

REMARKS OF ROBERT MORGAN  
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I want to talk to you briefly about insurance rate making in North Carolina--what I believe from my experience as Attorney General after five years' of intervening in insurance rate cases is wrong with the system that we now have; and some of my feelings on how it can be improved.

Insurance is a business; a lot like most other businesses. A product is sold for profit. The profit enables the insurance companies to stay in business.

Following a 1945 Supreme Court case holding that the insurance industry, like other industries in this country, was subject to our antitrust laws, congress passed the McCarren Ferguson Act. That act exempted insurance companies from federal antitrust laws to the extent they were regulated under state law. Immediately following the passage of that act, there was a rush by insurance companies to establish state regulation in all states, including North Carolina.

I said a moment ago that insurance companies were like most other businesses. They are; but there are some important differences. Perhaps the most important is that the ultimate

product they sell, is deferred. The consumer does not immediately receive what he ultimately pays for and may never receive any tangible benefit because he may not sustain a loss. To make sure the company is still around when the loss is incurred, the public has an unusual interest in seeing that insurance companies stay solvent.

Let me give you an example. If a bread company goes out of business, that is of no particular concern to the public. Other companies will make and sell bread. But if an insurance company sells insurance at a price leading to eventual bankruptcy, the public is concerned.

Insurance is a necessity and one of the cornerstones of our modern economy. The North Carolina Supreme Court recognized as much in a 1971 fire insurance rate case. Without insurance, everything from the availability of home mortgages to the ability to drive your personal car on public roads of the state would be adversely affected. And insurance is worthless unless there is some guarantee that the insurer will be in business to pay a loss when it occurs. That is the basic rationale behind all government regulation of insurance companies--to provide some assurance that legitimate insurance companies will still be in business at the time of loss, and to prevent the unscrupulous from selling worthless policies and then vanishing.

That basic theory is sound and should be preserved in North Carolina. However, the present practice has departed considerably from the original theory with some unfortunate results.

Take as an example the regulatory scheme established in North Carolina for automobile liability insurance rates. There are some 294 companies licensed to write automobile liability insurance in this State. They vary tremendously in size. Some operate more efficiently; other less. With that many sellers, this would appear to be an ideal situation for the forces of competition to benefit the consumer. If competition were at work, more efficient operations should be reflected in lower prices.

But under present North Carolina law, there is absolutely no competition as to price among the 294 insurance companies for automobile liability insurance. North Carolina is among a minority of less than five states that absolutely sets all rates for automobile liability insurance.

Under North Carolina law, automobile liability insurance rates are determined by the Commissioner of Insurance. Under our law, all companies are to be treated as one company for rate making. The Commissioner of Insurance theoretically sets rates as though there were only <sup>one</sup> gigantic company servicing all North Carolina policies. This, of course, is a myth; and does not

square with reality. The mythical model set up under North Carolina law has produced some absurd results.

In order to cope with the model established in this State and similar models existing in other states, the insurance industry has come up with a number of formulas. The formulas are designed to set out what they believe their profits, losses, and expenses should be. Yet these figures do not represent the actual profits, losses, or expenses of any company. Because of this, consumers are deprived of price advantages they might otherwise realize from the most efficiently run companies.

I am not saying that price is the only criterion a consumer should use in choosing an insurance company. I am saying that it is one that should be available to him.

As most of you know, since I became Attorney General in 1969, our office has intervened in all automobile liability insurance rate hearings before the Commissioner and in the Courts. We have appeared in an adversary role with our lawyers and experts, opposing insurance lawyers and experts, so that the interest of the people would be at least represented. Because of our representation, the insurance consuming public has been saved tens of millions of dollars beyond that asked for in rate increases.

I am proud of this record because we did the best that could be done under existing law for the consumer. However, I do not believe that the existing framework is best either for consumers or the insurance industry.

You may know that, I have for some time favored open competition on insurance rates. I believe that the natural forces of the marketplace, when adequately supervised to assure solvency in insurance companies and to prevent collusion among them, would, in the long run, be healthier for the industry and produce lower prices for the consumer. I have talked to many people in the insurance industry and believe that you in the industry and the consuming public would welcome a system that puts a premium on free enterprise and efficient corporate operation.

A bill was introduced in the present session of the North Carolina Legislature to provide for rate competition among insurance companies. Despite the fact that I have long favored rate competition, I could not support this bill. The trouble with the bill was that it had no effective means of preventing collusion among insurance companies who should be competitors. In fact, the bill sanctioned collusion. Strong anticollusion measures are necessary if any law is to produce genuine competition among insurance companies.

At the outset of my remarks I said that I would offer some suggestions for improving the present system. Basically I

believe the system should be made competitive. It should be regulated to guarantee solvency and to prevent collusion.

To achieve these objectives the present North Carolina rating system for automobile liability insurance would have to be abolished. Companies would set their own rates. The companys' financial data on loss experience, expenses, and income would be submitted to the North Carolina Commissioner of Insurance who would monitor each company to insure financial solvency. This data, except for actual loss data would be held in strict confidence by the Commissioner of Insurance. The aggregate of loss data would be made public so that each company could more accurately determine the true nature of the risk of being insured.

Data for individual companies would not be made public nor would companies be permitted to exchange internal cost data. This is necessary because if competitors are permitted to know each others' internal financial details, collusion is a natural temptation, difficult to prevent, and almost impossible to prove. By close monitoring from the Commissioner's office and strong enforcement of traditional antitrust principles from either the Commissioner's office or from the Attorney General's office, I believe collusion could be prevented.

Another important, and in fact vital, role for the Commissioner would be to publish information as to the true cost and benefits

of policies offered. Competition requires that the consumer be informed, and this is especially important where the product is something as complex as an insurance policy.

There are some people who might charge that if the market in insurance were opened to competition, rates would rise to the highest possible level. If that is true, then the entire basis for the free enterprise system is faulty. Absent illegal price fixing, there is no reason to believe that the law of supply and demand will not work just as well in the insurance industry as it does in other areas of our economic system.

In conclusion let me give you one specific recent example of why I believe competition would be more effective than our present regulatory system.

As you may know, my office was recently successful in obtaining an interim reduction in insurance rates due to the energy crisis. The action was vigorously contested before Commissioner Ingram who ruled in favor of our position. We, of course, support Commissioner Ingram's Order and commend him for his prompt action in response to what we felt was a situation calling for an immediate reduction. Commissioner Ingram's Order was to become effective on March 26 of this year but was appealed by the industry to the North Carolina Court of Appeals. Thus, the Order has not yet become effective and while we, as an

adversary, will take every action to see that it is upheld as quickly as possible, there is no way to tell when it might be resolved.

Regulatory bodies must proceed upon evidence, findings of fact, and conclusions of law. Their mechanisms are thus somewhat cumbersome.

In contrast, let me point out that in December of last year, when the energy crisis in gasoline was first beginning to be felt, one of the country's five largest insurers took immediate action to effectively reduce rates. The company was not acting out of charity when it did this, but in its own self-interest in an effort to preserve its market and perhaps gather a larger share. The consumer was the ultimate beneficiary of their action. The company, unlike our office and the Commissioner of Insurance, did not have to wait for evidence to develop but rather made the reduction in the exercise in its own sound business judgment.

It is my position and belief that sound business judgment, open and honest competition, and regulated solvency, will ultimately be of greater benefit to both the public and the industry in North Carolina.

Thank you very much for your attention.