American Property Casualty Insurance Association
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VIA ELECTRONIC MAIL

November 5, 2020

The Honorable Neil Breslin
c/o Mr. William Melofchik
General Counsel
NCOIL National Office
2317 Route 34 S, Suite 2B
Manasquan, New Jersey 08736

RE: The Role of "Proxy Theory" in the Unlawful Discrimination Landscape

Senator Breslin:

We write on behalf of the American Property Casualty Insurance Association (APCIA) as a follow-up to our October 22nd letter addressed to Mr. Tom Considine on the topic proxy discrimination. We understand the National Council of Insurance Legislators (NCOIL) is engaged in an effort to define that term and we hope what follows provides additional information that will be useful in the NCOIL effort.

Unlawful discrimination

"Unlawful discrimination" based on protected class characteristics has been the law for the 55 years since Congress enacted the Civil Rights Act in 1964. The definition of unlawful discrimination and the standard by which a defendant's policies or practices are judged have been worked out over that time largely in the employment context.[1] Regardless of context, the definition and the standard for imposing protected class liability on defendants have remained consistent. As for the business of insurance, statutory and regulatory rating standards universally prohibit rates that are "excessive, inadequate or unfairly discriminatory" and define "unfairly discriminatory" as treating policyholders or consumers with similar risk profiles differently. Most state insurance laws also make clear that failure to account for differences in expected losses constitutes prohibited "unfair discrimination."[2]

Protected class liability theories

There are various types of protected class liability theories. The two theories most applicable in the insurer/policyholder or consumer context are as follows:

1) *Intentional discrimination* in which "intent" is the sole focus and
2) *Disparate impact discrimination* where "intent" *plays no role at all*.

Disparate treatment discrimination, including proxy theory

Title VII of the Civil Rights Act of 1964 prohibits intentional discrimination and disparate treatment is a form of intentional discrimination.[3] In the insurer/policyholder or consumer context, disparate treatment occurs when a defendant insurer treats a policyholder or consumer less favorably than others *because of* the individual's membership in a protected class.[4] "Proxy theory" was adopted by the courts as an element of disparate treatment discrimination to recognize a policy should not be allowed to use a technically neutral classification as a proxy to evade Title VII's prohibition against intentional discrimination.[5] Because "intent" is a primary focus in disparate treatment cases, when relying on proxy theory, plaintiff must demonstrate that defendant *was motivated by a discriminatory purpose* in choosing the proxy about which plaintiff complains.[6]

As a form of intentional discrimination, disparate treatment challenges (including those that rely on proxy theory), ask one question – Has plaintiff put on sufficient evidence to establish that defendant either intended to discriminate against a protected class or was motivated by a discriminatory purpose in choosing the challenged proxy.[7] If the answer is "yes" then the challenged policy must be eliminated. Because defendant's bad act (either defendant's discriminatory intent or discriminatory motive in choosing the proxy) is an essential element of every disparate treatment challenge, plaintiff is entitled to equitable relief, attorneys fees, and monetary damages in the form of compensatory and punitive damages depending upon the underlying facts of the case.[8]

Disparate impact discrimination

Disparate impact discrimination did not exist until 1971 when the United States Supreme Court determined it constituted unlawful discrimination after which disparate impact discrimination became a basis for unlawful discrimination claims most frequently in the employment context.[9] Disparate impact discrimination was not codified into federal law until the Civil Rights Act of 1991 was enacted.[10] Disparate impact claims challenge practices that are not intended to discriminate, but in fact have a disproportionately adverse effect on a protected class and which are otherwise unjustified by a legitimate rationale.[11]

As a result, courts in disparate impact challenges ask a series of three questions consistent with the history of disparate impact jurisprudence in claims based on Title VII. They begin by asking: Does the challenged policy or practice have an adverse effect on a protected class? If the answer is "yes", then courts ask a second question: "Is there a valid interest served by the challenged policy?" And, if the answer is "yes", then the final question asked is whether there's an alternative policy or practice that serves the same valid interest with less disparate impact and less cost. If no such alternative policy exists, then the challenged policy stands, and the claim fails.[12] Because intent plays no role in disparate impact claims and proxy theory is associated exclusively with disparate treatment discrimination, courts may award equitable relief and attorneys' fees to successful plaintiffs but not compensatory or punitive damages.[13]

Disparate Treatment Discrimination	**Disparate Impact Discrimination**
• Intent is the focus[14]	• Intent plays no role
• Proxy theory applies	• Proxy theory never applies
• A finding of intent (or discriminatory purpose in choosing the proxy) ends the inquiry	• A finding of adverse effect on a protected class does not end the inquiry • The inquiry continues with the question whether there is a valid interest served by the challenged policy or practice • The inquiry continues further with the question whether there is an equally effective alternative with less adverse effect on plaintiff and cost to defendant
• If the requisite intent or discriminatory purpose is found, depending upon the facts, plaintiff is entitled to – Equitable relief, – Attorneys' fees, – Compensatory damages and – Punitive damages	• If no valid interest exists or there is an equally effective alternative, the challenged policy or practice is enjoined and only attorneys' fees may be awarded • If a valid interest exits and there is no equally effective alternative, the challenged policy or practice stands, and the claim fails
• The goal is to eliminate the challenged policy or practice	• The goal is to mitigate the adverse effect of the challenged policy or practice where a valid interest is served

Summary

To define and apply "proxy theory" in the disparate impact context is to impose a legal concept on a body of law where it has been not applied to date either by the courts or legislatures.[15] Doing so would unsettle the 55 years of jurisprudence and statutory law governing discrimination cases brought predominately under the Civil Rights Act, the Age Discrimination in Employment Act, the Rehabilitation Act, the Americans with Disabilities Act and the Fair Housing Act. Further, applying proxy theory to disparate impact claims is wholly inconsistent with the balancing of valid interests with equally effective alternatives and the mitigation goal of disparate impact jurisprudence generally.[16] Equally important is that application of proxy theory to disparate impact claims in the context of property and casualty insurance would conflict with current state law and regulations governing pricing and underwriting and would likely require an overhaul of both. This is true particularly as it relates to complying with state mandates prohibiting rates that are "excessive, inadequate or unfairly discriminatory".[17]

Proposed definition of the term "proxy" in the context of unlawful discrimination

A proxy is a policy, practice, factor, or equivalent that is technically neutral, but is otherwise used to evade statutory prohibitions against intentional discrimination regarding individuals or prohibitions against disparate treatment regarding a category of individuals because of their membership in a protected class. Unlawful discrimination by way of proxy (as defined herein) arises when a challenged policy, practice, factor or equivalent is directed at a category of individuals predominately composed of individuals in a protected class for the purpose of excluding or otherwise depriving them of a benefit available to others or where such is a motivating factor in choosing the proxy.

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[1] The law in the area of unlawful discrimination has developed primarily in the employment context, including litigation arising out of the Civil Rights Act (1964), the Age Discrimination in Employment Act (1967), the Rehabilitation Act (1973), and the Americans with Disabilities Act (1990). Albeit fewer, unlawful discrimination has been the subject of claims brought under the Fair Housing Act (1968). *See*, *Community Services, Inc. v. Wind Gap Municipal Authority*, 421 F3d 170 (3d Cir. 2005) (a disparate treatment case) and more recently in *Texas Department of Housing and Community Affairs, et al. v. The Inclusive Communities Project, Inc.*, 576 U.S. 519 (2015) (a disparate impact case).

[2] For example, Utah law provides that "[a] rate is unfairly discriminatory if price differentials fail to equitably reflect the differences in expected losses and expenses after allowing for practical limitations." UTAH CODE ANN. § 31A-19a-201(4)(a); *see also, e.g.*, ARIZ. REV. STAT. ANN. § 20-383(D); COLO. REV. STAT. § 10-4-403(1)(c); MICH. COMP. LAWS ANN. § 500.2403(1)(d); MINN. STAT. ANN. § 70A.04(4); MO. ANN. STAT. § 379.318(4); NEV. REV. STAT. ANN. § 686B.050(4); N.H. REV. STAT. ANN. § 412:15(I)(d); N.M. STAT. ANN. § 59A-17-6(E); N.C. GEN. STAT. ANN. § 58-40- 20(e); TENN. CODE ANN. § 56-5-103(a) and (d), among other states.

[3] *McWright v. Alexander*, 982 F.2d 222, 227-228 (7th Cir. 1992).

[4] *Ricci et al. v. DeStefano, et al*, 557 U.S. 557, 577 (2009) quoting *Watson v. Fort Worth Bank and Trust*, 487 U.S. 977, 986 (1988). See also, *Community Services, Inc. v. Wind Gap Municipal Authority*, 421 F.3d 170, 178 (3d Cir. 2005).

[5] *McWright*, 982 F.2d at 228. Affirmed in *Community Services*, 421 F.3d 170 (3d Cir. 2005) and *Bowers v. National Collegiate Athletic Association*, 563 F. Supp. 2d 508 (D.N.J. 2008).

[6] "A disparate-treatment plaintiff must establish that the defendant had a discriminatory intent or motive [for taking adverse action against plaintiff]". *Watson*, 487 U.S. at 986.

[7] *Community Services*, 421 F.3d at 177.

[8] U.S. Equal Employment Opportunity Commission, "Remedies for Employment Discrimination" at https://www.eeoc.gov/remedies-employment-discrimination as of November 3, 2020.

[9] *Griggs v. Duke Power Co*., 401 U.S. 424 (1971).

[10] *Ricci*, 557 U.S. at 578.

[11] *Inclusive Communities*, 576 U.S. at 524-525. See also *Rizzo*, 557 U.S. at 577. When reviewing disparate impact claims under the Fair Housing Act (FAA) and Fair Housing Act as Amended (FHAA), courts have borrowed from the framework of Title VII of the Civil Rights Act of 1964. See, e.g., *Tsombanidis v. W. Haven Fire Dep't*, 352 F.3d 565 (2d Cir.2003) and *Lapid–Laurel, L.L.C. v. Zoning Bd. of Adjustment*, 284 F.3d 442 (3d Cir.2002).

[12] See the burden-shifting framework in *Inclusive Communities*, 576 U.S. 519 (2015).

[13] *Supra*, endnote 8.

[14] In addition to intentional discrimination (including disparate treatment) and disparate impact discrimination, other discrimination claims in the Title VII context include pattern or practice, cat's paw, failure to accommodate, harassment, retaliation, and negligence. Except for disparate impact and negligence claims, all other listed claims require "intent" or discrimination as "a motivating factor".

[15] This fact is acknowledged by advocates who argue in support of "making law" by applying proxy theory in the disparate impact context and, thereby, extending it beyond its long-standing and exclusive role in disparate treatment discrimination, a form of intentional discrimination . See, Anya E.R. Prince and Daniel Schwarcz, *Proxy Discrimination in the Age of Artificial Intelligence and Big Data*, 105 IOWA L. R. 1257, 1269-1270 (2020).

[16] *Supra*, endnotes 1 and 12.

[17] State insurance law affirmatively permits (and most require) risk-based pricing and underwriting in order to comply with the "excessive, inadequate, or unfairly discriminatory" rating standard. See examples, *supra*, endnote 2. As explained in the Casualty Actuarial Society Statement of Ratemaking Principles, "[a] rate is reasonable and not excessive, inadequate, or unfairly discriminatory if it is an actuarially sound estimate of the expected value of all future costs associated with an individual risk transfer." For purposes of state insurance law, rates are "unfairly discriminatory" if "premium differences . . . do not correspond to expected losses and average expenses or if there are expected average cost differences that are not reflected in the premium differences." *See*, Casualty Actuarial Society, *Statement of Principles Regarding Property and Casualty Insurance Ratemaking*, Principle 4 (May 1988), https://www.casact.org/professionalism/standards/princip/sppcrate.pdf.

Respectfully submitted,

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