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Mr. Allan Cleiren, CA, ICD.D
Chair
Automobile Insurance Rate Board
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Dear Mr. Cleiren,

Thank you for the opportunity to participate in the AIRB's annual review of auto insurance trends and rates for basic and additional coverage. IBC retained Dr. Ron Miller to review Oliver Wyman's preliminary report, *Annual Review of Industry Experience as of December 31, 2016 Private Passenger Vehicles*, and to undertake an analysis of the loss experience of the grid vehicle population. Our commentary reflects Dr. Miller's review as well as the views of insurers operating in Alberta's private passenger vehicle insurance market.

More so than during the previous annual reviews, this year's analyses from Oliver Wyman and Dr. Miller show the scope of the deterioration in the market since accident year 2011 and a level of instability continuing to come from tort claims and natural catastrophes as well as coming from recent developments in vehicle thefts and health levy transfers. The current state of the market has put the AIRB in a position to have to make difficult decisions, particularly when adjusting the grid base premiums and when adjudicating insurers' rating programs.

Grid Vehicle Population

The table below shows the grid population's market share since 2007.

Market Share of Grid Vehicles based on Car-Years Earned Exposure

2007	2008	2009	2010	2011	2012	2013	2014	2015	2016
8.8%	9.1%	8.0%	7.5%	7.4%	7.6%	7.1%	6.6%	6.1%	5.5%

IBC based on data from Dr. Ron Miller.

Since the annual review in 2012, when the AIRB began adjusting the grid base premiums upwards by between 5% and 8%, the number of vehicles insured with grid premiums has declined by 2.1 percentage points, from 181,373 or 7.6% of insured vehicles in 2012 to 146,852 or 5.5% of insured vehicles in 2016. The effect of the 8% increase that the AIRB announced last year will not be known until the 2017 data is available.

The table below shows the loss costs and loss ratios for basic coverage for the grid population and the non-grid population for the past five accident years.

Loss Costs and Loss Ratios for Basic Coverage

	Grid Loss Costs	Grid Loss Ratio	Non-Grid Loss Costs	Non-Grid Loss Ratio
2012	\$1,308	101%	\$443	89%
2013	\$1,353	100%	\$479	93%
2014	\$1,500	107%	\$508	94%
2015	\$1,684	113%	\$556	98%
2016	\$1,435	89%	\$527	87%

IBC based on data from Dr. Ron Miller. Includes ULAE and the health levy.

Prior to 2016, which had an unusually low loss cost for the grid population, the grid population's loss cost had been increasing at a higher rate than the non-grid population's loss cost. Specifically, for the grid population, it increased by 29%. For the non-grid population, it increased by 26%.

Also prior to 2016, although the grid population's size and market share had declined by a fair amount, the overall claims cost that the grid population had incurred and the overall underwriting losses had increased. The table below shows those results.

Estimated Underwriting Results for Grid Vehicles for Basic Coverage by Accident Year

	2012	2013	2014	2015	2016
Total Claims Costs	\$237,252,205	\$236,839,171	\$255,604,489	\$271,275,514	\$210,765,682
Underwriting Results	(\$52,159,602)	(\$54,872,433\$)	(\$69,861,519)	(\$86,064,629)	(\$28,652,492)

IBC based on data from Dr. Ron Miller. Includes ULAE and the health levy. Operating expenses were estimated based on data from GISA and Dr. Miller.

As noted above, between 2015 and 2016, the grid population's loss cost and underwriting result for basic coverage improved significantly. The cause of the improvement was a large decline in the claim frequency rate. As shown in the table below, the frequency rate declined by 7%, from 10.2 to 9.5 claims per 100 vehicles.

Claim Frequency per 100 Vehicles for Grid Vehicles for Basic Coverage by Accident Year

	2012	2013	2014	2015	2016
Claim Frequency	10.1	10.2	10.2	10.2	9.5

Data from Dr. Ron Miller.

The decline in the frequency rate seems more like an outlier than an indication of a new trend. Dr. Miller's position is that the long-term trend indicates that loss costs that had been increasing in recent years will once again increase in 2017 and in 2018. For the total market, both Oliver Wyman and Dr. Miller estimate that loss costs will continue increasing at a high rate. Given that the grid population's claims cost tends to increase at an even higher rate than the non-grid population, a significant adjustment to the grid base premiums is warranted again.

An adjustment of this nature is particularly important this year because of the size of approved non-grid rate increases in recent years. The table below shows the approved average rate increase for basic coverage weighted by market share for the past eight quarters. During this time period, basic coverage non-grid rates increased by 14.1%.

Basic Coverage Non-Grid Rate Increases

	Q3 2015 to Q2 2016	Q3 2016 to Q2 2017
Weighted Average Basic Coverage Increase	7.8%	6.3%

IBC based on data from the AIRB. Figures represent the largest insurers in Alberta, representing 75% of the total market.

Unless the government introduces reforms to reduce and contain third-party liability bodily injury (TPL-BI) loss costs, costs will continue increasing and premiums could also continue increasing. The government is expected to conclude its review of the *Minor Injury Regulation* this fall. To date, it has not indicated that it intends to introduce reforms to reduce and contain TPL-BI claims costs.

For these reasons, we recommend that the AIRB increase the grid base premiums by a percentage greater than the previous adjustments. Otherwise, the difference between premiums set competitively and grid premiums will decline and the market share of the grid population will increase, leaving the average consumer in Alberta with the unfair responsibility of subsidizing the cost of insuring more higher-risk drivers.

Loss Development, Trend Rates and Other Benchmarks

The table below shows the loss cost by sub-coverage for accident year 2016 based on the loss development factors that Oliver Wyman, Dr. Miller and the actuaries at GISA used for their individual analyses. It also shows the percentage changes over a five-year period.

Loss Cost by Sub-Coverage Comparison

	OW 2016	RM 2016	GISA 2016	OW 5-Year Change	RM 5-Year Change	GISA 5-Year Change
TPL-BI	\$356	\$337	\$339	27.9%	21.3%	22.1%
PD	\$155	\$153	\$153	(0.5%)	(1.4%)	(1.3%)
AB-MR	\$36	\$36	\$35	25.6%	25.9%	23.6%
AB-DI	\$12	\$11	\$11	12.4%	1.9%	1.8%
COLL	\$232	\$236	\$235	1.8%	3.5%	3.1%
COMP	\$252	\$253	\$252	44.1%	44.3%	44.2%

Includes ULAE but excludes the health levy.

Due to methodological differences, Oliver Wyman's TPL-BI loss cost differs from Dr. Miller's estimate. Dr. Miller's estimate aligns with GISA's estimate.

Dr. Miller also identified adverse development in a few selected accident years for TPL-BI, accident benefits med/rehab (AB-MR) and accident benefits disability income (AB-DI). For TPL-BI, Dr. Miller attributes it potentially to one or a few large insurers having changed their reserving practices. For AB-MR and AB-DI, due to their small cost size, Dr. Miller attributes the adverse development to random fluctuations that could be associated with a few catastrophic-type claims based on Saskatchewan's benefit levels.

The table below shows the future loss cost trend rate by sub-coverage from Oliver Wyman and Dr. Miller.

Future Loss Cost Trend Rate by Sub-Coverage

	OW	RM	Difference
TPL-BI	+7.75%	+6.67%	(1.08 p/p)
PD	+1.50%	+2.83%	1.33 p/p
AB-MR	+3.50%	+4.32%	0.82 p/p
AB-DI	+4.50%	+3.98%	(0.52 p/p)
COLL	+2.00%	+3.29%	1.29 p/p
COMP	+5.00%	+6.60%	1.60 p/p

Data from Oliver Wyman and Dr. Ron Miller.

There are modest differences in the trend rates for TPL-BI, property damage (PD), collision (COLL) and comprehensive (COMP). The TPL-BI difference is because of Oliver Wyman's higher loss cost for 2016. Dr. Miller's TPL-BI trend rate accounts for a 10.5% level change in the second half of 2011. Without the level change, Dr. Miller's trend rate would be 9.1%.

Dr. Miller also accounts for an 11.4% level change in the first half of 2015 in the AB-MR trend rate, a 34.7% level change in the first half of 2015 in the COMP-theft trend rate and a (32.1%) level change in the second half of 2011 in the COMP-theft trend rate.

Dr. Miller notes that if the AIRB wants Oliver Wyman to incorporate weather and economic conditions in its trend analysis, it should use a consistent model for frequency, severity and loss cost. Dr. Miller suggests that Oliver Wyman find a way to project the associated variables forward in the near-term, which is not easy, and to incorporate the level changes for these variables from the past to the near-term future into the analysis through forward projection via the trend regression models, instead of a single forward annual trend rate.

Commentary on Bodily Injury Claims

The table below shows the loss cost by sub-coverage for the past six accident years estimated by Dr. Miller. This time period accounts for the change in the TPL-BI loss cost trend that happened in the second half of 2011 and the first half of 2012. The change in trend coincides with the January 2012 Court of Queen's Bench's decision in *Sparrowhawk v. Zapoltinsky* on the application of the cap on non-pecuniary damages prescribed in the *Minor Injury Regulation*.

Loss Cost by Sub-Coverage by Accident Year

	TPL-BI	TPL-PD	AB	COLL	COMP
2011	\$250	\$154	\$38	\$227	\$110
2012	\$278	\$155	\$42	\$227	\$175
2013	\$306	\$166	\$41	\$245	\$168
2014	\$338	\$168	\$41	\$252	\$187
2015	\$372	\$169	\$51	\$249	\$190
2016	\$337	\$153	\$49	\$236	\$253
Annual Change	6.2%	0.0%	5.2%	0.8%	18.1%

Data from Dr. Ron Miller. Includes ULAE but excludes the health levy.

Besides COMP, the sub-coverage that sustained the largest year after year of rising costs is TPL-BI. The unusual decline in the claim frequency rate in 2016 caused the decline in TPL-BI loss costs. Oliver Wyman's and Dr. Miller's future trend rates show that despite this development, they expect the cost of these claims to continue increasing at a high rate.

As the table below shows, the rising average TPL-BI claims cost was exclusively responsible for the rising loss cost since 2011. Over the six-year period, the average cost increased by 55.1% or by 9.2% per year.

TPL-BI Claims Experience by Accident Year

	Frequency per 100 Vehicles	Average Claims Cost	Loss Cost
2011	0.60	41,523	\$250
2012	0.59	46,856	\$278
2013	0.59	51,950	\$306
2014	0.59	57,376	\$338
2015	0.57	65,098	\$372
2016	0.52	64,387	\$337

Data from Dr. Ron Miller. Includes ULAE but excludes the health levy.

The TPL-BI claims affected most by the sudden change in trend have been claims with incurred amounts of less than \$15,000, which is a proxy for claims that settle within the cap. Between 2005 and 2011, the percentage of claims with incurred amounts less than \$15,000 hovered between 79.6% and 83.5%, with an average of 81.1%. In 2012, the percentage suddenly declined to 75.6%. In 2013, the percentage continued to decline, reaching 73.6%. In only two years, the percentage declined by almost eight points from the historical average. The table below shows this sudden change in trend.

TPL-BI Claims Size Distribution at Three-Year Development Level by Accident Year

	2005	2006	2007	2008	2009	2010	2011	2012	2013
Claims <\$15,000	14,414	18,576	17,667	13,857	13,073	13,813	13,733	12,916	13,134
Total Claims	17,786	22,260	21,427	17,387	16,299	17,013	17,242	17,074	17,856
Under \$15,000	81.0%	83.5%	82.5%	79.7%	80.2%	81.2%	79.6%	75.6%	73.6%

IBC based on data from GISA, exhibits AUTO5001-AB. GISA does not develop the size of claim distribution exhibits to ultimate values. So, the estimates are based on claims at a three-year development level, which is the most up to date level for accident year 2013.

The experience of the past six accident years, evidence that fewer claims have been settling within the cap and the future trend rates indicate that regulatory reform is needed to address the effect of the *Sparrowhawk* decision and reduce and contain TPL-BI claims costs. The table below shows Dr. Miller's projected loss costs for TPL-BI claims for 2017 to 2019.

Projected TPL-BI Loss Cost

	2016	2017	2018	2019
Loss Cost	\$337	\$392	\$418	\$446

IBC with data from Dr. Ron Miller. Includes ULAE but excludes the health levy.

Dr. Miller projects that without reform, TPL-BI claims costs will continue increasing at a high rate, reaching \$446 by 2019, which is 32% higher than in 2016 and 78% higher than in 2011. With the total loss ratio being over 80% for four years and with the current cost projections, there is significant pressure on the premiums that consumers pay.

Commentary on Accident Benefits Claims

Dr. Miller attributes the increase in the 2015 AB-MR average claims cost to the prevailing economic conditions and/or more legal involvement in claims. Dr. Miller also attributes the increase in the 2015 AB-DI average claims cost to random fluctuations.

Commentary on Vehicle Damage and Theft Claims

Dr. Miller attributes the decline in the 2016 COLL average claims cost to random variations in the data. He notes that there was an increase in the COMP-theft level in the first half of 2015 as well as a decline in level in the second half of 2011. Dr. Miller did not attribute these changes to any developments.

The recent COMP-theft claims development is unique to Alberta. The table below shows the COMP-theft claim frequency rate in Alberta, Ontario and Atlantic Canada for the past five accident years.

COMP-Theft Claim Frequency Rate per 100 Vehicles by Accident Year

	Alberta	Ontario	Atlantic Canada
2012	0.22	0.13	0.08
2013	0.24	0.11	0.08
2014	0.24	0.10	0.07
2015	0.32	0.11	0.07
2016	0.36	0.11	0.07
Change	58%	(18%)	(16%)

Data from GISA. Claims are at the six-month development level.

Over the five-year period, the COMP-theft claim frequency rate increased by 58% in Alberta while it declined by 18% and 16% in Ontario and Atlantic Canada, respectively. That for years Alberta has had a much higher COMP-theft claim frequency rate than Ontario and Atlantic Canada makes the recent increase more surprising.

Catastrophe Provision

Because of the increases in damages from natural catastrophes in recent years, Dr. Miller continues to recommend using a provision based on the weighted average of the past five accident years instead of Oliver Wyman's approach that is based on an average of the weighted average factors for the past five and ten accident years with an adjustment downwards to account for COMP-theft claims experience.

For the most recent five-year period, the weighted average is 66%, in comparison to 55% selected by Oliver Wyman. Dr. Miller expects that based on GISA's forthcoming 2016 *Catastrophe Report, Province of Alberta*, which will likely include significant losses from several major hail, wind and water events, the catastrophe provision based on the most recent five-year period will be even higher.

Data from CAT-IQ, which estimates the amount of insured losses from natural catastrophes that cause at least \$25 million in total insured damages, shows that in 2016, a few events caused significant damages to insured vehicles.

- The hail, wind and water event that struck Okotoks, Calgary and Edmonton between June 28th and June 30th caused \$25 million in insured vehicle damages.
- The hail, wind and water event that struck Calgary on July 15th and July 16th caused \$28 million in insured vehicle damages.
- The hail, wind and water event that struck Medicine Hat between July 18th and July 20th caused \$21 million in insured vehicle damages.
- The hail, wind and water event that struck Calgary, Airdrie, and Fort McMurray between July 30th and August 1st caused more than \$178 million in insured vehicle damages.

Health Cost Recovery

Oliver Wyman implies that insurers should reflect the 2017 health levy of \$155 million in their filings for rating program changes up until the government announces the levy for 2018. The table below shows the increases to the levy between 2012 and 2017.

Health Levy Amounts (in millions)

	2012	2013	2014	2015	2016	2017
Health Levy	\$95	\$100	\$105	\$120	\$135	\$155

Data from the Alberta government.

Notably, in addition to the recent increases being by at least \$15 million compared to \$5 million previously, the 2017 health levy of \$155 million is \$15 million more than \$140 million health levy that the government originally planned to establish. Dr. Miller recommends that because of the size of the recent increases, the AIRB should allow insurers to account for a potentially higher levy, which will be applicable to many policies written in 2019 at rates approved based on filings made during 2018.

Investment Income on Cash Flow

Because of the Bank of Canada’s recent increase to the overnight rate, Dr. Miller notes that Oliver Wyman’s selected rate of 1.75% is reasonable.

Operating Expenses

Dr. Miller continues to recommend basing the expense ratio on total earned premium instead of using the expense ratio in GISA’s *Automobile Insurance Financial Information Industry Expense Report*, which is based on total written premium. The expense ratio based on using earned claims costs and earned premiums is 27.6%, in comparison to 26.7% selected by Oliver Wyman.

Conclusion

We understand that the AIRB cannot fix all the problems in the market. The AIRB is not in a position to reform the *Minor Injury Regulation* to reduce and contain TPL-BI claims costs. Nor is it in a position to control the weather or curb vehicle thefts. It can only make decisions on the grid base premiums and on insurers’ rating programs within the environment that it operates. As mentioned, we recognize that for this year’s review and into 2018, these decisions will be more difficult than in the past.

In advance of the public hearing, we want to leave the AIRB with the following comments and recommendations:

- The significant decline in the TPL-BI claim frequency rate for accident year 2016 is likely an outlier and not indicative of a new trend;

- The grid base premiums warrant a significant increase that accounts for the loss cost trend for basic coverage, the increasing size of underwriting losses and the size of the recently approved non-grid rates for basic coverage;
- Without reforming the *Minor Injury Regulation*, the cost of TPL-BI claims will continue increasing at a high rate; and
- When adjudicating rating program changes,
 - Insurers may present with reasonable trend rates and assumptions that may differ from Oliver Wyman's selected rates and assumptions,
 - Changing climate patterns support using a COMP catastrophe provision based on five years of loss experience,
 - The size of the increases expected to the health levy support allowing insurers to account for a higher levy in 2018 and in 2019, and
 - An expense ratio based on direct earned premium is more appropriate than an expense ratio based on direct written premium.

Again, thank you for the opportunity to provide input for the annual review. We look forward to meeting with the AIRB on August 15th.

Sincerely,



William A. Adams

cc: Del Dyck, Executive Director, AIRB