

Private Motor Insurance

Royal & Sun Alliance Insurance plc

Summary Submission to the Competition Commission

1. Introduction

- 1.1 Royal & Sun Alliance Insurance plc ("RSA") welcomes the Competition Commission's market investigation into private motor insurance in the UK, believing that this is the appropriate forum to deliver a thorough and holistic review of the present market structure with a view to facilitating an appropriate, comprehensive solution.
- 1.2 The RSA Group is a global insurer, employing around 23,000 people worldwide. Operating in 33 countries, the RSA Group provides products and services to over 17 million customers in around 140 countries in total through a global network of local partners¹. RSA has been operating in the UK since 1710 and is the fourth largest personal lines and the largest commercial lines insurer in the UK. In 2011, RSA net premiums written were £8.1 billion.
- 1.3 This global background and 300-year heritage coupled with considerable private motor insurance experience (including that gained through recent key and relevant litigation in the UK Courts), gives RSA a unique insight into the evolution of the UK private motor insurance market and the nuances of the contrasting models in place in other countries around the world, particularly in Canada and Italy.
- 1.4 RSA welcomed the review initiated by the OFT in its Call for Evidence last year and engaged fully and pro-actively with the OFT throughout the subsequent market study². RSA was therefore fully supportive of the OFT's Final Report on the private motor insurance market study (the "Final Report"), dated 28 September 2012, and the ensuing market investigation reference. It is generally understood that the present market structure is not working well as a result of a complicated and interconnected set of issues which drive inefficiencies, increasing costs and leakage outside the industry; ultimately these issues result in higher consumer premiums. RSA believes that the CC's ability to review the market as a whole, encompassing all market participants, is a real opportunity to create and apply a comprehensive pan-market solution.
- 1.5 In particular, RSA welcomed the OFT's findings that the market was not particularly concentrated, there was a high degree of competitive rivalry between insurers and that consumers were generally shopping around effectively. RSA also agreed with the OFT's findings that premiums have risen in the period 2009-2011³ and that the key driver of those increases was a rise in the cost of bodily injury claims (mainly whiplash)⁴. There can be no doubt that market conditions remain challenging – with an industry combined operating ratio of 106% in 2011, private motor insurers are still paying out £1.06 in costs for every £1 of premium received and this is part of a backdrop of industry underwriting losses in every one of the past 15 years.

¹ RSA is the over-arching corporate brand and also a market brand in a number of countries. In addition, the RSA Group operates under a number of unique local brands including Codan, LINK4, TRYGG, HANSA, MORE TH>N and ANSWER.

² RSA Overview Submission of 27 February 2012 and Response to Proposal to make a Market Investigation Reference of 6 July 2012. In addition, RSA met with the OFT on a number of occasions.

³ OFT Report on the Market Study, May 2012. At paragraph 2.7, the OFT stated that premiums rose by 12% between 2009 and 2010 and a further 9% in the first three quarters of 2011.

⁴ Ibid.

- 1.6 As the CC will be aware, separate initiatives have been launched by Government⁵ to address the issues surrounding fraudulent claims and bodily injury. Certain reforms have now been made, with implementation of the first wave due for April 2013 and more promised. Whilst not complete solutions in their own right, these are important reforms and RSA considers it essential that Government drives them to implementation as planned, beginning in April next year. Indeed, RSA would be very concerned if there were any delay to these reforms as a result of the present investigation.
- 1.7 Clearly, given the need for a comprehensive solution, it will be essential to ensure consistency between these wider Government initiatives and the CC's market investigation. Whilst RSA considers that the main focus of the market investigation should be on the two particular areas identified by the OFT, i.e. credit hire and third party repairs, these cannot be reviewed in isolation from the wider issues (in particular whiplash and fraud) currently under consideration by the Ministry of Justice and Department for Transport. RSA considers that a key focus should be on the role played by third party non-insurers (including accident and claims management companies ("AMCs" and "CMCs"), credit hire organisations ("CHOs"), brokers, vehicle manufacturers and suppliers) and the impact this has had on overall claims costs.
- 1.8 As the CC will be aware from RSA's submissions to the OFT, RSA considers that there are no short-term fixes and that an in-depth review into the costs of providing temporary replacement vehicles ("TRVs") and third party repairs is required before any comprehensive and effective solution can be implemented successfully. RSA notes that, to the extent possible, insurers have moved to drive costs down, as evidenced by the increasing number of bilateral agreements entered into and in negotiation over the course of the past six months. RSA looks forward to engaging constructively with the CC over the course of the market investigation with a view to delivering a comprehensive solution for the market as a whole, including the issue of third party intervention.
- 1.9 As requested by the CC, section 2 below summarises the key points RSA made to the OFT in its previous submissions, where appropriate highlighting those areas which have developed since the OFT's May Report.

2. Summary of RSA's previous submissions

- 2.1 The OFT's Final Report concluded that the test for reference was met in respect of two features:
- (i) A lack of control and choice over third party claims costs (specifically repairs and the provision of TRVs); and
 - (ii) The potential (and possibly incentive) for insurers and relevant non-insurer third parties (such as CMCs, AMCs, brokers, CHOs and credit hire providers etc.) to exploit this by generating additional revenues (for example through referral fees, rebates or similar benefits), increasing the costs of not-at-fault claims ultimately subrogated to at-fault insurers.
- 2.2 RSA agrees with the OFT that the current system for handling third party repairs and the provision of TRVs has resulted in higher claims costs (in particular as a result of third party non-insurer intervention). However, the main drivers of cost are bodily injury (in particular whiplash) and fraud. Given the on-going Government reviews which focus in particular on reforms to the bodily injury claims process, RSA considers that the focus of the market

⁵ Ministry of Justice and Department for Transport reviews.

investigation should be on the two areas identified by the OFT (whilst ensuring consistency with those wider Government reviews).

2.3 In summary, RSA considers the following to be the key issues:

- (a) Intervention by third parties (including other insurers and non-insurer service providers seeking to take control of not-at-fault claims) has led to increasing costs being introduced into the system. These include additional frictional costs as insurers try to 'capture' claims early in the process, to defend attempts by third parties to take over the claim and/or the costs of recovering disputed at-fault claims from other insurers;
- (b) As more not-at-fault claims are handled and processed by third parties (i.e. by AMCs, CMCs, CHOs, vehicle manufacturer main dealer garages etc), there has been an increasing lack of control and a corresponding inability for the ultimate paying party to keep repair and hire costs in check;
- (c) Where not-at-fault claims are controlled by insurers, the benefit of the margin on TRV and repair costs will, via the vigorous competition which exists between insurers, place downward pressure on premiums, offsetting the higher cost of reasonable cost recovery. However, where claims are controlled by non-insurers, the available margin will lead to higher profits for non-insurers. As identified by the OFT, the proliferation of non-insurer entities offering claims management, repair and hire services, has therefore had a direct upward pressure on premiums;
- (d) The mark-ups on claims costs are particularly evident in the supply of TRVs. Looking at third party claims costs (repair and TRV costs together), RSA estimates that as much as £150-200m could be leaking out of the system each year as a direct result of non-insurer third party intervention into the claims process; and
- (e) The most significant drivers of cost are fraud and bodily injury.

Bodily injury

2.4 The Legal Aid Sentencing and Punishment of Offenders ("LASPO") Act 2012 is set to introduce a ban on referral fees as of April 2013. The ban will apply both to the payment and receipt of referral fees on any claim involving personal injury by a 'regulated person', (i.e. solicitor, barrister, insurer or CMC).

2.5 LASPO also implements other key parts of the Jackson package of reforms introducing changes to the funding of personal injury claims due to come into effect in April 2013 (as stated above, RSA considers it essential that these reforms continue without delay). The most significant changes relate to success fees and 'after the event' insurance which will no longer be recoverable from defendants. To compensate claimants (who will need to pay for this) pain, suffering and loss of amenity awards will be uplifted by 10%. Finally, LASPO also brings the introduction of damages-based contingency fees (i.e. fees assessed as a percentage of damages) as an alternative mechanism of funding for personal injury claims.

2.6 The Government also intends to implement other parts of the Jackson reforms, including a review of the level of the existing fee⁶. However there remains uncertainty around what the level of the fee will be, and whether this will now be implemented in time for April. RSA considers that this element of the reforms is likely to deliver the single biggest impact to reducing overall costs. Again, these reforms must therefore be allowed to proceed without

⁶ Recoverable in the Ministry of Justice portal.

any further delay to avoid placing yet more strain on the system. Introduction of fixed costs throughout the whole fast track (covering claims up to £25,000) is also being explored⁷.

- 2.7 RSA welcomes these reforms and consultations which on aggregate provide for far more balanced and proportionate arrangements for funding injury claims and looks forward to further evolution of reform in this area. However, RSA recognises that these proposals can only work as part of a broader package and indeed Government has recognised that a ban on referral fees alone would not address the underlying issues – this can only be achieved by also seeking to take some of the costs out of the process.
- 2.8 RSA considers that whilst the CC's investigation will need to be closely aligned to the outcomes of these reviews, the primary focus of the market investigation should be on those areas identified by the OFT, i.e. repairs (to the extent that not-at-fault repairs are handled by third parties) and the provision of TRVs.

Provision of TRVs and repairs

- 2.9 As the CC will be aware, the accident repair and credit hire models developed by insurers such as RSA have evolved from the well-established legal system which enables and incentivises insurers and third parties to capture and maximise the margins between actual and 'reasonable' costs available on such claims. Indeed, the key principle that recovery at a 'reasonable cost' does not prevent insurers making and retaining any margin between actual and 'reasonable' costs was most recently ratified in litigation involving RSA in the case of *Coles v Hetherington*⁸. The latest judgment in this case⁹ has clarified that insurers may recover costs relating to 'diminution of value' and not just actual repair costs. This principle also means that recovery for TRV costs may be higher than the actual costs of the hire. This will likely be the case for example where an insurer has successfully negotiated favourable hire rates with its hire car provider.
- 2.10 For its own part, RSA's decision to develop its own in-house accident and repair model was a direct reaction to increased underwriting losses and costs in the period since 2009¹⁰. Developed as a natural extension of the long-established legal framework¹¹, RSA (along with other insurers) developed models to generate alternative income streams with a view to offsetting these underwriting losses and ultimately to keeping consumer premiums lower than would otherwise be the case.
- 2.11 RSA's accident repair model is explained in detail at section 4 of RSA's Overview Submission to the OFT¹². In short, RSA operates a vertically integrated system through RSA Accident Repairs Limited ("RSAAR"), a wholly owned subsidiary. RSAAR manages and carries out repairs on behalf of RSA, performing some repairs at wholly owned repair centres and in other cases subcontracting repairs (mainly to an approved network of authorised repairers).
- 2.12 In its submissions to the OFT, RSA set out that a significant proportion of the increase in TRV and repair costs identified by the OFT can be attributed to the intervention of non-insurer organisations such as CHOs or CMCs who generate income streams (and margin) through seizing control of the claims process. In particular, RSA's submissions explained

⁷ A consultation on the small claims limit for personal injury claims was due to be published on 7 September, but was postponed for up to 4 weeks because of the recent Government ministerial reshuffles.

⁸ *Coles v Hetherington* [2012] EWHC 1599 (Comm).

⁹ 4 October 2012.

¹⁰ See further RSA's Overview to the OFT of 27 February 2012.

¹¹ Including RSA's defeat in the Court of Appeal in *Bee v Jenson (No. 2)* [2008] Lloyd's Rep IR 221.

¹² RSA's existing TRV solution is also set out at section 4 of the same submission. [CONFIDENTIAL].

how the TRV and repair cost margins earned by non-insurers “leak out” of the insurance sector.

Bilateral Agreements

- 2.13 Increasingly over the last six months [CONFIDENTIAL] RSA has noted a rise in the number of bilateral agreements being negotiated between insurers as insurers seek to keep costs down. Given the competitive market, it is to be expected that these savings will place downward pressure on consumer premiums.
- 2.14 Bilateral agreements serve as a model for cost efficiency, enabling large reductions in the costs contained in the final not-at-fault claim bill received by participating insurers and significantly reducing the prospect of litigation. Accepting that this is in no way a comprehensive solution, RSA has now entered into several such bilateral arrangements with a number of other insurers [CONFIDENTIAL]. These arrangements nevertheless represent an important step by insurers seeking to lower overall claims costs.
- 2.15 [CONFIDENTIAL]
- 2.16 While RSA considers that such bilateral agreements between insurers are a useful tool in the context of the current market structure, RSA does not believe that they address the issue of third party non-insurer intervention in the claims process. Without reducing the 'leakage' caused by non-insurer led claims, which have a detrimental impact on overall net claims costs and hence ultimately on prices charged to customers, a network of bilateral agreements alone would fail to address the underlying issues.

3. **Next Steps**

- 3.1 RSA looks forward to engaging constructively with the CC over the course of the market investigation and considers that it is uniquely placed to take a leading role in helping to shape a comprehensive, industry-wide solution to the issues under consideration. In the meantime, RSA would like to extend the offer made to the OFT and would be very happy to meet with the CC at an early stage if that would prove helpful.