Understanding How Insurers Use Credit Information

UNDERSTANDING HOW INSURERS USE CREDIT INFORMATION

Many personal auto and homeowners insurance companies look at several factors, including consumer credit information, to decide:

- Whether to issue or renew an insurance policy
- How much premium to charge for insurance

This brochure will help you understand how insurance companies use your credit information and how this business practice affects how much you pay for insurance.

1. Can an insurance company look at my credit information without my permission?

Yes. The Federal Fair Credit Reporting Acts (FCRA), says that insurance companies may look at your credit information without your permission for underwriting purposes. The federal law may be found at http://www.ftc.gov/. Arkansas also has a law regarding the use of credit information obtained from a credit bureau. That law is the Use of Credit Information in Personal Insurance Act of 2003 (Ark. Code Ann. §§23-67-401 through 415).

2. Why do insurance companies use credit information?

Some insurance companies have shown that information in a credit report can predict which consumers are likely to file insurance claims. They believe that consumers who are more likely to file claims should pay more for their insurance.

3. How do I know if an insurance company is using my credit information?

Ask your insurance agent or company if they use credit information for underwriting or rating. If credit history is used for underwriting, ask them how it affects your eligibility for coverage. If credit history is used for rating, ask them how it affects your insurance premium. You should also ask if they will check the credit history of other people insured on your policy, such as family members, and how they will affect your policy.

4. If I don't have a credit history, will it affect my insurance purchase?

Possibly. Use of Credit Information in Personal Insurance Act of 2003 generally requires that in situations where a consumer's credit file does not contain sufficient information, the insurance company must not penalize the insured for the lack of information. A company may ask for an exception or use some other factor or factors in place of credit.

If you think you have a credit history but the insurer cannot find it, make sure your agent or insurance company has your correct name, address, social security number and birth date.

5. How do insurance companies use credit history?

Insurers can use your credit history, in addition to other factors, to **underwrite** your insurance policy or to **rate** your insurance policy.

- **Underwriting.** Underwriting is a process where an insurance company gathers information and decides whether or not they will insure you. The Use of Credit Information in Personal Insurance Act of 2003 determines when credit information may be used in underwriting.

- **Rating.** Rating is a process that determines how much you pay for insurance. Many insurers charge higher premiums based on various attributes of an individual's claim history and characteristics of the property insured. Use of Credit Information in Personal Insurance Act of 2003 allows credit information to be used as characteristics in rating. Some of those characteristics are described in question 6.

6. What kind of credit information do insurance companies use?

Most companies that use credit information use an "insurance credit score." An insurance credit score is calculated using information about your credit history. Many insurance credit scores are weighted using recent credit history more heavily than old credit history. The factors used in many scoring models are:

- **Public records** (such as bankruptcy, collections, foreclosures, liens, and charge-offs). Public records generally have a negative effect on your insurance credit score.

- **Past payment history** (the number and frequency of late payments and the days between due date and late payment date). Late payments tend to have a negative effect on your insurance credit score.

- **Length of credit history** (the amount of time you've been in the credit system). A longer credit history tends to improve your insurance credit score.

- **Inquiries for credit** (the number of times you've recently applied for new credit, including mortgage loans, utility accounts, and credit card accounts). Shopping for new credit tends to have a negative effect on your insurance credit score.

- **Number of open lines of credit** (including the number of major credit cards and department store credit cards). Having too much credit tends to have a negative effect on your insurance credit score. However, it generally is not a good idea to cancel a credit account that you have had for a long time. A long credit history may help your score.

- **Type of credit in use** (such as major credit cards, store credit cards, finance company loans, etc.). Major credit cards may be treated more favorably than other types of consumer credit, such as store credit card or loans from a finance company.

- **Outstanding debt** (how much you owe compared to your available credit). Too much outstanding debt tends to have a negative effect on your insurance credit score.

Insurance credit scores are not uniform among insurance companies. Insurance companies have different views on which factors are more important based on their experience and business practices. For example, one company might feel that public records are more important than past payment history. Another company might take the opposite view. How much weight a company gives each of the factors determines, to a large extent, your insurance credit score with that company.

7. What is a good insurance credit score?

There is no single answer to this question. Generally, a good insurance credit score will result in a lower premium. However, insurance companies use different scoring calculations, so different insurers will likely give you a different score. That is why it pays to shop around on a regular basis to make sure your premiums are competitive.

8. Is my premium based entirely on my insurance credit score?

No. Both auto and homeowners premiums are based on factors other than credit history. Your auto insurance premium is based on factors such as your driving record, the type of car you drive, and where you live. Your homeowners premium is based on factors such as where you live and the cost to replace your home. Credit history is only one of a number of factors insurers use to rate your policy.

9. Must an agent or company tell me what my insurance credit score is?

No. In fact, the agent or company underwriter might not even know your score. In most instances, all the agent or underwriter may know is that your credit score qualifies you for a particular rate or for a particular company within the group. However, The Use of Credit Information in Personal Insurance Act of 2003 requires that the insurance company inform you if it is using credit either by a statement on the application or by written notice. If the application is taken over the telephone or electronically, it must provide the notice in the same medium.

Even if you know your insurance credit score, it may not be useful to you. Your insurance credit score is a "snapshot in time," and a significant change in your credit activity or a creditor's report can change your score. These can be positive or negative factors. It is possible to have more positive factors than negative factors and still not have a score high enough to get the best rate available but still get a better rate than if credit had not been used at all. Due to the FCRA, unless you get the best rate, the insurance company must disclose that fact to you. The Use of Credit Information in Personal Insurance Act of 2003 requires the insurer to provide you with the four most important factors. You can use these factors to see where you have managed your credit well and where you can improve it even more.

10. If I don't know my score, and my score varies from company to company, how will I know if my credit history affects my insurance purchases?

Ask your insurance agent or insurance company. The FCRA requires an insurance company to tell you if they take an "adverse action" because of your credit information. FCRA defines "adverse action" to include denying or canceling coverage, increasing premiums, or changing the terms, coverage, or amount of coverage in a way that harms the consumer. Examples of an "adverse action" include:

- Canceling, denying, or non-renewing coverage
- Refusing to quote a premium
- Giving the consumer a limited coverage form
- Limiting benefits, such as eligibility for dividends
- Issuing coverage other than that applied for
- Not giving the consumer the best rate

- Not giving the consumer the best discount
- Adding a premium surcharge
- Failing to give a premium discount
- Changing an existing premium
- Any offer of insurance made to a consumer who has not requested the offer that is solely, or in part, based upon a consumer report

If your insurer takes an adverse action due to your credit history, it must also tell you the name of the national credit bureau that supplied the information. You are also entitled to a free copy of your credit report from the credit bureau that supplied the credit information.

Federal law says you have a right to a free copy of your credit report if you've been denied credit or insurance, if you are on welfare, unemployed, or if you are a victim of identity theft. Otherwise, you may have to pay a small fee. (The current fee charged by a credit bureau varies. Usually you can expect to pay around $8 to $15 for each report.) Most consumer groups suggest you get a copy of your credit report once a year and review it for errors.

11. What can I do if there is incorrect information in my credit report?

Tell the credit bureau. If you report an error, the credit bureau must investigate the error and get back to you within 30 days. The credit bureau will contact whoever reported the information. Credit information is often reported by banks, credit card companies, collection agencies, or a court clerk. If the investigation shows the information is wrong or if there is no proof it is true, the credit bureau must correct your credit record.

You can ask the credit bureau to send a notice of the correction to any creditor or insurer that has checked your file in the past six months. Once the errors are corrected, it is a good idea to get a new copy of your credit report several months later to make sure the incorrect information has not been reported again. You should also get a copy of your credit report from the other national credit bureaus, which are listed below. If you correct an error on one report, it will not "fix" incorrect information on the other reports.

If the information in your credit report is correct, the credit bureau will not change it. However, the FCRA lets you file a 100-word statement explaining your side of the story, and the credit bureau must include your statement with your credit information each time they send it out. Make sure your insurance company has a copy of your statement, and ask if the company will take your statement into account.

The three national credit bureaus are:

- **Equifax (www.credit.equifax.com or 800-685-1111);**
- **Experian (www.experian.com or 888-397-3742); and**
- **Trans Union (www.transunion.com or 800-888-4213).**

Tell your insurance company. Don't wait until the credit bureau investigates the errors to contact your insurer. Tell your insurance company right away, and ask if the errors will make a difference in your insurance.

If the errors are big, tell your insurer that you are disputing the information and ask if they will wait to use your credit information until the errors are corrected. Small errors may not have much effect on your credit score. Large errors can make a significant difference in your premium.

12. How can I improve my insurance credit score if I have been adversely affected?

You must find out what attributes of your credit history were used to calculate your insurance credit score. An "attribute" is a piece of your credit history, such as filing bankruptcy or paying bills late. Companies that develop insurance credit scores, such as Fair Isaac and Choice Point, provide insurance companies with up to four attributes that have had a negative impact on your insurance credit score. Under the Use of Credit Information in Personal Insurance Act of 2003, the agent or company must tell you which four attributes of your credit history had the most impact on your score.

Potential ways to improve your credit score:

- Don't try to "quick fix"' your credit overnight. You could end up hurting your score. For example, your score may go down if you cancel a credit card that you have had for a long time.
- Don't pay someone to "fix" your credit history. Some credit repair firms promise, for a fee, to get inaccurate information taken out of your credit report. Accurate information cannot be deleted from your credit report. Some credit repair firms promise to "fix" your credit report by challenging information in it. They charge you a fee to do that. This is something you can do for yourself without paying the fee.
- Create a plan to improve your credit over time. Pay your bills on time. Pay at least the minimum balance due, on time, every month. If you cannot make a payment, talk to your creditor. Work to reduce the amount you owe, especially on revolving debts such as credit cards.
- Limit the number of new credit accounts you apply for. Several applications for credit in a short time will usually lower your credit score.
- Keep at it. Your credit history will improve over time if you make changes now and continue to improve. If you manage your credit better, your credit score will improve over time.

13. Where can I go for help with credit problems?

If you cannot resolve your credit problems alone, a non-profit credit counseling organization may be able to help you. Non-profit counseling programs are often operated by churches, universities, military bases, credit unions, and housing authorities. You can also check with a local bank or consumer protection office to see if they have a list of reputable, low-cost financial counseling services.

14. Will my credit history haunt me forever?

Probably not. Credit history is just that – history. Once you find out what attributes of your credit history are affecting your insurance credit score, you can work to improve your record. If your premiums are high because of your credit history and you take steps to improve your record, you should:

- Ask your insurance company to re-evaluate your insurance credit score at renewal.
- Shop for new insurance at renewal to see if better prices are available.

15. Does using credit information penalize minorities or low-income consumers?

Statistical studies have not conclusively determined whether insurance credit scoring disproportionately affects minorities or the poor. Insurance regulators nationwide are currently examining this issue.

Consumer groups worry that insurance credit scores will be lower for low income and minority groups. Consumer groups also point to the fact that most insurers and insurance credit scoring model vendors will not make their insurance scoring models public so consumers can see how they use credit data to calculate a score.

16. Where can I get more information?

- Ask your insurance agent or company if they have educational material that explains how they use credit.
- Contact the Department of Insurance by calling our Consumer Assistance Hotline toll free at **1-800-852-5494** or visit our website at **www.insurance.arkansas.gov.**
- Contact the Federal Trade Commission for information about the FCRA or review their consumer brochures on credit. Call 1-877-382-4357 toll free or visit their website at www.ftc.gov.
- Choice Point offers a service which allows consumers to see their insurance credit scores. The service cost $12.95 and is available at www.choicetrust.com.
- Search the Internet, but be sure the information you find explains how insurers (not lenders) use credit information.
- Contact your Cooperative Extension Service for information about improving your credit history.

17. Final Points to Remember

- There is a good chance your current or prospective insurer is looking at your credit.
- Ask your insurance agent or company if they use credit information, how they use it, and whether it affects your state.
- Get a copy of your credit report from each of the three national credit bureaus and correct any errors. Tell your insurance agent and company about any errors and tell them your side of the story.
- Improve your credit history if you have had past credit problems. Ask your agent or company for the top reasons (factors) that your insurance credit score is low, and work to improve those pieces of your credit history. If you are paying higher premiums because of your credit history, ask your insurer to re-evaluate you when you improve your credit. If your insurer will not agree to re-evaluate you, it is probably time to "shop around."
- Shop around for insurance. Insurance companies use credit information in different ways, so your rates can vary dramatically from company to company.

For more information contact:

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