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January 22, 2021

The Honorable Mark Mullet
5th Legislative District
415 Legislative Building
Post Office Box 40405
Olympia, Washington 98504

RE: Responses to questions on Senate Bill 5010

Senator Mullet,

Thank you for reaching out over email to follow up on Senate Bill 5010 after the public hearing in the Senate committee on Business, Financial Services & Trade.

The attached memo includes our responses to the four questions you emailed to Jon Noski and I on Wednesday, Jan. 20.

If you have any additional questions after reading and reviewing the attached please let us know.

Sincerely,

Mike Kreidler
Insurance Commissioner

cc: Jon Noski, Legislative Liaison, Policy & Legislative Affairs Division

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Memorandum

To: Senator Mark Mullet, Chair, Business, Financial Services & Trade Committee

From: Mike Kreidler, Insurance Commissioner

Date: January 22, 2021

Subject: Responses to questions on Senate Bill 5010

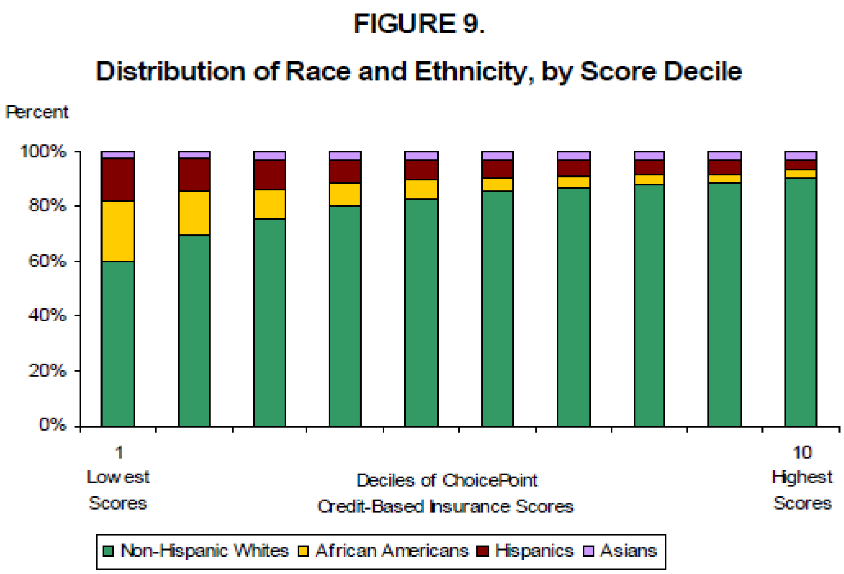
Question 1) If the bill were to pass, what percentage of communities of color would see their insurance premiums increase? What percentage would see a reduction? Do we have a sense of the size of those changes?

Some people will pay more and some will pay less. Who will be impacted and by what amount will depend on the degree to which an insurer has relied on credit scoring. While a dynamic and detailed analysis might be possible if policyholder-level data were available, such data is only available to the insurers.

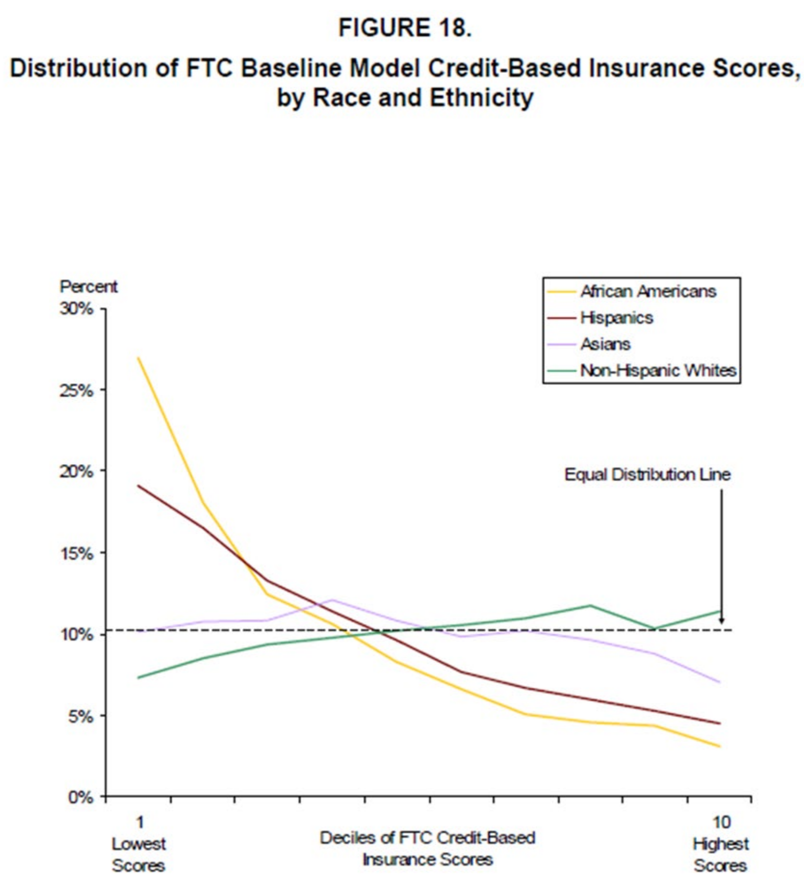
If insurers are prohibited from using consumer credit information for pricing, their pricing models will change and, as you note in a later question, the weight of other pricing factors will also change. Simply removing credit from currently pricing models will not indicate how insurers will respond.

Figures 9 (page 134) and 18 (page 142) from this Federal Trade Commission Report to Congress, shown on the following page, gives an idea of who benefits the most from the status quo, and who would be more likely to receive premium increases if the use of credit were banned. For example, among African Americans there are disproportionately more individuals in the lowest credit score categories and disproportionately fewer individuals in the highest credit score categories. This means we can expect that banning the use of credit would result in lower premiums for African Americans overall, but some individuals could see premium increases.

Contact: Jon Noski | 360.725.7101 | JonN@oic.wa.gov



Source: This chart can be found on page 134 of this report: [Credit-based Insurance Scores: Impacts on Consumers of Automobile Insurance, July 2007.]()



Source: This chart can be found on page 142 of this report: [Credit-based Insurance Scores: Impacts on Consumers of Automobile Insurance, July 2007]().

Any premium increases will be tempered by two important factors. First, due to the pandemic we have seen a significant reduction in the number of vehicles on the road and miles traveled. When insurers file new rates, as will be required by SB 5010, this reduced driving activity will be reflected in their claims data, leading to a reduction in rates. Second, it is important to understand that, despite insurers' claims to the contrary, they use consumer credit information for more than predicting claims. They use consumer credit information for predicting the "value" of the consumers and tools like price optimization and consumer lifetime value scores can disadvantage communities of color.

We know this because insurer Chief Executive Officers (CEO) have explained this to investment analysts, as cited in a presentation by Mr. Birny Birnbaum, Center for Economic Justice (CEJ), to the National Association of Insurance Commissioners (NAIC)Special Committee on Race and Insurance in Dec. 2020[1].

From slides 20 and 21 of the above mentioned presentation:

> In 2005, then Allstate Chairman and CEO, Edward Liddy, told investment analysts about how credit scoring was helping Allstate avoid the wrong customers[2].
>
> *Tiered pricing helps us attract higher lifetime value customers who buy more products and stay with us for a longer period of time. That's nirvana for an insurance company. That drives growth on both the top and bottom line.*
>
> *This year, we've expanded from 7 basic price levels to 384 potential price levels in our auto business.*
>
> *Tiered pricing has several very good, very positive effects on our business. It enables us to attract really high quality customers to our book of business.*
>
> *The key, of course, is if 20% or 23% of the American public shops, some will shop every six months in order to save a buck on a six-month auto policy.* ***That's not exactly the kind of customer that we want.*** *So, the key is to use our drawing mechanisms and our tiered pricing to find out of that 20% or 23%, to find those that are unhappy with their current carrier, are likely to stay with us longer, likely to buy multiple products and that's where tiered pricing and a good advertising campaign comes in.*

Additional comments from insurer CEOs as cited in Mr. Birnbaum's presentation to the NAIC Special Committee on Race and Insurance from Dec. 2020. From slides 21 & 22 of the presentation:

> <u>Allstate CEO to Investment Analysts, May 2017</u>[3]
> *The insurer's "universal consumer view" keeps track of information on 125 million households, or 300 million-plus people, Wilson said.*

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[1] Presentation to NAIC Committee on Race & Insurance Workstream 4 on Dec. 10, 2020:
https://content.naic.org/sites/default/files/call_materials/cej_presentation_naic_race_life_201210.pdf

[2] Transcript of Presentation to Edward M. Liddy, Chairman and CEO, The Allstate Corporation Twenty-First Annual Strategic Decisions Conference, Sanford
C. Bernstein & Co., June 2, 2005.

[3] "Allstate CEO: Agents Will Have Access to Data on 125 Million Households," Best's New Service, May 30, 2017

"When you call now they'll know you and know you in some ways that they will surprise you, and give them the ability to provide more value added, so we call it the trusted adviser initiative," said Wilson.

Progressives CEO to Investment Analysts, November, 2020[4]
Gary Ransom, analyst: Usually that just means your price is lowest on the comparative raters there. But is there more to it than that as well? Are they – are you seeing more coming into the agents? Is there -- are there agents' incentives or other things going on there?

Tricial Griffith, CEO: But, yes, we have -- we do incentives and we have different commissions based on the type of customer that we get in namely preferred.

Comments like these made by insurer CEOs to investment analysts confirm that insurers will be reluctant to raise rates in the absence of credit scoring because they will not want to drive away those customers they view as the most valuable. Insurers know that if they raise rates on these prized customers too much, these consumers will be encouraged to shop around to find lower rates from competitors.

While unfair discrimination on the basis of race is one reason for banning the use of consumer credit information by insurers it is not the only one. Credit scoring also should be banned for the additional following reasons;

- Despite insurer claims that consumer credit information measures "consumer responsibility," this blaming-the-victim rationale is false. The overwhelming percentage of consumer bankruptcies result from medical debt, job loss or divorce. Insurance credit scoring penalizes consumers from all communities for economic conditions outside of the consumer's control.

- The Consumer Financial Protection Bureau has documented how consumer credit data is unreliable

- Credit scoring penalizes victims of predatory lending, including consumers whose only access to credit are payday lenders or other fringe lenders. Such predatory lending has historically targeted military personnel – which is why Congress passed specific protections in the Military Lending Act – and communities of color – who were disproportionately harmed by the predatory lending associated with the financial crisis of 2008.

- Tens or hundreds of thousands of Washingtonians will be further penalized as the CARES Act protections against foreclosures, evictions, and reporting of delinquent loan payments end. It is no exaggeration to say that the current increase in loan delinquencies will pale in comparison to the tsunami to come.

[4] https://seekingalpha.com/article/4385047-progressive-corporation-pgr-ceo-tricia-griffith-on-q3-2020-results-earnings-call-transcript

Question 2) The committee was confused by the comments from the American Association of Retired Persons (AARP) saying this bill would save seniors on fixed incomes on insurance rates. Does the data you have indicate this is true? Many people on the committee thought that seniors statistically have higher credit scores given their longer credit histories.

The confusion seems to be distinguishing between average credit scores for seniors, which may actually be higher than for younger people, with a common burden faced by some individual seniors, as mentioned by AARP below.
Poor credit means something different for seniors than it does for non-seniors – it means a lack of credit. For seniors, many are done with mortgages, car payments and credit card debt. That should not make them bad insurance risks.

AARP provided the following in response to this question:

> *A credit score tries to predict the likelihood you'll pay your debts. Lenders use it when deciding to offer a mortgage, auto loan or credit card. Insurers also look at it to set auto and homeowners policy premiums. Prospective landlords and utility companies will scrutinize your score if you move to an apartment. Plus, your score will be a factor if you cosign a student loan.*
>
> *The problem for many older people is that their score declines because they no longer use credit (debit cards don't affect scores). As their house, car, credit card payments and other credit activity wind down, their credit report eventually becomes so thin that it can't maintain a score or produces only a low one.*

Additionally, there is a burden on seniors to maintain their economic activity in order to maintain a higher credit score. Higher credit scores are necessary to keep their borrowing power, retain access to lower insurance rates, meet credit score thresholds for renting, etc. This has serious implications for seniors on a fixed income or who are unable to be economically active. This article from Experian has additional information on this topic.

Question 3-1) If credit can't be used by insurance companies, what factors will be weighted more heavily in deciding rates?

Likely every remaining rating element would receive more weight, though it would vary from insurer to insurer and depend on each insurer's exact methods for ratemaking. Insurers typically use sophisticated statistical models for ratemaking that solve for numerous rating factors simultaneously. So when you remove one rating element all the other elements in the model could pick up some additional weight.

As discussed in response to your first question, insurers will modify their pricing models and non-credit pricing factors will change. Insurers may push to expand telematics programs that match prices to actual driving behavior or they may give more weight to miles driven or a consumer's driving history.

Question 3-2) What data does OIC have to ensure that those new factors do not increase racial disparities in rate setting?

While many pricing factors likely have some correlation to race, consumer credit information is clearly the worst, as shown by the National Consumer Law Center's Racial Divide report, Mr. Birnbaum's report to the Ohio Civil Rights Commission and as cited by Mr. Birnbaum in his testimony. The Missouri Department of Insurance's analysis found that the best predictor of the average credit score in a zip code was the minority population of the zip code. Communities of color will receive additional benefit from a ban on insurance credit scoring, just as they now suffer disproportionately from insurers' use of it.

Question 4) Does OIC have data to prove that states that have implemented this policy have better equity outcomes for communities of color in regard to insurance rates?

No, but we do have data that suggests implementing this policy will not result in overall higher premiums.

Under California state law, insurers' pricing is limited to what is allowed under law and is approved by regulation. Credit scoring was never allowed by law nor was it approved by regulation. We believe that the basic trajectory of Hawai'i and Massachusetts are similar to California. It can be said that rates are more equitable in California, Hawai'i, and Massachusetts, with regards to the lack of differential in the premiums for drivers at different credit levels.

In addition, California passed Proposition 103 in 1989. The results included:

- The average liability premium in California has decreased by 5.7%. between 1989 and 2015. Saving California drivers $154 billion, or around $6 billion a year.

- Over the same time period the national average liability premium has increased by 58.7%.

Hawai'i also banned credit scoring, and between 1989 and 2015, the average liability premium dropped by 2% (Consumer Federation of America: "Auto Insurance Regulation, What Works 2019")

In addition to your questions above, you previously mentioned a concern you heard about the possibility that traffic infractions are also racially biased so giving more weight to them might work counter to racial equity. Here is how these issues could be addressed:

- If driving violations are racially biased, the best approach to this problem is at the law enforcement level – training or reform to end the racial bias in enforcing traffic laws.

- If credit scores are racially biased, the best approach is to stop using credit scores as a gatekeeper for financial services. There is an element of a self-fulfilling prophecy in using credit for insurance. When a consumer has low credit it makes them a bad risk in the eyes of the insurers so they are charged higher premiums. However, paying more for insurance can make it difficult for a consumer to spend more on their outstanding debt to improve their credit score. Which in turn keeps their credit low and the cycle perpetuates itself.