

NATIONAL ASSOCIATION OF INDEPENDENT INSURERS

Getting a C.L.U.E. About the Impact of Loss History on Homeowners Insurance Rates

For many of us, buying a home is the single most important - and expensive - purchase we make. Finding the home that meets our needs is a tough job that requires a significant amount of effort.

Consumers rely on the representations made by the seller - whether an individual or a construction company - regarding the condition of the home. In fact, many states mandate that sellers provide buyers with certain information regarding the condition and history of the home.

Insurance companies also need information to determine a fair and accurate price for such insurance based on the risk characteristics of the property and the homeowner. When considering an application to write a new policy on an existing home, insurers have always requested the claim history on the person applying for insurance, as well as information on the condition and maintenance of the home that is about to be purchased.

However, many consumers often do not recall important details about prior losses they have experienced, such as the exact date of the loss or the amount paid to repair the damages. Home buyers also have no information on a property other than that provided by the seller. For insurers, this meant expending substantial time and resources to track down the specifics of prior loss information, including searching public records and requesting information from the home seller's current insurance company.

Advances in technology have streamlined this process, making the exchange of this information much more expedient, and allowing insurers to price their products more accurately. This benefits home buyers, home sellers, realtors and insurers. In the early 1990s, some insurance companies began to use a loss history database operated by an outside vendor to access important underwriting information.

By agreeing to post its company's loss data to the database, an insurance company gained the ability to access loss data from other companies. This allows all participating insurers to access accurate information about losses, including specific dates, causes, and the extent of damage. Moreover, consumers can access their own loss histories, an important feature when selling a home or switching insurance companies.

One of the leading vendors of claim history information is ChoicePoint, a data management company located in Alpharetta, Georgia. ChoicePoint compiles and

distributes the loss information in a database known as C.L.U.E. (Comprehensive Loss Underwriting Exchange). Another significant provider of such information is the Insurance Services Office (ISO), whose database is known as the Automated Property Loss Underwriting System (A-PLUS). Many people commonly refer to reports from either vendor as "C.L.U.E. reports."

Some realtors and real estate sales organizations contend that C.L.U.E. reports are an unnecessary obstacle to buying and selling homes. Some insurance regulators have expressed concerns that C.L.U.E. reports contain too much data, particularly in situations where a loss may have occurred but the insurance company was not contractually obligated to pay - usually because the loss was below the policyholder's deductible.

Despite these objections, there is no evidence to suggest that home sales have been affected by a supposed inability to obtain homeowners insurance. In fact, the National Association of Realtors recently reported that existing homes sold at an annualized rate of 6.09 million houses in January 2003, a 3 percent gain from December 2002, and the strongest monthly rate ever.

The Importance of Historical Data as an Underwriting Factor

The concept of risk-based pricing is the cornerstone of insurance underwriting because insurance contracts look forward at what *might* happen during the policy period. Insurers have always relied on historical data to help them accurately underwrite and price insurance policies. Generally speaking, the higher the risk (the greater the probability that the insurance company will have to pay a severe claim or a high number of frequent claims), the higher the price. This assures that prices are fair to all consumers and that lower risk consumers are not forced to subsidize the losses of their higher risk peers.

That's why a person's driving record is one of the most important factors that insurance companies use to determine a fair and accurate price for auto insurance policies. Individuals with a history of moving violations and accidents - even if they don't result in an insured loss - and a history of previous insurance claims are statistically much more likely to have more frequent and more severe insured losses in the future. As such, these higher risk individuals will pay more for their auto insurance policies.

Likewise, claims history is one of the most important factors that insurance companies use to underwrite and rate homeowners insurance policies. For a homeowners policy, loss history has two parts:

- a) a particular property's claims history (how many claims have been reported; how many resulted in loss payments; and how much each loss cost); and

b) b) an individual's claims history (how many claims has a person filed and the circumstances of each).

The price of insurance for homes and homeowners with a history of losses will be generally higher than for those without such claims. And in some cases, fewer companies will compete for these types of risks.

In cases where loss history does not exist - the purchase of a newly constructed home, for instance - insurers will rely more heavily on factors such as type of construction and material, geographic location, amount of coverage, and proximity to police and fire stations to determine an accurate price for the policy.

Of course, most of the information used to underwrite and rate policies comes from information on the application. Insurers also use outside sources to confirm information on the application and seek information most applicants simply do not have. C.L.U.E. reports are the most common source for such information.

In order to clarify the most common misconceptions about this important underwriting and rating tool and to help legislators, regulators, the news media, and consumers better understand the value of C.L.U.E. reports to insurers, realtors, and consumers, the National Association of Independent Insurers (NAII) has developed the following "Frequently Asked Questions" about C.L.U.E.

FREQUENTLY ASKED QUESTIONS ABOUT C.L.U.E. AND HOMEOWNERS INSURANCE UNDERWRITING

1) What is C.L.U.E.?

C.L.U.E. is a loss history information exchange that enables insurance companies to access prior loss information in the homeowners underwriting and rating process. C.L.U.E. personal property reports contain up to five years of personal property losses and include policy information such as name, date of birth, and claim information such as date of loss, type of loss and amounts paid. The C.L.U.E. homeowners database is 10-years old. More than 600 companies representing over 90 percent of the homeowners market provide loss data to C.L.U.E. and over 40 million claims are currently loaded into the system.

2) Why are C.L.U.E. reports important?

C.L.U.E. personal property reports help insurers and agents deliver fast, more accurate, and less expensive, underwriting decisions. C.L.U.E. reports speed up the insurance transaction, facilitate prompt real estate transactions, and provide homeowners and potential homeowners important information before making one of the most significant investment decisions of their lives. C.L.U.E. reports also have some fraud detection and prevention benefits, although the database was not developed as a fraud-fighting tool.

3) How did insurers obtain this information before C.L.U.E. was created?

Insurers have always utilized loss histories as a primary underwriting and rating factor for homeowners insurance policies. Prior to the advent of C.L.U.E., insurers considering an application to write a new policy on an existing home obtained property loss histories in various ways: searching public records, requesting information from the applicant, and requesting information from the insurer currently writing the coverage for the property. The advent of C.L.U.E. has made the exchange of this information much more accurate and expedient, benefiting home buyers, home sellers, realtors and insurers.

4) Who contributes to the C.L.U.E. database?

Only insurance companies that subscribe to C.L.U.E. can submit loss data and access C.L.U.E. reports. Consumers can access C.L.U.E. reports on themselves and their own properties, although potential homebuyers can certainly require that sellers provide a current copy of the property's C.L.U.E. report prior to sale.

5) Who decides what information is reported?

Information for the database, including what fields to use, reporting requirements, and the rules for reporting data was developed by a panel of insurance companies that contribute information to C.L.U.E. This was done to assure that all loss histories submitted to C.L.U.E. - and all information that is accessed by insurers and consumers - are uniform and consistent.

6) What type of information is in the database?

C.L.U.E. reports contain specific information on the dates of initial reports of possible claims plus a brief description of the claims status. Reports also reflect changes in the claim as it is investigated, adjusted and settled. If the expected loss were significant or catastrophic, the C.L.U.E. report would show an "Open Claim" with the amount paid by the insurance company as of the date of the report. The C.L.U.E. report would reflect changes in the status of such claims as the company records them.

Some state legislators and insurance regulators are encouraging insurers to report only losses that result in a claim payment to C.L.U.E. However, many insurers and even some realtors contend that such information is not only a valid consideration for underwriters, but also for prospective home buyers, who are entitled to know detailed loss history for the property they are planning to purchase.

7) Is there any other information besides loss history in the database?

Only loss history information is stored in the database. No other sources of data - credit reports, criminal records, civil lawsuits, legal judgments - are incorporated into C.L.U.E. reports.

8) How do insurers use C.L.U.E. reports?

C.L.U.E. reports are used almost exclusively to underwrite and rate *new* policies. Most insurers renewing existing policies do not access C.L.U.E. reports at renewal, largely because they already have loss histories for these properties in their own database. Also, since the average homeowner files an insurance claim only once every 10 years, the vast majority of C.L.U.E. reports - 70 percent - have no reported claims or paid losses.

Each insurer decides how to use the C.L.U.E. report based on its own underwriting and rating standards. For instance, a home with two water damage claims within the past five years may qualify for standard pricing with some companies, while for others it may trigger a move to a higher risk pricing tier. Still others may decide to not underwrite the risk at all. The homeowners insurance market is extremely competitive in most states with many insurers vying for business on the basis of price, quality of insurance product, and service. Loss histories are only one of many different factors that companies consider.

Most state insurance laws provide insurance companies 60 days to review all the underwriting factors, including C.L.U.E. reports, after issuing a policy. However, a policy often must be in place at the closing, which typically occurs long before the 60-day insurance company review window closes. Insurers and realtors are currently discussing this issue in several states.

However, it is important to note that there is no evidence - statistical or anecdotal - that indicates that the 60-day underwriting period or the review of C.L.U.E. reports is having a negative impact on the real estate market. In fact, the National Association of Realtors recently reported that existing homes sold at an annualized rate of 6.09 million houses in January 2003, a 3 percent gain from December 2002, and the strongest monthly rate ever.

9) Who has access to C.L.U.E.?

Insurance companies that contribute loss data to C.L.U.E. can withdraw information from the exchange. In addition, some insurance agents, with the authority of the company they represent, can withdraw data.

Equally important, consumers have access to the C.L.U.E. report on themselves and their own properties. It is an extremely valuable tool and, like your credit report, it should be checked periodically to make sure all the information contained on the report is accurate and up to date.

C.L.U.E. reports are playing an increasingly important role in real estate transactions. It is important for consumers to remember that only sellers have access to a C.L.U.E. report on their own property. However, many buyers are now stipulating that a copy of the report be disclosed as a condition of the real estate contract. In fact, some states are even considering legislation that would make this a requirement of any real estate transaction.

10) How can consumers review their homes' C.L.U.E. reports?

Consumers can access the C.L.U.E. report for their own home through one of two Web sites maintained by ChoicePoint - www.consumerdisclosure.com or www.choicetrust.com. Consumers can order the reports online or print the application form and request a report by mail for a charge ranging between \$8.00 - \$12.95.

11) How can consumers correct erroneous information on their C.L.U.E. report?

Though statistics show that C.L.U.E. reports are 99.9 percent accurate, there is a well-defined path for consumers to follow in investigating and correcting any suspected errors. If consumers discover an error on their C.L.U.E. report - an invalid claim report or an incorrect loss payment, for instance - they can contact ChoicePoint directly and report the problem. ChoicePoint will then contact the insurance company on the consumer's behalf and ask for clarification on the matter. The company has 30 days to respond to ChoicePoint and provide evidence that the information on the C.L.U.E. report is accurate. ChoicePoint will follow-up with the insurer after 20 days if the company does not respond and again after 28 days without a response. If the company does not respond within 30 days, ChoicePoint will remove the information

from the database. It is important to note, however, that a vast majority of disputes are resolved within two weeks.

12) Can insurers add notes to a consumer's C.L.U.E. file?

Only consumers can add notations to their individual C.L.U.E. reports. For instance, if a dog bite claim occurs and the homeowner gets rid of the dog, the consumer can add this notation to the C.L.U.E. report for that property. Insurance companies are not allowed to add notations to the database.

13) Can C.L.U.E. reports distinguish between an inquiry and a claim?

C.L.U.E. reports indicate losses by type. Consumers should be aware that contacting their company or their agent to discuss an actual loss is generally considered reporting a claim, even if the company does not end up making a claim payment. This is because a loss has occurred that may be covered by the terms of the policy, which requires the company to take specific actions within specified time frames.

For instance, a consumer may contact her agent to report an event, such as a broken water pipe, and to determine the extent of coverage in order to decide whether or not to go forward with the claims process with the company. The insurer may not indemnify the consumer for this loss for a variety of reasons: the amount of damage may be below the deductible; the consumer may decide to pay for the damage himself; or there may be no coverage for such a loss under the terms of the policy.

Even though the insurer may not make a loss payment on this claim, this information is recorded by the company and may appear on a C.L.U.E. report. The important fact remains, however, that a loss has occurred and, especially with regards to water damage, prospective buyers should be informed of this event.

An inquiry is generally regarded as a call by a consumer to a company representative or agent to discuss terms of coverage where no actual loss has taken place. Most companies will not report such information to C.L.U.E. Many insurers are working on ways to inform their policyholders about the important distinction between a loss and an inquiry.

Insurers and other interested groups are discussing these issues with public policy makers in an effort to develop effective solutions without burdensome legislation or regulation. However, some states have considered legislation on this matter. At least one state, Georgia, has issued a directive defining a claim to be used in making an underwriting decision.

14) How often does the consumer challenge C.L.U.E. report information? How often do such inquiries result in changes to C.L.U.E. reports?

Only four out of every thousand C.L.U.E. reports ordered (four-tenths of 1 percent) result in a consumer requesting a copy of his or her report. Disputes over information in a C.L.U.E. report arise only in only three out of every 10,000 cases (three-hundredths of 1 percent).