

PRIVATE MOTOR INSURANCE MARKET INVESTIGATION

Summary of response hearing with Accident Exchange held on 4 March 2014

1. Accident Exchange said that the credit hire industry had evolved over the last 30 years, and the customer's needs were at the centre of this evolution. The courts, the regulatory system, the insurers and the credit hire sector had ensured that the consumer was never entitled to claim for more than they were legitimately entitled to claim, whether that was in terms of the type of vehicle received, the period for which it was hired, the rate charged, or the services that were provided by anybody else in ensuring they received their legal entitlement. Balanced against that position, the insurer was never obliged to pay any more than that, and had every opportunity to use the legal system to provide a challenge to determine whether or not the claim that was being made was greater than it ought to be.
2. Accident Exchange reaffirmed that it had a number of concerns regarding the Competition Commission's (CC's) assessment of adverse effect on competition (AEC), and presented four high-level issues regarding the AEC.
3. First, the CC's benchmark against which the status quo was being assessed was an idealised frictionless world in which direct hire was provided despite the fact that, absent credit hire, insurers did not have any incentive to provide direct hire. The status quo, which was a mixture of credit hire and direct hire, had been compared with this idealised world, in which everything was provided at direct hire rates and no frictional costs were incurred, either by credit hire companies or by consumers themselves. Such an idealised benchmark for assessing the competitiveness of the status quo led to a danger that the status quo would look like there was an AEC relative to that benchmark. This would lead to the CC looking for a remedy to solve the apparent 'problem'; a problem which appeared as a result of the idealised benchmark by which the status quo was compared. It was also likely to be the case that any of the remedies being considered would, if they were the status quo, look like an AEC relative to the idealised benchmark used by the CC. Adopting such an idealised benchmark pushed the CC into a position of looking for a remedy, even though the remedy worlds might not be any better. These were very important considerations that the CC should take into account in the AEC assessment and in its analysis of the proportionality of remedies.

4. Furthermore, attractive features of the status quo had been not been recognised by using an idealised benchmark by which to assess the status quo. These attractive features of the status quo included: (a) the consumer did not need to spend much time and/or cost extracting their legal entitlement as they could effectively outsource this to credit hire companies; and (b) at-fault insurers' incentives to provide direct hire existed because they were pre-empting and intervening before credit hire happened. In the CC's idealised benchmark these features had disappeared and not been considered. This was particularly important in relation to the benchmark by which remedies were assessed to avoid an asymmetric treatment of the status quo compared with remedies assessment.
5. Second, while the CC said that it took consumers' legal entitlement as given, this was not reflected in the approach that the CC adopted. Essentially the CC was assuming that the quality of service differential under direct hire compared with credit hire was small enough not to be recognised. This was not correct as (a) in a number of respects direct hire quality of service was less good than credit hire; (b) the judgement about whether the difference was material should be a quantitative rather than a qualitative judgment; and (c) there were distributional issues given that even if quality of service differentials were small (which Accident Exchange disagreed with) on average, they may still be very large for the people who were more likely to be the victim of an accident.
6. Third, Accident Exchange believed that the quantification of the AEC was inadequate and had a large number of flaws including the following: (a) the sample size on which direct hire rates were based was incredibly small; (b) the implicit assumption that direct hire rates would be the same in the absence of credit hire did not hold; (c) there were a large number of costs omitted from the calculations; and (d) there were a large number of benefits or quality of service differentials also omitted from the calculations. Accident Exchange's view was that all of these factors were amenable to quantitative analysis, and the CC should quantify all of them as precisely as possible.
7. Fourth, there was a decomposition issue, namely that the difference between credit hire costs and direct hire costs (as identified by the CC as the alleged detriment arising from credit hire) could be (and should have been) decomposed into two constituent differences: the difference between direct hire and GTA, and the difference between the GTA and credit hire. It was important for the CC to perform this decomposition exercise for two reasons. First, it would test the robustness or otherwise of the overall difference that had been identified. Secondly, it was hard to propose remedies, when all one had was the difference between credit hire and direct hire rates without knowing the locus of the problem, ie the extent to which that notional increase

in cost fell within the difference between GTA and credit hire or between direct hire and GTA. Accident Exchange noted that after the correction of the VAT issue, credit hire rates, which included VAT, and GTA rates when VAT was added on to them, came out at essentially the same, which suggested that the entirety of the delta identified by the CC between direct hire and credit hire was not sitting between GTA and credit hire, but was sitting between direct hire and GTA. This raised doubts about the robustness of the CC's analysis given that the CC had taken the view that the GTA was an efficient mechanism to settle claims and frictional costs were arising in relation to claims outside of the GTA.

8. Accident Exchange presented its concerns in relation to the CC's net detriment estimation (see third high-level point above) in more detail after discussing these four high-level points. Accident Exchange restated that the CC had calculated a net difference of £213 between credit hire and direct hire costs and then raised a number of specific concerns in relation to this calculation.
9. There were potential issues regarding the insurers' and brokers' costs and revenues cited in the provisional findings. The CC was told that it was not clear to Accident Exchange what credit hire companies' rates had gone into the calculation of credit hire costs, and it had a concern that if Enterprise was excluded, that could result in pushing up the credit hire cost calculations. Accident Exchange was also concerned that the direct hire rates that were being used were based only on three insurers' direct hire rates, accounting for 5 to 10% of the market, which was a tiny sample.
10. Another concern Accident Exchange had about the direct hire rates was that they did not reflect the full costs of direct hire (such as add-ons). The credit hire rates had lots of add-ons (tow bars, disabled vehicles, estate cars, automatic cars, extra driver, etc), which were part of the legal entitlement, so, essentially, the provision of add-ons was not being challenged, but the cost of those being provided was in the credit hire cost calculations and not in the direct hire cost calculations. Accident Exchange estimated that an adjustment to take into account the cost of these add-ons would amount to £26 which was more than 10% of the delta of £213.
11. Accident Exchange raised the issue of bracketing, ie that if direct hire providers and insurers agreed on bracketed rates (same rates for several different car categories), and direct hire providers were under a contractual obligation to provide the car within that bracket according to availability, then car hire companies would be expected generally to be providing cars towards the lower end of the bracket. This might be distorting direct hire rates and Accident Exchange noted that the materiality of it had been addressed by

Compass Lexecon as part of Accident Exchange's response to the Provisional Findings.

12. A further concern was that there might be a broader commercial relationship between the car hire company and the insurer which would result in direct hire rates being lower than they otherwise would be.
13. There was also an issue of payment timing, namely that insurers benefited from settling their credit hire invoices much later than their direct hire bills. Accident Exchange estimated that taking this difference in timing into account could lead to a £42 benefit to insurers under credit hire (which was about 20% of the delta of £213) which should be taken into account by the CC.
14. Accident Exchange suggested that the CC might want to explore whether, in some circumstances, the fault insurer who was procuring the direct hire services bore the risk of those vehicles. This was a cost that would be borne by insurers under a direct hire model and not under credit hire.
15. Accident Exchange also raised three 'dynamic issues' which the CC should take into account when assessing the AEC and remedies. First, there was evidence that the GTA had become more efficient which could lead to a cost saving in relation to credit hire of £27.27. Second, the rate of GTA settlements had been increasing over time, and therefore if the CC was assessing remedies on a prospective basis, it might be appropriate to build in some ongoing increase in the settlement rate within the GTA under the status quo. Third, the 2012 data credit hire companies submitted to the CC covered claims that were not settled at the time of the submission and therefore included some provisioning. Provisioning errors could lead the CC to under- or overestimate the difference between credit hire and direct hire.
16. On the issue of quality and service differences, Accident Exchange identified several factors, including that consumer frictional costs had been omitted entirely. Accident Exchange estimated that if it took non-fault drivers only one hour more to obtain a replacement car under direct hire than under credit hire that would cost £37 for those consumers. On quality of car, the CC's approach embedded an assumption that the basic grade of car and the duration was held constant across credit hire and direct hire, but Accident Exchange indicated that the quality of car went beyond just its grade. Collision damage waiver was an issue that was touched on in the provisional findings, but was not fully investigated. Accident Exchange noted that Quindell had provided some evidence indicating a cost of £15 for collision damage waiver. Uninsured loss recovery was a significant issue that was acknowledged in the provisional findings but not quantified. The presence of credit hire companies within the market meant that liability was resolved more often, whereas in a

world without them, insurers may find it in their interests not to resolve liability. Finally there were issues around collection and delivery.

17. Finally, Accident Exchange noted that the CC had sent out additional data requests and intended to do further analyses, which might require the CC to publish revised provisional findings. It also stated that if the CC was considering a remedy which was the variant of Remedy 1(A) as set out in the CC's Remedies Notice, it would need to consult on this variant before the provisional decision on remedies.