Testimony of

American Property Casualty Insurance Association (APCIA)
before the
House Economic Matters Committee

House Bill 168- Motor Vehicle- Use of Credit in Rating Policy
House Bill 221- Motor Vehicle Insurance - Use of Credit History in Rating Policies

February 11, 2021

<u>Letter of Opposition</u>

The American Property Casualty Insurance Association (APCIA) is a national trade organization representing nearly 60 percent of the U.S. property casualty insurance market. APCIA appreciates the opportunity to provide written opposition to House Bill 168 and House Bill 221 which would ban the use of credit history in rating a private passenger auto policy. House Bill 168 and House Bill 221 prohibit a private passenger motor vehicle insurer from using an applicant's or insured's credit history to rate a risk in any matter.

APCIA and the property casualty insurance industry recognize that today, there is greater scrutiny of racial and social equity, justice, and inclusion issues. The industry is committed to creating a more diverse and inclusive workforce, providing fair treatment to all customers, and helping provide our unique expertise in risk mitigation, risk management and loss prevention to make insurance more affordable in low income, minority and traditionally underserved communities. We have assembled a new Board Working Group on Social Equity & Inclusion, to identify areas for constructive change, balanced with strong, continued support and promotion of risk-based pricing as the foundation of the business of insurance and fairness for consumers.

Use of Credit in Maryland

Maryland laws provide very specific criteria and restrictions in the use of credit in rating Maryland private passenger auto policies. Section § 27-501(e-2) of the Maryland Insurance Article provides the guidelines for the use of credit. An insurer may not refuse to underwrite, cancel, refuse to renew, or increase the renewal premium based, in whole or part, on the credit history of an application. An insurer may use credit to rate a **new policy** but 1) may only use credit history going back five years; 2) advise the applicant that credit is used and if requested identify the portion of premium based on credit; 3) may not use the lack of credit or number of credit inquiries as a factor in rating; 4) must review an insured's credit history every two years or by request; and if there is an improvement adjust the premium to reflect the improvement.

Maryland laws provide very specific criteria in regulating underwriting practices of private passenger auto insurers. Section § 27-501(a)(1) of the Maryland Insurance Article prohibits unfair discrimination in underwriting by making clear that an insurer or insurance producer may not cancel or refuse to underwrite or renew a risk or class of risk based wholly or partly on race, color, creed, sex, or blindness of an applicant or policyholder or for any arbitrary, capricious or unfairly discriminatory reason. Further, this Section states that an insurer or insurance producer may not cancel or refuse to underwrite or renew a risk or class of risk except by the application of standards that are reasonably related to the insurer's economic and business purpose. In addition, Maryland only permits the use of credit for underwriting private passenger auto but does not permit it for the use of homeowner's insurance.

Insurers Use of Credit

It is important to understand how insurers use credit information and to note that there are significant differences between the credit scores used by lenders and the credit-based insurance scores used by many insurers. Although both are derived from information found on credit reports, the information is measured differently. Insurers use credit information in developing insurance scores to predict the likelihood of future insurance loss. Credit-based insurance scores provide an objective measurement of how one manages the risk of credit. Lending institutions, on the other hand, use credit scores to determine the availability, amount and price of credit products offered to the consumer. Lending institutions use credit to determine the likelihood of repayment. The most significant difference between insurers and lending institutions is that insurers never consider income.

In addition to income level, one's address, ethnicity, religion, gender, familial status, nationality, age education, occupation and marital status are also not considered within a credit score calculation. Further, there is no reliable evidence that points to insurance scoring resulting in higher insurance rates for any specific class of individual. Low credit scores do not correlate to a specific territory or class of individuals. On the contrary, both high and low scores are found across all income levels, and territories.

Every serious and reputable actuarial study on the issue, including a study released in 2007 by the Federal Trade Commission[1], has reached the same conclusion: there is a very high correlation between insurance scores and the likelihood of filing insurance claims. A number of states have reached the same conclusion is in conducting their own studies. The Virginia Bureau of Insurance[2] concluded in 1999 that "[i]n every case where insurers have proposed to use credit scoring as a rating factor…the use of credit scoring has been found to be statistically correlated to losses." More recently, the Vermont Department of Financial Regulation stated, in a 2016 report, that "[c]redit-based insurance scores are a predictor of claims risk that appears to provide a financial benefit to many Vermont policy holders.[3] Credit-based insurance scores allow insurers to write business that they may not have accepted in the past, and to offer lower rates to many insureds. The majority of consumers have good credit-based insurance scores and benefit accordingly – with rates refined to reduce disproportionate subsidies of higher risk individuals. An annual survey released by the Arkansas Insurance Department between 2005 and 2017[4] consistently found approximately 50 percent of consumers in that state save money due to insurers' use of credit information while only 20 percent pay more because of that same use. The remaining 30 percent are otherwise unaffected. To put it another way, policies decreasing in premium due to insurance scoring outnumbered policies increasing in premium by a factor of 3 to 1.

Greater access to information allows insurers to "grant and price coverage more efficiently, producing

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[1] [1]https://www.ftc.gov/news-events/press-releases/2007/07/ftc-releases-report-effects-credit-based-insurance-scores
[2] Available upon request.
[3] https://legislature.vermont.gov/assets/Legislative-Reports/Credit-based-Insurance-Scoring-Report-12-15-16.pdf
[4] https://insurance.arkansas.gov/uploads/resource/documents/2017credit.pdf

cost savings that could result in lower premiums," and permits insurers to "evaluate risk with greater accuracy, which may make them more willing to offer insurance to higher-risk consumers for whom they otherwise would not be able to determine an appropriate premium."[5] An indicator of the competitiveness is the market share of Maryland Automobile Insurance Fund, (MAIF) who is the writer of auto insurance of last resort. MAIF's market share has dropped from 4.69% of the total written premium for private passenger auto in 2005 to 1.40% in 2019.[6] The fact that MAIF's market share has decreased while other writers have increased would indicate that insurers are willing to accept more risk because they can better evaluate risk using various risk factors. Thus, more and more Marylanders are no longer being insured through MAIF.

Further demonstrating the value of the use of credit, APCIA has been analyzing data demonstrating that credit-based insurance scores correlate to specific risky driving behavior. For example, consumers with higher credit scores are less likely to brake hard or excessively accelerate -- risky driving behavior associated with higher loss costs.

Contrary to the claim that credit-based insurance scores do not predict risky behavior but instead unfairly discriminate against groups, when our analysis is complete, this data could provide a real-world demonstration that certain driving behavior is in fact captured by credit. Prohibiting the consideration of these factors, as HB 168 and 221 would, creates inequity by leading to pricing that is not risk-based.

We understand the desire of legislators to address social inequities, but undermining risk-based pricing by prohibiting the use of certain actuarially justified rating factors could actually exacerbate those inequities. If credit information is eliminated from consideration, it is highly probably that auto insurers will come to rely even more heavily on other factors like driving history as recorded in motor vehicle records (MVRs).

MVRs are notoriously incomplete, In fact, it is these very deficiencies with MVRs that lead to, in part, the widespread use of credit-based insurance scores. Overreliance on MVRs can be especially harmful for minorities who are more likely to be the subject of traffic law enforcement actions, as shown by multiple studies, including the Stanford Open Policing Project[7].

Placing greater weight on a consumer's prior driving history by eliminating the use of other factors more predictive of risk not only harms the very consumers the proposed legislation seeks to protect, but also undermines the fairness and solvency purposes of state regulations that require rates to reflect the risk of future losses. Although helpful, over-reliance on motor vehicle records or prior accidents diminishes insurers ability to accurately predict future claims experience.

What happens when a state bans credit?

In 2002, Maryland did just that with respect to homeowner's insurance and rates went up. The rates went up at a faster rate than the rest of the country (53% to 36%) between 2002 and 2007, and they went up faster than they did in neighboring states and at least one company left the market.

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[5] Id. Federal Trade Commission, July 24, 2007

[6] "Id. The Maryland Insurance Administration's 2006 Report on the Effect of Competitive Rating in the Marketplace" & '2019 NAIC Annual Statement data calculated by APCIA using the S&P Global Market Intelligence database.

[7] https://openpolicing.stanford.edu/

Restrictions on the use of underwriting factors such as credit could harm the marketplace, thereby negatively impacting a state's economy. Such limits create unfair subsidies among consumers, stifle competition, limit innovation, and force insurers to be more cautious about writing new business or expanding into new markets. As a direct result, consumers enjoy less choice, less availability, and higher average costs. This not only increases the uncertainty risk premium, but insurers are further forced to rely on a decreasing number of legitimate predictive factors, factors that are not necessarily proportionately distributed among different groups. Individual consumers who fare poorly with a small range of very limited factors may have vastly fewer and affordable insurance coverage options without the use of a multiplicity of factors.

For these reasons, APCIA asks the Committee to provide unfavorable reports on House Bills 168 and 221.

Respectfully submitted,

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