

MINUTES OF THE HOUSE COMMITTEE ON INSURANCE.

The meeting was called to order by Chairperson Patricia Barbieri-Lightner at 3:30 p.m. on January 21, 2003 in Room 527-S of the Capitol.

All members were present except: Excused: Nile Dillmore, David Huff, Joe Humerickhouse

Committee staff present: Renae Hansen, Ken Wilke, Bill Wolff

Conferees appearing before the committee: Mike McGrew - Chair, Credit Scoring Task Force

Others attending: 18 others, see attached list for those who signed the register.

Meeting was called to order by Chair Barbieri-Lightner. Credit Scoring Task Force presentation was heard.

Mike McGrew-Chair, Credit Scoring Task Force, introduced other task force members present: Linda DeCoursey, Bruce White, Vanda Easley, and Brad Smoot. Written Testimony was furnished to the Committee and copy of that testimony is (Attachment #1) attached. The task of the force was to do the homework, gather research, and put together a report that included recommendations and findings so that the Legislators could start at a higher point instead of having to do all the homework themselves. Bill language was not included, but recommendations are included with some conclusions. Included in the report also are some issues that they were not able to come to agreement on, with differing opinions and reasons attached in the report.

Questions were posed to Mr. McGrew and task force members present by Representatives Barbieri-Lightner, Phelps, Schwab, Goico, Kirk and Cox.

Thank you to Mr. McGrew and all members of the task force was extended.

Meeting Adjourned.

Next meeting January 23, 2003.

HOUSE INSURANCE COMMITTEE GUEST LIST

DATE: January 21, 2003

| NAME | REPRESENTING |
|--------------------------|--------------------------------------|
| Mike McGrew | Insurance Credit Scoring Task Force |
| Robert Choromanski | KTLA |
| Name Ann Power | KS Governmental Consulting |
| Kevin Davis | Am Family Ins. |
| David Hanson | KS Insur Assns + NAII |
| Jerry Wells & John Buntz | Ks. Dept. of Insurance |
| James Wilkerson | Formerly - KS Ins. Dept |
| Lee Wright | FARMERS- |
| Carol Lindsay | Farmers |
| Vanda Easley | State Farm - Ins. Scoring Task Force |
| Bruce White | Farmers Alliance Co's. - Task Force |
| Dr. Patricia Ann Smith | KID HIA |
| BILL YANEK | Ks Assn of REALTORS |
| Brod Smoot | AIA |
| Robert Choromanski | KTLA |
| D. H. Sizer | State Farm |
| | |
| | |
| | |
| | |



Credit Scoring Task Force

January 13, 2003

The Honorable Doug Mays
Speaker, Kansas House of Representatives
300 SW 10th Avenue, Room 380-W
Topeka, KS 66612

The Honorable David Kerr
President, Kansas State Senate
300 SW 10th Avenue, Room 359-E
Topeka, KS 66612

The Honorable Patricia Lightner
Chair of the House Committee on Insurance
300 SW 10th Avenue, Room 175-W
Topeka, KS 66612

The Honorable Ruth Teichman
Chair, Senate Committee on Commercial and
Financial Institutions and Insurance
300 SW 10th Avenue, Room 143-N
Topeka, KS 66612

Dear Senators and Representatives:

Pursuant to 2002 Senate Concurrent Resolution 1623, I am transmitting to you for your consideration the report of the Credit Scoring Task Force. This group was established to consider the desirability of regulation of insurance scoring practices for the benefit of Kansas consumers. The attached report was approved by all task force members.

Currently, the Kansas law does not provide specific statutory oversight of the usage of credit based insurance scores. It was the consensus of the Task Force that neither unfettered use of the credit-based insurance scoring nor total ban of credit-based insurance scoring is an appropriate remedy or outcome. Should the Kansas Legislature consider any legislation on the topic of credit-based insurance scoring, the report contains our recommendations.

Governor Graves appointed me to serve as Chair and consumer representative of the Credit Scoring Task Force. I would like to thank each of the Task Force members for their thoughtful work. I appreciate the courteous debate and discussions that were held, and am very pleased that we could come together and endorse the final report. I believe the report and recommendations should assist the Kansas Legislature in Educating Kansas consumers, as well as foster a healthy insurance market.

If you have any questions, please feel free to contact me at 1501 Kassold, Lawrence, KS 66047 Phone:785-843-2055; Fax: 785-838-8248 Email: MikeMcGrew@CBMcGrew.com

Sincerely,



Michael C. McGrew
Chair, Credit Scoring Task Force

House Insurance
Date: 1/21/03
Attachment # 1



Credit Scoring Task Force

REPORT OF THE CREDIT SCORING TASK FORCE

To the

Speaker of the House of Representatives

President of the Senate

Chair of the House Committee on Insurance

Chair of the Senate Committee on Financial
Institutions and Insurance

Chairperson: Michael C. McGrew

Vice-Chairperson: Marta Linenberger

Other members: Sens. Ruth Teichman and Paul Feleciano
Reps. Garry Boston and Jim Garner

Non-legislative members: Matt All, Tony Kimmi, Jim Harwood, Brad Smoot, Richard Turano, Bruce White, Vanda Easley, Cindy Hower and Duane Becker

Task force staff: Linda De Coursey, Brent Getty, and Jarrod Forbes

Date due: On or before January 13, 2003

Credit Scoring Task Force

CREDIT-BASED INSURANCE SCORES

CONCLUSIONS AND RECOMMENDATIONS

It was the consensus of the Task Force that neither unfettered use of credit-based insurance scoring nor total ban of credit-based insurance scoring is an appropriate remedy or outcome. The Task Force concluded after deliberations that Kansas law does not provide specific statutory oversight of the usage of credit based insurance scores, and that Kansas consumers need appropriate knowledge of the use of credit scores and how it impacts their insurance.

The Task Force recommends the following components be considered in any legislative language proposed. The Task Force:

- Recommends the FCRA definition of adverse action be interpreted as “anything other than the best possible rate”.
- Recommends addressing the importance of requiring insurers to advise and explain to consumers if credit-based insurance scores are used in underwriting and rating pursuant to standards established by the Kansas Insurance Department.
- Recommends requiring companies to file their credit-based insurance scoring methodology and formulas with the Kansas Insurance Department providing it is held confidential and as a trade secret under Kansas law.
- Recommends rules prohibiting use of credit information that is: identifiable disputed information; identifiable medical trade lines; items related to identity theft; information relating to income, gender, address, zip code, ethnic group, religion, marital status or nationality of the consumer.
- Recommends limitations on: use of the number of “hits” or inquiries on an individuals credit report; or “no hit or thin files” which are individuals with little or no information in their credit history.
- Recommends requiring the insurer to re-rate or re-underwrite a policy if wrong information is corrected on the consumer’s credit history for the shorter time frame of policy period or twelve months.
- Recommends insurers hold harmless agents, both captive and independent.
- Recommends a confidentiality section.

The following issues did not receive complete agreement. The Task Force believes these are key points the Kansas Legislature may wish to explore further. The differing opinions are presented in the report.

- Allowing the use of insurance credit scoring upon renewal.
- Consideration of internal company consumer appeal processes.
- Consideration of how credit based insurance scoring effects other lines of insurance than those considered personal, particularly with respect to the numerous family owned farms in Kansas.

BACKGROUND

In May 2002, the Kansas Legislature approved Senate Concurrent Resolution No. 1623 which provided for the formation of a Task Force to study the desirability of regulation of insurance credit scoring practices.

The Task Force consisted of 15 members appointed by the Governor, Commissioner of Insurance, President of the Senate, Speaker of the House of Representatives and the minority leaders of the Senate and House. The Governor appointed the Chair and the Vice-Chair of the task force.

The members of the Credit Scoring Task Force were as follows:

Chairman

Michael C. McGrew, Lawrence

Vice-Chairwoman

Marta Linenberger, Carbondale

Legislators

Sen. Ruth Teichman, (R-Stafford)

Sen. Paul Feliciano (D-Wichita)

Rep. Garry Boston (R-Newton)

Rep. Jim Garner (D-Coffeyville)

Insurance Department

Matt All, Assistant Commissioner,
Lawrence

Insurance Companies

Tony Kimmi, Kansas Association of
Property & Casualty Insurance Domestic
Companies Representative, Farm Bureau
Mutual, Manhattan, KS

Jim Harwood, Kansas Association of
Property & Casualty Insurance Foreign
Companies Representative, Farmers
Insurance Exchange, Overland Park, KS

Brad Smoot, American Insurance
Association Representative, Topeka, KS

Richard Turano, National Association of
Independent Insurers Representative
Allstate Insurance, Denver, CO

Bruce White, Alliance of American Insurers
Representative, Farmers Alliance,
McPherson, KS

Vanda Easley, National Association of
Mutual Insurance Companies Rep.
State Farm Insurance, Kansas City, KS

Agent Representatives

Cindy Hower, KAIA Representative
Kellerman Insurance, Holton, KS

Duane Becker, KAIA Representative
Charlton-Manley Insurance, Lawrence, KS

TASK FORCE ACTIVITIES

The Task Force is authorized by SCR 1623 to:

- Conduct a study of the desirability of regulation of insurance scoring practices for the benefit of Kansas consumers; and
- Issue a report containing the results of such study and the task force's recommendations and conclusions emanating therefrom.

The Task Force was directed to report the results of this study along with the recommendations and conclusions to the Speaker of the House, the President of the Senate and the Chair of the House Committees on Insurance and the Chair of the Senate Committee on Financial Institutions and Insurance, "no later than the convening of the 2003 Kansas Legislature..."

SCR 1623 was written without designating the Legislative Research Department to staff the task force. Linda De Coursey, Director of Government Affairs Division; Jarrod Forbes, Assistant to the Director of Government Affairs, and Brent Getty, staff attorney from the Kansas Insurance Department volunteered to assist the task force.

Meetings of the Task Force were held at the State Capitol Building in Topeka, Kansas on Friday, October 11, 2002; Friday, October 25, 2002; Monday, November 25, 2002; Wednesday, December 18, 2002; and Wednesday, January 8, 2003. Official corresponding minutes of the meetings can be found attached to this report.

At the first meeting of the Task Force, members determined the format for a series of meetings to appropriately determine the pros and cons of credit scoring.

In the course of its deliberations, the Task Force received testimony from: Eric Ellman, Consumer Data Information Association; Eric Rosenberg, TransUnion; Lynn Knauf, Alliance of American Insurers; Jeffery Skelton, ChoicePoint; Eddy Lo, Fair Isaac; Kathly Olcese, Allstate Insurance; Catherine Rankin, State Farm Insurance; Larry Magill, Kansas Association of Insurance Agents; Gary White, Kansas Trial Lawyers Association; Brent Getty, Staff Attorney at Kansas Insurance Department; and Ken Grotewiel, Director of Consumer Assistance Division at the Kansas Insurance Department.

Current Regulatory Authority

The Kansas Insurance Department currently has no direct regulatory authority over the use of credit scoring as an underwriting factor. Authority does exist to ensure that insurance companies do not discriminate against insureds in the setting of rates (K.S.A. 40-951, et seq). Using this authority over rates, the insurance department indirectly regulates credit insurance scoring.

Other State Laws and Models

In a report by the National Conference of State Legislatures (NCSL), legislation to address the use of credit by insurers was introduced in 30 states in 2002. According to NCSL, eight states passed laws. Maryland became the first state to forbid the use of credit in homeowners insurance, while Hawaii has barred the use of credit scoring on autos for many years. Most states, however, have looked for middle

ground. Arizona, Colorado, Idaho, Illinois, Maryland (for auto insurance), Minnesota, Missouri and Washington enacted measures that address specific concerns rather than outright bans.

The Model Act Regarding Use of Credit Information in Personal Insurance by the National Conference of Insurance Legislators (NCOIL) was distributed at the December meeting of the Task Force. The model act was adopted by the NCOIL Executive Committees on November 22, 2002. The model act was negotiated by the national insurance trades, agents association and the NCOIL staff.

In their deliberations for the conclusions and recommendations of this report, the Credit Scoring Task Force used some language from the NCOIL model. Some task force members endorse the NCOIL model, and oppose anything that extends beyond the scope of the model.

Credit Score = to determine credit worthiness (love for lending)
Credit Based Insurance Score = to predict future insurance loss
Credit Score vs. Credit-Based Insurance Score (for insurance)

A credit score is a computer generated number, calculated by a consumer credit reporting agency (credit bureau). There are three national credit bureaus: Equifax, Experian and TransUnion.

Presenters pointed out that confusion often exists with regards to credit scores. Credit-based scores are designed to determine credit worthiness, or rather the likelihood of delinquency or non-payment of credit obligations. Credit-based insurance scores are used to predict future insurance losses. While both types of scores use information from the consumer credit files, they are used for different purposes, one for lending, the other for insurance, and consider credit history differently.

Credit-based insurance scores are calculated from complex formulas that are developed based on specific factors in a person's credit history.

Elements built into a credit based insurance model often includes, but are not limited to: bankruptcy, late payments, factual account payment information such as personal finance, bank installments, bank revolving, department and other retail store accounts. What is NOT in the insurance model: nationality, age, religion, race, gender, location/address, net worth/salary, income, marital status and occupation. Other common exclusions or restrictions include: non-consumer inquiries, inquiries from insurance companies, medical collections and multi-inquiries from consumers shopping for home or auto loans.

Formulas used to calculate credit-based insurance scores are established, developed and maintained by companies such as Fair Isaac or ChoicePoint. Some insurance companies develop their own formulas for use on their own policyholders.

Presenters cited the Tillinghast-Towers Perrin study that indicated with most insurance scoring models higher credit-based insurance scores translate statistically into better insurance risks.

A summary of how an insurance credit score is calculated by an insurance company using an outside credit scoring source is as follows: The insurance company contacts a credit scoring company. The credit scoring company contacts the various credit reporting agencies to obtain information on an applicant or insured's credit history, using the insured's social security number. The credit scoring company's established model formula is applied to specific credit criteria factors obtained for the individual

from the credit reporting agency and an insurance credit score is calculated automatically. The insurance credit score is provided to the insurance company. They apply the appropriate discount based upon the company's predetermined tier discount underwriting standards.

Fair Credit Reporting Act

The Fair Credit Reporting Act (FCRA), 15 U.S.C. 1681, et. seq., enacted in 1970, allows insurers to use credit reports in insurance underwriting. Disclosure to the consumer is not required unless an adverse action is being taken.

The law requires credit bureaus to maintain maximum possible accuracy. The law prohibits those that furnish data to consumer reporting agencies from furnishing data they know is erroneous and requires them to correct and update the information. Consumers have a right to dispute information on their credit reports with consumer reporting agencies and the law requires dispute resolution in not more than 30 days (45 days in certain circumstances). If a dispute cannot be verified, then the information must be removed in the consumer's favor. Any reporting agency that violates any provision of the credit report law is subject to a private right of action.

Credit reports are accessible to all consumers and the FCRA prohibits a charge of more than \$9 for consumer disclosures unless the consumer is a fraud victim, unemployed and seeking employment, on public assistance, or has been denied credit or insurance on the basis of a credit report, in which cases the consumer is entitled to the credit report for free. The FCRA provides a clear framework of consumer rights for notice, access, and correction in inaccurate data.

The definition of a "consumer report" is any written, oral, or other communication of any information by a consumer reporting agency bearing on a consumer's credit worthiness, credit standing, credit capacity, character, general reputation, personal characteristics, or mode of living which is used or expected to be used or collected in whole or in part for the purpose of serving as a factor in establishing the consumer's eligibility for whatever reason. Secondly, the law refers to credit or insurance to be used primarily for personal, family, or household purposes (15 U.S.C. § 1681a.).

Under the Act, a consumer reporting agency may only provide a consumer report under certain circumstances, including the following two circumstances relevant to the insurance purposes: 1) In accordance with the written instructions of the consumer to whom it relates, or to a person which it has reason to believe... and 2) intends to use the information in connection with the underwriting of insurance involving the consumer. 15 U.S.C. § 1681b.

A consumer report under the Act may trigger additional notice requirements. Whenever any person takes an "adverse action" either in whole or in part on any information contained in a consumer report" shall: 1) provide oral, written or electronic notice of the adverse action to the consumer; 2) provide the consumer orally, in writing, or electronically (certain contact information of the consumer reporting agency); 3) provide to the consumer an oral, written or electronic notice of the consumer's right(s) to the disclosure of the copy of the consumer report and to dispute some report. 15 U.S.C. § 1681m.

The triggering event for the additional disclosure requirements by the "person" taking the "adverse action" means a denial

or cancellation of, an increase in any change for, or a reduction or other adverse or unfavorable change in the terms of coverage or amount of, any insurance, existing or applied for in connection with the underwriting of insurance. 15U.S.C. § 1681a(k)(1)(B)(i).

Task force members reviewed a letter from the Federal Trade Commission (FTC). The FTC was responding to a request for interpretation with regards to the underwriting of insurance and adverse action. The legislative history of this section causes the FTC to believe that Section 603(k)(1)(B)(i) of FCRA, 15 U.S.C. § 1681 a(k)(1)(B)(i) is to be read broadly. "It is the Committee's intent that, whenever a consumer report is obtained for a permissible purpose under section 604(a), any action taken based on that report that is adverse to the interests of the consumer triggers the adverse action notice requirements under section 615."

The informal opinion further stated that the insurer has taken "action that is adverse to the interest of the consumer" whether the consumer is quoted and then denied the lower rate, or a current policyholder or new applicant is considered for the lower premium and does not receive it. The insurer's determination places the consumer at a financial disadvantage, an act clearly adverse to his or her interests. Thus, the TFC believes the insurer must provide the Section 615(a) notice in these situations.

Industry Views on Credit-Based Insurance Scoring

Presenters pointed out the prevalence in the use of credit data as a part of the underwriting or rating process for homeowners and/or automobile insurance.

A nationwide survey found that 92 percent of the nation's largest automobile insurers use credit data to underwrite new business. More than 50 percent use credit data to determine the eligibility and rating classification. Over half of those largest companies began using credit data after 1998.

Coinciding with the rise in the use of credit as an insurance tool, the level of legislation and regulation of the use of credit by states has also risen.

Those companies dealing with credit based insurance scores state that such scores represent an objective and fair way of measuring likelihood of insurance losses. It is lawful, commercially accepted and statistically proven. It promotes competition by providing a tool that is scalable and actuarially sound, and lowers costs and can lead to more choices for consumers in the marketplace.

Companies believe that credit-based insurance scoring has a positive impact for a large portion of insurance consumers. They feel that restricting the use of credit-based insurance scoring would most likely create subsidization. Elimination of cross-subsidization is an important issue to both insurers and consumers. Individuals with better insurance scores would most likely pay more to offset the rates that would otherwise be charged to other individuals with poorer insurance scores.

Another issue presented was that restricting the insurer's ability to use credit insurance scoring could have a significant negative impact for the insurance market in the state of Kansas. According to insurers, the insurance market in Kansas is currently challenged with less competition and rising insurance costs. Restricting the use of

credit-based insurance scoring could potentially drive insurance carriers away from Kansas further challenging the Kansas insurance marketplace.

Agents Perspective

Consumers understand and accept the relationship between a bad driving record, claims, and other factors historically used by the industry to rate automobile insurance, but have a much harder time understanding the relevance of a "credit score". Especially when a bank agreed to lend them hundreds of thousands of dollars to buy a home, but an insurance company refuses to insure or treat them substandard for an insurance score the company can't or won't explain and the consumer doesn't understand.

Agents are very frustrated by their inability to explain to the consumer how the credit insurance scores are determined or how the consumer can correct the problem.

A survey was conducted of the membership of the Kansas Association of Insurance Agents. Within days over 147 responses were received (35% of the membership). Sixty-seven percent of the members answering the survey said that insurers only notify consumers that a score will be obtained. Sixty-eight percent indicated that only "some or "never" is the consumer told that their score resulted in a higher premium. Sixty percent of the time, credit scoring is "always or frequently" the only factor considered.

Agents included in this survey overwhelmingly support seeking reasonable statutory or regulatory control over credit-based insurance scoring in Kansas.

Kansas Trial Lawyers Association Perspective

The Kansas Trial Lawyers Association offered their perspective on credit insurance scoring practices. There is no unified voice to speak out on this issue for Kansas consumers. Consumer groups in other states, as well as on the national level, are sounding alarms about the negative impact the use of credit-based insurance scores has on consumers.

Concerns expressed about credit scoring relating to insurance are: 1) secrecy and lack of documentation provided by the insurance industry; 2) credit scoring unfairly discriminates against consumers; and 3) questionable accuracy of the information used in credit scoring.

When the insurance industry refuses to document any cause and effect relationship between credit score and driving ability, it is difficult to understand how a person who paid a bill late once will be any more likely to be hit by another driver or have a hailstorm ruin their roof.

Because of the concerns, the KTLA recommended that some type of regulatory authority be issued to safeguard Kansas consumers.

Kansas Insurance Department Consumer Data

On average, the Kansas Insurance Department's Consumer Assistance Division receives 60 to 100 calls a day from consumers on various issues. With the data system in place for filing complaints, there are several categories. The category where complaints would be about credit scoring is "premium and rating". Under the "premium and rating" category for the first 10 months of 2002, complaints for auto rates increased from 163 to 223 over the previous

comparable period in 2001. For the first 10 months of 2002, the complaints on premiums and rating for homeowners insurance increased from 70 to 141 over the previous comparable period in 2001. For all lines, complaints rose from 298 to 467. Unfortunately, the category does not reflect if all complaints contained a credit scoring issue. The data system does not provide detailed information other than “premium and rating”. Those files specifically having been tagged as involving a credit scoring issue were less than ten, however, it was believed there were substantially more. Without pulling all files in that category and reviewing them specifically, data would be inconclusive as to actual numbers.

Education Component

Some groups commenting before the Task Force discussed disconnects in the education component regarding the credit-based insurance scoring issue. It was suggested that to protect consumers, while not damaging the benefits of the credit insurance scoring, better agent education is needed and consumers need more information about the scores.

CONCLUSIONS AND RECOMMENDATIONS

The Credit Scoring Task Force (Task Force) received testimony on a variety of factors, as well as studied legislation recently passed around the country. The Task Force only received testimony on personal lines of insurance. To that purpose, “personal lines of insurance” means: private passenger automobile, homeowners, motorcycle, mobile-homeowners and non-commercial dwelling fire insurance policies.

The Task Force recommends the following components be considered in any legislative language proposed.

- *Adverse Action.* The Task Force recognizes the Fair Credit Reporting Act (FCRA) applies to the use of insurance scores, particularly when the insured has been adversely impacted. The Task Force agrees that “an increase in any charge for” from the FCRA language¹ should be interpreted as “anything other than the *best* possible rate”. This issue arose from testimony of how different insurers develop their rating and underwriting tiers. The Task Force believes this interpretation still fits the intent of FCRA while removing the possibility of ambiguity.
- *Information and Explanation to Consumer.* The Task Force also discussed how the insurer should inform and explain credit based insurance scoring to applicants and or insureds. The Task Force believes the consumer should be advised and informed if their credit history will be used when computing their underwriting risk and rating. The Task Force is comfortable with the consumer being informed through the same medium as the transaction of business or potential thereof. In the event an adverse action is taken against the consumer or insured the individual(s) should be adequately informed as to how their personal credit information influenced that decision. Pursuant to FCRA this notification must be oral, electronic or in writing.

¹ The FCRA defines “adverse action” to mean A denial or cancellation of, an increase in any charge for, or a reduction or other adverse or unfavorable change in the terms of coverage or amount of, any insurance, existing or applied for in connection with the underwriting of insurance. 15 U.S.C. § 1681a(k)(1)(B)(i).

However, with respect to the required written notification, the Task Force believes the Kansas Insurance Department, subject to the limitations of FCRA, should develop standards for the written notification along with reasonable parameters with which each company must comply. It is not the intent of the Task Force for the written notification to be uniform throughout the industry.

- *Company Methodology and Formulas.* Due to the lack of knowledge concerning the methodology utilized in creating an insurance score, the Task Force recommends the methodology and formulas should be confidentially filed with the Kansas Insurance Department and considered a trade secret.
- *Prohibitions.* The Task Force spent a great deal of time addressing what prohibitions should be placed on the insurance scoring methodology utilized by the industry. The following language was suggested: Any given insurer should not be allowed to use the following: a) disputed information identified as such on an individual's credit report or history, b) identifiable medical trade lines in a collection status that are reflected on an individual's credit report or history, c) adverse credit information that can be related to identity theft and is identified as such, d) an insurance score that is calculated using income, gender, address, zip code, ethnic group, religion, marital status, or nationality of the consumer. The Task Force recognizes there are factors in (d) that are currently permissible in the underwriting of policies. However, it is the intent of the Task Force to prohibit the use of such information only when

computing an individual's insurance score.

- *Limitations.* The Task Force addressed "hits" or inquiries on an individual's credit report or history that are not generated by the consumer's own activity, or are generated by the named individual in attempt to check their own credit rating and or score. The Task Force believes that such hits should not be considered at all. Multiples of any other related types of "hits" or inquiries within a thirty (30) day period should be considered as one "hit" or inquiry when computing the individual's insurance score.
- *Limitations.* There are individuals that are considered to have "no hit and or thin files". These individuals either have very little or no information in their credit history. The Task Force recommends that an insurer shall not: a) take an adverse action against a consumer solely because he or she does not have a credit card account, without consideration of any other applicable factor independent of credit information; b) consider an absence of credit information or an inability to calculate an insurance score in underwriting or rating personal insurance, unless the insurer does one of the following: 1) Treat the consumer as otherwise approved by the Insurance Commissioner, if the insurer presents information that such an absence or inability relates to the risk for the insurer; 2) Treat the consumer as if the applicant or insured had neutral credit information, as defined by the insurer; 3) Exclude the use of credit information as

a factor and use only other underwriting criteria.²

- *Corrected Information.* The Task Force recognizes the fact that errors can be present on an individual's credit report or history, therefore it believes if the wrong information is corrected the insurer should be obligated to retroactively re-rate and or re-underwrite the individual for the shorter time frame of the policy period or twelve (12) months upon written receipt that the credit report relied upon has been corrected.
- *Hold Harmless Clause.* The Task Force believes the following should be adopted on behalf of insurance agents, both captive and independent: An insurer shall indemnify, defend, and hold agents harmless from and against all liability, fees, and costs arising out of or relating to the actions, errors, or omissions of an agent who obtains or uses credit information and or insurance scores for an insurer, provided the agent follows the instructions of or procedures established by the insurer and complies with any applicable law or regulation. Nothing in this language shall be construed to provide a consumer or other insured with a cause of action that does not exist in the absence of this language.³
- *Confidentiality.* In recognizing the information needed to create an insurance score is derived from an individuals credit report and/or history;

² This language is taken from the National Conference of Insurance Legislators (NCOIL) Model Act Section 5.

³ This language was taken from National Conference of Insurance Legislators (NCOIL) Model Act Section 10.

the Task Force understands the importance of privacy and recommends the following be addressed regarding the sale of policy term information by consumer reporting agencies: A) No consumer reporting agency shall provide or sell data or lists that include any information that in whole or in part was submitted in conjunction with an insurance inquiry about a consumer's credit information or a request for a credit report or insurance score. Such information includes, but is not limited to, the expiration dates of an insurance policy or any other information that may identify time periods during which a consumer's insurance may expire and the term and conditions of the consumer's insurance coverage. B) The restrictions provided in section (A) does not apply to data or lists the consumer reporting agency supplies to the insurance agent from whom the information was received, the insurer on whose behalf such agent acted, or such insurer's affiliates or holding companies. C) Nothing in this language shall be construed to restrict any insurer from being able to obtain a claims history report or a motor vehicle report.⁴

The following issues did not receive complete agreement. The Task Force believes these are key points the Kansas Legislature may wish to explore further. For that reason, differing opinions are provided for each issue:

- *Viewpoint 1. Use of insurance scoring upon renewal.* The Task Force discussed whether the use of credit-based insurance scoring, specifically used at renewal, should be allowed. The

⁴ This language was taken from National Conference of Insurance Legislators (NCOIL) Model Act Section 11.

debate it had related to long-term existing business. The supporters of this viewpoint believe if credit based insurance scoring is valid during the application process, then insurance scoring should also be valid during the renewal process. The supporters also make the point that non-renewals and cancellations can be due to one factor (such as excessive claims) and that an individual's insurance score should not be treated any differently than any other given factor.

Viewpoint 2. Use of insurance scoring upon renewal. The disagreement is over current policies originating prior to the use of insurance scoring. The supporters of this viewpoint do not feel it is correct for the insurer to have the ability to terminate or non-renew based on credit information since credit information was not used when writing the original policy. The supporters of this viewpoint believe that if an individual has been a good risk for the insurer for the life of the policy to that point, then an individual's credit information should not change that position so drastically that the individual is canceled or non-renewed. They also point out the difficulty individuals have in finding coverage after being terminated or non-renewed.

- *Viewpoint 1. Consumer Appeal Process.* The Task Force explored the notion of an insured initiated review of their own insurance score. The language the Task Force used for their discussion was the following:

Consumers who are charged more based on their credit report should be able to request, at least annually, that the insurer run their credit score and *adjust accordingly* their premium if it has *changed*.

While many agree that individuals should do all they can to improve their insurance rates, supporters of this viewpoint, recognize the cost associated with an insurer running an individual's insurance score and do not want to burden the industry with every individual constantly asking for a new score.

Viewpoint 2. Consumer Appeal Process. The other opinion expressed is reflected in the following language:

Consumers who are charged more based on their credit report should be able to request, at least annually, that the insurer run their credit score and *lower* their premium if it has *improved*.

Essentially, the supporters of this viewpoint do not feel the insurer should be allowed to raise the rates of an individual who asks for their score to be run again. The thought is the insurer would not have known the individual's score had negatively changed if it were not for the insured requesting a new score. Furthermore, they believe individuals will not ask for a new score if they know it may negatively affect them and that individuals should be encouraged to do all they can to improve their rates.

- *Viewpoint 1. Extraordinary circumstances appeal.* The Task Force discussed an appeals process for the insured, through the insurer, in the event of extraordinary circumstances. One viewpoint is reflected in following language:

Insurers *may* offer reasonable underwriting exceptions if an extraordinary personal circumstance adversely impacts a

consumer's/insured's credit history, provided that any exceptions made or not made under such a process will not be deemed a non compliance with an insurer's filed rules and rates, or any other provision of Kansas law.

View point 2. Extraordinary Circumstances Appeal. However, the second view point would like to replace "may" with "must" which would require the insurer to establish an extraordinary circumstances appeal.

Insurers *must* offer reasonable underwriting exceptions if an extraordinary personal circumstance adversely impacts a consumer's/insured's credit history provided that any exceptions made or not made under such a process will not be deemed a non compliance with an insurer's filed rules and rates, or any other provision of Kansas law..

- o *Viewpoint 1. Scope applicable to only personal lines of insurance.* The Task Force received testimony only on credit-based insurance scoring on personal lines of insurance. Personal lines means: private passenger automobile, homeowners, motorcycle, mobile-homeowners and non-commercial dwelling fire insurance policies. Some members of the Task Force were reluctant to agree with making a recommendation that credit-based insurance scoring legislation be applicable to other lines of insurance. They believe that the scope should be only for personal lines of insurance.

Viewpoint 2. Scope applicable to only personal lines of insurance. The other opinion expressed was that the Task Force recommend the scope be applicable to personal lines, and that the Kansas legislature consider how credit

based insurance scoring effects others lines, particularly with respect to the numerous family-owned farms in the state that are insured under the commercial lines of insurance.



Credit Scoring Task Force

Minutes

*Friday, October 11, 2002
State Capitol Building, Room 245-N
Topeka, Kansas
1:30 p.m. – 3:30 p.m.*

Call to Order:

Chairperson Michael McGrew called the meeting to order. All members were present. **Michael McGrew**, Chair, Consumer interest, Lawrence; **Marta Linenberger**, Vice-chair, Consumer interest, Carbondale; Legislators: Sens. **Ruth Teichman**, Stafford; **Paul Feleciano**, Wichita; Reps. **Garry Boston**, Newton; **Jim Garner**, Coffeyville. Insurance Department: **Matthew All**, Lawrence. Insurance Companies: **Tony Kimmi**, Kansas Association of Property & Casualty Insurance Domestic Companies, Manhattan; **Jim Harwood**, Kansas Association of Property & Casualty Insurance Foreign Companies, Overland Park; **Brad Smoot**, American Insurance Association representative, Topeka; **Richard Turano**, National Association of Independent Insurers representative, Denver; **Bruce White**, Alliance of American Insurers representative, McPherson; **Vanda Easley**, National Association of Mutual Insurance Companies representative, Kansas City. Agent Representatives: **Cindy Hower**, KAIA representative, Holton; **Duane Becker**, KAIA representative, Lawrence.

Interested persons attending: Larry Magill, KAIA; Catherine Rankin, State Farm; Bill Wempe, Kansas Insurance Department; Ed Sable, Kansas Insurance Department; Ron Gaches, Consumer Protection Information Association; Gary Holle, Bremer Farmers Mutual; David Hanson, Kansas Insurance Associations; Bill Sneed, State Farm; Bill Wolff, Legislative Research; Brent Getty, Kansas Insurance Department; Brenda Dutton, Armed Forces Insurance; Barbara Conant, Kansas Trial Lawyers, and Martin Hawver, Hawver News.

Introduction:

Chairperson McGrew asked members of the task force to introduce themselves and state their representation on the task force.

Task Force Charge:

Chair McGrew welcomed all members. He stated that he was a lifelong citizen of Lawrence and a Realtor. He expressed being honored to be the chairman for this important task force, and that his intentions are to encourage professional and courteous debate. He recognized the challenging state of affairs in the insurance industry, and stated that he felt that task force members should be open-minded. He asked members that if anyone had preconceived notions about insurance credit

scoring, to set those opinions aside and take an honest look at the information to be developed in the course of the task force meetings. He stated the importance of having an open and thorough discussion, and to consider all points of view on the subject of insurance related credit scoring. Chair McGrew stated the importance of a final report that is balanced between the needs of insurance consumers and the needs of insurance companies.

Chair McGrew asked Linda De Coursey to discuss the handouts members received at the meeting.

Education component:

Ms De Coursey discussed the handouts. She asked members to forward email addresses to her before the end of the meeting, because that is the desired mode of communication. She pointed out that in the handouts was a copy of SRC 1623. She read the following charge of the task force:

- Conduct a study of the desirability of regulation of insurance scoring practices for the benefit of Kansas consumers
- Report the results of such study and the task force's recommendations and conclusions emanating therefrom to:
 - the speaker of the house, the president of the senate, the chair of the house committee on insurance, and the chair of the senate committee on financial institutions and insurance
 - no later than the convening of the 2003 Kansas legislature (January 13, 2003).

Also included in the handouts is a consumer alert designed by the NAIC and one that the Kansas Insurance Department uses to send out to consumers to inform them what credit scoring is all about. Also included was a report by the National Conference of State Legislatures on what other states have done so far with regards to laws on credit scoring. In a much more detailed chart, the NAIC compendium of state law lists all the state's credit scoring laws, she pointed out that two bills were noted on the Kansas site. Those two bills were discussed by the legislation in the 2001 session, HB 2234 and SB 185. These two bills had to do with the enactment of the Fair Credit Score Disclosure Act (California law), but it was limited to mortgage lending decisions. She pointed out the handout the official report of the legislative committee on those two bills.

Discussion ensued regarding allocation of resources in which to assist the task force to achieve the charge. Ms. De Coursey explained that normally Legislative Research staff would have been designated in the resolution, however, it had not be included. The Kansas Insurance Department (KID) had volunteered to staff the task force. Matt All, Assistant Commissioner, indicated that KID had sufficient legal staff and others to assist the task force. Dr. Bill Wolff, present at the meeting, indicated his willingness to assist us if the need arose.

Where do we go from here?

Chair McGrew opened the floor for discussion as to how the members of the task force wanted to proceed in order to accomplish the charge to the task force. Chair McGrew reminded task force members of the deadline of January 13, 2003 for the final report to be sent to appropriate designees stated in SCR 1623. He asked members to consider: Should we have public input? Should we have industry or regulatory input from outside sources? What other resources do we

need? What should our work schedule be? What should our "draft recommendation" target date be?

Discussion ensued and the members requested the following. 1) Find out what goes into building a credit score, and how the information is used, and why it was developed in the first place. 2) Look at both pros and cons of the issue. 3) Develop open hearings. 4) Answer two basic questions: is there a correlation between risk life style or the need of more money, and which side of the line the issue falls on. It was pointed out that in many areas gender is not allowed because it is considered discriminatory, but it is allowed in many areas of insurance. 5) Look at developing standards for the companies. 6) How many different models are used? 7) Information not sufficient from the companies to the agents when the company turns down a potential insured and the agents. 8) The potential benefits of using credit scoring as a tool, along with other indicators, such as driving records, etc. 9) How to define fairness if credit scoring is established as a good indicator: Adverse selection versus honoring 10) How are credit scores weighted? 11) Issue of credit scoring information being proprietary, i.e. the black box. 12) Consumers need to be educated about credit scoring. 13) What happens to the market if use credit scoring, and what happens to market if a company doesn't use it. 14) Using credit scoring as sole indicator for coverage. 15) Potential for red-lining.

Next meeting

Task Force members decided on an all day format to discuss the pros and cons of credit scoring. It was decided to ask for presentations from the Credit Information Trade Association for perspective of the data information; to hear from the several companies that build credit scores (ChoicePoint; Fair Isaac; and Allstate); and any industry points of view. Depending on the better date for these groups, the meeting will be set for Friday, October 25 or if not that date, the back up date would be Friday, November 1. An all day meeting would be considered from 10:00 to noon and 1:30 to 4 p.m.

A meeting for the consumer side of the issue will be scheduled for Monday, November 25.

Subsequent meetings in December will be held to finalize the report.

In the meantime, Ms. De Coursey was asked to forward American Insurers Association report to all task force members. Members received an additional handout from KAIA Management & Leadership Conference regarding Credit Scoring.

Adjournment

Being no further business, the meeting was adjourned.



Credit Scoring Task Force

Minutes

Friday, October 25, 2002
State Capitol Building, Room 526-S
Topeka, Kansas
10:00 p.m. – 5:00 p.m.

Call to Order:

Chairperson Michael McGrew called the meeting to order. The following members were present: **Michael McGrew**, Chair, Consumer interest, Lawrence; **Marta Linenberger**, Vice-chair, Consumer interest, Carbondale; Legislators: Sen. **Ruth Teichman**, Stafford; Rep. **Garry Boston**, Newton; Insurance Department: **Matthew All**, Lawrence. Insurance Companies: **Tony Kimmi**, Kansas Association of Property & Casualty Insurance Domestic Companies, Manhattan; **Jim Harwood**, Kansas Association of Property & Casualty Insurance Foreign Companies, Overland Park; **Brad Smoot**, American Insurance Association representative, Topeka; **Richard Turano**, National Association of Independent Insurers representative, Denver; **Bruce White**, Alliance of American Insurers representative, McPherson; **Vanda Easley**, National Association of Mutual Insurance Companies representative, Kansas City. Agent Representatives: **Cindy Hower**, KAIA representative, Holton; **Duane Becker**, KAIA representative, Lawrence. Members not present: Rep. **Jim Garner**, Coffeyville, and Sen. **Paul Feleciano**, Wichita;

Presenters in attendance: Eric Ellman, Consumer Data Information Association; Eric Rosenberg, TransUnion; Lynn Knauf, Alliance of American Insurers; Jeffery Skelton, ChoicePoint; Eddy Lo, Fair Isaac; Kathy Olcese, Allstate Insurance; Catherine Rankin, State Farm Insurance.

Interested persons attending: Gary Holle, Bremer Farmers Mutual; Larry Magill, KAIA; Ron Gaches, Consumer Protection Information Association; Mike Stewart, TransUnion; Neil Alldredge, NAMIC; David Hanson, Kansas Insurance Associations; Kevin Davis, American Family; Ernest Kutzley, AARP; Rick Wilborn, Farmers Alliance; Barbara Conant, Kansas Trial Lawyers. Jim Newins, Bill Wempe, Ken Grotewiel, Brent Getty, Jarrod Forbes, and Linda De Coursey, Kansas Insurance Department.

Introduction:

Chairperson McGrew asked members of the task force to introduce themselves and state their representation on the task force.

Approval of minutes:

It was moved and seconded to approve the minutes of the October 11th meeting as read. Motion carried unanimously.

Presentations:

Departmental Regulation of Credit Insurance Scoring – Brent Getty

At the last meeting, task force members asked for a briefing of current law and regulatory authority concerning credit insurance scoring. Brent Getty, staff attorney for the Kansas Insurance Department, presented that currently the department has no direct regulatory authority over the use of credit scoring as an underwriting factor. Authority does exist to ensure that insurance companies do not discriminate against insured in the setting of rates (K.S.A. 40-951 et seq.) Using this authority over rates, the insurance department indirectly regulates credit insurance scoring.

Under current law, an insurance company cannot discriminate in the tier rating system. Mr. Getty explained that to distinguish between two consumers, the insurer must show an actuarial basis for the different rates. The industry has been able to show such a showing in the use of credit insurance scoring.

The department has addressed the situation when an insured has successfully disputed the information contained in the credit insurance score. The company will correct the rate charged to the insured and refund any overcharge. The Department also requires that the companies periodically update the credit insurance score information.

Since insurance companies do not file their underwriting criteria with the Department, there is limited ability to regulate the renewal of personal automobile insurance policies. The Department indirectly regulates underwriting through the ability to conduct market conduct examinations on insurance companies. Mr. Getty explained, for example, during one examination, the department discovered that although the company had indicated that credit insurance scoring was not the sole criteria for underwriting purposes, several underwriting files contained evidence that credit insurance scoring was the sole reason for declining a new applicant. However, all the department could do is note this discrepancy in its final report.

Consumer Data Industry Association – Eric Ellman

Mr. Ellman presented the issue of credit insurance scoring. He said, for a number of years, a growing trend in the insurance business is to use credit information as a part of the underwriting or rating process for homeowners and/or automobile insurance. Coinciding with the rise in the use of credit as an insurance tool, the level of legislation and regulation of the use of credit by states has also risen dramatically.

There is a prevalence in the use of credit data. A nationwide survey found that 92% of the nation's largest automobile insurers use credit data to underwrite new business. More than 50% use credit data to determine the eligibility and rating classification. Over half of those largest companies began using credit data after 1998.

Mr. Ellman explained that often confused with credit scores that determine creditworthiness, an insurance score is designed to measure risk of loss. Insurance scores often, but not always contain credit information. Often credit information is one part of an overall score that also may include information like application information, MVA data, claims history, home or auto information, and more.

Scores or credit data are used because they are predictive. Mr. Ellman expounded that credit histories by themselves, or as part of insurance scores, are used by insurers because they are highly predictive of risk of loss. He cited the Tillinghast-Towers Perrin study that indicated the numbers don't lie. Higher credit scores translate statistically into better insurance risks. The aforementioned study reviewed nine books of business and found that either of the books showed a 99 percent confidence level in the relationship between credit scores and loss potential. The other book showed a 92 percent level. He said there hasn't been a study that does not show a correlation.

Mr. Ellman indicated that consumers support the use of credit. He cited a Harris poll that found 70% of those surveyed support the use of credit for insurance purposes.

Mr. Ellman also shared with the task force that the federal Fair Credit Reporting Act (FCRA), 15 U.S.C. 1681 et seq heavily regulates the consumer report industry. Credit bureaus are required to maintain maximum possible accuracy. The federal law prohibits those that furnish data to consumer reporting agencies from furnishing data they know is erroneous and requires them to correct and update information. Consumers have a right to dispute information on their credit reports with consumer reporting agencies and the law requires dispute resolution in not more than 30 days (45 days in certain circumstances). If a dispute cannot be verified then the information must be removed in the consumer's favor. Any reporting agency that violates any provision of the credit report law is subject to private rights of action. Also data furnishers are prohibited from furnishing data they know is inaccurate and have to have an affirmative duty to correct and update information. The use of credit for insurance purpose is lawful.

Credit reports are accessible to all consumers, and are easy to obtain. FCRA prohibits a charge of more than \$9 for consumer disclosures unless the consumer is a fraud victim, unemployed and seeking employment, on public assistance, or has been denied credit or insurance on the basis of a credit report, in which cases the consumer is entitled to the credit report for free.

As discussed earlier, the law imposes accuracy standards on consumer reporting agencies and data furnishers. In addition to legal standards, there are operational standards in place to ensure reliability. An important part to remember, stated Mr. Ellman, is what does one consider to be an inaccuracy. The bottom line is that not all inaccuracies are inaccuracies that reflect on one's ability to obtain credit. In reality, in a majority of reinvestigations are completed in five days or less and 70% are resolved in day days or less.

CDIA debunks the public interest reports citing their attempts to perpetuate the myth of inaccuracies, stating the sampling size was not representative of the population, nor were the conclusions drawn statistically sound.

Mr. Ellman concluded that the use of credit information for insurance purposes is lawful, commercially accepted, and statistically proven. Credit scores are designed to measure creditworthiness while insurance scores are designed to gauge risk of loss. Credit data is but a small piece of a much bigger pie that is in an insurance score. Credit reports are reliable because the law requires it, industry tests it, and the economy demands it.

TransUnion, Eric Rosenberg

Mr. Rosenberg discussed the credit report basics. TransUnion believes that an informed consumer is a smart consumer. Knowing about the credit report system, what goes into a credit report, and how to get recourse are important factors in maintaining or increasing a consumer's creditworthiness. TransUnion provides many channels for consumers to receive their file disclosures. In 2001, 45,661 Kansas consumers obtained their credit reports. Mr. Rosenberg noted that if Kansas consumers are denied insurance or are notified of another insurance-related adverse action in which a TransUnion credit report was used, that the federal law (Fair Credit Reporting Act) requires within 60 days those consumers to receive a free copy of their credit report. Mr. Rosenberg distributed copies of the brochure, "Credit Reports, Consumer Reporting Agencies, and the Fair Credit Reporting Act – the Everything You Need to Know guide to consumer rights in consumer credit reporting.

Mr. Rosenberg also discussed how to dispute information contained in the credit reports. Again, once a dispute is received, TransUnion must follow certain procedures to investigate that dispute within 30 days of receiving the dispute. Under the law, agencies may not charge for any of the reinvestigation or for the corrected reports. He also discussed briefly how to get fraud victims assistance.

TransUnion believes that there are benefits of credit bureau-based scoring systems to lenders, insurers, and to consumers. He explained that credit bureau scoring models are based exclusively on objective credit bureau-based information and do not use (nor do records contain data on) race, gender, or national origin. Records do include: factual account payment information from thousands of financial institutions and retailers, reported each month, including: 1) Demographic information (name, address, phone number, employer, and date of birth). 2) Public records such as information on civil judgments within the last 7 years, unpaid tax liens, paid tax liens, and bankruptcies. 3) Collection information on accounts that have been turned over to debt-collecting firms. 4) Account information that provides factual payment history on credit accounts. 5) Inquiry information that displays which companies have received the consumers credit file over the last two years. 6) Consumer dispute or fraud alert statements (if any). Mr. Rosenberg stated that approximately 1.5 billion individual updates of accounts are processed each month. TransUnion updates the entire national database on a one-week cycle so that updates received are very quickly moved on to the consumer's files.

Mr. Rosenberg indicated that predictability of risk is important to both risk managers and consumers, because the more predictable the risk, the less hedging must be built into the price of the financial instrument, including insurance policies. Scalability is also an important advantage to insurers using credit scores in two ways: They are independent of volume; they can be used to uniformly evaluate 10 or 1,000 or 1,000,000 decisions each day. Secondly, they can be scaled to create tiers of risk. This implies the ability to move away from less discrete rate groups such as "premium, standard and non-standard" toward more finely tuned pricing strategies that more closely correspond to the degree of risk.

Using insurance credit-scores promotes competition by providing a tool that is scalable, objective, and actuarially sound. It helps auto, property and casualty insurers to compete nationally and in previously underserved areas. The lowering of barriers to competition lower costs and can lead to more choices for consumers in marketplace.

Mr. Rosenberg stated that TransUnion recognized that consumers and policy makers have expressed concern on the practice of using credit scores in underwriting. TransUnion's perspective on four of these concerns: 1) Uniform application. It is important that insurers using credit scores apply them uniformly. They must be used for all populations. 2) Not a Sole Factor. TransUnion's standard contractual agreement with insurance customers using the Fair Isaac-developed ASSIST model provides that factors other than the ASSIST score must be used in the underwriting decision. They support regulations that prohibit the sole use of credit or insurance score for underwriting decisions. 3) Credit scores are not a proxy for other decision criteria. 4) Consumer education concerning credit scores.

In summary, the use of credit information in insurance underwriting is providing the opportunity for fairer pricing, as well as for more competition. The information is objective and comprehensive, and is clearly related to loss ratios. For those adversely affected by the use of credit reports and credit scores, the federal Fair Credit Reporting Act provides a clear framework of consumer rights for notice, access, correction of inaccurate data and notification of prior report recipients. Credit reporting agencies don't have and we cannot have access to all the variables that go into a credit lending or underwriting decision. TransUnion recognizes the educational role that they have in providing information to consumers about credit scores.

Alliance of American Insurers – Lynn Knauf

Alliance believes that insurers should maintain the right to consider credit information in their underwriting and rating decisions. With respect to underwriting, insurers should be permitted to consider credit along with other traditional underwriting factors. Credit-based insurance scores are fair and accurate tools that allow insurers to underwrite and rate risks with greater certainty. Consumers directly benefit from the insurers use of more sophisticated underwriting and rate tools. It is critical for healthy competition to preserve the right of insurers to consider credit information in their underwriting and pricing decisions; and its critical to allow consumers the right to seek out insurers who may offer actuarially-justified discounted rates based on their favorable credit history.

Ms. Knauf states that the relative "newness" of credit scoring, compounded, unfortunately, with their slow response to adequately explain credit scoring to their own agents and policyholder, has led to credit scoring becoming a controversial issue in many states. She cited that legislation to address the use of credit scoring surfaced in at least 31 states this past year. Of the 31 states, only 8 states passed laws to further regulate (above and beyond regulation already in place in every state) insurer use of credit scoring. (Arizona, Idaho, Maryland, Minnesota, Missouri, Rhode Island, Utah and Washington) Two states do have partial bans: Hawaii bans the use of credit scoring in rating and Maryland bans the use of credit in homeowners lines and auto underwriting, but not rating.

Ms. Knauf briefed the task force members that the National Association of Insurance Commissioners is looking at three areas: 1) a matrix; 2) consumer education brochure; and 3) actuary study.

She stated it is important to understand how insurers use credit information. Unlike lending institutions that consider credit histories and credit scores to determine one's ability to repay a loan, insurers consider credit information to measure one's ability to manage credit. It represents an objective and fair way of measuring subjective factors—factors of responsibility and stability.

She presented that credit habits are predictive, and correlates with the likelihood of accidents. Credit scores are primarily affected by credit habit patterns. Further, she stated, credit scores used by insurers do not discriminate against lower-income individuals. In actuality, people of all economic levels have good and bad credit records. Income is NOT a factor considered in an insurance credit score. She listed other things not considered within a credit score calculation.

She defied the charge that an insurer uses the credit information to charge a higher premium or for denying business. She states that any insurer who would attempt to deny as much business as possible, or unfairly rate or tier their policies would not remain in business very long. They believe that credit information has proven to be an effective tool.

She addressed the concerns regarding inaccuracies or errors and reiterated the federal laws (FCRA). She also suggested consumers have choices, if they do not believe their company has unreasonably changed a rate based only on credit. Consumers are free to shop for another insurance company. She suggested that not all insurers will choose to use credit information, and those that do use credit information will not use them in the same manner. Making insurers all use it in the same manner would take away the competition necessary for a healthy insurance market. Alliance believes that the use of credit reports and insurance scores has positive effects on consumers. A score allows the underwriter to look at a trend, not just a few incidents. Older items on credit reports will carry less weight, so mistakes will not haunt consumers forever.

Alliance believes that 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 underwrite and price risks using nondiscriminatory and statistically valid tools available to them.

She also mentioned that the vast majority of insurers are now making a great effort to explain to their agents and policyholders how credit scoring works and the advantages of credit scoring. Publications have been produced by the national trade associations, and numerous companies have now produced educational materials in an effort to more openly communicate with their customers.

Choice Point. Jeffrey A. Skelton

ChoicePoint supports the use of a consumer's credit information when used in conjunction with other information sources to evaluate a consumer's eligibility for automobile and homeowners insurance. This concept is supported because they believe that a consumer should be evaluated more upon his or her merits or behaviors, and not upon a generic classification of grouping such as race or gender. However, ChoicePoint is sensitive to consumer's concerns about the use of information that seems somewhat "disconnected" from driving or occupant behaviors.

From ChoicePoint's perspective, there should be several requirements that must be met before an insurance risk score is used for underwriting or pricing. 1) Companies that build or promote insurance scores should be completely open with regulators, legislators, customers, and consumers about the elements that are considered and how those elements effect a consumer's score. 2) insurance score should be used in conjunction with other behavioral information and not used alone to deny coverage. 3) Consumer reporting agencies and insurance companies have an obligation to explain to consumers the scoring process including how negatively affected consumers can contest the information used to deny coverage or impose a surcharge.

Mr. Skelton pointed out that it is important to stress that scores for insurance purpose differ from the credit scores used by banks to determine credit worthiness. Insurance scoring models are not predicting an individuals ability to repay a loan or determining how much money consumers should be allowed to borrow. Insurance scores help insurance companies rank order risks by predicting frequency and severity of claims in the next twelve months.

ChoicePoint provides models to the insurance industry that include claims history information with credit elements in order to get a predictive outcome. Elements built into the model include but are not limited to: personal finance, bank revolving, bank installment, department stores and other retail accounts. What is NOT in the model: nationality, age, religion, race, gender, locations/address, net worth/salary, income, marital status and occupation. Other common exclusions or restriction include: non-consumer inquiries, inquiries from insurance companies, medical collections and multi-inquiries from consumers shopping for home or auto loans.

Why use insurance scores? Absent knowing exactly what the future holds, the best that can be done is statistically predict the future. Consumers are placed into groups with similar predictive characteristics. In doing so, insurers can offer the most competitive rate to each customer. Placing consumers in groups does not reflect on consumers as being "good" or "bad" people.

Insurance scoring is the same as what we have come to know about traditional underwriting criteria. Insurers look for objective measures to help predict the future. With this information insurers are able to more accurately group their policyholders and offer them the best possible rate. The insurance score does not indicate that individual "x" will have an accident on a particular day. Rather, it gives the ability to group policyholders with similar performance characteristics. In the end, consumers are treated more fairly and are less apt to be subsidizing consumers who file more claims.

Mr. Skelton discussed consumer issues. While states have been reviewing this issue closely through public hearings and appointed commissioners and examined the actuarial justification of insurance scoring and the impact to consumers. The math clearly supports the use of insurance scoring, but questions still remain concerning the causation. For instance, what does paying my credit card on time have to do with my driving? Mr. Skelton suggests that they are not predicting if someone will have an accident. Insurance scores are helping insurance companies accurately group policyholders based on how other similarly scores consumers perform.

What can be done to protect consumers, while at the same time not damaging the benefits of insurance scoring? ChoicePoint suggests that: Better agent education; Consumers need more information about insurance scores. Models need to focus on credit plus claims history to provide more accurate results. And, open the models to regulators for examination.

Fair Isaac, Eddy Lo

Eddy Lo discussed with the task force members that Fair, Isaac is a global provider of custom analytics and decision technology. They are widely recognized the their pioneering work in credit scoring, and revolutionized the way lending decisions are made. He said the company helps make more objective, consistent, and efficient decisions that increase the value of customer relationships.

Mr. Lo discussed the definition of credit-based insurance scores. Fair, Isaac credit-based insurance score is a predictor of a consumer's credit file at a particular point in time. More specifically, scores are developed to rank order the applicant or policyholder's likely loss ratio performance relative to other consumers. Fair, Isaac credit-based insurance scores are available at the three major consumer reporting agencies and through ChoicePoint.

He talked of the distinction between credit-based insurance scores and credit bureau scores. While both types of scores use information from consumer credit files, the credit-based scores are designed to predict the likelihood of delinquency or non-payment of credit obligations. Credit-based insurance scores are built to predict future insurance loss ratio relativity.

Additionally, Mr. Lo remarked about the Fair Credit Reporting Act, and information not used in Fair, Isaac credit-based insurance scores. He indicated the information used in the Fair, Isaac credit-based scores are: payment history; amounts owed; length of credit history; new applications for credit, and types of credit in use. The score considers both positive and negative information in the credit report. For instance, late payments will lower a score, but establishing or re-establishing a good track record of making payments on time will raise the score.

Mr. Lo informed the task force that Fair, Isaac pioneered the development of insurance risk scores based on consumer credit information in the early 1990's. The scores were developed by analyzing large samples of auto and home insurance policies to determine the statistical correlation between information on consumer credit bureau reports and subsequent insurance loss ration. Through the development process, the final models rank-order the likely loss ratio relativity of individual new applicants at the time of application, or in case of a policyholder, at the time of renewal. Represented by a three-digit number, the score ranges from the 100's to the 900's. The higher the scores, the lower the likely loss ration relativity and the better the risk. Although Fair, Isaac developed the algorithms and software used to general credit-based insurance scores, the score is calculated by the consumer reporting agencies based on the information in their credit data bases, and the score is delivered by the credit reporting agencies to the insurer, along with the underlying credit report upon which the score is based.

Mr. Lo states that the predictive power of Fair, Isaac credit-based insurance scores have been validated by independent entities including: 1) Tillinghast-Towers Perrin Study (1996), supports the relationship between credit data and loss ratio; 2) Virginia Bureau of Insurance Study (1999), concludes that there is a concrete statistical correlation between insurance scores based on the credit bureau data and the likelihood of an individual filing an insurance claim. It also found that credit scoring would be an ineffective tool for discriminatory redlining, since neither race nor income alone were reliable predictors of scores. 3) American Insurance Association Study (1999). This report concluded that the insurance score is not significant correlated with income, and that based on information from AIA company's policyholders, there is no evidence that insurance scores based on credit bureau data unfairly discriminate against lower income groups.

By using scoring, insurers save resources, make faster approvals, and better manage their books of business. Fair, Isaac suggests that: 1) Insurance use the credit-based insurance scores in conjunction with other important sources of underwriting information, and NOT solely on credit-based insurance scores. 2) Insurers use the credit-based insurance scores to identify expected good performing risks in

traditionally poor risk segments and to identify expected poor performance risks in traditionally better risk segments. 3) Insurers that are evaluating credit-based insurance scores to conduct a retrospective analysis to validate the strength of the models on their book of business and determine underwriting policies based on the credit-based insurance score and other information. 4) Insurers track and analyze the result associated with the use of the Fair, Isaac credit-based insurance scores to monitor scores distribution trends, measure the performance of the scores on their book of business and refine their strategies. 5) State insurance departments allow modelers to discuss modeling issues and when disclosure is requested, protection for the intellectual property be provided. It is important that the public not be allowed to access the models, learn of the characteristics in the model and manipulate their credit behaviors for the only purpose of achieve higher scores. The lack of protection would lessen the predictiveness and reduce the competition.

Mr. Lo concluded by stating that the credit-based insurance scores are legal, proven, fair, consistent, accurate, efficient, cost effective and regulatory friendly.

Allstate Insurance Company. Kathy Olcese

Ms. Olcese stated that Allstate uses credit history to help establish premium to increase the availability affordability of insurance and because use of credit history accurately reflects differences in loss potential. They use credit history in addition to other assessment tools. Allstate began using credit information in Kansas as an underwriting tool in the early 1990's. She believes that in Kansas using credit history has allowed us to accept more customers (with recent claim history) into their standard/preferred companies. Allstate does not reject anyone in Kansas solely due to credit history.

Their models were developed by Allstate, and are a significant advance in cost-based pricing. The use of credit history is a strong predictor of loss.

Ms. Olcese presented to task force members some slides showing the average loss cost by driving record incidents and then shows the average loss cost by insurance score and driving record incidents. The advantage, she stated, is holistic consideration of credit report information. Positive and negative characteristics make up an insurance score. And, it has a greater predictive power. For instance, auto insureds in the worst 10% group will have over 60% more losses than the best 10% of the group. Homeowners in the worst 10% will have well over twice as many losses than those in the best 10% group.

Ms. Olcese discussed the advantages of a score model. She also points out what Allstate considers in its scoring model and what it does not. She discussed the accuracy of the credit report. She stated that Allstate always informs customers of the use of credit reports when dealing with new applicants or quotes. Information is used objectively and consistently, and the consumer report is kept confidential. They notify consumers when premiums are higher based on information in a credit report, including how to get a copy of the credit report. If any mistakes are corrected, Allstate will change the customer's premium back when the credit report was initially ordered. For customers with no credit history, Allstate assigns a specific score based on the experience of this group.

In summary, Allstate believes that premiums should match risk of loss and she stated the benefits of using credit history.

State Farm Insurance, Catherine Rankin

Ms. Rankin reported that State Farm Insurance uses credit insurance scoring for auto new business only. And, that they do use credit insurance scoring for underwriting purposes only. They do not use credit insurance scoring for rates.

In State Farm's informational brochure, they point out that State Farm uses the most predictive factors in a person's credit history along with their driving record to determine the likelihood people applying for coverage will be involved in future losses. The model was developed solely to help predict future auto insurance losses. They do consider credit factors such as number of revolving accounts, late payments and collections. They do NOT use income, wealth, location, gender, race, address or any factors prohibited by law.

State Farm also provides the insured with information on how to correct information included in the credit record. And, State Farm makes a point of discussing the privacy of that information.

State Farm believes in requiring the same information from all new applicants for auto insurance. Credit, each driver's loss history record, and each driver's motor vehicle record information will be used to evaluate all new applicants. This treats all new applicants equally.

Ms. Rankin also discussed a white paper written by American Insurance Association with specific emphasis regarding the results of analysis of income with credit scores. AIA's study included data used to test the fairness of using credit scoring on a variety of individuals from all income levels; the nature of the statistical analysis, and the results. The analysis concluded that credit score is not significantly correlated with income for the AIA companies' policyholders. The AIA believes that credit history is a source of affordable, objective information that is useful to insurers, readily available in the market, and beneficial to consumers. Insurers are expressly authorized to use credit history pursuant to the federal Fair Credit Reporting Act. The white paper points out for insurance regulatory purposes that any misconduct is discoverable and punishable under existing state unfair trade practices laws.

Progressive Group

Ms. De Coursey pointed out to the group that written testimony was received from the Progressive Group. A representative from that group could not be present. The written materials stated that The Progressive group is the largest writer of private passenger auto insurance through independent agents and the fourth largest auto insurer in the country.

Using credit as an underwriting factor has allowed Progressive to offer more accurate and lower rates to more people. The written material states that Progressive actually has been able to offer standard and preferred rate levels to many consumers who otherwise would have been eligible only for nonstandard rates. Progressive never uses credit to reject a consumer or to cancel or raise the rates of an existing policyholder. Progressive feels that credit insurance scoring is a valuable tool that has helped their agents write and retain more business.

Progressive points out that: 1) Credit has proved to be a very powerful and independent predictor of future loss. 2) Many direct and captive companies use credit to prescreen mailing lists. If the use of credit were to be eliminated or unreasonably restricted at the state level, the federal Fair Credit

Reporting Act would still permit these companies to prescreen lists for solicitation. This could give a competitive edge over independent agents by allowing them to specifically target and write more profitable, higher retention business. 3) Credit scores focus mainly on a person's bill-paying behavior and not contain any information on income, race, color, creed, physical handicap or disability. 4) There is a difference in credit scores that a mortgage company uses and what is used by insurance company. 5) Restricted use of credit would cause auto insurance rates to increase for many consumers.

Progressive also listed its proactive business practices on the use of credit, for instance, Progressive does not use credit history to cancel, non-renew or refuse to insure someone. And, an individual's personally identifiable credit information is not disclosed to any third party, including independent agents.

Progressive believes in and actively works toward the following: 1) a new, easy to understand, credit model that will openly be shared with consumers, agents, customers, regulators, legislators and medial. 2) Where required or encouraged by state regulators, they will file the scoring algorithm and not request trade secret protection. 3) A credit assistance team, with a toll-free phone number for consumers and agents to call to assist them with concerns about the credit process. In summary, Progressive would oppose an outright prohibition of the use of credit in underwriting. They believe that responsible use of credit in underwriting is good for consumers and independent agents.

Task Force discussion and where do we go from here?

Discussion ensued among task force members when the chair asked for feedback of the day's session. Mr. Harwood suggested that many questions developed at the last meeting had been answered, such as who uses credit insurance scores, why they are being used and if they are predictive and correlative. He stated his comfort level about the "black box" is much better. But, Mr. All, on the other hand, wasn't sure that his comfort level was that high when looking at what exactly is in the black box, and the ability to fix bad information. Other members discussed that there is a definite disconnect between the carriers and agents.

Task Force members asked for more information regarding the Fair Credit Report Act for the next meeting. At what point is the consumer informed: at the application point or at adverse action.

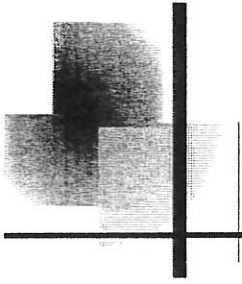
Next Meeting

The next meeting is scheduled for November 25. The meeting room will be announced at a later date, but will be at the Capitol. At the November 25th meeting, presentations and testimony will be taken from persons wishing to appear before the Task Force, and also the consumer side of the issue.

Subsequent meetings in December may be held to finalize the report.

Adjournment

Being no further business, the meeting was adjourned.



Credit Scoring Task Force

Minutes

Monday, November 25, 2002
State Capitol Building, Room 526-S
Topeka, Kansas
10:00 p.m. – 5:00 p.m.

Call to Order:

Chairperson Michael McGrew called the meeting to order. The following members were present: **Michael McGrew**, Chair, Consumer interest, Lawrence; **Marta Linenberger**, Vice-chair, Consumer interest, Carbondale; Legislators: Sen. **Ruth Teichman**, Stafford; Rep. **Garry Boston**, Newton; Insurance Department: **Matthew All**, Lawrence. Insurance Companies: **Tony Kimmi**, Kansas Association of Property & Casualty Insurance Domestic Companies, Manhattan; **Jim Harwood**, Kansas Association of Property & Casualty Insurance Foreign Companies, Overland Park; **Brad Smoot**, American Insurance Association representative, Topeka; **Richard Turano**, National Association of Independent Insurers representative, Denver; **Bruce White**, Alliance of American Insurers representative, McPherson; **Vanda Easley**, National Association of Mutual Insurance Companies representative, Kansas City. Agent Representatives: **Cindy Hower**, KAIA representative, Holton; **Duane Becker**, KAIA representative, Lawrence. Members not present: Rep. **Jim Garner**, Coffeyville, and Sen. **Paul Feleciano**, Wichita.

Presenters in attendance: Larry Magill, Kansas Association of Insurance Agents; and Gary White, Kansas Trial Lawyers Association.

Interested persons attending: Gary Holle, Bremer Farmers Mutual; Phil Dresser, KAIA; Ron Gaches, Consumer Protection Information Association; Shery Diel, KS Real Estate Association; Catherine Rankin, State Farm; David Hanson, Kansas Insurance Associations; Kevin Davis, American Family; Rick Wilborn, Farmers Alliance; Lee Wright, Farmers Insurance; Barbara Conant, Kansas Trial Lawyers; John Shoemaker, Legislative Aide. Bill Wempe, Ken Grotewiel, Brent Getty, Jarrod Forbes, and Linda De Coursey, Kansas Insurance Department.

Introduction:

Chairperson McGrew asked members of the task force to introduce themselves and state their representation on the task force.

Approval of minutes:

A draft of the minutes had previously been sent to members for perusal.

IT WAS MOVED BY MATT ALL AND SECONDED BY JIM HARWOOD TO APPROVE THE MINUTES OF THE OCTOBER 25, 2002 MEETING AS READ. MOTION CARRIED.

Presentations:

Fair Credit Reporting Act – Brent Getty

At the last meeting, task force members asked for a briefing of the Fair Credit Reporting Act (FCRA). Brent Getty, staff attorney for the Kansas Insurance Department, discussed that the act regulates the disclosures of consumer reports by consumer reporting agencies. He focused on the sections of the act that applied to insurance transactions. He talked about the definition of “consumer report” and how a consumer reporting agency may only provide a consumer report under certain circumstances: 1) written instructions by the consumer to whom it relates and whom has reason to believe; and 2) intends to use the information in connection with the underwriting of insurance involving the consumer.

He further discussed that under the act, issuance of a consumer report may trigger additional notice requirements. Mr. Getty presented the definition of “adverse action” under the act.

He stated that a key portion of the Act’s definition is that it applies only to insurance either “existing or applied for”. Discussion ensued regarding when application occurred. He pointed out that depending on how “applied for” is defined, either by legislation or regulation, such transaction may involve a consumer report being issued for a permissible purpose but not involve an adverse action, because the underwriting decision was made prior to the consumer actually applying for insurance.

Kansas Association of Insurance Agents – Larry Magill

Mr. Magill stated that consumers understand and accept the relationship between a bad driving record, their MVR, claims, teenage drivers and other factors historically used by the industry to rate automobile insurance, but have a much harder time understanding the relevance of a “credit score”. Especially when a bank agrees to lend them hundreds of thousands of dollars to buy a home, but an insurance company refuses to insure or treats them as substandard for an insurance score the company can’t or won’t explain and the consumer doesn’t understand.

He pointed out to task force members that credit scoring and multiple tiered rate structures have allowed some consumers’ insurance rates to double in some cases, when normal base rate increases would never have been allowed to increase that much. While base rates that require prior approval by the insurance department may increase 10 to 15%, a consumer’s cost can now increase 100% because of their credit score. He related a KAIA member told him that she had a client’s homeowners insurance premium increase from \$718 to \$2,250 a year due to the client’s credit score. This particular insurer had recently implemented a 9-tier homeowners rating system.

Another affect that credit scoring has had on the consumer is the ability to shop for insurance. Where agents once could use comparative rating software and rate a consumer with every company they represent, they can no longer use that system. Each insurer may use a different credit scoring service, resulting in a time consuming, not to mention expensive process.

Mr. Magill presented the results of the KAIA survey. He indicated that based on the huge response to a recent fax-back survey, no other issue carries as much importance for the members or creates more “heart burn” for them dealing with their customers as does the credit score issue. Within days over 147 responses to the survey were received, which is 35% of the membership. They overwhelmingly support seeking reasonable statutory or regulatory control over credit scoring in Kansas.

He indicated that agents are very frustrated by their inability to explain to the consumer how the scores are determined or how the consumer can correct the problem. Sixty-seven percent of the members answering the survey said that insurers only notify consumers that a score will be obtained. Sixty-eight percent indicated that only "some" or "never" is the consumer told that their score resulted in a higher premium. Sixty percent of the time, credit scoring is "always" or "frequently" the only factor considered.

Mr. Magill pointed out that other national organizations were studying the issue, and that in all 50 states credit scoring continues to be one of the hottest topics. As recent as Friday, November 22, the National Council of Insurance Legislators (NCOIL) adopted a model law, and several insurance groups supported the concept.

The KAIA would support the following points to be included in any legislation: 1) Address all lines of insurance, not just personal lines; 2) Adverse action would be defined to include charging anything more than the lowest rate available from the insurer, after considering all other rating factors; 3) Cannot use credit scoring on renewals; 4) Consumers who are charged more based on the credit report should be able to request (annually) that the insurer run their credit score and lower the premium if it has improved; 5) Insurers should be required to inform consumers that they are using a credit score in underwriting and/or rating; 6) Standardized disclosure of process and results; 7) Credit scoring "black box" should be filed with the Insurance Department and be closed as a trade secret; 8) Listed seven prohibitions and limitations including: refuse to insure solely on basis of credit score, "hits" on a persons credit; etc.; 9) Appeals process; 10) Limitations on the use of "no hits" and "thin files"; 11) Corrected information should require an insurer to go back to the beginning of the policy term and refund the overcharge; 12) Hold harmless clause for agents; 13) Agents and consumers information must be kept confidential.

Mr. Magill discussed some disconnects between credit, income and wise choices. For example, the fact that a low mortgage balance compared to the value of a home is not a plus and yet being a smart consumer and refinancing your home to take advantage of lower interest rates is a minus due to length of credit relationship. Yet, you may only owe \$100,000 on a \$200,000 house, but for scoring purposes it's a minus because having not paid down much of the refinanced mortgage.

Mr. Magill handed out a state by state activity report of the credit scoring issue, and a copy of the NCOIL model law. Mr. Magill expressed KAIA's willingness to work through the issues and urged the task force to craft reasonable limitations on credit scoring.

Kansas Trial Lawyers Association – Gary White

Mr. White stated that as advocates for consumers, the Kansas Trial Lawyers Association (KTLA) would support efforts that discourage negligent, careless behavior and ensure the safety of products and services Kansans rely on and enjoy. For that reason, KTLA is offering a consumer's perspective on insurance credit scoring practices. Unfortunately, there is no unified voice to speak on this issue for Kansas consumers. He pointed out that consumer groups in other states, as well as on the national level are sounding alarms about the dangers of relying on this inadequately regulated practice and are studying the negative impact the use of credit scores has on consumers. Also, current Kansas law does not give the Kansas Insurance Department direct authority to regulate the use of credit scoring.

Because of these concerns, Mr. White stated that the KTLA believes that the State of Kansas should, at a minimum, adopt regulatory and enforcement oversight to ensure credit scoring information used for insurance purposes are properly and accurately maintained, protected and is not used as a sole indicator for insurance underwriting or rate setting.

Concerns about credit scoring relating to insurance are:

- 1) Secrecy and lack of documentation provided by the insurance industry. The current system places consumers wholly in the dark about the underwriting factors used by insurance companies in creating a person's credit score. The insurance industry refuses to document any case and effect relationship between credit score and driving ability. How is a person who paid a bill late once any more likely to be hit by another driver or have a hailstorm ruin their roof? Mr. White cited a Washington Post article stating "insurers can't really explain the correlation between credit scores and risk. Because the scores are proprietary, regulators can't parse them to make sure they are used fairly – that they are not, for example a way around the prohibition on using race as a underwriting criterion."
- 2) Credit scoring unfairly discriminates against consumers. Insurance credit scores tend to discriminate against senior citizens, racial minorities, small business owners, people with little or no credit, victims of identity theft, people who have been laid off or divorced and people who have experienced a medical catastrophe. These are individuals who often have little or no credit or credit history, use cash rather than credit cards, and have not taken out large loans. Other states studying the issue, Michigan for instance, did a survey and showed disparities in auto rates of up to 17% in cities with similar population sizes and auto theft rates, but with different racial make-up. Mr. White cited the Michigan Attorney General concluding: "the finding of the study are compelling and disturbing to say the least. Time has come for the industry to be more up front with their customer. Consumers pay thousands of dollars a year to keep their homes and cars insured...they deserve to know how the rates are calculated." Mr. White also cited the Florida Task Force conclusion: "it does appear that the use of credit reports has a negative impact on young people, minorities and people with low incomes."
- 3) Questionable accuracy of the information used in credit scoring. A state-based non-profit, non-partisan, consumer and environmental watchdog group whom studies the accuracy of consumer credit reports found that 29% of credit reports surveyed contained errors serious enough to cause the denial of credit, insurance, employment or other benefits. Mr. White points out that for consumers at either end of a bell curve, with either very bad or very good credit, errors may not matter. However, for consumers on the margin, errors resulting in a decreased credit score can result in credit or insurance denial, or with the increased use of risk-based pricing models, significantly higher (sub-prime) credit or insurance premium (high risk pool) costs.

Because of the widespread use of this practice, KTLA strongly encourages the Task Force to recommend the legislature consider legislation to either ban the use of insurance credit scores or provide regulatory authority to safeguard Kansas consumers.

Mr. White's handouts included: Credit Report in Insurance; Credit Scores Driving Insurance Rates Higher; Credit Scoring: The Return of Discriminatory Underwriting; The Inaccuracies of Credit Scoring; A summary of state legislation regarding the use of insurance credit score; and a law enacted by the 2002 Washington State Legislature.

Task Force Discussion

Task Force members asked if any information existed and could be presented from the Kansas Insurance Department from the Consumers Assistance Division. Ken Grotewiel said he would be happy to present some complaint stories and share some numbers with the task force. The presentation was set up after the lunch break.

Ken Grotewiel, Director of the Consumer Assistance Division, reported that the division receives approximately 60 to 100 phone calls a day from consumers on various issues. He planned to relay some of the typical stories and scenarios about credit scoring complaints from insureds. One story was about a person, knowledgeable about credit scoring, who was informed her rates were going up. The division was successful in getting the company to rerun her credit score, and it actually lowered her premium. The second story was regarding non-renewal. The person did have a judgment against their name, but the judgment had been paid off for several years. The division was not successful in getting the company to renew the person. Mr. Grotewiel stated that credit scoring problems can exist, but can be connected with other issues as well. Another story, Mr. Grotewiel related was about a widow. Most of her life, credit was established by her husband. She really didn't have a credit history in her own name. Because of that, the insurers raised her premium.

Generally, the division saw an increase in calls starting in July of this year. The consumers tell their stories, they get angry, and then they are frustrated because they feel they are good customers and do not understand why their rates have been doubled.

Mr. Grotewiel explained that their sophisticated data base for filing complaints is split into several categories. Where they would look for credit scoring problems would be under "premium and rating". For the first 10 months of 2001, complaints on premium and rating increased from 163 to 225. For the first 10 months of 2002, the complaints on premiums and rating increased from 70 to 141...nearly doubled. For all lines, complaints rose from 298 to 467. He reported that specifically tagged as "credit scoring issue" only showed eight to nine files. He actually pulled the files that he knew were credit scoring issues, and even he had not tagged it as credit scoring. While actually tagging complaints specifically to a credit scoring issue is not always accomplished, Mr. Grotewiel believes they will get better at doing so. Without pulling all the files under "premium and rating" complaints, and going through them individually, a firm number cannot be certain.

Further Task Force Discussion

Discussion ensued whether or not enough information has been received for the Task Force to move toward deciding what to include in the report to the Legislature.

IT WAS MOVED BY ALL AND SECONDED BY HOWER THAT THE SENSE OF THE TASK FORCE IS THAT NEITHER UNFETTERED USE OF CREDIT SCORING NOR TOTAL BAN OF CREDIT SCORING IS AN APPROPRIATE REMEDY OR OUTCOME. MOTION CARRIED.

With that decision, the Task Force discussed how to address the changes they wanted to recommend. It was finally determined that the Task Force would use the broad suggestions for change made by the Kansas Association of Insurance Agents as a starting point for discussion. The points of discussion were:

- 1) Applicable to all lines of insurance or limited lines
- 2) Adverse means paying more than lowest rate
- 3) Not used on renewals
- 4) Consumer requested review
- 5) Inform and explain
- 6) Standardized disclosure of process and results
- 7) Black Box filings
- 8) Prohibitions and limitations
- 9) Appeals process
- 10) No hits and thin files
- 11) Corrected information
- 12) Hold agents harmless clause
- 13) Confidentiality

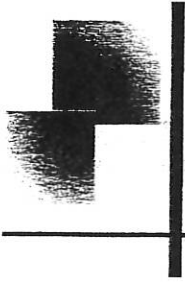
Discussion ensued on several of these items, and it was determined that another meeting would be necessary to complete the discussion, and to allow members time to think about the various issues.

Next Meeting

The next meeting for the task force is scheduled for Wednesday, December 18, 2002. It is envisioned that another meeting would be needed to finalize the report, and that meeting is scheduled for Wednesday, January 8, 2003. Both meetings will be held in Room 526-S at the Capitol, and meeting times are 9 a.m. to 5 p.m.

Adjournment

Being no further business, the meeting was adjourned.



Credit Scoring Task Force

Minutes

Wednesday, December 18, 2002
State Capitol Building, Room 526-S
Topeka, Kansas
9:00 p.m. – 5:00 p.m.

Call to Order:

Chairperson Michael McGrew called the meeting to order. The following members were present: **Michael McGrew**, Chair, Consumer interest, Lawrence; **Marta Linenberger**, Vice-chair, Consumer interest, Carbondale; Legislators: Sen. **Ruth Teichman**, Stafford; Rep. **Garry Boston**, Newton; Insurance Department: **Ken Grotewiel**. Insurance Companies: **Tony Kimmi**, Kansas Association of Property & Casualty Insurance Domestic Companies, Manhattan; **Jim Harwood**, Kansas Association of Property & Casualty Insurance Foreign Companies, Overland Park; **Brad Smoot**, American Insurance Association representative, Topeka; **Richard Turano**, National Association of Independent Insurers representative, Denver; **Bruce White**, Alliance of American Insurers representative, McPherson; **Vanda Easley**, National Association of Mutual Insurance Companies representative, Kansas City; and Rep. **Jim Garner**, Coffeyville. Agent Representatives: **Cindy Hower**, KAIA representative, Holton; **Duane Becker**, KAIA representative, Lawrence. Members not present: **Matthew All**, Insurance Department; Rep. **Garry Boston**, Newton; and Sen. **Paul Feleciano**, Wichita.

Interested persons attending: Ron Gaches, Consumer Protection Information Association; Bill Yanek, KS Real Estate Association; Bill Sneed, State Farm; David Hanson, Kansas Insurance Associations; Kevin Davis, American Family; Lee Wright, Farmers Insurance; Barbara Conant, Kansas Trial Lawyers; John Shoemaker, Office of Senator Praeger, Larry Magill, Kansas Association of Insurance Agents. Bill Wempe, Ken Grotewiel, Brent Getty, Jarrod Forbes, and Linda De Coursey, Kansas Insurance Department.

Introduction:

Chairperson McGrew asked members of the task force to introduce themselves and state their representation on the task force.

Approval of minutes:

A draft of the minutes had previously been sent to members for perusal.

IT WAS MOVED BY DUANE BECKER AND SECONDED BY SEN. TEICHMAN TO APPROVE THE MINUTES OF THE NOVEMBER 25, 2002 MEETING AS READ. MOTION CARRIED.

Discussion of NAIC meeting information:

Ms. De Coursey reported that she had attended the winter meeting of the National Association of Insurance Commissioners (NAIC). The Credit Scoring Working Group met and she distributed information from that meeting. The NAIC working group had asked the American Academy of Actuaries to study four of the prominent reports on the insurance credit scoring issue. A copy of the report from the American Academy of Actuaries was distributed to the Task Force members. It is a good summary document of each of the papers: Impact of Personal Credit History on Loss Performance in Personal Lines; Insurance Scoring in Personal Automobile Insurance – Breaking the Silence; Predictiveness of Credit History for Insurance Loss Ratio Relativities; and Use of Credit Reports in Underwriting. Ms. De Coursey said that information from these reports had been referred to in previous presentations before the Task Force.

Ms. De Coursey also distributed the NAIC Draft of Credit-Based Insurance Scoring: Regulatory Options, which gave the pros and cons relating to credit insurance scoring. Also included in the information is the NAIC Consumer Brochure, which was indicated that publication would be in January 2003. A letter from the Federal Trade Commission (FTC) was also included. She discussed with the Task Force members that a representative from the FTC was present at the NAIC meeting and discussed the letter at length. This information is pertinent to the Task Force in the discussion of adverse action. The FTC states that the legislative history of Section 603(k) of the Fair Credit Reporting Act is to be read broadly. That is: "Whenever a consumer report is obtained for a permissible purpose under section 604(a), any action taken based on that report is adverse to the interests of the consumer triggers the adverse action notice requirements under section 615." In other words, whether the consumer is quoted and then denied the lower rate, or a current policyholder or new applicant is considered for the lower premium and does not receive it...the action places the consumer at a financial disadvantage. The FTC believes the insurer must provide the Section 615(a) notice in these situations.

Discussion of state by state comparison document

Mr. Forbes discussed the comparison of other state law passed and the points of discussion that the Task Force is using for consideration of recommendations. He researched the eight states' laws that actually passed in the last year and compared it to those discussion points the Task Force is using for discussion. The report is to demonstrate to the Task Force where its discussions are with other states' law.

Continuation of task force discussion on recommendations

Two other reports were distributed for members' edification: The Use of Insurance Credit Scoring in Automobile and Homeowners Insurance – A report to the Governor, the Legislature and the People of Michigan; and Model Act Regarding Use of Credit Information in Personal Insurance by the National Conference of Insurance Legislators (NCOIL).

At the November meeting, it was determined that the Task Force would use the broad suggestions for change made by the Kansas Association of Insurance Agents as a starting point for discussion. The points of discussion were:

- 1) Applicable to all lines of insurance or limited lines
- 2) Adverse means paying more than lowest rate
- 3) Not used on renewals

- 4) Consumer requested review
- 5) Inform and explain
- 6) Standardized disclosure of process and results
- 7) Black Box filings
- 8) Prohibitions and limitations
- 9) Appeals process
- 10) No hits and thin files
- 11) Corrected information
- 12) Hold agents harmless clause
- 13) Confidentiality

Discussion ensued on several of these items at the November meeting. The Chair decided to start from the top for final discussion purposes.

- 1) *Point for discussion:* Applicable to all lines of insurance or limited lines. *Discussion:* Discussion ensued that presentations really only addressed the personal lines of insurance. Some members were reluctant to agree with making a recommendation that any law passed should be applicable to all lines of insurance. Discussion ensued regarding farms. Farm insurance is considered commercial line and not personal lines. However, the task force suggested that language be written in the final report that would ask the legislature to look at how credit based insurance scoring effected other lines of insurance, specifically the family owned farms. For the purposes of the Task Force's final report, personal lines shall mean: private passenger automobile, homeowners, motorcycle, mobile-homeowners and non-commercial dwelling fire insurance policies.
- 2) *Point for discussion:* Adverse action means paying more than lowest rate. *Discussion:* The task force agreed that the Fair Credit Reporting Act (FCRA) language should be interpreted as "anything other than the best possible rate." The FCRA defines adverse action as: A denial or cancellation of, a increase in any charge for, or a reduction or other adverse or unfavorable change in the terms of coverage or amount of, any insurance, existing or applied for in connection the underwriting of insurance. 15 U.S.C. § 168a(k)(1)(B)(i).
- 3) *Point for discussion:* Insurers should not be allowed to non-renew or rate up existing business due to a poor credit score. *Discussion:* While a lengthy discussion ensued regarding this matter, the Task Force members could not come to agreement on this issue. Some believe if credit based insurance scoring is valid during the application process, then it should also be valid during the renewal process. Others believe that insurers should not be allowed to non-renew or rate up policies, since credit information was not used when writing the original policy.
- 4) *Point for discussion:* Consumers requested review. Consumers who are charged more based on their credit report should be able to request, at least annually, that the insurer run their credit score and adjust accordingly their premium if it has changed. *Discussion:* Some members feel that while individuals should do all they can to improve their premium, it could be a burden on the insurer with individuals constantly asking for a new score. Others wanted the language to read: Consumer who are charged more based on their credit report should be able to request, at least annually, that the insurer run their credit score and lower their premium it has improved. Some members indicated that this should not be a one-way street, in other words, only adjust the

premium down because of a positive change in the individual's credit score. Possibilities could exist where a new credit score could cause the premium to increase.

- 5) *Point for discussion:* Inform and explain. Insurers should be required to inform consumers that they are using a credit score in underwriting and rating. *Discussion:* Task Force members agreed that consumers should be informed that their credit history will be used, in whatever medium the transaction of business is being used. In the event an adverse action is taken against the consumer, they should be adequately informed as to how their personal credit information influenced that decision, pursuant to the Fair Credit Reporting Act.
- 6) *Point for discussion:* Standardized disclosure. *Discussion:* Task Force members agreed that subject to the limitations of the Fair Credit Reporting Act, the Kansas Insurance Department should develop standards for the written notification along with reasonable parameters with which each company must comply. However, it is not the intent of the Task Force for the written notification to be uniform throughout the industry.
- 7) *Point for discussion:* Black Box. The credit scoring "black box" should be filed with the Insurance Department and could be closed as a trade secret. *Discussion:* Task Force members agreed that the methodology and formulas should be confidentially filed with the Kansas Insurance Department and considered trade secret.
- 8) *Point for discussion:* Prohibitions and limitations. *Discussion:* The task force agreed on the following prohibitions and limitations: Insurers should **not** be allowed to:
 - a) Use disputed information on an individual's credit report or history;
 - b) Use identifiable medical trade lines that are reflected on an individuals credit report or history;
 - c) Use "hits" on a persons credit if they are not generated by the consumer's own activity, are insurance related, or are generated by the consumer to check their own credit rating. Multiple inquiries within a 30-day period should be treated as one.
 - d) Use adverse credit information related to identity theft;
 - e) Use a score that is calculated using income, gender, address, zip code, ethnic group, religion, marital status, or nationality of the consumer. Certainly some of these categories are currently used in insurance underwriting practices, however, it is the intent of the Task Force to prohibit the use of such information only when computing the insurance score.
- 9) *Point for discussion:* Extraordinary Circumstances Appeal Process. There should be an exception process where the score is influenced by catastrophic illness or injury, death of a spouse, business debts, or other extenuating circumstances. *Discussion:* Task Force members debated the need for the process. While some agreed on the following language, others did not: Insurers may offer reasonable underwriting exceptions if an extraordinary personal circumstance adversely impacts a consumer/insured's credit history. The variant wanted by other members was to change the word "may" to "must". It was the contention of some that if you leave it up to the insurer, they will not create such a process, even if some do, all will not.
- 10) *Point for discussion:* No hits and thin files. *Discussion:* The task force agreed on the following:

- a) Use "no hits or thin files" in the following manner:
- i. Take an adverse action against a consumer solely because he or she does not have a credit card account, without consideration of any other applicable factor independent of credit information;
 - ii. Consider an absence of credit information or inability to calculate an insurance score in underwriting or rating personal insurance, unless the insurer does one of the following:
 1. Treat consumer as otherwise approved by the Insurance Commissioner, if the insurer presents information that such an absence or inability relates to the risk for the insurer;
 2. Treat the consumer as if the applicant or insured had neutral credit information as defined by the insurer;
 3. Exclude the use of credit information as a factor and use only other underwriting criteria.

11) *Point for discussion:* Corrected information. If information is corrected on a consumers credit score, an insurer should go back to the beginning of the policy term and refund the overcharge based on the new, lower score. *Discussion:* Task force members agreed that errors could be present on an individual's credit report or history. They agreed that if the wrong information is corrected, the insurer should be obligated to retroactively re-rate and/or re-underwrite the individual for the shorter time frame of the policy period or twelve (12) months.

12) *Point for discussion:* Hold agents harmless. Agents should be held harmless by insurers for providing information and following underwriting guidelines. *Discussion:* Task Force members agreed to language found in the National Conference of Insurance Legislators (NCOIL) model act. The language applies to both captive and independent agents: An insurer shall indemnify, defend, and hold agents harmless from and against all liability, fees, and costs arising out of or relating to the actions, errors, or omissions of an agent who obtains or uses credit information and or insurance scores for an insurer, provided the agent follows the instructions of or procedures established by the insurer and complies with any applicable law or regulation. Nothing in this language shall be construed to provide a consumer or other insured with a cause of action that does not exist in the absence of this language.

13) *Point for discussion:* Confidentiality. *Discussion:* The Task Force understands the importance of privacy and agreed with the language found in the NCOIL model act. The Task Force believes that the following language should be considered by the legislature regarding the sale of policy term information by consumer reporting agencies:

- a) No consumer reporting agency shall provide or sell data or lists that include any information that in whole or in part was submitted in conjunction with an insurance inquiry about a consumer's credit information or a request for a credit report or insurance score. Such information includes, but is not limited to, the expiration dates of an insurance policy or any other information that may identify time periods during which a consumer's insurance may expire and the term and conditions of the consumer's insurance coverage.

- b) The restrictions provided in section (A) do not apply to data or lists the consumer reporting agency supplies to the insurance agent from whom the information was received, the insurer on who's behalf such agent acted, or such insurer's affiliates or holding companies.
- c) Nothing in this language shall be construed to restrict any insurer from being able to obtain a claims history report or a motor vehicle report.

Next Meeting

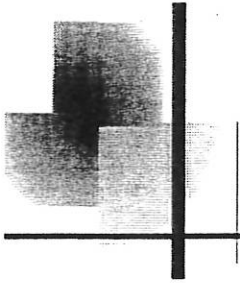
The next meeting for the task force is scheduled for Wednesday, January 8, 2003. The meeting will be held in Room 526-S at the Capitol, and meeting time is at 10 a.m. The purpose of the meeting is to review the draft of the final report due by January 13, 2003.

Discussion ensued on the format used in writing the report. Since the task force members could not provide a consensus on all issues, it was determined that the report would be divided into sections: issues the Task Force agreed upon and then those issues in non-agreement to have the differing opinions both represented. Ms. De Coursey had provided a couple of copies of the format that Legislative Research staff uses. She indicated trying to keep near that format, with a summary of the conclusions and recommendations at the front. Then background information about the Task Force, how it was established, the membership, task force activities and presentations, and then the full discussion of conclusions and recommendations.

Ms. De Coursey was instructed to get the draft final report out to members by January 3, 2003. Task Force members are asked to return comments to her before the January 8th meeting.

Adjournment

Being no further business, the meeting was adjourned.



Credit Scoring Task Force

Minutes

Wednesday, January 8, 2003
State Capitol Building, Room 526-S
Topeka, Kansas
10:00 a.m. – 12:30 p.m.

Call to Order:

Chairperson Michael McGrew called the meeting to order. The following members were present: **Michael McGrew**, Chair, Consumer interest, Lawrence; **Marta Linenberger**, Vice-chair, Consumer interest, Carbondale; Legislators: Sen. **Ruth Teichman**, Stafford and Sen. **Paul Feleciano**, Wichita. Insurance Department: **Ken Grotewiel**. Insurance Companies: **Jim Harwood**, Kansas Association of Property & Casualty Insurance Foreign Companies, Overland Park; **Brad Smoot**, American Insurance Association representative, Topeka; **Bruce White**, Alliance of American Insurers representative, McPherson; **Vanda Easley**, National Association of Mutual Insurance Companies representative, Kansas City; and **David Hanson**, National Association of Independent Insurers representative. Agent Representatives: **Cindy Hower**, KAIA representative, Holton; **Duane Becker**, KAIA representative, Lawrence. Members not present: **Matthew All**, Insurance Department; Rep. **Garry Boston**, Newton; **Tony Kimmi**, Kansas Association of Property & Casualty Insurance Domestic Companies, Manhattan; **Richard Turano**, National Association of Independent Insurers representative, Denver; and Rep. **Jim Garner**, Coffeyville.

Interested persons attending: Representative of Consumer Protection Information Association; Larry Magill, Kansas Association of Insurance Agents, Rick Wilborn, Alliance; and Catherine Rankin, State Farm. Bill Wempe, Jim Newins, Brent Getty, Jarrod Forbes, and Linda De Coursey, Kansas Insurance Department.

Call to order:

Chairperson McGrew called the meeting to order. Persons sitting in for absent members to introduce themselves.

Approval of minutes:

A draft of the minutes had previously been sent to members for perusal.

IT WAS MOVED BY DUANE BECKER AND SECONDED BY BRUCE WHITE TO APPROVE THE MINUTES OF THE DECEMBER 18, 2002 MEETING AS READ. MOTION CARRIED.

Credit Scoring Task Force Final Report Review:

Task Force members were presented an edited report containing suggestions received previously from four task force members. The Task Force reviewed those suggestions and made changes appropriately to produce the final report.

IT WAS MOVED BY MARTA LINENBERGER AND SECONDED BY SEN. RUTH TEICHMAN TO CONCEPTUALLY AGREE WITH THE REPORT AS EDITED. MOTION CARRIED.

Next Step:

The Task Force staff was instructed to complete the changes that were approved and forward the final report to members by email in the next few days. Task Force members were instructed to email the approval of the final document to staff by Sunday evening, January 12. The report will be delivered to the appropriate legislators on Monday, January 13, 2003. If any objections are found to the final changes, please let staff know by email or phone ASAP after you receive it.

Adjournment:

Being no further business, the meeting was adjourned.