**Statement of**
**Robert Hunter, Director of Insurance**
**Consumer Federation of America**
**on the**
**The State of Private Passenger Automobile Insurance in the District of Columbia**
**Before the**
**DC Department of Insurance, Securities and Banking**
**Public Hearing Washington, DC**
**March 25, 2019**

Commissioner Taylor, I appreciate your invitation to appear before you today to consider the effects and impacts on District consumers of the use of sophisticated models by automobile insurance companies as the basis for developing rates and rating classifications.

I will comment on each of the five areas in your letter in a minute. Before that, it is vital to reflect on why this hearing is so important since we do not usually focus sufficient attention on lower-income good drivers' inability to afford District-required auto insurance and how that can hamper their lives.

Consider the District's role in auto insurance for these folks:

First, the District tells its lower-income citizens, "You must have minimum auto insurance of $25,000/$50,000 BI and UMBI, $10,000 PD and $5,000 UMPD," which are higher limits than at least 14 states.

Second, the District, through your Department, Commissioner, is responsible for regulating the rates for this coverage and making sure people can afford the coverage it requires.

Third, and finally, the District penalizes residents who drive without insurance. The penalties include Suspension of registration tags, a fine of $30 for not being able to show proof of insurance, a fine of $150 for a lapse of 30 days or less and a fine of $7 per day for lapse over 30 days up to $2,500.

That second step, this Department's key role in assuring good drivers can afford required insurance, makes it vital for the Department to do everything in its power to make sure lower-income residents can afford the insurance you require.

According to the Federal Insurance Office, three ZIP Codes in DC have average auto insurance rates that are unaffordable to their residents. These are 20019, 20020 and 20032. That means about 140,000 District residents live in ZIP Codes where rates have been deemed unaffordable. Many more people throughout DC may also face unaffordable premiums.

One of the reasons poorer, good driving people can't afford auto insurance here is that unfair socio-economic classes are used to price the coverage. If a person has less education, he pays more. If a person has a lower-paying job, she pays more. If a person has poor credit, perhaps caused by the vagaries of living paycheck-to-paycheck, he pays more. If a person rents her home rather than owns it, she pays more for auto coverage. If a person was previously uninsured he pays a higher premium, as he does if he was insured, except by the "wrong" – that is, non-standard – previous insurer. There is a "widow penalty," in which women are surcharged when their husbands die. In fact, women pay more for coverage on average, contrary to widely held beliefs. Often, the cost of having these socio-economic related surcharges on your policy will require someone with a perfect driving record to pay more, and sometimes much more, than a person with wealthy characteristics despite accidents and tickets on their record. The good driver will even pay more, in some instances, than a richer driver with a drunk driving conviction.

Insurance companies should judge you on how you drive, not who you are. But, in the District, they don't.

This is intolerable when you reflect on the fact that, for most low- and moderate-income households, not having a car imposes significant constraints on life choices. Limited mobility affects access to potential employers, and may restrict access to health services, education, shopping at discount stores, and a vast array of recreational activities. That is especially the case for employment. Many District residents face what is referred to in academic literature as a "spatial mismatch," the increasing difficulty people have getting to work because of the increased geographic dispersion of both jobs and residences.

While the District provides relatively effective public transit, it is insufficient for many people living here trying to get good jobs in places like the Dulles corridor or other suburban job growth areas, as well as late-night and overnight employees.

It is not surprising to me that, in 2016, the Insurance Research Council estimated that 15.6 percent of citizens of the District drive uninsured, more than the national average of 13 percent. Having a car is vital to live a decent life in 2019. If the choice is between paying for insurance and feeding my family, I know what I would do.

That means that if the answers to any of the five questions raised in the hearing notice reveal a problem that needs fixing, the Department must find a way to resolve it in order to ensure that good drivers can afford District-required auto insurance.

Let's consider your 5 questions:  Your first question was

1. **How the models affect the overall premiums paid by consumers in the District.**

If the models setting prices in the District are used to raise the price of auto insurance above risk-related price that should be charged, these models must be altered.

In recent years, we have seen a growth in industry efforts to adopt models specifically designed to raise premiums above the risk level.  A clear example of this is price optimization, where insurers raise the price of the coverage based upon the shopping habits of people, using elasticity of demand models rather than risk relationship as a pricing tool.  It is apparent that carriers do not approach price optimization in the zero-sum game manner that traditional rate setting is approached; rather, insurers do not aim to balance out higher premiums from a higher risk class with lower premiums for lower risk drivers. Under these new, risk-neutral models, insurers only care about how much they can squeeze out of each customer, so, depending upon the model and the customer profiles, insurers could be using the models to generate excessive premium.

Thankfully, in recognition of the inappropriateness of these models, you, Commissioner, banned this practice.  In 2015, you notified insurance companies that so-called "price optimization" is unfair discrimination and illegal in the District.  We applaud your leadership among the states in this area.

But, the fact that many insurers were implementing such a pernicious model is fair warning that other models trying to overprice people could already be in the works, if not in use.  So, **we urge you to continue vigilance here and review company plans to ensure that there is not a surreptitious use of improper models, such as price optimization.**

Your second question was:

2. **How the models distribute the cost among different classifications of District consumers.**

This is the area where we at CFA have the most concern, Commissioner.

CFA has done many studies on this subject; a list with links to the studies and thumbnail descriptions of the findings is available on our website and are worth serious study by your experts, Mr. Commissioner. https://consumerfed.org/cfa-studies-on-the-plight-of-low-and-moderate-income-good-drivers-in-affording-state-required-auto-insurance./

The findings show the unfair discrimination faced by lower-income people resulting from the rating plans in use by insurers to price auto insurance. I mentioned these earlier, the unfair socio-economic rating factors employed here such as education, occupation and credit score.

A key reason auto insurance required by DC is unaffordable for many residents is the cumulative impact of the socio-economic identifiers allowed in rating plans in use in the District.

There is another very important issue regarding models for classifying. Namely, some classes can be proxies for prohibited classes such as race and income. Surely, classifications like education, occupation, home ownership, and credit score raise serious concerns about violation of a protected class's protection.

But there is a new wave of potentially discriminatory practices about to impact District drivers. The introduction of artificial intelligence (AI) raises serious questions about rating impacts on protected classes. Law professors Daniel Schwarz and Anya Prince have recently analyzed AI's tendency toward "proxy discrimination," a specific type of practice producing a disparate impact. AIs, they explain, are inherently structured to engage in proxy discrimination whenever they are deprived of predictive data. Simply denying AIs access to the most intuitive proxies for predictive variables does nothing to alter this process; instead it simply causes AIs to locate less intuitive proxies. The proxy discrimination produced by AIs therefore has the potential to cause substantial social and economic harms by undermining existing anti-discrimination regimes.

**CFA recommends that the District consider making driver record, miles driven and years of driver experience the three most important rating factors and eliminate or minimize the use of socio-economic factors. A model for such reform is found in California's Proposition 103, outlined in recent CFA studies. We also recommend that the Department petition the NAIC to study the impact of Big Data and AI on protected classes so that discrimination against protected classes does not creep into the pricing models.**

Your third question was:

3. **The concentration of the District's automobile insurance market and whether rates are impacted by market concentration.**

Using the test commonly employed by the United States Department of Justice (DOJ) to measure market concentration, the Herfindahl-Hirschman Index (HHI),[1] the concentration of insurers in DC is the highest in the nation. DC's HHI is 1928. The closer a market is to being a monopoly, the higher the HHI index. The DOJ considers a market with a score of less than 1,000 to be a

[1] The HHI is calculated by squaring the market share of each firm competing in a market and totaling the resulting figures.

competitive marketplace, a score of 1,000-1,800 to be a moderately concentrated marketplace and 1,800 or greater to indicate a highly concentrated marketplace. By this measure, DC's auto insurance market is highly concentrated.

This concentration of market has the effect of restricting competition, which can harm District drivers. **Steps to enhance competition should be undertaken, such as:**

- **Balancing supply and demand. Since people have to purchase auto insurance, insurers should have to sell it to them (at least as long as they maintain good driving records);**
- **Requiring that insurers offer good drivers the lowest price they have in their entire group of insurers doing business in D.C., blocking the nefarious industry practice of shunting lower-income good drivers into higher priced insurance group subsidiaries; and**
- **Improving the availability of information on insurance prices so that consumers can use the tool to find the lowest priced insurers for them.**

Your fourth question was:

**The insurers' return on net worth and its impact on premiums.**

From 1989 to 2016, DC's auto insurance rate of return on net worth was 12.8%. Nationally, it was 7.7%. From 2007 to 2016, DC's auto insurance rate of return on net worth was 9.9% compared with 4.2% countrywide.

Since the long-term profit of auto insurers in the District was greater than that in the rest of the country, the models used for reviewing rates should be reviewed by the Department's actuaries. While recent data show that profits have tempered over the past decade, industry profits in D.C. are still double the national average. **I recommend that the Department look for ways to ensure fairer overall rates by reviewing the rules for ratemaking that California regulators have adopted for that state's prior approval process. In addition to a systematic review of actuarial selections related to loss trends, development, and other key loss data, the rules aim to remove expenses that are not properly charged to policyholders but should be charged to stockholders (such as the costs of fines, penalties, excessive salary levels, excessive overhead costs, etc.)**

**We also see high profits as a potential indicator of excessive fees – including installment fees, policy fees, cancellation fees, and more. We urge you to review the fees in use by carriers selling policies in the District.**

Your fifth question was:

4. **The possibility of establishing standard and low-cost plans.**

California and New Jersey have taken action to help lower-income good drivers. **The District should address the large number of uninsured drivers by providing good drivers who are poorer a lower cost option.** California offers such a program that sells policies to lower-income drivers for between $267 and $642 per year, without requiring subsidy from other drivers or taxpayers. A sub-$500 annual policy in Los Angeles shows the power of this program to reduce auto insurance prices. This amazing result is possible since only lower-income drivers with good driving records qualify for the program. **The District should look at the California system as a model for reform here.**

I'd be pleased to respond to any questions you might have, Commissioner.