

PUBLIC INTEREST AND THE COMMISSIONERS'—ALL INDUSTRY LAWS

HERBERT C. BROOK* †

Three years, more or less, have now passed since practically every state enacted insurance rate regulatory laws patterned after the Commissioners'—All Industry bills.¹ For three years, more or less, preceding that mass phenomenon there was a period of intense feeling and activity on the part of the insurance industry and state regulatory officials generated by the *SEUA* case.² There has now been lapse of enough time for some appraisal to be made of the operation and effect of these laws and yet not sufficient lapse that they have acquired a settled place in the fabric of our laws. Then too, during these three years there have been substantial changes in the personnel of many insurance departments. The considerations that led their predecessors to support such legislation may on sober second thought and in the light of subsequent developments have lost some of their validity and certainly most of their urgency. It would seem, therefore, that this is an opportune time to review such laws from the point of view of whether they are in the public interest or whether they do not stifle legitimate competition, hamper insurers in developing new coverages, and add a wholly unjustified expense to the costs of doing business.

I

INSURANCE WAS ALREADY HIGHLY REGULATED

Before the passage of this rating legislation³ insurance already was one of the most highly regulated industries in the American economy. There were detailed laws in every state designed to protect the public against loss through the insolvency of insurers. There were other laws dealing with the policy forms a company could use. Long and extremely detailed annual statements covering the insurer's business during the year and its year-end financial condition were required to be filed. There were prohibitions against monopolies, discrimination, and rebating. Some states had laws regulating rates. Most states provided for the licensing of insurance brokers, agents, and other producers. And every state had an insurance department to provide constant and extensive supervision over the the business of insurance. This list is by no means complete, but it indicates the detail with which insurance was regulated.

* A.B. 1932, Northwestern University; J. D. 1936, University of Chicago. Member of a law firm at Chicago, Ill. Lecturer on Insurance Law, Northwestern University Law School.

† The views expressed herein are to be understood as reflecting solely the personal views of the author.

¹ For convenience, laws patterned on the Commissioners'—All Industry Model Fire and Casualty Rating bills will be referred to herein as Commissioners'—All Industry laws.

² *United States v. South-Eastern Underwriters Association*, 322 U. S. 533 (1944).

³ Every state passed rating legislation during the period 1945-1948. Most of the legislation was passed in 1947.

To the uninitiate, it must seem strange that with the business already so highly regulated there should be any need to give the commissioners power over insurance rates. To the same uninitiate, it must seem even stranger to learn that the giving of such power at this time was not demanded by the public to eliminate some abuse but was sought by powerful elements within the insurance industry itself. That distinguishes this legislation from practically all that preceded it. The earlier laws were passed because of some abuse to the public either actual or potential on the part of the insurers sought to be reached by the regulation. Thus the reserve requirements for life insurance were first passed in Massachusetts in 1858 at the instance of Elizur Wright in order to prevent loss to policyholders because of the maintenance of insufficient reserves by such companies.⁴ The requirement that standard fire policies be used was due in part at least to the unscrupulous practice of companies loading their policies with restrictive provisions in fine print.⁵ The present requirements governing life policy provisions stem from abuses uncovered by the Armstrong Investigation in New York in 1905 and 1906,⁶ and in the same manner the accident and health standard provisions were a result of abuses uncovered in that state a few years later.⁷

But when the legislation in question was passed⁸ the public was not threatened with any abuse on the part of insurers. Indeed, as a result of the *SEUA* decision,⁹ the reason for passing much of the regulatory law in earlier years, namely, the need to cope with combinations of companies fixing their rates in concert and engaging in other monopolistic activities, was eliminated.

Prior to the *SEUA* decision there was no general sentiment among the states that comprehensive insurance rating laws were necessary or desirable. A number of states regulated in one degree or another rates for fire insurance, and a somewhat lesser number had laws respecting the rates for such specialized lines as workmen's compensation and automobile insurance. Only a few states such as New York and Louisiana had laws regulating the rates generally of fire and casualty lines. The New York law was passed in 1922 as a result of abuses found to exist there by a legislative committee,¹⁰ but, as noted above, the practice did not spread to other states. Nonetheless, within approximately three years after the *SEUA* decision, almost every state, as a result of the efforts of two strong groups, had passed laws regulating with great detail and strictness the rates for practically all lines of fire and casualty business.

II

SPONSORS OF THE STRICT RATE REGULATORY LAWS

The first of these groups was the National Association of Insurance Commissioners. The commissioners naturally were jealous of the prerogatives and powers

⁴ FOURTH ANNUAL REPORT OF COMMISSIONERS 30-31 (Mass., 1859), reprinted in *THE BIBLE OF LIFE INSURANCE*, AMERICAN CONSERVATION COMPANY (1932).

⁵ ALBERT H. MOWBRAY, *INSURANCE* 67-68 (3rd ed. 1947).

⁶ *Id.* at 175, 502-503.

⁷ *Id.* at 503-504.

⁸ See note 2 *supra*.

⁹ 322 U. S. 533 (1944).

¹⁰ MOWBRAY, *op. cit. supra* note 5, at 506.

of their states over insurance, and the project of obtaining passage of strict rate regulatory laws had from the earliest been pitched on a "states'-rights" plane. The one thing the commissioners wanted probably above all else was to have laws passed which would have the greatest likelihood of keeping the Federal Government completely and forever out of the insurance field. After the passage of Public Law 15¹¹ on March 9, 1945 and the subsequent *Robertson*¹² and *Benjamin*¹³ decisions in June 1946, it seems obvious that there was little legal basis for apprehension as to the future of state regulation of insurance.

The other group responsible for the passage of these laws was the All Industry Committee. This Committee was organized in May 1945¹⁴ and consisted of nineteen members which are listed in the footnote.¹⁵ Without in anywise questioning their sincerity, it may be helpful to the subsequent consideration of the Commissioners'—All Industry laws to examine its membership briefly in the light of the interest of the respective members in such legislation.

Of the nineteen members, six had no interest in the rating requirements of the fire and casualty model bills because either the bills expressly exempted their lines of insurance¹⁶ or they did not write fire or casualty business.¹⁷ Of the four producer organizations at least two were actively opposed to the rigor of the bills.¹⁸

Of the remaining nine members, three represented participating insurers.¹⁹ It is manifest that any legislation which would require or tend to establish uniformity in rates would work to the advantage, at least for the short run, of insurers who operate on the mutual or participating basis. Through their dividends they can, in effect, underquote on any risk they deem desirable. While the proposed bills provide in Section 3 that due consideration should, among other things, be given

¹¹ 59 STAT. 33-34 (1945), 15 U. S. C. §§1011-1015 (Supp. 1949).

¹² *Robertson v. California*, 328 U. S. 440 (1946).

¹³ *Prudential Ins. Co. v. Benjamin*, 328 U. S. 408 (1946).

¹⁴ The Committee was organized at a joint meeting of the Federal Legislation Committee of the National Association of Insurance Commissioners and representatives of the insurance industry "to aid in the formulation of a legislative program to strengthen existing state laws within the meaning of Section 2b of the McCarran Act." *Insurance as Interstate Commerce—The First 2 Years—Insurance Section*, American Bar Association.

¹⁵ American Institute of Marine Underwriters; American Life Convention; American Mutual Alliance; American Reciprocal Association; Associated Factory Mutual Fire Insurance Companies; Association of Casualty and Surety Executives; Bureau of Personal Accident and Health Underwriters; Health and Accident Underwriters Conference; Inland Marine Underwriters Association; Insurance Executives Association; Life Insurance Association of America; National Association of Casualty and Surety Agents; National Association of Independent Insurers; National Association of Insurance Agents; National Association of Insurance Brokers; National Association of Mutual Insurance Agents; National Board of Fire Underwriters; National Fraternal Congress of America; Surety Association of America.

¹⁶ The model fire bill exempted among other things, marine insurance, and the casualty bill exempted, among other things, accident and health insurance; hence American Institute of Marine Underwriters, Bureau of Personal Accident and Health Underwriters, and Health and Accident Underwriters Conference had no concern in the bills except to see that they retained these exemptions.

¹⁷ In this category are American Life Convention, Life Insurance Association of America, and National Fraternal Congress of America.

¹⁸ National Association of Insurance Brokers and National Association of Casualty and Surety Agents.

¹⁹ American Mutual Alliance, American Reciprocal Association, and Associated Factory Mutual Insurance Companies.

to "dividends, savings or unabsorbed premium deposits allowed or returned by insurers to their policyholders, members or subscribers," it is apparent that, as a practical matter, the provision is essentially meaningless, because a participating company can avoid its effect simply by becoming a subscriber to a rating bureau instead of filing its own rates.²⁰ So long as independent insurers could freely establish rates to give due consideration to the relative hazards of the particular risk, a mutual could not have this competitive advantage. But under the Commissioners'—All Industry laws the mutual can use the rates and rating plans available to other insurers, and in *addition* by virtue of its dividends underquote on any desirable piece of business.²¹ Hence, at least from the short run point of view, the mutual organizations could see a very real competitive advantage in sponsoring rate regulation such as the model bills which would require all insurers to file rates.

²⁰ Section 6(c) of the Model Bills provides as follows:

"No rating organization shall adopt any rule the effect of which would be to prohibit or regulate the payment of dividends, savings or unabsorbed premium deposits allowed or returned by insurers to their policyholders, members or subscribers."

²¹ See address of John A. Diemand, *Resistance to Change* (Pamph., p. 2), given at White Sulphur Springs, October 7, 1941:

Rating and anti-discriminatory laws, coupled with so-called scientific rating created a condition under which stock companies could neither deviate nor legislate in their own interest, but which left non-stock companies free to deviate through their dividends. Realizing that they were free and that the stock companies were not, the non-stock companies proceeded to invade industrial centers, first selecting only those risks known to be profitable. . . .

"Let it be noted that these surpluses [of mutual companies] were nurtured by laws which make bedfellows of mutual and stock companies in rate-making bodies and provide for the development of a single rate level for both types of companies, which is at once high enough to guarantee the dividends of mutual companies, yet inflexible enough to prevent stock companies from competing on any risk of size and importance.

"But who raised a voice in protest? In fact, there is a suspicion that some of those regulatory statutes were encouraged to prevent so-called unbridled competition on the part of a minority of stock companies whose ideas of rating and policy forms differed from the majority."

Address of Edward C. Stone, *Public Law 15: Its Purpose and Effect* (Pamph., p. 9) given at Peoria, Illinois, September 16, 1946:

"Now it so happens, as already pointed out, there are states that proceed along these lines and do not make rates or require either prior approval or subsequent disapproval of rates, but allow the fullest of competition as to rates. Such a state, for example, is Rhode Island, and conditions in that state can easily be compared with conditions in Massachusetts where workmen's compensation rates are subject to prior approval and compulsory automobile liability rates are made by the Commissioner. . . .

"No better opportunity exists to compare conditions as to rates, on the one hand, and opportunities for agents, on the other, than in these two states. The Providence, Rhode Island agent or broker, with a customer in Providence or Pawtucket, Rhode Island, can compete with anyone, and his company is on an equal footing with any other, even the mutual or participating companies, because rates may be quoted based upon competition, and the public thus may get the benefit of competition as to price. If, for example, competition is had between a stock company agent and the mutual direct writer that ordinarily pays a 20 per cent dividend, the agent can, as to a Rhode Island risk, start quoting, where the so-called manual rate is \$1.00, at \$.80. Not so, however with the Massachusetts risk just across the State line. In Massachusetts, but one rate ordinarily is available, to-wit, the prior approved rate. If this be, for example, \$1.00, the stock non-participating carrier and its agents are in a strait-jacket. They can quote only the \$1.00 whereas the direct-writing mutual, obliged initially to charge the \$1.00, may pay its dividend of \$.20, thus making its net rate \$.80 and the agent can do nothing about it."

Probably the National Association of Independent Insurers should also be placed in this category since a majority of its members were participating carriers. Of the remainder some belonged to rating bureaus and others regularly wrote at bureau rates.²² Its membership either specialized in automobile insurance or wrote this line exclusively so that it was not truly representative of the independent insurers of the country.²³

The remaining five members of the All Industry Committee represented the fire and casualty companies, which for years had fixed their rates in concert. After the *SEUA* decision it was necessary for such companies either (1) to change their methods of operation and the operations of their various rating bureaus to conform to what was permissible concerted action under the anti-trust laws,²⁴ or (2) to induce the various states to pass legislation permitting and regulating their concerted activities.

The first alternative seems never to have been seriously considered. From the time the Government appealed from the decision of the District Court sustaining a demurrer to the indictment in the *SEUA* case²⁵ the fire organizations sought legislation, first on the national level,²⁶ and being unsuccessful there, then at the state level, to permit them to continue their methods of doing business. Can anyone seriously think that had Congress exempted insurance from the anti-trust laws that they would then have been clamoring to strengthen the hands of the states in the regulation of insurance rates?

The Commissioners'—All Industry laws do not deal with the coercive, intimidatory and boycott practices aimed at by the Justice Department in the *SEUA* prosecution,²⁷ but they do permit concert of action in rate fixing which would otherwise

²² See BEST'S INSURANCE REPORTS, CASUALTY, SURETY, AND MISCELLANEOUS (1946).

²³ OTTO PATTERSON, INSURANCE AT THE CROSSROADS—THE MENACE OF THE ALL INDUSTRY BILLS 14-15 (1947).

²⁴ See *Maple Flooring Mfg.'s Ass'n v. United States*, 266 U. S. 563 (1925); *Cement Mfg.'s Protective Ass'n v. United States*, 268 U. S. 588 (1925); see also *Carroll v. Greenwich Ins. Co.*, 199 U. S. 401, 411-412 (1905).

²⁵ 322 U. S. 533 (1944).

²⁶ At their instance the Walter-Bailey-Van Nuys bill (H. R. 3270, H. R. 3269 and S. 1362) was introduced in Congress in September 1943. The bill passed the House, but not the Senate, and it died when Congress adjourned. The essential provision of this bill was:

"That nothing contained in the Act of July 2, 1890, as amended, known as the Sherman Act, or the Act of October 15, 1914, as amended, known as the Clayton Act, shall be construed to apply to the business of insurance or to acts in the conduct of that business or in anywise to impair the regulation of that business by the several States."

²⁷ According to the opinion of the Supreme Court in the *SEUA* case (322 U. S. 533 at 535-536) the indictment made the following charges:

"The member companies of S. E. U. A. controlled 90 per cent of the fire insurance and 'allied lines' sold by stock fire insurance companies in the six states where the conspiracies were consummated. Both conspiracies consisted of a continuing agreement and concert of action effectuated through S. E. U. A. The conspirators not only fixed premium rates and agents' commissions, but employed boycotts together with other types of coercion and intimidation to force non-member insurance companies into the conspiracies, and to compel persons who needed insurance to buy only from S. E. U. A. members on S. E. U. A. terms. Companies not members of S. E. U. A. were cut off from the opportunity to re-insure their risks, and their services and facilities were disparaged; independent sales agencies who defiantly represented non-S. E. U. A. companies were punished by a with-

come within the condemnation of the Sherman Act. This may be desirable, but the laws go further. They take in the entire industry—those who fix their rates in concert as well as those who do not. What is the effect of this all-inclusive scope? Does it not preserve for those who previously engaged in practices such as those set forth in the *SEUA* indictment as much as possible of the existing set-up with the blessing of the state? It is true that the state does not, in such rating laws, sanction coercive, intimidative, or boycott practices. What was the purpose of such practices? The obvious purpose was to destroy competition and to make the entire industry conform to the standards of those acting in concert. What this portion of the industry can no longer get by coercive, intimidative, and boycott practices, it can achieve to the extent that the laws have the effect of destroying competition, or even partially destroying existing competitive markets.

With the passage of this legislation the law relating to concerted action in insurance has made a full circle. In one generation, laws were passed to protect the public from insurers fixing rates in concert;²⁸ in this generation those same insurers obtain the passage of laws to protect themselves from competition!

III

EFFECT OF THE COMMISSIONERS'—ALL INDUSTRY LAWS UPON COMPETITION

The effect of the Commissioners'—All Industry laws in destroying competition and stifling initiative and enterprise will be considered from the effect, (1) upon independent insurers, (2) upon bureau members, and (3) upon the public and industry generally.

A. Effect Upon Independent Insurers

Generally speaking competition in insurance can be expressed in terms of lower rates, more satisfactory coverage, or service to the assured. Of these, only the third is ordinarily available as among members of a rating bureau competing for the same risk.²⁹ But all three are available to an independent insurer in competing against either a bureau member or another independent. Formerly it was not uncommon that if a bureau company was in competition with a non-bureau company for a particular risk, the bureau would, in effect, permit its member to meet price competition by authorizing such lower premium as the company might think proper for the risk.

When it became necessary for bureau companies to seek protection from the anti-

drawal of the right to represent the members of S. E. U. A.; and persons needing insurance who purchased from non-S. E. U. A. companies were threatened with boycotts and withdrawal of all patronage. The two conspiracies were effectively policed by inspection and rating bureaus in five of the six states, together with local boards of insurance agents in certain cities of all six states."

²⁸ See *Carroll v. Greenwich Insurance Co.*, 199 U. S. 401 (1905); *German Alliance Ins. Co. v. Hale*, 219 U. S. 307 (1911); *German Alliance Ins. Co. v. Kansas*, 233 U. S. 389 (1914).

²⁹ Testimony of E. L. Williams at *Joint Hearings before the Subcommittees of the Committees on the Judiciary on S. 1362*, 78th Cong., 1st Sess. 324 (1943).

trust laws through state legislation there were two choices available as to the handling of bureau members: Laws could be passed permitting and regulating bureaus but not requiring filings and not requiring bureau members to be bound by bureau rates, or laws could require the filing and approval of bureau rates and require members to be bound thereby. California adopted the first choice and the Commissioners'—All Industry laws represent the second. Under the latter laws, bureau members obviously would be at a competitive disadvantage in situations such as the above, and in order to eliminate their disadvantage these laws required that *all* insurers must make filings.

It is not to be presumed that the bureau companies in meeting the competition such as noted above obtained less premium than they thought adequate for that particular risk. Scales of rates are prepared for the normal or standard risk. In any classifications there likely will be risks the individual characteristics of which make for either greater or lesser hazards than those contemplated in the standard rate. The competition is for those involving lesser hazards, and there certainly is nothing wrong for such risks to be charged less than the standard rates. Indeed, strictly speaking, unjust discrimination results unless a lesser rate is charged. But if the competitor is required to file a scale of rates, its scale should, as a practical matter, conform generally to the rating scale in use by the majority of companies writing that business, otherwise the scale will tend to develop an adverse selection of risks. To illustrate, suppose an insurer, on the basis of its judgment and experience, prepares a scale based upon either a different rating basis or a different classification of risks than is in general use. The result will be a tendency for this insurer to be offered those risks for which its rates are less than the rates of the other insurers, and it will be offered few, if any, of the risks for which its rates are higher, except those which have been declined by the other insurers. Consequently universal filings will cause all scales to tend to become uniform.

Another phase of competition which the Commissioners'—All Industry laws were designed to eliminate was the ability which independent insurers formerly had of providing coverages to meet exactly the needs of their assureds, as compared to bureau companies which, in general, had to use standard bureau forms. This ability to furnish "tailor-made" contracts was not only a great competitive advantage to them, but it obviously was to the advantage of assureds. Not only could the insurer make such changes in the usual policy to conform it to any unusual conditions in the position or operation of the assured, but it could also combine in one contract various coverages to give the assured full protection. In this way also new forms of coverage were developed through experimentation. Independent insurers were in a position to render a maximum service to the insuring public, and their freedom to experiment assured progress and development of the industry. This flexibility is effectually circumscribed in the laws in question since they require that rate filings "shall indicate the character and extent of the coverage contemplated."³⁰

³⁰ See Kelly, *New Trends in Insurance Regulation*, AMERICAN MANAGEMENT ASS'N INSURANCE SERIES No. 76, 16-17 (1948), in which the author in discussing the effects of the new rating legislation upon

The net results of the foregoing so far as the independent insurer is concerned are: (1) It will have lost much if not all of the competitive advantage it formerly had in the matter of rates and forms; (2) it will have been put to great expense in making individually the various filings required by the bills. So far as getting business is concerned it will be in no better position under its filing than a bureau company, and so far as expenses are concerned it will be much worse off. The indicated course for it to follow is to join a bureau. This is undoubtedly what the industry proponents intended when they sponsored the bills. But the question may be asked: Who profits by this lack of flexibility—bureau companies or the insuring public?

B. Effect Upon Bureau Members

Proponents of the Commissioners'—All Industry laws are wont to point to Section 7 which provides for the filing of deviations by bureau members as showing there is room for reasonable competition. Rather than having this effect, even a cursory study of this section indicates that whatever was intended, in operation it will assure bureau members a not too strenuous competition from other members. In the first place, notice must be given to the bureau, and it is permitted to oppose the granting of the deviation. In the second place, the general scale, having already been approved, will be presumptively correct, and the burden will be upon the applicant to prove that the deviation is proper. Since the general scale will be deemed to represent the best judgment of the experts in the bureau (as well as of the commissioner since he approved it) as to the proper rate, the applicant will have to be able to produce figures which will establish either that its loss record or its expenses vary sufficiently from the normal to justify the deviation. As against whatever figures the applicant can produce, the bureau will in the usual case be able to produce others which it has assembled so that the applicant faces a difficult, and in the usual case, a discouraging if not impossible task. Finally, a deviation is effective only for one year so that if a renewal is desired, the whole procedure must again be followed.

Provisions substantially the same as these have been in existence for years in various

the operations of the Associated Factory Mutuals said:

"The most important change as far as the Factory Mutuals are concerned is that we will have much less flexibility in our forms, rates and underwriting practices. . . .

"In the past, when one of our insureds had an unusual problem, it was possible for our underwriters to develop promptly a special form to meet his situation and to establish a rate which they felt reasonable, adequate and non-discriminatory for the coverage desired. Although this can still be done, it will of necessity take more time, since any form which differs from those already on file must be submitted to the state insurance department and any rate made for such form must be filed in accordance with the law. If the insurance department feels that the rate proposed is unreasonable or is discriminatory, it may reject the filing, whereupon the form must either be abandoned or the cumbersome procedure for hearing an appeal must be followed. . . .

"The new law gives to every policyholder the assurance that he is receiving the same treatment as every other policyholder. In the case of the companies I represent, we never felt that any such assurance was required. Our policyholders will have it now, nevertheless. On the other hand, the tailor-made form and rate for an unusual situation, in which judgment and sales ability on the part of both insurance company and policyholder are paramount factors, will not be as easy to secure."

states which had rate regulatory laws, and as a practical matter few deviations were approved.³¹

The recent experience of the Insurance Company of North America in respect to its application for a deviation in Pennsylvania will illustrate what a task the deviation procedure may impose upon the applicant. The Company sought to reduce its fire rates 15 per cent on certain classes of risks in certain territories on the ground that it has effected economies in its commission arrangements which justified the decrease. The deviation was granted,³² but subsequently a committee representing over 100 other members of the rating association filed a complaint to have the approval rescinded. Extensive hearings were held, and as a result the commissioner reduced the general scale of rates so as virtually to parallel the deviation which had been granted.³³ While the opposition to the deviation boomeranged in this instance, it seems fairly obvious that the deviation route is a rugged and expensive one for a company to travel.³⁴ On this question of competition, the burdensome procedure for deviation in the Commissioners'—All Industry laws should be compared with the provision in the California law³⁵ which not only does not require any formalities for a member to deviate from its bureau's rate, but on the contrary, prohibits members from agreeing to be bound by such rates.³⁶ In this connection, the Bulwinkle Act³⁷ which was passed by Congress in 1948 may be of significance. This law for the first time permitted railroads to fix rates in concert. However,

³¹ Belcher, *Insurance Regulation and Free Enterprise*, PROCEEDINGS OF INSURANCE LAW SECTION, AMERICAN BAR ASS'N 23, 26 (1947).

³² N. Y. Journal of Commerce, May 16, 1949, p. 12, col. 1.

³³ The general reduction was ordered October 1, 1949, and the Commissioner held that this had the effect of terminating the deviation. Subsequently an order was entered denying the complaint and holding that the deviation was proper. The National Underwriter, July 20, 1950, p. 6, col. 1.

³⁴ Former New York Superintendent of Insurance, Robert E. Dineen, in speaking at Syracuse, N. Y., May, 1950 explained the reason he considered and approved Aetna's output policy (discussed under III C) as a direct filing was because of the difficulties the company would have had getting the policy through the various rating bureaus to which it belonged. As reported in Insurance Advocate, May 13, 1950, p. 17, col. 1, Mr. Dineen said:

"We had had experience with experts in the art of dilatory tactics—men who could use the parliamentary machinery of rating organizations as devices to delay their competitors from introducing new forms of coverage and rate changes."

³⁵ CAL. INS. CODE §1853.6 (Supp. 1949); Missouri (for casualty insurance) (MO. REV. STAT. ANN. §6077 (1939)) and Montana (REV. CODES MONT. 1948 §40.2404) have similar laws.

³⁶ Of interest in this connection is the following comment from an address by James F. Crafts, entitled *The Challenge of the Future* (Pamph., p. 15), given before Risk Research Institute, May 25, 1950: "In our home state, [California] where there is considerable latitude granted to insurers, it has been particularly interesting to compare the developments there during the past two and one-half years with those in the remaining states, where the business is generally operating under the so-called All-Industry statute.

"From a private enterprise point of view those who supported maximum control legislation have found that they are faced to an increasing degree with the kind of supervision and direction which, I am sure, they had hoped to avoid. Independency of thought and action is provided only through the filing of deviations, with the supporters and opponents going through long drawn-out hearings in order to find the answer from a supervisory official who seems to fully enjoy his policing authority. In California it can be said that we have the opportunity to solve our problems, free of arbitrators, regardless of how well qualified."

³⁷ 62 STAT. 472 (1948), 49 U. S. C. § 5b (1949). A provision to this effect must be specifically included in any agreement. See Western Traffic Ass'n—Agreement, 276 I.C.C. 183 (1949).

it specifically prohibited any agreement among railroads which did not accord to each party the right freely to take independent action at any time.

The only alternative to the cumbersome deviation procedure available to a member (except to leave the bureau) who wants some change made in a filing or a new filing made is to request the bureau to amend its rates or coverage or to make the new filing. In such a case the bureau's internal procedure would, at best, entail substantial delay.³⁸ If any member of the bureau objected to the proposal there would be further delay, and if the opposition was strong enough the proposal would be shelved. This is not said in spirit of criticism but solely to illustrate how under the bills in question enforced adherence to a bureau's filings will delay and perhaps prevent well founded changes desired by enterprising members.³⁹

C. Effect Upon the Public Generally

The general untoward effect of the Commissioners'—All Industry laws upon the public and industry will be considered from the points of view: (1) tendency to increase the difficulties poor risks will have in getting insurance, and (2) tendency to cause uniformity in insurances with a consequent lessening of the scope for the development of new coverages.

1. Difficulties imposed on poor risks

In subsection III A, the point was made that rating scales are drawn up for the so-called standard or average risk so that in any classification there likely will be some risks for which, because of individual characteristics, a greater or lesser rate than the standard would be proper. In that subsection the advantage of a freely competitive market to the better-than-average risk was pointed out. But a free

³⁸ The following question and answer will illustrate this problem (Kelly, *New Trends in Insurance Regulation*, AMERICAN MANAGEMENT ASS'N INSURANCE SERIES No. 76, 14, 19-20 (1948)):

"QUESTION: Can you change your filings?"

"MR. KELLY: Yes, we can. But, as I said, when you come to a change in filing, it starts 'running through channels.' Suppose you are dealing with a factory mutual company. You have a special or unusual clause in your form. You take this form up with them. You say, 'We sincerely hope you are going to be able to keep this form in effect.' The insurer replies, 'We will take it up with the Forms Committee of the Factory Mutual Rating Bureau.'

"Let us assume that the Forms Committee goes over it and agrees that it is an excellent form which might well be written more widely. They ask the Rates Committee whether any adjustment in rate is necessary for this form, and the Rates Committee studies it. That means a further delay until the next Rates Committee meeting. They decide that your form requires no additional rate; that the hazard has not increased; and that the Forms Committee has merely stated the problem more clearly so that you know more specifically what coverage you have.

"Then the recommendations of the Forms and Rates Committees go to the board of directors of the Rating Bureau, which approves them, and the filings are then made. Assuming that there is no substantial element of controversy and that we are merely trying to clear up what might be an ambiguity in a special case, let us suppose the filings are all approved. Between the time we start our re-examination and the time we have the approval of the state, there will be a minimum of three months' procedural time and I can conceive of cases involving controversy where it could be six months or longer."

³⁹ Aside from this, the mere fact that when once a member has accomplished its purpose of getting the proposed change filed it will be equally available to the other members will not encourage the member to make the struggle.

market is also an advantage to the poorer-than-average risk. Such a risk may not be acceptable to an insurer at standard rates, but would be acceptable at an increase in premium commensurate with the increases in its potential hazard. In the absence of regulation imposed either by private or governmental authority, insurance will respond to economic laws in the same manner as other commodities. An increase in price will bring out an increase in the supply of insurance the same as it will for other goods or services. Thus, in a free market an additional premium could be charged for the below standard risk, and it could be placed. But in a market where all insurers are bound by filed scales of rates, if the risk is not acceptable at standard rates it will be difficult and perhaps impossible to place it.⁴⁰ To meet this difficulty the casualty bill contains a provision for assigned-risk pools.⁴¹ There is no corresponding provision in the fire and marine bill, but at best this is not a very satisfactory solution to the assured, and it results in another organization having to be maintained.⁴² If there is no assigned-risk pool available such a risk must go uninsured unless it can be placed under an Excess or Surplus Line law⁴³ with an insurer not authorized to do business in that state. In the usual case the reason it can be placed with the non-authorized insurer and not in the authorized market is because a higher premium can be paid the non-authorized insurer. If there is a free market in the state so that insurers can charge additional premium for the so-called substandard risks, much of these difficulties will be eliminated.

In the old days, life insurance tended to follow the rule that either a risk was acceptable at standard rates or it was, to use the common expression, "uninsurable." In recent years this attitude has been changing so that risks that once would have been "uninsurable" will now be accepted at a higher than standard rate.⁴⁴ It seems anomalous that at the very time life insurance is getting out of the "uninsurable" attitude this attitude will become stronger in the fire and casualty business when all companies will be writing by the "book" because of the strict rating legislation. This throttling of the ability of insurers freely to adjust their rates to the individual characteristics of risks serves no useful purpose and will impose a definite hardship on insureds.

2. Tendency to cause uniformity in insurances with consequent lessening of scope for development of new coverages

It was also suggested in subsection III A that where all insurers are required to

⁴⁰ The Commissioners'—All Industry laws contain an impractical section (4g) to the effect that a rate higher than the filed rate can be used for a particular risk if the assured makes a written application to the commissioner "stating his reasons therefor" and the commissioner approves the application. Some commissioners also accept special filings not made on the application of the insured. The administrative detail and expense in making any such special filings are obvious.

⁴¹ Usually all insurers writing the particular kind of insurance will belong to the pool. Risks which cannot obtain insurance through normal channels go into the pool and are assigned, on the basis of some formula, to the respective members.

⁴² To the extent carriers must accept insurances under assigned risk plans at less than adequate rates, the claimed purpose of the bills to maintain solvency is defeated or other risks must make up the deficiency in rates.

⁴³ E.g., ILL. REV. STATS. c. 73 §§1057.

⁴⁴ Increases up to 500 per cent of normal mortality rating are now written. See *The Weekly Underwriter*, April 1, 1950, p. 800, col. 1.

file rates there would be a natural tendency for such filings to be uniform, otherwise an adverse selection of risks would develop. But aside from this, the administration of the laws will encourage if not compel uniformity in rates. Needless to say, it would simplify work in the commissioners' offices if there was a single scale of rates for all risks and standardized forms for each coverage. And might a commissioner not contend that if the laws are to provide any benefit to the public it must be by assuring them of equitable rates; that so far as the public is concerned if the commissioner does his job in regulating rates the premium for an insurance should be the same whether it was provided by one company or by another? While, so far as the language of the laws are concerned, different insurers may be entitled to charge different rates for the same coverage, it is doubtful if a layman would be able to understand what useful function the commissioner served in that situation. Then too, an insurer might question why it should be limited to a lesser rate than another company simply because the expenses of the latter were higher. If, by reason of economies in its operations, the expenses of one company are less than the expenses of another, why should not the first, if it so desires, retain the benefit of its superior management by enjoying a greater margin of profit than the second. The cost to the public will be the same. As a result of considerations such as these, it seems inevitable that the tendency will be for commissioners to work toward uniform rates⁴⁵ which will of necessity give some effect to the expenses of the least efficient insurer.⁴⁶

With a standardization of rates and of forms there will be little if any incentive and less scope for the development of new coverages or the combinations of old to simplify and reduce rates. The public will then have no choice but to accept what the commissioner has seen fit to approve or go uninsured.⁴⁷ The strict filing requirements of the Commissioners'—All Industry laws have already caused considerable hardship to assureds in preventing them from obtaining coverages to fit their exact needs.⁴⁸

⁴⁵ The defendants in their brief filed in the Supreme Court in the *SEUA* case very frankly admitted (at pages 34 and 49) that both the purpose and effect of state rating laws were to secure uniformity in rates.

⁴⁶ See *Jordan v. American Eagle Fire Ins. Co.*, 169 F. 2d 281, 293 (D. C. Cir. 1948).

⁴⁷ Situations such as the one now obtaining in Texas in respect to windstorm and hail insurance will tend to become the rule. The Texas Board of Insurance Commissioners in 1946 ruled that all such insurances must be written on the basis of a \$100 deductible. An assured sought to have the order set aside so that he could buy full coverage, but was unsuccessful. (*Board of Ins. Comm'rs v. Carter*, 228 S. W. 2d 335 (Tex. Civ. App. 1950)); *The National Underwriter*, p. 1, col. 2, March 9, 1950. This sort of a mandatory ruling is just as absurd as would be one by a commissioner that men's trousers could reach only to the knees. Certainly there is nothing immoral about full coverage windstorm insurance. If a person wants to pay the additional premium and there are companies willing to write it, he should be able to satisfy his wants.

⁴⁸ See comments of H. E. Goodell, President of Risk Research Institute, on February 23, 1950, as reported in *The Eastern Underwriter*, March 3, 1950, p. 1, col. 1, as follows:

"Referring to the preliminary discussions by a small group of buyers in Chicago, December 14, 1949, looking toward a national organization, Mr. Goodell said that the initiators of this conference 'have watched with growing concern the restricting insurance coverage under prescribed policy forms and the increasing use of non-competitive rates.'

"'It is their belief,' he continued, 'that no insurable and ratable risk should go un-

There is currently much interest in multiple line insurances and most states have within recent years amended their laws to permit more extensive multiple line underwriting. This will make it possible for companies to give broader protection in single policies, but in a measure the passage of the strict rating laws frustrates the efforts of companies to utilize their broader powers. Even if a company does not belong to a bureau and is therefore spared the effort necessary to persuade the other members that a new plan has merit and should be filed, the company faces a big task in getting a new plan of insurance approved by the commissioners. If it should involve several classes of insurance, it will in the usual case have to be considered by more than one division in the commissioners' offices. Usually the rating plan for combination and package policies will develop a lesser premium than will the rating plans filed by the company for each element if written separately. The amount of the discount for the combination of coverages will be a matter of judgment, and the probabilities are that somewhere along the line some official will want to substitute his judgment for that of the company. In any event, the filing process will involve time and expense even if it is limited to one state. If the company wants to use it in other states, the problem will be magnified by at least as many times as the number of states involved.

The efforts of Aetna Insurance Company to obtain approval of a newly developed manufacturers' output policy are illustrative.⁴⁹ This was a combination policy made up of various fire, inland marine, and casualty coverages. A single-rate method was adopted for rating the policy instead of building up a combination rate from the rates for each coverage. Conversations were started with the New York department in the fall of 1948.⁵⁰ In December 1949 New York accepted the plan as a direct filing and thereafter the company submitted it to various other states. As of May 1950 the filing had been approved by approximately twenty-five states and had been disapproved by seven.⁵¹

protected. The purpose of the meeting was to find some common ground on which buyers of insurance throughout the country would unite to the end that they might secure the full protection they need, at a fair price, written on adequate, simplified policy forms."

See also Kenney, *Effect of State and Federal Regulation Upon the Insured*, U. S. Investor, May 27, 1950, p. 77.

⁴⁹ According to Bruce Gentry, Secretary of Aetna, the development of the policy as filed was prompted by the following circumstances:

"The year was 1947, the period was the moratorium which has been granted the companies by Congress to get their affairs re-shaped under the impact of the S. E. U. A. case.

"Like all companies, we were bringing up for review any unusual policies which had been written prior to the tightening up of regulation and which must now be either cancelled or reformed, or otherwise made to meet the requirements of more complete regulation. Among these unusual contracts were four policies which our automobile department had been writing for some years, called 'automobile output policies.' All were special typewritten forms." *The Weekly Underwriter*, June 3, 1950, pp. 1290-1291, col. 1.

⁵⁰ *Insurance Advocate*, May 13, 1950, p. 8, col. 2.

⁵¹ The reason for disapproval by Louisiana, as reported in *The National Underwriter*, March 23, 1950, p. 12, col. 4, is as follows:

"Commissioner Martin of Louisiana states that the plan was rejected at this time for the reason there is not available, in the opinion of the department, sufficient statistical data to justify the fixing of a rate which would be 'non-discriminatory, non-excessive, fair

IV

THE FILING OF RATES ACCOMPLISHES LITTLE IN INSURING
THAT RISKS ARE PROPERLY RATED

Theoretically, the whole complicated and restrictive procedure set up in the Commissioners'—All Industry laws for the filing and approval of rates is to ensure that the rates of an insurer are not "excessive, inadequate or unfairly discriminatory."

The laws studiously avoid any definition of these terms so that, in the first instance at least, their content will depend upon the attitude of the commissioner in any particular situation. Such discretionary power would seem to be both improper and unnecessary, but passing that objection, an analysis of the bills will show that the strict requirements accomplish little or nothing in preventing inadequate or unfairly discriminatory rates and actually will facilitate the charging of excessive rates by combinations of insurers.

A. Excessiveness of Rates

The first standard to be observed in rate making is that the rates shall not be "excessive." There is a public purpose here in view of the permission given by the laws for companies to act in concert, but no rate regulatory laws of the scope of these bills are necessary to protect the public from excessive rates. Excessiveness of rates cannot be determined from a short-term view. An insurer engaging in a new line of insurance must be given wide latitude in pitching its rates at such level as it thinks necessary. The same is true for hazardous lines, or lines which have consistently showed a worsening experience. If rates in the latter case can be increased only to the extent indicated by the previous years' losses the insurer will never catch up but will consistently lose money.⁵² Nor is there anything to fear in a free economy in any such situation, because as soon as the business does become consistently profitable other companies will come into the market. So long as there is no monopoly, their competition will bring the rates down. It is, therefore, only when insurers writing a line of business have or tend to have a price fixing monopoly that the public can be made to suffer. In order to prevent or, if it exists, to remedy any such situation, the best solution is to encourage the existence of independent companies who will be in a position to compete. State supervision cannot give adequate protection.

The Commissioners'—All Industry laws give the commissioner in fact, or

and reasonable' as contemplated by law and sound insurance rating."

It would seem that a fair query is why Aetna with its financial strength and background of insurance knowledge should not be given the benefit of its judgment that the rating plan it adopted was "sound insurance rating." Also, if the coverage cannot be written, when can the necessary "statistical data" be obtained?

⁵²The real danger here is that increases in rates will not be made promptly either for political reasons or simply because of administrative slowness. The result will be that insurers will drop out of the market and others will become more selective so that assureds, in general, will be worse off than in a free market where the insurers can immediately increase their rates.

at least in effect, the power to fix rates.⁵³ However, there probably exists some area in which the judgment of the bureau or insurer can operate, particularly when the question arises whether a rate already approved and in use should be decreased. In such a situation unless the commissioner can demonstrate that the proper rate is substantially below the lower limit of that judgment area, the bureau is probably entitled to retain its high rate. It is for this reason that the Supreme Court, in *Georgia v. Pennsylvania R.R.*,⁵⁴ held that the fixing of transportation rates by combinations of carriers acting through rate bureaus was in violation of the anti-trust laws even though such rates had been approved by the Interstate Commerce Commission.

Whether or not intended so to operate, the Commissioners'—All Industry laws inescapably tend to destroy the free play of competitive forces by subjecting independent insurers to the same rigid filing requirements as companies acting in concert.

B. Inadequacy of Rates

The next standard is that rates shall not be inadequate. The argument runs that in a free economy "cut-throat" competition⁵⁵ forces rates below the amount necessary to carry the risk. Consequently, by strict regulation, adequacy of rates will be assured and thereby also solvency. This argument, if it has any validity, is much overdrawn.

In the first place there should be an understanding of what is meant by solvency and also what is meant by inadequate rates. Certainly solvency does not mean that a company once launched is entitled to remain in existence irrespective of the ineptness and lack of capacity on the part of its management.⁵⁶ It is no worse for an ill-

⁵³ Belcher, *Insurance Rate Regulation and Free Enterprise*, PROCEEDINGS OF INSURANCE SECTION, AMERICAN BAR ASSOCIATION 23, 24-25 (1947).

⁵⁴ 324 U. S. 439 (1945). The Court said (pp. 460-461):

"The *Keogh* case indicates that even a combination to fix reasonable and non-discriminatory rates may be illegal. 260 U. S. p. 161. The reason is that the Interstate Commerce Act does not provide remedies for the correction of all the abuses of rate-making which might constitute violations of anti-trust laws. Thus a 'zone of reasonableness exists between maxima and minima within which a carrier is ordinarily free to adjust its charges for itself.' *United States v. Chicago, M. St. P. & P. R. Co.*, 294 U. S. 499, 506. Within that zone the Commission lacks power to grant relief even though the rates are raised to the maxima by a conspiracy among carriers who employ unlawful tactics."

⁵⁵ The expression "cut-throat competition" is easy to use but hard to define. In many cases, on close examination, it undoubtedly means no more than that the prices of a competitor are such that the one complaining can no longer enjoy the same ease or margin of profit (whatever it may have been) as formerly. For example, the complaining companies in the North America rate deviation controversy discussed under III B contended that North America was attempting to gain an "unfair competitive advantage" (The National Underwriter, July 20, 1950, p. 6, col. 3) which presumably is equivalent to "cut-throat competition." In any event, since combinations of insurance companies are permitted and since such combinations represent a large part of the insurance capacity of the country, any danger of injury to the public or to the industry by "cut-throat competition," whatever that may mean, seems rather remote.

⁵⁶ See Tom C. Clark (then United States Attorney General, now Associate Justice of the United States Supreme Court), *Insurance, Bulwark of Free Enterprise*, Best's Fire and Casualty News, June 1947, p. 19, col. 1.

"Freedom of enterprise means that new firms are free to enter an industry and that old firms are free to leave it. It means that business stands on its own two feet and does not lean for support on a governmental crutch. It means innovation, change, progress—with no absolute guarantee of security. And finally, it means competition, with each firm acting independently."

managed insurance company to have to cease underwriting than for any other business enterprise to have to close its doors. The thing that the various laws relating to solvency attempt to accomplish is to ensure that the policyholders of a company and those entitled to the benefits of its policies do not thereby suffer any substantial loss, that is, that the company always have on hand enough assets so that it can, at any time, pay its obligations on policies then outstanding. If this is done and the company nevertheless gets into difficulties, it will be a comparatively simple matter to reinsure its policy obligations so that when it must cease underwriting there will be no loss under its policies. There are now extensive laws designed to insure this condition, and if it is thought that they are insufficient the remedy is to correct their deficiency by direct legislation, not to suppose that it can be done indirectly through the supervision of rates.⁵⁷

Inadequate rates within the meaning of the Commissioners'—All Industry laws cannot, as a practical matter, mean that the rate for each and every risk will be adequate. As pointed out in subdivision III A, there likely will be risks in any rating classification that involve above normal hazards and for which, as a matter of good underwriting, a higher than standard rate should be received. If a company accepts an undue proportion of such risks and is not able to compensate for the greater exposure through expense economies, it will lose money. But is this anything a commissioner can prevent through rate supervision? To illustrate, a large New York casualty company was found to be in financial difficulties in 1947. Fortunately it was saved through loans totaling \$8,000,000 from the Reconstruction Finance Corporation. According to Best's⁵⁸ this company adhered to the rates and rules promulgated by the various rating bureaus to which it belonged. In addition a very large share of its business was under state rate regulation. But, nonetheless, this significant sentence appears in Best's report:

A considerable portion of the business in force at the end of 1946 had been written at inadequate rates and a large amount of undesirable⁵⁹ business had been accepted.

⁵⁷ The suggestion might be made that the present system of permitting companies to prepare their own annual statements with examinations by commissioners periodically, usually every three years, is not adequate to detect difficulties before they become so serious as to result in loss to policyholders, etc. A possible alternative would be to require annual statements to be audited by an insurance auditor chosen from a panel approved by the commissioners. This auditor would have to certify that in his opinion the company *then* had sufficient assets to meet all of its policy obligations. In this way, the individual characteristics of the company could be taken into account, and if it was having a higher than normal loss ratio or higher than normal expenses, this would be taken into account by the auditor in reaching his conclusion. In the event the auditor and company disagreed then the commissioner should immediately resolve the difference by an examination, if necessary. If this procedure was followed, any tendency towards insolvency due to the collection of insufficient premiums to pay losses plus expenses, whatever the latter may be, would be detected before real harm to the public could be done. At the same time, a company which charged low rates but which had lower than average expenses would not be penalized.

Inadequacy of rates in life insurance is largely prevented by statutory reserve requirements. (MOWBRAY, *op. cit. supra* note 5, at 375; EDWIN W. PATTERSON, *THE INSURANCE COMMISSIONER IN THE UNITED STATES* 270, 283 (1927).

⁵⁸ BEST'S INSURANCE REPORTS, CASUALTY, SURETY AND MISCELLANEOUS 337 (1948).

⁵⁹ The question might be asked, why was the business undesirable? Was it because of bad moral hazards or simply because the risks were such that a much larger than standard premium should have been charged? Presumably most, if not all, would fall in the latter category.

Can anyone seriously think that if all the states then had rate regulatory laws such as the Commissioners'—All Industry laws the difficulties of this company would have been averted?

In the second place, and as a matter of history, those states which have attempted to supervise rates have been primarily, if not exclusively, concerned with the prevention of exorbitant rates.⁶⁰ The genesis of rating legislation was the belief that the combinations of fire insurers were charging excessive rates. While some statutes such as the original one in Kansas⁶¹ gave the Superintendent authority to compel the raising of rates, it probably is a fair surmise that this power was given primarily to prevent discrimination and the freezing out of competitors rather than to protect the solvency of the insurers.⁶²

Inquiry of those in a position to know the cause, or causes, of the various failures of insurance companies in Illinois during the early Thirties discloses that those failures were due to investments becoming valueless, improper management including excessive salaries, and improper claim handling. In none could the failure be attributed to the charging of below market rates.⁶³

In sharp contrast to the lack of evidence tending to show that supervision of rates will prevent insolvency is the evidence that rate supervision not only does not prevent the charging of inadequate rates, but actually may cause inadequate rates to be charged. The difficulties of the New York company mentioned above is an example, since a very large part, if not most, of its insurances were under state regulation.

There is evidence that on at least one occasion automobile insurance rates fixed by the Commissioner of Massachusetts were so inadequate that several companies became insolvent.⁶⁴

That state supervision of rates is no guarantee that adequate rates will be charged is illustrated in the following table.⁶⁵

⁶⁰ It is stated in the brief filed in the Supreme Court by the Appellees in the SEUA case that twenty-nine states had laws relating to fire insurance rates (pp. 51, 52) of which six gave the commissioner authority to compel increases in rates. (p. 56.)

⁶¹ See *German Alliance Ins. Co. v. Kansas*, 233 U. S. 389, 390-393 (1913).

⁶² Immediately upon passage of the Kansas law the Superintendent reduced fire rates 12 per cent. *Id.* at 397.

⁶³ See MOWBRAY, *op. cit. supra* note 5, at 458, in which the author states on the basis of analysis of individual cases of loss to policyholders due to life company insolvencies that the principal causes of loss were dishonesty in management, incompetence in the investment of funds, failure to set up proper reserves, and failure of state officials to act when the company was found in difficulties.

⁶⁴ Stone, *supra*, note 21:

"Incidentally, it may be observed that the mutual liability companies formed in Massachusetts to write compulsory automobile liability policies, which companies later became insolvent, blamed their downfall and the consequent injury to the public (in the way of policyholder and injured claimant under the policies) on the inadequate rate made by the Commissioner! Thus, even rates made by commissioners may turn out to be inadequate."

⁶⁵ *Insurance Advocate*, July 22, 1950, p. 10.

AUTOMOBILE BODILY INJURY LIABILITY AGGREGATES (STOCK COMPANIES)

Year	COUNTRYWIDE			NEW YORK STATE	
	<i>Earned Net Premiums</i>	<i>Losses In- curred to Premiums Earned</i>	<i>Expenses</i>	<i>Premiums Earned</i>	<i>Losses In- curred to Premiums Earned</i>
1945	\$200,161,551	56.4%	47.2%	\$37,584,571	63.1%
1946	261,388,308	64.4	47.8	50,907,193	70.9
1947	347,455,921	55.4	45.8	69,541,725	63.6
1948	416,951,566	52.0	44.4	86,104,527	60.6
1949	473,938,918	48.3	44.1	103,468,916	54.3

Is it any wonder that the New York company mentioned above got into financial difficulties? And yet it has been generally agreed that if any state was equipped to administer properly the laws patterned on the Commissioners'—All Industry bills it was New York. This state has had general rating laws since 1922, and in many respects the Commissioners'—All Industry laws followed a New York law passed in 1939.

Finally, it is to be noted that not only do the Commissioners'—All Industry laws not give the commissioners specific power to regulate acquisition costs or other expenses, but it was agreed by the commissioners and the All Industry Committee that the model bills did not give the commissioners any such power.⁶⁶ It is just as easy for a company to become insolvent by excessive expense outlays as by the collection of inadequate premiums. In some lines, as for instance fire insurance on dwellings, there has been more tendency to compete for such business by acquiring more and more desirable agents by increasing commission allowances than by reducing rates.⁶⁷ In making this reference, it is not to be understood that the writer advocates state regulation of such expenses. It is mentioned only to illustrate that for still another reason the contentions of the proponents of the Commissioners'—All Industry laws that strict regulation of rates was necessary to prevent insolvency are unsound. They knew this possibility for competition existed. And, if one might hazard an opinion, if these strict rate regulatory laws remain on the books it will be only a question of time before the commissioners seek legislation to control acquisition costs, for the reason, if for no other, that such authority is necessary for them to perform their duty adequately under the rating laws.

C. Unfair Discrimination in Rates

The third standard is that rates shall not be unfairly discriminatory. Before the rating legislation many states had anti-discrimination laws in one form or another, and until the *SEUA* decision they appeared to have been adequate and to have given satisfaction. All that the commissioners under the rating laws can do that has not heretofore been accomplished is to consider whether a rating plan or rating scale

⁶⁶ Elmer Warren Sawyer, *Can We Audit the Past in Terms of the Future* (Pamph., p. 12), address given at Ohio State University, March 21, 1949.

⁶⁷ See Dineen, *Acquisition Cost Conferences—1949 Developments*, Ins. L. J. 269, 274 (April 1949); *The National Underwriter*, August 25, 1949, p. 8, col. 1.

shows on its face that it is discriminatory. But unfair discrimination, if there is any, will in the usual case not appear in the construction of the plan or scale but in its *application*.⁶⁸ The present laws can add nothing to those already on the books in detecting this situation.

As against any advantages to the public that can accrue in this respect from the rating laws, there are certain disadvantages. As heretofore pointed out, when risks are classified for rating purposes the better-than-average risks in a classification pay an unduly high premium, and the poorer-than-average risks pay less than they should. This grouping for classification purposes is essential for rate filings, and yet it of necessity makes for a certain amount of discrimination. To avoid an undue amount of such discrimination, an insurer may attempt to construct a different method for classifying or rating risks. In the usual case, the new method will involve a substantial amount of underwriting judgment. In a free economy the insurer could experiment, perhaps on a small scale, to perfect the system. But under the present rating laws, he must file and have it approved before it can be used. Not only will this involve time and expense, but the commissioner, on the basis of his judgment, may decline to approve the method.⁶⁹ Thus the rating laws will tend to freeze present classifications and prevent the development of new and improved ones.

V

COMPARISON BETWEEN CALIFORNIA LAW AND THE COMMISSIONERS'—ALL INDUSTRY LAWS

It is not to be understood that the Commissioners'—All Industry laws were passed without opposition, but except in a few states, notably California,⁷⁰ the combined strength of the commissioners and the organized mutuals and stock companies acting as the All Industry Committee were sufficient to force the passage of the legislation. There is a fundamental difference in philosophy between the Commissioners'—All Industry laws and the California law. The philosophy of the latter is that there should be a maximum of competition with the minimum of regulation which will permit and yet regulate concerted action.⁷¹ Prior to this

⁶⁸ See REPORT ON EXAMINATION OF NEW YORK FIRE RATING ORGANIZATION BY STAFF OF NEW YORK DEPARTMENT 15-16, 34-35 (October 15, 1946), in which there are numerous examples of different rates being established for the same risk by different raters using the same rating plans.

⁶⁹ Lemmon, *Rate Administration and Agents*, Best's Fire and Casualty News, Nov. 1948, pp. 25-26.

⁷⁰ CAL. INS. CODE §§1850-1860.3 (Supp. 1949). Montana (MONT. REV. CODES 1947, §§40.2401-2416) and Missouri (for casualty insurances) (MO. REV. STAT. §§6077.1-6077.11 1939) adopted laws patterned on the California law.

⁷¹ See following extract from the memorandum submitted to California Legislative Joint Interim Committee by sponsors of the bill which was the basis for the law as eventually passed, pp. 1-2, November 12, 1946:

"We believe that excessive and unnecessary regulation is not in the public interest. Regulation which provides for specific approval for almost every act performed in developing rates would be a costly venture for California citizens. In this regard we have a comparison with the State of New York where insurance legislation, similar to the All-Industry Bill, was passed some years ago. In that state the Insurance Department budget for the year ending March 1, 1947 is \$1,505,305. The cost of operation of the California Insurance

legislation California had no rate legislation except in workmen's compensation, and this lack of regulation had worked satisfactorily.⁷² A comparison of some of the significant provisions of the respective laws will illustrate how the philosophy of the California law differs from that of the Commissioners'—All Industry laws.

Commissioners—All Industry Laws

Sec. 1. The purpose of this Act is to promote the public welfare by regulating insurance rates to the end that they shall not be excessive, inadequate or unfairly discriminatory, and to authorize and regulate cooperative action among insurers in rate making and in other matters within the scope of this Act. Nothing in this Act is intended (1) to prohibit or discourage reasonable competition, or (2) to prohibit, or encourage except to the extent necessary to accomplish the aforementioned purpose, uniformity in insurance rate, rating systems, rating plans or practices. This Act shall be liberally interpreted to carry into effect the provisions of this Section.

California Law

Sec. 1850. The purpose of this chapter is to promote the public welfare by regulating insurance rates as herein provided to the end that they shall not be excessive, inadequate or unfairly discriminatory, to authorize the existence and operation of qualified rating organizations and advisory organizations and require that specified rating services of such rating organizations be generally available to all admitted insurers, and to authorize cooperation between insurers in rate making and other related matters.

It is the express intent of this chapter to permit and encourage competition between insurers on a sound financial basis and nothing in this chapter is intended to give the Commissioner power to fix and determine a rate level by classification or otherwise.

Needless to say, in a particular case this difference in the statement of purpose might substantially influence the decision of a court in considering the propriety of a position taken by the Commissioner in respect to a filing.⁷³ The gist of the Commissioners'—All Industry laws is that competition is to be deprecated.

As noted under section IV, the Commissioners'—All Industry laws contain no definitions of the terms excessive, inadequate or unfairly discriminatory. Their content is left essentially to the discretion of the Commissioner except in so far as other parts of the laws, including the statement of purpose quoted above, may tend to circumscribe his discretion. Compare with this generality the definitiveness of the California law:⁷⁴

Department for the year ending June 30, 1946 was \$382,245.21.

"We cannot concur that it was ever the intent of the Congress to impose upon the citizens of the country additional cost running into millions. It always must be remembered that the federal and state Anti-Trust laws involve no plan for the administrative regulation or control of a business; in fact, their very purpose is to invite the maximum of competition in business, therefore the minimum of regulation. In drafting the proposal which we submit to you we have kept that thought uppermost in our minds."

⁷² Sawyer, *supra* note 66, at 5:

"How is it that, in the State of California, where, until January 1 of last year there was no regulation of rates except for workmen's compensation insurance, the insurance business, second only in volume to the State of New York, has been regulated quite as successfully as in New York and with, perhaps, better satisfaction to the public?"

⁷³ See *United States v. American Trucking Associations*, 310 U. S. 534 (1940).

⁷⁴ CAL. INS. CODE §1852 (Supp. 1949).

(a) Rates shall not be excessive or inadequate, as herein defined, nor shall they be unfairly discriminatory.

No rate shall be held to be excessive unless (1) such rate is unreasonably high for the insurance provided and (2) a reasonable degree of competition does not exist in the area with respect to the classification to which such rate is applicable.

No rate shall be held to be inadequate unless (1) such rate is unreasonably low for the insurance provided and (2) the continued use of such rate endangers the solvency of the insurer using the same, or unless (3) such rate is unreasonably low for the insurance provided and the use of such rate by the insurer using same has, or if continued will have, the effect of destroying competition, or creating a monopoly.

In keeping with its philosophy of free competition, the California law does not require *any* filings to be made with the commissioner. The responsibility is left with the bureaus and insurers to comply with the statutory standards in rating risks, subject to the right of the commissioner to confirm such fact through making examinations.

Under III B the burdensome deviation provisions of the Commissioners'—All Industry laws were discussed. The California law, on the other hand, not only does not require members or subscribers to adhere to the rates of their rating bureau but it expressly prohibits them from agreeing to use such rates.⁷⁵

Bearing in mind that the only circumstance that precipitated the recent rating legislation was the necessity for that portion of the industry which fixed its rates in concert either to change its methods or obtain state regulation of its activities, it is difficult to see why the California law is not a sufficient and excellent solution. Those who want to get their rates from bureaus can continue their methods of doing business, and those who want to fix their own rates can continue to do so without incurring the cost and burdens of the filing requirements of the Commissioners'—All Industry laws.

VI

THE DETAILED REGULATIONS OF THE COMMISSIONERS'—ALL INDUSTRY LAWS ARE MORE APT TO RESULT IN FEDERAL REGULATION THAN WOULD A MINIMUM OF REGULATION

As stated in Section II, the proponents of the Commissioners'—All Industry type of strict rate regulation identified their cause with that of "states-rights." Their objective, among others, was to have each state pass legislation which would, they hoped, close every possible opening through which the Federal government might move into the field of insurance regulation. To this end, they sponsored, in addition to the fire and casualty rating bills, a model accident and health bill and a model fair trade practices bill. Without at all disagreeing with this objective, the question may still be raised whether there is not more likelihood that the strict rate laws of

⁷⁵ *Id.* §1853.6 provides in part as follows: "Members and subscribers of rating or advisory organizations may use the rates, rating systems, underwriting rules or policy or bond forms of such organizations, either consistently or intermittently, but, except as provided in Sections 1853.5, 1853.8 and Article 5, shall not agree with each other or rating organizations or others to adhere thereto. . . ."

the Commissioners'—All Industry type will result in federal intervention than laws such as California's which provide a maximum of insurance freedom and a minimum of administrative control and expense. To the extent history is a guide, it would seem likely that the federal government will intervene in the matter of insurance regulation⁷⁶ only if there is dissatisfaction with state regulation, either by assureds or insurers. It is to be remembered that the *SEUA* indictment resulted from an investigation that was started because of a complaint by the Attorney General of Missouri that fire companies through their associations and bureaus were engaging in monopolistic activities inimical to the public welfare which the states were powerless to prevent.⁷⁷ The recent action of the Federal Trade Commission in entering the "mail-order" insurance field and issuing a Code of Fair Trade Practices⁷⁸ was due, in part at least, to an invitation from certain of such companies. It probably was due, in part, also to the fact that the problem of accident and health mail-order insurers had been a troublesome one for years, and the states seemed unable adequately to deal with the problem.

Under Public Law 15⁷⁹ the federal antitrust laws are still in effect in all jurisdictions in respect to matters of coercion, intimidation, and boycott. No amount of state regulation can prevent federal intervention, either on the part of the government or on the part of a private litigant, within this area. It is difficult to understand why this area of federal jurisdiction was retained, unless Congress was doubtful that the states could adequately control such interstate combinations as the one involved in the *SEUA* case. Whatever the reason, its presence will make it that much easier for the government, in case of complaints respecting state regulation, to take over more jurisdiction in insurance matters.

Consequently, since strict regulation of rates will, for the reasons discussed herein, be more apt to cause dissatisfaction to the public than would a lesser degree of control such as obtains under the California law, if the states really desire to preserve their control over interstate insurance it would seem that they would be well advised to amend their laws accordingly.⁸⁰

The situation in respect to interstate risks formerly insured through the Interstate Underwriters Board might be an illustration. Without entering into the controversy as to the merits of the rating plan used by that Board, the fact does remain that in-

⁷⁶ This is to be distinguished from the interest the government may have in insurance institutions because of their concentration of wealth and economic power.

⁷⁷ *Joint Hearings before the Subcommittees of the Committees on the Judiciary on S. 1362*, 78th Cong., 1st Sess. 80, 168, 181 (1943).

⁷⁸ CCH TRADE REG. REP. ¶20,268 (January 31, 1950).

⁷⁹ 59 STAT. 33-34 (1945), 15 U. S. C. §§1011-1015 (Supp. 1949).

⁸⁰ Most states have for some years required the filing and approval of life and accident and health insurance forms. It is virtually impossible to get a form approved in all states without making special amendments to fit the demands of particular states. This difficulty has led to the expression from time to time by company officials that perhaps a single national authority over such matters would be preferable. With the wider range and greater detail of the rating laws it would seem that such laws will be even more likely to foster this sentiment than the policy laws.

surances placed through it apparently were satisfactory to the assureds and to the companies.⁸¹ Under the strict rate regulatory laws, the operations of this Board were discontinued on June 30, 1948, and it has not been possible, even now, to work out a satisfactory solution for the handling of risks formerly insured through this Board.⁸² This has been a source of considerable dissatisfaction as well as hardship to assureds, and doubtless also to the companies involved. Under a California type law this problem would never have arisen.

The differences in the views of the commissioners on this problem⁸³ as well as on the manufacturers' output policy mentioned under III C demonstrate what seems to be an inescapable fact and that is that when laws such as the strict rating laws give the commissioners authority and discretion in matters of policy and detail and which are peculiarly the province of management there are certain to be irreconcilable points of view. The result is, of necessity, frustration, because any substantial plan of insurance will involve more than one, and likely many, commissioners, and unless all agree, essentially nothing can be done.

VII

CONCLUSION

It is submitted that the Commissioners'—All Industry laws with their burdensome filing requirements and all-inclusive scope are not in the public interest. Even as to companies that fix their rates in concert, the laws go beyond what was necessary to preserve states-rights in their regulation. From the standpoint of assuring that every rate is adequate but not excessive or unfairly discriminatory, such laws will operate no more effectively than would laws of the California type, and so far as preserving competition among bureau members, laws of the latter type would be much more effective.

As to independent companies that did not and do not fix rates in concert, it is difficult to see how any public purpose was served by subjecting them to the rigid rate controls of the Commissioners'—All Industry laws. On the contrary, their inclusion in these laws has played into the hands of those companies which in the past have operated in concert and which for years have had the objective of getting the whole industry to conform to their ideas and practices in insurance. This objective is now accomplished with the blessing of both the State and Federal Governments—the blessings of the states through the Commissioners'—All Industry laws and of the Federal Government through Public Law 15. These laws cannot but stifle competition and eliminate the facility independent companies formerly

⁸¹ *Joint Hearings, supra* note 77, at 425-475, 596-597.

⁸² Sheldon, *Fire Insurance on Multiple Location Risks*, INSURANCE L. J. 29 (January, 1950). The National Underwriter, July 27, 1950, p. 5, col. 1.

⁸³ Sheldon, *supra* note 82, at 32-33.

had for developing new coverages, conforming standard coverages to the needs of particular risks, and adjusting rates to the relative hazards of individual risks.

These laws will inevitably increase the costs of doing business of all insurers, and if they are conscientiously administered, they will greatly increase the costs of maintaining the various state insurance departments. All such costs must be borne by the insuring public. And for the reasons given, the public will not thereby get more satisfactory service from the insurance industry, but the service will become progressively less satisfactory.

