PCI Property Casualty Insurers Association of America

Shaping the Future of American Insurance

Statement of Property Casualty Insurers Association of America On Credit-Based Insurance Scoring

September 14, 2009

Thank you for the opportunity to comment on insurers' use of credit information in the underwriting and rating of personal passenger automobile and homeowners insurance. My name is Alex Hageli and I represent the Property Casualty Insurers Association of America (PCI) -- a national property casualty trade association comprised of over 1,000 member companies, representing the broadest cross-section of insurers of any national trade association. PCI members insure 62.9 percent of the personal lines market in Wisconsin and 39.9 percent nationwide.

PCI strongly supports the use of actuarially justified underwriting and rating factors as the best way to assure fair and accurate insurance rates. Accordingly, we believe that insurers should have the right to use credit information in their underwriting or rating practices if they wish to.

The federal Fair Credit Reporting Act first authorized insurers to consider credit information nearly 40 years ago. Within the past several years, however, the use of credit information in insurance has grown considerably as insurers have continued to perfect its use and witness first hand just how accurate it is. Insurance scoring (also known as credit-based 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. Low credit scores do not correlate to a specific territory or class of individuals. On the contrary, both high and low scores are found across all income levels, and territories.

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. The study was based on a countrywide sample of nearly 2.7 million automobiles. 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, 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 most recently a report issued by the Federal Trade Commission in 2007, 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 there is more choice in the marketplace is borne out by the fact that state residual markets, including Wisconsin's, have seen double-digit percentage declines over the past five to eight years. It is the general consensus of the industry that this dramatic decrease in population is directly attributable to insurance scoring.

Credit-based insurance scores allow insurers to write business that they may not have accepted in the past, and to offer lower rates to many insureds. The majority of consumers have good credit-based insurance scores and benefit accordingly – with rates refined to reduce disproportionate subsidies of higher risk individuals. The Arkansas Insurance Department issues an annual survey of the use of insurance scoring that consistently shows approximately 33 percent of policyholders enjoying a discount because of that use, while only approximately 10 percent pay more.

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 matter, and would be happy to address any questions you may have on.

Alex M. Hageli
Manager, Personal Lines