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Introduction

ChoicePoint is a Georgia-based publicly traded company. We spun off from Equifax in 1997. The best way to tell you who we are is to first tell you who we are not…we are not a credit bureau nor are we an insurance company. We do not collect premium or pay claims.

We do provide underwriting tools to insurance companies for automobile and homeowners policies. Listed here are some of the more popular services provided by ChoicePoint:

- C.L.U.E. ®
- credit reports
- motor vehicle reports
- insurance scores

Credit Reports – Part of the underwriting process.

I like to begin the discussion of insurance scoring by starting with a basic understanding of how insurance scores are developed. I am not an expert on credit reports, but will cover some of the elements from the credit report that are a part of the scoring model.

There are many elements in a credit bureau report.

- Credit grantor-contributed payment record information
- Public Record information, collections
- Records of consumer initiated inquiries
- Delivered only with permissible purpose
- Consumer report - FCRA protections

This list is a sample of some of the elements used for insurance scoring. These elements include information about who you are, to whom you owe money and whether you have applied for any credit cards.

The reporting of this information is governed by the federal Fair Credit Reporting Act.

There are three bureaus that provide credit information. Each bureau may have different information about any one consumer. These bureaus operate in a very competitive market and the accuracy of their data is critical to their survival.

Over 2 million credit reports are ordered every day and there are approximately 206 million credit active Americans. Home mortgage loans and automobile loans are closed everyday based upon the accuracy of these reports. If there were fatal flaws or high rates of error, commerce would be greatly affected.

Federal law protects consumers from improper use of credit report information. Consumers have the right to dispute information on their report and can expect timely resolution to their complaints.

Insurance Scores – Credit-based underwriting tool.

Insurance scores are also referred to as credit scores or credit-based scoring.

While the science of insurance scoring is relatively new, the use of credit reports in underwriting is decades old. Underwriters were looking at credit reports in a much more subjective fashion prior to the development of objective scoring methodology.

Following is a timeline of ChoicePoint's development of insurance scores. We are now the leading provider of insurance scores in America.

- 1990 - 1993 Research & Development
- 1993 - First Insurance/Credit Model - Property
- 1994 - 1995 Analysis and Results
- 1996 - Auto Model Introduced
- 1998 - New Models developed
- 1999 - New "ATTRACT" Models Introduced

While this science may be new to the insurance industry, the use of statistical modeling is not new. This is a proven science that has been used in medicine for measuring cancer risk and used by the forest service to fight forest fires.

Insurance scores are developed for our customers--the insurance industry—in the following way:

- Gathering External Data - credit report
- Merge with Policy Performance Data
- Data Clean-up - cap losses, etc.
- Modeling of Predictive Attributes
- Validation sample selection
- Implementation

This process is designed to determine the most predictive data elements and to construct a model. After the model is finalized, individual customer validations are completed. All of this is done to satisfy the user that the model works and to aid the user in providing support material to Insurance Departments for rate and form filings.

There are only a small number of elements on a credit report that have proven statistically sound for predicting frequency and severity of future loss. Our models can also combine claims history information with credit elements.

Insurance scores are no different than other factors used by insurance companies in that we are looking at past performance to predict the future. All of this is done in an effort to ensure that the insurer collects enough premium to pay received claims.

The elements built into the model include but are not limited to:

- Credit Union, Savings & Loan, Mortgage
- Personal Finance
- Bank revolving
- Bank installment
- Department stores
- Other retail

Again, it is important to point out that our models are not predicting a consumer's ability to pay back a loan, but rather are designed to assist insurance companies in predicting future losses.

Each element has characteristics that are measured. This is a sample of how an element might be measured.

- Inquiry Activity
  - Number of inquiries in the last 6 months
  - Number of inquiries with finance companies in the last 24 months
  - Number of months since most recent inquiry

Here is another sample of characteristics.

- Age of Credit File
  - Age of oldest account
  - Age of youngest account
  - Average number of months since account opened

As a tool, insurance scoring looks at many variables not just one. While it would be easy to criticize the model by saying that one could find a correlation between any two variables (say rainy days and super bowl victories) this would be a mischaracterization of how models work. We look at many variables and their relationships to each other.

While it is important to know what is in the model to better understand how it works, it is just as important to know what is NOT in the model. None of the elements listed here are used in our models:

- Nationality
- Age
- Religion
- Race
- GenderLocation/Address
- Net Worth/Salary
- Income
- Marital Status
- Occupation

I would also point out that inquires from insurance companies are not considered when calculating a score. We encourage people to shop for the best rate and don't want consumers to be penalized for shopping.

<u>Predictive Power</u> - Correlation

While insurance company data is the most compelling in showing the correlation between insurance scores and future loss, I have included some charts using sample data from our customers.

As you can see (attachment A) the lower the score the higher the loss ratio and the higher the claims frequency.

I have included sample national data and segmented the groupings into ten percent intervals. Each company using insurance scores will segment the scores to meet their own purposes.

The same trends hold true for non-standard auto. (attachment B)

In both auto models, the swings run from around 60% to 140%. Again each company's book of business may reflect narrower or wider swings.

The trends hold true for homeowners insurance. (attachment C)

The swings for homeowners run wider and approach 200% for the lowest score. This means that the person with the lowest score will have almost twice the loss ratio as the average consumer.

<u>Insurance 101</u> – Why use insurance scores?

It is important to cover the basics of how insurance works so that we can better understand the causation between financial behavior and future loss.

As we know, nobody has a crystal ball. Absent knowing exactly what the future holds, the best we can do is statistically predict the future. It is important that these predictions be as accurate as possible because at the end of the day the insurance company must collect enough premium to pay its claims.

Part of this process includes placing consumers into groups with similar predictive characteristics. In doing so, insurers can offer the most competitive rate to each customer. If this is not done, every driver would pay the same for his/her insurance, which would mean a consumer with five speeding tickets and a D.U.I. would pay the same as a consumer with a clean driving record.

Over time consumers have been educated to understand the value of grouping risks. We now understand that certain factors can cause us to have higher premiums and that there are actions we can take to keep our premiums down.

We also know that placing consumers in groupings does not reflect on consumers as being "good" or "bad" people. We are not bad homeowners because we don't live next door to a fire station. Just as we are not good homeowners because we installed a security system or deadbolts.

Insurance scoring is the same as what we have come to know about traditional underwriting criteria. We are looking for objective measures to help predict the future.

A person earning $25,000 per year is unlikely to find a bank willing to lend the person $1 million, even though the person manages their finances well. For the bank, this person is a bad credit risk for such a large loan.

However, from an insurance perspective, this same person exhibits behavior that would represent a low risk and thus receive favorable treatment.

With this information insurers are able to more accurately group their policyholders and offer them the best possible rate.

The insurance score does not indicate that individual "x" will have an accident on a particular day. Rather, it gives us the ability to group policyholders with similar performance characteristics.

In the end, individual consumers are treated more fairly and are less apt to be subsidizing consumers who file more claims.

Because of the competitive nature of insurance, there are as many ways of developing and using insurance scores as there are companies using them. Thus, consumers shopping insurance will find differences in rates and service, whether those differences are based on an insurance score or other underwriting variables. All of which improves the consumer's ability to work with their insurance agent to get the right coverage for their needs.

States have reviewed this issue closely through public hearings and appointed commissions that have examined the actuarial justification of insurance scoring and the impact to consumers. While the math clearly supports the use of insurance scoring, questions still remain concerning the causation.

Here are the most common questions asked by consumers and regulators:

What does paying my credit card on time have to do with my driving?

In order to answer this question let me ask why insurers offer a good student discount. What is the causation here?
As a society, we have decided that students who get high grades will get a discount on their insurance. As a group, we have found that if students study, attend class, pay attention and do their homework, they will earn higher grades. Students who work hard to avoid the risk of failure also have risk averse behavior in other aspects of their life. As a group, insurance companies have seen the correlation between high grades and lower loss ratios. It should come as no surprise then that people who avoid risky financial decisions also exhibit risk averse behavior in other aspects of their lives…including managing their property. As a group they are more diligent about the proper maintenance of their home and auto. Proper maintenance leads to lower severity of claims.

How does the hailstorm know to hit the house with the lowest score the hardest?

No, mother nature does not buy insurance scores from ChoicePoint and then target homes. Presumably, all the homes in a cul-de-sac are hit the same by the hailstorm.

As a group, people who are risk averse in managing their finances tend to be more diligent about maintaining all of their assets. They keep their homes in good repair so that when the hailstorm does eventually hit the amount of damage is less on their home than on the home of the owner that did not keep the roof in good shape.

The same hailstorm that hit the house may have also caused some damage to the car parked in the driveway. If the cost to fix the dented car is $300 and your deductible is $250 what will you do? As a group, the people with high insurance scores will likely not file the claim and conversely, consumers with a low insurance score will be more likely to file the claim.

What if I do not use credit cards? Will this result in higher premiums?

ChoicePoint recognizes that some people may not have substantial activity on their credit report and therefore, we believe these people deserve special consideration. We have developed a model for people who do not have substantial publicly reported financial activity. Again, it is important to point out that companies use different models.

People in under-served markets have worse credit, so won't they be charged higher premiums?

Most allegations that the use of credit-based scoring is discriminatory have been anecdotal. The one exception is a 1999 Freddie Mac consumer credit survey. However, the National Fair Housing Advocate reported that the survey was incorrect and drew faulty interpretations. Congresswoman Maxine Waters (D-CA) has publicly stated that the survey was incomplete, dishonest and racist.

A study by the VA Bureau of Insurance found no evidence supporting the racial allegations and the NAIC is commissioning the American Academy of Actuaries to study the issue.

The Oregon Consumer Advocate was quoted recently as saying - “This isn’t a system that targets poor people.”

Academic studies and actual company experience indicate no evidence of discrimination. Company experience in inner cities has been one of writing more business in these markets since the introduction of credit.

Will one late pay result in higher premiums?

Insurance scoring models are multi-variant tools measuring trends in financial behavior. As was already mentioned, insurance companies create groupings to help them in underwriting and rating. Groupings create wide ranges, thus small changes in the score will likely not result in changes in premium. However, it is worth pointing out that states that have placed too many restrictions on the use of scoring models have actually harmed consumers by forcing each variable to receive higher weighting. A model with 50 variables is more beneficial to consumers than a model with only 10 elements. The lack of flexibility by carriers ultimately minimizes the benefits to consumers and reduces competition.

Is insurance scoring fair?

Yes it is fair. It allows for the objective, equal application of individual data and helps insurers place individual risks in similar groups. Insurance scoring creates greater protection for consumers from being charged too much for their insurance, while at the same time honoring the principle of shared risk that is the underpinning of insurance. Remember, we are not measuring people’s access to credit or the interest rates they are charged. We are measuring how they handle the credit they do have. And, as just pointed out, we have special scoring models for people without substantial credit history.

How do I improve my score?

If consumers pay more or less due to groupings, they may want to know what the “best” class is - for example, in traditional underwriting consumers have been educated about what to look for in a new car or home that will save them money on insurance. We all know that living close to professional fire departments is best, having no tickets or accidents is best and driving cars with anti-lock breaks and air bags is better.

"Best" for credit would mean no bankruptcies, paying your bills on time, not running up high balances on your credit cards and only having credit cards that you truly need.

<u>Closing</u> – Consumer Friendly Practices

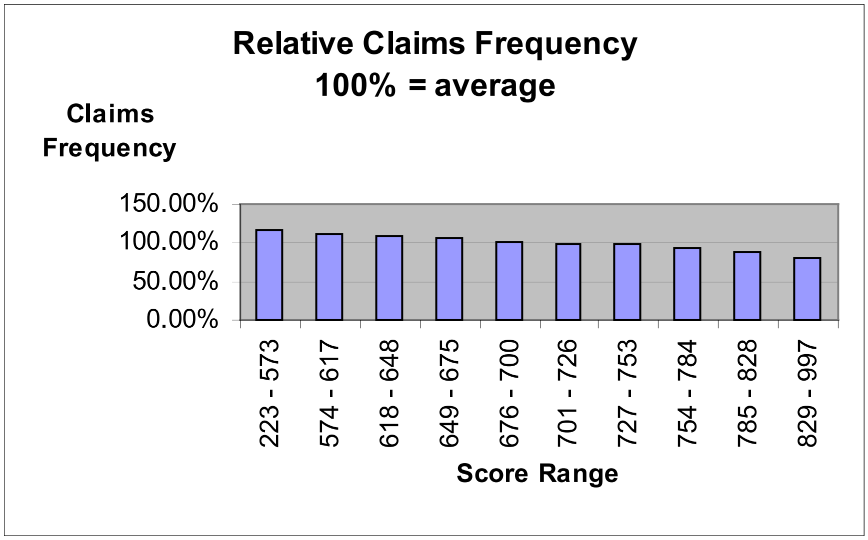
In meetings with legislators and regulators, questions have been asked about what can be done to protect consumers, while at the same time not damaging the benefits of insurance scoring. The industry is not of one mind on these recommendations. But here are a few:

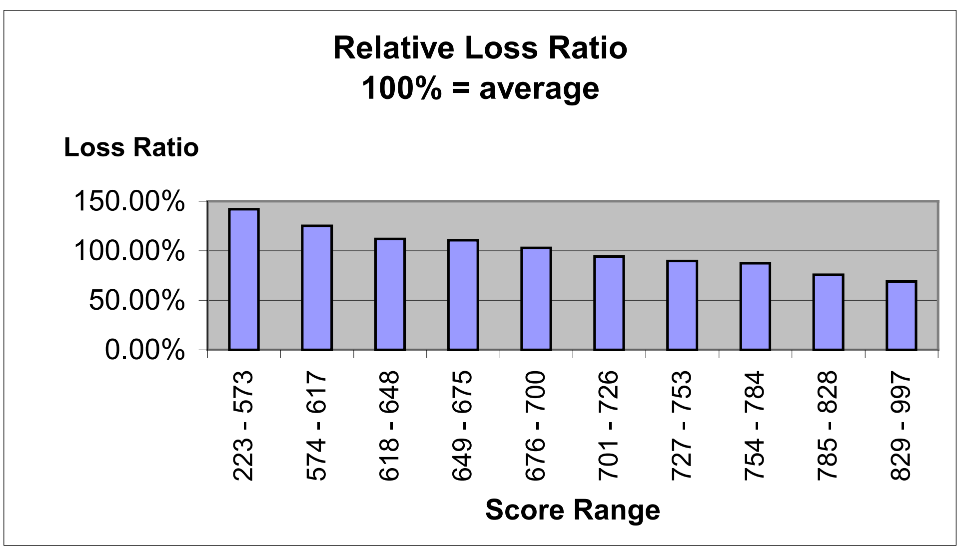
- Agent education has been spotty. ChoicePoint is working with the Big I and PIA to develop a distance learning continuing education course.
- Consumers need more information about insurance scores. Therefore, ChoicePoint has launched choicetrust.com and consumerdisclosure.com to help consumers.
- Our models focus on credit plus claims history to provide more accurate results.
- Our models are open to regulators for examination.
- Good public policy has lead to providing consumers with some protection against medical catastrophe, absence of any credit information and ability of consumers to correct or repair their credit report and get rescored by the insurance company.

Thank you for your time today.
I would be happy to answer any questions you might have.

Attachment A

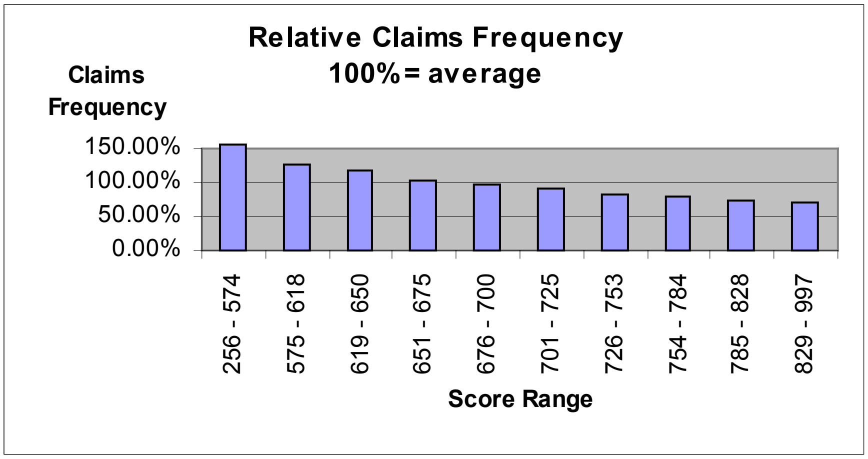
Standard Auto

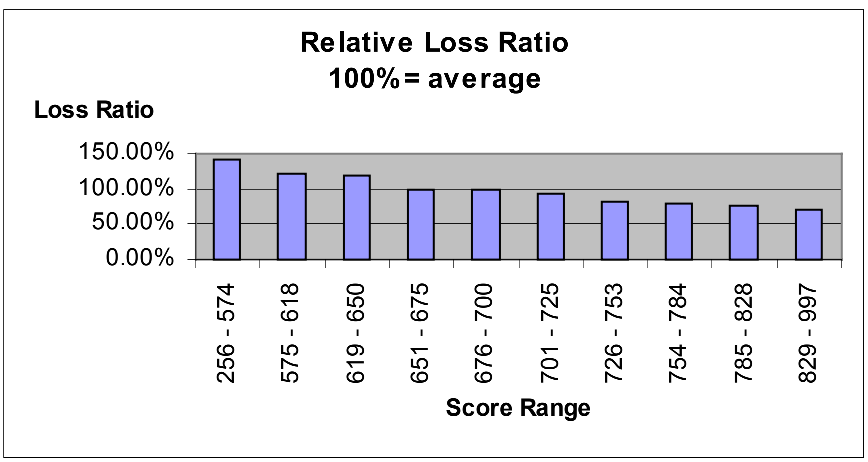




Attachment B

Non-Standard Auto





Attachment C

Homeowners