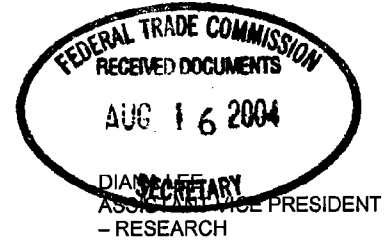




**Property Casualty Insurers
Association of America**

Shaping the Future of American Insurance

2600 South River Road, Des Plaines, IL 60018-3286



August 16, 2004

Federal Trade Commission
Office of the Secretary
Room H-159 (Annex N)
600 Pennsylvania Avenue, NW
Washington, DC 20580

RE: FACT Act Scores Study, Matter No. P044804

Property Casualty Insurers Association of America Comments

The Property Casualty Insurers Association of America (PCI) offers the following comments to the FACT Act Scores Study (Matter No. P044804). PCI, a leading property and casualty trade association, represents over 1,000 companies that write 38 percent of the US property/casualty insurance market. PCI member companies write all lines of coverage, including automobile, homeowners, workers' compensation, surplus lines and reinsurance, in all 50 states and the District of Columbia. The membership is comprised of every type of insurance company – stock, mutual, reciprocal and Lloyds.

Pricing accuracy is a key component of the competitive insurance market. Faced with less accurate pricing information, insurers may become more conservative in determining which risks they will accept. Credit information is just one of a variety of factors many insurers use to price and underwrite property and casualty insurance. It is an important factor and one that provides information about a risk that no other factor can provide. Policyholders have benefited from the use of credit-based insurance scores, as credit risk evaluation increases the availability of property-casualty insurance coverage to more consumers and helps to keep current policies in force. If this factor were no longer allowed to assess risk, policyholders would be placed into less refined and less accurate rating categories. Generally, if insurers were precluded from using this factor, those policyholders who are better insurance risks would have rate increases.

We understand that you are speaking with Michael J. Miller of EPIC Consulting, LLC regarding the possibility of using data he has gathered for automobile insurance and a methodology to study the effects of credit-based insurance scores. We encourage you to continue working with Mr. Miller in your efforts to study this issue, and also suggest that you review the November 15, 2002 American Academy of Actuaries' report, entitled *The Use of Credit History for Personal Lines Insurance: Report to the National Association of*

Insurance Commissioners. Specifically, the section on “Designing a Study to Evaluate Whether the Use of Credit History Disproportionately Affects Protected Classes or Low-Income Groups” (p. 38) may be relevant to your charge.

Below, we have responded to the specific questions in the Request for Comments. These responses pertain to the study of the effects of the use of credit-based insurance scores as they relate solely to property/casualty insurance. Since some of the questions overlap in content, we have grouped those together. We hope that these comments will aid in ensuring a methodologically sound study that addresses the interests of the insurance-buying public.

1. How should the effects of credit scores on prices and availability of property/casualty insurance be studied? What is a reasonable methodology for measuring the impact of credit scores on insurance?

A reasonable study on credit-based insurance scores should examine the relationship between such scores and insurance loss likelihood. It can determine whether the use of insurance scores adds any new information about losses that is not provided by other underwriting or rating factors. A reasonable methodology for measuring the impact of credit-based insurance scores on insurance prices and availability) includes a multivariate statistical analysis so that all risk factors are measured simultaneously, based on the loss cost (i.e., average loss per insured vehicle, or combined claim frequency and claim severity).

Insurance companies vary in their proprietary insurance scores and the types of models used to determine scores, hence making aggregation of meaningful data impossible. Therefore, we recommend that a uniform credit-based insurance score from one source (e.g., Attract scores from ChoicePoint Services, Inc.) be obtained to match insurance policies with the corresponding credit histories of the named insured in each policy. Other underwriting variables such as age, gender, and driving history can be controlled using multivariate regression analysis. Multivariate analysis, then, can be an effective tool to measure the impact of credit information upon the likelihood of insurance losses and, consequently, the ultimate price of the insurance product

With regard to availability of insurance, studies of the insurance marketplace often use the size and direction of the residual market mechanism for a specific given line of insurance to measure the competitive nature of the market as well as the availability of that coverage. Generally, we have seen that the size of residual market population is small and declining. We have not seen insurer use of credit information negatively affecting the availability of personal lines insurance.

2. What is a reasonable counterfactual to the current use of credit-based insurance scores?

Interpreting this question broadly, we suggest one counterfactual, or alternative hypothesis. That is, the FTC could evaluate whether credit information is not predictive of insurance losses or that it does not carry any additional predictive power not already explained by other currently used rating elements.

3. – 6. What is the appropriate technique for studying prohibited factors and to determine whether insurance scores or specific factors in credit scores result in “negative or differential treatment” of protected classes? What data would be required? What data are available?

Since insurance companies do not collect data on policyholders' race, ethnicity or income, nor do they access this information when underwriting applicants, credit-based insurance scores are used in an objective and legitimate manner. There is no deliberate negative or unfair treatment made against any individual consumer or any group of consumers.

The issue to examine should be: “Can insurance scores act as a proxy for the race or income of insurance consumers when other characteristics are held constant?” In general, a multivariate analysis could be performed to determine if individual scores tend to have any statistical relationship with race/ethnicity and income separately. Other insurance characteristics could be controlled for distributional differences across various groups. One way to study this is to build a multivariate model to predict individual insurance scores using traditional insurance factors, along with selected demographic information. In this way, the distribution-adjusted results could be studied to see if they are predictive of race or income.

With respect to data, ideally, the race or ethnicity and income level of each policyholder would be needed to conduct this analysis with total accuracy. Such information, however, is not readily available. Some have suggested the use of census data as a surrogate for race, ethnicity or income level. Without commenting on the wisdom of such use, allow me to raise issues for your consideration. First, we believe there are limitations as to inferences about individual characteristics that can be made based upon where someone lives. For example, census data contains information on both insurance purchasers and non-insurance purchasers. Using census data, depending on the context in which it is used, could lead to conclusions as to individuals within the larger group that are not consistent with the smaller insurance-buying subset.

Before any such study is conducted, we strongly recommend that you first employ the chosen methodology to evaluate a non-controversial variable, such as driving record or claims history. You will then have a benchmark against which to measure credit history. Otherwise, all you will have at the end of the study will be a certain degree of variance based on credit history, with no objective measure of whether that variance is significant or not.

7. – 8. Are data on geography, income, ethnicity, race, etc. available? If not, what proxies are available?

Insurers generally collect data by various categories including geography, gender and age. In addition, experience by gender and marital status is used for statistical reporting purposes in most states. On the other hand, insurers do not collect data on income, ethnicity, race, color, religion and national origin as part of the underwriting process.

9. – 10. What type of analysis would allow for inferences to be drawn using proxies instead of actual data or individual characteristics? What limitations are there to inferences drawn about the characteristics of the location where an insurance customer resides in place of individual characteristics?

First of all, we would like to emphasize that ECOA-protected groups are irrelevant to property/casualty insurance. The ECOA prevents, for example, “age” from being used in credit scores. But “age” is a well-justified and generally accepted variable in insurance. The same is true for the “territorial” factor currently used in insurance rate structures.

That being said, when evaluating the impact of insurance scores on premiums among ECOA-protected groups or among different geographic areas, the geographic risk should be adjusted to eliminate any possible biases. The geographic risk could be normalized by using population density or census block data; while these types of data are not as specific as zip+4 or zip code in identifying an individual, they do provide more precise data related to race or income. (Note, however, that some zip codes over only a one-year period do not contain sufficient insurance claim information and, hence, would be unusable.) Moreover, again note our concerns on limitations on inferences about individual characteristics based upon one’s residence identified above in point #3. - 6.

PCI appreciates the opportunity to comment on the prescribed methodology and research design of the study. We are also included as part of another response to Matter No. P044804 that has been filed jointly with two other insurance trade associations. If you would like to discuss any of these comments, please do not hesitate to contact me via telephone at 610-692-9960 or via e-mail at diana.lee@pciaa.net.

Respectfully submitted,



Diana Lee