SESSION V
“PUBLIC CONCERNS AND MARKET CHOICES”

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QUESTIONS TO BE ADDRESSED

Purpose: Share some thoughts in order to discuss these 2 questions.

1. IS THERE A «BEST PRACTICE» FOR PUBLIC POLICY TOWARD P&C BUSINESS IN CANADA?

2. HOW TO NEGOTIATE THE POLITICAL ECONOMY OF REGULATING P&C BUSINESS IN CANADA?
« BEST PRACTICE »
A DEFINITION

– Not easy to define such a concept.

– Suggested definition:

   Public policies in a given jurisdiction can be considered to be « best practice » policies if their performance is at least as good as that of policies in other jurisdictions with similar objectives and priorities.
PUBLIC POLICY TOWARD BUSINESS: BACKGROUND

- Most public policies toward business are related to the place of «competition» in a market economy:
  - Some policies promote competition;
  - Others prevent it,
  - Others supplant it by taking an activity «out of the market place».

- In practice, this subject is as much concerned with issues of «equity» as with «efficiency».
THE POLITICAL ECONOMY OF INTERVENTIONISM IN CANADA

- Green in his 1980 book *Canadian Industrial Organization and Policy* discusses the case of Canada in these terms:
  - « interventionism has been considered the natural and necessary result of Canada’s peculiar geographic and demographic characteristics ».
  - « much economic legislation is enacted at the provincial level. Unfortunately, the provinces are much less likely to see the « national » implications of their economic legislation ». 
PUBLIC POLICY TOWARD P&C BUSINESS IN CANADA

1. Competition policy
   – **Easy entry** for both Canadian and Foreign companies;
   – Prevents undue concentration in the industry:
     • P/C is a less concentrated market than L/H and Banking;
   – **Should be continued**, given that international competition is likely to make domestic providers more efficient.
2. Public ownership

- Arguments usually given:
  - Incomplete coverage of needy users
  - Theoretically lower administrative costs.

- Choice belongs (by Constitution) to provinces
  - Likely to reflect geographic variation in objectives and priorities.

- Comes often with No-fault but not always.
  - Social pricing and perverse incentives?
2. Public ownership (cont’)

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

• P&C Insurers are subject to regulation of their pricing (auto), distribution and investments activities.

• Regulation should bring welfare benefits to the parties involved
  – Whether it does or not is a complex issue!

• Regulation theories (1970’s) teach us that regulation can be a “trap”, both economically and politically.
3. Regulation (cont’)

- Example of a possible “regulatory trap” for consumers:
  "Rate regulation in automobile insurance".

- Strong evidence from the U.S. that, in the long run, rate regulation has not resulted in lower prices [Cummins et al, (2001), Harrington (2001)];

- Also evidence (both in the U.S. and Canada) that rate regulation (prior approval) leads to greater volatility of automobile insurance premiums [e.g., Harrington (2001) and Leadbetter, Voll & Weider (IBC, 2003)].
3. Regulation (cont’)

- Solvency regulation is an example where Canada seems to be doing relatively well!
  - Consistency of federal (solvency) regulation is a positive factor which should be maintained
  - Kleffner and Jorgensen (1997): «… federal regulation of insurers in Canada is more consistent than regulation of insurers on a state by state basis in the U.S.. Canadian regulation also appears to have been more timely and proactive than in the U.S., particularly with respect to risk-based capital standards… ».
  - In regulating P&C insurers’ solvency, it is important to account for the interaction between investments, leverage and product line mix (Lamm-Tennant, 1995).
HOW TO NEGOTIATE THE POLITICAL ECONOMY OF REGULATING P&C?

– By recognizing that ultimately, choices belong mostly to provinces.
– Public policy toward P&C is likely to continue to vary across Canada.
– Types of auto insurance reforms:
  • One dealing with the parameters of the current system (tort provinces) – short-time
  • One proposing a migration to a new model – long-term
HOW TO NEGOTIATE THE POLITICAL ECONOMY OF REGULATING P&C?

– Provincial auto insurance reforms must address this key question:
  • What is the primary purpose of automobile insurance?
    – Is it to establish liability?
    or,
    – Is it to facilitate recovery?

– Two different purposes are likely to lead to different models.
HOW TO NEGOTIATE THE POLITICAL ECONOMY OF REGULATING P&C?

- Quebec picked «facilitate recovery» as an answer back in 1978 and migrated to an «hybrid» system designed as follows:
  - Pure No-fault for bodily injuries
  - Private insurance for liability and property damage with a «direct compensation agreement»

- Without being perfect, the Quebec model is certainly worth analyzing by provinces with a similar objective.

- It is functioning with a relatively high degree of overall satisfaction to the different stakeholders. Something must be done right in that context!