Speaking Notes for a talk by Brian Lee Crowley, President, AIMS
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Ladies and Gentlemen,

Thank you to Dianne Kelderman and the NSCC for the kind invitation to be here to day.

Every person who buys insurance is mad as hell right now, and I'm no exception. My office has had to take on $8000 more in insurance premiums to cover errors and omissions – in other words if somebody acts on my policy advice, and I make a mistake and they sue me, I'm covered. At least, then, I'm covered if I screw up today. Sue me and my insurance company will take care of the bill. I've paid for it and I'd like someone to be able to enjoy it.

More seriously, the heart of my talk is really about the principle that just because something makes you angry, it doesn't mean that it is wrong or unjustified, and it doesn't mean that every possible action that you might take to fix the thing that makes you angry is going to make the situation better. We have to be thoughtful about what we do, because believe me, there are always ways to make a bad situation worse.

Take business owners, homeowners and drivers, all are rightly angry about the rising cost of their insurance. Big premium increases like those of the last year or two hurt people's pocketbooks and divert their money from things that are more important to them. That damages their standard of living. Sometimes people can't even get coverage when they're willing to pay the premiums. That's even worse than having premiums go through the roof. So, insurance today is an issue fraught with emotion. But emotion is never the best basis on which to settle complex public policy issues, especially when the costs of an ill-considered and hasty decision are likely to be with us for a very long time to come.

It is always when emotion is at its highest that people are vulnerable to the latest scheme that sounds like it will solve the problem with the wave of a magic wand. And nationalization of the car insurance industry and "regulation" or nationalization of business and other forms of insurance is the flavour of the month in this category. To hear its advocates tell the story, nationalization and regulation will lower costs, improve service, eliminate "excessive" profits and perhaps cure SARS too.

But here are a couple of things to mull over.

First, my view is that what consumers want more than anything else is price stability. If we put up the price of insurance, and left it there unchanged for 10 years, people might grumble every time they got the bill, but there would be no public controversy about it. It is price volatility that upsets people. They hate it when the cost of something shoots up. It gets their attention, and it is always an angry attention.

Look at this, not in the context of insurance, but gasoline prices. In Nova Scotia, where the price of gasoline fluctuates with the market price of the commodity, with great peaks and valleys, gasoline pricing is a big political issue. In PEI, where the price is regulated and therefore the price oscillations are masked from consumers, it is much less so. And consumers in Nova Scotia look at PEI every time their gas prices spike and cry out for the government to bring back price regulation so that we can have all the advantages of PEI.

Well, be careful what you wish for. It is quite easy to demonstrate that consumers in PEI, not Nova

Scotia, are the losers. The cost of that price stability for Islanders is that regulation smoothes out the price declines as much as the price rises, and over time, NS consumers are clearly better off than their Island confreres. And we won't even talk about the gasoline retailers, who are the ones who bear the brunt of the cost when prices rise. It certainly isn't the oil and gas majors, who certainly don't lower their prices for PEI consumers. They sell a commodity to those who want to pay the current price.

There's an object lesson here that I think we should bear in mind. In the context of competition, prices mean something quite important. Prices are signals about the cost of doing things, about the costs of the choices that we make. The gasoline price in NS follows the international price of crude in lockstep. So when the price of the raw material rises, we all smart, and that's what gets people's attention. But the price at the pump follows the commodity price down as well as up. And that's because prices also signal something else: opportunity.

When pump prices are high relative to the cost of crude, that's an opportunity for somebody who would like to win market share, and make his money on volume rather than price. Knowing about the gap between current cost and the retail price draws people to compete for customers because there's money to be made. That's why price hikes are almost always followed by price wars. Study after study of the gasoline market, like most other markets, shows that any 'excess' profits at the pump are quickly competed away and the saving passed on to consumers. No one retailer can hold out against the tide, because people buy gas on price. People think that all retailers having the same price is evidence of lack of competition. On the contrary, it is a sign that all of the retailers are what economists call "price takers" – they are forced by competition to converge on the lowest price in the market. No gas station can afford to be a serious outlier on the high or the low side for very long.

But nationalisation or ham-fisted regulation prevent that balancing act that freely formed prices and competition make possible. Regulation slows the whole process down and makes it impossible for companies and consumers to adjust their behaviour to changing conditions. And politics gets in the way of rational economic or business decisions. The extreme case, of course, is nationalisation, a solution promoted in this province for auto insurance by the NDP, and in New Brunswick by the Liberals as well.

Politicians in these circumstances face huge pressures to make premiums politically popular, or at least palatable. One way they do that is by pandering to the riskiest segments of the population by telling them that companies discriminate against them in rate setting, and promising them rate relief. But such relief can only come at the expense of lower risk categories of drivers who must pay more to compensate.

The proponents of this solution to our insurance problem like to put it about that nationalisation, by eliminating the profit motive, makes insurance cheaper, but anyone in business knows that this is complete nonsense. Profit is not an additional cost added on top of the fixed costs of carrying on a particular type of business. In fact, most costs are extremely variable depending on circumstances, and profit is the reward you get for keeping your costs low relative to the price of the product you're selling in the market. Any businessperson who can't offer their product or service cheaper than a public sector bureaucracy could, and still make a profit, is a disgrace to their industry and should get into another line of work. Otherwise, we would all save huge amounts of money by nationalising every industry and running it as a public sector monopoly bureaucracy. The reason why we don't do that for cars, groceries, televisions, vacations, and clothes and housing is exactly the same reason we shouldn't want to do it for insurance.

But even if you don't accept these arguments here, in my view is the key question to ask those people pushing nationalization, for instance of the car industry, today: why didn't Bob Rae do it?

Bob Rae was the NDP Premier of Ontario. He won office in the early 1990s with a handsome parliamentary majority. State monopoly car insurance had not only been long-time NDP policy, but Rae himself had campaigned for it.

But the NDP faced the discipline of power, the fact that they and all the citizens and taxpayers of the province had to live for a long time with the consequences of what they were going to do. And the government began to realize that those consequences not only were not positive, but were disastrous.

You cannot conjure a state-run insurance scheme out of the air. There are huge start-up costs. You have to borrow hundreds of millions of dollars to create a new organization from the ground up and to fund the new insurance liabilities. Borrowing rises while tax revenues decline. You have to cause major employment dislocation, as all the dozens of private sector insurers close down their operations, some of them significant regional head office operations, and leave the province.

All of the people in communities around the province who live from selling auto insurance lose significant revenue, as the state-run government schemes cut back on commissions to agents.

Taking responsibility for auto insurance also meant that now the electorate would blame politicians for every bad experience with a claim that goes wrong or with premium increases. And the politicians knew that there would be premium increases, because an insurance scheme can only pay out in claims and expenses as much as it takes in premiums. Here in the Maritimes, for example, insurance costs are rising, chiefly due to the rising cost of claims for various kinds of non-permanent injuries awarded by the courts. Insurance certainly is not rising because the companies are making excessive profits. Indeed premiums are rising because companies have lost money recently. Costs have risen faster than premiums.

At election time, though, it is tempting for politicians who have a monopoly on car insurance to freeze or even reduce insurance premiums, and jack them up between elections, or else keep them artificially low for too long. Either way, the outcome is usually a bailout funded by taxpayers or drivers or both, whether through straight transfers of tax dollars or through driver's licence fees, gasoline taxes or other means. This kind of politically motivated premium behaviour is easily observable in several of the western provinces, such as B.C., that have state-run car insurance.

One of the ways that these provinces make their insurance appear cheap compared to elsewhere is to force drivers to shoulder more insurance risk, while leaving premiums unchanged. This is done by simply raising the deductible you pay when you make a claim. Most people in the Maritimes have quite low deductibles, but in the provinces where car insurance has been nationalized, the minimum deductibles are very high: $500 in Manitoba and $700 in Saskatchewan for both collision and comprehensive coverage. That's far more risk than Maritimers have been willing to bear when given the choice.

And that's really the key issue: choice. When we're dissatisfied with our premium, or the service we get, or the level of our deductible, we can shop around. We can get multiple vehicle discounts. We can get an insurance agent who works harder for us to get a good deal out of the company. None of these things are available under government monopoly insurance.

Don't believe me? Then ask Judge Coulter Osborne of the Ontario Supreme Court. Premier Rae asked him to study the NDP's proposed state car insurance and report back with his recommendations. Judge Osborne, after extensive inquiry, found "…there are no benefits to the taxpayer or consumer to converting to public auto insurance."

Now when I have pointed this out to the advocates of insurance nationalisation, I often get back a truly astoundingly vacuous answer: well, we, or the “public” or the government, or somebody, are a lot more demanding than any judge would be, implying that the judge somehow didn’t take his job seriously and in any case can be fooled and sloughed off by the shoddiest of arguments.

This is patent nonsense. The whole point of a judicial inquiry is to take the debate out of the hands of interested parties, whether political parties trolling for votes, or angry consumers clutching at straws as to how to deal with the price volatility that I’ve already referred to. The judge gets to take a searching, probing look into the issues in an impartial way, helped by expert testimony and his own researchers. Putting it before a judicial inquiry in this way is a *much* tougher test to pass than the test of public opinion based on the emotions of the moment.

So to sum up, in a competitive market, prices will rise and fall in response to unpredictable circumstances. Gas rises and falls in response to wars in Iraq, revolutions in Venezuela, environmental regulations in the US and policy decisions by OPEC in Vienna. Insurance premiums rise and fall in response to the cost of capital, returns in the stock market, trends in claims, and huge unexpected events that cannot be predicted or controlled, such as earthquakes, September 11th and outbreaks of infectious disease.

I want to remind you that your business freedom is at stake here too. You adjust your prices up and down unpredictably according to circumstances, many of which you don’t control – taxes, minimum wage and other legislation, wholesale price increases, world commodity price movements, interest rates, etc., etc. Sometimes you do so to the great annoyance of your customers and sometimes you even lose custom. Why shouldn’t others have this freedom?

I hope that no one will come to me and say that you’re in favour of that freedom for small businesses but not for the Big Guys. I don’t buy for one moment that “big international corporate conspiracy to do down us little folks” theory. I have yet to hear a businessperson say, “Yippee! That huge international corporation Wal-Mart is coming to town. They are a conspiracy against consumers and raise prices with impunity. Now I’ll be able to put my prices up too.” One of the reasons that the big box retailers are so coveted by consumers is that they drive down prices while offering consumers more choice. If that’s an international conspiracy, give me more of them. Similarly, since I am here to say unpopular things, I don’t believe for a moment that insurance brokers lobby against the entry of banks into the retail insurance market, because the brokers fear that it will force them to raise their prices… In my view, more competition is always in the interests of consumers, and consumers are, or at least should be, king.

So, to return to my conclusion, when we allow the prices of things to be freely formed, we cannot predict with certainty what the price will be at any given moment. What we can predict with confidence is that there will be a constant and irresistible pressure in the marketplace to lower prices to the marginal cost of production. Why? Because it is in the interests of producers to do so. It is also in the interests of consumers, of course, but that’s not what drives it. If producers are to win the business of consumers, they are always looking for ways to provide their product more cheaply. High prices are therefore a signal of opportunity to producers, and those high prices will be competed away over time. Consumer choice is the indispensable mechanism by which these benefits are produced.

When government nationalises or regulates, we may satisfy our desire for price stability, but we do so at the expense of these competitive pressures, and the experience generally is that we purchase that stability at the cost of a lower standard of living over time, as well as the distortions in the insurance market that political pressure inevitably introduces. You can buy almost anything you want, if you’re willing to pay the price. The question is, is price stability really what we’re after in the insurance market, and what are we willing to pay to achieve it? My answer is that it is not very valuable in itself, and nationalisation or heavy-handed regulation are far worse cures than the disease of price volatility.

Does that mean that there is nothing we can do about rising business insurance costs? Not at all. Here are four practical things that can and should be done:

1. Make it clear to the people who supply you with insurance that you are mad as hell. I certainly am. And I heard every business person in this room today say that they listen when their customers tell them something, and I see no reason to think that insurers are any different. That’s why forums like this one provide such an excellent value and why the NSCC is to be so warmly congratulated for organising it. We need to tell the industry that we expect better, and that old established relationships with brokers and insurers will not survive. And the industry needs to be held to account and to explain itself, as Don Forgeron has done today on behalf of the Insurance Bureau of Canada. I actually have little doubt that the message is getting through to insurers and that they are searching for new ways to protect their business by improving prices and service.
2. Open the insurance industry to all providers who have the capitalisation and other qualifications necessary. We should be removing regulatory barriers to e.g. banks entering the market so that if they can do so more cheaply using their existing branch network and pass those savings along to consumers, they are not prevented from doing so.
3. Demand that the tax burden on insurance be lowered. Jack Mintz, one of Canada’s leading tax policy experts and the President of the C.D. Howe Institute, the top think tank in the country, wrote a piece in the newspaper just the other day pointing out that the tax burden on insurance in Canada is the highest in the industrialised world. Governments are benefiting from your pain, and are a major cause of it, and they should be held accountable for that.
4. Ensure that “liability creep” is not allowed to emerge from the court system. We seem to be headed in the same direction as the United States, where the courts are condoning a general shift of legal responsibility away from holding individuals accountable for their own actions and decisions, and toward making others bear those costs. Often those others are businesses who, in good faith, have supplied goods or services to responsible adults who then abused them or used them irresponsibly, hurt themselves, and want compensation. The cost of these behaviours is inevitably going to drive up the cost of property and casualty and other liability insurance. We shouldn’t want the mentality here that if you spill hot coffee on yourself, you sue the restaurant and get settlements in the millions. Someone has to pay the cost, and it is businesses and their customers, not insurance companies with mythical “deep pockets”. Those pockets are only as deep as the premiums they collect, and those premiums come from you and me. Tort reform is going to have to move up the political agenda as these unjustified costs rise.

Thank you.