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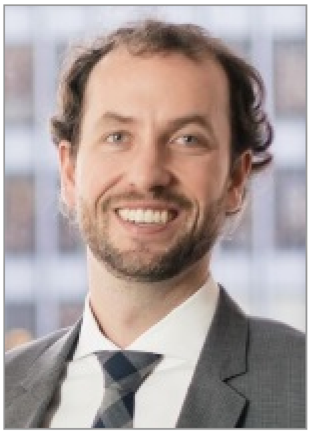
High Risk Versus Low Risk

Differentiation allowed to determine risk in insurance

By **Tom Macmillan**



Tom Macmillan

(October 9, 2019, 9:35 AM EDT) -- A CBC.ca story about a man who was denied life insurance, apparently as a result of a disclosed history of having generalized anxiety disorder, made national news this summer. It may come as a surprise to some that the *Ontario Human Rights Code* explicitly permits insurers to differentiate on the basis of age, sex, marital status, family status or disability when entering into a contract of automobile, life, accident or sickness, or disability insurance.

This exception is specifically set out in s. 22 of the Code, which allows for such differentiation so long as it is reasonable and based on bona fide grounds.

In its decision of *Zurich Insurance Co. v. Ontario (Human Rights Commission)* [1992] 2 S.C.R. 321, the Supreme Court of Canada addressed the issue of differentiation among insureds. In that case, a young male insured challenged the fact that the insurer, Zurich, charged higher insurance premiums for automobile policies insuring men under the age of 25.

In dismissing the appeal, the Supreme Court agreed with the Ontario Court of Appeal that the Code permits an insurer to discriminate based on age in this context.

In support of the reasonableness of Zurich's decision to differentiate based on age and sex, the court pointed to actuarial evidence that showed that single male drivers aged 25 or younger represented the highest claim frequency, highest loss per car insured and highest average claim cost of any category of driver.

The Supreme Court rejected the respondent's argument that there exists a reasonable alternative to the insurer's policy of charging increased premiums. It was argued that it would be simple for the insurer to have the category of young male drivers subsumed by the wider pool of insureds, so that the risk and premium burdens would be shared more equitably throughout the pool. The Supreme Court found that forcing other policyholders to subsidize the risk posed by young male drivers would be unfair.

This is significant, as it appears to challenge one of the foundations of the concept of insurance itself: that being the sharing of risk and costs across a group. The question of how far we are prepared to go in sharing risk is of paramount importance when considering whether, for example, we wish to set up a system of insurance that prevents differentiation on the basis of a pre-existing diagnosis for generalized anxiety disorder, and whether we are ready and willing to share more widely the risk and premium burden of that group.

While the Supreme Court rejected the argument that the insurance risk posed by young male drivers should be shared more broadly than was the industry standard at the time, the idea of shared risk remains the fundamental underpinning of the concept of all insurance.

Life insurers are permitted to differentiate between individuals on the basis of perceived risk. The issue, of course, is how much differentiation we wish to tolerate as a society, as the more widely and aggressively such differentiation is employed, the closer we get on the spectrum to the model where risk is no longer being shared by the group but is instead borne by each individual.

As radical as it may seem, it is worth asking why it is that any differentiation at all should be tolerated. If insurance is the spreading of risk across policyholders, is it not truer to the form of insurance that everyone (or almost everyone) be covered, with the risks and premiums being shared evenly? Would the costs of such a model not be outweighed by the benefit of ensuring that there is appropriate coverage for all potential personal disasters?

The answer may lie in the extent to which self-interested individuals are prepared to buy into a system of equally shared risk. Most people do not give much thought to the extent to which they may be subsidizing other individuals who may be higher risk, but when they do it may be accompanied by a sense of unfairness on the part of low-risk individuals who feel that they disproportionately contribute.

Without some amount of differentiation to quell grumbling on the part of low-risk contributors, then when premiums are too high there could be a risk of widespread opting out. If a sense of excessive unfairness starts creeping into the system, there is a risk of it crumbling.

Thus is exposed the fragility of a system of insurance that relies on optional participation. While contributors to the insurance pool are prepared to abide by some level of disproportionate payment (because who knows if or when one is visited by misfortune), there is a point at which individuals want some reassurance that they are paying less than higher-risk individuals.

With respect to differentiation on the basis of mental health, an optimistic view is that the industry will change as we learn more about the associated risks. Our understanding of these issues is still very much in its infancy; with further time and study we will gain a more complex and nuanced understanding of the magnitude and nature of the risks involved.

It is unlikely that there will be an overhaul of the system of differentiation to a more egalitarian model. The more likely outcome for the future of life insurance coverage is more precise differentiation by insurers on the wings of more understanding of mental health concerns.

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