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Towards A Civil Rights Approach to Insurance Anti-Discrimination Law

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TOWARDS A CIVIL RIGHTS APPROACH TO INSURANCE ANTI-DISCRIMINATION LAW

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CONTENTS

INTRODUCTION 659
I. THE CURRENT SYSTEM FOR REGULATING INSURANCE DISCRIMINATION 663
A. *Insurance Discrimination in Rating and Underwriting* 663
B. *State Prohibitions on "Unfair Discrimination"* 666
C. *State Prohibitions on Actuarially Justified Discrimination* 669
II. DEFICIENCIES IN INSURANCE ANTI-DISCRIMINATION LAW 670
A. *Inefficient and Impractical: State Prohibitions on "Unfairly Discriminatory" and "Excessive" Rates* ... 671
B. *Gaps and Ineffectiveness in State Anti-Discrimination Law: Disparate Impact and Proxy Discrimination* ... 673
1. *The Disparate Impact Produced by Facially Neutral Insurance Practices* 674
2. *The Disparate Impact Generated by Some Insurer Practices Is Normatively Troubling and Requires Regulatory Attention* 677
a. Insurance Practices that Disparately Impact Protected Groups Impede Economic Mobility 677
b. Insurance Practices That Disparately Impact Protected Groups May Not Promote the Efficiency of Insurance Markets 678
c. Insurance Practices that Disparately Impact Protected Groups May Amount to Unintentional Proxy Discrimination 683

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III. TOWARDS A CIVIL RIGHTS APPROACH FOR INSURANCE ANTI-DISCRIMINATION LAW 686
A. De-Regulating: Eliminating Public Utility Style Rate Regulation 687
B. Re-Regulating: Establishing a Civil Rights Oriented Approach to Insurance Anti-discrimination Law 688
1. Data and Disclosure of Insurance Practices 689
2. A Private Cause of Action for Disparate Impact and Proxy Discrimination 694
CONCLUSION 697

Discrimination is fundamental to the business of auto and homeowners insurance. Yet state insurance law does remarkably little to police against the risk that this discrimination will unfairly harm minority or low-income communities. Not only do state insurance regulators completely ignore the prospect that facially-neutral insurance practices might disparately impact vulnerable populations, but they affirmatively suppress the production and dissemination of data that would advance a better understanding of this risk. Meanwhile, most states continue to cling to an antiquated, ineffective, and inefficient scheme of "public utility style" rate regulation that purports to prohibit "excessive, inadequate, or unfairly discriminatory" insurance rates. This scheme not only undermines the operation of efficient insurance markets, but also helps to shield the industry and state regulators from scrutiny regarding how insurance practices impact larger social goals—like facilitating socio-economic mobility. This Article argues that insurance law should scrap its regime of public utility style rate regulation in favor of a civil rights approach to anti-discrimination law. Such an approach should, at a minimum, promote the collection and public disclosure of company-specific, transaction-level data on insurance applications, purchases, losses, and policyholder membership in legally protected groups—much in the manner of the Home Mortgage Disclosure Act. Further paralleling modern anti-discrimination regimes in consumer finance, this civil rights approach should afford private parties a cause of action against insurers based on a modified disparate impact theory that reflects the important role of risk-based discrimination in insurance markets. This could be accomplished by recognizing that insurance discrimination based on factors that genuinely predict claim frequency or severity, even after controlling for prohibited characteristics, constitutes a "legitimate non-discriminatory" practice under the familiar burden-shifting scheme for disparate impact liability.

INTRODUCTION

Discrimination is fundamental to the business of auto and homeowners insurance. From deciding who they will cover, to how much they will charge for coverage, to what forms of coverage they will provide, property and casualty insurers devote immense attention to classifying individuals into various different groups and sub-groups.[1] These classifications have immeasurable practical consequences, impacting people's wealth, where they can live, what jobs they can take, and their financial security. Insurance discrimination, in short, is both ubiquitous and enormously important in shaping peoples' lives.

Despite the significance of insurance discrimination in modern America, the law does remarkably little to police against the risk that this discrimination will unfairly harm minority or low-income communities. For instance, state laws prohibiting "unfair discrimination" in property and casualty insurance markets simply require insurers to have an actuarial justification for their discriminatory practices.[2] Although some states also prohibit discrimination on the basis of factors like race, ethnicity, national origin, or income, courts and regulators construe these laws extremely narrowly.[3] As a result, these more specific anti-discrimination laws merely prohibit insurers from formally incorporating prohibited characteristics into their models or intentionally constructing proxies for these characteristics.[4]

By contrast, state insurance law and regulation entirely ignores the prospect that facially-neutral practices might disparately impact minority or low-income populations.[5] This, of course, is a risk whenever a correlation exists between a policyholder trait used by insurers (such as zip code) and a suspect policyholder characteristic (such as race or income). Insurers and some commentators vehemently defend this approach, suggesting that disparate impact analysis of any kind is fundamentally incompatible with risk-based insurance pricing.[6] And undermining risk-based pricing, the argument goes, risks jeopardizing

1. *See generally* KENNETH ABRAHAM & DANIEL SCHWARCZ, INSURANCE LAW AND REGULATION (6th ed. 2015).

2. *See* Daniel Schwarcz, *Ending Public Utility Style Rate Regulation in Insurance*, 35 YALE J. REG. 941, 988 (2018); Anya E.R. Prince, *Insurance Risk Classification in an Era of Genomics: Is a Rational Discrimination Policy Rational?*, 96 NEB. L. REV. 624, 630 (2017).

3. *See* Ronen Avraham, Kyle Logue & Daniel Schwarcz, *Understanding Insurance Antidiscrimination Laws*, 87 S. CAL. L. REV. 195, 215–16 (2014).

4. *Id.* at 198–99.

5. *See, e.g.*, Ojo v. Farmers Grp., Inc., 356 S.W.3d 421, 422 (Tex. 2011) (holding that Texas law does not consider whether facially neutral discrimination disparately impacts members of protected groups).

6. *See* Michael J. Miller, *Disparate Impact and Unfairly Discriminatory Insurance Rates*, CASUALTY ACTUARIAL SOC'Y E-FORUM, Winter 2009, at 276, 276; *see also Our Positions: Disparate*

the competitiveness and efficiencies of personal lines insurance markets in the United States.[7]

But state insurance laws fundamentally err by ignoring when and how personal lines insurance practices impact minority and low-income communities. Given the necessity of auto and homeowners insurance for social and economic advancement, insurance discrimination can reinforce preexisting inequalities and undermine economic mobility.[8] In fact, there is substantial evidence that numerous types of insurance discrimination—such as insurers' pricing of coverage based on credit information, marital status, geography, and occupation—do exactly this.[9]

These public policy concerns deserve legal and regulatory attention even if, as is surely the case, insurance discrimination also frequently serves the important purpose of promoting risk-based pricing. Some types of insurance discrimination, for instance, may disparately impact vulnerable communities even though their primary value to insurers is to extract profit from relatively price-inelastic consumers, rather than to price risk.[10] In these cases—which appear to be relatively common in some auto and homeowners insurance markets—insurers' own arguments for resisting disparate impact are simply inapplicable. But even when insurance discrimination that harms vulnerable populations is indeed risk-based, it hardly follows that insurers do not have less discriminatory alternatives available to limit the harmful impact of their practices while preserving the benefits.

States' refusal to interrogate the impact of facially-neutral, risk-based insurance discrimination is problematic for another reason as well: It fails to police against the risk that the predictive power of a facially-neutral trait derives from its correlation with a suspect trait, like race or income.[11] Unlike ordinary disparate impact, such "proxy discrimination" exists only when the usefulness to the insurer of a facially-neutral practice (like zip code) is directly attributable to its

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Impact Rule NAMIC, https://www.namic.org/Issues/disparate-impact-rule (last visited Oct. 29, 2019) [hereinafter *Our Positions*].

7. *See* Miller, *supra* note 6; *see also Our Positions*, *supra* note 6.

8. *See* Julia Angwin et al., *Car Insurance Companies Charge Higher Rates in Some Minority Neighborhoods*, CONSUMER REP. (Apr. 21, 2017), https://www.consumerreports.org/consumer-protection/car-insurance-companies-charge-higher-rates-in-some-minority-neighborhoods/ [hereinafter ProPublica Study].

9. *See* discussion *infra* Part II.

10. *See* discussion *infra* Part II.

11. *See* Anya Prince & Daniel Schwarcz, *Proxy Discrimination in the Age of Artificial Intelligence and Big Data*, IOWA L. REV. (forthcoming 2020); Darcy Steeg Morris, Joshua C. Teitelbaum & Daniel Schwarcz., *Do Credit-Based Insurance Scores Proxy for Income in Predicting Auto Claim Risk?*, 14 J. EMPIRICAL LEGAL STUD. 397, 398–99 (2017).

correlation with a suspect classifier (like race). Thus, while insurers' use of credit information to price coverage disparately impacts African Americans and low-income applicants, whether this practice arises to "proxy discrimination" depends on why credit information is predictive of future claims.[12] If poor credit history is predictive of insurance costs because it identifies low-income policyholders who are more likely to file claims only moderately above their deductible, then insurer use of this information would constitute proxy discrimination for income; the predictive power of credit information—and thus its usefulness to insurers—would derive from its correlation with a legally suspect characteristic (i.e., income).[13]

Proxy discrimination in insurance is substantially more troubling than ordinary disparate impact because it strikes at the heart of the logic behind state laws that limit actuarially justified insurance discrimination. Such laws are premised on the notion that insurers should not penalize policyholders for being members of certain groups *even if* group membership is predictive of risk. In some cases, as with race or ethnicity, allowing such discrimination would reinforce and exacerbate preexisting inequalities. In other cases, like income, this discrimination could undermine broader goals of economic mobility. Proxy discrimination produces these results by indirectly targeting members of protected groups for higher premiums. As such, it partially replicates (depending on the effectiveness of the proxy) the outcomes that would result if insurers directly discriminated against members of protected groups.[14]

States' laws governing insurance discrimination thus do little to protect discrete minority groups. But this is only half the problem. They also produce massively inefficient regulation that serves no legitimate public policy goal. Countless state regulators spend innumerable hours attempting to understand increasingly complex insurer pricing algorithms in an effort to determine whether they are actuarially justi-

12. *See* FTC, CREDIT-BASED INSURANCE SCORES: IMPACTS ON CONSUMERS OF AUTOMOBILE INSURANCE (July 2007), https://www.ftc.gov/sites/default/files/documents/reports/credit-based-insurance-scores-impacts-consumers-automobile-insurance-report-congress-federal-trade/p044-804facta_report_credit-based_insurance_scores.pdf [hereinafter FTC Study].

13. Most states do not formally include income among the characteristics that insurers are prohibited from considering in their rating and underwriting models. Nonetheless, as the Federal Trade Commission has recognized since 2007, insurer discrimination based on income "appears to be generally regarded as an illegitimate variable for those purposes." FTC Study, *supra* note 12. This understanding has only become more clear since 2007. *See* Steeg Morris, Teitelbaum & Schwarcz, *supra* note 11.

14. *See* Prince & Schwarcz, *supra* note 11.

fied.[15] Such rate regulation is designed not only to police against "unfair discrimination," but also to prevent insurers from charging "excessive" rates. These were real risks when insurance rate regulation was established in the early-to-mid twentieth century, as the law explicitly permitted insurers to collectively set their rates, thus undermining competitive market forces.[16] But the law no longer tolerates such collusion in property and casualty insurance markets. To the contrary, state laws and relatively low barriers to entry ensure that most property and casualty insurance markets are extremely competitive with respect to rates.[17] As a result, there is simply no need for state regulators to police insurance rates to ensure that they are neither excessive nor premised on unsound actuarial assumptions.

Addressing both the inefficiencies and the deficiencies in insurance anti-discrimination law requires moving from the outdated public utility model of rate regulation that currently predominates in the states to a civil rights approach to insurance anti-discrimination law. How this might be accomplished could vary by state. But one promising option would be for states to abandon their prohibitions on "excessive" or "unfairly discriminatory" insurance rates, while simultaneously mandating that insurers collect and publicly disclose company-specific, transaction-level data that includes premiums, claims payouts, coverage features, policyholders' zip codes, income, and membership in legally protected groups[18]—much in the manner of the Home Mortgage Disclosure Act.[19] This reform would allow interested parties to analyze how individual insurers' practices impact minority and low-income communities. Further paralleling modern anti-discrimination regimes, private parties might be afforded a private cause of action based on a modified disparate impact theory that reflects the important role of risk-based discrimination in insurance markets.

This redesign of insurance anti-discrimination law could increase the efficiency of state insurance regulation while better protecting members of legally protected groups and enhancing economic mobil-

15. *See* Schwarcz, *supra* note 2, at 951. As it has become increasingly obvious that state insurance regulators do not have the resources or expertise to conduct these audits, they have yielded more and more responsibility to staff at the National Association of Insurance Commissioners (NAIC)—a private entity that is not subject to state laws governing transparency and accountability. *See* NAIC, BIG DATA WORKING GROUP CHARGES, BIPARTISAN POL'Y CTR., https://www.naic.org/cmte_ex_bdwg.htm; *see also Improving U.S. Insurance Regulation*, BIPARTISAN POL'Y CTR. (Apr. 2017), https://bipartisanpolicy.org/wpcontent/uploads/2019/03/Improving-U.S.-Insurance-Regulation.pdf.

16. *See* Schwarcz, *supra* note 2.

17. *Id.* at 945.

18. *See* discussion *infra* Part III.

19. *See* 12 U.S.C. § 2803 (2012); 12 C.F.R. pt. 203 (2013).

ity. It would allow states to finally jettison their increasingly futile efforts to audit the accuracy of insurers' rating models. Not only would this save substantial regulatory resources, but it would decrease unnecessary compliance costs for insurers and eliminate some of the potential distortions associated with traditional insurance rate regulation, such as increasing the stickiness of insurers' rating schemes and deterring valuable innovation. At the same time, embracing a civil rights approach to insurance anti-discrimination law would directly confront the inequalities that are reinforced by current market practices. Perhaps even more importantly, it would lay the foundations for adapting to a new age of insurance discrimination, which will be driven more by artificial intelligence (AI) and Big Data than by traditional statistical models and the exercise of human discretion.[20]

I. The Current System for Regulating Insurance Discrimination

Insurance anti-discrimination rules—like most other forms of insurance law and regulation—are principally set by the states. This Part provides an overview of these regimes as they apply to property and casualty insurers. Part I.A sets the stage by explaining how and why insurers discriminate in the first place. Part I.B then describes state laws prohibiting "unfair discrimination" in property and casualty insurance markets and the enforcement of these rules through regulatory rate review. Finally, Part I.C describes state laws that prohibit insurance discrimination irrespective of whether it can be actuarially justified.

A. Insurance Discrimination in Rating and Underwriting

Insurance is the business of transferring risk from policyholders to insurers. For this business to remain viable, insurers generally must discriminate among policyholders. Failing to do so can trigger the twin insurance problems of adverse selection and moral hazard, causing premiums to increase and individuals to gradually opt out of the insurance marketplace.[21] Even in the absence of substantial moral hazard or adverse selection, insurers can increase their profits by doing a better job than their competitors of accurately assessing and pricing poli-

20. As used here, "artificial intelligence" and big data encompass "a broad array of computational techniques for predicting future outcomes based on analysis of vast amounts of past data" gathered from disparate sources. Prince & Schwarcz, *supra* note 11. For extended discussion of these topics in the insurance setting, see *id.*

21. *See generally* Abraham & Schwarcz, *supra* note 1.

cyholder risk.[22] The resulting risk signaling can encourage policyholders to invest in more effective precautions or to efficiently decrease their activity levels.[23]

Insurers discriminate among different types of policyholders through both their underwriting and rating processes. Underwriting traditionally referred to the decision whether to accept or reject an insurance applicant. Increasingly, however, underwriting also encompasses insurers' assignment of policyholders to different (i) "rating tiers" within a single insurance entity or (ii) "standard" and "nonstandard" insurance companies within a commonly-owned "insurance group."[24] Once applicants are assigned to their appropriate groupings, a second level of discrimination typically occurs through the assignment of rates to policyholders within each rating tier or company to determine their premiums.[25] The insurer typically assigns a base rate for each group of policyholders, which is varied for each individual policyholder based on various rating factors that are contained in the insurer's rating manual or automated rating engines.[26]

In practice, the line between rating and underwriting has become increasingly blurred in recent decades. Insurers often use underwriting to develop dozens or even hundreds of different rating tiers, with the effect that underwriting ends up more substantially affecting the rates that policyholders are charged than whether or not they are offered coverage.[27] And like the rating process, underwriting is now frequently carried out through complex algorithms and AI, rather than by a human underwriter who must exercise individualized judgment.[28] Not only has underwriting become increasingly similar to rating, but rating is at least theoretically capable of replicating the traditional function of underwriting: rating algorithms that generate exorbitant

22. *Id.*

23. Omri Ben-Shahar & Kyle D. Logue, *Outsourcing Regulation: How Insurance Reduces Moral Hazard*, 111 MICH. L. REV. 197, 209–10 (2012); Peter Molk, *Playing With Fire? Testing Moral Hazard in Homeowners Insurance Valued Policies*, 2018 UTAH L. REV. 347, 392 (2018) (examining the link between insurer pricing and policyholder behavior).

24. GEOFF WERNER & CLAUDINE MODLIN, CASUALTY ACTUARIAL SOC'Y BASIC RATEMAKING 16 (2010).

25. *See id.*

26. *Id.* at 13.

27. *See* NAIC, *Price Optimization White Paper* (2015), http://www.naic.org/documents/committees_c_catf_related_price_optimization_white_p-aper.pdf [http://perma.cc/E5FN-63JX]; *see also* Robert J. Walling III, *Underwriting Power Tools for Small Business Insurance*, PINNACLE MONOGRAPH (2008), https://www.pinnacleactuaries.com/Portals/0/SiteContent/Publications/P-innacle_Monograph_Underwriting_Power_Tools_Walling.pdf.

28. *See* Rick Swedloff, *Risk Classification's Big Data (R)evolution*, 21 CONN. INS. L.J. 339, 354 (2014). Subjective underwriting by individuals still persist in some commercial coverage lines where each prospective policyholder is perceived to present unique risks.

prices for a subset of policyholders deemed to be high-risk can, as a practical matter, amount to a refusal to offer coverage.

Both insurance rating and underwriting have increased dramatically in sophistication over the last decade. Historically, insurers used relatively simple univariate statistical models to develop their rating plans.[29] The relationship between any individual rating factor and rates was relatively intuitive in these models. Underwriting guidelines were generally even more straight-forward to understand, consisting less of statistical models and more of relatively straight-forward rules and standards that were applied by human underwriters.[30] In recent years, however, insurers have deployed increasingly complex statistical models in their rating and underwriting.[31] For instance, most insurers have now replaced univariate statistical models with substantially more complex generalized linear models to set their rates, including not just logistic regression, but also Poisson regression, gamma regression, and multinomial regression.[32] And many insurers go much further, deploying models using random forest, decision trees, or neural networks.[33] Often, these models incorporate the output of sub-models, such as credit scoring models.[34]

These complexities are greatly multiplied when insurers' statistical models are developed through machine learning techniques, as is becoming more common. Such machine learning relies on an AI to develop algorithms based on training datasets for which the outcome of interest is known.[35] Training datasets generally include external data that insurers acquire from third-parties, rather than directly from the insurance applicant.[36] Unlike traditional statistical models, machine-learning models are not driven by a human's intuition or hypothesis regarding cause and effect.[37] Instead, they use raw computing power to identify attributes that predict their programmed outcome of inter-

29. NAIC, *Regulatory Review of Predictive Models* (2019), https://www.naic.org/documents/-comte_c_catf_predictive_model_white_paper_190510_clean.docx [hereinafter *Predictive Models Whitepaper*].

30. *See* WERNER & MODLIN, *supra* note 24.

31. *Id.* at 176.

32. *Id.* at 177.

33. *Id.* at 185–86.

34. *Id.*

35. Solon Barocas & Andrew D. Selbst, *Big Data's Disparate Impact*, 104 CALIF. L. REV. 671, 673–79 (2016).

36. N.Y. DEPT. FIN. SERVS., INSURANCE CIRCULAR LETTER NO. 1: USE OF EXTERNAL CONSUMER DATA AND INFORMATION SOURCES IN UNDERWRITING FOR LIFE INSURANCE (2019), https://dfs.n-y.gov/industry_guidance/circular_letters/cl2019_01.

37. JUDEA PEARL & DANA MACKENZIE, THE BOOK OF WHY: THE NEW SCIENCE OF CAUSE AND EFFECT 349 (2018).

est. For this reason, the ultimate statistical models that AIs derive are often nearly impossible to explain intuitively.[38]

B. State Prohibitions on "Unfair Discrimination"

Although discrimination in insurance rating and underwriting serves important economic goals, virtually every state in the country prohibits property and casualty insurers from engaging in "unfair discrimination."[39] This prohibition against "unfair discrimination" is also an important professional norm for underwriters, actuaries, and others involved in the pricing, design, and sale of insurance products.[40] It is widely understood within both the regulatory community and the industry to require that discrimination by insurers must be grounded in sound actuarial data and principles.[41] In general, this requires that insurers who discriminate among different policyholders must have a reasonable and empirically grounded basis for believing that such discrimination reflects differences in risk levels.[42]

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38. *See, e.g.*, MATT TUREK, EXPLAINABLE ARTIFICIAL INTELLIGENCE (XAI), DARPA, www.darpa.mil/program/explainable-artificial-intelligence (last visited Oct. 29, 2019).

39. *See, e.g.*, 44 C.J.S. INSURANCE § 104, Westlaw (database updated Sept. 2019) ("Insurance rates may not be unreasonable, excessive, inadequate, or unfairly discriminatory."); ARIZ. REV. STAT. § 20-448 (2015) (Arizona); CONN. GEN. STAT. ANN. § 38a-686 (West 2017) (Connecticut); GA. CODE § 33-6-4 (b) (2014) (Georgia); N.J. STAT. ANN. §§ 17:29A-4; 17:22-6.14a1 (2013) (New Jersey); N.Y. INS. LAW § 2303 (McKinney 2000) (New York); N.C. GEN. STAT. ANN. § 58-3-120 (West 2001) (North Carolina); S.C. CODE 1976 ANN. § 38-55-50 (effective Jan. 1, 2005) (South Carolina); TENN. CODE. ANN. § 56-8-104 (7)(C) (2008) (Tennessee); WASH. REV. CODE. ANN. § 48.18.480 (1984) (Washington). The scope of these laws varies by state. Some states only prohibit "unfair discrimination" in consumer-oriented markets. Finally, at least one state (Illinois) does not prohibit unfair discrimination outside of the health insurance context, though whether this is true depends on the interpretation of a confusing statutory provision that on its face is not limited to health insurance, but which is contained within a part of the Illinois insurance code that is dedicated to health insurance. *See* 215 ILL. COMP. STAT. ANN. 5/364 (West 2015) (Illinois) ("Discrimination between individuals of the same class of risk . . . in the amount of premiums or rates charged for any insurance covered by this article . . . is prohibited."); 50 Ill. Admin. Code § 906.10 (repealed 2011) ("The effect of the Illinois Law is to require that all fire, casualty, inland marine or surety insureds of the same class shall be treated alike.").

40. *See* ASS'N OF HOME OFF. UNDERWRITERS & CANADIAN INST. OF UNDERWRITERS, GUIDING PRINCIPLES FOR THE UNDERWRITER (2013), https://alu-web.com/about-us/guiding-principles/ [hereinafter UNDERWRITING GUIDING PRINCIPLES] (describing as one of the guiding principles for underwriters the need to "[f]ollow established risk classification principles that differentiate fairly on the basis of sound actuarial principles and/or reasonable anticipated mortality or morbidity experience."); CASUALTY ACTUARIAL SOC'Y, STATEMENT OF PRINCIPLES REGARDING PROPERTY AND CASUALTY RATEMAKING (1988), https://www.casact.org/professionalism/standards/princip/sppcrate.pdf ("A rate is reasonable and not excessive, inadequate or unfairly discriminatory if it is an actuarially sound estimate of the expected value of all future costs associated with an individual risk transfer.").

41. *See* Prince, *supra* note 2.

42. *See* UNDERWRITING GUIDING PRINCIPLES, *supra* note 40.

State prohibitions on "unfair discrimination" are almost universally paired with prohibitions against "excessive" or "inadequate" insurance rates. Laws prohibiting "inadequate" rates were originally designed to preserve insurer solvency, but are now largely a dead letter in most insurance lines because they have been supplanted by more effective solvency tools, such as risk-based capital and reserve requirements.[43] By contrast, many states—depending on the particular insurance commissioner in power during the examined timeframe—devote extensive attention to preventing "excessive" or "unfairly discriminatory" rates.[44] In practice, these two restrictions on insurance rates are tightly related: Rates are typically deemed excessive when they allow insurers to make a supra-competitive profit, and one of the core ways that can happen is if consumers are charged rates that are greater than what is actuarially justified.[45]

State prohibitions on "unfairly discriminatory" or "excessive" rates generally date back to the early twentieth century, when they were adopted based on the widespread perception that property and casualty insurance markets shared key characteristics with natural monopolies.[46] Market conditions in both settings were believed to stymie competition among rival firms.[47] In the natural monopoly setting, this result was easy to see, as single firms dominated individual markets. In the insurance setting, by contrast, inadequate competition resulted not so much from a lack of competing firms, as from the fact that these ostensibly competing insurers collectively set their rates and designed their coverage.[48] Such collusion was largely understood to be uniquely necessary in insurance markets so that insurers could accurately predict losses and avoid "ruinous competition."[49]

Some individual states, and eventually the federal government, were only willing to tolerate insurers' continued price and product-design collusion if they were paired with rate regulation designed to prevent excessive or unfairly discriminatory rates. States pioneered the design of this rate regulation in the early twentieth century, patterning it on the rate regulation that had recently emerged in the natural monopoly setting.[50] In both settings, rate regulation was designed to ensure that consumers were charged "fair" prices that were based

43. *See* ABRAHAM & SCHWARCZ, *supra* note 1, at 117.
44. *See* Schwarcz, *supra* note 2, at 943, 945.
45. *Id.* at 973–74.
46. *Id.* at 952.
47. *Id.* at 945.
48. *Id.* at 946.
49. *Id.*
50. Schwarcz, *supra* note 2, at 948.

on the actual cost of the service they purchased and which did not allow firms to extract an unreasonably large profit.[51] This public utility oriented version of rate regulation was encoded into virtually every state's law when Congress passed the McCarran Ferguson Act in the mid-twentieth century.[52] While declaring the primacy of the states in regulating the business of insurance, the Act conditioned a key component of this primacy—the limited insurance exemption from federal antitrust laws—on the states "regulating the business of insurance."[53] The federal government made clear that the regulation contemplated by this provision consisted of public utility oriented rate regulation.[54] States responded by promptly and uniformly embracing such rate regulation, prohibiting "inadequate, excessive, or unfairly discriminatory" insurance rates.[55]

Although some individual states have moved away from public utility style rate regulation in recent decades, most states continue to devote extensive resources to policing against "unfairly discriminatory" or "excessive" rates. Virtually all states require insurers to file an extensive array of documents with the state insurance department whenever they seek to alter their rates.[56] Some states require these filings to be approved before insurers can change their rates, while others simply retain the authority to disapprove filed rates within a specified period of time.[57] The intensity of this regulatory review var-

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51. *See id.*

52. McCarran Ferguson Act, 15 U.S.C. § 1012 (2018).

53. *Id.* § 1012.

54. Spencer Kimball & Ronald Boyce, *The Adequacy of State Insurance Rate Regulation: The McCarran-Ferguson Act in Historical Perspective*, 56 MICH. L. REV. 545, 556 (1958) ("As stated perhaps most clearly by Attorney General Biddle: 'The view we hold toward insurance is not unlike our policy toward railroad rates, that the fixing of rates by private groups . . . without active and definite state approval, is a clear contravention, not only of the [Sherman] act, but of the whole theory that underlies the act, the theory that competition should be free unless it is specifically regulated by the appropriate body.'").

55. *See* Schwarcz, *supra* note 2.

56. For example:

> *New Hampshire requires under New Hampshire Law (55:8 Property and Casualty Insurance; Rate Filings)* Every insurer shall file with the commissioner every manual, predictive models or telematics models or other models that pertain to the formulation of rates and/or premiums, minimum premium, class rate, rating schedule or rating plan and every other rating rule, and every modification of any of the foregoing which it proposes to use. Personal lines filings shall include underwriting rules used by insurers or a group of affiliated insurers to the extent necessary to determine the applicable rate and/or policy premium for an individual insured or applicant . . . .

Minutes of Auto Insurance Working Group (June 30, 2017), https://www.naic.org/meetings-1708/cmte_ex_bdwg_2017_summer_nm_materials.pdf?1530403237253.

57. For a detailed breakdown of which states use which rate review procedures for each line of coverage, see R.J. Lehmann, *2018 Insurance Regulation Report Card*, R STREET (2018), https://www.rstreet.org/wp-content/uploads/2018/12/RSTREET163.pdf.

ies substantially across states, time periods, and lines of coverage. In many states, however, this regulatory review is quite extensive, requiring regulators to scrutinize thousands of documents to assess factors such as historical claims data, anticipated trends in future claims, non-claims expenses, investment returns, and the rates of profit necessary to retain and attract capital to the industry.[58]

C. State Prohibitions on Actuarially Justified Discrimination

In addition to prohibiting "unfair discrimination," many states also prohibit certain forms of insurance discrimination irrespective of whether or not they can be actuarially justified. However, these laws vary significantly by state and line of coverage. Most—though not all—states prohibit insurers from discriminating on the basis of race, ethnicity, or national origin.[59] And a substantial number of states also ban the use of sexual orientation and gender in certain lines of coverage, like auto and homeowners insurance.[60] But these restrictions hardly exhaust the examples of prohibited forms of potentially actuarially-justified discrimination in insurance. For instance, some states ban the use of age and gender in coverage lines like auto and homeowners insurance and others ban the use of policyholder income in some coverage lines.[61] Additionally, some states ban insurer use of specific potential proxies for prohibited characteristics. For instance, two states ban the use of location or zip code (which has historically proxied for race) in property and casualty insurance, and several others prohibit insurer discrimination in auto on the basis of credit information (which some claim proxies for race or income).[62]

States generally enforce these restrictions on insurance discrimination against specific subgroups in a highly limited fashion, such that they extend only to explicit or intentional discrimination. Of course, these laws clearly prohibit insurers from overtly incorporating prohibited characteristics into their rating manuals or underwriting guidelines. Additionally, they also are generally understood to prohibit insurers from intentionally discriminating against protected groups by relying on a facially neutral characteristic that is intended to proxy for

58. *See* ABRAHAM & SCHWARCZ, *supra* note 1.

59. Avraham, Logue & Schwarcz, *supra* note 3, at 234–36, 240 (reviewing prohibitions against insurers' consideration of race in insurance).

60. *See id.* at 251–52.

61. *Id.* at 244–51, 259–65. With respect to income, there are few, if any, state laws that explicitly prohibit the use of this factor. However, state regulators often treat discrimination on the basis of income as suspect under the more general prohibition against unfair discrimination. *See* FTC Study, *supra* note 12.

62. *See* Avraham, Logue & Schwarcz, *supra* note 3, at 201.

a prohibited characteristic.[63] In fact, the insurance industry had a long history of doing just that: During the mid-twentieth century, many insurers refused to cover anyone living in "red-lined" geographic areas that were predominantly African American.[64] Although insurers publicly claimed that such redlining had nothing to do with race, the evidence suggests otherwise: Redlining arose directly out of insurers' explicit prejudices against African Americans, whom they believed were inherently more likely to incur claims.[65] By contrast, to date, states have rejected the notion that insurers might violate state laws prohibiting discrimination against discrete subgroups by unintentionally relying on a facially-neutral characteristic that correlates with an explicitly prohibited characteristic.[66]

II. Deficiencies in Insurance Anti-discrimination Law

The state-based regime governing insurance discrimination in property and casualty insurance markets is designed to address a problem that no longer exists. At the same time, it inappropriately ignores many of the ways in which insurance discrimination can harm minority and low-income groups. This Part explains these conclusions. Part II.A first elaborates on why state laws prohibiting "unfairly discriminatory" or "excessive" rates simply do not make sense in modern insurance markets. Part II.B then explains why state insurance law ought not to ignore the impact of insurance discrimination on low-income and minority populations, focusing both on disparate impact

63. *See generally* NAIC, Market Regulation Handbook (2009) (describing when insurer use of proxies for prohibited characteristics run afoul of the law).

64. *See* Gregory D. Squires, *Racial Profiling, Insurance Style: Insurance Redlining and the Uneven Development of Metropolitan Areas*, 25 J. Urb. Aff. 391, 396–97 (2003).

65. *See, e.g.*, *id.* For instance, insurance textbooks from the 1950s warned underwriters of the importance of determining applicants' race and ethnicity in assessing their riskiness. Brian Glenn, *Post-Modernism: The Basis of Insurance*, 6 Risk Mgm't & Ins. Rev. 131, 134 (2003). As one commentator explained in the late 1970s, "[a]lthough the core concern of the underwriter is human characteristics of the risk, cheap screening indicators are adopted as surrogates for solid information about the attitudes and values of the insured . . . . Even generalized underwriting texts include occupational, ethnic, racial, geographic, and cultural characterizations certain to give offense if publicly stated." Robert Works, *Whatever's FAIR – Adequacy, Equity, and the Underwriting Prerogative in Property Insurance Markets*, 56 Neb. L. Rev. 445, 471 (1977); *see also* Regina Austin, *The Insurance Classification Controversy*, 131 U. Pa. L. Rev. 517, 537–38 (1983) (describing insurers' reliance on occupational and cultural stereotypes without any empirical support for these stereotypes). Studies showed that such redlining did not, in fact, accurately reflect the riskiness of the affected areas. *See* Robert W. Klein, *Availability and Affordability Problems in Urban Homeowners Insurance Markets*, *in* Insurance Redlining: Disinvestment, Reinvestment, and the Evolving Role of Financial Institutions (Greg D. Squires ed., 1997).

66. *See* Miller, *supra* note 6, at 284; *see also Our Positions*, *supra* note 6.

generally and on the more specific phenomenon of unintentional proxy discrimination.

A. Inefficient and Impractical: State Prohibitions on "Unfairly Discriminatory" and "Excessive" Rates

The lynchpin of state insurance law's anti-discrimination regime—its prohibition on "unfair discrimination"—is both obsolete and becoming increasingly difficult to meaningfully enforce. Aside from public utilities, insurance is the only domain in the entire economy where regulators devote extensive attention to auditing the accuracy of private firms' prices to ensure that they properly reflect the costs of providing a service.[67] In most settings, of course, ordinary economic forces are generally understood to work much better than command-and-control regulation in setting prices. As described above, the logic for carving out insurance from this default has historically been that insurers affirmatively colluded to set their prices, thus undermining competition.[68]

But as I have explored at length elsewhere, insurers no longer engage in any of the anti-competitive practices that motivated state prohibitions of "unfairly discriminatory" or "excessive" rates.[69] Until the early 1990s, many insurers collusively set their rates based on the publication of "advisory rates" by statistical firms that they ran.[70] In response to increasing federal pressure, however, state insurance regulators gradually acknowledged that promoting accurate information about expected insured losses did not require collusive rate setting among insurers.[71] To the contrary, insurers merely needed to share data about their past losses in order to promote collective knowledge of risk exposures.[72] All of the additional information impounded into rates—including desired profit margins, the value of the float on insurers' premiums, or insurers' costs for overhead, marketing, or distribution—need not be publicly shared to accomplish this goal.[73]

Consistent with this logic, during the 1990s, states broadly moved to prohibit publication of advisory rates or other forms of anti-competitive collusion in insurance markets. States now require that the statistical entities that collect and disseminate information about past losses

67. *See* Schwarcz, *supra* note 2, at 942–43.
68. *See supra* Part I.
69. *See* Schwarcz, *supra* note 2, at 945.
70. *Id.* at 967.
71. *Id.*
72. *Id.* at 967–68.
73. *Id.* at 970.

must be independent from operating insurers and licensed by state regulators.[74] These statistical agents, as well as all other firms, are broadly prohibited from disseminating any information that could factor into insurers' rate calculations, aside from narrowly-circumscribed information about past insured losses and some related data.[75] And even these data can only be published in industry-aggregate form, so that the pricing strategies of individual insurers are not detectable.[76]

As a result of these changes, insurers' sharing of data unambiguously promotes competition rather than thwarting it. Armed with industry-produced loss data, insurers can confidently enter new markets even though they do not have their own historical loss data on which to base prices.[77] Meanwhile, there is essentially no risk that the modern data-sharing practices described above could result in explicit price-fixing or tacit collusion.[78] Most property and casualty insurance markets include way too many competing firms for such collusion to be possible. And such collusion is becoming increasingly difficult as a practical matter because insurance products are becoming more and more heterogeneous.[79]

Not only do state prohibitions on "unfairly discriminatory" or "excessive" rates no longer make sense in modern-day insurance markets, but they are becoming increasingly infeasible to implement. As described above, insurance rating and underwriting is increasingly driven by complex statistical models that rely on Big Data to produce predictions.[80] Moreover, the complexity of these statistical models is accelerating quickly as insurers integrate machine-learning techniques into their model development.

These developments are making it increasingly difficult for state regulators to meaningfully review insurers' models so as to assess their accuracy, as the traditional insurance regulatory regime demands.[81] Indeed, "many state insurance departments do not have in-house actuarial support or have limited resources to contract out for support when reviewing rate filings that include use of predictive models."[82]

74. *Id.*

75. *See* Schwarcz, *supra* note 2, at 970.

76. *Id.*

77. *Id.* at 976.

78. *Id.*

79. *See generally* Daniel Schwarcz, *Reevaluating Standardized Insurance Policies*, 78 U. CHI. L. REV. 1263 (2011).

80. *See supra* Part I.A.

81. As one report penned by state regulators understates the matter, "it may take more than a casual introduction to statistics to comprehend the construction of" these complex nested statistical models. *Predictive Models Whitepaper*, *supra* note 29.

82. *See id.*

According to a recent report of state insurance office staffing, approximately forty states have no more than three actuaries on staff to review rate filings.[83] Instead, states increasingly rely on rate or form "analysts" to review the rate filings of every insurer operating in their state.[84] Yet most analysts simply do not have the technical background or experience to have the slightest chance of understanding, at any level of depth, the statistical rating and underwriting models that insurers are now deploying; such analysts are often hired right out of college, generally have no graduate degree, and are typically paid much smaller sums than could be fetched in private industry.[85]

States have used several strategies to respond to these deficiencies. Most commonly, many state insurance departments simply approve rate filings without subjecting them to any real scrutiny. This approach, of course, preserves many of the costs of regulation without providing any plausible public benefit. Other times, state insurance departments delegate responsibility for initial review of rating models to private contractors hired by the department or to staff of the National Association of Insurance Commissioners (NAIC). But this strategy has problems of its own: It either requires states to make policy judgments based on material they do not fully understand, or it practically empowers private actors to transform their own policy judgments into state regulatory action.

In sum, traditional state efforts to directly monitor whether rates are "unfairly discriminatory" or "excessive" in insurance simply do not make sense as a theoretical or practical matter. Such regulation promotes no discernible public interest, yet it consumes scarce regulatory resources and imposes substantial costs on insurers—at least some of which are presumably passed on to policyholders.

B. Gaps and Ineffectiveness in State Anti-Discrimination Law: Disparate Impact and Proxy Discrimination

Responding to the various deficiencies of state insurance anti-discrimination law would be relatively straight-forward if there were no

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83. *See* NAIC, REGULATORY RESOURCES REPORT (2018), https://www.naic.org/prod_serv/STA-BB-19-01.pdf.

84. *Id.*

85. Warren S. Hersch, *State Regulators May Be Undermanned as Duties Grow, Critics Warn*, LIFE ANNUITY SPECIALIST (Sept. 23, 2019), https://www.law.uconn.edu/sites/default/files/in_the_media/09-23-2019_State%20Regulators%20May%20Be%20Undermanned%20as%20Duties%20Grow.pdf; *see also* Daniel Schwarcz, *Preventing Capture Through Consumer Empowerment Programs: Some Evidence From Insurance Regulation*, *in* PREVENTING CAPTURE: SPECIAL INTEREST INFLUENCE AND HOW TO LIMIT IT (Moss & Carpenter eds., Cambridge Univ. Press 2013).

public policy problems created by insurance discrimination. But, of course, this is certainly not the case. Even discrimination that is perfectly rational from the perspective of insurers can have substantial public policy implications by undermining socio-economic mobility, perpetuating and legitimizing past discrimination, intruding on policyholder privacy, and unfairly stereotyping non-conforming members of groups. Many states' laws ostensibly recognize this reality by limiting or prohibiting insurance discrimination against discrete groups of policyholders.[86] But as this Sub-Part explores, in practice, state insurance anti-discrimination law willfully ignores these pressing regulatory issues, shielding insurers from any scrutiny so long as they do not formally incorporate suspect policyholder characteristics into their models.

1. The Disparate Impact Produced by Facially Neutral Insurance Practices

As described above, state insurance law generally does not even consider whether facially neutral insurance practices have a disparate impact on ostensibly protected groups. The insurance industry has been particularly vocal in arguing that any such disparate impact standard could fundamentally undermine otherwise healthy insurance markets, as virtually any type of discrimination could potentially disparately impact protected groups.[87] Consistent with this view, insurers routinely refuse to collect any data about legally-suspect policyholder characteristics, and some states affirmatively prohibit the collection of such data.[88] The lack of this data makes it much harder for regulators or potential litigants to establish whether an insurer's practices have a disparate impact in the first place.[89]

Despite these legal obstacles, there is, in fact, substantial evidence that a variety of insurer practices do indeed disparately impact protected groups. For instance, several studies have shown that insurers' use of credit-based insurance scores in pricing auto and homeowners

86. *See supra* Part I.C.

87. *See, e.g.*, David Snyder, *The Insurance Interview: A Discussion About Big Data With David Snyder, VP of International Policy for PCI*, https://www.faegrebd.com/en/insights/publications/-2017/7/the-insurance-interview-a-discussion-about-big-data-with-david-snyder-vp-of-international-policy-for; Miller, *supra* note 6; *Our Positions*, *supra* note 6.

88. *See* discussion *infra* Part III.

89. *See* ProPublica Study, *supra* note 8 ("Insurance companies do not collect any information regarding the race or ethnicity of the people they sell policies to. They do not discriminate on the basis of race," said James Lynch, chief actuary of the institute.). For a description of state laws forbidding collecting this info, see generally Daniel Schwarcz, *Transparently Opaque: Understanding the Lack of Transparency in Insurance Consumer Protection*, 61 UCLA L. REV. 394 (2014) [hereinafter Schwarcz, *Transparently Opaque*].

coverage disproportionately harms African Americans and low-income policyholders.[90] The most important was a 2007 Federal Trade Commission (FTC) study, which investigated insurers' use of credit scores to predict four types of automobile coverage claim risk: property damage liability, bodily injury liability, collision, and comprehensive.[91] The study confirmed that African Americans and Hispanics were disproportionately harmed by insurers' use of credit scores: insurance scoring increased the expected price of auto coverage for African Americans by approximately 10%, and the expected cost of such coverage for Hispanics by 4.2%.[92] It also found some evidence that individuals living in low-income zip codes were harmed by insurers' use of credit information.[93]

Similarly, several recent studies have provided powerful evidence that insurers' use of zip code in rating and underwriting has a disparate impact in auto and homeowners insurance. For instance, a recent study by the Massachusetts Attorney General's Office found that policyholders living in regions with high concentrations of minorities pay higher auto insurance premiums than comparable policyholders living in predominantly white regions.[94] In "the most heavily concentrated minority and lowest income communities," the report found, "drivers pay nearly twice as much for significantly less coverage than drivers with comparable driving records in the whitest and most affluent communities."[95] Another recent investigation by ProPublica found similar trends.[96] Focusing on California, Illinois, Texas, and Missouri, the study found persistent differences in the amount that a single hypo-

90. Several studies commissioned by state insurance departments also have found that insurers' use of credit information has a disparate impact on African Americans and low-income individuals. *See* TEX. DEP'T OF INS., USE OF CREDIT INFORMATION BY INSURERS IN TEXAS (2004), https://www.tdi.state.tx.us/reports/documents/creditall04.pdf; TEX. DEP'T OF INS., USE OF CREDIT INFORMATION BY INSURERS IN TEXAS: THE MULTIVARIATE ANALYSIS (2005), http://www.tdi.texas.gov/reports/documents/credit05sup.pdf; BRENT KABLER, MISS. DEP'T OF INS., INSURANCE-BASED CREDIT SCORES: IMPACT ON MINORITY AND LOW INCOME POPULATIONS IN MISSOURI (2004), http://www.insurance.mo.gov/reports/credscore.pdf.

91. FTC Study, *supra* note 12. The FTC was mandated to conduct by the 2006 Fair and Accurate Credit Transactions Act (FACTA). *See generally* 15 U.S.C. § 1681 (2012).

92. FTC Study, *supra* note 12.

93. *Id.*

94. *See* MASS. ATT'Y GEN., PREMIUM DISPARITIES AFFECTING MINORITY AND LOW-INCOME DRIVERS (Feb. 2, 2018), https://blog.harvardlawreview.org/wpcontent/uploads/2018/03/AG-Healey-to-Financial-Services-Committee-Feb22018.pdf.

95. *See id.* ("The disparity is so pronounced that experienced drivers with excellent records (no recent history of at-fault accidents or violations) in the communities with the most highly concentrated minority population pay higher average liability premiums than drivers in communities with the least concentrated minority population who had a recent history of at-fault accidents and/or violations and who purchased, on average, significantly more coverage.").

96. *See* ProPublica Study, *supra* note 8.

thetical policyholder—a 30-year old female safe driver who is a teacher with a bachelor's degree and excellent credit—would be charged for auto liability insurance in predominantly minority neighborhoods relative to majority white regions.[97] Similarly, numerous studies by the Consumer Federation of America have found that insurers charge consumers higher rates when they have socio-economic indicators associated with low-income and minority populations.[98]

Although use of credit information and zip code are the most well studied insurance practices that disparately impact protected groups, it is likely that many other forms of insurance discrimination have a similar disparate impact. For instance, many insurers include in their rating or underwriting models factors such as policyholders' occupation, marital status, or status as a renter or homeowner.[99] Preliminary research suggests that each of these factors is likely to disparately impact protected groups.[100] Meanwhile, at least some insurer practices—like charging more for commercial property insurance to building owners that rent to individuals receiving Section 8 federal housing assistance—so obviously disparately impact minority populations that no study is needed.[101]

Available evidence suggests that the disparate impact produced by these facially-neutral practices can substantially harm low-income and minority populations. For instance, a recent study on the affordability of auto insurance by the Federal Insurance Office (FIO) found that the average cost of auto liability insurance exceeds two percent of median income within 845 majority-minority or low-income U.S. zip codes.[102] This measure almost certainly understates the true affordability issues that low-income and minorities face in purchasing coverage, as it excludes the cost of comprehensive, collision, and un-

97. *See id.*; *see also* TOM FELTNER & DOUGLAS HELLER, CONSUMER FED'N OF AM., HIGH PRICE OF MANDATORY AUTO INSURANCE IN PREDOMINANTLY AFRICAN AMERICAN COMMUNITIES 3 (2015) (finding that premiums for those living in predominantly African American neighborhoods are 70% higher than premiums charged in predominantly white regions).

98. *See* DOUGLAS HELLER & MICHELLE STYCZYNSKI, CONSUMER FED'N OF AM., MAJOR AUTO INSURERS RAISE RATES BASED ON ECONOMIC FACTORS: LOW-AND MODERATE-INCOME DRIVERS CHARGED HIGHER PREMIUMS 2 (2006), https://consumerfed.org/wpcontent/uploads/2016/06/6-27-16-Auto-Insurance-and-Economic-Status_Report.pdf.

99. *See* GOOD DRIVERS PAY MORE FOR BASIC AUTO INSURANCE IF THEY RENT RATHER THAN OWN THEIR HOME, CONSUMER FED'N AM. (Feb. 8, 2016), https://consumerfed.org/press_release-/good-drivers-pay-more-for-basic-auto-insurance-if-they-rent-rather-than-own-their-home/.

100. *See id.*

101. *See* Jean M. Zachariasiewicz, *Not Worth the Risk: The Legal Consequences of the Refusal to Insure Properties with Section 8 Tenants*, 33 BANKING & FIN. SERV. POL'Y REP. 19, 19 (2014).

102. *See* U.S. DEP'T OF TREAS., FED. INS. OFF., STUDY ON THE AFFORDABILITY OF PERSONAL AUTOMOBILE INSURANCE 2 (2017).

derinsured motorists (UIM) coverage and it does not take into account the cost of coverage in non-voluntary markets—which is typically substantially higher than in voluntary markets.[103]

2. *The Disparate Impact Generated by Some Insurer Practices Is Normatively Troubling and Requires Regulatory Attention*

According to the insurance industry and state regulators, any disparate impact produced by property and casualty insurers' practices are irrelevant from a public policy perspective, because they are based on sound actuarial principles. Importing disparate impact principles into insurance law would disrupt otherwise well-functioning insurance markets, subjecting legitimate risk-based pricing to constant second-guessing by regulators and overly-aggressive plaintiffs' lawyers. Moreover, it would produce both moral hazard and adverse selection, as rates become increasingly untethered from risk.

These arguments are not without merit. Insurance is, in many ways, the business of discrimination. As such, subjecting all aspects of the insurance business to disparate impact analysis could well be unduly disruptive to the industry and consumers. Moreover, distorting risk-based pricing could indeed increase the likelihood of accidents by allowing relatively high-risk policyholders to be shielded from responsibility for their actions.

Yet the conclusion that insurance law and regulation should completely ignore even quite substantial disparate impacts produced by facially neutral insurance practices is nonetheless deeply misguided, for at least three reasons. First, the disparate impact produced by the insurance industry undermines economic mobility. Second, insurance practices that disparately impact protected groups may not be necessary for insurers to price risk efficiently. Third, in some cases these practices may amount to unintentional proxy discrimination, which directly targets members of protected groups for worse outcomes.

a. Insurance Practices that Disparately Impact Protected Groups Impede Economic Mobility

Property and casualty insurance is in many ways a prerequisite to socio-economic mobility. Without auto liability insurance, people in most states cannot drive, meaning that they face barriers to working and securing an education. And without homeowners insurance, most people cannot secure a mortgage, which means that they cannot purchase a home. For these reasons, insurance practices that dispa-

103. *See id.* at 5, 10.

rately impact minority populations can have an outsized impact on socio-economic mobility.[104] Put simply, the fact that auto insurance or homeowners insurance is, on average, more expensive or less available for African Americans than whites impedes the ability of African Americans as a group to own homes, drive cars, maintain employment, or secure an education. This is true even if the reason why insurance is relatively expensive or unavailable to these groups is because they are, on average, more likely to incur claims.

To be sure, these arguments are hardly unique to insurance. For instance, many of these same arguments could be leveled against employers, banks, landlords, and universities that rely on facially-neutral practices that disparately impact protected groups. But that is precisely why all of these types of entities are subject to some form of government scrutiny when they employ facially-neutral practices that disparately impact protected groups. Moreover, insurance is plausibly distinguishable from most other fundamental ingredients to socio-economic mobility because, in at least some settings, the government is directly responsible for making insurance so necessary. Most obviously, it is the state that mandates liability insurance to drive a car. But even the requirement that mortgage applicants must maintain homeowners insurance stems from the rules of the pseudo-government mortgage giants. Because the state helps elevate insurance into a practical necessity, it also bears some distinct responsibility for ensuring that doing so does not impede the broader goal of promoting socio-economic mobility. Simply dismissing any consideration of these harms because of countervailing considerations regarding the efficiency of insurance markets—as insurers and regulators currently do—fails to meaningfully grapple with the relative costs and benefits of affirmatively exempting the insurance industry from the disparate impact regime that applies to virtually all other providers of consumer financial services.

b. Insurance Practices That Disparately Impact Protected Groups May Not Promote the Efficiency of Insurance Markets

Despite the insurance industry's arguments, there is good reason to believe that at least some facially-neutral practices that produce a disparate impact in insurance markets are not necessary for these markets to thrive.

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104. This point is related to several articles that examine using insurance anti-discrimination laws to redistribute wealth. *See generally* John R. Brooks et al., *Cross-Subsidies: Government's Hidden Pocketbook*, 106 GEO. L.J. 1229 (2018); Kyle Logue & Ronen Avraham, *Redistributing Optimally: Of Tax Rules, Legal Rules, and Insurance*, 56 TAX. L. REV. 157 (2003).

First, at least some practices that produce a disparate impact may not be driven by risk-based pricing but by differences in policyholders' demand elasticity. Indeed, the ProPublica report described earlier not only found a substantial difference in the rates charged in predominantly minority and white neighborhoods, but it also found some evidence that these rate differences might not reflect differences in risk.[105] In particular, the study identified differentials in insurance rates across zip codes by securing premium quotes for auto liability coverage from numerous insurers based on a single hypothetical person living in different zip codes.[106] It then found that these premium differentials could not be justified by aggregate risk-based differentials in the zip codes—in the aggregate, policyholders in predominantly minority regions experienced similar (or lower) insured losses than policyholders in white regions.[107]

To be sure, as both the industry and state regulators have persuasively argued, the implications of these findings are hardly crystal clear. Most importantly, the experience of individual insurers who charged higher rates in predominantly minority neighborhoods might not be consistent with the broader industry trends. For any individual insurer, the higher rates it charged in minority regions might well reflect the fact that its particular policyholders in these regions did indeed have higher aggregate claims, in contrast to the aggregate industry experience. Additionally, the aggregate industry data on claims does not necessarily apply to the hypothetical person for whom quotes were generated for purposes of the study; perhaps there really is more risk in insuring the particular type of driver the study focused on—a thirty-year old female safe driver who is a teacher with a bachelor's degree and excellent credit—when she lives in a predominantly minority zip code.

At the very least, however, the ProPublica report raises a substantial possibility that the disparate impact produced by insurers' practices are not justified by cost-based considerations. As the ProPublica report itself explained, the objections lodged by the industry and regulators are unlikely to explain the study's finding of a "consistent pattern of higher prices for minority neighborhoods" that were no riskier than white neighborhoods.[108] Moreover, the Massachusetts Attorney General's study also found some similar evidence of racial disparities that were potentially not cost-justified: according to that study, even

105. *See* ProPublica Study, *supra* note 8.
106. *Id.*
107. *Id.*
108. *Id.*

policyholders with good driving records living in minority communities paid more for auto insurance than individuals living in white neighborhoods who had recently had accidents.[109] Furthermore, the limitations in the ProPublica study were a byproduct of the fact that the industry and regulators do not make individual insurers' claims data publicly available, thus precluding ProPublica or any other independent researcher from attempting to respond to the study's design limitations.

If insurance practices do indeed disparately impact protected groups for reasons that are untethered to risk, the explanation likely involves the phenomenon of price optimization. Price optimization refers to the practice of pricing coverage based on inferences about policyholders' price sensitivity.[110] For instance, a price optimizing insurer might increase rates on renewing policyholders who it has identified as unlikely to actively shop for alternative coverage. Such price optimization thrives in competitive settings like insurance because it allows individual firms to extract consumer surplus without forgoing the business of more price-sensitive consumers. It is therefore hardly surprising that price optimization has been identified as an increasingly common trend among some insurers, even though the leading insurance industry groups maintain that insurers only base rates on risk-based factors.[111]

Although a number of states have issued bulletins purporting to ban this practice as "unfair discrimination," many states have not done so. More importantly, precisely because of the increasing complexity and opacity of insurers' rating and underwriting models, it is unclear how well this prohibition on price optimization is enforced. Further reinforcing this conclusion is the fact that, as described above, most current forms of rate regulation almost completely ignore discrimination via underwriting, even though rating and underwriting are becoming increasingly intertwined.[112] In fact, insurers generally are not legally required to file their underwriting guidelines with regulators. As such, regulators' elaborate rate review processes cannot detect potential price optimization that occurs via underwriting rather than via rating. Although regulators can review underwriting guidelines during mar-

109. MASS. ATT'Y GEN., *supra* note 94.

110. *See Price Optimization White Paper*, *supra* note 27, at 7 (2015). It is thus simply the insurance version of the economic phenomenon known as price discrimination.

111. *See* Letter from Dave Snyder, PCI, to Working Group (Aug. 31, 2018) (on file with author). For more recent evidence regarding the prevalence of price optimization in U.S. insurance markets, see *The Markup Whitepaper* (forthcoming 2020).

112. *See supra* Part I.A.

ket conduct exams, such exams are sporadic and cover a massive range of potential issues in addition to underwriting.

Additionally, price optimization may result from a combination of insurers' marketing and rating/underwriting practices in a way that would likely evade detection by state insurance regulators. For instance, insurers may directly or indirectly encourage agents who sell coverage in regions where consumers tend to be relatively less price sensitive to place applicants in subsidiaries that principally cater to "substandard" risks.[113] Such steering of customers in low-income or minority areas to relatively high-cost products was well documented among mortgage-brokers in the lead-up to the 2008 financial crisis.[114] Because this type of discrimination operates through the interaction of marketing/sales and rating/underwriting, state regulatory review of rates would be unlikely to detect these trends.

Price optimization is a prime explanation for insurance practices that produce a disparate impact because minority or low-income policyholders may be particularly likely to have relatively inelastic insurance demand. Insurance is a unique product because most individuals are legally or practically required to buy it. Yet low-income individuals who live in traditionally underserved areas are likely to have comparatively limited financial literacy, which may impair their ability to identify insurance that provides the best combination of coverage and price.[115] Moreover, they may have less access to individuals who are familiar with the insurance industry and can offer trustworthy advice on this issue. As such, they may be particularly likely to simply retain the coverage they initially select without actively shopping for alternatives.

To be sure, it is also entirely possible that some low-income individuals are relatively likely to shop aggressively for insurance based on rates, because relatively small rate differences disproportionately impact their marginal utility. However, the point here is not that price optimization necessarily or inevitably disparately impacts minority populations. Instead, it is that there is a substantial risk of such a disparate impact, yet absolutely no data to test for such an effect. More-

113. *See* KEVIN M. MCCARTY, FLA. OFF. OF INS. REG., REPORT OF COMMISSIONER: THE USE OF OCCUPATION AND EDUCATION AS UNDERWRITING/RATING FACTORS FOR PRIVATE PASSENGER AUTOMOBILE INSURANCE (Mar. 2007), https://www.floir.com/siteDocuments/OCC RateRpt.pdf.

114. *See generally* Justin P. Steil et al., *The Social Structure of Mortgage Discrimination*, 33 HOUS. STUD. 759 (2018).

115. *See generally* Annamaria Lusardi, *Financial Literacy Skills for the 21st Century: Evidence from PISA*, 49 J. CON. AFF. 639 (2015) (describing studies showing a link between socio-economic status and financial literacy).

over, there are other potential variants of price optimization that could more clearly disparately impact low-income or minority groups, even though information about their prevalence is limited. For instance, insurers may price optimize based on cross-selling potential rather than price sensitivity, causing them to offer discounts to relatively wealthy customers so as to obtain their business for other product lines.[116]

Facially-neutral insurance practices that implement price optimization strategies should be legally restricted to the extent they disparately impact protected groups. Unlike risk-based pricing, there is no good social welfare reason for allowing insurers to price optimize. For instance, price-optimized premiums do not address legitimate insurance market concerns like moral hazard or adverse selection because the practice targets policyholders who are comparatively non-responsive to rates. Consumers who are unlikely to alter their purchasing decisions in response to differences in rates are also presumably unlikely to alter their levels of care on this basis. Additionally, precisely because price optimization is a new phenomenon that is inconsistent with the traditional prohibition against "unfair discrimination," it can hardly be the case that rooting out the practice would unduly harm the insurance industry.

A second reason that facially-neutral insurance practices producing a disparate impact may not be necessary for insurance markets to operate efficiently is that there may be less discriminatory alternatives. The availability of such alternatives, of course, is often a key consideration in lawsuits advancing disparate impact claims. But insurance law and regulation have rarely pressed insurers to determine whether they can substitute away from risk-classification practices that disproportionately harm protected groups while maintaining their ability to effectively classify risks.[117]

That possibility is becoming increasingly realistic. In the last decade, a suite of technologies have emerged that allow insurers to directly measure factors more closely linked to policyholder risk then credit or zip code. Some auto insurers, for instance, are now using telematic technologies that measure a range of directly relevant factors related to auto insurance risk—including number of miles driven, frequency of sudden stops, and travel above the speed limit. Such direct risk-

116. I thank Da Lin for suggesting this point.

117. The one exception is that the 2007 FTC study did indeed examine whether it was possible to come up with a less discriminatory alternative than credit. FTC Study, *supra* note 12. The study found that it was not. However, whether that continues to be the case given the rapid pace of technological development in the insurance analytics domain is unclear.

based measurement holds the potential to reflect each individual's driving tendencies rather than imperfectly proxying for these tendencies using factors, like credit, that disproportionately harm minorities. Similarly, property insurers are now using technologies, like drone-based video assessments, to more accurately measure the risks associated with individual properties. Rather than charging more to landlords who rent to Section 8 tenants because their properties may not generally be "kept up" as well, it may be possible for insurers to directly measure property conditions both before and after coverage is bound.[118] As these technologies that directly measure risk improve and become more socially accepted, they hold the very realistic possibility of allowing insurers to price risk more directly through less discriminatory means than socio-economic factors like zip code or credit-based insurance scores.

The mere fact that these techniques for pricing insurance coverage have not yet supplanted more traditional insurance-pricing strategies does not undermine this point. In part, this is because insurers will not take into account the social benefits of decreasing reliance on risk-based pricing and underwriting tools that disproportionately harm protected groups. But it is also because insurers may have inadequate incentives to invest in improving their risk-classification schemes, because such schemes are generally non-excludable.[119] In particular, improved risk-classification methods can often be easily mimicked by competitors, resulting in individual insurers having insufficient incentives to develop, implement, and test such technologies.

c. Insurance Practices that Disparately Impact Protected Groups May Amount to Unintentional Proxy Discrimination

As described above, proxy discrimination is a particularly pernicious type of disparate impact. It exists whenever the statistical usefulness to the discriminator of a facially-neutral practice is directly attributable to its correlation with a suspect classifier. For instance, reconsider auto insurance discrimination on the basis of zip code. There is little doubt that such discrimination disparately impacts African Americans.[120] But such discrimination would also constitute proxy discrimination if the reason that insurers discriminated on the basis of zip code was because zip code correlated with a suspect characteristic,

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118. For another example, life insurers are now directly measuring health-related activities through technologies like smart watches. *See* Swedloff, *supra* note 28.

119. Kenneth S. Abraham, *Efficiency and Fairness in Insurance Risk Classification*, 71 VA. L. REV. 403, 404, 406 (1985).

120. *See supra* Part I.

like race. That, of course, is exactly what happened historically, when insurers red-lined predominantly African American communities: insurers relied on the facially-neutral classifier of zip code because doing so helped them covertly achieve their intended goal of discriminating against African Americans.[121]

Importantly, however, proxy discrimination need not amount to intentional discrimination. Instead, an insurer might rely on a facially-neutral characteristic whose statistical usefulness derives from its correlation with a suspect characteristic like race, gender, or income without the insurer appreciating or intending that result. Returning to the zip code example, insurance discrimination on the basis of zip code would amount to proxy discrimination if zip code helped predict insurance claims because of the correlation between zip code and income (which is generally regarded as a suspect characteristic under state insurance law). This could happen if low-income policyholders are relatively likely to file claims slightly above their deductible, or relatively unlikely to promptly repair their cars. In this scenario, insurers would find that policyholder zip code helped them to predict claims without understanding that the reason for this result was that it allowed them to target low-income policyholders for higher prices.

In the insurance setting, unintentional proxy discrimination can arise not only when a facially-neutral practice helps insurers to predict claims by proxying for a suspect characteristic; it can also arise when facially-neutral discrimination allows insurers to price optimize by proxying for a suspect characteristic. Once again returning to the example of zip code-based discrimination, recall that one explanation for why insurers charge higher prices in predominantly minority communities is because individuals living in these communities may be less price-sensitive when it comes time to renew their coverage. Suppose the reason they are less price-sensitive is because low-income individuals are disproportionately unlikely to have reliable access to internet services, which is practically necessary to comparison shop for insurance coverage. In that event, insurance discrimination on the basis of zip code would constitute proxy discrimination for income: the very reason that zip code would be statistically useful to the insurer is that it proxies for the suspect characteristic of income.

Even unintentional proxy discrimination produces harms that go well beyond the harms of ordinary disparate impact. This point is easiest to see by recognizing that proxy discrimination can produce the exact same results as intentional discrimination against protected

121. *Id.*

groups, depending on the effectiveness of the proxy. In both settings, an individual who is a member of a protected group is treated differently because of their membership in that group. Even if this occurs without the discriminator intending or knowing this result, many of the traditional harms of intentional discrimination follow. Members of groups that have been traditionally discriminated against are effectively targeted and penalized for their membership in that group, irrespective of their individual traits or risk levels. The result is not simply to undermine socio-economic mobility, but to reinforce and perpetuate historically-embedded inequalities, which generally are responsible for the increased risk associated with insuring protected groups.[122]

Because diagnosis of proxy discrimination depends on why a particular form of discrimination is predictive of risk, the prevalence of such insurance discrimination is contested and, in most settings, unclear. As suggested above, whether credit-based insurance discrimination constitutes proxy discrimination is still a matter of debate: although the weight of the evidence suggests that credit information predicts risk by measuring past care levels (and hence does not arise to proxy discrimination), some continue to argue that the predictive capacity of credit derives from its correlation with income. Similarly, insurers that charge more for commercial property coverage to building owners that rent to Section 8 tenants claim they are not engaging in proxy discrimination because the predictive power of renting to Section 8 tenants stems from neutral factors, like the complexities associated with the program, which tend to slow property improvements. Unfortunately, state insurance regulators have not carefully studied these issues, at least in part because these distinctions do not currently matter under state law; so long as insurers do not explicitly include race or income in their rating or underwriting guidelines, they comply with state law.

However prevalent proxy discrimination is in modern insurance markets, it is almost certain to become a much worse problem in the near future, as insurers increasingly turn to machine learning techniques to develop their rating and underwriting algorithms. This is because AIs are inherently structured to proxy discriminate whenever they are deprived of information about membership in a legally-suspect class that is genuinely predictive of a legitimate goal, like minimizing insurance claims.[123] Recall that predictive AIs locate

122. *See* Prince & Schwarcz, *supra* note 11. For discussion of why using actuarially-justified race and gender based statistics is normatively troubling in the torts context, see MARK A. FRANKLIN ET AL., TORT LAW AND ALTERNATIVES (10th ed. 2016).

123. *See* Prince & Schwarcz, *supra* note 11, at 18–20.

correlations between input data and programmed "target variables" by combing through massive amounts of training data.[124] This process results in AIs inevitably locating proxies for genuinely predictive characteristics when direct data on these characteristics is not made available to the AI due to legal prohibitions.[125] Simply denying AIs access to the most intuitive proxies for predictive variables does little to thwart this process; instead it simply causes AIs to locate less intuitive proxies.

III. Towards a Civil Rights Approach for Insurance Anti-discrimination Law

State anti-discrimination law is premised on an antiquated understanding of property and casualty insurance markets. It is past time for that regime to evolve by directly targeting the primary public policy justification for continuing to regulate discrimination in these markets: that such discrimination may unfairly target low-income or minority populations. This reframing of insurance anti-discrimination law requires limiting the inefficiencies embedded within the current U.S. system for regulating insurance rates while more directly targeting socially-problematic forms of insurance discrimination.

This part sketches out what a reformed approach to insurance anti-discrimination law might look like. Part A begins by suggesting that states repeal their laws prohibiting "inadequate, excessive, or unfairly discriminatory" insurance rates, as well as the unwieldy system of rate filing that is designed to facilitate regulatory review of insurance rates. Part B then suggests a pair of reforms that would more directly and efficiently target the risk of insurance discrimination that unreasonably impacts low-income or minority populations. First, it suggests imposing disclosure requirements on property and casualty insurers that mirror those contained in the Home Mortgage Disclosure Act (HMDA).[126] These reforms would require insurers to collect and publicly disclose transaction-level data on insurance applications and purchases, including information about consumers' membership in protected groups. Second, it proposes establishing a limited cause of action against insurers for disparate impact, which would focus on identifying proxy discrimination and price optimization that disproportionately burdens protected segments of the population.

124. *See* Lee Epstein & Gary King, *The Rules of Inference*, 69 U. Chi. L. Rev. 1, 19–20 (2002).

125. *See* Barocas & Selbst, *supra* note 35, at 691–92.

126. Home Mortgage Disclosure Act of 1975, 12 U.S.C. §§ 2801-2809 (2012).

A. De-Regulating: Eliminating Public Utility Style Rate Regulation

For the reasons described in Part II.A, state laws prohibiting "inadequate, excessive, or unfairly discriminatory" rates in property and casualty insurance markets should be repealed. So too should state laws authorizing state regulators to disapprove rate changes in insurance markets. Because state prohibitions against "inadequate" rates have already been displaced as a practical matter by modern methods of solvency regulation,[127] the primary impact of this reform would be to eliminate state regulators' scrutiny of whether property and casualty insurers' rates are excessive or unfairly discriminatory.

Although this proposal would substantially impact most states' insurance markets, it is hardly revolutionary. In fact, Illinois effectively adopted this reform in 1971, when its legislature failed to re-authorize its scheme of rate regulation.[128] Since that time, several studies have found that Illinois's property and casualty insurance markets have fared quite well from a macro-perspective.[129] In fact, auto and homeowners insurance premiums are generally lower in Illinois than in other states, in part because a relatively large number of competing carriers operate in the state.[130] Their profit margins are comparable to those that predominate in other competitive consumer financial services markets, and rate changes are generally driven principally by changes in claims experiences.[131]

Illinois's experience is consistent with that of many other states that have limited, but not completely abandoned, their regulation of property and casualty insurance rates. A substantial number of states have adopted such deregulatory reforms, typically by establishing presumptions that rate changes reflect competitive market conditions or by exempting certain market segments from rate review.[132] Most studies of these reforms have found that they generally improve the overall health of the underlying insurance markets. In particular, states that deregulate generally see an increased number of competing insurers, a decreased residual risk pool, frequent and modest rate changes that track claims experiences, and insurer profit levels that are comparable to those that predominate in comparable markets.[133]

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127. *See* ABRAHAM & SCHWARCZ, *supra* note 1.

128. *See* Schwarcz, *supra* note 2, at 963.

129. Stephen P. D'Arcy, *Insurance Price Deregulation: The Illinois Experience in* DEREGULATING PROPERTY-LIABILITY INSURANCE 248, 281 (J. David Cummins ed., 2002).

130. *See id.*

131. *Id.* at 281–82.

132. *See* Schwarcz, *supra* note 2, at 963.

133. Martin F. Grace, Robert W. Klein & Richard D. Phillips, *Auto Insurance Reform: Salvation in South Carolina*, *in* DEREGULATING PROPERTY-LIABILITY 148–49 (2002); Sharon Tenny-

Finally, it is worth noting that countries in the European Union have also experienced positive results from abolishing insurance rate regulation.[134] In the early 1990s, the European Parliament passed insurance reforms that eliminated member states' capacity to regulate insurance rates.[135] Prior to that time, many member countries exercised substantial regulatory control over rates.[136] Since then, member countries have generally seen an increase in the competitive conditions of property and casualty insurance markets, causing premiums to decline and the number of competing firms to increase.[137]

B. Re-Regulating: Establishing a Civil Rights Oriented Approach to Insurance Anti-discrimination Law

Of course, eliminating existing regulatory schemes is much simpler than creating new regulatory mechanisms that effectively and efficiently target public policy concerns. As described in Part II.B, discrimination in property and casualty insurance markets ultimately raises the same public policy concerns as discrimination in other consumer financial services markets: that it may disproportionately and unreasonably burden low-income or historically-disadvantaged groups. And while discrimination in insurance markets is indeed essential from an economic perspective, this is also the case in many other consumer-financial markets, such as consumer finance. For these reasons, long-standing federal regimes for combatting unlawful discrimination in the provision of credit provide a good template for redesigning insurance anti-discrimination law.

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son, *The Impact of Rate Regulation on State Automobile Insurance Markets*, 15 J. INS. REG. 502, 516 (1997). For a systematic description of many of these studies, see SCOTT E. HARRINGTON, INSURANCE DEREGULATION AND THE PUBLIC INTEREST (2000); Richard Derrig & Sharon Tennyson, *The Impact of Rate Regulation on Claims: Evidence from Massachusetts Automobile Insurance*, 14 RISK MGMT. & INS. REV. 173, 174 (2011); Lauren Regan et al., *The Relationship Between Auto Insurance Rate Regulation and Insured Loss Costs: An Empirical Analysis*, 27 J. INS. REG. 23, 27 (2009); Mary Weiss et al., *The Effect of Regulated Premium Subsidies on Insurance Costs: An Empirical Analysis of Automobile Insurance*, 77 J. RISK & INS. 597, 599 (2010); Sharon Tennyson, *The Long-Term Effects of Rate Regulatory Reforms in Automobile Insurance Markets*, INS. RES. COUNCIL 17 (2012), http://www.namic.org/pdf/13memberAdvisory/131113_IRC_Tennyson.LongTermEffectsRateRegulatoryReforms.pdf [http://perma.cc/5LXZ-5X2C].

134. Angelo Borselli, *Insurance Rates Regulation in Comparison with Open Competition*, 18 CONN. INS. L.J., 109, 142–43 (2011).

135. Council Directive 92/49/EEC, art. 29, 1992 O.J. (L 228).

136. *See* Borselli, *supra* note 134.

137. *See id.*; *see also* Retail Insurance Market Study, Europe Economics 100, 104–05 (Nov. 26, 2009), http://ec.europa.eu/internal_market/insurance/docs/motor/20100302rim_en.pdf. *See generally* Giuseppe Turchetti & Cinzia Daraio, *How Deregulation Shapes Market Structure and Industry Efficiency: The Case of the Italian Motor Insurance Industry*, 29 GENEVA PAPERS ON RISK & INS. 202 (2004).

1. Data and Disclosure of Insurance Practices

The first step in structuring insurance law and regulation to combat unfair discrimination against protected groups is for the law to facilitate the public availability of relevant data. The reason is simple: without reliable data about how insurers treat low-income or minority insurance applicants, it is impossible to identify practices that unreasonably harm members of these groups. And given state regulators' substantial resource constraints and historical inattention to this issue, other constituencies—including academics, think tanks, journalists, lawyers, and other regulators—can and should play a role both in identifying potentially unfair practices and in inducing state regulators to act on that basis.

Such a reform could be patterned after the HMDA,[138] which requires virtually all mortgage lenders to collect and publicly report loan-level data on a broad range of information that can be used to identify potentially discriminatory practices.[139] Since its implementation in the 1970's, the HMDA has required public reporting of data on each mortgage application submitted to virtually all mortgage lenders, including (i) the identity of the lender; (ii) whether the loan was approved or denied; (iii) specific characteristics of loans originated; (iv) the census tract in which the underlying property is located; (v) loan pricing information, including interest rate; and (vi) information about the applicant, including their membership in a protected class and income.[140] The Dodd-Frank Act expanded the reported data to include additional information about the loan's characteristics relating to loan repayment risk, such as the existence of pre-payment penalties and balloon payments.[141]

Although commentators debate the relative costs and benefits of the HMDA, there is little doubt that the data made available via the HMDA has been immensely valuable in identifying and addressing gaps in the availability and affordability of coverage across demo-

138. *See* 12 U.S.C. § 2803 (2012); 12 C.F.R. pt. 1003 (2013).

139. Others have previously proposed this type of reform. *See* Gregory D. Squires, *Bank Reform Offers Opportunity to Address Insurance Redlining*, HUFF. POST (July 13, 2010, 12:59 PM), http://www.huffingtonpost.com/gregory-dsquires/bank-reform-offers-opport_b_644542.html. *See generally* Gregory D. Squires, *Racial Profiling, Insurance Style: Insurance Redlining and the Uneven Development of Metropolitan Areas*, 25 J. URB. AFF. 391 (2003).

140. *See generally* Neil Bhutta, Steven Laufer & Daniel R. Ringo, *Residential Mortgage Lending in 2016: Evidence from the Home Mortgage Disclosure Act Data*, 103 FED. RES. BULL. 1 (2017). Some of these data, such as loan amount, are reported in broad categories to limit the risk that individual loan applicants could be identified using the data.

141. *See* KRIS D. KULLY, CONSUMER FIN. SERV. REV., CFPB ISSUES FINAL GUIDANCE ON PUBLIC DISCLOSURE OF HMDA DATA (Jan. 2, 2019), https://www.cfsreview.com/2019/01/cfpb-issues-final-guidance-on-public-disclosure-of-hmda-data/.

graphic groups. The data collected and publicly disclosed pursuant to the HMDA has been used in hundreds of studies of mortgage lending discrimination.[142] Additionally, it has facilitated innumerable private and public actions that successfully addressed discriminatory lending practices.[143]

There is every reason to believe that the public disclosure of HMDA-style insurance data would produce similar benefits. As suggested in Part II, efforts by non-regulators to understand how protected groups are impacted by current insurance practices have been substantially impeded by the limited availability of relevant data. For instance, the ProPublica and Consumer Federation of America studies have been forced to approximate how specific insurers treat different types of consumers by securing price quotations for hypothetical consumers; as a result, it is often hard to know whether these results generalize across the population.[144] Similarly, the ProPublica study was subject to legitimate industry criticism—it was forced to rely on aggregate-industry loss experience in targeted regions when assessing whether differentials in the quotes provided to hypothetical consumers could be justified by loss experience.[145] Even the Federal Insurance Office faced significant data availability limitations in attempting to assess the impact of insurer practices on protected populations, a fact which is particularly notable given that it was able to use substantial amounts of data that were voluntarily provided by states and the industry.[146]

Importantly, developing a HMDA-like public disclosure regime for property and casualty insurance would create limited compliance costs

142. *See, e.g.*, Charles L. Nier, III & Maureen R. St. Cyr, *A Racial Financial Crisis: Rethinking the Theory of Reverse Redlining to Combat Predatory Lending Under the Fair Housing Act*, 83 TEMP. L. REV. 941, 948–49 (2011); Charles M. Lamb et al., *HMDA, Housing Segregation, And Racial Disparities in Mortgage Lendings*, 12 STAN. J. CIV. RTS. & CIV. LIBERTIES 249 (2016).

143. Henry M. Jay, *Full Disclosure: How Should Lenders Respond to the Heightened Reporting Requirements of the Home Mortgage Disclosure Act?*, 10 N.C. BANKING INST. 247, 247 (2006).

144. *See supra* Part II.

145. *See* James Lynch, *I.I.I.: Why ProPublica Auto Insurance Report Is Inaccurate, Unfair and Irresponsible*, INS. J. (Apr. 5, 2017), https://www.insurancejournal.com/news/national/2017/04/05/447012.htm; PROPUBLICA, *The Car Insurance Industry Attacks Our Story. Here's Our Response.* (Apr. 17, 2017), https://www.propublica.org/article/the-car-insurance-industry-attacks-our-story-our-response#.

146. U.S. DEP'T OF TREAS., *supra* note 102, at 2, 10 ("This is the first use of the FIO Affordability Index, and conclusions drawn from this study should be limited because FIO was unable to analyze comprehensive premium data for all auto insurance policies issued in the fifty states and the District of Columbia."). Monitoring Availability and Affordability of Automobile Insurance, 81 FED. REG. 45,372 (July 13, 2016), https://www.govinfo.gov/content/pkg/FR-2016-0713/pdf/-2016-6536.pdf (describing data limitations).

or logistical challenges for insurers. This is because insurers already report most of the relevant data to statistical agents for reasons that should persist irrespective of legal reforms.[147] For instance, private passenger auto insurers must regularly report data to statistical agents that includes premiums, losses, coverage types, and underwriting factors, which are broken down by zip code or rating territory.[148] Statistical agents use these data for two purposes. First, they produce a variety of reports for state regulators to facilitate their review of whether rates *are* "excessive, inadequate, or unfairly discriminatory"; these reports would no longer be necessary if the underlying state laws were repealed, as suggested above.[149] Second, statistical agents produce "annual statistical compilations" that report industry-aggregated data so as to facilitate insurers' rate-making processes; this function is essential to facilitating insurers' predictions of future losses and minimizing barriers to entry, and would thus persist notwithstanding any legal reforms.[150]

Although the existing statistical reporting infrastructure would facilitate the development of a HMDA-like regime for property and casualty insurance, that infrastructure is not currently adequate to identify and police against insurance practices that unfairly harm members of protected groups.[151] This is for three broad reasons. The first is that statistical agents do not currently collect the right types of data so as to facilitate analysis of how insurer practices impact vulnerable populations, a fact which is hardly surprising given that their data collection has historically been designed to support rate-making and regulatory review under the "inadequate, excessive, or unfairly discriminatory standard." To illustrate, unlike the HMDA, statistical agents do not collect any information about policyholders' membership in protected groups.[152] Indeed, many states affirmatively prohibit insurers from collecting this information, ostensibly to limit the risk that insurers might intentionally discriminate.[153] Similarly, statistical agents do not collect various other types of data that would clearly be relevant to assessing the impact of insurers' practices on availability and af-

147. *See* Schwarcz, *supra* note 2.

148. *See id.*

149. *See supra* Part III.A.

150. *See* Schwarcz, *supra* note 2, at 169, 171.

151. *See* Da Lin, *Missing Data and Anti-Discrimination Laws*, HARV. L. REV. BLOG (Apr. 2018), https://blog.harvardlawreview.org/missing-data-and-anti-discrimination-laws/.

152. *See* NAIC, STATISTICAL HANDBOOK OF DATA AVAILABLE TO INSURANCE REGULATORS (2012), http://www.naic.org/documents/prod_serv_statistical_sta_zu.pdf [hereinafter STATISTICAL HANDBOOK].

153. *See* Schwarcz, *Transparently Opaque*, *supra* note 89.

fordability issues, including (i) price quotations, (ii) policy applications, or (iii) policy renewals/cancellations.[154]

Although the specific data that statistical agents collected from insurers would indeed change under a HMDA-like regime, most of the necessary adjustments to these data have already been worked out through public processes. For instance, a working group of state regulators operating under the auspices of the NAIC's Auto Insurance Study Group defined in detail the exact parameters of a data call to facilitate study of the impact of auto insurers' practices on low-income and minority groups.[155] Unfortunately, this proposal was scrapped at the last minute.[156] Similarly, at least one draft bill in the U.S. House of Representatives contains a reasonable initial description of what data could be publicly disclosed so as to allow for the identification of insurance discrimination that may unfairly target low-income or minority communities.[157]

The second reason that the data that statistical agents currently collect is limited in its ability to facilitate study of affordability/availability is that it is inconsistent in fundamental ways. In particular, some statistical agents, like the Insurance Services Office, collect transaction level data, while other statistical agents only collect summary data that aggregates numerous transactions.[158] As suggested by the structure of the HMDA, transaction level data is substantially more useful than summary data when it comes to facilitating analysis of how insurer practices impact vulnerable populations, as it allows for more robust data analysis that can be tailored to address particularized concerns.[159] Nor is this the only important inconsistency in current data collection by statistical agents. Perhaps just as importantly, while some statistical agents and insurers report data broken down by zip code,

154. *See* STATISTICAL HANDBOOK, *supra* note 152; Monitoring Availability and Affordability of Automobile Insurance, 81 FED. REG. 45,372 (July 13, 2016) ("Notice; advising adoption of methodology to monitor affordability of personal automobile insurance.").

155. *See* CONSUMER FED'N OF AM. & CTR. FOR ECON. JUST., *Comments of the Consumer Federation of America and the Center for Economic Justice to the NAIC Auto Insurance Working Group Regarding the August 10, 2018 Draft "Report" Outline* (July 31, 2017), https://consumerfed.org/wp-content/uploads/2018/09/cfa-cej-comments-naicautowg.pdf.

156. *See id*.

157. *See* Rep. Takano Proposed Bill, H.R.__115th Cong. (2018), https://takano.house.gov/imo/-media/doc/The%20FAIR%20RATES%20Act.pdf.

158. This difference in how data is reported generally depends on whether the statistical agent is also an advisory organization that performs data analysis for its member carriers or is instead simply a creature of insurers that is designed to facilitate regulatory reporting. *See* Schwarcz, *supra* note 2, at 968–89.

159. Indeed, it is for precisely this reason that advisory organizations like ISO and AAIS collect transaction level data from insurers.

others report the data based on territorial rating zones.[160] This distinction is essential, because while there are well developed studies of how zip codes match on to minority and low-income populations, no corresponding data exists for insurers' rating territories.[161]

Finally, current data collection by statistical agents does not support analysis of affordability and availability issues because much of this data is not made available to the public, or even to regulators. Statistical agents do not make any data freely publicly available; in fact, their business model relies on being able to sell this data to paying customers.[162] Perhaps even more importantly, the only data that statistical agents do provide for a substantial price tag consists of industry-aggregate data that is designed to facilitate loss prediction rather than to identify discriminatory practices.[163] In fact, statistical agents have historically refused to provide state insurance regulators with insurer-specific data, claiming that their contracts with insurers preclude making such data available.[164] Industry aggregate data is not only limited because of its summary nature, but also by the fact that it does not allow for the identification of whether a subset of insurers are engaging in practices that target vulnerable populations.

The insurance industry has consistently and successfully resisted reforms that would address these data limitations by citing trade secret concerns and state laws regarding confidentiality.[165] But the argument that any of the data described above would reveal insurer trade secrets is belied by the fact that similar data is released for mortgages without undermining competition in that domain.[166] More fundamentally, the argument is facially implausible. To be sure, insurers do in-

160. *See* STATISTICAL HANDBOOK, *supra* note 152.

161. *Id.*

162. *See* ABRAHAM & SCHWARCZ, *supra* note 1.

163. *See* Schwarcz, *supra* note 2, 969–71.

164. *See* Minutes of Auto Insurance Working Group, *supra* note 56 (describing how ISO refused to provide Texas regulators with insurer-specific data, causing Texas to abandon the traditional statistical agent model).

165. *See* Letter from Dave Snyder, *supra* note 111 (arguing that the NAIC should not even release industry aggregated data bearing on availability/affordability issues because that data is "is a trade secret . . . which, if disclosed, would cause substantial injury to the competitive position of the subject enterprise. This data, despite its aggregation, is still data that is not publicly available. Furthermore, the information has commercial value and was acquired at great cost to companies. Release of the data into the marketplace would pose the risk of substantial injury to the competitive position of the subject insurers.").

166. *Id.* Admittedly, the data that would be collected under this Article's proposal differs from the data that is currently collected from mortgage lenders via HMDA. In particular, HMDA does not require lenders to disclose their losses on mortgages, whereas such data collection is necessary in the insurance context to determine whether an individual insurer's pricing is, in fact, risk-based.

deed compete in part by identifying more reliable ways to assess insurance applicants' risk of incurring claims.[167] But there is no plausible way for a competitor to reverse-engineer an insurer's risk-assessment algorithms simply by examining limited transaction-level data on the quotations and coverages that it provides. This is because publicly released data would exclude the vast majority of factors that are fed into these algorithms, such as credit information, driving history, property characteristics, or telematics information. At most, then, the public release of HMDA-like data would allow insurers to identify which of their competitors are best at pricing risks (by comparing premiums and losses incurred) but would provide them with no means of replicating that success by reverse engineering their competitors' pricing strategies.

For similar reasons, the proposal could be implemented in a way that would limit any meaningful risk that it could facilitate collusion among competing firms. To be sure, this risk exists any time competing firms' prices are publicly disclosed. But because most of the information that individual insurers use to predict risk would be excluded from the data, it would be immensely difficult for any firm to replicate the pricing patterns of its competitors based on the disclosed data. Perhaps even more importantly, there is little reason to suspect that such implicit price matching would emerge as an attractive strategy for insurers, given that most property and casualty personal lines markets are served by numerous competitors who regularly seek to undercut one another on price.[168] To the extent that collusive pricing were a meaningful concern notwithstanding these countervailing considerations, one option would be to only release the data after a delay of several years. This would ensure the ability of the public to police the impact of insurers' pricing practices while eliminating the practical capacity of the data to facilitate collusive pricing.

2. *A Private Cause of Action for Disparate Impact and Proxy Discrimination*

Making HMDA-like data publicly available for personal lines of insurance would go a long way to enhancing understanding of how low-income and minority populations are impacted by insurers' practices. This understanding, in turn, could prove immensely influential in triggering legal or regulatory action at both the state and federal levels. But such public responses cannot, of course, be assured, as they de-

167. *See* ABRAHAM & SCHWARCZ, *supra* note 1.
168. *See* Schwarcz, *supra* note 2.

pend on numerous political and practical considerations. For that reason, it is sensible to pair the HMDA-style reforms described above with a private cause of action for insurance discrimination producing a disparate impact on protected groups.

This proposal is hardly radical. Such a disparate impact cause of action has long been available against mortgage lenders under federal statutes like the Fair Housing Act (FHA) and Equal Credit Opportunity Act.[169] Moreover, property insurers have potentially been subject to disparate impact liability under the FHA for decades, though this issue has been complicated by a number of legal questions, including reverse preemption under the McCarran Ferguson Act.[170] In 2015, HUD published a supplement to an earlier review clarifying that the FHA's disparate impact standard does indeed apply to insurance.[171] However, more recently, HUD—under the control of the Trump Administration—issued a Proposed Rulemaking that would reverse its earlier interpretation of the FHA's application to insurance.[172]

As suggested by the 2015 HUD rule, a disparate impact cause of action could largely mimic the well-established burden-shifting framework that courts have developed over the decades.[173] Plaintiffs would need to make out a prima facie case of discrimination by demonstrating that a facially-neutral practice disproportionately impacted members of a protected group.[174] If this burden were met, then the burden would shift to the insurer to show that the challenged practice had a legitimate non-discriminatory purpose that was rooted in business necessity. Finally, to the extent that the insurer could demonstrate such a business necessity, then the plaintiff could only prevail if it showed that the insurer could achieve its legitimate aims with a less discriminatory alternative.[175]

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169. *See* Alan M. White, *Borrowing While Black: Applying Fair Lending Laws To Risk-Based Mortgage Pricin*g, 60 S. C. L. REV. 677, 692–94 (2009); Alex Gano, *Disparate Impact and Mortgage Lending: A Beginner's Guide*, 88 U. COLO. L. REV. 1109, 1166 (2017).

170. Dana L. Kaersvang, *The Fair Housing Act and Disparate Impact in Homeowners Insurance*, 104 MICH. L. REV. 1993, 2018 (2006); Matthew J. Cochran, *Fairness in Disparity: Challenging the Application of Disparate Impact Theory in Fair Housing Claims Against Insurers*, 21 GEO. MASON U. CIV. RTS. L.J. 159, 160 (2011).

171. *See* Application of the Fair Housing Act's Discriminatory Effects Standard to Insurance, 81 FED. REG. 69,012 (Oct. 5, 2016).

172. *See* HUD's Implementation of the Fair Housing Act's Disparate Impact Standard, 84 FED. REG. 42,854 (Aug. 19, 2019).

173. *See* George Rutherglen, *Disparate Impact Under Title VII: An Objective Theory of Discrimination*, 73 VA. L. REV. 1297, 1298 (1987).

174. Griggs v. Duke Power Co., 401 U.S. 424, 431 (1971).

175. *See id.* at 432.

Despite insurers' many objections, this disparate impact scheme could be easily adapted to target the particularized public policy concerns described in Part II, while respecting the importance of risk-based pricing in insurance. This is because courts could—and should—hold that insurance discrimination based on factors that genuinely predict claim frequency or severity, even after controlling for prohibited characteristics, constitute a "legitimate non-discriminatory purpose." The impact of this holding would be that insurers would only be liable under a disparate impact theory if their facially-neutral practices disparately impacted members of protected groups and (i) were driven by considerations of price elasticity or cross-selling rather than risk, (ii) operated as a proxy for a prohibited characteristic, or (iii) could be replaced by an equally effective, but less discriminatory, alternative.

In fact, this framework for applying disparate impact to insurance is similar to the framework that courts have already developed in the credit setting. In a number of cases, courts have held unlawful practices that produce higher borrowing costs for members of protected classes and that cannot be justified based on those borrowers' creditworthiness.[176] In particular, lenders that charge higher prices to applicants who are relatively less likely to comparison shop for better mortgage rates are guilty of unlawful discrimination to the extent these practices produce a disparate impact.[177] Just as in insurance, attempts to extract profit from less price-sensitive consumers of credit, rather than to accurately price the risks associated with lending to individual consumers, do not constitute the type of "legitimate business necessity" that can justify facially-neutral practices that disparately impact members of legally-protected groups.[178]

The framework proposed here would go beyond these holdings on credit in only one way: by recognizing that discrimination based on factors that predict risk primarily because they are correlated with

176. *See generally* Robert Bartlett et al., *Consumer-Lending Discrimination in the Fintech Era* (drft. 2019).

177. A.B. & S. Auto Serv., Inc. v. S. Shore Bank of Chi., 962 F. Supp. 1056, 1060 (N.D. Ill. 1997); Lewis v. ACB Bus. Servs., Inc., 135 F.3d 389, 406 (6th Cir. 1998); Miller v. Countrywide Bank, NA, 571 F.Supp.2d 251, 258–59 (D. Mass. 2008).

178. To be sure, it is possible that insurers could attempt to manipulate the "business necessity" standard by arguing in court that practices like price discrimination based on cross-selling potential constitute business necessity. *See generally* Ian Ayres, *Market Power and Inequality: A Competitive Conduct Standard for Assessing when Disparate Impacts are Unjustified*, 95 CAL. L. REV. 669 (2007). But court's rejection of these types of arguments in lending cases limits this risk. Moreover, to the extent that insurers do indeed have legitimate business needs to price optimize for reasons that are not simply about extracting consumer surplus, then it may well be appropriate for these factors to be taken into account.

protected characteristics also do not constitute a legitimate business necessity, because they amount to proxy discrimination.[179] Implementing this principle would not be unduly burdensome. In fact, well-developed statistical techniques already exist to test whether a factor used by insurers predicts risk principally because it proxies for a protected characteristic.[180] First, the insurer's statistical model must be re-estimated, so as to explicitly include data on legally prohibited characteristics. Second, the challenged facially-neutral variable must be examined to determine the extent to which it retains predictive power even after having accounted for the legally-prohibited variable. If so, then its predictive power does not primarily derive from its capacity to proxy for a protected characteristic. If not, then the opposite conclusion applies.

Conclusion

State insurance regulation has long clung to an antiquated, ineffective, and immensely costly set of anti-discrimination laws. State regulators generally defend this regime because it is familiar to them and assures them of job security. Insurers also defend this regime, as they have learned how to navigate it reasonably well so as to limit the extent to which it actually constrains their business decisions. The current regulatory scheme produces the added benefit for insurers of deterring new competitors from entering the marketplace, as was well illustrated when Google decided to end its brief effort to compete in insurance due to the uniquely cumbersome regulatory environment that prevailed in each state.[181] The only victims of this scheme are the public in general, and low-income and minority groups in particular. For this reason, it is past time for the state-based scheme of insurance anti-discrimination law to adapt to the 21st Century. Doing so requires jettisoning the public utility model of insurance rate regulation that persists in the states and replacing it with a civil rights-oriented regime that promotes competition while protecting vulnerable groups, so as to facilitate socio-economic mobility.

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179. *See supra* Part II.B. *See generally* James Grimmelmann & Daniel Westreich, *Incomprehensible Discrimination*, 7 Calif. L. Rev. Online 164 (2017).

180. *See* Devin G. Pope & Justin R. Sydnor, *Implementing Anti-Discrimination Policies*, *in Statistical Profiling Models*, 3 Am. Econ. J.: Econ. Pol'y 206, 207 (2011); *see also* FTC Study, *supra* note 12.

181. Amy O'Connor & Don Jergler, *Exclusive: Google to Shut Down Online Insurance Site, Partners Say*, Ins. J. (Feb. 22, 2016), https://www.insurancejournal.com/news/national/2016/02-/22/399490.htm.