

## **Credit-based Insurance Score – Homeowners Insurance – P044804**

### **Comments of the Center for Economic Justice on**

#### **Model Section 6(b) Order for Data from Insurance Companies for Use in FACT Act Section 215 Study of Insurance Scoring**

**June 18, 2008**

The Center for Economic Justice (CEJ) supports the Commissioners' resolution to use the FTC's compulsory process pursuant to Section 6(b) of the FTC Act and Section 215 of the Fair and Accurate Credit Transactions Act (FACTA). The compulsory process will help to insure that a more accurate data set be collected. There is no need to rely upon "cooperation" by insurers as the basis for obtaining necessary data. Insurers can demonstrate their willingness to cooperate by timely complying with the request for data.

#### **General Recommendations**

**1. Request similarly detailed data from auto insurers to revisit and improve the analysis of insurance scoring in auto insurance.**

The draft data request generally provides for greatly expanded data for analysis than data used in the prior insurance scoring study for personal auto insurance. The differences include, among others:

- Application data, which are essential for any meaningful analysis of the impact of insurance scoring on the availability and affordability of insurance generally and on protected classes specifically;
- Identification of individual companies, which is essential for data quality review, for identification of company-specific impacts of insurance scoring and for identification of whether business was or was not underwritten on the basis of consumer credit information;
- Identification of additional variables to include and better control for other explanatory factors in the FTC's analytic models.
- Comprehensive data, which is essential for data quality review and reconciliation to other insurance reports, such as the statutory annual statement;
- Data from a greater number of insurers, which is essential to provide a review of all relevant markets, including geographic, type or risk and type of product.

In short, the proposed data request represents the data necessary for a study responsive to congressional intent in Section 215 of the FACT Act and not simply data insurers choose to provide, as was the case in the auto study. The proposed data request will allow for a much more meaningful, rigorous and independent analysis than the auto study.

The Board's Order and subsequent data request acknowledges the limitations of the prior study of insurance scoring and auto insurance. Consequently, the data request should be expanded to include data for auto insurance – specifically, lines 19.1, 19.2 and 21.1 of the state page of the property casualty annual statement.

**2. Provide a formal role for the National Association of Insurance Commissioners (NAIC) by:**

- a. Establishing a formal peer review process by the NAIC of FTC processes and analyses related to data collection, data quality review, data analysis and conclusions; and**
- b. Collaborating with state insurance regulators for any necessary prospective data collection for application and sales data.**

Although FTC staff has significant expertise in economic analysis, the collection of and analysis of insurance data related to insurance scoring requires experience and expertise with insurance data, underwriting, risk classification and rating. The FTC should obtain this additional expertise by establishing a formal peer review process with insurance regulators through the NAIC. The formal peer review should include data requests, data quality review and verification, data analyses and resulting conclusions.

Insurers are likely to fight the proposed request for data with many objections. One likely objection will be that insurers do not maintain application data for any period of time required by the data request. Even if true, application data is absolutely essential for any meaningful review of the impact of insurance scoring on the availability and affordability of auto and homeowners insurance. Consequently, if insurers are unable or unwilling to provide the historical application data necessary for the study, and if the FTC does not have the authority to compel insurers to collect, retain and report data on a going-forward basis, the FTC should collaborate with state insurance regulators who clearly have such authority to ensure that the necessary application data is obtained on either a historical or prospective basis.

### **Technical Recommendations**

- 3. Include all type of products and policy forms reported in the statutory annual statement state page line 1, fire, and line 4, homeowners insurance; distinguish between residential and commercial for line 1.**

The proposed data call request specific types of products and policy forms, but omits others which are included in line 1, dwelling fire, and line 4, homeowners, of the state page of the property casualty statutory annual statement. The data request should ask for all policies issued which were reported in these two annual statement lines and identify the type of product and policy form for each policy. This approach will both enable a review of data completeness through reconciliation with the statutory annual statement and include critical products like policies for manufactured homes. Analysis of manufactured home policies is relevant and necessary because such the purchasers of such homes and related property insurance will likely be heavily weighted towards protected classes.

Line 1, dwelling fire, of the state page includes both residential and commercial policies. Consequently, the policy information should include an identifier for residential versus commercial to enable the FTC to exclude the commercial policies after using the commercial data for reconciliation purposes.

- 4. Reconcile reported premium and loss amounts to the statutory annual statement;**

As stated in item 3, the data should be reconciled to the state page lines 1 and 4 of the statutory annual statement to ensure completeness of data submissions. Reporting insurers should be required to report any substantial deviations between annual statement totals and sums of premium and losses in the data request reports.

- 5. Include identification of individual insurance company issuing the policy within the insurer group**

Insurers typically operate a number of insurance companies within an insurance group. The data request should require that all insurance companies within the insurance group writing the affected lines of insurance report their experience and the reports should include an individual company identifier. The company identification is necessary to allow reconciliation to the statutory annual statement of the insurance company and to allow a variety of data analyses based on individual company attributes. Individual company analysis within an insurance group is necessary because insurers typically dedicate different insurance companies to different markets, where a market may be preferred risk or standard risk.

## **6. Distinguish between residual market mechanisms**

The proposed data call requests data from insurers for the voluntary and involuntary market. It is necessary to distinguish different types of involuntary or residual market mechanisms. An assigned risk plan, typically found with auto insurance, is an assignment mechanism whereby consumers seeking insurance from the residual market are assigned to private market insurers. Consequently, insurers have policies issued through both their voluntary market operations and policies assigned through the assigned risk plan. Most homeowners insurance residual markets are FAIR plans, in which the residual market actually issues the policy and is effectively a stand-alone insurer. With FAIR plans, insurers will not be issuing the residual market policies and, consequently, will not have any information on residual market insureds. The data request should limit reporting by insurance companies to those residual market mechanisms by which the insurer issues a policy and not include FAIR plan type policies.

## **7. Include coverage information**

It is important and necessary to include coverage information to reasonably evaluate the price of insurance. The data request should include reporting of important exclusions which significantly affect coverage and price of the product as well as information on deductibles, which can also dramatically affect coverage and price

## **8. Require reporting of all claims by cause of loss; do not ask insurers to segregate claims by catastrophe vs. non-catastrophe**

The data call should require the reporting of all individual claims during the experience period with date of loss and cause of loss. This type of reporting will enable the FTC to identify catastrophe events and exclude catastrophe losses on a consistent basis. The FTC can also analyze the relationship between catastrophe losses and insurance scores; in theory, there should be no relationship, but the presence of a correlation would suggest insurance scoring as a proxy for other causal factors. Further, this approach to reporting claims and identify catastrophe claims will ensure consistent treatment of catastrophe claims and catastrophe events and avoid different reporting companies employing different definitions of catastrophe losses, which will affect the analysis of non-cat losses.

The reporting of claims by cause of loss will enable the FTC to evaluate the relationship between insurance scores and specific types of claims. In addition to catastrophe vs. non-catastrophe, the FTC would be able to analyze the relationship of insurance scores to fire losses separately from liability losses separately from theft losses, for example. The analysis of insurance scores by type of loss is analogous to evaluating insurances versus type of auto coverage – third party liability vs. first party physical damage – and allows the examination of the relationship of insurance scores to at-fault versus not-at-fault claims and allows the examination of the pseudo-scientific theories about insurance scoring and psychological makeup offered by insurers and their apologists as a defense for insurance scoring.

**9. Evaluate the impact of catastrophe events on insurance scores**

The FTC should evaluate the impact of catastrophe events on policyholders' insurance scores by comparing insurance scores of policyholders before the policyholder made a catastrophe claim and a year after the catastrophe claim. Such an analysis may shed light on the impact of catastrophes on insurance scores with resulting implications for the availability and affordability of insurance.

**10. Include more than the top nine writers of homeowners insurance.**

Based on the 2006 Market Share Reports for Property Casualty Insurance, published by the National Association of Insurance Commissioners, the top writers of homeowners insurance, as reported in line 4 of the state page of the statutory annual statement, were:

1. State Farm
2. Allstate
3. Zurich (including Farmers and Foremost)
4. Nationwide
5. Travelers
6. USAA
7. Liberty Mutual
8. Chubb
9. American Family

In addition to these nine insurers, we recommend the following insurers (insurance groups) be included in the request for data:

10. Auto Owners Group – significant regional writer, top ten in market share in several states for homeowners, 11<sup>th</sup> largest writer nationwide of dwelling fire;
11. Erie – significant regional writer, top ten in market share in several states;
12. Safeco – significant regional writer, top ten in market share in several states;
13. Hartford – significant national writer, top ten in many states, focuses on older consumers through affiliation with AARP, 19<sup>th</sup> largest writer nationwide of dwelling fire;
14. California State Auto Group – 2006 homeowners premium of over \$400 million, representing an amount larger than total market in many states;
15. AIG – largest writer, by far, of dwelling fire insurance;
16. FM Global – fourth largest writer of dwelling fire insurance;
17. Assurant – fifth largest writer of dwelling fire insurance

From the NAIC Market Share Report, the following were the top writers of dwelling fire (line 1) insurance by nationwide share of written premium:

1. AIG – 21.1%
2. Travelers – 6.5%
3. Zurich – 6.0%
4. FM Global – 5.4%
5. Assurant – 5.3%
6. Liberty Mutual – 3.5%
7. Allianz – 2.25%
8. Allegheny – 2.07%
9. Citizens (Florida) – 1.9%
10. Balboa – 1.8%
11. Auto Owners – 1.8%

By including the additional 8 insurers listed above, the FTC will obtain data necessary to cover the top writers in almost all states for both homeowners and dwelling fire insurance.

**11. Evaluate impact of different scoring models on individual insurance scores;**

The FTC should obtain different scoring models from individual insurers using proprietary models and from vendors whose models are used by reporting companies. The FTC should then run individual consumer credit information through various models to evaluate the impact of various models on a consumer's score and the impact of an insurer's choice of model on the availability and affordability of insurance. The FTC should particularly evaluate differences in models targeted at standard or preferred markets and models targeted to different types of marketing segments.

**12. Identify which scoring model was used for individuals and what resulting insurance score was; Identify insurance scoring factor / tier utilized in underwriting and rating based on insurance score.**

Insurers have choices of insurance scoring models. The selection of the scoring model is itself a channeling device for underwriting of applicants. The FTC should identify which models were used and if the selection of models by insurers has a disparate impact against low-income and minority consumers.

In addition, the data request should include the insurance score which was used for the underwriting and rating of the policy and the insurance score rating factor. With these data items – or with the insurance score factor, alone – the FTC will be able to analyze the relationship between insurance scores and actual prices quoted consumers. Of course, this information should be part of both policy and application data sets.