to go without insurance because they simply cannot afford it. According to data from the Houston and Austin municipal courts, police issue hundreds of thousands of drivers receive citations annually for "failure to maintain financial responsibility" – driving without insurance. If we extrapolate the 220,000 citations a year in Houston and the 40,000 citations a year in Austin statewide, over 1,000,000 drivers a year receive citations for driving without insurance.

The number of citations issued for no insurance is increasing faster than the rate of population growth. This may be an indication of an increase in the number of uninsured drivers.

The costs of unaffordable insurance for poor people are far greater than a ticket and fine for no insurance. Officer David Powe, a police officer from Richardson, Texas, testified before the House Insurance Committee in 1994 that fully one-third of the 5,000 prisoners in the Richardson jail facility were there because they could not pay the fines for driving without insurance. The combination of mandatory insurance and insurer redlining has criminalized poverty and created modern day debtor's prisons.

Redlining, combined with high rates for minimum liability coverage, creates an environment where illegal activities, such as counterfeit proof of insurance cards, can flourish because the cost of illegal activity – including the potential for fines and other punishment — is less than the cost of purchasing insurance. In addition, there are some areas in the state where, because strict enforcement of financial responsibility would put half the driving population in jail, the laws can simply not be enforced.

Redlining, combined with high rates for minimum liability coverage, creates an environment where illegal activities, such as counterfeit proof of insurance cards, can flourish because the cost of illegal activity – including the potential for fines and other punishment — is less than the cost of purchasing insurance.

Recommendations

- **Implement regulations to ensure that insurers offer drivers with no moving violations or at-fault accidents a policy in their standard or preferred company and give all consumers equal opportunities to purchase affordable insurance.**

No evidence exists that low income or minority drivers are involved in more accidents than affluent or white drivers. Yet, insurance companies use factors like a person's occupation or credit history to determine the cost of insurance. Good drivers should pay the lowest rates for liability insurance, regardless of their occupation, credit history or other factors not related to their likelihood of causing an accident. Good Driver regulations give people with clean accident and ticket histories the right to purchase insurance at the lowest price from the company they choose.

- **Cap the cost of a policy offered through the TAIPA at 145 percent of the standard market benchmark rate.**

Rapid TAIPA rate increases over the past three years caused a dramatic reduction in applications to the plan. Moreover, since the large rate increase effective July, 1, 1995, the number of vehicles insured through TAIPA plummeted. From June 30, 1995 to September 30, 1996 the number of vehicles insured through the TAIPA dropped by 480,000, or 60 percent. Even worse, the number of drivers applying to TAIPA dropped by over 80 percent. As TAIPA rates increased, many drivers were priced out of the market and simply went without insurance. Setting TAIPA rates below county mutual rates will allow more drivers to be able to afford to purchase insurance.

- **Enforce existing anti-redlining statutes and regulations by taking action against insurers who violate them.**

The Commissioner of Insurance has promulgated 55 rating territories. Each represents a grouping of similar geographic risks. By definition, insurers should make insurance equally available within rating territories. The study shows clearly that insurers do not make insurance equally available. For example, Harris County is all one rating territory. TDI should investigate unequal insurance availability and enforce Texas Insurance Code Art. 21.21-6, which prohibits discrimination on the basis of geographic location.

The Department of Insurance should also vigorously enforce existing regulations designed to end other unfair insurance practices. For example, 28 TAC Sec. 5.401(b) prohibits insurers from using an applicant's historical lack of prior insurance in determining a rate if the applicant has been continuously insured for the past 12 months. Further, 28 TAC Sec. 5.7016 (the not-at-fault rule) prohibits auto insurers from non-renewing an auto policy for weather-related claims regardless of the number of such claims, or for other comprehensive claims (theft, vandalism, etc.) which do not exceed one in any 12 month period.

In 1996 one insurer began to require consumers to show two or three years of continuous insurance before admitting them to the standard or preferred company--making it much more difficult for those who were once uninsured to remain in compliance.

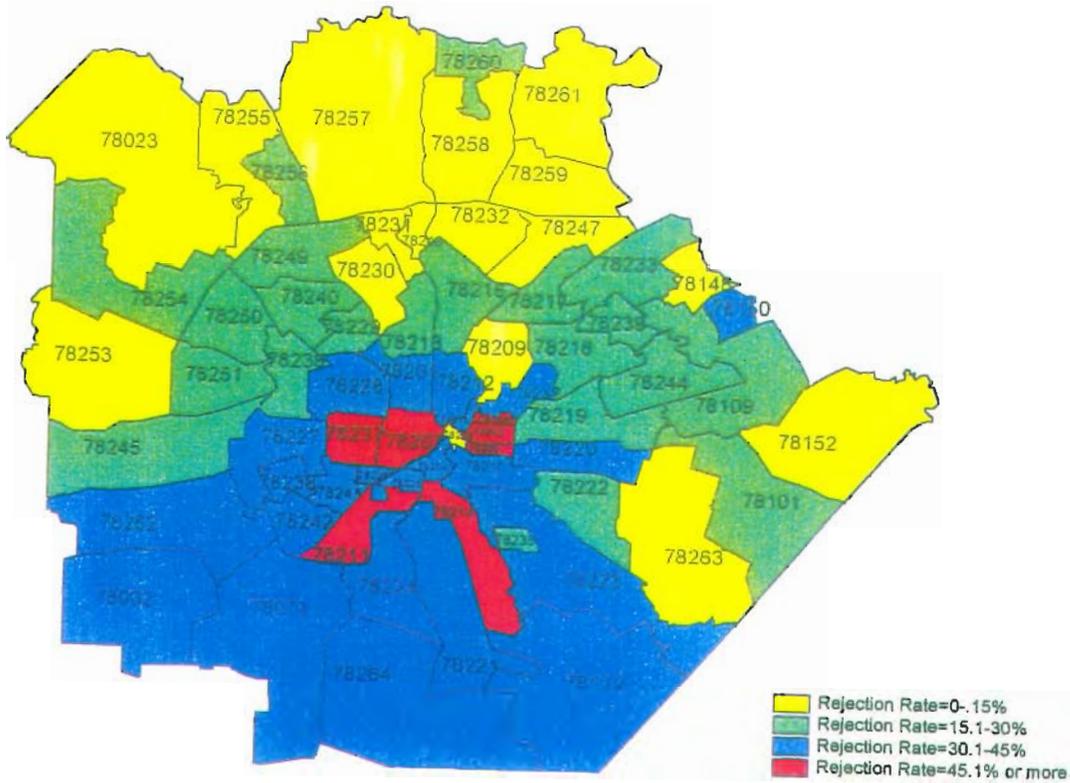
Another insurer adopted new underwriting guidelines which indicate that the company will not insure drivers who have any "incidents" within three years. Incidents include one theft claim in a three year period and more than two hail claims in a three year period.

- **Prohibit the use of unfair underwriting and rating factors, including credit history and prior insurance carriers.**

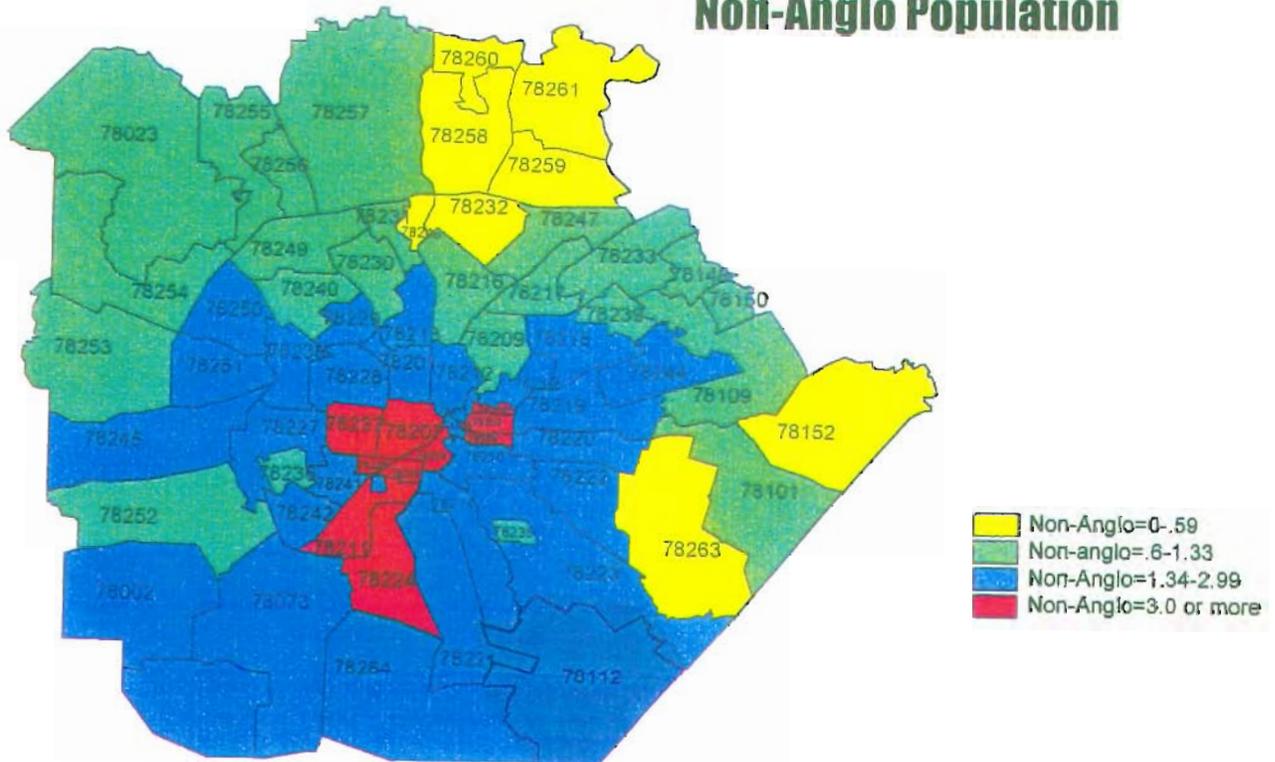
Insurers that use credit history to reject consumers for coverage at standard rates unfairly penalize lower income individuals who may be unable to pay a bill from time to time but are not more likely to get into an auto accident than any other consumer. Insurers who penalize those who were formally uninsured by charging them substantially higher rates discourage compliance with financial responsibility laws and promote the criminalization of poverty.

Bexar County

Insurance Availability

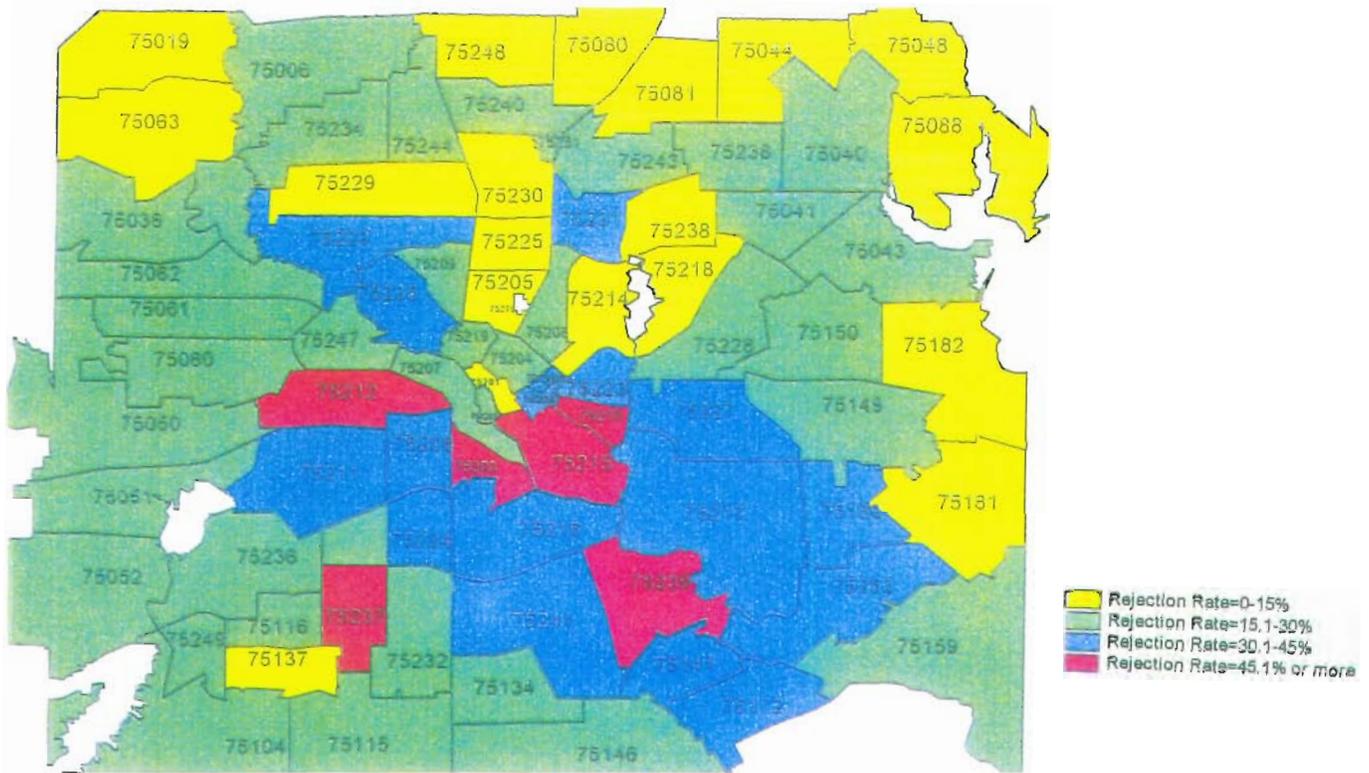


Non-Anglo Population

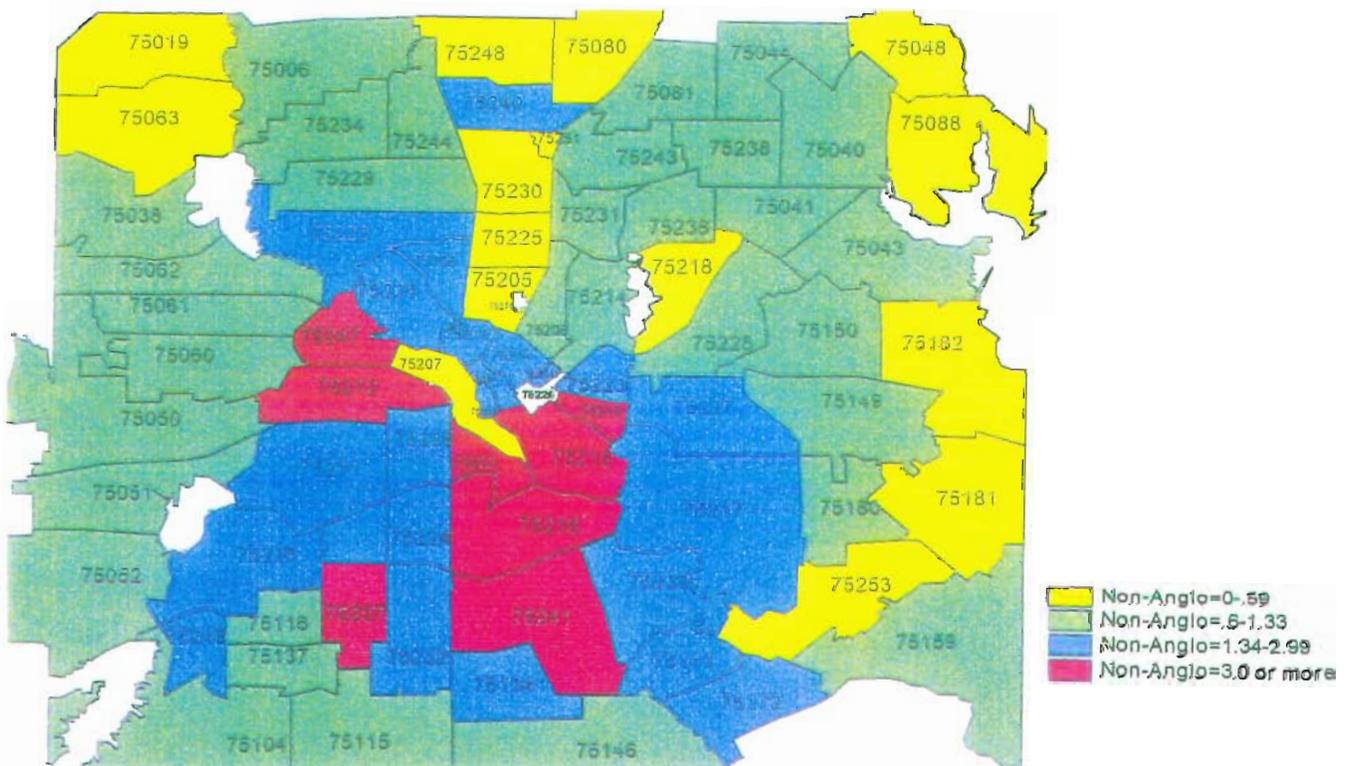


Dallas County

Insurance Availability

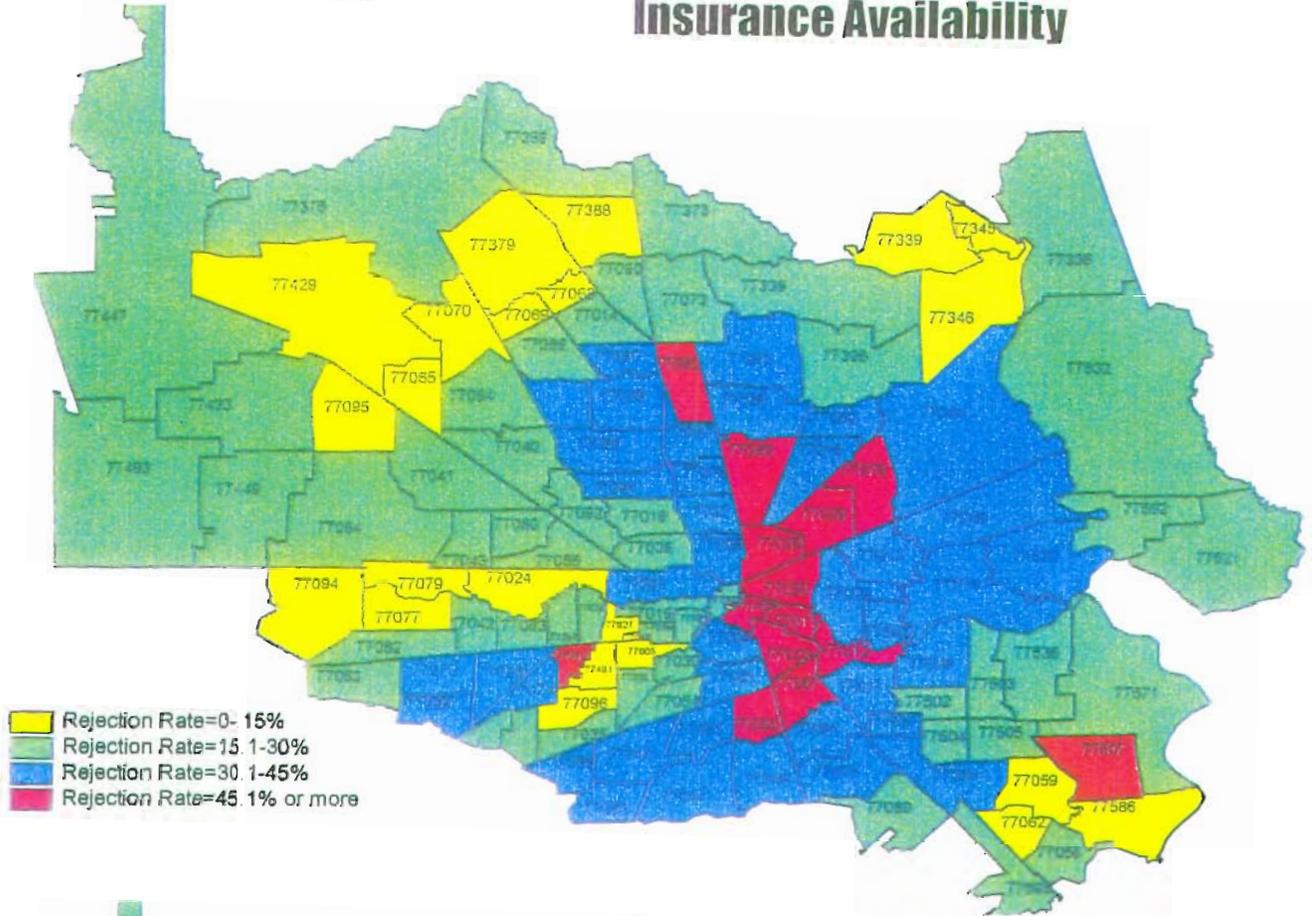


Non-Anglo Population

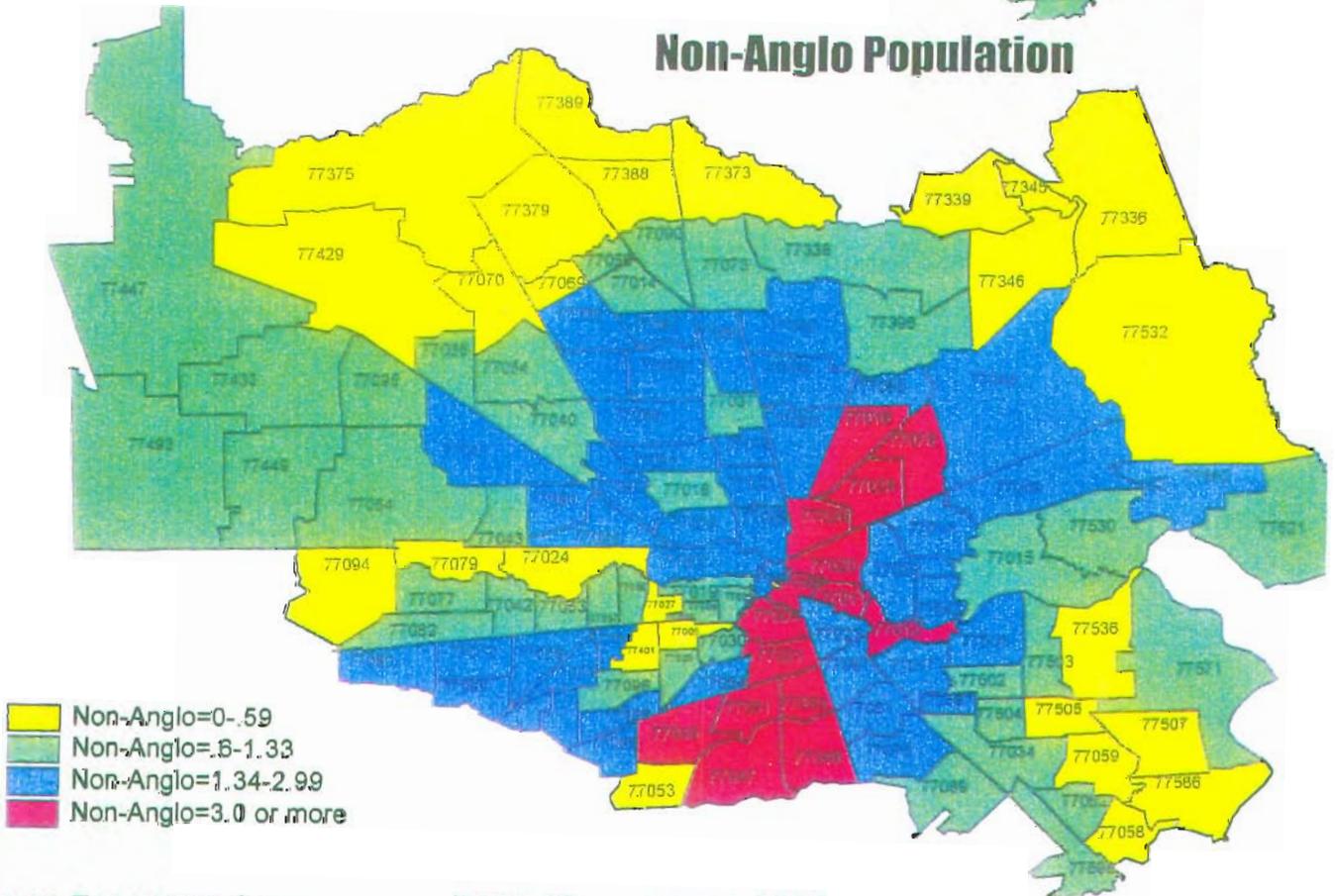


Harris County

Insurance Availability

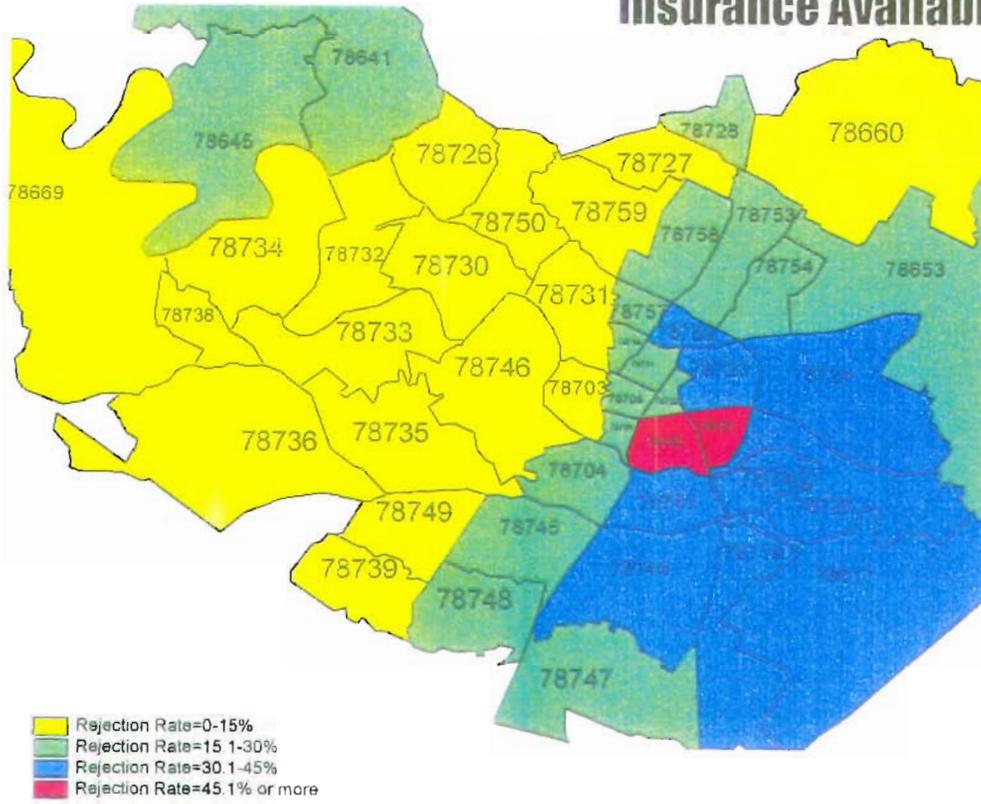


Non-Anglo Population



Travis County

Insurance Availability



Non-Anglo Population

