Issues Paper

USE OF CREDIT SCORES BY INSURERS

Credit Scoring Working Group

June 2011

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1. Canadian Council of Insurance Regulators -CCIR

The Canadian Council of Insurance Regulators (CCIR) is an inter-jurisdictional forum of provincial, territorial and federal insurance regulators with a mission to work cooperatively among themselves and with other financial services regulators, policy makers and stakeholders, toward solutions to common regulatory issues.

In the spring of 2009, there was considerable media attention about the use of consumer credit information by insurance companies. The CCIR decided to establish a Working Group with a mandate to research and gather the facts surrounding credit-based insurance scores and how they are used in today's regulatory environment.

The work of the CCIR Credit Scoring Working Group is in alignment with CCIR's strategic priorities of identifying common emerging issues (fact gathering), and engaging stakeholders and policy makers so that the right information is in the hands of those in charge of making policy decisions in a timely manner. It is also in alignment with CCIR's risk-based approach to regulation.

2. Introduction

This paper sets out CCIR's understanding of insurers' use of credit -based insurance scores, the types of consumer risks that can potentially arise, and the rules that currently exist in response to these potential risks.

CCIR is seeking the views of consumers and the industry on the following:

- Whether all potential risks have been identified
- Whether the potential risks identified are already addressed under law, and if so, how.

It is beyond the scope of this paper to address the issues of whether or not there is a correlation between credit scores and the filing of an insurance claim, and the impact of credit score use on certain demographic groups. This is a debate that has garnered a lot of public attention in the United States and has become, for the most part, a "battle of studies". Advocates for the use of credit scoring rely upon their actuarial studies that have identified a strong statistical link between a person's credit score and the likelihood that they would make a claim[1]. Similarly, advocates against the use of credit scoring rely upon studies that have some evidence that although racial and ethnic minorities are found at all levels of insurance credit scores, they are "over represented" on the lower end of the credit score scale[2]. There are no equivalent studies in Canada[3]. CCIR is not proposing to undertake such studies nor is it seeking comments on the academic debates of actuarial evidence, and whether or not the use of credit-based insurance scores can be challenged as discriminatory under insurance or human rights law. Yet, the CCIR welcomes the observations and ideas of those stakeholders who wish to cover these topics within the context of their response to the specific feedback requested in this Issues Paper. Also, if you are in disagreement with the facts as presented in this Paper, let us know.

Similarly, the question of whether or not to ban the use of credit scores goes beyond the scope of CCIR's review. Ultimately, this is a government decision dependent upon a combination of political and socio-economic conditions within a jurisdiction.

The potential risks outlined in this paper are those that the CCIR believes could potentially impede the following marketplace outcomes:

[1] See for example, National Association of Insurance Commissioners, "Credit Reports and Insurance Underwriting". 1996; Miller, Michael J. and Richard A. Smith, "The Relationship of Credit-Based Insurance Scores to Private Passenger Automobile Insurance Loss Propensity, An Actuarial Study" by EPIC Actuaries, LLC, 2003; Texas Department of Insurance, "use of Credit Information by Insurers in Texas: The Multivariate Analysis" (Jan. 31, 2005); Federal Trade Commission, "Credit-Based Insurance Scores: Impacts on Consumers of Automobile Insurance," 2007.

[2] See for example Federal Trade Commission, "Credit-Based Insurance Scores: Impact on Consumers of Automobile Insurance," 2007; Texas Department of Insurance, "Use of Credit Information by Insurers in Texas" (Dec. 30, 2004); Kabler, Brent, "Insurance-Based Credit Scores: Impact on Minority and Los Income Populations in Missouri," 2004.

[3] The Canadian Association of Direct Response Insurers (CADRI) gathered member statistics, which show a correlation of credit scores to claims experience. Intact Insurance also gathered data that shows the loss ratio and frequency of their personal property portfolio improves as a customer's credit score increases.

- fair treatment of consumers;
- disclosure of information to enable consumers to make informed choices;
- compliance with the law; and,
- good corporate governance.

It is our hope that by describing the facts gathered to date, we will build a common understanding about the topic among regulators, policy-makers, consumers and industry stakeholders.

3. Credit-Based Insurance Scores

3.1 What is a credit-based insurance score?

CCIR uses the term *credit-based insurance score* throughout this document to refer to the three digit numerical ranking used by insurers as a snapshot of the credit performance and financial health of an individual at a specific point in time. It is derived from credit information contained in credit reports collected and maintained by credit reporting agencies.

In Canada, two credit reporting agencies, Equifax and TransUnion, track consumer credit information to compile a consumer's credit report. Credit reporting agencies obtain their information from private and public sources such as banks and collection agencies. A credit report is composed of a variety of credit characteristics, such as:

- payment history
- type of credit,
- outstanding debt amounts,
- length of credit history,
- type of credit in use,
- foreclosures,
- bankruptcies

Credit reports do not include personal characteristics such as:

- income,
- race,
- religion,
- gender,
- ethnic group,
- disability, or
- marital status.

Credit-based insurance scores are similar to more traditional (financial) credit scores, but they are not the same. Both are derived from information contained in a credit report, but the mathematical model used is different and takes into consideration different credit characteristics. Traditional credit scores are used to predict the likelihood that a consumer will default on a loan. Credit-based insurance scores are especially calculated for insurance purposes to attempt to predict the likelihood that a policyholder will file an insurance claim. The credit-based insurance score may be purchased by the insurer from a credit reporting agency (i.e. Equifax, TransUnion), or it may be calculated independently by the insurer for its own use. In both cases, the formula or scoring model is confidential.

Insurers use credit-based insurance scores in their rating and underwriting risk classification systems to determine the risks they will insure, and the amount of premium they will charge. When used for underwriting and/or rating, the credit-based insurance score can cause one of four actions to occur:

1. The consumer receives a discount due to better-than-average score.
2. The consumer receives a surcharge due to a lower-than-average score.
3. The consumer does not benefit nor is adversely affected due to the score.
4. The insurer declines to offer insurance to a consumer due to a lower-than-average score.

3.2 What makes credit-based insurance scores different from other risk factors?

In insurance, there has always existed a form of "rate discrimination" that is considered to be fair if the rates are based on underlying insurance costs. As long as the risk classification system is based on actuarial evidence (i.e. a rating factor cannot be used without adequate justification that it is predictive of future losses) and is a legally accepted business practice, equal treatment of applicants and policyholders is not required. Insurers can charge different rates to different risks, but they cannot charge different rates to risks of essentially the same hazard.

Both physical and behavioural hazards will affect whether or not an applicant is eligible for coverage, and if so under what terms. For example, a wood frame building is more susceptible to fire than a brick structure so all else being equal, a wood home is more expensive to insure. Similarly, any behavioural factor (e.g. number of claims made in the last three years, a conviction etc.) that according to actuarial evidence is predictive of losses will place an applicant in the "riskier pool", which determines the base premium rate.

Some jurisdictions have rate caps and/or prohibit certain rating factors for some lines of insurance (e.g. mandatory automobile insurance) for various public policy reasons. However, in general, there is a competitive market for purchasing insurance. Each company is able to decide what factors they can use in deciding to accept a risk, and the premiums they will charge.

Insurers use a combination of physical and behavioural factors in their rating and underwriting decisions. Many factors clearly relate to the losses they are designed to predict (e.g. having an automated sprinkler system for insured fire loss), while with others the relationship is less apparent (e.g. gender and marital status for auto insurance, credit scoring).

In the case of credit scoring, the link between a person's credit score and likelihood to make a claim is not intuitive. Some insurers claim -and at least one psycho-behavioural study supports this view[4]-that

[4] 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.

credit scores are indicative of personal responsibility because it is reasonable to believe that the responsibility required to prudently manage one's finances is associated with other types of responsible and prudent behaviours for example proper maintenance of homes and safe operation of cars.

Unlike factors such as gender and age, a credit-based insurance score is a mechanism that insurers use to assess the way a person manages his or her financial affairs and, as such, an uncomfortable subject for many of us.

3.3 Who is using credit-based insurance scores?

Recently, the province of Newfoundland and Labrador prohibited the use of credit information for both automobile and personal property insurance. Alberta and Ontario do not allow the use of credit information and credit scores for mandatory automobile insurance coverage, but there are no restrictions regarding personal property (except to provide a quote in Alberta). Other provinces and territories currently permit the use of credit information and credit scores for both auto and property.

According to the April 2009 survey conducted on behalf of CCIR by Financial Services Commission of Ontario (FSCO), not all property insurers are currently using credit scores. FSCO directed a questionnaire to chief executive officers and chief agents of 35 property insurers representing 75% of the property insurance market in Ontario. The findings showed that 19 companies (55% market share) currently use credit scores, and a further 6% of the market share plan to use credit scoring within the next three years.[5]

Although Québec did not take part in this exercise, the Québec regulator reports that the use of credit scoring is even more widespread there. Out of the 80 insurers who underwrote private passenger vehicles in 2009 in Québec, 28 used this criterion, representing 86% of the market. Assuming that these insurers also used credit scoring for home insurance, a similar proportion of this market is likely affected.

[5] A copy of the FSCO credit scoring survey can be found at: www.ccir-ccrra.org

4. Current Regulatory Framework

4.1 In Canada

Privacy legislation

Across Canada, the use of credit scores by insurers is subject to the (federal) *Personal Information Protection and Electronic Documents Act* (PIPEDA), which give individuals the right to access and request correction of any personal information (including credit information) an organization may have collected about them, and requires prior consent for its collection and use. Some provinces have laws substantially similar to PIPEDA that regulate the collection, use and disclosure of personal information by businesses and other organizations and provide individuals with a general right of access to, and correction of their personal information.

Credit Reporting Legislation

Use of credit scores by insurers is also subject to the requirements of credit reporting laws. All provinces (except New Brunswick, Quebec, the North West Territories, Yukon and Nunavut) currently have legislation or regulations in place to address the use of credit reports produced by credit reporting agencies (i.e. consumer reporting legislation). In general, this legislation outlines practices that must be adopted by credit reporting agencies and users of credit reports (e.g. insurers) to protect the right of consumers. Some obligations are only imposed on the credit reporting agencies, such as the prohibition to collect certain type of information (race, religion etc.), and to maintain accurate files. Other obligations, such as consent and confidentiality, and disclosure requirements, especially if an adverse decision is taken as a result of the use of a consumer's credit file, are imposed on users, so an insurer would have to comply with these rules.

Consumers, on the other hand, have the right to review and correct errors contained in their credit reports. In general, if errors are corrected, the credit reporting agency must notify those provided with the previously inaccurate information (e.g. an insurer). There is, however, substantial variation across provinces in the content of credit reporting legislation, especially as it relates to the production of credit reports for the purposes of underwriting insurance.

Industry best practices guidelines

On January 20, 2010, the Insurance Bureau of Canada (IBC) issued a *Code of Conduct for Insurers' Use of Credit Information* intended to provide insurers who use credit information as part of their underwriting activities with clear guidelines based on fundamental principles of consumer protection and applicable federal and provincial laws. The IBC guidelines deal with, among other things, obtaining informed consent from a consumer before using his/her credit information, making sure the underlying credit information from which a score is calculated is accurate and up-to-date, and notifying consumers if an adverse decision is taken based on credit information or a credit score. The IBC guidelines, however, are voluntary.[6]

4.2 In the United States

Since the enactment of the *Fair Credit Reporting Act* (FCRA) in 1970 insurers are allowed to use credit scores in the underwriting process for both automobile and personal lines property insurance. It is estimated that over 90% of automobile insurance companies in the US use credit scores as a means of setting rates. The use of credit-based insurance scores is also prevalent in property lines.

The use of credit scoring by insurers in the United States is controversial and has created a heated debate. Most states have taken some form of legislative or regulatory action to control or prohibit its use. The scope of regulatory provisions adopted in each state varies considerably.

Twenty-seven states have approved laws that follow the basic National Conference of Insurance Legislators ("NCOIL") Model Act, which regulates the insurance industry's use of credit in-formation. NCOIL's position is that insurance scoring is a valuable underwriting tool provided its use is regulated. The NCOIL Model Act requires insurers to:

- notify applicants and policyholders that credit history information may be used as an underwriting or rating factor;
- notify applicants or insureds that adverse credit-related decisions have been taken;
- reevaluate underwriting and rating decisions based on disputed information found to be incorrect; and,
- provide state insurance departments with actuarial justifications to support the use of insurance scoring models.

A few states (Georgia, Hawaii, Maryland, Oregon, and Utah) have banned the use of credit information in certain circumstances. For the most part, these prohibitions pertain to private auto insurance coverage.

Several state governments as well as consumer advocate groups have commissioned or completed significant studies on credit-based insurance scores. Although much of the debate has focused on the two opposing ends of the policy option continuum– either allow its use or ban it - there are many policy options that fall between the two extremes, and that have been enacted by some states in accordance to their unique political and regulatory structures. For example:

- Illinois allows the use of credit-based insurance scores but directs companies to consider exempting those who undergo extraordinary life events;

- Oregon limits the use of credit-based insurance scoring to new business only; prohibits the re-evaluation of credit-based insurance scores if an insured experiences a death or divorce of a spouse; and prohibits an insurer from increasing the premium if an insured's score deteriorates.

[6] A copy of the IBC Code can be found at: www.ibc.ca

- Minnesota prohibits rejection, cancellation or non-renewal of a private passenger automobile or homeowner policy. If no credit-based insurance score is available the insurer must exclude the use of credit in the rating of a policy. The insurer *must* provide a reasonable underwriting exception for catastrophic injury/illness, temporary loss of employment or death of an immediate family member.

5. Potential Risks to Consumers

The CCIR would like to engage stakeholders in a discussion on the types of consumer harms or potential risks that may arise as a result of the use of credit-based insurance scores. In particular, the CCIR would like to obtain feedback on whether or not, in your opinion, the items listed below:

a) Represent a risk or have the potential to harm consumers (e.g. outcomes desired such as fair treatment of consumers, adequate disclosure to enable consumers to make informed decisions etc. are not accomplished)

b) Whether the risk is adequately addressed under PIPEDA, provincial privacy statutes or provincial consumer reporting legislation

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.

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.

The survey conducted by FSCO indicated that all insurers advise their applicants and policyholders at the qualification stage or via the application that a credit score will be used and obtain consent before using credit information as per federal and provincial privacy and Consumer Reporting legislation. However, a poll conducted in December 2010 for the Ontario brokers association (IBAO) on the use of credit scores by property insurers showed that 75% of consumers were unaware of the practice. A consumer survey in Alberta in June 2010 commissioned by the Consumer Representative to the Automobile Rating Board (AIRB) found that 48% of consumers did not know if insurers were using their credit information.[7]

There seems to be a discrepancy between what insurers and consumers are reporting, which suggests to the CCIR that the consent given is not sufficiently informed. For example:

- Are insurers disclosing to the consumer the specific ways that the insurer will use the credit information or the credit-based insurance score (e.g. to approve a payment plan, to provide a quote, for underwriting, for rating)?
- Is the consumer's consent in a verifiable form?
- Do consumers know for how long they are giving consent for, or is the consent given continuous and not re-obtained at renewal?
- Do consumers know that they can refuse or withdraw consent at any time?

[7] A copy of the survey can be obtained at: www.airb.alberta.ca/public_meetings/2010/0615-airb-consumer-rep-submission.pdf

Provincial credit reporting statutes require that insurers obtain consent prior to using the credit information. Privacy principles under PIPEDA and provincial privacy statutes deal with identifying the purpose of consent, capacity to consent, and form of consent.[8] The IBC voluntary guidelines recommend that consent be informed and defines the elements of informed consent.

5.2 Unreliable credit data

Potential risk: 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.

The CCIR does not know the frequency of inaccuracies or omissions found in the underlying data from which insurers calculate a credit score. There are conflicting reports. According to a 2005 study by the Public Interest Advocacy Centre (PIAC), 18% of Canadians who checked their credit rating found inaccuracies.[9] There is, however, no consensus on the magnitude of these inaccuracies. When asked by the PIAC about whether they kept records of the number of requests to correct inaccurate information, both Equifax and TransUnion declined the request saying this was competitive business information, and not helpful because there are inaccuracies in credit reports that may not affect the credit worthiness of an individual.

Some provincial reporting statutes impose an obligation on credit reporting agencies to correct errors and notify all persons who have been supplied with an erroneous credit report. However, many Canadians do not request or correct credit reporting agencies information. According to the survey conducted by AIRB, only 35% of consumers have checked their credit report.[10]

Privacy legislation also imposes obligations on credit reporting agencies to maintain accurate files. In December 2010, a Federal Court awarded damages after one of the credit reporting agencies in Canada sent inaccurate information to a bank, thus breaching PIPEDA.[11] The court awarded damages because the credit inaccuracies directly led to the failure of the plaintiff to secure a loan for a business

[8] On May 6, 2011 the Office of the Information and Privacy Commissioner for British Columbia issued an Order ordering an insurer to review the consent it had been using on its insurance applications and to provide its customers with adequate notice of the purpose for collecting their credit scores. According to the Commissioner, in order to satisfy the notice requirements and provide meaningful consent, individuals must be informed that their credit information may be collected for the purpose of assessing future risk of loss in underwriting a policy. For full Order see http://www.oipc.bc.ca/PIPAOrders/2011/OrderP11-02.pdf

[9] See Public Interest Advocacy Centre (PIAC), *Credit Reporting: How are Consumers Faring?* (August 2005). This is a national survey of Canadian consumers and other stakeholders on the credit reporting system as well as the accuracy and reliability of credit reports. Also, in the US, a study conducted in 2000 by the National Credit Reporting Agency and the Consumer Federal of America reported 29% of individuals who reviewed their credit reports found significant errors, averagely translating into a 50 point score error or more.

[10] PIAC estimates that only 17% percent of Canadian 18 and over have checked their credit report in the last three years.

[11] See *Nammo v. Transunion of Canada Inc*. 2010 FC 1284.

opportunity. The Court also took issue with the credit agency's failure to inform the bank of its mistake. This was the first ruling where the court awarded damages for a breach of PIPEDA.

5.3 Availability and affordability of insurance

Potential risk: 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.

There is concern that the use of credit-based insurance scores may make insurance unavailable to some. The CCIR would like to obtain feedback on whether or not this is a potential risk. As the CCIR understands it, credit-based insurance scores are usually one factor of many in an insurer's underwriting evaluation. If this is the case, no insurance coverage would be denied solely based on a credit score. However, there have been instances reported by consumers where a policy has not been renewed because of an insurer's use of a credit score.

There is also a concern that the use of credit scores as a risk factor by insurers may cause too much of a difference in the premiums charged to the most and the least desirable policyholders. According to a cover story in *Canadian Underwriter*, in a bulletin to brokers, one insurer calls for a 20% increase on 'B-rated,' second-tier credit risks. In response, another insurer discusses the need to 'protect itself' by implementing a 25% surcharge on property policies transferred by the above insurer.[12]

On the other hand, since not all insurers currently use credit scores to rate or to underwrite applicants, and those who do may apply risk variables differently in their actuarial models, someone who is offered a higher rate by one company may get a better quote from another company that has a different rating mechanism, stimulating competition.

The use of credit scores may decrease the price of insurance for people with good scores, and increase the price for people with poor credit scores. However, it is uncertain how many consumers received a premium increase or a premium decrease due to credit scoring in Canada. There are no publicly available studies documenting this. According to the survey conducted by FSCO, not many companies disclose to consumers discounts and surcharges attributable to credit scoring.

There are some statistics from the United States on the number of personal polices that received a premium increase and decrease due to credit scoring. A 2007 report of the Arkansas Insurance Department found that 30% of all policies in that state received a premium reduction due to credit scoring and 9% received a premium increase due to credit scoring. The Federal Trade Commission 2007 study projected that 59% of consumers could expect a premium discount on their auto insurance if credit scores were used.

[12] See Gambrill, David, *Wild West of Credit Scoring*, Canadian Underwriter p.56 (October2009).

The Financial Consumer Agency of Canada estimates that about 75% of Canadians have a good or average credit score, so one could assume that more consumers would benefit from its use to determine premiums, than be adversely affected, but more fact-based data from insurers is necessary to confirm this assumption.

5.4 Insufficient disclosure

Potential risk: Consumers may not have sufficient information about how to modify their behaviour in order 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.

Because credit-based insurance scores are calculated using proprietary mathematical models, which are considered confidential under privacy legislation, it may be difficult for consumers to know exactly what factors go into the model, and then what weight is given to the credit-based insurance score itself during the underwriting and rating process. Without this information, consumers may not be able to react and take action to repair their credit rating.

Due to variations in the application of credit scores amongst insurers there seems to be a lack of clarity on how insurers use credit variables to determine the score, and a lack of transparency regarding the process.

Understanding how the process works and how much weight was given to the credit score is especially important if the insurer is denying, cancelling or increasing a premium (i.e. adverse action) based on credit information. In Saskatchewan, Ontario, Manitoba, British Columbia and Prince Edward Island, anyone who uses credit information to deny a benefit or increase the cost of a benefit (i.e. adverse action) must notify the affected individual as per the consumer reporting laws. However, according to the survey conducted by FSCO, 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.

Furthermore, usually the purposes of an adverse action disclosure obligation is to empower the consumer to identify what information or lack thereof led to the adverse action, to be able to correct or update inaccurate or missing information, or improve a record over time. It is uncertain the extent to which this objective is being met. The information disclosed by insurers may not be sufficient for a consumer to take corrective action and endeavour to improve its credit score over time. This is different from other insurance rating factors where the consumer knows exactly what to do to improve the rating (e.g. abstain from getting speeding tickets), thus encouraging behavioural changes.

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.

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

Consent provisions- already contained in privacy and consumer reporting statutes -may be meaningless if an insurer unduly penalizes consumers who do not provide consent. If consent is not given, are insurers abstaining from providing a discount or penalizing the applicant or policyholder with a hefty surcharge?

Some people, particularly those new to Canada, those who choose not to use credit, and the younger, may have what is called a "thin file" or "no-hit" file, that is , a file with no or very few entries. According to CADRI, a members study they conducted showed that "no hit" files had a claim and loss experience that was about average. According to FSCO's survey, 11 insurers (representing 38% of market share) indicated that there would be no effect on premiums if an applicant does not have a credit score. The NCOIL model act allows insurers to treat those who have thin files as if they had neutral credit information or to simply exclude the use of credit information altogether. The IBC voluntary guidelines recommend insurers do not deny coverage to customers with no credit information, without consideration of any other applicable rating and underwriting factors that are relevant and available to the insurer.

A decrease in a credit score may be directly influenced by a catastrophic event like the death of a spouse, loss of employment, or identity theft. The IBC voluntary guidelines and the NCOIL model Act in the U.S. both recommend that insurers exercise their discretion to offer reasonable exceptions if a poor credit score is a result of extraordinary life circumstances.

5.6 Privacy breaches

Potential risk: Insurers may breach confidential credit information.

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

Consumers are usually concerned that the private nature of their credit information may not be adequately protected by insurers. Whereas privacy breaches are always a potential risk, the CCIR considers that this risk is adequately addressed under PIPEDA (and provincial privacy statutes, where applicable). These privacy laws apply to credit information and to both insurers and credit reporting agencies.

Privacy principles under these statutes include: accountability; consent; identifying purpose; limiting collection; limiting use, disclosure and retention; accuracy; safeguards; transparency; individual access; and challenging the accuracy of the personal information and have it amended as appropriate.

Individuals can make- and have done it- complaints to the Privacy Commissioner of Canada or to provincial Privacy Commissioners if any of these principles are violated.

5.7 Lack of understanding

Potential risk: 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.

According to consumer surveys both in Canada and in the United States, consumers may not have a good understanding of how their credit information is being used by insurers and the extent to which the information contributed to a rating decision. They may not know how to improve a credit-based insurance score to change a rate.

In May of 2009, the Iowa Insurance Commissioner's Office arranged for a survey of 1,200 Iowa consumers regarding their attitudes, knowledge and beliefs about the use of insurance based credit scoring. The survey findings showed that most Iowans believe that the use of credit scores to set insurance rates is unfair, but it also found that consumers are seriously uninformed about insurance fundamentals (i.e. what it means to spread the risk), and that their knowledge of the purpose of credit scores is inadequate.

A 2005 U.S. Government Accountability Office (GAO) report found that although most consumers knew what a credit score was, and approximately one-third had obtained their credit scores, many did not know that some behaviours – such as using all their available credit – could negatively affect their scores.

According to the consumer survey in Alberta by the AIRB, only 34% of consumers are comfortable with insurers using their credit information. However, after telling consumers that using credit information can result in lower insurance costs for people with good credit, the proportion of those who are comfortable increased to 48%.

The CCIR is interested in learning:

- How insurers currently explain their use of credit-based insurance scores to consumers;
- If some of the objections regarding its use are based on misinformation about the practice; and
- Who should be responsible for educating the public (including what role, if any, insurance brokers and other intermediaries should play in communicating to consumers the impact, if any, that a credit score may have in their insurance rates).

According to the federal Task Force on Financial Literacy, educating the public (i.e. providing consumers with the knowledge, skills and confidence to make responsible financial decisions) is a priority and a shared responsibility. To support the development of financial literacy the Task Force recommends on its February 2011 report for financial services providers to put a strong emphasis on delivering educational information and ensuring that it is fully understood by Canadians.

6. Conclusion

The CCIR welcomes the comments, suggestions and ideas of the industry and consumer associations on the potential risks identified in this report. Thorough knowledge of potential consumer harms and impediments to desired regulatory outcomes increases the possibility that government and/or industry solutions can be found before potential risks become major problems.

To ensure that there is a common understanding amongst all stakeholders, the CCIR seeks specific feedback on the following:

- Whether all potential risks have been identified
- Whether the potential risks identified are addressed under specific- purpose statutes (e.g. PIPEDA, provincial privacy statutes or provincial consumer reporting legislation), and if so, how.

However, as stated earlier, 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.

6.1 Consultation Details

An electronic copy of this document is available on CCIR's website at www.ccir-ccrra.org/.

We look forward to receiving your submissions by August 14, 2011.

Electronic submissions are preferred and should be forwarded to ccir-ccrra@fsco.gov.on.ca.

Written submissions should be forwarded to:

CCIR Secretariat
5160 Yonge Street, Box 85
Toronto, Ontario M2N 6L9

CCIR intends to make the submissions received publicly available. If you indicate that you do not want your submission or specific parts of your submission to be made public, we will treat the submission, or the designated parts, as confidential to the limited extent permitted by law.