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Discrimination by Gender in Automobile Insurance: A  
Note on *Hartford Accident and Indemnity Co. v.*  
*Insurance Commissioner*

Richard A. Miller\*

I

On September 27, 1984, the Supreme Court of Pennsylvania decided that automobile insurance rates based on the gender of the insured were "unfairly discriminatory" under Pennsylvania law.<sup>1</sup> Philip V. Mattes, who filed a complaint with the Pennsylvania Insurance Commissioner challenging the legality of gender-based rates, was insured by the Hartford Accident and Indemnity Company; as a 26 year old male with no accident history he paid a premium of \$360, while a similarly situated female paid \$212, about 40 percent less for identical coverage. No differences existed other than sex. The Commonwealth's Insurance Commissioner disapproved Hartford's rate plan based on gender. The commonwealth court upheld the disapproval, and the Pennsylvania Supreme Court affirmed.

The Pennsylvania Surety Rate Regulation Act (Rate Act) requires due consideration not only of actuarial or underwriting practice, judgment, and experience but also of all other factors within and outside the Commonwealth.<sup>2</sup> Classification of risks is allowed for rate making purposes,<sup>3</sup> but, under section 3(d), rates "shall not be excessive, inadequate or unfairly discriminatory."<sup>4</sup>

An earlier Pennsylvania case held that "actuarial soundness cannot be the sole test of the validity of a rate, . . . [hence] actuarial

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1. *Hartford Accident & Indemnity Co. v. Insurance Comm'r of Pa.*, 65 Pa. Commw. 249, 442 A.2d 382, *aff'd*, 482 A.2d 542 (1984) (decided under section 3(d) of the Casualty and Surety Rate Regulation Act, June 11, 1947, P.L. 538, § 3(d), 40 PA. CONS. STAT. ANN. § 1183(d) (Purdon 1971)).

2. P.L. 538 § 3(a), 40 PA. CONS. STAT. ANN. § 1183(a) (Purdon 1982).

3. 40 PA. CONS. STAT. ANN. § 1183(c).

4. *Id.* § 1183(d).

justification does not operate without a limit,"<sup>5</sup> despite the stipulation that the rates were actuarially sound and hence not in dispute. In the latter case, a possibly important variable had been omitted in the actuarial calculations for hospitalization insurance rates for the elderly; the Commissioner disapproved, and the commonwealth court declined to interfere. Thus, actuarial soundness has been held in Pennsylvania not to provide a complete defense to the level of insurance rates.

In *Hartford v. Insurance Commissioner*, the commonwealth court likewise upheld the Commissioner's decision, holding that the Commissioner was well within his discretionary authority to consider the Equal Rights Amendment to the Pennsylvania Constitution<sup>6</sup> as a relevant "other factor" under the Rate Act to avoid "unfair discrimination" based on sex. The court concluded that the Commissioner "considered the actuarial factors and also, as required by section 3(a) 'all other relevant factors within and outside the Commonwealth,' in determining that the sex-based auto insurance rate classification was 'inherently unfairly discriminatory' because it failed to treat 'equals equally'."<sup>7</sup>

The Pennsylvania Supreme Court initiated its affirmation of the commonwealth court's ruling by assuming that discrimination based on sex existed: "There is no attempt to suggest that Mattes was not in fact discriminated against because of his sex. The inquiry must begin by accepting that a gender based discrimination exists. The question to be resolved is whether such discrimination falls within the parameters of the Rate Act's prohibition against

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5. 65 Pa. Commw. at 255-56, 442 A.2d at 385 (quoting *Capitol Blue Cross v. Insurance Dep't*, 34 Pa. Commw. 584, 383 A.2d 1306 (1978), a case not involving discrimination by sex).

6. "Equality of rights under the law shall not be denied or abridged in the Commonwealth of Pennsylvania because of the sex of the individual." PA. CONST. art. I, § 28. Hartford argued that the Commissioner had exceeded his statutory authority. According to the insurance regulations, "This Chapter does not prohibit insurers from differentiating in premium rates between sexes where there is sound actuarial justification." 31 PA. ADMIN. CODE § 145.1, implementing the Unfair Insurance Practices Act of July 22, 1974, P.L. 589, 4D PA. CONS. STAT. ANN. §§ 1171-1171.15 (Purdon 1982). See 65 Pa. Commw. at 257, 442 A.2d at 386.

7. 65 Pa. Commw. at 258, 442 A.2d at 386. President Judge Crumlish dissented on the ground that the decision "unduly extends the Insurance Commissioner's authority." *Id.* at 258, 442 A.2d at 387 (Crumlish, J., dissenting). The Commissioner, he argued, "has strayed beyond the bounds of the insurance field and into the sphere of policy determination, an area properly reserved to the elected body." *Id.* at 260, 442 A.2d at 387 (Crumlish, J., dissenting). The Commissioner, the judge felt, should have limited himself to consideration of "actuarial evidence."

'unfairly discriminatory rates'.<sup>8</sup> The supreme court maintained that section 3(d)'s phrase "unfairly discriminatory" would be "mere surplusage"<sup>9</sup> if actuarial considerations (allowed in other sections of the Rate Act) were all that were necessary to justify differential rates between men and women; section 3(d) must have some meaning beyond "actuarial fairness," otherwise the section would be "redundant," with "no independent effect." The Pennsylvania Equal Rights Amendment was likewise relevant to the court. Hartford's sex-based rates "rely on and perpetuate stereotypes similar to those condemned" in a series of cases brought under the amendment.<sup>10</sup> "Unquestionably, sex discrimination in this Commonwealth is now unfair discrimination . . . . To read the term 'unfairly discriminatory' as excluding sex discrimination would contradict the plain mandate of the Equal Rights Amendment to our Pennsylvania Constitution."<sup>11</sup>

The difficulty with the court's decision in *Hartford* is the controlling assumption that discrimination existed in the first place. The court started with this assumption, and thus neglected any serious consideration of what should be *the* basic and initial question: did discrimination in a meaningful way actually exist? Assumption of an answer cannot suffice for considered argument, of which there was none. The case should have turned, but did not, on the issue of whether true discrimination existed. My argument here is that the court's analysis rests on an assumed answer to an unasked question, and the assumed answer is almost certainly wrong.

## II

The provision of automobile insurance in the marketplace involves an economic exchange: drivers wishing to be insured

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8. — Pa. —, 482 A.2d. at 546.

9. *Id.* at 547.

10. *Id.* at 548 (citing *Commonwealth ex rel. Spriggs v. Carson*, 470 Pa. 290, 368 A.2d 635 (1977); *Adoption of Walker*, 468 Pa. 165, 360 A.2d 603 (1976); *Butler v. Butler*, 464 Pa. 522, 347 A.2d 477 (1975); *Commonwealth v. Santiago*, 462 Pa. 216, 340 A.2d 440 (1975); *DiFlorido v. DiFlorido*, 459 Pa. 461, 331 A.2d 174 (1975); *Commonwealth v. Butler*, 458 Pa. 289, 328 A.2d 851 (1974); *Henderson v. Henderson*, 458 Pa. 97, 327 A.2d 60 (1974); *Conway v. Dana*, 456 Pa. 90, 320 A.2d 139 (1974). None of these cases touches on the issue raised within this note—that the recognition of differences between men and women is necessary to *avoid* discrimination.

11. 482 A.2d at 549. The court noted that the Commissioner not only "is charged with the execution of the Rate Act [but also has] sworn to uphold the Constitution and laws of this Commonwealth." *Id.*

purchase coverage, exchanging dollars for a policy with specific provisions on what is covered for a specific period of time. Thus, it is appropriate to discuss discrimination in auto insurance in terms of markets and economics. Discrimination is often defined, at least as a first approximation, as selling the same commodity to different buyers at different prices, and in the instant case Hartford certainly charged different prices for identical insurance coverage to Mattes and to an otherwise equally placed young female. This definition is the one implicitly adopted by the commonwealth and supreme courts.

The problem with this first-approximation definition is that it is incomplete and hence possibly, as here, misleading. What if costs of supply and delivery of the same commodity to different customers differ substantially, say because of different locations of the two customers, one close to the supplier, the other far away? (The distance from Hartford, Connecticut, is not a factor in auto rates, although the location of the insured may be; auto insurance rates for a Manhattan, Boston or Pittsburgh resident certainly differ from rates for residents of rural New York, Massachusetts or Pennsylvania). A purchaser of a ton of steel delivered to Pittsburgh from a Pittsburgh mill should pay less than a purchaser of an identical ton delivered to Philadelphia, Scranton or State College from that same Pittsburgh mill; the different delivered prices should reflect different transportation costs. Similarly, products which are not identical but are "similar" should also exchange at prices which reflect those differences in product characteristics. We do not expect Cadillacs and Chevrolets to have the same price. These examples thus contain a warning: prices should reflect costs of supplying the "identical" commodity.

Consider a second kind of example, one involving identical prices: the delivery of a letter from the sender to the recipient within the United States for .22. Certainly the cost of delivery of a letter from Philadelphia to Harrisburg is considerably less than the cost of delivery for an identical letter from Philadelphia to Anchorage or Honolulu or even Erie. We would probably agree that if Chevrolets and Cadillacs carried the same price, discrimination would be involved. These examples thus contain a second warning: prices which are "equal" but do not reflect differences in cost thus embody discrimination, despite their equality in price.

These two examples suggest that costs (of production and transportation—costs of supplying a commodity to a customer) should be reflected in the prices that customers pay; where costs are high

prices should be high, and where costs are low prices should be low. Otherwise discrimination will exist. Different prices to different customers, despite identical costs of supplying those customers, involves discrimination; similarly, identical prices to different customers, despite different costs of supplying those customers, also involves discrimination. A more appropriate, accurate, and helpful definition of discrimination (than the first-approximation) requires a reference to costs. Nobel Laureate George Stigler defines discrimination "as the sale of two or more similar goods [to different customers or in different markets] at prices which are in different ratios to marginal cost."<sup>12</sup> The leading study of discrimination in price includes the following definition: "price discrimination should be defined as implying that two varieties of a commodity are sold (by the same seller) to two buyers at different *net* prices, the net price being the price (paid by the buyer) corrected for the cost associated with the product differentiation [by location, time, or quality]."<sup>13</sup> It is thus naive and unrealistic to define discrimination without reference to costs, as the court has done implicitly in *Hartford*. The "unfairly discriminatory" language of the Rate Act can easily and properly be interpreted as rates not adequately related to costs of providing insurance.

Actuarial studies in insurance embody a sophisticated attempt to identify the costs associated with supplying the product, insurance, to specific customers. The nature of the product involves probabilities—of loss, should an accident occur, or of no loss, should no accident occur. In addition to these probabilities, the costs of supplying insurance also involve probability calculations of accident severity and hence the amounts of possible claims. Statistical evidence clearly indicates that young men have more and bigger accidents than young women; costs of providing insurance to young men are thus higher than those costs for young women, and

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12. G. STIGLER, *THE THEORY OF PRICE* 209 (1966). Stigler notes: "Price differences do not necessarily indicate discrimination . . . . Conversely, price equality does not demonstrate the absence of discrimination." *Id.* The author of the leading text in the economics of industrial organization defines discrimination thus:

No simple, all-inclusive definition of price discrimination is possible. Succinctly, price discrimination is the sale (or purchase) of different units of a good or service at price differentials not directly corresponding to differences in supply cost. Note that this definition includes not only the sale of identical product units to different persons at varying prices, but also the sale of identical units to the same buyer at different prices . . . and the execution of transactions entailing different costs at identical prices . . . .

F. SCHERER, *INDUSTRIAL MARKET STRUCTURE AND ECONOMIC PERFORMANCE* 315 (1980).

13. L. PHILIPS, *THE ECONOMICS OF PRICE DISCRIMINATION* 6 (1983).

the prices of providing such insurance should reflect those differences in costs. Not to do so, as the Supreme Court of Pennsylvania now requires, is the equivalent of requiring the insurance industry to discriminate by sex in the provision of automobile insurance to young people. There may have been an element of discrimination by sex prior to *Hartford*; now the gender discrimination will certainly be increased, and likely by a substantial amount.

If one is not convinced by this argument, consider the extreme case. Assume that young women without exception are cautious and safe drivers, rarely involved in accidents, and incur very low claims against their insurance policies. Assume also that young men by contrast and with few exceptions, are reckless and dangerous drivers, frequently involved in accidents; they make substantial claims against their insurance policies. No difference in principle intrudes in this extreme. Is discrimination involved (a) if young men and young women pay the same insurance rates, or (b) if young men pay substantially higher rates than young women? The answer to (a) is certainly yes; the answer to (b) depends on how closely the rates set for men and women approximate *costs*: "past and prospective loss experience within and outside the Commonwealth, . . . underwriting practice and judgment, . . . catastrophe hazards, . . . a reasonable margin for underwriting profit and contingencies, . . . dividends, savings or unabsorbed premium deposits, . . . past and prospective expenses"; in short, costs as allowed by section 3(a) of the Rate Act and as allowed by the classification schemes of section 3(c).<sup>14</sup> So, when the majority writes, "Unquestionably, sex discrimination in this Commonwealth is now unfair discrimination,"<sup>15</sup> the court is failing to recognize that for nondiscriminatory treatment to exist, different prices on insurance should be charged to young men and women; the coverage is provided at different costs, because there are basic differences in accident histories between the two groups. "Sometimes the grossest discrimination can lie in treating things that are different as though they were exactly alike."<sup>16</sup>

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14. 482 A.2d at 544-45.

15. *Id.* at 549.

16. *Jeness v. Fortson*, 403 U.S. 431, 442 (1971). See also THE PRICING AND MARKETING OF INSURANCE: A REPORT OF THE U.S. DEP'T OF JUSTICE TO THE TASK GROUP ON ANTITRUST IMMUNITIES 308-09 (1977): "It is not 'unfair' discrimination to offer insurance at a lower premium to persons who have a lower expense cost than others. In fact, the failure to grant a preference in rates reflecting the expense differential results in unfair discrimination." And, "We have already examined the question of unfair discrimination, concluding that fairness requires that prices be reasonably related to costs." *Id.* at 328.

## III

In a concurring opinion in *Hartford*, Justice Flaherty, with Justice Hutchinson joining, writes "to emphasize that, were it not for the Equal Rights Amendment, Pa. Const. Art. I, § 28, resort to gender-based insurance rate classifications would not be 'unfairly discriminatory' under 40 P.S. § 1183(d) (1971), since such classifications may indeed be actuarially sound."<sup>17</sup> That is, the "people's will on gender-based classifications," as expressed in the Equal Rights Amendment, prohibits different insurance rates for equal coverage, despite different costs of coverage for young men and women.

Thus, sex cannot be used as a consideration in rate setting, even to avoid actual discrimination based on cost differences. The Equal Rights Amendment, however, is written in the most general of terms: "Equality of rights under the law shall not be denied or abridged in the Commonwealth of Pennsylvania because of the sex of the individual."<sup>18</sup> Interpreting the amendment, the court quoted *Henderson v. Henderson*: "The thrust of the Equal Rights Amendment is . . . [to] eliminate sex as a basis for distinction . . . . The law will not impose different benefits or burdens upon the members of a society based on the fact that they may be man or woman."<sup>19</sup> But surely the new requirement, that insurance rates become equal for young men and young women despite cost differences, automatically imposes *different* "benefits" and "burdens" based on sex. The burden will (with equal insurance rates) now fall more heavily on women: the benefits will accrue to men, and the costs and benefits falling to young men and women will fall in unequal proportions, that is, will fall in a discriminatory manner. Put another way, there will now be a redistribution of income or wealth from women to men. Surely this is not what the Pennsylvania Equal Rights Amendment means; nor, I suspect, is it what Pennsylvania voters thought they were voting for when they adopted the Equal Rights Amendment.

## IV

Two Justices, McDermott and Zappala, dissented in *Hartford*, each joining the other's opinion. Justice McDermott emphasized the importance of costs in determining rates, to avoid "unfair dis-

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17. 482 A.2d at 550.

18. PA. CONST. art. I, § 28.

19. 458 Pa. 97, 101, 327 A.2d 60, 62 (1974).

crimination" prohibited by the Rate Act. He noted the differences in accidents for those 25 to 29 years old: 7.28 accidents per one hundred licensed male drivers in Pennsylvania (presumably per year), compared with 2.96 accidents per one hundred licensed females. He also noted the differences in losses—annual costs of accidents—for unmarried males and females aged 17 to 20 (\$195 to \$255).<sup>20</sup> Requiring equal rates, he concluded, "unfairly treats as alike those who are, at least on the highways, demonstrably different."<sup>21</sup> The Commissioner thus exceeded his power under the Rate Act: "The basic policy behind the Act was set: that there must be a reasonable relationship between proposed insurance rates for a particular class and the risk [cost] posed by members of that class."<sup>22</sup> As Justice McDermott also noted, twice in the years after the Equal Rights Amendment was passed (1971), the legislature had the opportunity "to outlaw the usage of gender-based classifications in insurance rates but specifically chose not to do so."<sup>23</sup>

Justice Zappala's opinion distinguished other cases in which the supreme court had condemned "sexual stereotypes . . . . We [have] rejected the employment of presumptions which were based upon social prejudice or meritless characteristics ascribed to a class."<sup>24</sup> He embraced fully the notion that costs for a class, even based on gender, should be reflected in rates: "It is not unfairly discriminatory, however, to treat individuals who are not in the same position differently. It is self-defeating to suggest that similar individuals should be treated as such not only where differences do not exist, but also that they should be treated as the same where differences undeniably do exist."<sup>25</sup> And here differences do exist—"not those which are presumed or manufactured to reinforce social prejudices." "[I]n our zeal to rectify perceived discrimination, we may create discrimination."

A puzzling footnote in Justice McDermott's opinion, however, suggests that the full meaning of the relationship between costs and prices, to avoid discrimination, may have escaped him: "Insur-

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20. 482 A.2d at 553.

21. *Id.*

22. *Id.* at 554.

23. *Id.* In a footnote Justice McDermott noted "that the Commissioner adjudicated this case in the face of an Insurance Commission regulation which prohibits insurers from denying benefits or coverage on the basis of sex, but specifically 'does not prohibit insurers from differentiating in premium rates between sexes where there is sound actuarial justification.'" 482 A.2d at 554 n.9 (citing PA. ADMIN. CODE § 145.1 (1977)).

24. 482 A.2d at 556.

25. *Id.* at 557.

ance rate classification inherently envisions *some* discrimination. In this uneven world, some urban areas generate more occasion for accident. Persons living in them by choice or necessity bear higher premiums. The ideal classification would be homogeneous, practical and objective, so the factors would be beyond manipulation."<sup>26</sup> Either this is a comment on the impossibility of complete classification, to make each class or group completely homogeneous within that class or group (a correct statement), or it is a minor slip at variance with the rest of his dissent.<sup>27</sup>

## V.

In 1944 Federal antitrust laws were held applicable to the insurance industry,<sup>28</sup> and Congress acted promptly to prevent such application.<sup>29</sup> As Justice McDermott argues, "The [McCarran-Ferguson] Act . . . was passed to shield insurers against antitrust enforcement under the Robinson-Patman Act which was partially aimed at inhibiting unfair price differences."<sup>30</sup> In fact the Robinson-Patman Act declared it to be unlawful "to discriminate in price between different purchasers of commodities of like grade and quality . . . where the effect of such discrimination may be

26. *Id.* at 551 n.1.

27. The same point is made in the context of mortality tables for life insurance and annuities:

Grouping males and females together will not eliminate the application of averages to individuals, and it in fact will actually aggravate rather than alleviate any unfair discrimination. In insurance, one of the purposes of grouping smaller (i.e. by age and by sex), rather than larger (i.e. combining sexes and/or ages), is to try to determine averages that more closely resemble the individual characteristics and individual mortality of the members. Grouping larger makes members less alike rather than more alike . . . . The larger the group, the more dissimilar the individuals are to the average, and the more unfairly discriminatory is the grouping. Therefore, separate male and female tables come closer to having averages which fairly represent individuals than do male and female combined tables.

Lautzenheiser, *Sex and the Single Table: Equal Monthly Retirement Income for the Sexes*, 2 EMPLOYEE BENEFITS J. 8 (1976) (cited recently in Brief for Defendant-Appellant United States, *Manufacturers Hanover Trust Co. v. United States*, No. 84-6051 (2d Cir., argued June 15, 1984)). For a discussion of discrimination in the field of annuities, see Miller, *How to Discriminate by Sex: Federal Regulation of the Insurance Industry*, 17 CONN. L. REV. (forthcoming 1985).

28. *United States v. South-Eastern Underwriters Ass'n*, 322 U.S. 533 (1944).

29. 59 Stat. 33, 15 U.S.C. §§ 1011-1015 (1983).

30. 482 A.2d at 552 (footnote omitted). Actually, the *South-Eastern Underwriters* case was aimed principally against the cartel activities of insurance companies appearing before state insurance commissions, which since the 1880's had been exercising the regulatory authority abandoned to them by the federal government. *South-Eastern Underwriters*, to the surprise of the insurance companies and the state regulators, found that property-liability insurance was in interstate commerce.

substantially to lessen competition or tend to create a monopoly . . . .” But there is an important proviso, termed the “cost defense”: “*Provided*, That nothing herein contained shall prevent differentials [in price] which make only due allowance for differences in the cost of manufacture, sale, or delivery resulting from the differing methods or quantities in which such commodities are to such purchasers sold or delivered . . . .”<sup>31</sup> Thus Robinson-Patman, from which insurers were freed by McCarran-Ferguson, at least recognizes the possibility that differing costs may be used to justify different prices to different customers; notwithstanding this acknowledgment, sex-based differences in insurance policies (and presumably prices of all other products—hair cuts?) are now outlawed in Pennsylvania, despite cost differences.

## VI

The Pennsylvania Supreme Court has thus declared the use of gender classifications to set insurance rates illegal under the Pennsylvania Equal Rights Amendment. This prohibition will not reduce or eliminate discrimination in insurance pricing; instead it will engender increased discrimination, since cost differences between the sexes cannot be considered by actuaries in pricing insurance coverage. Gender, at least in Pennsylvania, is no longer a variable to be allowed. This policy treats unequals as equals in the name of equality of treatment. One hopes that Pennsylvania policy makers do not outlaw completely any consideration of differences between men and women.

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31. Act of June 19, 1936, 15 U.S.C. § 13, *amending* Section 2 of the Clayton Act of 1914, which also contained a cost defense, albeit a more liberal one.