Comments of the Center for Economic Justice to the

NAIC Auto Study Group
Big Data Working Group
Property Casualty Committee
Market Regulation Committee

Priority Activities for Addressing
Insurance Affordability Measures and
Big Data Challenges for Regulators

August 1, 2016

The Center for Economic Justice (CEJ) offer comments in response to the Auto Study Group's request for comments on its future activities. We submit these comments to Big Data Working Group and Property Casualty (C) and Market Regulation (D) Committees because the issues before the Auto Study Group transcend the group's work and overlap with the ongoing activities of the Big Data Working Group and C and D Committees. Our recommendations are presented in order of importance.

1. **Prioritize the Work of the Auto Study Group to Developing Measures of Insurance Affordability and Availability**

NAIC members are now aware that the Federal Insurance Office (FIO) has announced an auto insurance affordability index along with plans to collect data from insurers to annually produce this index for selected ZIP Codes throughout the country. Despite state regulators being on notice since July 2010 that Congress had tasked FIO with monitoring affordability and accessibility of insurance in traditionally underserved areas, state insurance regulators have done nothing to pre-empt FIO's incursion into state-based regulation in this areas. After each of these milestones, state insurance regulators and the NAIC did nothing:

- The passage of the Dodd Frank Act memorializing Congress's interest in monitoring the affordability and accessibility in underserved areas.
- FIO's request to the NAIC for comments and suggestions on how to approach this task
- FIO's publication of a proposed index and related data requirements
- Widespread criticism of FIO's proposed index

At any step along the way, the NAIC could have asserted the relevance and vitality of state-based regulation by developing a more substantive and granular measure of affordability coupled with state-based collection of the more granular data needed not just for measuring affordability, but for implementing a more robust market analysis program. Rather than putting effort into developing the data collection necessary to answer Congress's questions and to generate greater efficiencies and effectiveness of market regulation, the NAIC has put its market regulation efforts into a market regulation ~~accreditation~~ certification program on the premise that the greatest threat to state-based regulation is criticism of market conduct exams. In contrast to the massive efforts to produce principles-based reserving and market regulation certification, the NAIC has produced nothing to meaningfully address the challenges posed by FIO and Congressional interest in big data in insurance, emerging risk classification issues, more effective market regulation and monitoring affordability of insurance. Now, with FIO's published affordability index, the NAIC and state insurance regulators find themselves reacting to yet another incursion into state-based insurance regulation.

CEJ recommends the NAIC respond to these issues facing state-based insurance regulation by prioritizing the work of the Auto Study Group and the Big Data Working Group to develop a better tool for measuring insurance affordability and develop the necessary resources at the NAIC for assisting the states with data collection and analysis related to monitoring insurance markets.

Auto Study Group Charge:

Develop a More Granular Measure or Measure of Affordability Than That of the FIO

FIO's affordability measure – 2% or less of median household income in a ZIP Code – lacks the granularity to both identify communities facing affordability problems and shed light on the causes to inform public policy debates. Examples of limitations of the FIO approach include, but are not limited to:

- ZIP Codes too large a geographic area / comprising multiple communities with different affordability profiles
- No loss data to indicate whether high premium charges are a result of high claim costs, socio-economic rating factors and/or other factors
- Failure to include data on quotes not resulting in a policy sale, thereby excluding those priced out of the market
- Failure to factor in other indicators of affordability into the index, including, for example, uninsured motorist rates, force-placed insurance rates or non-standard insurers' market share at a granular geographic level.
- Failure to distinguish between different household composition and affordability
- Failure to include physical damage coverage in the analysis or index, despite the vast majority of vehicles purchased with loans requiring such coverage.

State insurance regulators – through the NAIC – should develop more granular and meaningful measures of affordability for personal auto and residential property insurance, including flood. Done correctly, the NAIC's affordability measures can roll up into FIO's measure or, far better, become adopted by FIO because of the clear superiority.

Of course, the development of an improved affordability measure is tied to improved – more granular – collection of data on market outcomes, discussed in the next priority activity.

2. **Prioritize the Work of the Big Data Working Group Develop to develop enhanced data collection for market analysis**

The granular data need to operationalize a meaningful affordability analysis are the same data needed for the more robust market analysis needed for more efficient and effective market regulation. The data needed for a robust market analysis – one that includes the ability to monitor the affordability and accessibility of insurance in underserved areas as well the ability to perform enhanced market analysis to focus regulatory resources on problem companies and problem markets – is transaction data on premium quotes, policies issued and claims. Insurers are fully engaged in many Big Data applications. Stated differently – regulatory big data is needed.

Other financial regulators, including banking regulators and the Consumer Financial Protection Bureau collect and analyze large, transaction-level data sets. Examples include loan-level data reported by lenders pursuant to the Home Mortgage Disclosure Act and the loan-level data collected and analyzed by the CFPB in its study of payday lending. State insurance regulator market regulation data collection has not meaningfully progressed, is unsuited to today's market regulation needs and is, by far, the main impediment to improving the efficiency and effectiveness of state-based insurance market regulation.

3. **Prioritize the Work of the Big Data Working Group to develop improved regulatory tools for examining risk classification issues**

The issue of insurance risk classification is intertwined with insurers' use of Big Data. Insurers are utilizing a variety of non-insurance databased of individual consumer information for pricing, claims settlement, anti-fraud, marketing and other activities. It should be clear to insurance regulators that federal agencies have great interest in these issues as evidence by the discussion in reports by the White House, the Federal Trade Commission and the Federal Insurance Office. But, it should also be clear to insurance regulators that you are being overwhelmed by the advanced statistical techniques and vast databases used by insurers. In response, CEJ recommends the following.

Develop a template for states to use, with assistance from the NAIC for collection of requested information, to request from insurers the sources and uses of data for various insurance functions. Insurers would provide a list of all sources of data used for pricing (including underwriting) , marketing, claims settlement, antifraud and other. For each source of data, the insurer would provide a name/description of the data, the source of the data and the use or uses of the data. This periodic survey will provide regulators with the basic overview of what types of information are being used by insurers and what the information is being used for. This information is essential for regulators to respond to policy makers and to foster public discussion over potentially controversial types of data.

Finalize the risk classification survey currently with the Auto Study Group and strongly encourage states to issue the survey. This risk classification – with the simple purpose of providing regulators with a comprehensive list of risk classifications, whether styled as an underwriting guideline, tier placement factor or rating factor – has been under discussion at the NAIC for ten year or more. The current survey lists all the known characteristics of consumer, vehicle and policy used for risk classification for personal auto insurance and ask the insurer to report whether the insurer uses the characteristic and, if so, if the characteristic is used on its own or as part of a composite risk classification. Finally, the survey asks the insurer to provide the range of impact on premium for the characteristic. CEJ has provided a straight forward instruction for calculating and reporting the range of impact:

> Calculate the range of impact by dividing highest (worst) criterion relativity by the lowest (best) criterion relativity, all other factors constant. For example, if the worst credit score relativity is 2.0 and the best is 0.5, then the range of impact is 4.0. If the criterion is part of a composite rating factor, isolate the range of impact for the criterion holding all other criteria in the composite factor constant. If the range of impact varies based on values of other criteria, calculate the range of impact for the target criterion using the other criteria producing the largest range of impact.

4. **Prioritize the Work of the Casualty Actuarial and Statistical Task Force to develop a detailed plan for establishing resources at the NAIC to assist the states in their analysis of the new pricing models filed and used by insurers.**

The CASTF has begun to look at this issue. Just as the NAIC provides resources to assist the states in other areas – technical/actuarial capability at the NAIC to assist the states with PBR; collection and compilation of massive amounts of financial statement data to assist with financial analysis, collection and compilation of Market Conduct Annual Statement data to assist states with market analysis, to name just a few examples – the NAIC should develop resources to assist states in analyzing new pricing models. The NAIC resource would not be a regulator and would not provide regulatory opinions. Rather, the NAIC resource would provide states with technical – actuarial and statistical – expertise to answer states' questions about a pricing model. The NAIC resource would also assist states in accepting and processing large data sets as part of analysis of a pricing model.

5. **Transfer Further Examination of the TransUnion CarFax Vehicle Score to the Big Data Working Group**

The Auto Study Group has heard a presentation by TransUnion and CarFax about the new Vehicle Score rating system developed by TransUnion and CarFax utilizing data primarily collected by CarFax. The issues of concern raised about the Vehicle Score are not unique to auto insurance or to the Vehicle Score, but are the same issues raised for a number of Big Data pricing tools, including but not limited to questions about:

- Accuracy and completeness of data used in developing the model;
- Disproportionate impact on low-income or minority consumers;
- Disclosure to the consumer of data used;
- Disclosure to the consumer of adverse action resulting from insurer's use of the vehicle score;
- Ability of the consumer to view the data used, correct erroneous data and request re-rating based on accurate data

6. Initiate, at the C and D Committees, Discussion and Review of the Adequacy of Existing Rating Laws for Providing Regulatory Oversight of and Public Accountability for Insurer Risk Classification Practices.

The rating laws in all but one or two states are premised on regulators having complete access to and oversight of the data and analytics used by insurers for pricing. The rating laws are grounded in a requirement for cost-based pricing and the ability to distinguish consumers into groups of similarly-situated (in terms of the cost of the transfer of risk) consumers. These regulatory foundations face existential challenge from

- pricing practices that utilize data outside of the oversight of regulators to
- pricing algorithms beyond the ability of regulators to analyze or replicate to
- insurer pricing based on non-cost factors (e.g. price optimization) to
- use of risk classifications defended only by correlation and which undermine public policy goals for affordability and loss prevention.

The issue of the regulatory infrastructure regarding risk classification is linked to, but goes beyond, Big Data issue and represents another area in which the FIO and many others – see for example, recent state legislative concern over Progressive charging drivers more upon reaching 65 years of age in Maine or the Alaska governor vetoing legislation on insurance credit scoring and stating, "Credit report errors are common and can be difficult to correct. Missing or incorrect information in a credit report can negatively impact consumers' insurance scores, regardless of a person's driving record, the condition of their home, or whether they pay their bills on time. . . Because the bill relies on notoriously unreliable credit score ratings and would adversely affect consumers, especially low-income consumers, it should not become law."

State insurance regulators are the ones who see and review pricing practices at the ground level. The NAIC and its members should be taking the lead in educating legislators, policymakers and federal agencies on these important issues.