SB2208 Position: Proponent

Written Testimony of Tom Feltner, Director of Financial Services at the Consumer Federation of America

Before the Illinois Insurance Committee

May 5, 2016
Springfield, Illinois

Thank you Mr. Chairman and members of the Committee for the opportunity to express Consumer Federation of America's support for SB 2208 and other efforts to eliminate the harmful consequences of the use of credit score and other non-driving rating factors in setting auto insurance rates. My name is Tom Feltner and I am the director of financial services at CFA, a national organization of more than 250 nonprofit consumer groups that was founded in 1968 to advance the consumer interest through research, advocacy, and education.

CFA has researched auto insurance issues and advocated for fairness in the insurance market for over 20 years. We believe that when auto insurance is fairly priced, lower-income people can safely and affordably purchase, maintain and insure a car to get to the best job for which they are qualified.

We urge states to take immediate action to protect consumers from the unfair use of factors such as credit score, education, occupation and other factors unrelated to a driver's performance behind the wheel and outside the driver's control.

These factors strongly influence how auto insurance is priced and result in higher prices charged to lower-income drivers regardless of driving history and controlling for all other factors.

My testimony will focus on why we believe that auto insurance affordability is one of the most important economic development challenges faced by lower-wealth people. As part of this discussion, I would like to share the findings of CFA research that shows how drivers, particularly lower-income drivers are priced largely on socio-economic factors outside of their control rather than how they drive. These findings demonstrate the urgent need for reforms such as the prohibition on the use of credit score and other factors to set auto insurance rates.

We urge that you support SB 2208 and similar proposals to level the playing field for lower-income good drivers, increase the accessibility of auto insurance and reduce the incidence of uninsured motorists.

Low-wealth people need access to a car and affordable auto insurance

For most Americans, access to the best job for which one is qualified requires ownership of a car. As a result, car ownership among low- and moderate-income (LMI) households is high. According to a 2001 government survey, 65 percent of low-income households – or those making less than approximately $20,000 per year – and 86 percent of moderate-income households – or those making less than approximately $40,000 a year – own a car.

Without insurance, drivers face harsh penalties that do little to reduce the rate of uninsured motorists. In Illinois, drivers face high fines of up to $1,000 and suspension of their registration for three months.[1] CFA's research has shown that severe penalties have little impact on reducing the rate of uninsured motorists. Instead, our research suggests that there is a much stronger relationship between state poverty rates and the percentage of drivers without insurance.[2]

The use of credit score drives up rates in Chicago regardless of driver history

The use of credit scores by auto insurers to price policies has been a controversial issue over the past decade. Insurers argue that credit scores are correlated with claims frequency – the lower the credit score, the more frequent the claims – and can serve as a useful factor in their pricing of auto insurance policies. We reject this assumption since, even if there were a correlation between credit scores and claims, there is no plausible explanation as to why this is the case and having an explanation is central to classifying risk in a fair and responsible manner.[3] However, we do see a strong relationship between credit score and income, suggesting that, when used to set insurance rates, it results in higher prices for lower-income people.[4]

The severity of the rate hikes associated with credit scoring is staggering. For example, in 2013 CFA acquired data on insurance prices charged by the two largest auto insurers – State Farm and Allstate – for a 30-year old single woman with a good driving record (no accidents or moving violations) for the minimum required liability coverage (no collision or comprehensive coverage).

In the Chicago ZIP code tested as part of this study, Allstate Indemnity charged a driver with an excellent credit score $1,079 and a driver with a poor credit score $1,312 - $233 or a 22 percent increase. State Farm Mutual Auto charged a driver with an excellent credit score $341 and a driver with a poor credit score $761 – more than double (Figure 2).

The public is concerned about the use of credit score and other non-driving factors used to set insurance prices

When Americans are asked whether they think it is fair for auto insurers to use credit scores or other socio-economic factors in the pricing of auto insurance policies, a large majority say no.

In a 2009 survey commissioned by the Iowa Insurance Department that asked state residents whether people with poor credit scores should pay higher auto insurances rates, only 12 percent agreed while 65 percent disagreed.[5] When the Consumer Federation of America (CFA) commissioned a national survey in 2012 that asked a representative sample of more than 1,000 adult Americans whether they thought it

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[1] *Penalties for Driving without Auto Insurance by State*. Consumer Federation of America, January 2014. http://www.consumerfed.org/pdfs/140310_penaltiesfordrivingwithoutautoinsurance_cfa.pdf.

[2] Brobeck, Stephen, Michael Best, and Thomas Feltner. *Uninsured Drivers: A Societal Dilemma in Need of a Solution*. Washington, DC: Consumer Federation of America, March 2014. http://www.consumerfed.org/pdfs/140310_uninsureddriversasocialdilemma_cfa.pdf.

[3] Regarding the use of correlation by insurers, the American Academy of Actuaries "Risk Classification of Principles Statement" requires that there be the "existence of a plausible relationship between the characteristics of the class and the hazard insured against."

[4] Brobeck, Stephen, J. Robert Hunter, and Thomas Feltner. "The Use of Credit Scores by Auto Insurers: Adverse Impacts on Low- and Moderate-Income Drivers." Consumer Federation of America, December 2013. http://www.consumerfed.org/pdfs/useofcreditscoresbyautoinsurers_dec2013_cfa.pdf.

[5] St. Ambrose University, Use of Credit Scores by the Insurance Industry: Iowa Consumers' Perspective (2009), p. 20.

was fair for insurers to use credit scores in setting auto insurance rates, only 31 percent agreed while 67 percent disagreed, with 47 percent of the total sample strongly disagreeing (see Figure 1).[6]

The use of other socio-economic factors unfairly results in higher prices for lower-income drivers

The unfair use of non-driving rating factors is not limited to credit score. In previous reports, CFA collected premium quotes from individual companies' websites to assess the impact of various rating factors on the price of auto insurance. Using this method, previous research found, for example, that several major insurers charge significantly higher premiums to drivers with only a high school diploma than to those drivers with higher levels of education, such as a master's degree.[7]

These are unfair when used individually, but have a sizable, harmful impact on affordability when used together along with other socio-economic factors, as they often are for many lower-income people.

For example, CFA recently analyzed premiums quoted by GEICO to a driver with no traffic violations and a safe driving history living in the 60636 ZIP code in Chicago.

1. A married woman, living near 74th and South Damen, who is a bank executive with a clean driving record pays an annual premium of $606 for basic auto insurance.

2. However, if she were single, that same good driver would pay $719.

3. If she were a retail cashier instead of an executive, her premium would jump to $806, $200 more than the married executive despite the fact that she lives at the same address and has the exact same driving record.

4. To pay in installments costs her $60 a year, so her new premium is $866.

5. And if she didn't have current coverage, even if it was because she stopped driving for a few months, her premium skyrockets to $1,584.

CFA also found similar pricing in a ZIP code in Alton, Illinois.

1. A married woman, living in the 60, who is a bank executive with a clean driving record pays an annual premium of $504 for basic auto insurance.

2. However, if she were single, that same good driver would pay $576.

3. If she were a retail cashier instead of an executive, her premium would jump to $596, nearly $100 more than the married executive despite the fact that they live at the same address and have the exact same driving record.

4. To pay in installments costs her about $60 a year, so her new premium is $655.

5. And if she didn't have current coverage, even if it was because she stopped driving for a few months, her premium skyrockets to $1,119.

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[6] ORC International, Auto Insurance Omnibus (June 7-10, 2012).

[7] Brobeck, Stephen. "Use of Education, Occupation, and Other Non-Driving Factors Inflate Premiums for Low- and Moderate-Income Drivers." Washington, DC: Consumer Federation of America, September 24, 2012. http://consumerfed.org/pdfs/PR.AutoInsuranceRateFactorRelease.9.24.12.pdf.

Auto insurance premiums should signal to drivers that if they drive safely they will pay less. But right now, in Illinois, if you want to lower your auto insurance premium by hundreds of dollars, insurance companies are saying loud and clear that you should go back to college, get married, get a new job and fix errors on your credit report or pay off your outstanding medical debts. Those may be great ideas, but your ability to afford auto insurance and comply with state law should not depend on them.

Communities of color have less access to affordable auto insurance

In a 2015 report, Consumer Federation of America also found that. across the country, the price of state-mandated, minimum-limits auto insurance offered to a good driver increases where the proportion of African Americans living in a community increases.[8] In communities where more than three quarters of the residents are African American, premiums average 70 percent higher than in those with populations that are less than one quarter African American ($1,060 vs. $622). In the densest urban areas drivers in African American communities paid, on average, 60 percent more than similarly situated drivers in predominantly white communities, and in rural areas drivers in predominantly African American communities paid 23 percent more. Middle-income African American communities were similarly impacted. The average premium in upper middle-income, predominantly African American ZIP codes is 194 percent higher than the average premium charged to a similarly situated driver in an upper middle-income, predominantly white ZIP code ($2,113 vs. $717).

In the Chicago metropolitan region, drivers in predominantly African American communities paid, on average, 23 percent more for auto insurance than drivers in white communities.

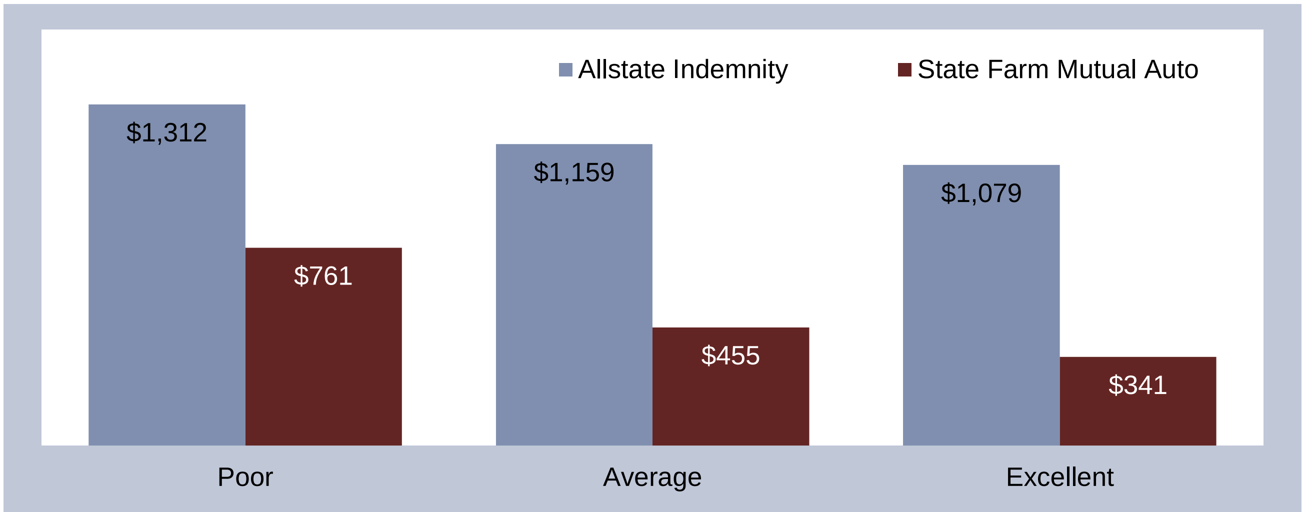
Conclusions

These findings raise important questions as to whether state-mandated auto insurance is priced fairly and affordably in Illinois. High insurance premiums act to deny these Americans economic opportunity and the ability to insure a car that is so critical to getting to the best job for which they are qualified and also help explain why so many low-wealth Americans drive without insurance.

Thank you for the opportunity to express CFA's support for SB 2208 and for the broader need to reduce the cost of auto insurance for lower-income drivers.

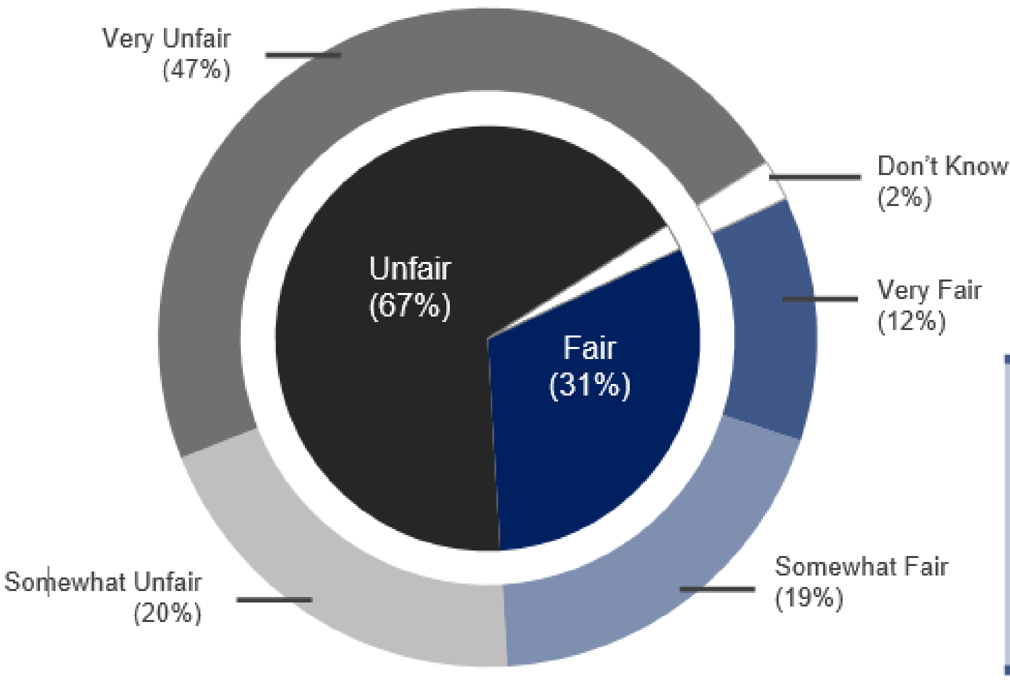
[8] Feltner, Thomas, and Douglas Heller. "High Price of Mandatory Auto Insurance in Predominantly African American Communities." Washington, DC: Consumer Federation of America, November 2015. http://consumerfed.org/wp-content/uploads/2015/11/151118_insuranceinpredominantlyafricanamericancommunities_CFA.pdf.

Figure 1. Controlling for all other factors, credit score increases insurance premiums at State Farm and Allstate



Source: CFA report entitled "The Use of Credit Scores by Auto Insurers: Adverse Impacts on Low- and Moderate-Income Drivers

Figure 2. Two-thirds of the public believe that using credit score to determine auto insurance rates is unfair



Source: 2012 Survey conducted by ORC International

Question: "How fair do you think it is for insurers to use each of the following factors in deciding on an auto insurance price for a driver?