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Motor accidents, insurance claims and the impact of regulation

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Introduction

1. As part of a study on the impact of claims management regulation the consultant is seeking to analyse whether claims management companies, and the regulation of them, has contributed to access to justice through more people who are entitled to claim compensation actually doing so. This paper is the first stage in this process and has been prepared as a basis for discussion with interested parties. The paper begins with an analysis of theoretical issues and then briefly examines the available evidence. The paper concentrates on the area for which most data is available, that is personal injury claims as a result of motor accidents, but also quotes some relevant data in respect of financial claims.

The starting point

2. Two key points form the starting point for the analysis of personal injury claims -
- Only a proportion of those eligible to claim for personal injury do so, largely because the size of the claim does not justify the effort needed to make a claim.
 - A small proportion of claims are fraudulent and of those that are fraudulent a disproportionate number are handled by claims management companies.

Have claims management companies increased the volume of personal injury claims?

3. A personal injury claim is a one-off product and solicitors who handle personal injury claims have no name awareness. Making a claim is perceived to be difficult, and solicitors are not the most customer-focussed of businesses. Also, many people do not realise that they are eligible to make a claim. It follows that only a proportion of people eligible to claim actually do so. Claims management businesses exist only because of reforms in the finding of personal injury claims, coming into effect from 2000. They have sought to introduce people with a potential claim to solicitors who handle claims through –

- National advertising on radio and television which has served to increase awareness of the ability to claim as well as persuading specific individuals with a potential claim to make a claim.
- Some local advertising.
- Those with access to people who may have a claim (vehicle repair businesses, minicab firms, car hire companies, medical professionals etc) introducing potential claims directly to solicitors or to a claims management company which in turn would package and to some extent process claims before passing them on solicitors.

4. There are no precise figures on the size of the market which in any event is not easy to define. Direct media advertising for personal injury claims is in the region

of £35 – £40 million while the total turnover of claims management companies in respect of personal injury cases is around £300 million a year.

5. It is only logical to conclude that such activities have increased the proportion of potential claimants who make a claim.

6. It is known that some personal injury claims are fraudulent, and that many fraudulent claims are handled through intermediaries. However, it is difficult to detect fraudulent claims; clearly if an insurer knows that a claim is fraudulent it will not pay it.

Has claims management regulation increased the volume of personal injury claims?

7. With effect from April 2007 claims management businesses were required to be authorised under the Compensation Act 2006

The objectives of regulation were set out in the Regulatory Impact Assessment for the Compensation Bill –

“This proposal aims to provide better safeguards for consumers of claims management services. It is designed to encourage the provision of quality services, to enhance consumer protection and to provide consumers with a clear route to redress. In particular, the proposal aims to improve the effectiveness and efficiency of the system for those who have a genuine claim to compensation, and to tackle practices that have helped to spread the misperceptions and false expectations of compensation claims amongst consumers. This will help to build consumer confidence and promote effective competition within the sector, whilst ensuring that the sector will be able to contribute effectively to the widening of access to justice.”

8. It is clear from this set of objectives that claims management regulation could be expected to increase the ratio of actual to potential claims and to decrease the number of fraudulent claims. Regulation would add a powerful marketing tool to claims management businesses who could say that they complied with strict government standards. To the extent that it increased standards and professionalism it helped claims management businesses transform an increasing proportion of potential cases into actual cases. Regulation also helped claims management businesses in their relationships with solicitors. Previously, some solicitors may have felt that “it was not the done thing” to deal with claims management businesses, which were seen as being rather murky and disreputable. Regulation helped to remove this inhibition.

9. There is also a case for arguing that regulation would facilitate the creation of new claims management businesses, because it provided an easy means by which a new business could quickly gain a badge of respectability.

10. In summary, a theoretical analysis suggests that both the advent of claims management companies, and more recently their regulation, could be expected to increase the proportion of potential claims that become actual claims, and that the increase in fraudulent claims caused by claims management companies should have been mitigated to some effect through the impact of regulation.

The statistical evidence

11. There are of course no precise statistics that enable any of the hypotheses outlined above to be tested. Rather it is necessary to look at a range of data –

- Survey data on the proportion of potential claims that become actual claims. The lower the starting point, obviously the greater the scope for an increase in the proportion.
- Statistics on the relationship between the number of motor accidents (as a good proxy for the number of potential claims), claims notified to the Compensation Recovery Unit and claims made to insurance companies.
- Statistics on the number and turnover of businesses authorised in respect of personal injury business under the Compensation Act 2006.
- Analyses of the market for personal injury claims.
- Anecdotal evidence from the insurance industry and others.

Survey data

12. The Department of Transport's National Travel Survey gave a best estimate for the annual number of road casualties as 800,000, of which 350,000 attend hospital and 80,000 are seriously injured. Bodily injury claims resulting from motor accidents are running at about 200,000 a year, 25% of the number of casualties and 57% of the number of people who attend hospital. At first sight this suggests that a high proportion of people who are injured in motor accidents do not make a personal injury claim. The Department of Transport has estimated the casualty related costs of reported accidents at about £9 billion a year; the total cost of insurance claims is around £1.5 billion a year, again suggesting that actual claims are a relatively small proportion of potential claims. The figures mean that there is substantial scope for genuine claims to increase.

Motor accidents and compensation claims

13 The DfT publication *Reported Road Casualties - Great Britain:2008* (<http://www.dft.gov.uk/adobepdf/162469/221412/221549/227755/rrcgb2008.pdf>) contains comprehensive statistics and analysis on reported road accidents and other relevant information. The report shows a steady reduction in casualties reported in police reports. Between 1996 and 2000 reported injuries were in a narrow range of 317,000 – 324,000; by 2005 the figure had fallen to 268,000 and by 2008 there had been a further fall to 228,000. However, it is known that only a proportion of all accidents are reported to the Police, and also changes in reporting practices can partly explain year-to-year variations. However, the downward trend is very clear, a fall of around 30% over 10 years. This is supported by the figures for deaths (all of which are reported to the police), which fell by 26% over the same ten year period.

14. However, other data has moved in the opposite direction. Between 1995/96 and 2007/08 the number of seriously injured according to police records fell by over 30% from 38,000 to 25,000, but the number of road traffic casualty admissions to hospitals increased by 18% from 34,000 to 40,000.

15. Compensation Recovery Unit motor liability claims have also moved in the opposite direction to casualties reported to the Police. The following table shows the data.

| Year | CRU Motor claims 000 | Of which no treatment recorded 000 | Injuries recorded by Police 000 |
|---------------------|----------------------|------------------------------------|---------------------------------|
| 2002/03 | 392 | 214 | 296 |
| 2003/04 | 400 | 221 | 285 |
| 2004/05 | 422 | 244 | 274 |
| 2005/06 | 459 | 279 | 265 |
| 2006/07 | 509 | 335 | 255 |
| 2007/08 | 537 | 370 | 242 |
| 2007/08/ 2002/03 | 37% | 73% | -18% |

16. The table shows that while injuries recorded by the Police fell by 18% CRU claims increased by 37%. It is perhaps also significant that the number of CRU claims where there was hospital treatment actually fell marginally over the period while the number where no treatment was recorded increased by 73%. The proportion of CRU claims where no treatment was recorded increased from 55% in 2002/03 to 69% in 2007/08.

17. [This is not the place for a detailed analysis of the sharply diverging trends of road deaths and injuries recorded by the police on the one hand and admissions to hospital and CRU claims on the other. An article by Matthew Tranter in *Reported Road Casualties - Great Britain: 2008* seeks to do so. While it is to be expected that the total number of injuries will be much higher than the number reported to the police the diverging trends are far more difficult to explain.]

Claims notified to insurance companies

18. Insurance company data is difficult to use because claims can take some time to settle and final information on claims made in any one year is only available only many years later. For the purpose of this paper the best dataset is the number of bodily injury claims notified as a result of motor accidents. This data is on a calendar year basis as opposed to financial year basis. The table below reproduces the table above with the addition of a column for the insurance company data

| Year | CRU Motor claims 000 | Of which no treatment recorded 000 | Injuries recorded by Police 000 | Bodily injury claims 000 |
|---------------------|----------------------|------------------------------------|---------------------------------|--------------------------|
| 2002/03 | 392 | 214 | 296 | 117 |
| 2003/04 | 400 | 221 | 285 | 116 |
| 2004/05 | 422 | 244 | 274 | 129 |
| 2005/06 | 459 | 279 | 265 | 159 |
| 2006/07 | 509 | 335 | 255 | 183 |
| 2007/08 | 537 | 370 | 242 | 204 |
| 2007/08/ 2002/03 | 37% | 73% | -18% | 75% |

Note: Bodily injury claims are for calendar years. Seeking to adjust them to financial year data (ie 2007/08 would take $\frac{3}{4}$ of the figure from 2007 and $\frac{1}{4}$ of the figure for 2008) would not change the trend significantly.

19. It will be seen that the number of bodily injury claims has increased much more rapidly than CRU motor claims. However, it still remains below the number of injuries recorded by the police and well below the number of CRU motor claims.

Businesses authorised under the Compensation Act

20. The author's report *Claims Management Regulation, Assessment update* (July 2009) analysed the trends in the number of authorised businesses doing personal injury work. Between June 2007 and June 2009 the number of authorised businesses increased from 1,128 to 1,508 and the annual turnover from £190 million to £287 million. Although the nature of the data is such that the figures are subject to a wide margin of error, the trend is clear. At first sight these figures mean a 50% increase in turnover in the first two years of regulation. If this figure is accurate then the bulk of this increase is likely to be new business rather than business that previously would have been directly captured by solicitors. However, the figure is likely to be an exaggeration, partly reflecting businesses seeking authorisation later than they should have done so.

21. The analysis also showed a steady increase in the number of new businesses seeking authorisation.

| Period | New authorisations of businesses handling personal injury claims |
|---------------|---|
| 2007 Q1 | 394 |
| 2007 Q2 | 660 |
| 2007 Q3 | 219 |
| 2007 Q4 | 122 |
| 2008 Q1 | 133 |
| 2008 Q2 | 136 |
| 2008 Q3 | 209 |
| 2008 Q4 | 260 |
| 2009 Q1 | 184 |
| 2009 Q2 | 288 |
| 2009 Q3 | 222 |

22. The report attributed part of the trend to larger companies breaking up into smaller units, perhaps to keep below the VAT threshold.

23. The report also included a quote from the 2008/09 report of the Chief Ombudsman of the Financial Ombudsman Service, which although specifically on financial services claims seems to lend support to the argument that claims management companies have increased the number of people making valid claims.

“One of the significant drivers of consumer complaints is the now substantially increased number and activity of claims-management companies, encouraging disadvantaged consumers to complain. The Ministry of Justice reports that it has authorised over 900 of these companies to trade in the areas of financial products and services. And apparently the number of companies applying for authorisation has been growing rapidly during the past year. No figures are available for the number of complaints these companies have made on behalf of their clients – or the extent to which the companies have given their clients appropriate advice.

The vast majority of claims-management companies operate in well-trodden territory where consumer detriment has been already identified. So they are a *symptom* of the problem and not its cause.

Consumers can make a complaint direct to a business – or to the ombudsman service – free of charge. If they make their complaint through a claims-management company, on the other hand, that company will charge a fee – usually a percentage of any compensation awarded. These fees have been criticised as being disproportionate – especially in relation to the effort or expertise that some claims management companies actually deploy. So it is questionable what advantage consumers gain by using such companies.

But it is also undeniable that the marketing activities of claims-management companies have succeeded in identifying a very large number of consumers who have suffered loss. And this has resulted in many people being paid redress when they would otherwise have received nothing. Indeed, over half of the complaints we received during the year about payment-protection insurance (PPI) were brought to us on behalf of consumers by claims-management companies. And, as we report in this *annual review*, we upheld a very high proportion of these cases. So it is clear that the wider system is not working as it should.”

24. It is worth emphasising one sentence from this quote –

“But it is also undeniable that the marketing activities of claims-management companies have succeeded in identifying a very large number of consumers who have suffered loss. And this has resulted in many people being paid redress when they would otherwise have received nothing.”

While this was referred to financial claims there is no reason to think that the situation is any different for personal injury claims.

Analyses of the market for personal injury claims

25. The author’s *Assessment Impact Update* included a quote from a report by Oxera Consulting Ltd *Marketing costs for personally injury claims* (ABI Research Paper 15, 2009) -

“The final dynamic in the market is competition between solicitors for a relatively stable supply of PI work from referral companies. Referral fees have indeed increased over time. Evidence suggests that the payment of explicit referral fees began in 1999, at a level of approximately £50 per referral. For some BTE referral companies, this explicit referral fee was paid in addition to the solicitor accepting a number of unprofitable, non-injury, cases for every PI case referred. As the business model of such referral companies altered, and the non-injury cases were handled in-house, referral fees for the PI cases rose quickly to around £250. By 2006, fees of approximately £600 were considered typical and, more recently, fees of £850–£1,000 were considered not uncommon.”

26. Oxera went on to analyse the factors behind this increase –

“This section concludes that legal fees charged by claimants’ solicitors are not subject to sufficient market constraints; therefore, the expenses incurred in

marketing are not constrained by the claimant's willingness to pay. Within this structure, referral fees paid by solicitors (or the level of marketing costs they are willing to incur in-house) are likely to be the residual between the costs of actually executing the case and the costs that can be recovered via the administrative procedure from the defendants.

Both theory and practice indicate that, under the prevailing system, marketing costs will expand to take up the difference between the costs incurred by solicitors in actually executing the case and the costs they can recover. This is likely to induce a higher level of marketing spend than what would be observed in competitive markets where prices and costs are subject to a market constraint."

27. It is reasonable to conclude that increased marketing spend in a market where only a small proportion of people claim is likely to increase that proportion.

Evidence from the insurance industry

28. Some fairly anecdotal comments from the insurance industry have attributed the rise in claims in the past year (not recorded in any of the data in this paper) to the activities of claims management companies. Stephen Hester, Chief Executive of RBS, was quoted as mentioning this as a factor explaining RBS's poor motor insurance profits a few months ago, and expressing the hope that this was a one-off factor. The ABI has attributed the increase in claims in 2009 to "more intense activities of claims management activities". KPMG, in a presentation to the insurance industry, attributed motor business loss activity in 2009 partly to "claims farming".

Conclusion

29. Bringing the analysis together, it is reasonable to conclude that the advent of claims management companies and of claims management regulation has increased the number of those who have suffered injury who chose to claim. Quantifying the effect is difficult because of imperfections and time lags in the data and the number of factors that may have influenced claims. The following table brings the key data together.

| Year | CRU Motor claims 000 | Injuries recorded by Police 000 | Bodily injury insurance claims 000 | Insurance claims/CRU claims % | Insurance claims/police records % |
|-------------|-----------------------------|--|---|--------------------------------------|--|
| 2002/03 | 392 | 296 | 117 | 30 | 40 |
| 2003/04 | 400 | 285 | 116 | 29 | 41 |
| 2004/05 | 422 | 274 | 129 | 31 | 47 |
| 2005/06 | 459 | 265 | 159 | 35 | 60 |
| 2006/07 | 509 | 255 | 183 | 36 | 72 |
| 2007/08 | 537 | 242 | 204 | 38 | 84 |

30. Significant changes in trend occurred in 2005/06, and less clearly in 2007/08, partly attributable to claims management regulation. The table also suggests that if the CRU trends are correct there is plenty of scope for insurance claims to rise further for a given number of incidents of bodily injury. The substantial increase in the number and turnover of authorised claims management companies in the personal injury sector supports the view that claims management companies, and also the regulation of them, has increased the propensity to claim.