Automobile Insurance Reform in Canada: Increasing Costs and Proposed Solutions

Gilles Bernier and Anne E. Kleffner
WRIA Meeting - Las Vegas
January 3, 2004
Outline of Presentation

- Automobile Insurance in Canada
- Evidence of Crisis
- Public Policy Issues
- Current Reforms
- Tort versus No-Fault
- Implications & Hypotheses
- Future Work
## Automobile Insurance in Canada

<table>
<thead>
<tr>
<th></th>
<th>Tort</th>
<th>No-fault</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td>Quebec (1978)</td>
</tr>
<tr>
<td>Private</td>
<td>All Others</td>
<td>Ontario (1990)</td>
</tr>
</tbody>
</table>
Automobile Insurance in Canada

- Not one “best” system
- Each with its own advantages/disadvantages
  - Public versus Private
  - Tort versus No-fault
- Recently, provinces with private insurance have experienced “crises”
Evidence of Crisis

- Increasing number of bodily injury claims per 100 vehicles despite decreasing number of property damage claims per 100 vehicles.
- Compensation awards for sprains and strains have risen dramatically.
- Claim costs per earned vehicle is increasing much faster than CPI.
- Increasing dissatisfaction of consumers
Evidence of Crisis

- Premiums increased by 27% over the period 1997-2002, yet cost of injury claims grew by 74% and cost of claims for vehicle damage grew by 42%.

- Medical and rehabilitation costs incurred by auto insurers in Alberta, Ontario and the Atlantic region have increased on average 37% per year since 1990, compared to a 2.5% increase in general healthcare costs.
Key Question for Reform

- What is the primary purpose of automobile insurance?
  - Is it to establish liability?
  - Is it to facilitate recovery?

- Different answers will likely result in different automobile insurance systems.
Public Policy Issues

- Ultimately, choices belong to provinces.
- Public policy toward auto insurance is likely to continue to vary across Canada.
- Types of auto insurance reforms:
  - One dealing with the **parameters** of the current system – short-term
  - One proposing a **migration** to a new model – long-term
Reforms in Public Provinces

- Québec: Planning to modify its Pure No-fault in cases of criminal car accidents (e.g., drunk driving). Victims and/or families would regain the right to sue.

- Québec also plans to separate the functions within the QAIB in order to:
  - make it profitable again (heavy investment losses in 2002); and
  - make it more accountable as an insurance entity;
Reforms in Public Provinces

- **Manitoba**
  - In 2000, MPI added an optional IRE to top-up the standard maximum yearly income insured under PIPP;
  - In 2003, MPI stretched into fifth year of rate stability.

- **British Columbia**
  - ICBC must now submit its rate application to the Utilities Commission for review and approval. Effective for 2004 rates.

- **Saskatchewan**
  - Jan.1, 2003: Choice between tort or no fault.
## Status of Provincial Reforms: Private Provinces

<table>
<thead>
<tr>
<th></th>
<th>AB</th>
<th>ONT</th>
<th>NB</th>
<th>NS</th>
<th>PEI</th>
<th>NFLD</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Legislation</strong></td>
<td>Bill 53</td>
<td>Bill 59</td>
<td>Bill 1</td>
<td>Bill 1</td>
<td>Bill 8</td>
<td>New govt</td>
</tr>
<tr>
<td></td>
<td>Royal assent</td>
<td>passed. New</td>
<td>enacted Aug,</td>
<td>enacted Nov,</td>
<td>enacted Dec,</td>
<td>studying issue</td>
</tr>
<tr>
<td><strong>Price Freeze</strong></td>
<td>Rates frozen</td>
<td>Rates frozen</td>
<td>Rates frozen.</td>
<td>Rates frozen.</td>
<td>NA</td>
<td>NA</td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>Mandatory</td>
<td>20 % rollback</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>rebates</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Cost action</strong></td>
<td>Tort-based</td>
<td>Containing</td>
<td>Cap on P&amp;S</td>
<td>Cap on P&amp;S</td>
<td>Cap on P&amp;S</td>
<td>NA</td>
</tr>
<tr>
<td></td>
<td>refinements</td>
<td>AB costs:</td>
<td>awards for</td>
<td>awards for</td>
<td>awards for</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td>PAF model</td>
<td>minor injuries</td>
<td>minor injuries</td>
<td>minor injuries</td>
<td></td>
</tr>
<tr>
<td><strong>Industry</strong></td>
<td>Major reforms</td>
<td>Unknown</td>
<td>Increased</td>
<td>Increased</td>
<td>Increased</td>
<td>NA</td>
</tr>
<tr>
<td><strong>regulation</strong></td>
<td>pending</td>
<td></td>
<td>price regulation</td>
<td>price regulation</td>
<td>price regulation</td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td></td>
<td>regulation</td>
<td>regulation</td>
<td>regulation</td>
<td></td>
</tr>
</tbody>
</table>
Reforms in Private Provinces

- Restrictions on rating criteria (prohibit use of age, sex and marital status).
- Restrictions on underwriting criteria (prohibit insurers from refusing to insure a person because of age, age of car, lapse in coverage, etc.)
- Caps on pain and suffering awards for minor injuries ($2,500 - $4,000)
- Increased price regulation
Private versus Public Ownership in Canada

- Public ownership and NF generally come together (except in B.C.)

- Performance of provinces with public auto insurance is somewhat questionable:
  - Evidence of higher average auto insurance costs (and for NF provinces) [Kleffner & Schmit (1999)]
  - Evidence of higher auto collision, death/injury/property damage rates in those provinces than those with market-based insurance. [Fraser Institute (2003); Kovacs & Leadbetter (IBC, 2003)]
No-fault versus Tort

Advantages of No-Fault
- Full compensation for economic losses;
- Potentially higher relative benefits for claimants;
- Reduction in claim investigation and litigation costs;
- Provision of a more equitable distribution of benefits to car accident victims.

Disadvantages of No-Fault
- Limits or prohibits a person’s right to sue.
- Could lead to less safety (e.g. an increase in fatal auto accident rates);
- Could lead to a cost increase due to greater eligibility for benefits and greater incentives to fraud.
Implications

- Impact of no-fault on total costs is ambiguous. Average severity is expected to decline, but there is an increase in the number of eligible claimants. Also, there is an expected decrease in LAE. Costs will decrease if the reduction in average claim severity and LAE exceeds the cost of greater number of claims.

- H1: No-Fault systems reduce overall automobile insurance costs per insured vehicle (Kleffner & Schmit JIR, 1999). Evidence.
Implications

- Lower LAE imply that the average loss ratio in NF provinces should be higher than in tort provinces (IL/EP). However, IL are expected to rise in NF. Given data limitations, hypotheses regarding the Gross Loss Ratio (IL + LAE/EP) are less straightforward.

- H2: The gross loss ratio (IL + LAE)/EP is higher in no-fault provinces than tort provinces due to lower risk (Kleffner & Schmit JIR, 1999).

- Evidence
Data and Models

- 1991-2002
- Eight jurisdictions: (Atlantic provinces and the territories are combined).

\[(IL + LAE)/Earned\ \text{Exposures} = f(NF, GOV, Wage, Pop)\]

\[(IL + LAE)/EP = f(NF, GOV, Year)\]
Future Work

- Conduct tests to determine whether average auto insurance costs per insured vehicle, and gross loss ratios, are lower in no-fault provinces.
- Examine the impact of reforms in individual provinces.
- Examine the impact of choice no-fault in Saskatchewan.
Factors that Drive the Cost of Auto Insurance

Claims Experience & Operating Expenses

Taxes
- Premium Taxes
- Capital Taxes
- Health Levies
- HST payable on claims
- Income Taxes

Repairing Physical Damage
- Severity of accident
- Cost of auto parts
- Type of vehicles
- Mechanic prices
- Tow truck fees
- Frequency of Accidents

Compensating Personal Injuries

Schedule B Benefits
- Regulation of Health Care providers
- Medical Fees
- Frequency of treatment
- Length of treatment
- Statutory Benefit levels

Tort Costs
- Frequency of Accidents
- Severity of Accidents
- Regulation of legal professions
- Legal thresholds
- Court awards