F I S C A L   I M P A C T   R E P O R T

SPONSOR Sanchez, M. **DATE TYPED** 2/3/2004 **HB**

SHORT TITLE Prohibit Certain Actions By Vehicle Insurers **SB** 246

ANALYST Garcia

APPROPRIATION

Appropriation Contained		Estimated Additional Impact		Recurring or Non-Rec	Fund Affected
FY04	FY05	FY04	FY05		
			See Narrative.		

(Parenthesis ( ) Indicate Expenditure Decreases)

SOURCES OF INFORMATION
LFC Files

Responses Received From
Public Regulation Commission

SUMMARY

Synopsis

This bill prohibits insurers from either canceling or raising premiums on automobile policies due to unsatisfactory credit reports.

Significant Issues

The New Mexico Insurance Superintendent's Credit Scoring Task Force, other state legislatures, and many parties in the insurance community have studied this issue.

1) According to the Insurance Division, research evidence shows there is an undeniable correlation between insurance credit score and personal auto and homeowners claim costs. Although the causes of this correlation are subject to speculation, insurers are nonetheless permitted by actuarial principles to include insurance credit score as a rating element, just as they are with age, gender and other rating factors with known predictive value. Furthermore, the federal Fair Credit Reporting Act explicitly allows insurers to use credit report information in underwriting and rating.

2) Nonetheless, according to the Insurance Division, perceived abuses have arisen in its application, and many states believe they have the authority to curb these abuses through legislation and/or regulation. Such perceived abuses include:

- Canceling, non-renewing or otherwise denying coverage to customers because of an adverse credit score;
- Penalizing customers and applicants who do not have a credit history;
- Making no exceptions for the credit-damaging effects of job layoffs, catastrophic illnesses and other extraordinary life events;
- Failing to recalculate credit scores after errors in the underlying credit reports are corrected;
- Unfairly discriminating against low-income and minority citizens, if these citizens do indeed tend to have worse credit scores.

3) The Insurance Division claims that section A (which prohibits rate increases due to credit-scoring) of the bill would have a major impact on the personal auto insurance marketplace in New Mexico. The vast majority of personal auto policies issued in New Mexico include credit score as a rating element. Removing this element would raise rates for the approximately two-thirds of policyholders who have "good" credit scores and would lower rates for the remaining third who have "bad" credit scores.

The reason it would likely raise rates for "good' credit scores is that the insurer has less reliable information about the insured without credit scores and would have to treat all potential policyholders the same. Consequently, all potential policyholders (i.e. "good" and "bad" credit scores) would likely be lumped together where the premiums for those who are "good" increasing and those who are "bad" decreasing.

FISCAL IMPLICATIONS

Most insurers would have to re-file their rating plans with the Insurance Division, removing the credit-scoring element. This may likely increase the workload of processing rating plans from the Insurance Division staff. This can have a marginal effect on the Insurance Division's operating costs such as increasing for overtime or temp employees, but can likely be absorbed at current staffing and budget levels. The impacted fund can either be the General Fund or other state funds. The Insurance Division has numerous non-reverting funds that can be used.

ADMINISTRATIVE IMPLICATIONS

The state may be sued by insurance companies for attempting to curtail their rights under the federal Fair Credit Reporting Act.

OTHER SUBSTANTIVE ISSUES

1) The debate on credit scoring is equally valid (actuarially, legally and politically) for homeowners insurance as well as personal auto insurance. The Legislature might therefore wish to consider including homeowners in the scope of this bill. If so, homeowners will come under another part of the Insurance Code.

2) The bill, as currently written, does not prohibit insurers from using credit scores when assessing applications for auto insurance. This is the most significant underwriting use of credit scoring by insurers.

3) According to the Insurance Division, regulating instead of prohibiting the use of credit scoring in rating personal auto insurance may be more beneficial to the auto insurance marketplace in New Mexico. Such regulation can include requiring insurers to:

- File and obtain the Insurance Division's review and approval of all credit-scoring models, rating factors, and underwriting guidelines prior to their use;
- Treat customers who have little or no credit history as if they had an average or above-average credit score;
- Disclose to all policyholders the use of their credit information as well as the key elements of their credit history that have affected their credit score;
- Recalculate credit scores when errors in the underlying credit reports are corrected.

4) The National Council of Insurance Legislators (NCOIL) has written a Model Act on credit scoring which has been enacted into law by about a dozen states so far. This NCOIL model law addresses most of the key abuses of credit scoring that have been identified by consumer advocates, the National Association of Insurance Commissioners' Credit Scoring Working Group, and the New Mexico Insurance Superintendent's Credit Scoring Task Force.

5) The Insurance Task Force has recommended that non-renewal, as well as cancellation, of policies be prohibited because of adverse insurance credit scores. This can be accomplished by amending Section B as follows: "B. An insurer shall not cancel <u>or non-renew</u> a vehicle insurance policy…"

DG/yr