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March 25, 2003

William Robinson and James Curley
Actuaries
Arizona Department of Insurance

By Electronic Mail

Re: Proposed Credit Unemployment and Credit Property Loss Ratio Standards and Prima Facie Rates

Dear Messrs. Robinson and Curley:

We write to comment on the actuarial reports and recommendations for credit unemployment and credit property loss ratios and prima facie rates. Thank you for your thoughtful draft reports and for the opportunity to comment.

In addition to providing comments on your draft reports, we also write to request copies of comments submitted by any other interested party on your draft reports.

We see no rationale for the proposed 50% loss ratio and strongly urge a loss ratio standard of at least 60% for single life credit unemployment coverages, at least 70% for joint life credit unemployment coverages and at least 60% for credit property coverages.

The proposed 50% standard is unreasonably low for several reasons. First, the NAIC models include a 60% minimum loss ratio standard. The most recent effort by the NAIC, after a year of extensive discussion, was to establish a 60% minimum loss ratio standard for credit property. Even after challenge by the National Conference of Insurance Legislators of the loss ratio standard, the NAIC upheld the 60% standard. We see no Arizona-specific facts or circumstances that warrant a standard lower than the 60% standard developed by the NAIC.

Second, the California Department of Insurance held a **two-year proceeding** on credit unemployment and credit property rates with extensive written testimony and public hearings. The CDI selected 60% minimum loss ratio standards based on that very extensive review. We strongly recommend that the Commissioner and Arizona Department of Insurance staff review some of the documents in the California proceeding, available at the following web address: http://www.insurance.ca.gov/docs/FS-WhatsNew.htm. We also strongly recommend that the Commissioner and Arizona Department of Insurance staff contact the California Department of Insurance actuary who worked on these regulations – Eric Johnson. We also attach testimony we provided in that proceeding which demonstrated the reasonableness of loss ratios of 60% or higher.

Third, the insurers' own rate filings for credit unemployment call for a 55% loss ratio *on average* – even with inflated commissions, overstated profit and understated investment income. The loss ratio standard should be geared to the least efficient insurer, but to a standard that ensures good value to the consumer.

Fourth, the issue of fluctuation or margin should **not** lead to a reduction in loss ratio to 50%. Fluctuation or margin is already considered in the profit provision. Consequently, a further reduction in the loss ration would double count a provision for fluctuation or margin. Also, fluctuation in credit unemployment claim costs should be addressed by reviewing a longer period of historical experience and/or adjusting recent experience for current unemployment rates. The recently promulgated California credit unemployment regulation does exactly this, while maintaining a 60% loss ratio. Projected credit property claim costs should include a provision for catastrophes, but the target loss ratio should be at least 60%. Stated differently, a cat provision should affect the estimate of expected claim costs, but should not affect the target loss ratio that represents the minimum benefits to consumers in relation to premium costs.

Fifth, because of reverse competition, historical expenses and commissions can not be considered reasonable expenses and commissions. Historical expense and commission experience is therefore not a reasonable basis for establishing loss ratio standards.

Sixth, a higher loss ratio standard does not penalize credit insurers. Credit insurers can simply enrich the benefits in the policy to achieve the higher loss ratio standard. A good example is moving from a credit property policy form with numerous exclusions to an all risk policy. In contrast, a lower loss ratio simply means a lower percentage of the premium dollar going to claims and an unreasonably low amount of benefit in relation to premium for the consumer.

In summary, every bit of available information suggests a loss ratio standard of at least 60% for single life credit unemployment coverages, at least 70% for joint life credit unemployment coverages and at least 60% for credit property coverages. We see no facts to support a lower loss ratio standard in Arizona than in the NAIC models.

It is important to keep in mind the reverse competitive structure of credit insurance markets. Insurers compete by offering greater commissioners to the producer of the business and generally seek to sell the highest cost, highest profit coverages to consumers. A high loss ratio standard is reasonable and necessary to ensure that consumers get reasonable benefits in relation to the premiums charged. A higher loss ratio for joint life products is necessary to ensure that lenders do not have an incentive to sell the joint life product regardless of the needs of the consumer.

Thanks again for your consideration. Please let me know if we can provide any additional information.

Sincerely,

Birny Birnbaum
Executive Director

Attachments: California Credit IUI and Credit Property Regulation
January 2001 testimony of Consumers Union in California
September 2002 testimony of Consumers Union in California