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COMPTROLLER GENERAL OF THE UNITED STATES
WASHINGTON, D.C. 20548

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January 10, 1980

HSE 1500

The Honorable Jack Brooks
Chairman, Committee on Government
Operations
House of Representatives

Dear Mr. Chairman:

Reference is made to your letter of October 25, 1979, requesting our comments on H.R. 5646, a bill to transfer coverage of certain insurance records, to improve information practices in the insurance industry, and for other purposes.

Title I of the bill--Records Subject to Privacy Act--adds a new subsection to the Privacy Act of 1974 which excludes its applicability to insurance records maintained by Federal agencies or their contractors if the maintenance and disclosure of such insurance records are subject to the provisions of the Fair Insurance Information Practices Act. Title II of the bill is cited as the Fair Insurance Information Practices Act. The coverage extended by title II to insurance records is similar in most respects to that presently provided by the Privacy Act for systems of records maintained by Federal agencies.

Insurance companies Records management Disclosure laws Information disclosure Regulation

The underlying purpose of the Privacy Act, assuring a degree of personal privacy and fairness in determining matters affecting individuals served by the Federal Government, is adopted in the provisions of title II for the benefit of consumers in the insurance industry. In the bill, this is provided in provisions addressing expectations of confidentiality (sec. 203), notification of insurance information practices (sec. 204), information collection practices (sec. 205), individual access to personal information (sec. 206), and correction, amendment, or deletion of recorded personal information (sec. 207).

GAO STUDY OF STATE REGULATION
OF THE INSURANCE BUSINESS

In our report "Issues and Needed Improvements in State Regulation of the Insurance Business" (PAD-79-72, October 9, 1979), we confirmed some of the findings concerning the absence of adequate State regulations reported earlier by

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the Privacy Protection Study Commission. The Commission was established by the Privacy Act of 1974 and tasked, among other things, to conduct a study broadly assessing practices in both the public and private sectors. The Commission's report "Personal Privacy In An Information Society" made extensive recommendations for improvements in privacy and fair information handling by the insurance industry--areas of data collection and use which the States were not actively regulating. One large company, however, was identified in the report as voluntarily adopting a broad range of fair information practices advocated by the Commission and adopted in this bill.

Adverse underwriting decisions

Section 208 of the bill generally requires that when an individual is subject to an adverse underwriting decision insurers must inform the individual of the fact and of the individual's rights under the law. It requires that upon request the insurer provide the basis for the decision and names of organizations supplying information leading to the decision.

In our report on State regulation of the insurance business, we presented information on automobile insurance that is especially relevant to section 208. We found that most States already require that consumers be notified of the reason for cancellation of an automobile insurance policy. However, only 29 States require that companies provide the reasons for nonrenewal, and 14 of those 29 States require disclosure only at the request of the customer. Apparently, very few States require that consumers be provided the reasons for the rejection of an initial application for insurance. We did an on-site evaluation in a sample of 17 States. Only 3 of these 17 States require insurance companies to provide the reasons for rejection, and then only on written request of the consumer.

We found that rejection leads to adverse consequences such as limited coverage and higher rates in either the residual market, i.e., assigned risk plan, or with so-called substandard companies. We also found that there are apparent problems of consumer information regarding the availability of the assigned risk plan. Since substandard rates are far higher than assigned risk plan rates in some States, we are led to conclude that consumers are not being adequately informed by agents, companies, and insurance departments about their options in the assigned risk plan.

We believe that section 208 of the bill is consistent with our assessment that consumers should be informed of the reasons behind adverse underwriting decisions. We believe that the reason for the rejection should accompany the notice of rejection on new applications as well as renewals. This requirement may have the effect of requiring insurers to rationalize highly subjective underwriting practices that may be unfairly prejudicial to particular classes of persons. Since insurers presumably have specific reasons for denying insurance to an individual, they should not incur any substantial burden by being systematically required to state those reasons to the individual at the time the decision is communicated. Moreover, the prospective insurer may be in a position to correct erroneous information used for such adverse decisions to the benefit of both the consumer and the company.

Subsection 208(e), requiring that individuals must be informed when an agent submits their application to the residual market or a substandard insurer, is a remedy to the problems we discussed above with regard to consumer information about these matters. The subsection, however, may need to be clarified. Presumably, the phrase, "whenever the other provisions of this section do not apply," means that the subsection only applies when an individual is not first subject to an adverse underwriting decision. However, it is unlikely that individuals would be placed in the residual market plan unless their applications for insurance first were rejected. It is precisely the people who are first rejected who need the protection of subsection 208(e). Moreover, the protection most needed is not information on where the agent is applying but information about the availability of the residual market plan as an alternative to substandard insurers. We suggest, therefore, that section 208 be changed to apply to all situations where agents make application to the residual market or substandard companies and that it be broadened to also require agents to supply information about the residual market mechanism together with notice of the adverse underwriting decision.

The cost of complying with regulations does not now impose any significant burden on insurers according to our extensive discussions with leading insurance companies. We believe that compliance with the requirements in this legislation also would not incur costs which are significant in relation to the general administrative and claims costs of insurers.

ENFORCEMENT, PENALTIES AND THE IMMUNITY PROVISION

As the principal enforcement mechanism, the bill provides civil and criminal penalties for improperly disclosing or obtaining personal information and further provides civil penalties in liquidated damages for enforcing the fair information practices provisions of the bill. The bill also contains an immunity provision which limits the applicability of penalties; however, the scope of immunity is unclear.

Specifically, section 211 provides that damages for non-compliance may be assessed against insurance institutions by the courts. When actual damages are awarded under subsection 211(a) for improper disclosure of personal information by an insurance institution, agent, or insurance support organization, the court may also assess general damages of up to $10,000 under subsection 211(b).

Additionally, the bill provides criminal penalties of a fine up to $10,000 and imprisonment for not more than 1 year for (1) anyone improperly obtaining personal information from an insurance institution (sec. 214) or (2) the insurance institution's officers or employees providing personal information to a person not authorized to receive it (sec. 215).

Aside from these damages for improperly obtaining or disclosing personal information, an aggrieved individual may be awarded $1,000 in liquidated damages under subsection 211(c) when the fair information provisions of the bill are intentionally violated. These fair information provisions include areas of information collection practices, individual access to personal information, correction or amendment of information, and adverse underwriting decisions (sections 203-208).

Section 210 provides general immunity to insurance institutions and their employees for damages except as a result of a disclosure of or receipt of information required by the bill that is false and intentionally disclosed. Since the immunity provision applies "except as otherwise provided," it is not clear how the other provisions of the bill would be affected. The intended effect of the immunity provision on these penalty provisions should be clarified.

FEDERAL OVERSIGHT

No provisions are made in the bill for assessing the effectiveness of its procedures and reporting on its implementation, i.e., by a responsible Federal executive branch instrumentality, which would provide a basis for congressional review. We believe consideration should be given to establishing oversight responsibility in the executive branch.

The Subcommittee on Government Information and Individual Rights staff requested that we meet with them to discuss any comments we might have on the bill prior to the hearings on the bill which commenced on November 27, 1979. As requested, we met with the Subcommittee staff on November 14 and 19, 1979.

Sincerely yours,

Comptroller General
of the United States