The American Property Casualty Insurance Association (APCIA) respectfully submits this statement to the Committee on Financial Services’ Subcommittee on Housing, Community Development and Insurance for its hearing entitled “Drivers of Discrimination: An Examination of Unfair Premiums, Practices, and Policies in the Auto Insurance Industry.” APCIA is the largest and most diverse trade organization for the property and casualty insurance industry, with over 1,000 member companies who provide 60 percent of the property casualty insurance in the U.S. and who underwrite most of the nation’s auto insurance.

APCIA and our members are committed to three important goals: (1) expanding the availability and affordability of insurance while treating consumers fairly; (2) “being there” for policyholders when the worst happens; and (3) maintaining a healthy and competitive insurance market.

At the outset, let us be clear. The insurance industry works to ensure that the property and casualty market is inclusive and available to everyone. To broadly exclude categories of consumers from purchases is fundamentally inconsistent with open and healthy markets. We work to make insurance widely available in full compliance with legally established standards of conduct, especially prohibitions against discrimination. Violations of state and federal anti-discrimination laws are neither supported nor tolerated by our members or the industry at large.

As the primary regulators of the insurance industry, the States comprehensively and stringently require that auto insurance rates not be “excessive, inadequate or unfairly discriminatory” and that they be based on risk. This statutory formulation is understood and applied by regulators and the industry to mean that rates must be based on the actuarially determined risk that a particular policyholder or applicant for insurance presents. In addition, the States have clearly defined illegal discrimination in the insurance context and the nearly 11,000 state insurance regulators have a full panoply of tools ranging from fines through license revocations to enforce rate-setting and discrimination laws in the insurance context.

Understanding that this Committee has multiple bills before it related to the federal regulation of the auto insurance industry, we will not only describe the extensive state based regulatory structure in place preventing discrimination, we will also take this opportunity to explain why we believe these bills would undermine and diminish the effectiveness of state regulatory efforts and the very goals those efforts and this Committee seeks to achieve.

By eliminating actuarially determined, risk-based factors, legislation such as H.R. 1756 unintentionally imperil the very fairness they and the insurance industry are committed to ensuring
in the auto insurance market. Although support for these bills seems to be based on claimed benefits to consumers, we assert, based on extensive research published in academic journals and conducted by state insurance departments, that both bills will in reality do harm to the vast majority of consumers. They will undermine proven, effective state regulation of insurance and the financial health of the insurance market; they will assure that auto insurance rates are less risk-based and as a result less fair; and they will eliminate factors that actually serve as price discounts for many, if not most, policyholders.

Changing insurance pricing from reflecting risk, as both bills would do, artificially makes insurance more affordable for a few higher risk individuals while making it less affordable for the majority of others. The result, contrary to long established state regulatory standards, is to make auto insurance rates excessive for most, inadequate for others and unfairly discriminatory for all. This is not just a pricing issue. By requiring that risk and rates be matched, state standards for rate-setting assure insurer solvency and, thereby, consumer confidence. Departing from those standards not only creates unfairness but imperils solvency and erodes consumer confidence in the insurance market.

Separate from today’s focus on anti-discrimination efforts, insurers are keenly aware that auto insurance is regrettably unaffordable for some consumers. We recognize that with auto insurance required in 49 out of 50 states and the reliance that many consumers have on personal automobiles for childcare, work, and jobs, access to affordable auto insurance is paramount. Because of this, we work hard each and every day to make insurance more affordable for everyone through efforts to prevent crashes and reduce crash-related costs that make up the vast majority of each auto insurance premium dollar.

STATE REGULATORY STRUCTURE FOR FAIRNESS, ANTI-DISCRIMINATION AND CONSUMER PROTECTION

Every state and territory of the United States has legislated the same foundational standard and prohibited rates that are “excessive, inadequate or unfairly discriminatory.” Fundamentally, this means that insurance rates must be risk-based and that similar risks must be treated similarly. In this way, the “excessive, inadequate or unfairly discriminatory” standard balances “fairness” for policyholders and “solvency” for the industry, both of which are essential for healthy and competitive markets. In other words, whether rates are “excessive” is determined based on the risk of loss individual policyholders present and the focus is on “fairness in pricing”. Whether rates are “inadequate” is likewise determined based on individual policyholders’ projected risk of loss with the focus on solvency for the insurers assuming those risks. Rates are “unfairly discriminatory”, according to the statutory standard and related cases, when they result in treating policyholders with similar risk profiles differently.

To enforce this standard, 49 of 50 states plus the District of Columbia require insurance companies to file auto insurance rates with state regulators for review and/or approval for the specific purpose of ensuring they do not violate this statutory standard. In addition, many states have enacted

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specific definitions of protected classes (such as race, religion, national origin or sexual preference) and have prohibited pricing based on those classes.

Under the current state regulatory framework, insurers create a full risk profile for each policyholder using multiple factors predictive of future losses and relying on historical data. By doing this, consumers are not harmed by reliance on a single risk factor. In contrast, H.R. 1756 give much more weight to the policyholder’s prior driving record by prohibiting the use of other factors that have been repeatedly demonstrated to be predictive of future losses. For example, a reliance solely on driving records would punish first-time drivers, immigrants, and low-income families and minorities. While helpful, driving history and driving records alone do not accurately predict the likelihood of a future accident. According to one APCIA member company, 70 percent of auto losses in its nonstandard business and 90 percent of losses on their motorcycle program involve policyholders with no record of past violations. According to the company, having a prior driving violation makes a policyholder only about 25 percent more likely to have a claim, while there are many other factors that have been proven to be more accurate predictors of loss. Adding more weight to the policyholder’s prior driving record (as both these proposals do) and eliminating the use of other factors more predictive of loss, not only harms the very consumers the proposed legislation seeks to protect, but also undermines the fairness and solvency purposes of state regulations that require rates to reflect the risk of future losses.

State statutes and regulations requiring rates to reflect the risk of future loss serve important affordability and availability purposes as well. Failing to set rates exclusively based on objective and predictive risk, would result in the following outcomes:

- Lower-risk policyholders would have to be overcharged for insurance, while others would not pay a rate commensurate with the risk they present.
  - When individuals are overcharged relative to the risk they present, some low-risk policyholders opt out of the insurance market where possible, which in turn raises prices for everyone. That, then, leads to more opt outs, which drives prices even higher, thereby continuing the downward spiral in take-up rates and threatening insurer solvency.
  - Where opting out is not possible, there are significant fairness concerns, as individuals posing lower risks are required, in effect, to subsidize riskier policyholders.
- The financial incentive for policyholders to reduce risks (e.g., obey traffic signals and signs, avoid speeding, forego texting while driving or driving while under the influence) would be reduced. When policyholders do not realize the benefit of reducing risk, they have less incentive to take actions that will.
- Where insurers lack the ability to rate risks according to specific risk-profiles, they would likely withdraw from affected lines of business, leading to less availability of insurance and less competition in the market.

As it relates to “fairness” in pricing, our public opinion research indicates consumers expect their insurance premiums to accurately reflect their individual risk of loss. And, they reject notions of

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subsidizing the premiums of other, higher risk policyholders for any reason, including for reasons of making insurance even more available.

STATE SOLVENCY REGULATION AND CONSUMER MARKET CONFIDENCE

A primary goal of state insurance regulation is to protect policyholders and the market against insurer insolvency for the purpose of paying consumers’ claims. Consideration of factors predictive of risk in setting prices is essential in achieving that goal. As part of solvency regulation, state regulators review insurers capitalization, asset quality, purchases of reinsurance, and their liquidity. The surplus produced to capitalize the business, purchase reinsurance, and facilitate overall liquidity derives not only from the return on investments, the transfer of risk to reinsurers, and other surplus preservation strategies, but also from underwriting surplus. And underwriting surplus is the premiums retained after covered losses are paid. The total underwriting surplus over a book of business produces a significant portion of the aggregate surplus that ensures solvency and, thus, the insurer’s ability to pay current and future claims. This primary regulatory concern for solvency through underwriting surplus is embedded in state insurance laws that prohibit rates that are “excessive, inadequate, or unfairly discriminatory”—the same standard that ensures fairness in pricing for consumers.

If insurers are not permitted to fully take into account actuarial risks in pricing insurance, the underpricing of risk presented by individual policyholders over time across the business would be expected to adversely impact underwriting surplus and hence solvency. Although well intentioned, H.R. 1756 will undermine the state regulatory standards that have assured solvent companies and financially sound insurance markets for the protection of consumers for more than 100 years.

Eliminating risk factors from auto insurance pricing, as H.R. 1756 would do, makes the prediction of future loss less accurate such that the charged premium for individual policyholders will not as closely match the risk the insurer assumes. As a result of this mismatch, the insurer will eventually need to consider not renewing or underwriting certain policies in order to preserve the insurer’s ability to pay claims. Eliminating risk factors would compound this effect across the insurance market and, thereby, limit availability more broadly over time.

UNINTENDED CONSEQUENCES OF FEDERAL LEGISLATION AND INTERVENTION IN STATE BASED REGULATION OF INSURANCE

H.R. 1756 is a wholesale intervention into the state-based regulation of insurance, which has succeeded in delivering well-functioning, highly competitive, and financially strong markets for more than 100 years. Additionally, the bills under consideration (and other federal legislation restricting aspects of insurance underwriting) directly undermine the work of State legislatures,

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3 Shauhin Talesh, Insurance Law As Public Interest Law, 2 UC IRVINE L. REV. 985, 1005-06 (2012) (“As articulated by most states, the goals of insurance regulation include fair pricing of insurance, protecting insurance company solvency, preventing unfair practices by insurance companies, and ensuring the availability of insurance coverage.”) (emphasis added); National Association of Insurance Commissioners, The U.S. National State-Based System of Insurance Financial Regulation and the Solvency Modernization Initiative § 2.3 (August 14, 2013), https://www.naic.org/documents/committees_e_us_solvency_framework.pdf (“The state regulatory system in the United States has had over a 100 year history of solvency regulation.”).
State regulators and the public by prohibiting factors that have been debated and supported, often by the consumers who would be directly impacted.

Each state routinely reviews rates to assure compliance with legal and regulatory standards and roughly half mandate prior approval even before a rate can be charged in the market. In addition, states engage in market conduct examinations to review and examine, among other things, the usefulness, appropriateness, and impact of certain rating factors. While a very small number of states as a result of market conduct examinations have prohibited the use of some of the factors these two bills prohibit, the overwhelming number of states continue to support and authorize their use having determined that the rating factors targeted by both bills are predictive of risk, benefit consumers and are not unfairly discriminatory.

States have routinely supported the use of risk-based underwriting factors because banning them will result in over-charging most and undercharging others, which is prohibited by state statutes as “excessive” and “inadequate” rates. Aside from the implications for insurer solvency described earlier, eliminating risk-based underwriting factors can be expected to negatively affect availability when low risk, over-charged policyholders opt-out and insurers pull back from underwriting artificially underpriced risks as a result. Insurance rates would be expected to become similar from one insurer to the next, which leads to reduced competition and fewer opportunities for consumers to improve their rates as well as fewer new entrants in the market (including technology firms) to drive innovation.

Following are some of the risk-based factors that some have advocated to prohibit in determining a consumer’s eligibility for auto insurance or in calculating the associated premium accompanied by the related consequences for consumers:

- **Gender** is a factor that generally provides a risk-based discount for younger female drivers. According to the Insurance Information Institute, statistically, women have fewer crashes generally, fewer driving-under-the-influence crashes (DUIs) and, most importantly, less serious crashes than men. All things being equal, women often pay less for auto insurance than their male counterparts. And, insurers have adjusted as states increasingly offer alternatives to binary gender identification.

- **Education and occupational status** frequently result in discounts. While some assert insurers use education and occupation as a proxy for income and penalize consumers in low-wage jobs, this is fundamentally untrue. The use of education and occupation is a proven, accurate predictor of risk and they form the basis of affinity group discounts. According to one large writer of affinity groups, both teachers and firefighters have a lower risk profile than doctors, and thereby typically receive lower auto insurance premiums. Additionally, certain professional and educational groups, such as minority chambers of commerce and construction trades, offer discounts to their members through affinity groups. As an example of on-going state review of auto insurance rating, Maryland recently

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conducted an examination of the use of education and occupation and affirmed the importance of risk-based pricing, saying their use does not violate Maryland law.5

- **Employment status**, like education and occupational status, allows for affinity group discounts for people in designated fields and its elimination would negatively affect a wide range of incomes and groups. Additionally, the use of employment is again a risk factor that is not used as a proxy for income. For example, according to a recent Insurify report, dry cleaners have better driving records than chiropractors. And police detectives have better driving records than fitness club managers.6

- **Homeownership status** allows insurers to reduce their operational costs and pass the savings on to consumers by allowing the bundling of policies.7 According to one APCIA member, it is also very predictive as a variable on its own.

- **Zip code, adjacent zip codes and census tracts** are risk-based measures reflecting different driving and other conditions that are directly relevant to the comparative risks of being in a crash or having a claim covered by the auto policy. Auto insurance is a package policy with liability, property damage and uninsured motorist coverages that for a claim require other people or property. In reality, the likelihood of a claim against any of those coverages increases when the number of people and vehicles increase. The State of Missouri in a recent study found that there are certainly differences in average rates between zip codes but that the differences reflect differences in insured costs.8

- **Marital status** has generally been used to reduce otherwise higher costs for single people.

- **Credit based insurance score or consumer report**, more fully discussed below, is a proven risk-based rating factor that serves as a discount for most policyholders. Credit scores are different from credit-based insurance scores. Credit scores measure the likelihood a borrower will repay a debt. Credit-based insurance scores measure a consumer’s propensity to file an insurance claim and the cost of such claim. Insurers are required by state law to make exceptions in credit-based insurance scores for extraordinary life circumstances.

- **Previous insurance status** can be used to estimate the driving history of a policyholder and it serves as an indication of the policyholder’s regard for insurance requirements imposed on consumers by the states (e.g., financial responsibility and rules of the road).

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Banning these factors will have a negative impact on availability of coverage—a problem that does not now exist. By allowing insurers to effectively differentiate based on the probability of future loss, the prohibited factors allow insurers to provide MORE coverage because they have a better understanding of the aggregate risk they assume. Banning these factors also penalizes consumers who are lower risks by requiring them to subsidize higher risk consumers. And, as at least one company has indicated, banning risk-related factors will likely shrink the company’s risk appetite.

To reiterate, APCIA’s public opinion research indicates that consumers expect their auto insurance premium to accurately reflect their individual risk of loss and they reject subsidizing the premium of higher-risk policyholders. Contrary to this desire, the legislation will create subsidies because premiums will be less risk-based and, as a result, a less accurate reflection of each policyholder’s risk.

CREDIT-BASED INSURANCE SCORES (CBIS) AND THE PROVEN BENEFITS FOR CONSUMERS.

CBISs are significantly different from traditional credit scores. Credit scores measure the ability and likelihood of a borrower to repay a debt. Credit-based insurance scores measure the propensity of a policyholder or an applicant for insurance to file an insurance claim and the cost of such claim. CBISs have been thoroughly researched and their relationship to risk has been demonstrated by government and private studies alike. The most extensive federal report is the 2007 FTC Report to Congress entitled, “Credit –Based Insurance Scores: Impacts on Consumers of Automobile Insurance”.9

More recently, a 2016 report entitled, “Empirical Evidence on the Use of Credit Scoring for Predicting Insurance Losses with Psycho-social and Biochemical Explanations” published in the North American Actuarial Journal found as follows: “Credit scores predict insurance losses in automobile insurance at a statistically significant level. In fact, they are among the most useful predictor variables available to underwrite and price automobile (and homeowners) insurance.”10

The introduction of CBIS corresponded with the increase in availability of auto insurance from insurance companies and a decrease in the populations of shared markets as well as pools for difficult to insure drivers established by the states. According to the 2018 NAIC Auto Insurance Database Report11 and APCIA calculations, from 2013 to 2015 (most current), the personal auto shared market liability earned exposures (vehicles) have dropped approximately 24 percent.

By considering credit-based insurance scores (along with other familiar factors such as driving experience, previous claims, and vehicle age), insurers can develop a more complete picture of a consumer’s insurance risk.

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The State of Arkansas, for example, publicly released a report in 2017 that showed 57.4% of the time that credit-based insurance scores were used in underwriting auto insurance policies, the consumer saw a decrease in premium. While 19.2% of the time, the use of credit-based insurance scores was a neutral factor and did not have any impact on the premium.  

Like Arkansas, the Vermont Insurance Commissioner in a 2016 report entitled, “A Study of Credit-based Insurance scoring for Motor Vehicle Insurance” drew a similar conclusion. “Compared to vehicles with premiums using credit-based insurance scores, the median annual premium is $219 higher when credit-based insurance scores are not used to assist with calculating premiums. If the use of credit-based insurance scores was prohibited, approximately two thirds of vehicles with premiums calculated with credit-based insurance scoring would see an increase in premium.”

Credit-based insurance scores are clearly predictive of future insured loss, even when compared to traditional factors like prior driving experience. This is true, in part, because diversions and plea bargains for traffic offenses (for example, probation before judgment) combined with the failure to report low-cost crashes under state statutory thresholds means state motor vehicle records are often incomplete. Based on the foregoing studies, if credit-based insurance scores were prohibited nation-wide, most policyholders would see premiums increase because the prediction of future risk is less accurate.

STRONG STATE REGULATION OF CBIS AND CONSUMER PROTECTION

In addition to consumer protections under federal law (including the Fair Credit Reporting Act, as amended) the use of CBISs are regulated by most states through specific state-enacted legislation based on the National Conference of Insurance Legislators’ (NCOIL) Model Act Regarding Use of Credit Information in Personal Insurance. The NCOIL model act provides the following additional consumer protections regarding insurers’ use of credit information:

- Insurers may not use a score that is calculated using income, gender, address, zip code, ethnic group, religion, marital status or country of nationality as a factor.
- Insurers may not develop a renewal rate or deny, cancel or non-renew coverage solely on the basis of credit information without an independent factor and the independent factor may not include a prohibited factor – namely, income, gender, address, zip code, ethnic group, religion, marital status or country of nationality.
- Insurers must give special consideration to people in the absence of credit information.
- Insurers may not take an adverse action unless the credit information has been calculated within the last 90 days.
- Insurers must refresh the credit information used.
- Insurers may not use the following as negative factors: credit inquiries not initiated by the consumer, insurance inquiries, collection accounts with a medical industry code, and multiple lender inquiries.
- Extraordinary life circumstances when brought to the attention of the insurer, must provide reasonable exceptions for a catastrophic event, serious illness or injury of person or


immediate family member, death of family member, divorce, identity theft, involuntary interruption or temporary loss of employment, military overseas deployment or other events.

- If the credit information is wrong, the insurer must re-underwrite or re-rate the policyholder.
- Insurers must provide upfront notification of the use of credit information.
- Insurers must provide adverse action notifications with reason codes.
- Insurers must file their scoring models with the states in which they are authorized to do business.

Even where not specifically enacted, NCOIL’s model act and its consumer protections have become the de facto standard for the auto insurance industry nationwide.

**AFFORDABILITY IS A PRIORITY WE SHARE**

As an industry, we recognize that auto insurance is regrettably unaffordable for some people. Accordingly, we work to reduce the underlying costs that make up roughly 80% of the auto insurance premium dollar (which includes claims costs like health care, auto repair and litigation-related expenses and awards). Examples of insurers’ affordability efforts include:

- Creating and supporting the Insurance Institute for Highway Safety and Advocates for Highway and Auto Safety;
- Communicating with policyholders and the general public on how to avoid crashes;
- Advocating for highway safety measures including primary enforcement seatbelt legislation, anti-texting and driving and other distractions, anti-drunk and other impaired driving laws;
- Advocating for measures to reduce medical, litigation, and repair costs; and
- Working with communities and law enforcement to reduce fraud and auto theft.

It is far better to achieve affordability via reductions in claims-related costs rather than through artificial rate constraints. The former saves lives and consumer resources while avoiding the unintended consequences of the latter.

**STATE AUTO INSURANCE MARKETS ARE WELL-FUNCTIONING BY OBJECTIVE MEASURES**

Congress has repeatedly affirmed state-based insurance regulation  and has intervened only where there was a demonstrated market failure. The auto insurance market exhibits no such indications of market failure. In fact, the personal auto insurance market as measured by relevant metrics is a well-functioning market.

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14 The 2010 Dodd Frank Act

15 The National Flood Insurance Program and/or The Terrorism Risk Insurance Act.
• **Number of Companies** – Approximately 2,300 insurers write property casualty business in the U.S. and more than half of them (1,220) provide auto insurance with a low degree of concentration, which according to the Herfindahl-Hirschman Index means the industry is close to a perfect level of competition.\(^\text{16}\)

• **Distribution Channels** – **According to an APCIA member**, there were an estimated 36,500 independent agencies in the United States in 2018, joined by thousands of captive agents combined with online and telephone sales options.

• **Complaints** – The states record far less than one complaint for every 12,000 consumer interactions.\(^\text{17}\)

• **Solvency** – The insurance industry rating agency AM Best maintained its Stable outlook for the U.S. property casualty insurance industry segment for 2019.\(^\text{18}\) And, AM Best’s latest report on company impairments in the insurance industry (incl. P/C and L/H) indicates new company impairments continue to trend lower, with only 3 impairments in 2018.\(^\text{19}\)

• **Reasonable Profits** – The 2009-2018 10-year average RONW shows the all-industry return of 13.7% is 140% higher – or 2.4 times larger – than the p-c industry 10-yr average of 5.7%; the p-c industry 10-year average RONW is 58% less than the all-industry 10-year average.\(^\text{20}\)

Our greatest concern is that the proposed legislation will disrupt and destabilize an otherwise well-functioning state insurance market, harm consumers by removing discounts, create availability problems when they do not now exist and establish the precedent for more such unnecessary and potentially harmful interventions in the future.

Critics who support the proposed bills often point to California. The rate regulatory system in California is very different from most states and it reflects public policies made under a unique combination of circumstances that led to Proposition 103. That combination of circumstances was: (a) rapidly rising costs from an increasing number of crashes and (b) court decisions that allowed the imposition of third-party bad faith damages.

The California market was disrupted for years during the transition to the new regulatory system. And, the claimed savings actually resulted from reductions in crash-related costs through highway safety and anti-fraud measures (which state regulators and insurers both supported), combined with the reversal of the most troubling judicial decisions on appeal. Perhaps most telling is this –

\(^{16}\) The Herfindahl-Hirschman Index (HHI) is a common measure of market concentration and it is used to determine market competitiveness. The U.S. Department of Justice classifies any market with an HHI under 1,500 as unconcentrated and any market with an HHI over 2,500 as highly concentrated. An HHI lower than 1,500 indicates nearly perfect competition for the targeted market. The HHI for the property and casualty insurance market is 302.2.

\(^{17}\) Lawrence S. Powell, PhD, “Big Data and Regulation in the Insurance Industry”. 2017, Alabama Center for Insurance Information and Research, University of Alabama


since Proposition 103 was adopted by California more than 30 years ago, no state has followed California’s example.

We also note that critics often use quote generation webpages to arrive at their conclusions. But while these websites may provide an initial quote for some comparison purposes, the actual premium charged may vary from the quote depending on further underwriting data to better establish the risk-based price that most accurately reflects the future risk presented by the policyholders.

CONCLUSION

State regulated auto insurance markets are characterized by financial strength, competition, inherent fairness, and consumer protection. There is no evidence at the state or national level that supports the preemption of state regulation of auto insurance, as H.R. 1756 would do.

Although well intentioned, the proposed bills will make auto insurance rates far less risk-based and outlaw factors that provide discounts for many policyholders of widely different income levels. Over the last 100 years, the state regulation that currently governs the business of property and casualty insurance has produced a framework that delivers fairness to consumers and ensures a solvent and competitive insurance marketplace, which makes insurance widely available.

Federalizing insurance regulation by restricting risk-based pricing in a fundamental way will bring about second and third order consequences that erode the fairness, solvency and availability of insurance products that state regulation has been designed to deliver. We therefore respectfully ask you to reject H.R. 1756 and the FAIR Study Act and instead work with us to address the underlying causes of unaffordability wherever and for whomever they exist.