Auto Insurance
Restoring the Balance

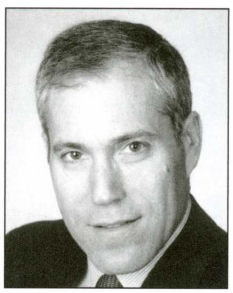
"Tort law's capacity for fairness and justice should not be ignored . . . The public's expectations and sense of fairness would be offended if the more seriously injured were not permitted to have access to compensation for both economic and non-economic loss assessed on an individual case-by-case basis."[1]

BY RICHARD C. HALPERN

In my view, many tort limiting reforms to auto insurance have been misguided and unnecessary, allowing a bloated and inefficient first party benefit system to emerge that all but ignores fundamental rights of access to justice.

The Insurance Act requires a review of auto insurance every five years and is currently being reviewed by the Superintendent of Insurance. As stakeholders consider auto insurance reform for this year's review, it is hoped that they will heed the words of the Honourable Coulter Osborne (in his 1988 Inquiry into Motor Vehicle Accident Compensation in Ontario). In his report Mr. Osborne pushed for a "peaceful coexistence between tort and no fault." Unfortunately, since 1990, when enhanced first party benefits were first introduced, the balance between tort rights and first party benefits has been upset by ill-considered reforms. This process has failed to introduce any stability to auto insurance, has generated increasing complexity and also added unnecessary cost to the system.

Access to justice has been compromised once again through additional tort limiting changes affecting accidents occurring on and after Oct. 1, 2003, introduced at a time when reform was not called for and when any perceived problems in auto insurance arguably had no direct connection with tort rights.



Richard Halpern

Access to Justice and Insurer Profits

The verbal threshold affecting claims for pain and suffering established in 1996 is now subject to a regulation[2] which purports to define it for accidents occurring on and after Oct. 1, 2003. At that time, the deductible applying to those claims (where they do not exceed $100,000) was increased from $15,000 to $30,000.

In 1988, Osborne warned that threshold no-fault was inefficient and arbitrary. In November 2007, Osborne delivered a further report to the Attorney General on Civil Justice Reform.[3] While auto insurance was not part of the Terms of Reference, Osborne apparently felt compelled to comment on the verbal threshold and the deductibles, as matters relating to access to justice. He pointed out the significant transaction costs associated with the verbal threshold. He was referring to the fact that the determination of whether the threshold is met is not determined until the end of the case, after considerable expenditure by both parties, exhausting judicial resources and resulting in uncertainty. He also raised issues about the redundancy of having both a threshold and a deductible and raised concerns about the discriminatory nature of the threshold.

In my view, the additional reforms in 2003 were a response to deteriorating returns on equity (ROE) for auto insurers in Ontario. While it is true that ROE for 1999 to 2002 was below acceptable levels, the dismal financial results for that period could not be directly attributed to bodily injury claims costs and therefore additional limitations on tort rights were unjustified. At the same time, in 2003 auto insurance in Ontario made a substantial recovery, without the impact of the 2003 changes.

Claims costs for 1999 to 2002 were entirely predictable, particularly for bodily injury. Since at least as early as 1992 claims costs have followed a consistent pattern of change without any meaningful deviation. While claims costs have been historically stable, ROE has not. Plotting ROE on a graph shows a wavy pattern which has been described as cyclical.

The cyclical nature of auto insurer profit is not a direct function of claims costs. It is also not a direct function of changes in returns on investments,

which have also followed a consistent trend since at least 1996 (albeit downward). The cycles are caused by pricing that fails to properly follow predictable claims cost patterns and by an environment that allows a lag between the need for rate change and the implementation of any rate change.

Responding to cycles in profitability by imposing limitations in tort is therefore inappropriate. Such measures have failed and will continue to fail to address the underlying problems. It is important to recognize this fact and work to re-establish that "peaceful co-existence" between tort and first party benefits. Limiting tort rights cannot and never will bring stability to auto insurance. If participants in this process are going to achieve any success in providing the Ontario public with a stable product and value for their premium dollar, it is time to undo the errors of earlier reforms and identify where the problems really lie.

The environment that allows large swings in ROE includes market forces within the auto insurance industry itself and insurer behaviour. At least in 2003 through 2006 the auto insurance industry in Ontario enjoyed handsome profits. That profitability has, to some extent, increased competition in the insurance market and helped drive premiums down. A pattern of declining premiums, competition for policy holders and diminished margins inevitably leads to decreased ROE. Unfortunately for Ontario consumers, rather than allowing market forces to dictate fiscal recovery, poor ROEs have led to calls for reforms to reduce costs, in essence legislating insurers out of a fiscal slump on the backs of innocent accident victims.

This is a pattern that continues to repeat itself. In 2004 premiums rose 11.8 per cent, while average claims costs dropped 10 per cent. In 2005 premiums went down by 3.3 per cent while claims costs went up by 5.5 per cent. If pricing more closely tracked cost developments (which are relatively predictable), were made in a more timely way and were introduced more gradually to consumers, there is good reason to believe that the perceived crises of the last couple of decades would have been prevented and the unwarranted reforms of the past avoided.

Superintendent Julie Dickson, of the Office of the Superintendent of Financial Institutions Canada, in a May 22, 2008 speech stated:

"The P & C industry is facing stress, once again, and numerous stresses. While all the stresses are not caused by the industry itself, some are, and I have to stop and ask why the players in the . . . P & C industry have trouble learning from the past . . . "[4]

One way to help the industry learn from the past, which would also result in considerable benefit to the public, is to make it clear that regulatory and legislative reform to auto insurance will be reserved for matters of public interest and will not be used to compensate for poor pricing practices or market forces within the industry.

In the mid-1980's the perceived insurance crisis which led to the first enhanced no-fault system in 1990 (OMPP) was largely based on anecdotal evidence and much rhetoric. Currently, some submissions for the five-year review of auto insurance adopt a similar approach, giving little consideration to other important factors, other than that of industry profitability. Given that auto insurance is compulsory, a much broader approach is called for.

In his 1988 inquiry into auto insurance Osborne said that "given the bodily injury cost trends, premiums which should have been increased earlier and more gradually, were increased in 1985/86 . . . the premium increase was probably justified, but given its sudden implementation consumer complaints were to be expected." The same is true for the period between 1999 to 2002. A similar pattern is emerging today. To a large extent, the insurance industry is its own worst enemy. The industry, however, ought not to expect the government to bail it out of diminished ROE by reforming the product. From an access to justice and public policy perspective, where auto insurance reform is needed, surely these changes ought not to be made on the backs of innocent accident victims.

Comprehensive reform

Having said that, there is little doubt but that costs associated with the auto insurance system are substantially too high. The first party benefit system is unnecessarily consuming huge amounts of premium dollars. The problem is not only the fact that the average claim per car for accident benefits is up over 21 per cent in the last three years. As significant is the fact that the existing first party benefit system is too complex and inefficient. We should not wait for insurer profitability to decline to address waste in the system.

Assessment costs are an incredible financial drain on the system, resulting in large sums being diverted away from compensation for real losses. The Insurance Bureau of Canada claims that for claims between $1,000 and $20,000, assessment costs added an additional 70 to 80 cents to every dollar spent on treatment. This is clearly not putting the money to good use. These transaction costs are entirely disproportionate to the matter at stake and an unjustified waste of our premium dollars. Reducing transaction costs, lowering assessment costs and introducing the concept of proportionality into the first party system is sorely needed.

Comprehensive reform of auto insurance is needed to achieve savings and a fair auto insurance product. Fixing the first party benefit system cannot be done by tinkering. The important interests of an affordable insurance product for consumers, the rights of accident victims and the need to ensure a viable and healthy insurance industry must figure prominently in any approach to reform. Restoring the balance means removing the waste from first party benefits and easing some of the restrictions on tort rights.

Richard Halpern is chair, Ontario Bar Association Working Group on Auto Insurance Reform; immediate past president, Ontario Trial Lawyers Association; partner, Thomson Rogers.

1 Report of Inquiry into Motor Vehicle Accident Compensation in Ontario, 1988, The Honourable Mr. Justice Coulter A. Osborne, Supreme Court of Ontario Commissioner, Volume 1, page 44, paragraph F113.

2 Ont. Reg 461/96, sections 4.1 and 4.2.

3 Civil Justice Reform Project, Summary of Findings and Recommendations, the Honourable Coulter Osborne, November 2007.

4 Remarks by Superintendent Julie Dickson, Office of the Superintendent of Financial Institutions Canada, to the Langdon Hall Property and Casualty Insurance Industry Forum, May 22, 2008.