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

AUGUST 27, 1984

B-213348



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The Honorable James J. Exon  
United States Senate

Dear Senator Exon:

Subject: Comments on the Economic Implications of the  
Exon Amendment to the Fair Insurance  
Practices Act (GAO/OCE-84-7)

On July 11, 1983, you requested that we comment on how your proposed amendment to S. 372, the proposed Fair Insurance Practices Act, would alter the cost implications of the bill, which we have described in our recent report, "Economic Implications of the Fair Insurance Practices Act" (GAO/OCE-84-1, April 6, 1984).

#### THE FAIR INSURANCE PRACTICES ACT

The Fair Insurance Practices Act, as originally introduced, would have prohibited distinctions based on race, color, religion, sex, or national origin in the marketing and pricing of insurance and pensions. So far as we know, the only one of these characteristics which is explicitly used as a risk factor in the pricing and marketing of insurance and pensions is sex. The bill would have required that sex-distinct premiums and benefits in existing and future insurance and pension contracts be equalized. The bill also would have required that no one's benefits be reduced as part of the equalization process.

#### PROVISIONS OF THE PROPOSED AMENDMENT

The proposed amendment would make several substantial changes in the bill. First, while it would continue to prohibit discrimination on the basis of race, color, religion, or national origin, distinctions based on sex would be defined as discriminatory only in connection with employee benefit plans. For individual insurance contracts, practices such as denial of coverage [Sec. 4(a)(1)], retaliatory discrimination [Sec. 4(b)(2)], and targeted marketing [Sec. 4(b)(3)], as well as distinctions in prices [Sec. 4(a)(2)], would not be prohibited if based on sex.

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Second, the proposed amendment would prohibit discriminatory payments of employer-financed benefits earned after the effective date of the act, but would permit unequal payments based on service performed before the effective date of the act.

Third, none of the bill's provisions would apply to existing individual insurance contracts. The prohibition against discrimination based on race, color, religion, or national origin would apply to individual insurance contracts issued or applied for after the legislation's effective date.

Fourth, the proposed amendment would make clear that it would be permissible to base the rates charged a group under group pension and insurance contracts on the sex composition of the group or on its loss experience, as long as contributions and benefits of each member of the group did not vary according to the participant's sex.

Finally, the proposed amendment would (1) eliminate the explicit authorization of punitive damages provided for in the original bill, (2) delegate more of the enforcement authority under the act to the states, and (3) delay the effective date of the act until 2 years after the date of enactment.

#### OBJECTIVES, SCOPE, AND METHODOLOGY

To respond to your request, we used the same approach as we did in our earlier report on the original bill. We analyzed four major categories of economic effects of the proposed amendment-- (1) unfunded liabilities (the increase in liabilities for pension funds and insurance companies resulting from the bill which would not be matched by any corresponding increase in assets); (2) redistributive effects (shifts of money from one group of people to another); (3) economic efficiency effects (changes in how cost-effectively the industry satisfies consumer demands); and (4) administrative costs (costs to insurance companies and pension plans of revising existing policies and pension plans and preparing new ones). We limited our analysis to the ways in which the economic effects of the substitute bill would differ from those of the original bill; a full analysis of the economic effects of the original bill is contained in our earlier report. Our review was performed in accordance with generally accepted auditing standards.

ECONOMIC EFFECTS OF THE PROPOSED AMENDMENTUnfunded liabilities

The proposed amendment would eliminate the provisions in the original bill which would have required benefit increases and/or premium reductions for pension plan participants and insurance policyholders. By eliminating the applicability of the bill to pension benefits earned in the past (i.e., past accruals), the proposed amendment would eliminate the estimated \$7.7 to \$15.1 billion in pension benefit increases that might have been required by the original bill, and thus would eliminate all of the unfunded liabilities for pension plans which we described in our earlier report. By eliminating the applicability of the bill to either existing or individual contracts, the proposed amendment would eliminate the benefit increases and/or premium reductions for individual policyholders that would have been required by the original bill. This would eliminate the estimated \$8.3 to \$17.1 billion in unfunded liabilities for life insurance companies which we described in our earlier report.

Redistributive and efficiency effects

The proposed amendment also eliminates almost all of the redistributive effects and efficiency effects of the original bill. In employee benefit plans, all employers with 15 or more employees are already prohibited from discriminating on the basis of sex under title VII of the Civil Rights Act (as interpreted by the Supreme Court in the recent Norris decision). The proposed amended bill would extend these requirements to the smaller plans not covered by title VII, but the redistributive effects and efficiency effects of this provision would probably be minor. Department of Labor data indicate that about 3 percent of participants in employee benefit plans are employed by firms not covered by the Civil Rights Act. In individual insurance contracts, the proposed amended bill would prohibit discrimination only on the basis of race, color, religion and national origin. Our prior review of existing studies of discrimination in pensions and insurance suggests that these factors are not used as the basis of overt discrimination. Thus, we believe that this provision would have few, if any, redistributive or efficiency effects.

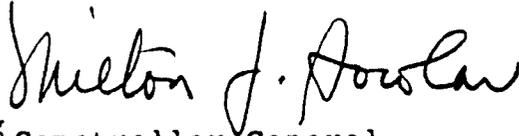
Administrative costs

Finally, the proposed amendment would also eliminate most of the original bill's administrative costs. In our earlier report, we reported the American Academy of Actuaries' estimate that the administrative costs of effecting the changes required by the original bill would be \$1.3 billion. Because the substitute bill would eliminate virtually all of the original bill's requirements for changes in current practices, it would also eliminate virtually all of the original bill's administrative costs. The substitute bill would still impose some administrative costs for small employers not previously covered by the Civil Rights Act. We cannot estimate the exact size of these administrative costs.

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As arranged with your office, further distribution of this report will be restricted for thirty days. At that time, we will make the report available to those who request it.

Sincerely yours,



Acting Comptroller General  
of the United States