Suggested Language for "A Consumer's Guide to Auto Insurance"

From the Center for Economic Justice, the Consumer Federation of America and the Michigan Insurance Consumer Advocate

August 15, 2010

In response to CEJ's comments of August 13, 2010, attached to these comments, Consumer Representative Brenda Cude asked for some specific language reflecting the CEJ comments. CEJ, CFA and the Michigan Automobile and Home Insurance Consumer Advocate offer the following as an example of language which informs and empowers consumers.

In the section of the guide "How Insurers Determine Your Premium," the working group's proposed language is:

- Your credit-based insurance score. Those with better scores often pay lower premiums. Some states restrict the ways insurers can use credit-based insurance scores.

> **Credit-based insurance scoring.** Most insurers use the information in your credit report along with other information to calculate a credit-based insurance score. They do this because studies show a correlation between this score and the likelihood of filing a claim. Credit-based insurance scores are *different* from other credit scores.

This language provides no information to empower a consumer regarding insurance credit scoring and very little information to even inform consumers about insurance credit scoring practices.

"Those with better scores often pay lower premiums." What does better mean? This provides no useful information to a consumer shopping for insurance.

"Some states restrict the ways insurers can use credit-based insurance scores." Which states restrict the use and how is the use restricted in those states? This provides no useful information to a consumer shopping for insurance.

"Most insurers use the information in your credit report along with other information to calculate a credit-based insurance scores." This is not accurate. Most insurers use credit scores derived with information only from credit reports. More important, this statement provides no useful information to a consumer shopping for insurance. It makes no difference if the insurer does or does not build a model based only on credit information or credit information supplanted with other information. This is an industry talking point – "credit is just one of many factors insurers use."

"They do this because studies show a correlation between this score and the likelihood of filing a claim." This is another industry talking point which provides no useful information to a consumer shopping for insurance. Of course insurers believe credit is correlated with claims – why else would legislatures and regulators permit its use?

"Credit-based insurance scores are *different* from other credit scores." This is the beginning of useful information, but, as stated, is an industry talking point instead of information that informs and empowers a consumer.

We suggest the following language for the section on insurance credit scoring and suggest that this type of approach should be used in other sections. We include in brackets and italics discussion of the proposed language.

> **Insurance Credit Scoring**
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> In most states, insurers may use information from your credit report to determine whether to offer you a policy and how much premium to charge you for a policy. As of August, 2010, insurers are not allowed to your credit report information for auto insurance in California, Massachusetts and Hawaii. *[This section uses plain language to explain what insurers do at a level meaningful to consumers. It also lists the states which prohibit the use of credit information – essential information for consumers living in those states. The language is specific and, unlike "some states restrict the ways insurers . . ., empowering to a consumer.]*
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> If permitted, most insurers obtain your credit report from a credit bureau (Experian, Equifax or TransUnion), pull selected information from the report and produce a score. Insurers call these credit scores "credit-based insurance scores" because these scores will be different from the credit scores you get when you try to borrow money. *[This section contains plain language to explain what insurers do and explains the important difference between an insurance score and a lending score.]*
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> Insurance credit scores have become one of the most important factors in determining whether an insurer will offer you insurance and at what price. The difference in premium associated with good and bad insurance credit scores can be very large – one consumer could pay twice as much or more than another consumer based only on the insurance credit score. *[This section contains vital information for a consumer about the importance of credit history in determining insurance premium.]*
>
> Insurers' use of consumer credit information is controversial. Insurers and some insurance agents' groups claim that insurance credit scores are fair because they are highly correlated with the likelihood of a consumer filing a claim. Consumer, civil rights and other insurance agents' organizations argue that insurance credit scoring is unfair

because it penalizes victims of economic catastrophes – job loss, high medical debt, divorce or identify theft – and that low-income and minority consumers have a disproportionate share of bad credit scores. For more information on the debate about insurance credit scoring, see the following links:

[NAIC Credit Scoring Hearings Page]

[House Financial Services Hearings Page]

[This section sets out the basic controversy about credit scoring and provides links to neutral sites for more information. This is the best way to address a consumer's skepticism about insurance scoring – as opposed to providing industry talking points]

There are many varieties of insurance credit scores. If you have a bad insurance credit score with one insurer, you are likely to have a bad insurance credit score with another insurer, but that may not be the case, so shop around. *[This section contains two pieces of vital information – credit scoring models vary among insurers and shopping around may help.]*

Some of the items included in insurance credit scores may include:

1. Late payments – late payments are bad, more late payments are worse, recent late payments are generally worse than older late payments.
2. When you first obtained credit accounts and how long you have had accounts – the younger you were when you first obtained credit and the longer you have had credit, the better.
3. Public records – bankruptcies and foreclosures are bad
4. Inquiries – an inquiry is when there is a request for your credit report by a lender because you are seeking a loan or other service. You get inquiries when you apply for loan, apply for insurance or apply for mobile phone or utility service, among other things. A lot of inquiries in recent years is bad.
5. Types of credit – some types of loans are good, while others are bad.
6. Amount borrowed – if your credit card has a limit of $5,000 and you owe $4,500, that's bad. Lower debt-to-limit ratios are good, higher debt-to-limit ratios are bad.
7. Number of accounts – A couple of bank credit cards is good, but a lot of department store and bank credit cards is bad.

[This section contains plain language which informs and empowers a consumer.]

When insurers want to use your consumer credit information, you have important rights guaranteed by federal and state law. Three of the most important rights are:

1. You must give the insurer permission to obtain your consumer credit report when you apply for insurance coverage. You may refuse to allow the insurer to obtain your credit information. However, if you do refuse, the premium offered you may be higher than if the insurer was able to evaluate your credit information. An insurer does not need your permission to obtain a new credit report if you are already a policyholder with the insurer.
2. If an insurer uses your credit information and, based on information in your credit report, denies you coverage or charges you a higher premium, the insurer must notify you that this “adverse action” occurred. This adverse action notice provides you information about which credit bureau to contact to get a free copy of your credit report and, usually, some of the reasons why the insurer took the adverse action. The reasons are usually a list of items in your credit report.
3. You have the right to correct errors in your credit report and have your insurer re-evaluate your credit information.

[This section contains important information to empower a consumer by setting out three important rights of the consumer.]

For a growing number of consumers, job loss, medical debt, divorce, identify theft and other “life events” can result in financial stress because of loss of income or dramatically increased expenses. In some states, some insurers will consider a “life event” exception when considering your credit history. For example, if you have a number of late payments on your credit report because of a life event, an insurer may give you an average credit evaluation instead of a bad credit evaluation. **If you have experienced a hardship which may have hurt your credit report, be sure to ask your insurer if they will consider a life event exception.**

[This section provides important information to empower a consumer and information particularly relevant given NAIC best practices on insurance scoring and recent changes to the NCOIL model law.]

Be wary of insurance credit scoring “discounts.” As described in the Discounts section, sometimes a “discount” does not mean a better-than-average rate. Regardless of whether your insurer is giving you a credit “discount,” be sure to ask if you are getting a better-than-average rate because of your credit information.

[This section provides important information to a consumer, when combined with the additional language on discounts, below, because of some insurers' practice of raising the base rate to the level charged for the highest premium and offering only "discounts" off that high base rate.]

Discounts *[This section should be prominently featured in the section on discounts]*

In auto insurance, a discount does not always mean you are being charged less than average. The premium offered to you by the insurance company is generally calculated by applying rating factors to the base rate. For example, young drivers may get a surcharge – pay more than the base rate – while 50-year old drivers may get a discount – pay less than the base rate. Here is an example using credit scoring:

Insurer A uses the average premium of $100 as the base rate. Half the drivers get a 25% discount (good credit score) while the other half the get a 25% surcharge (bad credit score). A discount is applied by multiplying the base rate by one less the discount percentage and a surcharge is applied by multiplying the base rate by one plus the surcharge percentage.

The premium charged to those with good credit scores is 0.75 times $100 = $75.

The premium charged to those with bad credit scores is 1.25 times $100 = $125.

Insurer B charges the identical premiums – half pay $75 and half pay $125, but decides to make its base rate $150 instead of $100. Insurer B now gives those with good credit scores a 50% discount and those with bad credit scores a 17% "discount."

The premium charged to those with good credit scores is 0.5 times $150 = $75.

The premium charged to those with bad credit scores is 0.83 times $150 = $125.

In the second example, even though all consumers are getting a "discount," half the consumers are really getting a surcharge and paying more than average.

When you ask your agent or insurance company about discounts, be sure to ask what the range of discounts is for that rating factor, if the discount you are getting means you are getting a better-than-average rate and, if not, why not. By knowing why you are not getting the most favorable rate or discount, you may be able to correct errors made by the agent or the insurance company or change your behavior so you can get the best discounts. *[This section provides critical information to help empower a consumer to understand and question how his or her premium charges are determined and to act on that understanding.]*

As mentioned above, the same approach could be taken with driving record, including an explanation of insurers' use of claims history databases and consumers' rights to obtain copies of those CLUE and similar reports.

Another example of information needed to inform and empower a consumer would be a section on what to do if you feel you have been treated unfairly. Given that very few consumers know that they can dispute an insurers' action or file a complaint with any regulator, a section like the one outlined below is essential.

If You Feel You Have Been Treated Unfairly – Consumer Complaints

[Describe the process for filing a complaint with the insurance department]

[Describe other avenues for filing a complaint, such as the state attorney general]

[For credit scoring complaints, also file with the Federal Trade Commission]

Subject: Consumer Guide to Auto Insurance
Date: Fri, 13 Aug 2010 14:23:42 -0400

Dear Commissioners,
A revised Consumers Guide for Auto Insurance will be presented to the C Committee for adoption in Seattle. CEJ has reviewed the document and we ask that some additional and important issues be added to the guide.

1. The guide does not discuss how or why a consumer can file a complaint with the regulator or otherwise protest or challenge a decision by the insurer regarding underwriting, rating or non-renewal.

2. The guide briefly mentions credit scoring, but makes no mention of the availability of life event exceptions allegedly offered by many insurers. Surely, this is vital information for consumers in a period of record foreclosures and bankruptcies and skyrocketing medical debt.

3. The discussion of credit scoring is very weak and one-sided and biased towards use of credit scoring. The document states "Some states restrict the ways insurers can use credit-based insurance scores." In fact, three states prohibit the use of insurance scores -- prohibition is quite different than restricting the ways insurers can use the score. There is no description of what is meant by restrictions and what such restrictions mean for consumers. There is not link to a list of restrictions by state, which is essential for consumers to make use of the information.

The additional verbiage -- those with better scores often pay lower premiums – is useless for consumers. What leads to a better score? The document states that most insurers use credit information and other information to calculate a credit-based insurance score. While some insurers combine credit with other information, such as losses, to produce a score, most scores are based only credit information. Moreover, what is the point of this statement? It does not help a consumer to know that some scores are based on credit and other information. Moreover, it is not relevant to the point at hand -- informing consumers that insurers use consumer credit information and how a consumer should be prepared to deal with that fact. The boxed entry regurgitates insurer talking-points -- the consumer guide should not be an insurers' advertisement for credit scoring.

Any description of insurance scoring should discuss, among other things, the presence of errors in credit reports and explain how consumers can identify errors, get the credit information fixed and get the policy re-rated.

In summary, the description of credit scoring is structured in a way to keep consumers in the dark about the use of and problems with credit scoring instead of informing consumers about the issues and providing links to resources to further educate and empower consumers.

4. The guide provides little information for how consumers can get help in shopping for insurance and that information is at the end of the document. The document should lead with a list of sources of more information on a variety of topics and the purpose of the additional

information should be explained. For example, the document's additional information includes getting a copy of the CLUE report or credit report. There is no explanation why a consumer should do so, what to look for in the free reports or what to do if errors are found.

The Consumer Guides working group has done good work to date on the consumer guide, but the guide needs some important additional information. We ask that C Committee return the document to the working group to address these important omissions.

Thanks for your consideration,
Birny Birnbaum
Executive Director
Center for Economic Justice