State of Idaho

DEPARTMENT OF INSURANCE

C.L. "BUTCH" OTTER
Governor

700 West State Street, 3rd Floor
P.O. Box 83720
Boise, Idaho 83720-0043
Phone (208)334-4250
FAX # (208)334-4398

WILLIAM W. DEAL
Director

BULLETIN NO. 12-01

(Replaces Bulletin No. 08-09)

DATE: April 30, 2012

TO: Property and Casualty Insurers

FROM: William W. Deal, Director

SUBJECT: Use of Credit Information for Rating and Underwriting

---

The purpose of this bulletin is to notify insurers using credit history for rating purposes that the Department is modifying its approach to determining what constitutes compliance with Idaho Code section 41-1843, which governs the use of credit information in insurance rating. This bulletin replaces Bulletin No. 08-09.

Idaho Code section 41-1843 prohibits insurers from charging a higher premium than would otherwise be charged, canceling, non-renewing or refusing to issue a property or casualty policy or coverage based primarily upon an individual's credit rating or credit history. "Based primarily" is defined to mean that the weight given to credit history exceeds the weight given to all other criteria considered in making the rating or underwriting decision.

Current Approach

In the past, the Department has tested compliance with Idaho Code section 41-1843 by requiring that insurers demonstrate that the difference in premium charged a person with the worst credit score and a person with the best score is not more than one-half of the total premium charged the person with the worst score. This approach screens out all other variables used in the rating decision by assuming that the person with the best score and the person with the worst score are identical in all respects other than credit history. The Department has considered the difference between the amount charged the person with the best score and the amount charged the person with the worst score to be the amount of premium attributable to the use of credit. If that amount was greater than one-half of the total premium, the Department's position has been that the weight given credit outweighs the weight given all other factors, and the rating methodology was considered not in compliance with section 41-1843. For example, if the person with the best credit score is charged $100, and an identical person with the worst credit score is charged $300, the Department has taken the position that the difference between the two premium amounts ($200) is the amount attributable solely to credit, and $100 of the $300 premium is attributable to other factors. Because the portion of premium attributable to credit exceeds the amount attributable to other factors in this example, under the current approach the Department would conclude that this rating system violates Idaho Code section 41-1843.

Modified Approach: Use of a "Neutral Score" to Determine Compliance

A number of insurers have requested that the Department modify its approach to reviewing the impact of credit history by allowing insurers to use a "neutral" score or rate. The neutral rate would represent the amount an insurer would charge if credit was not included as a factor in the rating process. Under this modified approach, if the premium calculated without using credit (the neutral rate) is equal to or greater than one-half of the premium rate calculated for a person with the worst credit score, then the insurer would be considered to be in compliance with section 41-1843. For example, if the neutral rate is $200, and the rate for a person with the worst credit score is $300 (i.e., the highest rate charged based on credit), the rating system would be considered to be in compliance with section 41-1843 because the neutral rate is more than one-half the highest rate charged based on credit. Under this approach, as long as the highest rate charged is not more than double the neutral rate, the rate would be treated as meeting the requirements of section 41-1843.

Based upon information submitted by interested parties and discussions with a consulting actuary, the Department has determined that the use of a neutral rate meets the requirements of Idaho Code section 41-1843 if an insurer is able to demonstrate that it has developed a truly neutral rate. To calculate the premium rate without using credit, the insurer must be able to demonstrate that it has applied all noncredit variables, but has replaced the actual credit factor with an average credit factor. The average credit factor must be calculated from the actual distribution of business by credit factor at the time the credit scoring system was implemented or when the system was last revised. For the purposes of this bulletin, "revised" means any subsequent changes to the credit scoring system utilized by the insurer being applied as part of its overall rate filing.

The Department will not accept a "no score" value as a neutral value. A "no score" value is a value that the insurer represents it would apply if credit information were not available. This approach is problematic because the value may be, in part, arbitrary, and may also reflect the degree of reliance that an insurer places on credit information.

Because a “no score” value may not be truly neutral, it may not be used to demonstrate compliance with section 41-1843. In addition, because section 41-1843 applies to rates actually charged rather than quoted rates, a quote-weighted average may not be used to develop a neutral rate to demonstrate compliance.

Conclusion

Insurers that use credit history in any way to develop rates must demonstrate that no rate charged will be based primarily on credit history. A company may establish compliance with section 41-1843, Idaho Code, in one of two ways. The first method is by demonstrating that the difference between the premium charged the person with the worst credit score and that charged the person with the best score is less than or equal to one-half the total premium charged the person with the worst score. In other words, the worst score rate may not be more than double the best score rate. In the alternative, an insurer may demonstrate compliance by showing that the amount that would be charged if credit history were not considered in the rating process is greater than or equal to one-half of the total premium charged. To establish what would be charged without considering credit, the insurer must use all noncredit variables and replace the credit variable with the average credit factor.

Section 41-1843, Idaho Code, also prohibits insurers from declining to issue coverage based primarily on an applicant’s credit history. A determination by an insurer that an applicant is ineligible for coverage with a “preferred” company based primarily on a credit score or credit history is considered by the Department to be a declination based on credit history, even if the applicant is offered coverage through a related company. Use of either the current approach or the modified approach discussed in this bulletin may be applied by an insurer to either or both initial rate making and renewal.