HOUSE BILL REPORT
HB 2544

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: Representatives Cooper, Benson, Santos, Clements, Simpson, McIntire, Armstrong, Hunt, Romero, Dickerson, Upthegrove, Chase, Ogden, Haigh, Conway, Kenney, Campbell and Linville; by request of Governor Locke, Insurance Commissioner and Attorney General.

Brief History:
Committee Activity:
Financial Institutions & Insurance: 1/30/02, 2/8/02 [DPS].

Brief Summary of Substitute Bill

- 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, subject to conditions.
- Regulates an insurer's use of credit history in the process of premium rate setting for personal insurance.
- Requires an insurer to file its insurance scoring model with the Insurance Commissioner.

HOUSE COMMITTEE ON FINANCIAL INSTITUTIONS & INSURANCE

Majority Report: The substitute bill be substituted therefor and the substitute bill do pass. Signed by 6 members: Representatives Cooper, Chair; McIntire, Vice Chair; Hatfield, Miloscia, Santos and Simpson.

Minority Report: Do not pass. Signed by 5 members: Representatives Benson, Ranking Minority Member; Barlean, Cairnes, Mielke and Roach.

Staff: Edie Adams (786-7180).

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 Office of the Insurance Commissioner (OIC) 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 OIC 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 Substitute Bill:

An insurer's decision to cancel or not renew an existing policy cannot be based - in whole or in part - on an insured's credit history.

For new customers applying for personal insurance, an insurer can consider credit history in deciding whether to insure the applicant, but credit history cannot be the principal reason for denying insurance to an applicant.

An insurer that takes any adverse action against a consumer based on credit history must provide a written explanation describing why the consumer does not meet underwriting standards. The insurer must also inform the consumer that the consumer is entitled to a free copy of his or her credit report. Insurers cannot take adverse action based on the absence of a credit history, the number of credit inquiries, health-related credit history, types of items financed by credit, the type of credit card, disputed credit information in the process of being reviewed, and other factors the Insurance Commissioner (commissioner) determines are unfair.

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. The commissioner is given discretion to further limit the categories of credit information that may be considered by an insurer if the commissioner finds that such information is unfairly discriminatory or results in discrimination against a protected class.

Substitute Bill Compared to Original Bill:

The substitute bill allows an insurer to consider credit history in evaluating a new customer, but credit history cannot be the predominant reason for denying insurance to the new customer.

The substitute bill imposes disclosure requirements on insurers when adverse actions are taken against an insured based upon credit history. Insurers are barred from basing adverse actions on specified categories of credit information.

An insurer must file its credit scoring model with the commissioner before it may consider credit information in rate setting or eligibility determination. The limits on premium rate adjustments are eliminated.

Appropriation: None.

Fiscal Note: Not Requested.

Effective Date of Substitute Bill: The bill takes effect on January 1, 2003.

Testimony For: This bill addresses a fairness issue regarding how insurance companies use credit scoring. Credit scoring is not uniform among companies, and how much weight each company places on credit scoring or how a particular credit report is scored is a mystery. Credit scoring should not be used without a fair indicator of how the number is apprized. Insurance rates should be based on the merits of one's actions. There have been hundreds of complaints filed in the OIC regarding insurance companies use of credit scoring for underwriting and rate setting purposes. For example, one woman who paid her premiums and never had an accident was told that her premiums went up because her credit rating was bad due to a period of unemployment. A woman who had her insurance premium rates increase by 46 percent, even though she paid all her premiums on time, discovered that her credit score was low due to a bankruptcy filed by her ex-husband. A couple was denied access to reasonable rates because they paid all their bills in cash and, therefore, had no credit history. There are many reasons for a low credit score that do not take into account individual circumstances or credit-worthiness. Using credit scoring to determine if a consumer qualifies for insurance and how much they will pay for coverage is a concern for several reasons. The factors used may disadvantage protected classes of people. Some ethnic groups and religious groups do not use credit and their credit scores may be low or non-existent because of this. Credit reports are not always accurate and it is very difficult to correct errors. Credit scoring penalizes people who encounter temporary hardships. Consumers would like an outright ban on insurance credit scoring, however, this bill simply regulates the insurance companies use of credit scoring.

Testimony Against: The restrictions on insurers use of credit based insurance scores will require low risk consumers to pay staggeringly higher home owner and auto insurance premiums in order to subsidize the losses of higher risk policy owners. Using insurance scores for underwriting and rating has helped make insurance coverage more available for millions of drivers and home owners. Credit data helps insurers determine a fair pricing structure by better matching of rates with risk of loss. Any restriction that tends to impose uniformity on how insurers use credit based insurance scores would hamper their ability to enter new markets or take on more customers. Credit information provides an objective, unbiased tool for underwriting and rating risk. Insurance scores do not consider income, address, race, ethnicity, religion, gender, marital status, disability, nationality or age. Insurance scores have proven to predict future losses. The 20 percent cap is arbitrary and without any actuary support. Many insured will see a rate increase if the cap is implemented. For example, one company indicates that 80 percent of its customers have discounts of 25 percent or more; therefore, 80 percent will see their premiums go up. Insurance companies place risks in categories and then charge premiums for those categories. The problem for the industry is that they are not supposed to look at an individual; they are supposed to classify risks and make sure that

within a risk category there is enough premium charged to pay the bills when a claim is made.

Testified: (In support) Representative Cooper, prime sponsor; Michael Kreidler, Insurance Commissioner; Ahndrea Blu, Governor’s Office; Christine Gregoire, Attorney General; Robert Pregulman, WashPIRG; Mike Dunkin, Insurance Agent; Jenni D’aris and Ron Romer, citizens; Curtis Fackler, Payroll Plus; and Gene Forrester, Senior Citizens Lobby.

(With concerns) Bruce Pleasant, Allstate Agent; Bill Stauffacher, Independent Insurance Agents and Brokers; and Clark Sites, Professional Insurance Agents.

(Opposed) Michael Harrold, National Institute of Independent Insurers; Mike Kapphahn, Farmers Insurance; Larry Kibbee, Alliance of American Insurers; Scott Spriggs, Progressive Auto Insurance; Elizabeth Moceri and Jim DeBruler, Allstate Insurance; Jean Leonard, State Farm Insurance/Alliance of American Insurers; and Basil Badley, American Insurance Agency.