

ALASKA LEGISLATURE COMMITTEE FILES, 2003-2004 8672

11216 SENATE (LABOR & COMMERCE (

Idaho

SB 1408

LAW!
Signed by Governor
March 25, 2002

Prohibits an insurer from charging a higher premium, cancel or nonrenew a policy based primarily on a person's credit rating or credit report.

Illinois

Consumer complaints received.

Indiana

SB 178

Similar to NCOIL Model

SB 294

Use of credit records by auto insurance companies. Provides that: (1) a motor vehicle insurance rating plan may not use, as a rating factor, adverse credit report information; and (2) a motor vehicle insurer may not consider adverse credit report information in certain underwriting activities.

HB 1187

Use of credit information by insurers. Prohibits the use of credit information in underwriting, issuance, renewal, or cancellation of property and casualty insurance. Makes a violation an unfair and deceptive act and practice in the business of insurance.

HB 1213

Credit scoring. Imposes several requirements on an insurer's use of credit information in the underwriting of personal property and casualty insurance.

HB 1323

In Committee

Similar to the NCOIL Model

HB 1406

in Committee

Allows for credit scoring with restrictions.

HB 1634

In Committee

Cannot be the sole reason.

Prohibits insurance credit scoring.

Kansas

Kentucky

HB 94

In Committee

HB 142

In Committee

Prohibits insurers from rating p/c insurance in whole or part of an individuals credit history.

SB 12

In Committee

Prohibits rating based in whole or in part on an individuals credit history. The Commissioner determines if there is a substantial correlation between and insurance credit score and the risk of loss.

Louisiana
Louisiana Dept. of
Insurance
Complaint Form

HB 53

In Committee

Declare the use of credit reports or credit scores for auto and homeowners insurance to be an unfair trade practice if they are used to deny or cancel a policy.

<u>Maryland</u>	LAW! Signed on May 17, 2002	Prohibits an insurer from refusing to underwrite a policy, or increase the premium on an existing policy due to the credit history of the applicant.
<u>Michigan</u>	<u>Michigan Department of Insurance Complaint Form</u>	Consumer complaints received.
<u>Minnesota</u>		Consumer complaints received.
<u>Missouri</u>	LAW! Signed July 13, 2002	Effective as of July 1, 2003, prohibits insurers from using credit-based information as the sole factor in underwriting decisions and would require insurers to disregard it as an underwriting factor if the individual has no credit history. They are also prohibited from basing decisions on credit information contained in a credit report that the insurer knows is in dispute. It also provides that they may not use credit information in renewing a contract until at least three years after the policy was issued.
<u>New York</u>	<u>New York Dept. of Insurance Complaint Form</u>	Consumer complaints received.
<u>Ohio</u>		Consumer complaints received.
<u>Oklahoma</u>		
<u>Oregon</u>	SB 260	Prohibits insurer from using credit history or insurance score of consumer applying for or renewing personal property or casualty insurance when making underwriting or rating decision.
	SB 280	Establishes requirements for use of credit history in personal insurance underwriting and rating. Requires Director of Department of Consumer and Business Services to report to Seventy-third Legislative Assembly on use of credit history for personal insurance.
	<u>Oregon Department of Insurance Complaint Form</u>	Consumer complaints received.
<u>Pennsylvania</u>	<u>PA Dept. of Insurance Online Complaint Form</u>	An insurance company would not be permitted to deny coverage or increase a customer's insurance premium by more than 20 percent as a result of credit grading. Insurance companies that violate the law would face penalties ranging from fines to license revocation.
	Insurance Credit Scoring Hotline: 1-800-468-0092	
<u>Rhode Island</u>		
<u>S. Carolina</u>		
<u>S. Dakota</u>		

Tennessee

Texas

Texas Department of Insurance Complaint Form [Click Here](#) for more information.

HB 600
SB 400

Prohibits the practice of insurance credit scoring.
Rolls back rates to 2001 levels.
Requires insurers to receive prior approval for rate increases.

SB 91

Prohibits the practice of insurance credit scoring.

HB 115
HB 45
HB 81
SB 99

Allows for insurance credit scoring in setting a premium payment plan.

HB 265
SB 130

Permits insurance scoring with some limitations.
Calls for an appeals process.

Utah

HB 110

LAW!
Signed by Governor! March 26, 2002

Allows insurers to use credit-based insurance scores only to provide discounts to auto insurance policyholders.

Vermont

Virginia

Washington

HB 2544

LAW!
Signed by Governor! April 4, 2002

Prohibits insurers from canceling or nonrenewing policyholders in whole or in part on credit history or insurance score, and allows insurers to deny personal insurance only in combination with other "substantive" underwriting factors. Lists a number of credit characteristics that can not be considered or are limited in their use in underwriting and rating. The characteristics include: the absence of credit history; number of credit inquiries; collection accounts identified with a medical industry code; the initial finance or purchase of a vehicle or a house; use of a particular type of credit, charge or debit card; and total available line of credit.

Wisconsin

**Fax Cover Sheet**Alaska State Office | 3601 "C" Street, Suite 1420 | Anchorage, AK 99503
907-341-2277 | 907-341-2270 (FAX) | www.aarp.org**To:** SENATOR CON BUNDE**From:** Pat Luby**Company:****Date:****Fax number:** 1-907-465-3871**Total number of pages including cover:****Notes/Comments:**

AARP is a nonprofit, nonpartisan membership organization for people 50 and over. We provide information and resources; advocate on legislative, consumer, and legal issues; assist members to serve their communities; and offer a wide range of unique benefits, special products, and services for our members. These benefits include AARP Webplace at www.aarp.org, Modern Maturity and My Generation magazines, and the monthly AARP Bulletin. Active in every U.S. state and territory, AARP celebrates the attitude that age isn't just a number — it's about how you live your life.



Honorable Con Bunde, Chair
Senate Labor and Commerce Committee
Alaska Capitol, Room 506
Juneau, AK 99801-1182

April 21, 2003

RE: SB 13 (Elton and Cowdery) - Support

Dear Chair Bunde:

On behalf of the AARP members in Alaska, we encourage you and your colleagues on the Senate Labor and Commerce Committee to support SB 13, authored by Senators Klm Elton and John Cowdery and co-sponsored by your Committee colleague Hollis French and by Senators Ellis, Dyson, Guess and Lincoln.

AARP believes that insurance rates should be based on risk-classification systems that fairly and accurately reflect the risks associated with individual characteristics. Arguably, this is not the case with credit scoring.

We believe that the Alaska Division of Insurance should have extensive review powers that would include the opportunity to exercise oversight over companies that claim credit scores are appropriate. Proof of this assertion should be provided to the Division of Insurance for review prior to rate approvals.

We know that there are problems with the accuracy of credit scores. According to a December, 2002 national study by the Consumer Federation of America, almost one in ten consumers runs the risk of being excluded from the credit marketplace altogether because of incomplete records, duplicate reports, and mixed files. Setting aside the inherent accuracy problems of credit reports, it is still worthwhile to examine what relevance credit has to do with insurance risk.

It challenges the imagination to conclude that good or bad credit, using credit or not using credit, has anything to do with whether one is a safe driver or if one's home is more at risk for an insurance claim than another's. Why not charge more for left handed drivers? We are sure the insurance industry could come up with some conclusion that there is logic there that is similar to drawing a relationship between credit and insurance claims.

A January, 2003 study of the Washington State University for the Washington Insurance Commissioner indicated that, despite more research needing to be done, initial findings

leaned toward unequal impacts on people of color and that low income people are more likely than higher income people to have their rates raised as a result of credit scores. More significantly, the study indicated that results varied greatly from firm to firm. The study was not able to include two significant issues—how many insurers refused coverage based on credit scores and how did insurers deal with the inaccuracy of credit scores.


There are undoubtedly some very valid predictors that can be used to accurately predict insurance risk. We do not believe credit scoring, based on the information provided by the industry, is one that should be included.

AARP urges an "AYE" vote on SB 13.

Should you have any questions about our position, please feel free to contact Marie Darlin (907.586.3637), Coordinator of the AARP Capital City Task Force; Patrick Luby (907.762.3314), AARP Legislative Representative; or me (907.245.5259).

Thank you for your consideration.

Sincerely,



Marguerite Stetson
AARP Alaska
Executive Council Member for Advocacy
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cc: Vice-Chair Ralph Seekins
Senator Gary Stevens
Senator Bettye Davis
Senator Hollis French
Senator John Cowdery
Senator Kim Elton
Senator Johnny Ellis
Senator Fred Dyson
Senator Gretchen Guess
Senator Georgianna Lincoln

Marie Darlin
Patrick Luby

**Testimony of Birny Birnbaum
Before the Alaska Senate Labor and Commerce Committee**

Insurance Credit Scoring and SB 13

April 22, 2003

Thank you for the opportunity to offer testimony in support of a prohibition against insurers' use credit scoring for underwriting, rating and conditioning payment plan eligibility for personal lines insurance. In addition to this testimony, I have previously submitted:

- A report I recently submitted to the Ohio Civil Rights Commission, which concludes that insurers' use of credit scoring very likely has a disproportionate impact on poor and minority communities;
- Tables from the *2000 Statistical Abstract of the United States*, which show a vivid correlation between income and the credit characteristics most heavily weighted in insurance credit scoring models.
- Comments on the problems with the National Conference of Insurance Legislators model law on credit scoring;
- Preliminary comments on a recent study by the Bureau of Business Research at the University of Texas.
- Comments submitted to the House State Affairs Committee on 3/29/03
- Comments submitted to the Senate Labor and Commerce Committee on 4/8/03

I have previously laid out my arguments why it is reasonable and necessary to prohibit insurers' use of consumer credit information for personal lines insurance underwriting, rating and payment plan eligibility – the practice is inherently unfair, discriminates against certain classes of consumers, undermines the insurance mechanism, undermines regulatory oversight of rates and violates actuarial principles for risk classification.

I wanted to use my time today to respond to some of the industry arguments on credit scoring and the comments of Mr. Niehaus of Progressive, in particular. On April 8, Mr. Niehaus offered a number of assertions regarding credit scoring.

First, he said that a ban on credit scoring would force Progressive to raise rates for two-thirds of their policyholders. This is, of course, not true. A ban on credit scoring will simply prevent insurers from using this unfair classification tool. Insurers choose the rates they charge, subject to review by the insurance commissioner.

Bad Scores = Bad credit ?

Also, since when did we determine whether a practice was fair based on how many people benefited from the practice? In America, the minority is supposed to be protected against unfair practices by the majority.

However, you should know that several years ago in Arizona, after the Arizona Senate had passed a bill to prohibit credit scoring, Progressive and an industry trade association sent letters to their policyholders threatening rate increases if the credit scoring ban was enacted. And after credit scoring was banned for homeowners insurance and severely restricted for auto insurance in Maryland, insurers sent notices with renewal policies implying that the state legislature had forced the insurers to increase rates.

The bottom line is that the legislation to prohibit insurers from using credit scoring should also contain a provision to include a notice to consumers upon policy issuance or renewal along the lines of:

Your legislature has banned the use of your personal credit information by insurers to determine if you are eligible for coverage and how much you will pay. No insurer is required to raise rates or charge you more as a result of this law.

Second, Mr. Niehaus argues that good drivers will subsidize bad drivers if the use of credit is prohibited. The Texas study showed that for the consumers with the worst credit scores, there were 12 claims out of a hundred policies and for the best credit scores there were 9 claims out of a hundred policies. So the shift of about one claim per hundred evens out the frequency of claims among all groups. The bottom line is that most consumers don't file claims in a given year and the movement of one claim from one group of consumers to another can change that group from being "good" drivers to "bad" drivers.

Third, Mr. Niehaus argued that a ban on credit scoring would create an unlevel playing field where direct writers would have an advantage. This is not correct. The FCRA allows all insurers to use credit to get mailing lists of consumers. But once a solicitation is sent, the insurer is subject to the insurance laws of the state. All sorts of insurers use credit for direct mail insurance solicitation – Allstate, State Farm, Progressive, GEICO and many others – with and without agents. This argument has no merit.

Fourth, Mr. Niehaus failed to identify Maryland as a state that banned the use of credit scoring in recent years – for homeowners. And Maryland severely restricted the use of credit. Although insurance industry lobbyists have been successful at fighting good credit scoring legislation in many states, there are a number of states today where either the state senate or the state house has passed a law banning the use of credit.

Fifth, Mr. Niehaus argued that a ban on credit would damage an Alaskan market that is already in bad shape. He said that Alaska was 47th out of 51 states and the DC in profitability and that insurers had lost money in three of the last four years. Since these are the years that insurers have used credit scoring, it appears that credit scoring is the factor damaging the market! Again, the bottom line is that a ban on credit scoring will not "damage the market." It will simply make the underwriting and rating of insurance policies fairer because that underwriting and rating will be based on factors that consumers understand and that provide consumers with an economic incentive to prevent losses.

Sixth, Mr. Niehaus suggested that the legislature look at the NCOIL model as an alternative. The NCOIL model was developed as a compromise between some agents groups and the insurance industry. In exchange for supporting credit scoring, the agents got a liability shield for carrying out credit scoring practices on behalf of insurers. The NCOIL model provides very few consumer protections. Rather, it simply endorses the practices of most insurers.

Attached please find a description of the Progressive scoring model, which was presented at a hearing last year in Michigan. It should be noted that Progressive's credit scoring practices are among the most consumer friendly in the industry – the least bad among many bad practices. So when you are looking at Progressive, remember that other insurers' practices are much worse.

But even looking at the relatively simple Progressive model, here are the nine factors:

1. Months you have managed credit
2. Age at which you first established credit
3. Number of times a payment was past due more than 30 days
4. Number of loans and accounts with a satisfactory current payment record
5. Number of credit card accounts currently past due more than 30 days
6. Percent of available credit limit currently being used on revolving accounts
7. Percent of available credit limit currently being used on all open accounts
8. Months since your most recent auto loan was made
9. Credit inquiries you initiated in the past 25 months

Note how little these factors have to do with how well a consumer manages his or her credit. Items 1 and 2 are directly related to a consumer's age, not how they manage credit. Item 3 makes no distinction between a consumer who had a difficult time years ago – perhaps because of unemployment or a medical catastrophe – and one having trouble today. Item 5 is strongly correlated to income, as shown in the Statistical Abstract charts I provided earlier. How does the timing of your auto loan relate to how you manage credit?

And this is among the most consumer friendly of any insurer's scoring models! It should be clear that even if there is a statistical relationship between any of these factors and expected loss, the factors are pulling in people who manage credit well in addition to people who do not manage credit very well.

Finally, today, I would like to discuss the Texas study. The industry has argued that the Texas study cements their assertion that credit is correlated to risk of loss. That is not the case. There has never been much dispute that insurers can produce numbers showing that credit scores are correlated to expected losses. The question has always been, is this correlation due to credit itself or is it due to some other factor that credit is correlated to? In 1996, the NAIC credit scoring working group dismissed the simple loss ratio analysis – credit scores versus loss ratio – as insufficient to demonstrate a true correlation between credit and risk of loss. Rather, the NAIC group called for a multi-variate analysis – an analysis that takes into account all the other underwriting and rating factors used by insurers -- to determine what credit's unique contribution to risk of loss might be. The NAIC wanted to know if credit was correlated with some other factor – something already used by insurers but mispriced or something prohibited.

The Texas study regarding correlation relies upon the same loss ratio methodology rejected by the NAIC in 1996. As such, the study offers nothing new on the correlation controversy.

However, the study also showed that the average and median credit scores for the standard market were substantially higher than the scores for the non standard market insurers. Since the scores were taken from policies issues in the beginning of 1998 – specifically chosen because the insurers were not using credit at the time – we would expect a random distribution of credit scores between the two groups. In other words, because the scores were taken before insurers were using credit, we expect the average credit scores in the two markets to be the same. But they weren't – not by a long shot. This means that insurers were already using some underwriting factor or factors to distinguish risk of consumers that is correlated to credit. *The Texas study showed that credit is duplicating some other factor or factors that insurers are already using!*

Since the best evidence to date shows that credit is a surrogate for other factors, we have further information to support a ban on insurers' use of credit scoring.

Personal insurance credit inquiry for John Doe

With your permission, Progressive reviews selected information from your credit history when you request a quote for insurance. Your rate is based on many factors: the car you drive, where you live, the amount and type of coverage you select, your driving and claims history, and your payment and credit history.

	<u>You</u>	<u>Average</u>
Experience you have with managing credit		
Months you have managed credit	48 Months	96 Months
Age at which you first established credit	16	21
Number of times a payment was past due more than 30 days	4	1
Current payment status of installment loans and revolving accounts		
Number of loans and accounts with a satisfactory current payment record	2	5
Number of credit card accounts currently past due more than 30 days	0	0
Use of available credit		
Percent of available credit limit currently being used on revolving accounts	88%	35%
Percent of available credit limit currently being used on all open accounts	70%	56%
Months since your most recent auto loan was made	12 Months	4 Months
Credit inquiries you initiated in the past 25 months	5	4
Insurance Credit Score	116	100

Your payment and credit history information was obtained from Experian. More detailed information can only be obtained by you by calling Experian at 1-888-397-3742. You may order a copy of your credit report free of charge.

Definitions

Installment loans have fixed terms with regular payments, such as a car loan, home loan, student loan, or personal loan. Revolving accounts have varying payments depending on the balance of the account. This includes all major credit cards and cards from department stores.

Personal insurance credit inquiry for John Doe

How your insurance credit score is determined

A lower score is better, as it indicates that you have carefully and consistently managed credit over many years. Consumers who use credit responsibly are statistically less likely to be involved in auto accidents and may be eligible for lower rates. To determine your insurance credit score, we subtract points for items that are better than average and add points for items that are worse than average.

Every consumer starts with the same number of points **100**

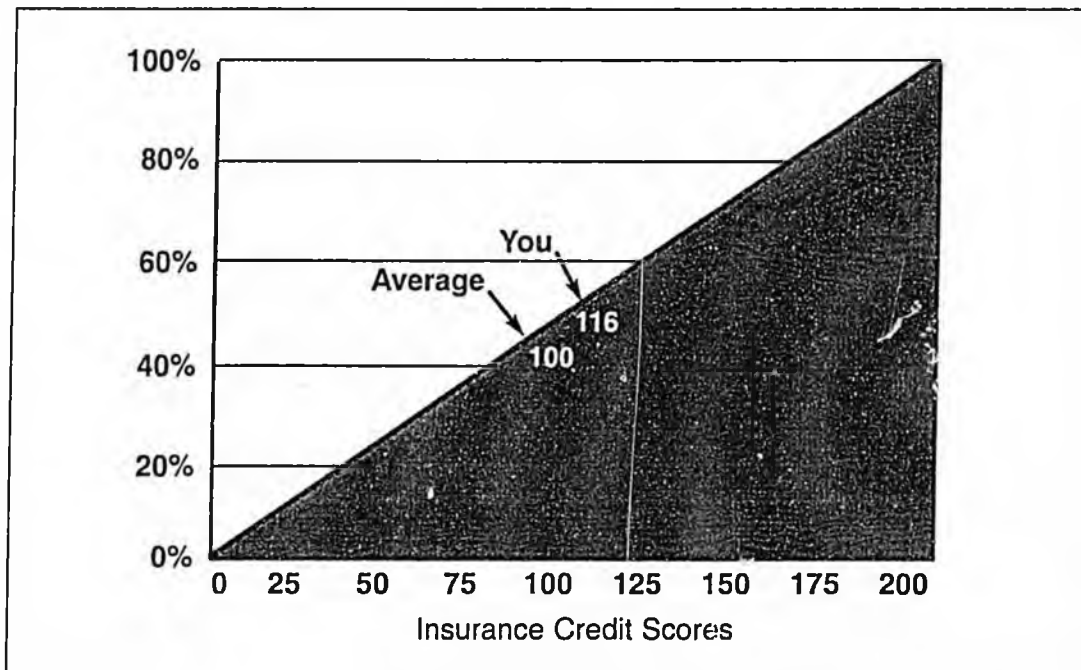
Items better than average:

First established credit at age 16	-10	
12 months since last auto loan was made	<u>-7</u>	
Total of all better than average items		-17

Items worse than average:

Managed credit for 48 months	18	
2 loans and accounts that are current	8	
88% of available credit in use	4	
5 credit inquiries in the past 25 months	<u>3</u>	
Total of all worse than average items		<u>33</u>

Your insurance credit score = **116**



Consumers who received a quote from Progressive in the past 6 months had an average insurance credit score of 100.

Your insurance credit score is 116 and is lower than 44% of consumers who received a quote from Progressive in the past 6 months, but is higher than the average.

April 22, 2003

RE: Insurance Scoring

Dear Members,

Please accept my apology for not appearing in person as I am on jury duty this month and have been ordered to appear for yet another trial.

I am in favor of this Senate Bill outlawing the use of one's credit score as a means of adjusting risk. The reasons follow:

Many of these same people are low income and have had trouble paying their bills on time and as a result have been credit scored low. While some would say paying your bills on time shows financial responsibility, and I agree, it can also be said we all have had times when the money is short and circumstances were out of our control.

Let us then agree that these very same people are just the ones we want insured. Should they be involved in an accident, they are the ones to less likely to have the financial wherewithal to pay their share of the damages.

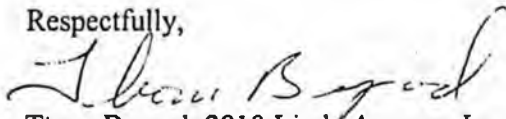
If the insurance companies statistical models suggesting the people with lower credit scores are in a higher risk group, we definitely want this group insured at the very least to help to protect, financially, the rest of the population from the damage they may cause. Placing another financial impediment upon this group will just increase the already too large numbers of uninsured motorist currently plying the streets of Alaska.

It is not reasonable to look at a persons credit score and use that information to adjust the premium because some don't use credit. Some are too young to have established credit; some have had medical or financial bankruptcies; some have fallen prey to easy credit and failed to realize, until it was too late, the mess they have gotten themselves into.

Insurance should be based on the established personal driving record of the individual alone.

I've been told several insurance companies will pull out of Alaska if this becomes law. The reason is they will lose money. Well, that's business. If they can not compete and their product is not conducive to this market they should get out. But I know there are insurance companies out there willing to write policies in our great state and they will make money. After all, is it not the law we all must have auto insurance. I remember when that became law... the insurance companies made millions over that.

Respectfully,



Thom Buzard, 2910 Linda Avenue, Juneau, Alaska 99801 (321-5457) (789-2550)

**Testimony of Birny Birnbaum
Before the Alaska Senate Labor and Commerce Committee**

Insurance Credit Scoring and SB 13

April 8, 2003

Thank you for the opportunity to offer testimony in support of a prohibition against insurers' use credit scoring for underwriting, rating and conditioning payment plan eligibility for personal lines insurance. In addition to this testimony, I am submitting for your information the following documents:

- A report I recently submitted to the Ohio Civil Rights Commission, which concludes that insurers' use of credit scoring very likely has a disproportionate impact on poor and minority communities;
- Tables from the *2000 Statistical Abstract of the United States*, which show a vivid correlation between income and the credit characteristics most heavily weighted in insurance credit scoring models.
- Comments on the problems with the National Conference of Insurance Legislators model law on credit scoring;
- Preliminary comments on a recent study by the Bureau of Business Research at the University of Texas.
- My testimony from last week on HB 5 and HB 47

It is reasonable and necessary to prohibit insurers' use of consumer credit information for personal lines insurance underwriting, rating and payment plan eligibility. Insurance credit scoring is inherently unfair, discriminates against certain classes of consumers, undermines the insurance mechanism, undermines regulatory oversight of rates and violates actuarial principles for risk classification.

What other rating or underwriting factor penalizes consumers:

- For legal, rational and beneficial behavior?
- Who are the victims of an economic or medical catastrophe?
- For being the victim of identify theft?
- For paying in cash?

There are obvious problems with credit scoring, but what are the benefits? The insurers' claims collapse upon examination.

- What is Fair? Insurers versus Everyone Else
- The Big Lie – "Credit Scoring Rewards Financially Responsible Consumers"
- Who Cares If It's Fair? "Most Consumers Benefit"
- No Free Lunch – "We Only Offer Discounts"
- Black is White – "Credit Scoring Promotes Competition"
- Insurers Want to Choose Who Gets A Subsidy

No. 791. Flow of Funds Accounts—Assets of Households: 1980 to 1999

[As of December 31 (6,563 represents \$6,563,000,000,000). Includes nonprofit organizations]

Type of instrument	Total (bil. dol.)							Percent distribution		
	1980	1985	1990	1995	1997	1998	1999	1980	1990	1999
Total financial assets	6,563	10,100	14,963	21,834	27,628	30,583	34,948	100.0	100.0	100.0
Deposits	1,517	2,484	3,265	3,366	3,807	4,165	4,338	23.1	21.8	12.4
Foreign deposits	-	8	13	23	42	42	45	-	0.1	0.1
Checkable deposits and currency	251	342	409	505	445	461	442	3.8	2.7	1.3
Time and savings deposits	1,203	1,941	2,477	2,388	2,725	2,924	3,013	18.3	16.6	8.6
Money market fund shares	62	193	365	449	595	738	838	0.9	2.4	2.4
Credit market instruments	425	849	1,503	1,885	1,873	1,781	1,960	6.5	10.0	5.6
Open-market paper	38	35	63	48	59	63	69	0.6	0.4	0.2
U.S. Government securities	166	270	620	922	721	552	639	2.5	3.5	1.9
Treasury issues	160	251	462	700	511	391	347	2.4	3.1	1.0
Savings bonds	73	80	126	185	187	187	186	1.1	0.8	0.5
Other Treasury	88	171	335	515	325	204	160	1.3	2.2	0.5
Agency issues	5	19	67	122	209	162	312	0.1	0.4	0.9
Municipal securities	104	346	574	458	464	475	528	1.6	3.8	1.5
Corporate and foreign bonds	30	77	192	448	521	581	596	0.5	1.3	1.7
Mortgages	87	120	144	109	109	109	110	1.3	1.0	0.3
Corporate equities	875	1,058	1,807	4,122	5,690	6,339	8,009	13.3	12.1	22.9
Mutual fund shares	46	198	468	1,265	2,057	2,501	3,104	0.7	3.1	8.9
Security credit	16	35	62	128	215	277	319	0.2	0.4	0.9
Life insurance reserves	221	264	392	566	665	718	772	3.4	2.6	2.2
Pension fund reserves	971	2,087	3,462	5,768	7,894	9,079	10,360	14.8	23.1	29.6
Investment in bank personal trusts	265	384	552	803	943	1,001	1,117	4.0	3.7	3.2
Equity in noncorporate business	2,154	2,607	3,230	3,640	4,172	4,395	4,630	32.8	21.6	13.2
Miscellaneous assets	74	133	224	292	312	327	339	1.1	1.5	1.0

- Represents zero. ¹ Only those directly held and those in closed-end funds. Other equities are included in mutual funds, life insurance and pension reserves, and bank personal trusts. ² See also Table 846.

Source: Board of Governors of the Federal Reserve System, "Federal Reserve Statistical Release, Z.1, Flow of Funds Accounts of the United States", published: 10 March 2000; <<http://www.bog.frb.fed.us/releases/Z1/20000310/data.htm>>.

No. 792. Financial Assets Held by Families by Type of Asset: 1992 to 1998

[Median value in thousands of constant 1998 dollars (13.1 represents \$13,100). Constant dollar figures are based on consumer price index data published by U.S. Bureau of Labor Statistics. Families include one-person units; for definition of family, see text, Section 1, Population. Based on Survey of Consumer Finance; see Appendix III. For definition of median, see Guide to Tabular Presentation]

Age of family head and family income	Any financial asset ¹	Transaction accounts ²	Certificates of deposit	Savings bonds	Stocks ³	Mutual funds ⁴	Retirement accounts ⁵	Life insurance ⁶	Other managed ⁷
PERCENT OF FAMILIES OWNING ASSET									
1992, total	90.2	86.9	16.7	22.3	17.0	10.4	39.6	34.9	4.0
1995, total	91.0	87.0	14.3	22.8	15.2	12.3	45.2	32.0	3.9
1998, total	92.9	90.5	15.3	19.3	19.2	16.5	48.8	29.6	5.9
Under 35 years old	88.6	84.8	6.2	17.2	13.1	12.2	39.8	18.0	1.9
35 to 44 years old	93.3	90.5	9.4	24.9	18.9	16.0	59.5	29.0	3.9
45 to 54 years old	94.9	93.5	11.8	21.8	22.6	23.0	59.2	32.9	6.5
55 to 64 years old	95.6	93.9	18.6	18.1	25.0	15.2	58.3	35.8	6.5
65 to 74 years old	95.6	94.1	29.9	16.1	21.0	18.0	46.1	30.1	11.8
75 years old and over	92.1	89.7	35.9	12.0	18.0	15.1	16.7	32.5	11.6
Less than \$10,000	70.6	61.9	7.7	3.5	3.8	1.9	6.4	15.7	(B)
\$10,000 to \$24,999	89.9	86.5	16.8	10.2	7.2	7.6	25.4	20.9	4.9
\$25,000 to \$49,999	97.3	95.8	15.9	20.4	17.7	14.0	54.2	28.1	3.9
\$50,000 to \$99,999	99.8	99.3	16.4	30.6	27.7	25.8	73.5	39.8	8.0
\$100,000 and more	100.0	100.0	16.8	32.3	56.6	44.8	88.6	50.1	15.8
MEDIAN VALUE⁸									
1992, total	13.1	2.6	12.6	0.7	9.1	18.3	16.0	3.5	22.8
1995, total	16.5	2.3	10.6	1.1	9.6	21.2	18.1	5.3	31.9
1998, total	22.4	3.1	15.0	1.0	17.5	25.0	24.0	7.3	31.5
Under 35 years old	4.5	1.5	2.5	0.5	5.0	7.0	7.0	2.7	19.4
35 to 44 years old	22.9	2.8	8.0	0.7	12.0	14.0	21.0	8.5	25.0
45 to 54 years old	37.8	4.5	11.5	1.0	24.0	30.0	34.0	10.0	39.3
55 to 64 years old	45.6	4.1	17.0	1.5	21.0	58.0	46.8	9.5	65.0
65 to 74 years old	45.4	5.6	20.0	2.0	50.0	60.0	38.0	8.5	41.3
75 years old and over	38.6	6.1	30.0	5.0	50.0	59.0	30.0	5.0	30.0
Less than \$10,000	1.1	0.5	7.0	1.8	14.0	6.0	7.5	3.0	(B)
\$10,000 to \$24,999	4.8	1.3	20.0	1.0	10.0	26.0	8.0	5.0	30.0
\$25,000 to \$49,999	17.6	2.5	14.5	0.6	8.0	11.0	13.0	5.0	15.0
\$50,000 to \$99,999	57.2	0.0	13.3	1.0	13.0	25.0	31.0	9.5	32.0
\$100,000 and more	244.3	19.0	22.0	1.5	55.0	65.0	93.0	18.0	100.0

¹ Basic figure too small. ² Includes other types of financial assets, not shown separately. ³ Checking, savings, and money market deposit accounts, money market mutual funds, and call accounts at brokerages. ⁴ Covers only those stocks that are directly held by families outside mutual funds, retirement accounts and other managed assets. ⁵ Excludes money market mutual funds and funds held through retirement accounts or other managed assets. ⁶ Covers IRAs, Keogh accounts, and certain employer-sponsored accounts. ⁷ Cash value. ⁸ Includes personal annuities and trusts with an equity interest and managed investment accounts. ⁹ Median value of financial asset for families holding such assets.

Source: Board of Governors of the Federal Reserve System, *Federal Reserve Bulletin*, January 2000, and unpublished revisions.

No. 793. Flow of Funds Accounts—Liabilities of Households: 1980 to 1999

[As of December 31 (1,426 represents \$1,426,000,000,000). Includes nonprofit organizations]

Type of instrument	Total (bil. dol.)							Percent distribution		
	1980	1985	1990	1995	1997	1998	1999	1980	1990	1999
Total liabilities	1,426	2,326	3,679	4,982	5,708	6,206	6,841	100.0	100.0	100.0
Credit market instruments	1,374	2,238	3,554	4,783	5,438	5,910	6,467	95.4	96.6	94.5
Home mortgages	905	1,408	2,461	3,252	3,698	4,058	4,480	63.5	66.0	65.5
Consumer credit	355	604	805	1,123	1,264	1,332	1,429	24.9	21.9	20.9
Municipal securities	17	81	87	98	115	127	137	1.2	2.4	2.0
Bank loans, n.e.c. ¹	28	31	18	57	67	73	65	2.0	0.5	1.0
Other loans	55	79	101	160	191	204	219	3.8	2.7	3.2
Commercial mortgages	15	33	83	92	104	117	137	1.0	2.2	2.0
Security credit	25	51	39	79	131	153	222	1.7	1.1	3.3
Trade payables	14	24	69	103	120	126	133	1.0	1.9	1.9
Unpaid life insurance premiums ²	13	15	16	18	19	17	19	0.9	0.4	0.3

¹ Not elsewhere classified. ² Includes deferred premiums.

Source: Board of Governors of the Federal Reserve System, "Federal Reserve Statistical Release, Z.1. Flow of Funds Accounts of the United States"; published: 10 March 2000; <http://www.bog.frb.fed.us/releases/Z1/20000310/data.htm>

No. 794. Financial Debt Held by Families by Type of Debt: 1992 to 1998

[Median debt in thousands of constant 1998 dollars (19.9 represents \$19,900). See headnote, Table 792]

Age of family head and family income	Any debt	Home-secured debt	Installment	Other lines of credit	Credit card balances ²	Other residential property	Other debt ³
PERCENT OF FAMILIES HOLDING DEBTS							
1992, total	73.2	39.1	46.0	2.3	43.7	5.7	8.4
1995, total	74.5	41.0	45.9	1.9	47.3	4.7	8.5
1998, total	74.1	43.1	43.7	2.3	44.1	5.1	8.8
Under 35 years old	81.2	33.2	60.0	2.4	50.7	2.0	9.6
35 to 44 years old	87.6	58.7	53.3	3.6	51.3	6.7	11.4
45 to 54 years old	87.0	58.8	51.2	3.6	52.5	6.7	11.1
55 to 64 years old	76.4	49.4	37.9	1.6	45.7	7.8	8.3
65 to 74 years old	51.4	26.0	20.2	(B)	29.2	5.1	4.1
75 years old and over	24.6	11.5	4.2	(B)	11.2	1.8	2.0
Less than \$10,000	41.7	8.3	25.7	(B)	20.6	(B)	3.6
\$10,000 to \$24,999	63.7	21.3	34.4	1.2	37.9	1.8	7.0
\$25,000 to \$49,999	79.6	43.7	50.0	2.9	49.9	4.1	7.7
\$50,000 to \$99,999	89.4	71.0	55.0	3.3	56.7	7.7	12.2
\$100,000 and more	87.8	73.4	43.2	2.6	40.4	16.4	14.8
MEDIAN DEBT⁴							
1992, total	19.9	50.2	5.3	2.3	1.1	28.5	2.9
1995, total	23.4	54.9	6.4	3.7	1.6	31.9	2.1
1998, total	33.3	62.0	8.7	2.5	1.7	40.0	3.0
Under 35 years old	19.2	71.0	9.1	1.1	1.6	66.0	1.7
35 to 44 years old	55.7	70.0	7.7	1.4	2.0	40.0	3.0
45 to 54 years old	48.4	68.8	10.0	3.0	1.8	40.0	5.0
55 to 64 years old	34.6	49.4	8.3	4.9	2.0	41.0	5.0
65 to 74 years old	11.9	29.0	6.5	(B)	1.1	56.0	4.5
75 years old and over	8.0	21.2	8.9	(B)	0.7	29.8	1.7
Less than \$10,000	4.1	16.0	4.0	(B)	1.1	(B)	0.6
\$10,000 to \$24,999	8.0	34.2	6.0	1.1	1.0	34.0	1.3
\$25,000 to \$49,999	27.1	47.0	8.0	3.0	1.9	20.0	2.2
\$50,000 to \$99,999	75.0	75.0	11.3	2.8	2.4	42.0	3.8
\$100,000 and more	135.4	123.8	15.4	5.0	3.2	60.0	10.0

(B) Base figure too small. ¹ First and second mortgages and home equity loans and lines of credit secured by the primary residence. ² Families that had an outstanding balance on any of their credit cards after paying their most recent bills. ³ Includes loans on insurance policies, loans against pension accounts, borrowing on margin accounts and unclassified loans. ⁴ Median amount of financial debt for families holding such debts.

No. 795. Percent Distribution of Amount of Debt Held by Families: 1995 and 1998

[See headnote, Table 796]

Type of debt	1995		1998		Purpose of debt	1995		1998		Type of lending institution	1995		1998	
	1995	1998	1995	1998		1995	1998	1995	1998		1995	1998		
Total	100.0	100.0	Total	100.0	100.0	Total	100.0	100.0	Total	100.0	100.0	100.0	100.0	
Home-secured debt	73.3	71.9	Home purchase	70.4	68.1	Commercial bank	35.1	32.6	Savings and loan	10.8	9.6	11.8	12.8	
Installment loans	11.8	12.8	Home improvement	2.0	2.0	Credit union	4.5	4.2	Finance or loan company	3.2	4.2	1.9	3.7	
Credit card balances	3.9	3.8	Investment, excluding real estate	1.0	3.2	Brokerage	1.9	3.7	Real estate lender	32.7	35.9	5.0	3.4	
Other lines of credit	0.6	0.3	Vehicles	7.5	7.5	Individual lender	5.0	3.4	Other nonfinancial	0.8	1.3	1.3	0.6	
Other residential property	7.5	7.4	Goods and services	5.7	6.0	Government	1.3	0.6	Credit and store cards	3.9	3.8	0.9	0.7	
Other debt	2.8	3.7	Investment real estate	8.2	7.8	Other loans	0.9	0.7						
			Education	2.7	3.4									
			Other loans	2.4	1.9									

Source of Tables 794 and 795: Board of Governors of the Federal Reserve System, "Federal Reserve Bulletin, January 2000, and unpublished data.

No. 796. Ratios of Debt Payments to Family Income: 1992 to 1998

[In percent. Constant dollar figures are based on consumer price index data published by U.S. Bureau of Labor Statistics. Families include one-person units; for definition of family, see text. Section 1, Population. Based on Survey of Consumer Finance; see Appendix III. For definition of median, see Guide to Tabular Presentation]

Age of family head and family income (constant (1998) dollars)	Ratio of debt payments to family income						Percent of debtors with—					
	Aggregate			Median			Ratio above 40 percent			Any payment 60 days or more past due		
	1992	1995	1998	1992	1995	1998	1992	1995	1998	1992	1995	1998
All families	14.1	13.6	14.5	16.1	16.1	17.6	10.9	10.5	12.7	6.0	7.1	8.1
Under 35 years old	16.5	17.1	16.6	16.6	16.9	17.4	10.5	11.0	11.8	8.3	8.7	11.1
35 to 44 years old	17.8	16.6	17.0	19.0	18.1	19.4	11.8	9.2	11.6	6.8	7.7	8.4
45 to 54 years old	14.6	14.8	16.3	16.1	16.6	17.8	10.2	10.4	11.6	5.4	7.4	7.4
55 to 64 years old	11.4	11.5	12.9	14.5	14.0	16.7	14.3	14.5	13.9	4.7	3.2	7.5
65 to 74 years old	7.8	6.9	8.5	10.6	12.2	13.9	7.8	7.8	17.5	1.0	5.3	3.1
75 years old and over	3.4	2.9	3.9	5.0	3.4	8.9	8.7	8.9	20.9	1.8	5.4	1.1
Less than \$10,000	10.8	19.5	19.4	19.5	15.4	20.3	28.4	27.6	32.0	11.6	8.4	15.1
\$10,000 to \$24,999	14.8	16.1	16.2	15.3	17.7	17.8	15.5	17.3	19.9	9.3	11.3	12.3
\$25,000 to \$49,999	16.5	16.2	17.4	16.3	16.6	18.1	9.6	8.0	13.8	6.3	8.6	9.2
\$50,000 to \$99,999	15.3	16.0	17.4	17.0	16.9	18.3	4.4	4.2	5.7	2.2	2.7	4.5
\$100,000 and more	10.7	8.7	10.0	13.7	11.1	13.1	2.2	1.7	2.1	0.5	1.3	1.5

Source: Board of Governors of the Federal Reserve System, *Federal Reserve Bulletin*, January 2000, and unpublished data.

No. 797. Household Debt-Service Payments as a Percentage of Disposable Personal Income: 1980 to 1999

[In percent. As of end of year. Seasonally adjusted. The household debt-service burden is an estimate of the ratio of debt payments to disposable personal income. Debt payments consist of the estimated required payments on outstanding mortgage and consumer debt]

Year	Total	Consumer	Mortgage
1980	12.41	7.99	4.42
1981	12.34	7.62	4.72
1982	12.33	7.47	4.85
1983	12.33	7.46	4.88
1984	12.83	7.80	5.03
1985	13.74	8.29	5.44
1986	14.18	8.50	5.69
1987	13.71	7.92	5.79
1988	13.34	7.58	5.77
1989	13.51	7.57	5.94
1990	13.24	7.11	6.14
1991	12.56	6.51	6.05
1992	11.70	6.03	5.67
1993	11.59	6.13	5.46
1994	12.01	6.52	5.49
1995	12.70	7.05	5.65
1996	13.09	7.44	5.65
1997	13.17	7.47	5.70
1998	13.29	7.57	5.72
1999	13.51	7.58	5.93

Source: Board of Governors of the Federal Reserve System, "Household Debt Service Burden," published: 24 March 2000; <<http://www.bog.frb.fed.us/releases/housedeb/default.htm>>.

No. 798. Banking Offices by Type of Bank: 1980 to 1999

[As of December 31. Includes Puerto Rico and outlying areas. Covers all FDIC-insured commercial banks and savings institutions. Commercial banks include insured branches of foreign banks. Data for 1980 include automatic teller machines which were reported by many banks as branches]

Item	1980	1985	1990	1994	1995	1996	1997	1998	1999
All banking offices	(NA)	82,367	84,332	81,135	81,273	82,466	83,514	94,332	85,404
Number of banks	(NA)	18,033	15,192	12,641	12,002	11,478	10,945	10,483	10,238
Number of branches	(NA)	64,334	69,140	68,494	69,271	70,988	72,569	73,849	75,166
Commercial banks	53,172	57,660	62,710	65,055	65,827	66,733	68,691	69,873	71,142
Number of banks	14,434	14,407	12,377	10,489	9,972	9,553	9,165	8,794	8,598
Number of branches	38,738	43,253	50,333	54,566	55,855	57,180	59,526	61,079	62,544
Savings institutions	(NA)	24,707	21,622	16,080	15,446	15,733	14,823	14,459	14,262
Number of banks	(NA)	3,626	2,815	2,152	2,030	1,925	1,780	1,689	1,640
Number of branches	(NA)	21,081	18,807	13,928	13,416	13,808	13,043	12,770	12,622

NA Not available.

Source: U.S. Federal Deposit Insurance Corporation, *Statistics on Banking*, annual and *The FDIC Quarterly Banking Profile Graph Book*.

No. 815. Consumer Credit Outstanding and Finance Rates: 1980 to 1999

[In billions of dollars, except percent (349.4 represents \$349,400,000,000). Estimated amounts of seasonally adjusted credit outstanding as of end of year; finance rates, annual averages]

Type of credit	1980	1985	1990	1993	1994	1995	1996	1997	1998	1999
Total	349.4	593.2	789.3	839.2	960.7	1,096.0	1,182.4	1,234.1	1,300.5	1,395.4
Revolving.....	55.1	124.7	238.6	310.0	365.6	443.2	499.5	531.3	560.7	596.0
Nonrevolving ¹	294.3	468.5	550.7	529.2	595.1	652.8	682.9	702.8	739.8	799.4
FINANCE RATES (percent)										
Commercial banks:										
New automobiles (48 months) ²	14.32	12.91	11.78	8.09	8.12	9.57	9.05	9.02	8.72	8.44
Other consumer goods (24 months).....	15.48	15.94	15.46	13.47	13.19	13.94	13.54	13.90	13.74	13.39
Credit-card plans.....	17.31	18.69	18.17	16.83	16.04	15.90	15.63	15.77	15.71	15.21
Finance companies:										
New automobiles.....	14.82	11.98	12.54	9.48	9.79	11.19	9.83	7.12	6.30	6.66
Used automobiles.....	10.10	17.58	15.99	12.79	13.49	14.40	13.53	13.27	12.64	12.00

¹ Comprises automobile loans and all other loans not included in revolving credit, such as loans for mobile homes, trailers, or vacations. These loans may be secured or unsecured. ² For 1980, maturities were 36 months for new car loans.

Source: Board of Governors of the Federal Reserve System, *Federal Reserve Bulletin*, monthly.

No. 816. Credit Cards—Holders, Numbers, Spending, and Debt, 1990 and 1998, and Projections, 2000

[The complete publication including this copyright table is available from the U.S. Government Printing Office and the National Technical Information Service]

No. 817. Usage of General Purpose Credit Cards by Families: 1989 to 1998

[General purpose credit cards include Mastercard, Visa, Optima, and Discover cards. Excludes cards used only for business purposes. All dollar figures are given in constant 1998 dollars based on consumer price index data as published by U.S. Bureau of Labor Statistics. Families include one-person units; for definition of family, see text, Section 1, Population. Based on Survey of Consumer Finance; see Appendix III. For definition of median, see Guide to Tabular Presentation]

Age of family head and family income	Percent having a general purpose credit card	Median number of cards	Median new charges on last month's bills	Percent having a balance after last month's bills	Median balance	Percent of cardholding families who—		
						Almost always pay off the balance	Some-times pay off the balance	Hardly ever pay off the balance
1989, total.....	56.0	2	\$100	52.1	\$1,300	52.9	21.2	25.8
1992, total.....	62.4	2	100	52.0	1,100	53.0	19.0	27.4
1995, total.....	66.4	2	200	56.0	1,600	52.4	20.1	27.5
1998, total.....	67.5	2	200	54.7	1,900	53.8	19.3	26.9
Under 35 years old.....	58.3	2	200	71.6	1,500	39.0	22.5	38.5
35 to 44 years old.....	71.3	2	200	62.5	2,000	46.5	19.1	34.4
45 to 54 years old.....	76.3	2	200	59.2	2,000	40.2	22.7	29.1
55 to 64 years old.....	76.0	2	200	48.8	2,300	61.0	20.1	18.9
65 to 74 years old.....	71.2	2	200	33.9	1,000	74.0	14.9	11.1
75 years old and over.....	50.8	1	100	16.7	700	86.3	7.8	5.9
Less than \$10,000.....	23.2	2	100	64.0	900	46.4	19.9	33.8
\$10,000 to \$24,999.....	50.8	2	100	56.9	1,200	52.3	19.3	28.4
\$25,000 to \$49,999.....	73.2	2	100	58.2	1,700	48.3	20.5	31.2
\$50,000 to \$99,999.....	89.6	2	200	55.9	2,400	53.9	20.2	25.9
\$100,000 and more.....	97.9	2	800	36.4	3,100	72.0	13.8	14.1

¹ Among families having a balance.

Source: Board of Governors of the Federal Reserve System, unpublished data.

Comments of Birny Birnbaum
On Behalf of the Center for Economic Justice
Before the National Conference of Insurance Legislators

November 21, 2002

Proposed Model Law Regulating Insurers' Use of Consumer Credit Information in Personal Lines Insurance

Thank you for the opportunity to testify before the Property Casualty Committee today. And as requested, I will direct my comments towards the proposed model law. I do want to preface my comments with a statement of our position on insurance credit scoring. We oppose it and strongly believe the practice should be prohibited. I would like to go into some of the reasons for that position and hope that one of the committee members might ask me a question following my prepared testimony.

With regard to the proposed model law regulating insurers' use of consumer credit information, there are three overriding reactions. First, our thanks to the legislators and agents who have worked diligently to address the many problems associated with insurance credit scoring. The models before NCOIL are clearly an improvement over the current market practice.

Second, we are struck by the how many restrictions and prescriptions are necessary for the use of credit as an underwriting or rating factor. Given the tremendous regulatory resources necessary to enforce the proposed model and given the many concerns with credit scoring reflected in the model, one would think that there are some powerful reasons for allowing insurers to use insurance credit scoring. But, in fact, there are no such powerful reasons. All the industry has is an alleged correlation. Surely that cannot be enough to justify the use of insurance scoring.

Third, the proposed model – or any statute or regulation attempting the things in the proposed model – will not benefit consumers because of lack of enforcement. Some of the provisions are simply unenforceable, while others would require a commitment of regulatory resources that legislators will be unable to provide.

Regarding the three proposals – the proposed model, the proposed substitute and Representative Eiland's amendments – the proposed substitute generally improves upon the proposed model with some notable exceptions. And Representative Eiland's proposed amendments are much needed, although some fine-tuning is necessary.

I will work down section by section from the proposed substitute.

The changed title is an improvement. I suggest adding Insurers' Use of Consumer Credit Information to the title and the purpose. The revised purpose better captures the broader intent of the model.

Personal Insurance might be defined as a personal auto or residential property or personal inland marine insurance policy.

The definition of adverse action is slightly lacking because it seems to revolve around change from a current situation instead of an offer from the insurer of something other than most favorable provisions because of credit information. We suggest the following definition.

Any action by the insurer to offer a consumer other than the most favorable price, terms of coverage, rating tier, payment plan or other feature of the personal auto or residential property insurance policy upon initial application or renewal by the consumer.

Throughout the model, the actions of insurers are generally described as underwriting and rating. For clarity and completeness, we suggest inclusion of tier selection, terms of coverage and payment plan eligibility to go along with underwriting and rating.

The definition of credit information is somewhat circular. The key word in the concept is credit and that is also the key word in the definition. Credit information should be defined as any information from a consumer credit report as defined by the FCRA and then add specific exemptions for purposes of the model for things like CLUE and MVR.

The original definition of credit report is much better than the proposed definition. The definition of insurance score should describe the purposes as underwriting, tier selection, rating, terms of coverage, pay plan eligibility.

Section 5

This section describes various prohibitions regarding underwriting and rating risks. To this list should added tier selection and determining terms of coverage. This section should also include a provision prohibiting the use of consumer credit information to condition pay plan eligibility. The use of insurance scores for pay plan eligibility is illogical, unnecessary and contrary to public policy. It is illogical because the scoring models are purportedly developed to predict claims and not payments. Insurers go to great lengths to distinguish insurance scoring from credit scoring. It is unnecessary because insurers are never in a position to offer coverage without payment. It is contrary to public policy because the availability of payment plans is essential for insurance availability.

Subsection A prohibits the use of several types of information / consumer characteristics. However, the information in credit reports could easily be correlated with these prohibited characteristics. In fact, an econometrician could easily develop a scoring model that predicts income, race, gender or age based upon information in the credit reports. It is of limited value to prohibit consideration of certain factors if there are easily available proxies for those factors.

Further, what is the public policy for prohibiting consideration of these factors? And why doesn't that same public policy apply to credit scoring itself?

Subsections B and C prohibit use of credit as the sole factor for an adverse action and specifically defines tier placement not to be cancellation, denial or nonrenewable. First, prohibiting something as the sole factor is not meaningful. An insurer could use, for example, credit and vehicles valued at less than \$50,000 to avoid the prohibition literally but not

substantively. Second, where is the consumer protection if the insurers' use of credit results in an offer for very high cost insurance is the worst rate tier with no pay plan? This subsection allows insurers to effectively decline coverage without literally doing so. And it worsens the current situation by purporting to provide consumers with protections that, in fact, do not exist.

Subsection D attempts to prohibit adverse actions based upon absence of a credit card. Again, the "sole" language enables an insurer to effectively avoid the prohibition. For example, an insurer could deny coverage if there was no credit card and a vehicle valued at less than \$50,000.

In Subsection E, paragraph 1 removes the substance of restriction because regulators are unable to perform independent review of the studies presented by insurers. Credit is unique in this regard because regulators collect data on other underwriting and rating characteristics through designated statistical agents and authorized statistical plans. See the discussion below for a requirement on data collection that would allow regulators to perform the type of independent review envisioned by this section. In addition, this section envisions yet additional work and necessary resources for regulators. We fear the likely result from overtaxed regulators will be routine approval of restrictions based upon thin credit files.

Subsection F seems to provide a very big window for new business credit reviews. We found Subsection G confusing and could not figure out the exact intent.

The restrictions in Subsection H are very good. We again raise the issue of how difficult enforcement will be for state regulators. Private lawsuits are the logical means of enforcing these provisions. Again, we ask what are the benefits of credit scoring that warrant the use of an underwriting and rating factor that elicits such restrictions and concerns? A simple correlation is not sufficient benefit to either consumers or the insurance system.

The dispute resolution in Section 6 is excellent and we support it.

Section 7 deals with initial notification regarding use of credit information. We support Representative Eiland's proposed amendments. These amendments go to the heart of informing a consumer how credit is used in the underwriting, rating, and tiering process. The type of information suggested by Representative Eiland informs consumer in a manner that encourages consumers to engage in less risky behavior and, consequently, to reduce overall claim costs.

Section 8 provides for adverse action notification. Such notification must be strengthened to better inform consumers of the precise aspects of their credit reports. For example, compare the difference between a consumer being uprated and told the reason was two at-fault claims versus being told the reason was too many retail accounts. The first reason is specific and understandably related to claim costs. The second reason is non-specific and not understandably related to claim costs. The standard industry explanations are inadequate.

The consumer disclosure requirements in the Fair Credit Reporting – and those in the proposed credit insurance model are based upon the notion that an error in the credit report wrongly resulting in an adverse action against the consumer will be the incorrect presence of some negative information in the credit report. For example, if a consumer is denied a loan or

insurance coverage because of a recent bankruptcy, then the consumer is entitled to review the credit history to see if a bankruptcy has been incorrectly reported. Then the consumer can correct the false information and reverse the adverse action.

This consumer disclosure framework is wholly inadequate for insurance scoring because a consumer's insurance score is determined as much – if not more – by the presence or absence of positive factors as it is by the presence or absence of negative factors. A consumer's credit score can be low (i.e., bad) even if there are no negative factors, such as bankruptcies, public records, delinquencies or late payments. A poor insurance score can arise from the absence of certain types of credit (e.g., no real estate-secured loan), the types of credit (e.g., loans from a finance company lead to a lower score than the same loan from a bank and a retail credit card leads to a lower score than a bank credit card), and/or the absence of credit activity or credit information (e.g., a consumer typically pays in cash, has only one credit card or uses financial institutions that don't report payment activity to credit bureaus, such as check-cashing, payday lending and/or rent-to-own businesses).

With insurance scoring, the traditional form of FCRA adverse action disclosure is insufficient because; one, most consumers don't know their credit history is used for underwriting and/or rating; two, even if consumer did know their credit history was being used, the insurer typically does not explain how it is being used or what aspects of the credit report led to the adverse action; and, three, even if the insurer provided the specific reasons, the consumer is unable to determine if information that could have helped the score is missing. Consequently, adverse action and other credit-related disclosure requirements for insurers must be far broader than those set out in the FCRA.

The trade secret exemption to public disclosure in Section 9B is far too broad. It closes much of what is open today. There is no evidence that public disclosure of what insurers do with credit information has harmed any insurer or vendor.

We also recommend the following language for data collection:

Data Collection and Independent Regulatory Analysis. The Commissioner shall direct statistical agents to collect insurer-specific premium, exposure and loss data broken out by raw credit score and credit score category assigned to consumer in addition to other data categories required in approved statistical plans. As soon as such data are available to perform an actuarially credible and/or statistically significant analysis, the Commissioner shall perform an analysis of the correlation of credit information to frequency and severity of claims and to other underwriting and rating factors both permitted and prohibited.

Section 10 provides for indemnification of agents and insurers. We are unclear of how this section will work. What happens if a bunch of consumers are overcharged because of faulty calculations? Do they have any recourse?

Thanks for the opportunity to comment on the proposed model.

Preliminary Comments on the BBR Study

First, the study is really an executive summary. There is no description of many key elements of the study necessary for a review of the reasonableness of the study. For example, how did the researchers acquire the data? Were the researchers able to verify that the data were randomly generated or did they rely upon industry promises? Were the researchers able to verify that the data were selected from a complete data set and not from an artificially restricted data set. The study refers to a variety of regressions, but the regressions themselves and the actual regression output are not provided. It is impossible to review a study for reasonableness when all you get is the results.

While the study promises to have some important results, there is no way that anyone could reasonably endorse the study as definitive and reliable based solely on the 16 pages provided to date.

Second, the authors have a strong ideological bias towards the industry position on credit scoring and this bias causes them to miss an important result of the study. The authors spend considerable time discussing the role of rating factors in pricing. This description is the industry version of cost-based pricing. This explanation – that insurers always seek to price based on every possible explanation of risk of loss – is both untrue and inadequate. There are many other factors that go into determining the acceptance of a rating or underwriting factor than a simple correlation. The industry wants to reduce the debate over credit scoring to whether such a correlation exists, when the questions about the appropriateness of credit scoring go far beyond the issue of correlation.

But the authors ideological bias compromises their study when they fail to explain the importance of the difference between standard market scores and non-standard market scores in terms of credit scoring and, instead, natter on about the wisdom of an unregulated system. The key finding here is that credit scoring is correlated to some other factor that insurers already use – somehow, in the absence of credit scoring, insurers were able to distinguish standard from non-standard risks – and when the credit scores were added, the average standard credit score was higher than the average non-standard score. The authors discussion of the wisdom of the current system is gratuitous and irrelevant. The question in this study is not whether rate regulation or the absence of rate regulation is good or desirable. The question is the impact of credit scoring. When the authors fail to point out a major result – that credit scoring is correlated to some other factor that insurers already consider and, therefore, duplicates an existing underwriting guideline or rating factor and instead offer arguments to support the industry plea for no regulation of rates for county mutuals, the credibility of the authors is compromised.

Third, the authors analysis utilizes loss ratios to evaluate the relationship between credit scoring and risk of loss. But the validity of the loss ratio approach – that differences in loss ratio can be attributed to the one factor being analyzed – is predicated on accurate pricing (accurate pricing as described by the authors). But it is well known that insurers routinely depart from the accurate pricing necessary to support the authors models. It is quite common to see insurers apply or file for actual rate increases that are substantially

lower than their indicated rate increases. A study I performed for the OPIC showed a difference of over 20% between indicated and selected rate changes. Further, insurers knowingly misprice certain factors for marketing and other purposes. And insurers are required to give a discount to consumers who complete a driver training course, even though the majority of folks who take the course are doing it to expunge a ticket and the loss experience of those who take the defensive driving course is no better and often worse than consumers not taking the course and getting the discount.

This loss ratio method of analysis has long been discredited. The NAIC rejected this method of study as early as 1996.

Fourth, the study does indicate that insurance scores are correlated to income. The study shows that consumers insured in non-standard carriers have lower scores, on average, than consumers insured in standard carriers. And, as stated above, these outcomes were generated before most insurers were using consumer credit information for underwriting or rating. Research by the Center for Economic Justice shows that consumers who live in poor and /or minority neighborhoods are 3 to 4 times more likely to be denied coverage by standard insurers and end up in the non-standard market.

Fifth, it is unclear why the authors chose auto insurance and not homeowners insurance for their study or why the study did not look at results by coverage.

Several Organizations oppose the use of insurance credit scoring:

John Bryant, Agent Champion, is Terminated

John Bryant was an agent for a very large insurer. He treated his clients the way they deserve to be treated and even went to bat for them in the game of "insurance credit scoring". He was terminated for his efforts

The Center for Economic Justice

"David "Birny" Birnbaum, of the Center for Economic Justice, recently said, "There has been no comprehensive **independent** [emphasis added] study of a link between credit problems and car accidents. The industry is accepting "statistics" from the company that provides that information and programs!" ¹

The National Association of Professional Allstate Agents

The National Association of Professional Allstate Agents (NAPAA) has studied the issue of "credit scoring," or "insurance scoring," and because Allstate was one of the earliest users of credit scoring algorithms to underwrite and rate insurance policies, Allstate insurance agents have the most experience dealing with this system and its adverse effect on our customers. Our conclusions based on this unique experience are:

- o It is a secret methodology, not subject to examination by Insurance Commissioners, which affects the premium and/or acceptance of insurance applicants and existing customers.
- o Credit scoring appeared when insurance companies were denied the ability to overtly Redline geographical areas and certain minority groups.
- o Credit scoring is a new method of Redlining meant to replace the old method.
- o Particularly affected are minorities, low-income groups, senior citizens and others who rarely, or never, make use of credit. Other affected people are those who have had divorces, the death of a spouse, large medical bills or even those who check their own credit regularly to be sure the information is accurate.
- o The insurance/credit score is a moving target - Today one may have a "score" of 4, next month a score of 2. The consumer just has to hope they get lucky when they apply, because they are stuck with whatever the score happens to be at that time, with no possibility of improvement, for the life of the policy.
- o Credit scoring allows a company to take rate increases at their sole discretion by merely adjusting their never examined and secret algorithm by changing the weighting of certain values.

Credit scoring for insurance is not socially acceptable. It violates the values Americans hold dear. The American way is to be judged on those things that are directly relevant to the

subject: Tickets, accidents, vehicle usage etc. for auto insurance and condition of premises, past losses and upkeep etc. for property insurance. Credit scoring for insurance purposes is Redlining. NAPAA strongly opposes Redlining, thus we have no choice but to oppose credit scoring.

United Farmers Agents Association

"Our industry struggles with a bad reputation already. The misuse of credit scoring will further erode consumer confidence. It's time for the industry to step up and commission an independent study of the relationship between credit and future losses. It's time for the industry to force the release of the rating factors in the FICO programs. Its time to change the rules so consumers can get specific answers about their scores."

The National Association of State Farm Agents, Inc.

Resolution Sept 28, 2001

The National Association of State Farm Agents, inc. (NASFA) hereby resolves that we are opposed to any insurance company using credit scoring for the purpose of Property & Casualty underwriting and rating. We further support legislation to prohibit credit scoring for the purpose of Property & Casualty underwriting and rating. We believe this form of underwriting is profiling clients who would otherwise be eligible for Property & Casualty business.

The Coalition of Exclusive Agent Associations

Credit Scoring POSITION STATEMENT Adopted March 11,2002

"In the absence of full and good faith disclosure to the consumer and appropriate state insurance officials of all weighting factors and the respective percentage(s) or importance of their weighting, the CEEA opposes the use and consideration of credit status and/or credit scoring in any manner in connection with the acceptance, rejection, renewal or determination of insurance coverage or with respect to the determination of insurance rates and/or rate increases. It is the position of CEEA that credit information, written or otherwise, should not be given any consideration as a basis for determining the acceptance, rejection or renewal of insurance coverage or insurance rates."

National Auto Agents Alliance

"The National Auto Agents Alliance recently issued a statement that credit scoring is "unreliable, inaccurate, and so against public interest as to endanger the insurance industry to the wrath of the public... The NAAA feels that credit scoring may even suggest a level of redlining that segments insureds into "haves and have-nots."

National Association of Insurance Commissioners

"In a White Paper issued recently by the NAIC, which now wants this credit scoring practice monitored, it was suggested that insurers not be allowed to **deny policies based solely on credit reports**. It also recommends that the industry develop objective, verifiable guidelines for ordering credit reports"

**This information is from the following website.
www.geocities.com/insurance_credit_scoring**

National Association of Professional Allstate Agents

Toll Free: 877-627-2248 Fax: 877-621-1786 www.napaausa.org
42015 Ford Road #261 • Canton, MI 48187-3669



Commissioner Mike Kreidler
Washington Department of Insurance
Insurance Building/14th & Water
Capitol Campus
P.O. Box 40255
Olympia, WA 98504-0255

October 15, 2001

Dear Commissioner Kreidler,

The National Association of Professional Allstate Agents (NAPAA) has studied the issue of "credit scoring," or "insurance scoring," and because Allstate was one of the earliest users of credit scoring algorithms to underwrite and rate insurance policies, Allstate insurance agents have the most experience dealing with this system and its adverse effect on our customers. Our conclusions based on this unique experience are:

- It is a secret methodology, not subject to examination by Insurance Commissioners, which affects the premium and/or acceptance of insurance applicants and existing customers.
- Credit scoring appeared when insurance companies were denied the ability to overtly Redline geographical areas and certain minority groups.
- Credit scoring is a new method of Redlining meant to replace the old method.
- Particularly affected are minorities, low-income groups, senior citizens and others who rarely, or never, make use of credit. Other affected people are those who have had divorces, the death of a spouse, large medical bills or even those who check their own credit regularly to be sure the information is accurate.
- The insurance/credit score is a moving target - Today one may have a "score" of 4, next month a score of 2. The consumer just has to hope they get lucky when they apply, because they are stuck with whatever the score happens to be at that time, with no possibility of improvement, for the life of the policy.
- Credit scoring allows a company to take rate increases at their sole discretion by merely adjusting their never examined and secret algorithm by changing the weighting of certain values.

Credit scoring for insurance is not socially acceptable. It violates the values Americans hold dear. The American way is to be judged on those things that are directly relevant to the subject: Tickets, accidents, vehicle usage etc. for auto insurance and condition of premises, past losses and upkeep etc. for property insurance. Credit scoring for insurance purposes is Redlining. NAPAA strongly opposes Redlining, thus we have no choice but to oppose credit scoring.

Insurance commissioners, in various states, are conducting hearings to better understand how the use of credit impacts the insurance consumer. Captive Allstate agents wish to participate and contribute at these meetings since they are closest to the consumer and see firsthand how implementation of credit directly affects the customer. However, they have been discouraged to do so under threat of retaliation by Allstate. If an agent's presence at these hearings were made mandatory, we would make every effort to assure the presence of a NAPAA representative.

Sincerely,

Janice Mathison
Executive Director

National Association of Professional Allstate Agents

Toll Free: 877- 627-2248 Fax: 877-621-1786 www.napaausa.org
42015 Ford Road #261 • Canton, MI 48187-3669



Washington Department of Insurance
Commissioner Mike Kreidler
Insurance Building/ 14th & Water
Capitol Campus
P.O. Box 40255
Olympia, WA 98504-0255

- Carol Sureau
- Gigi
- Lisa Smego
- Bill D.

October 22, 2001

Dear Commissioner Kreidler,

In a previous letter to you from our association (copy attached), we informed you of NAPAA's position on Credit Scoring. In that letter, we explained that captive insurance agents who may desire to participate and contribute at hearings regarding Credit Scoring and Redlining have been prevented from doing so by threats of retaliation by their companies.

Agents have more knowledge of the effects of this practice on their clients than any other segment involved in the process. Yet, contrary to the public good, insurance companies exert every effort to prevent such knowledge from being made public.

On October 12, 2001, NAPAA informed the Allstate insurance agents in the state of Washington of the public hearings to be held on Credit Scoring. We encouraged them and their clients to attend one of the meetings. Allstate reacted swiftly to our bulletin. In a letter dated October 15, 2001, Field Vice President A. Darryl Page warned Allstate agents against participating in those hearings. We have attached a copy of his letter.

It is clearly not in the best interests of the citizens of Washington state, efforts of your office to regulate insurers, or those of legislators representing their constituents for a private company to deny access to the information possessed by insurance agents; valuable and insightful information.

We urge you to find a way that would allow agents to participate, to testify at public hearings, in legislative committee hearings and other government venues without fear of retaliation by their associated companies. Otherwise, how can our system of government function as it was intended?

NAPAA stands ready to assist in any effort you may make to ensure that your department and the citizens of Washington hear the truth.

Sincerely,

Janice Mathison
Executive Director

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North Star Examinations, Inc.

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April 18, 2002

Honorable Kim Elton
Senator,
Alaska State Senate

Juneau, AK 99811

Re: Credit History and Credit Scoring in Insurance

Dear Senator Elton

I read in the paper yesterday that you have proposed legislation to prohibit the use of credit history and credit scoring in the State of Alaska for underwriting and selection of personal automobile insurance and homeowners insurance. I support your efforts to do so and would like to offer some observations that may be of interest.

By way of background, I am a retired state employee (as of 3/31/97), having worked at the Alaska Division of Insurance for more than 27 years as its Chief of Market Surveillance. I was responsible for rate review, form review and market conduct examinations. I also spent considerable time working with legislators and staff on a variety of insurance issues. Currently I continue to reside in Juneau and operate a small consulting firm that provides market conduct examination services for state insurance departments. I have no Alaska contracts. States currently using my services include Delaware, New Mexico and North Dakota. For these states I establish examination processes, develop state specific handbooks on how to perform such examinations, train examiners, supervise and conduct examinations. My views do not reflect those of the states for whom I provide services, they are my own.

In 1995 when credit history was first being used by insurers in personal automobile insurance, The National Association of Insurance Commissioners appointed a working group to look into the issue and ultimately develop a white paper as a guide for states considering what to do about the issue. I chaired the initial working group but after several meetings asked Maryland to assume the chair since I was somewhat over-committed at the time. I continued to remain active with the working group. I can recall one meeting in Northbrook Illinois that was of particular interest. We had about a dozen

regulators from a number of states meet with an insurer to gain an understanding why they felt the credit history should be an underwriting consideration. Our group was comprised of a good cross section of expertise including actuaries, economists, and examiners.

The company data presented suggested that there was a considerable correlation between the propensity for loss and credit history. There were several problems for which we could not elicit satisfactory answers and essentially these remain unchanged today. They are:

1. The data was based on the Company's customer database and since that had spent considerable time, effort and money to develop the system, they did not want another company to copy their data and use it as their own. They felt that such action, which is fairly commonplace, would place them at a competitive disadvantage. We were not able to look at the underlying data or supporting calculations. The data would appear to be more supportive of rate differentials rather than selection differentials.
2. In our attempts to understand how poor credit could tie into increased likelihood of loss only one person made an analytical observation that made some sense. He said that the intended form of credit scoring was in a sense a quantification of responsibility. It would appear that poor credit history is a reflection of responsibility and attitude that according to the presenters carried over into how a person drives an automobile or does things that might reduce an insurers exposure to loss. This tie was not demonstrated, it was theorized.
3. The insurer at that point had not developed the process to the point that duplication for factors already considered in other underwriting considerations could be avoided.
4. Fiscal emergencies were not factored out of the process. Someone with a longstanding good credit history who has an expensive medical emergency that temporarily revises the persons payment history would not receive special consideration even though the underlying attitude to paying on their commitments was unchanged. A similar issue arises in a depressed economy when layoffs occur. Being unable to continue to meet obligations is not the same as being unwilling to meet them and credit scoring does not make the distinction.

Many insurers these days are trying to outsource functions or parts of functions to independent vendors. They do this in part because it is difficult for the regulator to achieve a comprehensive view of the company's operations. They also do it for perceived gains from savings on expenses. The savings often come from reduced management oversight of the outsourced function.

During the past few years, I have been involved in the examination of eight major auto and homeowners insurers, six of those directly and the other two as a supervisor. Some do not use credit history, some do not use credit scoring. Some use credit only for placement in a rating tier. Some use credit only on new business. I believe that the


system as I have seen it is inherently flawed and are unfairly discriminatory. Insurance is by its nature discriminatory and that is not unreasonable. Unfair discrimination is quite another story. Some examples of why I think Credit History and Credit Scoring is unfair are:

1. If credit history and credit scoring is intended to reflect responsibility then it is unfair because that connection has not been established and no efficient method has been established to identify exceptions.
2. Most insurers use credit scoring only at the initial underwriting and that is to determine into which rating tier the person should be written. That is unfair since attitudes can change, credit history can change, and no opportunity is provided to assure that the selection criteria and measurement has remained unchanged. If a person's score improves is he/she locked into the tier that resulted from the initial review? This might arguably be a conflict with the federal Fair Credit Reporting Act that contains a limit on how long the information in a credit report can be used.
3. The fact that scoring information is secret is unfair. If the information developed on a person and how it is used is secret, how is anyone to know that it has been properly used? It makes the Insurance Director's job to oversee a fair insurance marketplace very difficult if not impossible to achieve.
4. The nature of the scoring is that a large transaction such as the purchase of a house has a negative influence on the credit score thus presenting the buyer with problems when he/she attempts to insure the house. It's a sort of "Catch 22" kind of effect which comes up frequently in complaints. A contact with other state insurance departments concerning their complaints on credit history and credit scoring might prove enlightening.

At this juncture, my own preference is for an outright ban on the use of credit history and credit scoring for personal lines automobile insurance and homeowners insurance. If the legislature wishes to proceed with some form of limitation, I would urge caution because that would tend to give a flawed program sanction. Better not to act or to assure that the Director of Insurance has adequate rulemaking authority to provide for protection of the public. I would also urge caution about the structure of a ban because there are insurance lines of business where credit history review is appropriate, for example some of the commercial financial products and possibly fidelity and surety products.

I am sorry that my late awareness of this as a legislative issue in Alaska and my somewhat bizarre travel schedule prevents me from providing more direct input. I will be on travel status for the next three weeks but can be reached at my cell phone (907) 321-4084.

Very truly yours,


Donald P. Koch, CIE
President

1/17/03

DON'T BASE INSURANCE RATES ON ...

Credit ratings

A. GAIN THIS year, the Legislature will have the chance to end the insurance industry's controversial use of credit ratings to determine how much auto and home insurance will cost Alaskans.

A measure introduced by Sens. John Cowdery, R-Anchorage, and Kim Elton, D-Juneau, would bar the use of credit scoring to set premiums.

Critics of credit scoring say it opens the door to financial and even racial discrimination. Its proponents say it is a fair and accurate assessment of potential losses.

The practice is under fire in more than two dozen states. Similar legislation was introduced last year in the Alaska Legislature, but died in the Senate Labor and Commerce Committee as time ran out in the session and questions remained about exactly what the bill should contain.

Credit scoring is how many insurers nowadays calculate, in whole or in part, the amount of your insurance premiums. They obtain personal information from credit bureaus, including debt amount, collections, bankruptcies, payment history, amount and types of credit. They feed it into a computer model and you receive a score. A good score means lower rates. A bad score can mean you pay more.

Insurers say the use of credit histories and scoring is necessary because it allows them to identify drivers who will cost the company the most in losses. They say studies which themselves have stirred questions — have shown that people who keep their financial house in order are better risks.

Opponents of credit scoring say it reared its head after insurance companies some years ago were barred from "redlining" certain geographical areas and minorities. Additionally, they say the practice zeros in on the elderly, the young, people with little credit, renters and others, even those with errors in their credit history. Purchasing a home, for instance, can affect your credit rating, and the insurance you will have to buy for the home.

Testimony introduced last year before the state Senate Transportation Committee illustrates the point.

A woman with a clean driving record and who already had insurance — but who rented her home — received a \$452 increase on her six-month insurance bill because of her credit score. At the same time, a man with with good credit who was buying his home qualified as a preferred customer — even though his driving record included a DWI with an accident.

It would seem to us that driving records or a history of losses should count toward calculating insurance premiums, not a person's credit history or a score generated from information that may be flawed, from a system immune from public scrutiny.

Cowdery and Elton are on the right track in pursuing this legislation. Hopefully it will fare better than it did last year.

OUR VIEW

Credit scoring

Either reform or abolish this insurance shortcut

Insurance companies love the practice of credit scoring because it's cheap and easy. By some magic known only to actuarial wizards, a person's credit records can be converted into a number that companies find useful to decide whether to insure a person or how much to charge him. No need to spend a lot of time tracking down motor vehicle files, checking property records or evaluating other information that directly bears on what kind of risk the applicant poses.

And if there is no logical connection between a person's credit history and the odds that she will make auto or home insurance claims? No problem. It's magic, but it works.

Except that it doesn't always.

Some people with good driving records get socked with big rate increases because of what's in their credit file.

The whole exercise of credit scoring is premised on the assumption that what is in a person's credit file is accurate. Many an Alaskan can testify to the contrary.

Some people with good credit but bad driving records get lower rates they don't deserve.

Some people have less than perfect credit records for reasons beyond their control. They may have suffered a medical catastrophe. A recent divorce may have scrambled their finances. An angry ex-spouse may be withholding child support payments.

And the whole exercise of credit scoring is premised on the assumption that what is in a person's credit file is accurate. Many an Alaskan can testify to the contrary.

Credit scoring has drawn plenty of criticism, even from inside the insurance industry. The National Association of Professional Allstate Agents has condemned it on multiple grounds. The methodology is secret, with no oversight by state insurance commissioners. Credit scores can change frequently, calling their reliability into question. Noting the impact it has on minorities, the poor, senior citizens and others who don't use much credit, the group calls credit scoring "a new method of redlining."

Anchorage state Sen. John Cowdery, R-Lower Hillside, is leading the charge to ban credit scoring in Alaska. Hardly an advocate of big government, he knows first hand from his daughter's experience how credit scoring can punish someone with a clean driving record. He's joined by colleagues from both ends of the spectrum: conservative Republican Fred Dyson of Eagle River and Democrats Kim Elton of Juneau and Gretchen Guess and Johnny Ellis of Anchorage.

ADN 1/27/2003

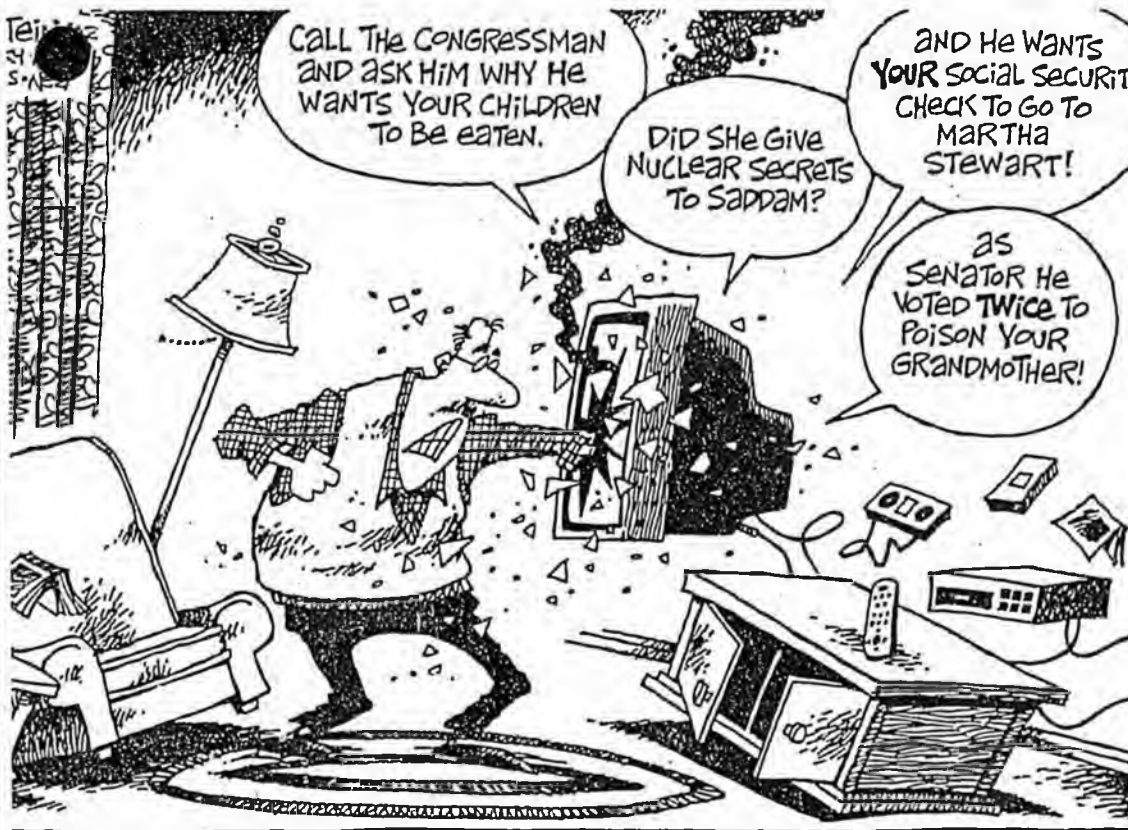
At minimum, some reforms are essential.

Exclusive reliance on credit scores should be banned. Customers must have a way to make sure their credit records are accurate and get refunds if errors cause them to be overcharged for insurance. Those with little credit history should not be penalized for it. State insurance regulators must be able to scrutinize the mystery formulas so

they can judge how appropriate the process is.

By the time insurance companies comply with reasonable conditions like these, credit scoring may no longer be such a cheap and easy way to decide coverage and set rates. If insurance companies aren't willing to mend the practice of credit scoring, though, the Legislature should end it altogether.

The methodology is secret, with no oversight by state insurance commissioners. Credit scores can change frequently, calling their reliability into question.



TOUCH-SCREEN VOTING

Juneau hospitality shines

By JIM POWELL
 Thank you to the hundreds of people and businesses that participated in last week's site selection visit by the Winter Game's Inter-Committee. Saturday morning, with large crowds at the airport, it rained in the fog as the commercial jet circled overhead. As the plane hickened and it became clear that no planes were going to land, it looked as if the carefully prepared visit was in jeopardy. Juneau's welcoming committee met Saturday night and decided the entire program. Normally, the committee met in Juneau and once the Winter Game's support team arrived at the airport, the hockey rink, the high school, and at the International Convention Center.

and other skiers and snowboarders waving signs and chanting "Juneau 2006." Inside the lodge, an impressive presentation by local experts was given about our ski facilities and capabilities for the ski, snowboard and snowshoe events. The games would take place in early March and records show Eaglecrest has never failed to have a large snow pack then. Our large volunteer and family oriented ski area was highlighted. During the warm informal reception that followed there were lots of one-on-one conversations between committee members and the skiing public. Then on to Douglas, where two Douglas Fire Department trucks escorted us to the hockey rink. The welcome committee

Alaskan Native Elder Agnes Ballinger. The lunch was capped off with a short DVD produced by the Juneau Convention and Visitors Bureau, Mad Dog Graphx, Damon Struebner, and others. The high school complex, where the 2,000-plus student athletes would be housed, was the final venue. The committee entered the gym to welcome signs and cheers by the JDHS cheerleaders. The dance team performed its light show. A very impressive selling point was our renovated high school. Our ability to house, feed, and have a safe place for athletes to meet is one of our bid's strongest components. Concerning the weather, the committee was very responsive to Juneau's proposals for contingency plans for back-up ferry transportation.



What do you think?

Last week's question:

Sens. John Cowdery, a Republican, and Kim Elton, a Democrat, have pre-filed a bill to prohibit "credit scoring," the insurance industry practice of setting rates based on a customer's credit history. Should the cost of someone's insurance be based on credit history?

YES	NO	UNSURE
34	259	5
11%	87%	2%

Number of respondents: 298

Comments:

A person with a perfectly clean driving record and who may have lost a business or employment causing creditors to take legal action to collect a debt should not be penalized by paying higher car insurance rates.

Does owning a small business make you a bad driver? Do medical bills you can't pay make you a bad driver? Does an acrimonious divorce make you a bad driver? Does cutting up your credit cards or paying cash for your car make you a bad driver? All those things give you a bad credit score. Credit scoring has to go.

If the insurance companies insist on basing my insurance on my credit report, then I can make them an offer: For each year I complete as a safe driver with no claims against my policy, the insurance company should reimburse me the moneys I have awarded them for that year.

A person should be allowed to buy insurance at a reasonable price regardless of their credit history.

This week's question:

A citizens group, BEARS Inc., is proposing a center where garbage bears would be placed in an attempt to rehabilitate them. The center also would be a place to view bears and educate people

far as I can see. It insults me and it violates my civil rights," said Boisean Michael Howard, whose insurance agent told him a month ago that his homeowner's policy would be canceled because his credit score had plummeted. Now, he said, he has a new homeowner's insurance policy, and the coverage that used to cost him \$265 a year is up to \$725 a year.

and more common in recent years to use credit history to help determine homeowner's and auto insurance premiums. They contend that records of collections, tax liens, bankruptcies and civil court judgments are as helpful in figuring insurance rates as a person's driving record, and those predictions help keep rates down.

Opponents contend credit scores are unfair, hurt people arbitrarily and lead to people going without insurance.

Wayne Hoffman

• [Senate Bill 1408](#)

"They've got too many tools to rip off the public whenever they want," he said.

Credit scores come from a person's credit history. A person who pays bills on time and has little revolving credit, for example, might have a good credit score, while a person who is months behind on bills and has burgeoning credit card debt might have a bad credit score.

Insurance companies say bad credit scores tend to correlate to future claims the company will have to pay.

Boise insurance agent Bob Ricketts said the practice is neither fair nor logical. It is legal in Idaho, though.

"If you have a person with a DUI and they have good credit, they will be accepted in a preferred-rate class now," said Ricketts, chairman of the Independent Insurance Agents of Idaho.

Coeur d'Alene Sen. John Goedde is the group's president. He's proposing legislation that would restrict the use of credit scores by insurance companies when figuring automobile and homeowner's insurance. About half of the state legislatures across the

CAPITOL

ARCHIVE

CALENDAR

MULTIMEDIA

BACKGROUND

KEY PLAYERS

MORE

- him
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 out
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country are looking at similar legislation.

Goedde, a freshman Republican, said he's heard of homeowner's insurance rates shooting up 300 percent, and said the biggest losers are the elderly, the very young and members of minority groups. His legislation, Senate Bill 1408, would restrict insurance companies from using credit scores as the primary reason for denying insurance or jacking up a customer's insurance rates.

The measure will have a hearing today.

Another insurance agent, Republican Rep. Bill Deal of Nampa, said it would be OK to use credit scores for new customers. But he calls the trend of the past 10 years -- using credit scores to judge existing customers -- "very inequitable and morally wrong."

Boise insurance agent Eric Jeglum said he opposes the proposed legislation. He said studies have proved "without a doubt" that credit scores are a reliable predictor of future insurance claims. The worse the credit score, the more claims are likely, he said. And the better the credit score, the fewer the claims, in general.

If that tool were not available to insurance companies, he said, rates would climb 20 percent for people who are now categorized as having good credit.

"Credit scoring allows us to accurately indicate what the rates should be," Jeglum said.

He equates it to what happens when insurance companies figure the premium for teen drivers. Not all of them are unreliable behind the wheel, but insurance companies assign a higher premium to them because young drivers, as a group, tend to be a higher risk than older drivers with more experience.

Max Marshall of Boise doesn't buy it. He had to file bankruptcy for health reasons, and now he says he can't insure his home for anything less than \$325 a year.

"I don't understand why my credit rating would affect home insurance," Marshall said. "I don't think it's fair. It seems to be discrimination."

"Now, not only do we have the health bills, everything is going to cost more for something

that is beyond our control."

"We've been anecdotalized to death on this," said Michael Harrold of the National Association of Independent Insurers, whose group favors the use of credit scoring. There's always going to be someone who appears to be an exception to the pattern when it comes to credit scores. But the bottom line, said Harrold, the association's Northwest regional manager, is, "You're not hearing from the 50 to 60 to 70 percent of policyholders who are getting a discount" because of good credit scores.

"Really, insurance is about predicting future loss. It's not always about what you've done in the past. (Credit scores) are a phenomenally predictive tool," he said.

As the number of delinquent accounts, tax liens, bankruptcies and civil court judgments increase, so do insurance companies' losses, according to Harrold's data from the credit-scoring company Fair, Isaac.

"I don't see why it's pro-consumer to prohibit the use of a mechanism to allow people to pay the most fair insurance rate," Harrold said.

Ralph Buchanan, president of the United Farmers Agents Association, said the reason is simple: It's wrong.

"The old way of rating auto insurance, I could go out and get a five-year history of tickets and accidents for you. That for years and years has told me whether you're a good driver or bad," Buchanan said.

But the American Insurance Association contends people are paying a fairer rate for insurance now that credit scores are available to guide insurers.

Restricting the use of credit scores would result in less competition among companies and require the good customers to subsidize the bad, association members say.

Two-thirds of customers have good credit, and they will see their rates go up to pay the claims of the one-third with bad credit, said Bill Gausewitz, AIA's assistant vice president for state affairs.

For Howard, that's little comfort.

"Tripling your homeowner's rate because of your credit rating assumes quite a lot," he said. "It's nothing short of stealing."

To offer story ideas or comments, contact reporter Wayne Hoffman at whoffman@idahostatesman.com or 377-6416

Insurers get an earful from senators
Panel: Industry's use of credit history is wrong

By Wayne Hoffman
The Idaho Statesman

A Senate committee chastised the insurance industry Thursday for its use of people's credit history in figuring insurance premiums and voted 7-2 to restrict the practice.

8 R 5 + 1 D

Senators on the Commerce and Human Resources Committee said the use of credit scores to set rates and sometimes to deny insurance coverage is arbitrary, mysterious and flat wrong.

Senate Bill 1408, now on its way to the full Senate, would restrict the use of credit scores so that they cannot be the primary basis for an insurance company's decision to change rates or drop automobile or homeowner's insurance coverage.

Some insurance trade associations contend the credit scores have proven to be excellent indicators of potential insurance claims, and they're used to keep rates down.

Others contend the practice discriminates and that there's nothing to prove the scores really reflect much of anything.

Half of the states in the country are considering legislation restricting in some fashion the use of credit scores.

"For me to try to explain to my customers why this is taking place ... it's confusing," said Boise insurance agent Bob Ricketts of the Independent Insurance Agents of Idaho, who is against the practice.

He said he has plenty of proof to show that clients who have a history of claims were renewed with double-digit reductions in premiums while some clients with no insurance claims are showing double-digit increases in premiums.

Sen. Brent Hill, R-Rexburg, found the insurance industry's explanations so nebulous and frustrating that he grilled insurance agent Jennifer Oldenburg for her support of credit scores.

Oldenburg said credit scores have been helpful in selling insurance at competitive prices.

"It's not the only thing that's used" to determine premiums, Oldenburg said.

But Hill said he had yet to hear a good reason for where credit scores come from and how they are applied. He expressed dismay that Oldenburg can't counsel people on how to get their credit back in good standing.

"I'm not surprised you don't know. Your customer doesn't either," Hill said.

Oldenburg said insurance companies have the right to pick the best mechanisms for figuring insurance rates.

"That's right. They have that right -- at the present time," Hill retorted.

American Insurance Association lobbyist Phil Barber acknowledged the insurance industry "has done a very poor job in informing agents and informing me and the public in general" about credit scoring.

But he said lawmakers should avoid passing Senate Bill 1408 in haste when a compromise could be reached.

Barber said the industry would be willing to accept a restriction that says insurance companies can't use the scores as the sole reason to cancel or jack up rates.

But senators voted 7-2 against that proposal, saying it would leave consumers in no better a position than they're in now. Insurance companies will merely make credit scores the majority reason for the decision and throw in a miniscule second factor to comply with the law, they said.

To offer story ideas or comments, contact reporter Wayne Hoffman at whoffman@idahostatesman.com or 377-6416.

So, what's in the Score?

Scoring model vendors refuse to divulge the methodology of these studies, the underlying data for independent verification, or the details of the study results. They claim these models are a "trade secret" and 'fear' that disclosure would lead to outside infringement.

What we do know is:

Information used in scoring models:

Outstanding Debt
Length of Credit History
New Application for Credit
Types of Credit in Use
Late payments
Collections
Bankruptcies
Inquiries

Information NOT used in scoring models:

Ethnic Group
Religion
Gender
Familial Status
Handicap
Age
Marital Status
Address
Nationality
Income -????.

And they use the following to determine the score:

Number of delinquencies.

The number of months since the most recent delinquency.

The number of trade lines open.

The number of adverse public record items (bankruptcies, judgments, liens, and foreclosures).

The number of months since the most recent public record item.

Trade account balances.

Ratio of the trade account balance to the credit limit available on the account.

Number of inquiries.

How this score is calculated and the actual score is unknown to the consumer. ***Update** - the credit bureaus are now offering your insurance credit score - at a price. (If anyone uses this service, please let email if you understand it anymore than before you obtained the score - Thanks!). Incidentally, because the methodology is given to **no one**, credit scoring models are completely **unverified for accuracy, uninvestigated for legality, and unregulated by regulators**. The scoring model vendors believe that if the consumer had access to the score and methodology of the score that:

1. consumers will not understand the score and;
2. if consumers did have the score, they may change their behavior and skew the results.

So this means the industry does not want us to change our behavior and become better drivers? No, because again, these scores are not being determined using driving records but whether or not you are likely to file a claim for an incident. **The industry is more concerned with their bottom line than they are for your safety.**

Credit reports can be manipulated, (Rapid ReScoring), and as long as the consumer is unaware as to how he/she is scored, the numbers will correlate. Obviously, the industry has found the use of insurance credit scoring to be extremely profitable as they fight mightily to keep it unrestricted, this leads me to believe there may be underlying reasons. (See my theories here.)

It may seem to make some sense that a person with a poor insurance credit score might be more likely to need compensation for an accident but that is only until you learn the type of individuals who have characteristics that score poorly in an insurance scoring model. A few of these include:

Small business owners.

Home-based business owners.

Consumers who pay off their mortgages and/or auto loans early.

Consumers who shop around for mortgage and/or auto loans for more than two weeks.

Consumers with little or no credit histories, referred to as a "thin credit file".

Consumers who do not believe in using credit.

Consumers who seek credit counseling.

Does this appear to indicate financial irresponsibility to you?

Then you have to consider the victims, the individuals who have poor insurance credit scores through no fault of the own:

Victims of identity theft. (The **fastest** growing crime in America.)

Victims of terrorist attacks.

Employees who lose their health coverage.

Consumers who experience a death in the family.

Consumers who divorce.

Consumers who experience catastrophic illnesses within the family.

Consumers who file medical bankruptcies.

Lower income Americans are more likely, in many cases, to have credit files that score poorly. (thin files). They are also less likely to have the disposable income necessary to settle an accident without the insurance company.

**This information is from the following website.
www.geocities.com/insurance_credit_scoring**



Alaska Independent Insurance Agents & Brokers, Inc.

April 18, 2003

Senator Con Bunde, Chairman
Senate Labor and Commerce Committee
State Capitol Building, Room 506
Juneau, AK 99801-1182

RE: Senate Bill 13 – Insurance Discrimination by Credit Rating

Dear Senator Bunde:

The Alaska Independent Insurance Agents & Brokers (AIIAB) is a professional trade association representing independent business people throughout Alaska. Our members bring a unique perspective to the issue of using credit data in the insurance industry. We work with our insurance company partners while representing the interests of our clients. Because we deal with the Alaskan consumer on a daily basis, we are particularly sensitive to the needs and concerns of consumers. We believe the best consumer protection is a healthy competitive insurance marketplace.

The use of credit scoring in both the underwriting and pricing of insurance products is a highly complex issue. On one hand, most agents strongly support tools that foster enhanced competition and the fair and accurate pricing of risk. At the same time, the increased use of credit by insurers has forced us all to consider the manner in which credit scoring is used in the marketplace and to evaluate whether changes need to be implemented.

For many years, credit data has been utilized by the financial services industry. Lenders, for example, use such information to evaluate loan applications, determine creditworthiness, and predict the likelihood of default and delinquency. They measure the potential borrowers against millions of other similarly situated individuals. Similarly, the insurance industry uses credit data to predict future losses and claim costs and to determine prices in a more accurate manner. Many studies have shown that an individual's credit history is an accurate predictor of potential for future loss. In 1996 a study by Tillinghast-Towers-Perrin of nine personal insurance companies, concluded that the relationship between credit scores and loss ratios ranged from 92% to 99%. In 1999, the Virginia Bureau of Insurance reached the conclusion that there appears to be concrete

data indicating that a correlation exists between credit scores and losses. Thus, insurers have begun to use credit based scoring with other traditional factors to determine who to insure and what price to charge. Why would it be reasonable for one segment of the financial services industry to use credit data and not all of the insurance industry to utilize the same credit data to match the price of their products with the expected cost of those products.


There remain, however, additional concerns: 1) the use of credit data as the exclusive criteria in insurance underwriting or the inflexible use of credit data, 2) the lack of ability for regulators to review the proprietary credit algorithms or formulas as insurer filings can become public information for competitors to review, 3) credit information may be inaccurate and 4) lack of disclosures to consumers that credit information is obtained and its utilization in insurance underwriting or rating.

A final point that causes great concern for our Alaskan members is that a total ban on the use of credit data will likely have unintended consequences and cause more harm than good. One reason for this is the Federal Fair Credit Reporting Act. The FCRA gives insurers the power to prescreen a group of potential insureds by utilizing credit reports and credit data and any effort by the states to restrict that ability, is preempted by federal law. Companies that utilize direct solicitation methods and prescreen consumer records will essentially be unaffected by state attempts to ban the use of credit, but independent agency companies (which are used by our Alaskan members for their clients) will be prevented from using this powerful tool. This would create an uneven playing field for local independent agents and would do little to address the concerns that fuel the desire to enact such reforms. **Thus, AIIAB opposes all efforts to totally ban the use of credit or to regulate its use in an overly restrictive manner.**

Senate Bill 13, in its current form, is something we cannot support. However, we strongly urge you to consider the actions taken by the State Affairs committee in the House with CSHB47 (STA). This is a version our Association could support. By supporting a version similar to the House State Affairs language, we are hopeful a bill could be moved out this session thereby resolving the issue and relieving the legislature of the matter during the Second Session.

Independent Insurance Agents through out the State of Alaska are committed to working with yourself & your committee in finding an equitable solution that will foster a healthy competitive insurance marketplace while protecting the interest of the consumer.

Respectfully yours,


John N. Sweeney
President AIIAB

cc: Members of Senate Labor and Commerce Committee
AIIAB Lobbyist, John Walsh

Insurance Scoring 'Color Blind,' Says Arkansas Insurance Commissioner

04142003

Best's Insurance News

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OLDWICK, N.J. (BestWire) - Credit-based insurance scoring is a fair predictor of risk, said the president of the National Association of Insurance Commissioners, adding he doesn't expect the association to conduct a study on whether it has disparate effects on certain classes of people.

Mike Pickens, Arkansas insurance commissioner and NAIC president, said insurance scoring is valid and credible, pointing to a recently released University of Texas study showing a high correlation between credit scores and frequency, probability and degree of loss.

The study "was the first one not bought and paid for by an insurance company," Pickens said. "It basically legitimizes everything we heard. Why it works, I don't know, but it does work."

If people take care of their most important asset --their finances--they are likely to exercise the same amount of responsibility in other areas of their lives, Pickens said. They're also more likely, if they have a minimal loss, to pay for the loss themselves "because they have the financial wherewithal, rather than file a claim."

The NAIC has a task force, led by the Washington state and Oregon insurance departments, looking at insurance scoring. They've issued an educational brochure for consumers, and the efforts at the NAIC have been aimed at disclosure, Pickens said.

But funded consumer representatives at the NAIC want state commissioners to go further and determine whether the use of insurance scoring adversely impacts "minorities and other protected classes," he said. "It's a tough issue to get your arms or mind around. It could open up a lot of other legitimate underwriting criteria to scrutiny," he said.

Pickens said he was speaking as the Arkansas insurance commissioner. "Credit scoring seems to be a fairly color blind way of making a determination of risk," he noted. "When you look at credit you don't know what their ethnicity or age is."

A valid and credible study on whether the use of credit has a disparate affect on certain classes of people would involve polling consumers, he said. "I don't know if you'll see the NAIC pursue a study in this area because it's time consuming and costly and probably wouldn't be very constructive at the end of the day."

Insurance commissioners have taken a balanced and thoughtful approach on this issue, which is what's taken place legislatively in a majority of states, Pickens said.

The Texas University study helps demonstrate causality, but more needs to be done to explain why there is a correlation, he said. "Why is the primary question for regulators and legislators. They want more information on why. The Texas study didn't try to answer that question."

Speaking during an April 11 Deloitte & Touche presentation entitled "Credit Scoring: The Regulations, the Models and the Alternatives," Pickens said a "great deal" of legislative activity is going on in the states this year concerning the issue of insurers' use of credit information in underwriting.

Some 41 bills on the subject have been introduced in legislatures around the United States, he added.

In his home state for example, two bills were introduced in this legislative session. One was based on a model bill approved by the National Conference of Insurance Legislators. Pickens said his department worked with the Independent Insurance Agents & Brokers, and the American Insurance Association.

But another legislator wanted to place a total ban on the use of credit information for personal passenger automobile insurance rates, along with other credit information-related restrictions, Pickens said.

What ended up being passed by the Arkansas legislature was a bill that sets "pretty reasonable standards on the way credit scoring is used," and one with which independent agents and insurance companies are comfortable, Pickens said.

As in Arkansas, the scope of the bills introduced around the country varied. Pickens said many states started out with legislation that was pretty restrictive, "but most states have done something reasonable and come up with something close to the NCOIL model," he said.

Part of the reason for the consumer outcry and flurry of legislative activity, not only this year, but for a few years, is that insurance companies didn't do a good job of educating consumers or agents prior to using credit information in underwriting, Pickens said.

"The industry didn't educate consumers and agents as they should have," Pickens said.

Regulators would be open to other predictive variables besides insurance scoring if insurers explain what it is and why it works, he said. But if the industry is not open to more regulation and scrutiny.

(By Dennis Kelly, Washington bureau manager, BestWeek: Dennis.Kelly@ambest.com)



National Association Of Professional Allstate Agents, Inc.

www.napaausa.org

TO: Edward M. Liddy

Chairman and Chief Executive Officer

and

Allstate Insurance Company

2775 Sanders Road

Northbrook, Illinois 60062

FROM: National Association of Professional Allstate Agents (NAPAA)

Janice Mathison, Executive Director, NAPAA

Association Management Specialists

DATE: September 27, 2002

Dear Mr. Liddy:

We, the National Association of Professional Allstate Agents ("NAPAA"), its executive director Janice Mathison, and its management company Association Management Specialists, apologize for the improper and wrongful transmission of e-mails purporting to originate from "Eliddy@allstate.com" to more than 150 Allstate agents on or about October 12, 2001. The e-mails were plainly improper, should not have been sent, and originated from NAPAA's computer and NAPAA's e-mail account by an employee of NAPAA's management company, Association Management Specialists. Allstate did not authorize the e-mails. Although NAPAA maintains it did not approve the false e-mails, NAPAA takes full responsibility for the sending of unauthorized e-mails using Mr. Liddy's name. In this regard, NAPAA and Association Management Specialists have agreed to compensate Allstate for these false e-mails and also have agreed to enter into a consent injunction which bars any such further misconduct.

We acknowledge that the e-mails' designation of origin was false and misleading and highly inappropriate. The e-mails purported to come from Mr. Liddy, Allstate's CEO, and encouraged agents to advocate against the use of credit scoring in insurance at an insurance department hearing in Washington. We have understood at all times that Allstate favors the use of credit scoring, that Allstate believes credit scoring is important to its

business plans and that, in Allstate's view, it would be improper for agents to participate in the hearing without prior management approval. Prior to Allstate determining the e-mails' source of origin and demanding an acknowledgement of responsibility and apology, NAPAA took no steps to advise recipients that the e-mails had neither been sent by Mr. Liddy nor authorized by Allstate.

We cannot in any way condone this use of Allstate's trademark, its e-mail system, or its e-mail addresses, and we wish to assure you that we have taken steps to prevent any such use from occurring again.

Sincerely,

National Association of Professional Allstate Agents

By: *Jim Fish*
JIM FISH, President

By: *Janice Mathison*
JANICE MATHISON, Executive Director

Association Management Specialists

By: *Janice Mathison*
JANICE MATHISON, Member

Credit scoring is a useful tool for insurance companies; don't ban it

As an Alaska insurance agent, I am very concerned about proposed legislation that would ban the use of credit for setting insurance rates. Those who question credit's validity need only to look at the numerous studies that prove its accuracy in identifying people who should receive discounts because they will have fewer losses.

Your editorial of Jan. 26 brings up some valid points on the use of credit for insurance scoring, such as medical catastrophes. These issues can be addressed with some reasonable limitations. However, the philosophy of "I don't like it or understand it, so let's ban it" ignores the irrefutable fact that it is accurate and helps to promote healthy competition in the insurance industry, something Alaska desperately needs.

Let's not allow the government to pass another law to restrict business, especially a law that will prevent insurance companies from identifying people who should be rewarded for responsible behavior. If any of these bills pass, those who will suffer will be consumers and small-business owners like me.

-- Devery Prince

Anchorage

Credit scoring rewards consumers who will incur fewer losses

As an insurance agent who takes pride in providing my customers with outstanding service and fair rates, I was disappointed by your editorial ("Credit scoring: either reform or abolish this insurance shortcut," Jan. 26) endorsing legislation banning the use of credit to set insurance rates.

The reason credit is a predictor of risk is not "magic." Numerous scientifically designed studies and data from the industry have proven the connection between a person's credit history and the number of losses they will incur. The way a person cares for their finances can reflect the way they maintain their homes, and taking financial risks can mirror risky behavior in activities such as driving. Why would the industry use it if it wasn't accurate?

Credit scoring will allow an insurance company to reward consumers who will have fewer losses with lower rates. If we have found an accurate predictor so we can offer those discounts to the majority of our customers, why should it be taken away by the Legislature? That seems highly unfair to those people who are responsible and deserve good insurance rates. People with responsible behavior should not have to subsidize the insurance rates of those who are irresponsible.

-- Stan Tebow

Palmer

Attached below is the link

<http://www.adn.com/letters/story/2599476p-2646324c.html>

Web posted Monday, February 24, 2003

Credit scoring powerful tool for predicting risky behavior

By Devery Prince
For the Journal

Centuries ago, anyone with a new idea that went against popular belief was shunned by society or its leaders. It didn't matter if they could prove their idea; the fact that it went against the beliefs of the day made it detestable to those who wanted to maintain the status quo. A well-known example is Galileo, who was sentenced to prison for writing that the earth is not the center of the universe.

Today, some members of the state legislature appear ready to eliminate insurance companies' ability to use credit information for insurance scoring simply because they don't understand it. The fact is numerous studies have proven that using certain information contained in credit reports is an accurate predictor of insurance losses.

Two of the largest statistical consulting companies, Tillinghast-Towers, Perrin and Fair, Isaac have both published studies showing a statistically significant correlation between credit scores and insurance losses. Studies such as these employ statistical analysis methods similar to those used by universities, scholars, laboratories, businesses and a host of other groups for their research.

If you discredit the studies proving the accuracy of the use of credit scoring, then millions of other studies must be invalidated because they all depend on similar mathematical models to determine relationships between factors. Opponents of the use of credit have yet to produce a single study that suggests that credit history is not a valid predictor of insurance losses.

Instead of looking at the compiled data and research on millions of insurance customers, the critics endlessly repeat statements that have no credible evidence or studies to back them up. The volume of evidence compiled by insurance and independent research companies overwhelms the anecdotal reports being fed to the unknowing public by those opposed to credit scoring.

The bottom line is that the insurance industry wants to be able to use the tools that will allow customers to pay premiums that accurately reflect their risk of loss. Just like factors such as age, marital status, gender, driving record, miles driven and car type, an insurance score based on credit has proven to be very accurate in predicting the likelihood of insurance losses. If these weren't valid predictors, the insurance industry wouldn't use them.

Credit is, as proven by studies and industry data, the single most powerful predictor of future loss and aids the industry in fairly and accurately pricing insurance for consumers.

Banning the use of credit will take away the ability of insurance companies to identify responsible customers who should be rewarded with lower premiums. Instead, those

responsible customers will have to pay higher premiums to subsidize those who are more likely to incur a loss.

Is it fair to use unproven accusations against the use of credit simply because someone doesn't understand it or because it is new? The unfortunate victims of this campaign will be those whose good insurance scores show that they are less likely to incur losses, and yet will be forced to pay more because this accurate factor cannot be considered.

Make no mistake: Someone will pay for the costs. The difference is that some legislators want one group to subsidize another group in the form of higher premiums, and insurance companies just want to reward those who are less likely to incur losses.

Devery Prince is the principal of Anchorage-based Devery Prince Agency, which provides insurance to individuals and businesses across Alaska. He can be reached at 907-279-9000.

Web posted Friday, February 14, 2003

Level playing field

House Bill 47, which would disallow the use of credit information in insurance underwriting and rating, is being considered in the House State Affairs and Labor and Commerce committees. If passed, this bill (as well as companion bills HB 5 and SB 13) will have the unintended effects of reducing the level of competition in Alaska's insurance market and raising premiums for many consumers.

The use of certain credit information, in conjunction with other underwriting factors, has proven to be highly predictive of future losses. Scientific studies show time and again a correlation between credit score and the likelihood of future claims. This information is an invaluable tool in helping insurance companies choose their business and price their products appropriately. Assessing risk accurately and collecting adequate premium is critical to insurers' abilities to maintain financial stability and solvency, without which they cannot deliver on the claims promises they've made to their customers. Using effective predictors, like credit score, also allows insurers to offer lower premiums to customers who pose lower risk.

Just as with traditional underwriting criteria, insurers have the legal ability to choose how they use credit information to place business and position themselves in the marketplace. These differences between the companies are the very essence of competition, and result in greater choices for consumers.

If passed, HB 47 will competitively harm local insurance agents like myself. While I will be unable to use credit information to favorably place a policyholder at a fair price, HB 47 will not stop direct mail and phone solicitation companies - primarily out-of-state insurers - from collecting lists of consumers with high credit scores and offering policies based on that information. Driving insurance business to out-of-state companies that don't have to play by the same rules hurts Alaska's local business people and consumers.

Reuben Willis
Juneau

COMPASS: Points of view from the community

By RICHARD L. LOWELLEllen Goodman
comment

(Published: February 24, 2003)

Insurance crisis demands attention

As a veteran insurance broker with 26 years of experience in Alaska, I am alarmed by the never-before-seen insurance crisis in our state with regard to the large number of personal-lines companies ceasing to do business in Alaska. My fear is that, if this trend continues, the effects will be disastrous for consumers, our businesses and, ultimately, our economy. That is why it is imperative that we examine what the Legislature is proposing very closely while there is still time to make corrections.

As evidenced by three bills in the Legislature, a recent concern is the use of credit scoring to obtain a proper insurance rate. While all of us know of isolated circumstances where credit scoring may have had a negative impact on an individual consumer, the hard reality is that if the Legislature does not allow insurance companies to use some sort of credit scoring as a tool in conjunction with other guidelines, they will cease doing business in Alaska. This will reduce even further the number of insurance companies operating here.

The benefit to consumers of the use of credit is that those who will have fewer losses can be more easily identified and rewarded with discounts. Credit is another predictive factor such as age, marital status, gender and type of car. Good drivers should not be made to unfairly subsidize poor drivers.

I believe that a compromise is needed between the insurance companies and the Alaska Division of Insurance. It is critical to ensure that both consumers and insurance companies are being protected and treated fairly. The past few years have been extremely difficult within the tumultuous insurance industry. Alaska has lost many national companies representing home and auto including Kemper, Fireman's Fund, AAA, United Pacific, Deerbrook, InsurQuest, Colonial, Windsor, Atlanta Casualty, Industrial Indemnity, Alaska Insurance Co. and Continental. In particular, the loss of two major home and auto companies, Fireman's Fund and Kemper, were especially difficult for the market. Fortunately, many of these customers went with Safeco, a company that uses credit scoring in addition to its other underwriting guidelines.

Another major concern is the hastiness of this legislation at a time when a new director of insurance is being selected. Ideally, the new director should be given time to get situated into the new position and work toward a compromise between the insurance companies and the Legislature.

The proposed bills to ban the use of credit scoring are very shortsighted. We need healthy insurance competition in Alaska. Banning the use of credit scoring will serve only to drive more companies from our state as well as take away a valuable, proven tool to set rates fairly. The Legislature should withhold any action until the new director of insurance achieves a compromise that benefits everyone.

Richard L. Lowell is an independent insurance broker with Ribelin Lowell and Co. in Anchorage.

Credit information helps insurance firms create fair rates for everyone

There has been much debate recently over the use of credit information by insurance companies. As a local insurance agent, I urge consumers to look at this issue in its entirety before considering elimination of a tool that results in lower premiums for many deserving people.

Insurers must assess potential risk when deciding whom to insure and how much to charge. The more accurately a company can predict future losses, the better able it is to match the level of risk to the premium that is charged. There are many factors that serve as predictors, and one that has proven highly accurate is credit score.

No one questions the fact that insurers charge younger drivers higher rates despite their individual driving records, or that discounts are offered to good students. Yet, the fact that responsible financial management might translate into responsible driving behaviors seems incomprehensible.

Whether we understand the correlation between responsible use of credit and the propensity to file claims is not really the issue; the issue is that the correlation exists, and to ignore something that benefits many consumers would be irresponsible.

In order to provide the best service at the most fair rates, insurers must use every tool at their disposal to make sure that lower-risk policyholders are not picking up the tab for those that present higher risk.

-- Curtis Green,
CLU, agent, State Farm Insurance
Anchorage

Credit scoring powerful tool for predicting risky behavior

Centuries ago, anyone with a new idea that went against popular belief was shunned by society or its leaders. It didn't matter if they could prove their idea; the fact that it went against the beliefs of the day made it detestable to those who wanted to maintain the status quo. A well-known example is Galileo, who was sentenced to prison for writing that the earth is not the center of the universe.

Today, some members of the state legislature appear ready to eliminate insurance companies' ability to use credit information for insurance scoring simply because they don't understand it. The fact is numerous studies have proven that using certain information contained in credit reports is an accurate predictor of insurance losses.

Two of the largest statistical consulting companies, Tillinghast-Towers, Perrin and Fair, Isaac have both published studies showing a statistically significant correlation between credit scores and insurance losses. Studies such as these employ statistical analysis methods similar to those used by universities, scholars, laboratories, businesses and a host of other groups for their research.

If you discredit the studies proving the accuracy of the use of credit scoring, then millions of other studies must be invalidated because they all depend on similar mathematical models to determine relationships between factors. Opponents of the use of credit have yet to produce a single study that suggests that credit history is not a valid predictor of insurance losses.

Instead of looking at the compiled data and research on millions of insurance customers, the critics endlessly repeat statements that have no credible evidence or studies to back them up. The volume of evidence compiled by insurance and independent research companies overwhelms the anecdotal reports being fed to the unknowing public by those opposed to credit scoring.

The bottom line is that the insurance industry wants to be able to use the tools that will allow customers to pay premiums that accurately reflect their risk of loss. Just like factors such as age, marital status, gender, driving record, miles driven and car type, an insurance score based on credit has proven to be very accurate in predicting the likelihood of insurance losses. If these weren't valid predictors, the insurance industry wouldn't use them.

Credit is, as proven by studies and industry data, the single most powerful predictor of future loss and aids the industry in fairly and accurately pricing insurance for consumers.

Banning the use of credit will take away the ability of insurance companies to

identify responsible customers who should be rewarded with lower premiums. Instead, those responsible customers will have to pay higher premiums to subsidize those who are more likely to incur a loss.

Is it fair to use unproven accusations against the use of credit simply because someone doesn't understand it or because it is new? The unfortunate victims of this campaign will be those whose good insurance scores show that they are less likely to incur losses, and yet will be forced to pay more because this accurate factor cannot be considered.

Make no mistake: Someone will pay for the costs. The difference is that some legislators want one group to subsidize another group in the form of higher premiums, and insurance companies just want to reward those who are less likely to incur losses.

Devery Prince is the principal of Anchorage-based Devery Prince Agency, which provides insurance to individuals and businesses across Alaska. He can be reached at 907-279-9000.

Click here to return to story:

http://www.alaskajournal.com/stories/022403/view_20030224012.shtml

Subject: Information for 4/22 Hearing on Credit - SB13


Date: Mon, 14 Apr 2003 21:23:32 -0400

From: Mark_Niehaus@progressive.com

To: jane_alberts@legis.state.ak.us

Please find attached data in support of Progressive Insurance's use of credit information for rating of auto insurance in Alaska. This same exhibit also includes the nine variables that the company uses in its credit algorithm. Both of these items were requested by the Labor and Commerce Committee during my testimony on April 8th. Thank you for your help, and feel free to call if there are any questions. Mark Niehaus
916-864-6024

(See attached file: Filing Credit Questionnaire ExB.doc)

 Filing Credit Questionnaire ExB.doc

Name: Filing Credit Questionnaire ExB.doc

Type: WINWORD File (application/msword)

Encoding: base64

PROPRIETARY AND CONFIDENTIAL

Progressive Financial Responsibility Model (A21)

Exhibit 1

Adjusted Pure Premium Data by Credit Score

Adjusted pure premium by coverage for each credit tier. In order to isolate credit from other rating variables, pure premium is adjusted for other rating variables.

<u>Credit Score</u>	<u>Adjusted Pure Premium</u>			
	<u>BIPD</u>	<u>COLL</u>	<u>COMP</u>	<u>PIP</u>
0-70	\$184	\$175	\$57	\$53
71-75	\$208	\$192	\$62	\$62
76-80	\$216	\$206	\$64	\$69
81-85	\$232	\$226	\$73	\$82
86-90	\$251	\$247	\$80	\$90
91-95	\$279	\$269	\$84	\$92
96-100	\$291	\$288	\$95	\$115
101-105	\$316	\$308	\$100	\$119
106-110	\$326	\$325	\$110	\$122
111-115	\$356	\$354	\$120	\$155
116-120	\$363	\$361	\$129	\$160
121-125	\$385	\$383	\$132	\$181
126-130	\$415	\$408	\$138	\$197
131-135	\$404	\$422	\$150	\$198
136-140	\$437	\$427	\$155	\$196
141-145	\$470	\$458	\$173	\$233
146-155	\$477	\$481	\$184	\$236
156+	\$476	\$552	\$202	\$252

Data Source

The Progressive A21 credit model was based on country-wide, new and renewal business policies, over a period from September 1998 through April 2001. Credit reports were ordered on the principal named insured at the time of new business quoting. If a credit report could not be obtained on the named insured, then credit was ordered on the eligible spouse. Loss performance was tracked from new business policy inception to either the last policy expiration date, cancellation date, or April 2001, whichever came first. The data set consisted of some 3.8 million credit reports.

Multiple Regression Model

In order to separate the correlation of loss performance to credit from other underwriting variables, a multiple regression model was used. Specifically, SAS PROC GLM was used for the multiple regression. The independent, or predictive, variables included both credit variables and non-credit underwriting variables. Specifically, the non-credit underwriting variables include prior coverage, lapse days, and certain prior claims. These non-credit variables are not used in calculating the ultimate credit score. Rather, they are included in the multiple regression as co-variates, in order to obtain accurate weights for the credit variables.

The initial set of candidate credit variables included only those which were shown to be predictive of loss performance in prior pre-screening analysis. Credit variables which were highly correlated with one another were iteratively removed from the regression model. Variables were retained in the model only if the correlation to loss performance was statistically significant. The end result of this process was a model which included nine credit variables, in addition to the non-credit underwriting variables.

To convert the multiple regression model to a credit scoring algorithm, the non-credit underwriting variables were simply dropped from the equation. The credit model was validated using a holdout validation data set independent of the data used to create the model.

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Progressive Financial Responsibility Model (A21)

Exhibit 3

Progressive A21 Score Calculation

The Progressive A21 proprietary financial responsibility score starts with a baseline score of 100. Points are added or subtracted based on the following variables:

Number of current satisfactory trades

missing	+22 points
0	+22
1	+11
2	+8
3	+3
4	+1
5+	0

Number of derogatory installment trades

missing	0 points
0	0
1 - 5	+8
6+	+16

Age of Person when earliest trade was opened (years)

<15	0 points
16 - 20	-9
21 - 25	0
26 - 30	+3
31 - 35	+7
36 - 40	+9
41 - 45	+12
46 - 50	+18
51+	+12

Number of Trades ever with Delinquency Rating 30 days late or greater

missing	-8 points
0	-8
1+	0

Age of Most Recent Auto Trade (months)

missing	+2 points
0 - 11	0
12 - 47	-7
48+	-9

Ratio of Revolving Trade Balances to Total High Credit for All Revolving Trades

0 - 9%	-6 points
10 - 19%	-4
20 - 39%	0
40% +	+4
missing (9998+) 0	

Ratio of Total Balances to Total High Credit for All Non Closed Trades

0 - 94%	0 points
95 - 99%	+3
100%+	+8
missing (9998+) +7	

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Progressive Financial Responsibility Model (A21)

Exhibit 3

Progressive A21 Score Calculation (cont'd)

Number of non-Insurance Inquiries

missing	-19 points
0	-19
1	-14
2	-10
3	-3
4	0
5	+3
6	+6
7	+10
8	+13
9 - 11	+20
12+	+34

Age of Oldest Trade Line (months)

missing	+16 points
0 - 12	+32
13 - 60	+18
61+	0

Progressive A21 Credit Data Adjustments

Loss Ratio: Incurred losses were capped at \$100,000 per claim.

Trade Lines: Excludes any trade lines which are identified on the credit report as disputed by the consumer. In addition, the trade line is not used in our scoring algorithm if the credit report indicates that a credit card is lost or stolen, or used by someone other than the authorized user, or if the ownership of the credit card is in dispute.

Total High Credit: Total High Credit is the credit limit for revolving trade lines, and the initial loan amount for installment trade lines. If the credit limit or initial loan amount is not available, then the highest balance in the history of the account is used. If the balance or the high credit amount exceeds \$35,000, then the trade line is not used. This is done to avoid having the ratio skewed by a mortgage loan, for example. Note that a consumer's total debt does not impact the credit score. The ratio is the same regardless of whether a consumer has a \$500 balance with a \$1,000 limit, or a \$5,000 balance with a \$10,000 limit.

Number of Non-Insurance Inquiries: The credit report displays which companies have ordered the consumer's credit report, and the purpose of the inquiry. The number of inquiries counted excludes insurance inquiries, promotional inquiries, account review inquiries and consumer inquiries to obtain their own credit report

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Progressive Financial Responsibility Model (A21)

Exhibit 4

**Progressive Financial Responsibility Formula
Diagnostic Statistics (SAS Output)**

UW_GROUP = the combination of non-credit underwriting variables.
 TRD_SATISFACTRY_CNT = Number of current satisfactory trade lines.
 INSTL_CUR_SEVDRG = Number of derogatory installment loans.
 CRED_AGE_CH = Age of person when earliest trade line was opened.
 TRD_30DPD_CNT = Number of trades ever with delinquency rating 30 days late or greater
 AUTO_YNG_MO = Age of most recent auto loan (months).
 REVL_BAL_HICRED = Ratio of revolving trade balances to total high credit for all revolving trade lines.
 NONCLOS_BAL_HICRED = Ratio of total balances to total high credit for all non-closed trades.
 NON_INS_CNT = Number of non-insurance inquiries.
 OLDEST_TRD_MO = Age of oldest trade line (months).

The GLM Procedure
 Dependent Variable: TIER_FACTOR
 weight: BASE

Source	DF	Sum of Squares	Mean Square	F Value	Pr > F
Model	67	2.6708698E+12	39863728044	133.36	<.0001
Error	4.85E+06	1.4500167E+15	298914776.6		
Total	4.85E+06	1.4526876E+15			

Source	DF	Type III SS	Mean Square	F Value	Pr > F
UW_GROUP	28	529528877080	18911745610.0	63.27	<.0001
TRD_SATISFACTRY_CNT	5	40400205459	8080041091.8	27.03	<.0001
INSTL_CUR_SEVDRG	2	24065656093	12032833046.0	40.26	<.0001
CRED_AGE_CH	8	134921420475	16865177559.0	56.42	<.0001
TRD_30DPD_CNT	1	26241731010	26241731010.0	87.79	<.0001
AUTO_YNG_MO	3	41909298939	13969766313.0	46.73	<.0001
REVL_BAL_HICRED	4	33264635459	8316158864.8	27.82	<.0001
NONCLOS_BAL_HICRED	3	7440582920	2480194306.7	8.30	<.0001
NON_INS_CNT	10	401978956984	40197895698.0	134.48	<.0001
OLDEST_TRD_MO	3	134514699735	44838233245.0	150.00	<.0001

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Progressive Financial Responsibility Model (A21)

Exhibit 4

Progressive Financial Responsibility Formula
Diagnostic Statistics (SAS Output) (cont'd)

Parameter		Estimate		Standard Error	t value	Pr> t
Intercept		99.02449933	B	2.04519568	48.42	< .0001
UW_GROUP	UNKNOWN	-17.18005470	B	5.74266688	-2.99	0.0028
UW_GROUP	NOP - _0	18.60955500	B	1.20707491	15.42	<.0001
UW_GROUP	NOP - _1	27.77092070	B	2.05169430	13.54	<.0001
UW_GROUP	NOP - _2	36.60055719	B	4.41292785	8.29	<.0001
UW_GROUP	0- _1_1	10.27552086	B	2.20003205	4.67	<.0001
UW_GROUP	0- _1_2	38.13899226	B	4.98745751	7.65	<.0001
UW_GROUP	0- _2_0	-15.71232002	B	1.39176358	-11.29	<.0001
UW_GROUP	0- _2_1	-4.56517301	B	2.05726338	-2.22	0.0265
UW_GROUP	0- _2_2	-0.73006433	B	4.64353283	-0.16	0.8751
UW_GROUP	0- _4_0	-18.64753652	B	1.26691665	-14.72	<.0001
UW_GROUP	0- _4_1	-8.03926534	B	1.76455554	-4.56	<.0001
UW_GROUP	0- _4_2	-4.94625074	B	2.82397274	-1.75	0.0799
UW_GROUP	1-30_1_0	4.52332703	B	2.04878234	2.21	0.0273
UW_GROUP	1-30_1_1	19.29928242	B	3.83865331	5.03	<.0001
UW_GROUP	1-30_1_2	44.03727445	B	8.18584460	5.38	<.0001
UW_GROUP	1-30_2_0	-10.38772021	B	2.35633834	-4.41	<.0001
UW_GROUP	1-30_2_1	2.99490648	B	4.49764010	0.67	0.5055
UW_GROUP	1-30_2_2	24.51300188	B	9.83392901	2.49	0.0127
UW_GROUP	1-30_4_0	-16.01595196	B	2.33100685	-6.87	<.0001
UW_GROUP	1-30_4_1	-0.48527095	B	3.72621197	-0.13	0.8964
UW_GROUP	1-30_4_2	6.45058137	B	8.46186175	0.76	0.4459
UW_GROUP	NOP - _3+	85.03037650	B	8.32859831	10.21	<.0001
UW_GROUP	0- _1_3+	61.93176410	B	10.11346364	6.12	<.0001
UW_GROUP	0- _2_3+	22.13727961	B	8.78956381	2.52	0.0118
UW_GROUP	0- _4_3+	6.77035919	B	5.78590630	1.17	0.2419
UW_GROUP	1-30_1_3+	64.65105808	B	15.02128547	4.30	<.0001
UW_GROUP	1-30_2_3+	28.77051663	B	17.50616538	1.64	0.1003
UW_GROUP	1-30_4_3+	35.80443131	B	14.91672406	2.40	0.0164
UW_GROUP	0- _1_0	0.00000000	B	.	.	.
TRD_SATISFACTRY_CNT	0	21.95625403	B	2.06546445	10.63	<.0001
TRD_SATISFACTRY_CNT	1	11.20957819	B	1.44308698	7.77	<.0001
TRD_SATISFACTRY_CNT	2	8.15421946	B	1.35756405	6.01	<.0001
TRD_SATISFACTRY_CNT	3	2.88370719	B	1.36411743	2.11	0.0345
TRD_SATISFACTRY_CNT	4	1.16991899	B	1.39069781	0.84	0.4002
TRD_SATISFACTRY_CNT	5+	0.00000000	B	.	.	.
INSTL_CUR_SEVDRG	0	0.00000000	B	.	.	.
INSTL_CUR_SEVDRG	1-5	7.68964088	B	1.06179405	7.24	<.0001
INSTL_CUR_SEVDRG	6+	16.45167308	B	2.33895957	7.03	<.0001
CRED_AGE_CH	< 15	0.98053516	B	2.60998990	0.38	0.7072
CRED_AGE_CH	16-20	-9.41188805	B	0.98221576	-9.58	<.0001
CRED_AGE_CH	21-25	0.00000000	B	.	.	.
CRED_AGE_CH	26-30	3.20624514	B	1.17660257	2.73	0.0064
CRED_AGE_CH	31-35	6.75904754	B	1.30889187	5.16	<.0001
CRED_AGE_CH	36-40	8.59457699	B	1.50344440	5.72	<.0001

Progressive Financial Responsibility Formula
Diagnostic Statistics (SAS Output) (cont'd)

Parameter		Estimate		Standard Error	t value	Pr> t
CRED_AGE_CH	41-45	11.85180279	B	1.80993088	6.55	<.0001
CRED_AGE_CH	46-50	17.76243095	B	2.26353919	7.85	<.0001
CRED_AGE_CH	51+	11.50617564	B	1.98431720	5.80	<.0001
TRD_30DPD_CNT	0	-8.10178990	B	0.86468600	-9.37	<.0001
TRD_30DPD_CNT	1+	0.00000000	B	.	.	.
AUTO_YNG_MO	MISSING	1.73704528	B	1.16761158	1.49	0.1368
AUTO_YNG_MO	0-11	0.00000000	B	.	.	.
AUTO_YNG_MO	12-47	-6.80873825	B	1.23074630	-5.53	<.0001
AUTO_YNG_MO	48+	-8.61030391	B	1.39628786	-6.17	<.0001
REVL_BAL_HICRED	0-9	-6.02356659	B	1.10018602	-5.48	<.0001
REVL_BAL_HICRED	10-19	-4.05405978	B	1.33411884	-3.04	0.0024
REVL_BAL_HICRED	20-39	0.00000000	B	.	.	.
REVL_BAL_HICRED	40+	3.72243091	B	1.09475013	3.40	0.0007

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Progressive Financial Responsibility Model (A21)

						Exhibit 4
REVL_BAL_HICRED	MISSING	-1.80313379	B	1.70477104	-1.06	0.2902
NONCLOS_BAL_HICRED	0-94	0.00000000	B	.	.	.
NONCLOS_BAL_HICRED	95-99	3.42232510	B	2.05319439	1.67	0.0955
NONCLOS_BAL_HICRED	100+	8.24543070	B	1.72153876	4.79	<.0001
NONCLOS_BAL_HICRED	MISSING	6.53727030	B	2.91061286	2.25	0.0247
NON_INS_CNT	0	-19.40273636	B	1.43584977	-13.51	<.0001
NON_INS_CNT	1	-13.75954578	B	1.42751858	-9.64	<.0001
NON_INS_CNT	2	-9.65052762	B	1.46534563	-6.59	<.0001
NON_INS_CNT	3	-3.43135712	B	1.53691354	-2.23	0.0256
NON_INS_CNT	4	0.00000000	B	.	.	.
NON_INS_CNT	5	2.84365181	B	1.78099339	1.60	0.1103
NON_INS_CNT	6	6.46549769	B	1.94148240	3.33	0.0009
NON_INS_CNT	7	10.33557603	B	2.12508397	4.86	<.0001
NON_INS_CNT	8	13.08241236	B	2.34425541	5.58	<.0001
NON_INS_CNT	9-11	20.36634574	B	2.00624963	10.15	<.0001
NON_INS_CNT	12+	33.95261132	B	2.00335467	16.95	<.0001
OLDEST_TRD_MO	0-12	32.22906129	B	1.92504724	16.74	<.0001
OLDEST_TRD_MO	13-60	17.66992096	B	0.97457299	18.13	<.0001
OLDEST_TRD_MO	61+	0.00000000	B	.	.	.
OLDEST_TRD_MO	MISSING	16.30627413	B	4.57908486	3.56	0.0004

NOTE: The X'X matrix has been found to be singular, and a generalized inverse was used to solve the normal equations. Terms whose estimates are followed by the letter 'B' are not uniquely estimable.

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March 28, 2003

Representative Bruce Weyhrauch
Chairman, House State Affairs Committee
State Capitol, Room 102
Juneau, AK 99801-1182

Re: House Bill 47
House Bill 5

Dear Representative Weyhrauch:

I am writing to you on behalf of State Farm regarding House Bill 47 and House Bill 5. I understand there is going to be a time limit for individual testimony, so I thought it might be helpful to provide some additional background information. To that end, I am enclosing herewith a copy of a March 5, 2002, letter I sent to Senator Stevens of the Senate Labor and Commerce Committee relating to the credit scoring legislation pending before that Committee last year. I am also enclosing herewith a copy of a work draft we reached agreement on last year with the sponsor of Senate Bill 320. Finally, I am enclosing herewith a copy of a brochure that explains State Farm's underwriting model.

I appreciate the opportunity the Committee gave to me to testify earlier this year. I was asked a number of questions during that hearing about studies that might show the effect of the use of underwriting scores based on credit by various insurers. There are a number of studies that are in existence. These include a recent review of various studies by the American Academy of Actuaries and most recently a study done by the University of Texas. I have enclosed copies of both of these documents for your review, as well as the very thorough study done by James E. Monaghan. I am sure you are also aware of the study done by the Alaska Division of Insurance as well as the Washington Division of Insurance.

The study by the University of Texas was based on 175,647 separate auto policies, which were transferred to Choicepoint. Choicepoint then provided credit scores for this sample of policies. This study found "there is less than a 1 in 10,000 chance that the relationship observed between credit score and relative loss ratio could be due to chance alone." The charts contained in this report vividly demonstrate the relationship between credit score and loss.

Senator Dave Donley
March 28, 2003
Page 2

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You are probably also aware that the issue of credit based insurance scoring has been before the National Association of Insurance Commissioners. We understand the NAIC recently asked to American Academy of Actuaries to review the recent studies mentioned above.

We continue to believe this tool to be a very valuable one and urge the Committee to allow its use. Should there be any further information we can provide to you, please let us know.

Sincerely,

LESSMEIER & WINTERS

By: 
Michael L. Lessmeier

MLL/caf

Rep Weyhrauch-01-MLLwpd.wpd

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March 5, 2002

Senator Ben Stevens
Chairman of Senate Labor and Commerce
State Capital, Room 119
Juneau, Alaska 99801-1182

Dear Senator Stevens:

I am writing to you on behalf of State Farm to express our concerns with CSSB 320, which is pending before the Senate Labor and Commerce Committee. State Farm presently writes approximately 24.4% of the automobile insurance premiums written in Alaska and 34.7% of the homeowner's insurance premiums written in Alaska. Many of the vehicles insured by State Farm in Alaska are insured by State Farm Mutual, a company owned by its policy holders. When its loss experience in Alaska has been better than anticipated, State Farm Mutual has returned significant sums to its Alaskan policy holders.

Over the last nineteen years, we have been involved in many issues that have come before the Alaska legislature. When providing input on legislation, we have sought to find a balance that allows the insurance market to compete freely and fairly, as we strongly believe consumers are best served by fair competition in the insurance market, just as in any other market. We have provided input to committees such as yours in light of the reality that affordable insurance is a basic necessity of modern life. Automobile liability insurance is required by law in Alaska. Homeowner's insurance is required as a matter of course to obtain home financing. It is hard to imagine a small business owner without liability insurance. Unless these coverages are freely available and affordable, they are of little use to those who need them. It is from this perspective that we provide the following comments to you on CSSB 320, which would prohibit the use of credit scoring in any aspect of insurance rating.

For many years insurers have used factors such as a person's age and driving experience to decide whether to insure that person and what premium to charge. Many studies have shown that an individual's credit history is an accurate predictor of the potential for future loss. Thus, insurers throughout the country have begun to use credit based scoring with other traditional underwriting factors to determine who to insure and what premium to charge. This allows an insurer to more accurately correlate risk with different levels of expected loss and to then match the price of its products with the expected cost of those products.

Senator Ben Stevens
Chairman of Senate Labor and Commerce
March 5, 2002
Page 2

Just as with the use of other traditional underwriting factors, the purpose of using additional factors such as credit based scoring is to match the price with the expected cost to insure the risk. We believe it fair for those who present a higher level of risk to pay a higher premium. We believe it also fair for those who present a lower level of risk to pay a lower premium. If we cannot accurately match price with the expected cost to insure the risk we cannot hope to achieve this basic fairness. The end result is that one group of policy holders through no fault of their own can end up subsidizing another. We believe such a result is inconsistent with the concept of personal responsibility and unfair to our policy holders as a whole. Yet this is the result the proponents of CS&B 320 apparently wish to achieve, as this legislation would prevent the use of this valuable tool.

State Farm does not presently use credit based scoring for purposes of setting rates in Alaska. In February of 2001 State Farm began to use an underwriting score which utilizes credit history along with traditional underwriting criteria to determine whether to accept new business. This underwriting score is used primarily to accept customers that would not otherwise be accepted and also to place customers in State Farm Mutual who would not otherwise be so placed. As a result of utilization of this tool new automobile insurance written by State Farm in 2001 in Alaska more than doubled. State Farm only uses this underwriting score to make the determination of whether to accept a new applicant, and then to place that applicant in the appropriate company. It does not use this underwriting score for rating purposes, to cancel insurance or for any other purposes. We are very concerned that this legislation would restrict the use of this important tool.

This bill was introduced on February 19, 2002. The Committee Substitute, which significantly broadens the scope of the credit scoring prohibition, was disclosed to us shortly before the bill was heard by the Transportation Committee on February 28, 2002. No one had any meaningful opportunity to examine or comment on the Committee Substitute before it was passed out of the Transportation Committee. We believe this is unfortunate, as the issues raised by this legislation are important to all insurance consumers.

This rush to legislate is not only unfortunate, but unnecessary, for there already is a comprehensive legislative scheme in place to protect Alaska insurance consumers from excessive rates and from unfair discrimination. Insurance rates in Alaska must first be approved by the Division of Insurance. AS 21.39.010 *et. seq.* provides regulatory authority to the Division of Insurance to prevent insurance rates that are "excessive, inadequate, or unfairly discriminatory. . ." AS 21.39.030 expressly prevents insurance rates from being excessive, inadequate or unfairly discriminatory. AS 21.36.090 prevents by making an unfair trade practice "arbitrary or unfair discrimination between insureds or property having like insuring or risk characteristics, in the premium or rates charged. . ." A similar prohibition is contained in AS 21.36.120. Any insured affected by a rate can appeal a rating action to the Division of Insurance under the provisions of AS. 21.39.090.

Senator Ben Stevens
Chairman of Senate Labor and Commerce
March 5, 2002
Page 3

To the extent that credit based scoring is being used in Alaska to set insurance rates, that use has been approved by the Division of Insurance. Such approval could only be given after a finding by the Division that the rate in question is neither excessive or unfairly discriminatory. If any insured is dissatisfied by the application of a rate, he or she can appeal that action to the Division of Insurance.

Given the protections already present in Alaska law, it is hard to see the justification for the rush to adopt the blanket prohibition of credit based scoring set forth in CSSB 320. Such a rush to judgment inevitably results in errors, particularly when one seeks to make changes to an industry that is already the subject of complex and extensive regulation by professional regulators. The dangers of such a rush to judgment are apparent from the Sponsor's Statement, which unfortunately contains a number of errors, which we have identified below.

The first error is that statement that a credit score has "EVERYTHING" to do with what one pays for automobile insurance. This statement is not verified by any data we are aware of and we do not believe it to be true. State Farm does not use credit based scoring to determine rates in Alaska. If it were to do so, the credit score would merely be one factor it would use to determine the appropriate rate. While we are not privy to what other companies do, we do not believe it common for other companies to base a rate totally on a credit score, nor do we believe the Division of Insurance would approve such a rate.

The second error in this statement is the claim that the Division of Insurance has a statutory mandate to prevent discrimination. The mandate is not to prevent discrimination, but to prevent "unfair" discrimination. For example, it is not unlawful to charge a higher premium to someone who presents a higher risk because of their poor driving record. Nor is it unlawful to charge a lower premium to someone who presents a lower risk, like someone who qualifies for the 55 or older discount of AS 21.89.025. Any time someone is placed in a higher or lower category of risk and charged a premium based on that category of risk there is arguably discrimination, but this is not the "unfair" discrimination which is what our statutes seek to prevent. It is difficult to see how credit based scoring causes "unfair" discrimination. If it did, its use would not be allowed by the Division of Insurance.

The third error is the claim that "credit has nothing to do with risk". This statement is disproved by numerous studies and our own experience. If you would like to review some of these studies, we would be happy to provide them to you. We believe it beyond reasonable dispute that there is a strong correlation between credit history and future loss performance.

The fourth error is the implication that credit scores are "many times inaccurate" and "difficult and cumbersome to correct". A Federal Act, the Fair Credit Reporting Act, provides numerous protections to consumers from the use of inaccurate information, including the right of notification that credit information is being used and the right to immediate correction. Any insurer that uses credit information to make a decision relating to an insured is required to so

Senator Ben Stevens
Chairman of Senate Labor and Commerce
March 5, 2002
Page 4

advise its customer and to furthermore advise its customer of how to obtain corrective action. Any information that is inaccurate, incomplete or unverifiable must be deleted.

The fifth error is the attempt to categorize those the author of this statement claims to be unfairly discriminated against. One must remember that credit based scoring is merely one factor used among many. It is used differently by different insurers. Those who are good risks will continue to be rewarded by the market, so long as the market is allowed to function freely. If the market is allowed to function freely, those who are poor risks will pay a premium commensurate with that risk, a premium which is approved in advance by the Division of Insurance.

It is difficult to respond specifically to anecdotal claims of unfairness without knowing the details of each situation in question. But we do know that the generalizations contained in the Sponsor Statement are not accurate. We do not believe it accurate to claim that any minority is unfairly discriminated against by the use of credit based scoring. To make such a claim is to also claim that any such minority does not responsibly manage their credit, a claim we believe is not supported. Nor is it accurate to claim that credit based scoring favors the wealthy. Credit based scoring does not consider income, but rather whether one responsibly manages his or her credit. Many lower income people do responsibly manage their credit and thus would not be adversely affected by credit based scoring.

We do not believe the implication that people without a credit history usually pay 25% more simply because of credit based scoring is accurate. Credit based scoring is typically used in connection with other factors to determine an appropriate rate. While this tool is used differently by different insurers, we are unaware of any support for such a blanket statement such as this. We likewise are not aware of any support for the implication that small business owners pay 40% more simply because of credit based scoring.

The sixth error we wish to respond to is the argument that Hawaii insurance premiums are among the lowest in the nation, somehow because Hawaii does not allow the use of credit history. We believe the decreases in Hawaii automobile insurance rates are due to significant reform of the Hawaii no fault law and to repeal of the take-all-comers law, which helped restore competition to the marketplace. None of these decreases had anything to do with lack of credit use.

We know of no logical connection between the level of insurance premiums consumers pay as a whole and credit based scoring. Insurance premiums are determined by the frequency of loss and the severity of loss. Credit based scoring has no effect on either. It simply provides insurers with one more tool to use to more fairly allocate the cost of insurance to those with the higher levels of risk. Conversely, those with lower levels of risk pay less.

Senator Ben Stevens
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Page 5

The seventh error we wish to respond to is the claim that the "insurance industry wants to utilize this easy method to raise rates." We again are not aware of any logical basis for this statement. We have a significant share of both the Alaska automobile and homeowner markets. We are not utilizing credit based scoring to raise rates. To our knowledge, no insurer has utilized credit based scoring to support a claim for across the board rate increases. Even if an insurer tried to make such a claim, we doubt if any regulator would approve it.

The final claim we wish to respond to is the claim that credit based scoring will make it more difficult and expensive for consumers to obtain insurance. That certainly has not been our experience nor has it been the experience of our policyholders. It is hard for us to understand how a tool that has proven to be an accurate predictor of risk and a tool that accordingly will allow insurers to more fairly allocate the cost of that risk will make it either more difficult or expensive for consumers to obtain insurance. The goal of a more fair allocation of the cost of risk is a goal that is in the best interests of all of our policy holders. This tool will help us achieve that goal.

As you consider this legislation, we hope you will keep in mind the fact that as set forth above, the insurance industry is already heavily regulated. Any rate changes already must be approved in advance by the Division of Insurance. It is already an unfair trade practice to unfairly discriminate. Clearly, there are adequate tools already in place to prevent an insurer from somehow misusing credit based scoring, which is the real concern of the sponsor.

We do not believe the intent of the sponsor is to prevent a more fair allocation of the cost of risk. Yet the effect of this legislation is to do just that. We strongly believe this to be contrary to the interests of our policyholders as well as to the vast majority of Alaska consumers.

We thank you for your interest in this legislation. Please let us know should you have any questions relating to this issue.

Sincerely,

LESSMEIER & WINTERS

By: _____
Michael L. Lessmeier

cc: Members of Senate Labor and Commerce Committee

Ribelin Lowell & Company

3111 C Street Suite 300 Anchorage, Alaska 99503
Phone 907-561-1250 In State 800-478-1251 Fax 907-561-4315

FACSIMILE TRANSMITTAL SHEET

DATE: January 31, 2003

TO: Con Bunde

FAX NUMBER: 907-465-3871

FROM: Richard I. Lowell

PAGES: 4

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Phone 907/561-1250 Fax 907/561-4315 In State 800/478-1251
e-mail: msurvey@ribeliplowell.com

January 31, 2003

Dear Senator,

As a veteran Insurance Brokerage with 26 years experience in the Alaska market, we are faced with a never-before-seen crisis in this state, with regards to the alarming number of companies ceasing to do business in Alaska. Our fear is that if this trend continues, the effects will be disastrous to the consumers, our businesses, and ultimately our economy. That is why it is imperative that action is taken now, while there is still time to make corrections.

A recent concern to the consumer and the insurance industry is the use of credit scoring to obtain a proper rate. While all of us know of isolated circumstances where credit scoring may have had a negative impact on an individual consumer, the hard reality is that if our Legislature does not permit companies to use some sort of credit scoring as a tool in conjunction with other guidelines, Insurance Companies will cease doing business in the State of Alaska. This will reduce even further the number of Insurance Companies providing all lines of insurance.

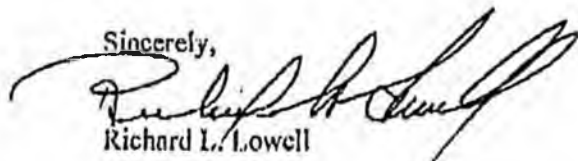
No one company will write every consumer. We must have a number of companies from which to choose. Without that diversity, there will be people in this state who cannot obtain insurance. While Alaska does have a state pool for auto, there is no such pool for homeowner insurance and other personal insurance.

We believe that a compromise is needed between the insurance companies and the State of Alaska Division of Insurance. We are striving to ensure that the consumers and insurance companies are being protected and treated fairly. As an Insurance Broker, the past two years have been extremely difficult within the tumultuous insurance industry. Alaska has lost many national companies representing home and auto, including Kemper, Fireman's Fund, Triple A, United Pacific, Deerbrook, InsurQuest, Colonial, Windsor, Atlanta Casualty, Industrial Indemnity, Alaska Insurance Company, and Continental. We have had to deal with the impact of losing two of our major home and auto companies, Fireman's Fund and Kemper. We were able to move the majority of those policies to Safeco Insurance Company, a company that utilizes credit scoring along with their various underwriting guidelines.

Another major concern is the selection of a new Director of Insurance. Ideally, a new Director is given time to get situated into his position and work toward a compromise between the Insurance Companies and the consumers.

We would ask that you postpone any legislative actions until a compromise is obtained between the Division of Insurance and the Insurance Companies.

Sincerely,



Richard L. Lowell

P.S. Attached is information on credit scoring.

The "real-world" experience of using credit information

➤ CONSUMERS BENEFIT REGARDLESS OF INCOME OR RACE:

It is unfortunate that anyone would assume that low-income or minority consumers manage credit poorly. A study by a major insurance company shows great similarity in the average credit score for all income groups. After much study, the National Association of Insurance Commissioners could not find any studies in the insurance field that demonstrates the use of credit history in underwriting an insurance risk has had a disproportionate impact on protected classes.

➤ CONSUMERS SUPPORT THE USE OF CREDIT REPORTS:

According to a Harris poll, nearly 70 percent of the public favors using credit information so financially stable people can pay lower premiums.

➤ CREDIT REPORTS ARE RELIABLE:

Studies by Arthur Andersen and the Insurance Research Council have found credit reports are much more reliable than motor vehicle records. Arthur Andersen found that only 2 percent of the 15,000 credit reports studied contain disputed information. Consumers also have a clearly defined review process to ensure the accuracy of their credit report.

credit

It provides an accurate
predictor of loss.

It fairly allocates the cost of coverage
based on a consumer's claim potential.

It provides an objective tool for
decision-making that does not
discriminate against any protected
class members.

It increases the availability and
affordability of insurance for consumers.

It allows insurers to underwrite
some consumers who would not
receive coverage using more traditional
underwriting criteria.

"What's Credit Got to Do With It?"

HOW PROPERTY AND
CASUALTY INSURERS USE
CREDIT INFORMATION
IN UNDERWRITING

➤ CONSUMER BENEFIT

Most people have good credit and this information may be beneficial. Good credit may enable you to qualify for lower insurance rates. In some cases it can even offset a less than perfect driving record.



National Association
of Independent Insurers



National Association
of Independent Insurers

Setting the record straight:

THE USE OF CREDIT HISTORY BY PROPERTY AND CASUALTY INSURERS.

As the practice of using credit information in connection with insurance has grown more common, a number of state legislators and consumer groups have expressed concern about its impact on consumers. However, major insurance companies and organizations such as Fair, Isaac and Company and Tillinghast-Towers Perrin have studied the issue and found data to support using credit history as a predictor of claim-filing. The Arizona and Virginia Insurance departments also have reaffirmed these findings through comprehensive studies of their own on the issue. After decades of use, insurance companies have found that using credit information can help them write more business and allow consumers to pay less.

How are credit histories used?

- > **TO MAKE WELL-INFORMED DECISIONS:**
Insurers are interested in having available as many tools as possible to assist them in making a fair and objective underwriting decision. Credit history provides a consistent tool to evaluate risk that does not discriminate against any specific group of customers. It actually results in every customer paying his or her fair share for insurance.
- > **ONE OF MANY FACTORS:**
Most companies that use credit information treat it as just one of several factors in the underwriting decision. Generally your credit rating alone is not likely to keep you from getting insurance or cause you to pay more for it, although it can help you get insurance.
- > **TO INCREASE BUSINESS:**
An NAII survey found that credit histories helped insurers write more policies. Companies said that they are able to accept some customers because the credit report offsets other information. One NAII member found that using credit histories enables it to charge 70 percent of its customers lower premiums than otherwise would be the case.

What is a credit score?

A credit score provides a numeric assessment of an individual's credit risk at a particular point in time. As new information is added to the report, the score can change. The score looks at specific credit information and assigns a weighted numerical value. It reflects credit payment patterns and looks at items such as collections, bankruptcies, outstanding debt, length of credit history, types of credit in use and the number of new applications for credit.

What's not included?

Only credit-related information is used in determining a score. The Equal Credit Opportunity Act prohibits the use of race, religion, gender, marital status and birthplace in determining a credit score.

What about privacy?

Most insurers only receive the credit score rather than the complete credit report. This protects the consumers privacy. Insurers are more interested in how well a consumer handles their assets rather than how much money the consumer makes or who they owe.

...continued on back page

As early as 1970, the U.S. Congress passed the Fair Credit Reporting Act (FCRA), which permits insurers to use credit information in making underwriting and rating decisions.

Statistical independent studies have proved a strong connection between credit history and the likelihood of an individual filing a claim.

Credit information is an objective tool for decision making. This tool avoids subjective value judgments because the information is based solely on credit-related material.

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OPINIONS

COMPASS: Points of view from the community

By RICHARD L. LOWELLEllen Goodman
comment

(Published: February 24, 2003)

Insurance crisis demands attention

As a veteran insurance broker with 26 years of experience in Alaska, I am alarmed by the never-before-seen insurance crisis in our state with regard to the large number of personal-lines companies ceasing to do business in Alaska. My fear is that, if this trend continues, the effects will be disastrous for consumers, our businesses and, ultimately, our economy. That is why it is imperative that we examine what the Legislature is proposing very closely while there is still time to make corrections.

As evidenced by three bills in the Legislature, a recent concern is the use of credit scoring to obtain a proper insurance rate. While all of us know of isolated circumstances where credit scoring may have had a negative impact on an individual consumer, the hard reality is that if the Legislature does not allow insurance companies to use some sort of credit scoring as a tool in conjunction with other guidelines, they will cease doing business in Alaska. This will reduce even further the number of insurance companies operating here.

The benefit to consumers of the use of credit is that those who will have fewer losses can be more easily identified and rewarded with discounts. Credit is another predictive factor such as age, marital status, gender and type of car. Good drivers should not be made to unfairly subsidize poor drivers.

I believe that a compromise is needed between the insurance companies and the Alaska Division of Insurance. It is critical to ensure that both consumers and insurance companies are being protected and treated fairly. The past few years have been extremely difficult within the tumultuous insurance industry. Alaska has lost many national companies representing home and auto including Kemper, Fireman's Fund, AAA, United Pacific, Deerbrook, InsurQuest, Colonial, Windsor, Atlanta Casualty, Industrial Indemnity, Alaska Insurance Co. and Continental. In particular, the loss of two major home and auto companies, Fireman's Fund and Kemper, were especially difficult for the market. Fortunately, many of these customers went with Safeco, a company that uses credit scoring in addition to its other underwriting guidelines.

Another major concern is the hastiness of this legislation at a time when a

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new director of insurance is being selected. Ideally, the new director should be given time to get situated into the new position and work toward a compromise between the insurance companies and the Legislature.

The proposed bills to ban the use of credit scoring are very shortsighted. We need healthy insurance competition in Alaska. Banning the use of credit scoring will serve only to drive more companies from our state as well as take away a valuable, proven tool to set rates fairly. The Legislature should withhold any action until the new director of insurance achieves a compromise that benefits everyone.

Richard L. Lowell is an independent insurance broker with Ribelin Lowell and Co. in Anchorage.

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February 20, 2003

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By Electronic Mail

The Honorable Con Bunde, Chairman
Senate Labor and Commerce Committee
Alaska State Capitol
Room 506
Juneau, AK 99801-1182

Re: Alaska Senate Bill 13

Dear Senator Bunde:

I am a partner in the law firm of Morrison & Foerster LLP, and have been a partner in this firm since 1976. My specialty is financial services and consumer protection law. More importantly for purposes of this letter, I have worked extensively on privacy-related issues, including questions under the federal Fair Credit Reporting Act ("FCRA"), for more than 25 years. In fact, I am the author of the leading legal treatise on this subject, *The Law of Financial Privacy*.

If enacted, Alaska Senate Bill 13 would prohibit an insurer or underwriter from basing a standard, rate, or rating plan, in whole or in part, directly or indirectly, on a person's credit rating or credit score. For purposes of this letter, I assume that the reference to a person's credit rating or credit score in Senate Bill 13 would include a rating or score derived from information in a "consumer report," as that term is used in the FCRA. That is, I assume Senate Bill 13 would prohibit an insurer or underwriter from basing a standard, rate, or rating plan on a consumer's credit rating or credit score, when that rating or score is derived from information in a consumer report.

Several provisions in the FCRA clearly contemplate that insurance companies may use consumer reports (including credit scores) in connection with insurance underwriting. In general, the FCRA provides that a person may obtain and use a

MORRISON & FOERSTER LLP

The Honorable Con Bunde
February 20, 2003
Page Two

consumer report for any "permissible purpose" provided for under the law. In particular, the FCRA states that a person may obtain and use a consumer report "in connection with the underwriting of insurance involving the consumer."¹ In addition to obtaining a consumer report in connection with insurance underwriting, the FCRA provides that an insurance company may obtain a consumer report in connection with insurance transactions that are not initiated by the consumer, so-called "prescreened" or "preapproved" transactions.² If a consumer report is used in connection with a prescreened transaction, the FCRA requires that a "firm offer of insurance" be provided to consumers who meet the criteria used to select consumers, along with certain disclosures.³

Based on my extensive knowledge and experience in this area, I have the following comments on the impact of the FCRA on Senate Bill 13, and, in particular, on efforts to restrict the use of consumer credit report information in insurance underwriting or rating decisions. The FCRA clearly contemplates that insurance companies may obtain consumer reports (including credit scores) in connection with the underwriting of insurance transactions. In fact, the Federal Trade Commission Commentary on the FCRA makes it clear that a person may obtain a consumer report in connection with the underwriting of insurance without the consumer's permission or even over the objection of the consumer.⁴ To the extent a state prohibits an insurer from obtaining or using a consumer report (including a credit score) in connection with the underwriting of insurance, the FCRA likely would preclude the enforcement of that state restriction.

More specifically, the FCRA, by its terms, generally prevails over inconsistent state laws, and directly preempts certain types of state laws.⁵ In particular, the FCRA clearly would preempt any state law that purports to prohibit the use of consumer report information to underwrite or select consumers for prescreened or preapproved offers of insurance, such as certain direct mail offers and telephone solicitations.⁶ Specifically, the FCRA provides that "[n]o requirement or prohibition may be imposed under the laws of any State" with respect to prescreenings of consumer reports.⁷ In addition, it is

¹ 15 U.S.C. §§ 1681b(a)(3)(C), 1681b(f).

² 15 U.S.C. § 1681b(c).

³ 15 U.S.C. §§ 1681b(c), 1681m(d).

⁴ 16 C.F.R. pt. 600, App., § 605--*General*, 2.

⁵ 15 U.S.C. § 1681t(a).

⁶ 15 U.S.C. §§ 1681t(b)(1)(A), 1681t(b)(1)(D).

⁷ 15 U.S.C. §§ 1681t(b)(1)(A), 1681t(b)(1)(D).

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Page Three

quite likely that the FCRA also would preempt a state law that purports to prohibit the use of consumer report information for underwriting consumer insurance applications, as well as prescreened solicitations.

In this regard, it is implausible that Congress would have given insurance companies greater latitude in using credit history information to underwrite insurance for consumers who have *not* applied for insurance (*i.e.*, recipients of prescreened offers of insurance), than to underwrite insurance for consumers who have actually completed and submitted applications for such insurance, or who are currently insurance policyholders. The establishment of more restrictive rules on the use of credit history information for insurance applicants or existing policyholders than those permitted under the FCRA for prescreened insurance offers would have the anomalous effect of encouraging insurance companies to use credit history information to underwrite people who have never applied for insurance because those insurance companies might be precluded from using that same credit history information for insurance underwriting purposes after those same individuals submit applications for the same insurance. Congress could not possibly have intended such a result.

Therefore, the FCRA clearly would preempt any state law that purports to limit the use of consumer report information to make prescreened insurance offers, whether such offers are extended by mail or by telephone. Also, I believe that the FCRA would prevail over an attempt to preclude the use of consumer report information when making an underwriting or rating decision in connection with applications for new insurance coverage or renewals of existing insurance policies. Thus, the FCRA clearly would preempt Senate Bill 13 with respect to the use of credit information to make prescreened insurance offers, whether such offers are extended by mail or by telephone. Also, I believe that the FCRA would prevail over an attempt to use Senate Bill 13 to preclude the use of credit rating or scoring information to underwrite or rate insurance, including whether or not to issue a policy for insurance sold within the state.

Should you have any questions regarding the scope of the FCRA, or its preemptive effect on state law, I would be pleased to discuss them with you.

Sincerely yours,

L. Richard Fischer
Morrison & Foerster LLP



**Statement of the
National Association of Independent Insurers
on the Use of Credit Information by
Personal Lines Insurance Companies**

March 25, 2003

This statement addresses the following issues:

- The legal authority for personal lines insurers' use of credit information
- The development and nature of credit-based insurance scores
- How the use of insurance scores achieves the fundamental goals of insurance underwriting and rating
- Answers to concerns about insurers' use of credit information

Legal Authority for Personal Lines Insurers' Use of Credit Information

The use of credit information by personal lines insurers is nothing new. For more than thirty years, federal law has authorized personal lines insurers to use credit information for underwriting and rating.

Fair Credit Reporting Act

The federal Fair Credit Reporting Act (FCRA) was enacted in 1970. The Act regulates the use of credit information about consumers. The FCRA specifies that consumer reporting agencies (also called "credit bureaus") may only provide consumer credit reports without written authorization for certain permissible purposes. One of the FCRA's express permissible purposes for providing a credit report is "in connection with the underwriting of insurance involving the

consumer.”¹ The FCRA defines “consumer report” to include a report to establish a consumer’s eligibility for “insurance to be used primarily for personal, family, or household purposes.”²

The use of credit information for personal lines insurance underwriting takes in a range of activities. For the purposes of the FCRA, “underwriting” includes the decision whether or not to issue a policy, the decision whether or not to renew or cancel a policy, the amount and terms of coverage, the duration of the policy, and the rates to be charged.³ A personal lines insurer may use credit information for all of these activities.

The FCRA imposes responsibilities on an insurer that receives credit information from a consumer reporting agency. The insurer must certify that it is obtaining the credit information for a permissible purpose.⁴ In addition, whenever insurance is denied or the charge for insurance is increased because of information contained in a credit report, the insurer must notify the consumer and must supply the consumer with the name, address and toll-free telephone number of the consumer reporting agency that provided the credit report. The consumer must also be advised by the insurer that the consumer has a right to a free copy of the credit report and may dispute the accuracy or completeness of any information in the report.⁵

State Laws

To some extent, the FCRA preempts state laws relating to the collection, distribution and use of credit information about consumers. The Act’s preemption of state laws has two aspects.

First, a state law is preempted if it is inconsistent with the FCRA.⁶ Generally, state laws are not inconsistent with the FCRA when the state laws provide greater protection to consumers.⁷ The question of whether a state law prohibiting insurers’ use of credit information is inconsistent with the FCRA has not been addressed by any reported court decisions.

Second, the FCRA lists a number of subjects on which states are preempted from imposing any requirement or prohibition.⁸ The list includes prescreening activities. “Prescreening” is the process whereby a consumer reporting agency compiles a list of consumers who meet specific criteria and provides the list to an insurer for the insurer’s use in making firm offers of insurance to consumers on the list. The preemption of state laws relating to prescreening remains in place until January 1, 2004.⁹

¹ 15 U.S.C. §1681b(a)(3)(c).

² 15 U.S.C. §1681a(d)(1).

³ FTC Official Staff Commentary on 15 U.S.C. §1681b(a)(3)(c).

⁴ 15 U.S.C. §1681e(a).

⁵ 15 U.S.C. §1681m(a).

⁶ 15 U.S.C. §1681t(a).

⁷ Credit Data of Arizona, Inc. v. Arizona, 602 F.2d 195, 198 (9th Cir. 1979)

⁸ 15 U.S.C. §1681t(b).

⁹ 15 U.S.C. §1681t(d)(2)(A).

Credit-Based Insurance Scores

Development of Insurance Scores

Although credit information was authorized for underwriting and rating personal lines insurance, credit reports were not widely used by personal lines insurers until the past few years. The major reason for the limited use of credit information was that many individual underwriters do not have the expertise to evaluate credit history as it relates to loss potential. The evaluation of the relationship between credit information and the likelihood of insured losses requires a high degree of analytical skill.

During the past decade, Fair, Isaac, ChoicePoint, and some insurance companies have developed systems which analyze how certain credit characteristics relate to loss ratios for automobile and homeowners insurance. Credit-based insurance scores are products of these systems.

The insurance scoring systems are based on analyses of the credit reports and loss ratios of millions of automobile and homeowners insurance policyholders. The analyses have produced mathematical models that weigh various credit characteristics based on how each characteristic relates to loss ratios. The models are used to generate credit-based insurance scores. Insurance companies use the insurance scores to help them make decisions, including whether to write a policy, whether to renew a policy, and what premium to charge for a policy.

The availability of insurance scores has given insurance companies the ability to use objective, highly skilled analyses of credit information in their underwriting and rating processes. The biases and limited expertise that individual underwriters brought to the examination of credit reports are eliminated by insurers' use of insurance scores.

Insurance Scores vs. Credit Scores

Insurance scores are different than credit scores. Financial institutions and other businesses use credit scores to evaluate the likelihood that a person will repay a loan or make payments on a credit purchase. Personal lines insurance companies use insurance scores to evaluate the likelihood that a person will have an insured loss.

Credit scores and insurance scores may consider some of the same items in credit reports, but the analysis of the credit characteristics is different. When the same item of credit information is considered by both a credit score and an insurance score, the credit score and the insurance score will give the item different weights. Credit characteristics are weighted differently because the purposes of the credit score and the insurance score are completely different.

The distinction between a credit score and an insurance score explains the situation where a person is able to find homeowners insurance coverage but is unable to qualify for a home loan because of his or her credit score and also the rare situation where a person qualifies for a home loan but his or her application for homeowners insurance is denied by an insurance company because of the person's insurance score. The credit score measures the likelihood that the person will make his

or her home loan payments. The insurance score measures the likelihood of future insurance losses based on an analysis of the person's past financial behavior.

Underwriting and Rating Goals

Credit-based insurance scores are not a departure from the fundamental goals of insurance underwriting and rating. Personal lines insurance companies use insurance scores to better achieve the goals of objectivity, completeness, equity, efficiency, and insurance availability.

Objectivity

Leaving the evaluation of credit report information to the judgment of individual underwriters can potentially produce inconsistent and unfair results. Insurance scores are based on objective, unbiased analyses of credit information. Insurance scores eliminate individual biases from underwriting and rating. Credit-based insurance scores have nothing to do with "gut feeling" and insurance scores have no "good days" and "bad days."

The objectivity that insurance scores add to the underwriting process does not mean that computers make underwriting decisions. An insurance score is simply a tool which underwriters use to help them make decisions which are consistent with the insurance company's underwriting standards.

Completeness

Insurance scores supplement other underwriting and rating information. They help to give a more complete picture of a risk of loss.

Some information which insurers use to make underwriting and rating decisions has limitations. Insurance application information is subject to concealment, misrepresentation and negligence. Studies have found that as many as 75% of all claims in the Comprehensive Loss Underwriting Exchange (CLUE) Auto and Property reports are not disclosed on insurance applications.¹⁰ It is estimated that incorrect information results in an overall 10% premium inadequacy.¹¹ Third-party data sources provide insurers with important information but they have some shortcomings. An Insurance Research Council study found that only 40% of the accidents which should have been in Motor Vehicle Records were actually there.¹² Even insurance claims records do not capture the complete picture of a person's accident experience. Some accidents are not entered into the CLUE system because no insurance coverage was involved. And not all insurance companies participate in the CLUE database.

¹⁰ D. H. Pillsbury, "Rough Notes System Establishes Link to Equifax," *Rough Notes*, March 1996, p. 3.

¹¹ D. Finnegan and S. Moffat, "Auto Insurance Pricing Crisis," *Quality Planning Corporation*, 2000.

¹² *Adequacy of Motor Vehicle Records in Evaluating Driver Performance* (Insurance Research Council, 1991).

Insurance applications, MVRs, and CLUE reports remain critical elements in insurance underwriting and rating. But that does not mean that these sources of information are complete. Insurance scores help insurers gain a more complete understanding of the risk of loss.

Equity

Insurers have a responsibility to continually refine their risk classifications and their rating procedures so that premiums reflect loss potential. In fact, competitive market pressures compel insurers to make sure that they use rates which are commensurate with the likelihood of loss. When rates do not reflect loss costs, some consumers must pay higher premiums to subsidize higher risk individuals.

There is an established relationship between credit-based insurance scores and loss ratio relativities. The reality is that aspects of a person's credit history correlate to the likelihood that the person will have an insured loss covered by his or her automobile or homeowners insurance policy. If insurers are forced to ignore this reality, the result will be pricing inequity. Many consumers will have to pay more than they should be paying because insurers are prevented from considering the consumers' true risk of loss.

Efficiency

Insurance scores make underwriting and rating more efficient. The availability of credit-based insurance scores streamlines the underwriting process and reduces costs. Ready access to credit-based insurance scores allows a company to decide that it will not order motor vehicle records or claim reports on new business applications above a certain insurance score, thereby saving underwriting costs. Or, an insurer may determine that it needs to focus more careful underwriting review and collect additional information on applicants who fall below a certain score.

By using insurance scores, insurers are able to make underwriting and pricing decisions quickly. This gives consumers immediate information for comparison shopping.

The efficiency and cost-saving which insurance scores provide allow insurers to hold down administrative expenses. Lower expenses result in lower premiums for consumers.

Availability

We surveyed a sample of NAII personal lines insurers on their use of credit information. A cross-section of members, ranging from large to small-sized insurers, participated in this survey. Survey results indicate that there are companies that currently use credit information to accept applicants, who probably would otherwise not be accepted for personal auto or homeowners insurance coverage. In addition, insurance companies are now renewing policies that probably would not be renewed, were it not for the use of credit information. Certain insurers have even stated that, as a result of using credit information, they are now more likely to write some cars and homes more aggressively, including cars and homes in urban areas.