REPORT OF COMMISSIONER, KEVIN M. MCCARTY

FLORIDA OFFICE OF INSURANCE REGULATION

THE USE OF OCCUPATION AND EDUCATION AS UNDERWRITING/RATING FACTORS FOR PRIVATE PASSENGER AUTOMOBILE INSURANCE

MARCH 2007

EXECUTIVE SUMMARY

The Office of Insurance Regulation ("Office") held a public hearing on February 9, 2007 in Tallahassee to review the use of occupation and education as underwriting or rating factors for private passenger auto insurance and its potential impact on Floridians.

In Florida, as well as nationally, the insurance industry has had a checkered past in its use of race and other proxy factors that intentionally or unintentionally negatively impact minorities and low-income individuals. While the use of race as a rating factor was outlawed in Florida, the two factors mentioned above, occupation and education, have emerged in the rating and underwriting of auto insurance and appear to be highly correlated to race and income-level.

Under some rating plans, consumers with more professional occupations (doctors, lawyers, architects), and advanced college degrees are being offered preferred driver rates. Conversely, individuals with blue-collar jobs, and a high school education or less are paying higher premiums for similar risk factors, as exhibited by several online quotes for auto insurance requested by the Office from one of the major auto insurance writers in Florida. With all other factors remaining equal, except for changes to the online applicant's education and occupation, the results were startling. One online quote comparison demonstrated a significant difference in the quoted auto insurance rate when the two factors are adjusted, accounting in that instance in a 300% higher rate for the less educated and less skilled applicant.

Testimony at the public hearing on February 9, 2007, and documents received and reviewed prior, during and after the hearing reveal:

- ***There is a demonstrable correlation between occupation, education and income-level and ethnicity, which was not disputed by the insurance industry.***

- ***Insurance industry representatives all claim ignorance of the relationship between occupation, education and income-level and race despite the existence of publicly available U.S. Census Bureau Data***

- ***Insurers do not collect data from consumers on race or income-level, and refuse to study the impact of underwriting practices on minority and low-income consumers.***

- ***The insurance industry does not believe that corporate responsibility extends to ensuring its practices do not disparately impact minority or low-income Floridians; but instead maintains that it is the Florida Legislature's responsibility to define public policy on this matter in the insurance marketplace.***

- ***It appears that wealthier individuals are more likely to pay small claims out-of-pocket, and avoid making insurance claims, giving some occupations better loss ratios despite higher accident rates.***

- ***As measured by one company's use of occupation and education the magnitude of the premium difference can be very significant.***

- ***Companies that do not use occupation and education as rating factors may potentially be at a competitive disadvantage because they may lose the wide range of business offered by higher income policyholders. Foregoing whatever predictive value these factors may have might also put these companies at a disadvantage. Thus, from an economic point of view, this practice is likely to proliferate regardless of its negative effects on policyholders struggling to overcome disadvantages.***

- ***While the prohibition of the use of these factors, much like in the prohibition of the use of race, could lead to some economic inefficiencies in insurance markets, it may be beneficial to the overall economy and citizenry to prohibit use of these factors as a matter of public policy***

- ***At least one major auto insurer that currently uses education and occupation as part of its underwriting, asserts it would absolutely not use these factors if it were determined the factors had a disparate impact on protected classes.***

- ***A national insurance organization whose members write 56 percent of the private passenger auto insurance market in Florida stated that a public policy concern can override the use of these factors even if there is an actuarial basis for it.***

The transcript of the public hearing held on February 9, 2007, consisting of two volumes, is attached to this Report as **Exhibits 1 and 2**.

Background on the Use of Education & Occupation as Rating Factors

One of Florida's greatest strengths is its rich culture and ethnically diverse population. Regrettably, Florida has another history: one of slavery, Jim Crow laws, as well as discrimination that led to the modern civil rights era. This willful discrimination was pervasive and permeated the institutions of education, government, and commerce --- even the insurance industry. While Florida leaders have since prohibited the use of factors such as race in determining employment and housing decisions, some vestiges of discrimination remain.

In 2000, the National Association of Insurance Commissioners ("NAIC") initiated a Race-Based Premium Working Group to examine the use of race-based premiums for life insurance. The Office was an active participant in this endeavor, which included a questionnaire to all life insurance companies nationwide about past practices. This ultimately resulted in several multi-state market conduct examinations, and multi-million dollar settlements to correct past wrongdoing.

The review period varied based on the company, but usually encompassed 1900-1970, although many policies were still "on the books." The findings were disturbing. Historically several life insurance companies bifurcated rate tables for "Caucasian" and "not-Caucasian," charging higher rates for non-Caucasians. Company documents offered a very interesting defense for this policy: they claimed this was not discriminatory, but merely reflected the statistical differences between life expectancies for Caucasians versus non-Caucasians. Although there may have been some validity to this statement, the insurance industry does not exist in a moral, ethical, or historical vacuum. Despite this "actuarial justification," legislatures around the country banned the use of race regardless of the statistical reasoning.

In reaction to these changes, some companies adjusted their underwriting standards in an unexpected manner: they began to use other factors that served as proxies for race and income status. The two most notable factors included education and occupation.

According to one multi-state examination report concluded by Maryland[1], after the race question was deleted from the application in the 1960s, several companies "appeared to use occupation as a substitute for race." ***Occupations subject to substandard rating included maids, bootblacks, busboys, car wash workers, garbage or ash collectors and janitors.*** The multi-state reported noted, "Non-Caucasian workers were disproportionately represented in the [these] disadvantaged occupations."

The report further compared rating books before and after race was removed from the application and noted:

1) The rating books removed race from the rating methodology, and
2) Occupational Rating Classification replaced the use of race, and
3) No other changes were made.

Both the company and regulators agreed the company engaged in "socio-economic underwriting." All four states involved in the examination, Maryland, Florida, Pennsylvania and Virginia believed there was enough evidence to conclude that the use of occupation in this instance violated all four states' statutes regarding non-discriminatory practices.

In a similar examination conducted by the State of Ohio a rating book for Cooperative Life Insurance Company[2] (CLIC), not only was there ***a substandard rating for occupations like butlers, barbers, valets, cooks, elevator operators and waiters — but the rating book warned against, "low-grade industrial or illiterate types."***

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[1] The State of Florida, Pennsylvania, and Virginia also joined this examination. Monumental Multi-State Exam Report # 789-00 (Maryland).
[2] Actuarial Report – Race Based Pricing Activities with Respect to the Life Insurance Business of Nationwide Life Insurance Company, July 6, 2004 – State of Ohio.

The Use of Occupation and Education as Rating Factors Continues

The presumption that the use of occupation and education as rating factors ended with the conclusion of the aforementioned life insurance industry multi-state examinations is erroneous. The venue, however, has changed --- to the underwriting and rating of private passenger auto policies.

On March 20, 2006, the Consumer Federation of America ("CFA") issued a press release warning that the nation's fourth largest auto insurer, GEICO, was using occupation and educational attainment to rate auto insurance policies, and that Liberty Mutual Insurance and Allstate Insurance were beginning to use these rating factors as well. J. Robert Hunter, Director of Insurance for CFA, and the former Insurance Commissioner for the State of Texas, challenged state insurance regulators to ban the use of education and occupation for rating policies as these factors are highly correlated with race and income level.

In response, The Property Casualty Insurers Association of America (PCI), a trade association that represents 1,000 member companies that write roughly 40% of the nation's property & casualty business issued its own press release on March 21, 2006. The PCI defended GEICO's use of education and occupation as "valid factors for insurers to use in the marketplace."

As early as 2004, the Office began taking active measures to have auto insurers remove the occupation and education variables from the insurers' underwriting/rating plans used in Florida. In 2004, as a condition of "approving" a filing, those auto insurers using either occupation or education, or both factors, in their underwriting plans were advised to cease doing so within 1 year.

In response to these measures taken by the Office, AIG, in a letter dated May 5, 2004, expressed that AIG "is amiable to remove this factor [occupation] from our scoring models contingent on the following conditions: The [Office] promulgate a Regulation that requires all personal automobile writers to stop using the occupation factors at the same time, or, all carriers using this factor have agreed to remove the factor within the same time frame."

While Florida law specifically outlaws the use of race for rating insurance policies, there is no specific statutory prohibition against using potential proxy factors that are highly correlated to race, such as educational attainment and occupation that would create a disparate impact on racial minorities and low income Floridians.

Section 627.917, Florida Statutes, states that the Financial Services Commission can establish a uniform statewide risk classification reporting system for auto policies provided it does not discriminate based upon race, creed, color or national origin. Pursuant to this private passenger auto risk classification reporting system statute: "The classification system may include any difference among risks that can be demonstrated to have a probable effect upon losses or expenses …"

The insurers that have begun to use occupation and/or education as rating factors claim these factors are predictive of losses, and thus are not prohibited by Florida Statute, regardless of the potential impact. The auto rating statute states that rates are not unfairly discriminatory with respect to a group even though they are lower (and, by implication, higher) than rates for nonmembers of the group. Rates are only unfairly discriminatory if they clearly fail to reflect equitably the difference in expected losses and expenses or if they are not actuarially measurable and credible and sufficiently related to actual or expected loss and expense experience of the group to assure that nonmembers of the group are not unfairly discriminated against. It is this definition that governs the Office's determination of whether a rate is unfairly discriminatory.

THE PUBLIC HEARING ON THE USE OF OCCUPATION AND EDUCATION AS RATING FACTORS FOR PRIVATE PASSENGER AUTO INSURANCE

The Florida Insurance Commissioner, through a Notice of Hearing to the industry, as well as subpoenas directed to auto insurers currently using occupation and education as rating factors, compelled testimony from the industry, consumer advocacy groups, and from the public to explore this issue, and the rationalization underlying the use of these factors. Members from four insurance groups testified including GEICO, Liberty Mutual, the AIG Insurance Group, and New Jersey CURE Auto Insurance. In addition, members from insurance trade organizations including the Property and Casualty Insurance Association of America (PCI), the Consumer Federation of America, the National Association of Mutual Insurance Companies (NAMIC), the Insurance Information Institute (III), the Florida Insurance Council, the Florida Justice Association, and Florida's Consumer Advocate also testified.

The issue is simple: allowing the use of occupation and education as rating factors appear to disproportionately favor non-minorities and higher-income individuals while negatively impacting minorities and low-income individuals by charging these groups, albeit somewhat indirectly, higher auto-insurance rates relative to others with similar risk characteristics.

Following the Office's attempts in 2004 to have automobile insurance carriers in the state remove the two factors, the Office began monitoring this trend, and has recently been very specific in not "approving" the rate filings that use the two factors at issue, but instead, warning companies that although the Office is concerned about the impact of these practices, it does not have statutory authority to deny these practices. While the Office has not "approved" these plans, it had no other recourse under current statutes and rules but to allow them to come into effect due to the deemer provisions of the law.

This issue also has gained national attention following the Consumer Federation of America's letter to all insurance commissioners explaining its research regarding

GEICO's practices. In 2006, Commissioner McCarty commissioned an internal study of the correlation between education/occupation and ethnicity and income, which found strong correlations, ultimately concluding that logically any plan that utilized these factors would negatively impact minorities and low-income individuals.

Prior to the public hearing, the Office identified eight main investigatory questions to understand these issues:

1. Is there a correlation between occupation/education and race and/or income status?
2. Is the insurance industry aware of such correlation between occupation/education and race or income?
3. Does the insurance industry believe its corporate responsibility extends to ensuring its policies do not negatively impact people due to race or income-level?
4. Has the insurance industry researched the impact of its practices on Floridians as it relates to minority or low-income individuals?
5. Is there a correlation between occupation/education and loss ratios and or accident statistics?
6. If it is demonstrated the use of occupation and education negatively impact protected classes, what is the magnitude of this impact?
7. If the Florida Legislature does not change the laws, and this practice is allowed to proliferate, what will be the potential impact on the auto insurance industry?
8. If these factors were not allowed for underwriting factors, would the auto insurance industry still be competitive?

THE CURRENT USE OF OCCUPATION AND EDUCATION AS RATING FACTORS

Even before the eight investigatory questions are explained, it is important to understand how the industry is currently using occupation and education. Although a few industry representatives stated broadly, "they have been using these factors for years," the current incarnation of the usage of these factors is a relatively new phenomenon, and is utilized in different forms by three auto insurers in Florida that collectively write approximately 17.1% of the auto insurance market in Florida, insuring over 1.9 million vehicles.

The testimony elicited the forms of current use, and revealed several critical facts. It is important to understand that these factors can be used in two different phases: (1) Underwriting --- which is to determine whether to insure the individual; and (2) Rating –

which is to determine the actual premium paid by the customer. During this investigation, the Office learned about another practice, which is a blending of underwriting and rating, the practice of "tiering"

GEICO utilized "tiering" most directly, and this report will use this company's experience as an example. Currently GEICO has four companies that operate in the State of Florida: Government Employees Insurance Company (which is the origin of the name "GEICO" but does not technically incorporate that acronym), GEICO General, GEICO Indemnity, and GEICO Casualty. During the underwriting phase, a customer will apply for coverage on-line or via a telephone operator, and believes they are applying for coverage from "GEICO." Based on the underwriting criteria (including occupation and education), customers are placed into different companies. The preferred-risk customers are placed into Government Employees Insurance Company or GEICO General (with the lowest rates), the intermediate-risk customers are placed into GEICO Indemnity, while the sub-standard risk customers are placed into GEICO Casualty. Based on GEICO's placement statistics, it appears that customers gaining the preferred status (and lowest premiums) are far more common:

GEICO Coverage in Florida, 2006

Company	# of Insured Vehicles	Avg. Annual Premium
GEICO /GEICO General	990,262	$938.70
GEICO Indemnity	174,823	$1,183.70
GEICO Casualty	110,613	$1,474,90

It also appears that GEICO is not equally receptive to all segments of the population (favoring those with higher education and better occupational status). During the testimony, the Office learned that customers are usually not informed they were rejected for the preferred company (Government Employees Insurance Company or GEICO General), and placed into another company.[3]

[3] GEICO is currently defending itself against a lawsuit filed in 2006 in federal court by several African-Americans who were either former or current GEICO policyholders, alleging that the use of education and

Liberty Mutual has two companies writing auto insurance in Florida, Liberty Mutual Insurance Co. (the preferred company with lower rates), and Liberty Insurance Co. (sub-standard risks and higher rates). In the initial determination, occupation, employment status, and education are determinants for being offered coverage from Liberty Mutual Ins. Co. In response to direct questioning during the public hearing, Christopher Cunniff, VP of Personal Marketing, stated, "Yes, it is possible that some small segment of customers, the use of that variable [education and occupation] does push their slotting decision from one company to another."[4] However, once in the insurance companies, education and occupation are not used as rating factors by the Liberty Mutual Companies. This contrasts with GEICO, where further tiering decisions are made within each company.

One potential problem of this "slotting" technique is that individuals may be "parked" in the substandard risk company. Even if a person achieves a higher level of education, or changes to a more preferred occupation, they can only switch companies after three years, "if they are clean," remarked VP Cunniff.[5]

The American International Group, Inc. ("AIG") Companies use occupation, but do not use education in their underwriting and premium practices. While AIG does have three auto insurers writing in Florida, AIG does not use the same type of "tiering" techniques used by GEICO and Liberty Mutual, but places customers based on their distribution channels. However, within their underwriting tiers (which ultimately affects rating and premiums), occupation is used as a determining factor.

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occupation factors are discriminatory or have a discriminatory impact, Patricia Amos, et al. v. GEICO, U.S. District Court for the District of Minnesota, Case # 06-cv-1281. Transcript of public hearing, Volume 1, page 81, lines 2 – 14; Vol. 1, page 88, lines 8 – 13. GEICO states the allegations are "absolutely baseless".

[4] Transcript of public hearing, Volume 1, page 97, lines 14 – 17.
[5] Vol. 1, page 97, lines 23 – 25.

The Office is vested with the responsibility to ensure rates are not "excessive, inadequate, or unfairly discriminatory,"[6] and it appears that these underwriting and rating factors will *prima facie* result in higher premiums for those who can least afford it: lower-income, and less educated individuals.

I. IS THERE A CORRELATION BETWEEN THESE FACTORS AND RACE AND/OR INCOME STATUS?

Although racial differences between education and occupation have narrowed since the "Jim Crow" period examined during the race-based life insurance premiums initiative --- a wide gap still exists.

The U.S. Census Bureau conducted a comprehensive study of race/ethnicity and occupation in for its *Selected Occupational Groups by Race and Hispanic Origin for the United States, 2000.* The table below, based on U.S. Census Bureau Data, shows disparities among the types of jobs by different races & ethnicities:

Category	Management, Professional, & Related Occupations
Caucasian & Asian*	**37%**
Black/African American	**25%**
Hispanic or Latino**	**18%**
American Indians, Native Alaskans, Hawaiians, & Pacific Islanders	**24%**

* *Non-Hispanic*
** *Any Race*

Although this is national data, we can still observe dramatic differences: Caucasians and Asians are twice as likely as Hispanics to have management or professional jobs.

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6 Section 627.0651, Florida Statutes.

The chart below, based on data from he U.S. Census Bureau, shows educational attainment also has large disparities across ethnic and racial groups in Florida:

Bachelor's Degree or Higher
Florida, 2005

Category	Percent with Degrees
Caucasian & Asian*	**29%**
Black/African American*	**13%**
Hispanic or Latino**	**21%**

** Non-Hispanic*
*** Any Race*

Source: U.S. Census Bureau: Educational Attainment of the Population 18 Years and Over, by Age, Sex, Race Alone, and Hispanic Origin, for the 25 Largest States: 2005

Unlike the occupational data, this is Florida specific data, and also shows large disparities: Caucasian and Asian non-Hispanics are more than twice as likely to have a college degree as Blacks/African Americans.

For both occupation and education, as a group, Caucasians and Asians are more likely to have professional and managerial jobs, as well as college degrees. Not only would utilizing these factors negatively impact minorities (as a group), but also using a combination of these factors may magnify the "inequality effect."

II. IS THE INSURANCE INDUSTRY AWARE OF SUCH CORRELATION BETWEEN OCCUPATION/EDUCATION AND RACE OR INCOME?

Although one may think it is "common knowledge," that there are inequalities in America that contribute to minorities being less likely to obtain college degrees, or have higher incomes, shockingly the representatives of the insurance industry claim to be oblivious of such a relationship. In fact, at times the public hearing was reminiscent of hearings involving the tobacco industry where tobacco lobbyists claimed there were no studies proving tobacco use caused cancer.

Asked pointedly by Commissioner McCarty whether the use of occupation and education would disparately impact protected classes of minorities, Hank Nayden, VP and General Counsel for the GEICO group answered, "…to our knowledge, there is no credible data and no credible study reflecting that."[7] Later in the testimony, Commissioner McCarty asked the same witness if he has looked at the U.S. Census Bureau data on this relationship between occupation and race, Mr. Nayden conceded, "I have not."[8]

The Commissioner again emphasized this question with representatives testifying on behalf of Liberty Mutual. Asking whether the company had looked at U.S. Census Bureau data regarding the relationship between occupation, education, and race and/or income, Christopher Cunniff, VP of Liberty Mutual's Personal Marketing admitted, "I have not, and I'm not aware of anyone at Liberty who has."[9]

Similarly, during the questioning of AIG company representatives, when asked by Deputy Commissioner Belinda Miller about studies showing relationships between occupation and income or race, Mr. Fedak VP of AIG Direct's Southeast Region, answered, "I'm not aware of any studies, other than analyzing our own book of

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7 Vol. 1, page 38, lines 7 - 10.
8 Vol. 1, page 50, line 24.
9 Vol. 1, page 101, lines 23 – 24.

business."[10] Further questioning revealed that since AIG does not collect data regarding ethnicity or income, no such relationship studies could be performed based on their book of business.

The industry's denial of knowing about the statistical correlations between education, occupation and race and/or income strained credulity, Steve Parton, General Counsel for the Office asked rhetorically whether this was "willful blindness" by the industry. However, it should be noted that CFO Eric Poe of New Jersey CURE Auto Insurance Company committed to not using this factors stated:

> ***"...for an entire industry that is predicated on how smart we are, we would be probably the dumbest industry in the world not to know that those statistical correlations exist."***[11]

III. DOES THE INSURANCE INDUSTRY BELIEVE ITS CORPORATE RESPONSIBILITY EXTENDS TO ENSURING ITS POLICIES DO NOT NEGATIVELY IMPACT PEOPLE DUE TO RACE OR INCOME-LEVEL?

Based on the testimony presented February 9, 2007, the simple answer appears to be "no."

During his testimony at the public hearing, Alex Hageli of the Property & Casualty Insurance Association of America (PCI) stressed that as long as the outcomes are actuarially based, the insurance company should be allowed to use it. . Moreover, when asked about disparities in outcomes and whether that should be allowed he stated, "I believe that's a question the Legislature needs to address."[12]

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[10] Vol. 2, pages 160 – 11, lines 25 and 1.
[11] Vol. 1, page 33, lines 14 – 17.
[12] Vol. 2, page 128, lines 15 –18.

When asked to contemplate hypothetical variables like eye color, cell phone usage, the number of plasma TVs in the household or birth order, Mr. Hageli answered plaintively, "If there's an actuarial basis for it, it should be used unless there is some overriding public policy concern"[13] Later when asked pointedly about the use of race in rating life insurance (as it was conceded African-American's have lower life expectancies than Caucasians), Mr. Hageli implied it could be used, "Except for the fact that it's prohibited by law."[14]

Other industry representatives did not go this far. Commissioner McCarty asked GEICO representatives, "If, in fact, it were determined, hypothetically, that it [using occupation and education as rating factors] had a disparate impact on protected classes, would GEICO continue to use it?"[15] Mr. Nayden of GEICO responded, "absolutely not."[16] However, after presented with U.S. Census data showing disparities, Mr. Nayden seemed unconvinced of the relationship: "And to our knowledge, there is no credible data and no credible study reflecting that [disparate impact]."[17]

When Commissioner McCarty asked the same question of Liberty Mutual's representatives: "If education and occupation criteria used in underwriting or rating were shown to have a disparate impact on protected classes of people …would your company continue to use it?"[18] Mr. Cunniff of Liberty Mutual waffled: "Well that's a hypothetical question which I can't answer, and certainly we wouldn't comment in advance on business plans with our company."[19]

While they too did not specifically state it is the companies' responsibility to understand these relationships, the AIG companies were less vociferous in defense of this practice. Mr. John Fedak, VP of AIG Direct's Southeast Region summarized their companies' position: "…if the OIR requires insurance carriers to remove occupation from the rating

[13] Vol. 2, page 135, lines 17 – 21.
[14] Vol. 2, page 141, lines 13 – 14.
[15] Vol. 1, page 37, lines 20 – 23.
[16] Vol. 1, page 37, line 24.
[17] Vol. 1, page 38, lines 7 – 8.
[18] Vol. 1, page 101, lines 3 – 8.
[19] Vol. 1, page 101, lines 9 – 12.

process, our tiering model will be revised and will become less accurate in predicting losses."[20]

In summary, the industry does not seem to believe that it is within their corporate responsibility to ensure that rating and underwriting practices do not negatively impact society, as long as the practices have actuarial justification. Instead, it is the perception of the industry that this is a public policy question, and it is the responsibility of the Florida Legislature and regulators --- not the insurance industry to ensure these practices do not negatively impact society.

IV. HAS THE INSURANCE INDUSTRY RESEARCHED THE IMPACT OF ITS PRACTICES ON FLORIDIANS AS IT RELATES TO MINORITY OR LOW-INCOME INDIVIDUALS?

The insurance industry professes ignorance as to the relationship between occupation, education and income-status or race, and believes it is the Florida Legislature's responsibility, not that of the industry, to determine what factors are inappropriate. Given these facts, it should not be surprising the industry has not researched this question. It has not.

Yet what is surprising is the industry has established a mechanism that makes it impossible for any auditor to research this specific information by intentionally never collecting any relevant data. While the industry portrays this as the moral high road because policyholders may be offended by being asked information about income or race, it uses the resulting ignorance to claim that anything it may do cannot possibly be discriminatory because it does not even have race or income information. The argument confuses intent with results but sounds appealing at first.

The State of Florida application for employment asks the ethnicity and age of the applicant on a voluntary basis for information purposes (to ensure non-discrimination),

[20] Vol. 2, page 155, lines 1 – 4.

while mortgage companies and credit card companies routinely request income information. Insurers make hyperbolic statements such as, "No study has shown our policies have a disparate impact". Such statements are true by tautology --- no study can be conducted without the information of the race and income level of the applicant.

This opinion was most passionately advocated by Mr. Nayden of GEICO who stated, "There is no study that finds that the use of education or occupation as a risk selection characteristic has an adverse impact on minorities or low income individuals."[21] Yet, when asked whether GEICO could collect and/or analyze this data to determine potentially negative impacts, Mr. Nayden responded emphatically, "We have no interest in collecting or analyzing any data on race."[22] This comment was echoed by Mr. Cunniff of Liberty Mutual: "Liberty does not ask or measure or track either income or race, so we have no internal studies …"[23] We may observe that no external studies are possible either, given that the entities in control of the information desire to remain blissfully ignorant.

To demonstrate the nexus between occupation groups and income level, Eric Poe of the CURE New Jersey Auto Insurance showed that GEICO's rating manual offered the worst (highest premium) category for military personnel in Pay Grade E-4 or lower, which equates to someone earning less than $24,000 a year.[24] Based on GEICO's 2004 rating manual filed with the Office of Insurance Regulation – this is correct.

In response Mr. Nayden remarked the Office has "an old underwriting guideline," but the newer guidelines do not use military pay grades.[25] However, upon further questioning by Susan Dawson, Assistant General Counsel with the Office, Mr. Nayden admitted GEICO currently uses military rank, which is highly correlated to income level within the military.[26]

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[21] Vol. 1, page 46, lines 5- 8.
[22] Vol. 1, page 38, lines 20 – 22.
[23] Vol. 1, page 113, lines 17 – 21.
[24] Vol. 1, page 22, lines 9 – 23.
[25] Vol. 1, pages 41 - 42.
[26] Vol. 1, page, 42, lines 22 – 25, and page 43.

The industry's position is that using education and/or occupation is "blind" based on race or income. Yet, without collecting any data on this issue, the impact itself must remain invisible. Some of the occupations in GEICO's preferred auto group include doctors, lawyers, and engineers while those in the lowest rating categories include blue and gray-collar workers, service and long-haulers, it is difficult to fathom how their policies could not produce a negative impact on disadvantaged groups.

While the Office agreed that collecting information about race and income could be perceived as offensive, minorities and low-income individuals may be equally offended to learn much larger proportions of them are paying higher rates than the majority racial group and higher income white-collar professionals, and are being rejected by the preferred companies within an insurance group without their knowledge.

V. IS THERE A CORRELATION BETWEEN OCCUPATION/EDUCATION AND LOSS RATIOS AND OR ACCIDENT STATISTICS?

Underlying the industry's entire argument is a statistical correlation between occupation, education and auto loss ratios. Representatives from AIG were even more specific, in that by using multivariate regression analysis, there is an *independent* relationship between occupation and auto loss ratios, which can be demonstrated when other factors are held constant. Regrettably, these data cannot be reviewed in this report as some of this involves proprietary information.

During the public hearing, Attorney Susan Dawson elicited testimony from representatives from GEICO regarding a 2003 study completed by Quality Planning Corporation, a division of Insurance Services Office, Inc. (ISO). This study showed that several white-collar careers had higher risk for an accident:

2004 Quality Planning Corporation Study
Accidents Per 1,000 Per Year

Rank	Occupation	Accidents per 1,000
# 1	Student	152
# 2	Medical Doctor	109
# 3	Attorney	106
# 4	Architect	105
# 5	Real Estate Broker	102
# 6	Enlisted Military	99
# 7	Social Worker	98
# 8	Manual Laborer	96
# 9	Analyst	95
# 10	Engineer	94

Many of these occupations including medical doctor, attorney, architect, and engineer appear in GEICO's most preferred rating class.

When asked to explain this apparent discrepancy, Mr. Hageli of PCI speculated that certain jobs may require travel at unusual hours, or be subject to greater distractions (including cell phone usage) causing a greater risk of accident.[27] When pressed for an example, he gave a real estate broker. Yet, Mr. Hageli's explanation seemed unconvincing, as high cell phone usage by attorneys, doctors, and real estate brokers should make their premiums higher --- not lower.

A better explanation was presented by Eric Poe of New Jersey CURE Auto Insurance who stated, "Studies have shown up to 50 percent of eligible claims are not even reported to insurance companies because of the fear that their rates will go up. Unfortunately, lower income individuals do not have the ability to make that choice."[28] For evidence, Mr. Poe cited a report by the 1998 Joint Economic Committee from the U.S. Congress.

Paul Lavrey, actuary for GEICO, agreed stating that "our experience would be based on what we know about, which is the losses that are reported." Moreover, "I'm sure some

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[27] Vol. 2, page 126, lines 21 – 25.
[28] Vol. 1, page 14, lines 7 – 9.

claims aren't reported and we don't know about them so we wouldn't have that."[29] Regarding the number of claims that are not reported Mr. Nayden added, "We're not aware of a study, but we would certainly like to review it, if you have one."[30] Mr. Cunniff, of Liberty Mutual, did try to offer a better defense of this stating that many auto claims are third party claims that would be difficult to nonreport, moreover, there are some legal requirements that require multi-car accidents to be reported.[31]

Yet the end result is the same, assuming both the industry studies showing preferred white-collar jobs like doctors, lawyers and architects, have lower loss ratios, yet according to Quality Planning's study have greater amounts of car accidents, it does appear there is some "self-insurance." Basically, wealthier consumers are paying lower-amount claims out-of-pocket rather than filing claims.

VI. IF IT IS DEMONSTRATED THAT THE USE OF OCCUPATION AND EDUCATION NEGATIVELY IMPACT PROTECTED CLASSES, WHAT IS THE MAGNITUDE OF THIS IMPACT?

Another factor is the amount of the effect. Even assuming occupation and education are accurate predictors of auto loss ratios, and that industry data has roughly similar experience in this regard, it does seem odd that the variations among insurers are of such a significant magnitude, especially given its actuarial basis.

AIG Company representatives (which use only occupation, not education) assert the differences are not significant: "There's a potential in certain extreme circumstances for a person's tier that they're assigned to move by two tiers based on the occupation variables, and that would result in approximately a 30 percent rate difference."[32] When

[29] Vol. 1, page 77, lines, 16 – 22.
[30] Vol. 1, page 78, lines 8 – 12.
[31] Vol. 1, page 109, lines 11 – 20.
[32] Vol. 2, page 168, Mr. Bowman's testimony.

asked specifically whether it could be higher, Mr. Fedak stated, "That would be a maximum."[33]

While the Liberty Mutual testimony focused on other areas, the GEICO testimony elucidated several interesting numbers regarding differences in occupation, education, and its affect on premiums. One of the reasons GEICO is easy to analyze is that it has an interactive rate estimator on its website which can be used to see the effect of specific occupations and education levels while holding other demographic information constant. The Office of Insurance Regulation presented three comparisons:

	High School/ Blue-Collar	Advanced Degree/ Professional	% Difference
Comparison 1[34]	$4,225.36	$1,403.59	201%
Comparison 2[35]	$884.84	$714.04	24%
Comparison 3[36]	$1,027.29	$1,280.79	25%

Eric Poe of New Jersey CURE Auto Insurance stated the differences varied by as much as 50-70%, although in some cases the difference could be as much as 200% as in Commissioner McCarty's example.[37]

While GEICO representatives seem to imply these were isolated incidents, interestingly a reporter from the St. Petersburg Times conducted his own research on his vehicle, comparing the rates for "Bob" --- a 50 year-old janitor with no high school education, and "Joe" a Ph.D. computer executive attempting to insure the same 2002 Toyota Camry in

[33] Vol. 2, page 168, line 6.
[34] Example included a single male, age 23, living in Hialeah, with a 2000 Chevrolet Malibu LS, 4 door sedan, Drives up to 15,000 miles a year, one speeding ticket, no accidents within 3 years. BI limits $15,000/$30,000; PD $10,000; PIP $10,000 with $250 deductible; UM: $15,000/$30,000; non-stacked, Comprehensive $500 deductible, Collision $500 deductible. Six-month policy.
[35] Example included a single male, age 25, living in Jacksonville, with a 2005 Honda Accord, 4-door sedan, Drives up to 15,000 miles a year, one speeding ticket, no accidents within 5 years. BI limits $25,000/$50,000; PD $25,000; PIP $10,000 with $0 deductible; UM: $25,000/$50,000; non-stacked, Comprehensive $500 deductible, Collision $500 deductible. Six-month policy.
[36] Example included a single male, age 24, living in West Palm Beach, with a 2002 Buick Park Avenue, 4-door sedan, Drives up to 15,000 miles a year, one speeding ticket, no accidents within 3 years. BI limits $15,000/$30,000; PD $10,000; PIP $10,000 with $250 deductible; UM: $15,000/$30,000; non-stacked, Comprehensive $500 deductible, Collision $500 deductible. Six-month policy.
[37] Vol. 1, page 12, lines 7 – 11.

the Tampa area.[38] His results: Bob the janitor would be pay premiums 66% higher for the exact same vehicle.

While GEICO claims their models incorporate up to 27 factors, it does appear that some factors are given greater weight than others --- and that education and occupation factors may be more important than miles driven, marital status or age in calculating an insurance premium.

VII. IF THE FLORIDA LEGISLATURE DOES NOT CHANGE THE LAWS, AND THIS PRACTICE IS ALLOWED TO PROLIFERATE, WHAT WILL BE THE POTENTIAL IMPACT ON THE AUTO INSURANCE INDUSTRY?

The problem is simple: if occupation and education are truly predictors of loss, the companies that do not adopt these practices are at a competitive disadvantage vis-à-vis insurance companies that do adopt this practice.

The most pervasive use of this practice is currently that of GEICO, which is the third largest private passenger auto writer in Florida, and the fourth largest writer in the United States.[39] In a statement to the Commissioner and the panel, Mr. Cunniff of Liberty Mutual observed, "I would say that as a general rule we are aware of what competitors are doing."[40]

In their defense, Mr. Nayden of GEICO used as evidence GEICO's double-digit growth and that "the company's growth across all occupations and educational levels give the lie to any notion that certain individuals are being harmed by our underwriting practices."[41] The fact that nearly 1 million policyholders are in GEICO's preferred company, while less than 300,000 have policies with the substandard companies casts serious doubt on

[38] "GEICO Gives Different Rates for Drivers Depending on their Jobs," St. Petersburg Times, Robert Trigaux, February 12, 2007.
[39] Vol. 1, page 35, lines 15 – 17.
[40] Vol. 1, page 119, lines 23 – 25.
[41] Vol. 1, page 48, lines 9 – 15.

this assumption --- while all companies may be growing, GEICO companies appealing to those with higher occupation and more professional occupations seem to have achieved greater market penetration.

In his testimony, Eric Poe stated about CURE New Jersey Auto, "…we [the insurance community & state government] have to make moves to ban the use of this or we are going to be compelled to adopt this rating practice."[42] The Consumer Federation of America voiced its agreement, "…GEICO's continued use of the education and occupation criteria will lead to negative competition in the insurance marketplace and that it will encourage GEICO's competitors to follow suit, because those competitors will see that GEICO is taking away their more affluent clients."[43]

Based on the testimony provided, it would appear that auto insurer's use of these factors is poised to increase. These factors, could lead proliferate within the auto insurance industry, in much the same way that the use of race as an underwriting factor became pervasive throughout the life insurance industry between 1900 to 1970.

VIII. IF THESE FACTORS WERE NOT ALLOWED FOR UNDERWRITING FACTORS, WOULD THE AUTO INSURANCE INDUSTRY STILL BE COMPETITIVE?

Other than having predictive value, the main argument for the inclusion of education and occupation as rating factors is the concept of competition. Perhaps best articulated by Dr. Robert Hartwig of the Insurance Information Institute, "…a system of rates that accurately reflects risk and costs is fair and it is equitable. States that restrict actuarially valid underwriting criteria implicitly subsidized drivers with relatively poor records at the expense of the state's better drivers."[44]

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[42] Vol. 1, page 10, lines 7 – 18.
[43] Vol 2, page 149, lines 7 – 12.
[44] Vol. 2, page 193.

Even more dramatically, representatives from PCI stated this will lead to overall price increases: "When you have less competition, you have less market forces forcing prices down," Mr. Hageli continued, "If you begin, as regulators, to tell them what they can and cannot do, they're going to be more conservative. I mean that to me seems to be pretty commonsensical."[45] NAMIC also agreed, "... limitations and restrictions on underwriting freedom stifle innovation and thereby hamper competition, ultimately harming consumers and society in general."[46]

These arguments do have some merit. However, this can be applied to all types of regulation --- as regulation, whether it be standardizing forms that people can understand, prohibiting use of specific language in advertising, or creating solvency requirements to ensure against bankruptcy --- all regulation implicitly limits freedom of insurance companies in exchange for a perceived societal benefit.

The one statement that remained unanswered was posed by the Insurance Commissioner Kevin McCarty during the testimony of PCI: "Certainly the life insurance business is as robust today as it's ever been and we don't allow race-based rates."[47] Moreover, in the same vein, disallowing the use of a factor by all companies (in this instance race) creates a level playing-field for all insurance companies to compete based on factors that are allowed. Based on information received as part of the Office's investigation of this matter, companies that use the factors view the college-educated population as a more profitable group. Companies that do not use occupation and education as rating factors may potentially be at a competitive disadvantage because they may lose the wide range of business offered by higher income policyholders.

[45] Vol. 2, page 131, lines 14 – 20.
[46] Vol. 2, page 185, lines 4 – 14.
[47] Vol. 2, page 131, lines 8 – 13.

Florida's Office of Consumer Advocate also agrees, "I believe that if a particular rating variable has an extraordinary disparate impact on a particular prohibited class or group of prohibited classes, that that variable in effect is a proxy for prohibited classes and should be prohibited."[48] Thus, even though some inefficiencies in the auto insurance market may be created by disallowing the use of factors such as race, income level, or factors that may be intentional or unintentional proxies for race and income levels such as credit scores, occupation and education --- the prohibition of such use may be in the public interest, despite modest insurance sector inefficiencies. The relationship between race and income is illustrated by data from the U.S. Census' "Income, Earnings, and Poverty From the 2004 American Community Survey," issued August 2005:

Median Incomes by Race

Race and Hispanic Origin	Men	Women
Caucasian alone	$42,707	$32,034
Caucasian alone, not Hispanic	$45,573	$32,678
African-American alone	$32,686	$28,581
American Indian	$32,113	$25,752
Asian alone	$46,888	$36,137
Hawaiian and Pacific Islander	$32,403	$27,989
Other Race	$26,679	$23,565
Two or More Races	$37,025	$30,729
Hispanic Any Race	$26,749	$24,030

Median Incomes by Education

Education	Men	Women
Less than High School	$21,760	$13,280
High School Graduate	$31,183	$19,821
Some College or Associates Degree	$37,883	$25,235
Bachelor's Degree	$52,242	$35,195
Graduate or Professional Degree	$68,239	$46.004

[48] Vol. 2, page 217, lines 16 – 21.

Median Incomes by Occupation

Occupational Fields	Men	Women
Management	$65,393	$48,118
Business and Financial Operations	$57,922	$42,256
Computers and Math	$66,130	$56,585
Architecture	$64,496	$51,581
Health Care Practitioner	$69,124	$45,380
Health Care Support	$25,774	$22,658
Farming, Fishing	$22,124	$17,098
Construction	$33,064	$29,289
Transportation	$31,840	$22,434
Personal Care and Service	$27,258	$19,789
Educational	$47,963	$36,891
Office and Admin Support	$35,216	$29,006

One of Florida's greatest strengths is its rich culture and ethnically diverse population, and it would be unfortunate if the insurance industry, through its practices, either intentionally or unintentionally, engaged in discriminatory practices based on a person's ethnicity or income status. Similar to credit scoring, it is possible that clear legislation with rule making authority will be needed to restrict the use of education and occupation as underwriting and rating factors.