



Intact Financial Corporation

AIRB Annual Review



Introduction

Insurance isn't just about homes, cars and businesses – it's about people.

When the unexpected happens, Albertans rely on insurance to recover quickly, and deserve that protection and peace of mind at affordable rates. Across our three brands, we wrote over \$1.4 billion in written premiums in 2017, representing 22% of market share.

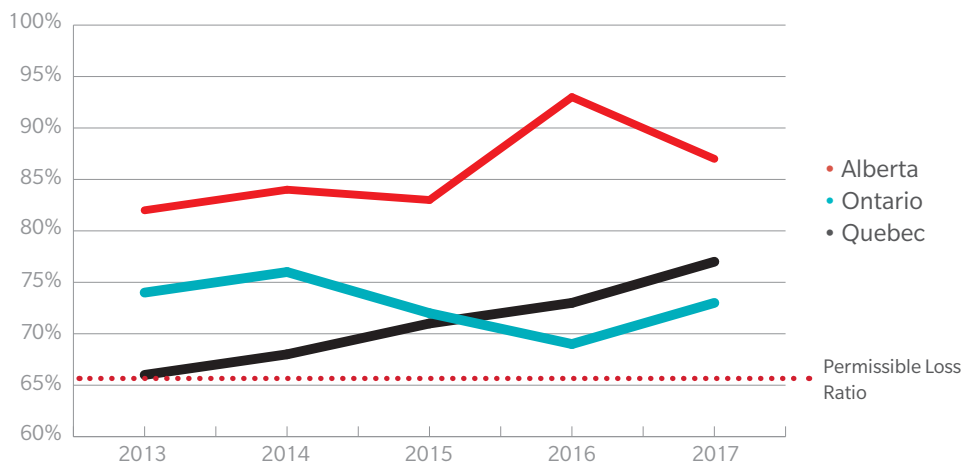
As the insurance company of record for 525,000 customers, and the employer of 1,400 Albertans across Intact Insurance, Novex and belairdirect, we are committed to ensuring Albertans can access the insurance they need at affordable and predictable rates. To do so, we believe Alberta must have:

- An agile, competitive and customer-driven insurance market
- Predictive trending that closely reflects current costs and payouts
- A regulatory framework that aligns to today's realities

Today's reality

In 2017, the industry loss ratio was 87.7%, indicating auto insurance rates were not accurately reflecting the experience on Alberta roads. This trend is not new: since 2013, the loss ratio in Alberta in personal auto has continually increased, reaching a 5-year high of 95.1% in Q1 2018. Loss ratios in Alberta have also been considerably and consistently higher than other Canadian provinces, with a widening gap in 2016/2017.

Industry Loss Ratio Personal Auto



These trends not only indicate a challenge for the industry – they directly impact Albertans through their insurance rates. If the current state is sustained, product availability (and accessibility) will continue to decline.



Making impactful change now

Stabilizing loss ratio trends, in the face of these emerging rating pressures, requires a regulatory framework that is stable, yet agile, to protect Albertans from significant rate fluctuations and ensure fair and equal access to insurance.

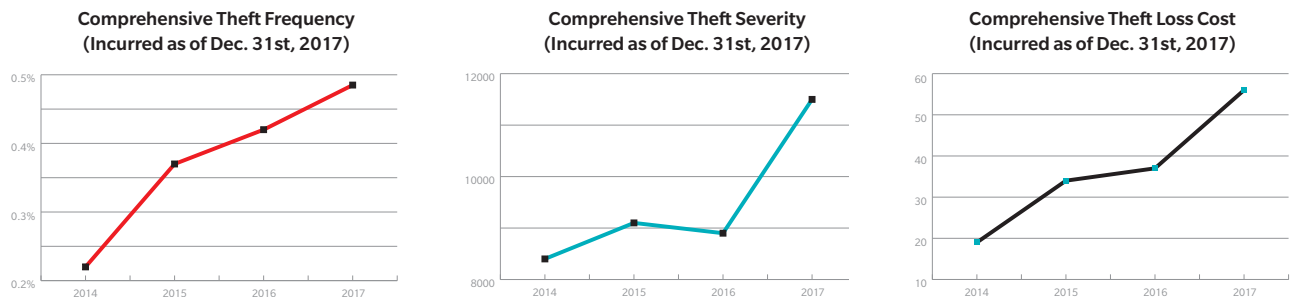
A. Adjust claim amount development factors for third party liability (bodily injury)

Oliver Wyman's report, *Annual Review of Industry Experience – Preliminary Report as of Dec 31, 2017* (OW Report), suggests, when compared to previous review, higher incurred losses have been recorded in the 6-12, and 12-18 month maturities after a claim. IFC observed similar patterns for the accident year 2015 to 2017 claims. Based on the continued cost pressures observed in settling bodily injury claims, we believe that selecting development factors closer to those that have emerged in the latest period would be more responsive to the changing bodily injury environment and would lead to a more realistic estimate of ultimate bodily injury losses.

B. Adjust loss trend benchmark to reflect the actual increase in comprehensive claims costs

After reviewing the OW Report and analyzing our internal data, we found that our trends were generally consistent with the findings of the report with the exception of the items highlighted below.

Theft: From accident years 2016 – 2017, the industry's theft loss cost increased by about 40%, while IFC saw an increase of 48.7% (likely attributable to the economic environment in Alberta). To better reflect current and future realities, we suggest that a higher theft trend (rather than the selected 11% theft trend) be used to project the overall comprehensive future trend. We re-state our recommendation that a future trend of at least +6% for comprehensive loss cost is appropriate (versus the +5.5% noted in the OW Report). This is still conservative given the observed accident year 2015-2017 loss cost increase.



Third Party Liability – Bodily Injury: Recognizing the rising costs of TPL BI costs and the high development in the recent years, we agree with the increased past trend of +8.5%. However, this trend poses affordability risks for automobile insurance in Alberta and as such, reinforces the need to continue the legislative reform to reverse the observed trends in the minor injury regulation.

C. Continue reform of the Minor Injury Regulation

On May 17, 2018, the Alberta Government decided to remove the September 30, 2018 expiry date for the Minor Injury Regulation (MIR) and amend the regulations to clarify the treatment of some injuries arising from accidents on or after June 1, 2018. There are two types of injury which are likely to now be considered under the definition of minor injuries:

- Minor temporomandibular joint (TMJ) or jaw injuries.
- Less significant psychological or pain conditions or symptoms which arise from, and resolve with, other minor injuries and generally last for only a limited time period which will need to be interpreted by the courts but will likely not exceed 12 months.

IFC has long held the view that substantial reform of the MIR was an important step towards ensuring an affordable and sustainable automobile insurance product is provided in Alberta. Based on our analysis, we are concerned the financial impact of the recent changes will be limited in scope and subject to a large degree of uncertainty based on the interpretation of the reforms by the courts in Alberta.

We support the Alberta government's recent reform and encourage continued evolution, particularly related to the following as areas which limit the applicability of the MIR when determining whether an injury qualifies as "minor", and any consequent reduction in loss cost as a result of the reforms.

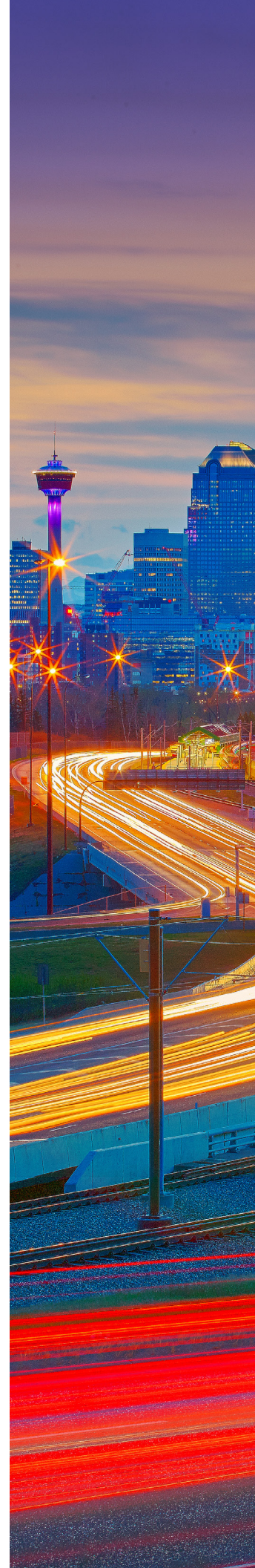
- The express exclusion of TMJ injuries that include "damage to bone or teeth" or "damage to or displacement of the articular disc" limit the applicability of the MIR to fairly simple TMJ injuries but this is in line with the intent of the regulation.
- Due to difficulty in determining the cause of symptoms for jaw injuries, MRI examinations will often be required to demonstrate whether a TMJ injury is subject to the cap or not.
- In the event of dispute over a TMJ injury, there is an obvious gap in the MIR regime as dentists are not included in the approved list of Certified Medical Examiners. This means that any TMJ injuries where specialised dental intervention is required would arguably not be considered minor.
- The amendments (and the MIR in general) do not refer to damage to cartilage explicitly, and only provide clarity for injuries to the articular disc. This continues to be a source of ambiguity in the determination of injuries as minor.
- The Diagnostic and Treatment Protocols Regulation ("DTPR") does not provide guidance regarding the diagnosis or treatment protocols to be followed with regards to TMJ injuries or physical or psychological conditions or symptoms related to minor injuries.
- The reforms do not provide any further clarity on interpretation for the terms "serious impairment" or "substantial inability", which are major factors in determining whether injuries are considered minor in relation to the severity and duration of the symptoms.

Without continued reform, these limitations stand to increase pressure on Alberta's healthcare system with increased requests for MRIs, as well as substantially longer settlement periods due to medical wait times and potentially contested diagnoses.

D. Adopt Bank of Canada benchmark interest rate for pre-judgement interest

Pre-judgment interest is meant to compensate for the loss of use of money and not as a punishment on the at-fault party. Since 1984, the interest rate has been set at 4%, which is 2.5% higher than the current bank rate, potentially incentivizing longer settlement periods and increasing claims costs.

In January 2015, Ontario passed legislation linking the pre-judgment interest rate to the bank rate in the province, effectively balancing compensation and long-term rate stability. The Bank of Canada interest rate sets the standard for our country and would set a stable and predictable foundation for pre-judgment interest. Adopting the benchmark interest rate will almost immediately improve the affordability of automobile insurance in the province, while ensuring those awarded pre-judgment interest receive fair compensation.



E. Remove Ministerial 5% Rate Cap Order

Government has sought to protect Albertans, but has unwittingly created circumstances that could cause significant spikes in future insurance costs.

On December 24, 2017, the Ministerial Order No.25/2017 imposed a 5% limitation on private passenger rate increase for any filings submitted during the period November 1, 2017 to November 30, 2018.

As previously mentioned, Alberta automobile insurers have been challenged in dealing with factors putting additional pressure on the cost and at the end of Q1-2018, the industry loss ratio hit 95.1%, the highest in more than five years. We believe that the extension of the capping beyond November 30, 2018 expiry will have the following consequences in the Alberta automobile industry:

- Customers will have fewer options due to a tightening of the industry in certain areas, such as Section C coverage eligibility, deductible and limit options and endorsements eligibilities. This leaves customers with fewer options and reduced coverages.
- Fewer automobile insurance options will be available to customers as the current environment creates uncertainty for existing insurers to operate profitability.
- The cap would also create a barrier for new players to enter the market.

To protect Albertans from significant rate fluctuations and ensure fair and equal access to insurance, the 5% cumulative rate cap on rate increases for Personal Passenger Vehicles should not be extended.

The pressure on the cost to do business continues to increase with high bodily injury costs, increase in the health levy, and legalisation of cannabis. If a similar order is issued again this year, Alberta risks a crisis where insurance coverage will be very limited to a significant portion of the population.

Improving insurance for Albertans in the future

Our vision: a future where Albertans will have a greater choice of insurance providers, more products and benefits to choose from, better customer service, including a more efficient approach for dealing with injured motorists, and a wider range of prices ranging from cost saving alternatives to more premium offerings.

Certain emerging factors (in particular, cannabis and climate change) will introduce more uncertainty and put additional pressures on pricing stability.

Limited data on the impact of recreational legalized cannabis introduces greater uncertainty in auto rating.

In preparation for the upcoming legalization of recreational cannabis, IFC has reviewed global data. In the three U.S. states where cannabis was legalized, the increase in collision claims ranged from 4.5% to 13.9%.¹ This uncertainty highlights the need for caution when estimating the influence legalized recreational cannabis could have on insurance rates.

As such, based on our preliminary interpretation of the findings of these studies, and our assessment of their relevance considering differences between the US and Canada, we believe that the increased prevalence of recreational cannabis use could lead to an increase in collision claims frequency of 3% or more, depending on the province. Long term rate stability will derive from accurate data collection and analysis, emphasizing the importance of fully and effectively tracking cannabis-related collision data as early as possible.

¹ - Recreational marijuana and collision claim frequencies, Highway Loss Data Institute, Bulletin April 2017

In addition, we believe that there is a gap in public education and awareness about driving under the influence of cannabis. In last year's Consumer Representative Report, the majority of Albertans felt it was not safe to drive under the influence of cannabis, suggesting that public awareness and education campaigns will significantly encourage drivers to make behavioural changes, a contributing factor in reducing collision frequency.

Changes in our **weather are impacting Albertans.**

From 1983- 1989, the IBC recorded 13 catastrophic events; 57 from 1990-1999, 58 from 2000 – 2009, and 85 events from 2010 – 2017. This steady increase in the number of smaller, more frequent events signals a defining shift in our climate – particularly for Albertans.

Severe weather is not a new phenomenon in Alberta; last year, six of the 15 events impacted the province, after two major catastrophic events: the Fort McMurray fire in 2016 and Calgary flood in 2013.

We find that the catastrophe provision of 65% (2016) appears reasonable at this time, however we will make further comments after the review is completed by OW.

Others factors, like technology, provide innovative solutions to stabilize rating that also meet the evolving expectations of Albertans.

Technology and telematics can help to improve road safety and stabilize rates through education and awareness.

Drivers can pick up unconscious habits like harsh braking, rapid acceleration and distracted driving. As some of the leading causes of collisions, educating Albertans on these issues can contribute to safer roads while also improving rate predictability.

According to a 2016 study² conducted by the City of Edmonton, 94% believe that distracted driving behaviours such as texting or talking on the phone is a serious threat to safety, but 33% said they've recently done it while driving. This suggests more needs to be done to influence or change behaviour: from January – March 2017, over 24,000³ collisions were a result of distracted driving. Albertans agree⁴ our current penalties for distracted driving are not enough of a deterrent, and more needs to be done to address dangerous behaviours at an individual level.

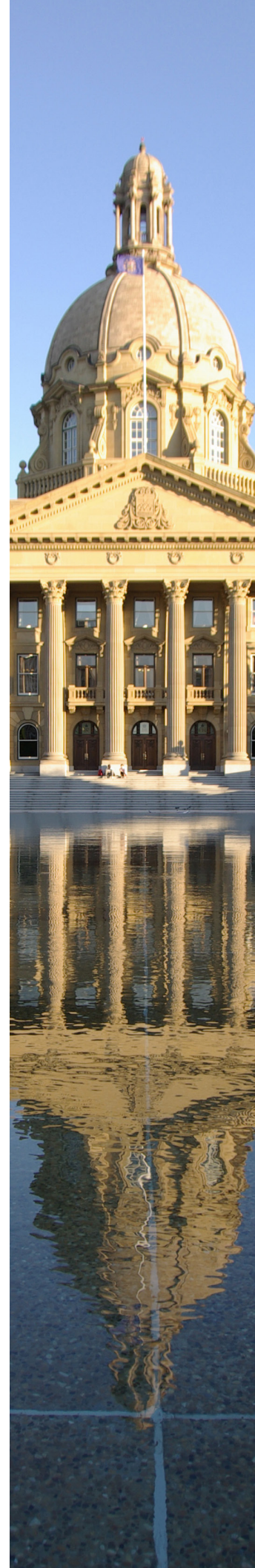
With more drivers willing to try usage-based insurance, telematics is a viable solution to reward good driving behaviours and incentivizing others to make the right changes to reduce collisions caused by distracted driving. Through a combination of individual awareness and public education campaigns, the industry can encourage (and reward) behaviours that reduce collision frequency and contribute rating stability.

As an industry, we must focus on leveraging opportunities and mitigating challenges that these and other emerging trends create in order to ensure Albertans benefit from responsive, balanced and fair insurance.

2 - <https://www.edmonton.ca/transportation/RoadsTraffic/TrafficSafetyCultureSurveyReport2016.pdf>

3 - <https://ama.ab.ca/2018/01/02/distracted-driving-stats-double-standard>

4 - <http://www.airb.alberta.ca/industry-information/annual-review/2017/AIRB-Annual-Review-PPV-2017-Report-Appendix-C-Consumer-Representative.pdf>



As part of our commitment to achieving this future, we are making changes to how we conduct business – upgrading legacy technology to make it easier for customers to access insurance solutions, introducing the Intact app to make insurance more accessible for Albertans, managing expenses, and leveraging telematics to provide customers with customizable rating experience in personal auto. We are also working to ensure Albertans have access to information to help adapt to our changing climate through awareness and strategic changes to homes and vehicles.

But our actions are not enough. We need to partner with the industry and the Alberta government to establish a regulatory framework that drives increased competition and consumer choice, availability of agile and responsive insurance products, and stabilized pricing for insurance products. Alberta has the opportunity to be a Canadian leader and implement an approach to regulation that delivers best outcomes for Albertans and supports a robust insurance industry which fully provides for the needs of tomorrow.

Conclusion

As we stated, insurance is about people not things. We are committed to working with the Alberta government to ensure insurance can be fairly and affordably accessed by all Albertans.

As we look ahead to the future, Albertans will continue to face new challenges brought on by our changing society, technology and weather. We believe that providing rate stability and affordable insurance solutions can be better achieved by:

- Reinforcing an agile, competitive and customer-driven insurance market
- Adjusting trending to more closely reflect current costs and payouts
- Aligning regulation to today's realities for the benefit of all Albertans

We look forward to working with the AIRB to address these important issues that impact customers, employees and all Albertans.



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