MICROFILM DIVIDER

OMB/RECORDS MANAGEMENT DIVISION
SFN 2053 (2/85) 5M

GREAT SEAL STATE OF NORTH DAKOTA

ROLL NUMBER

DESCRIPTION

1428

2001 HOUSE INDUSTRY, BUSINESS AND LABOR

HB 1428

2001 HOUSE STANDING COMMITTEE MINUTES

BILL/RESOLUTION NO. HB 1428

House Industry, Business and Labor Committee

☐ Conference Committee

Hearing Date Feb. 5 2001

Tape Number	Side A	Side B	Meter #
2	X		7.05-27.07
3	X		9.08-15.59
Committee Clerk Signature			

Minutes: Chairman R. Berg, Vice-Chair G. Keiser, Rep. M. Ekstrom, Rep. R. Froelich, Rep. G. Froseth, Rep. R. Jensen, Rep. N. Johnson, Rep. J. Kasper, Rep. M. Klein, Rep. Koppang, Rep. D. Lemieux, Rep. B. Pietsch, Rep. D. Ruby, Rep. D. Severson, Rep. E. Thorpe.

Rep Mike Grosz: Sponsoring bill to define the rating score for insurance companies.

Rep Johnson: How do you police this?

Rep Grosz: They would have to give you two reasons why you are being denied.

Rep Kim Koppelman: Currently you can be denied insurance because of a credit problem even if your credit is an unrelated issue. This is a post consumer regulation.

Pat Ward: *ND Domestic Insurance Co.* **Opposed with written testimony.**

Rep Froseth: How is potential-to-earn rated?

Ward: It's based on performance with credit but flexibility is offered.

Kent Olson: *NDPIA* We are mildly opposed.

Vice-Chairman Keiser: We'll close the hearing on HB 1428.

Rep Keiser: I move a do not pass.

Rep Koppang: I second.

13 yea, 0 nay, 2 absent **Carrier Rep Froseth**

Date: 2-5-01
Roll Call Vote #: 1

2001 HOUSE STANDING COMMITTEE ROLL CALL VOTES
BILL/RESOLUTION NO. ~~Click here to type Bill/Resolution No.~~ 1428

House Industry, Business and Labor Committee

☐ Subcommittee on

or

☐ Conference Committee

Legislative Council Amendment Number

Action Taken Do Not Pass

Motion Made By Keiser Seconded By Koppang

Representatives	Yes	No	Representatives	Yes	No
Chairman- Rick Berg	✓		Rep. Jim Kasper	✓	
Vice-Chairman George Keiser	✓		Rep. Matthew M. Klein	✓	
Rep. Mary Ekstorm	✓		Rep. Myron Koppang	✓	
Rep. Rod Froelich			Rep. Doug Lemieux		
Rep. Glen Froseth	✓		Rep. Bill Pietsch	✓	
Rep. Roxanne Jensen	✓		Rep. Dan Ruby	✓	
Rep. Nancy Johnson	✓		Rep. Dale C. Severson	✓	
			Rep. Elwood Thorpe	✓	

Total (Yes) 13 No 0

Absent 2

Floor Assignment Rep Froseth

If the vote is on an amendment, briefly indicate intent:

REPORT OF STANDING COMMITTEE (410)
February 6, 2001 8:03 a.m.

Module No: HR-21-2434
Carrier: Froseth
Insert LC: . Title: .

REPORT OF STANDING COMMITTEE

HB 1428: Industry, Business and Labor Committee (Rep. Berg, Chairman) recommends **DO NOT PASS** (13 YEAS, 0 NAYS, 2 ABSENT AND NOT VOTING). HB 1428 was placed on the Eleventh order on the calendar.

2001 TESTIMONY

HB 1428

NEWS YOU CAN USE

Credit-scoring secrets are soon to be revealed

BY PAUL J. LIM

You lost, scoring *only* 550. Your dutiful neighbor won, with an 800, headed for that five-bedroom manse in the suburbs. Your sister is right on the cusp, with a 626, her loan application sitting in purgatory awaiting further review.

This is the world of credit scoring, where a little-known three-digit number called your "FICO score" pretty much determines whether you'll get the house of your dreams or the car of your fantasies. It's not unlike high school, when SAT scores separated the most likely to succeed from the also-rans. Someone is still keeping tabs, in a decision-making process obscured from public view.

But that's about to change. Before the end of March, Fair, Isaac & Co. of San Rafael, Calif., creator of the FICO credit-scoring system, and Equifax, a leading credit bureau, will begin making these scores—which range from 300 to 900—available at their Web sites for a nominal fee. Fair, Isaac still won't disclose the precise methodology by which it determines the creditworthiness of borrowers, based on the amount of debt they have outstanding and their history of paying bills. But even though the scoring process may seem hard to fathom, knowing your FICO number is helpful in figuring out how to get the best deal on many types of loans. That's valuable information because 75 percent of all mortgage loans are sorted on the basis of FICO scores. "Lenders are *increasingly relying* on these scores," says Chris Larsen, CEO of online lender E-Loan. Dependence on credit scores has deepened since the FICO model was established in 1988 as an increasing number of lenders moved to automated loan approvals. "Many loan products, including some home-equity loans and auto loans, are based almost entirely on your FICO score," adds Larsen.

Despite their importance, FICO scores have largely been kept secret from consumers. But growing pressure from consumer groups led to congressional hearings late last year, and California will require lenders to disclose credit scores beginning this summer, along with an explanation of why scores weren't higher.

By the numbers. The changes couldn't have come at a better time. Even with the slowing economy, home sales are strong. Rates on 30-year fixed-rate mortgages have fallen from 8.65 percent last May to around 7 percent now, opening up a floodgate of refinancing activity.

Now, armed with your FICO number, you will be able to review your credit practices and begin making adjustments to boost your scores. However, you may be surprised to find out that some moves may actually be counterproductive—such as closing out a little-used credit card dating back to college, which shortens your credit history. You will learn that searching often for the best online mortgages can have a deleterious effect on your credit score, suggesting a hunger for debt that will unnerve potential lenders.

Most of those lenders will be happy if your score is 700 or higher. Even though you may still qualify for a loan with a lower score, it will cost you. E-Loan recently examined auto loans and found that consumers with scores of 720 or higher could expect rates of about 7.1 percent, while those scoring between 680 and 719 were getting loans at 9 percent. Meanwhile, if you scored 640 to 679, you would have been charged 10 percent. Anything under 640 and you'd likely be looking at rates of 11 percent or more. The differences add up. A $20,000 car loan for five years at 11 percent will wind up costing you $5,600 more for the life of the loan than if financed at 7.1 percent.

But what if your score falls below 680, the point at which many lenders begin examining an application more closely, or below 620, which many lenders consider problematic? What can you do to improve your score? First, you need to understand how your score is calculated:

Payment history. This is the key determinant of your score: Thirty-five percent of the number is based on whether you've

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paid your bills on time. Fortunately, most consumers do so. Sixty percent of borrowers score 700 or higher, which is considered good, if not excellent. Meanwhile, only 13 percent fall below 600.

Debt levels. Your total amount of debt, including balances on credit cards, car loans, and student loans, accounts for the next 30 percent of your score. "So keep balances low in general, especially on revolving debt," notes Fair, Isaac general manager Cheri St. John. That's exactly what Paul Makris did two years ago. In an effort to refinance his home mortgage at the lowest rate, the 48-year-old attorney in Huntington Beach, Calif., cashed in some stock market winnings and paid off about $46,000 on two outstanding car loans. He then used another $10,000 to pay off the balances on four credit cards. The move raised his score, already in the 700s, by about 20 points, his mortgage broker told him. Though pleased, Makris says he "was a bit shocked" that erasing his debts didn't improve his credit more.

Makris's experience points out one of the many quirks in the FICO system. Makris quite naturally thought he would get more credit for eliminating his card balances. "Everyone would agree that paying off revolving debt is a good thing," says Fair, Isaac spokesman Craig Watts. But all things being equal, "having a little balance on a line of credit is a little better than no balance at all," he says. A zero balance provides less information to the FICO scoring model about one's ability to manage debt than keeping a small balance.

Credit history. How long you have had credit counts for 15 percent of the FICO score. In addition to keeping credit card balances at zero, many cardholders go the extra step and close out old accounts. While financial planners say this is a good move, it could end up lowering your score. FICO scores take into account both the age of your oldest account and the average age of all your accounts. By closing out old cards, you may inadvertently lower your score by shortening your credit history.

Closing old accounts can hurt in another way. The FICO model rewards consumers who maintain a big cushion between their outstanding balances and

ILLUSTRATION BY GARY KENNIE FOR USN&WR

their credit limits—say, $1,000 owed on a card with a $10,000 limit. But close out an old account with no balance, and you will also reduce the overall amount of credit available to you. At the very least, "Don't try to consolidate your accounts into one or two cards if that pushes you over the limits on those cards," recommends St. John.

New debt. When interest rates are falling, consumers often shop for lower-rate cards. While this may reduce your monthly minimum payments, it might hurt your score, of which 10 percent is based upon your application history. Each time you apply for credit, the lender pulls a credit report. All this shopping around makes it look as if you are hungry to take on more debt.

"If you look at it from the credit issuer's point of view, they don't want someone who constantly jumps from lender to lender," says Steve Rho founder of Myvesta.org, a counseling agency. "They want someone who establishes a line of credit and keeps it."

Credit mix. The final 10 percent of your score is based on how much credit you have and the types of debt you have incurred. Having too many accounts—say, a card from every store in town—could be harmful to your score.

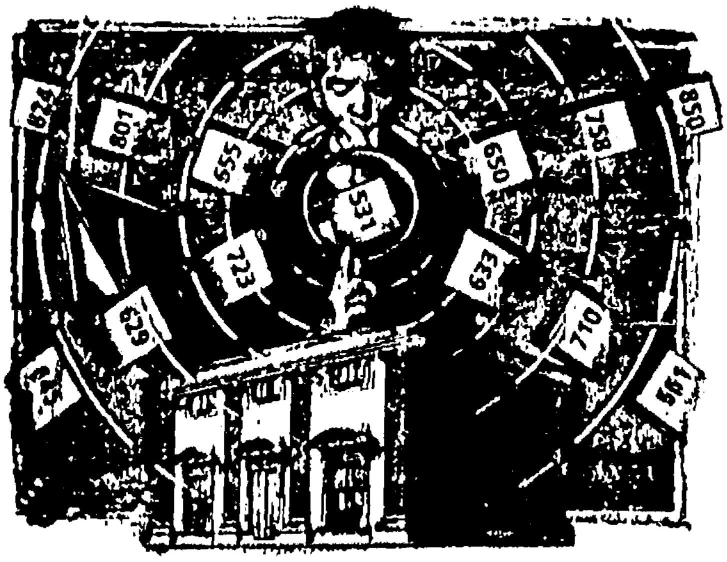
Now that the scores are becoming more widely available, lenders and credit counselors advise getting to know them. Mistakes do occur. Perhaps a lender credited an auto payment to the wrong account, or your payment got lost in the mail. It pays to recognize these instances and correct them. "I run my own score and my wife's twice a year every year to put my mind at ease," says Jeff Lazerson, a mortgage broker and president of Portfolio Mortgage in Lake Forest, Calif. In October, Lazerson discovered that some credit information belonging to his brother, whose Social Security number is just two digits different from his, found its way into his report. Luckily, it didn't affect his score because his brother also maintains good credit.

Keep in mind that not all lenders report to the three credit bureaus. Because some information may be lacking from a credit report, the FICO score you get through Equifax may not be the same as the FICO scores associated with your Experian or Trans Union credit reports.

If your lender rejects a loan because your Trans Union FICO score is, say, 600, but your Equifax score is 640, use that fact to negotiate with the lender. The bottom line: Take the same active role in managing your credit score as you would with any other financial matter, like your 401(k), for example. "People are really doing a good job of managing their assets," says E-Loan's Larsen. "We think consumers need to think about their debt the same way. They need to be opportunistic." •

MONEY MANEUVERS

Playing the mortgage game to win



As a lender, whom would you rather have as a customer? An unemployed artist who has no savings but pays bills on time? Or an investment banker earning $500,000 a year, with a pocket full of credit cards?

Seems obvious: the banker, right? But under the widely used credit scoring system, the two applicants might get surprisingly close scores. "FICO is a very good measure of what someone's credit looks like," says Stanford Kurland, CEO of Countrywide Home Loans in Calabasas, Calif. "But it's by no means the full picture."

While some auto loans are decided almost entirely on FICO scores, mortgage lenders also consider income, assets, or net worth, which FICO doesn't take into account.

The extra review could work to your advantage if your FICO score isn't sterling. Land a 720 or better, and you probably won't need to do much to secure the best available loan rate, notes Chris Larsen, chief executive of the online lender E-Loan. Drop down to between 620 and 679, and you may be asked some questions about your income and credit history. Be prepared to discuss late payments or heavy credit-card debt. Those scoring 619 or below will be red-flagged for serious inquiry. But people with low scores yet high incomes, or sizable investment portfolios, may still find lenders courting them. That's even more true in a competitive market, where lenders may be seeking a specific type of business or expanding into a new region.

Financial profile. At Freddie Mac, which buys mortgages from lenders, FICO scores are one of many variables that go into the company's mortgage scoring system, known as Loan Prospector. Other factors include the applicant's income and savings, and the size of a down payment.

"If someone with a 620 puts 5 percent down, then that score becomes very relevant," says David Andrukonis, chief credit officer for Freddie Mac in McLean, Va. "But if that borrower puts down 50 percent, the score might not matter as much."

Another factor you can control is the type of loan you choose. Lenders are tougher on borrowers seeking adjustable-rate mortgages rather than fixed-rate loans, because the payment on an adjustable could rise sharply if interest rates spike. Scores also tend to matter more when applying for a 30-year mortgage instead of a 15-year loan, as a person builds up equity more slowly in a longer-term mortgage. And they are more significant when purchasing a new home rather than refinancing. That's because when homeowners refinance at lower rates, they automatically reduce their monthly payments, thereby improving their financial position. *–P.J.L.*

ILLUSTRATION BY CARL HENRIE FOR USN&WR

The "real-world" experience of using credit information

Consumers benefit regardless of income or race: It is unfortunate that anyone would assume that low-income or minority consumers manage credit poorly. A study by a major insurance company shows great similarity in the average credit score for all income groups. After much study, the National Association of Insurance Commissioners could not find any studies in the insurance field that demonstrates the use of credit history in underwriting an insurance risk has had a disproportionate impact on protected classes.

Consumers support the use of credit reports: According to a Harris poll, nearly 70 percent of the public favors using credit information so financially stable people can pay lower premiums.

Credit reports are reliable: Studies by Arthur Andersen and the Insurance Research Council have found credit reports are much more reliable than motor vehicle records. Arthur Andersen found that only 2 percent of the 15,000 credit reports studied contain disputed information. Consumers also have a clearly defined review process to ensure the accuracy of their credit report.

So what's credit got to do with insurance underwriting?

- It provides an accurate predictor of loss.
- It fairly allocates the cost of coverage based on a consumer's claim potential.
- It provides an objective tool for decision-making that does not discriminate against any protected class members.
- It increases the availability and affordability of insurance for consumers.
- It allows insurers to underwrite some consumers who would not receive coverage using more traditional underwriting criteria.

NAII **National Association of Independent Insurers**

"What's Credit Got To Do With It?"

A Consumer Benefit

Most people have good credit and this information may be beneficial. Good credit may enable you to qualify for lower insurance rates. In some cases it can even offset a less than perfect driving record.

NAII **National Association of Independent Insurers**

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How Property and Casualty Insurers Use Credit Information in Underwriting

Setting the record straight:

The use of credit history by property and casualty insurers.

As the practice of using credit information in connection with insurance has grown more common, a number of state legislators and consumer groups have expressed concern about its impact on consumers. However, major insurance companies and organizations such as Fair, Isaac and Company and Tillinghast-Towers Perrin have studied the issue and found data to support using credit history as a predictor of claim filing. The Arizona and [illegible] insurance departments also have [illegible] these findings through [illegible] studies of their own on the [illegible]. After decades of use, insurance [illegible] have found that using credit [illegible] can help them write more [illegible] and allow consumers to pay less.

How are credit histories used?

To make well-informed decisions:
Insurers are interested in having available as many tools as possible to assist them in making a fair and objective underwriting decision. Credit history provides a consistent tool to evaluate risk that does not discriminate against any specific group of customers. It actually results in every customer paying his or her fair share for insurance.

One of many factors:
Most companies that use credit information treat it as just one of several factors in the underwriting decision. Generally your credit rating alone is not likely to keep you from getting insurance or cause you to pay more for it, although it can help you get insurance.

To increase business:
An NAII survey found that credit histories helped insurers write more policies. Companies said that they are able to accept some customers because the credit report offsets other information. One NAII member found that using credit histories enables it to charge 70 percent of its customers lower premiums than otherwise would be the case.

What is a credit score?

A credit score provides a numeric assessment of an individual's credit risk at a particular point in time. As new information is added to the report, the score can change. The score looks at specific credit information and assigns a weighted numerical value. It reflects credit payment patterns and looks at items such as collections, bankruptcies, outstanding debt, length of credit history, types of credit in use and the number of new applications for credit.

What's not included?

Only credit-related information is used in determining a score. The Equal Credit Opportunity Act prohibits the use of race, religion, gender, marital status and birthplace in determining a credit score.

What about privacy?

Most insurers only receive the credit score rather than the complete credit report. This protects the consumer's privacy. Insurers are more interested in how well a consumer handles their assets rather than how much money the consumer makes or who they owe.

continued on back page

[illegible] Practice

[illegible], the U.S. Congress passed the Fair [illegible] Act (FCRA), which permits insurers to [illegible] in making underwriting and

A Strong Link

Several independent studies have proven a strong connection between credit history and the likelihood of an individual filing a claim.

An Objective Tool

Credit information is an objective tool for decision-making. This tool avoids subjective value judgments because the information is based solely on credit related material.