



## ANALYSIS OF THE IMPACT OF BANNING AFTERMARKET PARTS

For more than 20 years, there has been much interest in crash parts that are used to repair damaged vehicles. These parts comprise the sheet metal or plastic components forming the vehicle's exterior, such as hoods, door and bumper panels, fenders, side moldings, etc. Specifically, the issue relates to the use of original equipment manufacturers' (OEM) parts versus aftermarket (also known as non-OEM or replacement) parts that are not supplied by the original auto manufacturers. Because aftermarket parts are much less expensive than OEM parts, these generic crash parts are often used by insurance companies in an effort to reduce repair costs. In this way, consumers benefit by receiving premium savings resulting from lower claim costs. Although some critics question the quality of non-OEM parts, studies have found that these parts serve no safety function and do not compromise the safety of a vehicle.<sup>1</sup>

This PCI analysis estimates the cost impact if the use of aftermarket parts is banned. In summary,

- prohibition of competitive replacement parts would result in an additional \$3.25 billion in insurance costs per year; and
- there would be a vehicle damage rate increase of about 6.7 percent more per insured car, or an overall auto insurance liability and physical damage premium increase of about 3.8 percent more per insured car. On average, this translates to an additional \$36 per insured car to the overall premium.

The above results were derived using various findings from other studies; they include the following:

- according to the Certified Automotive Parts Association (CAPA),<sup>2</sup> aftermarket parts represent 20 percent of the total cosmetic crash parts market;
- as a group, OEM parts are said to cost about 60 percent more than aftermarket parts,<sup>3</sup> and
- the cost of labor for sheet metal is estimated to be about 25 percent of total auto body work.<sup>4</sup>

Using industrywide data from the National Association of Insurance Commissioners (NAIC) and extrapolating loss experience from the Fast Track Monitoring System,<sup>5</sup> the following figures<sup>6</sup> reflecting the 12-month period ending 3<sup>rd</sup> quarter of 2008 are determined:

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<sup>1</sup> U.S. General Accounting (now Accountability) Office, "Motor Vehicle Safety: NHTSA's Ability to Detect and Recall Defective Replacement Crash Parts is Limited," January 2001; and Insurance Institute of Highway Safety, *Statement Before the Property-Casualty Insurance Committee of the National Conference of Insurance Legislators*, "Institute Research on Cosmetic Crash Parts," July 7, 2005

<sup>2</sup> "Fact Sheet: Generic Auto Crash Parts," [www.genericautoparts.net/fact\\_sheet.htm](http://www.genericautoparts.net/fact_sheet.htm)

<sup>3</sup> Alliance of American Insurers (now part of the PCI)

<sup>4</sup> PCI, based on data obtained from U.S. Department of Treasury "Market Segment Specialization Program: Auto Body and Repair Industry," August 1995, (p. 35), [www.irs.gov/pub/irs-mssp/autobody.pdf](http://www.irs.gov/pub/irs-mssp/autobody.pdf).

<sup>5</sup> NAIC *2005/2006 Auto Insurance Database Report* (2008). The Fast Track Monitoring System is produced by PCI and two other statistical agents; the countrywide data represent about 70 percent of the industry.

<sup>6</sup> These figures do not include Minnesota, since this state does not allow the use of aftermarket parts (source: PCI). The analysis, however, assumes that all companies use aftermarket parts.

- There are roughly 22.5 million claims reflecting collision, property damage liability, comprehensive (excluding theft), and uninsured/underinsured motorist (property damage) coverages. Of these claims, 4.5 million involve non-OEM parts and 18.0 million involve OEM parts.
- The current total vehicle damage loss dollars reflecting all crash parts are about \$53.41 billion. The cost of non-OEM parts and labor is estimated to be \$7.21 billion and the cost of OEM parts is estimated to be \$46.20 billion.

Using a 75%-25% distribution between parts and labor costs, about \$5.41 billion are spent on non-OEM parts. If the use of these components were banned, the total losses for parts would be increased by 60 percent, or about \$8.66 billion (\$5.41 billion x 1.60) reflecting former non-OEM parts. In other words, an extra \$3.25 billion (\$8.66 billion - \$5.41 billion) would be added to the total parts cost of insured vehicle damage.

The following table provides a breakdown of the number of claims and paid losses between OEM and non-OEM parts before and after any proposed restriction on the use of aftermarket parts.

<b>Estimated Impact of Banning Aftermarket (Non-OEM) Parts on Paid Losses for Crash Parts</b>					
	<b>(1) No. of Claims</b>	<b>(2) Current Paid Losses</b>	<b>(3) Impact on Banning Non-OEM (Increase Parts by 60%)</b>	<b>(3) OEM Paid Losses (After Ban)</b>	<b>(4) = (3) - (2) Difference Before and After Ban</b>
<b>Non-OEM</b>	<b>4.5 million</b>	<b>\$ 7.21 billion</b>			
Parts		\$ 5.41 billion	\$ 8.66 billion		
Labor		\$ 1.80 billion			
<b>OEM</b>	<b>18.0 million</b>	<b>\$ 46.20 billion</b>			
Parts		\$ 34.65 billion		\$ 43.31 billion	
Labor		\$ 11.55 billion		\$ 13.35 billion	
<b>Total</b>	<b>22.5 million</b>	<b>\$ 53.41 billion</b>		<b>\$ 56.66 billion</b>	<b>+\$ 3.25 billion</b>
<p><i>Notes: 1) Labor costs would not be impacted by the prohibition of aftermarket parts. The cost of parts would increase by 60 percent, or \$3.25 billion (\$8.66 billion - \$5.41 billion).</i></p> <p><i>2) The above figures exclude Minnesota, since this state already bans the use of non-OEM parts.</i></p> <p><i>Sources: Fast Track Monitoring System (year-end 3<sup>rd</sup> Qtr., 2008) and NAIC</i></p>					

Based on the loss costs (i.e., losses per insured vehicle)<sup>7</sup> of the various coverages affected by the use of non-OEM parts, it is estimated that the total insurance vehicle damage loss cost would increase by 6.7 percent if these parts were no longer allowed. Since the vehicle damage loss cost represents about 50 percent of the total loss cost (reflecting all liability and physical damage coverages), the total insured loss cost would increase by about 3.8 percent. In other words, consumers with liability and physical damage coverages would pay an additional 3.8 percent (or \$36) more per insured car if aftermarket parts were no longer allowed.<sup>8</sup>

*The Property Casualty Insurers Association of America (PCI) is a trade association consisting of more than 1,000 insurers of all sizes and types, and representing 40.1 percent of the property/casualty business and 52.9 percent of the personal auto market in the nation.*

<sup>7</sup> Loss costs are obtained from the NAIC and Fast Track Monitoring System.

<sup>8</sup> The average premium reflects 2006 from the NAIC 2005/2006 Auto Insurance Database Report (2008).