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August 3, 2011

CCIR Secretariat
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SUBJECT: Use of Credit Scores by Insurers – Response to Issues Paper

Thank you for the opportunity to respond to your issues paper on the subject of the use of credit scores by insurers. As you noted in the report, I surveyed Alberta automobile insurance consumers on this issue in 2010. I repeated several of these questions in my 2011 survey and had similar results. In addition to the telephone survey, I conducted two focus groups and contacted 10 rural consumers by telephone to further discuss their views on this and other issues.

From my discussions with Alberta consumers, I believe that the greatest concern is with respect to the issue of 'unexpected life events'. Particularly with the downturn in the economy, a number of respondents had experienced job loss or a downturn in business. They also reflected on others who had been through a divorce, death or other event that impacted their credit rating. While IBC guidelines may encourage discretion in using credit score, there is a risk that this is not always appropriately applied.

The other common comment from consumers was that 'credit score has nothing to do with a person's driving record'. Regardless of actuarial studies that may indicate a correlation, the consumers that I spoke to have difficulty accepting the relationship.

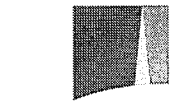
I hope these comments are of some value in your deliberations. If any member of your working group would like to discuss these comments, I would be pleased to do so.

Yours truly,

Merle Taylor

Consumer Representative
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AVIVA
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August 12, 2011

Via email transmission (cir-ccrra@fsco.gov.on.ca)

CCIR Secretariat
5160 Yonge Street, Box 85
Toronto, Ontario
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Dear CCIR Secretariat and Members:

RE: Consultations on the Use of Credit Scores by Insurers

The following comments have been submitted in response to the CCIR's questions outlined in the Issues Paper: Use of Credit Scores by Insurers ("Issue Paper"). Aviva Canada Inc. ("we" or "Aviva") believes that this consultation will provide an impartial voice in the debate regarding the use of credit information by insurers and demonstrate that any potential risks to consumers are being addressed by the industry. We hope that you find our comments helpful in your efforts to understand how credit is used by insurers and how it can be used to advance the consumers' interests.

1. General Remarks

a. Code of Conduct for Insurers' Use of Credit Information ("Code of Conduct")

By attempting to indentify all of the potential consumer-related risks an insurer's use of credit information may create, the Issue Paper also brings attention to how the insurance industry has been proactive in its efforts to either eliminate or mitigate these risks. The Code of Conduct the industry has developed addresses every concern and issue identified in the Issue Paper. Aviva has long been an advocate of the responsible use of credit information by insurers and we believe that adherence to the Code of Conduct achieves this and ensures that consumers' interests are being prioritized.

Nevertheless, Aviva believes that the current consultation is critical to further protecting consumers from other possible risks. The consultations may be able to bring attention to other, additional consumer risks that have not yet been identified or not yet known to the insurance

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industry. Doing so would provide the insurance industry with the opportunity to amend the Code of Conduct and ensure that *all* potential risks are addressed.

b. Regulatory Risk

From the outset, the Issue Paper establishes that it intends to identify all risks to consumers related to the use of credit information. However, based on the definition of "risk" the Issue Paper utilizes (more specifically, "fair treatment of consumers") there is one risk that is left unaddressed: regulatory risk where a prohibition of the use of credit contributes to unfair prices for low risk consumers.

The situation where lower-risk consumers are unfairly burdened with disproportionately higher premium prices to help cover the claims costs of their high-risk counterparts is generally known as cross-subsidization. It is the result of limited accuracy in the rating process where the insurer is unable to properly identify the degree to which different groups of consumers will contribute to the total expected losses for the year. Without accurate rating tools, it is more difficult to differentiate lower risk consumers from high-risk ones and offer commensurate policies prices to each. As a result, the insurer is forced to spread the anticipated claims costs throughout its consumer base, causing low-risk consumers to subsidize the losses of higher risk consumers and carry an unfair and disproportionate share of the total losses.

As the Issue Paper notes, independent studies have routinely demonstrated that credit information is highly accurate and a reliable indicator of the number of claims an individual is likely to make as well as the expected total dollar amount of those claims.[1] Credit's strong correlation with insurance-related risks allows insurers to better identify high-risk individuals and establish premiums and policies that are commensurate with their level of risk, ensuring lower risk consumers are not unnecessarily subsidizing their losses. As a result, an insurer is able to establish fair prices for all of its consumers.

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[1] Commonwealth of Virginia, State Corporation Commission, Bureau of Insurance, "Use of Credit in Underwriting," 1999. Fair Isaac, "Predictiveness of Credit History for Insurance Loss Ratio Relatives," October 1999.

Monaghan, James E., "The Impact of Personal Insurance Credit History on Loss Performance in Personal Lines," Winter 2000, *Casualty Actuary Society Forum.*

American Academy of Actuaries and Risk Classification Subcommittee of the Property/Casualty Products, Pricing, and Market Committee, "The Use of Credit History for Personal Lines of Insurance: Report to the National Association of Insurance Commissioners," 2002

"The Use of Insurance Credit Scoring In Automobile and Homeowners Insurance," A Report to the Governor, the Legislature and the People of Michigan, Frank M. Fitzgerald, Commissioner Office of Financial Services, December 2002.

Kellison, Bruce, Patrick Brocket, Seon-Hi Shin, and Shihong Li, "A Statistical Analysis of the Relationship Between Credit History and Insurance Losses," Bureau of Business Research, University of Texas at Austin, 2003.

Miller, Michael J. and Richard A. Smith, "The Relationship of Credit-Based Insurance Scores to Private Passenger Automobile Insurance Loss Propensity: An Actuarial Study," EPIC Actuaries, LLC, 2003.

Wu, Cheng-Sheng Peter and James C. Guszcza, "Does Credit Score Really Explain Insurance Losses? Multivariate Analysis from a Data Mining Point of View," 2003, *Proceedings of the Casualty Actuarial Society*, pg. 113-138.

Texas Department of Insurance, "Use of Credit Information by Insurers in Texas," December 2004

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Brokett, Patrick L. and Linda L. Golden, "Biological and Psychobehavioral Correlates of Credit Scores and Automobile Insurance Losses: Toward an Explication of Why Credit Scoring Works," The journal of Risk and Insurance, 2007, Vol. 74, No, 1, 23-63

c. Differences from Other Risk Factors

Section 3.2 of the Issue Paper does well to explain the differences between credit information and other variables insurers rely on to assess risks. However, it fails to note credit's most distinguishing feature: it is the variable over which consumers have the greatest amount of control and influence. Consumers can do little to nothing to affect their age, weather patterns in their area or their neighbourhood's claims history. However, excluding certain extraordinary circumstances, individuals have control over how they manage their financial affairs, how they behave when credit has been extended to them and their resulting credit scores. Unlike other rating factors, consumers can control their credit scores and impact their premium prices. Consequently, when discussing the differences between credit information and other rating factors, Aviva believes that it is important to highlight the amount of influence and control individuals have over their credit scores.

2. Consumer Risks Identified by the Issue Paper

a. Inadequate Consent

The Issue Paper identifies the potential risk of consumers receiving disclosures that are inadequate for providing informed consent. Aviva firmly believes that when dealing with private information and financial matters, providing clear and meaningful disclosures in order to obtain informed consent is of the utmost importance. For Aviva customers, our brokers provide a clear statement if credit is to be used. This statement also explains why and how it will be used and that the information will be protected.

Aviva believes these types of disclosures are crucial for ensuring that consumers understand exactly what it is they have agreed to. Not only is this consistent with proper business practices, but it also reflects an insurer's obligations as established by PIPEDA as well as the Code of Conduct. The disclosure provisions in the Code of Conduct more than adequately prioritize the consumers' interests and ensure that they receive disclosures sufficient to provide informed consent. Consequently, Aviva believes that the Code of Conduct, the existing legal framework as well as our own practices ensure that there is no material risk to the insureds in terms of the adequacy of disclosures.

However, Aviva is surprised by the research cited in the Issue Paper to illustrate the potential risk of inadequate consent. The Issue Paper refers to a survey in which 75% of the participants stated they were unaware that insurers use credit information. To begin, these types of disclosures are only provided for new business, which represent a mere 10-15% of insurance transactions per year. The study does not seem to have screened new business from renewals so it is impossible to gauge how many years it has been since the participants provided consent. It would not be reasonable to expect consumers to recall information on rating and underwriting that had been disclosed to them several years prior to participating in the survey. Furthermore, the study does not refer to the participants' understanding of other factors that would have also been disclosed, making it difficult to determine the value of the results regarding credit. While this particular study is plagued with issues, Aviva believes that a proper audit of insurers' credit-related disclosures would show that they are adequate and that consumers are providing informed consent.

b. Unreliable Credit Data

The Issue Paper next questions whether or not consumers are at risk of insurers utilizing inaccurate or unreliable information. However, the reliability of the credit information used by insurers is another risk that the Code of Conduct does well to address and mitigate. The Code of Conduct requires insurers to use only current and accurate credit information. In fact, the Code of Conduct establishes a duty for insurers to update the information they use upon request and to re-rate and re-underwrite when informed of a correction by a credit rating agency.

What seems to be overlooked by the Issue Paper's discussion on the risk of using unreliable credit data is the fact that using inaccurate or unreliable credit information is in stark contrast to the insurer's interest. Inaccurate data of any kind negatively impacts an insurer's ability to properly assess risks. The insurance industry is highly competitive and insurers rely heavily on their ability to accurately identify risks and establish commensurate, yet attractive policy prices. Any deficiencies in term accuracy of the variables being used would place an insurer at a distinct disadvantage, resulting in rates that are either uncompetitively high or insufficient to cover future losses. Consequently, insurers have an invested interest in utilizing only accurate and up-to-date credit information.

The concern the Issue Paper raises speaks more to the importance of Canadian consumers remaining vigilant and regularly checking with rating agencies to ensure their credit information is as up-to-date and accurate as possible. While potential problems with credit scores could result in premiums that are too high or too low with insurance transactions, the effects could be far more severe in other areas of a consumer's life where credit information is used (i.e., obtaining a mortgage or loan).

c. Availability and Affordability

The Issue Paper questions whether or not the use of credit information could possibly have a negative impact on both the availability and affordability of insurance. In terms of availability, the concern is that credit scores may be used to decline coverage or refuse to provide a quote. At Aviva, our policy is that we will not refuse to quote or decline a risk based on credit information. And, with the Code of Conduct, this policy is shared across the industry.

Also, Canada's insurance industry has recognized that there may be concern within the public regarding the potential for availability issues resulting from the use of credit and has since worked to alleviate these anxieties. The Code of Conduct prohibits insurers from refusing quotes and denying, cancelling or not renewing a policy based solely on a consumer's credit information. These provisions also prevent insurers from using credit as the only variable in rating and underwriting practices. Aviva believes that the provisions in the Code of Conduct more than adequately address any concerns regarding credit's impact on availability.

In terms of credit's impact on affordability, Aviva only uses credit information to provide discounts and reductions in premiums. Our use of credit never results in premium increases or surcharges. Therefore, in terms of our use of credit information, there are no affordability issues or risks to consumers.

In addition, the Canadian insurance industry is highly competitive and marked by diversity in operations. The fierce competition over consumers is driven by rates, which places a significant emphasis on the methods used to assess risk and determine policy prices. In terms of attracting

new customers, superior risk indicators allow insurers to offer lower premium prices by demonstrating that a competitor's prices are higher than the actual risk a consumer poses. This only highlights the importance of insurers having access to accurate and strong indicators of risk, such as credit information. Also, the level of competition and variety within the market in addition to the fact that credit information is only used with the consent of the consumer gives consumers a greater degree of choice and options in their efforts to find attractive coverages and prices and essentially eliminates any concerns related to credit's impact on affordability.

d. Insufficient Disclosure

Similar to questions regarding the adequacy of disclosures, the Issue Paper raises the concern that an insurer might provide insufficient disclosure. However, Aviva believes that certain aspects of what is described in the Issue Paper relate more to a general lack of understanding of the importance of prudent financial practices and the need for greater awareness in society of how individuals can control and improve their credit scores. This, of course, is distinct from issues or disclosures that are relevant to the use of credit by insurers.

Aviva believes that knowledge of proper personal finance and educating the public on the importance of their credit scores (i.e., the ways in which it may be used and how to manage it properly) are critical. However, we do not believe that insurers should be considered the appropriate source of the kind of information that would be required for such an extensive campaign.

The Issue Paper notes that an insurer's adverse action disclosures may not enable consumers to identify missing or inaccurate credit information or understand how to improve their credit scores over time. However, the insurer would not be privy to this type of information. Insurers would only know what the score is and not the factors or practices that resulted in that particular score. Consequently, it would be beyond the insurer's capability to provide tailored financial advice on how a particular individual could improve a credit score or identify potential errors in the information being used by a rating agency.

Insurers, however, do have an obligation to advise consumers when adverse action is taken as a result of their credit information. This is a practice that is required of them by the Code of Conduct. While this disclosure may not assist consumers in indentifying how the different aspects of their financial history have ultimately resulted in a given score, it provides a crucial first step in indentifying a potentially problematic credit score and the need to contact the appropriate or relevant institutions and potentially adjust financial behaviour.

e. Undue Impact on Certain Groups

The Issue Paper raises the concern that the use of credit information may negatively impact groups of individuals who generally fall outside of the norm in terms of credit scores. To be more specific, the Issue Paper lists those with no or thin credit scores and those whose scores have been negatively impacted by extraordinary life circumstances as being vulnerable and at risk of being essentially penalized by insurers who utilize credit information. However, this is another concern that the industry has proactively identified and worked to eliminate. The Code of Conduct establishes requirements for insurers in terms of the fair treatment of those who do not have credit scores, those who refuse to provide them and those whose scores have been affected by extraordinary events. Aviva believes that the insurance industry's practices and procedures,

which are backed by the Code of Conduct, do a more than adequate job of protecting their interests.

f. Privacy Breaches

Aviva considers the handling and protection of personal, private information of any kind to be of the utmost importance in financial services. Breaches of a consumer's privacy can have significantly troubling affects for consumers. As a result, insurers and other financial services providers have developed elaborate processes and controls to ensure that a consumer's private information, including credit scores, is adequately protected. These processes and controls are backed by a series of legal and regulatory requirements. For insurers who use credit information, the Code of Conduct also establishes further requirements and guidelines to which insurers must adhere.

Consequently, although we believe the issue to be important, Aviva does not believe that there is a material risk to the consumer's interests in terms of the handling of credit information. Insurers fully understand the nature and importance of privacy concerns, have vast experience in properly handling private and sensitive information and rely on internal policies and existing legal frameworks to prevent possible breaches.

g. Lack of Understanding

The final potential consumer concern the Issue Paper addresses is the lack of understanding of credit-based insurance scores and how credit information is used by insurers. The Issue Paper also questions whether or not objections to its use have been based on misinformation. Unfortunately, the debate around credit has been plagued by reoccurring misinformation. The most commonly raised misstatement is in regards to credit information's relationship with risk. As noted above, the strong correlation between credit scores and the potential for future insurance claims as well as their costs have been repeatedly demonstrated. While this relationship is well established and understood, opponents of it use will attempt to manipulate the public's general lack of understanding of rating and underwriting processes and claim the credit is somehow unrelated to insurance risk and used as part of some unknown calculations. These types of statements ignore a long history of actuarial data and independent research and seem intended to simply raise anxiety among insurance consumers.

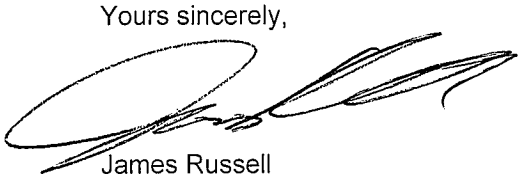
Another commonly seen misstatement of fact that has been used by opponents of the use of credit in advocating a ban includes the notion that a prohibition would promote consistency in regulation. The argument is that since the use of credit in auto insurance is prohibited, prohibiting its use in property insurance would promote consistency in regulating the two lines of insurance. However, the opposite also holds true: permitting its use in auto insurance would also promote consistency between the two lines. Opponents who have argued for consistency never seem to question how the insured is impacted by a prohibition and whether or not the existing ban in auto insurance advances the consumer's interests.

Not only do such misstatements detract from the potential for reasonable public discussions regarding insurers' use of credit information, they also shift focus away from the fact credit is a sound and reliable actuarial variable. What also gets lost is that when used in adherence to the provisions of the Code of Conduct (i.e., responsibly), credit can provide a host of advantages for consumers.

3. Conclusion

Aviva appreciates having the opportunity to submit comments and assist in the CCIR's efforts to understand the potential risks to consumers that may arise from the use of credit information by insurers and how these potential risks are addressed by the Code of Conduct. It is expected that the consultations will provide an impartial voice in the debate regarding the use of credit and we believe that it will also show how well the Code of Conduct does to mitigate any risk to consumers and ensure that their interests are being advanced.

Yours sincerely,



James Russell
Executive Vice President, Chief Underwriting Officer



Québec, le 12 août 2011

Madame Danielle Boulet
Présidente du CCRRA
Conseil canadien des responsables
de la réglementation d'assurance
5160 Yonge Street
PO Box 85
Toronto (Ontario) M2N 6L9

Objet : Commentaires portant sur le document de réflexion intitulé « Utilisation des pointages de crédit par les assureurs »

Madame,

La Corporation des assureurs directs de dommages du Québec (**CADD**) répond à l'invitation du Conseil canadien des responsables de la réglementation en assurance (**CCRRA**), comme intervenant de l'industrie en assurance de dommages, afin de commenter et de partager ses réflexions sur la question de l'utilisation des pointages de crédit par les assureurs telle qu'énoncée dans le document de réflexion du groupe de travail mis sur pied par le CCRRA.

La CADD regroupe 12 assureurs dont le mode de distribution est généralement par le biais d'agents à leur emploi et de travailleurs autonomes ayant adhéré à des ententes d'exclusivité. La CADD distribue et supporte présentement plus de 50 % des consommateurs québécois en matière d'assurance automobile et habitation.
Les membres sont actuellement :

- Assurances générales Banque Nationale inc.
- Compagnie d'assurance générale RBC
- Desjardins Groupe d'assurances générales
- Groupe Allstate du Canada
- Groupe Promutuel
- Industrielle Alliance Assurance auto et habitation inc.
- La Capitale assurances générales inc.
- La Compagnie d'assurance Belair inc.
- La Compagnie mutuelle d'assurance Wawanesa
- La Federated, Compagnie d'assurance du Canada
- SSQ, Société d'assurances générales inc.
- TD Assurance

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Fondée en 1991, la CADD a poursuivi plusieurs objectifs dont :

- la promotion du libre choix du consommateur en matière de distribution des produits et services d'assurance de dommages;
- l'exercice de la profession en harmonie et en collaboration avec tous les intervenants;
- la recherche et le maintien de l'équité entre les réseaux de distribution;
- l'assurance que les membres de la CADD ont le pouvoir et la capacité de faire face aux nouvelles réalités du marché;
- l'assurance de la souplesse et de l'efficacité des réglementations.

C'est par conséquent à titre d'intervenant très présent dans le marché de l'assurance de dommages au Québec que la CADD intervient dans cette consultation.

C'est également à ce titre qu'elle a pris connaissance du document de réflexion du comité de travail portant sur l'utilisation des pointages de crédit par les assureurs. Ce document soulève les bons enjeux, pose les bonnes questions en identifiant les risques potentiels et énonce clairement les règles existantes qui ont pour objectif de limiter les risques et de protéger adéquatement le consommateur. Il témoigne également de l'expérience dans les différentes provinces canadiennes en fonction de la réglementation et des règles propres pour chacune des provinces.

Comme le souligne le document de réflexion, l'utilisation des pointages de crédit est déjà très largement répandue au Québec : « […] l'Autorité des marchés financiers confirme que l'utilisation du pointage de crédit est plus répandue dans sa province [le Québec]. Des 80 assureurs ayant souscrit de l'assurance automobile privée en 2009, 28 d'entre eux représentant 86 % du marché ont utilisé ce critère. En assumant que ces mêmes assureurs utilisaient aussi le pointage de crédit en assurance habitation, nous avons calculé qu'une portion similaire du marché est touchée. » Or, cette utilisation n'a pas entraîné au Québec les conséquences potentiellement néfastes mentionnées dans le document de réflexion. L'industrie de l'assurance de dommages du Québec évolue présentement dans un environnement sainement compétitif, soucieux de respecter les droits des consommateurs. Les primes et l'accessibilité en assurance de dommages semblent bien perçues par ces derniers. Les membres de la CADD ont d'ailleurs constaté que l'Autorité des marchés financiers (**AMF)** est fière de présenter les résultats émanant du Québec, tant en matière de risque automobile qu'en matière d'accessibilité en assurances de dommages.

La CADD a par ailleurs pris connaissance des commentaires émis par **CADRI** (Canadian Association of Direct Response Insurers) sur la question et l'expérience de l'utilisation des pointages de crédit dans l'ensemble des provinces canadiennes et elle endosse totalement la position et les commentaires émis par celle-ci. Elle supporte également la position du Bureau d'assurance du Canada (**BAC**) qui a publié un code de conduite et des lignes directives auxquelles tous les membres de la CADD adhèrent actuellement.

La CADD considère cependant qu'il est important de faire ressortir le contexte d'utilisation qui prévaut au Québec, étant la province où cette utilisation est la plus répandue et la mieux perçue par le consommateur.

La CADD présente donc, dans le présent document, les commentaires et les suggestions de ses membres sur certains des risques potentiels identifiés dans le document de réflexion et qui permettront de mettre en relief les pratiques actuelles au Québec.

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Commentaire sur les risques potentiels pour le consommateur

La CADD considère que les risques potentiels liés à l'utilisation des pointages de crédit dans les activités de souscription et de tarification en assurance de dommages au Québec sont gérés de façon appropriée. Les lois actuelles qui encadrent cette industrie offrent des protections adéquates et complètes pour le consommateur. Les pratiques actuellement répandues au Québec sont professionnelles, prudentes et respectueuses des droits des consommateurs. La CADD considère que ce serait plutôt le retrait de l'utilisation des pointages de crédit qui représenterait un risque pour le consommateur. D'une part, ce retrait provoquerait des changements de prime lors de la période de transition et, d'autre part, le retrait priverait les assureurs d'un outil qui leur permet de fixer des primes justes et équitables pour l'ensemble des assurés.

En ce qui concerne les risques spécifiquement identifiés dans le document de réflexion (réflexion de juin 2011 faite par le groupe de travail sur l'utilisation des pointages de crédit par les assureurs) voici, d'autre part, quelques commentaires et réflexions :

5.1 Consentement inadéquat

La CADD considère que le consentement est effectivement essentiel et extrêmement important pour que le consommateur sache à quoi et pourquoi il a donné son consentement. Au Québec, l'industrie s'est dotée de saines pratiques en la matière et utilise ce procédé avec beaucoup de transparence. Les assureurs informent clairement le consommateur pour qu'il sache et comprenne le type d'information que l'assureur veut obtenir et comment l'assureur a l'intention de l'utiliser. Au Québec, les consentements sont très explicites et conservés dans le dossier du client. La brochure d'information publiée par le BAC Québec à l'intention des consommateurs est d'ailleurs un excellent outil d'information, et traduit le fait qu'il n'y a pas de tabou dans l'utilisation du pointage de crédit au Québec.

Le code de conduite également émis par le BAC a justement permis aux assureurs de développer de saines pratiques d'utilisation. L'ensemble des assureurs membres de la CADD a adhéré à celles-ci, de même qu'aux lignes directrices visant à encadrer cette utilisation dans les activités de souscription et de tarification. La CADD recommande d'ailleurs que l'adhésion à ce code soit obligatoire et non volontaire. Cela assurera que l'ensemble de l'industrie se soumette à ces règles.

5.2 Données de crédit non fiables

La CADD est tout à fait d'accord sur la question de la fiabilité des données transmises par les agences d'évaluation du crédit. Ces agences doivent se doter de mécanismes de contrôle de la qualité afin de fournir aux consommateurs et aux assureurs des renseignements exacts et totalement à jour. Cette question relève par ailleurs des mécanismes d'autoréglementation des agences de crédit. La qualité des renseignements ne semble toutefois pas être un enjeu au Québec et n'a soulevé aucun débat, ni du côté des assureurs ni du côté du consommateur. *La Loi sur la protection des renseignements personnels dans le secteur privé*, L.R.Q., ch. P-39.1 encadre d'ailleurs de façon rigoureuse la création, la gestion et la mise à jour des dossiers créés dans le secteur privé. La CADD est d'avis qu'un consommateur doit facilement pouvoir demander et obtenir accès à son dossier pour en vérifier son contenu et sa pertinence, à même le processus de demande d'accès prévu par la loi. Les mécanismes mis en place encadrent déjà une bonne partie de cette pratique.

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5.3 Disponibilité et accessibilité de l'assurance

La CADD et tous ses membres endossent pleinement le principe voulant que le processus de pointage de crédit ne soit pas utilisé comme motif de refus d'assurer le consommateur. La CADD ne pense pas qu'il s'agit là d'un risque potentiel. Par ailleurs, si le consommateur refuse d'accorder son consentement à utiliser son pointage de crédit dans la tarification, il doit être clairement avisé qu'il ne pourra pas profiter de la meilleure offre.

5.4 Divulgation insuffisante

Au Québec, le consommateur profite d'une tarification juste et équitable dans un contexte de compétitivité saine et qui lui est même profitable. Chaque assureur a effectivement développé son modèle mathématique qui lui est propre, tout en respectant une saine compétition. Les lois qui encadrent déjà la distribution des produits d'assurance, la protection des renseignements privés et toute la réglementation qui concerne le consommateur lui assurent par ailleurs une protection adéquate. La CADD est d'avis cependant que toute l'industrie et tous ses intervenants doivent rendre l'information disponible sur le sujet notamment dans sa documentation, sur les sites WEB, de concert avec les agences de crédit et le BAC. De cette façon le consommateur aurait accès facilement à l'information pertinente pour mieux comprendre cette utilisation. La divulgation rencontre cependant certaines limites: la confidentialité des informations contenues au dossier et le respect de la vie privée. À cet égard, les agents à l'emploi d'assureur n'ont pas directement accès au dossier de crédit du consommateur et rencontre de ce fait des limites à leur capacité à informer adéquatement la clientèle sur la façon de modifier leur comportement pour réduite les coûts d'assurance en lien avec leur dossier de crédit

5.5 Incidence indue sur certains groupes

La CADD appuie totalement le principe voulant que tous les assureurs traitent équitablement le consommateur qui a subi, au cours de sa vie, une situation extraordinaire, indépendante de sa volonté ou qui a exercé son droit de refuser de donner son consentement. Le guide élaboré par le BAC de même que les lignes directives comportent des directives en ce sens. Le fait d'adhérer au guide, comme c'est le cas pour les assureurs au Québec, rassure les consommateurs d'être traités équitablement.

5.6 Violations de la vie privée

Les lois, les règlements et tous les mécanismes mis en place actuellement au Québec protègent adéquatement le consommateur en matière de protection de la vie privée. En effet, la Commission d'accès à l'information du Québec, la Commission des droits de la personne, l'AMF, de même que les tribunaux administratifs et de droit commun offrent au consommateur une série de mécanismes qui lui permettent de protéger et de faire respecter ses droits. En plus du guide élaboré par le BAC, les mécanismes et formules mathématiques prévus par les assureurs dans l'utilisation du pointage de crédit prévoient protéger et préserver la confidentialité des renseignements recueillis.

5.7 Incompréhension

Il revient effectivement aux différents intervenants de l'industrie d'informer pleinement le consommateur sur les buts visés par l'utilisation des pointages de crédit, sur l'utilisation qui en est faite et sur les effets sur la tarification pour l'ensemble des assurés. Il revient à l'industrie de créer un climat de confiance dans la transaction entre le consommateur et l'assureur. Selon l'expérience des membres de la CADD, il y

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aurait eu très peu d'objections à l'utilisation du pointage de crédit au cours des dernières années, et les très rares refus ont été reliés souvent à des choix personnels que les assureurs ont respectés, plutôt qu'à de l'incompréhension face à l'utilité du processus. Les membres de la CADD mettent d'ailleurs tout en œuvre pour que le processus soit transparent afin que le consommateur comprenne le but recherché, c'est-à-dire une tarification adaptée au risque juste et équitable pour l'ensemble de la population. Les informations prévues dans la brochure émise par BAC Québec sont d'ailleurs fort utiles en ce sens.

La CADD appuie totalement le document que CADRI a déposé pour l'ensemble des assureurs directs des provinces canadiennes. Leurs commentaires, réflexions et suggestions très pertinents permettront au CCRRA de mieux saisir tous les enjeux entourant ce processus et d'en saisir toute la portée pour l'industrie.

La CADD remercie très sincèrement le CCRRA de lui avoir donné la possibilité de faire part de ses commentaires comme intervenant de l'industrie en matière d'utilisation des pointages de crédit. Le CCRRA peut d'ailleurs compter sur la pleine collaboration des tous les membres de la CADD pour participer, collaborer et travailler à l'élaboration de règles ou de guide visant à bien encadrer cette pratique et à diffuser le maximum d'information au consommateur.

En espérant que ces commentaires et quelques réflexions éclaireront davantage le CCRRA sur cette pratique et rassureront le consommateur en la matière.

Recevez, Madame, l'expression de nos sentiments les meilleurs.

Henry Blumenthal
Président de la CADD

Use of Credit Scores in Personal Lines Insurance

Submission to the

Canadian Council of Insurance Regulators
Credit Score Working Group

On the Use of Credit Scores by Insurers Issues Paper

August 14, 2011

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CADRI is an organization of insurers selling and servicing property and casualty insurance products through direct marketing and distribution. Our members offer both home and auto insurance products across Canada through their own work force of well-trained licensed insurance professionals supported by advanced know-how and technology in telephony, processes and on the internet Buying direct from the insurance company offers consumers an important alternative to the use of the broker channel. Consumer benefits include extended hours of service and fast, cost effective, technology-enabled sales and services, all at a low cost option. The advantages are significant and the utilization of direct insurance channels is growing as consumers seek increased convenience for the purchase of their home and automobile insurance while keeping costs down.

Introduction

Numerous American studies have indicated a strong correlation between credit scores and claims risk. The studies show that the lower the credit score, the greater the likelihood and severity of claims. The American Academy of Actuaries and the Insurance Information Institute are among the prominent organizations the have endorsed the use of credit scores in the insurance industry.

As the CCIR Issues Paper notes, however, there have been no equivalent studies in Canada. To help address this shortcoming, CADRI commissioned Baron Insurance Services, of Toronto, to conduct a statistical study using solely Canadian data to determine what, if any, correlation exists between credit score and insurance losses. This analysis was based on aggregate consumer data provided by five major Canadian insurance companies. Overall, the analysis of the data showed a strong correlation between credit scores and insurance losses. Better credit scores correlated with lower claim frequency, lower claim costs, lower pure premium and lower cost ratios.

We have included with our submission a full copy of the study, which was authored by Barb Addie and Brad Neilson of Baron Insurance Services.

While this and other studies show a strong correlation between credit scores and claims

risk, they do not detail the reasons why. However, logic would suggest that a person who manages their finances responsibly and carefully also takes care of their property and also drives more responsibly. Thus, for a P&C insurer, this person represents a lower risk than someone who is not diligent with their financial affairs. The fact is most people manage their finances well and have a good credit score, and thus benefit from the use of credit scores through stable or lower insurance premiums.

Many of the objections to the use of credit scores raised by groups in the United States, such as the over-representation of certain ethnic or racial groups in lower-score categories, are not as relevant in Canada. This is because we benefit from much lower levels of income inequality and a much stronger social safety net.

It's important to understand that insurance credit scores do not evaluate income, assets or liabilities, but rather the consumer's credit behaviour. Consumers who pay their bills and don't abuse their access to credit will have a high score, regardless of their income or assets.

This is not a case, as some have charged, of the poor having to pay more. There is no evidence in Canada that there is correlation between income level and credit score. Our own anecdotal experience would suggest the opposite – that consumers with good and consumers with bad credit scores are spread across all income levels.

In that sense, the use of credit scores, along with other underwriting criteria, enable insurers to treat consumers more fairly because the premium established for an individual reflects as accurately as possible the risk he or she represents. In fact, an argument could be made that credit scores are more fair than many other underwriting factors (such as age, sex, local crime and accident rates, etc.), because consumers can directly control their credit scores through their credit behaviour.

In terms of regulation, we believe that fairness of price is a basic cornerstone of an effective insurance market. The fewer underwriting factors allowed in determining risk, the less accurate and fair the premiums, and the less dynamic and competitive the market. We also believe that it is clearly not fair for low-risk clients to pay more in order to subsidize high-risk clients. And because they are not penalized for their negative behaviour, there is no incentive for high-risk clients to take corrective action -- i.e., improve their credit scores through better financial discipline.

We appreciate the opportunity to outline our position on the use of credit scores and to comment specifically on each of the issues raised in Section 5 of the document, as follows.

5. Potential Risks to Consumers

The Insurance Bureau of Canada's "Code of Conduct for Insurers' Use of Credit Information" outlines a fair and effective approach to the use of credit scores by insurance companies. As such, it addresses the potential consumer-related concerns

raised by the CCIR Issues Paper. Although this code is voluntary, all CADRI members have agreed to sign and follow it. Any practices by CADRI members that fell short of the Code have or are being updated to ensure they adhere to both the principles and procedures outlined in the Code.

In addition, we strongly believe that it is in the best interest of consumers and the insurance industry if all insurance companies, and their intermediaries, agreed to follow the code.

5.1 Appropriate Consent

CADRI Position: Gaining appropriate consumer consent to request and use their credit score is critically important. In alignment with the Code of Conduct, consumers must give their consent freely, directly and expressly, and the request for consent must be clear and understandable.

Regulator Concern: Consumers may not know that they have given permission to an insurer to use their credit information or a credit score for determining a consumer's eligibility for insurance and the premium to be charged.

Desired outcome: Prior to using the information, insurers ask consumers for their permission. Consumers know and understand the type of information the insurer is seeking to obtain, including how the insurer intends to use the information.

As the FSCO survey cited in the Issues Paper indicated, all insurers do follow Federal and Provincial regulations in gaining the consent of applicants and policyholders to use their credit information. The question is, are insurers explicit enough in explaining why and how the credit information will be used?

On the one hand, consumer credit information is regularly used in a number of industries, including lending, credit cards, apartment rentals, cell phone plans and more. As such, it is not unusual for consumers to allow organizations to check their credit file.

Given that an insurance policy is a financial contract, typically involving hundreds or even thousands of dollars, it is not surprising that insurers would be interested in the credit worthiness of their consumers.

On the other hand, insurance differs from lending and other related industries in that credit information is also used, along with various other factors, to predict claims frequency and cost. As a result, it can impact the consumer's premium, either positively or negatively.

Does this require that insurers be more explicit in communicating with consumers about their use of credit information than other industries?

The IBC Code of Conduct for Insurers' Use of Credit Information outlines clear principles and procedures for gaining explicit consumer consent to collect and use their credit information:

"The insurer must secure prior consent to collect and use credit information from the consumer in accordance with the following principles and procedures:

Consent must be informed.

a) The following are characteristics of informed consent:

- Customers must not feel obliged to give consent;
- Customers must understand the nature and scope of the request. The request for consent must be clear and understandable to ensure that customers know specifically what they are consenting to and how that consent will be used;
- Consent must be specific and the insurer must not presume consent will be given. Consent may be given verbally, in writing or via an e-medium. E-medium consent should be a field that the policyholder can click on directly in order to give consent.

Prior to an agent or broker collecting credit information, the consumer consent field (agent's or broker's screen) must be clear and explicit for the user. The field must not default to *yes.*

b) No one can give consent for another person. Consent must be obtained directly from each individual in the household if their credit information is to be used. Any applicant or co-applicant about whom credit information will be collected and used must either provide a signed consent form or provide verbal consent directly to the agent or broker.

c) Consent retention: The insurer must maintain the trail or proof of consent in the consumer file (paper, e-medium or other). The retention period for the consumer file is the minimum period required by law.

d) Duration of consent: The consent is valid for the duration that the policy is in effect. Unless withdrawn by the policyholder, consent is valid for as long as the policyholder has a continuous business relationship with the insurer, i.e., the policy is in force until cancelled. Under these circumstances, the insurer can request the insured's credit record or credit information from the consumer reporting agency, by relying on the initial consent.

Wording of consent question (Verbal or written)

Key elements to be included in the consent request:

i. Authorization to collect information from consumer reporting agencies;
ii. Nature of the information sought (e.g. credit information);
iii. Use made by the insurer of the credit information (what will it be used for);
iv. Consent use period (validity);
v. Right to withdraw and consequences (an insured may withdraw consent at any time in writing; however, he or she might not benefit from the insurer's best quote)."

Given some of the news coverage and surveys results cited in the CCIR Issues Paper, it's evident that insurers need to do a better job in explaining why and how they use credit scores *inclusive of potential benefits to consumers*. The IBAO survey also suggests this need for improved consumer information and education. Rather than condemning the use of credit, the IBAO survey highlights the need for the entire industry to do a better job of explaining the use of credit scoring. The IBC Code of Conduct provides an effective approach as a means to accomplish this objective.

5.2 Reliability of Credit Data

CADRI Position: Like other organizations that rely on credit information, insurance companies have no control over the accuracy of the data provided by the credit agencies. These agencies are regulated by government and are required to maintain accurate files, and to correct inaccuracies when so informed. Insurance companies have a role to play by using the most current credit score available and encouraging consumers to check and update their credit files (if required).

Regulator Concern: The underlying credit data from which the credit based insurance score is derived may be unreliable.

Desired outcome: Insurers are using current and accurate credit information

Since credit scores are used in a variety of different industries on a multitude of levels, concerns surrounding unreliable credit information reach far beyond the insurance industry. Industries using credit information include the following:

Banking	Credit Cards
Landlords	Retail companies
Cell phone companies	Utilities

Insurers use the credit information provided by the two major credit agencies in Canada, Trans-Union and Equifax. Both of these are large, international, reputable and established businesses. They maintain more than 20 million consumer credit bureau files in Canada, and help consumers better manage their credit. Both organizations are subject to government regulations requiring that they keep accurate, up-to-date records, and maintain consumer privacy.

Canada's insurers use and follow only the credit information provided by these two

organizations. As such, all consumers are treated consistently and fairly.

Government, financial, consumer protection and other organizations actively encourage consumers to check their credit information – which can be done free of charge – to ensure it is current and accurate. In addition, the consumer information about credit score is frequently highlighted in the news media.

As mentioned previously, all CADRI members have committed to following the IBC Code of Conduct for Insurers' Use of Credit Information. This requires that the credit information used be current and accurate, as follows:

- "When informed by a consumer reporting agency of a correction, supplement or deletion to an individual's credit file, the insurer must immediately make the necessary adjustments to the file and shall re-underwrite and re-rate the consumer as soon as practical;
- After re-underwriting or re-rating the insured, the insurer shall make any further adjustments that are consistent with its underwriting and rating practices;
- If an insurer determines that the insured has overpaid premium it shall comply with pertinent regulations relating to refunding of overpayments;
- At the request of the consumer, the insurer shall inform the consumer of the source/supplier of the credit information used (i.e. identifying the specific consumer reporting agency that supplied the credit information);
- The customer/applicant for insurance is responsible for contacting the consumer reporting agency to verify his/her file and, if applicable, request that it be corrected."

5.3 Availability and affordability of insurance

CADRI Position: Credit scores are one of many underwriting variables that are used in determining a consumers risk profile and premium. A credit score is never used on its own.

Regulator Concern: Insurance may be unavailable or no longer affordable due to credit based insurance scores.

Desired Outcome: The basic insurance mechanisms (e.g. pooling of risk) and public policy goals for insurance are met.

As the Issues Paper states, credit scores are only one factor among many in an insurer's underwriting evaluation. The IBC Code of Conduct clearly states that credit score cannot be used as the sole variable:

"The insurer must not refuse to quote or base an insured's renewal rates, or deny, cancel or non-renew a policy of personal insurance solely on the basis of credit information without consideration of other non-credit underwriting or rating variables."

In some instances, a low credit score may prompt an insurer to take a closer look at a policyholder – for example, to do a home inspection – to determine if there are other risk factors that should be considered. In rare circumstances, a low score combined with other underwriting factors – such as a large number of claims – may lead to changes in a consumer's premium or, in extreme cases, to cancellation of policy. However, since insurance companies use different underwriting variables, the same consumer may receive a lower rate, or be approved, by other insurers.

In addition, consumers who are penalized because of a low credit score can take steps to improve their credit rating. This will benefit them well beyond any insurance savings, as a low credit record will increase the cost of borrowing, along with many other products and services. Fortunately, numerous consumer and government agencies provide advice to consumers to help them better manage their finances and improve their credit record.

As the Issues Paper states, about 75% of Canadians have a good or average credit score, according to the Financial Consumer Agency of Canada. It is not unreasonable to assume that the percentage is even higher among Canadians who have reached the point in their lives where they have acquired homes, cars and other possessions that require insurance coverage.

Certainly, the experience of CADRI members shows that the majority of consumers see their premiums go down or stay the same with the introduction of credit scoring. There is no evidence in markets such as Quebec, where credit scoring is widely used for both auto and property insurance, that it has negatively impacted the availability or affordability of insurance.

5.4 Disclosure and Financial Literacy

CADRI Position: CADRI supports government and financial industry initiatives to promote greater financial literacy in Canada. This would include the importance of maintaining a good credit rating, as it can affect the cost and availability of many services and products. Insurers have a particular role to play in helping consumers understand the impact of their credit score and how they can check and improve their credit information.

Regulator Concern: Consumers may not have sufficient information about how to modify their behaviour in order to reduce insurance costs.

Desired Outcome: Consumers know how to improve their credit based insurance score if an insurer takes an adverse action due to a low score.

Credit score is used in a variety of areas in an individual's life, and a low score can impact a consumer in many ways. Credit scores are not based on income, wealth or assets, but on financial behaviour – for example, whether bills are paid on time.

While different insurers use different scores they all reflect an individual's history of debt payment and financial discipline.

The Internet provides consumers with an incredible amount of information on credit score, on why good credit is required, and what to do to ensure you maintain or improve your credit score.

- There are numerous website links from standard blogs, to financial institutions, regulator websites to tweets, and provincial consumer regulation acts
- Canadian Bankers Association (CBA), Financial Consumer Agency of Canada (FCAC), and provincial consumer ministries contain a great deal of information spelt out in laymen terms for the average consumer to understand.

These organizations provide both printed and online information to help consumers understand their credit report/score, how they can build a good credit history, and steps they can take to repair their credit ratings.

Other sources of good credit information include the two credit agencies, Trans-union and Equifax, and the Insurance Bureau of Canada (IBC).

According to the IBC's Code of Conduct, insurers must, upon request, provide consumers with an explanation of any changes in their policy as a result of accessing their credit information. Consumers can then contact the two credit agencies and take action to correct any inaccurate information or other necessary steps to improve their credit rating.

The Code also requires that the insurer, once informed by a policyholder that his or her credit file has been updated, confirm with the credit agency and then make the necessary adjustments to the consumer's file and re-underwrite and re-rate the policy as soon as practical.

Should a consumer be unhappy with the insurer's use of his or her credit information, each insurer has complaint procedures in place, as required under federal and provincial regulations.

5.5 Fair Treatment

CADRI Position: We believe that the use of credit scores, along with other underwriting criteria, enables insurers to treat all consumers fairly because the premium established for an individual reflects as accurately as possible the risk he or she represents. We do not believe that the use of credit scores is disadvantageous to any particular group. Under the IBC Code of Conduct, credit scores are not used for those individuals who have not yet established a credit file. We also support the Code's recommendation that insurers use their discretion when it comes to consumers whose credit file is adversely affected by an extraordinary life event.

Regulator Concern: Insurers may unduly penalize consumers who refuse to provide consent, or who do not have a credit history, or whose credit score has been negatively affected by extraordinary life circumstances.

Desired Outcome: Insurers treat consumers who have experienced unexpected life events beyond their control or who have exercised their right to refuse consent fairly.

CADRI believes that insurance should be:

- accessible
- affordable
- priced to reflect risk.

Consequently CADRI members do not refuse to quote, sell or renew a policy based on a consumer's credit score, which would reduce our portfolio and would be counter-productive to our business.

Some stakeholders are concerned that credit scores will be lowest amongst the lower income segments who are already under financial strain and that it would not be fair to burden those persons with higher insurance premiums. CADRI members note that credit score is an objective, fair and accurate tool. There is no correlation between credit score and income. Furthermore, income levels have no bearing on responsible financial management. Almost all provinces have Consumer Reporting Legislation and prohibit the collection of information as to race, creed, colour, sex, ancestry, ethnic origin, or political affiliation in a credit report.

Some CADRI members have conducted their own independent analysis to confirm that income and credit scores are not correlated. This is not to say that examples of a low income person having a bad credit score cannot be found. The same challenge exists with all underwriting variables such as accident history or traffic violations but there is no call to waive a speeding ticket due to an individual consumer's income level.

As the Issues Paper points out, the IBC Code of Conduct provides special allowances for consumers who have not established credit information. In such cases, the insurer cannot deny coverage, cancel or refuse to renew their policy based solely on the absence of credit information. "In the absence of credit information, underwriting and rating decisions will be based upon the relevant information that is available to the insurer." This is a fair approach for the newcomer to Canada or the young person who does not have enough credit history to build a file.

The Code of Conduct is also clear in the event a consumer refuses to give consent to use their credit information. It states: "the insurer shall not refuse to provide an insurance quote to the consumer, nor refuse to insure a consumer, nor terminate or refuse to renew a policy." However, the consumer may not benefit from the best rate. Again, this is only fair.

Finally, the Code also recommends that insurers use their discretion when it comes to

consumers whose credit file is adversely affected by an extraordinary life event, such as the death of a spouse or identity theft.

As mentioned previously, CADRI supports the IBC Code of Conduct, and all CADRI members have agreed to sign and follow the Code.

5.6 Privacy

CADRI Position: While the collection of any additional confidential information naturally increases the risk of privacy breaches, all insurers have their own privacy code available online and in print versions, as per Federal privacy legislation. CADRI members and other insurers already collect a large variety and quantity of client data, and the obligation and means to protect this data is well established.

Regulator Concern: Insurers may breach confidential credit information.

Desired outcome: Insurers have sufficient controls in place to safeguard personal credit information.

The risk to consumers is no greater than the risk that already exists with other confidential client information such as driving history, conviction history and claims history that are collected and housed by insurers with adequate safeguards. In fact, some information in a claims file is far more sensitive than your typical underwriting information and the protections required are long established and long practiced by the insurance industry. For example, salaries, medical history and family history are commonly collected in the handling of an accident benefits or bodily injury claim file.

In addition, it is worth noting that the credit information used by insurers is typically a credit score and not the complete credit report. This type of information is of limited use to fraudsters and reveals little about the individual in the unlikely event that it were to fall into the wrong hands.

Moreover, violations and sanctions for privacy breaches relating to credit scoring are covered under PIPEDA legislation and applicable provincial privacy legislation.

5.7 Consumer Understanding

CADRI Position: Although there is great deal of information available to consumers about credit reports and scores, their application to insurance is not as easily understood. Consequently, CADRI members and other insurers could expand their efforts to build consumer understanding.

Regulator Concern: Consumers may not be sufficiently educated regarding credit-based insurance scores.

Desired Outcome: Consumers have a good understanding of credit-based insurance scores and are confident in their dealings with their insurers.

In order to obtain proper consent from consumers to gather and use credit information, insurers disclose what information will be gathered and the ways in which the information will be used. This is legislated under PIPEDA and forms part of the IBC Code of Conduct for Insurer's Use of Credit Information.

Obviously, consumers' general knowledge and education about credit applies to credit-based insurance scores. As mentioned earlier, education about the significance of credit history and score is the responsibility of the entire financial industry, as well as government agencies. There is already a wealth of information that is easily accessible to consumers, and efforts are being made to increase consumer education.

That being said, the application of credit scores in insurance underwriting may not seem obvious to consumers. Insurers need to build consumer understanding of the overwhelming evidence showing that credit scores are highly predictive of risk and therefore allow insurance policies to be more fairly and accurately priced.

Many insurers have information on their websites explaining their use of credit scores. In addition, insurance agents are trained to answer consumer questions. Nonetheless, given the recent media attention, and survey results, it could be argued that the industry should be doing more to build consumer understanding -- including the fact that the use of credit scores results in unchanged or lower premiums. .

Insurers, insurance brokers and other intermediaries all have a role to play in proactively educating consumers about credit-based insurance scores and their uses. More of this can be done via conversations at the time of quoting and/or binding policies, via general information published on-line, and via print material.

Conclusion

In conclusion, we would again like to thank the CCIR for the opportunity to comment on these issues. We encourage the Working Group to review the IBC Code of Conduct in detail, as we strongly believe that it addresses all of the consumer protection concerns raised in the Issues Paper.

We would also encourage the group to examine the situation in Quebec, where credit scores are widely used for both property and auto insurance.

As mentioned in the introduction, CADRI believes that the more predictive rating variables that can be used, the more dynamic, innovative and competitive the market. These market characteristics are essential to ensuring that consumers have access to affordable products, and that products and service standards are evolving to meet their changing needs.

Our objective as insurers is to price each risk as accurately as possible, by using as many variables as possible to fully understand the risk. As so many studies have demonstrated, including the Canadian Study by Baron Insurance Services, credit scores are predictive of the number of claims consumers file and the total cost of those claims. The use of scores is therefore likely to make the price of insurance better match the risk

of loss posed by the consumer. Thus, on average, higher-risk consumers will pay higher premiums and lower-risk consumers will pay lower premiums.

However - and this is important to remember - it is only one underwriting factor among many others in understanding the consumer's risk profile.

We hope that the Working Group members find the Baron study of interest, and we would be more than happy to elaborate on any of the points raised in this submission.

Canadian Life
and Health Insurance
Association Inc.

Association canadienne
des compagnies d'assurances
de personnes inc.

August 19, 2011

CCIR Secretariat
5160 Yonge Street, Box 85
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DELIVERED VIA E-MAIL: ccir-ccrra@fsco.gov.on.ca

Dear Sir / Madam:

CCIR Issues Paper on the 'Use of Credit Scores by Insurers'

I am writing at this time to provide the life and health insurance industry's comments on the CCIR Issues Paper on 'Use of Credit Scores by Insurers' and, in particular, to describe briefly the use of credit scores in our industry.

As you are aware, CLHIA represents companies which together account for 99 per cent of Canada's life and health insurance business. The industry, which provides employment to almost 135,000 Canadians and has investments in Canada of $514 billion, protects more than 26 million Canadians through products such as life insurance, annuities, RRSPs, disability insurance and supplementary health plans. It pays benefits of almost $65 billion a year to Canadians and administers over one-half of Canada's pension plans.

While the focus of the Issues Paper appears to be completely on automobile and other property insurance, we thought it would be useful to provide you with some information on the use of credit scores in the life and health insurance industry, for the purpose of ensuring that your fact gathering is as complete as possible. To begin, we would note that life and health insurers use "credit scores" as part of the industry's risk classification

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process, particularly in the context of financial underwriting. From our perspective, we see a “credit score" as a point on a numerical scale which represents one factor in determining the risk that a particular individual or organization will be able to pay for their insurance coverage in the future.

Financial underwriting is an integral part of the underwriting of some life insurance and / or accident and sickness insurance products. It includes the assessment by an insurance company as to whether the prospective policyholder will be able to pay, in the future, for the insurance that is being applied for at present. (Other components of financial underwriting include, for example, confirming the need for insurance and verifying the appropriateness of the amount of insurance coverage sought.) Financial underwriting is part of the overall assessment of an insurance risk and will indicate the financial strain, if any, and the possible consequences of such strain, on a prospective policyholder.

Credit scores may be taken into consideration as part of the financial underwriting of some insurance products (e.g., primarily for large life, disability or critical illness insurance policies), with the informed consent of the prospective policyholder. A key consideration in determining whether or not to use a credit score during financial underwriting is the amount of the insurance coverage that is being sought and, correspondingly, the amount of the premiums that would have to be paid by the prospective policyholder to keep the insurance protection in place. The question in these circumstances is whether the prospective policyholder has the financial ability to pay the premiums.

In this context, and with the informed consent of the prospective policyholder, the insurer seeks to obtain financial information about the prospective policyholder, which can be an individual or an entity such as a corporation. This is done by obtaining an inspection report and / or a credit report. In general, an inspection report is completed by a third party to which the insurer outsources the collection of information to confirm and elaborate on the information previously submitted on the insurance application by the prospective policyholder. For example, the information in an inspection report may relate to such matters as a person’s avocations, finances, occupation, and health history. A

credit report contains various pieces of credit information, including a credit score. It is important to note that a credit score is only one factor in financial risk assessment and can be either a positive or a negative factor.

To reiterate, when a credit report is obtained to complete the financial underwriting for the prospective sale of certain products, a credit score is one of the pieces of data obtained as part of that report and may be used by the insurer when assessing the financial risk. As noted above, these reports are obtained in underwriting applications primarily for large life, disability or critical illness insurance policies.

Indeed, it is interesting to note that our industry's understanding and use of credit scores appears to be very much consistent with what the Issues Paper refers to (in the last paragraph at page 5) as "traditional (financial) credit scores" which "… are used to predict the likelihood that a consumer will default on a loan".

* * * * *

The life and health insurance industry would be pleased to discuss its use of credit scores in more detail, as needed. In the meantime, should you have any questions or require any additional information, please feel free to contact me by e-mail at fzinatelli@clhia.ca or by telephone at 416-359-2044 at your convenience.

Yours very truly,

"Frank Zinatelli"

Frank Zinatelli
Vice President and General Counsel

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Via Courier and E-Mail

August 14, 2011

Canadian Council of Insurance Regulators
5160 Yonge Street, P.O. Box 85
Toronto, Ontario
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Attention: CCIR Secretariat (email: ccir-ccrra@fsco.gov.on.ca)

Dear Sirs:

RE: CCIR Issues Paper on Use of Credit Scores by Insurers (the "Paper")

I am the Vice-President, Legal Counsel and Chief Privacy Officer of Equifax Canada Inc. ("Equifax"), the largest credit reporting agency in Canada.

My responsibilities include legal services, global sourcing, all security and compliance, government and legislative relations, corporate governance and privacy functions. As well, I act in many corporate capabilities, including Equifax Corporate Secretary, and am a member of our Canadian senior leadership team.

Equifax, would like to sincerely thank CCIR for the opportunity to present our views on the following two topics outlined in the Paper:

(1) Whether all potential risks have been identified; and

(2) Whether the potential risks identified are already addressed under law, and if so, how.

1. Whether all potential risks have been identified

Equifax believes CCIR has adequately covered the potential risks associated with the use of credit scores in the industry. But, we would like to add the following observations and some salient facts and information in our submission.

a. Use of Equifax Credit Scoring Services

Typically, the credit information provided to the insurance organizations by Equifax is actually a credit score developed by Equifax.

The use of a scoring model based upon the information in a credit file to assess risk associated with, for example, the underwriting of insurance, is a generally widespread practice throughout North America.

For a number of years, Equifax has been offering products in both Canada and the United States to assist insurance underwriters in assessing various risks associated with insurance.

b. Custom Scores

A product, like Canadian Property Loss Scores (aka "CPLS") provided by Equifax to the insurance organizations, is an Equifax Scoring Service, which represents a number of predictive models that are proprietary to Equifax and its partners. These predictive models involve the use of proprietary algorithms based on Equifax's consumer credit files. The scoring service, CPLS has been developed specifically for the homeowner's insurance marketplace. These are called Custom Scores.

c. Generic Scores

Credit files are compilations that represent the past behaviour of consumers with respect to, among other things, applications for credit and payment histories. The predictive

models result in the development of a "number" or "score" associated with an individual's past credit behaviour as represented by their credit file. These are referred to as Generic Scores.

The credit information provided by the Equifax Scoring Services are not an individual's actual credit file, but rather are a series of calculations based upon an analysis of behavioural characteristics associated with an individual's past credit behaviour. The "score" is driven from the individual's credit file, but is independent of the file, and essentially automates a process that could otherwise be accomplished by the insurance underwriter.

d. Correlation Between Consumer Behavior and Risk - a Statistical Analysis

Equifax has determined through testing and research that there is a correlation between consumer behavior and the risks associated with insurance underwriting.

These scoring services are provided to Equifax clients under contractual terms and conditions that limit the use of Equifax Scoring Services. The use of these scores is optional for the insurance industry. Some underwriters and agents have determined that the use of these scores enhances their risk assessment processes. Under the contractual arrangements with Equifax, subscribers to the Equifax Scoring Services may not use the scores provided by the service as the sole determinant of risk associated with a particular applicant. Equifax stipulates in its contractual arrangements that:

> *"client agrees that Equifax Scores shall not be the sole basis for any decision it makes affecting a specific consumer and acknowledges that prudent credit-granting decisions must be based on factors beyond the Equifax Scores."*

It is clear, therefore, that any underwriter may chose to use, or not to use Equifax Scores in their determination of risk, provided that the use of the Equifax Scores is not the sole determinant of whether the underwriter decides to provide or refuse to provide, for example, homeowner's insurance, or how they may price their insurance offerings.

The chart below shows that credit file attributes are an important predictor of higher expected loss insurance rates. For instance, for the bottom 10% of applicants as ranked by the score, the loss rate is approximately 150%. For the next 10%, the loss rate is approximately 120%. The graph also shows that 50% of applicants, as ranked by the credit file attributes, will generate a loss rate of 100% (above 1.00 on the vertical axis) or that it will be a breakeven proposition for the underwriter. This data has been proven to be statistically significant.



The following table shows the relationship between past credit performance (summarized in the credit score) and the number of claims submitted.

It demonstrates there is a significant lift from having credit information as one of the

indicators of an insurance applicant's likelihood of submitting a claim as compared to a random assessment without the use of a credit score.

	Bureau Score Decile				
	10%	20%	30%	40%	50%
% Claims Submitted	11%	23%	34%	45%	55%
Lift vs. no score	*13%*	*13%*	*13%*	*12%*	*9%*

e. Assessment of Risk & Potential Negative Impact to Canadian Consumers

The ability to assess risk is a critical requirement for the provision of insurance. While each underwriter develops their own methods and procedures for determining risk, the decisions resulting from these procedures have a significant bearing regarding the provision and pricing of insurance products and services, and also help to influence the ongoing success of organizations providing insurance products.

Without the ability to assess risk, insurance underwriters would not be able to determine whether a client represents a potential for a profitable business relationship. Several results would potentially occur in the marketplace. There would be little differentiation of products and services, as risks would not be a determinant in the provision of products, and therefore a "one size fits all" approach would likely ensue.

Further, since risk would not be assessed, all customers requiring coverage would be lumped into the same category, resulting in higher costs to the insurance underwriters, and the likely pricing of insurance products significantly above current levels, thereby negatively impacting all Canadian consumers.

Insurance organizations should be free to develop their risk models based upon information that has value in determining the risk of a business relationship, provided that information is in accordance with laws and regulations, including consumer reporting and privacy laws.

2. Whether the potential risks identified are already addressed under law

Equifax believes most potential risks are already covered sufficiently under consumer reporting and privacy legislation. CCIR has addressed this in the Paper. But, Equifax would like to add the following information.

a. Consent for Collection, Use or Disclosure of Personal Information

We submit federal and provincial privacy acts in the country adequately deal with the consent for collection, use or disclosure of personal information. For example, British Columbia's PIPA provides guidance for obtaining consent from individuals for the collection, use or disclosure of their personal information. PIPA states:

> ***6*** *(1) An organization must not*
>
> *(a) collect personal information about an individual,*
>
> *(b) use personal information about an individual, or*
>
> *(c) disclose personal information about an individual.*
>
> *(2) Subsection (1) does not apply if*
>
> *(a) the individual gives consent to the collection, use or disclosure,*
>
> *(b) this Act authorizes the collection, use or disclosure without the consent of the individual, or*
>
> *(c) this Act deems the collection, use or disclosure to be consented to by the individual.*

b. Consumer Reporting Laws and Insurance

According to consumer credit reporting legislation across the country, the use of credit information in the insurance industry is also adequately addressed. For example, the Ontario *Consumer Reporting Act* states under Section 8:

To whom reports may be given

8.(1) No consumer reporting agency and no officer or employee thereof shall knowingly furnish any information from the files of the consumer reporting agency except,

(a) in response to the order of a court having jurisdiction to issue such an order;

(b) in accordance with the written instructions of the consumer to whom the information relates;

(c) in response to an order or direction made under this Act; or

(d) in a consumer report given to a person who it has reason to believe,

(i) intends to use the information in connection with the extension of credit to or the purchase or collection of a debt of the consumer to whom the information pertains,

(ii) intends to use the information in connection with the entering into or renewal of a tenancy agreement,

(iii) intends to use the information for employment purposes,

(iv) intends to use the information in connection with the underwriting of insurance involving the consumer,

(v) intends to use the information to determine the consumer's eligibility for any matter under a statute or regulation where the information is relevant to the requirement prescribed by law,

(vi) otherwise has a direct business need for the information in connection with a business or credit transaction involving the consumer, or

(vii) intends to use the information for the purpose of up-dating the information in a consumer report previously given to the person for one of the reasons referred to in subclauses (i) to (vi). R.S.O. 1990, c. C.33, s. 8 (1); 1997, c. 24, s. 210.

Section 8(1)(iv) of the Act specifically references the interaction between our credit information services and the insurance underwriting industry.

c. Appropriate Steps to Assess Risk under Applicable Law

For example, as the underwriting of homeowner's insurance involves a number of risks, it is reasonable to assume that an insurance organization should take the appropriate steps, in accordance with the provisions of applicable laws, to properly assess those risks in order to determine the appropriateness (including pricing) of entering into an agreement with an applicant.

Equifax has demonstrated in the charts and tables at section 1(c) above, that the use of credit information plays an important function in the assessment of those risks, and therefore the collection of this information, we believe is reasonable and practical by insurers.

Given that organizations typically provide sufficient written notice of the intent to collect credit information on their insurance applications, and that the collection and use of credit information are reasonable in order to assess risk, it is therefore appropriate under privacy laws for the collection of credit information, with consent, for the purpose of obtaining, for example, homeowner's insurance.

d. Consumer's Unlimited, Free Access to Credit Files under the Law

In Canada, Equifax provides the ability for individuals to have unlimited access to their credit information at no cost, and to make corrections, if necessary.

This capability allows an individual to ensure that their credit information is as accurate as possible, and complies with the requirements of privacy and consumer reporting legislation for access and correction of personal information.

Conclusion

Equifax submits CCIR has demonstrated in the Paper the reasonableness of the collection of credit information for the purpose of evaluating risk associated with the provision and pricing of insurance, and that this practice is reasonable under the guidance of privacy and consumer reporting legislation across the country.

Yours truly,



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August 10, 2011

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(Via Email – CCIR Secretariat, ccir-ccrra@fsco.gov.on.ca)

RE: CCIR Credit Scoring Working Group – "Use of Credit Scores by Insurers" Issues Paper

Dear Superintendent Boulet,

Fair Isaac Corporation (FICO™) is a leading provider of analytics and decision management technology internationally. The company offers a wide range of market leading products and services including the FICO® credit risk score that was introduced in 1989. FICO scores are the most widely used credit bureau risk scores, powering over 10 billion decisions a year.

In addition, FICO introduced credit-based insurance scores (CBIS) to the insurance industry in 1993. While we are the leading provider of CBIS scores through our credit reporting agency data and delivery partners – Equifax, Experian and TransUnion – in the United States, there are a number of insurers using our Canadian Property Loss Scores™ via Equifax Canada, as well.

Given FICO's extensive experience and significant interest in this subject, we are offering the following comments to assist the CCIR in its understanding of the purpose, use and value of credit-based insurance scores. There is overwhelming evidence that CBIS is a valuable risk management tool, which provides significant benefits to both insurance companies and consumers. Please note that much of our comments below reference developments in the United States and where appropriate we cite to applicable U.S. law and related U.S. government entities as well as independent studies. Our comments do not address the applicability of Canadian law to the current use or practices associated with credit-based insurance scores.

Overview of CBIS Models

Credit-based insurance score models are built for the sole purpose of predicting insurance losses. The FICO CBIS models are complex mathematical algorithms that are built through an analysis of millions of insurance loss results from past empirical data, using hundreds of credit characteristics as inputs to the model, and looking for statistical correlations between the two. The analysis finds patterns among the factors that have a significant correlation to insurance losses and builds those patterns into rules. The models are multivariate: each factor works in combination with all other factors in the models. There are no assumptions built into FICO CBIS models other than mathematical assumptions. There are no policy decisions, no judgments, and no attempts to anticipate or direct the results of the models.

It is important to note the difference between a credit-based insurance score (CBIS) and a credit risk score. A CBIS score predicts likely future insurance loss ratio relativities, while a credit risk score predicts the likelihood of future serious delinquencies or defaults on credit obligations. At FICO, our analytic and model development techniques are similar for both sets of models but the models are developed to

predict completely different outcomes. While some credit variables have proven to predict each outcome to some degree, the significance (or predictive value) of these variables to the respective outcomes can vary greatly.

In the U.S., state insurance regulation prohibits the use of credit risk scores in insurance underwriting. A CBIS score, not a credit risk score, is designed to be used by insurers. We believe it is important that Canadian regulators promulgate rules that ensure that only the appropriate tools are permitted to be used for insurance underwriting and pricing.

Research Supports a Correlation between Credit Behavior and Insurance Risk

In the United States, there is an impressive body of research that supports the use of CBIS as effective predictors of insurance risk in the property and casualty market.

In its July 2007 report, "Credit-Based Insurance Scores: Impacts on Consumers of Automobile Insurance," the U.S. Federal Trade Commission stated: "Credit-based insurance scores are effective predictors of risk under automobile policies. They are predictive of the number of claims consumers file and the total cost of those claims. The use of scores is therefore likely to make the price of insurance better match the risk of loss posed by the consumer."

Separate studies by the Texas Department of Insurance (TDI), the University of Texas, Tillinghast Towers-Perrin, EPIC Consultants, and others have also shown that credit history correlates with the risk of insurance loss. The TDI study included the following key findings:

- The average loss per vehicle for people with the worst credit-based insurance scores is double that of people with the best credit-based insurance scores.
- Homeowners insurance loss ratios (claims paid/premium paid) for people with the worst credit-based insurance scores are triple that of people with the best scores.
- Drivers with the best credit history are involved in about 40 percent fewer accidents than those with the worst credit history.

(Source: Insurance Information Institute, January 2005)

Consumer Benefits Derived from CBIS

There are a number of key consumer benefits derived from the use of CBIS. These include:

Lower Premiums. The U.S. Federal Trade Commission noted in its July 2007 report, "Credit-Based Insurance Scores: Impacts on Consumers of Automobile Insurance" that "if credit-based insurance scores are used, more consumers (59%) would be predicted to have a decrease in their premiums than an increase." According to insurers, up to 75 percent of their policyholders pay lower premiums because of the insurer's use of credit-based insurance scoring within their underwriting process. Insurers use CBIS to significantly reduce the "risk premium" they need to charge when they lack effective risk segmentation data. As "risk premium" is reduced through CBIS, the majority of consumers see lower premiums.

Better Availability. The use of scoring enables insurers to make more accurate, objective, consistent and timely underwriting and pricing decisions. As a result of this improved accuracy, insurers have more confidence in their assessments of the insurance risk presented by their applicants, which allows them to underwrite more policies.

Competition in the marketplace is good for consumers. The use of insurance scores keeps the insurance marketplace competitive, resulting in the availability of lower prices, better service, and more choices for consumers. Underwriters gain opportunities to identify and write insurance for people who in the past may have been declined because of incomplete information. Also, a good credit history can offset negative underwriting factors such as a prior loss, thereby enabling someone to get insurance who might otherwise have been denied or charged more.

Accuracy of Credit Data

The data at credit reporting agencies is one of the most accurate set of consumer data available to insurers. A 2011 study conducted by the Policy Economic and Research Council found that less than one percent of U.S. consumer credit reports contain errors that lead to a significant change in the score. In discussing the accuracy of the data contained in credit reports, the authors note:

> Of the 81,238 credit, collections, and public record tradelines examined, 435, or less than 1 percent (0.54 percent), contained information that was disputed. It should be mentioned that 19.2 percent of the credit reports examined by consumers were set aside as containing one or more pieces of header or tradeline data that a consumer believed could be inaccurate. Of note, 37% of these potential disputes only related to header, or "above the line," information that could have no bearing on a credit score (e.g., the spelling of a former street address or maiden name). (p. 8)

In addition, other studies have revealed that the error rate in credit reports is considerably lower than the error rate found in U.S. motor vehicle records, as found by the Insurance Research Council.

Models Are Not Discriminatory

CBIS models are built with depersonalized data, and do not include demographic factors such as race, religion, ethnicity, age, sex, marital status, etc. There are no social judgments, assumptions (except mathematical) or biases that can influence the CBIS models. Thus, credit-based insurance scores help overcome the concern that insurance underwriting can be discriminatory.

Proxy. Some critics of credit-based insurance scores say that the scores, which are built with depersonalized credit data, are unfairly discriminatory because they are a proxy for other factors that are illegal to use for underwriting or rating purposes.

By definition, a factor is a proxy for a second factor if the first factor is used as a substitute for the second factor with the intent to circumvent a prohibition against the use of the second factor and achieve the result that would be expected if the second factor had been used directly. The use of a "proxy" is illegal because it is a method of overt discrimination. FICO CBIS scores are not a proxy for race, ethnicity, income, disability, unemployment, marital status, or any other prohibited insurance rating factor, as there is no correlation between any one of these factors and a person's credit-based insurance score. There may be more of a correlation between a driver's prior accidents (as an underwriting or pricing factor) and the driver's age or race, since young drivers living in urban areas have more accidents than the general population; nobody has argued that the use of prior accidents is a proxy for racial discrimination.

Double-counting. Critics have suggested that even if credit-based insurance scores are not used as a proxy for illegal underwriting or rating factors, the scores have the effect of "double-counting" certain characteristics. For example, a credit-based insurance score may predict a policyholder's capacity

for fiscal self-discipline and management of resources, which could be correlated to age or location that are already incorporated into an insurer's underwriting and pricing models. There is ample evidence that credit-based insurance scores provide further predictive lift; otherwise, insurance companies would not use the scores.

Credit Factors That Impact CBIS Models

With respect to FICO CBIS models, the general category factors that contribute the most to credit-based insurance scores are as follows:

- 40% of a consumer's final FICO CBIS score will have been influenced by information from a variety of credit variables that reflect "payment history" to include the number, severity and recency of any delinquencies;
- 30% of a final score will have focused on multiple variables that reflect "outstanding debt" or overall "limits-to-balances" considerations;
- 15% of a final score will have considered the predictive value of factors that reflect "length of credit management history" for all credit accounts as well as the average lengths of those credit accounts;
- 10% of a final score will reflect factors that focus on whether a consumer has sought or obtained new credit obligations in the past year; with adjustments in place for multiple mortgage and auto loan inquiries; and
- 5% of a final score will reflect the predictive value of "credit mix" (e.g., revolving credit vs. installment credit accounts) to future insurance loss ratio relativities.

Promoting Consumer Education

Consumer education is an important element to ensuring understanding of and confidence in CBIS.

To aid in consumer education and understanding of CBIS, it is important to note that each CBIS score based on credit reporting agency data is accompanied by up to four (4) score reasons to help consumers who receive an adverse action notice identify where they may have lost points, providing insight into how credit behaviors are impacting scores, underwriting decisions and pricing. Consumers who believe these score reasons misrepresent their credit history can obtain their credit reports from the applicable credit reporting agency and request an investigation of any information that they find to be inaccurate or incomplete.

In addition, FICO maintains a consumer education website at www.insurancescore.fico.com that provides information, such as "Answers to Your Questions about FICO Credit-Based Insurance Scores" and "FICO Credit-Based Insurance Scores – Fact Sheet", which help instruct insurers, brokers, regulators, legislators, and consumers about the FICO scoring tools:

- How consumers benefit from insurers' use of FICO CBIS models
- How consumer credit information is used as one of many predictive tools by insurers
- What's in a consumer's credit report
- Information that is NOT considered in FICO CBIS models
- Facts and fallacies about credit-based insurance scoring
- FICO credit-based insurance score and FICO credit risk score differences

- Credit practices a consumer might follow to improve a score over time

This educational site has proven to be an effective way to communicate key consumer information on a range of CBIS topics.

Conclusion

FICO has a strong interest in ensuring that credit-based insurance scoring models are fully understood. FICO CBIS models are empirically derived, demonstrably, and statistically sound mathematical algorithms, built with depersonalized, legally acceptable data. The models are not a proxy for any kind of unfair discrimination. They are predictive and extremely valuable as a risk management tool for insurance companies. Without CBIS models, the selection process for the pool of applicants would be less sophisticated, and a great majority of applicants—most of whom are good insurance risks—would pay higher premiums. FICO believes it would be a mistake to restrict the industry's use of CBIS models, which have proven to be a valuable risk management tool, and, by more accurately predicting risk, a mechanism to deliver fairer results for consumers. Moreover, CBIS models are specifically designed to predict likely future insurance loss ratio relativities. The use of credit risk scores that are developed to predict serious delinquencies on credit obligations should not be used for other unintended purposes such as insurance underwriting and pricing.

Thank you for allowing us to present this information for your consideration. I look forward to responding to any questions from the CCIR and/or the opportunity to meet with the CCIR to expand on our thoughts.

Sincerely,



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Use of Credit Scores by Insurers

Submission to the Credit Scoring Working Group, August 2011

The Issues

The issues, as identified by the CCIR discussion paper are:

Have all the risks of insurance-based credit scoring been identified?

1. Inadequate consent
2. Unreliable credit data
3. Availability and affordability of insurance
4. Insufficient disclosure
5. Undue impact on certain groups
6. Privacy breaches
7. Lack of understanding

Guiding the discussion of identified risks are the principles of:

a) Fair treatment of consumers
b) Disclosure of information to enable consumers to make informed choices
c) Compliance with the law
d) Good corporate governance

Are the identified potential risks adequately addressed under law, and if so, how?

Overview

WHY CREDIT SCORES ARE OBTAINED

The reasons insurers and other providers of goods and services obtain credit data are typically:

1. **Assessing credit worthiness**: This is a common and widely understood reason for obtaining credit information; indeed, hotels and car rental outlets routinely obtain a credit-card imprint at initial point of sale to qualify the customer's ability to pay the bill. However, since the premium is earned over the term of the insurance policy, insurers need not get financially extended: they can cancel the policy for non-payment. When a premium payment plan is offered, the provider of that financing may require credit information.

2. **Risk assessment**: It is becoming more common for landlords and employers to do credit checks on potential tenants and employees. As one reference-verification provider states on its website: "Desperate people may do desperate things. If a prospective candidate is in poor financial condition or has exhibited a lack of financial accountability in the past, they may not be the most suitable individual for handling your company's assets." Similarly, insureds whose credit scores indicate financial difficulty may be statistically more likely to view a fraudulent claim as a means of quickly liquidating his or her assets. For at least one insurer, a claim triggers a credit check at the next policy renewal. Presumably, a change for the worse in the insured's credit score, combined with the recent claims history, could put this insured at risk of a higher premium or a declination.

   Loss-reduction strategies will always be a part of an insurer's best practices. But is credit-based insurance scoring (CBIS), as currently practiced, the appropriate tool? Insurers say that more than half of all habitational claims today are for water damage; how many of these are intentional losses to obtain a new floor or cash equivalent? Is the current CBIS model a blunt instrument that should be refined so that innocent, honest customers who are experiencing temporary financial challenges don't get hammered by it?

   What are an insured's rights and recourse if he is declined or penalized with a premium increase based on a downturn in his credit worthiness? Brokers have reported advocating for the insured with the insurer in such instances; if the insured had just accepted the situation, the insurer may not have disclosed the reason for it. Currently the only definition of what is fair and acceptable practice by insurers is the IBC Voluntary Code of Conduct, but there is no accountability or transparency as to whether any insurer that obtains credit information actually follows the Code. What is actually meant when an insured provides consent for credit information to be used "for the purposes of … underwriting my policies"? We submit that of the three common reasons for using credit information shown herein, risk assessment is the only one that fits the definition of "underwriting purposes".

3. **Identifying the desirable market strata**: Although credit reporting agencies purport to not collect information on income and marital status, this may be specious. Some of the data collected – credit limits, number of charge cards – are indicative of the income level of the household, and this, along with other information brokers collect as to value of home and other assets, can provide clues to the overall net worth of the client and his or her likelihood of having more assets to insure in the future. Even though market-conduct regulations are intended to maintain a clear delineation between the banking and insurance pillars, the fact is that there are plenty of instances in which banks and credit unions and their subsidiary insurers and brokerages are cross-soliciting A-list clients. This is an additional bonus of CBIS, to which consumers often don't realize they have agreed since it's not overtly stated in consent forms, but is rolled into the blanket term "for the purposes of communicating with me". We submit that this is the main reason for using CBIS; however, it's not overtly disclosed.

Insurers argue that if other corporate entities can do credit checks (and reap the marketing benefits), they should be able to as well. After all, they are entering into a contract to indemnify the client against the loss of a major asset. Be that as it may, in this paper, we will argue that there are many grey areas in current laws that have the potential to cause hardship to consumers, and as such consumers are not adequately protected.

HOW CBIS IS HANDLED IN THE BROKERAGE

For this submission, a small, random poll of brokerages around B.C. was conducted. Among the findings:

Who's using CBIS and where: Brokers, especially those in urban centres, are aware that the larger, national insurers they represent use CBIS. In some cases the insurer has officially disclosed its practice only recently, even though there was unspoken awareness of it for some period prior.

For the most part, smaller, regional carriers do not seem to use CBIS, and their brokers do not deal with credit scoring at all in their offices. Similarly, "program brokers" who issue their own policies do not deal with credit scoring. These program policies are in some instances be underwritten by the same large, national insurers that practice CBIS. At least one insurer that has been among the most open about its CBIS practices for its brand-name lines sold in owner-operated brokerages underwrites the in-house line of at least one major, multi-location brokerage in B.C., without CBIS. Since the use of CBIS is seen as proprietary, it's not known to what degree the aggregate experience of an insurer's CBIS sales are determining its non-CBIS pricing and acceptance of business.

How CBIS is being disclosed at point of sale: In some cases insurers have provided their brokers with instructions and guidelines (including a pamphlet for the customer) on how a credit score will be obtained and used, and in some cases they have not. In some cases the credit score will be obtained from the person initiating the insurance transaction for the household; in some cases it will be obtained from the oldest person in the household or from the person with the best credit score. The manner in which consent is obtained varies from use of the insurer's proprietary consent form, use of the standard consent clause in the CSIO application (with the broker pointing it out and explaining it, or not) or verbal disclosure. As will be noted later in this submission, broker management systems do not facilitate retention of a hard copy of the consent for client files.

The CSIO consent clause has changed over the years (please see Appendix), and older versions appear to be still in wide use. A few prudent brokers have perceived a void here and have devised their own CBIS consent form, and have expressed that some regulations or standards of practice would be welcome. None of the brokers polled advise their customers of a time period that the consent will be in effect. And none of the brokers polled advise their customers that they can refuse or withdraw consent for obtaining a credit score at any time, and how to do so. While we did not poll brokers on this question specifically, we feel that many brokers (and insurers) would not be aware that a separate consent would be required for a new credit score to be obtained for a purpose different from an earlier one.

How CBIS is affecting premiums: One broker reports: "Some companies do not use [CBIS] to deny insurance or charge a higher premium; depending on clients' credit score, some nebulous discount is applied, which is never known upfront and only appears once the credit score is determined. That is why sometimes we will go to a second insured at the same address to see if they come up with a better credit score. This has also resulted in our no longer being able to quote from manuals."

Many customers would welcome being told that their good credit management entitles them to a discount on their insurance. However, if the credit information is being obtained to identify the customer's likelihood of undertaking a fraudulent intentional act for an insurance pay-out, one should be able to assume that a reasonable credit score would be adequate for that purpose, and there should be no need to do checks on other household members to obtain the best premium. If the intent is to identify the A-list consumers in the household for further solicitation, they should be informed of that so that they can opt out if they wish.

Another broker reports: "We see renewals for loss-free policies that have dramatic premium increases in the order of 70 to 100% from at least one underwriter that uses scoring. The increases may not be as large from other insurers using scoring, but the increases are there; how do we know what led to the increase on the policy on which CBIS was applied? It could be due to rating by peril or it could be due to a credit score. The facts are buried in their rating tool and that lack of transparency makes it difficult, if not impossible, to prove violation of the law regarding adverse effects."

Discussion of the Risks

INADEQUATE CONSENT AND INSUFFICIENT DISCLOSURE

Not only do consumers sometimes not realize they have given consent, in some instances, they may not have given consent for the actual use of the credit information, or they may not have given consent at all.

Insurers initiate the request for credit information for their credit reporting agencies; however, in B.C., where about 90% of all insurance transactions are intermediated, the consent for the collection of personal information is obtained by the broker. This consent covers the actions of other parties in the supply chain: the insurer, the third-party credit reporting agency and, where applicable, the financial institution that owns the brokerage.

There is a lack of consistency in how insurers involve their brokers in the collection of consent for credit-scoring purposes:

- Not all insurers disclose their CBIS practices to brokers, so potentially insufficient or no consent is obtained.
- Not all insurers provide their brokers with instructions, guidelines or tools for the collection of CBIS consent.
- Practices vary: verbal disclosure, use of the standard consent clause on CSIO applications, use of insurer or broker proprietary clauses. The CSIO consent statement was revised in 2008, but the 2003 version is still in use in many brokerages (updates are done by providers of broker management systems like Compu-Quote or The Agency Manager).
- Increasingly transactions are effected by telephone, email or a combination thereof. Brokers try to have the client come in to sign the application in person, but some clients are resistant.

There is a lack of disclosure as to the intent of the credit check. In a recent decision [2011 BCIPC No. 16], the Privacy Commissioner for B.C. determined that the use of credit scoring for the purposes of risk assessment is distinct from its use for the purposes of assessing credit worthiness.

There is no standardization as to which household member's credit information is accessed: the first name on the application, the highest or lowest credit score in the household, or the oldest individual named on the application. There is also no standardization as to when a credit check is repeated. We refer to your August 2009 survey for more detail here.

Disclosures may be verbal [*Financial Institutions Act,* Marketing of Financial Products Regulation, 573/2004, Sec. 4; *Personal Information Protection Act,* Sec. 8], but they must still be made, and many brokers maintain an office standard of keeping written proof of disclosure on file. The propensity for some insurers to be less than forthcoming about their CBIS practices, and the trend to paperless transactions are making it difficult for brokers to retain written copy of consents. As one broker points out: "If we want company quotes based on their scoring model, the broker management system (BMS) shows the consent on the computer screen, but does not allow the consent to be printed or copied and saved. If we wish to print it, we must save a screen shot and print that. If insurers are serious about being transparent in their dealings, why do they prohibit printing of the consents? They may argue it is a BMS matter, but that doesn't wash since the BMS providers get rate downloads and instructions from the insurance companies."

UNRELIABLE CREDIT DATA

As has been pointed out in the CCIR discussion paper and other reports, Canadians' financial literacy is low [see *www.financialliteracyincanada.com*]. A credit score can be affected by a temporary loss of employment, change in marital status and even a lack of use of credit. It is likely that very few Canadians would make the connection between an overdue charge-card account and the insurability of their home. For the purposes of this submission one volunteer made several attempts to directly access his credit information from a credit reporting agency, and was unable to.

AVAILABILITY AND AFFORDABILITY OF INSURANCE

The CCIR discussion paper alludes to the public obligations of insurance. We surmise that this refers to the insurance market's obligation to provide indemnification to the point where government is willing to step in with compensation from public coffers. Our concern is that CBIS without proper regulation could create a gap in which some consumers are left with no markets available to them. CBIS is another way of crunching the numbers to identify the attractive, profitable customers. Presumably, the early adopters will get to those customers first and will profit the most. When all insurers are using CBIS, it will no longer provide a competitive advantage, and it will segment the least desirable customers and potentially leave them unable to obtain affordable insurance. Regulators may have to step in with a solution along the lines of a facility association that forces all insurers to take their fair share of these customers. And we'll be back where we started before CBIS entered the marketplace.

PRIVACY BREACHES

On this point we refer you to 2011 BCIPC No. 16 [*www.oipc.bc.ca/PIPAOrders/2011/OrderP11-02.pdf*], which considered whether the collection of a credit score by an insurer for the purpose of assessing risk complied with the *Personal Information Protection Act* (PIPA).

The adjudicator acknowledged that the *Business Practices and Consumer Protection Act* (BPCPA) allows insurers to collect credit scoring information for underwriting purposes. However, consent must still be obtained as with any other personal information: "The effect of the BPCPA is not to dispense with the need for informed consent, but to underscore its importance."

The adjudicator noted that the complaint would be assessed according to sections 6, 7, 8, 10 and 11 of PIPA.

Section 11 requires any collection of personal information be only for the purposes that a reasonable person would consider appropriate in the circumstances, and she found that: "It is reasonable and appropriate to collect this personal information for the purpose of underwriting homeowner's insurance as occurred here." [Para. 76 of the decision].

Section 7 limits the circumstances under which an organization can require an individual to consent to collection of information: it must be integral to the provision of the product or services in that it plays a significant role in enabling the organization to achieve the purpose for which the information is collected.

She agreed that collecting the CPLS is necessary for assessing the future risk of loss in underwriting homeowner's insurance policies in circumstances where a claim has been made. [Para. 80.]

Section 8 specifies circumstances in which individuals will have been deemed to have given consent. She found that none of these circumstances applied [89].

"…There is a great deal of consumer misconception and lack of awareness about the use of credit scoring for the purposes of risk assessment in the personal insurance industry. The

use of credit scores for this purpose is distinct from their use for the purposes of assessing credit worthiness."

Finally, she concluded, "I find that the notice on the CSIO homeowner's insurance application the complainant and his spouse completed in 2003 did not adequately inform them that their credit information (specifically, a credit score) would be collected for the purpose of underwriting or assessing future risk of loss."

She specified that the insurer must review the consents it has obtained from home insurance policyholders since PIPA came into effect on Jan. 1, 2004, and then submit the notice it intends to provide to policyholders who have not been provided with adequate notice.

LACK OF UNDERSTANDING

With a lack of understanding within the insurance industry itself, a lack of disclosure and lack of information to assist consumers in making informed choices, it's no wonder consumers are also lacking in understanding. This is a recipe for a public backlash and some hints of consumer dissatisfaction have already appears, such as the 2010 episode of CBC Marketplace [*http://www.cbc.ca/marketplace/2010/rate_hike_outrage/main.html*].

Conclusion

To assist CCIR in identifying the risks of credit-based insurance scoring, we have provided some perspective based on brokers' day-to-day experiences with it.

IBABC, along with its sister associations, has long advocated for a prohibition on CBIS. We recognize that "the question of whether or not to ban the use of credit scores goes beyond the scope of CCIR's review." We are of the opinion that the identified potential risks of CBIS are not adequately addressed under law, and Canada's insurance regulators should impose appropriate controls to protect consumers' access to affordable insurance markets.

Consumers are at a disadvantage in Canada because we lack harmonized legislation across the country to protect consumers with respect to the types of information collected and the disclosure obligations on insurers and reporting agencies with respect to adverse decisions and incorrect credit information. IBC's Voluntary Code of Conduct is not sufficient. If, as the CCIR discussion paper points out, B.C. law already requires insurers to notify affected individuals when credit information causes an insurer to deny a benefit or increase cost, then clearly the insurance companies are not complying. The finding that "if there is an adverse decision due to a poor credit score, almost half of insurers that use credit scores as rating criteria do not notify the applicant" is damning evidence and proof enough that regulatory guidelines are required to protect consumers. If scoring is to be allowed, the insurers should be subject to regulatory guidelines similar to those suggested in the NCOIL Model Act.

The CCIR discussion paper states: "… It is up to policy-makers in each jurisdiction to determine – based on their unique political and public policy objectives – their level of tolerance in relation to the risks identified, and whether or not specific restrictions or

prohibitions are required so that the regulatory goals of fair treatment of consumers and compliance with laws can be met." We are disappointed that no broader regulatory market conduct relating to CBIS is being contemplated. We submit that its connection with blanket consents and other market conduct regulations in the *Bank Act* and PIPEDA makes this a national issue.

Such legislation should also incorporate some of the limitation and exemptions applied in some United States – such as those for extraordinary life events: deaths, divorces, catastrophic illnesses, etc. If NCOIL-type legislation were enacted, insurers would be forced to make better disclosure about the risk factors and credit data used to establish premiums.

Recommendations

1. Given that there is an acknowledged lack of understanding by consumers, the acquisition of a credit score should only be done with full, prior, informed consent. An information pamphlet should be provided to consumers by insurers at the point when a decision to obtain credit information is made (we acknowledge that a couple insurers are voluntarily doing this now). Further, insurers should be required to make appropriate disclosure to regulators so that the practice can be monitored. Credit-based insurance scoring should not be an underground activity.

2. The collection of credit information should be done in a manner that increases consumers' financial literacy. If a credit score is a determining factor in insurability or a premium increase, the consumer should know the rules of engagement, what information was used in the rate increase or declination and why, the source of the information, and contact information for follow-up and remediation. He should be allowed to have his application reviewed upon request. If a discount is promised for a good credit score, or a penalty is imposed as a result of a poor one, the consumer should have the opportunity to obtain the discount or remove the penalty with an annual review, rather than waiting two to three years for an accrued benefit. If the credit information is being obtained for future cross-selling and solicitation purposes, the client should be informed, and have the opportunity to opt out.

3. The use of blanket consents should be reviewed by regulators across all lines of financial products and services. Too often vague consent statements made at one point of sale are deemed to cover the activities of affiliated organizations.

4. There should be no differentiation between "soft hits" and "hard hits" – terminology used to describe a credit check that doesn't leave a notation on the customer's credit record versus one that does, the implication being that multiple credit checks for which no credit has been granted can have a detrimental effect on a credit score. However it's done, a credit check is a sharing of important personal information.

5. Harmonized regulatory guidelines similar to those suggested in the NCOIL Model Act should be implemented.

Thank you for the opportunity to provide input to your review.

Appendix

CSIO Habitational Insurance Application form consent statements:

2003: I have provided personal information in this document and otherwise and I may in the future provide further personal information. Some of this personal information may include, but is not limited to, my credit information and claims history. I authorize my broker or insurance company to collect, use and disclose any of this personal information, subject to the law and to my broker's or insurance company's policy regarding personal information for the purposes of communicating with me, processing my application for insurance and underwriting my policies, evaluating claims detecting and preventing fraud and analyzing business results. I confirm that all individuals whose personal information is contained in this document have authorized that I agree to the above on their behalf.

2008: I have provided personal information in this document and otherwise (e.g., by telephone) and I may in the future provide further personal information and/or any policy issued as a consequence of this application. Some of this personal information may include, but is not limited to, my credit information and claims history. I authorize my broker or the insurer to collect, use and disclose any of this personal information, subject to my broker's or the insurer's policy regarding personal information, for the purposes of communicating with me, assessing my application for insurance and underwriting my policies, evaluating claims, detecting and preventing fraud, analyzing my broker or the insurer's business results such as evaluating claims results and setting insurance rates, and when otherwise permitted or required by law. If I apply for a premium payment plan, I also authorize the broker and the insurer to obtain and use my credit report for that purpose. I declare that all individuals whose personal information is contained in this document have authorized me to agree to the above on their behalf. I may obtain a copy of or ask questions about my broker's and the insurer's personal information policies by contacting their respective privacy officers.

IBC BAC | Insurance Bureau of Canada
Bureau d'assurance du Canada

Gregor Robinson
Senior Vice-President, Policy & Chief Economist
Vice-président principal, Établissement des politiques et économiste en chef

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August 15, 2011

Sent by e-mail to ccir-ccra@fsco.gov.on.ca

Danielle Boulet
CCIR Chair
Canadian Council of Insurance Regulators
5160 Yonge Street, P.O. Box 85
Toronto, ON M2N 6L9

Dear Ms. Boulet,

Re: Use of Credit Score by Insurers

On behalf of Insurance Bureau of Canada (IBC), I am pleased to provide you with our submission in response to CCIR's issues paper *Use of Credit Scores by Insurers*. IBC welcomes the opportunity to work with the CCIR on this important public policy matter.

The CCIR paper identifies seven potential consumer risks associated with insurers' use of credit information. IBC's submission outlines how these potential consumer risks are either currently addressed through established practices, or suggests measures that can be taken to appropriately tackle these issues.

If you would like to further discuss any of the contents of this submission, please feel free to contact me.

Sincerely yours,

Gregor Robinson
Senior Vice-President, Policy and Chief Economist

Attachment

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Bureau d'assurance du Canada

IBC Response to CCIR's Issues Paper *Use of Credit Scores by Insurers*

A Submission to the Canadian Council of Insurance Regulators

~ August 2011 ~

Insurance Bureau of Canada (IBC)

This submission has been prepared by Insurance Bureau of Canada (IBC), the trade association representing over 90 percent by premium volume of the private property and casualty (P&C) insurance industry in Canada. The P&C insurance industry is one of the largest sources of employment in Canada, providing over 114,000 jobs. In 2010 our industry invested more than $77 billion in federal, provincial, municipal government and corporate bonds. P&C insurers also paid over $7.2 billion in taxes across Canada based on 2009 data. Our industry also works to improve the quality of life in our communities by promoting injury prevention, safer roads, crime prevention, improved building codes, and coordinated preparation for coping with natural disasters.

I. Introduction and Summary

1. IBC is pleased to provide feedback on CCIR's issues paper *Use of Credit Scores by Insurers.* The paper provides a thorough overview of the issues surrounding insurers' use of credit information for underwriting and/or pricing. It also identifies some reasonable concerns about possible implications of this practice for consumer protection.

2. As the CCIR paper notes, the regulatory consumer protection and privacy requirements relevant to credit information vary considerably across provinces. To address this concern, the industry has developed the Code of Conduct for Insurers Use of Credit Information (Code), which supplements the existing regulatory framework, while providing a uniform level of consumer protection across the country.

3. While the Code is voluntary, companies representing 85% of the personal lines market share of IBC and CADRI members have made a formal commitment to adhere to the Code. Any signatory company that subsequently failed to comply would be exposed to potential disciplinary action from the Financial Consumer Agency of Canada (FCAC) for making a false claim. All provincial or territorial governments also have the ability to assess the degree to which these companies are in compliance with the Code.

4. In addition, some of the questions raised in the CCIR paper deal with issues of consumer understanding of concepts such as credit scoring and underwriting or how to manage their own credit rating. While these issues are important, they are far from unique to insurers' use of credit information. The recent federal Task Force on Financial Literacy called for concerted efforts by many stakeholders - including the insurance and other financial sector industries, financial intermediaries, governments, and educators – to equip Canadians with the knowledge that is essential for effectiveness and success in the conduct of their personal financial affairs.

5. The CCIR raises seven potential consumer risks that may be associated with insurers' use of credit information. This paper outlines how these risks are either currently dealt with through established practices, or suggests measures that can be taken to appropriately tackle these issues.

II. Reasonableness Of Insurers' Use Of Credit Information

6. As the industry association representing P&C insurance companies, IBC neither supports nor opposes insurers' use of credit information. As we have stated in the past, we believe that providing insurers with the flexibility to use appropriate rating and underwriting criteria, including credit information, supported by a robust and competitive insurance marketplace, ultimately leads to more consumer choice.

7. IBC's member companies see support for this position in the recent decision of the British Columbia Information and Privacy Commission, which concluded that the collection of personal credit information for insurance purposes is reasonable. As the Adjudicator in the case stated:

> *"…I find that the purpose for which the CPLS[1] is collected is reasonable. The ability to assess risk accurately is a central concern of the insurance industry generally. Improvements in the accuracy of risk assessment can affect the cost of insurance in ways that benefit some consumers. The evidence establishes that credit scoring generally and the CPLS specifically are statistically valid and useful predictors of future risk of loss. "*

8. The adjudicator's central point needs to be emphasized. The core business and unique expertise of P&C insurers is to accurately assess and price risk. When this is done well in a competitive market, consumers pay the appropriate price to cover the risk that the insurer assumes on their behalf. There is no debate – as the BC adjudicator acknowledges – that the appropriate use of credit information can strengthen the insurer's ability to charge the "right" premium to all customers. While credit information is not and should not be the only tool for assessing risk, insurers who use it have strong evidence that it helps allocate premium fairly; that is, in accordance with risk, across their customer base.

[1] CPLS stands for the Canadian Property Loss Score. The British Columbia Information and Privacy Commission defines CPLS as follows:

"The CPLS is not the same as an individual's credit report or credit history. It is a number that is derived from selected items of information in an individual's credit report using a particular statistical tool. In the literature, this number is also referred to as a 'credit score' or an 'insurance score'."

9. Echoing the findings of the academic literature, we believe that most consumers benefit from insurers' use of credit information insofar as it helps to ensure that consumers pay the best price consistent with their risk. This is not to say that policyholders who combine a weak credit score with other attributes, such as a history of making claims, should not see this reflected in higher premiums. But research shows that people with these characteristics are a small minority. Were they not required to pay higher premiums in recognition of their higher risk, the rest of the insurance-buying public would pay more.

10. IBC understands that concerns about consumer protection can arise with the use of credit scoring to support underwriting activities. As the CCIR paper notes, the concept of voluntary, informed consent can be misunderstood by consumers, or consumers can consider themselves to be without recourse when they experience the consequences of having a low credit score. IBC's code is meant to provide safeguards to protect consumers. Licensed insurance professional also have a role to play in providing consumers with a better understanding of insurance products.

III. Risks To Consumers

11. Recognizing the public policy concerns regarding insurers' use of credit information raised in the CCIR paper, IBC developed a Code of Conduct for Insurers' Use of Credit Information. The Code supplements the current consumer protection framework, while providing a uniform level of protection across the country where insurers choose to use credit information for rating and/or underwriting purposes. The Code is based on the highest standards of consumer protection across Canada and in many respects goes beyond current legislative or regulatory requirements.

12. The CCIR raised seven types of consumer harms or potential risks that may arise as a result of insurers' use of credit information. We believe that, as the next section of this paper describes, most of these risks are effectively addressed by the Code.

5.1. Inadequate Consent

Potential Risk: Consumers may not know that they have given permission to an insurer to use their credit information or a credit score for determining a consumer's eligibility for insurance and the premium to be charged.

13. This risk is addressed by Section 3 in the Code - *Gathering prior consent to collect and use credit information (written or verbal)* – which requires that insurers obtain a customer's informed and *express* consent when collecting their credit information.

14. Section 17 (B), *Personal Information Consent,* of the CSIO habitational insurance application form, which is used by the majority of insurers in Canada requires insurers to obtain customers' informed consent when collecting their credit information. IBC's Code goes further than this language by requiring insurers to obtain express consent from everyone whose credit information may be accessed in underwriting or pricing an insurance policy. IBC is currently working with CSIO to amend the consent language in the habitational application form to require express consent.

15. The CCIR paper raises the issue about whether customers understand the rights and responsibilities they undertake in filling out and signing an application for insurance. The paper cites consumer surveys which found that many customers are not aware that some insurers use credit scoring. While this information is on the application form and explained to consumers by licensed insurance professionals, many do not have the time to properly read all of the information presented to them. This is an issue of financial literacy which is common to the insurance sector and other financial sectors in general.

5.2. Unreliable Credit Data

Potential Risk: The underlying credit data from which the credit-based insurance score is derived may be unreliable.

16. Responding to this concern, Section 2 in IBC's Code - *Ensure Credit Information is Current and Accurate* - stipulates that insurers:

- Must use up-to-date credit information by:
  - Not using credit information that is not current; and
  - At the customer's request, updating any customer credit information.

- After being informed of a correction, supplement or deletion to an individual's credit file – the Code requires insurers to immediately make the necessary adjustments to the customer's file and re-underwrite and re-rate the customer as soon as practical.

17. In addition to these requirements of IBC's Code, PIPEDA and most of the provincial privacy laws contain provisions that enable consumers to review their credit information and engage in effective dispute processes to correct mistakes.

5.3 Availability and Affordability of Insurance

Potential Risk: Insurance may be unavailable or no longer affordable due to credit-based insurance scores.

18. Section 5 of the Code - *Use of Credit as a Sole Variable* – addresses to this concern by requiring insurers not to refuse to quote or base an insured's renewal rates, or deny, cancel or non-renew a policy of personal insurance *solely* on the basis of credit information without consideration of other non-credit underwriting or rating variables.

19. It is already established practice that insurers who use credit information to price or underwrite a policy do so in conjunction with other variables, and do not employ it as a sole factor. Hence, it is unlikely that customers would be unable to find or afford insurance solely because of unfavourable credit scores. As the CCIR points out, not all insurers use credit information, and a competitive marketplace allows customers to shop around and find insurance rates that best suit their individual needs and circumstances.

5.4 Insufficient Disclosure

Potential Risk: Consumers may not have sufficient information about how to modify their behaviour in order to reduce insurance costs.

20. Section 8 b) in the Code - *Taking Adverse Action as a Result of Credit Information* - stipulates that the insurer must disclose to the consumer any adverse action taken only as a result of credit information. The Code explains this to mean that:

- Notification should be provided to the consumer explaining the reason for the adverse action and in accordance with applicable consumer reporting legislation.

21. Insurance companies need to be transparent about their use of credit information for rating and/or underwriting purposes. However, while insurers can and should

communicate to consumers that they are using their credit information, they are typically not able to disclose details pertaining to how credit-based insurance scores are calculated – for, as the CCIR points out, these scores are derived using proprietary mathematical models and, to our knowledge, are calculated for insurers by credit rating agencies.

22. More importantly, we believe that, together with the delivery of adequate consumer information, consumers need to be able to understand the information they are presented with. For example, if consumers understand that a good credit score is a reflection of responsible financial behaviour, and that it impacts many aspects of their lives, not just insurance, they are more likely to take appropriate action to improve their credit scores. This issue again speaks to the need for increased financial literacy of Canadians, which will be discussed further in section 6 of this submission.

5.5 Undue Impact on Certain Groups

Potential Risk: Insurers may unduly penalize consumers who refuse to provide consent, or who do not have a credit history, or whose credit score has been negatively affected by extraordinary life circumstances.

23. The following three sections of the IBC Code speak to this risk:

Section 8 a) in the Code - Taking Adverse Action as a Result of Credit Information - stipulates that the insurer must treat consumers fairly when they have no record of credit information or are unable to create a credit score. The Code explains this to mean that:

- Customers with an absence of credit information shall not be denied coverage, cancelled or non-renewed a policy of personal insurance without consideration of any other applicable underwriting factors;
- In the absence of credit information, underwriting and rating decisions will be based upon the relevant information which is available to the insurer.

- Section 9 in the Code - *Refusal of Consent* – prescribes that insurers:
  - Shall not refuse to provide an insurance quote to the customer, nor refuse to insure a customer, nor terminate or refuse to renew a policy because the customer refuses to give consent to use their credit information. In this situation the

customer will be offered a competitive rate but may not qualify for related discounts or the insurer's best quote.

- Shall not refuse to provide an insurance quote to a customer, nor terminate or refuse to renew a policy solely because of unfavourable credit information.

- Section 10 of the Code – *Extraordinary Life Circumstances* - provides guidance for situations where a consumer believes that his/her credit information has been adversely impacted by an extraordinary life circumstance. If the customer provides the insurer with appropriate documentation verifying how and why their credit history was adversely impacted, the insurer would then review the decision to use credit information as a rating and underwriting factor.

5.6 Privacy Breaches

Potential Risk: Insurers may breach confidential credit information.

24. Section 4 in the Code – Keeping Customers' Credit Information Confidential and Private – prescribes that insurers:

    - Must respect the confidential nature of personal information and that the only persons to have access to such information are those who require it to do their job; and

    - Must fully comply with relevant Canadian consumer and privacy protection laws, including PIPEDA.

25. Insurers' legal obligations under PIPEDA and relevant provincial legislation (i.e. in Alberta, B.C., and Quebec) are a robust response to the privacy risk raised by CCIR. The insurance industry has strong safeguards and practices in place with respect to its collection and retention of consumer information, and IBC is not aware of any privacy breaches involving the P&C insurance industry.

26. Insurers have a proud record of following legal requirements in retaining consumer information, in many cases for information that is more sensitive than credit information. Insurers collect information about the value of a customer's home and its contents in order to underwrite a risk or assess the value of coverage. Consumers trust insurance companies with the privacy and confidentiality of highly sensitive health and financial information following a claim; such information may include doctor's reports, hospital

records, income tax returns, employment records, etc. There is no reason to believe that insurance companies would stray from these established practices in the case of consumer credit information. The industry will continue to enforce its strong safeguards and abide by legal requirements with respect to its collection and retention of sensitive information, including credit information.

5.7 Lack of Understanding

Potential Risk: Consumers may not be sufficiently educated regarding credit-based insurance scores.

27. As we have stressed above, consumer education on financial matters is a key element in helping consumers cope with the realities of the sophisticated world we live in. This is a shared responsibility that needs to be embraced by all stakeholders, including financial institutions, governments, financial intermediaries, and educators. (see section 6)

IV. Voluntary Nature Of The Code

28. The CCIR paper appears to question the meaningfulness of the IBC Code on the basis that it is "voluntary". By way of background, as a trade association IBC is prevented by federal competition rules from imposing any uniform business standards or practices on our members which might be construed as unduly promoting standardization in the market or limiting competition.

29. Notwithstanding the fact that adoption of the Code is voluntary, 85% of the personal lines market share of IBC and CADRI member companies have signed the Code, indicating their willingness to voluntarily follow guidelines that ensure maximum consumer protection. Should an insurance company that has signed the Code fail to comply with its provisions, it would risk exposure to potential disciplinary action from the Financial Consumer Agency of Canada (FCAC).

30. The Code could serve as a framework for oversight of company practices, as an alternative to a total ban on the use of credit information. To this end, several options are available for consideration by provincial governments:

    a) Making companies' compliance with the Code a legal requirement;

b) While continuing the Code's current status, requiring proof of companies' compliance through auditing, in the event of a complaint, failing which administrative action could be taken; and/or

c) Conducting periodic risk-based governance-style surveys to assess industry compliance.

V. Financial Literacy

31. To the extent that some of the concerns raised by CCIR are not addressed by current legislative or regulatory requirements or IBC's Code, we believe that best and most effective answer to these issues lies in improving the financial literacy of Canadians. In this regard, the CCIR paper identifies three potential consumer risks:

> *5.1. Inadequate Consent* - **Potential Risk: Consumers may not know that they have given permission to an insurer to use their credit information or a credit score for determining a consumer's eligibility for insurance and the premium to be charged.**
>
> *5.4 Insufficient Disclosure* - **Potential Risk: Consumers may not have sufficient information about how to modify their behaviour in order to reduce insurance costs.**
>
> *5.7 Lack of Understanding* - **Potential Risk: Consumers may not be sufficiently educated regarding credit-based insurance scores.**

32. IBC holds that financial services companies need to be transparent and disclose adequate information to consumers about insurance or any other financial products or services. Equally important is the need to enhance consumers' financial literacy so that they have sufficient knowledge and skills to be able to properly read this information and understand its consequences. Financially literate consumers are more likely to ask the right questions and ultimately alter their financial decision-making behaviour in ways that could positively affect many aspects of their lives.

33. The need to strengthen the financial literacy of Canadians was the reason for the federal government's establishment of the Task Force to examine Canadians' financial literacy

and to identify a strategy to address these issues. The federal Task Force has identified the following as key elements in the definition of financial literacy:

- "Knowledge" - understanding personal and broader financial matters.
- "Skills" – being able to apply that knowledge in everyday life.
- "Confidence" - feeling self-assured enough to make important decisions. This is often a key factor in galvanizing people into action.
- "Responsible financial decisions" - being able to use the knowledge, skills and confidence that people have gained to make choices that are appropriate to their particular circumstances.

34. According to the Task Force, when asked about the content of a credit report, around 57% of Canadians did not know the answer to the question, or answered it incorrectly. The report also provides many more examples that indicate problems with financial literacy among Canadians. These findings are not surprising and speak to a common problem affecting all financial sectors.

35. Credit information can be used for much more than insurance purposes. In the sophisticated and interconnected world we live in, credit scores can often impact Canadians' ability to find employment, rent an apartment, rent a car, obtain a loan/mortgage, etc. Because restricting the use of credit information for one sector will not shield customers from the impact that their credit scores will have in many other aspects of their lives, we believe that a broader approach is needed to raise public knowledge of credit information, how it can be used, and how it is affected by an individual's conduct of his/her personal financial affairs.

Shared Responsibility

36. As the findings of the Federal Task Force on Financial Literacy have indicated, consumer education is a shared responsibility that needs to be embraced by all stakeholders, including financial institutions, governments, intermediaries and educators. Extensive work has already been done by various public, private and non-governmental organizations aimed at improving the level of public knowledge of personal financial management. Still, much of this effort gives comparatively little attention to insurance products and the role that insurance plays in peoples' overall financial arrangements.

37. In our view, this gap also opens an opportunity for the industry and CCIR to work together to improve consumer literacy on insurance issues, such as:

    - The risk pooling function of insurance and how this enhances consumer welfare by protecting individuals and families against calamities at a cost that the pool makes affordable.
    - The importance to insurance companies and their customers of accurately assessing the risks associated with particular insurance contracts.
    - The risks and obligations assumed by insurance companies and customers when they enter into an insurance contract.
    - What consenting to the use of credit information on an insurance application means - and what it does not mean.
    - The role of insurance intermediaries in educating and otherwise assisting consumers with their insurance needs.

What the Industry Has Done

38. Recognizing that more work is required, the following are some examples of activities that the industry has undertaken in order to increase consumer awareness about insurance products and transactions, with particular reference to the use that some insurers make of credit information.

    - IBC has made a formal request to the federal Minister of Finance, Mr. James M. Flaherty, asking to be involved in the stewardship of the Financial Literacy project. Furthermore, we have put forward the name of IBC's President and CEO, Don Forgeron, with the hope that he will be appointed a member of the yet-to-be-named Advisory Council on Financial Literacy.
    - IBC has developed state-of-the-industry brochures - available in print and online - for each province across Canada, which contain information on the importance of:
        - Choosing the insurance policy that best suits individual consumer needs and finances;
        - Carefully reading the insurance policy and who to ask if there are questions; and
        - Shopping around for insurance.

- IBC's website also contains educational materials on a range of insurance topics, including:
  - Insurers' use of credit information, including IBC's Code of Conduct, and Qs & As about insurers' use of credit information;
  - How insurance works;
  - What customers can do to control the cost of their insurance; and
  - The types of home insurance policies that customers can buy and what they cover.

39. The industry will continue to work on improving consumer education with respect to insurance issues and we hope that the members of CCIR will join us in making this effort a robust success.

Conclusion

40. In conclusion, we believe that most of the concerns that the CCIR has raised in its paper regarding insurers' use of credit information are either addressed by established practices required by law or are within the provisions of IBC's Code of Conduct.

41. We see an opportunity to encourage all stakeholders to step up efforts to significantly improve the state of financial literacy among all Canadians.

42. IBC would be happy to discuss any of the ideas and suggestions raised in this submission with any members of the CCIR.

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IBAO Response to CCIR Consultation Paper "Use of Credit Scores by Insurers"

The Insurance Brokers Association of Ontario (IBAO) welcomes the opportunity to respond to the Canadian Council of Insurance Regulators (CCIR) paper, *Use of Credit Scores by Insurers*. IBAO commends the CCIR for taking on this important matter. Discussion on this topic by our country's regulators is overdue.

IBAO represents over 11,500 insurance brokers that serve millions of consumers across Ontario. Insurance brokers are educated professionals with very strong community ties. Our priority is to protect the interests of consumers from the purchase of a policy right through to when they may need an independent advocate at the time of claim. This response is informed by the experiences of our members and customers.

For some time now, IBAO has been advocating that the use of credit scoring to rate and underwrite insurance should be banned for all forms of personal lines insurance. IBAO believes this practice is unfair to consumers, not transparent and inappropriate as a rating tool. It is IBAO's top public policy priority to see the use of credit information to underwrite personal lines insurance banned, once and for all.

A growing number of insurers are using credit scoring to significantly increase home and other property insurance premiums. The use of credit scoring is NOT being used to predict whether customers will pay their bills. Indeed, IBAO submits that credit scoring has nothing to do with the insured risk. More importantly, credit scores are a factor that consumers have very little control over. Most are unaware what their credit score is, let alone that it is being used to determine the price they pay for insurance. Therefore, for all of these reasons, IBAO believes that the use of credit scoring is harming consumers.

In 2005, the Ontario government banned the use of credit information from auto insurance because it determined that it was not in the public interest. In 2010, Ontario tightened up the rules and stripped the use of credit information from all aspects of the insurance transaction. This was a response to quoting practices that some insurers were using to get around the 2005 prohibitions. Thus, our submission references the use of credit scoring on personal property insurance as the Ontario regulator agreed that the use of credit scoring was harmful in the auto context. IBAO can see no reason why the same regulator continues to permit this practice in other personal property lines.

Identified Risks/Harms to the Consumer

The CCIR paper asks whether all potential risks have been identified and whether the potential risks identified are already addressed under law. The risks identified in the paper are:

1) Inadequate consumer consent
2) Unreliable credit data
3) Availability and affordability of insurance for consumers
4) Insufficient consumer disclosure
5) Undue impact on certain consumer groups
6) Privacy breaches
7) Lack of understanding by consumers

IBAO submits that the risks identified do indeed exist, and they are widespread and systemic. Furthermore, **none of these risks are adequately addressed by current law.** Consumers have nowhere to turn if they are looking for protection from this unfair practice. IBAO also contends that the meagre privacy protections that do exist are rarely enforced.

IBAO also submits that one harm/risk has not been identified:

8) Back door subversion of current credit prohibitions.

This and the others will be elaborated on one-by-one in the following discussion. As IBAO is an Ontario Association, our comments pertain to the Ontario legislative and jurisdictional context, but they do have significant similarities to most other Canadian jurisdictions.

1) Inadequate consumer consent/ 4) Insufficient Consumer Disclosure/7) Lack of Understanding by Consumers

Items 1, 4, and 7 are closely related. IBAO believes they cannot be discussed in isolation.

IBAO conducted a poll related to consumer awareness/understanding in November 2010. Consumers were asked if they were "aware that insurance companies use consumer credit scores when determining what a consumer pays for home insurance?" 75% said "No" they were not aware. Given that a majority of insurers are using credit scores, this tells us that insurers are not doing a very good job of informing their policyholders that they are using this very private and sensitive information. In Alberta, the Consumer Representative to the Automobile Rating Board (AIRB) found that 48% of consumers did not know if insurers were using their credit information.[1] The CCIR's own survey from 2009 revealed 68.4% of insurers using credit scores don't even reveal to the policyholder if there is a negative or positive effect of using credit scores.[2]

[1] www.airb.alberta.ca/public_meetings/2010/0615-airb-consumer-repsubmission.pdf

[2] CCIR Report on the Credit-based Insurance Scoring Questionnaire – August 2009, pg. 15

It is apparent that consumers are not aware that credit is being used to rate and underwrite their property insurance. One of the Personal Information Protection and Electronic Documents Act's (PIPEDA) principles is that consumers must give informed consent and that information collected only be used for the purpose indicated. Principle #4 of PIPEDA states that "The collection of personal information shall be limited to that which is necessary for the purposes identified by the organization..."

IBAO knows of no insurer in the Ontario context that uses credit scoring for rating and underwriting that explicitly reveals this fact to its customers. Many ask for consent to collect credit data, but nowhere can IBAO find an insurer that discloses that a consumer's rates or even eligibility will be determined by this collected credit data. Most obfuscate the issue at best, falsely leading consumers to believe that any credit information collected is used merely to determine if that consumer can be counted on to pay his/her premiums.

IBAO submits that the PIPEDA rules that exist are not being followed here in Ontario. Property applications, i.e. the CSIO standard Habitational Insurance Application, combines the language obtaining the consumer's consent for the insurer to obtain credit information with a disclosure statement; a statement which in essence warrants that the consumer has provided truthful and accurate information to the best of their ability.

This creates two separate and important considerations for compliance with PIPEDA. First, many insurers have only recently implemented their new credit based rating systems. It is clear they are relying on the permissions granted on the original application to access an individual's credit score or credit information, even if it was signed many years ago at a time when its use in rating had not even been contemplated by the insurer. The permissions collected, therefore were never intended to provide a transparent explanation of the reasons for the collection or use of the credit information. The majority of consumers will have no expectation or have any understanding that an application they signed many years ago is what their insurer is relying upon to suggest they are authorized to collect this sensitive information, and to use it in a manner that has a direct financial impact upon the consumer, again, without their express understanding.

Second, the disclosure statement **must** be signed by the consumer in order to obtain coverage. With the application forms currently set up the way they are now, what choice does a consumer have to deny a company access to their credit information? We would argue they have no choice. Without this section separating the language into two separate signature areas within the application, the language of the disclosure and permissions are too broad in scope. If the consumer did not have a reasonable expectation that their credit information would be accessed as a means to price their policy, what recourse is available to them to object, after signing this? The best that can be said about such a process is that the consumer is signing under duress.

Toronto Star columnist Ellen Roseman sums up this consumer dilemma well in her column of May 17, 2011:

> *"**It's not disclosed.** When you apply for credit, the lender asks permission to check your credit score. You must agree before the application goes ahead. When you apply for home insurance or renew a policy, most insurers don't ask permission to check your credit score. That's why consumer awareness is so low...*
>
> *Not many companies send explicit letters to customers, as Co-operators General Insurance did when adopting the practice in June 2009.*
>
> *"If you do not allow us to access your credit score, we will respect your wishes," said Coseco Insurance, a Co-operators affiliate. **"However, we will not be able to provide an accurate or competitive premium that reflects the risk we are insuring. As a result, you will not receive the best possible premium available."***(emphasis added)
>
> *This means you can have excellent credit and still pay higher premiums if you deny access to your credit records by your home insurer."*[3]

Impossible to get informed consent

IBAO submits that it is nearly impossible for any insurance intermediary to get informed consent from its customers because of the very nature of the information being used. The issue is particularly vexing because the methodology insurers are using is proprietary and nebulous. Credit information is so broadly defined it can be interpreted as meaning anything related to the insured's credit rating. As a result, an intermediary can't advise what credit information will be sought by the insurer. Accordingly, they have no control over what credit information is being collected by the insurer and whether it is being used strictly for the insurer's summarized uses or for other unknown uses.

For these reasons alone, related to consumer disclosure, consent and understanding, IBAO believes that the use of credit scores should be banned. Essentially, the consumer does not have a true "choice" even if insurers did the bare minimum under current privacy laws and revealed the true nature and use of the credit data they intend to collect.

2) Unreliable Credit Data

Because the world of credit rating and/or scoring is so proprietary and murky, it is difficult to obtain good data on how reliable credit is. The Public Interest Advocacy Centre (PIAC) is one of the few sources of information on the reliability of credit information in the Canadian context. The 2005 PIAC study reported that 18% of Canadians who checked their credit rating found mistakes.[4]

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[3] Toronto Star, http://www.moneyville.ca/article/992868--roseman-home-insurers-raise-rates, May 17, 2011

[4] Public Interest Advocacy Centre (PIAC), *Credit Reporting: How are Consumers Faring?* (August 2005).

We argue that the current marketplace makes it extremely difficult, if not impossible, for a client to identify a problem or correct it. As an example, consider a consumer whose credit score is incorrect resulting in a surcharge on their policy. We submit that it is highly unlikely they would be able to correct the problem in any reasonable fashion. First, the consumer must be aware that a surcharge has been added to the policy. As the results of the CCIR credit survey clearly show, almost no insurer is providing this information on their policy disclosure pages. Second, they would need to then determine their credit score, an incredibly involved and complicated process with two separate credit rating agencies. In some cases, the consumer would need to incur an additional expense to obtain this information. Third, they then need to be able to determine what the overall impact this has had. Current market practices use credit in sophisticated algorithms, the makeup of which is not disclosed to staff or their intermediaries. A few insurers even refuse to re-run the algorithm once a policy has been issued.

This lack of transparency and access to one's credit scores coupled with insurers' proprietary algorithms and general subterfuge on this topic make it all but impossible for a consumer to protect his/her interest. One of our member brokers who has dealt with customers who are victims of inaccurate data expressed frustration on behalf of his customers:

> "With the way the credit markets are changing today, if insurers are obtaining credit info, how fresh is it? There seems to be no process for changing a credit score once obtained, or more accurately, there is no mechanism for altering the impact it may have on rating. Consumers are left to go back to Equifax or Transunion on their own, as there is no mechanism to change it."

Some insurers only check credit scores upon initial underwriting of a policy and never again (which notably is offside with the IBC "code of conduct"). Of course this means even if a person's credit improves, their rate won't over time.

Finally, Consumer Protection columnist for the Toronto Star, Ellen Roseman, best summed it up this way:

> "***It's dangerous.*** *Credit reports can be wrong. I often hear from people struggling to erase mistaken information from their records. Ontario's two credit bureaus, Equifax and Transunion, don't make it easy to check your credit record for free by mail. Their websites showcase the charges you have to pay for instant access to your credit record. At least a credit record is based on facts, which can be amended or changed. That's not the case with a credit score – a newer measure not governed by any provincial legislation. With a credit score, judgment comes into play. The credit bureaus blend your credit history with other factors to come up with a three-digit score, using computer algorithms not disclosed to the public. I think credit bureaus are too secretive and have too much power already. So, why are we allowing them into the insurance field? Finally, if you're turned down for home insurance because of a credit score, you may find other companies won't take your business. You could be blackballed and forced to self-insure."*[5]

[5] Toronto Star, http://www.moneyville.ca/article/992868--roseman-home-insurers-raise-rates, May 17, 2011

3) Availability and affordability of insurance for consumers

Our members' experience on the ground is instructive. Insurers are increasing rates by up to 80% based on credit scores. IBAO maintains that a double digit increase of up to 80% is an affordability issue and indeed is an availability issue. Massive hikes for consumers with low credit scores are designed to remove that consumer from the insurer's book of business. Furthermore, we have seen evidence of certain insurers denying coverage outright either by refusing to write certain customers or by refusing to write customers migrating from insurers that have rated them as high risk because of their credit score.

IBAO sampled property renewals from 12 different brokerages that deal with one specific insurance company known to be utilizing credit scoring aggressively. Of the 54 policies sampled:

- The average premium increase was 73%
- The largest premium increase was 155% or $762, annually
- The smallest increase was 11%
- They noted no premium decreases

*Seven policies included claims related increases and were excluded from the sampling.

Conversely, two mechanisms are used commonly in today's marketplace to limit premium reductions offered to consumers. The first, which is common for new business, is the setting of a maximum percentage by which a policy premium can be discounted. These percentages vary widely. The second, more common on renewal, is the use of negative rate capping, currently as low as 0%, meaning no discount is provided on renewal. Examples of greater than 10% are rare. It is important to point out that the majority of policies are in renewal status, and as such, even as carriers move to these new credit-based systems, rate capping prevents the true savings promoted by many insurers today. For this reason, IBAO submits that the use of credit in current rating systems asymmetrically favour higher premiums over consumer savings; and therefore has a direct negative influence on affordability and availability for all consumers.

5) Undue impact on certain consumer groups

IBAO strongly believes that credit scoring is an inappropriate rating tool for various reasons; chiefly being that the practice discriminates against certain groups including those with low incomes. IBAO is on record stating that the use of credit scoring has a disproportionate negative impact on retired seniors, newcomers, and single income families amongst others. Unfortunately, there is not a lot of research on this in the Canadian context. However, the issue has been studied in the United States.

While credit scoring is not an explicitly discriminatory tool, evidence from studies in the United States shows that credit scores do have a disproportionately negative impact on certain groups in society. In other words, the results are shown to be absolutely discriminatory.

The State of Missouri Department of Insurance conducted a study on this matter. It concluded the following:

> *"The Insurance credit-scoring system produces significantly worse scores for residents of high minority ZIP codes."*[6]

In a July 2007 report to the US Congress, the Federal Trade Commission (FTC) confirmed these findings:

> *"Credit-based insurance scores are distributed differently among racial and ethnic groups, and this difference is likely to have an effect on the insurance premiums these groups pay, on average..."*
>
> *"...African-Americans and Hispanics are substantially overrepresented among consumers with the lowest scores (the scores associated with highest predicted risk) and substantially underrepresented among those with the highest scores."*[7]

With respect to credit scoring's effect on low-income consumers, the same report states: *"Low-to-moderate income consumers are somewhat over represented in the lower score deciles..."*[8] The Missouri study also concluded: *"Insurance credit-scoring systems produce significantly worse scores for residents of low-income ZIP codes."*[9]

Kevin McCarty, the State of Florida's Insurance Commissioner, in testimony to the US Congress' House Committee on Financial Services, stated the following in 2008:

"Credit reports also disproportionately negatively affect recent divorcees, recently naturalized citizens, the elderly, the disabled, those with certain religious convictions, and younger individuals who have not established credit histories."[10]

Therefore, IBAO maintains, and the evidence supports, that credit scoring has a disproportionately negative effect on certain groups. To say otherwise is just plain wrong. The Insurance Brokers Association of Ontario believes strongly that regulators should not ignore this evidence as a matter of public interest.

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[6] **Insurance Based Credit Scores: Impact on Minority and Low-Income Populations in Missouri**, *State of Missouri Department of Insurance*, page 1, January 2004

[7] **Credit-Based Insurance Scores: Impacts on Consumers of Automobile Insurance**, *A Report to Congress by the Federal Trade Commission*, July 2007, page 3

[8] Ibid, page 55 and Figure 10

[9] **Insurance Based Credit Scores: Impact on Minority and Low-Income Populations in Missouri**, *State of Missouri Department of Insurance*, page 1, January 2004

[10] Testimony of Kevin McCarty, Florida Insurance Commissioner, Florida Office of Insurance Regulation and Representing the National Association of Insurance Commissioners before the Subcommittee on Oversight and Investigations of the House Committee on Financial Services regarding: "The Impact of Credit-Based Insurance Scoring on the Availability and Affordability of Insurance"

6) Privacy Breaches

It is very difficult for IBAO to provide direct evidence as to how widespread insurer violations of privacy laws are. This is because, as discussed, most consumers aren't even aware that their credit info is being used, or, if they did, what it's used for. Most importantly, privacy infractions that may or may not exist cannot be exposed unless someone within the insurance organization reveals such wrongdoing.

The best evidence to date comes from an investigation and ruling from the Province of British Columbia (BC) British Columbia's Information and Privacy Commissioner (BCIPC).[11] In its ruling issued May 6, 2011, the BCIPC said that Economical Insurance Company violated BC's privacy statute which prohibits organizations from collecting, using or disclosing personal information about an individual unless, among other things, the individual has consented to its collection, use or disclosure.

According to the BCIPC, two separate requirements must be met. First, the organization must have provided the individual with notice of the purpose for the collection of the information before or at the time consent is sought, as set out in s. 10(1)(a). Second, having received notice of the purpose, the individual must consent. BC's *Personal Information Protection Act* (PIPA) stipulates that express consent is consent that is informed by the purpose for which the information will be collected. **The BCIPC ruled that there was no deemed consent by the complainant as defined in PIPA and that the Insurer did not give adequate notice of its purpose in collecting the complainant's credit information.**

So, can this recent finding be extrapolated to other customers and jurisdictions? First, IBAO believes that the requirements and principles contained in the BC PIPA are similar in all privacy statutes including Canada's PIPEDA. Second, IBAO believes that most insurance companies operating in Ontario, not just Economical, are not obtaining informed consent, nor are they providing adequate disclosure about the purpose for which the information is being collected.

This observation comes not only from IBAO member feedback, but also from CCIR's own survey on the topic.[12] In 2009, the Canadian Council of Insurance Regulators (CCIR) determined that many insurers were not being transparent about the purpose of the credit data they were collecting. Indeed, 7 of the 16 companies that were using credit scoring at the time of the survey did not inform their customers the purpose for which they were collecting credit information.[13] Only one disclosed the result on the consumer's policy. In our opinion, this is not informed consent.

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[11] **Information & Privacy Commissioner for British Columbia**, Order P11-02 www.oipc.bc.ca/PIPAOrders/2011/OrderP11-02.pdf

[12] **CCIR Report on the Credit-based Insurance Scoring Questionnaire – August 2009** http://www.ccir-ccrra.org/en/init/Credit_scor/CBIS_Report_2009_CCIR_EN.pdf

[13] ibid

8) Back door subversion of current credit prohibitions

The Insurance Brokers Association of Ontario would like to point out that the industry track record has been poor with existing prohibitions. When credit scoring in auto insurance was banned in 2005 in Ontario, some insurers continued to defy the ban by resorting to objectionable quoting practices, denying auto insurance quotes to consumers based on credit and other lifestyle factors despite admonitions from the Financial Services Commission of Ontario (FSCO) that this violated the intent and spirit of the law. Only when new regulations, as part of Ontario's 2010 auto reforms, came into place was this behaviour curbed.

Our member brokers, unfortunately, are well acquainted with violations of current Ontario law, namely the prohibition from using credit information in any way, shape or form in the Ontario auto product. Some insurers are using their wide-open access to credit information in their property portfolios to indirectly rate auto insurance. In our view, insurers who write joint auto/property policies place exorbitant surcharges on property premiums to deter consumers from buying or renewing coverage for both lines of business, as the majority of consumers have been urged to maximize discounts (as much as 15%) and place both policies with the same insurer. Consumers who receive these surcharges are often forced to find other alternatives for their property coverage, and in the process, move their automobile coverage and lose their multi-policy discount. Either way, the use of credit scoring in property has a direct impact on the automobile insurance premium. From the insurer's point of view, it is "mission accomplished". IBAO submits that this type of outcome is by-design and is in violation with public policy set out in Ontario auto regulations.

IBC "Code of Conduct"

The CCIR paper makes reference to the Insurance Bureau of Canada's (IBC) "Code of Conduct," that purportedly protects consumers with respect to the use of credit information. As part of their defence of credit scoring, IBC holds up this voluntary "code of conduct" to mollify consumers and decision-makers.

IBAO would like to point out that, to our knowledge, no insurer in Ontario that uses credit scoring is in compliance with this voluntary "code of conduct". Despite having a code of conduct since at least January 2010, IBC still cannot provide any evidence that any insurer is in compliance with it. There is also no effective enforcement of this code of conduct in the event that an insurer declared that it was complying with the code. **The creation of this "code of conduct" is merely a public relations exercise to deflect criticism away from this unfair practice intended to give consumers and regulators a false sense of security that consumers are protected, which they are not.** In any event, no use of credit scoring is acceptable or fair to consumers whether there is a "code of conduct" or not.

Sincerely,

Randy Carroll
Chief Executive Officer
Insurance Brokers Association of Ontario



Canadian Council of Insurance Regulators

A submission on the issues paper *Use of Credit Scores by Insurers*

Prepared by Intact Insurance
August 2011

INTRODUCTION

In response to the Canadian Council of Insurance Regulators' (CCIR) June 17 2011 issues paper entitled "Use of Credit Scores by Insurers", Intact Insurance would like to comment on the paper and the positive impact of credit score use on consumers and competition as it relates to property and casualty insurance.

Intact Insurance is Canada's largest home, auto and business insurance company protecting more than 2.5 million customers. We are the industry leader, with a proven record of sound and responsible financial management. Our coast-to-coast presence, along with our strong relationships with insurance brokers, means we provide the outstanding service, comfort and continuity that our customers deserve.

We believe that the CCIR paper rightly acknowledges the potential risks of using credit scores. However these risks can be mitigated through industry standards and guidelines. More specifically, by enshrining the Insurance Bureau of Canada's Code of Conduct into the legislative framework. In addition, further controls, as outlined in this paper will alleviate the concerns and risks identified in the CCIR paper.

We address many of these risks in our paper, but more importantly we outline the many advantages associated with the use of credit scores by enhancing the competitive landscape for the benefit of consumers. Enhancing competition by using credit scoring magnifies the number of potential product offerings in the marketplace. This ensures that the right product and price is available to all consumers.

Indeed, some consumers have concerns about the use of credit scoring in insurance. However, with the appropriate level of consumer awareness and transparency, consumers should have sufficient information with which to make their insurance purchase decision. Not all insurers use credit scoring, just as not all insurers offer the same products and prices. Accordingly, for consumers not comfortable with insurers using credit scoring, they have the ability to seek out insurers who more closely match their desires. This is the key attribute of a competitive marketplace and needs to be maintained by ensuring that companies have the

flexibility to create and price products and ultimately service customers. Without this flexibility the competitive landscape diminishes and the consumer suffers.

Unfortunately, credit has been misused by some in the industry. This has often painted the use of credit scoring in a bad light. However, these exceptions should be managed on a case-by-case basis by regulators, rather than outright bans due to the actions of a few.

We would like to address many of the issues raised in the CCIR paper, including several of the potential risks to consumers identified in the paper.

CREDIT SCORING IMPROVES AVAILABILITY AND AFFORDABILITY OF INSURANCE

We have been using credit-based discounts as part of our rating program for a number of years. During that time, there were no concerns regarding the availability of our own products.

In addition, we also adopted a set of further guiding principles that clearly articulates how we use credit information. These guiding principles are as follows:

- Intact Insurance does not see credit reports.
- A customer's credit score will not affect their existing coverage or eligibility for insurance.
- If a customer refuses to provide consent, we will provide a quote and/or policy at our best possible base rate *(less any discounts the customer may qualify for).*
- Individual credit scores are kept in a secure database and cannot be seen by anyone handling policies.

We use financial stability variables to offer our customers two types of discounts.

A credit-related factor is often incorporated into our rating programs, where allowed. In addition, we also recognize our financially-responsible customers through the use of a mortgage-free discount.

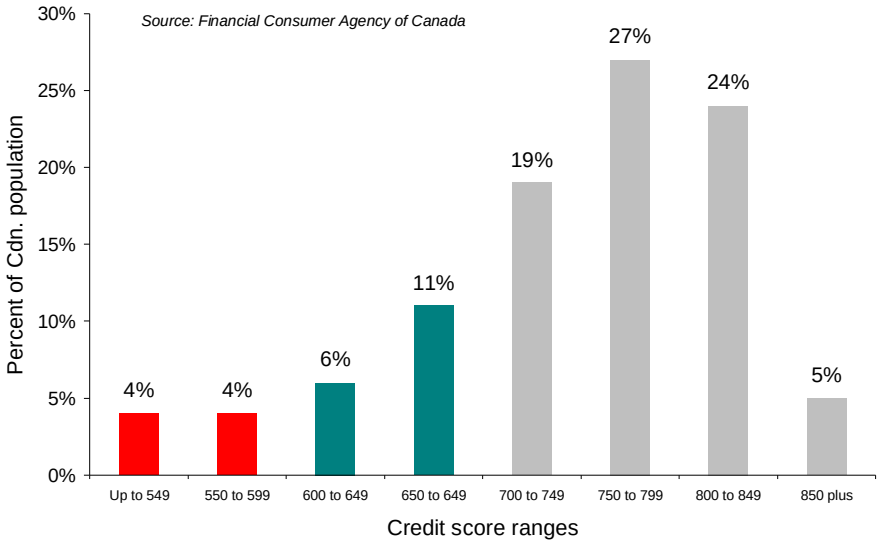
Financial stability indicators are therefore valuable segmentation tools that are used to the benefit of consumers.

CREDIT SCORES ARE STRONG PREDICTORS OF FUTURE CLAIMS

The use of credit scores is a normal and widely-accepted practice for a broad range of businesses. Maintaining a strong credit rating is a necessity for all consumers, personal and commercial alike.

While the industries that use credit scores may measure them differently, Canadians are by far and large financially responsible with 75% of the population with a credit score of 700 or more.

Canadian national distribution of credit scores, 2008



Many studies, in North America and abroad, indicate a strong correlation between financial stability and the cost of future insurance losses for both personal and business customers.

Our own data also clearly demonstrates this fact. As can be seen in the following chart both the loss ratio and frequency of our own personal property portfolio improve as a customer's credit score increases. We experienced the

same type of correlation in commercial lines, further reinforcing the predictive power of financial stability indicators as they relate to future claims trends.

Correlation between financial stability and loss ratio/frequency of personal property insurance, 2007 - 2009



Incorporating individual financial stability into our pricing and segmentation strategy has allowed us to provide our customers with premiums which accurately reflect their specific-risk characteristics. We believe that it is fair and equitable to reward deserving customers who have lower claims potential with more attractive premiums, appropriately reflect their risk profiles.

There is a lot of debate around causation versus correlation of credit scores to loss experience. Causation is related to one's behaviour. We believe that financial stability is a strong indicator of how people take care of their belongings and who live a more disciplined lifestyle and therefore serves as a predictor of the risk a person represents from an insurance perspective.

Credit scoring is predictive and this is the only reason it is used by insurers. If a credit score was not predictive, it would not be used. Accordingly, losing the ability to rate with credit scores would have negative consequences on the marketplace as another predictive variable would be lost, which ultimately leads to a reduction in the potential offerings available to consumers.

GAINING CONSENT IS THE FIRST STEP

Clearly, without appropriate consent, credit scoring cannot and should not be used by insurers.

The IBC Code of Conduct is very clear with respect to obtaining consent. Complying with this code will ensure that the process of obtaining consent is clear and precise.

At Intact we only use credit scores with the customer's consent. Attached in the appendix, is an example of the type of material used at Intact for underwriters, customers and brokers. This communication strategy ensures a high level of transparency to our customers. Many of the risks identified by CCIR can be mitigated by a solid and thorough approach to transparency.

In addition to the standard CSIO habitation application, we seek a supplemental consent from the customer specifically regarding credit score. We are continually reviewing our processes and recently made a change to make the process of obtaining credit consent easier for our brokers. More specifically, we developed a new supplemental consent form that includes useful information about credit scoring and how it is used at Intact as well as an area where customers can sign indicating they have allowed us to obtain their credit score.

At all times customers can decline consent for credit scoring and have the right to withdraw their consent at any time in the future. The same consent process is followed within our online quoting system that our brokers use.

The customer also receives a customer information page each year that will list the information of the various variables we use in determining their premium. We show the customer whether we have their consent on file to order their credit score.

Through these actions, we are transparent to our customers with respect to providing credit consent.

In addition, collecting credit scores by insurance companies is regarded as a "soft hit" by the credit reporting agencies. Meaning that the process of collecting

a credit score does not impact the actual credit score itself, unlike an application for further credit.

CREDIT DATA IS OF GOOD QUALITY

One of the concerns regarding credit scoring that we hear consistently from many stakeholders is the quality of the data underlying the credit score.

The credit reporting agencies are governed by very strict regulation across the country and the management of data errors is a critical component of the regulatory process. Each credit reporting agency is governed provincially by a credit reporting regulator. We encourage each of the provincial insurance regulators to reach out to their respective credit reporting regulators to assess the quality of credit data in order to achieve a totally unbiased perspective on this matter.

Further, many institutions and industry's use credit scores on a daily basis with the volume of credit score requests far exceeding that of the P&C insurance industry.

In the rare case that a customer identifies an error in their credit file, we gather the new credit score and use the corrected score in our rate setting process.

Lastly, one of the many important elements that govern credit reporting agencies is the right of consumers to access credit information at any time and for as many times throughout a year as they wish.

CREDIT SCORING IS FAR FROM INITUITIVE FOR SOME

The use of financial stability indicators, such as individual credit, in insurance, is far from intuitive for brokers and consumers. As a result, we have enhanced our communication efforts to provide them with a clear understanding about the role that financial stability can play in the determination of insurance premiums. As part of this initiative, extensive training was provided to our brokers and a detailed information sheet was prepared for our customers. Our goal was to ensure that our use of personal credit scores was transparent and clear for customers and brokers alike.

Many states in the US are currently active with consumer-awareness campaigns given that credit scoring is widely used by so many industries, well beyond the P&C insurance industry. We believe it would be beneficial to consumers if Canadian regulators, not just insurance-related regulators, could investigate the effectiveness of these campaigns and assess whether similar approaches should be taken in Canada.

CREDIT SCORING SHOULD BE USED RESPONSBILY

Many have raised concerns about the impact of unforeseen circumstances. Firstly, as we have shown above the vast majority of Canadians have good credit scores. While events can occur that can have a dramatic impact on one's life, what ultimately drives a worsening of a credit scores is a continual occurrence of credit troubles. These events are rare. However, we believe the IBC's Code of Conduct effectively deals with these exceptional circumstances. Further, we have a process in place at Intact to handle such events.

We also encourage governments to prohibit the use of individual credit variables to decline insurance coverage to current or prospective customers. This will ensure that consumers are treated in a fair and transparent way and consumers will continue to be protected from severe or punitive actions.

Lastly, credit scoring reflects one's ability to live within one's means. It's not about wealth, income, race, etc. The distribution of credit scores is relatively consistent across all of these types of non-credit related attributes. Accordingly, when credit scoring is used in a transparent and appropriate way, it enhances the competitive landscape of the insurance market in Canada.

WE TREAT PRIVACY VERY SERIOUSLY

The various privacy acts across the country deal with all parts of personal information, including credit information. We have a high level of controls in place to ensure our processes meet the needs of our customers and their personal information. The controls that we have in

place for credit information are no different. A limited number of people have access to a customer's credit information. Our front-line staff, underwriters or brokers, do not have access to a customer credit information.

THE UNINTENDED CONSEQUENCES OF BANNING CREDIT SCORING

At Intact Insurance, we are customer-focused during the claims and the underwriting/rating process. The use of individual financial stability indicators, in the form of a discount for consumers, not only allows us to make our product widely available but also helps us to stabilize pricing levels for consumers. In doing so, we contribute to supporting the policy objectives of ensuring that insurance is affordable and accessible.

The data, as outlined above, supports a discount-based approach for positive credit scores. Canadian consumers and our own customers are by far and large financially responsible. Removing financial stability as a rating factor would result in most of our customers having to pay higher premiums. We are convinced that such an undesirable consequence is not the policy outcome that government wants to achieve.

CONTROLLING THE USE OF FINANCIAL STABILITY VARIABLES

We understand many government's concerns regarding the improper use of such indicators. In this regard, we encourage governments to prohibit the use of individual credit variables to decline insurance coverage to current or prospective customers.

However, rather than adopt a full credit scoring ban in pricing and underwriting, we would suggest a more balanced approach that would ensure that consumers continue to benefit from the advantages that credit scoring provides, while being protected from severe or punitive actions.

We recommend that any proposed regulation enshrine the ability of insurers to use individual financial stability variables for pricing and segmentation purposes.

We would also strongly encourage regulators to consider the adoption of protocols to monitor and control the use of

individual credit information. Implementation of a code of conduct, based on our own guiding principles outlined above, in addition to the code of conduct developed by the Insurance Bureau of Canada would ensure that consumers would be protected from unfair practices.

APPENDIX: INTERNAL COMMUNICATION TO UNDERWRITERS

IMPACT ON BROKERS' PROCESSES

Question	What you need to know
Is a signed consent form required with all new applications?	The form must accompany all new business submitted via paper application, even though the application is also signed. Note: The form is not required for new business processed via SaversPlus, but the broker can choose to follow this workflow when processing in SaversPlus.
Is a signed consent form to be obtained at every renewal?	No. The form is only required on renewal if adding a Named Insured, or if changing the consent from 'No' to 'Yes.'
Is a signed consent form required with every midterm change?	No. The form is only required for a midterm change adding a Named Insured, or if changing the consent from 'No' to 'Yes.'
Is a separate consent form required for every policy?	Yes. Even if a customer has more than one policy with Intact, a separate signed consent form is required for each policy. My Home and Auto policies would require one consent form. A 'Client Details' screen may be associated with more than one policy for a given customer, so proper procedures should be followed.
Are brokers expected to go through the form with their customers before it is signed?	We expect brokers to discuss credit scoring in enough detail so that customers fully understand what they are signing and why. Many brokers are already discussing credit scoring, and the new form provides them with additional support materials. As an added benefit, the top section can be provided to customers for their reference.
Is credit consent required even for quoting?	Credit scores cannot be ordered until specific consent is obtained from the customer, either using the credit consent form or a properly documented verbal agreement. Quotes should not include credit until the customer has given consent.
Can brokers use their own consent forms?	The Intact Insurance credit consent form should be used. If brokers have their own form, it may be used providing that it fully encompasses Intact's wording.
What is the impact if they don't use our (or any) consent form?	The new credit consent form ensures the customer is given accurate information about credit scores, including how and why Intact Insurance uses them. If the form is not signed at the time of new business, then we will not pull the customer's credit score.
What if the customer refuses to sign the credit consent form?	If the customer refuses to sign the credit consent form, but has signed the application, credit consent should be considered as 'No.' This applies to both lines of business.
Can a broker obtain verbal consent instead?	We acknowledge that some brokers conduct a lot of their business over the phone, and prefer to obtain verbal consent from their customers. Consent can be obtained verbally instead of using the new form, provided the broker properly documents this in a very consistent manner.

APPENDIX: INTERNAL COMMUNICATION TO UNDERWRITERS

Question	What you need to know
What must be documented when verbal consent is provided?	There must be a clear comment made on the General Page in Halcion or the Notes section in Savers Plus. It must indicate that verbal consent was given by the customer.
How should consent be handled with portfolio transfers?	There is no change to how this is handled currently. Portfolio transfer agreements may specifically address this issue, and the appropriate processes should be followed. No assumptions should ever be made regarding credit consent. If it is unclear whether consent has been provided, then consent is 'No.'

IMPACT ON SYSTEMS & UNDERWRITING PROCESSES

Question	What you need to know
What underwriting action is expected regarding credit?	Credit is not an underwriting variable. Credit consent and credit scores cannot be used to affect coverage or eligibility for insurance in any way.
Should new policies or endorsements be held until the signed form is received?	Until we receive a signed consent form – or a properly documented verbal agreement – the credit consent field should always indicate 'No.' If the file cannot be held to wait for proper consent to be obtained, the new policy or endorsement should be issued with the 'CR CHK' field coded as "N," together with a follow-up to the broker. Once credit consent is received, the 'CR CHK' field can be changed to "Y" and the file re-rated.
What is the impact to payment plan options?	Anytime 'Yes (But No Credit Check)' is selected, the Halcion consent value will be 'N,' regardless of a payment plan.
Can we make assumptions regarding credit consent?	No assumptions should ever be made regarding credit consent. If it is unclear whether consent has been provided, then consent is 'No.'
How should consent be handled when combining to create 'My Home & Auto' policies?	If the lead policy has the 'CR CHK' field coded as "Y," and a new line of business is being added: • If the Named Insureds are the same, consent can remain as 'Yes,' unless the customer is not willing to provide credit consent • If the Named Insureds are different, a new consent form is required If the lead policy has the 'CR CHK' field coded as "N," and a new line of business is being added: • If credit consent is obtained for the new line of business, and the Named Insureds are the same, consent can be changed to 'Yes' If the Named Insureds are different, a consent form for the lead policy is required before changing the consent to 'Yes'
If there is a "Y" in the CR CHK field, does new consent have to be obtained?	Even if the 'CR CHK' field is already coded as "Y" on a given policy, a new consent form has to be obtained if a Named Insured is being added, or when the customer requests to change the credit consent from 'No' to 'Yes.'

APPENDIX: INTERNAL COMMUNICATION TO UNDERWRITERS

Question	What you need to know
What about policies that have been with Intact for a long time and a signature cannot be confirmed?	The policy should be left with 'Yes' to consent. The new credit consent form is a change to be used moving forward, to further strengthen our process. A new consent form has to be obtained only if a Named Insured is being added, or when the customer specifically requests to change the credit consent from 'No' to 'Yes.'
What documentation is expected for policies processed in Halcion?	There should be a clear comment made on the General Page in Halcion indicating that the signed credit consent form has been received.
What comments are uploaded from Savers Plus into Halcion?	If 'Yes' is selected for consent: • *"Verbal consent is 'Y' and credit consent in Halcion is 'Y'"* If 'Yes (But No Credit Check)' is selected for consent: • No payment plan: *"Verbal consent is 'N,' no payment plan, credit consent in Halcion is 'N'"* • Payment plan: *"Verbal consent is 'N,' but due to payment plan (D/3 or D/Q) selected, credit consent in Halcion is changed to 'Y' per section 13 of auto application"* Regarding consent being obtained on behalf of someone else: • If 'Yes': *"The applicant obtained consent to provide personal information on behalf of someone else"* If 'No': *"The applicant has not obtained consent to provide consent on behalf of someone else"*
Are there any impacts to third-party quoting tools?	Quoting tools provided by third-party vendors – such as Compu-Quote, PowerQuote & IntelliQuote – are not being changed.

DOCUMENT RETENTION GUIDELINES

Question	What you need to know
Do all consent forms need to be obtained by Intact and scanned?	There is no change to how this is handled currently: • If a consent form is received, it should be documented and scanned, as with any other form signed by a customer If records are retained in the broker's office, the consent form does not need to be scanned by Intact, and the broker should be audited appropriately as they are today
If brokers are paperless, do they need to retain the hardcopy form?	Paperless brokers will have existing procedures in place to maintain records in accordance with document retention guidelines. The new credit consent form should be incorporated into that process, unless the broker prefers to send it into Intact for scanning.
Have the document retention guidelines been updated?	Yes. The credit consent form must be retained for seven years, following our current guidelines for new applications. The document retention guidelines can be found in the Corporate Services database, and are also included in the Savers Plus User Guide.

APPENDIX: EXTERNAL COMMUNICATION TO CUSTOMERS AND BROKERS

An insurance company that understands you want protection and security.

Intact Insurance is Canada's largest home, auto and business insurance company protecting over three million customers. We are the industry leader and a financially strong and stable company. Our coast-to-coast presence, fortified by our strong relationship with insurance brokers, means we can provide the outstanding service and stability you deserve.

Our name is our promise

At Intact Insurance we are here to protect the things you care about. But, our strength is our ability to get you back on track. And you have our word that we will do it in a fair, respectful and easy manner.

Questions? Call your trusted insurance broker, your best source for information and advice.

HOME | AUTO | BUSINESS
www.intactinsurance.com

Your insurance broker:

Insurance and the use of credit scores



Intact Insurance is a company that wants to help people get the best premium available to them.

Credit scores are part of that.

59487 (07-2010)

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BARBARA BELLISSIMO, FCIP
CHIEF AGENT and SENIOR VICE PRESIDENT

August 12, 2011

To: CCIR Secretariat e - mail: ccir - ccrra@fsco.gov.on.ca

From: Barbara Bellissimo, Senior Vice President, State Farm Insurance

Re: Use of Credit Scores by Insurers

State Farm appreciates the opportunity to respond to the issues raised by the Credit Scoring Working Group of the Canadian Council of Insurance Regulators (CCIR) in its recently-released discussion paper.

State Farm is a mutual company owned by our policyholders and services over 81 million policies and accounts across Canada and the United States through 68,000 employees and 18,000 exclusive independent contractor agents.

The Canadian branch of State Farm opened its doors in Canada in 1938, and is currently active in Alberta, New Brunswick and Ontario, providing insurance and other financial services to 2.2 million policies and accounts.

State Farm's position is that credit information has been established as an appropriate, fair and valuable rating and underwriting tool, and its use is demonstrably effective in predicting the risk of loss. Our policyholders benefit from the use of these kinds of tools that facilitate accuracy in risk classification and pricing.

Legislation or regulation further restricting the use of credit information in insurance is unnecessary, unwise, and potentially anti-competitive. Restrictions on possible discrimination in the use of credit information should be no different than those applicable to other underwriting or rating factors. Existing prohibitions against unfair discrimination provide ample legal authority for regulators to address any possible instances of unfair use of credit information.

Affordability, Availability, Stability & Fairness

We strongly believe that insurance scoring is an important tool in achieving our goal of providing affordability, availability, stability and fairness to all consumers.

During a time when the use of credit-based information by insurers continues to capture some headlines across the country and has been the topic of discussion by politicians, regulators and the media, it is important that objective information form the basis for meaningful dialogue on this important public policy issue.

Insurance scoring's predictive properties help insurers identify more accurately the risk of loss each policyholder represents. As a result, the use of insurance scores benefits consumers by:

1. Lowering rates for many, as insurance rates are reduced for consumers who represent lower risk.

2. Better matching rates with risk. Higher-risk policyholders may pay higher rates that accurately reflect their higher risk of loss, and in turn lower-risk policyholders don't have to subsidize the cost of insurance for higher-risk policyholders.

3. Often allowing companies to take on a risk they might not write using only traditional factors.

We believe strongly that insurance companies should continue to use relevant information to give lower rates to groups of low-risk consumers who are expected to have lower loss costs, no matter the type of insurance. Fairness results when consumers pay into the insurance system according to the risk each poses. When insurance companies are permitted to establish prices as accurately as possible based on risk, they are encouraged to compete more vigorously and to make more insurance products available to consumers. This results in more choices for consumers, who can shop for an insurer and rate plan that best fit their own needs.

Experience has shown time and again how limitations on insurers' use of proven risk factors have upset competitive markets and increased prices. Prohibiting the use of credit-based insurance scores is counterproductive and harms, rather than benefits, insurance consumers.

State Farm's Use of Credit Information

As an example, State Farm's homeowner insurance risk models in Canada use certain credit information (where permitted by law) to develop a score. Our models were developed using statistics based on our book of business. Our models are not designed to assess wealth, income or creditworthiness, but to focus on predicting the likelihood of future insurance claims.

Our use of insurance risk scores takes into consideration extraordinary life events (ELE) such as death, divorce, major health issue or loss of employment over three (3) months. Our personnel work with an affected customer to document relevant ELE situations which can then result in a neutral score being used for the customer. State Farm provides disclosure at the point of sale about our use of credit information. If the applicant has insufficient credit history, a neutral score is applied.

Our models only make use of external credit information during the first three years of a new client coming to State Farm. After this period, we use information generated from our own internal statistics.

Misconceptions

A common misperception is that using credit-based insurance scoring generates more revenue for insurance companies. This is simply not the case.

Use of credit information for rating purposes is approximately revenue-neutral. If we stopped using credit-based insurance scoring, we would be collecting no more and no less premium than we are collecting today. Our use of credit-based insurance scoring involves only a redistribution of the aggregate premium based on a more precise measurement of risk.

Contrary to another misconception, credit-based insurance scoring does not involve disparate treatment of customers based on race, ethnicity, income, or any other legally prohibited characteristic. To the contrary, insurance scoring is a means of affording equal treatment in the rating process to all individuals,

regardless of race, ethnicity, or income. In fact, people earning high incomes do not necessarily have better credit scores, and those with lower incomes do not necessarily have worse credit scores.

Potential Risks to Consumers Cited by CCIR

The Working Group's paper asks for feedback on several potential risks or consumer harms identified in the paper as possibly arising from the use of credit-based insurance scores. We offer the following views on those items.

5.1 Inadequate consent

We agree that there is a need to ensure that insurance consumers are both aware of, and agree to, the use of their credit information – this should apply to insurance companies in the same general manner as any other business that uses consumer credit information. Our view is that federal and provincial privacy legislation adequately addresses the need to identify the purpose of consent, capacity to consent, and form of consent.

We do not agree, as suggested in the issues paper, that the results of either the IBAO poll on consumer awareness of the use of credit scores by property insurers or the related AIRB survey mentioned in the paper suggest that consumer consent is not sufficiently informed, or that these reports diverge in any way from FSCO's 2009 survey regarding informed consent.

Based on our understanding of the IBAO poll (as set out in "Final Report: Ontario Omnibus" (November 2010), posted on the website www. soaringinsurancerates.ca), the poll involved a survey of Ontario residents, whether or not they were purchasers of home insurance; we do not believe that the understanding of non-consumers is particularly relevant to the issue of informed consumer consent. Further, for those participants who were actually purchasers of home insurance, the IBAO poll at most assesses their recollection of the insurance quoting or purchasing transaction, which may have occurred many months prior to the survey; it does not reflect on whether or not sufficiently informed consent was actually provided at the time of the transaction. The AIRB survey finding mentioned in the issues paper (that 48% of Alberta consumers are uncertain whether insurers, in the automobile context, use credit information, in a jurisdiction where such use is largely prohibited) also does not address whether or not adequately informed consent was obtained in those Alberta situations where consumer credit information was actually sought by insurers.

5.2 Unreliable credit data

The use of our models is predicated on the need for current and accurate credit information and we have processes in place to assist consumers who believe that there may be errors in their credit reports. We agree that having insurers use current and accurate credit information is a desired outcome for consumers as a whole (taking into account that unreliable credit information concerning an individual consumer could be to that consumer's benefit or detriment, depending on the nature of the unreliability). The same outcome is equally desirable in industries other than insurance where credit information is used, and we believe that existing legislation targeted at credit reporting accuracy and errors should not be amended to in any way target the insurance industry with additional obligations.

5.3 Availability and affordability of insurance

We do not agree that there is a general risk that insurance coverage may be unavailable or no longer affordable due to credit-based insurance scores. The use of credit-based insurance scoring leads to more accurate placement and pricing of risks reflective of their potential for future insurance loss and, therefore, facilitates greater availability. Existing legislation or regulatory interpretations that preclude its use should be amended to permit its use.

Credible and impartial studies, including government studies conducted by the US Federal Trade Commission, the Texas Department of Insurance and the Arkansas Department of Insurance, as well as our own internal studies, clearly establish that information from credit reports is very effective in identifying groups of insureds that are likely to have different future insurance claim costs. Because of this high correlation, credit information and insurance scoring models are useful underwriting and rating tools for the proper selection and pricing of risks. There is no reliable evidence that we have found to refute the correlation.

The aforementioned studies have all determined that credit-based insurance scores are highly predictive of whether an individual will file an insurance claim. We encourage the CCIR to review these independent studies for a more comprehensive examination of their results and conclusions. We highly recommend that studies of this nature be undertaken in Canada, if any further restrictive policies are being contemplated.

While there is a dearth of Canadian studies available to ascertain the extent of premium increases or decreases, the Arkansas report cited in the paper found that almost a third of policies in that jurisdiction received a premium decrease due to the use of credit scores, while 9% received a premium increase, and our own internal results indicate similar numbers.

Recent studies also demonstrate that the recent economic downturn did not cause insurance credit risk scores to deteriorate (even if that might have occurred with lending risk scores);,and that insurance risk scores using credit report information have remained predictive through a variety of economic conditions over the past 10 to 15 years.

Some critics have argued that the use of credit information will make it more difficult to obtain coverage. To the contrary, using credit-based insurance scoring leads to more accurate placement and pricing of risks reflective of their potential for future insurance loss and, therefore, facilitates greater availability. The more accurate the insurer's ability to assess risk, the greater that insurer's ability to market its product and price it appropriately. Increased accuracy in underwriting and rating afforded by insurance scoring will enable some insurers, including niche writers, to identify good risks previously thought to be uninsurable.

State Farm recognizes that the use of credit information causes prices to be higher for certain individuals. At the same time our understanding is that the majority of consumers either experience lower prices or are not impacted by the use of credit information. If insurers are permitted to charge more accurate premiums that are more aligned with the risk and expected cost, then coverage will be made more available to consumers. It should be noted that the spread in rates among credit score groups is less than for some other rate factors, such as age of the driver, in those jurisdictions where the use of credit information is permissible in auto insurance.

Further, it must be stressed that many consumers could see their rates go up if insurance scoring is prohibited.

The issues paper mentions a concern that the use of credit scores as a risk factor "may cause too much of a difference in the premiums charged to the most and the least desirable policyholders". We believe that any such concern is unfounded. Desirability of policyholders is not at issue when assessing credit information; rather, only insurance risk is at issue. Further, premium differentials established through actuarially-justified pricing practices (using predictive factors such as credit scores) is justified on the grounds of cost-based pricing, and should not be arbitrarily classified as "too much" based on some unstated thresholds of what constitutes "too much" of a differential.

5.4 Insufficient disclosure

We do not believe that insurers should have an obligation to inform consumers how to modify their behaviour to get lower rates. Insurers assess potential risks presented to them on the basis of confidential proprietary models, and they should not be required to counsel consumers on which factors in a model caused rates to be higher than they otherwise would be.

As mentioned in the issues paper, consumer reporting laws in some provinces require anyone using credit information to deny a benefit (or increase the cost of a benefit) to notify the affected individual of certain information. This existing legislation serves to allow consumers to update or correct inaccurate or missing credit information, assess the elements of their credit information, and be aware of what elements of that information are susceptible to improvement, without posing any risk to the proprietary trade secrets of insurers. While we are not confident that it is actually a substantial risk, the possible risk of consumers not having sufficient information about their credit performance and financial health is addressed through this legislation.

5.5 Undue impact on certain groups

Based on our experience, we do not believe that there is a potential risk that insurers may unduly penalize those who do not consent or do not have a credit history. Charging rates that reflect risks is not a penalty and does not amount to a process of applying "hefty surcharges".

As well, when consumers demonstrate that extraordinary life events (such as a divorce or job loss) have caused adverse information on credit reports, insurers can institute procedures to ensure that policyholders are treated neutrally or their credit information is not used to underwrite or rate policies. State Farm has had a procedure in place since it began using credit information to deal with situations of this type.

We strongly believe that insurers who use insurance scores should be permitted to not quote, rate or accept applicants who do not permit access to the appropriate credit information. There is a legitimate concern that high-risk consumers would otherwise withhold consent in order to receive a premium rate which is lower than what it would otherwise be , thus requiring other consumers to pay more than their fair share for their insurance coverage.

5.6 Privacy breaches

We appreciate the high level of expectations that exists around protecting our customers' personal credit information. The risk of privacy breaches in connection with credit information is generally no different in principle from that risk in connection with other types of personal information, and we agree with the CCIR that this risk is adequately addressed under existing Canadian privacy laws.

5.7 Lack of understanding

We believe that when properly understood, the public generally accepts the use of credit scoring. For example, an Oregon ballot measure in 2006 prohibiting the use of credit scores in insurance was defeated by a nearly 3-to-1 margin when the public understood insurance industry arguments pointing out that rates for lower risk insureds would have to increase to subsidize rates for higher risk insureds, identifiable only by the use of credit.

We believe that all stakeholders in the insurance industry, including insurers, intermediaries, industry associations and insurance regulators, should work together on ensuring that steps are taken to better improve consumers' understanding of how credit information is used by insurers and how it increases the overall affordability and accessibility of insurance. Although it is certainly a desirable outcome, it is not possible to ensure that all consumers have a good understanding of this matter, as some may choose not to do so. Clear, objective and unbiased information and tools should be made available in order to facilitate improved consumer understanding.

Conclusion

In summary, State Farm believes that the use of credit-based insurance scores is beneficial for consumers:

- Many consumers pay less because of their insurance score, and insurance coverage is more available in the marketplace.
- Consumers have more choices, because different insurers use credit information in different ways. If one insurer applies scores in a way that is disadvantageous to a particular consumer, that consumer can shop with other insurers and find one whose rating plan is more advantageous for that consumer's own individual situation.
- Consumers are treated objectively and fairly.
- Lower-risk consumers are not forced to pay more for insurance, so that higher-risk consumers can pay less than their fair share for insurance coverage.

While some of the risks raised in the CCIR paper do exist, we believe that those risks are substantially addressed by existing legislation. In those Canadian jurisdictions where the use of credit for insurance rating purposes is currently prohibited for certain classes of insurance, an unintended and harmful consequence affects the majority of consumers, in the form of increased insurance rates.

If you would like further information about any of the matters set out in this letter, please feel free to contact Peter Hanycz at 519 649 3805.

Sincerely,

Barbara Bellissimo

Barbara Bellissimo
Chief Agent and Senior Vice President



Written Submission to the Canadian Council of Insurance Regulators Credit Scoring Working Group

Monday, August 8, 2011

the co-operators®
A Better Place For You®

The Co-operators is pleased to provide comments to CCIR's issues paper "*Use of Credit Scores by Insurers"*, and insight into our experiences and policies regarding the use of credit score as a rating factor for home, auto and farm insurance.

Our submission hopes to address CCIR's concerns that particular use and misuse of credit scores could impede marketplace outcomes such as:

- Fair treatment of consumers;
- Disclosure of information to enable consumers to make informed choices;
- Compliance with the law; and
- Good corporate governance.

In 2007 The Co-operators subsidiary L'Union Canadienne introduced credit score as a rating factor for home and auto in Quebec where it is widely used and accepted. Co-operators General Insurance Company and HB Group Insurance began implementing credit score as a rating factor for home and farm insurance in 2009. Although it had become common practice in the Canadian insurance industry since 2001, it was new to The Co-operators and our clients outside the province of Quebec.

As many other insurance companies had implemented its use, The Co-operators determined that failure to do so would not allow us to ascertain the most fair and accurate premiums for our clients. An anti-selection environment was apparent: clients with substantially lower loss costs were subsidizing those with higher loss costs (unfavourable credit score).

The value of credit score has been demonstrated as a useful and accurate predictor of future claims for property insurance. It is another rating factor used in addition to other traditional factors - such as claims history, age of home, and geographic location - to determine the level of risk and the appropriate premium.

We only use credit score for rating of our property and farm insurance portfolios, except in Quebec where its use is also permitted for auto insurance.

About The Co-operators

The Co-operators is a group of Canadian companies focusing on insurance. As a co-operative, our 45 member owners include co-operatives and credit union centrals representing a combined membership of millions of Canadians.

We are a partial member of the Insurance Bureau of Canada (for reporting purposes only) as we prefer to contribute to the policy development process independently. We are a co-operative as well as an insurance company and believe that we bring a uniquely Canadian and co-operative perspective to public policy consultations.

In 2011, The Co-operators was ranked #1 among the 50 Best Corporate Citizens in Canada by Corporate Knights and has just been chosen as one of Canada's "Green 30" employers for a second consecutive year.

As a national company, The Co-operators supports numerous organizations that focus primarily on education, youth, health, environment, and safety. We are strong believers in community

involvement and across the country our staff members contribute their time and energy in their individual communities. In 2010, $5.7 million dollars was contributed towards the betterment of Canadian communities.

❖ ❖ ❖

In its paper, CCIR noted several potential risks to consumers as a result of the use of credit-based insurance scores:

1. **Inadequate consent;**
2. **Unreliable credit data;**
3. **Availability and affordability of insurance;**
4. **Insufficient disclosure;**
5. **Undue impact on certain groups;**
6. **Privacy breaches; and**
7. **Lack of understanding.**

The following is a summary of observations, experiences, and recommendations we hope will provide CCIR with a better insight into all potential risks identified.

1. Inadequate Consent

CCIR noted that some consumers may not know that they have given permission to an insurer to use their credit score information or a credit score for determining a consumer's eligibility for insurance and the premium to be charged.

Prior to using the information, insurers should ask consumers for their permission and help them understand the type of information the insurer is seeking to obtain, including how the insurer intends to use the information.

We understand that clients view their credit score as sensitive and personal information. Therefore, we obtain explicit consent to check the credit score of every home and farm insurance client as part of the application process. We also notify all new clients of our need to collect personal information as part of our Disclosure and Privacy statement.

To alert and educate clients when we began implementing the use of credit score as a rating factor outside Quebec in 2009, we sent letters to each of our group home clients, and sent bill inserts and newsletters to notify our individual home and farm clients.

We also created an entire section on our website dedicated to credit score and any questions a client may have www.cooperators.ca/en/Insurance/home).

If clients or applicants tell us they do not want us to access their credit score, we respect their wishes. However, we will not be able to provide an accurate or competitive premium that reflects

the risk we are insuring. As a result, a client may not receive the best possible premium available. The Co-operators will not refuse to provide a quote or coverage if a consumer withholds permission to check their credit score.

2. Unreliable Credit Data

As noted in the CCIR paper, a study was conducted by the Public Interest Advocacy Centre (PIAC), which found that 18% of people surveyed discovered some type of error in their report. Most of the errors had only a small impact on their overall score and would have very little, if any, impact on their insurance premiums.

Credit reporting agency scores are based on the accuracy of the information collected from many other institutions, however, it is up to individual consumers to ensure the accuracy of their credit information.

Upon request from the consumer, credit reporting agencies must provide (by law and at no cost to the consumer) a complete account of all information on a consumer's credit report (a "Consumer Disclosure").

Consumers can then address any issues that may have led to an inaccurate credit score calculation. However, there is a cost to the consumer to obtain their credit score as it is not included with the report.

If all the information is correct on the report, and the consumer does not want to pay to obtain their score, they could expect their score to be accurate since it is based on the information contained in the report.

3. Availability and Affordability of Insurance

The Co-operators philosophy regarding the delivery of our insurance products is based on the following fundamental guiding principles:

- **Security:** At its most basic level, insurance provides peace of mind. Consumers should have adequate coverage that ensures an appropriate measure of financial protection.
- **Affordability:** Insurance must be affordable.
- **Availability:** Insurance consumers have the right to expect reasonable access to a variety of providers who can meet their coverage needs.
- **Simplicity:** Insurance consumers have a right to understand the product they are purchasing and the benefits to which they are entitled.

Currently 66% of Co-operators clients enjoy lower home insurance rates because of their credit score. A further 6% of our clients do not see any impact at all to their rates. The removal of credit scoring as a rating tool would result in increased premiums for the majority of our clients.

The Co-operators does not use credit score to deny quotes or cancel/deny coverage. We do not use credit score to underwrite, rate or cancel coverage in a product line or jurisdiction where this is prohibited. In all situations where credit score is used for rating, The Co-operators obtains explicit consent from clients and prospects.

While we understand and share the desire to provide an affordable product for our clients and the importance of sharing risk, we believe that those clients who pose a lower risk should have insurance rates reflective of that fact. Credit score is a tool that allows us to individualize coverage for our clients in this manner.

4. Insufficient Disclosure

The report notes that consumers may not have sufficient information on how to modify their behaviour in order to reduce insurance costs. In our view, it is in the consumers' best interest to be aware that credit score is being used as a rating variable; the details of how it is applied in our rating methodology are not crucial. Consumers are empowered by being aware that their credit score affects rates and understanding how they can check, correct if necessary, and improve their individual credit scores.

As part of our education process with clients, we encourage them to request a copy of their credit report from a credit reporting agency at least once per year to verify that their personal information is up-to-date, that their financial information is correct, and to ensure they have not been a victim of identity theft. They can also request a "Consumer Disclosure" which is a complete copy of their information, including all soft inquires by mail.

For a consumer, knowing how to manage their credit score is important for more than just insurance. Credit scores are far more critical to what they pay for their mortgage or car loans. It influences their ability to rent or acquire a cellular phone plan. It can even affect their ability to obtain a job.

Consequently, information abounds on how to manage your credit score. While the use of credit score is relatively new to the insurance industry, it is a long-established practice in other industries and consequently, information on how to manage your credit rating as a consumer abounds if you choose to look for it.

5. Undue Impact on Certain Groups

Credit score is simply a reflection of a person's level of responsibility and behaviour when it comes to managing their financial obligations. The connection to insurance is that those who manage their finances responsibly tend to demonstrate the same level of responsibility with their home and deserve to pay less for their insurance as a result.

We believe the use of credit score to measure a person's risk related to home, farm, auto and other personal property insurance is an appropriate and ethical practice. It has been in wide use across

Canada (including other industries) as a rating tool for many years. For example, financial institutions have long used credit score to determine lending practices and what a consumer pays for a mortgage or loan.

A British Columbia Privacy Commissioner's Office decision dated May 6, 2011, explains that credit score is proven to be a predictive tool, its use is reasonable, and attempts to apply findings of U.S. studies to our Canadian environment are mistaken. Our regulatory structure is markedly different from that of the U.S. In Canada, our residents are protected by our Human Rights Codes, privacy legislation, as well as regulatory regimes at the federal and provincial levels.

Some opponents of the use of credit scoring as an insurance rating vehicle have claimed – without backing the statement up with relevant facts – that seniors, low income earners, and new immigrants to Canada are not as responsible as the rest of the homeowner population, have lower credit scores as a group and therefore will be required to pay more for their home insurance if credit score is used. These claims are not supported by any research that we are aware of.

Before The Co-operators introduced credit score as a rating factor, we conducted extensive research. We wanted to confirm ourselves that this was valid and non-discriminatory. For example, to determine whether credit scores correlate with incomes, we used aggregate census data to compare high and low income neighbourhoods, using postal codes with credit score data. The average credit scores at all income levels were very similar, to the extent that they would not result in different premiums charged.

We were aware of the existence of US-based studies on credit score and we conducted similar studies to determine whether there were links between credit scores and business ownership or age. In both cases, we found no meaningful correlation.

In addition, we examined our loss experiences from 2006 to 2009 to determine whether there was evidence to demonstrate a link between credit score and losses. What we found was that the top quartile of our homeowner client base when segmented by credit score represented only 18% of claims dollars, whereas the bottom quartile represented 38% of claims dollars. The frequency of large losses was over three times greater for clients with a low credit score than those with an excellent credit score. This is much like the delinquency rates for excellent credit score vs. low scores. As a result of the research we believed that the use of credit score as a predicator was valid and non discriminatory and therefore implemented it as a rating factor nationally in 2009.

Moreover, some individuals (e.g. young adults) may not have a credit score due to a lack of credit history. If this is the case of an applicant, we will not apply a credit score rating factor to their home insurance premium. This means there will be no impact (up or down) on the premium.

6. Privacy Breaches

The Co-operators is committed to protecting the privacy, confidentiality, accuracy and security of the personal information we collect, use, retain and disclose in the course of conducting business – including the collection and use of our clients' credit scores.

The information we exchange with TransUnion travels through a secure data transmission channel. The data is encrypted in the system and is not accessible nor visible through general data sources. Specific and secure sources provide limited access to areas that require it. Therefore, a client's credit score is not visible to the vast majority in our offices and is automatically applied to the calculation of the home premium. We enforce a strict set of policies regarding confidentiality and the use of personal information.

7. Lack of Understanding

The Co-operators group of companies is in full agreement that there needs to be transparency in the use of credit scoring as a rating tool and that more needs to be done to educate consumers.

Co-operators agents are career agents who sell our multi-line products. We already have our own processes and practices in place dealing with client education. A recent CCIR audit confirms the rigorous nature of our internal controls.

A "needs analysis" is an important component of a client's visit to a Co-operators agent to purchase any of our Life & Wealth products. In addition, as part of our client service standards, we have a requirement to review all clients' coverages every three years; or more often if their circumstances change.

We also have an extensive section about credit score on our website: www.cooperators.ca/en/Insurance/home. We are not aware of any other company in Canada that has gone to these lengths to notify and educate clients about the use of credit score for home insurance.

Conclusion

We believe the use of credit score for insurance purposes is an appropriate and ethical practice under appropriate regulations and enforcement. We encourage regulators to continue – and even expand – the use of credit scores under clear regulations that create a level playing field for all insurers.

Although we are partial members of the Insurance Bureau of Canada (IBC) for reporting purposes only, we fully support the *IBC Code of Conduct for Insurers' use of Credit Information* which provides clear guidelines based on fundamental principles of consumer protection and applicable federal and provincial law to those insurers who use credit information as part of their underwriting activities.

The Co-operators group of companies would like to thank the Canadian Council of Insurance Regulators for providing an opportunity to participate in the consultation and to provide comments on the Credit Scoring Working Group's issues paper: *Use of Credit Scores by Insurers.*

As an organization, The Co-operators group of companies takes great pride in its open dialogue and regular communication with all stakeholders. We welcome the opportunity to have further discussion with the CCIR.

Independent of IBC, we remain committed to working directly and collaboratively with government to offer a unique voice for the Canadian policyholder to ensure that each insurance jurisdiction delivers products that provide security, are accessible, affordable, and easy to understand.

Sincerely,



George Hardy
Vice President, Personal Lines and Underwriting
The Co-operators

Saveria Villanti

From: Bob Gibson/EIG <Bob.Gibson@teig.com>
Sent: August-05-11 1:25 PM
To: CCIR-CCRRA
Cc: Catherine Coulson/EIG; Jorge Arruda/EIG
Subject: CCIR - Issues Paper - Use of Credit Scores by Insurers

Attention: CCIR Secretariate

Economical Insurance has reviewed the Discussion Paper on Credit Scoring and feel that you have identified all the potential risks.

We also feel that the potential risks identified are already addressed under law.

Sincerely,

Bob Gibson **BA, FCIP**
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TransUnion

August 14, 2011

The Canadian Council of Insurance Regulators Secretariat
5160 Yonge Street, Box 85
Toronto, Ontario
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On behalf of TransUnion, the following is our response to the Canadian Council of Insurance Regulators' (CCIR) Issues Paper – *Use of Credit Scores by Insurers.* We appreciate the opportunity to provide input on the CCIR's review.

About TransUnion

Trans Union is a multinational credit information management company that creates advantages for millions of people across the globe by gathering, analyzing and delivering information. For businesses, TransUnion creates efficiency, manages risk, reduces costs and increases revenue by delivering comprehensive data and advanced analytics. For consumers, TransUnion provides tools, resources and education to help manage credit health and achieve financial goals. Through this and other efforts, TransUnion works to build stronger economies and communities worldwide. TransUnion is governed by regulatory frameworks which exist federally and provincially across Canada, which touch all aspects of our business. TransUnion adheres strictly to these regulatory requirements.

Using Credit Information Provides Benefits to Consumers

Credit information has a diverse range of uses that provide benefits to consumers across numerous industries. It rewards consumers for responsible financial decisions and gives both consumers and businesses the power to achieve their respective financial goals. Credit information enables consumers to manage their financial decisions, their credit and protect themselves against fraud and identity theft. It allows businesses to better manage risk and customer relationships. Globally, 500 million consumers use TransUnion's services to put information to work for them.

One of our core businesses is to provide credit information to insurance companies for use in underwriting for insurance. This business is explicitly authorized as a permissible use of credit information by the legislation that regulates our activities in most of the provinces across Canada. [1]

[1] Alberta *Fair Trading Act* Section 44(1)(iv)
British Columbia *Business Practices and Consumer Protection Act* Section 108(1)(iv)
Manitoba *Personal Investigations Act* Section 5(b)
Nova Scotia *Consumer Reporting Act* Section 9(1)(c)(iv)
Ontario *Consumer Reporting Act* Section 8(1)(d)(iv)
Saskatchewan *Credit Reporting Act* Section 17(1)(a)(i)(iv)
Prince Edward Island *Consumer Reporting Act* Section 8(1)(d)(iv)

Our insurance company clients have consistently told us that a strong correlation exists between credit history and likelihood of submitting a claim on a home insurance policy. Specifically, insurance companies have demonstrated that persons with good credit histories or scores are less likely to submit claims. Further, those with good credit scores are likely to submit smaller claims when claims are actually submitted.

As a result, insurance companies offer lower premiums to those with good credit histories and scores. As the paper notes, the Financial Consumer Agency of Canada (FCAC) estimates that about 75% of Canadians have a good or average credit score. Based on this we can expect that most Canadians are actually benefitting from the use of credit information in insurance in the form of receiving lower premiums than they would otherwise receive if credit information was not used in determining rates.

We believe that the use of credit reports and scores in the insurance industry offers many positive benefits to Canadian consumers. These include the following:

- Fairness: Credit reports and scores are so highly correlated to loss ratios and claims frequency and therefore, insurers are able to price premiums more fairly. Further, credit reports contain no demographic information on race, ethnicity or religion.
- A Competitive Marketplace: The use of credit reports and scores is scalable, allowing smaller insurance providers to enter markets.
- Transparency: Offering all individuals rights of access and correction. Provincial credit reporting laws, and the Code of Conduct, described below, provide individuals with a robust set of consumer protections, including rights to notice of adverse actions, access and dispute, and correction of information, etc.
- Accuracy: Credit reports are in fact more accurate than most drivers' history databases. As discussed in greater detail below, credit reports have a high degree of accuracy and the use of credit scores based on credit report information has proven to be highly predictive of consumer behaviour.

At the same time, we recognize the importance of insuring that a strong framework is in place to provide transparency and to mitigate against unfair outcomes. We therefore fully support the CCIR's intended outcomes with regard to fair treatment of consumers, openness and industry-wide best practices. We believe that with a proper framework, consumers with strong credit histories can continue to benefit from the use of credit information while ensuring that these basic principles are protected and promoted.

With this objective in mind, there are several areas where we would like to provide additional information and clarification in order to better support the CCIR's review and recommendations.

Insurance Bureau of Canada (IBC) Code of Conduct

In 2008 the Insurance Bureau of Canada developed a Code of Conduct for Insurers' Use of Credit Information (Code).

TransUnion was consulted as part of the development of this Code and strongly supports its use within the insurance industry as a means of promoting fair treatment of consumers, transparency, openness and choice. More specifically, the Code addresses all of the public policy issues identified in the CCIR paper. Highlighted below are the core issues and the relevant provisions of the Code.

Consent

Element 3 of the Code requires insurers to obtain consumer consent prior to the collection and use of credit information. Element 3 requires the consent to be informed, clear and explicit. It also requires that the insurer explicitly indicate that a consumer has a right to withdraw their consent at any time. TransUnion

also has stringent requirements governing consent from its data suppliers and its customers, prior to ever doing business with them.

Reliability of Credit Data

Element 2 of the Code requires that insurers only use accurate and up-to-date credit data. This is consistent with legislative provisions across Canada[2] which require credit reporting agencies including TransUnion to maintain accurate records.

Availability and Affordability of Insurance

Element 5 of the Code states that insurers must not refuse to quote or base an insured person's renewal rates nor deny, cancel or non-renew a policy of personal insurance solely on the basis of credit information. This ensures that those Canadians with a poor credit history do not face the prospect of being unable to obtain or afford insurance coverage solely as a result of a poor credit history. Further, all individuals have an opportunity to review their credit reports, to dispute information, and to obtain correction of any information that is inaccurate or incomplete.

Insufficient Disclosure

Element 8(b) of the Code of Conduct addresses this concern. Under 8(b) an insurer must disclose to the consumer adverse action taken only as a result of credit information. This notification should include information on how to contact the appropriate credit reporting agency to review their credit information.

Undue Impact on Certain Groups

Element 8(a) indicates that a consumer with an absence of credit information shall not be denied coverage, cancelled or non-renewed a policy of insurance solely based on the absence of credit information. It also requires rating decisions to be based only on the information that is available to the insurer meaning that rates cannot increase solely because a person has no credit information.

Element 10 further protects consumers by requiring that, upon request, insurers must consider undue life circumstances as a mitigating reason for a poor credit score.

Element 9 of the Code ensures that consumers are free to refuse their consent to access credit information. Specifically Element 9 states: "The insurer shall not refuse to provide an insurance quote to the customer, nor refuse to insure a customer, nor terminate or refuse to renew a policy because the customer refuses to give consent to use their credit information. In this situation the customer will be offered a competitive rate, but may not qualify for related discounts or the insurers' best quote."

Making the Code Mandatory

The paper notes that the Code of Conduct is voluntary, however TransUnion believes that virtually all insurers who are using credit information have now publicly indicated that they have agreed to adopt the

[2] Alberta *Fair Trading Act* Section 45(1)
Nova Scotia *Consumer Reporting Act* Section 10(1)
Ontario *Consumer Reporting Act* Section 9(1)
Saskatchewan *Credit Reporting Act* Section 16
Prince Edward Island *Consumer Reporting Act* Section 9(1)
Quebec *Act respecting the protection of personal information in the private sector* Section 71

Code. If the concern of regulators is that the Code is voluntary, TransUnion recommends that regulators require insurers to follow the Code as a condition of doing business in the province.

Existing Legislative Framework

The existing legislative framework in Canada already addresses many of the issues raised in the Issues Paper. Specifically, the large majority of provinces have legislation regulating consumer reporting agencies including TransUnion, as well as specific regulators who monitor and enforce our compliance with the legislation. In addition, TransUnion and its customers are governed by *PIPEDA* and/or similar provincial privacy legislation.

Disclosure of Information

Through *PIPEDA*, we are required to provide consumers with access to their information, the ability to correct it, and to provide a dispute mechanism. TransUnion provides credit reports to individuals free of charge, by written, phone or in person requests. When an individual disputes the accuracy of information contained in a credit report, that individual can initiate an investigation through our dispute mechanism.

Informed Consent

The CCIR Issues Paper identified issues with regard to consumer consent to access credit information.

Insurers who utilize credit information for the purpose of determining insurance rates are bound by *PIPEDA* and similar privacy legislation to obtain the express written or oral consent of a consumer prior to accessing said information. Moreover, under *PIPEDA*, insurers cannot demand as a condition of providing insurance that a consumer consent to collection of this information.

TransUnion concurs with the CCIR on the importance of disclosure of information to consumers so that they can make informed choices. We are offering to work with the IBC and insurers to ensure that consumers better understand their existing rights and obligations regarding consent.

Adverse Action

The CCIR Issues Paper has suggested that consumers do not understand how to correct their insurance score if they are indeed a bad credit risk. Several Canadian provinces include what is called an *adverse action remedy* within consumer reporting legislation. These include: British Columbia, Saskatchewan, Manitoba, Ontario, Nova Scotia and Prince Edward Island.

Where these laws exist, when a benefit is denied to a consumer or an increase occurs either wholly or in part because of information provided by a consumer reporting agency, the individual (in this case the insurer) is required by law to inform the consumer within a set time period.

If contacted by the consumer, TransUnion is then required by law to provide information regarding how they can review their credit file and correct it if necessary. Furthermore, these same rights and obligations are included in the IBC Code of Conduct.

TransUnion recognizes that consumers must be aware of this and we are committed to working with our clients in the insurance industry to ensure that the broader public is fully educated on these procedures and the steps available to them to correct or improve their score.

Comments on Specific Issues Raised in the Paper

Reliability of Data

The reliability of TransUnion's data is beyond repute. Our own internal statistics, as well as that of our regulators and customers and independent research, all confirm that TransUnion's data is accurate, reliable and up-to-date.

TransUnion's own internal data demonstrates the accuracy of our information. During the two-year period ending December 2010, TransUnion delivered over 47 million online consumer credit files to business clients. Of these 47 million files delivered only 143,426 or 0.003% resulted in a Consumer Investigation Request. It is important to note that these requests do not necessarily represent a dispute or an inaccuracy; it simply means that these people requested an investigation.

This small percentage of concern is consistent with a recent independent, peer-reviewed study undertaken in the United States by the Policy and Economic Research Council (PERC). To undertake the study PERC randomly engaged consumers to examine thousands of credit report entries to identify potential inaccuracies, file disputes and openly discuss their satisfaction with the result.

The study, which was undertaken between February and May of 2011 found that less than 1% of credit reports have errors that would adversely impact consumers. It also found that 95% of all consumers who participated in the dispute process were satisfied with the outcome. Overall the study concluded that the vast majority of credit reports are accurate and that it was extremely rare (less than 1%) for a credit report error to materially impact a consumer's access to credit. A copy of the PERC study can be found at: http://www.transunion.com/corporate/aboutUs/CRStudies/Efficacy.page

The experience of our regulators also confirms that our reports are accurate. Our regulatory framework requires TransUnion to maintain accurate and up-to-date reports.[3] Any individual that feels we are not meeting these commitments can make a complaint to the relevant provincial regulator.

TransUnion is also required through *PIPEDA* to ensure the relevance of its data.

Perhaps the best evidence of the accuracy of our credit reports is supported by who are customers are and what they use the reports for. Most of the major banks, credit unions, credit card issuers, financial institutions and insurance companies in Canada access and use TransUnion credit reports for their day-to-day risk, pricing, collections and general business needs. With the consent of consumers, TransUnion's clients use credit reports to make decisions on extending and managing hundreds of billions of dollars in credit and services. Given the amount of money at stake our clients would not use our services if they were not completely satisfied in the accuracy of the information.

[3] Alberta *Fair Trading Act* Section 45(1)
Nova Scotia *Consumer Reporting Act* Section 10(1)
Ontario *Consumer Reporting Act* Section 9(1)
Saskatchewan *Credit Reporting Act* Section 16
Prince Edward Island *Consumer Reporting Act* Section 9(1)
Quebec *Act respecting the protection of personal information in the private sector* Section 71

Public Interest Advocacy Centre

The CCIR Issues Paper referenced a Public Interest Advocacy Centre (PIAC) study that claimed an unrealistically high percentage of inaccuracies in credit files. The rate claimed by PIAC is not at all consistent with the experience of other third-party studies, our own internal statistics, our regulators' experience or our customers' experience.

We feel that there are a number of significant shortcomings associated with the PIAC study that lead to this discrepancy, particularly compared to the research study undertaken by PERC. Some of these discrepancies include:

- Random Sample Versus Non-Random Sample

  The PERC study randomly selected consumers to participate in a study whereby they would review entries on their actual credit report. This produces a random and representative sample of the population. In the PIAC study the only people who were participants in the study were people who had indicated that they had checked their credit rating in the past three years, which PIAC admitted was only 17% of their respondents. By definition this would not be a representative sampling, in fact TransUnion would argue that the very fact that the only people surveyed for accuracy were those individuals who had checked their credit information would create an inherent bias because one of the reasons that people may check their credit report is that they are concerned that there may be an inaccuracy.

- Reported Errors Were Unverified

  Another key shortcoming of the PIAC report was that it simply asked respondents if their credit report was accurate. There was no actual confirmation that the credit information was inaccurate. In the PERC case consumers were asked to review actual credit entries, which were then tested for accuracy. In this way recording of actual inaccuracies was verified by the PERC study, as opposed to the PIAC study which simply relied on the response of the interviewee, without testing the accuracy of their response. Often consumers may believe an entry on their file is inaccurate when in fact it is accurate. One of the best examples of this is if a person signs a joint application for a credit card with another person. Even if the other person is the primary user of the credit card both signees are ultimately responsible for the debt. In this instance the report would be accurate; however, the consumer may not have understood the legal obligations that they signed for when applying for the credit card.

- Sample Size

  The PIAC study surveyed only 526 people about the accuracy of their credit rating. This is a small sample size and therefore translates to a greater margin of error. By comparison, the PERC study was far more robust, reviewing over 3,000 credit entries involving over 2,000 consumers, representing a study larger by a factor of 4.

- Material Errors

  The PIAC study simply asked respondents if there was an error on their credit report. It did not seek to understand if this error was one that would impact their credit or insurance score or whether it was

simply a typographical error; something as minor as neglecting to record a previous address, thereby not reflecting that a person had moved. The PIAC study found that 9% of people claimed inaccurate information, without bothering to ascertain if the error was at all material and therefore impacting on their credit or insurance score. By comparison, the PERC study found a less than 1% error rate that would materially impact a credit or insurance score. This would imply that most of the errors reported to PIAC were non-material, as identified above, because the errors reported in the PERC study were unverified, we do not believe the 9% figure is accurate even if all errors are included.

Use of Credit-Based Insurance Scores

As a point of clarity, TransUnion does not offer credit-based insurance scores to its Canadian customers. As the CCIR Issues Paper suggested that credit-based insurance scores are being used in Canada, we felt it important to clarify that, while we offer credit-based insurance scores in the United States, we have not been able to develop these in Canada because we do not have access to insurance claims data. It is our understanding that insurers take credit information and scores and combine them with insurance data to generate an insurance score internally.

TransUnion would welcome the opportunity to develop credit-based insurance scores for the Canadian marketplace. Within the United States, where Insurance Risk Scores are offered as a product, TransUnion's Insurance Risk product was designed to be entirely transparent at all levels – ensuring that both agents who use the score and the consumers impacted by them clearly understand their impact. The characteristics and algorithms used to develop the score are available on request to provide greater understanding of the factors that affect it. Moreover, like a credit score they are based solely on objective, factual, accurate credit report information and do not include information about income, age, race, marital status, religion, disability or gender.

Having said this, these two products are not interchangeable. Insurance scores predict claims loss ratios and were developed for insurance customers seeking a transparent, objective and accurate predictor of consumer risk. We strongly believe that an opportunity exists in Canada to improve transparency for individual consumers, and predictive performance for insurers, through development and implementation of credit-based insurance scores.

Conclusion

We believe in and are hopeful that the consultation will result in a solution that sees all provinces developing a framework governing the use of credit scores in insurance. This will allow the majority of Canadian consumers who have good credit histories to benefit from lower premiums and also guide insurance companies on the proper use of this information. We believe this can best be achieved by implementing the IBC Code of Conduct, and the development and implementation of credit-based insurance scores for Canada. Implementing the IBC Code of Conduct as a regulatory model for all provinces would ensure that:

- Credit information used is accurate and current;
- Informed consent is understood and employed at all times when collecting and using credit information;
- Credit information is not used as the only factor in determining insurance score;
- Customers are informed when they are denied or given a benefit as a result of their score;
- Consumers are not denied insurance as a result of a negative score; and
- Extraordinary life circumstances are factored in decisions regarding insurance quotes.

At the same time we believe that the Issues Paper has identified some areas where TransUnion, in conjunction with insurance companies and Governments, can do a better job. Specifically, educating

consumers about their rights and obligations regarding the use of credit information can be improved to ensure that consumers understand what they are consenting to. Further consumers need to understand what actions they can take to maintain a good credit score or improve their credit score. Finally consumers need to better understand how credit information is used in insurance. The vast majority of Canadians likely benefit from the use of credit information in insurance pricing. It is important that consumers understand how this works and how they are benefitting.

Again, thank you for the opportunity to provide input on the CCIR's review. TransUnion is open to being an active participant in the CCIR process and as such we are available to you and your offices should you require any additional information.



Ken Porter
President