Property Casualty Insurers
Association of America

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# Insurance scoring saves consumers money

## Get the facts: Frequently Asked Questions

**Q: What is credit-based insurance scoring?**

**A:** Credit-based insurance scoring is a practice whereby insurers consider a customer's credit information in underwriting and pricing decisions. It involves using credit information to calculate a score measuring a customer's relative risk of loss. Credit-based insurance scores thus provide an objective measurement of how a person manages the risk of credit. It is important to note, however, that insurance companies use insurance scoring in different ways to varying degrees. And most states impose restrictions on what type of information insurers may use to calculate a score and the extent to which they may rely on an insurance score in making underwriting and pricing decisions.

**Q: Why do insurance companies use credit history to set rates?**

**A:** Because it is one of the most, if not the most, accurate predictors of risk currently available to insurers. The more accurately insurance companies are able to predict loss, the better able they are to offer rates that match the level of risk a consumer represents.

**Q: How do insurers know that insurance scoring is accurate?**

**A:** Numerous studies by federal and state regulators, universities, independent auditors and insurance companies have all shown an individual's credit history is a proven, accurate indicator of how likely that person is to file a future claim and the potential cost of that claim. The way in which people manage their credit reflects how they are likely to behave in other aspects of their lives.

**Q: What does a consumer's credit history have to do with the price we pay for auto or homeowners insurance?**

**A:** Credit-based insurance scores are an accurate and fair predictor of risk of loss. Lower-risk policyholders should not have to pay the same rates as higher-risk policyholders for home and auto insurance, so it is important for insurers to accurately predict each policyholder's likelihood of filing claims and price coverage accordingly.

**Q: But why does it work? Why is credit information so predictive?**

**A:** We don't know exactly why. Some theorize that people who are fastidious in managing their credit are similarly disposed in other areas of their lives. Regardless of the actual reason why, it's important to remember insurers are not legally required to provide an explanation as to why a particular rating factor is predictive. Age, gender and marital status are all commonly used rating factors for which no definitive explanation exists as to why they work. They just do.

**Q: How do consumers benefit from credit-based insurance scoring?**

**A:** Studies show that most consumers receive a discount in the price of their insurance when credit information is considered. This is because the ability to accurately assess risk means lower-risk policyholders will not have to subsidize the cost of insurance for higher-risk policyholders. In addition, sound underwriting and rating allows insurers to write more business, meaning consumers have more choices when they shop around for the best price.

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**Q: What would happen if lawmakers ban this practice?**

**A:** Consumers could see rates go up if insurance scoring is prohibited. Because most people manage their credit responsibly, the use of credit-based insurance scores benefits a majority of consumers and saves them money. Banning such use would mean lower-risk consumers would have to pay more to subsidize the cost of insurance for higher-risk consumers. Also, without the ability to consider credit, many insurers would be less aggressive in their marketing and far more cautious in accepting new business, resulting in fewer options for consumers in the marketplace.

**Q: Are states in fact moving to ban insurers' use of credit history?**

**A:** No. Citizens and legislators nationwide have rejected laws to ban insurance scoring again and again over the past 22 years. Nearly every state has laws to ensure the fair and accurate use of credit information by insurance companies, but only two states completely prohibit the use of credit-based insurance scores (California and Massachusetts) and two ban its use for specific lines of insurance (Hawaii for auto and Maryland for homeowners). Legislators and regulators in 48 states have studied and debated insurers' use of credit information and have repeatedly reaffirmed that insurers should be allowed to use credit information in underwriting and rating decisions.

**Q: Does insurance scoring unfairly discriminate against low-income consumers?**

**A:** No. Insurance scores are objective and do not include income information. An insurance score only measures risk-relevant variables (i.e., payment history, public records, etc.) that are indicators of potential future risk. Living within one's means and paying bills on time are not characteristics that are specific to any income bracket.

**Q: Has the economic downturn caused average credit scores to drop?**

**A:** Despite the slumping economy, average credit scores across the country remain steady. In fact, the average credit score in most states has actually improved slightly since the start of the recession, according to the national consumer reporting agencies. Why? Because during this time most consumers are saving more, spending less and paying off credit card debt in record amounts.

**Q: What about consumers who suffer credit problems through no fault of their own because they or their loved ones have suffered a major illness or have recently gone through a divorce?**

**A:** Many states require insurers to provide reasonable exceptions in their use of credit information to consumers who have suffered from or been affected by extraordinary life circumstances, such as a job loss or divorce. Even in states that do not mandate such exceptions, many carriers offer such exceptions anyway.

**Q: Won't new technology make insurance scoring obsolete?**

**A:** New tracking technology will not make predictive tools like insurance scoring obsolete. It remains to be seen whether having access to more detailed driving records will substantially improve the accuracy of driving record as an underwriting and rating factor. Credit-based insurance scoring remains one of the most predictive and accurate tools for insurers. In addition, it's unlikely that any single rating factor will ever supplement the use of multiple factors.

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