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OFIR Disapproves Auto Rates Based on Credit Scoring

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LANSING – The Office of Financial and Insurance Regulation (OFIR) announced today that it has started disapproving insurance rate filings made by automobile insurance companies that use insurance credit scoring as a factor in determining their premiums. OFIR Commissioner Ken Ross has determined that premiums developed using insurance credit scoring are unfairly discriminatory and do not meet the requirements of Michigan's Insurance Code.

In 2005, OFIR promulgated rules banning the use of insurance credit scoring. The insurance industry challenged the rules and the issue has been working its way through the legal system for the last four years. The issue is currently before the Michigan Supreme Court.

"Michigan consumers expect insurance companies to follow the law," Ross said. "Rates filed with the agency are being evaluated carefully, on a case by case basis, to ensure they fully comply with Michigan law."

OFIR has already disapproved seven rate filings that use credit scoring as a rating factor because the filings did not meet the requirements of chapters 24 and 26 of the Insurance Code, which state that rates shall not be "unfairly discriminatory." Ross determined that the rates were unfairly discriminatory because they were based on insurance scoring which depends on information that is unreliable.

Credit information has been found to contain such a high rate of errors that there is an unacceptable likelihood that persons will be misclassified. Insurance scoring discounts are not based on a reasonable classification system and sound actuarial principles.

Insurance credit scoring relies on behavior, including debt and bill payment history that is unrelated to the risk presented when purchasing an auto insurance policy. Instead of basing auto insurance premiums on factors such as a consumer's driving record and experience, many insurers place huge weight on how high a credit score is, because statistics tell them that those with great credit file fewer claims.

During OFIR's hearings on the proposed rule to ban credit scoring, an insurance agent testified that he was able to get big discounts for a customer with "gold credit" even though the customer had a driving while intoxicated on his record. The agent was hard pressed to explain to another customer with a clean driving record, but blemished credit, why she was going to see increases in her premium.

OFIR has had the option of disapproving rates under consideration and last month Governor Granholm issued Executive Directive No. 2009 – 1, that directed OFIR to utilize every administrative tool at the agency's disposal to assure that the auto insurance company provides insurance at fair and equitable rates, including, but not limited to disapproval of rate increases or rejection of rate filings.

To read the entire Executive Directive, visit: <http://www.michigan.gov/gov/0,1607,7-168-36898-208124--,00.html>

A fact sheet on the credit scoring issue is below.

Credit Scoring Fact Sheet

Errors in Credit Scoring:

A number of studies have shown that credit information has been found to contain such a high rate of errors that there is an unacceptable likelihood that persons will be misclassified.

U.S. PIRG's *Mistakes Do Happen: Credit Reports Errors Mean Consumers Lose*, found that:

- 29% of the credit reports contained serious errors - false delinquencies or accounts that did not belong to the consumer - that could result in the denial of credit;
- 41% of the credit reports contained personal demographic identifying information that was misspelled, long-outdated, belonged to a stranger, or was otherwise incorrect;
- 20% of the credit reports were missing major credit, loan, mortgage, or other consumer accounts that demonstrate the creditworthiness of the consumer;
- 26% of the credit reports contained credit accounts that had been closed by the consumer but incorrectly remained listed as open;
- 70% of the credit reports contained either serious errors or other mistakes of some kind.

Consumer Federation of America's, *Credit Score Accuracy and Implications for Consumers*, found that:

Tens of millions of consumers are at risk of being penalized for incorrect information in their credit report

- Almost one in ten consumers run the risk of being excluded from the credit marketplace altogether because of incomplete records, duplicate files, and mixed files.

Rate Setting and Michigan Insurance Code:

According to Michigan Comp. Laws § 500.2403 and § 500.2603:

(d) Rates shall not be excessive, inadequate, or unfairly discriminatory.

[http://www.legislature.mi.gov/\(S\(y2fwdd45dyfezru4oea1ak55\)\)/mileg.aspx?page=getObject&objectName=mcl-500-2403](http://www.legislature.mi.gov/(S(y2fwdd45dyfezru4oea1ak55))/mileg.aspx?page=getObject&objectName=mcl-500-2403)

[http://www.legislature.mi.gov/\(S\(y2fwdd45dyfezru4oea1ak55\)\)/mileg.aspx?page=getObject&objectName=mcl-500-2603](http://www.legislature.mi.gov/(S(y2fwdd45dyfezru4oea1ak55))/mileg.aspx?page=getObject&objectName=mcl-500-2603)

History of OFIR's Credit Scoring Legal Case:

In 2004, Governor Granholm and then-OFIR Commissioner Linda Watters proposed a new state rule to reduce base rates for all insurance customers by prohibiting the use of credit scoring in determining rates for homeowners and auto insurance sold in Michigan.

In March, 2005, after extensive public hearings across the state, the commissioner promulgated these rules. The Insurance Institute of Michigan, the Michigan Insurance Coalition, and several insurers challenged the rules in the Barry County Circuit Court.

In April, 2005, Judge James Fisher issued an opinion and order declaring the rules invalid and permanently enjoined the commissioner from enforcing them against any plaintiff in the action. Commissioner Watters immediately appealed Judge Fisher's decision to the Michigan Court of Appeals.

In August, 2008, the three Michigan Court of Appeals judges issued a split decision and three separate opinions. The common points among the three opinions resulted in the Court of Appeals vacating Circuit Judge Fisher's order and injunction and lifting the stay he had imposed on the enforcement of the rules. However, the stay continues in force as the Michigan Supreme Court is considering appeals.

On October 1, 2008, current Commissioner Ken Ross filed an application for leave to appeal and specifically asked the Michigan Supreme Court to rule that the insurance credit scoring rules are valid. On October 2, 2008, the insurance industry Plaintiffs filed an application for leave to appeal and specifically asked the Michigan Supreme Court to reverse the Court of Appeals and reinstate the order of Judge Fisher.

Both sides filed briefs in support of the applications, and each responded to the brief filed by the opposing party. The Michigan Supreme Court has taken no action yet on these counter applications for leave to appeal.

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