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James J. McGraw

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AUTOMOBILE INSURANCE RATES: PROMULGATION, REGULATION, AND EQUAL PROTECTION

INTRODUCTION

THE INTEREST in the price one pays for automobile insurance continues to grow at a rapid pace. The reason for this growing consumer interest may be attributed to the equally increasing need for automobiles, the price paid for them, and consequently, the need for insurance protection. This insurance protection has developed into a matter of major economic consequence to the auto owner. It has evolved from a type of luxury into a necessity for most. With all due respect to the insurance industry and their justified motive of making money, the auto owner is dependent on the product of the industry. Although most states do not statutorily require all drivers to have insurance, insurance is accepted, not as an option, but as an integral part of the automobile or the operator's license. An uninsured automobile driver is by far the exception and not the rule.

Accordingly, the interest of the policyholder in the cost he must pay for his various insurance coverages is manifested in rate regulation. It is this regulation or the ability to control automobile insurance rates which is the primary concern of this comment. Traditionally, regulation has been effectuated through state legislation, state insurance departments, and the insurance industry itself. Whether the legislators, the insurance commissioners, or the insurance companies themselves sufficiently protect the interests of the insured is here in question. A brief discussion of the background of insurance regulation is followed by a criticism of the basic statutory law for promulgation and regulation of automobile rates.

The key to improved and efficient rate-watching is in the good faith efforts and perseverance of the policyholders themselves. Accordingly, an examination of the effects of consumerism along with a discussion of modern rate and regulatory developments is offered to show the present relationships and interactions of the groups involved.

In addition to controlling insurance rates via the traditional channels, there is also a fundamental and feasible consideration which can be effectively implemented into rate promulgation and regulation. This consideration is a constitutional one, and its proposal is the major impetus of this comment: that certain classifications comprising auto rates may be in violation of equal protection standards.

The following discussions and arguments are leveled at the insurance rates and surrounding controls in Ohio only because it is a convenient example. The condition of rates and their related problems in Ohio is fairly representative of the situation in most states.

THE BACKGROUND OF REGULATION

From 1868 to 1944 it was generally believed that insurance was not commerce and was therefore immune from federal regulation.¹ While the attempts to legislate federal control were generally unsuccessful, detailed laws were enacted in every state in the 1800's and early 1900's to protect the public from various problems and practices of insurance companies. Regulation of insurance rates did not begin until 1909 when Kansas adopted the first rate regulatory law affecting property and casualty insurance. But it was not until 1914 that the states first found themselves clearly possessed with the power to control rates. In 1914 the Supreme Court in *German Alliance Ins. v. Lewis*² held that insurance was a "business affected with a public interest," thereby giving the states regulatory power over insurance rates. Thereafter, every state sought to regulate rates.

The first Ohio legislation regarding insurance rate regulation came in 1917 as a result of a legislative committee study. This legislation required all fire insurance companies to become members of rating bureaus³ whose rates were to be filed with the Superintendent of Insurance if he so requested. The primary purpose of this legislation was to regulate price competition among the companies and keep them from driving their own rates to uneconomical levels. This mandatory bureau scheme remained in effect until the mid 1940's when the U.S. Supreme Court in *United States v. South-Eastern Underwriters' Assn.*⁴ held that intrastate activities of insurance companies constituted interstate commerce and were therefore subject to federal control under the Commerce Clause of Art. I sec. 8⁵ of the United States Constitution. As a direct result of the decision, the McCarren-Ferguson Act⁶ was enacted in 1945, restoring to the states the power to regulate insurance. The McCarren Act was a compromise between the Congressional advocates

¹ Paul v. Virginia, 75 U.S. (8 Wall.) 168 (1868).

² German Alliance Ins. Co. v. Lewis, 233 U.S. 389 (1914).

³ 107 OHIO LAWS 743-747 (1917), repealed in 1947.

⁴ United States v. South-Eastern Underwriters Ass'n, 322 U.S. 533 (1944).

⁵ U.S. CONST. art. I, § 8, cl. 3.

⁶ 15 U.S.C. §§ 1011-15 (1964). § 1012 provides:

(a) The business of insurance... shall be subject to the laws of the several States which relate to the regulation or taxation of such business.

(b) 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... *Provided:* That after June 30, 1948... the Sherman Act... the Clayton Act, and ... the Federal Trade Commission Act, as amended, shall be applicable to the business of insurance to the extent that such business is not regulated by State law.

of complete exemption from the Sherman Anti-Trust laws and the supporters of heavy surveillance by the federal government.⁷

The state commissioners of insurance, aided by the insurance companies, prepared model bills for regulating rate making for submission to state legislatures. Most of the states adopted such "all-industry" bills,⁸ being motivated by various factors involving improving the quality and scope of state regulation of rates, the desire to enable insurance companies to escape the provisions of federal statutes, and the desire to maintain intact state control and taxation of the insurance industry.⁹ Ohio adopted the all-industry approach¹⁰ for life insurance and the file and use approach¹¹ for previously unregulated casualty insurance. Ohio has undergone nebulous change in its rate regulation since the adoption of these laws in 1947.

LEGISLATION FOR PROMULGATION AND REGULATION

Under the Ohio laws,¹² rates must be based on loss experience, physical hazards, a reasonable margin for profit, and other relevant factors. A particular insurer may file directly with the Department of Insurance or indirectly through a rate bureau licensed by the Department.¹³ The rates,¹⁴ themselves, originate in the bureaus or in advisory organizations. Besides establishing rates, the rating bureaus have a further profound effect on the industry by promulgating underwriting rules, policy forms, and conducting loss-prevention inspections. In addition to rate bureaus, advisory organizations play a major role in rate competition. The Ohio Revised Code defines advisory organizations as, "[E]very group, association, or other organization of insurers . . . which assists insurers . . . in rate making, by the collection and furnishing of

⁷ For a discussion of motivating factors behind the Act see S. REP. NO. 20, 79th Cong., 1st Sess. p. 41 (1945); See, e.g., 91 Cong. Rec. 1087 (1945); 90 Cong. Rec. 6532 (1944).

⁸ See Rose, *State Regulation of Property and Casualty Insurance Rates*, 28 O.S.L.J. 669, 696 (1967).

⁹ S. KIMBALL, *ESSAYS IN INSURANCE REGULATION* 29, 30 (1966).

¹⁰ Under the all-industry laws, proposed rates must be filed with the insurance commissioner prior to use. Actual approval of rate filings is not required because rates are deemed approved if not disapproved within a given number of days.

¹¹ Under file and use, rates and supporting materials must be filed for informational purposes with the appropriate state regulatory agency. Rates become effective upon filing or at a later date specified in the filing.

¹² OHIO REV. CODE §§ 3935.03, 3937.02 (Page 1971).

¹³ OHIO REV. CODE §§ 3935.04(B), 3937.03(B) (Page 1971).

¹⁴ "Premium" and "rate" are commonly used interchangeably. Technically, the "rate" is the cost of insurance per unit; used as a means or base for the determination of premiums. "Premium" is the total of the "rates" for all the units in a given policy. M. LEVY, *A HANDBOOK OF PERSONNEL INSURANCE TERMINOLOGY* 421, 453 (1968).

loss or expense statistics or by the submission of recommendations, but which do not make filings. . . ."¹⁵

Such groups must operate pursuant to other provisions of rate regulatory statutes. Neither the rate bureaus nor the advisory organizations are governmental bodies, however the Ohio Department of Insurance has express statutory authority to investigate the operations of both.¹⁶

The Ohio Revised Code is anything but specific as to the standards to be used in rate composition. Section 3937.02 (D) states that casualty rates may not be "excessive, inadequate, or unfairly discriminatory." The precise interpretation of these terms is not found in the Code and their regulatory scope has been narrowed appreciably so that one may say these legislative goals are reasonableness, adequacy and equity, terms that mean nothing more than expressions of generally perceived concepts concerning insurance.¹⁷ By way of superficial application, the principal cause for the erosion of the three statutory terms of art involves poor promulgation by the legislature only paying lip service to the idea of strict regulation of insurance rates. Nevertheless, the duty of the Department of Insurance remains the enforcement of the three regulatory terms of art.

Unfortunately the failure of the Ohio Revised Code to set guidelines which may be referred to in order to construe the words "excessive," "inadequate," and "unfairly discriminatory" has resulted in allowing insurance companies much freedom in affecting the economic priorities of the consumer. Clearly then, the key to regulation of casualty rates by the Ohio Department of Insurance is their enforcement of Code section 3937.02 (D). Enforcement, of course, directly depends on interpretation. What are the theories and considerations behind the department's interpretation of section 3937.02 (D)? What can the legislature do to make this interpretation more consistent with the goals of the statutes in protecting the public welfare as opposed to merely the industry's welfare? Can the insurance consumer take any measures to promote affordable protection or will his pleas be ignored by the insurance machine?

In general, rate excessiveness has been determined by setting a goal of rate reasonableness. The idea of "reasonableness" seems to have originated with *United States v. Chicago, M., St. P. and P. R.R.*¹⁸ in which the Court said: "On its face the provision that rates shall not be excessive . . . appears to establish a zone of reasonableness between the maxima and

¹⁵ OHIO REV. CODE §§ 3935.12(A), 3937.09(A) (Page 1971).

¹⁶ OHIO REV. CODE §§ 3935.11, 3935.12, 3937.11 (Page 1971).

¹⁷ Rose, *Regulation of Property and Casualty Insurance Rates in Ohio*, 32 O.S.L.J. 487, 498 (1971).

¹⁸ *United States v. Chicago, M., St. P. & P. R.R.*, 294 U.S. 499, 506 (1935).

minima within which a carrier is free to fix its charges." It would seem that rate reasonability should be a combination of reasonable profits after expenses to the insurers and economic feasibility to the policyholders.

In defining "excessive," however, the Ohio Department of Insurance has looked to the level of underwriting profits for each company involved in a particular rate filing. If the rate will provide an underwriting return or profit above a certain target level, which depends on that company's past underwriting returns, the rate is characterized as excessive.¹⁹ Under this method, what is excessive for one company may not be for another, regardless of the fact that it is excessive to the insured.

Just how much the insurance department has ignored the customer historically in determining what rates are "excessive" is open for argument. Notwithstanding the past, the efforts of consumerism are causing economic feasibility to become at least a consideration in rate nonexcessiveness. The concept of economic affordability rests on the concept that insurance, in this case automobile insurance, is such a vital ingredient for the effective functioning of the economy and the social system that no one should be denied it.²⁰

The best way to determine what is "excessive" should not depend solely on how hard different pressure groups ride the back of the insurance commissioner. Express statutory definitions accounting for the interests of all parties should be promulgated. The test used in Indiana²¹ and several other states²² is a step in this direction. These laws provide: "No rate shall be excessive unless such rate is unreasonably high for the insurance coverage provided and a reasonable degree of competition does not exist in the area with respect to the classification to which the rate is applicable."

Not unlike excessiveness, "inadequacy" has been determined by focusing on the level of underwriting profits. Rates must be adequate not only to generate an insurance fund sufficient for paying legitimate claims and related expenses, but also to offset the drain on surplus resulting from an increasing number of policyholders, to provide for expanded contingency reserves, and to provide stock insurers a means to assure a return to investors.²³ The need for rate adequacy was inspired by many company insolvencies in the 1800's. These company failures were caused by high competition for customer business in which the insurers merely

¹⁹ Rose, *supra* note 17 at 502.

²⁰ See, e.g., *In re Filing Made by N.C. Fire Ins. Rating Bureau*, 165 S.E.2d 207, 219 (N.C. Sup. Ct. 1969).

²¹ IND. ANN. STAT. § 39-5341(4) (Burns Supp. 1972).

²² See, e.g., CAL. INS. CODE § 1852(a) (West 1972); GA. CODE ANN. § 56-507(a) (Supp. 1972).

²³ Rose, *supra* note 17 at 500.

priced themselves out of existence. Today, however, insolvencies result from factors other than inadequate rates, such as inept internal management, and consequently the adequacy standard takes a third place in importance to "excessiveness" and "unfair discrimination." Notwithstanding its diminished priority, a statutory test for rate adequacy offers the best method for uniform application of the insurance department's duties.

Such a desirable statute provides:

No rate shall be held to be inadequate unless such rate is unreasonably low for the insurance coverage provided and is insufficient to sustain projected losses and expenses; or unless such rate is unreasonably low for the insurance coverage provided and the use of such rate has, or if continued, will have, the effect of destroying competition or creating a monopoly.²⁴

It seems that "unfair discrimination," even in absence of a statutory definition, has created few problems. Generally it has meant that subject to practical limitations, rates for various classes must be proportional to expected claims or losses and expenses attributable to each class of insurance.²⁵ So as long as each homogeneous group of policyholders pays its proportionate share to cover the insured's loss ratio in that group, the rates are considered equitable. Although this concept of equity has met little opposition in the past, it makes discrimination possible unless the groups and classifications of policyholders are regulated. In other words, the greater the number of groups or classifications, the greater the possibility that distinctions will arise which reflect social inequalities which in turn result in inequitable rates. To most, it is readily understandable why insurers charge a higher premium to cover the reckless driver with several past accidents. But from an equitable viewpoint it is difficult to understand why individuals should be required to pay higher rates than others owing to factors over which they have no control, such as race, sex, or geographical location. It is these types of classifications which may be discriminatory. While there is apparently an absence of substantial public interest in this social equity, this does not mean the discrimination does not exist. Whether or not there is a Constitutional violation involved will be examined later.

EFFECTS OF CONSUMERISM

It is becoming clearer every day that the insurance industry must be more cognizant of the customers' needs and wants. The consumer is entitled to understandable product and service information.²⁶ If the

²⁴ IND. ANN. STAT. § 39-5241(4) (Burns Supp. 1972).

²⁵ OHIO REV. CODE §§ 3935.09, 3937.08 proscribe misclassifications by implication.

²⁶ *Contra*, THE NATIONAL UNDERWRITER, Dec. 22, 1972, at 1 (property and casualty ins. ed.).

consumer is denied a satisfactory voice in the industry's programs or at least an easy access to corrective action, he will surely turn toward the lawmakers for redress of his grievances. Perhaps the perfect example of lawmakers heeding to consumerism is the no-fault concept of liability insurance.²⁷ The goal of the consumer is affordable insurance protection. Just how to affect the price of insurance in a just way, balancing his goal with that of the industry for competition, is the problem he faces. Direct contact with the insurance industry, tougher regulation by the Department of Insurance and lastly, new legislation are the three avenues open to the reform of the present situation.

Modern consumerism, a broad-based and diverse movement to improve the quality of goods, is an outgrowth of the affluent, highly organized movement presently under the leadership of Ralph Nader.²⁸ Consumerism's biggest achievement in the insurance industry has been to plant firmly in the minds of the public and politicians the idea that every person has the right to buy insurance at an affordable price, thus overturning the basic principles of risk and rating which have existed for centuries. These principles have centered in the past, not around affordability, but around loss experience. Other consumerism interests have involved such things as credit reports, auto insurance systems, health care and financing, and safety in many forms.²⁹

A regulatory product of the Ralph Nader effort is the belief that insurance commissioners wear two hats with respect to the consumer. They represent a general "public interest" which is a reconciliation of the conflicting interests of insurers, insureds, and citizens indirectly affected by the action or inaction of the industry and the insurance departments. These third parties include the victims of unsafe products, purchasers of products and services who might bear the cost of loss or of insurance against loss, stockholders and investors, product design experts, academicians, and insurance company employees and agents.

Thus commissioners have the double duty of adjudicating disputes between particular interests or individuals and of seeing to it that interests otherwise unrepresented be heard and considered, and that if they are not formally heard, that they nevertheless be considered.³⁰

It is conceded by many industry officials and regulators that consumer interests have become a major factor in rate making or rate

²⁷ A currently successful state no-fault law is Mass. Stat. 1970, ch. 670. For a disfavorable opinion of federal no-fault insurance see Smith, *Federal Automobile Insurance, The Defense Bar's Position*, 38 INS. COUNS. J. 413 (1971).

²⁸ THE NATIONAL UNDERWRITER, Dec. 15, 1972, Part I, at 1 (property and casualty ins. ed.).

²⁹ *Id.* at 34.

³⁰ THE NATIONAL UNDERWRITER, Sept. 22, 1972, at 41 (property and casualty ins. ed.).

regulation. But pragmatically speaking, little attention has been given to the insured's need for a voice in these matters. This neglected goal of rate regulation can be approached by educating the consumer on the rate-making and rate regulatory processes and by providing him with effective ways of expressing his views or obtaining relief.

Most individuals know little about the insurance enterprise and are undoubtedly intimidated by the complexity of its product. Their lack of knowledge has resulted in animosity toward companies and agents alike. Neither the insurance department nor insurers provide the public with information about the types of insurers offering coverage, the kinds and costs of available coverage, the rights of policyholders under the rate regulatory statutes, or the activities and services of the department.³¹ If the public could understand auto insurance and its inherent rating system, the high wall of distrust would be lowered considerably. The query then is how should insureds become informed?

The information insureds do receive concerning the auto insurance industry is mainly in the form of sales advertising. Arguably, this type of "education" can itself be seen as opposed to the public interest.³² But on the other hand, maybe some of the need for restrictive legislation and administrative regulation could be alleviated by the industry itself, by means of an open and honest communication program which justifies the policyholder's related coverages in straight-forward, non-technical language.³³

Realistically, the better view appears to be that the insurance companies cannot be relied upon to inform the public due to their past performance. The insurance department, acting as an instructor, would discover a much more receptive audience. Several possibilities for information dissemination by the Ohio Department of Insurance have been proposed. One is the conducting of public hearings on major bureau, deviation, and independent rate filings. Another, perhaps more effective method, is a consumer information program.³⁴

Once the consumer knows some of the principles which compose and control his auto insurance premium he is in a much better position to express his views and claims to the insurance department when given the opportunity to do so. One such vehicle used for expression of consumer interests is insurance department advisory committees formed pursuant to Ohio Revised Code section 121.13.³⁵

³¹ Rose, *supra* note 17, at 514, 515.

³² Smith, *The Miscegenetic Union of Liability Insurance and Tort Process in the Personal Injury Claims System*, 54 CORNELL L. REV. 645, 703 (1969).

³³ THE NATIONAL UNDERWRITER, Dec. 1, 1972, at 6 (property and casualty ins. ed.).

³⁴ Rose, *supra* note 17, at 515.

³⁵ OHIO REV. CODE § 121.13 authorizes departmental directors, subject to the approval of the governor, to appoint advisory groups to aid them in conducting their work.

On the national level, in September of 1972, Ralph Nader and Peter J. Patkas, on behalf of the Corporate Accountability Research Group, introduced eight specific proposals for expanded and more meaningful participation by consumers and consumer spokesmen in the affairs of the National Association of Insurance Commissioners (NAIC). These proposals include:

- Inclusion of consumer advocates on NAIC advisory committees;
- Appointment by NAIC of a consumer affairs officer;
- Publication of citizens' handbooks on the industry's regulation;
- Sponsorship of a monthly or quarterly consumer newsletter highlighting regulatory developments of interest to the public.³⁶

Finally, protection of the insureds' interests and rights may be advanced by way of class actions.³⁷ Class actions for insureds is a recent development which has been greatly enhanced by Rule 23 of Ohio's new Rules of Civil Procedure effective July 1, 1970. In regards to the constitutional attack proposed *infra* on the present composition of insurance rates in Ohio, a class action on behalf of auto insureds in a particular classification would be appropriate.³⁸

RATING AND REGULATORY DEVELOPMENTS

In April 1971 the industry formed the Insurance Service Office from six smaller rating bureaus. The ISO at that time jointly set and filed standard rates for all but five of the major auto insurers.

As discussed earlier, the Department of Insurance does not compose the auto rates itself. The rates are submitted to them and they then determine whether or not the new rate(s) comply with the requirements of Ohio Revised Code section 3937.02 (D). But in recent years "open-rating" has been introduced in Ohio and a few other states to promote competition. "Open-rating" generally allows companies to change rates before notifying insurance authorities. While the Department of Insurance may still strike down the rate change, its approval is not required for the new rates to take effect. The Insurance Services Office is now promoting the success of "open-rating" by making sure that company personnel do not participate in the rate-making process for rates promulgated by them.³⁹

³⁶ For a complete enumeration of the eight proposals see THE NATIONAL UNDERWRITERS, Sept. 16, 1972, at 1 (life and health ins. ed.).

³⁷ See generally Starrs, *The Consumer Class Action—Part I: Consideration of Equity*, 49 B. U. L. REV. 211 (1969); Starrs, *The Consumer Class Action—Part II: Considerations of Procedure*, 49 B. U. L. REV. 407 (1969).

³⁸ *Id.* Part II at 496.

³⁹ The Wall Street Journal, Dec. 14, 1972, at 3 col. 2. *Contra*, THE NATIONAL UNDERWRITER, Dec. 15, 1972, Part I, at 3 (property and casualty ins. ed.).

The latest trend in rate-making is for auto insurers to phase out jointly setting standard insurance rates in an effort to further increase price competition. The effect is lower rates for the customer⁴⁰ and the Insurance Service Office taking on more of an advisory capacity. The rate cuts have been made possible by a surge in profits, accompanied by anticipated loss reductions from 1973 model automobiles.⁴¹ Although everyone is naturally in favor of lowering auto insurance premiums, the Department of Insurance will have to keep a close watch on insurers, curbing their zest for volume with the reminder of their huge underwriting losses of the 1960's.⁴²

At the other end of the scale, not all attempted revisions of auto rates in Ohio have been in the consumer's favor, nor have they all been approved by the insurance commissioner. Included in the proposed revision of rates, most of which became effective January 1, 1973,⁴³ was a provision assigning for the first time separate rates to Ohio Territories 11, 12, and 13.⁴⁴ As a result, Territory 11 showed an increase in every coverage category. The reason for the increase may be categorized as higher losses in an underprivileged neighborhood. Fortunately the commissioner found the increase inordinate, held that it could well indicate excessiveness or unfair discrimination or both in the rating application and/or process, and ordered that Territories 11, 12, and 13 continue to be combined for rate-making purposes.⁴⁵ The overall effect of

⁴⁰ On Nov. 9 and 10, 1972, the Insurance Services Office of Ohio and the Ohio Bureau of Casualty Insurers respectively, made revision filings with the Ohio Dept. of Insurance under Ohio Rev. Code § 3937.03. This revision was submitted with respect to Territorial base rates applying to Private Passenger Automobile Liability, Physical Damage and Medical Payments Coverage for both the Private Passenger Automobile Manual and the Special Package Automobile Policy Supplement. The filings indicated that this revision of rates would produce an overall percentage change for the State of Ohio which would represent a reduction of 9.6% (statewide average). The statewide average reduction for the Family Automobile Policy would amount to 8.6%. Finally, the average reduction for the Special Package Automobile Policy would amount to 8.6%. The computation in this revision utilized 2.92 years of projection. The proposed effective date for this revision was Jan. 1, 1973, with respect to all policies written to become effective on or after Jan. 1, 1973.

⁴¹ All 1973 model autos must meet federal bumper standards regarding damageability on minor impact. *The Wall Street Journal*, Dec. 14, 1972, at 3, col. 3.

⁴² "The increasing pressure to give undue weight to the latest favorable year of experience to produce a desired competitive result, despite the lesson of history that longer experience periods are sounder to stabilize results and markets, must be resisted by regulator and regulated alike." *The Wall Street Journal*, Dec. 14, 1972, at 3, col. 2.

⁴³ *Supra*, note 40.

⁴⁴ Territories are geographical areas within a state divided according to the various risks present which are in turn reflected in the base rates for the different coverages and their limits. Ohio is divided into twenty-three different territorial classifications. ISO filing effective Jan. 1, 1973.

⁴⁵ Order of the Ohio Dept. of Insurance served on The Insurance Services Office of Ohio and the Ohio Bureau of Casualty Insurers Nov. 20, 1972.

this order results in equality of premiums among policyholders within those territories and also manifests to those who consider the department insurer-biased the evidence that they will defend the interests of the insurance consumer. Whether their finding of unfair discrimination was prompted by the increasing awareness and accompanying pressures of the consumer movement remains to be seen.

RATE COMPOSITION AND THE EQUAL PROTECTION CLAUSE

Traditional automobile rate regulation has been discussed, together with its background and its present status. The consumer sector and its ever-increasing interest in this regulation has also been examined. But what about the rates themselves? As they are now approved by the insurance commissioner, do these rates actually meet the statutory and constitutional standard of being non-discriminatory? Have these rates ever been free from discrimination? While race and ethnic background are not variables in rate composition, geographical location is. Could not such a variable as neighborhood location indirectly result in race or ethnic discrimination? What about some of the other classifications that go into rate make-up? sex? marital status? Should any of these classifications be questioned under old or new equal protection standards?

The idea of discrimination in automobile insurance rates is not new. In June of 1968, the Senate Antitrust and Monopoly Subcommittee opened hearings on the automobile insurance industry.⁴⁶ In those hearings the New York City Human Rights Commissioner charged discrimination against low-income and minority groups in the ghettos. He said this action is very subtle, sophisticated and accepted. He pointed out that refusals to insure Negroes and Puerto Ricans in New York are based on geographical locales, rather than on the pure basis of race.⁴⁷ In a stronger attack, the directing attorney of the Santa Rosa, California, office of Rural Legal Assistance, charged that the industry is guilty of widespread discrimination against the "little man, the brown, and the black man."⁴⁸

There appear to be basically two types of discrimination here. One involves a flat refusal by a company to provide insurance coverage to a group of people in a particular geographical area. In the other type of discrimination, citizens in unfavorable or high risk areas are offered insurance policies, but at a higher premium than citizens in other sections of the community whose qualifications as to age, driving record, etc., are identical. It is this latter type with which the discussion herein is concerned, because it is this type of discrimination with which the

⁴⁶ *Hearings on S. Res. 233 Before the Subcomm. on Antitrust and Monopoly of the House Comm. on the Judiciary*, 90th Cong., 2nd Sess., pt. 13 (1968).

⁴⁷ *Id.* at 7527.

⁴⁸ *Id.* pt. 14.

insurance department is directly involved. More specifically, it is here submitted that automobile insurance rates using geographical locale as one variable may be in violation of the equal protection clause of the Fourteenth Amendment of the United States Constitution. In addition to geographic location, there are other classifications which have a major impact on a policyholder's automobile rate. These include, but are not limited to, good student discount, sex, marital status, and the distance the vehicle is driven to work. Arguably these classifications may also be the cause of unconstitutional private passenger automobile rates.

At the outset of this equal protection evaluation, it is imperative to establish that the Fourteenth Amendment guarantees are enforceable against the insurance companies. The mandate of *Reitman v. Mulkey*⁴⁹ proclaims that a state statute which authorizes or encourages discrimination significantly involves that state in private discrimination contrary to the Fourteenth Amendment. The Ohio Revised Code section 3937.02(C) states:

Risks may be grouped by classifications for the establishment of rates and minimum premiums. . . .

Classifications or modifications of classifications, or any portion or any division thereof, of risks may be predicated upon size, expense, management, individual experience, purpose of insurance, location or dispersion of hazard, or any other reasonable considerations, provided such classifications and modifications apply to all risks under the same or substantially the same circumstances or conditions. . . .⁵⁰

In addition to *Reitman, Shelly v. Kraemer*⁵¹ may be construed to hold that state action is present when groups which practice discrimination are licensed by the state.⁵² Ohio Revised Code section 3937.03 (B)⁵³ permits an insurer to become a member of a licensed rating organization; section 3937.05 deals with application for and issuance of a license as a rating organization, and section 3937.05(A) specifies: "If the superintendent finds that the applicant is . . . qualified to act as a rating organization . . . he shall issue a license specifying the kinds of insurance or subdivisions thereof for which the applicant may act as a rating organization."⁵⁴ Thus it is conclusive that the requisite significant state action is present in the Ohio automobile rate situation and the Fourteenth Amendment is available to protect the policyholder if his rights have in fact been abrogated.

⁴⁹ *Reitman v. Mulkey*, 387 U.S. 369 (1967).

⁵⁰ OHIO REV. CODE § 3937.02(C) (Page 1971).

⁵¹ *Shelley v. Kraemer*, 334 U.S. 1 (1948).

⁵² Mr. Justice Douglas concurring in *Reitman v. Mulkey*, 387 U.S. 369, 385 (1967).

⁵³ OHIO REV. CODE § 3937.03(B) (Page 1971).

⁵⁴ OHIO REV. CODE § 3935.05(A) (Page 1971).

In order to appreciate the value and feasibility of any equal protection attack on insurance rates, it is important to review in capsule form the development of equal protection and its present impact on economic legislation. There are two different approaches or tests which have grown up in the modern court and are used today. Historically, however, the impact of the equal protection clause was very limited, both in frequency of implementation and in scope of intervention. Court interference with economic legislation usually involved substantive due process rather than equal protection. In the 1940's the Supreme Court began to develop its hands-off approach toward intervention in economic legislation and substantive due process became history.⁵⁵ Soon thereafter Justice Jackson commented on the traditional equal protection test reflecting its narrow application by saying: "Invocation of the equal protection clause . . . does not disable any governmental body from dealing with the subject at hand. It merely means that the prohibition on regulation must have a broader impact."⁵⁶ This traditional equal protection criteria condoned much legislative permissiveness. Under the old standard the classification imposed by the state statute must be reasonable, not arbitrary, and must rest upon some ground of difference having a fair and substantial relation to the object of the legislation, so that all persons similarly circumstanced are treated alike.⁵⁷ The old test did prove and still proves successful under the proper circumstances.⁵⁸

The increasing popularity of equal protection as a widely available substantive restraint on legislation blossomed during the Warren Court and is partially explainable by a desire of some activist Justices such as Justice Douglas to protect values perceived as basic without reverting to the pitfalls of substantive due process.⁵⁹ The classic decision by Justice Douglas applying the new equal protection test is *Harper v. Virginia Board of Elections*⁶⁰ in which a Virginia poll tax was struck down. The Court held that where the law involved a suspect classification on the basis of wealth or the fundamental interest of the right to vote, any infringement must be carefully scrutinized. The ambiguity left by *Harper* as to whether a classification based on wealth could call for strict scrutiny analysis independent of a fundamental interest was later clarified in the affirmative in *McDonald v. Board of Election Commissioners*.⁶¹ The

⁵⁵ See, e.g., *Williamson v. Lee Optical Co.*, 348 U.S. 483 (1955); *Day-Brite Lighting Inc. v. Missouri*, 342 U.S. 421 (1952).

⁵⁶ *Railway Express Agency v. New York*, 336 U.S. 106, 112 (1949).

⁵⁷ *F. S. Royster Guano Co. v. Virginia*, 253 U.S. 412, 415 (1920).

⁵⁸ E.g., *Reed v. Reed*, 404 U.S. 71 (1971); *Morey v. Dowd*, 354 U.S. 457 (1957).

⁵⁹ See *Griswold v. Connecticut*, 381 U.S. 479 (1965).

⁶⁰ *Harper v. Virginia Bd. of Elections*, 383 U.S. 663 (1966).

⁶¹ *McDonald v. Board of Election Comm'rs*, 394 U.S. 802 (1969).

purpose of the *Harper* scrutinization was defined in *Kramer v. Union Free School District No. 15*.⁶² When legislation results in infringement of a suspect classification or a fundamental interest, the court must scrutinize the law to determine whether the exclusions are necessary to promote a compelling state interest.⁶³

The popularity of this new equal protection test has expanded swiftly and significantly. In addition to suspect classifications based on race,⁶⁴ wealth,⁶⁵ and alienage,⁶⁶ the list of judicially determined fundamental interests include the right to procreate,⁶⁷ the right to vote,⁶⁸ rights of illegitimate children,⁶⁹ and the right to travel.⁷⁰ To date, the Burger Court has refused to extend fundamental rights to include necessities⁷¹ and suspect classifications to include sex.⁷² Nevertheless, the new equal protection test is as viable as ever and inclusion of necessities and sex as well as First Amendment rights,⁷³ occupation,⁷⁴ and marital status,⁷⁵ are possible future additions to this compelling interest test. Whether the Court actually will expand new equal protection into these areas or even into other rights or classifications not yet contemplated remains only for educated speculation. Regardless, the door is now open for much economic legislation to come under constitutional attack. Finally then, we are left with a two-tier analysis: strict scrutiny where fundamental rights or suspect classifications are involved; minimum scrutiny in other areas.

The purpose here intended is to argue that some of the classifications involved in composition of premiums for private passenger automobiles violate equal protection by showing no "rationality" or "compelling interest" for the classifications. In order to facilitate demonstration of the change in a policyholder's premium resulting from some of the classifications used, a hypothetical insured is suggested. This insured owns

⁶² *Kramer v. Union Free School District No. 15*, 395 U.S. 621 (1969).

⁶³ *Id.*

⁶⁴ *See, e.g., Slaughter-House Cases*, 83 U.S. (16 Wall.) 36 (1873).

⁶⁵ *See, e.g., Douglas v. California*, 372 U.S. 353 (1963); *Griffin v. Illinois*, 351 U.S. 12 (1956).

⁶⁶ *E.g., Graham v. Richardson*, 403 U.S. 365 (1971).

⁶⁷ *E.g., Skinner v. Oklahoma*, 316 U.S. 535 (1942).

⁶⁸ *E.g., Harper v. Virginia Bd. of Elections*, 383 U.S. 663 (1966).

⁶⁹ *E.g., Levy v. Louisiana*, 391 U.S. 68 (1968).

⁷⁰ *E.g., Shapiro v. Thompson*, 394 U.S. 618 (1969).

⁷¹ *E.g., Lindsey v. Normet*, 405 U.S. 56 (1972); *Richardson v. Belcher*, 404 U.S. 78 (1971).

⁷² *See, e.g., Reed v. Reed*, 404 U.S. 71 (1971).

⁷³ *See, e.g., Williams v. Rhodes*, 393 U.S. 23 (1968).

⁷⁴ *See, e.g., Williamson v. Lee Optical Co.*, 348 U.S. 483 (1955); *Kotch v. Board of River Pilot Comm'rs*, 330 U.S. 552 (1947).

⁷⁵ *See Eisenstadt v. Baird*, 405 U.S. 438 (1972).

a 1973 mid-priced sedan and needs coverage for normal limits.⁷⁶ Insured is twenty-four, single, has a clean driving record, and drives to work one mile each way. He lives in Twinsburg, Ohio. Under these conditions his annual premium is \$446. However, if insured lived in the community of East Cleveland, Ohio, his premium would be \$590. On its face, this rather huge inconsistency in rates does not appear too startling, at least from an equal protection standpoint. Most assuredly, insurers can explain the rate differential between Twinsburg, a Cleveland suburb, and East Cleveland by their arsenal of actuarial data showing such facts as more people, cars, thefts, and accidents in the latter community than in the former. The theory then for justification of classifications based on geographical locale is that people residing in an area with a higher insurance loss ratio should be the ones to pay the price rather than policyholders in less hazardous communities. Notwithstanding this "justification," do geographical classifications advocate racial discrimination?

Twinsburg, Ohio is 99.2% white while 59.8% of East Cleveland is composed of blacks and other races.⁷⁷ The effectiveness of this percentage difference is somewhat deflated, however, by the overall population of the two areas: 6,432 in Twinsburg to 39,600 in East Cleveland.⁷⁸ Perhaps a case for racial discrimination is best exemplified by comparing East Cleveland with Cuyahoga Falls, Ohio. If insured lived in Cuyahoga Falls, his annual premium would be \$385, a difference of \$205. Yet Cuyahoga Falls is populated by 49,678 people, some 10,000 more than East Cleveland, 99.8% of whom are white.⁷⁹ Are blacks categorically more of a risk to insurance companies than whites? Unfortunately, the impact of any discrimination based on race may be lessened by the showing of white communities with rates as equally astronomical as East Cleveland. Perhaps it is sufficient to speak in generalities. The higher insurance premiums center in and around the large cities. Likewise the black population centers in and around these cities. Between 1960 and 1970 the black population inside central cities increased 20.8% while the white population decreased 7.8%.⁸⁰ Consequently, it is the blacks, who can generally least afford insurance, who are forced to pay higher rates for the same protection. Notwithstanding the fact that whites in some areas pay the same rate as blacks, the impact of the classification falls more

⁷⁶ Bodily Injury \$15,000 per person/\$30,000 per occurrence; Property Damage \$10,000 per occurrence; Medical Payments \$1,000 per occurrence; Full Coverage Comprehensive; \$100 Deductible Collision; Uninsured Motorist \$12,500 per person/\$25,000 per occurrence. Premiums are based on the ISO filing effective Jan. 1, 1973.

⁷⁷ U.S. DEPT. OF COMMERCE, BUREAU OF THE CENSUS, GENERAL POPULATION CHARACTERISTICS, 1970 CENSUS OF POPULATION, OHIO 78, 169.

⁷⁸ *Id.*

⁷⁹ *Supra*, note 77, at 168.

⁸⁰ *Id.* at 72.

heavily on the blacks. The law, unequal in its application, is enough to condemn it as incompatible with any fair conception of equal protection of the laws.⁸¹ If racial discrimination is the case, then, classifications based on geographical locale are susceptible to strict scrutiny equal protection standards.

In addition to geographical classifications advocating racial discrimination, what about unequal treatment based on wealth? As previously noted, wealth, like race, is a suspect class theoretically calling for application of the compelling interest test.⁸² Using the same geographical classifications as above, equal protection is violated based on economic status as well as race. The 1969 median income of families and unrelated individuals was \$12,095 in Twinsburg, Ohio while the median earnings for East Cleveland males sixteen years of age and over in the experienced civilian labor force was only \$7,595.⁸³ Clearly, at least when using Twinsburg and East Cleveland, the economically disadvantaged or "poorer" policyholder is forced to pay a higher price for the same insurance coverages as a policyholder in a wealthier community. It may be argued, of course, that a resident of such an underprivileged area is free to move to another community to escape this equal protection violation. Practically, however, it is that resident's economic wealth which freezes him in his neighborhood to exist with the surrounding consequence without redress. Notwithstanding the arguable weight of this equal protection attack based on wealth as a suspect class, the application of the compelling interest test is at least by definition proper.

It must be noted that the successfulness of this "wealth" argument is very doubtful at the present time based on recent Supreme Court decisions. The Court has been disappointing in consistently refusing to apply their strict scrutiny based on wealth as a suspect class in cases involving bankruptcy filing fees⁸⁴ and "good time" for criminal defendants.⁸⁵ But the most astonishing and detrimental example of the Burger Court's avoidance of the "wealth" class was seen in *San Antonio Independent School District v. Rodriguez*⁸⁶ where the Court upheld the Texas school financing system which is largely dependent on local property taxes. In upholding this system, similar to that used in almost all of the states, Mr. Justice Powell ignored "wealth" and held that education is not a fundamental right. Unfortunately, it appears that the

⁸¹ *Yick Wo v. Hopkins*, 118 U.S. 356 (1886).

⁸² *E.g.*, *Douglas v. California*, 372 U.S. 353 (1963).

⁸³ U.S. DEPT. OF COMMERCE, BUREAU OF THE CENSUS, GENERAL SOCIAL AND ECONOMIC CHARACTERISTICS, 1970 CENSUS OF POPULATION, OHIO 662, 748.

⁸⁴ *U.S. v. Kras*, 93 S. Ct. 631 (1973).

⁸⁵ *McGinnis v. Royster*, 41 U.S.L.W. 4259 (U.S. Feb. 21, 1973).

⁸⁶ 41 U.S.L.W. 4407 (U.S. Mar. 21, 1973).

feasibility of using wealth as a suspect class is non-existent under the present make-up of the Court. Fortunately, however, history has proven the flexibility of the Court with respect to reversing their prior rulings.

Another classification, relatively new in the auto insurance industry, is known as the "good student discount." This classification would seem to induce youthful drivers to strive for high grades in school to reap approximately a 15% deduction on their auto insurance premiums. Insured's premium would only be \$414 instead of \$446. Undoubtedly, "A" students must have a somewhat better driving record than "C" students or this discount would not exist. Yet, this classification seems totally unreasonable and arbitrary. This division of students into "good" and "not good" is a clear example of insurance companies revoking the basic idea of risk spreading. Under the rationality test, the classification must have a fair and substantial relation to the object of the legislation, so that all persons similarly circumstanced shall be treated alike.⁸⁷ This good student class emasculates the phrase "similarly circumstanced." If "good students" is such a rational classification it appears any class could be a rational one merely by showing they have a better driving record. Why not give a discount to people who attend church on Sunday? Actuaries could probably find that religious people have better records than the non-religious.

Furthermore, from a speculator's viewpoint, the degree of over-inclusiveness and under-inclusiveness must be great.⁸⁸ One's driving record can only be related to his grades in school through sheer coincidence. A reward for superior grades in school which is what this classification presents, lacks not only a fair and substantial relation to the object of insurance legislation; it lacks any relation whatsoever. It is a class within a class, repugnant to any purpose of risk spreading and in violation of traditional equal protection standards.

A classification of which auto owners often lack cognizance involves the distance the automobile is driven to work. If insured drove four miles to work every day instead of one or two, his premium would be \$479, an increase of \$33. This classification of drivers is readily susceptible to the traditional attack as involving excessive over-inclusion and under-inclusion. Pragmatically, this class is based on the number of miles the car is driven. The longer the auto is on the road, the greater the chance for it to be involved in some type of liability to the insurer. But on the other hand, if an automobile is classified for "pleasure" use, the total mileage actually driven is irrelevant. Accordingly, a "pleasure" driver could operate his vehicle all day every day and pay a lower premium than the

⁸⁷ 253 U.S. at 415.

⁸⁸ For the classic study of the traditional equal protection standards see Tussman & tenBroek, *The Equal Protection of the Laws*, 37 CALIF. L. REV. 341 (1949).

working man who only drives eight or ten miles per day. If there is a rationality for the "drive to work" class, it seems to be defeated by its application, thereby making the classification unreasonable and incompatible with equal protection standards.

Since the "pleasure" drivers can put more mileage on their automobiles at a lower premium, doesn't this adversely affect working men, who drive more than several miles to work, in another way? What about the right to pursue a particular occupation?⁸⁹ Undoubtedly, this "drive to work" classification would not be likely to cause one to refrain from engaging in a particular job. However, total deprivation of the right is not required. Under the new equal protection test, classifications which might invade or restrain a fundamental interest must be closely scrutinized and carefully confined.⁹⁰ In other words, any infringement of the right makes the test applicable. Does not this increased premium for those who drive to work over a specific distance infringe on their right to employment? Is not this a penalty related to employment? Notwithstanding the infringement, the viability of a new equal protection argument hinges on the recognition of occupation as a "fundamental interest." Although this interest has yet to be officially deemed "fundamental" by the Supreme Court, Justice Harlan, dissenting in *Shapiro v. Thompson*⁹¹ talks about "statutory classifications affecting such 'fundamental' matters as the right to pursue a particular occupation,"⁹² indicating that this right might be added to the list thereby making the "drive to work" classification amenable to the "compelling interest" standard.

A major factor involved in a policyholder's premium, at least if he is under 30, is his marital status. For example, our insured being single pays \$446 annually. But if he were married, his premium would only be \$264. Like all the classifications for automobile insurance, over-inclusiveness and under-inclusiveness based on driving records and the degeneration of risk spreading appear to be tenable arguments regarding the traditional equal protection standards. In addition, however, a strict scrutiny attack based on "marital status" as a suspect class could be successful. The major argument, of course, involves "marital status" as a suspect class.

The suspect classification aspect of the new equal protection test is seen as being very elastic, where every loser in the legislative process is by definition a minority, and at least potentially classifiable as

⁸⁹ See, e.g., *Williamson v. Lee Optical Co.*, 348 U.S. 483 (1955).

⁹⁰ 383 U.S. 663.

⁹¹ 394 U.S. at 661.

⁹² *Id.*

disadvantaged.⁹³ In the automobile insurance situation it is not marriage that is being infringed upon. Rather, the single person is the disadvantaged object of this classification. Recently, the Supreme Court struck down a Massachusetts statute in *Eisenstadt v. Baird*⁹⁴ which also set up single persons as the disadvantaged group. The statutory scheme permitted, *inter alia*, married persons to obtain contraceptives under certain conditions to prevent pregnancy, but prohibited single persons from doing the same. Although this decision was based on the right of privacy, the Court made several references to marital status. Justice Brennan at one point said, "Whatever the rights of the individual . . . may be, the rights must be the same for the unmarried and the married alike."⁹⁵ Indeed, *Eisenstadt* involved a basic right of all individuals. Nevertheless, the Court seemed to say that whatever the right, regardless of importance, it must be the same irrespective of marital status. Ultimately, if "marital status" can be recognized as "suspect," insurers may find the "compelling interest" requirements impossible to meet.

Finally, the classification used by insurers based on sex is a major variant in the policyholder's auto insurance premium. Insured's premium is \$446. Remarkably, however, if insured were a woman, the premium would be \$221 annually, less than one-half the original cost! Here the key seems to be the acceptance of sex as a suspect class thereby subjecting this rate classification to strict scrutinization.

In a recent sex discrimination case, *Reed v. Reed*,⁹⁶ the Supreme Court turned down the opportunity to rule on sex as a suspect class; instead striking down the statute on the traditional "rationality" standard. It is submitted, however, that it will be just a matter of time before sex is added to the suspect class list.⁹⁷ In *Alexander v. Louisiana*,⁹⁸ Justice Douglas in a separate opinion said, "Classifications based on sex are no longer insulated from judicial scrutiny by a legislative judgment that 'woman's place is in the home' or that woman is by her 'nature' ill-suited for a particular task."⁹⁹ Accordingly, the current trend of women leaving the home for outside careers and activities defeats the antiquated concept that a female only drives to the grocery, thereby being a lesser risk to the insurer. Clearly, the campaign to end sex discrimination is motivated by anti-female laws. Nevertheless, sex as a suspect class would apply equally

⁹³ Karst, *Invidious Discrimination; Justice Douglas and the Return of the "Natural—Law—Due—Process Formula,"* 16 U.C.L.A. L. REV. 716, 742-743 (1969).

⁹⁴ 405 U.S. 438 (1972).

⁹⁵ *Id.* at 453.

⁹⁶ 404 U.S. 71 (1971).

⁹⁷ *Sail'er Inn v. Kirby*, as Cal. Rptr. 329, 485 P.2d 529 (1971).

⁹⁸ *Alexander v. Louisiana*, 405 U.S. 625 (1972).

⁹⁹ *Id.* at 641.

to infringements on the male, such as the one presented in the auto insurance situation. Perhaps the adoption of the 27th Amendment to the Constitution will be the decisive factor in making the compelling interest standard applicable to classifications based on sex. In applying that standard, the classifications based on sex, marital status, distance to work, and geographical locale must be carefully tailored to the asserted purposes and if there are other reasonable ways to achieve those goals with a lesser burden on constitutionally protected classes, the state may not choose the way of greater interference.¹⁰⁰

¹⁰⁰ *Dunn v. Blumstein*, 405 U.S. 330 (1972).

CONCLUSION

The arguments that various classifications involved in constructing private passenger automobile rates may be resulting in unconstitutional rates are of course only proposals. Whether any of these categories would in fact fail to comply with the traditional or the compelling interest equal protection standard under the adjudicative process cannot be known until actually put to the test. It is conceded that the Burger Court's record thus far indicates the new Justices are disinclined to add to the list of fundamental interests unearthed by their predecessors.¹⁰¹ But time on the bench may change attitudes as to what is basic and priorities as to what interests must be preserved over others. Nevertheless, even if the present Court becomes less interventionist, equal protection will still be the preferred ground for constitutional arguments.

Tougher rate regulatory legislation, stricter enforcement by the Department of Insurance, and subjection of rates to strict or at least minimal scrutiny are all brought together by a common force: consumerism. It seems the importance and the desirability for these things depends upon the basic function of insurance. Is it a luxury? Is it private industry? Or has it developed into a public necessity? Perhaps insurance has become such a major part of our financial lives that the social responsibilities of the insurance companies for the consumer have outgrown and displaced the industry's own interests and rights for financial gain. Classifications, like those discussed, have clearly resulted in an erosion of the fundamental concept of spreading the risk. Accordingly, the role of social equality has not been pursued enough in insurance. Legislation, the Department of Insurance, and the equal protection tests are merely tools. They are tools the consumers can use to achieve the true scope of social equity which insurance should possess.

While the legislature and the Insurance Department are relatively old and established means of rate-watching, they have not been used to their fullest scope. Equal protection on the other hand is a new tool, whose potentiality is great with capabilities for effectiveness yet untapped.

JAMES J. MCGRAW

¹⁰¹ Gunther, *The Supreme Court 1971 Term, Foreword: In Search of Evolving Doctrine on a Changing Court; A Model for a Newer Equal Protection*, 86 HARV. L. REV. 1, 12 (1972).

