

Annual Report

For the Year Ending December 31, 2004.

Introduction

The Alberta Automobile Insurance Rate Board, constituted under subsection 653(1) of the *Insurance Amendment Act, 2004 (No. 2)*, is empowered under section 654 to carry out the powers and duties conferred on the Board under the *Insurance Act*, the *Automobile Insurance Premiums Regulation* and any other powers and duties assigned by the Minister.

The Automobile Insurance Rate Board replaced the Automobile Insurance Board on October 1, 2004. This annual report documents the activities of both Boards, as they were functional at different times during the period of January 1, 2004 to December 31, 2004. This report covers the period of January 1, 2004 to December 31, 2004.

The Alberta Automobile Insurance Rate Board

Board Members are drawn to represent various geographical regions of the province and for a range of expertise they bring to the organization.

Mr. Alfred H. Savage, Chair

Mr. Savage possesses over 30 years of private and public sector experience as a senior executive within some of the most progressive organizations in Canada and the United States. He has held senior positions in various municipalities in Alberta, Ontario such U.S. cities and New York and Chicago. Now retired, Mr. Savage devotes his time to board and community work. He was a Board Member and Chair of the Olds College from 1997-2003 and is currently an Officer for the Alberta Municipal Government Board. Additional community involvement has included volunteering for the 1987 Commonwealth Games and the 1998 World Student Games and serving as Director of the Calgary Downtown Rotary Club.

Mr. Harry Gough, Q.C.

Mr. Harry Gough, QC is a partner with Schumacher, Gough & Pederson in Drumheller and has been practicing law since 1974. Mr. Gough was a member of the Alberta Auto Insurance Board from 1997 – 2004. His community involvement includes member of the Criminal Law Practice Advisory Committee and member of the Custody and Mediation

Committee with the Alberta Law Society. Through his involvement with the former Alberta Auto Insurance Board, Mr. Gough has gained a strong knowledge of the various insurers across Alberta.

Mr. Lewis Klar, Q.C.

Prof. Klar is currently a Professor within the University of Alberta's Faculty of Law. He served as Dean of the Faculty from 1997 – 2002. His major teaching and research interests are in Tort Law and Insurance Law. Prof. Klar is a non-practicing member of the Alberta Law Society and was appointed Queens Counsel in 2002. He was recently elected to the American Law Institute, one of a very small number of Canadians who are members of this advisory body. He has also written advisory reports for the Alberta Law Reform Institute.

Ms. Patti Grier

Ms. Grier is the Executive Director, Office of the CEO and Government Relations for the Calgary Health Region. She was a Trustee and Vice Chair with the Calgary Board of Education from 1992-95 and served as Alderman, Ward 13 in the City of Calgary from 1995-2000. Ms. Grier has sat on a number of private, provincial and municipal boards and committees both through her professional work as well as through her personal commitment to the community.

Mr. Jack Halpin, FCA, Vice-Chair

Mr. Halpin is a Chartered Accountant working for Meyers Norris Penny, LLP in Calgary. His current board appointments include: ATB Financial, Alberta Cancer Board and Mancal Trust Company. He is a Committee Member of the Provincial Government Internal Audit Committee. Previously Mr. Halpin has been Chairman of the Calgary General Hospital Board, the Holy Cross Hospital Disposition, and the Finance Committee - Mayor of Calgary.

Mr. William Moore

Mr. Moore is a Fellow of both Canadian Institute of Actuaries and the Society of Actuaries. He is also a member of the American Academy of Actuaries. Prior to joining Towers Perrin, Bill practiced for 20 years as a consulting actuary to public and private sector pension plan sponsors in Western Canada. Prior to that time, Bill worked in the insurance industry in Canada and the United States. He continues to provide consulting services to clients in both the public and private sector, particularly assisting these clients with strategic management of their pension plans.

Ms. Merle Taylor, CMA, Consumer Representative

Ms. Merle Taylor is a partner in the consulting firm of Keefe Taylor & Associates. She has expertise in policy, operational and organizational reviews in the public and non-profit sectors. In addition to her work as a management consultant, Ms. Taylor has held several leadership positions with a range community and not-for-profit volunteer organizations.

Mr. David White

Mr. White has diverse experience in the insurance brokerage industry and was co-owner of a full services life, disability and group insurance company for 10 years. He has served on various boards and planned and facilitated policy workshops. He has a good financial management background and a facilitative style of leadership. Board experience includes, Lethbridge Youth Foundation, Lethbridge Family YMCA and the City of Lethbridge Standing Committee on Transportation, Utilities and the Environment.

Statement Of Purpose

The purpose of the Automobile Insurance Rate Board (the Board) is to regulate premiums for basic automobile insurance in Alberta and to monitor the rates of optional coverage for private passenger vehicles. The Board also approves the rating programs of new insurers, reviews and approves changes to an insurers rating plan at the request of the Superintendent of Insurance and accepts notices of revenue-neutral changes to rating variables within an insurers rating plan.

The Board is further mandated to fulfill the functions and responsibilities of the former Alberta Automobile Insurance Board in areas not addressed by amendments to the *Insurance Act* and the *Automobile Insurance Premiums Regulation*.

The Year In Review

The AIRB replaced the Alberta Automobile Insurance Board on October 1, 2004. The AIRB has not been functional for a full fiscal year for the period of this report. Moreover, the Freeze Order, implemented on October 30, 2003, effectively ceased the operations of the Board. Under the freeze, insurers were prohibited from modifying their rating plans for basic coverage for private passenger vehicles to increase their rates. They were also prohibited from increasing their rates for optional coverage. Rating plans for non-private

passenger vehicles were not affected by the Freeze Order, nor was the Board's ability to approve the rating plans of newly licensed insurers.

As well, it is important to note that this annual report does not deal with a cost accounting of the reform measures implemented in October 2004. The cost and effects of the reform will be included in the Board's 2005 annual report. If further information is sought on the costs and effects of the reform, please refer to Board Order No. 1-05: Annual Industry Wide Adjustment of Rates for Basic Coverage.

Rates

Insurers conducting business in Alberta are required by the *Insurance Act* to report their experience to a Canadian statistical plan. The results are compiled annually in Insurance Bureau of Canada published statistical exhibits that are then analyzed by the Board's actuarial consultant. The most recent available results are for 2003. Prior to the Freeze Order that came into effect on October 30, 2003, these analyses were used in weighted proportions with the insurers' own statistics and analyses performed by insurers' underwriting groups in considering proposals for rate changes.

A pattern of deteriorating results that emerged in the mid 1980s was sustained into the early 2000s, particularly for private passenger vehicles. The phenomenon was attributable to the growth in compensation for bodily injury claims under third party liability and, to some extent in more recent years, under accident benefits coverage. Premiums for third party liability and accident benefits rose steadily through the 1990s in response to rising claim costs, though competition tempered the process until 2001. Pricing for all categories of general insurance hardened in the latter part of 2001 and that course continued through 2002 until October 30, 2003 when rates were frozen.

Market

Until the Freeze Order, premiums for third party liability and accident benefits on Private Passenger vehicles continued to increase in response to claims experience. The escalation in premium abated somewhat during 1999 and 2000 but insurers strove for premium adequacy from the latter part of 2001 until the Government imposed rate freeze of October 30, 2003. Collision and comprehensive coverage have yielded satisfactory results since the mid 1990's. This in part offset adverse results for third party liability and accident benefits.

A very modest improvement in results for third party liability on private passenger emerged in 2001 and 2002. A continued and more apparent improvement was evident with the release of results for 2003.

Third party liability encompasses bodily injury and property damage. The area of concern for many years has been the persistent spiral in both average cost and frequency of bodily injury claims. After a steady spiral that peaked in 1998, frequency finally showed some modest declines since 1999 with the most significant change in 2003. There is uncertainty as to whether frequency will stabilize or continue to decline in the coming years. However, the frequency decline for 2003 does lend additional credibility to a positive outlook in which it will continue to go down.

It takes a number of years for third party liability bodily injury claims incurred in a given year to mature. Therefore, results for recent years are projected to their expected ultimate values based on historical observations of the maturation of such claims. Expectations are that over the five years ending in 2003, the average compensation for a bodily injury claim will have increased 36% while frequency of this type of claim will have decreased by 20%. The climb in settlement amounts and decline in frequency combines for a 7% increase in the claim cost per vehicle insured. In comparison, the average property damage claim will have increased by 43% while frequency of this type of claim will have actually fallen by 23%. For property damage, the claim cost per vehicle insured will have increased by 11%. Figures 1 and 2 (on page 7) track changes in average claim costs and frequency of claims for a longer period of ten years ending in 2003. Figure 3 (on page 8) displays loss costs per vehicle insured, which are total losses, divided by the number of vehicles insured. The figure relates the combined effect of average claim cost and frequency. Declining frequency has offset increasing average claim costs.

Over the past five years, the overall effect for third party liability coverage is a 39% growth in the average claim size while frequency will have declined 22%. The claim cost per vehicle insured will have increased by 8%. Bodily injury is expected to comprise 81% of total third party liability claim costs for 2003. Figure 4 (on page 8) shows the change in average claim costs and frequency of third party liability claims over a longer ten-year period.

Rising average claim costs has affected accident benefits in recent years. In the five years ending in 2003, the average claim cost will have increased by 40% while frequency of this type of claim decreased by 25%, having moderated slightly after peaking in 1998. The claim cost per vehicle insured will have risen 5%. Figure 5 (on page 9) shows the change in average claim costs and frequencies of claims over a longer ten-year period.

Compensation available under accident benefits coverage doubled for losses occurring as of October 1, 1995, contributing to increased average claim costs since 1996. Changes to accident benefits provisions effective October 1, 2004 are expected to increase average claim costs for future years. This increase is expected to be partially offset as the compensation is deducted from any third party liability claim.

Frequency for collision claims diminished for a number of years but has shown some fluctuation over the past five years. Frequency of comprehensive claims continues to diminish. Over the same five-year period, the average claim cost for collision will have increased by 41% while frequency will have decreased 19%. The claim cost per vehicle insured will have increased by 15%. The average claim cost for comprehensive will have increased by 71% while frequency will have dropped 43%. The claim cost per vehicle insured will have decreased by 3%. There have not been any weather related catastrophes that significantly impacted results. Figures 6 and 7 (on page 9 and 10) and show the change in average claim costs and frequencies of claims over a longer ten-year period. In summary, Figure 8 (on page 10) shows loss costs per vehicle insured for each coverage. All costs are in nominal dollars (unadjusted for inflation).

Traditionally, the standard market's criteria for acceptable risks responded to results. As loss experience improved, underwriting criteria relaxed and more drivers gained access to the standard market. Correspondingly, criteria became more stringent as results deteriorated. Drivers that were deemed undesirable by the standard market were directed to insurers that operated in the residual or non-standard markets at higher premiums. The Facility Association was the industry's mechanism for providing insurance to those consumers who were refused coverage elsewhere.

As of October 1, 2004, that model was replaced for private passenger vehicles by a take-all-comers rule and a Grid rating program that sets maximum premiums for third party liability and accident benefits coverage for any driver profile. The Facility Association will continue to operate as the industry's mechanism for providing insurance to those consumers who are refused coverage elsewhere for other than private passenger vehicles.

Figure 1

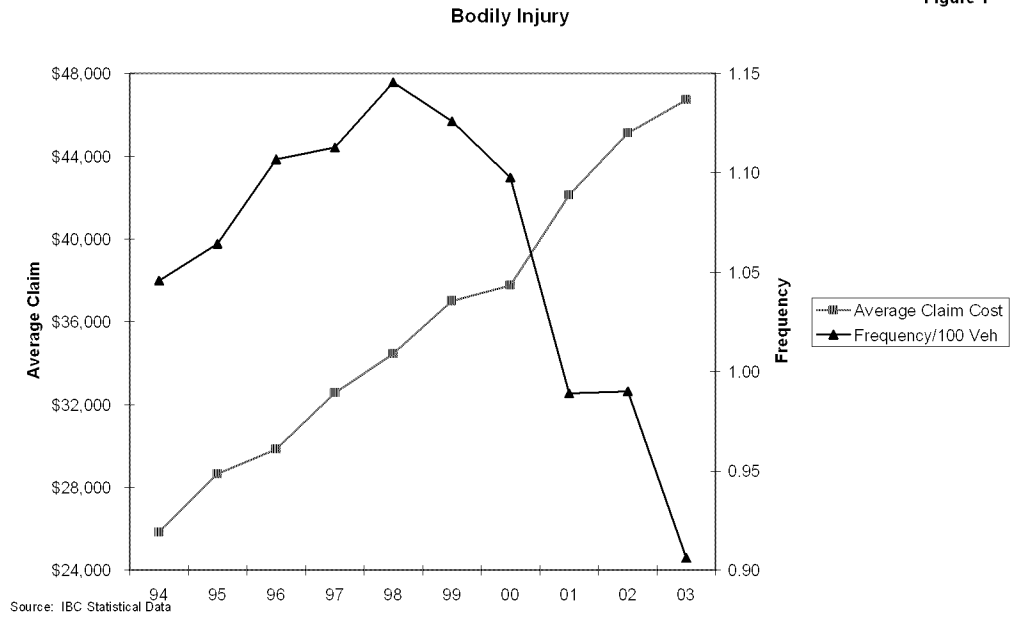
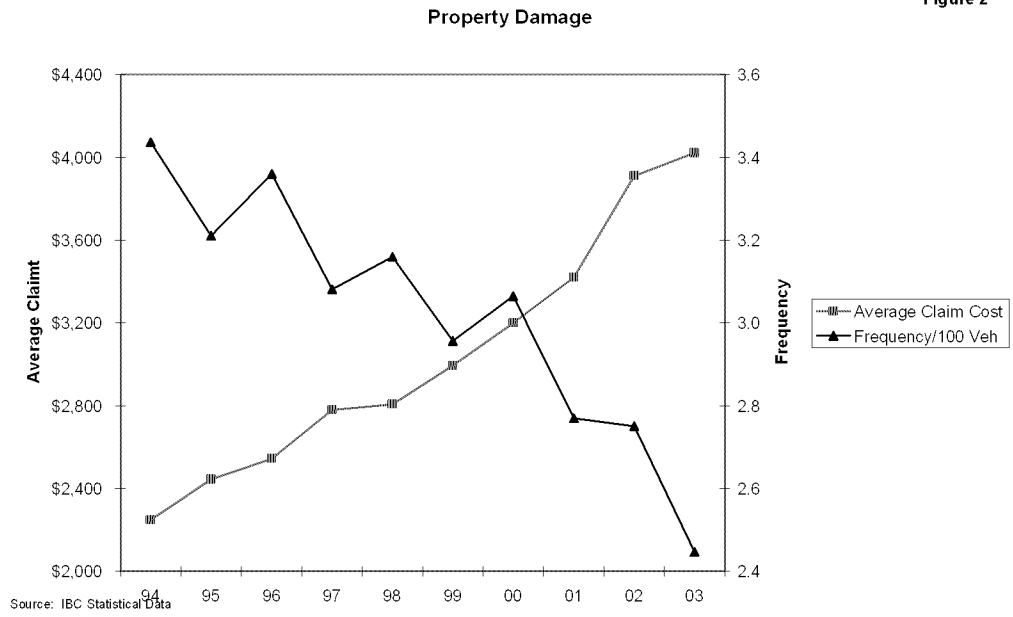
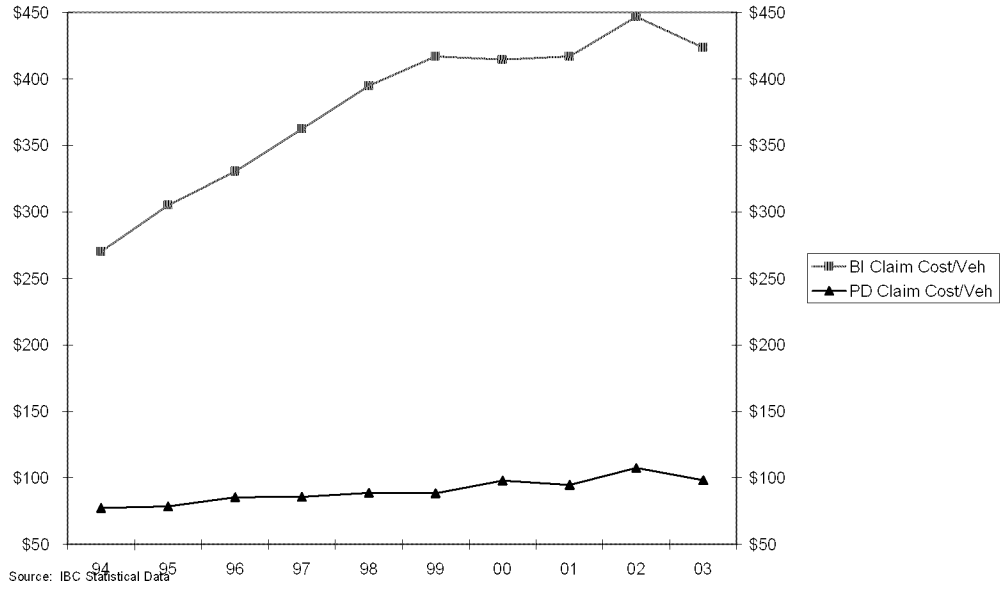


Figure 2



Bodily Injury & Property Damage

Figure 3



Third Party Liability

Figure 4

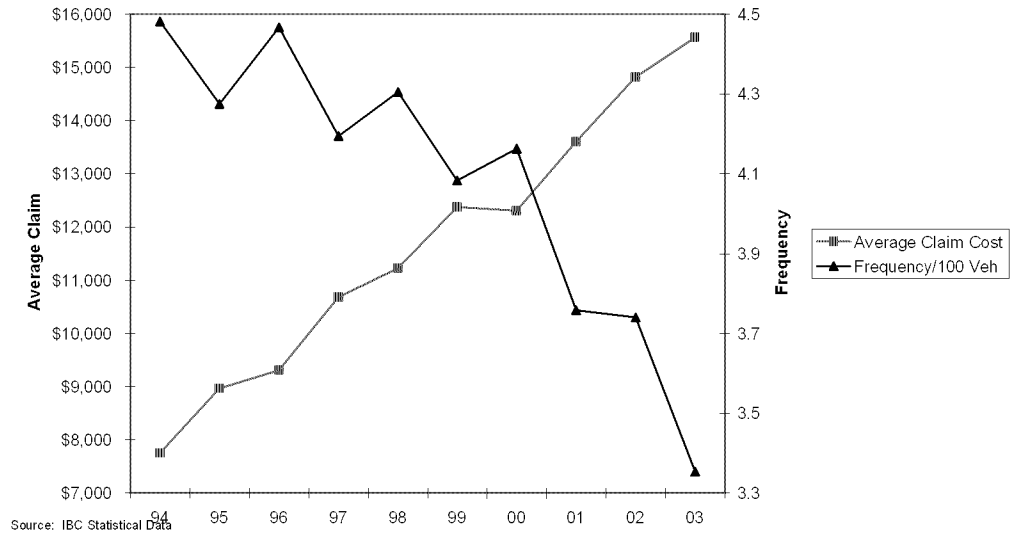


Figure 5

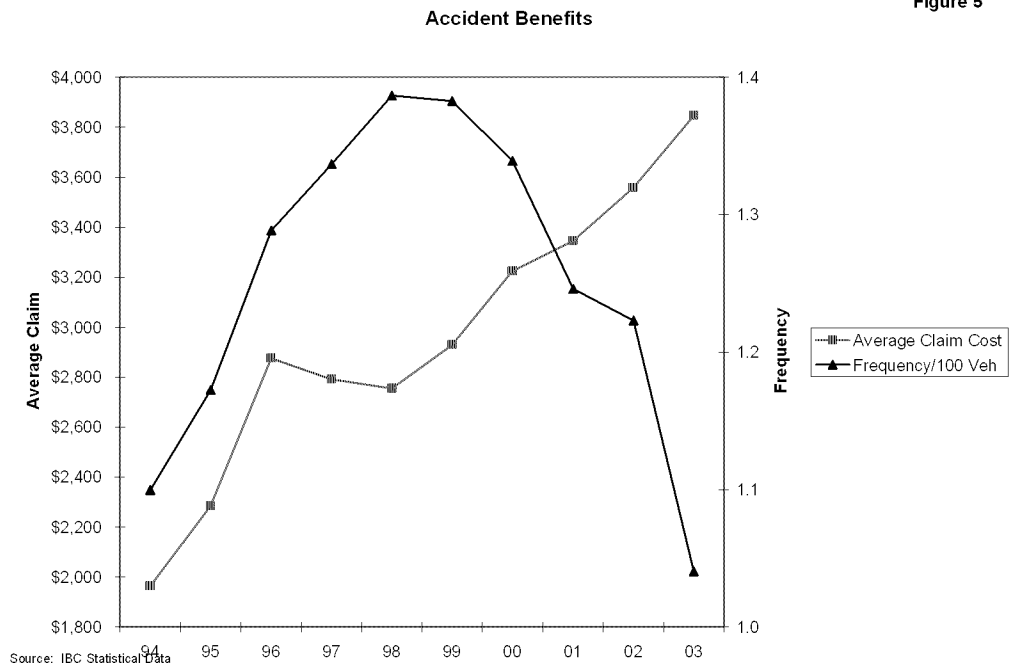


Figure 6

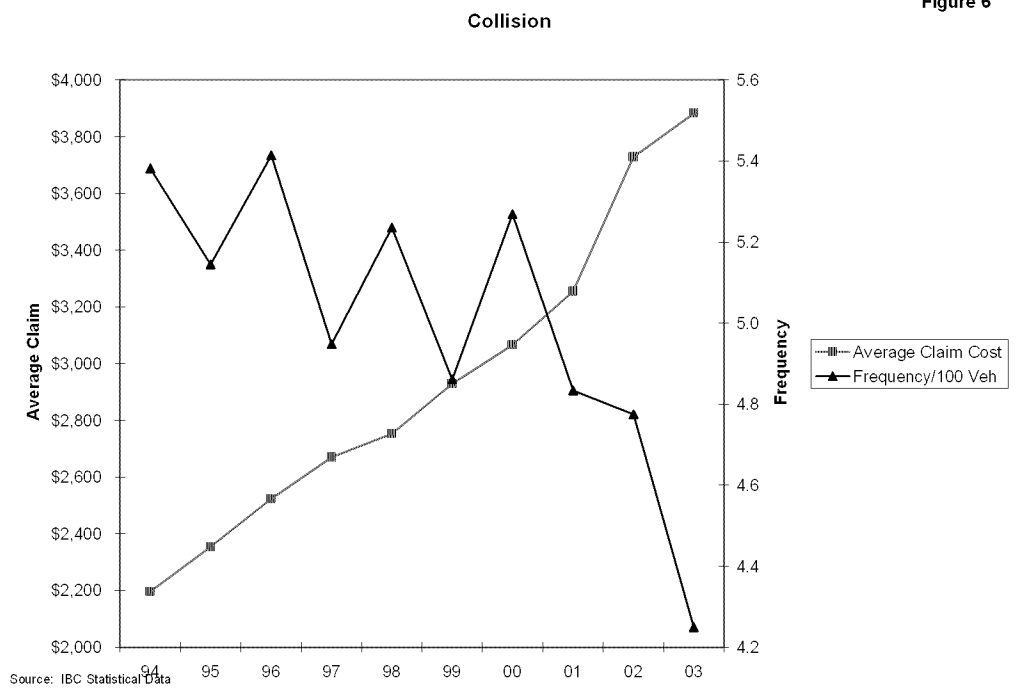


Figure 7

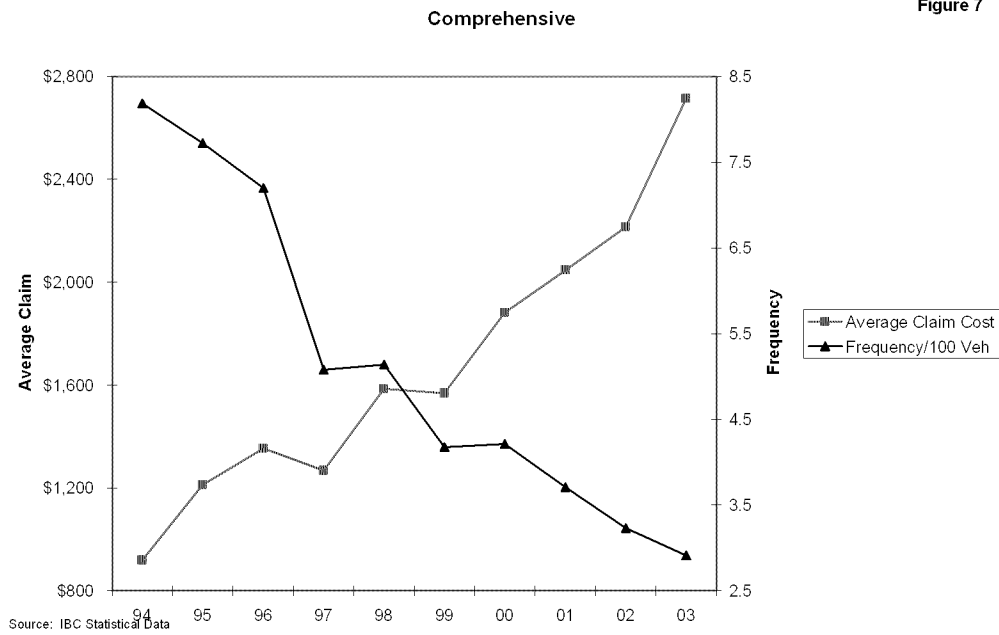
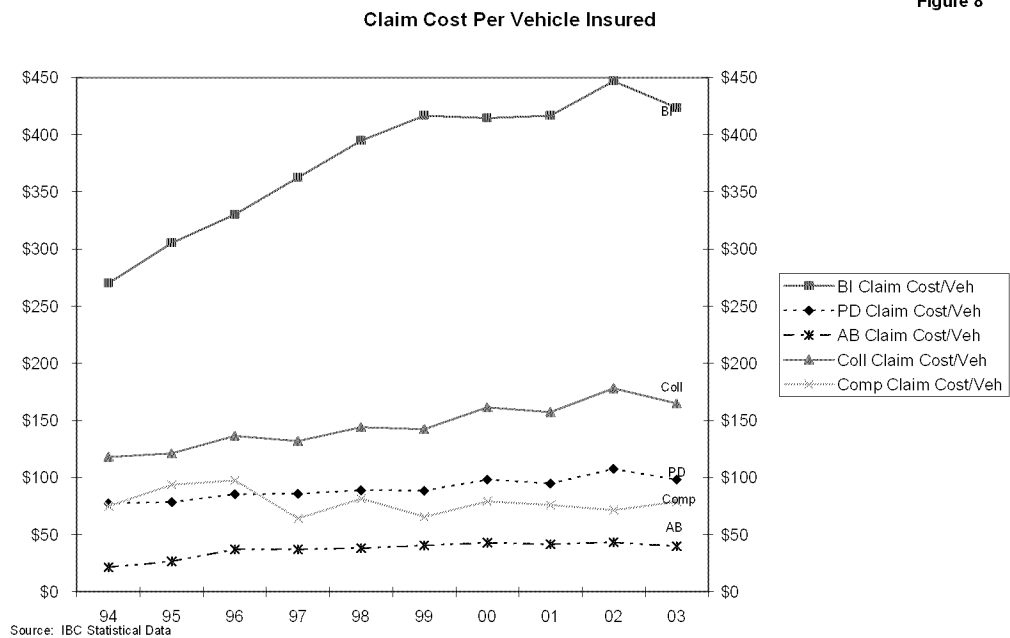


Figure 8



Meetings

Members were appointed to the Board on October 5, 2004 and held one meeting during October 1, 2004 and December 31, 2004 to provide orientation to the new Board members.

Staff

The Board is supported by 5 staff including, Peter Thomas who is the Executive Director and Secretary to the Board, Susan Steeves, Sophie Baran, Colin Leschert and Sonya McAdam.

Alberta Automobile Insurance Board

Meetings

Prior to October 1, 2004, the Board held 5 meetings during which 22 applications were examined. That number compares with 112 applications in 2003, 157 in 2002, 149 in 2001, 127 in 2000 and 123 in 1999. Due to the freeze that came into effect on October 30, 2003 there were no applications relating to change in premium level; 18 related to introduction of group merchandising programs and two dealt with introducing higher limits of liability in preparation for requirements pending for October 1, 2004.

Membership On The Board

There were no changes during 2004 until October 1, 2004 in which the Board was dissolved.

General

The Annual Report for 2003 summarized the Board's mandate, their activities between 1971 and 2003 and outlook on automobile insurance.