



**Property Casualty Insurers
Association of America**

Shaping the Future of American Insurance

ALEX M. HAGELI
MANAGER, PERSONAL LINES

April 30, 2009

The Honorable Michael McRaith
Chair, The Property and Casualty Insurance (C) Committee
National Association of Insurance Commissioners
2301 McGee Street
Kansas City, MO 64108

The Honorable Kim Holland
Chair, The Market Regulation and Consumer Affairs (D) Committee
National Association of Insurance Commissioners
2301 McGee Street
Kansas City, MO 64108

RE: The Use of Credit-Based Insurance Scores

Dear Director McRaith and Commissioner Holland:

Thank you for this opportunity to comment on insurers' use of credit-based insurance scores. My name is Alex Hageli and I represent the Property Casualty Insurers Association of America (PCI). PCI is a national property casualty trade association comprised of more than 1,000 member companies, representing the broadest cross-section of insurers of any national trade association. PCI members write 39.6 percent of all personal lines insurance sold in the United States.

While PCI does not endorse the use of any particular rating factor, we do support the right of insurers to use actuarially justified rating factors. As such, we believe they should have the ability to use credit-based insurance scores.

The federal Fair Credit Reporting Act first authorized insurers to consider credit information nearly 40 years ago. Within the past 15 years, however, the use of credit information in insurance has grown substantially as insurers continue to perfect its use and appreciate its accuracy. Credit-based insurance scoring, alternatively referred to simply as insurance scoring, is an objective and accurate method for assessing the likelihood of insurance losses. Insurers that consider credit information in their underwriting and pricing decisions do so for only one reason – insurance scoring allows them to rate and price business with a greater degree of accuracy and certainty. Sound underwriting and rating, in turn, allows insurers to write more business – a direct benefit for consumers.

It is important to understand how insurers use credit information and to note that there are significant differences between the credit scores used by lenders and the credit-based insurance scores used by many insurers. Although both are derived from information found on credit reports, the information is measured differently. Insurers use credit information in developing insurance scores to predict the likelihood of future insurance loss. Credit-based insurance scores provide an objective measurement of how one manages the risk of credit. Lending institutions, on the other hand, use credit scores to determine the availability, amount and price of credit products offered to the consumer. Lending institutions use credit to determine the likelihood of repayment. The most significant difference between insurers and lending institutions is that insurers never consider income. Insurers measure “how,” not “how much.”

In addition to income level, one’s address, ethnicity, religion, gender, familial status, nationality, age and marital status are also not considered within a credit score calculation. Further, there is no reliable evidence that points to insurance scoring resulting in higher insurance rates for any specific class of individual, or that higher scores correlate with higher incomes. In fact, Federal Housing Administration Commissioner Brian Montgomery declared in speech last year that the administration’s data, if anything, tended to show that families with lower incomes actually have *higher* credit scores.

A 2003 study by EPIC Actuaries (now part of Tillinghast), the largest and most comprehensive study ever undertaken on the connection between credit history and insurance risk, found that a consumer's credit-based insurance score is unquestionably correlated to that consumer's propensity for auto insurance loss. Even more significantly, the study found that insurance scores are consistently among the most important rating variables used by insurers. The EPIC researchers used a multivariate analysis technique to determine indicated risk factors. After fully accounting for all overlap and relationship with other risk factors, such as age/gender, territory, model year, driving record and coverage limit – credit was found to clearly be an independent and significant tool for predicting insurance loss. The propensity for loss was found to decrease as the insurance score increases. For example, after adjusting for other variables, individuals with the lowest insurance scores were found to incur 33 percent higher losses than average, while those with the highest scores incurred 19 percent lower losses than average.

Every serious and reputable actuarial study on the issue, including a 2007 study by the Federal Trade Commission, has reached the same conclusion: there is a very high correlation between insurance scores and the likelihood of filing insurance claims. Without the ability to consider credit, many insurers would be less aggressive in their marketing, and far more cautious in accepting new business. Thus, consumers would quickly have fewer choices in the marketplace.

That consumers do in fact enjoy more choices in the marketplace is borne out by the massive double-digit percentage declines in the population of state residual markets over the past 10 years. While no definitive study of this phenomenon is available, it is the general consensus of the industry that the decrease is directly attributable to the increased accuracy afforded by the use of insurance scoring.

Not only do credit-based insurance scores allow insurers to offer more coverage, it also allows them to offer coverage at lower rates. The majority of consumers have good credit-based insurance

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scores and benefit accordingly – with rates refined to reduce disproportionate subsidies of higher risk individuals. An annual survey issued by the Arkansas Insurance Department consistently finds approximately 32 percent of policyholders enjoy a decrease in premium while approximately nine percent of policyholders pay more because of insurance scoring (the remainder being otherwise unaffected), a ratio of 3.44 to 1.

Credit-based insurance scoring is an effective tool for insurers - and a fair one for consumers. To protect competition and consumer choice, it is imperative that insurers be permitted to fully price risks using nondiscriminatory and statistically valid tools available to them.

PCI appreciates the opportunity to provide our comments on this bill, and would be happy to address any questions you may have on this subject.

Sincerely,

A handwritten signature in black ink, appearing to read 'A. Hageli', with a long horizontal stroke extending to the right.

Alex M. Hageli