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# **No-Fault Automobile Insurance: Policy Issues**

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Department of Legislative Services  
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November 5, 1998

The Honorable Thomas V. Mike Miller, Jr., President of the Senate  
The Honorable Casper R. Taylor, Jr., Speaker of the House of Delegates  
The Honorable Members of the Maryland General Assembly

Ladies and Gentlemen:

This report on no-fault automobile insurance was prepared by the staff of the Department of Legislative Services' Office of Policy Analysis pursuant to a request by Delegate John Leopold. Given the introduction of related federal legislation and the annual introduction of no-fault legislation in the Maryland General Assembly, policy questions are raised about the effects of the implementation of a no-fault automobile insurance system. This report provides some guidance in understanding the public policy issues surrounding no-fault automobile insurance and in analyzing any related proposed legislation.

The report was prepared by Mr. Enrique Martinez-Vidal under the supervision of Ms. Tami Burt. The Department of Legislative Services appreciates the assistance and cooperation it received from all interested parties.

We trust this document will be useful to the General Assembly during the upcoming term.

Sincerely,



Karl S. Aro  
Executive Director

KSA:WGD/EMV/ncs



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## Executive Summary

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Most insurance policies today are comprehensive packages that include both first- and third-party coverages. First-party coverage, which is not fault based, includes collision and comprehensive benefits, medical benefits, and uninsured motorist coverage. Third-party coverage usually includes bodily injury liability and physical damage.

Automobile insurance systems are generally categorized as follows: the traditional tort system, the no-fault system, the "choice" no-fault system, and the "add-on" system. Twenty-seven states operate under the traditional tort liability system. Nine states have implemented a pure no-fault system with three of them employing a verbal threshold and the other six utilizing a monetary threshold. Three states allow policyholders to choose either tort-based or no-fault insurance (choice). Twelve states plus the District of Columbia either allow or require certain no-fault benefits in addition to their traditional tort system (add-on states).

The compulsory insurance law in Maryland requires every vehicle to be covered by insurance. Because Maryland combines the traditional tort liability coverage with partially optional no-fault personal injury protection coverage, it is considered an add-on state.

In 1971 Massachusetts became the first state to enact legislation to create a no-fault insurance system. Between 1971 and 1976, fifteen other states adopted some form of no-fault insurance. Since 1976 four states have repealed their no-fault laws: Nevada (1980); Georgia (1991); Connecticut (1993); and Hawaii (1998). Pennsylvania also repealed

its pure no-fault law in 1984 but reenacted a choice no-fault system in 1990.

Differences between the proponents and opponents of no-fault insurance system are based on a number of issues including: (1) cost of insurance premiums; (2) cost of litigation; (3) speed of benefit recovery; (4) distribution of compensation; (5) effects on driving behavior; and (6) propensity for dishonesty and fraud.

During the 1995, 1996, 1997, and 1998 sessions of the Maryland General Assembly, legislation was introduced to implement some form of no-fault automobile insurance; the bills were not enacted in any of those years. The 1995 and 1996 bills were similar to each other and would have created a "choice" no-fault system for Maryland drivers. Under the 1997 and 1998 bills, the current personal injury protection, uninsured motorist, and collision coverages would be replaced with "basic personal compensation" coverage, which would have been available without regard to fault.

In most of the reports and testimony addressing the issues related to automobile insurance, opponents and proponents of a particular system both agree that premium costs are too high. In addition to or instead of changing the insurance system, a number of reforms have been suggested to address insurance costs including: (1) establishing a Consumer Advocate Office; (2) repealing anti-group laws; (3) increasing insurance agent regulation; (4) increasing state regulation, including mandating rate roll-backs; (5) eliminating the collateral source rule and multiple recoveries; (6) limiting recovery of

non-economic damages; (7) requiring attorney contingency fee disclosure; (8) repealing the "seat belt" gag rule; (9) creating "Medical Injury Profiles;" (10) limiting medical reimbursements; and (11) seeking certain federal reforms.

Under a no-fault system, some studies show that premiums may decrease. But that decrease may occur only because policyholders will receive less benefits. Should non-economic damages be prohibited in non-serious cases, or should an injured party who experiences pain and suffering or mental anguish over the loss of a child be compensated? This is a philosophical question, not just a matter of lowered premiums.

From the evidence, it is not clear that litigation costs decrease under a no-fault system. Does the no-fault system encourage greater first-party suits because insurance companies will inherently deny any claim that they can? If an insurance carrier is prohibited from surcharging on claims that are not the fault of the policyholder, will a determination of negligence be required under no-fault system as well?

The many reports that have studied driving behavior under the no-fault system are contradictory and inconclusive. The studies on fraud are similarly inconclusive. It appears that automobile insurance in general contains inherent incentives that encourage a tendency towards fraud and dishonesty, regardless of the type of insurance system.

No difference exists between the percentage of claimants who are able to recover benefits within three months after an accident in a no-fault system as compared to in a traditional tort system. After three months, the tort system pays more slowly. The question remains open whether access to faster benefits outweighs the possibility of inadequate benefits. This is another philosophical question that cannot be determined by studies and numbers.

While it may be true that actuarially based conclusions show decreased benefits which could lead to lower premiums, the experiences from other states do not support that conclusion. It is possible that making a comparison between the potential outcomes under a proposed piece of legislation and similar systems in other states is not adequate. Showing positive illustrative results based solely on decreased benefits does not take into account many other possible tangential effects, including higher litigation costs, higher accident rates, or higher insurance carrier profits. As evidenced by the review of a multitude of studies, conclusive evidence is difficult to attain. In addition, a number of philosophical questions remain that cannot be answered on a purely empirical basis.

# No-Fault Automobile Insurance: Policy Issues

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## Introduction

In 1898 the Travelers Insurance Company provided the first automobile liability insurance policy. "An auto insurance policy is one that is purchased by the policyholder (first party) from the insurer (second party) that pays benefits to either the policyholder or a covered injured party (third party)."<sup>1</sup> Most insurance policies today are comprehensive packages that include both first- and third-party coverages.

Automobile insurance usually includes bodily injury liability and physical damage coverages. Bodily injury insurance protects any third party that a policyholder may injure in an accident. The coverage includes medical costs as well as legal fees and damages arising from any pain-and-suffering lawsuits. Physical damage insurance covers the automobile and sometimes the property within it. Physical damage insurance usually includes both collision and comprehensive coverage.

Several insurance coverages are not fault based. Collision automobile insurance pays benefits for accidental property damage that occurred to a driver's own vehicle through contact with another vehicle or other object. Comprehensive automobile insurance protects against damage to a car that is not related to a collision; this insurance covers certain events including theft, damage from fire, wind, flood, and vandalism. Medical benefits are usually paid to the driver and passengers of the covered vehicle regardless of fault. Uninsured motorist insurance is medical coverage for drivers and passengers of a vehicle that has been struck by another driver with no liability coverage or if they are struck by a hit-and-run driver.

## Automobile Insurance Systems

### The Traditional Tort System

A "tort" is a wrongful act that can be used as the basis of a civil lawsuit. Under the tort system, the courts assign blame or negligence to a person called the "tortfeasor." If the court determines that the tortfeasor caused the injury or damage and was guilty of fault, the tortfeasor is considered responsible. Under the traditional tort automobile insurance system, if a person is found to be negligent in operating the automobile, the wronged party can sue the negligent driver for injury or damages. An automobile

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<sup>1</sup> Eric Nordman, "The History of No-Fault Auto Insurance," *Journal of Insurance Regulation*, Vol. 16, No. 4 (Summer 1998), p. 459.

operator purchases liability insurance in order to be protected from lawsuits and financial losses stemming from negligent operation of the vehicle. The purchase of the liability insurance is to protect the assets of the policyholder, not to compensate the accident victim.<sup>2</sup> Under the tort system, in order to recover losses, accident victims must prove the negligence of the at-fault policyholder.

Under a traditional system of liability insurance, no restrictions are placed on a claimant's right to sue. At-fault drivers are responsible for paying both economic (e.g., medical costs, lost wages, and other monetary losses) and non-economic (e.g., pain-and-suffering, gross disfigurement, loss of child, loss of fertility, and other non-monetary losses) damages to the accident victims. The at-fault driver is not eligible to receive any liability benefits.

Forty-six states have adopted some form of the "comparative negligence" doctrine which allows a plaintiff to collect damages even if the plaintiff was contributorily negligent as long as the plaintiff's negligence was less than 50 percent of the combined negligence of all parties who were at fault. This is considered a "modified approach" to the "pure" comparative fault doctrine because it allows a plaintiff to recover only if the plaintiff's fault is not greater than the fault of the defendant or defendants. Otherwise, each negligent party would ordinarily bear that party's own losses.

In Maryland, however, the "contributory negligence" doctrine has been applied to causes of action based on negligence for almost 150 years. Contributory negligence is an all-or-nothing proposition. It completely bars recovery of damages by a person whose fault contributes to that damage, no matter how slight that fault might be, except in cases where the defendant's conduct is willful or wanton or the defendant had the "last clear chance" to avoid the event that caused the injury.<sup>3</sup>

## The No-Fault System

A no-fault automobile insurance system allows policyholders to collect financial losses from their own insurer regardless of fault or liability. These losses are usually restricted to only economic damages except under certain circumstances (e.g., an accident caused by a drunk or drugged driver). Claimants are guaranteed payment up to an amount specified by the policy for medical losses, lost wages, and other economic losses. In return for and to pay for these guaranteed payments, no-fault auto insurance limits a claimant's right to sue. Persons involved in accidents with no-fault coverage are entitled to benefits regardless of fault.<sup>4</sup> Non-economic damages may not be collected except in cases of serious injury.

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<sup>2</sup> *Ibid.*

<sup>3</sup> Department of Legislative Services, *Issue Papers: 1998 Legislative Session*, December 1997, p. 263.

<sup>4</sup> Elizabeth Sammis, "No-Fault Auto Insurance: Does It Provide Consumers More Benefits at a Lower Cost?" *Legislative Report Series*, Vol. 8, No. 3 (December 1990), p. 3.

An injured party may only argue for non-economic damages when the level of injury reaches a certain level or "threshold." Thresholds are barriers that prevent litigation and, theoretically, should aid in the reduction of premiums. Thresholds are either verbal or monetary. A monetary threshold is the point above which the restriction against tort lawsuits does not apply; this type of threshold is usually expressed in terms of medical cost dollars (i.e., "if medical costs exceed \$3,000"). A verbal threshold is a similar point above which litigation for non-economic damages may occur but, instead of a dollar amount, the level is expressed in a definition describing the severity of the injury (i.e., "if injury results in significant disfigurement, permanent loss of bodily function, or death").<sup>5</sup>

### **The "Choice" No-Fault Insurance System**

More recently, several states have instituted insurance systems that allow policyholders to choose between no-fault and traditional tort coverage. Under this system, if a policyholder who chooses coverage under the tort system is involved in an accident with another tort-covered policyholder, their rights remain as they currently do under the traditional tort system. If a policyholder chooses no-fault and has an accident with another no-fault driver, they both collect first-party benefits for economic damages; a negligent driver under the no-fault system can be sued for any economic damages that are above the policy limits of the injured party.

The scenario becomes more complicated when a tort-system driver has an accident with a no-fault driver. Tort-system drivers can recover both economic and non-economic damages, up to the policy limits, from their own insurance carrier. A tort-system driver can sue a negligent no-fault driver for any economic damages that exceed the tort-system driver's policy limits; the negligent no-fault driver is immune from being sued for non-economic damages.<sup>6</sup>

### **The "Add-On" Insurance System**

A number of states have an automobile insurance system under which certain aspects of the no-fault system have been combined with the traditional tort system. Under this "add-on" system, claimants receive certain specified benefits for economic losses regardless of fault. However, claimants who are not at fault may additionally recover both economic and non-economic damages from the at-fault driver or the driver's insurer.

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<sup>5</sup> American Insurance Association, *1998 Automobile Insurance Laws* (Washington, D.C.: AIA Law Publications, 1998), p. 1 of Explanatory Notes.

<sup>6</sup> U.S. Joint Economic Committee, "The Benefits and Savings of Auto-Choice," [<http://www.house.gov/jec/tort/auto/auto.htm>], April 1997.

In the 1970's laws were enacted to allow accident victims to recover financial losses (i.e., medical losses, lost wages) from their own insurance carriers.<sup>7</sup> The differences among the states that have adopted an "add-on" system occur mostly in the dollar limits which are allowable for medical expense, lost wages, funeral expenses, and replacement services.<sup>8</sup> Usually the first party benefit levels paid under an add-on system are substantially lower than those paid under a pure no-fault system. In addition, in a number of add-on states, the first party coverage may be optional.

## Current State Insurance Systems

Currently, twenty-seven states operate under the traditional tort liability system. Nine states have implemented a pure no-fault system with three of them employing a verbal threshold and the other six utilizing a monetary threshold. Three states offer policyholders the option to choose either tort-based or no-fault insurance. Twelve states plus the District of Columbia either allow or require certain no-fault benefits in addition to their traditional tort system (add-on states). The insurance systems by state are shown in **Exhibit 1**.

**Exhibit 1**  
**State Insurance Systems: 1998**

Insurance System	States
Traditional Tort (27)	Alabama, Alaska, Arizona, California, Connecticut, Georgia, Idaho, Illinois, Indiana, Iowa, Louisiana, Maine, Mississippi, Missouri, Montana, Nebraska, Nevada, New Mexico, North Carolina, Ohio, Oklahoma, Rhode Island, South Carolina, Tennessee, Vermont, West Virginia, Wyoming
No-Fault- Verbal (3)	Florida, Michigan, New York
No-Fault - Monetary (6)	Colorado, Kansas, Massachusetts, Minnesota, North Dakota, Utah
No-Fault - Choice (3)	Kentucky (monetary), New Jersey (verbal), Pennsylvania (verbal)
Add-On (12)	Arkansas, Delaware, District of Columbia, Hawaii, Maryland, New Hampshire, Oregon, South Dakota, Texas, Virginia, Washington, Wisconsin

<sup>7</sup> Ruth Gastel, "No-Fault Auto Insurance," *Insurance Issues Update* (New York: Insurance Information Institute, January 1997), p 7.

<sup>8</sup> "Replacement services benefits" are benefits for expenditures for services that the victim would normally perform without pay for the benefit of family members but for the injury. (AIA, 1998 *Auto Insurance Laws*: p. 2 of Explanatory Notes).

## **Maryland's Current Automobile Insurance System**

The compulsory insurance law in Maryland requires every vehicle to be covered by insurance. Because Maryland combines the traditional tort liability coverage with partially optional no-fault personal injury protection coverage, it is considered an add-on state.

### **Liability Comprehensive Coverage (Required)**

Sections 17-103 and 17-104 of the Transportation Article prohibit the Motor Vehicle Administration from issuing or transferring the registration of a motor vehicle unless the owner furnishes evidence of the required minimum security. The minimum security includes \$20,000 (one person) and \$40,000 (occurrence) for bodily injury or death to persons injured in accident; and \$10,000 for property damage to other vehicles and property. A policyholder may opt to increase coverage limits.

### **Uninsured Motorist Coverage (Required)**

Section 19-509 of the Insurance Article describes coverage which is provided to persons injured in an accident caused by a vehicle which is uninsured or underinsured. The minimum required coverage which must be secured under an automobile policy is \$20,000 (one person) and \$40,000 (occurrence) for bodily injury or death to anyone injured in accident and \$10,000 for property damage. These levels of coverage mirror the minimum bodily injury and property damage liability requirements. A policyholder may also increase uninsured motorist coverage limits but those limits may not exceed the bodily injury and property damage liability levels that have been purchased.

### **Personal Injury Protection (PIP) (Partially Optional)**

Section 19-505 of the Insurance Article requires insurance companies to provide \$2,500 for medical, hospital, and disability benefits under an automobile insurance policy. A policyholder may choose to purchase higher benefit levels. These benefits are provided to those injured in an accident regardless of fault. Only economic damages are paid under this coverage. The benefits are provided to the first named policyholder, the first named policyholder's family members, other persons injured while occupying the insured vehicle, and pedestrians injured in an accident in which the insured vehicle is involved. As this coverage is optional, a first named policyholder may waive PIP coverage for himself/herself, listed drivers, and other members of the first named

policyholder's family residing in that household who are 16 years or older. However, if the first named policyholder waives PIP on his/her own insurance policy, the person effectively waives PIP while riding in other private passenger vehicles. Even if waived, PIP still applies to family members under age 16, pedestrians, and for any passengers in the first named policyholder's vehicle who has not similarly waived PIP benefits.

### **Collision Coverage (Optional)**

Under Section 19-512 of the Insurance Article, optional collision coverage must be offered with benefits paid regardless of fault by the policyholder for accidental property damage to the policyholder's motor vehicle caused by physical contact with another vehicle or other object or by upset of the insured vehicle (i.e., the car has rolled). Insurance carriers usually surcharge claims under collision coverage.

### **Comprehensive Coverage (Optional)**

Optional comprehensive coverage provides insurance against property damage to the policyholder's vehicle caused by theft, vandalism, acts of God, and other damage not involving contact with another motor vehicle or stationary object (e.g., a tree falling on the vehicle, or hailstone damage). Claims are paid regardless of fault by the policyholder. A claim made under comprehensive coverage is usually not surchargeable.

## **The History of No-Fault Insurance**

The concept of no-fault insurance was first envisioned in 1932 by a group of Columbia University social science professors when they released the *Report by the Committee to Study Compensation for Automobile Insurance*. After several decades in obscurity, the idea was resurrected in 1965 by two law school professors, Robert A. Keeten and Jeffrey O'Connell, in their book, *Basic Protection for the Traffic Victim*.

In 1971 Massachusetts became the first state to enact legislation to create a no-fault insurance system. Between 1971 and 1976, fifteen other states adopted some form of no-fault insurance.<sup>9</sup> Since 1976 four states have repealed their no-fault laws: Nevada (1980); Georgia (1991); Connecticut (1993); and Hawaii (1998). Pennsylvania also repealed its pure no-fault law in 1984 but reenacted a choice no-fault system in 1990.

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<sup>9</sup> 1972: Florida; 1973: Connecticut, Michigan, New Jersey; 1974: Colorado, Hawaii, Kansas, Nevada, New York, Utah; 1975: Georgia, Kentucky, Minnesota; 1976: North Dakota; 1990: Pennsylvania.

No state enacted the "pure" no-fault system advocated by Keeten and O'Connell in 1965. All of them retained the ability to sue an at-fault driver if the accident resulted in a high level of injury. Threshold levels, which relate to the severity of injury, vary from state to state. Proponents of no-fault insurance claim that verbal thresholds and high monetary thresholds help restrict litigation and, therefore, reduce costs and delays in paying claims.<sup>10</sup> However, low threshold levels may not act as much of a deterrent to lawsuits. When a dollar amount is cited as a monetary threshold there may, in fact, be incentive for accident victims to view that amount as a potential target to be attained so that non-economic damages may be collected. In addition, monetary thresholds may be undermined by inflation and, more specifically, especially over the past decade, by medical costs inflation. On the other hand, verbal thresholds also may be eroded by broad judicial interpretation of the language of the verbal threshold which, in turn, may lead to increased costs. **Exhibit 2** depicts the threshold amounts for those states with monetary no-fault systems.

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**Exhibit 2**  
**Threshold Amounts in Monetary No-Fault States<sup>11</sup>**

State	Threshold
Colorado	\$2,500
Kansas	\$2,000
Massachusetts	\$2,000
Minnesota	\$4,000
North Dakota	\$2,500
Utah	\$3,000
Kentucky (Choice)	\$1,000

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## Automobile Insurance Systems Policy Issues

Proponents of a no-fault automobile insurance system believe that the traditional tort system is wasteful, unfair, expensive, cumbersome, and encourages fraud and dishonesty. They claim that the tort system encourages litigation which increases costs

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<sup>10</sup> Gastel, "No-Fault Auto Insurance," p. 1.

<sup>11</sup> AIA, 1998 *Auto Insurance Laws*.

leading to higher premiums. The payment of non-economic damages, usually at the rate of three times the economic damages, also increases premiums as higher benefits are paid. They also believe that under a no-fault system, because it relies on first party payments, compensation is paid more quickly than under what they see as a slow and cumbersome tort system. Because many insurance carriers would prefer to settle out-of-court for smaller claims, no-fault proponents claim that the tort system is inherently a more unfair system as smaller claims are paid proportionally higher benefits than larger more contentious claims that are litigated. In addition, if negligence cannot be proved by the injured party, no compensation is awarded from a driver who may have caused the accident. Because non-economic damages are linked to the level of economic damages, no-fault advocates also contend that fraud and dishonesty is encouraged, especially in the overutilization of medical services, so higher levels of economic benefits can be reached.

Opponents of the no-fault insurance system claim that premiums are lower under a traditional tort system since the adoption of the no-fault system may possibly lead to the elimination of safe driver discounts. They contend that the no-fault system causes good drivers to subsidize high risk drivers as no one is considered negligent. They believe that litigation and court judgments are the only means by which injured parties can be completely compensated for their injuries and any attending pain and suffering; non-economic damages reflect the true cost of the accident to the victim. Opponents also contend that litigation does not decrease under a no-fault system because injured parties must sue their own insurance companies in order to collect adequate compensation. Further, policy limits on medical benefits reduce care to injured parties and also have led to increased lawsuits. They also believe that the quicker payment of benefits under a no-fault system sacrifices adequate compensation since a longer period of time may be required to determine the full extent of the needed compensation and medical benefits. Lastly, opponents believe that abolishing negligence leads to riskier driving behavior as drivers are no longer held accountable.

The following section of this paper discusses the competing contentions and any related studies or documentation that may support or contest the arguments.

## **Insurance Premiums**

Insurance premiums have been steadily increasing over the past several decades. A number of studies have identified several underlying trends that are seen to be responsible for these increases, including: (1) more people are making claims for injuries even as accident rates decline; (2) many of these additional claims are for minor injuries; (3) medical expenses and insurance payments have been increasing; and (4) injured claimants are increasingly likely to seek attorney representation.<sup>12</sup>

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<sup>12</sup> Insurance Research Council, *Trends in Auto Injury Claims: Part Two: Analysis of Claim Costs* (Wheaton, IL: Insurance Research Council, December 1995), p. 1.

Proponents of the no-fault insurance system point out that the traditional tort system has higher transaction costs caused by attorney involvement.<sup>13</sup> Accident victims must hire lawyers to prove negligence on the part of the potentially at-fault driver and the insurance carriers also must hire their own lawyers. Because plaintiff's attorneys usually receive one-third of the recovery amount, there is an incentive to maximize the settlement. Defense attorneys, on the other hand, are usually paid by the hour and have an interest in prolonging the case. With one side trying to increase the settlement size and the other side seeking to extend the proceedings, litigation costs increase.<sup>14</sup> Proponents contend that limiting access to the liability system will decrease costs by curtailing litigation and decreasing allowable non-economic damages. This decrease in costs, in turn, will lead to lower premiums.

Most of these lower premium predictions are based on a number of studies published by the Rand Corporation's Institute for Civil Justice. Using an illustrative no-fault model in its 1991 study, a Rand report shows a 22 percent reduction in the total amount spent compensating injured people.<sup>15</sup> Its 1998 follow-up study, which advocates a choice no-fault system, estimates that, if all drivers were to choose the no-fault option, the costs for compensating accident victims would decrease by an average of 45 percent, resulting in a 21 percent savings in total premiums.<sup>16</sup> However, the authors do admit that the parameters of the no-fault system which a state adopts will affect the cost savings. Both the level of the threshold and the amount of the covered benefits will impact the costs.

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<sup>13</sup> See Below: Section on Litigation.

<sup>14</sup> Joint Economic Committee (JEC), "Auto-Choice," [<http://www.house.gov/jec/tort/auto/auto.htm>], April 1997.

<sup>15</sup> Stephen J. Carroll, James S. Kakalik, et al. *No-Fault Approaches to Compensating People Injured in Automobile Accidents*, (Santa Monica, CA: Rand Corporation's Institute for Civil Justice, 1991), p. 19. Their illustrative model assumes a no-fault system with a strong verbal threshold and a \$15,000 personal injury protection benefit level.

<sup>16</sup> Stephen Carroll and Allan F. Abrahamse, "The Effects of a Choice Automobile Insurance Plan on Insurance Costs and Compensation: An Updated Analysis" (Rand, 1998) [<http://www.rand.org/publications/MR/MR970/>]. Their illustrative choice model assumes that consumers who opt for the modified current system in the tort states are required to purchase bodily injury (BI) coverage to at least the state's financial responsibility level. In order to maintain the option to sue, they also are required to purchase a new form of insurance, tort maintenance, to at least that same level. They may purchase the same optional coverages available in the current system (i.e., medical payments, personal injury protection, uninsured motorist, and underinsured motorist). Consumers who choose the no-fault option are required to purchase personal protection insurance coverage to at least the state's financial responsibility level. They are also required to purchase BI coverage to at least the state's financial responsibility level.

The Rand reports have their critics. Most recently, the Network Project<sup>17</sup> testified before the U.S. Senate's Commerce Committee on the choice no-fault automobile insurance system. The Network Project criticized the 1991 Rand report for being highly speculative and "utilizing highly questionable and sometimes severely flawed assumptions; the resulting conclusions are inaccurate and often misrepresented."<sup>18</sup> The Congressional testimony enumerates the defects of the report's data and methodology including: (1) unverified and incomplete insurance industry data; (2) the use of industry "closed claim" data<sup>19</sup>; (3) unreliability of insurance industry supplied "special tabulations" with regard to pricing; and (4) a belief that consumer behavior will remain unchanged under a no-fault system.<sup>20</sup>

The Rand reports have also been criticized for confusing lowered costs with lowered premiums. Many opponents of no-fault admit that there may be some cost savings by way of lowered benefits but believe that, unless a mandatory roll-back of insurance premiums is required, the insurance carriers will keep any cost savings in the form of higher profits with consumer premiums remaining unchanged. Proponents contend that the competitive market will cause premiums to decrease as carriers vie for customers.

Critics of no-fault counter the cost-saving arguments of proponents by citing the 1991 Rand report itself: "All no-fault plans reduce transaction costs. However, with the exception of plans that ban claims for non-economic loss, the net reduction in total costs provided by reduced transaction costs is only about 10 percent; the rest of the savings must come from reduced compensation."<sup>21</sup> According to former Texas Insurance Commissioner and Federal Insurance Administrator J. Robert Hunter, in order to obtain a 30 percent reduction in personal automobile costs, benefits would have to be reduced by over 50 percent.<sup>22</sup>

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<sup>17</sup> The Network Project is a California-based nonpartisan, nonprofit consumer research and advocacy organization that works on insurance, health care, utility, and financial billing issues on behalf of consumers and taxpayers.

<sup>18</sup> Harvey Rosenfield, "No-Fault: Analysis of a Costly and Failed Experiment in Social Engineering," Testimony on S.625 before the U.S. Senate Commerce Committee. [[http://www.consumerwatchdog.org/public\\_hts/auto/nftestim.htm](http://www.consumerwatchdog.org/public_hts/auto/nftestim.htm)].

<sup>19</sup> Using "closed claims" data to estimate insurance costs is criticized because smaller claims are over-represented and larger more expensive claims are under-represented. *Ibid.* [[http://www.consumerwatchdog.org/public\\_hts/auto/nftestim.htm](http://www.consumerwatchdog.org/public_hts/auto/nftestim.htm)].

<sup>20</sup> See below: Section on Effects on Driving Behavior.

<sup>21</sup> Stephen J. Carroll and James S. Kakalik, *No-Fault Automobile Insurance: A Policy Perspective* (Santa Monica: Rand Corporation's Institute for Civil Justice, 1991), p. 17.

<sup>22</sup> Quote from J. Robert Hunter in Public Citizen's "Rand's Projected Cost Savings: Don't Believe the Hype," [<http://www.citizen.org/congress/civjus/nofault/rand.html>].

A 1990 report produced by the Maryland Department of Legislative Reference<sup>23</sup> states that between 1984 and 1989, the average automobile insurance premium in tort states was lower than in "in-balance" no-fault states (\$365.06 vs. \$388.29)<sup>24</sup>. The report included a statistical regression which revealed that the adoption of an "in-balance" no-fault system increases average automobile insurance premiums by \$26.80.<sup>25</sup>

A 1996 survey of empirical studies comparing the no-fault and tort insurance systems was undertaken for the Associated Economic Consultants.<sup>26</sup> The five studies that analyzed the relationship between the introduction of no-fault insurance and insurance premiums demonstrate a lack of consistency in the evidence supporting either the view that premiums increase or decrease but, for the most part, show that premiums increase.<sup>27</sup> However, the reviewer cautions that, in several of the studies, data, methodologies, statistical models, and a lack of consideration of other possible causation factors should cause concern as to whether accurate conclusions can be drawn.

Statistics compiled by the Insurance Research Council show that, in 1993, seven of the highest ten average bodily injury claim payments were made in states with no-fault insurance systems.<sup>28</sup> However, measuring the number of bodily injury claims per 100 property damage claims reveals that, in 1993, eight of the ten states with the lowest number of claims were no-fault states.<sup>29</sup> This outcome would be expected as most no-fault laws include a minimum threshold that must be met in order to make a liability claim. It appears that some injured parties in no-fault states can meet the threshold and, in turn, collect higher than average payments. As a cautionary note, it should be remembered that statutory benefit levels vary widely among states and could impact the level of compensation regardless of the type of insurance system in place.

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<sup>23</sup> The Department of Legislative Reference was combined with the Department of Fiscal Services. The newly reorganized department is now known as the Department of Legislative Services.

<sup>24</sup> Sammis, "No-Fault Auto Insurance," p. 10. For a no-fault state to be "in-balance", the no-fault pure premium should be about the same or lower than the estimated tort pure premium. Only an "in-balance" no-fault insurance system would offer comparable or lower auto insurance premiums than a traditional tort system.

<sup>25</sup> *Ibid.*, p. 13.

<sup>26</sup> Peter Sheldon, "No-Fault vs. Tort Insurance Schemes: A Survey of the Empirical Evidence," submitted to the Associated Economic Consultants Ltd., Vancouver, B.C., 1996.

<sup>27</sup> *Ibid.*, p. 3.

<sup>28</sup> Insurance Research Council, *Trends in Auto Injury Claims: Part One: Analysis of Claim Frequency* (Wheaton, IL: Insurance Research Council, December 1995), p. 5.

<sup>29</sup> *Ibid.*, p. 12.

A report by the U.S. Department of Transportation compares the average premiums in tort, "in-balance" no-fault and "out-of-balance" no-fault states.<sup>30</sup> Between 1976 and 1983, premiums increased by 126 percent in "out-of-balance" no-fault states, by 54 percent in "in-balance" no-fault states, and by 50 percent in traditional tort states.<sup>31</sup>

An analysis of premiums shows that the three states with the highest liability premiums in 1996 were no-fault states: New Jersey, Hawaii, and New York.<sup>32</sup> In 1996 Maryland was ranked 16th for average liability premiums and 14th for average expenditures.<sup>33</sup> **Exhibit 3** shows a comparison of average expenditures by insurance system using 1996 data from the National Association of Insurance Commissioners (NAIC).

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**Exhibit 3**  
**Private Passenger Automobile Insurance:**  
**State Average Expenditure, 1996<sup>34</sup>**

<u>Insurance System</u>	<u>Average Expenditure</u>
Traditional Tort	\$619
Add-On	\$657
No-Fault	\$729

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A comparison of growth by NAIC in average expenditures between 1992 and 1996 shows that average expenditures have risen by \$40 in traditional tort states, by \$68 in add-on states, and by \$80 in no-fault states during the same time period.<sup>35</sup>

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<sup>30</sup> See footnote 23 above.

<sup>31</sup> U.S. Department of Transportation (US DOT), *Compensating Auto Accident Victims: A Follow-up Report on No-Fault Auto Insurance Experiences* (Washington, DC: US DOT, May 1985), p. 68.

<sup>32</sup> National Association of Insurance Commissioners (NAIC), *State Average Expenditures and Premiums for Personal Automobile Insurance in 1996* (Kansas City, MO: NAIC, January 1998), Exhibit 4. [Note: Hawaii repealed its no-fault laws as of January 1, 1998].

<sup>33</sup> See Appendix I. [Note: Average Expenditures = (Written Premiums/Written Car-Years)].

<sup>34</sup> *Ibid.*, extrapolated from Exhibit 2.

<sup>35</sup> *Ibid.*

Critics of no-fault also point to liability premiums in states that choose to repeal their no-fault laws. Georgia consistently ranked by NAIC as being between the 16th and 19th most expensive state between 1987 and 1990. It repealed its law in 1991 and mandated a 15 percent rollback in insurance premiums; between 1992 and 1995, it dropped to being between the 32nd and 37th most expensive state. Connecticut experienced 8 to 10 percent annual liability premium increases between 1987 and 1993 and was one of the top three most expensive states every year between 1989 and 1993. It repealed its no-fault law in 1994 and saw an almost 10 percent drop in liability premiums the following year and a 0.4 percent increase in 1996.<sup>36</sup> Proponents of no-fault believe that the repealed no-fault systems in Georgia and Connecticut were flawed from the start and therefore do not serve as valid measures of possible savings.<sup>37</sup>

Proponents of no-fault take issue with the use of comparisons of premium levels between states.<sup>38</sup> They say that it is not a question of comparing one state to another but how would one particular state fare under a no-fault system as compared to the premiums it experiences under the tort system. It is a valid point that many other variables may influence premium levels across states more than a state's insurance system, including mandatory insurance levels, driving conditions, medical costs, and accident rates. However, it is difficult to defend a position that relies on the premise that no-fault insurance should be instituted because of its theoretical potential savings regardless of the real world outcomes in states where a no-fault system has been enacted.

## Litigation

Proponents of the no-fault insurance system claim that litigation costs under the traditional tort system cause premiums to rise. Because no-fault restricts the ability of accident victims to bring lawsuits, theoretically, the no-fault system should have lower costs. Opponents of no-fault believe that no-fault does not reduce litigation costs and question what percentage of premiums is caused by litigation.

A 1994 report by the Insurance Research Council (IRC) contends that "high levels of attorney involvement in auto injury claims are associated with high auto insurance costs."<sup>39</sup> The study cites several reasons why this association exists: (1) attorneys report more different kinds of injuries than injured parties without

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<sup>36</sup> Rosenfield Testimony, [[http://consumerwatchdog.org/public\\_hts/auto/nftestim.htm](http://consumerwatchdog.org/public_hts/auto/nftestim.htm)].

<sup>37</sup> David F. Snyder, "Breaking Through the Auto Insurance Gridlock," (Washington, DC: American Insurance Association, July 22, 1998), p. 5.

<sup>38</sup> *Ibid.*

<sup>39</sup> Insurance Research Council (IRC), *Auto Injuries: Claiming Behavior and Its Impacts on Insurance Costs* (Oak Brook, IL: IRC, September 1994), p. 6.

representation; (2) claimants with attorneys incur higher medical bills; and (3) claimants using attorneys make greater use of chiropractors, physical therapists, and outpatient visits to medical doctors.<sup>40</sup> **Exhibit 4** shows the average annual bodily injury cost per insured automobile by the level of attorney representation for all tort and add-on states that had a minimum of 250 bodily injury claimants per year.

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**Exhibit 4**  
**Average Bodily Injury Cost per Level of Attorney Representation<sup>41</sup>**

<u>Level of Attorney Representation*</u>	<u>Average Bodily Injury Cost</u>
Less than 40%	\$84
40% - 49%	\$114
50% or more	\$141

\* Includes only tort and add-on states with at least 250 bodily injury claimants

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Opponents of the no-fault system believe that reduced litigation is one of the great myths of the proponents' arguments. A 1986 article in the *Insurance Counsel Journal* concludes that no-fault coverage, and to a lesser extent uninsured motorist coverage, creates as much litigation as a tort system.<sup>42</sup> One result shows Michigan, touted as the model no-fault state, with 52 motor vehicle/insurance cases in the appellate court in 1968 increasing to 82 cases in 1984.<sup>43</sup> No-fault insurance appears to have caused the development of an entire new body of law. The author concludes that "whatever the advantages of no-fault, a reduction in court cases and court costs would not appear to be one of them."<sup>44</sup> In another report, between 1976 and 1989, 73 percent of the appellate opinions in Michigan dealing with no-fault cases were first party claims in which injured parties had to sue their own insurance companies in order to collect adequate benefits.<sup>45</sup>

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<sup>40</sup> Ibid.

<sup>41</sup> Ibid., p. 57.

<sup>42</sup> Norman K. Risjord, "Does No-Fault Reduce Litigation?," *Insurance Counsel Journal*, (July 1986), p. 391.

<sup>43</sup> Ibid.

<sup>44</sup> Ibid., p. 392.

<sup>45</sup> George T. Sinas, Jane R. Bailey, and Thomas H. Hay, *The Michigan Automobile No-Fault Experience: Myth V. Fact* (Lansing, MI: MTLA No-Fault Task Force), Exhibit 1.

The 1994 IRC report includes data that show that only 52 percent of all bodily injury claimants in tort and add-on states had attorney representation while there was 81 percent with attorney representation in no-fault states.<sup>46</sup> The explanation given for the higher percentage in no-fault states is that no-fault laws prohibit some minor injury accident victims from pursuing bodily injury claims and, therefore, the remaining claims are high cost and more attractive for attorney involvement. Comparing the average number of total bodily injury claims in no-fault (351) and tort/add-on states (712) would seem to support this explanation.

A 1996 study, utilizing claims data from 21 states, investigated the correlation between liability costs and a number of tort reform measures. The authors control for environmental, economic, and injury type variables and conclude that "attorney involvement is associated with an increase in the average individual claim size amount of 64 percent."<sup>47</sup> A related finding reveals that, among the major tort reforms, placing a cap on non-economic damages decreases the average claim size by 62 percent.<sup>48</sup>

The number of litigated claims in tort states may be higher because claimants have a higher awareness of their consumer rights, since they are permitted to consult and obtain representation from an attorney. In turn, they may exercise these rights at a higher rate which may result in more claims.<sup>49</sup>

According to no-fault opponents, litigation under a no-fault system also increases due to disagreements about threshold levels. Many claimants in Michigan, with a hybrid verbal threshold that allows non-economic damages in cases of serious injury or if economic damages exceeded a prescribed limit (a monetary threshold), had to file suit with their own companies to obtain medical and lost wage benefits. Opponents point to this increase in litigation as a demonstration that no-fault unjustly decreases benefits to innocent victims.<sup>50</sup> Proponents hold these monetary limits to be a weakness in existing no-fault systems which should be replaced with strict verbal thresholds.

Opponents of no-fault also point out that under a no-fault system, the number of claimants increases as two parties must now each submit a claim to their own insurance carrier. One study suggests that at least 40 percent more claimants are eligible to receive compensation under a no-fault system.<sup>51</sup>

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<sup>46</sup> Insurance Research Council, *Auto Injuries: Claiming Behavior*, pp. 49-50.

<sup>47</sup> Mark J. Browne and Robert Puelz, "Statutory Rules, Attorney Involvement, and Automobile Liability Claims," *The Journal of Risk and Insurance*, Vol. 63 (1) (1996), p. 79.

<sup>48</sup> *Ibid.*

<sup>49</sup> Lea-Ann Tratten, "The Truth About Auto Claims" (Consumer Attorneys of California), [<http://www.caoc.com/tratten.htm>].

<sup>50</sup> William P. Atkins, "Standing at the Crossroads: An Empirical Analysis of No-Fault Automobile Insurance and Its Potential Consequences for Maryland," *The Law Forum*, Vol. 21.2 (Spring 1991), p.13.

<sup>51</sup> Study by AIS Risk Consultants, Inc. (February 1996). Cited by Pamela Anagnos Liapakis in "No-Fault Bill May Curb Motorists' Rights and Add to Insurance Costs," *The National Law Journal*, (July 29, 1996).

There is disagreement as to what proportion of premiums are spent to pay for litigation costs. According to the Insurance Information Institute, in 1995, plaintiff attorney fees accounted for only 6 cents and defense attorney fees made up only 6 cents of each automobile insurance premium dollar.<sup>52</sup> Proponents point to a 1990 California Department of Insurance study which states that, in California, 27 cents of every premium dollar paid for bodily injury liability coverage goes to plaintiff attorney fees.<sup>53</sup> If measured against total premiums, defense legal costs (e.g., attorneys representing the insurance carriers) account for 10 cents per premium dollar and plaintiff legal costs are 9-10 cents per premium dollar as well.<sup>54</sup>

### Speed of Benefit Recovery

Proponents of no-fault insurance contend that benefits are paid to claimants more quickly under a no-fault insurance scheme than under a tort system. They believe that compensation from third-party insurance carriers is more cumbersome to collect. The 1991 Rand study shows that, under its illustrative no-fault system, compensation is paid an average of two months faster.<sup>55</sup> **Exhibit 5** shows the cumulative percentage of claimants by time period that it would take to collect an initial compensation under the two systems.

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**Exhibit 5**  
**Time Frames for Compensation Collection by Insurance System<sup>56</sup>**

<u>Months</u>	<u>Traditional Tort</u>	<u>Illustrative No-Fault</u>
0-3	45%	46%
4-6	68%	85%
7-12	90%	99%
more than 12	100%	100%

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<sup>52</sup> Insurance Information Institute (III), "Where the Auto Insurance Dollar Goes, 1995," (New York: III, 1996).

<sup>53</sup> California Department of Insurance, *Consumer Information Packet Based on Automobile Claims Study of Closed Claims Payment Patterns in California* (California Department of Insurance, August 1990), p. 9.

<sup>54</sup> California Department of Insurance, *Automobile Claims: A Study of Closed Claim Payment Patterns in California* (California Department of Insurance, August 1990), p. 3.

<sup>55</sup> Carroll, Kakalik, et al. *No-Fault Approaches* (1991), p. xii.

<sup>56</sup> *Ibid.*, p. 26.

While the exhibit shows that a lower percentage of claimants receive compensation within the first six months as well as within one year, there is virtually no difference in the number of claimants receiving immediate benefits (45 percent versus 46 percent). In addition, most opponents do not dispute the statistics that show quicker recoupment of benefits, however, they believe that the numbers are misleading because the compensation levels are lower under no-fault. To opponents of no-fault, longer time frames are acceptable because they reflect the time needed to determine the full impact of an accident so an injured claimant can recover just compensation. "Thus, while the traditional tort benefits might be slower, they do not run the risk of short changing victims."<sup>57</sup>

### Distribution of Compensation

According to proponents of no-fault insurance, the tort system unjustly rewards claimants with minor injuries by paying proportionally higher benefits and does not compensate fairly those who have serious injuries and have incurred high economic losses. The 1991 Rand report argues that "no-fault substantially reduces the proportion of claimants who receive compensation in excess of their economic loss and substantially increases the proportion of claimants who are fully compensated for their economic loss."<sup>58</sup> **Exhibit 6** shows the distribution of compensation under the traditional tort system and the Rand illustrative no-fault model.

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**Exhibit 6**  
**Distribution of Claimants by Compensation Ratio<sup>59</sup>**

<b>Ratio of compensation to economic loss*</b>	<b>Traditional Tort</b>	<b>Illustrative No-Fault Model</b>
More than 1	62%	22%
Exactly 1	7%	59%
Less than 1, more than 0	15%	3%
Exactly 0	12%	13%

\* The amount of gross compensation received per dollar of economic loss.

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<sup>57</sup> Atkins, "Standing at the Crossroads," p. 14.

<sup>58</sup> Carroll, Kakalik, et al. *No-Fault Approaches (1991)*, p. xi.

<sup>59</sup> *Ibid.*, p.24. Note: Numbers do not add up to 100 percent because accident victims with no losses are not included in the exhibit.

To investigate the claim of unfair compensation distribution under the traditional tort system, the IRC sampled injured persons by reimbursement ratio, which is the amount of reimbursement per dollar of loss. About one-third of claimants received compensation in excess of their economic losses, one-third were given compensation exactly equal to their economic losses, and another third accepted compensation that was less than their losses.<sup>60</sup> Claims with economic losses under \$1,000 averaged over \$2.00 per dollar of economic losses with claims under \$100 receiving over \$4.00 per economic loss dollar. Claimants with economic losses between \$1,000 and \$500,000 averaged between \$1.00 and \$2.00 per dollar of economic loss, while a claim with an economic loss over \$500,000 received only \$.70 on the economic loss dollar.<sup>61</sup>

Opponents of no-fault respond that the change in the distribution of compensation under the no-fault scenario is a result of restricting the compensation to victims. They use evidence from the Rand report itself to support their contention: "No-fault plans that slash costs tend to reduce the compensation less seriously injured people receive for non-economic loss, such as pain and suffering. And they don't substantially improve the traditional system's treatment of the more seriously injured, who rarely recover even their economic losses in wages, medical payments, and out-of-pocket expenses."<sup>62</sup>

Opponents of no-fault also point out that, in accidents that incur high economic damages, the reason many victims are compensated only a small percentage of those damages is because the injured person has reached the policy limits. If the policy limits are \$50,000 and medical costs are \$150,000, the injured person can be said to be under compensated with regard to economic damages spent. But this under compensation is not due to the tort system or the insurance carrier; the policyholder received \$50,000 worth of compensation which is what the policy required and what the policyholder paid for.<sup>63</sup> The same limitations would be true under the no-fault system unless there was no cap on benefits.

## Effects on Driving Behavior

One of the main arguments no-fault opponents present is that, because no-fault pays claims regardless of blame, it leads to a change in driving behavior. The tort system, because of its inherent reliance on punishing acts of negligence, functions as a deterrent to risky driving. They say no-fault shields careless and reckless drivers from legal liability for their actions. Proponents of no-fault contend that the deterrent effect

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<sup>60</sup> Insurance Research Council (IRC), *Paying for Auto Injuries* (Oak Brook, IL: IRC, May 1994), p. 14.

<sup>61</sup> *Ibid.*, p. 16.

<sup>62</sup> Rand Institute for Civil Justice, Press Release (National), p. 2. Cited in the Rosenfield Testimony (footnote 18), [[http://consumerwatchdog.org/public\\_hts/auto/nftestim.htm](http://consumerwatchdog.org/public_hts/auto/nftestim.htm)].

<sup>63</sup> Testimony of former Georgia Insurance Commissioner Tim Ryles on S. 625, The Auto Choice Reform Act of 1997 before the U.S. Senate Committee on Commerce, Science, and Transportation, September 9, 1998, p 8.

of automobile insurance is not affected by the type of compensation system. Bad drivers would still be affected by traffic laws and any ensuing premium increases caused by risky driving and accidents.<sup>64</sup>

An article by Gary T. Schwartz observes that much negligent behavior is inadvertent and not the result of a conscious decision to engage in risky activities.<sup>65</sup> On the other hand, not all negligence is based on inadvertence, but is the result of purposeful behavior, such as drunk driving or speeding. The study also notes that liability insurance actually imposes itself between a driver and the threat of liability in such a way that the deterrent effects are diminished. However, because automobile insurers have underwriting standards that take certain demographic factors into account when determining premiums, tort insurance increases the price of insurance for those drivers who are most likely to engage in risky driving behavior.

A number of studies have been conducted to analyze the correlation between the threat of liability and its deterrent effect. The empirical evidence from these studies show mixed results. A 1980 study conducted by Landes concludes that a no-fault system with moderate restrictions on tort suits leads to a 2-5 percent increase in traffic fatalities while more restrictive no-fault laws result in a 10-15 percent increase.<sup>66</sup> However, the Landes study has been criticized for using flawed methodology, misinterpreting results, and omitting other variables that could account for increased fatalities.<sup>67</sup> In 1982 Medoff and Magaddino studied the effect of state insurance systems on carrier loss ratios which are the percentage of premiums paid for claims and then weighted by the percentage of insured vehicles involved in accidents.<sup>68</sup> The results show increasing loss ratios as a state's insurance system increasingly limits tort liability; the authors' hypothesis that the no-fault insurance system reduces accident deterrence is supported. In a 1992 study, Cummins and Weiss look at the relationship between the no-fault insurance system and property damage and collision claims. They found that, under the no-fault system, the frequency of total property damage claims is higher; these findings imply that accident rates are higher under the no-fault system.<sup>69</sup>

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<sup>64</sup> Snyder, "Auto Insurance Gridlock," p. 4.

<sup>65</sup> Gary T. Schwartz, "Reality in the Economic Analysis of Tort Law: Does Tort Law Really Deter?," *UCLA Law Review*, Vol 42 (1994), pp. 377-444.

<sup>66</sup> Elisabeth M. Landes, "Insurance, Liability, and Accidents: A Theoretical and Empirical Investigation of the Effect of No-Fault Accidents," *Journal of Law & Economics*, Vol. XXV (April 1982), pp. 49-65.

<sup>67</sup> Sheldon, "No-Fault vs. Tort Insurance Schemes," p. 9.

<sup>68</sup> Marshall H. Medoff and Joseph P. Magaddino, "An Empirical Analysis of No-Fault Insurance," *Evaluation Review*, Vol. 6 (3) (June 1982), pp. 373-392.

<sup>69</sup> J. David Cummins and Mary A. Weiss, "Incentive Effects of No-Fault Insurance: Evidence from Insurance Claim Data," in *Contributions to Insurance Economics*, ed. by Georges Dionne (Boston, MA: Kluwer Academic Publishers, 1992), pp. 445-470.

Between 1985 and 1992, several studies were conducted demonstrating that the implementation of a no-fault system does not increase negligent behavior and lead to more accidents. In 1985 Kochanowski and Young examined cross-sectional data from the United States in 1975, 1976, and 1977.<sup>70</sup> They determined that no evidence could be found to show that the introduction of no-fault increased fatality rates. Using data from 1967 to 1980 for all 50 states and the District of Columbia, Zador and Lund found that the effect of no-fault auto insurance does not increase the number of fatal car accidents.<sup>71</sup> However, their model also has been criticized for not including a number of variables that could have possible explanatory power for these results.<sup>72</sup> A 1985 U.S. Department of Transportation study found that the introduction of no-fault laws did not lead to a detectable change in automobile accident rates. The study concludes that no-fault's effect on fatal and injury-related accident rates is less than 7 percent and, because "the effect is so small, it is impossible to distinguish the effects of no-fault insurance from the effects of other influence."<sup>73</sup> The study's methodology has been criticized for being too crude to determine any greater effects than were found.<sup>74</sup>

The 1994 Sloan study measures how automobile fatality rates for three age groups were affected by certain factors including a number of variables pertaining to tort law and insurance, alcohol consumption, criminal sanctions, number of miles driven, rural miles driven, and several state- and time-dependent variables.<sup>75</sup> The study concludes that tort liability has a deterrent effect on careless driving. For persons over 21 years old, the "results imply that increasing the fraction of accidents barred from tort liability by enacting no-fault automobile insurance statutes increases the traffic fatality rate...".<sup>76</sup> However, the study admits that the United States, due to its lack of experimentation with no-fault laws, is not the best location to study the effects of these incentives. The study also posits that tort liability is not the only deterrent and many other approaches for lowering traffic fatalities might have a greater effect than tort liability.

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<sup>70</sup> Paul S. Kochanowski and Madelyn V. Young, "Deterrent Effects of No-Fault Automobile Insurance: Some Empirical Findings," *Journal of Risk and Insurance*, Vol. 52 (1985), pp. 269-288.

<sup>71</sup> Paul Zador and Adrian Lund, "Re-Analysis of the Effects of No-Fault Auto Insurance on Fatal Crashes," *Journal of Risk and Insurance*, Vol. 53 (1986), pp. 226-241.

<sup>72</sup> Sheldon, "No-Fault vs. Tort Insurance Schemes," p. 11.

<sup>73</sup> U.S. Dept. of Transportation, *Compensating Auto Accident Victims*, p. 166.

<sup>74</sup> Schwartz, "Does Tort Law Deter?," p. 395 (see footnote 85).

<sup>75</sup> Frank A. Sloan, Bridget A. Reilly, and Christoph M. Schenzler, "Tort Liability versus Other Approaches for Deterring Careless Driving," *International Review of Law and Economics*, Vol. 14 (1994), pp. 53-68.

<sup>76</sup> *Ibid.*, p. 68.

Two studies were conducted to review accident rates following the initiation of no-fault in the Province of Quebec, Canada in 1978. Quebec instituted a "pure" no-fault system that provides for unlimited benefits for economic losses and completely abolishes tort liability for personal injury. Using an econometric model, Gaudry estimates the introduction of no-fault to be associated with a 6.8 percent increase in accidents with fatalities; a 26.3 percent increase in accidents with injuries; and an 11 percent increase in accidents with property damage only.<sup>77</sup> Using different data and different methodology, Devlin reports an estimated 9.62 percent increase in fatalities as the result of implementing no-fault.<sup>78</sup> However, at the time, non-experience rated premiums were also implemented; the study acknowledges that the data could not distinguish the proportion of the increase caused by each factor. The Devlin study also estimates a 27 percent increase in the number of bodily injury claims but also notes that approximately 17 percent of this increase was due to a "reporting effect."<sup>79</sup> After controlling for reporting effects, the increase in bodily injuries is approximately 10 percent.

The 1994 UCLA Law Review article distinguishes between two levels of deterrent affect of liability.<sup>80</sup> In its "strong" form, tort law deters in a comprehensive, systematic way; in its "moderate" form, it does not deter comprehensively but provides a meaningful amount of deterrence. After reviewing the information available about many types of tort law, including workers' compensation, automobile liability, medical malpractice, and products liability, the author concludes that tort law does not deter in its strong form but does work in its moderate form.<sup>81</sup>

## Dishonesty and Fraud

Proponents of no-fault believe that one of the greatest weaknesses of the tort system is that it inherently encourages fraudulent and dishonest behavior. Because the tort system includes compensation for non-economic damages for even minor injuries, there are incentives for causing accidents, inflating medical and other economic damage costs, or possibly faking injuries to increase compensation. Proponents of no-fault point to organized fraud rings in California as an example of the tort system encouraging people to stage accidents or file claims that never occurred.

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<sup>77</sup> Marc Gaudry, "Measuring the Effects of the No-Fault 1978 Quebec Automobile Insurance Act with the DRAG Model," in *Contributions to Insurance Economics*, ed. by Georges Dionne (Boston, MA: Kluwer Academic Publishers, 1992), pp. 471-498.

<sup>78</sup> Rose Anne Devlin, "Liability Versus No-Fault Automobile Insurance Regimes: An Analysis of the Experience in Quebec," in *Contributions to Insurance Economics*, ed. by Georges Dionne (Boston, MA: Kluwer Academic Publishers, 1992), pp. 499-520.

<sup>79</sup> Under the Quebec no-fault law, drivers are not penalized for reporting an accident as bodily injury or property damage, and may be compensated.

<sup>80</sup> Schwartz, "Does Tort Law Deter?," p. 387.

<sup>81</sup> *Ibid.*, p. 443.

Opponents of no-fault respond that there is no correlation between fraudulent behavior and the system of automobile insurance system. In fact, they point out that the easy availability of medical benefits and wage loss benefits encourages unnecessary claims in the no-fault system.<sup>82</sup> Opponents of no-fault question, if no-fault eliminates fraud, why the New York legislature is considering legislation to establish a fraud unit in the State Insurance Commission to combat automobile fraud.<sup>83</sup> Opponents also contend that no-fault encourages fraud because, under the assumption that, for the most part, an insurer wants to maintain its customer base, payments to their own policyholders will be more generous than to third party claimants. This incentive will make paying claims easier than conducting extensive investigations. As noted above, thresholds under a no-fault system could encourage injured parties to inflate claims in order to meet these thresholds.

In testimony before the U.S. Senate Committee on Commerce, Science, and Transportation, Tim Ryles, former Georgia Insurance Commissioner, notes that the inherent structure of the insurance industry does not provide incentives to discourage fraudulent behavior.<sup>84</sup> The insurance industry has "a mandated market<sup>85</sup>, a monopoly mentality of passivity<sup>86</sup>, a regulatory system that says an insurer can't lose money<sup>87</sup>, and insurer freedom to select its book of business.<sup>88</sup>" The systemic incentive do nothing to alleviate fraud as claims costs can be passed through to other policyholders and, if any single policyholder becomes too great a risk, the carrier can terminate coverage.

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<sup>82</sup> The Consumer Project, "The Absolute Failure of No-Fault: Premium Trends in No-Fault States," [[http://www.consumerwatchdog.org/public\\_hts/auto/nfreport.htm](http://www.consumerwatchdog.org/public_hts/auto/nfreport.htm)], July 1997.

<sup>83</sup> Lea-Ann Tratten, "The Truth About Auto Claims," [<http://www.caoc.com/tratten.htm>]. [Note: New York is a no-fault state].

<sup>84</sup> Ryles, Testimony on S. 625 (September 9, 1998).

<sup>85</sup> Automobile insurance is mandated by law in most states and, if a car is financed, a lending institution usually requires some sort of property damage insurance (Ryles).

<sup>86</sup> The system has cultivated a belief among insurers that auto insurance carriers are just "pass through" organizations, meaning they merely passively collect the premiums, pay claims, pass costs along to consumers, and take a profit for administering the program (Ryles).

<sup>87</sup> State laws governing auto insurance rates stipulate that rates cannot be "excessive, inadequate, or unfairly discriminatory." This means that state law imposes a statutory duty on insurance regulators to preserve carrier solvency. Insurers cannot lose money and stay in business (Ryles).

<sup>88</sup> Insurers can determine their own market by deciding who is eligible to buy a policy, who is not, who they keep, and who they terminate (Ryles).

## Federal Legislation

The U.S. Congress has recently considered the Automobile Choice Reform Act of 1997 (S.625). Under this legislation, which aims to promote a "choice" no-fault system, drivers would choose between a no-fault system with limited liability and the traditional tort system which retains the driver's ability to sue.<sup>89</sup> All individuals would be required to purchase first party "personal protection insurance" (PPI). Those policyholders who want to retain limited liability rights would purchase additional "tort maintenance coverage" (TMC).<sup>90</sup> If a TMC (tort) driver is in an accident with another TMC driver, the recovery system remains as it is currently under the traditional tort system. TMC drivers who are injured by a negligent PPI (no-fault) driver collect economic and non-economic damages up to the policy limits from their own insurance carrier; the negligent PPI driver can only be sued for any economic expenses that are not covered by the injured driver's own policy. A negligent PPI driver cannot be held liable for any non-economic damages unless the injuries were inflicted intentionally or were the result of drunken or drugged driving.

Proponents of the choice system cite benefits that closely mirror those benefits that they claim occur under a typical no-fault system. These benefits include improved reimbursement and fairer compensation for accident victims. In addition, choice proponents believe that the choice system promotes improved free market conditions for automobile insurance. Because policy coverage for non-economic damages are unbundled from economic damage coverage, insurers can adapt policy parameters that meet the varying demands of individual consumers.<sup>91</sup> Choice proponents also cite lowered premiums for those who choose the no-fault option. A 1998 Rand report analyzing the choice system estimates an average premium reduction of approximately 21 percent if insurers pass on the cost savings.<sup>92</sup> Low income drivers would save an average of 36 percent of premiums.<sup>93</sup>

Opponents of the federal choice no-fault legislation restate the same arguments which are used against a "pure" no-fault system. They argue that lowered premiums are not mandatory, negligent behavior increases, fraud is not addressed, and compensation is not distributed any more fairly, equitably, or quickly. The federal legislation also eliminates the threshold which exists under most no-fault systems; non-economic damages could not be collected except under certain circumstances.

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<sup>89</sup> See above: Section on Choice No-Fault.

<sup>90</sup> Joint Economic Committee (JEC), "Auto-Choice," [<http://www.house.gov/jec/tort/auto/auto.htm>], April 1997.

<sup>91</sup> *Ibid.*

<sup>92</sup> Carroll and Abrahamse, "The Effects of a Choice Automobile Insurance Plan," (1998), [<http://www.rand.org/publications/MR/MR970/>].

<sup>93</sup> JEC, "Auto Choice: Impact on Cities and the Poor," [<http://www.house.gov/jec/tort/cities/cities.htm>], March 1998.

In addition to the usual anti-no-fault arguments, opponents also attack the federal bill from the standpoint that it encroaches on the principles of federalism that separate state and federal powers. Under the McCarran-Ferguson Act of 1945, states have been responsible for regulating the business of insurance. Senate 625 contains legislative and administrative "opt-out" provisions where states can decide to not enact the choice system under certain conditions.<sup>94</sup> Proponents refer to these "opt-out" provisions as being consistent with federalism principles. Opponents assert that it is "illusory to think that 90 days after Congressional enactment...there would be sufficient time for state legislatures to meet or for state regulators to determine if consumers would realize a decrease of more than 30 percent in personal injury premiums as envisioned in S.625."<sup>95</sup> Opponents also contend that the "opt-out" provisions may be unconstitutional and violate the spirit of the recently-passed unfunded mandate law.<sup>96</sup>

Opponents also argue that the very structure of the insurance system envisioned by the Auto Choice bill promotes a false "choice" because "an injured motorist's recovery of legal damages would depend not on his/her choice of insurance coverage, but on the other driver's choice."<sup>97</sup> Full access to courts and full recovery of damages for those who choose the TMC option is only guaranteed if the accident is with another TMC policyholder.<sup>98</sup>

A Yale University law professor, George L. Priest, states that the costs imposed by risky drivers are internalized by the tort system as negligent drivers pay higher premiums. Under no-fault, high risk drivers no longer have to pay for the costs for which they are responsible, and premiums of low-risk drivers who are injured will increase because there is limited or no recovery from the at-fault driver.<sup>99</sup> Proponents answer that criminal and insurance premiums penalties for at-fault drivers are not affected by the choice no-fault system.<sup>100</sup> The unknown answer is whether insurance carriers will increase premiums of those policyholders who are not at fault yet, under no-fault's first party payment system, cause losses to that carrier.

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<sup>94</sup> S.625, 105th Congress, 1st Session, Section 8 (1997).

<sup>95</sup> Arizona State Senator Gary Richardson, Testimony on behalf of the National Conference of Insurance Legislators before the U.S. Senate Committee on Commerce, Science, and Transportation regarding the Auto Choice Reform Act (S.625).

<sup>96</sup> Mark Mandell, Testimony on behalf of the Association of Trial Lawyers of America before the U.S. Senate Committee on Commerce, Science, and Transportation regarding the Auto Choice Reform Act (S.625), [<http://www.atla.org/homepage/test0909.htm>].

<sup>97</sup> *Ibid.*

<sup>98</sup> U.S. Representative Bill Pascrell, Jr. (D-NJ), "The No-Fault Illusion," Opinion article in the *Washington Post*, December 23, 1997.

<sup>99</sup> George L. Priest, "Why 'Auto Choice' is a Lemon," Opinion article in the *Wall Street Journal*, July 21, 1998.

<sup>100</sup> Snyder, "Auto Insurance Gridlock," p. 4.

## Recent Maryland Legislation

During the 1995, 1996, 1997, and 1998 sessions of the Maryland General Assembly, legislation was introduced to implement some form of no-fault automobile insurance; the bills were not enacted in any of those years.<sup>101</sup> The 1995 and 1996 bills were similar to each other and would have created a "choice" no-fault system for Maryland drivers. Under these two bills, policyholders who choose the no-fault option would have first-party economic damages capped at \$50,000 per individual for medical services; \$2,000 per month in wage replacement for not more than three years from the date of the accident causing the injury; and \$2,000 for funeral, burial, or cremation expenses.

The 1997 and 1998 bills were similar to each other. Under those bills the current personal injury protection, uninsured motorist, and collision coverages would be replaced with "basic personal compensation" coverage, which would have been available without regard to fault. Basic personal compensation coverage would have been capped at \$25,000 per person which would have included medical expenses, loss of income, replacement services loss, and a death benefit of \$5,000; the bills included an option for a policyholder to purchase additional coverage up to \$250,000. The bills would not have affected the current requirements for bodily injury and property damage liability. Policyholders would have been allowed to seek damages in serious injury cases for non-economic loss, to seek damages for uncompensated economic losses in all cases, and to sue drunk or drugged drivers or drivers committing a felony.

During bill hearings, the Maryland Automobile Insurance Fund (MAIF)<sup>102</sup> testified that, according to its estimates, MAIF policyholders would experience an average decrease in premiums of 16.9 percent because many non-economic damage claims would not be compensable and uninsured motorist coverage would no longer be required.

Currently, MAIF maintains the Uninsured Division which processes and pays claims to Maryland residents who are involved in Maryland accidents with uninsured motorists or in hit-and-run incidents where no responsible party can be found. MAIF testified that, because uninsured motorist property damage and collision coverages would

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<sup>101</sup> House Bill 930 (1995); House Bill 114 (1996); House Bill 341 (1997); House Bill 330 (1998).

<sup>102</sup>The Maryland Automobile Insurance Fund (MAIF) was created by the Maryland State Legislature in 1972 for the purpose of providing automobile liability insurance for those residents of the State of Maryland who are unable to obtain it elsewhere in the private insurance market. MAIF is an independent agency of the State of Maryland, and as such, reports directly to the Governor and is responsible to the Maryland State Legislature.

be repealed under the proposed bills, the Uninsured Division would experience an increase in claim payments as a large number of automobile damages currently covered by other carriers' uninsured motorist coverage would be eligible for payment by the Uninsured Division. Currently the Uninsured Division is funded from uninsured motorist penalty fees collected from the Motor Vehicle Administration of about \$3.1 million annually. The Uninsured Division annually pays claims of \$3 million and also incurs some administrative expenses. MAIF estimates that, under these bills, claims eligible to be paid by the Uninsured Division could increase to as much as \$36.4 million.

The American Insurance Association (AIA) testified that, according to its actuarial analysis, Maryland policyholders could experience average premium reductions of 14.3 percent if the system envisioned by House Bill 341 (1997) was adopted. These reductions would come primarily from the elimination of current insurance carrier payments for bodily injury claims paid to at-fault drunk or drugged drivers and from a decrease in bodily injury and uninsured motorist non-economic damage payments for non-serious injuries. There would also be some reductions in payments for uninsured motorist claims as some of those claims would be covered by the injured party's own first-party coverage. In addition, under the AIA's actuarial analysis, the current personal injury protection costs would be replaced by basic personal compensation.<sup>103</sup>

## **Other Recommendations to Address Automobile Insurance Costs**

In most of the reports and testimony addressing the issues related to automobile insurance, opponents and proponents of a particular system both agree that premium costs are too high. As noted above, there is much disagreement about the effect of the insurance system on premium rates. The following section outlines a number of other suggested reforms to the insurance system that could be considered to help lower rates. These suggestions will, of course, have opponents and proponents as well.

### **Establish a Consumer Advocate Office**

A 1995 report by the National Association of Insurance Commissioners suggests that states utilizing a consumer advocate to monitor the insurance industry have 20 percent lower premiums than those states without such an office.<sup>104</sup> A survey by the Center for Insurance Research finds that a majority of consumers who call state insurance offices for assistance receive marginally useful or often misleading or no information.

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<sup>103</sup> See Appendix 2.

<sup>104</sup> NAIC, *1995 Insurance Department Resources Report*. Cited in Public Citizen, "The Road to Lower Insurance Premiums," [<http://citizen.org/congress/civjus/nofault/road.htm>].

The center recommends that states should evaluate the effectiveness of insurance department consumer services, develop and publish insurance buying guides and information brochures, and increase funding to those departments that are understaffed, possibly through the diversion of a portion of premium taxes.<sup>105</sup> In addition, more comprehensive complaint analysis may also help reveal industry fraud and inefficiencies.<sup>106</sup>

## Repeal Anti-Group Laws

Some states, including Maryland, prohibit consumers from uniting in groups to purchase automobile insurance so as to increase leverage with carriers or create economies of scale for carriers by spreading the risk.<sup>107</sup> This type of group purchasing is typical for health insurance.

## Increase Insurance Agent Regulation

Many states prohibit insurance agents from reducing their commissions in order to sell a policy for a lower premium. In addition, there is no requirement that an agent who is representing several companies place a consumer with the insurance carrier that charges the lowest premium.<sup>108</sup> Premiums charged by substandard carriers are higher than those charged by standard carriers, however, in many urban areas, agents only sell the substandard policies.<sup>109</sup> Maryland law prohibits an agent from collecting a premium or charge for insurance that is less than the amount applicable to that insurance under the classifications and rates filed and approved by the Commissioner. Further, an agent may not offer as an inducement to the insurance a rebate, discount, abatement, credit or reduction of the premium stated in the policy.

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<sup>105</sup> Center for Insurance Research, "State Insurance Consumer Hotlines: Tepid Help and Frequent Misinformation," [[http://www.essential.org/cir/survey\\_summ.htm](http://www.essential.org/cir/survey_summ.htm)], May 1996.

<sup>106</sup> NAIC, *1995 Insurance Department Resources Report*. Cited in Public Citizen, "The Road to Lower Insurance Premiums," [<http://citizen.org/congress/civjus/nofault/road.htm>].

<sup>107</sup> Maryland law allows only certain nonprofit organizations and public entities to pool for automobile insurance (see Sections 601 and 602 of the Insurance Article).

<sup>108</sup> Ryles, Testimony of S. 625 (September 9, 1998).

<sup>109</sup> The General Assembly sought to address concerns about automobile insurance availability with the enactment of Chapter 352 of 1995 which requires major insurers to file data with the Insurance Commissioner detailing, by rating territory or zip code, the amount of private passenger premium written by the insurer in the preceding calendar year and the number of policies represented by that premium in the State as a whole and in Baltimore City. An major insurer must file a marketing plan with the Commissioner. The marketing plan must be designed to ensure that the insurer makes insurance available to residents of Baltimore City who otherwise satisfy the eligibility conditions of the insurer in the same manner as it makes insurance available to residents of other jurisdictions of the State.

## Increase State Regulation

Rate-rollbacks have been suggested as a method for lowering premiums. A 1988 California-voter mandated 20 percent premium rate reduction has saved consumers approximately \$14.7 billion over the past eight years.<sup>110</sup> Other suggestions have been to increase funding for state insurance departments to hire additional investigators, auditors, and actuaries in order to determine appropriate insurance rates. In addition, increased disclosure of insurance industry data on premiums, investments, payouts, settlements, reserves, and other expenditures has been recommended for vigilant oversight of the insurance industry.<sup>111</sup>

## Eliminate Collateral Source Rule and Multiple Recoveries

It has been suggested that eliminating the collateral source rule, which prevents juries from hearing evidence that an injured party has received compensation from other sources such as health insurance or employer wage continuation programs, would decrease the third-party payments that are awarded to injured parties by the amount that has already been collected from another source.<sup>112</sup> A prohibition on multiple recoveries could also reduce non-economic damages as those amounts are usually based on the economic damages awarded. The Maryland Governor's Commission on Baltimore City Automobile Insurance Rate Reduction recommended in 1995 that personal injury protection benefits should only be paid if not otherwise covered by other sources and also that uninsured motorist benefits should be reduced by any compensation paid from collateral sources.<sup>113</sup>

## Limit Recovery of Non-Economic Damages

During the 1997 and 1998 sessions, the Maryland General Assembly considered legislation that would have limited the ability of an automobile owner who knowingly drove without the required insurance to sue an at-fault driver for non-economic damages, subject to certain exceptions. According to the California Insurance Commissioner, the voter-approved initiative in that state which bars uninsured motorists from collecting

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<sup>110</sup> Public Citizen, "The Road to Lower Insurance Premiums," using data from the National Association of Insurance Commissioners, [<http://citizen.org/congress/civjus/nofault/road.htm>].

<sup>111</sup> *Ibid.*

<sup>112</sup> Presentation by Jackson Williams (Defense Research Institute), "Defense Lawyers' Alternative Program for Reducing Auto Insurance Rates" and *The Final Report of the Governor's Commission on Baltimore City Automobile Insurance Rate Reduction*, p. 86.

<sup>113</sup> *Report of the Governor's Commission on Rate Reduction*, pp. 85-86.

pain and suffering damages has saved consumers \$250 million.<sup>114</sup> In addition, if uninsured motorist penalties increased and thereby caused a decrease in the number of uninsured motorists, then uninsured motorist coverage rates could decrease from the decrease in the number of uninsured motorist claims.

### **Require Attorney Contingency Fee Disclosure**

Defense attorneys argue that their bills are subject to audit while plaintiff attorneys usually charge one-third of the recovery amount. An argument is made that if disclosure was required for a plaintiff attorney to show how many hours were expended on a case, and a calculation was made on an hourly basis, consumers would become aware that fees may amount to hundreds of dollars per hour. This argument recognizes that insurance costs may not be directly affected by this disclosure.<sup>115</sup>

### **Repeal "Seat Belt" Gag Rule**

Under the "negligence per se" common law doctrine, juries should consider whether a plaintiff violated the law when considering if the plaintiff was negligent. Maryland, like most states, has created an exception to this rule for violating the seat belt law.<sup>116</sup> Under the seat belt gag rule, a plaintiff's failure to comply with a seat belt law cannot be used against the plaintiff when determining negligence even if the non-use contributed to the damages.<sup>117</sup>

### **Create "Medical Injury Profiles"**

The adoption of medical injury profiles or practice guidelines for non-serious injuries has been proposed for contesting the reasonableness or necessity of certain levels of medical care for an injured party.<sup>118</sup> These guidelines could address the issue of purported overutilization of medical services which both no-fault and tort proponents claim leads to elevated economic damages, either to increase non-economic damages under a tort system or to reach a threshold under a no-fault system.

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<sup>114</sup> J. C. Howard, "California Auto Profits in High Gear," *National Underwriter*, April 20, 1998.

<sup>115</sup> Williams, "Defense Lawyers' Alternative Program."

<sup>116</sup> Maryland law includes an exception to the "negligence per se" doctrine (see Section 22-412.3(h) of the Transportation Article).

<sup>117</sup> Williams, "Defense Lawyers' Alternative Program."

<sup>118</sup> Williams, "Defense Lawyers' Alternative Program."

## Limit Medical Reimbursements

The Maryland Governor's Commission on Rate Reduction recommended in 1995 that health care providers could not charge more for the treatment of soft-tissue injuries arising from automobile accidents than would be reimbursed by Medicare.<sup>119</sup> To deter incentives for over-utilization of medical services is the impetus behind this recommendation as well.

## Seek Federal Reforms

A number of other possible reforms can only be undertaken at the federal level. The McCarran-Ferguson Act gives the insurance industry an exemption from anti-trust laws. Proponents for the repeal of this exemption believe that the lack of competition in the insurance industry leads to higher premiums. Other requirements for decreasing deceptive insurance practices or requiring minimum standards for the disclosure of financial information from insurance carriers has been proposed as a method to standardize requirements across states and enable states to better hold companies accountable for premium increases.<sup>120</sup>

## Conclusion

This paper has reviewed a number of policy issues that should be considered when studying the possibility of altering an automobile insurance system. Under a no-fault system, premiums may decrease. But that decrease may occur only because policyholders will receive less benefits. Should non-economic damages be prohibited in non-serious cases, or should an injured party who experiences pain and suffering or mental anguish over the loss of a child be compensated? This is a philosophical question, not just a matter of lowered premiums.

From the evidence, it is not clear that litigation costs decrease under a no-fault system. Does the no-fault system encourage greater first-party suits because insurance companies will inherently deny any claim that they can? If an insurance carrier is prohibited from surcharging on claims that are not the fault of the policyholder, will a determination of negligence be required under no-fault system as well. Or will carriers pay claims and not increase premiums of any policyholder who makes the claim? This supports the argument that opponents to no-fault cite that no-fault will encourage reckless driving because risky drivers are not held responsible for their actions.

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<sup>119</sup> *Report of the Governor's Commission on Rate Reduction*, p. 88.

<sup>120</sup> Public Citizen, "The Road to Lower Insurance Premiums," [<http://citizen.org/congress/civjus/nofault/road.htm>].

The many reports that have studied driving behavior under the no-fault system are contradictory and inconclusive. The studies on fraud are similarly inconclusive. It appears that automobile insurance in general contains inherent incentives that encourage a tendency towards fraud and dishonesty, regardless of the type of insurance system. Policyholders see insurance companies as having "deep pockets." There is only faint recognition that fraudulent claims paid out by insurance carriers to only a few will cause premium increases for all policyholders.

There is no difference between the percentage of claimants who are able to recover benefits within three months after an accident in a no-fault system as compared to in a traditional tort system. After three month, the tort system pays more slowly. The question remains open whether access to faster benefits outweighs the possibility of inadequate benefits. This is another philosophical question that cannot be determined by studies and numbers.

Even some proponents of no-fault recognize that conclusive evidence of no-fault system's benefits is still missing. Consumer Reports concludes that "[t]he validity of O'Connell's theory, however, has yet to be proven over time."<sup>121</sup> The Governor's Commission studied many alternatives to reduce automobile rates in Baltimore City. Its 1995 report states that "data relating to actual premium reductions for no-fault laws that have passed are inconclusive."<sup>122</sup>

While it may be true that actuarially based conclusions show decreased benefits which could lead to lower premiums, the numbers from other states don't support that conclusion. It is possible that making a comparison between the potential outcomes under a proposed piece of legislation and similar systems in other states is not adequate. However, showing positive illustrative results based solely on decreased benefits does not take into account many other possible tangential effects, including higher litigation costs, higher accident rates, or higher insurance carrier profits. As evidenced by the review of a multitude of studies, conclusive evidence is difficult to attain. In addition, a number of philosophical questions remain that cannot be answered on a purely empirical basis.

In conclusion, before undergoing a massive effort to replace the current system, with all of its known inadequacies, with another system that is based on theoretical benefits, it may be preferable to try other remedies that address specific shortcomings in the current system.

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<sup>121</sup> Tobie Stanger and Bill Hartford, *Auto Insurance Handbook* (Yonkers, NY: Consumer Reports Books, 1993), p. 79.

<sup>122</sup> *Report of the Governor's Commission on Rate Reduction*, p. 56.



Appendix 1  
**Private Passenger Automobile Insurance  
 State Liability Premium Trends  
 1992-96**

State	1996		1995		1994		1993		1992		1995-96		1992-96	
	Average Premium	Rank	Average Premium	Rank	Average Premium	Rank	Average Premium	Rank	Average Premium	Rank	Percent Change	Rank	Percent Change	Rank
Alabama	\$313.60	40	\$296.24	40	\$279.11	43	\$263.31	43	\$252.82	42	5.86%	5	24.04%	11
Alaska	464.97	17	452.17	18	452.40	17	443.38	18	424.46	16	2.83%	27	9.54%	36
Arizona	514.67	11	489.87	14	506.79	11	492.53	13	468.79	13	5.06%	9	7.79%	34
Arkansas	331.12	38	297.98	39	299.38	37	266.44	42	246.90	43	11.12%	1	34.11%	3
California <sup>1</sup>	512.27	12	508.62	11	502.39	12	512.44	10	510.71	8	0.72%	34	0.30%	46
Colorado	481.50	15	472.89	16	475.52	15	458.62	15	422.27	17	1.82%	32	14.03%	24
Connecticut	605.23	5	603.11	6	600.93	5	665.25	2	614.73	3	0.35%	40	-1.55%	47
Delaware	568.57	8	564.70	7	556.34	7	530.28	7	529.13	6	0.68%	36	7.45%	39
District of Columbia <sup>2</sup>	576.46	7	548.41	8	545.84	8	518.07	9	517.80	7	5.11%	8	11.33%	32
Florida	512.23	13	490.50	12	440.73	19	500.25	11	486.72	11	4.43%	16	5.24%	42
Georgia	332.55	37	315.98	37	309.34	36	305.12	33	299.15	32	5.25%	7	11.17%	33
Hawaii	726.32	2	736.78	1	740.97	1	743.74	1	752.72	1	-1.42%	49	-3.51%	50
Idaho	284.36	44	273.32	45	271.23	45	260.69	44	242.89	44	4.04%	18	17.07%	22
Illinois <sup>3</sup>	363.09	28	353.51	28	336.27	30	318.44	30	295.55	33	2.71%	29	22.85%	14
Indiana	335.41	34	337.47	33	324.43	32	300.02	37	299.33	31	-0.61%	46	12.05%	27
Iowa	255.55	49	247.98	49	241.43	48	225.46	47	212.04	46	3.05%	23	20.52%	19
Kansas	271.31	46	261.68	46	252.96	46	231.11	46	211.85	47	3.68%	20	28.07%	7
Kentucky	381.18	25	364.11	27	345.25	29	330.98	28	307.98	28	4.69%	13	23.77%	12
Louisiana	543.35	10	547.55	9	535.88	9	525.76	8	495.39	10	-0.77%	47	9.68%	35
Maine	286.04	43	289.23	43	291.49	40	291.91	38	283.00	37	-1.10%	48	1.07%	45
Maryland	478.22	16	476.06	15	478.89	14	484.06	14	471.90	12	0.46%	39	1.34%	44
Massachusetts <sup>4</sup>	588.22	6	639.87	3	720.96	2	657.35	3	602.61	4	-8.07%	51	-2.39%	48
Michigan	348.49	32	343.22	32	358.44	26	375.93	25	359.43	23	1.53%	33	-3.05%	49
Minnesota	437.10	20	426.33	20	421.65	20	394.10	21	367.99	21	2.53%	30	18.78%	21
Mississippi	333.12	36	322.17	36	314.76	34	309.27	31	295.02	34	3.40%	22	12.92%	26
Missouri	355.99	30	345.50	31	331.91	31	307.05	32	286.96	36	3.03%	24	24.05%	10
Montana	275.93	45	273.97	44	272.03	44	250.46	45	227.85	45	0.72%	35	21.10%	18
Nebraska	262.03	47	250.58	48	243.88	47	224.46	48	195.37	48	4.57%	15	34.12%	2
Nevada	555.60	9	530.51	10	514.62	10	495.96	12	452.71	14	4.73%	11	22.73%	15
New Hampshire	371.09	26	371.97	25	379.37	25	398.88	20	390.53	20	-0.24%	43	-4.98%	51
New Jersey <sup>5</sup>	726.86	1	662.04	2	639.52	3	650.86	4	649.60	2	9.79%	2	11.89%	30
New Mexico	420.68	22	408.56	22	405.61	21	376.14	24	343.21	26	2.97%	26	22.57%	16
New York <sup>6</sup>	654.73	3	607.44	5	578.22	6	544.58	6	507.39	9	7.79%	3	29.04%	6

Appendix 1 (continued)  
**Private Passenger Automobile Insurance**  
**State Liability Premium Trends**  
**1992-96**

State	1996		1995		1994		1993		1992		1995-96		1992-96		
	Average Premium	Rank	Average Premium	Rank	Average Premium	Rank	Average Premium	Rank	Average Premium	Rank	Percent Change	Rank	Percent Change	Rank	
North Carolina	350.75	31	348.38	30	310.88	35	305.01	34	300.59	30	0.68%	37	16.69%	23	
North Dakota	214.13	51	204.49	51	198.40	51	188.00	51	170.87	51	4.72%	12	25.32%	9	
Ohio	341.11	33	327.21	34	317.89	33	302.14	35	304.46	29	4.25%	17	12.04%	28	
Oklahoma	333.72	35	324.91	35	298.69	38	280.46	39	262.89	39	2.71%	28	26.94%	8	
Oregon	382.37	24	373.27	24	380.91	24	383.88	23	358.85	24	2.44%	31	6.55%	41	
Pennsylvania	443.57	19	444.29	19	447.02	18	433.93	19	433.06	15	-0.16%	42	2.43%	43	
Rhode Island	615.83	4	619.18	4	611.59	4	605.83	5	550.24	5	-0.54%	45	11.92%	29	
South Carolina	396.06	23	395.84	23	401.83	22	390.99	22	364.75	22	0.06%	41	8.58%	37	
South Dakota	261.01	48	251.11	47	231.17	49	206.28	50	183.64	49	3.94%	19	42.13%	1	
Tennessee	313.01	41	293.65	41	287.67	41	273.84	41	257.95	41	6.59%	4	21.35%	17	
Texas <sup>7</sup>	504.88	14	490.31	13	494.95	13	448.36	16	420.48	18	2.97%	25	20.07%	20	
Utah	370.31	27	351.73	29	346.98	27	325.53	29	282.20	38	5.28%	6	31.22%	5	
Vermont	292.10	42	293.27	42	284.33	42	276.41	40	261.92	40	-0.40%	44	11.52%	31	
Virginia	358.32	29	371.57	26	346.86	28	343.63	27	335.25	27	-3.57%	50	6.88%	40	
Washington	455.97	18	453.01	17	459.92	16	446.19	17	400.03	19	0.65%	38	13.98%	25	
West Virginia	433.37	21	412.87	21	399.62	23	365.28	26	352.38	25	4.96%	10	22.98%	13	
Wisconsin	315.65	39	301.57	38	297.03	39	300.49	36	292.00	35	4.67%	14	8.10%	38	
Wyoming	238.90	50	230.56	50	223.10	50	207.17	49	180.27	50	3.62%	21	32.52%	4	
Countrywide	\$430.66		\$428.01		\$420.07		\$410.34		\$394.34		0.62%			9.21%	

- 1 The 1996 data for California has not been confirmed. (See Technical Notes for further explanation.)
- 2 Because the District of Columbia is entirely urban it may not be directly comparable to states with rural areas.
- 3 Contact the Illinois Department of Insurance to obtain more geographic specific information.
- 4 Data incorporates Safe Driver Plan credits and surcharges. (See Technical Notes for further explanation.)
- 5 See Technical Notes for further explanation.
- 6 Effective January 1, 1996, New York raised its minimum liability limits from 10,000/20,000/5,000 to 25,000/50,000/10,000.
- 7 Historical data reporting anomalies limit the comparability of Texas results with results from other states. (See Technical Notes for further explanation.)

AVERAGE PREMIUM = (Written Premium/Written Car-Years)

Sources: AAIS, ISO, NAIJ, NISS, Massachusetts Commonwealth Automobile Reinsurers, South Carolina Department of Insurance, Texas Department of Insurance, California Department of Insurance, and NAIC.

Appendix 1 (continued)  
**Private Passenger Automobile Insurance  
 State Average Expenditure Trends  
 1992-96**

State	1996		1995		1994		1993		1992		1995-96		1992-96	
	Average Expenditure	Rank	Average Expenditure	Rank	Average Expenditure	Rank	Average Expenditure	Rank	Average Expenditure	Rank	Percent Change	Rank	Percent Change	Rank
Alabama	\$577.86	33	\$549.10	33	\$524.03	34	\$513.04	32	\$497.58	32	5.2%	12	16.1%	22
Alaska	750.91	16	729.50	14	719.51	14	711.75	12	685.44	12	2.9%	36	9.6%	36
Arizona	785.05	12	727.11	15	730.97	12	700.00	14	667.41	15	8.0%	4	17.6%	18
Arkansas	557.70	34	499.87	42	507.48	37	445.42	42	424.29	43	11.6%	1	31.4%	3
California <sup>1</sup>	790.70	11	793.55	8	791.24	8	797.41	8	786.78	8	-0.4%	47	0.5%	47
Colorado	751.25	15	721.93	16	721.29	13	697.70	16	652.96	17	4.1%	24	15.1%	26
Connecticut	899.27	5	880.53	6	862.99	6	925.00	3	878.31	4	2.1%	41	2.4%	46
Delaware	806.05	8	783.74	10	776.00	9	738.47	10	744.61	9	2.8%	37	8.3%	40
District of Columbia <sup>2</sup>	993.07	2	958.58	3	923.88	4	878.62	5	880.03	3	3.6%	30	12.8%	30
Florida	783.23	13	739.49	12	655.52	19	698.24	15	683.98	13	5.9%	8	14.5%	28
Georgia	627.47	25	596.70	26	563.91	28	536.37	29	514.47	29	5.2%	13	22.0%	9
Hawaii	958.69	4	963.08	2	961.59	2	953.08	2	974.39	1	-0.5%	49	-1.6%	49
Idaho	464.59	47	446.81	47	445.11	46	429.24	45	402.03	44	4.0%	25	15.6%	24
Illinois <sup>3</sup>	637.98	24	612.27	24	586.70	25	572.36	25	533.94	27	4.2%	21	19.5%	16
Indiana	548.06	38	542.35	35	528.98	32	494.24	37	497.00	33	1.1%	43	10.3%	34
Iowa	445.39	50	428.66	49	421.85	48	396.98	49	379.17	47	3.9%	26	17.5%	19
Kansas	495.26	43	473.77	43	459.00	45	421.83	46	391.74	46	4.5%	18	26.4%	4
Kentucky	581.05	31	555.42	31	525.93	33	506.47	34	473.35	38	4.6%	17	22.8%	8
Louisiana	802.17	10	788.20	9	767.35	10	752.14	9	723.76	10	1.8%	42	10.8%	33
Maine	470.18	46	472.05	44	471.38	42	477.13	40	467.95	39	-0.4%	48	0.5%	48
Maryland	759.44	14	732.10	13	712.01	16	707.33	13	701.83	11	3.7%	28	8.2%	41
Massachusetts <sup>4</sup>	832.83	7	898.21	5	937.92	3	908.97	4	859.56	5	-7.3%	51	-3.1%	50
Michigan	697.38	18	645.49	21	665.27	17	677.12	17	662.46	16	8.0%	3	5.3%	44
Minnesota	653.98	23	628.07	23	619.90	22	595.27	22	566.08	22	4.1%	23	15.5%	25
Mississippi	604.17	27	579.29	28	556.85	29	541.39	28	518.51	28	4.3%	20	16.5%	20
Missouri	599.35	29	572.54	29	549.17	30	517.28	30	493.23	34	4.7%	16	21.5%	12
Montana	478.96	44	467.96	45	460.17	44	431.67	44	393.33	45	2.4%	39	21.8%	10
Nebraska	475.13	45	451.85	46	435.53	47	403.19	47	352.04	49	5.2%	14	35.0%	1
Nevada	802.50	9	758.82	11	748.03	11	726.11	11	672.54	14	5.8%	9	19.3%	17
New Hampshire	612.44	26	609.14	25	617.06	24	648.62	19	638.46	20	0.5%	44	-4.1%	51
New Jersey <sup>5</sup>	1,099.07	1	1,013.47	1	963.73	1	960.69	1	957.06	2	8.4%	2	14.8%	27
New Mexico	659.80	22	639.11	22	628.47	21	588.53	23	543.15	24	3.2%	34	21.5%	13
New York <sup>6</sup>	959.83	3	905.91	4	870.01	5	832.26	7	798.62	7	6.0%	7	20.2%	15

Appendix 1 (continued)  
**Private Passenger Automobile Insurance**  
**State Average Expenditure Trends**  
**1992-96**

State	1996		1995		1994		1993		1992		1995-96		1992-96	
	Average Expenditure	Rank	Average Expenditure	Rank	Average Expenditure	Rank	Average Expenditure	Rank	Average Expenditure	Rank	Percent Change	Rank	Percent Change	Rank
North Carolina	518.28	41	500.50	41	461.63	43	440.38	43	448.08	42	3.6%	32	15.7%	23
North Dakota	401.55	51	380.56	51	367.99	51	349.04	51	319.24	51	5.5%	11	25.8%	5
Ohio	553.27	36	531.13	36	516.97	35	493.15	38	503.22	31	4.2%	22	9.9%	35
Oklahoma	545.42	39	526.17	37	502.75	39	469.62	41	448.10	41	3.7%	29	21.7%	11
Oregon	584.76	30	564.69	30	565.84	27	564.07	27	534.71	25	3.6%	31	9.4%	37
Pennsylvania	687.43	19	667.23	18	657.12	18	645.10	20	641.76	19	3.0%	35	7.1%	42
Rhode Island	869.50	6	869.80	7	860.87	7	871.14	6	837.45	6	0.0%	46	3.8%	45
South Carolina	601.97	28	582.26	27	582.40	26	569.04	26	534.45	26	3.4%	33	12.6%	31
South Dakota	448.33	49	428.15	50	396.41	50	364.48	50	333.09	50	4.7%	15	34.6%	2
Tennessee	556.90	35	519.48	38	500.33	40	487.89	39	478.24	37	7.2%	5	16.4%	21
Texas <sup>7</sup>	726.05	17	710.52	17	714.17	15	665.88	18	645.95	18	2.2%	40	12.4%	32
Utah	580.72	32	547.49	34	539.72	31	515.36	31	463.08	40	6.1%	6	25.4%	6
Vermont	514.17	42	511.76	39	503.08	38	501.04	36	484.13	36	0.5%	45	6.2%	43
Virginia	549.67	37	552.91	32	514.50	36	508.08	33	503.28	30	-0.6%	50	9.2%	38
Washington	665.88	21	649.55	19	654.15	20	641.41	21	587.60	21	2.5%	38	13.3%	29
West Virginia	671.25	20	646.14	20	619.04	23	581.36	24	557.44	23	3.9%	27	20.4%	14
Wisconsin	533.49	40	505.56	40	496.46	41	503.24	35	491.53	35	5.5%	10	8.5%	39
Wyoming	451.62	48	432.89	48	421.67	49	401.00	48	366.25	48	4.3%	19	23.3%	7
Countrywide	\$685.11		\$667.47		\$650.64		\$635.09		\$617.65		2.6%		10.9%	

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- 4 Data incorporates Safe Driver Plan credits and surcharges. (See Technical Notes for further explanation.)
- 5 See Technical Notes for further explanation.
- 6 Effective January 1, 1996, New York raised its minimum liability limits from 10,000/20,000/5,000 to 25,000/50,000/10,000.
- 7 Historical data reporting anomalies limit the comparability of Texas results with results from other states. (See Technical Notes for further explanation.)

AVERAGE EXPENDITURE = (Total Written Premiums/Liability Car-Years)

Sources: AAIS, ISO, NAII, NISS, Massachusetts Commonwealth Automobile Reinsurers, South Carolina Department of Insurance, Texas Department of Insurance, California Department of Insurance, and NAIC.

Analysis of Maryland  
House Bill 341  
Estimated Loss Change for Voluntary Private Passenger Insured Vehicles  
BI, PD, UM/UM Liability, PIP All Limits  
Comprehensive and Collision With \$25,000 BPC

Coverages	Present System (1)			Under No-Fault	
	Claim Counts	Claim Severity incl ALAE	Total Cost	Estimated Loss \$ Change	Estimated % Change
BI (Serious)	13,210	\$12,144	\$160,422,000	(\$145,420,000) (2)	
BI (Non-Serious)	29,360	2,255	242,367,000		
BI (Out of State)	6,450	9,488	61,198,000	(20,562,000) (3)	
BI (Residual)	516	9,488	4,896,000		
BI (Alcohol and Drugs)	2,064	9,962	20,562,000	(112,781,000) (4)	
BI Basic Economic Loss Savings Savings on remaining BI medical losses					
Total BI	51,600	9,488	489,445,000	(278,763,000)	-57.0%
PD	155,100	2,178	337,808,000	0	0.0%
UM/UM (Serious)	1,377	12,197	16,795,000	(15,436,000) (2)	
UM/UM (Non-Serious)	3,086	2,338	25,727,000		
UM/UM (Out of State)	638	9,529	6,075,000	(11,906,000) (4)	
UM/UM Basic Economic Loss Savings Savings on remaining UM/UM medical losses					
Total UM/UM	5,100	9,529	48,597,000	(27,342,000)	-56.3%
Personal Injury Protection	64,800	2,216	143,597,000	(143,597,000)	-100.0%
Basic Personal Compensation	64,800	3,063	NA	198,482,000	New
Comprehensive	228,825	812	185,806,000	0	0.0%
Collision	184,170	2,219	408,673,000	0	0.0%
Total All Coverages Combined			\$1,613,926,000	(\$251,220,000)	-15.6%

Estimated Premium Change for Voluntary Private Passenger Insured Vehicles

Total All Coverages Premium Change (\$296,742,000) (5) -14.3%

Notes:

- (1) Claim counts and dollar amounts assume 3 million voluntary insured private passenger vehicles. (See Exhibit II)
- (2) Act eliminates right to recover non-economic losses for non-serious injuries. Estimated savings for this provision is 60% of the non-serious BI losses which is based upon 1992 IRC BI data for Maryland.
- (3) Act provides that accidents caused by drivers convicted of driving under the influence of alcohol or illegal drugs or of a felony are not insurable or recoverable under a liability policy.
- (4) Act eliminates right to recover basic economic losses under tort. Estimated savings is the basic economic losses which are estimated to be 28% of the serious and non-serious BI losses based upon review of Maryland IRC BI loss data. As provided by the Act, uninsured motorist cannot recover damages which would otherwise be covered by the basic personal compensation coverage.
- (5) Estimated all coverages loss reduction converted to premium savings recognizing fixed expenses.