

**AIRB Annual Review**

**For the Year 2015**

**Aviva Canada's Submission**

**July 2015**

## Introduction

Aviva Canada Inc. (“Aviva”) is the second largest property and casualty insurer in Canada and the sixth largest insurer in the world. We are privileged to work with more than three million policyholders across the country. Alberta automobile insurance is an important part of our business. In 2014, we insured over 200,000 automobiles in Alberta, sold insurance through more than 200 brokers and handled close to 17,000 Alberta automobile insurance related claims. Aviva employs 225 staff in Alberta. A stable and affordable automobile insurance market is critical for our customers.

This submission will focus on Loss Trends, the drivers of Bodily Injury claims costs and the treatment of ULAE.

### I. Loss Trends

Aviva is concerned about Alberta automobile insurance. Our results are deteriorating. Over the past three years, the Combined Operating Ratio (COR) has risen above 100%, including over 110% in 2014. This will translate into rising premiums. The deterioration is driven by escalating Bodily Injury claims costs.

There is significant uncertainty underlying the Bodily Injury ultimate losses used to derive selected trends. This is an issue which impacts the entire industry. In automobile insurance in any province in Canada, it would not be abnormal for actuaries to work with one accident year or calendar year impact in the data triangles. We have seen several intersecting calendar and accident year impacts in our Alberta Automobile Bodily Injury triangles as a result of:

- 2008 - 2009 constitution challenge to the Minor Injury Cap (*Morrow v. Zhang*);
- 2010 Aviva change in case reserving practices; and
- 2012 *Sparrowhawk v Zapoltinsky* decision.

These changes to the claims environment have increased the uncertainty significantly for this line as we strive to predict something that continues to change. In 2015, we now also have the *McLean v. Parmar* court decision which may further erode the Minor Injury definition and lead to a further increase in our estimates.

Given the length of time to settle Bodily Injury claims, and the intersecting calendar and accident year impacts that Aviva and the Industry are facing, it is not surprising that there is a high degree of uncertainty in our estimates.

Aviva is of the opinion that the loss trends in Oliver Wyman’s Report, “*Preliminary Review of Industry Experience as of December 31, 2014*”, are reasonable based on the industry data available at that point in time. However, it is possible that the selected trend underestimates the impact of the uncertainty associated with Bodily Injury (BI) claims as noted above. Oliver Wyman’s report will not yet reflect any impact as a result of the 2015 *McLean* decision. It is also important to

note that as each company has a different mix of business, the trends may not be appropriate for all companies.

## II. Causes of BI Severity Increase

There are a number of factors which alone, and in combination, are driving an increase in BI severity. Legal representation has a multiplier effect on other cost drivers.

### (a) Minor Injury Claims

Bodily injury costs are increasing due to erosion of the Minor Injury Claims definition through court decisions. Consequently, the number of claims settled within the Minor Injury cap is declining. In 2005-2007, Aviva resolved 83% of its claims as Minor Injury claims. This figure has now dropped to 79%.

This has a noticeable impact on results. The average severity of a minor injury claim is \$4,600. (\$2,800. when we include claims without payment). The average severity for a non-minor injury claim is \$90,000. We estimate that a 1% reduction in Minor Injury settlements represents approximately \$650,000 in additional claims cost. On this basis, the 4% erosion in recent years is driving at least \$2.6 million in additional claims costs annually.

The severity of claims settled within the Minor Injury Cap has remained relatively consistent over the years. However, it is worth noting that our average Minor Injury claim settlement is almost three times higher when the claimant is represented by counsel compared to unrepresented claimants. Increasing legal representation will drive up the severity of Minor Injury claims.

### (b) Legal Representation

Aviva has seen a dramatic increase in the rate of representation by plaintiff counsel. From 2005-2008, 4 -19% of our Bodily Injury claimants were represented by counsel. This number increased to 33% in 2009 and reached a peak of 41% in 2010. Subsequently, the incidence of legal representation has leveled off at 27%.

The increase in legal representation coincided with an increase in lawyer advertising that appears to have been sparked by a series of court decisions that were adverse to the industry. (The 2009 trial decision *in Morrow v. Zhang* that held the Minor Injury Regulation to be unconstitutional, the *Sparrowhawk* decision and most recently the *McLean* decision.) Each of these court decisions has resulted in uncertainty and publicity that led to an increase in lawyer advertising. We should expect this trend to continue.

The increase in legal representation has a financial impact. Claims with legal representation cost two to three times more than unrepresented claims. Plaintiff counsel will build up the claim, seek the appropriate documentation to the support that the injuries are no longer minor or seek to prove a special damages claim (which is not subject to the Minor Injury Regulation). In addition, insurers are exposed to plaintiff's costs and disbursements and will incur their legal expenses.

(c) Psychological Injuries

Commensurate with the increase in legal representation, we have seen an increase in the frequency of claims of psychological sequelae arising from the soft tissue injuries. Aviva carried out an in-depth claim study in 2014. Psychological sequelae was noted in 13% of closed claims with accident years prior to 2012. This number increased to 23% in claims arising after 2012.

Psychological sequelae is the number one reason from removing claims from Minor Injury. Because of the wording of the Minor Injury Regulation, if a claimant suffers psychological sequelae, the claim is automatically removed from Minor Injury; even if the impairments arising from the psychological sequelae are themselves only minor.

(d) Sparrowhawk and TMJ

The increase in TMJ claims started with the release of the *Sparrowhawk* decision in 2012. Prior to *Sparrowhawk*, less than 5% of our claims had TMJ injuries. We now see allegations of TMJ injury in more than 50% of our claims, but so far, we have only seen a 2.5% increase (from 5% to 7.5%) in the number of claims where we compensate the plaintiff for TMJ. For Aviva, each 1% increase in cases with TMJ payments represents approximately \$480,000 in additional annual claims cost, so the 2.5% increase since 2012 is adding approximately \$1.2 million per year in claims cost.

(e) McLean v. Parmer Decision

The *McLean v Parmer* court decision was released on February 23, 2015. We have started to see plaintiff lawyers argue that this case defines chronic pain. They argue that any plaintiff who has suffered from soft tissue injury symptoms for six months or more must be considered to have chronic pain, and the claim must therefore be removed from Minor Injury. We are monitoring our claims to see whether the plaintiff bar may be delaying the discussion of their client's injury claim for at least a year or more so that they can more easily establish six months of "suffering", and therefore fit the definition of "chronic pain" in the *McLean*

Although, there are good arguments that the plaintiff bar's interpretation of *McLean* is incorrect in law, it will take an appeal decision or a subsequent trial decision in another case to clarify that the plaintiff bar is not applying *McLean* correctly. Until then, we expect to see a significant increase in litigation on these claims as the plaintiff bar refuses to back off their position on *McLean* and the insurance industry refuses to adopt it.

(f) The Solution

In 2004, Aviva amended its claims handling practices to defend minor injury claims. We have made a sizable investment in our legal department in Alberta to support our strategy. Aviva continues to aggressively defend Bodily Injury claims in order to control costs. Ultimately, government action is needed to change the definition of Minor Injury to address the erosion caused by the court decisions noted above. The Minor Injury definition should be broadened to capture all minor injuries and associated sequelae, whether the injury is physical, psychological or emotional.

In the absence of a revised definition, the legal community will continue to erode the existing definition. Costs associated with relatively minor injuries will escalate and drive up premiums.

### III. Treatment of ULAE

We believe that it is reasonable for the provision for unallocated loss adjustment expense (ULAE) to be included in the data underlying the trend analysis. We agree that ULAE should be included, as it has been in the past, in order to avoid any bias that may be caused by individual insurers changing the categorization of claim costs from ALAE to ULAE or vice versa.

### Conclusion

We thank the AIRB for the opportunity to provide comments regarding automobile insurance trends. In conclusion, we recommend that the AIRB consider the following when establishing Industry Benchmark factors:

- Bodily injury claims costs are escalating.
- Oliver Wyman's loss trends are appropriate. There is considerable uncertainty in the Bodily Injury line. Oliver Wyman may be underestimating the extent of the uncertainty because of the length of time these claims take to settle and new developments, like the McLean decision.
- Government action is needed to amend the Minor Injury definition. In the absence of a fix, Bodily Injury claim costs will continue to increase.
- It is reasonable for the ULAE to be included in the data underlying the trend analysis.

We are committed to working collaboratively with the AIRB, Alberta regulator and Government to ensure that auto insurance remains affordable and accessible for our customers.

Any questions regarding this written submission can be directed to:

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