The Actuarial Profession
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The September 2012 updated report on third party motor claims from the Institute and Faculty of Actuaries

This is an update to the third annual report from the Institute and Faculty of Actuaries collating and analysing data for UK third party motor claims focusing on data collected to 31 Dec 2011.

A full copy of the long report is available on request. All supporting data for the key findings of the report can be found in the appendix.

- Page 1 – glossary and key findings of the report
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Glossary

TPI – third party injury: claims arising when a driver causes personal injury to other persons for which he/she is liable.
TPD – third party damage: claims arising when a driver causes damage to the property of other persons for which he/she is liable.
CMC – claims management companies

Key findings of the report

- **The frequency of TPI claims has increased by 6%.** This increase contrasts starkly with the decline of 11% in accidents giving rise to third party claims.

- **Whilst there was a 20% decrease in the number of injuries reported to the police in accidents between 2006 and 2011, data from the Institute and Faculty of Actuaries shows an increase of 40% in the number of TPI claims over the same period.** This data discrepancy supports the view that TPI claims are driven by a change in claiming behaviour rather than a change in the underlying risk.

- **The average size of a small* TPI claim in 2011 was £8,400.** This highlights an increase in the average size of small claims, for which we have reported an increasing trend since 2005. *(*small claims exclude any claims amount in excess of £100,00, in 2010 money, in excess of which would be associated with particularly serious personal injury claims.)*

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- **There has been a 5% decline in the number of authorised CMCs although their income rose by 21% to £455m in 2011.** (Source for income: Ministry of Justice annual claims regulation report).
- **The Northwest region of the UK continues to be a hotspot for TPI claims and this corresponds with the high concentration of CMCs per capita found in this region**. Scotland has the lowest ratio of third party injury claims to third party damage claims (TPI/TPD ratio) of anywhere in the UK and likewise the lowest concentration of CMCs per capita.

- **Birmingham postcodes dominate the 20 worst postcode districts for TPI claims frequency per capita in the UK** with 11 of its postcode districts listed.

- **There was a 19% increase in TPI claim costs in 2011 which led to an estimated £400m increase in costs to insurers**. However despite this increase insurers appear not to have passed on this cost to consumers – **the average cost of UK motor insurance premiums has fallen by 7.1% over the last 12 months** (source: Confused.com/Tower Watson Car Insurance Price Index July 2012).

20 worst postcode districts for TPI frequency

Postcode district	Nearest town/city
B8	Birmingham
B12	Birmingham
B10	Birmingham
B9	Birmingham
B6	Birmingham
B19	Birmingham
M13	Manchester
BD3	Bradford
M12	Manchester
BD8	Bradford
B21	Birmingham
BD9	Bradford
B66	Birmingham
M8	Manchester
B11	Birmingham

BD5	Bradford
N17	London-North
B18	Birmingham
B20	Birmingham
L7	Liverpool

20 best postcode districts for TPI frequency

Postcode district	Nearest town/city
KW16	Kirkwall
KW17	Kirkwall
IV26	Inverness
KW15	Kirkwall
ZE2	Shetland
NE70	Newcastle
IV15	Inverness
EH31	Edinburgh
IV19	Inverness
HS1	Hebrides
IV27	Inverness
AB33	Aberdeen
DG7	Dumfries
PH16	Perth
KA27	Kilmarnock
AB45	Aberdeen
AB55	Aberdeen
EH35	Edinburgh

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Appendix one: additional supporting data

Claim Frequency

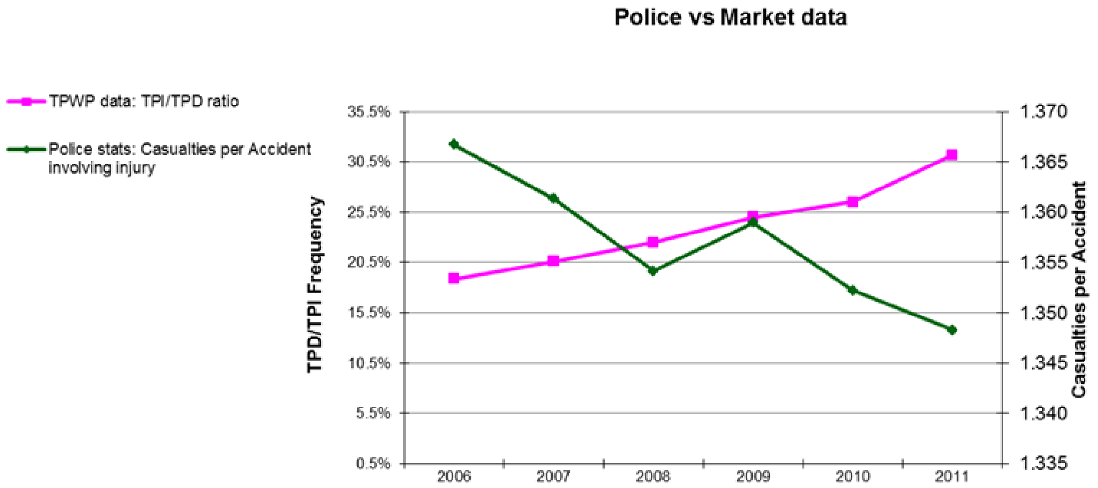
The frequency of TPD claims continues to fall (11% decrease in 2011) but the frequency of TPI claims continues to increase (6% increase in 2011).

We have compared our data with data from other sources with mixed results:

- Whilst Compensation Recovery Unit (CRU) at the Department for Work and Pensions (www.dwp.gov.uk/other-specialists/compensation-recovery-unit) data agrees with our observation of an increase in TPI frequency their data also shows an increase in the number of registered motor cases year on year. However this is not obviously the case with Police statistics (Source: stats 19).

- Whilst actuarial claims data shows an increase in the TPI/TPD ratio with inflation averaging at 19%. Police statistics show a decreasing trend in the number of accidents involving injuries. This supports the view that TPI frequency inflation is driven by a change in claiming behaviour rather than a change in the underlying risk. (see chart below)

Police vs Market data



TPWP – the third party working party, the group that put together this data within the Institute and Faculty of Actuaries

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Average claims amounts

As well as showing inflation driven by increasing numbers of claims, average individual claims amounts inflation is also increasing for smaller TPI claims. Both forms of inflation need to be considered before drawing any conclusions on the costs of insurance.

New research shows that the level of inflation on average claims amounts increased around 2008, since when it has been 8%. It is still too early to say whether Ministry of Justice reforms introduced in 2010 will reduce this inflation in the long run. However to date (for claims arising in 2010 and 2011), average claim cost inflation has sat somewhat lower at 6%.

Our data suggests that multiple whiplash claims costing between £10,000 and £20,000 have an average number of claimants per claims of 1.4.

Of more serious motor personal injury claims (with amounts in excess of the threshold[1]), average cost inflation is in excess of 10% driven by increasing proportions of very large claims in excess of £1m[2]. A certain amount of the increase could be earlier recognition by insurers of the seriousness of these very large claims. But there is undoubtedly real inflation at play. This inflation may have increased due to a precautionary approach being taken by insurers and anticipating the impact of a change to the Ogden rate**. For the very largest claims' severity inflation in excess of 20% is becoming more common.

**Ogden tables are a set of statistical tables and other information for use in court cases in the UK. These tables quote settlement amounts to be paid to claimants of particularly serious TPI at a range of "discount rates", based on case specific figures such as claimant's expected annual cost of care or their loss of earnings. The discount rate currently used is 2.5%. Lower discount rates would lead to higher amounts being paid to claimants. The discount rate is set by the Lord Chancellor's office and was last set in 2001. The rate is currently under review (as a result of the depressed investment market), but is subject to a number of ongoing consultations. Some insurance companies may have taken the precautionary assumption that the discount rate will reduce and increased their estimates of the amounts at which current claims will be ultimately settled.

[1] The threshold for excess claims is circa £100,000 (2010 money indexed at 7% p.a.)
[2] Indexed for inflation

Geographical differences

The report has conducted an exposure analysis splitting the UK into RSMB TV Regions as shown below.

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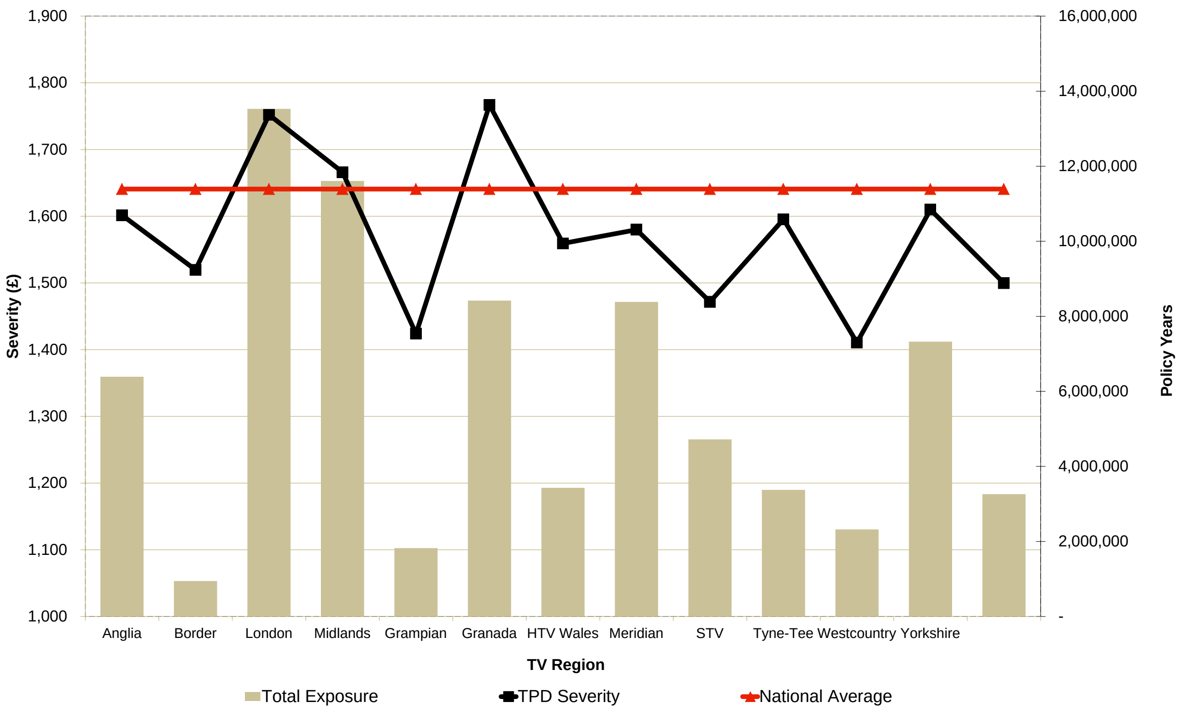
TPD Claims

London has a significantly higher TPD frequency than the rest of the country, followed by Manchester and Birmingham.

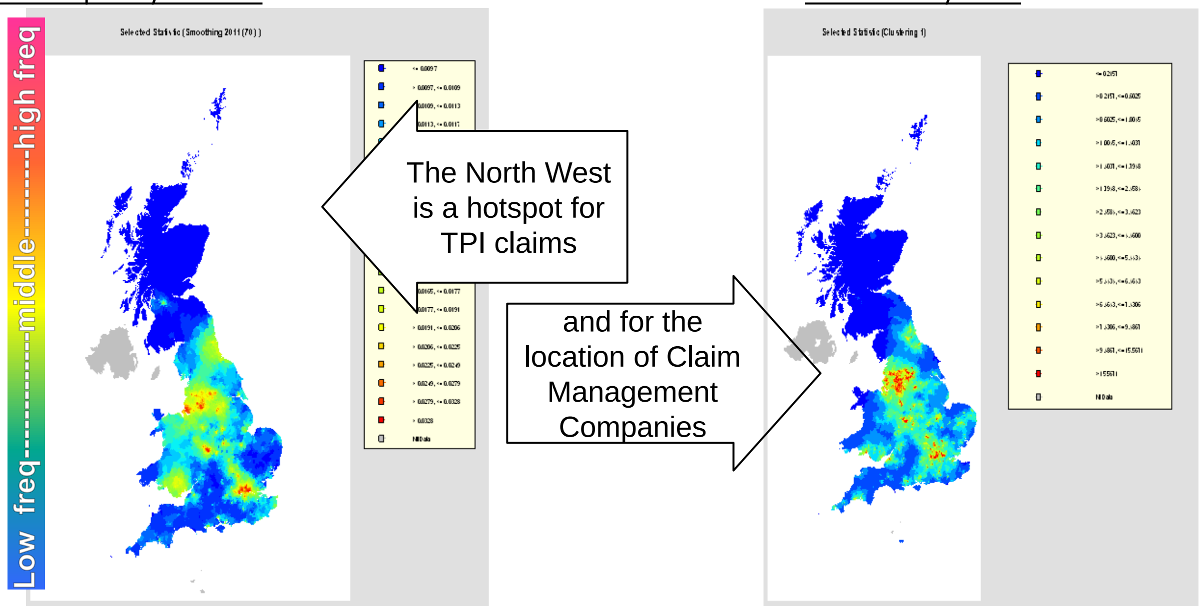
TPD Severity 2007-2011



TPI Claims

North West UK continues to demonstrate high TPI claim frequencies (Liverpool and Manchester in particular). This region also has the highest concentration of CMCs. London is a hotspot for TPI claims and also has the second highest density of CMCs.

TPI frequency in 2011 | CMC density 2011

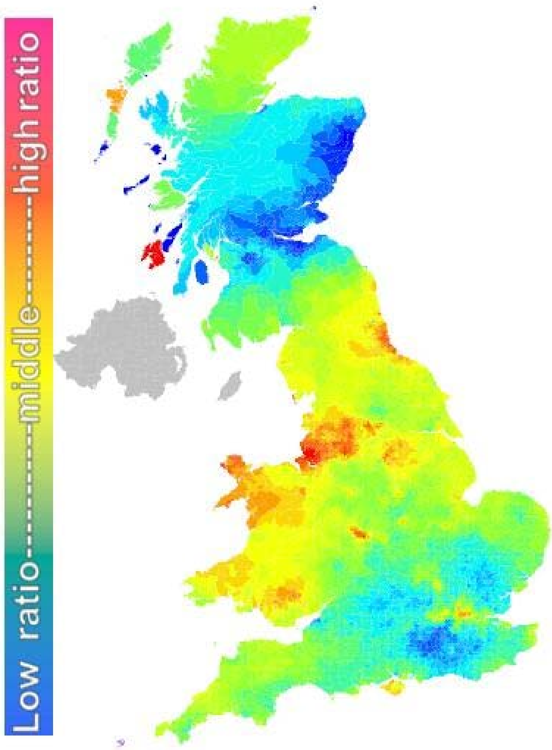


The Grampian, Border, West country, regions have shown very high TPI claim severities (2007-2011) compared to the national average.

TPI/TPD Claim ratios

In 2011, TPI/TPD ratios[3] vary between 15% and 43% across the UK. Liverpool exhibits the highest TPI/TPD ratio (over 50%). Manchester, Oldham and Bolton also exhibit high TPI/TPD ratios relative to the rest of the UK.

<u>TPI/TPD Ratio in Accident Year 2011</u>



Scotland has a lower TPI/TPD ratio in comparison to other areas, and this corresponds with the areas with the lowest concentration of CMC's.

There is consistency between the Police statistics in the UK regions with the highest number of reported casualties per accident and the regions with the highest TPI/TPD ratios.

At a regional level, there is a clear increasing trend in the TPI/TPD ratio in every region. Granada (North West UK) has consistently had the highest ratio and Grampian (North East Scotland) has a consistently low ratio. The TPI/TPD claim ratio for London has deteriorated, and is now equal to the national average.

[3] *Late reporting of claims is a particular issue for TPI. As such the TPI/TPD ratios are likely to be understated for 2011.*

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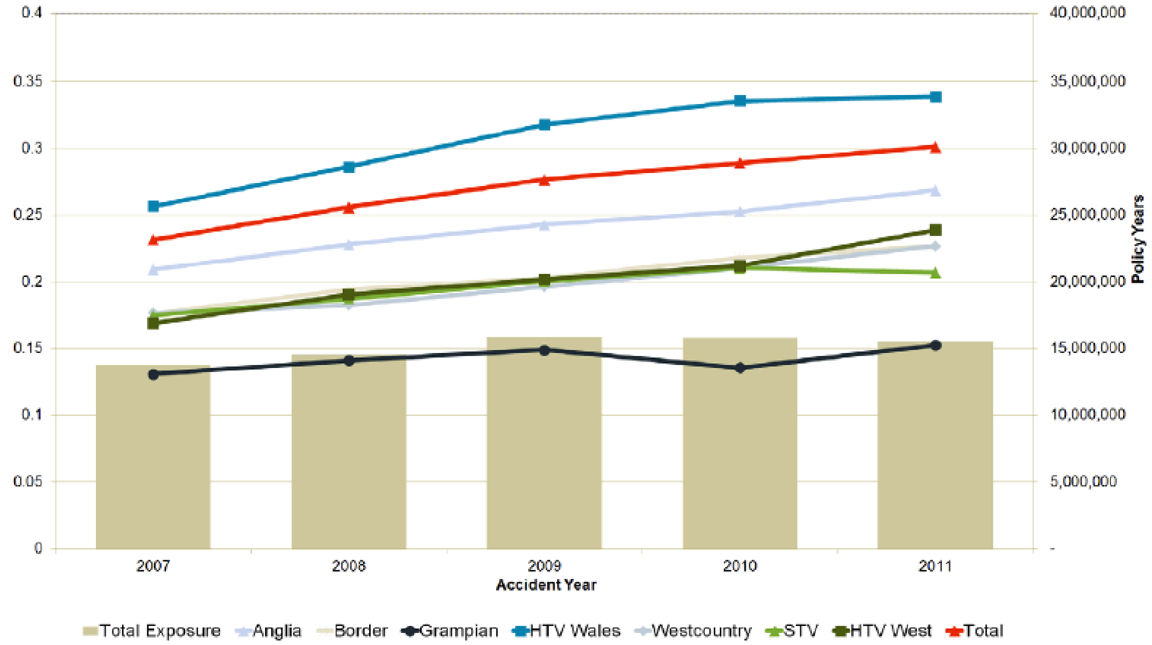
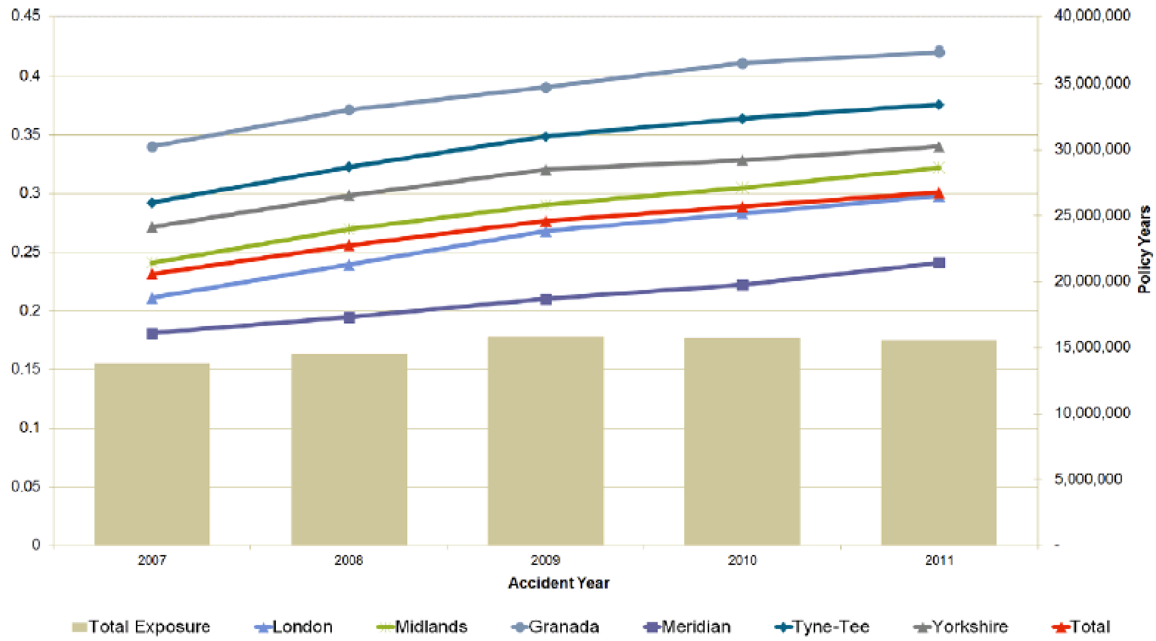
TPI/TPD Ratio Graphs





US state TPI/TPD claim ratios are now lower than those in the regions of the UK with the highest ratios (North West). The highest ratio in the UK is 43% in Granada compared with the highest ratio in the US of 38.8% in Louisiana.

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Worst states for BI/TPD ratio[4]

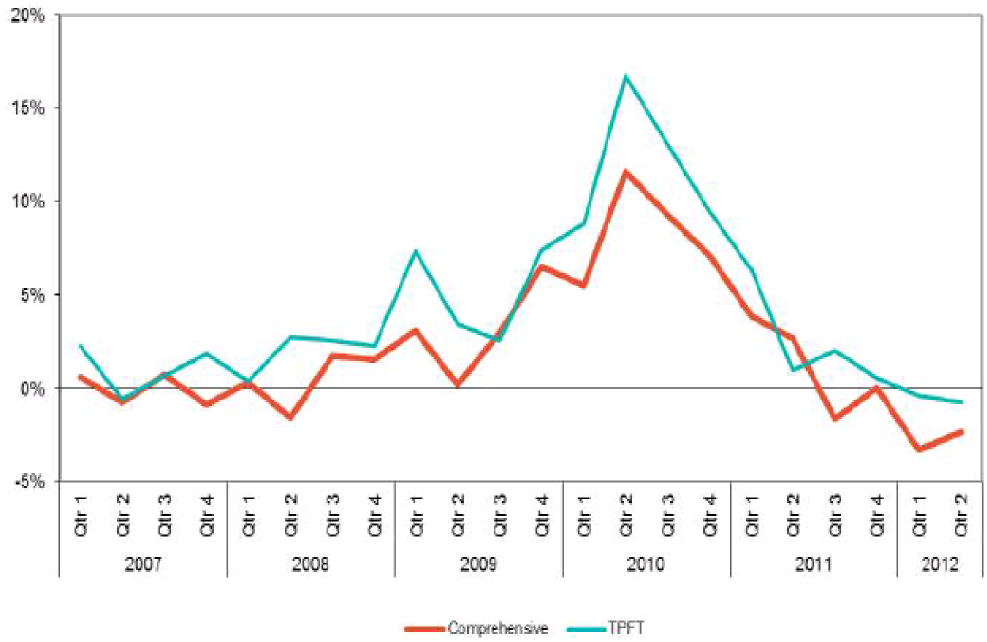
State	BI/TPD Ratio
Louisiana	38.8%
Nevada	37.7%
Rhoda Island	37.3%
Oregon	35.9%
South Carolina	34.3%
Washington	32.0%

The North West has experienced high TPI/TPD ratios since 2007, with the ratio increasing over the past 5 years. Hot spots are no longer restricted to urban areas as they were in 2007 but have now spread across to rural areas.

Falling UK Motor Premiums

Despite predictions of increasing premiums as a result of higher proportions of TPI claims, average premiums across the UK have fallen by 7.1% over the past 12 months and this includes a 2.3% decrease over Q2 2012. For the third quarter out of the last four, prices for comprehensive insurance fell having been flat in the final quarter of 2011. [5]

Motor Premium Rate Movements



[4] data is at YE2011 from ISS's Private Passenger Fast Track Data reports
[5] Data is from Confused.com/Towers Watson Car Insurance Price Index July 2012

Appendix two: Supporting background information

Background to the Institute and Faculty of Actuaries Motor Third Party Working Party that helped to produce this report

The Institute and Faculty of Actuaries has commissioned working parties since 2009 to investigate third party motor insurance claims as a result of some worrying inflationary trends being reported by individual insurers.

These findings were based on £8.5bn of earned premium data, a greater volume than collected ever before. Data is provided as at 31 December 2011.

Background to the Motor Insurance Industry

Motor insurance offers cover to both personal and commercial customers in the UK and is compulsory in respect of third party property damage and third party bodily injury. This paper focuses on comprehensive cover for private car insurance only, and excludes the much smaller non-comprehensive market. According to the Office of Fair Trading, the costs of third party claims represent 70% of motor insurance claims costs - TPI accounts for 50% and TPD for 20% - and so dominate the cost of insurance.

According to ABI figures insurers collect in excess of £10 billion in motor premiums each year. The earned premiums for private car comprehensive insurance earned in 2011 were £9.5bn. The motor insurance industry lost money in both 2010 and 2011 (as per the FSA returns based on combined operating ratios). In 2011 there was a loss of over 6p for every £1 of premium sold. Despite this the Confused.com/Towers Watson Insurance Price Index shows private car market rate reductions of 7.1% for comprehensive policies during the 12 months to June 2012. It is not unlikely that material future increases will be required before the UK private motor insurance market moves into profit.

Ministry of Justice Personal Injury Claims Reform

In April 2010 the Ministry of Justice introduced a new process for the handling of personal injury claims. These changes apply to all Road Traffic Accident personal injury claims worth between £1,000 and £10,000 occurring on or after 30 April 2010, which represents the majority of all bodily injury claims. The process has been drawn up to create quicker, simpler and cheaper access to compensation and includes fixed timetables to reduce both disputes and frivolous litigation.

Ministry of Justice Proposal in September 2011 – Banning Referral Fees

In September 2011 the Ministry of Justice proposed that referral fees should be banned. The news was welcomed by the Institute and Faculty of Actuaries, due to the link between the recent rise in motor insurance premiums and the rise in the number of claims management companies. However, this proposal has not yet been passed into law, and there is currently no recognised definition of a "referral fee". The Actuarial Profession also noted that there is some way to go before insurance companies stop losing money on private motor insurance policies, and so premium increases are unlikely to be a thing of the past.

The Ministry of Justice wrote to interested parties in February 2012 inviting views on its plans to extend the existing process for road traffic accidents to cover claims up to £25,000.The then Justice Minister Jonathan Djanogly indicated to Parliament that changes would take effect in April 2013. However, there has been no formal confirmation that this extension will take place or when.

The Ministry also sought views on a possible reduction in the level of fixed recoverable costs for claims. Many consider that a reduction in recoverable costs (both for claims and under the predictable costs regime) is a natural corollary of the ban on referral fees.

The Legal Aid, Sentencing and Punishment of Offenders (LASPO) Act received Royal Assent in May 2012 and is expected to come into force in April 2013 and introduces many of the reforms proposed by Lord Justice Jackson in his review of civil litigation costs. The Act will ban referral fees for personal injury claims, make success fees and After-the-Event legal expense insurance premiums unrecoverable from the liable insurer and introduce Damages Based agreements (whereby claimant solicitors take a percentage of any damages awarded)

The introduction of Qualified One-Way Costs Shifting, also proposed by Jackson, is not included in the Act but is widely expected to be introduced by an amendment to the Civil Procedure Rules from the same time. This would mean that (other than in exceptional circumstances) an unsuccessful claimant would not be liable for the defendant's costs, negating the need for legal expense insurance.

The Government is expected to issue a consultation paper shortly on options to reduce whiplash claims. Possible options include raising the small claims track limit for injury claims from £1000 to £5000. This would mean that legal costs would not be recoverable for the majority of whiplash claims. Another possible measure is to establish an independent panel of medical experts to diagnose whiplash injuries rather than relying on GPs.

The Office of Fair Trading recently completed a review into credit hire and repair. Its report was published in May and found that dysfunctional practices within the insurance industry added £10 to the average cost of a motor insurance policy. The OFT has now referred this matter to the Competition Commission.

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