How Does Your Credit Score Affect Car Insurance Rates?

by Laura Agadoni

You probably know that you need a good credit score to get the best rates on loans or to even qualify for a loan. That three-digit number, issued by the three credit-reporting agencies, indicates how responsible you are with your money. Sometimes you need a good credit score to be considered for certain jobs. What's more, your credit score can affect your car insurance rates.

Good vs. Bad Credit

If you are careless with your finances and have a bad credit score, your auto insurance provider -- rightly or wrongly -- might think you'd be a careless driver, too. The higher your credit score, the better you look to auto insurers. Conversely, the lower the score, the worse you look. Just as credit-reporting agencies use a formula to determine your credit score, many insurance companies go by an "insurance risk score." A main difference in how a credit score and an insurance risk score are determined is that 30 percent of your credit score is determined by how much you owe, but insurance companies don't really care about that. They are most concerned with how regularly you pay your bills, says Craig Watts with Fair Isaac Corp. in Insure.com.

Tips the Scales

At some insurance companies, your credit score can work for or against you regarding what type of premium you are charged or whether you can get insurance at all. For example, if you have some prior insurance claims but you have excellent credit, State Farm would be more likely to insure you, says Dick Luedke, a State Farm spokesperson at Insure.com. If all State Farm sees are prior claims and not your high credit score, the company may deny you insurance coverage.

Not Transparent

Critics of insurance risk scores are bothered that insurance companies won't reveal how they arrive at their numbers, as the credit-reporting agencies do. The five factors that determine your credit score, in order of importance, are your past payment history; the amount you owe; how long you've had credit; how much new credit you've opened; and the types of credit you have. But insurance companies develop their own models to determine what they consider a high- or low-risk customer, and they are unlikely to tell anyone this proprietary information. You can get a free copy of your credit report once every 12 months from Experian, TransUnion and Equifax and pay a nominal fee to see your actual score. But you probably cannot see your insurance risk score because insurers do not need to give you that information.

More Claims Filed

Although no one can pinpoint the exact reason, people with bad credit scores file about 40 percent more claims than drivers with good credit, according to the Insurance Information Institute. Based on this information, insurance companies charge people who have bad credit 20 percent to 50 percent more for premiums, says Clarence Smith of the research firm Conning & Co. in Bankrate.com. FICO credit scores range from 300 to 850. If you have an excellent credit score of 785 or higher, tell your insurance agent to make sure that score has been reflected on your premiums. Some states have banned insurance risk scoring, so check with your insurance agent to find out whether the practice might apply to you.