Consumer Perspectives on Insurance Credit Scoring

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Topics Covered

- Subprime Mortgage Disaster and Great Recession
- Review of Actual Insurance Scoring Model
- Evaluation of Great Recession on Insurance Scores
- Misconceptions and Misrepresentations About Insurance Scoring
- Beyond Insurance Scoring – Risk Classification Run Amok

Mortgage Meltdown, Great Recession

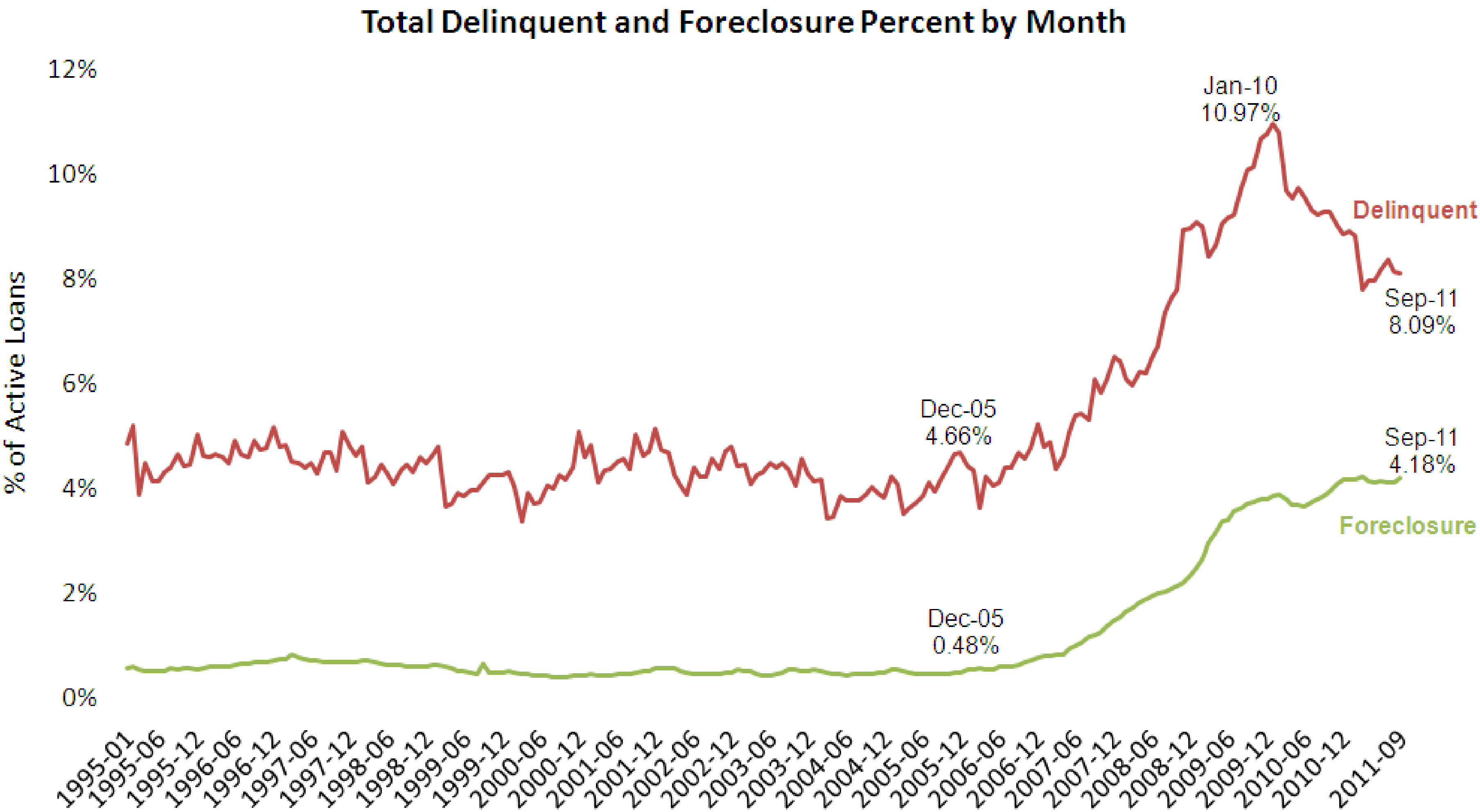
- Reckless and Fraudulent Lending
- Subprime Mortgage Targeted at Low-Income and Minority Consumers
- Foreclosures Disproportionately Impact Minority Communities

Prime vs. Subprime Mortgage Delinquencies

	2005	2006	2007	2008	2009	2010
Prime	2.3%	2.4%	2.9%	4.3%	6.5%	6.5%
Subprime	10.8%	12.3%	15.6%	19.9%	25.5%	25.9%

Source: Statistical Abstract of the United States 2010, Table 1194

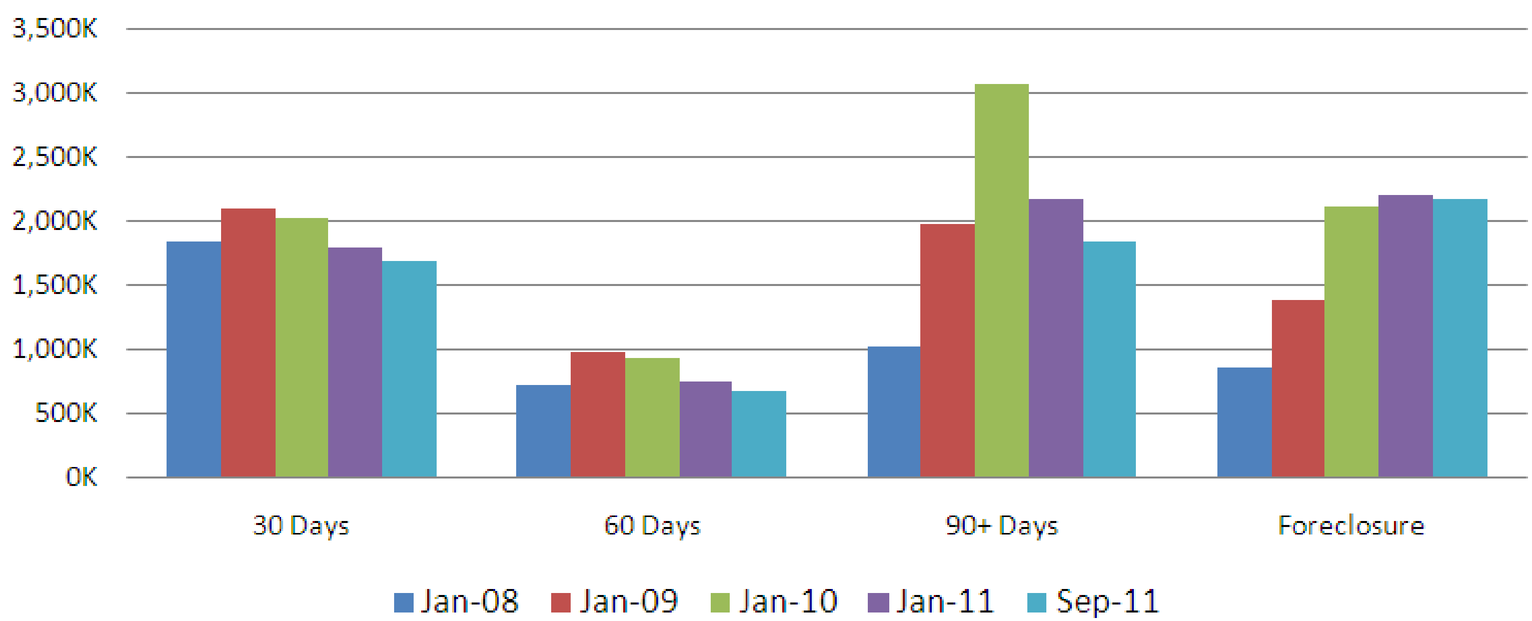
DQs are almost 2x, and foreclosures are 8x pre-crisis levels



Market Overview: Over 4MM loans are 90+ days delinquent or in foreclosure

Month	Total Active Count	30 Days	60 Days	90+ Days	Foreclosure	Total Non-Current
Jan-08	55,718,637	1,843,183	715,016	1,015,832	859,994	4,434,025
Jan-09	55,808,723	2,103,950	970,919	1,982,791	1,386,222	6,443,882
Jan-10	54,767,392	2,018,656	928,172	3,060,719	2,110,473	8,118,020
Jan-11	52,993,580	1,796,189	754,542	2,168,008	2,203,088	6,921,827
Sep-11	51,928,166	1,687,753	669,967	1,843,975	2,171,621	6,373,316

Average Days Delinquent: 90+ Days	Average Days Delinquent: Foreclosure
192	251
196	319
257	410
344	523
398	624



Credit Card Delinquencies

Source: Statistical Abstract of the United States, Table 1195

2005	2006	2007	2008	2009	2010
3.7%	4.0%	4.3%	5.0%	6.5%	4.9%

Review of Insurance Scoring Models

Texas requires insurance credit scoring models to be filed with the insurance department – like most other states.

Texas makes the models available to the public – unlike most other states

Variety of Models Filed in Texas

<u>FICO Auto</u>

Non Standard

Standard Minimum Limits

Standard Greater Than Minimum Limits

Preferred Minimum Limits

Preferred Greater Than Minimum Limits

Variety of Models Filed in Texas

<u>ChoicePoint Auto</u>

Standard Thin File
Standard Thick File
Standard With Claims
Non-Standard Thin File
Non-Standard Thick File
Non-Standard with Claims

Variety of Models Filed in Texas

<u>FICO Residential Property</u>

Dwelling Fire

HO 1

HO 2

HO 3

HO 4

HO 6

Actual Scoring Model – Standard Auto

Average Months in File of All Accounts

Value	Points
0-20	0
54-59	26
90-95	40
200-219	50
600+	56

Months Since Last Delinquency

Value	Points
0-2	34
9-11	54
18-23	63
48+	68
None	70

Number of Inquiries in the Last Year

Value	Points
0	9
1	8
2	6
3	4
4	1
5+	0

Months Since Oldest Date Opened

Value	Points
0-47	0
108-119	4
180-209	10
288-319	15
500+	20

Worst Delinquency in the Last Year

Value	Points
90+	34
60	35
30	36
Prior to Last year 60	42
Prior to Last year 30	49
Never	62
All Other	53

Months Since Most Recent Public Record

Value	Points
0-7	101
8-11	102
12-23	102
24-35	103
38+	107
None	125

Number of Public Records

Value	Points
0	107
1	105
2	104
3	102
4+	101

Number of Collections

Value	Points
0	73
1	72
2	70
3	69
4+	67

Months Since Most Recent Collection

Value	Points
0-11	67
12-23	68
24-59	69
60+	73
None	91

Number of Accounts in Default Status

Value	Points
0	47
1	44
2	41
3	37
4+	34

Number of Accounts Where Balance is 75% of Limit

Value	Points
0	50
1	35
2	17
3	8
4+	0
All Other	34

Number of Finance Company Accounts

Value	Points
0	26
1	21
2	18
3	16
4	13
5+	0

Number of Accounts 90+ Delinquent Ever

Value	Points
0	26
1	11
2	9
3	6
4	3
5+	0

Number of Accounts 60+ Delinquent in Last 2 years

Value	Points
0	25
1	10
2	7
3	5
4	2
5+	0

Misconceptions About Insurance Scores 1

"Credit Histories Reflect Credit Management Which Indicates How Well Consumers Manage Risk
Insurance – Insurance Scores Reflect a Consumer's Responsibility"

Every Part of This Rationale is Wrong.
Blaming the Victims of Insurance Scoring is Reprehensible –

Consumers Who Have Experienced Job Loss, Divorce, Medical Catastrophe, Abusive Lending, Historical Discrimination Are Not Irresponsible.

Misconceptions About Insurance Scores 2

"Insurance Credit Score Distributions Remain Stable"

Independent Data and Scoring Model Factors Indicate Otherwise.

If True, Insurance Scores Do Not Reflect Credit History – How Can Scores Remain Stable When All The Factors in the Scoring Model Have Gotten So Much Worse?

Misconceptions About Insurance Scores 3

"Consumers Benefit from Insurance Credit Scoring Because Scoring Allows Insurers to make More Accurate Underwriting and Pricing Decisions."

- Zero Evidence That Insurance Scoring Has Improved Insurance Availability; Available Evidence Indicates Insurance Scoring Has Discriminatory Impact on Low-Income and Minority Consumers

- Zero Evidence That Insurers Have Reduced Rates Because of Greater "Pricing Certainty." No Insurers Have Filed Rates With Lower Profit Provisions Because of Insurance Scoring

- Insurance Scoring Harms Consumers Because It Robs the Insurance Mechanism of Economic Incentives for Less Risky Behavior and Economic Disincentives for More Risky Behavior.

- Insurers Use Insurance Scoring and other Data Mining to identify the most profitable consumers -- Consider the comments of Ed Liddy, then-CEO of Allstate to investment analysts in 2005:

Liddy:

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.

Make no mistake about it, the economics of insurance are driven largely by retention levels. It is a huge advantage. And our retentions are as high as they have ever been.

Liddy:

The key, of course, is if 23% or 20% 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.

It (tiered pricing) has raised the profitability of the industry.

Misconceptions About Insurance Scores 4 "Insurance Credit Scores Don't Discriminate Against Minorities Because Race is Not Used in the Scoring Model"

- The Fact That a Characteristic is Not in Scoring Model Does Not Mean the Scoring Model is Not Correlated With or Predictive of That Characteristic – see Claims.
- There is No Question That Insurance Scoring Has a Disparate Impact on Low-Income and Minority Consumers
- MO DOI Study: Minority Population Concentration is Single Most Reliable Predictor of Insurance Scores
- Insurance Scoring Reflects and Perpetuates Historical Discrimination and Inequities

Beyond Insurance Credit Scoring: Risk Classification Run Amok

Deluge of New Rating Factors, No Oversight by Insurance Regulators

- Prior Insurance
- Prior Liability Limits
- Data Mining
  - ISO Environmental Risk Model
  - Internet Activity