

C11-11

ICBC_2006RR Exhibit C11-11



Automobile Insurance Review

[v.6]

March 1997

V.P.L.
BUSINESS AND
ECONOMICS

Report to the Honourable Andrew Petter

Minister of Finance and Corporate Relations, and Minister
Responsible for the Insurance Corporation of British Columbia

BUS-REF
368.572
A9392b
v.6

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Executive Summary

Introduction

The Review Team did its utmost, in a relatively short period of time, to understand all aspects of auto insurance in our province. Literature, analysis and critique were reviewed extensively. Experts on the subject, from inside and outside the province, were engaged in debate and analysis.

Review activity was centred in Vancouver and supported by a toll-free telephone line. The Review Team accommodated regional consultation where possible. This included visits to Kamloops and Victoria.

Consultations began in early December 1996 and continued until mid-February 1997. Some 800 submissions, in a variety of forms, including 75 oral presentations, were received and reviewed. More than 300 telephone calls were fielded, providing a wide range of comments, and suggestions.

Participants in the process included representatives from the legal profession, the insurance industry, consumer and automobile sector advocacy groups, accident victims groups, the health field, trade unions, engineering firms, community based organizations, sectoral organizations, the automotive industry, law enforcement and human rights groups.

Automobile Insurance in British Columbia

Although it is possible for society to take significant steps to reduce the number of

automobile accidents, even the best prevention measures will not result in the elimination of all accidents. It is therefore essential to have adequate insurance for all drivers.

The Insurance Corporation of British Columbia, the public and main automobile insurer, provides all mandatory basic coverage as well as an array of optional coverage including increased liability insurance, motor vehicle damage coverage and comprehensive coverage (windshield, theft, fire). A significant number of private insurance companies compete with ICBC for the optional coverage market, although ICBC has about 90 per cent of the optional insurance market.

Nature of the Challenge and the Case for Change

In recent months, a team of consulting firms, led by KPMG, Exactor Insurance Services Inc., and Eckler Partners Ltd. Actuaries and Consultants, released two major reports that found that claims costs, both for bodily injury and material damage, have increased sharply above the rate of inflation in the last decade, acknowledging a slight reversal of trend in the early 1990s before upward cost pressures were re-established. KPMG went on to say that the continuation of such real increases in claims costs can only result in large premium increases in the years ahead.

In their analysis, KPMG went on to address the underlying causes of the real

increases in claims cost. In the areas of material damage (damage to vehicles and other property), repair costs, the growing number of complex and sophisticated vehicles, and significant increases in vehicle theft were found to be the significant factors. For bodily injury, "social inflation" was suggested as the underlying problem. KPMG suggested that social inflation consisted of claimants wanting to maximize their awards, particularly those for pain and suffering, a growing sense of entitlement, greater reliance by claimants on legal representation, larger compensation awards in the Courts, and an increasing incidence of fraud.

For the years 1995 to 1998, KPMG suggested that claims costs per insured vehicle will increase by 5.5 per cent per annum after adjusting for inflation (5.0 per cent per year for bodily injury and 6.5 per cent per year for property damage). This assumes no change in accident prevention activities nor the implementation of other cost saving measures.

KPMG concluded that a status quo product and insurance environment cannot be sustained. *"By 1998, without a material change to the product and a focused attack on the underlying causes of trends, rate increases well into double digits may be required to bring ICBC back into a break-even operation position."*

The Review Approach

Given the above, the question is: what is the appropriate action or set of actions to address the problem?

From our perspective, it seems clear that all factors for possible improvement or change should be considered. The projected financial problem is large and will get larger unless corrective action is taken early. No one action is large enough in its own right to solve the problem. In addition, given ICBC's and KPMG's assessment of the problems, a behavioural change in our driving is also required.

Much has been written about auto insurance and the measures required to ensure such a system meets its objectives. Based on the literature and our discussions with a range of interested parties in British Columbia, the Review Team has concluded that, in addressing any type of auto insurance system, five principles must be paramount.

1. The auto insurance system should be fair and equitable.
2. The auto insurance system should be affordable.
3. The auto insurance system should be understood by those it serves.
4. The auto insurance system should foster good driving behaviour.
5. The auto insurance system should respond to need.

However, it differs from our current system in that it has an increased focus on care. It also reduces the benefits available for non-economic such as pain and suffering (damages). Although this product retains access to the court process, it places significant limitations on eligibility for non economic damages, and imposes a deductible.

Product Two is based on the KPMG Option C. This is a pure injury compensation system that focuses on providing care for all injured parties. Quebec and Manitoba have such products and the one in Saskatchewan is quite similar. This product assesses compensation for each claimant using a structured administrative and adjudicative process. The right of access to the court process is replaced by an alternate dispute resolution system.

There is no distinction in benefits between an innocent victim and an at-fault claimant. Income replacement is based on net income, with a weekly limit applying to all claimants. With this product, there is no compensation for pain and suffering, although there is limited compensation available for loss of function.

Product One represents a compromise and in some ways is a variant of the current ICBC product. It generally retains the distinction between innocent and at-fault except in the case of medical benefits and rehabilitation where everyone is treated the same. It is designed to meet the needs of those most seriously injured, either in the form of care or other damages. To succeed, it would require an effective co-existence between elements of a court-based system and an injury compensation system.

With the introduction of limits on other damages such as pain and suffering, accompanied by a deductible, it would be increasingly important for ICBC to provide economic benefits (income replacement, medical and rehabilitation care) early in the claims process, and in a fair manner.

Product Two represents more of a departure from our current auto insurance system. It has a particular focus on restoring all injured parties but also attempts to strike a balance between fairness, equity, meeting the need and efficiency, within the constraints of affordability. With this product, it would be essential for benefit levels to be high enough to restore injured parties and meet the needs of an average income earner. An external appeal process would be an important element of this approach.

In essence, the two products are not vastly different, since the care component, and therefore the policy priority to restore all seriously-injured claimants, is the same.

In the case of both products, it is not possible to retain all the benefits of the current product and still meet the affordability constraint that has been provided by government. However, it is possible to increase efficiency and redistribute benefits in a fairer manner; that is what we have tried to accomplish.

Given the affordability constraint, we believe that both products meet the tests in other areas.

If Product One was implemented, it is estimated that ICBC would have a small surplus in its rate stabilization fund at the end of 1998 and 1999, and be in a deficit by the end of 2000, with an increasing

deficit thereafter (see details in Appendix VII). In effect, this option provides two years to find additional solutions prior to returning to a deficit situation.

If Product Two was implemented, the rate stabilization fund would maintain a surplus over each of the next three years. However, annual operating deficits would begin after that point, and the rate stabilization fund would then be quickly eroded (see details in Appendix VII). This product provides some additional time to address underlying cost trends, and provides some financial resources to address them.

Several conclusions can be drawn from this analysis:

- Both products provide ICBC with temporary financial relief, with Product Two doing so for a longer period than Product One. Neither can control the long term underlying increasing cost trend.
- Modest accident reduction and service enhancement savings are not enough. The degree of commitment to these measures must be more substantial to generate greater savings. Without prompt action on these measures, significant rate increases will be inevitable.
- The time available to decide on and then implement change is very short. Action is required on both fronts: product change and preventative measures.

Conclusion

The measures discussed in this report are intended to make sure British Columbians continue to be protected, by auto insurance at a reasonable cost to themselves and to our province.

The Review Team believes that the key to this in the long term is accident prevention. Implementation of each of the items discussed in this report, if undertaken in a comprehensive manner, on a very large scale, and by 1998, could bring under control the rising costs of both personal injury and property damage.

The changes we have proposed are significant and will not be easy to implement. However, they are necessary if our auto insurance is going to be adequate and affordable, and if British Columbians are going to be safe on our roads.

Implementing change will be a major challenge for ICBC, for government and for every BC driver. However, the need for change is pressing. The time to act is now.

Appendix VII

Estimated ICBC Operating Surplus/(Deficit) in \$millions

	1997	1998	1999	2000
Status Quo	(385)	(384)	(676)	(971)
Product One	—	244	41	(226)
Product Two	—	417	272	6

Estimated ICBC Closing Rate Stabilization Fund in \$millions

	1997	1998	1999	2000
Status Quo	(193)	(577)	(1,253)	(2,224)
Product One	—	51	92	(134)
Product Two	—	224	496	502