

Lemons and Peaches: Comparing Auto Insurance Across Canada

Introduction

Myths abound on the issue of public versus private auto insurance. Some people posit that public auto insurance is safer, cheaper, less discriminatory, and more generous than private insurance.

None of these claims are true. In fact, the exact opposite of these statements is a closer description of reality.

For example, the first *Fraser Alert* in this auto insurance series presented data showing that vehicle collision rates are higher in the provinces with near-monopoly public auto insurance than elsewhere in Canada. The use of “social risk pricing,” whereby riskier drivers are subsidized by the rest, also leads to deliberate premium discrimination



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Main Conclusions

- **Provinces with public auto insurance have the highest premiums and the lowest claims payouts in Canada, producing low auto insurance value (claims payouts compared to premiums)**
- **Provinces with public auto insurance also have a high number of claims per driver, between two and four times the number in the private sector, pointing to lax system management**
- **Insurance value has been falling in provinces with public auto insurance systems for the past eight years and rising in provinces where drivers are insured by the private sector**
- **The Atlantic provinces provide the best insurance value on these measures, with low premiums and higher-than-average claims payouts. Alberta and Ontario have higher premiums but also pay the highest claims in Canada. All are peachy deals.**
- **By comparison, the public sector auto insurance systems are lemons, combining high premiums with very low claims payouts**
- **BC's public system is the most extreme case, with an average premium 20 percent above the national level and an average claim 50 percent below the national level. The equivalent of almost 40 percent of BC drivers make a claim every year.**

against safer drivers, who are predominantly older, more experienced, and female—and are more numerous.¹

Two later publications investigated the issue of premium levels and premium growth by province.²

This research found that provinces with public auto insurance schemes have relatively high premiums, partly owing to tax subsidies and inadequate financial reserves. Average premium levels have also been rising in all provinces, whether vehicles are insured publicly or privately, contrary to Statistics Canada’s consumer price indices, which inaccurately measured auto insurance premiums for a number of years in the late 1990s.

The present *Fraser Alert* extends this line of analysis to assess the degree to which provincial auto insurance systems offer good insurance value for money.

Insurance can be seen as a pooling of risk, with all policyholders paying premiums to ensure that some receive benefits if a collision, theft, or other misfortune

occurs. Though insurers act as intermediaries in this process, the fundamental truth is that the system is a self-insuring one, with funds circulating between policyholders.

An important measure of auto insurance value is whether the insurer is collecting more, about the same, or less than the amount of premiums necessary to pay the costs incurred by those who are insured. Not collecting enough can lead to bankruptcy, while collecting too much is wasteful. Collecting about the same as the amount paid out means that the insurer is acting as an efficient agent on behalf of those insured.

Therefore, the effectiveness of auto insurance can be assessed by comparing the average premium paid with the average value of a claim, somewhat akin to a cost-benefit type of calculation. The insurance product has more value in the hands of a claims recipient if the claims payment-to-premium ratio is relatively high. It is also in the interests of all policyholders to keep the number of claims low, so as to keep average premiums low.

Comparing Claims Payouts

With that starting point, figures 1 to 3 show average claims by province. The appendix discusses data and analytical issues associated with calculating the statistics presented in this report.

There are two conclusions to draw from this inter-provincial claims comparison.

First, average claim payouts in the private sector are much higher than those in the public sector, especially in Manitoba and BC. Claim payout levels in Saskatchewan and Quebec, which have publicly-provided auto insurance, are half those of Ontario, the province with private-sector auto insurance that paid out the highest average claims in 2002. Claim payout levels in Manitoba and BC, which also have publicly-provided auto insurance, are about 70 percent lower.

Second, private sector payouts have been increasing over time, while those in the public sector are relatively stagnant and are declining after adjustment for general inflation. Of the public

Figure 1: Average Claim (Private Sector Provinces)

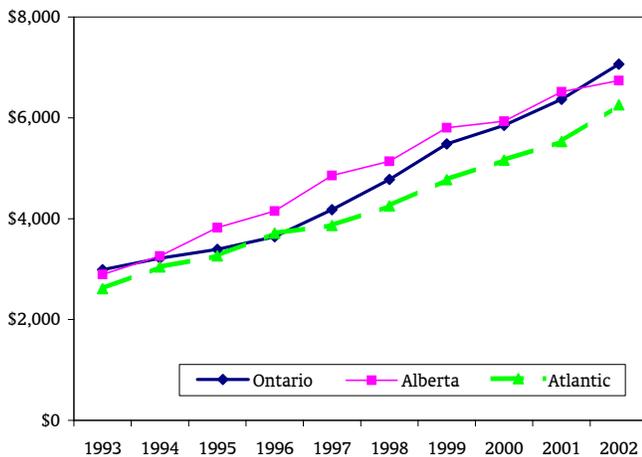


Figure 2: Average Claim (Atlantic Provinces)

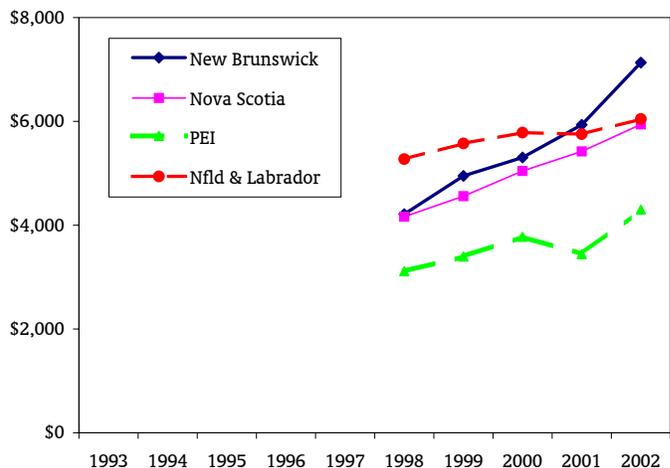


Figure 3: Average Claim (Public Sector Provinces)

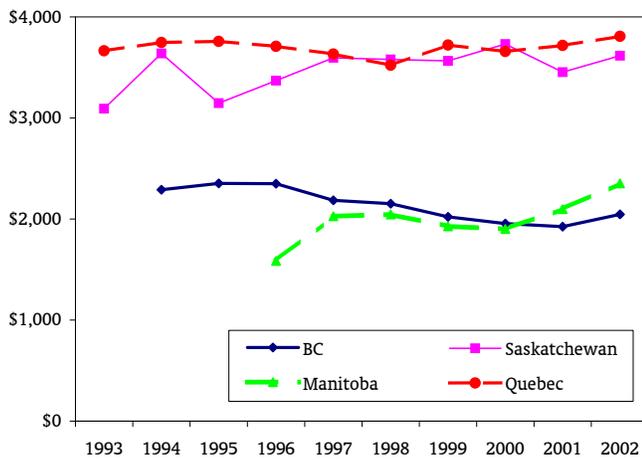


Figure 4: Claims per Driver (Private Sector Provinces)

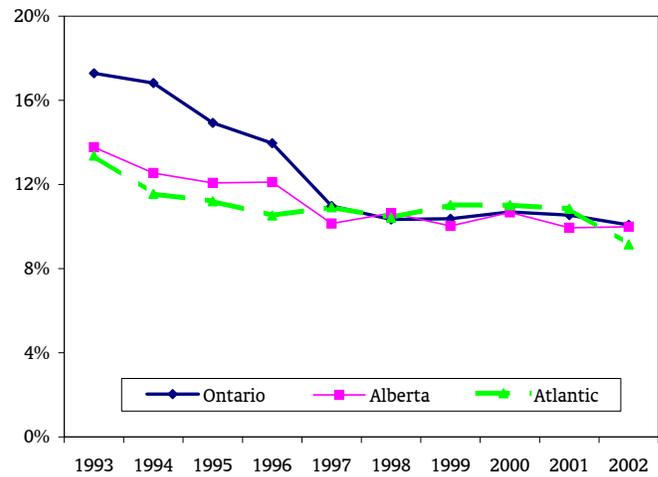


Figure 5: Claims per Driver (Atlantic Provinces)

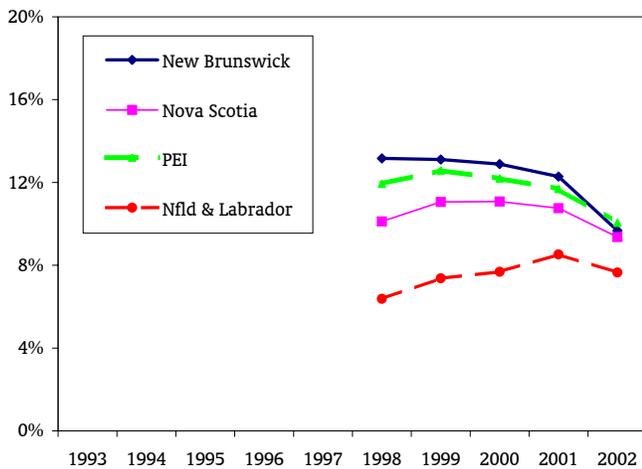
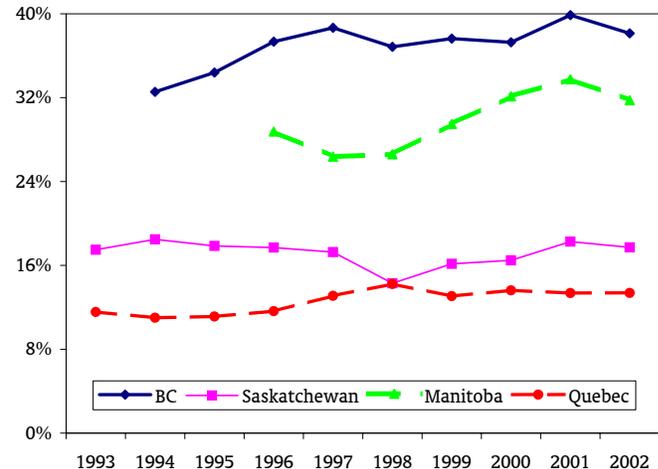


Figure 6: Claims per Driver (Public Sector Provinces)



insurers, only Manitoba, with a nominal growth rate of just over 4 percent annually for the past eight years, saw a significant rise in its average claim payout.

More detailed data from the public sector monopolies are difficult to obtain.

However, a closer look at the type of claim by province shows that the private sector makes collision and accident benefit payouts two to three times higher than do the public sector insurers in either Manitoba or BC. Whether the insurance system in the province is private or public, personal injury

claims are the most powerful force behind rising average claims in every province, while growth in collision claims has typically been slower.

Comparing Frequency of Claims

Figures 4 to 6 show another striking difference between the two auto insurance systems: the frequency of claims per driver is much higher in the provinces where vehicles are insured with a public program.

The six provinces with private sector auto insurance (Ontario, Alberta, and the Atlantic region) have annual claims rates of between almost 8 percent and 10 percent. Quebec, with its mixed private-public system, has a claims rate one-third higher at 13 percent. BC, meanwhile, with a purely public auto insurance system, is tops, with a claims rate at over 38 percent. Manitoba and Saskatchewan also have very high claims per driver.³

Unlike the average claims payout comparison, the frequency of claims against private sector

insurers are declining, while those against public auto insurers are rising. This is a key measure of efficiency in an insurance system, as a high frequency claims rate indicates payouts that are unrelated to the underlying risk of the insured pool. The private system thus seems to be better managed than the public system on this measure and is improving its management performance over time.

Again, more detailed evidence supports these conclusions regarding the overall number of claims per driver.

In British Columbia, collision claims per driver are three to six times higher, comprehensive claims frequency is 20 percent to two times higher, and accident benefit claims per driver are five to ten times higher than in the provinces with private sector auto insurance. Similarly, Manitoba property damage claims frequency is skewed higher. Property damage claims are also an important factor pushing claims frequency higher in many provinces.

Comparing Premiums

Figures 7 to 9 show average auto insurance premiums by province. As these numbers have been presented in earlier research,⁴ only the broadest conclusions will be discussed here. See the appendix for more on the premium calculation approach.

The four provinces with public sector auto insurance had relatively high average provincial premiums in 2002. Drivers in BC paid the most at just over \$1,000 per year, which is 20 percent above the premiums paid in the

Figure 7: Average Premium (Private Sector Provinces)

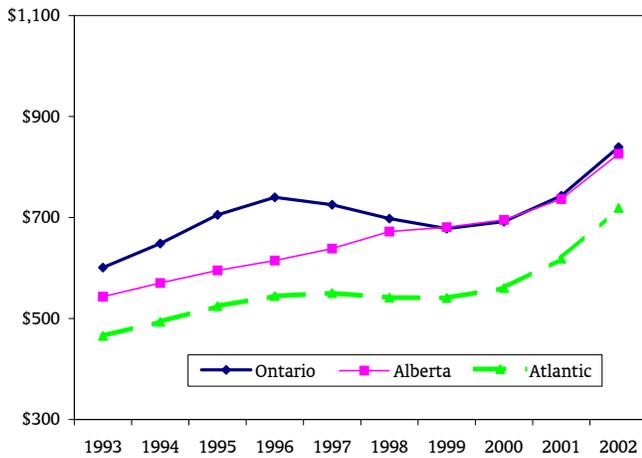


Figure 8: Average Premium (Atlantic Provinces)

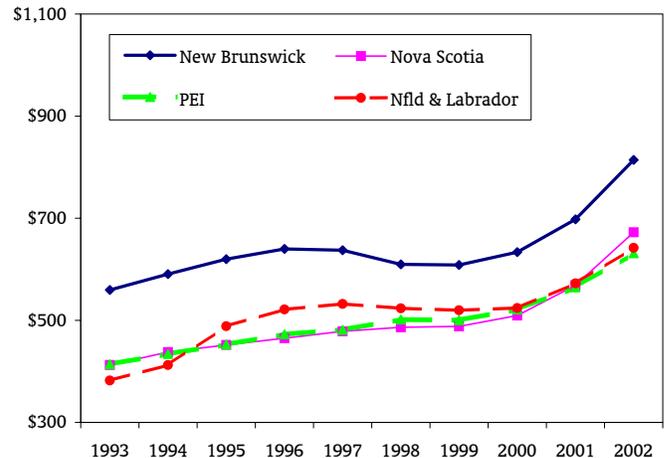


Figure 9: Average Premium (Public Sector Provinces)

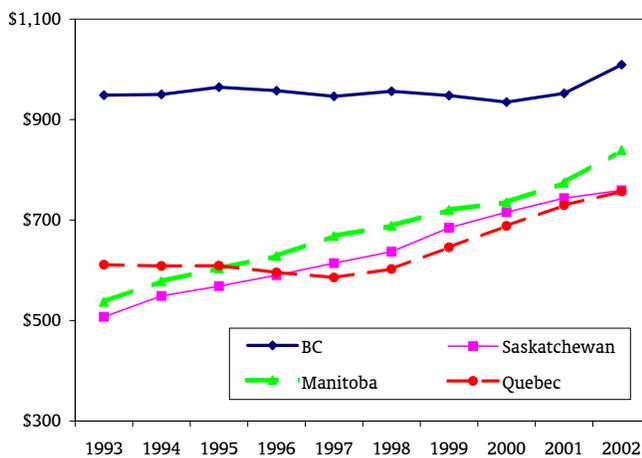
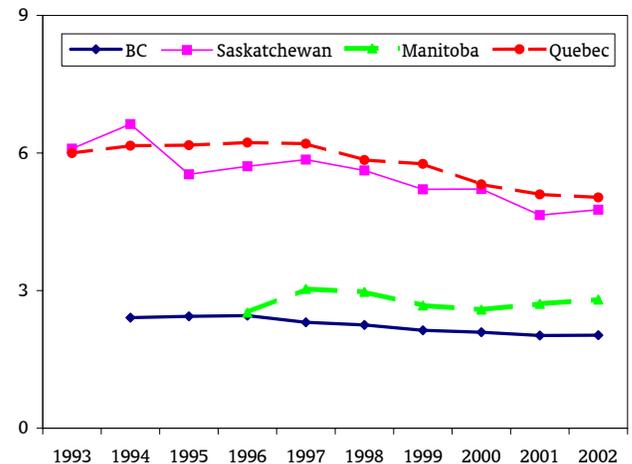


Figure 10: Claim-to-Premium Ratio (Public Sector Provinces)



provinces with the next three highest rates: Ontario, Manitoba, and Alberta. Saskatchewan and Quebec had mid-range premium rates, while the lowest premium rate was in PEI.

In all provinces, premiums have been increasing. The Canadian annual average premium growth rate over the eight years to 2002 was 2.8 percent. Only BC's premiums grew at a rate noticeably slower than that national average, with Quebec matching the national premium growth rate.

Comparing Insurance Value

Insurance value is defined here as the average claim payout compared to the average premium. A higher ratio indicates more value and an increasing ratio is reflective of rising value.

Ultimately, total premiums and total claims payouts must balance (absent changes in invested premium returns) to preserve financial solvency in the system. Over a long period, insurance value

should therefore generally reflect the trend in claims frequency, with higher claims frequency leading to lower insurance value.

Figures 10 to 12 show the levels of, and changes in, insurance value by province. Insurance value improved noticeably during the 1990s in the private sector, while it gradually declined in the provinces with a public auto insurance sector.

For example, in Ontario, where drivers are covered by private auto insurance, average claims were five times higher than average premiums in 1993; the ratio was over 8-to-1 in 2002.

By contrast, insurance value in all of the provinces with public sector auto insurance continuously declined in the 1990s and the ratio of average claims to average premiums ranged between 2 times and 5 times in 2002.

Table 1 shows the ranking of premiums, claims, and insurance value by province.

The Atlantic provinces offer the best deal, with relatively modest premiums and higher-than-average claims payouts. Ontario

and Alberta have high premiums but they also have the highest claims payouts. Saskatchewan and Quebec have mid-range premiums but low claims payouts. BC and Manitoba have an unattractive combination of high average premiums and low average claims, and also have very high and growing claims per driver.

These combinations are highlighted in figure 13, where average premiums and claims payouts are plotted. The ideal location is the southeast quadrant

Table 1: Auto Insurance Ranking of Provinces

Province	Lowest Premium	Highest Claim	Insurance Value
NF	2	4	1
NB	6	1	2
NS	3	5	2
ON	8	2	3
AB	7	3	4
PEI	1	6	5
PQ	4	7	6
SK	5	8	7
MB	8	9	8
BC	10	10	9

Note: 1 is best ranking, 10 is worst ranking in 2002.

Source: Author's calculations from IBC and insurer reports.

Figure 11: Claim-to-Premium Ratio (Private Sector Provinces)

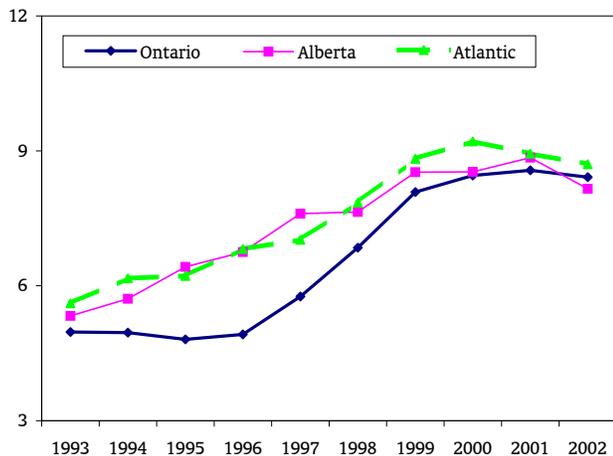
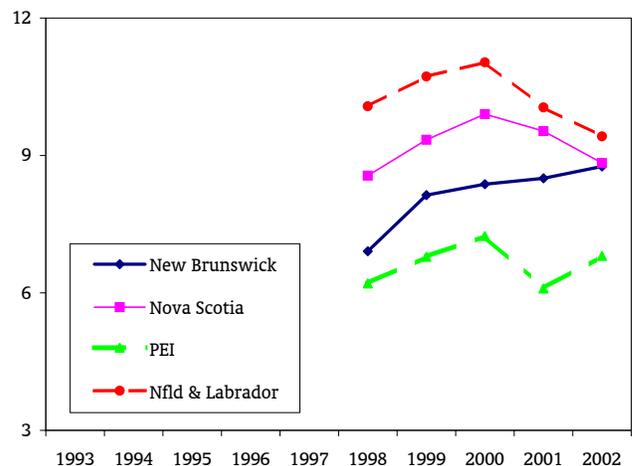


Figure 12: Claim-to-Premium Ratio (Atlantic Provinces)

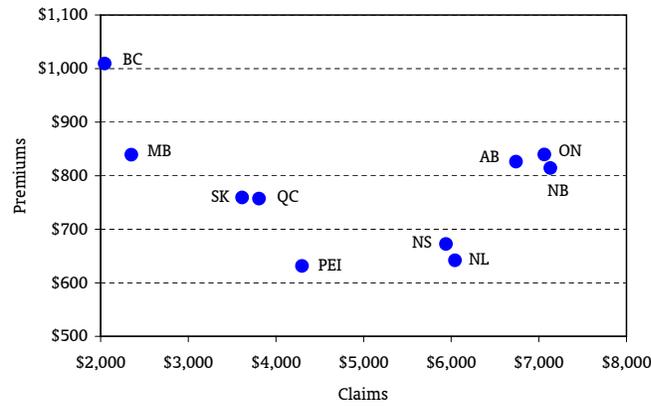


(low premium and high claims payout) and the worst position is the northwest quadrant. This highlights the large difference between first-ranked Newfoundland and Labrador and last-placed BC.

Recommendations

- Public insurance monopolies have relatively high premiums, yet make claims payouts that are fractions of those made by the private sector. This produces inferior insurance value.
- Public insurance systems are also marked by very high rates of claims per driver, indicating that claims are in excess of those justified by insurance pool risks.
- Provinces offering private sector auto insurance produce lower premiums, higher claims payouts, and lower claims per driver—all superior outcomes compared to the provinces with public auto insurance.
- To address these issues, a program of privatization and market restructuring in provinces with public auto insurance schemes would encourage new business entrants and better respond to consumer demand for auto insurance. It would also depoliticize this state-run system, which misprices risk and encourages excessive claims usage, in an effort to provide benefits to a broader-than-optimal group of policyholders.

Figure 13: Provincial Average Premiums vs. Average Claims



Appendix

All of the data in this *Fraser Alert* come from Statistics Canada, provincial ministries, the Insurance Bureau of Canada, and the annual reports and publications of the monopoly public insurers.

Claims amounts are based on incurred claims excluding associated costs. The claims are “developed,” thus including estimates of future costs from ongoing claims. Average claims are calculated as total claims divided by the number of drivers.

Private passenger claims growth is used from 1993 to 1997 for Ontario, Alberta, and the Atlantic region and all vehicles claims growth in those provinces thereafter. SGI Canada claims growth is used after 1996, as Saskatchewan Autofund data are unavailable. SAAQ claims growth was used after 1999 for Quebec private sector auto insurance growth for a similar reason.

Premiums are calculated as total premiums (adjusted for tax and reserve subsidies in the public sector) divided by a weighted base of drivers, driving age population, vehicles, and policies.

Notes

- ¹ See “Public Auto Insurance: A Mortality Warning for Motorists,” *Fraser Alert*, Fraser Institute, September 2003.
- ² See “Two Hundred Bucks More: The Premium Cost of Public Auto Insurance,” *Fraser Alert*, Fraser Institute, November 2003 and “Auto Premium Inflation: How StatsCan Rocked the Bank of Canada,” *Fraser Alert*, Fraser Institute, December 2003.
- ³ Of the public insurers, only Manitoba acknowledges this high claims rate in its public reports.
- ⁴ See “Two Hundred Bucks More: The Premium Cost of Public Auto Insurance,” *Fraser Alert*, Fraser Institute, November 2003.

Want to Know More?

Other relevant resources:

- www.abc.ca
- www.icbc.com
- www.mpi.mb.ca
- www.saaq.gouv.qc.ca
- www.sgi.sk.ca
- www.fraserinstitute.ca