

FINANCIAL SERVICES COMMISSION

Panel Discussion Presentation:

“Coordinating to Compete: Limitations of the Motor Vehicle Insurance Market”

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INTRODUCTION

Good afternoon, ladies and gentlemen. It is indeed a distinct pleasure to be invited to participate in this panel discussion on the motor vehicle insurance market. The Financial Services Commission (“FSC”) welcomes this opportunity to engage industry stakeholders and the wider public in dialogue.

FSC’ MANDATE

In keeping with Section 6 of the FSC Act, the FSC strives to (among other things) protect customers in the insurance, securities and pensions industries by,

- Regulating and supervising prescribed institutions for financial soundness,

- Promoting the adoption of procedures designed to control and manage risk, and
- Promoting public understanding and confidence of these financial institutions

Addressing the last point above; it could be said that the FSC has had mixed results as its ability to promote understanding is limited by its statutory remit and the expectations of the public.

Over the past ten years, the insurance companies have grown from strength to strength as the FSC has implemented and intensified a number of prudential requirements such as capital adequacy, asset quality and liquidity standards.

These measures aim at ensuring that insurance companies will have the required funds to satisfy claims that may arise from time to time, as well as to foster a sound and viable insurance industry.

DETERMINATION OF PREMIUMS

It is in this regard that FSC does not have nor desire the power to stipulate the premiums that insurance companies should charge or risks that they should accept. The FSC's authority is to ensure that the companies are adequately and appropriately capitalised to match their risks. If the FSC had been given such

authority to determine premiums and to determine risk exposures while having its existing power to demand that insurance companies increase their capital requirements, the regulatory framework in Jamaica would be heavy-handed, burdensome and stifle the stability and life of the insurance industry.

Furthermore any action relating to premiums can have a material impact on a company's capital and its ability to withstand shocks and meet its obligation to policyholders. Therefore there would be a conflict of interest as regulating price is not always compatible with the goal of ensuring that the companies are well capitalised and financially sound.

There are many examples worldwide where a governmental body has been established to review and approve increases in premiums e.g. USA and Canada. Again, care must be exercised as suppression of prices and consequently inadequate pricing could cause a drying up of the insurance market. That is, insurance companies decide to exit the market. This dislocation of the market has resulted in the establishment of market pool associations and an influx of business to market pool associations. Today in many states and provinces of the United States and Canada, there exist pool associations for health and motor classes. While market pool associations operated by governments tend to cover risks that private insurers consider too risky or unsustainable, the rates charged by these associations tend not to be among the lowest.

Pool associations are not able to guarantee the lowest prices as the fundamental principles of insurance still apply. One such principle is that premiums should be commensurate with the degree of risk an insurer accepts. Therefore when there is a high claims ratio for any class of business, that class of business is considered to be more risky and consequently insurers worldwide and locally would demand higher premiums since they are taking on greater risk.

In Jamaica, motor vehicle insurance is a class of business that has consistently had a high claims ratio of at least an average of 71 percent. That is, motor vehicle claims alone, not including expenses, expended 71 percent of premiums income for that class of business. Furthermore in the period of 2001-2010, motor vehicle claims consistently accounted for over 60 percent of total premium income for all classes. It should be noted that unlike other classes of business, insurers are not able to cede significant portion of the risk to overseas reinsurers and hence the local insurers have to fund these claims by themselves.

Currently there are ten active general insurance companies in the industry. With the three top firms accounting for 60 percent of the total combined gross premium written for the motor class of business and a Herfindahl-Hirschman Index of 1700, the motor class business is moderately concentrated.

Furthermore with many insurance brokers and agents, insurance companies have been discounting their premiums to gain market share. Given these conditions and the persistent high claim ratios, one company has elected to stop underwriting motor vehicle class of business while another has decided to reduce its third party risk.

If Jamaica had a public body – not necessarily the regulator –to review and approve premiums, it is possible that body would have to approve increases in premiums, given the very risky nature of the motor class. Additionally we must consider what the impact on competition within the industry would be.

MARKET CONDUCT

Pursuant to the Insurance Act 2001, the FSC also has responsibility for market conduct. One of the ways in which the FSC monitors market conduct is the handling and processing of complaints. For the past ten years, the FSC has annually handled over 100 complains relating to general insurance. We also process claims for the life insurance sector and the securities and pensions industries. For the fiscal year ended March 31, 2011, the FSC reviewed a total of 214 complaints. All complaints were acknowledged within 5 working days, that is, within the time period as required under the FSC's service standards.

For the general insurance industry, 140 complaints were reviewed; 85 percent of these complaints related to delays in claim settlement; 10 percent were related to claims not honoured by the company; and five percent related to disputes regarding the quantum of settlement. Where there is a breach of the Insurance Legislation, the FSC has power to give directions in these matters; however we have no authority to determine liability or the amount of settlement. These are issues for the Court or for settlement by agreement of the parties.

Having becoming aware of the issues based on the nature of the complaints, we are conducting research and developing appropriate policy positions. For example, in 2009, the FSC issued guidelines regarding market conduct behaviour and service standards for the settlement of claims.

We also monitor the industry for any violation of Regulation 142 which identifies and prohibits a list of unfair trade practices. This regulation makes it unlawful for any insurer to discriminate or refuse to offer coverage on certain conditions.

The best way to help consumers is to empower them. Over the ten years we have and continue to present seminars, workshops and community interactive talks to disseminate relevant information that will aid policyholders to know

their rights and to ask the relevant questions. We continue to make progress in developing a National Financial Literacy Programme (“NFLP”) aimed at equipping the Jamaican populace with the knowledge and skills to make informed financial decisions. Through the NFLP, consumers will be equipped with the requisite knowledge to (i) make sound financial decisions, (ii) plan for the future, (iii) protect their assets and themselves, (iv) evade fraud, and (v) exercise their consumer protection rights.

We welcome all information and encourage everyone to report any complaints or suspected breaches to the FSC.

Thanks for your time.