

settlement. To excuse their noncompliance, the Downeys were required to, at a minimum, show their reason for not complying. Their assertion that they did know that the policy provided UIM coverage did not meet this threshold requirement. It was well settled that uninsured motorist coverage inures to a person, not to a vehicle, the court stated. It was implicit in the Downeys' argument that they failed to learn of the UIM coverage because they simply did not read their policy. They were, however, in possession of the policy at all relevant times, and they were also represented by counsel. Where a named insured not only has possession of the policy, but also is represented by counsel, ignorance of the policy terms resulting from a failure to read the policy does not, as a matter of law, constitute an acceptable excuse for noncompliance with the notification requirements of the policy, the court concluded. // Holt

Underwriting/Credit Scores

Texas Law Allows Use of Credit Scores to Underwrite Insurance Regardless of Whether Such Scores Have Racially Disparate Impact on Availability and Price of Insurance

Texas Supreme Court Answers Question Certified from Ninth Circuit to Determine Whether Federal Disparate Impact Liability Would "Invalidate, Impair, or Supersede" Texas Law

Ojo v. Farmers Group, Inc. [et al], ___ S.W.3d ___, 2011 WL 2112778 (Tex., May 27, 2011)

Case at a Glance

Texas law permits insurance companies to use race neutral credit-scoring in underwriting insurance, even if it has a racially disparate impact.

Summary of Decision

The Question. This case is the answer of the Supreme Court of Texas to a question sent from the Ninth Circuit. The Texas answer is set forth above in

the "Glance," but here is the question:

Does Texas law permit an insurance company to price insurance by using a credit-score factor that has a racially disparate impact that, were it not for the [McCarran-Ferguson Act, 15 U.S.C. § 1012(b)], would violate the federal Fair Housing Act, 42 U.S.C. §§ 3601-19, absent a legally sufficient nondiscriminatory reason, or would using such a credit-score factor violate Texas Insurance Code sections 544.002(a), 559.051, 559.052, or some other provision of Texas law?

In the Ninth Circuit, the trial judge had ruled one way—in favor of Farmers early in the case—a three judge panel ruled the other way, and the Circuit sitting en banc was evidently uncertain, and asked for the answer to the question it submitted.

Factual and Legal Background. Ojo, an African-American resident of Texas, purchased homeowners insurance from Farmers. Although he had never made a claim under the policy, Farmers raised his premium by 9%, allegedly based on unfavorable credit information acquired through an automated credit-scoring system.

Ojo sued Farmers, and related entities, in federal court. Ojo's complaint alleged that the credit-scoring system used by Farmers employed various "undisclosed factors" that impacted minorities in ways violating federal Fair Housing Act (FHA), 42 U.S.C. §§ 3601-19. Various federal courts have interpreted the FHA broadly to prohibit racially discriminatory pricing of property insurance and to prohibit not just intentional acts of discrimination, but also race-neutral actions that have discriminatory effects on racial minorities (disparate-impact discrimination). Ojo's complaint alleged disparate impact discrimination.

Farmers argued that Ojo's federal FHA claim was "reverse-preempted" by the McCarran-Ferguson Act, (MFA), 15 U.S.C. § 1012(b), which says: "No act of Congress shall be construed to invalidate, impair, or supersede any law enacted by any State for the purpose of regulating the business of insurance, . . . unless such Act specifically relates to the business of insurance." Under the MFA, state law reverse preempts federal law when three prongs are satisfied: (1) the federal law does not specifically relate to insurance; (2) the state law was enacted for the

purpose of regulating insurance; (3) the application of federal law to the case might invalidate, impair, or supersede state law. The Ninth Circuit was satisfied that the FHA does not specifically relate to insurance and that the Texas Insurance Code (TIC) provisions mentioned in its certified question were enacted for the purpose of regulating insurance. The sticking point was whether a cause of action for disparate impact discrimination under the FHA might "might invalidate, impair, or supersede" Texas state law. Resolution of this question turned on whether the TIC allows disparate impact claims based on use of credit scoring in the pricing of insurance, which prompted the en banc panel to ask the Texas Supreme Court about whether Texas law allows insurers to use race neutral credit scoring factors that have a disparate impact on minorities. The supreme court answered the Ninth Circuit's question in the affirmative, creating an irreconcilable conflict between Texas law and the FHA with respect to the use of racially neutral credit-scoring factors in the pricing of insurance.

Texas Insurance Code Provisions Governing Use of Credit Scoring. The Texas Insurance Code expressly prohibits "unfair discrimination" and specifically states that "[a] person may not charge ... an individual a rate that is different from the rate charged to other individuals for the same coverage because of the individual's race, color, religion, or national origin." TEX. INS.CODE § 544.002(a)(2). An exception to this provision provides that "[a] person does not violate Section 544.002 if the refusal, limitation, or charge is required or authorized by law or a regulatory mandate." *Id.* § 544.003(c). Farmers pointed out that § 559.051 authorizes the use of race-neutral credit score factors, and argued that this authorization is the exception to § 544.002, which is recognized in § 544.003. Section 559.051 permits an insurer to "use credit scoring, except for factors that constitute unfair discrimination, to develop rates, rating classifications, or underwriting criteria." *Id.* § 559.051; *see also id.* § 559.052(a)(1) ("An insurer may not use a credit score that is computed using factors that constitute unfair discrimination...."). The rub, of course, is determining what factors "constitute unfair discrimination," a question the Texas Insurance Code does not address directly. However, the Code does define an "unfairly discriminatory" rate as one that "is based wholly or partly on the race, creed, color, ethnicity, or national

origin of the policyholder or an insured." *Id.* § 560.002(c)(3)(C) (emphasis added).

The Texas Supreme Court's Reasoning. Addressing a question of first impression in the Texas courts, the supreme court interpreted the TIC to prohibit only intentional discrimination. Focusing on the TIC's prohibition of credit score factors "based on" race and of rates that differ "because of" race, the court gave at least seven reasons for its view race neutral credit factors that have a racially disparate impact are permissible under Texas law.

First, the language of the TIC is clear: intentional, deliberate race-based discrimination is prohibited, but the statute says nothing about race neutral credit-scoring factors which have racially disparate consequences. Thus, if a credit-scoring system does nothing but report credit actualities, i.e., tell the whole truth, its results are not race-based, even if there are racial recognizable differences in such scores, amongst various groups. This is crystal clear, said the Court, so there is no ambiguity in the relevant language of TIC.

Second, Texas courts which have considered discrimination problems have used the "race-based" idea, or system of ideas. They have not used the "results-from" standard, sought by Oyo.

Third, the Texas Labor Code uses the concept of being race-based as the foundation of unlawful dealing with race discrimination. It does not use a "results from" test. *See Quantum Chemical Corp. v. Toennies*, 47 S.W3d 273 (Tex. 2001).

Fourth, the Texas legislature has had the opportunity more than once to enact a statute forbidding a "results-in" standard for prohibiting the kind of conduct at issue here, but has elected not to do so. This is true even though the legislature knew about the disparity resulting from the use of the credit-scoring system under consideration in this case.

Fifth, while the FHA and other federal statutes interpreted by courts to prohibit disparate impact discrimination contain language similar to the TIC prohibiting discrimination "because of" race, those federal statutes also contain broad prohibitory language not found in the TIC. Federal courts have refused to find discriminatory impact liability when a statute focuses only on the nature of an action, and not on its effects. This is exactly the nature of TIC.

Sixth, the legislative history of the relevant TIC

acts is inconsistent with Ojo's position. Some legislators specifically had argued for a "resulting from" standard for discrimination to be added to the relevant TIC sections. In addition, there was a specific report from the Department of Insurance pointing out that the result of no "result-based" standard was significant consequences for racial minorities.

Seventh, although the Texas Fair Housing Act, Texas Property Code § 301.002(3), is explicitly designed to mirror the federal FHA, and may permit discriminatory impact liability, the TIC provisions are more recent and specific and therefore should prevail.

Concurring Opinions. There were two concurring opinions. They might be described as *Justice Willett v. Chief Justice Jefferson*. Justice Willett's lengthy opinion challenges the court's reliance on legislative history. He didn't even think the court's

historical analysis was mistaken; he only thought it was a mistake to set it forth in this opinion where it was not necessary. After all, the clarity-of-language regarding the relevant TIC sections was perfect. Chief Justice Jefferson's concurring opinion is much shorter and directed at refuting the first concurring opinion.

Comment

Is the logic of the situation as clear as everyone seems to agree? Consider this: The use of an underwriting system affects a racial minority negatively. The underwriters know this. Yet they intentionally use that system knowing that it will affect members of a racial minority negatively. So, we have knowledge of harm, and action accompanying the knowledge. Why is this not discrimination? // Quinn