STATE OF FLORIDA
DIVISION OF ADMINISTRATIVE HEARINGS

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| THE FLORIDA INSURANCE COUNCIL, INC.; THE AMERICAN INSURANCE ASSOCIATION; THE PROPERTY CASUALTY INSURERS ASSOCIATION OF AMERICA; AND THE NATIONAL ASSOCIATION OF MUTUAL INSURANCE COMPANIES, | ) | Case Nos. 05-1012RP<br>05-2803RP |
| Petitioners, | ) | |
| vs. | ) | |
| OFFICE OF INSURANCE REGULATION AND FINANCIAL SERVICES COMMISSION, | ) | |
| Respondents. | ) | |
| FAIR ISAAC CORPORATION, | ) | |
| Petitioner, | ) | |
| vs. | ) | Case No. 06-2036RU |
| FINANCIAL SERVICES COMMISSION AND OFFICE OF INSURANCE REGULATION, | ) | |
| Respondents. | ) | |

FINAL ORDER

A final hearing was conducted in these consolidated cases on August 8 and 9, 2006, in Tallahassee, Florida, before Lawrence P. Stevenson, a duly-designated Administrative Law Judge with the Division of Administrative Hearings.

## APPEARANCES

For the Florida Insurance Council, Inc.; the American Insurance Association; the Property Casualty Insurers Association of America; and the National Association of Mutual Insurance Companies:

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For Respondents:

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## STATEMENT OF THE ISSUE

At issue in this proceeding is whether proposed Florida Administrative Code Rule 69O-125.005 is an invalid exercise of delegated legislative authority.

## PRELIMINARY STATEMENT

On February 11, 2005, Respondent Office of Insurance Regulation ("OIR") published proposed Florida Administrative Code Rule 69O-125.005 in the Florida Administrative Weekly,

vol. 31, no. 6, pp. 569-574 (the "Proposed Rule"). The Proposed Rule was designed to implement Section 626.9741, Florida Statutes,[1] created by Section 3 of Chapter 2003-407, Laws of Florida, for the purpose of regulating and limiting the use of credit reports and credit scores by insurers for underwriting and rating purposes.

On March 18, 2005, Petitioners Florida Insurance Council ("FIC"), American Insurance Association ("AIA"), and Property and Casualty Insurers Association of America ("PCI") filed a Petition to Determine the Invalidity of Proposed Rules (the "Initial Petition"). The Initial Petition alleged that proposed Florida Administrative Code Rule 69O-125.005 was an "invalid exercise of delegated legislative authority" pursuant to Subsection 120.52(8) and Section 120.56, Florida Statutes.

The Division of Administrative Hearings ("DOAH") assigned the matter DOAH Case No. 05-1012RP. On March 23, 2005, the case was assigned to the undersigned, who set the case for hearing on April 19 and 20, 2005. On March 29, 2005, the parties filed an Agreed Motion for Continuance. By Order dated April 4, 2005, the undersigned granted the continuance and rescheduled the hearing for May 26 and 27, 2005.

On March 31, 2005, Petitioners[2] filed an uncontested Motion for Leave to File an Amended Petition seeking to add the National Association of Mutual Insurance Companies ("NAMIC") as

a Petitioner. By order dated April 7, 2005, the motion was granted.

The parties filed a second Agreed Motion for Continuance on May 4, 2005. By order dated May 5, 2005, the undersigned granted the continuance and rescheduled the hearing for September 13 and 14, 2005.

On May 10, 2005, Petitioners filed a Motion for Summary Final Order, contending that the purported delegation of rulemaking authority by the Financial Services Commission ("FSC") to OIR was invalid and that OIR was therefore without authority to promulgate proposed Florida Administrative Code Rule 69O-125.005. On May 13, 2005, OIR filed a response that defended its authority to promulgate the proposed rule and challenged Petitioners' standing to bring the motion.

Without conceding its position, OIR presented the Proposed Rule to the FSC for its approval on June 16, 2005. The FSC approved the Proposed Rule, which was re-published on July 1, 2005, in the Florida Administrative Weekly, vol. 31, no. 26, pp. 2346-2350.

On August 3, 2005, Petitioners filed a second Petition to Determine the Invalidity of Proposed Rule (the "Petition"), identical in substance to the Initial Petition save for a renewed argument regarding the purported delegation of rulemaking authority from FSC to OIR. The case was given DOAH

Case No. 05-2803RP. On August 9, 2005, Petitioners filed a Motion to Consolidate, which was granted by order dated August 10, 2005.

Motions for Summary Final Order were filed by Petitioners and Respondents. Respondents' motion was denied by order dated September 16, 2005. Petitioners' motion was denied by order dated September 19, 2005. Pursuant to the parties' agreement in a status report dated September 26, 2005, the consolidated cases were rescheduled for hearing on December 12 through 14, 2005.

On November 29, 2005, Petitioners filed a Motion to Compel Deposition Answers by OIR witnesses, Steven H. Parton and Howard Eagelfeld. On December 1, 2005, Respondents filed a written response in opposition, and a telephonic hearing on the motion was held on December 2, 2005. On December 5, 2005, the undersigned issued an order denying the motion, and a separate order granting Petitioners' Motion for Stay Pending Certiorari Review of the substantive order. On May 8, 2006, the First District Court of Appeal issued an opinion denying on the merits Petitioners' petition for certiorari review of non-final agency action. Florida Insurance Council, Inc., et al. v. Office of Insurance Regulation and the Financial Services Commission, 928 So. 2d 489 (Fla. 1st DCA 2006). By order dated June 16, 2006, the stay was lifted. By order dated June 23, 2006, the

consolidated cases were scheduled for hearing on August 8 through 10, 2006.

On May 22, 2006, OIR issued "Informational Memorandum OIR-06-10M" (the "Memorandum"), the import of which was to inform all Florida property and casualty insurers that FSC had authorized OIR to begin implementation of the provisions of proposed Florida Administrative Code Rule 69O-125.005, beginning September 1, 2006, for all property and casualty insurers making a new rate, rule, or underwriting guideline filing making use of credit reports, and beginning December 1, 2006, for all property and casualty insurers using credit reports.

On May 30, 2006, Petitioners filed a Motion for Leave to File an Amended Petition, in order to challenge the Memorandum as an invalid agency statement meeting the definition of a rule. On June 12, 2006, Petitioner Fair Isaac Corporation ("Fair Isaac") filed a Petition Challenging as Non-Rule Policy the Memorandum ("Fair Isaac Petition"), which was assigned DOAH Case No. 06-2036RU. Also on June 12, 2006, Fair Isaac filed a Petition to Intervene in consolidated DOAH Case Nos. 05-1012RP and 05-2803RP, for the purpose of raising its challenge to the Memorandum in the ongoing proceedings. On June 14, 2006, Petitioners moved to consolidate DOAH Case No. 06-2036RU with DOAH Case Nos. 05-1012RP and 05-2803RP.

By order dated June 16, 2006, Petitioners' Motion for Leave to File an Amended Petition was granted. By order dated July 10, 2006, DOAH Case No. 06-2036RU was consolidated with DOAH Case Nos. 05-1012RP and 05-2803RP. Because this consolidation had the effect of making Fair Isaac a party to these proceedings for the limited purpose of pursuing its challenge to the Memorandum, there was no need to rule on Fair Isaac's Petition to Intervene.

The hearing was held on August 8 and 9, 2006. At the close of the hearing, Petitioners noted the virtual certainty that the September 1, 2006, effective date of the Memorandum would occur before a comprehensive final order could be issued in these cases. Petitioners requested that an order be entered prior to September 1, 2006, to address the limited question of OIR's authority to implement the requirements of proposed Florida Administrative Code Rule 69O-125.005 before these cases are resolved and the proposed rule is either invalidated or finally adopted pursuant to Subsection 120.54(3)(e), Florida Statutes.

Petitioners' request was granted, and a schedule was established for the parties to brief the issue. All parties timely filed briefs. On September 5, 2006, the undersigned entered a Partial Final Order finding that the Memorandum constituted an unpromulgated rule and directing OIR to

immediately discontinue reliance on the Memorandum to implement proposed Florida Administrative Code Rule 69O-125.005.

On September 8, 2006, Respondents filed a motion to withdraw the partial final order and to hold the issue of the Memorandum's effectiveness in abeyance until issuance of a final order disposing of all issues in the consolidated cases. By Order dated September 14, 2006, Respondents' motion was granted.

At the final hearing, Petitioners presented the testimony of Cecil Pearce, regional vice president of AIA; Neil Aldredge, vice president for state and regulatory affairs for NAMIC; Steven H. Parton, OIR's general counsel; Michael Miller, an expert in actuarial matters and insurance rate-making; Patrick Brockett, an expert in actuarial science, risk management, insurance, and statistics; and Guy Marvin, president of the FIC. By agreement of all the parties, Petitioners submitted the August 10, 2006, deposition testimony of William Stander, assistant vice president for PCIAA. Petitioners' Exhibits 1 through 13 were admitted into evidence. Petitioners' Exhibit 11 was the deposition testimony of Mr. Parton, and Petitioners' Exhibit 12 was the deposition testimony of Howard Eagelfeld, an actuary with OIR.

Fair Isaac presented the testimony of Lamont Boyd, a manager in its global scoring division. Fair Isaac offered no exhibits.

Respondents presented the testimony of Mr. Parton. Respondents' Exhibits 1 through 9 were admitted into evidence. Respondents' Exhibit 5 was the deposition testimony of Mr. Miller, and Respondents' Exhibit 6 was the deposition testimony of Mr. Brockett.

The Transcript of the final hearing was filed on September 5, 2006. The parties filed their Proposed Final Orders on September 15, 2006.

## FINDINGS OF FACT

### A. Petitioners

1. AIA is a trade association made up of 40 groups of insurance companies. AIA member companies annually write $6 billion in property, casualty, and automobile insurance in Florida. AIA's primary purpose is to represent the interests of its member insurance groups in regulatory and legislative matters throughout the United States, including Florida.

2. NAMIC is a trade association consisting of 1,430 members, mostly mutual insurance companies. NAMIC member companies annually write $10 billion in property, casualty, and automobile insurance in Florida. NAMIC represents the interests of its member insurance companies in regulatory and legislative matters throughout the United States, including Florida.

3. PCI is a national trade association of property and casualty insurance companies consisting of 1,055 members. PCI

members include mutual insurance companies, stock insurance companies, and reciprocal insurers that write property and casualty insurance in Florida. PCI members annually write approximately $15 billion in premiums in Florida. PCI participated in the OIR's workshops on the Proposed Rule. PCI's assistant vice president and regional manager, William Stander, testified that if the Proposed Rule is adopted, PCI's member companies would be required either to withdraw from the Florida market or drastically reorganize their business model.

4. FIC is an insurance trade association made up of 39 insurance groups that represent approximately 250 insurance companies writing all lines of insurance. All of FIC's members are licensed in Florida and write approximately $27 billion in premiums in Florida. FIC has participated in rule challenges in the past, and participated in the workshop and public hearing process conducted by OIR for this Proposed Rule. FIC President Guy Marvin testified that FIC's property and casualty members use credit scoring and would be affected by the Proposed Rule.

5. A substantial number of Petitioners' members are insurers writing property and casualty insurance and/or motor vehicle insurance coverage in Florida. These members use credit-based insurance scoring in their underwriting and rating processes. They would be directly regulated by the Proposed Rule in their underwriting and rating methods and in the rate

filing processes set forth in Sections 627.062 and 627.0651, Florida Statutes.

6. Fair Isaac originated credit-based insurance scoring and is a leading provider of credit-based insurance scoring information in the United States and Canada. Fair Isaac has invested millions of dollars in the development and maintenance of its credit-based insurance models.

7. Fair Isaac concedes that it is not an insurer and, thus, would not be directly regulated by the Proposed Rule. However, Fair Isaac would be directly affected by any negative impact that the Proposed Rule would have in setting limits on the use of credit-based insurance score models in Florida. Lamont Boyd, a manager in Fair Isaac's global scoring division, testified that if the Proposed Rule goes into effect Fair Isaac would, at a minimum, lose all of the revenue it currently generates from insurance companies that use its scores in the State of Florida, because Fair Isaac's credit-based insurance scoring model cannot meet the requirements of the Proposed Rule regarding racial, ethnic, and religious categorization. Mr. Boyd also testified that enactment of the Proposed Rule could cause a "ripple effect" of similar regulations in other states, further impairing Fair Isaac's business.

B. The Statute and Proposed Rule

8. During the 1990s, insurance companies' use of consumer credit information for underwriting and rating automobile and residential property insurance policies greatly increased. Insurance regulators expressed concern that the use of consumer credit reports, credit histories and credit-based insurance scoring models could have a negative effect on consumers' ability to obtain and keep insurance at appropriate rates. Of particular concern was the possibility that the use of credit scoring would particularly hurt minorities, people with low incomes, and young people, because those persons would be more likely to have poor credit scores.

9. On September 19, 2001, Insurance Commissioner Tom Gallagher appointed a task force to examine the use of credit reports and develop recommendations for the Legislature or for the promulgation of rules regarding the use of credit scoring by the insurance industry. The task force met on four separate occasions throughout the state in 2001, and issued its report on January 23, 2002.

10. The task force report conceded that the evidence supporting the negative impact of the use of credit reports on specific groups is "primarily anecdotal," and that the insurance industry had submitted anecdotal evidence to the contrary.

Among its nine recommendations, the task force recommended the following:

* A comprehensive and independent investigation of the relationship between insurers' use of consumer credit information and risk of loss including the impact by race, income, geographic location and age.

* A prohibition against the use of credit reports as the sole basis for making underwriting or rating decisions.

* That insurers using credit as an underwriting or rating factor be required to provide regulators with sufficient information to independently verify that use.

* That insurers be required to send a copy of the credit report to those consumers whose adverse insurance decision is a result of their consumer credit information and a simple explanation of the specific credit characteristics that caused the adverse decision.

* That insurers not be permitted to draw a negative inference from a bad credit score that is due to medical bills, little or no credit information, or other special circumstances that are clearly not related to an applicant's or policyholder's insurability.

* That the impact of credit reports be mitigated by imposing limits on the weight that insurers can give to them in the decision to write a policy and limits on the amount the premium can be increased due to credit information.

11. No evidence was presented that the "comprehensive and independent investigation" of insurers' use of credit

information was undertaken by the Legislature. However, the other recommendations of the task force were addressed in Senate Bills 40A and 42A, enacted by the Legislature and signed by the governor on June 26, 2003. These companion bills, each with an effective date of January 1, 2004, were codified as Sections 626.9741 and 626.97411, Florida Statutes, respectively. Chapters 2003-407 and 2003-408, Laws of Florida.

Section 626.9741, Florida Statutes, provides:

> (1) The purpose of this section is to regulate and limit the use of credit reports and credit scores by insurers for underwriting and rating purposes. This section applies only to personal lines motor vehicle insurance and personal lines residential insurance, which includes homeowners, mobile home owners' dwelling, tenants, condominium unit owners, cooperative unit owners, and similar types of insurance.
>
> (2) As used in this section, the term:
>
> (a) "Adverse decision" means a decision to refuse to issue or renew a policy of insurance; to issue a policy with exclusions or restrictions; to increase the rates or premium charged for a policy of insurance; to place an insured or applicant in a rating tier that does not have the lowest available rates for which that insured or applicant is otherwise eligible; or to place an applicant or insured with a company operating under common management, control, or ownership which does not offer the lowest rates available, within the affiliate group of insurance companies, for which that insured or applicant is otherwise eligible.

(b) "Credit report" means any written, oral, or other communication of any information by a consumer reporting agency, as defined in the federal Fair Credit Reporting Act, 15 U.S.C. ss. 1681 et seq., bearing on a consumer's credit worthiness, credit standing, or credit capacity, which is used or expected to be used or collected as a factor to establish a person's eligibility for credit or insurance, or any other purpose authorized pursuant to the applicable provision of such federal act. A credit score alone, as calculated by a credit reporting agency or by or for the insurer, may not be considered a credit report.

(c) "Credit score" means a score, grade, or value that is derived by using any or all data from a credit report in any type of model, method, or program, whether electronically, in an algorithm, computer software or program, or any other process, for the purpose of grading or ranking credit report data.

(d) "Tier" means a category within a single insurer into which insureds with substantially similar risk, exposure, or expense factors are placed for purposes of determining rate or premium.

(3) An insurer must inform an applicant or insured, in the same medium as the application is taken, that a credit report or score is being requested for underwriting or rating purposes. An insurer that makes an adverse decision based, in whole or in part, upon a credit report must provide at no charge, a copy of the credit report to the applicant or insured or provide the applicant or insured with the name, address, and telephone number of the consumer reporting agency from which the insured or applicant may obtain the credit report. The insurer must provide notification to the consumer explaining the reasons for the

adverse decision. The reasons must be provided in sufficiently clear and specific language so that a person can identify the basis for the insurer's adverse decision. Such notification shall include a description of the four primary reasons, or such fewer number as existed, which were the primary influences of the adverse decision. The use of generalized terms such as "poor credit history," "poor credit rating," or "poor insurance score" does not meet the explanation requirements of this subsection. A credit score may not be used in underwriting or rating insurance unless the scoring process produces information in sufficient detail to permit compliance with the requirements of this subsection. It shall not be deemed an adverse decision if, due to the insured's credit report or credit score, the insured continues to receive a less favorable rate or placement in a less favorable tier or company at the time of renewal except for renewals or reunderwriting required by this section.

(4)(a) An insurer may not request a credit report or score based upon the race, color, religion, marital status, age, gender, income, national origin, or place of residence of the applicant or insured.

(b) An insurer may not make an adverse decision solely because of information contained in a credit report or score without consideration of any other underwriting or rating factor.

(c) An insurer may not make an adverse decision or use a credit score that could lead to such a decision if based, in whole or in part, on:

1. The absence of, or an insufficient, credit history, in which instance the insurer shall:

a. Treat the consumer as otherwise approved by the Office of Insurance Regulation if the insurer presents information that such an absence or inability is related to the risk for the insurer;

b. Treat the consumer as if the applicant or insured had neutral credit information, as defined by the insurer;

c. Exclude the use of credit information as a factor and use only other underwriting criteria;

2. Collection accounts with a medical industry code, if so identified on the consumer's credit report;

3. Place of residence; or

4. Any other circumstance that the Financial Services Commission determines, by rule, lacks sufficient statistical correlation and actuarial justification as a predictor of insurance risk.

(d) An insurer may use the number of credit inquiries requested or made regarding the applicant or insured except for:

1. Credit inquiries not initiated by the consumer or inquiries requested by the consumer for his or her own credit information.

2. Inquiries relating to insurance coverage, if so identified on a consumer's credit report.

3. Collection accounts with a medical industry code, if so identified on the consumer's credit report

4. Multiple lender inquiries, if coded by the consumer reporting agency on the consumer's credit report as being from the home mortgage industry and made within 30

days of one another, unless only one inquiry is considered.

5. Multiple lender inquiries, if coded by the consumer reporting agency on the consumer's credit report as being from the automobile lending industry and made within 30 days of one another, unless only one inquiry is considered.

(e) An insurer must, upon the request of an applicant or insured, provide a means of appeal for an applicant or insured whose credit report or credit score is unduly influenced by a dissolution of marriage, the death of a spouse, or temporary loss of employment. The insurer must complete its review within 10 business days after the request by the applicant or insured and receipt of reasonable documentation requested by the insurer, and, if the insurer determines that the credit report or credit score was unduly influenced by any of such factors, the insurer shall treat the applicant or insured as if the applicant or insured had neutral credit information or shall exclude the credit information, as defined by the insurer, whichever is more favorable to the applicant or insured. An insurer shall not be considered out of compliance with its underwriting rules or rates or forms filed with the Office of Insurance Regulation or out of compliance with any other state law or rule as a result of granting any exceptions pursuant to this subsection.

(5) A rate filing that uses credit reports or credit scores must comply with the requirements of s. 627.062 or s. 627.0651 to ensure that rates are not excessive, inadequate, or unfairly discriminatory.

(6) An insurer that requests or uses credit reports and credit scoring in its underwriting and rating methods shall maintain and adhere to established written

procedures that reflect the restrictions set forth in the federal Fair Credit Reporting Act, this section, and all rules related thereto.

(7)(a) An insurer shall establish procedures to review the credit history of an insured who was adversely affected by the use of the insured's credit history at the initial rating of the policy, or at a subsequent renewal thereof. This review must be performed at a minimum of once every 2 years or at the request of the insured, whichever is sooner, and the insurer shall adjust the premium of the insured to reflect any improvement in the credit history. The procedures must provide that, with respect to existing policyholders, the review of a credit report will not be used by the insurer to cancel, refuse to renew, or require a change in the method of payment or payment plan.

(b) However, as an alternative to the requirements of paragraph (a), an insurer that used a credit report or credit score for an insured upon inception of a policy, who will not use a credit report or score for reunderwriting, shall reevaluate the insured within the first 3 years after inception, based on other allowable underwriting or rating factors, excluding credit information if the insurer does not increase the rates or premium charged to the insured based on the exclusion of credit reports or credit scores.

(8) The commission may adopt rules to administer this section. The rules may include, but need not be limited to:

(a) Information that must be included in filings to demonstrate compliance with subsection (3).

(b) Statistical detail that insurers using credit reports or scores under subsection

(5) must retain and report annually to the Office of Insurance Regulation.

(c) Standards that ensure that rates or premiums associated with the use of a credit report or score are not unfairly discriminatory, based upon race, color, religion, marital status, age, gender, income, national origin, or place of residence.

(d) Standards for review of models, methods, programs, or any other process by which to grade or rank credit report data and which may produce credit scores in order to ensure that the insurer demonstrates that such grading, ranking, or scoring is valid in predicting insurance risk of an applicant or insured.

12. Section 626.97411, Florida Statutes, provides:

Credit scoring methodologies and related data and information that are trade secrets as defined in s. 688.002 and that are filed with the Office of Insurance Regulation pursuant to a rate filing or other filing required by law are confidential and exempt from the provisions of s. 119.07(1) and s. 24(a), Art. I of the State Constitution.[3]

13. Following extensive rule development workshops and industry comment, proposed Florida Administrative Code Rule 69O-125.005 was initially published in the Florida Administrative Weekly, on February 11, 2005.[4] The Proposed Rule states, as follows:

69O-125.005 Use of Credit Reports and Credit Scores by Insurers.

(1) For the purpose of this rule, the following definitions apply:

(a) "Applicant", for purposes of Section 626.9741, F.S., means an individual whose credit report or score is requested for underwriting or rating purposes relating to personal lines motor vehicle or personal lines residential insurance and shall not include individuals who have merely requested a quote.

(b) "Credit scoring methodology" means any methodology that uses credit reports or credit scores, in whole or in part, for underwriting or rating purposes.

(c) "Data cleansing" means the correction or enhancement of presumed incomplete, incorrect, missing, or improperly formatted information.

(d) "Personal lines motor vehicle" insurance means insurance against loss or damage to any motorized land vehicle or any loss, liability, or expense resulting from or incidental to ownership, maintenance or use of such vehicle if the contract of insurance shows one or more natural persons as named insureds.

1. The following are not included in this definition:

a. Vehicles used as public livery or conveyance;

b. Vehicles rented to others;

c. Vehicles with more than four wheels;

d. Vehicles used primarily for commercial purposes; and

e. Vehicles with a net vehicle weight of more than 5,000 pounds designed or used for the carriage of goods (other than the personal effects of passengers) or drawing a trailer designed or used for the carriage of such goods.

2. The following are specifically included, inter alia, in this definition:

a. Motorcycles;

b. Motor homes;

c. Antique or classic automobiles; and

d. Recreational vehicles.

(e) "Unfairly discriminatory" means that adverse decisions resulting from the use of a credit scoring methodology disproportionately affects persons belonging to any of the classes set forth in Section 626.9741(8)(c), F.S.

(2) Insurers may not use any credit scoring methodology that is unfairly discriminatory. The burden of demonstrating that the credit scoring methodology is not unfairly discriminatory is upon the insurer.

(3) An insurer may not request or use a credit report or credit score in its underwriting or rating method unless it maintains and adheres to established written procedures that reflect the restrictions set forth in the federal Fair Credit Reporting Act, Section 626.9741, F.S., and these rules.

(4) Upon initial use or any change in that use, insurers using credit reports or credit scores for underwriting or rating personal lines residential or personal lines motor vehicle insurance shall include the following information in filings submitted pursuant to Section 627.062 or 627.0651, F.S.

(a) A listing of the types of individuals whose credit reports or scores the company will use or attempt to use to underwrite or rate a given policy. For example:

1. Person signing application;
2. Named insured or spouse; and
3. All listed operators.

(b) How those individual reports or scores will be combined if more than one is used. For example:

1. Average score used;
2. Highest score used.

(c) The name(s) of the consumer reporting agencies or any other third party vendors from which the company will obtain or attempt to obtain credit reports or scores.

(d) Precise identifying information specifying or describing the credit scoring methodology, if any, the company will use including:

1. Common or trade name;

2. Version, subtype, or intended segment of business the system was designed for; and

3. Any other information needed to distinguish a particular credit scoring methodology from other similar ones, whether developed by the company or by a third party vendor.

(e) The effect of particular scores or ranges of scores (or, for companies not using scores, the effect of particular items appearing on a credit report) on any of the following as applicable:

1. Rate or premium charged for a policy of insurance;

2. Placement of an insured or applicant in a rating tier;

3. Placement of an applicant or insured in a company within an affiliated group of insurance companies;

4. Decision to refuse to issue or renew a policy of insurance or to issue a policy with exclusions or restrictions or limitations in payment plans.

(f) The effect of the absence or insufficiency of credit history (as referenced in Section 626.9741(4)(c)1., F.S.) on any items listed in paragraph (e) above.

(g) The manner in which collection accounts identified with a medical industry code (as referenced in Section 626.9741(4)(c)2., F.S.) on a consumer's credit report will be treated in the underwriting or rating

process or within any credit scoring methodology used.

(h) The manner in which collection accounts that are not identified with a medical industry code, but which an applicant or insured demonstrates are the direct result of significant and extraordinary medical expenses, will be treated in the underwriting or rating process or within any credit scoring methodology used.

(i) The manner in which the following will be treated in the underwriting or rating process, or within any credit scoring methodology used:

1. Credit inquiries not initiated by the consumer;

2. Requests by the consumer for the consumer's own credit information;

3. Multiple lender inquiries, if coded by the consumer reporting agency on the consumer's credit report as being from the automobile lending industry or the home mortgage industry and made within 30 days of one another;

4. Multiple lender inquiries that are not coded by the consumer reporting agency on the consumer's credit report as being from the automobile lending industry or the home mortgage industry and made within 30 days of one another, but that an applicant or insured demonstrates are the direct result of such inquiries;

5. Inquiries relating to insurance coverage, if so identified on a consumer's credit report; and

6. Inquiries relating to insurance coverage that are not so identified on a consumer's credit report, but which an applicant or insured demonstrates are the direct result of such inquiries.

(j) The list of all clear and specific primary reasons that may be cited to the consumer as the basis or explanation for an adverse decision under Section 626.9741(3),

F.S. and the criteria determining when each of those reasons will be so cited.

(k) A description of the process that the insurer will use to correct any error in premium charged the insured, or in underwriting decision made concerning the insured, if the basis of the premium charged or the decision made is a disputed item that is later removed from the credit report or corrected, provided that the insured first notifies the insurer that the item has been removed or corrected.

(l) A certification that no use of credit reports or scores in rating insurance will apply to any component of a rate or premium attributed to hurricane coverage for residential properties as separately identified in accordance with Section 627.0629, F.S.

(5) Insurers desiring to make adverse decisions for personal lines motor vehicle policies or personal lines residential policies based on the absence or insufficiency of credit history shall either:

(a) Treat such consumers or applicants as otherwise approved by the Office of Insurance Regulation if the insurer presents information that such an absence or inability is related to the risk for the insurer and does not result in a disparate impact on persons belonging to any of the classes set forth in Section 626.9741(8)(c), F.S. This information will be held as confidential if properly so identified by the insurer and eligible under Section 626.9711, F.S. The information shall include:

1. Data comparing experience for each category of those with absent or insufficient credit history to each category of insureds separately treated with respect

to credit and having sufficient credit history;

2. A statistically credible method of analysis that concludes that the relationship between absence or insufficiency and the risk assumed is not due to chance;

3. A statistically credible method of analysis that concludes that absence or insufficiency of credit history does not disparately impact persons belonging to any of the classes set forth in Section 626.9741(8)(c), F.S.;

4. A statistically credible method of analysis that confirms that the treatment proposed by the insurer is quantitatively appropriate; and

5. Statistical tests establishing that the treatment proposed by the insurer is warranted for the total of all consumers with absence or insufficiency of credit history and for at least two subsets of such consumers.

(b) Treat such consumers as if the applicant or insured had neutral credit information, as defined by the insurer. Should an insurer fail to specify a definition, neutral is defined as the average score that a stratified random sample of consumers or applicants having sufficient credit history would attain using the insurer's credit scoring methodology; or

(c) Exclude credit as a factor and use other criteria. These other criteria must be specified by the insurer and must not result in average treatment for the totality of consumers with an absence of or insufficiency of credit history any less favorable than the treatment of average consumers or applicants having sufficient credit history.

(6) Insurers desiring to make adverse decisions for personal lines motor vehicle or personal lines residential insurance

based on information contained in a credit report or score shall file with the Office information establishing that the results of such decisions do not correlate so closely with the zip code of residence of the insured as to constitute a decision based on place of residence of the insured in violation of Section 626.9741(4)(c)(3), F.S.

(7)(a) Insurers using credit reports or credit scores for underwriting or rating personal lines residential or personal lines motor vehicle insurance shall develop, maintain, and adhere to written procedures consistent with Section 626.9741(4)(e), F.S. providing appeals for applicants or insureds whose credit reports or scores are unduly influenced by dissolution of marriage, death of a spouse, or temporary loss of employment.

(b) These procedures shall be subject to examination by the Office at any time.

(8)(a)1. Insurers using credit reports or credit scoring in rating personal lines motor vehicle or personal lines residential insurance shall develop, maintain, and adhere to written procedures to review the credit history of an insured who was adversely affected by such use at initial rating of the policy or subsequent renewal thereof.

2. These procedures shall be subject to examination by the Office at any time.

3. The procedures shall comply with the following:

a. A review shall be conducted:

(I) No later than 2 years following the date of any adverse decision, or

(II) Any time, at the request of the insured, but no more than once per policy period without insurer assent.

b. The insurer shall notify the named insureds annually of their right to request the review in (II) above. Renewal notices issued 120 days or less after the effective

date of this rule are not included in this requirement.

c. The insurer shall adjust the premium to reflect any improvement in credit history no later than the first renewal date that follows a review of credit history. The renewal premium shall be subject to other rating factors lawfully used by the insurer.

d. The review shall not be used by the insurer to cancel, refuse to renew, or require a change in the method of payment or payment plan based on credit history.

(b)1. As an alternative to the requirements in paragraph (8)(a), insurers using credit reports or scores at the inception of a policy but not for re-underwriting shall develop, maintain, and adhere to written procedures.

2. These procedures shall be subject to examination by the Office at any time.

3. The procedures shall comply with the following:

a. Insureds shall be reevaluated no later than 3 years following policy inception based on allowable underwriting or rating factors, excluding credit information.

b. The rate or premium charged to an insured shall not be greater, solely as a result of the reevaluation, than the rate or premium charged for the immediately preceding policy term. This shall not be construed to prohibit an insurer from applying regular underwriting criteria (which may result in a greater premium) or general rate increases to the premium charged.

c. For insureds that received an adverse decision notification at policy inception, no residual effects of that adverse decision shall survive the reevaluation. This means that the reevaluation must be complete enough to make it possible for insureds adversely impacted at inception to attain the lowest available rate for which comparable insureds are eligible,

considering only allowable underwriting or rating factors (excluding credit information) at the time of the reevaluation.

(9) No credit scoring methodology shall be used for personal lines motor vehicle or personal lines residential property insurance unless that methodology has been demonstrated to be a valid predictor of the insurance risk to be assumed by an insurer for the applicable type of insurance. The demonstration of validity detailed below need only be provided with the first rate, rule, or underwriting guidelines filing following the effective date of this rule and at any time a change is made in the credit scoring methodology. Other such filings may instead refer to the most recent prior filing containing a demonstration. Information supplied in the context of a demonstration of validity will be held as confidential if properly so identified by the insurer and eligible under Section 626.9711, F.S. A demonstration of validity shall include:

(a) A listing of the persons that contributed substantially to the development of the most current version of the method, including resumes of the persons, if obtainable, indicating their qualifications and experience in similar endeavors.

(b) An enumeration of all data cleansing techniques that have been used in the development of the method, which shall include:

1. The nature of each technique;

2. Any biases the technique might introduce; and

3. The prevalence of each type of invalid information prior to correction or enhancement.

(c) All data that was used by the model developers in the derivation and calibration of the model parameters.

1. Data shall be in sufficient detail to permit the Office to conduct multiple regression testing for validation of the credit scoring methodology.

2. Data, including field definitions, shall be supplied in electronic format compatible with the software used by the Office.

(d) Statistical results showing that the model and parameters are predictive and not overlapping or duplicative of any other variables used to rate an applicant to such a degree as to render their combined use actuarially unsound. Such results shall include the period of time for which each element from a credit report is used.

(e) A precise listing of all elements from a credit report that are used in scoring, and the formula used to compute the score, including the time period during which each element is used. Such listing is confidential if properly so identified by the insurer.

(f) An assessment by a qualified actuary, economist, or statistician (whether or not employed by the insurer) other than persons who contributed substantially to the development of the credit scoring methodology, concluding that there is a significant statistical correlation between the scores and frequency or severity of claims. The assessment shall:

1. Identify the person performing the assessment and show his or her educational and professional experience qualifications; and

2. Include a test of robustness of the model, showing that it performs well on a credible validation data set. The validation data set may not be the one from which the model was developed.

(g) Documentation consisting of statistical testing of the application of the credit scoring model to determine whether it results in a disproportionate impact on the classes set forth in Section 626.9741(8)(c), F.S. A model that disproportionately affects any such class of persons is presumed to have a disparate impact and is presumed to be unfairly discriminatory.

1. Statistical analysis shall be performed on the current insureds of the insurer using the proposed credit scoring model, and shall include the raw data and detailed results on each classification set forth in Section 626.9741(8)(c), F.S. In lieu of such analysis insurers may use the alternative in 2. below.

2. Alternatively, insurers may submit statistical studies and analyses that have been performed by educational institutions, independent professional associations, or other reputable entities recognized in the field, that indicate that there is no disproportionate impact on any of the classes set forth in Section 626.9741(8)(c), F.S. attributable to the use of credit reports or scores. Any such studies or analyses shall have been done concerning the specific credit scoring model proposed by the insurer.

3. The Office will utilize generally accepted statistical analysis principles in reviewing studies submitted which support the insurer's analysis that the credit scoring model does not disproportionately impact any class based upon race, color, religion, marital status, age, gender, income, national origin, or place of residence. The Office will permit reliance on such studies only to the extent that they permit independent verification of the results.

(h) The testing or validation results obtained in the course of the assessment in paragraphs (d) and (f) above.

(i) Internal Insurer data that validates the premium differentials proposed based on the scores or ranges of scores.

1. Industry or countrywide data may be used to the extent that the Florida insurer data lacks credibility based upon generally accepted actuarial standards. Insurers using industry or countrywide data for validation shall supply Florida insurer data and demonstrate that generally accepted actuarial standards would allow reliance on each set of data to the extent the insurer has done so.

2. Validation data including claims on personal lines residential insurance policies that are the result of acts of God shall not be used unless such acts occurred prior to January 1, 2004.

3. The mere copying of another company's system will not fulfill the requirement to validate proposed premium differentials unless the filer has used a method or system for less than 3 years and demonstrates that it is not cost effective to retrospectively analyze its own data. Companies under common ownership, management, and control may copy to fulfill the requirement to validate proposed premium differentials if they demonstrate that the characteristics of the business to be written by the affiliate doing the copying are sufficiently similar to the affiliate being copied to presume common differentials will be accurate.

(j) The credibility standards and any judgmental adjustments, including limitations on effects, that have been used in the process of deriving premium differentials proposed and validated in paragraph (i) above.

(k) An explanation of how the credit scoring methodology treats discrepancies in the information that could have been obtained from different consumer reporting agencies: Equifax, Experian, or TransUnion.

This shall not be construed to require insurers to obtain multiple reports for each insured or applicant.

(l)1. The date that each of the analyses, tests, and validations required in paragraphs (d) through (j) above was most recently performed, and a certification that the results continue to be applicable.
2. Any item not reviewed in the previous 5 years is unacceptable.

Specific Authority 624.308(1), 626.9741(8) FS. Law Implemented 624.307(1), 626.9741 FS. History-- New _____.

C. The Petition

1. Statutory Definitions of "Unfairly Discriminatory"

14. The main issue raised by Petitioners is that the Proposed Rule's definition of "unfairly discriminatory," and those portions of the Proposed Rule that rely on this definition, are invalid because they are vague, and enlarge, modify, and contravene the provisions of the law implemented and other provisions of the insurance code.

15. Section 626.9741, Florida Statutes, does not define "unfairly discriminatory." Subsection 626.9741(5), Florida Statutes, provides that a rate filing using credit reports or scores "must comply with the requirements of s. 627.062 or s. 627.0651 to ensure that rates are not excessive, inadequate, or unfairly discriminatory." Subsection 626.9741(8)(c), Florida Statutes, provides that the FSC may adopt rules, including standards to ensure that rates or premiums "associated with the

use of a credit report or score are not unfairly discriminatory, based upon race, color, religion, marital status, age, gender, income, national origin, or place of residence."

16. Chapter 627, Part I, Florida Statutes, is referred to as the "Rating Law." § 627.011, Fla. Stat. The purpose of the Rating Law is to "promote the public welfare by regulating insurance rates . . . to the end that they shall not be excessive, inadequate, or unfairly discriminatory." § 627.031(1)(a), Fla. Stat.

17. The Rating Law provisions referenced by Subsection 626.9741(5), Florida Statutes, in relation to ensuring that rates are not "unfairly discriminatory" are Sections 627.062 and 627.0651, Florida Statutes. Section 627.062, Florida Statutes, titled "Rate standards," provides that "[t]he rates for all classes of insurance to which the provisions of this part are applicable shall not be excessive, inadequate, or unfairly discriminatory." § 627.062(1), Fla. Stat.

18. Subsection 627.062(2)(e)6., Florida Statutes, provides:

> A rate shall be deemed unfairly discriminatory as to a risk or group of risks if the application of premium discounts, credits, or surcharges among such risks does not bear a reasonable relationship to the expected loss and expense experience among the various risks.

19. Section 627.0651, Florida Statutes, titled "Making and use of rates for motor vehicle insurance," provides, in relevant part:

> (6) One rate shall be deemed unfairly discriminatory in relation to another in the same class if it clearly fails to reflect equitably the difference in expected losses and expenses.
>
> (7) Rates are not unfairly discriminatory because different premiums result for policyholders with like loss exposures but different expense factors, or like expense factors but different loss exposures, so long as rates reflect the differences with reasonable accuracy.
>
> (8) Rates are not unfairly discriminatory if averaged broadly among members of a group; nor are rates unfairly discriminatory even though they are lower than rates for nonmembers of the group. However, such rates are unfairly discriminatory if they are not actuarially measurable and credible and sufficiently related to actual or expected loss and expense experience of the group so as to assure that nonmembers of the group are not unfairly discriminated against. Use of a single United States Postal Service zip code as a rating territory shall be deemed unfairly discriminatory.

20. Petitioners point out that each of these statutory examples describing "unfairly discriminatory" rates has an actuarial basis, i.e., rates must be related to the actual or expected loss and expense factors for a given group or class, rather than any extraneous factors. If two risks have the same expected losses and expenses, the insurer must charge them the

same rate. If the risks have different expected losses and expenses, the insurer must charge them different rates.

21. Michael Miller, Petitioners' expert actuary, testified that the term "unfairly discriminatory" has been used in the insurance industry for well over 100 years and has always had this cost-based definition. Mr. Miller is a fellow of the Casualty Actuarial Society ("CAS"), a professional organization whose purpose is the advancement of the body of knowledge of actuarial science, including the promulgation of industry standards and a code of professional conduct. Mr. Miller was chair of the CAS ratemaking committee when it developed the CAS "Statement of Principles Regarding Property and Casualty Insurance Ratemaking," a guide for actuaries to follow when establishing rates.[5] Principle 4 of the Statement of Principles provides: "A rate is reasonable and not excessive, inadequate, or unfairly discriminatory if it is an actuarially sound estimate of the expected value of all future costs associated with an individual risk."

22. In layman's terms, Mr. Miller explained that different types of risks are reflected in a rate calculation. To calculate the expected cost of a given risk, and thus the rate to be charged, the insurer must determine the expected losses for that risk during the policy period. The loss portion reflects the risk associated with an occurrence and the severity

of a claim. While the loss portion does not account for the entirety of the rate charged, it is the most important in terms of magnitude.

23. Mr. Miller cautioned that the calculation of risk is a quantification of expected loss, but not an attempt to predict who is going to have an accident or make a claim. There is some likelihood that every insured will make a claim, though most never do, and this uncertainty is built into the incurred loss portion of the rate.

24. No single risk factor is a complete measure of a person's likelihood of having an accident or of the severity of the ensuing claim. The prediction of losses is determined through a risk classification plan that take into consideration many risk factors (also called rating factors) to determine the likelihood of an accident and the extent of the claim.

25. As to automobile insurance, Mr. Miller listed such risk factors as the age, gender, and marital status of the driver, the type, model and age of the car, the liability limits of the coverage, and the geographical location where the car is garaged. As to homeowners insurance, Mr. Miller listed such risk factors as the location of the home, its value and type of construction, the age of the utilities and electrical wiring, and the amount of insurance to be carried.

## 2. Credit Scoring as a Rating Factor

26. In the current market, the credit score of the applicant or insured is a rating factor common to automobile and homeowners insurance. Subsection 626.9741(2)(c), Florida Statutes, defines "credit score" as follows:

> a score, grade, or value that is derived by using any or all data from a credit report in any type of model, method, or program, whether electronically, in an algorithm, computer software or program, or any other process, for the purpose of grading or ranking credit report data.

27. "Credit scores" (more accurately termed "credit-based insurance scores") are derived from credit data that have been found to be predictive of a loss. Lamont Boyd, Fair Isaac's insurance market manager, explained the manner in which Fair Isaac produced its credit scoring model. The company obtained information from various insurance companies on millions of customers. This information included the customers' names, addresses, and the premiums earned by the companies on those policies as well as the losses incurred.

28. Fair Isaac next requested the credit reporting agencies to review their archived files for the credit information on those insurance company customers. The credit agencies matched the credit files with the insurance customers, then "depersonalized" the files so that there was no way for Fair Isaac to know the identity of any particular customer.

According to Mr. Lamont, the data were "color blind" and "income blind."

29. Fair Isaac's analysts took these files from the credit reporting agencies and studied the data in an effort to find the most predictive characteristics of future loss propensity. The model was developed to account for all the predictive characteristics identified by Fair Isaac's analysts, and to give weight to those characteristics in accordance to their relative accuracy as predictors of loss.

30. Fair Isaac does not directly sell its credit scores to insurance companies. Rather, Fair Isaac's models are implemented by the credit reporting agencies. When an insurance company wants Fair Isaac's credit score, it purchases access to the model's results from the credit reporting agency. Other vendors offer similar credit scoring models to insurance companies, and in recent years, some insurance companies have developed their own scoring models.

31. Several academic studies of credit scoring were admitted and discussed at the final hearing in these cases. There appears to be no serious debate that credit scoring is a valid and important predictor of losses. The controversy over the use of credit scoring arises over its possible "unfairly discriminatory" impact "based upon race, color, religion,

marital status, age, gender, income, national origin, or place of residence." § 626.9741(8)(c), Fla. Stat.

32. Mr. Miller was one of two principal authors of a June 2003 study titled, "The Relationship of Credit-Based Insurance Scores to Private Passenger Automobile Insurance Loss Propensity." This study was commissioned by several insurance industry trade organizations, including AIA and NAMIC. The study addressed three questions: whether credit-based insurance scores are related to the propensity for loss; whether credit-based insurance scores measure risk that is already measured by other risk factors; and what is the relative importance to accurate risk assessment of the use of credit-based insurance scores.

33. The study was based on a nationwide random sample of private passenger automobile policy and claim records. Records from all 50 states were included in roughly the same proportion as each state's registered motor vehicles bear to total registered vehicles in the United States. The data samples were provided by seven insurers, and represented approximately 2.7 million automobiles, each insured for 12 months.[6] The study examined all major automobile coverages: bodily injury liability, property damage liability, medical payments coverage, personal injury protection coverage, comprehensive coverage, and collision coverage.

34. The study concluded that credit-based insurance scores were correlated with loss propensity. The study found that insurance scores overlap to some degree with other risk factors, but that after fully accounting for the overlaps, insurance scores significantly increase the accuracy of the risk assessment process. The study found that, for each of the six automobile coverages examined, insurance scores are among the three most important risk factors.[7] Mr. Miller's study did not examine the question of causality, i.e., why credit-based insurance scores are predictive of loss propensity.

35. Dr. Patrick Brockett testified for Petitioners as an expert in actuarial science, risk management and insurance, and statistics. Dr. Brockett is a professor in the departments of management science and information systems, finance, and mathematics at the University of Texas at Austin. He occupies the Gus S. Wortham Memorial Chair in Risk Management and Insurance, and is the director of the university's risk management and insurance program. Dr. Brockett is the former director of the University of Texas' actuarial science program and continues to direct the study of students seeking their doctoral degrees in actuarial science. His areas of academic research are actuarial science, risk management and insurance, statistics, and general quantitative methods in business. Dr. Brockett has written more than 130 publications, most of

which relate to actuarial science and insurance. He has spent his entire career in academia, and has never been employed by an insurance company.

36. In 2002, Lieutenant Governor Bill Ratliff of Texas asked the Bureau of Business Research ("BBR") of the University of Texas' McCombs School of Business to provide an independent, nonpartisan study to examine the relationship between credit history and insurance losses in automobile insurance. Dr. Brockett was one of four named authors of this BBR study, issued in March 2003 and titled, "A Statistical Analysis of the Relationship between Credit History and Insurance Losses."

37. The BBR research team solicited data from insurance companies representing the top 70 percent of the automobile insurers in Texas, and compiled a database of more than 173,000 automobile insurance policies from the first quarter of 1998 that included the following 12 months' premium and loss history. ChoicePoint was then retained to match the named insureds with their credit histories and to supply a credit score for each insured person. The BBR research team then examined the credit score and its relationship with prospective losses for the insurance policy. The results were summarized in the study as follows:

> Using logistic and multiple regression analyses, the research team tested whether the credit score for the named insured on a

> policy was significantly related to incurred losses for that policy. It was determined that there was a significant relationship. In general, lower credit scores were associated with larger incurred losses. Next, logistic and multiple regression analyses examined whether the revealed relationship between credit score and incurred losses was explainable by existing underwriting variables, or whether the credit score added new information about losses not contained in the existing underwriting variables. It was determined that credit score did yield new information not contained in the existing underwriting variables.
>
> What the study does not attempt to explain is why credit scoring adds significantly to the insurer's ability to predict insurance losses. In other words, causality was not investigated. In addition, the research team did not examine such variables as race, ethnicity, and income in the study, and therefore this report does not speculate about the possible effects that credit scoring may have in raising or lowering premiums for specific groups of people. Such an assessment would require a different study and different data.

38. At the hearing, Dr. Brockett testified that the BBR study demonstrated a "strong and significant relationship between credit scoring and incurred losses," and that credit scoring retained its predictive power even after the other risk variables were accounted for.

39. Dr. Brockett further testified that credit scoring has a disproportionate effect on the classifications of age and marital status, because the very young tend to have credit

scores that are lower than those of older people. If the question is simply whether the use of credit scores will have a greater impact on the young and the single, the answer would be in the affirmative. However, Dr. Brockett also noted that young, single people will also have higher losses than older, married people, and, thus, the use of credit scores is not "unfairly discriminatory" in the sense that term is employed in the insurance industry.[8]

40. Mr. Miller testified that nothing in the actuarial standards of practice requires that a risk factor be causally related to a loss. The Actuarial Standards Board's Standard of Practice 12,[9] dealing with risk classification, states that a risk factor is appropriate for use if there is a demonstrated relationship between the risk factor and the insurance losses, and that this relationship may be established by statistical or other mathematical analysis of data. If the risk characteristic is shown to be related to an expected outcome, the actuary need not establish a cause-and-effect relationship between the risk characteristic and the expected outcome.

41. As an example, Mr. Miller offered the fact that past automobile accidents do not cause future accidents, although past accidents are predictive of future risk. Past traffic violations, the age of the driver, the gender of the driver, and the geographical location are all risk factors in automobile

insurance, though none of these factors can be said to cause future accidents. They help insurers predict the probability of a loss, but do not predict who will have an accident or why the accident will occur.

42. Mr. Miller opined that credit scoring is a similar risk factor. It is demonstrably significant as a predictor of risk, though there is no causal relationship between credit scores and losses and only an incomplete understanding of why credit scoring works as a predictor of loss.

43. At the hearing, Dr. Brockett discussed a study that he has co-authored with Linda Golden, a business professor at the University of Texas at Austin. Titled "Biological and Psychobehavioral Correlates of Risk Taking, Credit Scores, and Automobile Insurance Losses: Toward an Explication of Why Credit Scoring Works," the study has been peer-reviewed and at the time of the hearing had been accepted for publication in the Journal of Risk and Insurance.

44. In this study, the authors conducted a detailed review of existing scientific literature concerning the biological, psychological, and behavioral attributes of risky automobile drivers and insured losses, and a similar review of literature concerning the biological, psychological, and behavioral attributes of financial risk takers. The study found that basic chemical and psychobehavioral characteristics, such as a

sensation-seeking personality type, are common to individuals exhibiting both higher insured automobile losses and poorer credit scores. Dr. Brockett testified that this study provides a direction for future research into the reasons why credit scoring works as an insurance risk characteristic.

### 3. The Proposed Rule's Definition of "Unfairly Discriminatory"

45. Petitioners contend that the Proposed Rule's definition of the term "unfairly discriminatory" expands upon and is contrary to the statutory definition of the term discussed in section C.1. supra, and that this expanded definition operates to impose a ban on the use of credit scoring by insurance companies.

46. As noted above, Section 626.9741, Florida Statutes, does not define the term "unfairly discriminatory." The provisions of the Rating Law[10] define the term as it is generally understood by the insurance industry: a rate is deemed "unfairly discriminatory" if the premium charged does not equitably reflect the differences in expected losses and expenses between policyholders. Two provisions of Section 626.9741, Florida Statutes, employ the term "unfairly discriminatory":

> (5) A rate filing that uses credit reports or credit scores must comply with the requirements of s. 627.062 or s. 627.0651 to

> ensure that rates are not excessive, inadequate, or unfairly discriminatory.
>
> * * *
>
> (8) The commission may adopt rules to administer this section. The rules may include, but need not be limited to:
>
> * * *
>
> (c) Standards that ensure that rates or premiums associated with the use of a credit report or score are not unfairly discriminatory, based upon race, color, religion, marital status, age, gender, income, national origin, or place of residence.

47. Petitioners contend that the statute's use of the term "unfairly discriminatory" is unexceptionable, that the Legislature simply intended the term to be used and understood in the traditional sense of actuarial soundness alone. Respondents agree that Subsection 626.9741(5), Florida Statutes, calls for the agency to apply the traditional definition of "unfairly discriminatory" as that term is employed in the statutes directly referenced, Sections 627.062 and 627.0651, Florida Statutes, the relevant texts of which are set forth in Findings of Fact 18 and 19 above.

48. However, Respondents contend that Subsection 626.9741(8)(c), Florida Statutes, calls for more than the application of the Rating Law's definition of the term. Respondents assert that in the context of this provision,

"unfairly discriminatory" contemplates not only the predictive function, but also "discrimination" in its more common sense, as the term is employed in state and federal civil rights law regarding race, color, religion, marital status, age, gender, income, national origin, or place of residence.

49. At the hearing, OIR General Counsel Steven Parton testified as to the reasons why the agency chose the federal body of law using the term "disparate impact" as the test for unfair discrimination in the Proposed Rule:

> Well, first of all, what we were looking for is a workable definition that people would have some understanding as to what it meant when we talked about unfair discrimination.
>
> We were also looking for a test that did not require any willfulness, because it was not our concern that, in fact, insurance companies were engaging willfully in unfair discrimination.
>
> What we believed is going on, and we think all of the studies that are out there suggest, is that credit scoring is having a disparate impact upon various people, whether it be income, whether it be race. . . .

50. Respondents' position is that Subsection 626.9741(8)(c), Florida Statutes, requires that a proposed rate or premium be rejected if it has a "disproportionately" negative effect on one of the named classes of persons, even though the rate or premium equitably reflects the differences in expected

losses and expenses between policyholders. In the words of Mr. Parton, "This is not an actuarial rule."

51. Mr. Parton explained the agency's rationale for employing a definition of "unfairly discriminatory" that is different from the actuarial usage employed in the Rating Law. Subsection 626.9741(5), Florida Statutes, already provides that an insurer's rate filings may not be "excessive, inadequate, or unfairly discriminatory" in the actuarial sense. To read Subsection 626.9741(8)(c), Florida Statutes, as simply a reiteration of the actuarial "unfair discrimination" rule would render the provision, "a nullity. There would be no force and effect with regards to that."

52. Thus, the Proposed Rule defines "unfairly discriminatory" to mean "that adverse decisions resulting from the use of a credit scoring methodology disproportionately affects persons belonging to any of the classes set forth in Section 626.9741(8)(c), F.S." Proposed Florida Administrative Code Rule 69O-125.005(1)(e). OIR's actuary, Howard Eagelfeld, explained that "disproportionate effect" means "having a different effect on one group . . . causing it to pay more or less premium than its proportionate share in the general population or than it would have to pay based upon all other known considerations." Mr. Eagelfeld's explanation is not incorporated into the language of the Proposed Rule.

53. Consistent with the actuarial definition of "unfairly discriminatory," the Proposed Rule requires that any credit scoring methodology must be "demonstrated to be a valid predictor of the insurance risk to be assumed by an insurer for the applicable type of insurance," and sets forth detailed criteria through which the insurer can make the required demonstration. Proposed Florida Administrative Code Rule 69O-125.005(9)(a)-(f) and (h)-(l).

54. Proposed Florida Administrative Code Rule 69O-125.005(9)(g) sets forth Respondents' "civil rights" usage of the term "unfairly discriminatory." The insurer's demonstration of the validity of its credit scoring methodology must include:

> [d]ocumentation consisting of statistical testing of the application of the credit scoring model to determine whether it results in a disproportionate impact on the classes set forth in Section 626.9741(8)(c), F.S. A model that disproportionately affects any such class of persons is presumed to have a disparate impact and is presumed to be unfairly discriminatory.[11]

55. Mr. Parton, who testified in defense of the Proposed Rule as one of its chief draftsmen, stated that the agency was concerned that the use of credit scoring may be having a disproportionate effect on minorities. Respondents believe that credit scoring may simply be a surrogate measure for income, and that using income as a basis for setting rates would have an

obviously disparate impact on lower-income persons, including the young and the elderly.

56. Mr. Parton testified that "neither the insurance industry nor anyone else" has researched the theory that credit scoring may be a surrogate for income. Mr. Miller referenced a 1998 analysis performed by AIA indicating that the average credit scores do not vary significantly according to the income group. In fact, the lowest income group (persons making less than $15,000 per year) had the highest average credit score, and the average credit scores actually dropped as income levels rose until the income range reached $50,000 to $74,000 per year, when the credit scores began to rise. Mr. Miller testified that a credit score is no more predictive of income level than a coin flip.

57. However, Respondents introduced a January 2003 report to the Washington State Legislature prepared by the Social & Economic Sciences Research Center of Washington State University, titled "Effect of Credit Scoring on Auto Insurance Underwriting and Pricing." The purpose of the study was to determine whether credit scoring has unequal impacts on specific demographic groups. For this study, the researchers received data from three insurance companies on several thousand randomly chosen customers, including the customers' age, gender, residential zip code, and their credit scores and/or rate

classifications. The researchers contacted about 1,000 of each insurance company's customers and obtained information about their ethnicity, marital status, and income levels. The study's findings were summarized as follows:

> The demographic patterns discerned by the study are:
>
> 1. Age is the most significant factor. In almost every analysis, older drivers have, on average, higher credit scores, lower credit-based rate assignments, and less likelihood of lacking a valid credit score.
>
> 2. Income is also a significant factor. Credit scores and premium costs improve as income rises. People in the lowest income categories-- less than $20,000 per year and between $20,000 and $35,000 per year-- often experienced higher premiums and lower credit scores. More people in lower income categories also lacked sufficient credit history to have a credit score.
>
> 3. Ethnicity was found to be significant in some cases, but because of differences among the three firms studied and the small number of ethnic minorities in the samples, the data are not broadly conclusive. In general, Asian/Pacific Islanders had credit scores more similar to whites than to other minorities. When other minority groups had significant differences from whites, the differences were in the direction of higher premiums. In the sample of cases where insurance was cancelled based on credit score, minorities who were not Asian/Pacific Islanders had greater difficulty finding replacement insurance, and were more likely to experience a lapse in insurance while they searched for a new policy.
>
> 4. The analysis also considered gender, marital status and location, but for these

> factors, significant unequal effects were far less frequent. (emphasis added)

58. The evidence appears equivocal on the question of whether credit scoring is a surrogate for income. The Washington study seems to indicate that ethnicity may be a significant factor in credit scoring, but that significant unequal effects are infrequent regarding gender and marital status.

59. The evidence demonstrates that the use of credit scores by insurers would tend to have a negative impact on young people. Mr. Miller testified that persons between ages 25 and 30 have lower credit scores than older people.

60. Petitioners argue that by defining "unfairly discriminatory" to mean "disproportionate effect," the Proposed Rule effectively prohibits insurers from using credit scores, if only because all the parties recognize that credit scores have a "disproportionate effect" on young people. Petitioners contend that this prohibition is in contravention of Section 626.9741(1), Florida Statutes, which states that the purpose of the statute is to "regulate and limit" the use of credit scores, not to ban them outright.

61. Respondents counter that if the use of credit scores is "unfairly discriminatory" toward one of the listed classes of persons in contravention of Subsection 626.9741(8)(c), Florida

Statutes, then the "limitation" allowed by the statute must include prohibition. This point is obviously true but sidesteps the real issues: whether the statute's undefined prohibition on "unfair discrimination" authorizes the agency to employ a "disparate impact" or "disproportionate effect" definition in the Proposed Rule, and, if so, whether the Proposed Rule sufficiently defines any of those terms to permit an insurer to comply with the rule's requirements.

62. Proposed Florida Administrative Code Rule 69O-125.005(2) provides that the insurer bears the burden of demonstrating that its credit scoring methodology does not disproportionately affect persons based upon their race, color, religion, marital status, age, gender, income, national origin, or place of residence. Petitioners state that no insurer can demonstrate, consistent with the Proposed Rule, that its credit scoring methodology does not have a disproportionate effect on persons based upon their age. Therefore, no insurer will ever be permitted to use credit scores under the terms of the Proposed Rule.

63. As discussed more fully in Findings of Fact 73 through 76 below, Petitioners also contend that the Proposed Rule provides no guidance as to what "disproportionate effect" and "disparate impact" mean, and that this lack of definitional guidance will permit the agency to reject any rate filing that

uses credit scoring, based upon an arbitrary determination that it has a "disproportionate effect" on one of the classes named in Subsection 626.9741(8)(c), Florida Statutes.

64. Petitioners also presented evidence that no insurer collects data on race, color, religion, or national origin from applicants or insureds. Mr. Miller testified that there is no reliable independent source for race, color, religious affiliation, or national origin data. Mr. Eagelfeld agreed that there is no independent source from which insurers can obtain credible data on race or religious affiliation.

65. Mr. Parton testified that this lack of data can be remedied by the insurance companies commencing to request race, color, religion, and national origin information from their customers, because there is no legal impediment to their doing so. Mr. Miller testified that he would question the reliability of the method suggested by Mr. Parton because many persons will refuse to answer such sensitive questions or may not answer them correctly. Mr. Miller stated that, as an actuary, he would not certify the results of a study based on demographic data obtained in this manner and would qualify any resulting actuarial opinion due to the unreliability of the database.

66. Petitioners also object to the vagueness of the broad categories of "race, color, religion and national origin." Mr. Miller testified that the Proposed Rule lacks "operational

definitions" for those terms that would enable insurers to perform the required calculations. The Proposed Rule places the burden on the insurer to demonstrate no disproportionate effect on persons based on these categories, but offers no guidance as to how these demographic classes should be categorized by an insurer seeking to make such a demonstration.

67. Petitioners point out that even if the insurer is able to ascertain the categories sought by the regulators, the Proposed Rule gives no guidance as to whether the "disproportionate effect" criterion mandates perfect proportionality among all races, colors, religions, and national origins, or whether some degree of difference is tolerable. Petitioners contend that this lack of guidance provides unbridled discretion to the regulator to reject any disproportionate effect study submitted by an insurer.

68. At his deposition, Mr. Parton was asked how an insurer should break down racial classifications in order to show that there is no disproportionate effect on race. His answer was as follows:

> There is African-American, Cuban-American, Spanish-American, African-American, Haitian-American. Are you-- you know, whatever the make-up of your book of business is-- you're the one in control of it. You can ask these folks what their ethnic background is.

69. At his deposition, Mr. Parton frankly admitted that he had no idea what "color" classifications an insurer should use, yet he also stated that an insurer must demonstrate no disproportionate effect on each and every listed category, including "color." At the final hearing, when asked to list the categories of "color," Mr. Parton responded, "I suppose Indian, African-American, Chinese, Japanese, all of those."[12]

70. At the final hearing, Mr. Parton was asked whether the Proposed Rule contemplates requiring insurers to demonstrate distinctions between such groups as "Latvian-Americans" and "Czech-Americans." Mr. Parton's reply was as follows:

> No. And I don't think it was contemplated by the Legislature. . . . The question is race by any other name, whether it be national origin, ethnicity, color, is something that they're concerned about in terms of an impact.
>
> What we would anticipate, and what we have always anticipated, is the industry would demonstrate whether or not there is an adverse effect against those folks who have traditionally in Florida been discriminated against, and that would be African-Americans and certain Hispanic groups.
>
> In our opinion, at least, if you could demonstrate that the credit scoring was not adversely impacting it, it may very well answer the questions to any other subgroup that you may want to name.

71. At the hearing, Mr. Parton was also questioned as to distinctions between religions and testified as follows:

> The impact of credit scoring on religion is going to be in the area of what we call thin files, or no files. That is to say people who do not have enough credit history from which credit scores can be done, or they're going to be treated somehow differently because of that lack of history. A simple question that needs to be asked by the insurance company is: "Do you, as a result of your religious belief or whatever [sect] you are in, are you forbidden as a precept of your religious belief from engaging in the use of credit?"

72. When cross-examined on the subject, Mr. Parton could not confidently identify any religious group that forbids the use of credit. He thought that Muslims and Quakers may be such groups. Mr. Parton concluded by stating, "I don't think it is necessary to identify those groups. The question is whether or not you have a religious group that you prescribe to that forbids it."

73. Petitioners contend that, in addition to failing to define the statutory terms of race, color, religion, and national origin in a manner that permits insurer compliance, the Proposed Rule fails to provide an operational definition of "disproportionate effect." The following is a hypothetical question put to Mr. Parton at his deposition, and Mr. Parton's answer:

> Q: Let's assume that African-Americans make up 10 percent of the population. Let's just use two groups for the sake of clarity. Caucasians make up 90 percent. If the application of credit scoring in

> underwriting results in African-Americans paying 11 percent of the premium and Caucasians paying 89 percent of the premium, is that, in your mind, a disproportionate affect [sic]?
>
> A: It may be. I think it would give rise under this rule that perhaps there is a presumption that it is, but that presumption is not [an irrebuttable] one.[13] For instance, if you then had testimony that a 1 percent difference between the two was statistically insignificant, then I would suggest that that presumption would be overridden.

74. This answer led to a lengthy discussion regarding a second hypothetical in which African-Americans made up 29 percent of the population, and also made up 35 percent of the lowest, or most unfavorable, tier of an insurance company's risk classifications. Mr. Parton ultimately opined that if the difference in the two numbers was found to be "statistically significant" and attributable only to the credit score, then he would conclude that the use of credit scoring unfairly discriminated against African-Americans.

75. As to whether his answer would be the same if the hypothetical were adjusted to state that African-Americans made up 33 percent of the lowest tier, Mr. Parton responded: "That would be up to expert testimony to be provided on it. That's what trials are all about."[14]

76. Aside from expert testimony to demonstrate that the difference was "statistically insignificant," Mr. Parton could

think of no way that an insurer could rebut the presumption that the difference was unfairly discriminatory under the "disproportionate effect" definition set forth in the proposed rule. He stated that, "I can't anticipate, nor does the rule propose to anticipate, doing the job of the insurer of demonstrating that its rates are not unfairly discriminatory."

77. Mr. Parton testified that an insurer's showing that the credit score was a valid and important predictor of risk would not be sufficient to rebut the presumption of disproportionate effect.

D. Summary Findings

78. Credit-based insurance scoring is a valid and important predictor of risk, significantly increasing the accuracy of the risk assessment process. The evidence is still inconclusive as to why credit scoring is an effective predictor of risk, though a study co-authored by Dr. Brockett has found that basic chemical and psychobehavioral characteristics, such as a sensation-seeking personality type, are common to individuals exhibiting both higher insured automobile losses and poorer credit scores.

79. Though the evidence was equivocal on the question of whether credit scoring is simply a surrogate for income, the evidence clearly demonstrated that the use of credit scores by insurance companies has a greater negative overall effect on

young people, who tend to have lower credit scores than older people.

80. Petitioners and Fair Isaac emphasized their contention that compliance with the Proposed Rule would be impossible, and thus the Proposed Rule in fact would operate as a prohibition on the use of credit scoring by insurance companies. At best, Petitioners demonstrated that compliance with the Proposed Rule would be impracticable at first, given the current business practices in the industry regarding the collection of customer data regarding race and religion. The evidence indicated no legal barriers to the collection of such data by the insurance companies. Questions as to the reliability of the data are speculative until a methodology for the collection of the data is devised.

81. Subsection 626.9741(8)(c), Florida Statutes, authorizes the FSC to adopt rules that may include:

> Standards that ensure that rates or premiums associated with the use of a credit report or score are not unfairly discriminatory, based upon race, color, religion, marital status, age, gender, income, national origin, or place of residence.

82. Petitioners' contention that the statute's use of "unfairly discriminatory" contemplates nothing more than the actuarial definition of the term as employed by the Rating Law is rejected. As Respondents pointed out, Subsection

626.9741(5), Florida Statutes, provides that a rate filing using credit scores must comply with the Rating Law's requirements that the rates not be "unfairly discriminatory" in the actuarial sense. If Subsection 626.9741(8)(c), Florida Statutes, merely reiterates the actuarial requirement, then it is, in Mr. Parton's words, "a nullity."[15]

83. Thus, it is found that the Legislature contemplated some level of scrutiny beyond actuarial soundness to determine whether the use of credit scores "unfairly discriminates" in the case of the classes listed in Subsection 626.9741(8)(c), Florida Statutes. It is found that the Legislature empowered FSC to adopt rules establishing standards to ensure that an insurer's rates or premiums associated with the use of credit scores meet this added level of scrutiny.

84. However, it must be found that the term "unfairly discriminatory" as employed in the Proposed Rule is essentially undefined. FSC has not adopted a "standard" by which insurers can measure their rates and premiums, and the statutory term "unfairly discriminatory" is thus subject to arbitrary enforcement by the regulating agency. Proposed Florida Administrative Code Rule 69O-125.005(1)(e) defines "unfairly discriminatory" in terms of adverse decisions that "disproportionately affect" persons in the classes set forth in

Subsection 626.9741(8)(c), Florida Statutes, but does not define what is a "disproportionate effect."

85. At Subsection (9)(g), the Proposed Rule requires "statistical testing" of the credit scoring model to determine whether it results in a "disproportionate impact" on the listed classes. This subsection attempts to define its terms as follows:

> A model that disproportionately affects any such class of persons is presumed to have a disparate impact and is presumed to be unfairly discriminatory.

86. Thus, the Proposed Rule provides that a "disproportionate effect" equals a "disparate impact" equals "unfairly discriminatory," without defining any of these terms in such a way that an insurer could have any clear notion, prior to the regulator's pronouncement on its rate filing, whether its credit scoring methodology was in compliance with the rule.

87. Indeed, Mr. Parton's testimony evinced a disinclination on the part of the agency to offer guidance to insurers who attempt to understand this circular definition. The tenor of his testimony indicated that the agency itself is unsure of exactly what an insurer could submit to satisfy the "disproportionate effect" test, aside from perfect proportionality, which all parties concede is not possible at least as to young people, or a showing that any lack of perfect

proportionality is "statistically insignificant," whatever that means. Mr. Parton seemed to say that OIR will know a valid use of credit scoring when it sees one, though it cannot describe such a use beforehand.

88. Mr. Eagelfeld offered what might be a workable definition of "disproportionate effect," but his definition is not incorporated into the Proposed Rule. Mr. Parton attempted to assure the Petitioners that OIR would take a reasonable view of the endless racial and ethnic categories that could be subsumed under the literal language of the Proposed Rule, but again, Mr. Parton's assurances are not part of the Proposed Rule.

89. Mr. Parton's testimony referenced federal and state civil rights laws as the source for the term "disparate impact." Federal case law under Title VII of the Civil Rights Act of 1964, 42 U.S.C. § 2000e-2, has defined a "disparate impact" claim as "one that 'involves employment practices that are facially neutral in their treatment of different groups, but that in fact fall more harshly on one group than another and cannot be justified by business necessity.'" Adams v. Florida Power Corporation, 255 F.3d 1322, 1324 n.4 (11th Cir. 2001), quoting Hazen Paper Co. v. Biggins, 507 U.S. 604, 609, 113 S. Ct. 1701, 1705, 123 L. Ed. 2d 338 (1993). The Proposed Rule does not reference this definition, nor did Mr. Parton detail

how OIR proposes to apply or modify this definition in enforcing the Proposed Rule.

90. Without further definition, all three of the terms employed in this circular definition are conclusions, not "standards" that the insurer and the regulator can agree upon at the outset of the statistical and analytical process leading to approval or rejection of the insurer's rates. Absent some definitional guidance, a conclusory term such as "disparate impact" can mean anything the regulator wishes it to mean in a specific case.

91. The confusion is compounded by the Proposed Rule's failure to refine the broad terms "race," "color," and "religion" in a manner that would allow an insurer to prepare a meaningful rate submission utilizing credit scoring. In his testimony, Mr. Parton attempted to limit the Proposed Rule's impact to those groups "who have traditionally in Florida been discriminated against," but the actual language of the Proposed Rule makes no such distinction. Mr. Parton also attempted to limit the reach of "religion" to groups whose beliefs forbid them from engaging in the use of credit, but the language of the Proposed Rule does not support Mr. Parton's distinction.

## CONCLUSIONS OF LAW

92. The Division of Administrative Hearings has jurisdiction over the parties and the subject matter of this proceeding pursuant to Section 120.56, Florida Statutes.

93. Subsection 120.56(1)(a), Florida Statutes, provides that, "Any person substantially affected by a rule or a proposed rule may seek an administrative determination of the invalidity of the rule on the ground that the rule is an invalid exercise of delegated legislative authority." Subsection 120.56(2)(a), Florida Statutes, provides that in challenges to proposed rules, "Petitioner has the burden of going forward. The agency then has the burden to prove by a preponderance of the evidence that the proposed rule is not an invalid exercise of delegated legislative authority as to the objections raised."

94. In order to prove that they are "person[s] substantially affected" in this case, Petitioners and Fair Isaac must show that they will suffer injury in fact of sufficient immediacy to entitle them to a hearing, and that their substantial injury is of a type or nature which the requested hearing is designed to protect. Agrico Chemical Company v. Department of Environmental Regulation, 406 So. 2d 478, 482 (Fla. 2d DCA 1981). The "injury in fact" aspect of the test deals with the degree of the injury, and the "zone of interest" aspect deals with the nature of the injury. Id. See also

Florida Board of Medicine v. Florida Academy of Cosmetic Surgery, Inc., 808 So. 2d 243, 250 (Fla. 1st DCA 2002); Lanoue v. Florida Department of Law Enforcement, 751 So. 2d 94, 96-97 (Fla. 1st DCA 1999).

95. Fair Isaac concedes that it would not be directly regulated by the Proposed Rule. However, Fair Isaac contends that it meets the standard for standing enunciated in Florida Board of Medicine v. Florida Academy of Cosmetic Surgery, Inc. In that case, the court held that certified registered nurse anesthetists ("CRNAs") had standing to challenge a proposed Board of Medicine rule requiring that an anesthesiologist be present during certain office surgical procedures, though the proposed rule did not directly regulate the CRNAs. The court explained that a challenger to a proposed rule may be substantially affected by the rule "even where the rule or promulgating statute does not regulate the challenger's profession per se." Academy of Cosmetic Surgery, 808 So. 2d at 251, citing Ward v. Board of Trustees of the Internal Improvement Trust Fund, 651 So. 2d 1236, 1238 (Fla. 4th DCA 1995). The court noted that in Televisual Communications, Inc. v. Department of Labor and Employment Security, 667 So. 2d 372 (Fla. 1st DCA 1995), it had held that a challenger can be substantially affected by a rule that has a collateral financial impact on the challenger's business.[16] In Academy of Cosmetic

Surgery, the court found it sufficient that several physicians had testified that they would not employ CRNAs for certain office surgeries if the presence of an anesthesiologist was required, because such would be redundant and not cost effective. Academy of Cosmetic Surgery, 808 So. 2d at 251.

96. In the instant case, Fair Isaac has offered evidence that its business in the State of Florida would be damaged, if not entirely eliminated, by the Proposed Rule. Testimony from the Petitioners' experts supported Fair Isaac's position that the Proposed Rule would effectively eliminate the use of credit scoring in setting rates for personal lines motor vehicle insurance and personal lines residential insurance in the State of Florida. Fair Isaac has shown that it would suffer an injury in fact if the Proposed Rule were adopted.

97. Fair Isaac has also shown that the injury is of a type that the hearing requested is designed to protect. The Proposed Rule sets forth requirements that, via restrictions on insurers' use of credit scoring, would directly impact Fair Isaac's manner of doing business in the State of Florida.

98. AIA, NAMIC, PCI, and FIC are all trade associations. An association has standing to challenge the validity of a proposed rule on behalf of its members "when that association fairly represents members who have been substantially affected by the rule." Florida Home Builders Association v. Department

of Labor and Employment Security, 412 So. 2d 351, 352 (Fla. 1982). To establish associational standing, an association "must demonstrate that a substantial number of its members, although not necessarily a majority, are 'substantially affected' by the challenged rule. Further, the subject matter of the rule must be within the association's general scope of interest and activity, and the relief requested must be of the type appropriate for a trade association to receive on behalf of its members." Id. at 353-354. This standard was reaffirmed in NAACP, Inc. v. Florida Board of Regents, 863 So. 2d 294 (Fla. 2003).

99. AIA, NAMIC, PCI, and FIC have established their standing under the associational standard set forth in Florida Home Builders. Substantial numbers of each Petitioner's members do business in Florida and would be directly regulated by the Proposed Rule. These trade associations' general scope of interest and activity is to represent their members' interests in regulatory and legislative matters in Florida. The Proposed Rule falls within the ambit of Petitioners' representation of their members, and a proceeding seeking to declare the Proposed Rule invalid is appropriate relief for a trade association to seek on behalf of its members.

100. Subsection 120.56(1)(e), Florida Statutes, provides that a rule challenge proceeding is de novo in nature and that

the standard of proof is a preponderance of the evidence. The Administrative Law Judge should consider and base the decision upon all of the available evidence, regardless of whether the evidence was placed before the agency during its rulemaking proceedings. Department of Health v. Merritt, 919 So. 2d 561, 564 (Fla. 1st DCA 2006) (concluding that the Legislature has overruled the court's holding in Academy of Cosmetic Surgery that an administrative law judge's role in a proposed rule is limited to a review of the record and a determination as to whether the agency action was supported by legally sufficient evidence).

101. Subsection 120.56(2)(a), Florida Statutes, provides that in a proposed rule challenge proceeding, the petitioner has the burden of going forward. The agency then has the burden to prove by a preponderance of the evidence that the proposed rule is not an invalid exercise of delegated legislative authority as to the objections raised. Thus, once a petitioner has established a factual basis for its objection to the proposed rule, the agency has the ultimate burden of persuasion of showing that the proposed rule is a valid exercise of delegated legislative authority. Southwest Florida Water Management District v. Charlotte County, 774 So. 2d 903, 908 (Fla. 2d DCA 2001), quoting St. Johns River Water Management District v.

Consolidated-Tomoka Land Co., 717 So. 2d 72, 77 (Fla. 1st DCA 1998).

102. Subsection 120.52(8), Florida Statutes, states as follows:

> "Invalid exercise of delegated legislative authority" means action which goes beyond the powers, functions, and duties delegated by the Legislature. A proposed or existing rule is an invalid exercise of delegated legislative authority if any one of the following applies:
>
> (a) The agency has materially failed to follow the applicable rulemaking procedures or requirements set forth in this chapter;
>
> (b) The agency has exceeded its grant of rulemaking authority, citation to which is required by s. 120.54(3)(a)1.;
>
> (c) The rule enlarges, modifies, or contravenes the specific provisions of law implemented, citation to which is required by s. 120.54(3)(a)1.;
>
> (d) The rule is vague, fails to establish adequate standards for agency decisions, or vests unbridled discretion in the agency;
>
> (e) The rule is arbitrary or capricious. A rule is arbitrary if it is not supported by logic or the necessary facts; a rule is capricious if it is adopted without thought or reason or is irrational;
>
> (f) The rule imposes regulatory costs on the regulated person, county, or city which could be reduced by the adoption of less costly alternatives that substantially accomplish the statutory objectives.
>
> A grant of rulemaking authority is necessary but not sufficient to allow an agency to

> adopt a rule; a specific law to be implemented is also required. An agency may adopt only rules that implement or interpret the specific powers and duties granted by the enabling statute. No agency shall have authority to adopt a rule only because it is reasonably related to the purpose of the enabling legislation and is not arbitrary and capricious or is within the agency's class of powers and duties, nor shall an agency have the authority to implement statutory provisions setting forth general legislative intent or policy. Statutory language granting rulemaking authority or generally describing the powers and functions of an agency shall be construed to extend no further than implementing or interpreting the specific powers and duties conferred by the same statute.

103. In this case, Petitioners challenge the proposed rule based on Subsections 120.52(8)(a) through 120.52(8)(e), Florida Statutes. Each of these potential reasons for invaliding the proposed rule is addressed below.

Subsection 120.52(8)(a), Florida Statutes

104. Petitioners initially alleged that FSC improperly attempted to delegate its rulemaking authority to OIR, and that OIR therefore lacked authority to promulgate the Proposed Rule. As noted in the Preliminary Statement above, FSC cured this alleged failure to follow applicable rulemaking procedures by approving the Proposed Rule on June 16, 2005. The Proposed Rule was then re-published in the July 1, 2005, edition of the Florida Administrative Weekly. No other colorable violations of

Subsection 120.52(8)(a), Florida Statutes, were alleged by Petitioners or Fair Isaac.

Subsection 120.52(8)(b), Florida Statutes

105. The specific authority cited for FSC's promulgation of the Proposed Rule is Subsections 624.308(1) and 626.9741(8), Florida Statutes. Subsection 624.308(1), Florida Statutes, provides:

> The [Department of Financial Services] and the [FSC] may each adopt rules pursuant to ss. 120.536 (1) and 120.54 to implement provisions of law conferring duties upon the department or the commission, respectively.

106. Subsection 626.9741(8), Florida Statutes, is set forth in full at Finding of Fact 11 above. For purposes of this discussion, the relevant language provides that FSC may adopt rules to administer Section 626.9741, Florida Statutes, and that those rules may include "[s]tandards that ensure that rates or premiums associated with the use of a credit report or score are not unfairly discriminatory, based upon race, color, religion, marital status, age, gender, income, national origin, or place of residence."

107. In their Proposed Final Order, Respondents also claim that Subsection 626.9741(4)(c)4., Florida Statutes, provides specific authority for the Proposed Rule. The cited subparagraph provides:

> (c) An insurer may not make an adverse decision or use a credit score that could lead to such a decision if based, in whole or in part, on:
>
> * * *
>
> 4. Any other circumstance that the Financial Services Commission determines, by rule, lacks sufficient statistical correlation and actuarial justification as a predictor of insurance risk.

108. An agency engaging in rulemaking must identify both the statutory authority for the rulemaking and a statute or act to be implemented by the rulemaking. Department of Children and Family Services v. I.B., 891 So. 2d 1168, 1171 (Fla. 1st DCA 2005), quoting Osterback v. Agwunobi, 873 So. 2d 437, 440 (Fla. 1st DCA 2004). Having failed to identify Subsection 626.9741(4)(c)4., Florida Statutes, as specific authority for the Proposed Rule, Respondents may not now rely upon that provision.[17] See Smith v. Department of Corrections, 920 So. 2d 638, 642 (Fla. 1st DCA 2005) (court implied that it would not have considered agency's claim of statutory authority had the agency not amended the rule to include a citation to the statute in question).

109. Nonetheless, the FSC's grant of rulemaking authority clearly encompasses the subject matter of the Proposed Rule, which is the use of credit reports and credit scores by insurers. Subsection 626.9741(8), Florida Statutes, provides

specific authority to FSC to adopt rules setting forth standards regarding the use of credit scoring as a valid predictor of risk and standards to ensure that rates or premiums associated with the use of credit reports are not unfairly discriminatory, based upon race, color, religion, marital status, age, gender, income, national origin, or place of residence.

Subsection 120.52(8)(c), Florida Statutes

110. The Proposed Rule cites Subsection 624.307(1) and Section 626.9741, Florida Statutes, as laws implemented. Subsection 624.307(1), Florida Statutes, states as follows:

> (1) The department and the [OIR] shall enforce the provisions of this code and shall execute the duties imposed upon them by this code, within the respective jurisdiction of each, as provided by law.

111. Section 626.9741, Florida Statutes, is set forth in full at Finding of Fact 11 above.

112. Petitioners contend that the Proposed Rule's definition of "unfairly discriminatory" enlarges, modifies, or contravenes the specific provisions of the laws implemented and of the Rating Law. Section 626.9741, Florida Statutes, employs the term "unfairly discriminatory" without defining the term. Petitioners contend that no definition was necessary because "unfairly discriminatory" has a common, actuarially-based meaning in the insurance industry and within Florida's Rating Law itself. A rate is deemed "unfairly discriminatory" if the

premium charged does not equitably reflect the differences in expected losses and expense factors for a given group or class of insureds. See Subsections 627.062(2)(e)6., and 627.0651(6), (7), and (8), Florida Statutes, set forth in full at Findings of Fact 18 and 19 above.

113. Petitioners cite the rule of construction that where the Legislature uses exact words in different statutory provisions, it may be assumed the words were intended to mean the same thing. St. George Island, Ltd. v. Rudd, 547 So. 2d 958, 961 (Fla. 1st DCA 1989). They contend that the term "unfairly discriminatory" in Subsections 626.9741(5) and (8) should be given the same technical meaning it has been given in the Rating Law provisions cited above. "Words of common usage in a statute should be given their natural, usual, plain, ordinary meanings unless they are used in a technical sense." State v. Brown, 412 So. 2d 426, 428 (Fla. 4th DCA 1982) (emphasis added).

114. Petitioners contend that the Proposed Rule impermissibly enlarges this definition by grafting onto the actuarial sense of "unfairly discriminatory," a second meaning not contemplated by Section 626.9741, Florida Statutes. The second meaning countenances "discrimination" as that term is used in state and federal civil rights laws. The drafters of the Proposed Rule employed the terms "disparate impact" and

"disproportionate effect" in an attempt to give insurers and the general public "some understanding as to what it meant when we talked about unfair discrimination," in the words of Mr. Parton.

115. Although Petitioners' argument is persuasive, Respondents' argument is more convincing as to the interpretation of the statute. Subsection 626.9741(5), Florida Statutes, already provides that rate filings using credit scores may not be "unfairly discriminatory" in the actuarial sense and incorporates the Rating Law's definitions of "unfairly discriminatory." If Subsection 626.9741(8)(c), Florida Statutes, merely reiterates the requirement that rate filings using credit scores may not be "unfairly discriminatory" in terms of actuarial soundness alone, then either Subsection (5) or (8)(c) must be surplusage.[18]

116. "It is an elementary principle of statutory construction that significance must be given to every word, phrase, sentence, and part of the statute if possible and words in a statute should not be construed as mere surplusage." Department of State v. Martin, 916 So. 2d 763, 768-769 (Fla. 2005), quoting Hechtman v. Nations Title Insurance of New York, 840 So. 2d 993, 996 (Fla. 2003). "It is also a basic rule of statutory construction that 'the Legislature does not intend to enact useless provisions, and courts should avoid readings that would render part of a statute meaningless.'" Borden v. East-

European Insurance Company, 921 So. 2d 587, 595 (Fla. 2006), quoting State v. Goode, 830 So. 2d 817, 824 (Fla. 2002).

117. To give significance and meaning to Subsection 626.9741(8)(c), Florida Statutes, it is concluded that the provision that the FSC may adopt rules, including standards ensuring that rates using credit reports are not "unfairly discriminatory, based upon race, color, religion, marital status, age, gender, income, national origin, or place of residence" must contemplate a level of scrutiny beyond the actuarial soundness already provided for in Subsection 626.9741(5), Florida Statutes.[19]

118. Petitioners contend that this case is identical to Department of Insurance v. Insurance Services Office, 434 So. 2d 908 (Fla. 1st DCA 1983). In that case, the Department of Insurance promulgated a rule that prohibited insurers from establishing classifications or premium rates for motor vehicle insurance based upon the sex, marital status, or scholastic achievement of the insured. The statute that the proposed rule purported to implement provided that, "No insurer shall, with respect to premiums charged for automobile insurance, unfairly discriminate solely on the basis of age, sex, marital status, or scholastic achievement." 434 So. 2d at 910-911. The DOAH hearing officer determined that the rule was an invalid exercise of delegated legislative authority, and the court affirmed.

119. Petitioners point out that in Insurance Services Office, the Department of Insurance argued, just as Respondents do in the instant cases, that the term "unfairly discriminatory" should be accorded its common, ordinary meaning and not the technical definition provided by the Rating Law, and that the court rejected that argument. Id. at 912.

120. However, Petitioners ignore a key difference between the instant cases and Insurance Services Office. In the latter case, the court found that the proposed rule exceeded the agency's delegated statutory authority because the rule flatly prohibited the use of sex, marital status, or scholastic achievement as bases for classifications or premium rates, whereas the statute merely prohibited "unfair discrimination" based on those factors. The court and the hearing officer agreed that the statute contemplated some degree of discrimination based on sex, marital status, and scholastic achievement so long as the discrimination was not "unfair" or based solely on those factors. Id. at 911. To support its view of the statute and the agency's overreach, the court noted legislative history indicating that the Legislature had considered and rejected legislation enacting a flat prohibition on the use of the listed factors. Id. The court concluded that the Legislature had, by implication, approved the view that rates based upon sex, marital status or scholastic achievement

are unfair only if those rating factors are found to be actuarially unsound. Id. at 913.

121. To support its proposed rule, the Department of Insurance argued that the term "unfairly discriminatory" should be given its ordinary meaning, which the Department contended meant that a rating factor would be unfairly discriminatory unless it had a causal connection to expected losses. Because sex, marital status, and scholastic achievement have no direct or causal connection to a person's driving habits, the Department contended they were necessarily, unfairly discriminatory rating factors. Id. at 912.

122. The hearing officer found that the Department did not establish that the use of the prohibited criteria would necessarily result in unfair discrimination; to the contrary, the evidence established that the classification factors of sex, marital status, and scholastic achievement enhanced the actuarial soundness of the rate classification schedule for automobile insurance. Id. at 912-913.

123. Thus, the primary distinction between the instant cases and Insurance Services Office is that in the latter, the proposed rule on its face exceeded the grant of rulemaking authority by enacting a flat prohibition on rating factors that the statute did not prohibit. The Proposed Rule in the instant

cases does not, on its face, enact a flat prohibition on the use of credit scoring in contravention of the authorizing statute.

124. A second distinction is that in Insurance Services Office, the court determined that there was no statutory basis for the Department's position that "unfairly discriminatory" meant anything other than actuarial soundness. In the instant cases, Section 626.9741, Florida Statutes, read in its entirety, provides support for Respondents' contention that Subsection 626.9741(8)(c), Florida Statutes, contemplates a definition of "unfairly discriminatory" that extends beyond actuarial soundness.

125. Respondents are correct in their conceptual argument that, under Subsection 626.9741(8)(c), Florida Statutes, "unfairly discriminatory" contemplates an added level of scrutiny, beyond actuarial soundness. However, this initial conclusion does not end the inquiry. The question remains whether the approach actually taken by FSC in the Proposed Rule enlarges, modifies, or contravenes the statutes it purports to implement.

126. Petitioners pointedly note that the terms "disproportionate" and "disparate" do not appear anywhere in the implemented statute. They contend that nothing in Section 626.9741, Florida Statutes, indicates a legislative intent "to subject policy holders to the invasion of privacy implicated by

divulging their religious affiliation, income, race, color or national origin every time they apply for automobile or homeowners insurance." If the statute had such an intent, Petitioners contend the Legislature would also have provided for the protection of this sensitive data to ensure that it is not used as a basis for intentional discrimination, and would have addressed whether an insurer can refuse to offer insurance to applicants who fail to answer "these sensitive questions, or cancel insurance for those who refuse to comply."

127. Respondents reply that an agency is allowed to provide a permissible explication and definition of statutory terminology without engaging in an invalid exercise of delegated legislative authority. Board of Podiatric Medicine v. Florida Medical Association, 779 So. 2d 658 (Fla. 1st DCA 2001) (upholding agency's definition of "human leg" as that term was used in the statutory scheme). Respondents are entitled to great deference in their interpretation of a statute they administer, unless there is clear error or conflict with the intent of the statute. Verizon Florida, Inc. v. Jacobs, 810 So. 2d 906 (Fla. 2002); BellSouth Telecommunications, Inc. v. Johnson, 708 So. 2d 594 (Fla. 1998); Florida Wildlife Federation v. Collier County, 819 So. 2d 200 (Fla. 1st DCA 2002); Department of Insurance and Treasurer v. Bankers Insurance Company, 694 So. 2d 70 (Fla. 1st DCA 1997).

128. Respondents are correct in asserting that this general rule of deference applies for rules that implement statutes that the agency is charged with enforcing. Beach v. Great Western Bank, 692 So. 2d 146, 149 (Fla. 1997); Purvis v. Marion County School Board, 766 So. 2d 492, 498-499 (Fla. 5th DCA 1997). While such deference is not absolute, it is required unless the agency's construction is an unreasonable interpretation or clearly erroneous. Legal Environmental Assistance Foundation, Inc. v. Board of County Commissioners of Brevard County, 642 So. 2d 1081, 1083-1084 (Fla. 1994).

129. However, the Proposed Rule does enlarge, modify, or contravene the specific provisions of law implemented. The Proposed Rule's definitional failure would grant Respondents unchecked authority to arbitrarily reject rate filings as "unfairly discriminatory," in derogation of the statute's provision that the FSC adopt "standards." The FSC had the statutory authority "to provide a permissible explication and definition" of the term "unfairly discriminatory," but the Proposed Rule fails either to explicate or define the term. The problem is not that terms such as "disparate" or "disproportionate" are missing from the implemented statute, because the potential exists that these terms could be defined consistently with the FSC's statutory mandate. The problem is

that the terms have no definite meaning as used in the Proposed Rule.

Subsection 120.52(8)(d), Florida Statutes

130. Petitioners correctly argue that the Proposed Rule is vague, fails to establish adequate standards for agency decisions, and vests unbridled discretion in the regulating agencies. The test for vagueness of a rule or statute is "whether men of common understanding and intelligence must guess at [the provision's] meaning" and differ as to its application. Department of Health and Rehabilitative Services v. Health Care and Retirement Corporation of America, 593 So. 2d 539, 541 (Fla. 1st DCA 1992), quoting State v. Cumming, 365 So. 2d 153, 156 (Fla. 1978) and State v. Rodriguez, 365 So. 2d 157, 159 (Fla. 1978). See also Witmer v. Department of Business and Professional Regulation, 662 So. 2d 1299, 1302 (Fla. 4th DCA 1995).

131. As found above, the Proposed Rule does not define the conclusory term "unfairly discriminatory" except through other conclusory terms, "disproportionate effect" and "disparate impact." None of these terms are defined in a way that would allow a person of "common understanding and intelligence" to understand what the Proposed Rule requires by way of a demonstration that "unfair discrimination" is not taking place. Respondents' own witnesses were unsure of how an insurer should

approach the problem other than by demonstrating that its own rate filings were perfectly proportional as to race, religion, color, and the other categories of persons listed in Subsection 626.9741(8)(c), Florida Statutes. Respondents' witnesses were also unsure how they as regulators would approach a filing that was less than perfectly proportional.

132. Compounding the vagueness is the Proposed Rule's failure to meaningfully narrow or refine the broad terms "race," "color," and "religion" in a manner that would allow an insurer to begin to compile a coherent set of data leading to the "statistical analysis" that the Proposed Rule would require.

133. The civil rights statutes that Mr. Parton testified were the model for the Proposed Rule's definition of "unfairly discriminatory," also employ broad terms such as "race," "color," and "religion." However, their enforcement mechanisms place the initial burden on a petitioner to demonstrate membership in a protected class of persons and to allege a specific, statutorily proscribed discriminatory practice. See, e.g., Ch. 760, Part I, Fla. Stat., the Florida Civil Rights Act of 1992 (particularly § 760.11, Fla. Stat., setting forth administrative and civil remedies).

134. The respondent in a case brought pursuant to Section 760.10, Florida Statutes, is required to address one petitioner's claim of employment discrimination, not all

possible claims of discrimination that could have been brought by any employee or applicant. The narrowness of the field of inquiry in a particular case obviates any concerns regarding the broadness of the general categories of protected persons set forth in a statute such as Subsection 760.10(1)(a), Florida Statutes: "race, color, religion, sex, national origin, age, handicap, or marital status."

135. The Proposed Rule, on the other hand, places the initial burden on an insurer to prove a massive negative proposition, i.e., to demonstrate that its credit scoring model does not "disproportionately impact any class based upon race, color, religion, marital status, age, gender, income, national origin, or place of residence." Absent some definitional narrowing or focusing of the broad terms employed, the Proposed Rule is vague.

136. In defense of the Proposed Rule's definition of "unfairly discriminatory," Respondents again cite the familiar principle that the exercise of discretion in an agency's interpretation of the statutes it administers is not only permissible, but is accorded substantial deference. Level 3 Communications, LLC v. Jacobs, 841 So. 2d 447, 450 (Fla. 2003). Respondents concede that the Proposed Rule is "complicated," but observe that the implemented statute shares that complexity and that "[t]he sufficiency of a rule's standards and guidelines may

depend on the subject matter dealt with and the degree of difficulty involved in articulating finite standards." Southwest Florida Water Management District v. Charlotte County, 774 So. 2d 903, 917 (Fla. 2d DCA 2001), quoting Cole Vision Corporation v. Department of Business and Professional Regulation, 688 So. 2d 404, 410 (Fla. 1st DCA 1997). Finally, Respondents cite the principle that, while the Legislature is obliged by the nondelegation doctrine to establish adequate statutory standards and guidelines, it may delegate subordinate functions "to permit administration of legislative policy by an agency with the expertise and flexibility needed to deal with complex and fluid conditions." Microtel, Inc. v. Public Service Commission, 464 So. 2d 1189, 1191 (Fla. 1985).

137. Relying on these authorities, Respondents contend that there is "simply no magic number that makes a rate filing request excessive, or inadequate, or unfairly discriminatory in the Rating Law." This contention is correct, but neglects the testimony of Respondents' own witness that "this is not an actuarial rule," and Respondents' own contention that the meaning of "unfairly discriminatory" in the context of the Proposed Rule does not conform to the meanings found in the Rating Law. Acceptance of these propositions leads to the conclusion that no special deference is due the agency's interpretation because, despite Respondents' testimonial analogy

to state and federal civil rights laws, the agency is here employing "unfairly discriminatory" in its "plain, ordinary meaning." Zopf v. Singletary, 686 So. 2d 680, 682 (Fla. 1st DCA 1996).

138. In the previously discussed Insurance Services Office case, the Department of Insurance contended that "unfairly discriminatory" should be accorded its common, ordinary meaning rather than the technical definition provided by the Rating Law. In assessing this contention, the court stated:

> Here, somewhat paradoxically, by urging a construction of these terms based upon their common, ordinary meanings, the Department disavows the utilization of any special "agency expertise" in its interpretation of the statute. This mitigates, if it does not entirely eliminate, the rule calling upon the court to accord "great deference" to the agency's interpretation of the statute. (citations omitted)

434 So. 2d at 912.

139. Less deference need be accorded to the agency's interpretation where, as here, the agency is departing from the traditional definition of a term. And Justice for All, Inc. v. Department of Insurance, 799 So. 2d 1076 (Fla. 1st DCA 2001). In any event, the deference to be accorded an agency's interpretation must be tempered where the agency has failed to present a workable definition of the key term in its Proposed Rule. As noted above, the Legislature authorized FSC "to

provide a permissible explication and definition" of the term "unfairly discriminatory," but the Proposed Rule neither explains nor defines the term.

140. Respondents' interpretation of Subsection 626.9741(8)(c), Florida Statutes, as requiring standards beyond the usual actuarial meaning of "unfairly discriminatory" may be permissible, but FSC's expression of that interpretation in the text of the Proposed Rule is vague, fails to establish adequate standards for agency decisions, and vests unbridled discretion in the agency.

Subsection 120.52(8)(e), Florida Statutes

141. Finally, Petitioners contend that the Proposed Rule is arbitrary and capricious. Florida Administrative Code Rule 120.52(8)(e) provides: "A rule is arbitrary if it is not supported by logic or the necessary facts; a rule is capricious if it is adopted without thought or reason or is irrational." Similarly, case law provides that an "arbitrary" decision is one not supported by facts or logic, or despotic, and a "capricious" decision is one taken irrationally, or without thought or reason. Board of Clinical Laboratory Personnel v. Florida Association of Blood Banks, 721 So. 2d 317, 318 (Fla. 1st DCA 1998); Board of Trustees of the Internal Improvement Trust Fund v. Levy, 656 So. 2d 1359, 1362 (Fla. 1st DCA 1995). In

undertaking this analysis, the undersigned is mindful that these definitions:

> add color and flavor to our traditionally dry legal vocabulary, but do not assist an objective legal analysis. If an administrative decision is justifiable under any analysis that a reasonable person would use to reach a decision of similar importance, it would seem that the decision is neither arbitrary nor capricious.

Dravo Basic Materials Company, Inc. v. Department of Transportation, 602 So. 2d 632, 635 n.3 (Fla. 2d DCA 1992).

142. Petitioners argue that the evidence demonstrated that it is impossible for insurers to comply with the Proposed Rule, because of the uncontested evidence that insurers cannot show that credit scoring does not "disproportionately affect" persons based on age. Petitioners also cite the lack of reliable data upon which an insurer can rely in attempting compliance with the Proposed Rule. Even if insurers began collecting the required racial, ethnic, and religious data as to their customers, the evidence at hearing established the unreliability of self-reported demographic characteristics.

143. These considerable practical difficulties of compliance have been considered. However, as detailed above, the factor that renders the Proposed Rule arbitrary and capricious is definitional, not practical. "Disproportionate effect" is not defined in such as way as to give an insurer any

indication of what it must prove to satisfy the agency that its rates are not "unfairly discriminatory." "Race," "color," and "religion" are terms so broad that the agency itself has not decided precisely how to treat them, and has intentionally thrown upon insurers the responsibility to sort out their meaning by submitting rate filings in a definitional vacuum.

144. The Proposed Rule is arbitrary and capricious.

## ORDER

Based on the foregoing Findings of Fact and Conclusions of Law, it is

ORDERED:

As to Case Nos. 05-1012RP and 05-2803RP, Proposed Florida Administrative Code Rule 69O-125.005 is an invalid exercise of delegated legislative authority. Case No. 06-2036RU is dismissed as moot.

DONE AND ORDERED this 29th day of December, 2006, in Tallahassee, Leon County, Florida.

LAWRENCE P. STEVENSON
Administrative Law Judge
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Filed with the Clerk of the
Division of Administrative Hearings
this 29th day of December, 2006.

ENDNOTES

1/ Unless otherwise indicated, all references to the Florida Statutes shall be to the 2005 version.

2/ In this Final Order, the petitioning insurance companies will be referenced collectively as "Petitioners." The other petitioning party, Fair Isaac Corporation, will be referenced as "Fair Isaac."

3/ Fair Isaac has alleged that the Proposed Rule will require the regulated insurers to request the disclosure of Fair Isaac's trade secret information concerning its product line of credit-based insurance score models. However, OIR convincingly argues that Section 626.97411, Florida Statutes, provides adequate protection to prevent public disclosure of Fair Isaac's trade secrets. In this regard, the only "injury" caused to Fair Isaac by the Proposed Rule would be to force a business decision as to whether it would disclose its credit scoring methodologies to OIR, which would then be statutorily prohibited from releasing the methodologies to the public.

4/ As noted in the Preliminary Statement above, the rule was republished on July 1, 2005, in order to cure a procedural objection raised by Petitioners.

5/ Mr. Miller testified that if an actuary deviates from the Statement of Principles in establishing a rate, the actuarial opinion must disclose the deviation.

6/ Not all seven of the insurers were using credit scoring as a rating factor at the time of the study. Mr. Miller obtained credit scoring data on all of the policy records from ChoicePoint, a credit reporting agency.

7/ For personal injury protection and medical payments coverages, the study found that insurance scores were the single most important risk factor. For bodily injury and property damages coverages, insurance scores were the second most important risk factor, behind the age/gender of the driver. For comprehensive and collision coverages, insurance scores were the

third most important factor, behind model year of the car and the age/gender of the driver.

8/ Petitioners attempted to take their argument a step farther, contending that the use of credit scoring has increased the availability and affordability of automobile insurance as evidenced by the decrease in the automobile residual markets nationwide since credit scoring became a common component of risk classification plans. Mr. Miller endorsed the notion of some causal connection between credit scoring and the decreased residual market, but he conceded there were no hard data to support that view. Petitioners did not establish that the use of credit scoring has improved the affordability and availability of automobile insurance.

9/ The Actuarial Standards Board is an independent entity established (with staff from the American Academy of Actuaries) to promulgate standards of practice for the actuarial profession in the United States.

10/ OIR's general counsel, Steven Parton, emphasized that Section 626.9741, Florida Statutes, is not part of the Rating Law, and, therefore, that the definition of "unfairly discriminatory" is not necessarily limited to the definitions found in Part I of Chapter 627, Florida Statutes.

11/ Respondents concede that the terms "disproportionately affects" and "disparate impact" are essentially synonymous.

12/ In fairness, the context of Mr. Parton's answer made it ambiguous as to whether he understood that the question related to "color" rather than to "race." Mr. Parton's answer would not be particularly helpful as guidance for either category.

13/ The deposition Transcript actually reads, "but that presumption is not a rebuttable one." The Transcript clearly deviates from the sense of Mr. Parton's testimony, and the undersigned has thus concluded that the Transcript was incorrect.

14/ The "trial" to which Mr. Parton refers is a rate filing proceeding conducted pursuant to the Rating Law. At the final hearing, Mr. Parton observed that:

> The insurer always has the burden of demonstrating that its rates are not excessive, are not inadequate and are not

> unfairly discriminatory. We're now saying that there is an additional burden which is: You shall demonstrate that it is not unfairly discriminatory based upon a disproportionate impact, if you will, on the protected classes named in the statute.

15/ Petitioners' position on this issue is not without merit. The Legislature's use of the term "unfairly discriminatory" in Subsection 626.9741(8)(c), Florida Statutes, is problematic, given that the term has a common meaning in the insurance industry, is employed in its actuarial sense in the Rating Law, and is not otherwise defined in Section 626.9741, Florida Statutes. Petitioners were not unreasonable in contending that the term should be given its actuarial sense in the Proposed Rule.

16/ In Televisual Communications, the court held that "a publisher of medical educational videos had standing to challenge a proposed rule that would require an instructor to be present whenever audio-visual materials were used in educational programs required for health care professional certification because the rule had the collateral effect of regulating the publisher's industry by precluding the sale of its home study videos." Academy of Cosmetic Surgery, 808 So. 2d at 251.

17/ Subsection 626.9741(8)(d), Florida Statutes, appears to provide virtually the same authority as does Subsection 626.9741(4)(c)4., Florida Statutes, in terms of ensuring that the insurer's use of credit scoring is valid in predicting risk.

18/ Petitioners have attempted to distinguish Subsection 626.9741(8)(c), Florida Statutes, as an "implementing" portion of the statute. Even if this distinction were accepted, the main portion of Subsection 626.9741(8), Florida Statutes, provides that the FSC "may adopt rules to administer this section," a grant of authority that includes the power to adopt rules implementing Subsection (5). Thus, the distinction would make no difference to Respondents' point that Subsection 626.9741(8)(c), Florida Statutes, must mean something more than a mere reiteration of Subsection (5).

19/ As noted in the immediately preceding endnote, Petitioners argue that Subsection 626.9741(8)(c), Florida Statutes, is not an "operative" portion of the statute, but merely an "implementing" portion that confers rulemaking authority, and, therefore, does not authorize a "deviation" from the definition

of "unfairly discriminatory" as applied in the "operative" portion of the statute. Petitioners presented no case authority for the proposition that the Legislature is thus limited by the structure of its own statute.

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## NOTICE OF RIGHT TO JUDICIAL REVIEW

A party who is adversely affected by this Final Order is entitled to judicial review pursuant to Section 120.68, Florida Statutes. Review proceedings are governed by the Florida Rules of Appellate Procedure. Such proceedings are commenced by filing the original notice of appeal with the Clerk of the Division of Administrative Hearings and a copy, accompanied by filing fees prescribed by law, with the District Court of Appeal, First District, or with the District Court of Appeal in the Appellate District where the party resides. The notice of appeal must be filed within 30 days of rendition of the order to be reviewed.