

"PAY AT THE PUMP" AUTO INSURANCE: THE VEHICLE INJURY PLAN (VIP) FOR
BETTER COMPENSATION, FAIRER FUNDING, AND GREATER SAFETY

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The Idea

This article summarizes the Vehicle Injury Plan (VIP). VIP would pay generous compensation to virtually everyone who suffers personal injuries in a motor vehicle accident, with the amount paid being unrelated to any assignment of fault. VIP would fund those benefits through a series of new charges related to driving—including about 30 cents per gallon of gasoline, leading some people to call VIP "Pay at the Pump." Because VIP would replace the current tort liability and insurance system for bodily injury, motorists would no longer buy insurance that now costs hundreds, and in some cases thousands, of dollars a year; as a result, for most motorists, the net cost of driving would be less than it is today. VIP would cover truck, bus, recreational vehicle, and motorcycle accidents, as well as auto accidents. Private insurers would be the primary administrators of VIP claims.¹

Money would be saved primarily from sharply reduced costs of claims

¹ VIP is an idea I have been developing over the past few years, simultaneously with Andrew Tobias, a Florida-based freelance writer who initially proposed the basic concept in his book *The Invisible Bankers* [1982] and who has focused his new book *Auto Insurance Alert!* [1993] on it. I present a more thorough discussion of VIP in my new book, *Pay at the Pump Auto Insurance* [Sugarman, 1993]. For other writings about the plan see Sugarman [1989, 1990a, 1990b, 1991, 1992].

administration, the curtailment of excess payments for "pain and suffering," fewer fraudulent claims, and better coordination with other compensation sources. Benefits would flow to more auto accident victims and would better replace out-of-pocket losses (especially for seriously injured auto accident victims who, today, find their injurer uninsured or inadequately insured more than half the time). The cost burden of the plan would be more equitably shared because the many scrofulaw motorists who now drive uninsured (at least 20 percent of drivers in California, for example) would have to contribute. Plan charges would be better targeted to promote safer cars and safer driving. These last two reasons make VIP preferable to a comprehensive auto no-fault plan of the traditional sort.

VIP in a Nutshell

The critical policy design issues for VIP are as follows: what happens to the current auto insurance regime, what new benefits will be paid, how they will be funded, and how VIP will be administered.

Eliminate Auto Insurance for Bodily Injury

Under VIP, people would no longer purchase motor vehicle insurance covering bodily injury. Most important, there would be no need for *liability* insurance for bodily injury—ordinarily the single most expensive item in the auto insurance policy—because motor vehicle accident victims could no longer sue their negligent injurers for money damages. Furthermore, since VIP would automatically provide motor vehicle accident victims with generous compensation, there would be no need either for *uninsured motorist* coverage for bodily injury or for motor vehicle accident *medical payments* coverage—two other significant types of protection now typically purchased by vehicle owners.

VIP Benefits

VIP would fund a generous compensation package, paying these benefits to motor vehicle accident victims on a no-fault basis:

1. Seventy percent of otherwise unreimbursed lost earnings, up to twice the average weekly wage from full-time employment (that is, up to approximately \$1000 a week or \$50,000 a year at present earning levels). For those who have no recent earnings experience, but whose injuries are long term and serious, income loss benefits would be calculated in terms of lost earning power, a provision aimed at children, students, homemakers, and the temporarily unemployed.
2. Otherwise unreimbursed and reasonably incurred medical expenses (and rehabilitation costs, where needed).
3. After a short waiting period, 80 percent of other reasonably incurred home expenses for up to a year of up to a stated maximum daily amount.
4. Moderate amounts for pain and suffering (based upon an award schedule) for those who either remain unable to return to their normal activities six months after the accident or who suffer a permanent and serious impairment or disfigurement. This threshold on recovery for pain and suffering is based on the successful experience with Michigan's similar

threshold in its auto no-fault plan. In adopting the award schedule, the VIP administering agency may draw, for example, on the successful experience with this approach under New Zealand's Accident Compensation plan, as well as Australian and British experience with scheduled pain and suffering awards in litigated cases.

VIP Funding

VIP would have three sources of income: The most important source, in terms of money raised, would be a surcharge on fuel consumption in the range of 30 cents per gallon. This would be collected at the pump by gasoline retailers and remitted to VIP, just as these dealers now remit fuel taxes to the appropriate taxing authorities. For this reason, VIP should be understood to be a specific version of those plans generally called "Pay at the Pump" (or sometimes "Pay as You Drive").

Additional charges would be imposed on drivers based upon their driving record and their experience. Good drivers age 20 and over would contribute at the rate of \$20 a year, payable when they renew their driver's licenses. Drivers with bad records, young drivers, and novice drivers would pay more, in some cases at least \$500 more.

Two types of charges would also be imposed on the owner of a vehicle. On the annual registration of an auto, the owner would pay a sum based upon the model's safety record. Cars of average safety would cost \$80 a year, safer cars \$40 a year, more dangerous cars up to \$200 a year. In addition, a one-time safety fee of \$250, payable to VIP, would be imposed on the purchase of a new car, against which various credits would be allowed if the car has certain safety features, such as air bags and antilock brakes. Both types of safety charges (the annual and one-time) would be posted on a car's "sticker" when sold out of the showroom or off the lot.

VIP Administration

VIP would be run by a new state body, perhaps housed within the Department of Insurance, or perhaps established independently. For claims processing, however, VIP would rely primarily upon the expertise of the existing insurance industry. Although a number of strategies for utilizing private enterprises are possible, the following scenario seems most promising:

Qualified claims administering companies (and their agents and brokers) could sign up as many "good drivers" as they wish and would be paid a capitation amount (that is, so many dollars) for every such person on their rolls. On the basis of the number of good drivers it signed up, the company would have to take its market share of "bad drivers" and would be awarded a capitation amount for each of them, too.

Out of the total of the capitation amounts it received, the company would have to pay the full VIP benefit to any person on its rolls who is injured in a motor vehicle accident. It could keep any extra money for administration, profit, and one additional thing: *Companies could offer cash rebates (out of the capitation amounts) to those who sign up with them.*

Motorists could sign up with any qualified claims administrator they wish, changing as often as once a year. Although existing auto insurers might well play key roles as claims administrators, other companies could also qualify

for the job. They might include health insurers, homeowner insurers, and possibly other enterprises as well, such as banks or large employers. Provision is also made for private claims administration of injuries to nondrivers.

Every time a claim was filed, the claimant would complete a claim satisfaction form that would be returned to the company and to the VIP board. Each year, a claims administrator would become entitled to a bonus capitation amount based upon two factors: its claimant satisfaction rating, and the proportion of those people on its rolls who choose to renew their affiliation for the next year.

A Few Numbers

Most of the analysis of VIP has been done for California where, as of this writing, the "Pay at the Pump" idea has gained the most attention.

About \$7.5 billion currently paid in annual auto insurance premiums would be eliminated were California to adopt VIP. Taking into account current figures and likely behavioral responses to the new plan, the three VIP funding sources are designed to raise that same \$7.5 billion among them: about \$4.5 billion from about 15 billion gallons of fuel at 30 cents a gallon; about \$1 billion from about 19 million licensed drivers; and about \$2 billion from charges on about 22 million motor vehicles.

A "typical" motorist would contribute just under \$300 a year to VIP—\$20 as a good driver, \$80 for a vehicle of average safety, and \$195 on 650 gallons of gasoline consumed by driving, for example, 13,000 miles at 20 miles per gallon. By driving a car that gets 30 miles to the gallon, this driver would save \$65 a year; a similar savings would be achieved by someone who drove about 9000 miles a year. In California today, by contrast, the typical motorist pays more than \$500 a year for the insurance coverage that VIP would eliminate. A 17-year-old with a good record, driving a 10-miles-to-the-gallon gas guzzler of average safety 8000 miles a year, would pay a total of about \$850 in VIP charges, reflecting the current pattern of higher insurance costs for riskier young motorists. The net cost to most motorists is anticipated to be even less than the numbers presented here because so many are expected to receive rebates from the claims administrator with whom they register.

The benefit plus claims administration costs of VIP are projected to be about 30 percent less than is now spent on benefits plus administration of personal injury claims. This is another way to show the plan's savings and a clear source of cost reduction (and rebates) to the typical motorist, who saves additionally because currently uninsured motorists are brought into the scheme.

Turning now to the victim: Even though the overall cost of the plan is less than today, because administrative costs (which run around 50 percent at present) are expected to be so much lower under VIP, the typical victim should net out nearly as much as under the current scheme. Benefits will, moreover, be spread over more victims, since, unlike under today's fault-based scheme, virtually all victims will qualify. Also, benefits will be much more carefully focused on meeting actual out-of-pocket losses.

The way in which the VIP revenues are designed is expected to reduce gasoline consumption about 4 percent in the short run, and as much as 12 percent over time (as larger behavioral adjustments are made in lifestyle and motorists shift to more fuel-efficient vehicles).

Solving Problems with the Existing Scheme

Very briefly, VIP is designed to help solve many different problems with the current regime: that auto insurance costs too much; that there are too many uninsured drivers; that too many seriously injured victims are vastly under-compensated; that too much of the auto premium dollar is lost to fraud (sometimes said to plague up to 20 percent of bodily injury claims), duplicates other sources of compensation, is wasted on claims administration, and is concentrated on pain and suffering awards; that bodily injury claims are subject to too many delays and the process is unsatisfying to too many claimants; and that safer driving of safer vehicles is insufficiently encouraged.²

Of course, some people would pay more under VIP, most significantly those who now go without insurance. If VIP's charges were thought unfairly to price poor people off the road, their driving could, if necessary, be subsidized. By combining VIP's risk-sensitive charge system with the ability of claims administrators to compete for business through cash rebates, the plan's funding should be at least as risk-based as is the current scheme. Moreover, it moves away from the gender-based and territorial-rating features of traditional auto insurance that are generally disliked by the public.

Obviously, lawyers who now profit from auto accident cases would lose under VIP, as would their clients, who are now able to obtain large recoveries for pain and suffering (especially when they are either "lucky" enough to have been hit by a "deep pocket" defendant, or are little injured but happy to claim "whiplash"). Long-distance drivers (including perhaps truckers) may also oppose VIP, along with members of the "highway lobby" (including gasoline retailers, motel owners, fast-food sellers, and concrete makers) who have a tendency to reject any reform designed to reduce driving. The position of insurers and independent insurance agents is likely to depend upon their appraisal of how they will fare under VIP's claim administration arrangements.

Lessons from Policy Analysis

VIP tries to take advantage of several lessons from policy analysis concerning matters such as private incentive effects, marginal pricing, efficient public administration, and internalizing the cost of externalities. It remains to be seen whether VIP's design is well-calculated to create a viable political coalition on its behalf—including not only individual motorist and consumer organizations, but also groups concerned, for example, about the environment, an expanded role for public transport, and energy efficiency and independence.

A bill reflecting many but not all of VIP's features was introduced in January 1993 into the California legislature, where it won the support of both the Democratic Chair of California's Senate Insurance Committee and California's elected Commissioner of Insurance. But the measure was at least temporarily withdrawn when it became clear that supporters of the current lawsuit system (and traditional allies of the trial lawyers) in the legislature's Judiciary

² For example, motorists who purchase air bags now obtain no reduction in their liability insurance premiums because, by protecting the victim, they serve to reduce the liability of others. VIP, by contrast, would reward the purchase of such options.

Committees would block the bill. As of this writing, there are plans to try to put some kind of "Pay at the Pump" scheme to the California voters by way of the initiative process.

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