Ratemaking and Disparate Impact

David Eckles

University of Georgia

Terry College of Business
UNIVERSITY OF GEORGIA

Ratemaking—Two Perspectives

- Legislators’ and Regulators
  - Insurers’ rates/premiums should be:
    - Adequate
    - Not excessive
    - Not unfairly discriminatory
- Economists’
  - Insurers set rates/premiums to cover:
    - Expected losses
    - Expected costs
    - “Rainy days”
    - Profits (where applicable)
  - Competitive markets drive out discrimination

Ratemaking and Discrimination

- Ratemaking is inherently “discriminatory”
  - Factors related to loss propensity (frequency and severity) are identified:
    - e.g. age, type of car, products sold, number of locations, etc.
  - Rating factors may create disparate impact
    - e.g. older individuals pay more for life insurance
    - Disparate impact is unintentional
    - Rating factors creating disparate impact are not necessarily illegal
  - Cannot be unfairly discriminatory

Disparate Impact and Proxy Discrimination

- Not synonymous
- Disparate impact
  - Resulting in a disproportionate negative effect on a protected class
- Proxy Discrimination
  - Resulting in a disproportionate negative effect on a protected class

    and

  - The factor (in this case) is used (at least partially) *as a substitute for the protected class*
- Disparate impact can be (relatively) easily established; proxy discrimination is less so

Legislative and Regulatory Role

- Disparate impact
  - Though not malicious, can nevertheless be rectified by legislation
  - Rating factors can be disallowed by legislatures even if they are predictive of loss
- Proxy Discrimination
  - Equivalent to “unfair discrimination”
  - Already under the purview of the regulatory authority (but undefined)
  - Defined in forthcoming amendment of NCOIL’s P/C Modernization Act
- Important to not equate disparate impact and proxy discrimination
  - Contrary to existing insurance statutory and regulatory ratemaking law