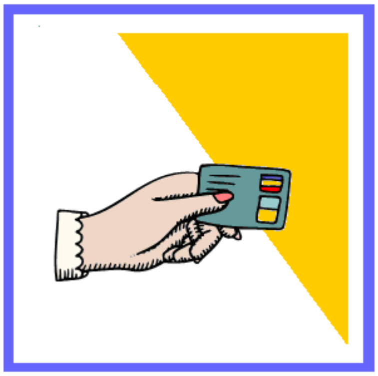
Colorado
Division of
Insurance

Credit Scoring and Insurance Premiums – Frequently Asked Questions

- **What is credit scoring?**



Certain companies, called **consumer reporting agencies**, collect information about a person's financial history. This can include the amount of credit available, the timeliness of payments, the number of open and closed accounts, any bankruptcies or discharged debts, collection activity and other information about the individual's financial status. This information is entered into a formula to produce a **credit score**.

An individual's credit score is a numerical value assigned according to the person's credit history at a point in time. Credit scores are often used to determine whether it's a good business decision to loan money to a consumer to purchase a home mortgage, to extend a credit card offer or increase the credit limit, to determine interest rates on credit purchases, or to allow the purchase of an item over time.

Insurance companies also use credit scores; however, they do not use the raw credit score as described above. Insurance companies use credit reporting agencies and the credit score to develop what some companies refer to as an **"insurance" score**. The insurance companies do not see the credit score in the same manner a lender or credit card company would see it. Insurance companies use this "insurance" score to evaluate the potential risk posed by a consumer. The risk the companies are evaluating is whether an insured is more (or less) likely to file a claim in the future.

The federal Fair Credit Reporting Act and the Colorado laws allow the practice of using credit/insurance scores to determine whether a company wants to accept the risk and/or to rate the risk accordingly.

- **Can an insurance company use my credit score to determine how much I will pay for insurance premiums?**

Yes, insurance companies can, and many do, use your credit or insurance score to help calculate insurance policy rates. The decision to use credit scoring is up to the company. A credit or insurance score is usually just one consideration combined with other factors, such as age, driving history, and the type of car driven. These factors are used by the insurance company to predict the level of risk an individual presents to the insurance company.

- **Is the use of credit scoring legal?**

A Federal law, called the Fair Credit Reporting Act, regulates the collection, dissemination, and use of consumer credit information. Along with the Fair Debt Collection Practices Act (FDCPA), it forms the base of consumer credit rights in the United States.

Under this law, the use of credit scoring to determine premium rates is legal.

- **Does Colorado have any state laws related to credit scoring or the use of credit information in setting insurance premiums?**

Colorado passed the Colorado Consumer Credit Reporting Act in 1996, which outlines the ways that consumer credit information can be used.

In part, this law says it is permissible to use credit scoring information when it is intended:

> *to use credit scoring information in connection with the underwriting or rating of insurance involving the consumer and such person establishes that the consumer has received written notification, or notification in the same medium as the application for insurance, that a credit report may be requested in connection with his or her application for insurance, and that credit scoring information may be used to determine either the consumer's eligibility for insurance or the premium to be charged to the consumer.*

CRS 10-4-116 contains requirements all insurers must follow if they are going to use credit to rate a private passenger automobile policy.

Insurers are not permitted to use the credit score as the *sole factor* in determining whether to deny, cancel or fail to renew a policy, or as the sole factor in determining the renewal premium.

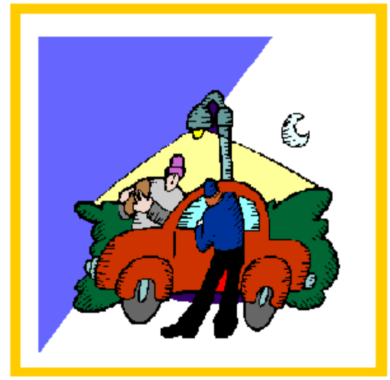
If a policyholder does not have sufficient credit history to calculate a credit score, the insurer must treat this individual as if they have a neutral credit score, or provide loss statistics to the Division of Insurance that demonstrates a policyholder's lack of credit history can be used to reasonably predict future claim experience.

For more information, you may wish to view these Colorado laws:

Colorado Consumer Credit Reporting Act,
Title 12 of the Colorado Revised Statutes, specifically CRS 12-14.3-101 *et seq.*

Use of Credit Information,
Title 10 (Insurance) of the Colorado Revised Statutes, specifically 10-4-116.

- **In addition to credit scoring, what other factors are used to set premium rates?**



Factors that may be considered include:

- the age of the driver,
- the gender of the driver,
- marital status of the driver,
- the risk level of the neighborhood where the driver lives,
- the driver's accident and traffic violation history,
- type of vehicle insured, and
- the amount of policy coverage and deductible.

- **What personal factors cannot be used in setting premium rates?**

Information such as income, ethnic group, disability, religion, and nationality are not considered when calculating the premium.

In addition, insurers cannot rate a policy using a credit score calculated using income, gender, address or zip code, ethnic group or nationality, religion, or marital status.

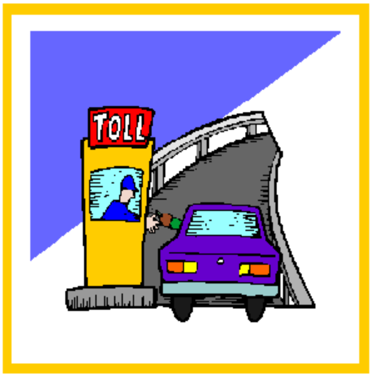
- **Does an individual's credit score predict the likelihood of filing an accident claim?**

Some studies support this statement, demonstrating that how a person manages personal finances, which is what an insurance score indicates, is a good predictor of insurance claims. Insurance scores help insurers identify individuals who are either lower or higher insurance risks. Companies can charge a premium relative to the risk they are assuming. Statistically, people who have a low insurance score are more likely to file a claim.

- **Is there an indication that, in some circumstances, use of credit scoring will help consumers?**

The explanation offered by some insurance companies is that competition in the insurance market has increased significantly, since credit scores have been used, leading to more choices for consumers. Additionally, the use of credit scoring and a company's ability to appropriately rate a risk results in fewer consumers being declined insurance. In theory, financially responsible consumers can be rewarded with the best rates. Without the use of credit scores, these "financially responsible" consumers with good driving records would pay more for insurance, subsidizing those who are more likely to have a loss.

- **What can I do if I receive a proposed premium increase and I feel the credit score information being used is incorrect or incomplete?**



You must contact the credit reporting agency to make any adjustments or correct any mistakes, if you feel that the credit score used is incorrect. The Division *does not see* and *cannot review* your credit records or credit score to determine whether the records provided to your insurance company are correct.

- **Do I have a right to protest the proposed premium increase on my auto insurance if I feel the credit score information used is <u>not</u> correct?**

It is important to note:
If you feel there is an error on your credit report, you must contact the credit reporting agency directly to remedy the record or fix any inaccuracies, and have the credit reporting agency provide the corrected information to your insurance company for consideration.

The Division of Insurance *cannot review, modify or correct consumer records*, including personal credit scoring or credit history reports.

Consumers have the right to protest an automobile insurance premium increase, although there is no guarantee the protest will be upheld or the premium reduced. The company is required by statute to provide the protest notice to the consumer to be signed and submitted to the Division. Information about information that may be considered in consumer auto protests is included in Colorado Revised Statute 10-4-629 and
Regulation **5-2-12.** http://www.dora.state.co.us/insurance/regs/5-2-12.pdf

Other types of insurance, such as homeowners insurance, do not have the same statutory right of protest. The right to protest a policy change (premium increase, cancellation, change in coverage or non-renewal of policy) is unique to private passenger automobile insurance policies in Colorado.