NAIC Credit Hearings

Eric C. Nordman, CPCU, CIE
Director of Regulatory Services

NAIC
National Association of Insurance Commissioners

Agenda

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- Why the Controversy?
- Lay of the Land
- The NCOIL Model
- NAIC Public Hearings
- Regulation of Vendors
- Data Call
- Summary

Historical Perspective

- One of the most important developments to automobile and homeowner insurance underwriting and rating has been the increased use of credit-based insurance scores
- During the past 20 years, many consumer groups and regulators have questioned two things:
  - The reliability and predictability of the scores
  - Possible disproportionate or disparate impact on minority or low-income populations

Historical Perspective

- Credit-based insurance scores are derived through sophisticated mathematical models using credit-related variables in an attempt to determine an insured's propensity for risk
- Insurers argue that the use of credit-based insurance scores is necessary to properly evaluate risk and charge individual policyholders rates that most closely align with their true risk

Historical Perspective

- Credit-based insurance scores were initially used by insurers for underwriting – to decide whether to offer or limit coverage
- Only within the last ten years have insurers decided to also use the scores for pricing

Why the Controversy?

- Some regulators and consumers are concerned with how the use of credit-based insurance scores might affect policyholders:
  - Though there is some knowledge of what credit characteristics go into a score, the weighting of the characteristics and the formulas that make up the scores are unknown to regulators and policyholders
  - Others are concerned that scores may be correlated with income or other demographic traits that might otherwise be prohibited as risk classifications
  - Still others have observed that the recent economic downturn may have a detrimental effect on certain policyholders who have been adversely affected by the economy

Lay of the Land

- States have reacted to the use of credit-based insurance scores in a number of ways
  - 4 states have banned its use
  - 26 states have adopted the NCOIL Model or provisions from it
  - Most states have adopted laws, regulations or bulletins guiding insurer's use of credit-based insurance scores

Lay of the Land

- Typical provisions in state law or regulation include requirements:
  - To file the model with regulators
  - That restrict the use of certain factors
  - That prohibit penalizing consumers with no credit history
  - That prohibit insurers from using credit-based insurance scores as the sole criteria for underwriting or pricing
  - To make certain disclosures about the use of credit-based insurance scores

The NCOIL Model

- The NCOIL insurance scoring model requires:
  - Disclosure and use of updated, accurate credit data
  - Bans consideration of certain personal information
  - Mandates filing of scoring models
  - Prohibits data selling, among other things
- According to NCOIL, the bill's provisions help young people with "thin" credit files, seniors without credit cards, low-income and minority citizens who use credit differently, and other constituencies

The NCOIL Model

- Recently NCOIL adopted changes to its model regarding extraordinary life circumstances including:
  - Federal or state-declared catastrophes
  - Serious illness or injury to a consumer or his/her immediate family
  - Death of a spouse, child, or parent
  - Divorce or involuntary interruption of legally owed alimony or support payments
  - Identity theft
  - Temporary and involuntary loss of employment for three months or more; and
  - Military deployment overseas

NAIC Public Hearings

- April 30, 2009 (8 Hours)
- June 15, 2009 (2 Hours)
- September 23, 2009 (2 Hours)
- December 7, 2009
  - Discussed at Committee Meeting
- March 28, 2010
  - Discussed at Committee Meeting

NAIC Public Hearings

- An explanation of what constitutes a credit-based insurance score
- An explanation of how insurers use credit-based insurance scores
- A discussion on how current economic conditions have affected policyholder premiums related to credit-based insurance scores

NAIC Public Hearings

- There are two outcomes from the hearings:
  - A proposal to develop a model law to regulate vendors of credit information that provide services to insurers
  - A data call to obtain specific information regarding how insurers are using credit-based information to price and underwrite insurance and to gather information about other personal lines risk classifications

Regulation of Vendors

- The proposed model law would establish a regulatory framework similar to that in place for regulation of advisory organizations
- Insurance scoring vendors currently provide information to insurers that insurers use in both pricing and underwriting
- These vendors are not currently subject to regulation even though the information they provide to insurers is used to establish price, eligibility and coverage limitations in ways similar to the development of advisory loss costs by advisory organizations
- The model law would provide a regulatory framework for licensing and oversight of insurance scoring vendors.

Data Call

- Purpose of the survey:
  - Evaluate how insurers use credit-based insurance scores.
  - Determine how current economic conditions have affected policyholder premiums related to credit-based insurance scores.
  - Evaluate the role played by credit-based insurance scoring vendors.
  - Evaluate the use of new and innovative risk classifications and risk evaluation tools used by the industry and what impact these risk classifications have on consumer rates.

Data Call

- The current draft of the survey asks:
  - About the use of over 30 risk classification factors for personal auto insurance
  - For a range of rate relativities for each risk classification
  - For information about the distribution of risks in various ranges

Data Call

- There have been two regulator to regulator calls to discuss the survey instrument
- Another regulator to regulator call is scheduled for May 27, 2010
- Once the regulators reach agreement on the survey instrument, it will be exposed for public comment

Summary

- Regulators have mixed feelings about the use of credit-based insurance scores
- Regulators generally believe the scores correlate with insured losses
- The public hearing proved unsatisfactory to get the information sought by the regulators
- The data call is the next step in the process


Thank You!!!
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