Center for Economic Justice
Review of NCOIL Insurance Scoring Model
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The NCOIL Model Fails to Provide Meaningful Consumer Protections

The insurance industry pushes the NCOIL model throughout the states, calling the model a balanced approach that represents a compromise among various stakeholders. In fact, the NCOIL model is neither balanced nor a compromise.

The NCOIL model was the result of a negotiation between insurer trade associations and one or two of the large independent agent groups. In exchange for a liability shield from insurers, the agents group endorsed credit scoring. And then it was rubber-stamped by NCOIL members who historically have been a very friendly forum for insurers.

A recent analysis by the Consumer Federation of America documents the excessive influence of the insurance industry on NCOIL decision making and many pro-insurance industry and anti-consumer actions by NCOIL. The development and vote of the NCOIL credit scoring model in the NCOIL Property Casualty Committee illustrates how biased the NCOIL process is towards the insurance industry.

In November 2002, the NCOIL P/C Committee adopted the credit scoring model by a vote of 20-5. Those in favor of adoption were:

Rep. Jay Bradford, AR **Chairman of the Board and CEO, First Arkansas Insurance Democrat**
Rep. Rich Golick, GA **Georgia Counsel for Allstate Republican**
Rep. Timothy Osmond, IL **Insurance Agents Republican**
Rep. Ronald Crimm, KY **Insurance, Thoroughbred Associates Republican**
Rep. Shirley Bowler, LA **Republican**
Rep. Dan Flavin, LA **Licensed Real Estate Broker Republican**
Sen. Bill Bullard, Jr., MI **Republican**
Rep. Stephen Ehardt, MI **Republican**
Rep. Andrew Richner, MI **Republican**
Sen. Alan Sanborn, MI **Republican**
Sen. Cal Larson, MN **"Consultant" Republican**
Rep. George Keiser, ND **Owner Printing Service Republican**
Rep. Frank Wald, ND **Insurance and Securities Broker Republican**
Rep. Leo Fraser, NH **Claim Auditor Republican**
Sen. Neil Breslin, NY **Elected Official, Lawyer, Democrat**
Assem. Nancy Calhoun, NY **Elected Official, Republican**
Rep. David Evans, OH **Retired State Farm Insurance Underwriter Republican**
Rep. Brian Kennedy, RI **Real Estate Broker Democrat**
Rep. Mark Young, VT **Banker, Republican**

adverse action notices to new business applicants who were treated adversely because of consumer credit information. The NAIC best practices paper provides a better definition of adverse action, which eliminates the ambiguity created by the Supreme Court in *GEICO.*

Second, the adverse action notice disclosure specifically allows insurers to use standard industry reason codes. These codes are meaningless to consumers. Even if the consumer could understand the terms – which is not the case for most of the reason codes – the reason provides no guidance as to what the problem in the credit report was. Attached are industry standard reason codes

2. Non-Substantive "Protection" – Prohibited Factors in Scoring Model

The NCOIL model bans the inclusion of income, gender, address, zip code, ethnic group, religion, marital status, or nationality of the consumer as a factor in the insurance score, but is silent about factors or scores which serve as a proxy for these factors. The data are clear that permitted factors are correlated to race and income. The claim of color-blind models is a fiction. Just because income or race are not included in the models does not mean that the models are not predictive or income or race; claims are not included in the models but the models are predictive of claims. The industry has a history of using of "color-blind" factors which discriminate against low-income and minority consumers, such as age and value of the home.

3. Non-Substantive "Protection" – No Sole Use

The NCOIL prohibits the use of insurance score as the sole factor for underwriting or rating. This provides no consumer protection as every insurer uses other factors for underwriting or rating already. These sections do not alter any insurers' use of insurance scoring and allow insurance scoring to have an unlimited impact on rates – as long as some other factor was "considered." The fact remains that consumers experience higher rates because of insurance scoring and insurance scoring alone.

The NCOIL also prohibits an adverse action based solely on the absence of a credit card account. As with the other "sole use" provisions, this provides no consumer protection and addresses an industry practice used in the early 1990's for a few months.

4. Non-Substantive "Protection" – Thin Files

The NCOIL model pretends to protect consumers with thin files or no scores from adverse actions, but provides three options which allow insurers to, in fact, take adverse action against huge portions of the population. Option 1 is anything the insurer can demonstrate with statistics, which is meaningless because no insurance regulator has any independent data to verify an insurer's claims. If an insurer comes to the regulator and shows a higher loss ratio for thin files, there is no way to verify this claim. Options 2 and

loan performance of lenders, insurance regulators, policy makers and the public have no independent information in insurance scoring policy debates.

Consumer Protections Missing from the NCOIL Model

Any effort to provide meaningful consumer protections must include the following provisions, all of which are missing from the proposed regulation. This list is not exhaustive.

1. The use of credit scoring is prohibited for conditioning payment plan eligibility. Payments plans are an essential tool for making insurance available to consumers by making insurance affordable to consumers. Insurers who require full policy payment up front are denying coverage to large numbers of insurers. Payment plan eligibility should be conditioned only a consumers' payment history with the insurer offering the policy. There is no reason to use credit scores for payment plan eligibility. Insurance scores, in theory, predict risk of loss and not likelihood of making a payment. Insurers stress this repeatedly in their efforts to distinguish lending credit scoring from insurance credit scoring. Further, even a lending credit score is irrelevant for insurance because the insurer is never in a position to provide coverage without payment. The proposed regulation does not address the use of credit information to condition payment plan eligibility.

2. An adverse action should be defined as any underwriting, tier placement or rating activity that results in an insurer failing to offer the most favorable terms of coverage and premium to a existing policyholder or new applicant who, if he or she had a more favorable consumer credit report, would have been eligible for the more favorable treatment. The proposed regulation fails to address insurer's abuse of the FCRA's adverse action language – the failure to provide adverse action notices to most or all new business applicants who failed to receive more favorable terms of coverage and rates because of the insurers' consideration of the consumer credit report. Insurers have mistakenly and inappropriately relied upon the "increase in any charge" language of the FCRA to argue that new customers cannot suffer an adverse action because there can be no increase in a charge for that consumer.

   For purposes of this regulation an "adverse determination" includes, but is not limited to, the following situations:

   a. An offer of insurance in an insurance company that is affiliated with an insurance company with lower rates, if the consumer does not qualify for coverage in the lower-rated insurance company because of the consumer's credit score. The lower-rated insurance company has taken an adverse action.

   b. An offer of insurance in an insurance company by an independent agent who also represents an insurance company with lower rates, if the consumer does not qualify for coverage in the lower-rated

insurance company because of the consumer's credit score. The lower-rated insurance company has taken an adverse action.

c. An offer of insurance at a premium or rate that is higher than the premium or rate the consumer would pay if the consumer had the best possible credit score, all other factors being the same. The company charging the higher premium or rate has taken an adverse action.

3. Provide meaningful information in the adverse action notice. Consumers should be provided with their credit score, the list of factors included in the credit score, the consumers' value for each of the factors and optimal value for each of the factors. The purpose of the adverse action reason disclosures is to empower the consumer to identify what information – or what lack of information – in the consumer credit report led to the adverse action and for the consumer to be able to either contest inaccurate information or change his or her credit characteristics over time.

   For example, compare the difference betw

information. Allowing insurers to keep credit scoring models secret would be like allowing the Insurance Services Office to hide both the derivation of its loss costs and the loss costs themselves because ISO claimed the analytic model and output as a trade secret. No insurance regulator would permit such an action by ISO, yet the proposed regulation contemplates the same type of secrecy for credit scoring models. Further, the trade secret claim made insurers and vendors for the various credit scoring models is without merit. In some states, insurers and vendors file

of inquiries because of how unrelated an inquiry can be to expanding a consumer's debt load. Length of time credit has been established should be prohibited because it is a proxy for age. Type of lender should be prohibited because it discriminates against consumers who live in neighborhood where the primary financial institution is a consumer finance company and not a bank branch. Vehicle service accounts – consumers are penalized if they have, say, a credit card for a tire store – should be prohibited because a consumer should not be penalized for having an account with a tire store. The number of credit cards should be prohibited because the credit evaluation should focus on management of actual debt, not on the fact that a consumer has a large number of cards that were used once and never again. As the models are made available to the public, this list may grow.

9. Insurers should be required to obtain and use a three-bureau merged credit report in developing credit scores. Consumers should not be penalized because of differences in credit information maintained by the different bureaus.

10. Insurers should be required to confirm the consumer's credit score two weeks after the initial credit score. Consumers should not be penalized because credit scores can depend upon the point in the credit card cycle that the credit report is generated.

11. Insurers should be prohibited from penalizing a consumer for a collection account or delinquency report resulting from a catastrophic or life event and should be required to establish a procedure for consumers to inform the insurer of such events. There must be greater consumer protection that a prohibition against consideration of collection accounts or delinquency reports identified with a medical industry code. This is insufficient protection for consumers who are the victims of a medical catastrophe because most medically-related delinquencies or collection accounts are not coded as medical industry. Rather, a consumer will likely pay medical bills with either a credit card or other form of credit and the collection or delinquency will show up on these other types of credit. The proposed regulation should prohibit insurers from considering collection accounts or delinquency reports resulting from a catastrophic event and provide the consumer with a procedure to inform the insurer about such events. For example, something along the lines of:

EFFECT OF EXTRAORDINARY EVENTS.

(a) Notwithstanding any other law, an insurer shall, on written request from an applicant for insurance coverage or an insured, provide reasonable exceptions to the insurer's rates, rating classifications, or underwriting rules for a consumer whose credit information has been directly influenced by a catastrophic illness or injury, by the death of a spouse, child, or parent, by temporary loss of employment, by divorce, or by identity theft. In such a case, the insurer may consider only credit information not affected by the event or shall assign a neutral credit score.

(b) An insurer may require reasonable written and independently verifiable documentation of the event and the effect of the event on the person's credit before granting an exception. An insurer is not required to consider repeated events or events the insurer reconsidered previously as an extraordinary event.

(c) An insurer may also consider granting an exception to an applicant for insurance coverage or an insured for an extraordinary event not listed in this section.

12. There should be a collar on the rate impact of credit scoring. There should be a maximum percentage differential of 25%, for example, between the rates (including consideration of rating tiers) for two consumers with, respectively, the best and the worst credit scores and with otherwise identical underwriting and rating characteristics. Credit scoring should not have greater impact on premiums than factors providing loss prevention incentives to consumers.

13. Insurers who use credit scoring should be required to file the following information with their credit scoring underwriting and rating plan:

    a. Any underwriting guidelines or tier placement guidelines based in whole or in part on consumer credit information;

    b. A complete description of any rating factor based in whole or in part on consumer credit information;

    c. A multivariate analysis of the relationship between credit and expected losses and which simultaneously considers the impact of all other rating, tier placement and underwriting factors on expected losses.

    d. An analysis of the expected impact on consumers of the insurer's use of consumer credit information, including the number of consumers paying less and the number of consumers paying more for insurance when consumer credit information is used compared to when consumer credit information is not used by the insurer. The analysis shall also include the number of consumers moving from one rating tier to another because of the insurer's use of consumer credit information.

    e. A report of the number of consumers in each credit score category used by the insurer by ZIP Code.

    With this information, the Commissioner and the public will be able to analyze the impact of credit scoring on insurance markets.