

HOUSE BILL REPORT

ESSB 6524

As Reported by House Committee On:
Financial Institutions & Insurance

Title: An act relating to using credit history for insurance purposes.

Brief Description: Restricting use of credit history.

Sponsors: Senate Committee on Labor, Commerce & Financial Institutions (originally sponsored by Senators Prentice, Deccio, Keiser, Kline, Winsley, Franklin, Benton, Regala, Rasmussen, Gardner, Hochstatter, Eide and Kohl-Welles; by request of Governor Locke, Insurance Commissioner and Attorney General).

Brief History:

Committee Activity:

Financial Institutions & Insurance: 2/27/02, 2/28/02 [DPA].

Brief Summary of Engrossed Substitute Bill
(As Amended by House Committee)

- Prohibits insurers from cancelling or refusing to renew a personal insurance policy due to a person's credit history.
- Permits an insurer to consider credit history in the evaluation of a new customer applying for insurance, provided such history is considered in conjunction with other substantive factors.
- Prohibits an insurer from considering certain types of credit history information in the process of underwriting and rate setting.
- Requires insurers to make specified disclosures to a consumer if credit history leads to an adverse action against the consumer.
- Requires an insurer to file its insurance scoring model with the Insurance Commissioner.

HOUSE COMMITTEE ON FINANCIAL INSTITUTIONS & INSURANCE

Majority Report: Do pass as amended. Signed by 6 members: Representatives Cooper, Chair; McIntire, Vice Chair; Hatfield, Miloscia, Santos and Simpson.

Minority Report: Without recommendation. Signed by 5 members: Representatives Benson, Ranking Minority Member; Barlean, Cairnes, Mielke and Roach.

Staff: Thamas Osborn (786-7129).

Background:

Credit reports have been used for many years by the insurance industry in making property and casualty underwriting decisions. More recently, the industry has used credit history information in the setting of insurance rates and the development of "credit scoring" models for underwriting and rate setting purposes. The credit reporting industry consists of over 600 credit bureaus that accumulate credit data on a local or regional basis. These bureaus, in turn, provide data to the three national credit reporting companies: TRW, Trans Union, and Equifax. It is these companies that generate the credit reports most often used by financial institutions, insurance companies, and other commercial entities.

Both the federal Fair Credit Reporting Act (15 USC, Section 1681) and the state Fair Credit Reporting Act (Chapter 19.182 RCW) explicitly allow consumer reporting agencies to release credit reports to insurance companies for insurance underwriting purposes. Accordingly, insurance companies have utilized these reports for many years as a factor to be considered in determining which individuals are eligible for coverage and/or what the terms of such coverage will be. The weight given to credit reports, in conjunction with other factors, varies widely within the industry, thus there is no one practice that can be ascribed to the industry as a whole.

In recent years, the review of an individual's credit report in the insurance underwriting process has given way to the consideration of the individual's "credit score." A credit score is a number generated via a computer program that analyzes the data in an individual's credit report. The computer program uses an algorithm to reduce credit report data to a single numerical score, ranging from 300 to 850. According to the proponents of credit scoring, an individual with a higher score poses a lower risk of loss to the insurance company than does an individual with a lower score.

Generally, credit scores are calculated either by the insurance company using its own computer model or by third-party vendors such as the Fair Isaac Company or Choice Point, who contract with insurers to do credit score calculations. Many different modeling programs are used throughout the industry, thus there is no uniformity between companies with respect to the criteria used in generating the score.

At present, there is no explicit state regulation of the insurance industry's use of either consumer credit information or credit scoring. However, the state Insurance Commissioner (commissioner) does have general legal authority to regulate the rate setting practices of those insurance companies doing business in Washington. This

authority is quite broad and provides a basis for regulatory action whenever a rate setting practice can be proved to be "excessive, inadequate, or unfairly discriminatory." Furthermore, pursuant to administrative rule, the commissioner requires that any rate setting process be "actuarially sound," which means that there must be a demonstrable statistical correlation between the premium rate and the actual risk of loss.

Summary of Amended Bill:

An insurer's decision to cancel or not renew an existing policy of personal insurance cannot be based - in whole or in part - on an insured's credit history. However, an insurer may use credit history as the basis for placing an insured with another company affiliated with the insurer.

An insurer is permitted to consider credit history in the evaluation of a new customer applying for insurance, provided such credit history is considered in conjunction with other substantive underwriting factors. An offer of placement with an affiliate insurer does not constitute a denial of coverage.

There are certain types of credit history information that can neither be considered in rate setting nor form the basis of an insurer's decision to deny coverage, including:

- An absence of credit history;
- The number of credit inquiries;
- Credit history related to medical care;
- Entries related to the initial purchase or finance of a house or car;
- Use of a particular type of credit, debit, or charge card (unless authorized by the commissioner via rule); or
- The dollar amount of a consumer's available credit.

An insured is provided with remedies if his or her insurance coverage is adversely affected by an inaccurate credit history.

An insurer that takes any adverse action against a consumer based on credit history must provide the consumer with written notice. The notice must identify those aspects of the consumer's credit history that played a significant role in the decision leading to the adverse action. The insurer must also inform the consumer that the consumer is entitled to a free copy of his or her credit report.

An insurer must file its insurance scoring model with the commissioner as a condition precedent to the consideration of credit history in either the setting of premium rates or in determining eligibility for coverage. Insurers are prohibited from considering specified categories of credit history information as part of the rate setting process.

The commissioner is required to report to the Legislature on the implementation of the act and regarding issues related to the use of credit history in personal insurance underwriting.

The provisions of the act pertaining to insurance underwriting are applicable to all policies of personal insurance issued or renewed after January 1, 2003.

The provisions of the act pertaining to premium rate setting are applicable to all personal insurance policies issued or renewed on or after June 30, 2003.

Amended Bill Compared to Engrossed Substitute Bill:

The amended bill revises the definition of "personal insurance" by deleting from the definition insurance for motorcycles and recreational vehicles.

Under the amended bill, in the process of underwriting or rate setting, an insurer may consider a consumer's use of a particular credit card, charge card, or debit card, provided that such consideration is explicitly approved by the commissioner via rule. Under the original bill, insurers are flatly prohibited from considering a consumer's use of such cards.

The amended bill states that an "offer of placement" with an affiliate insurer does not constitute a denial of coverage. The original bill stated that "placement" with an affiliate insurer does not constitute denial of coverage.

Appropriation: None.

Fiscal Note: Available.

Effective Date of Amended Bill: Ninety days after adjournment of session in which bill is passed.

Testimony For: (Amended bill) Senior citizen's groups support the passage of the bill. Regulation is necessary because the use of credit scoring by insurers has increased dramatically. Credit scoring has increased the cost of insurance for many consumers. It leads to inconsistent and unpredictable results, insofar as a single consumer may be given different scores by different companies. Many of these scores are too low. Seniors, minorities, and low income persons are most adversely affected by the practice. The bill would benefit these groups. Also, 70 percent of credit reports contain errors and a great many of these errors are significant enough to affect a credit score.

Independent insurance agents support the bill. The provisions requiring disclosures by insurers will assist agents in communicating with customers. The bill is balanced with

respect to the treatment of senior citizens. It is good that the bill explicitly lists the categories of credit information that insurers are prohibited from considering.

Testimony Against: The bill should not be passed because it will harm consumers, most of whom benefit from the use of credit scoring. The bill may have unintended effects on the insurance rates paid by hundreds of thousands of insureds. Credit scoring is a very effective tool for predicting loss, and the bill will make it difficult for the industry to use this tool in an effective manner. Insurers are already required to provide the commissioner with actuarial justification for their rates, thus it is not necessary to change current law regarding rate-setting.

Testified: (In support of amended bill) Gene Forrester, Washington Senior Citizens' Lobby; Carrie Tellefson, Office of the Insurance Commissioner; Ahndrea Blue, Governor's Office; and Bill Stauffacher, Independent Insurance Agents and Brokers.

(Opposed) Mel Sorensen, National Association of Independent Insurance Agents.