AIRB ANNUAL REVIEW

Automobile Insurance Rate Board

Submission on behalf of Intact Financial Corporation

July 2017

INTRODUCTION

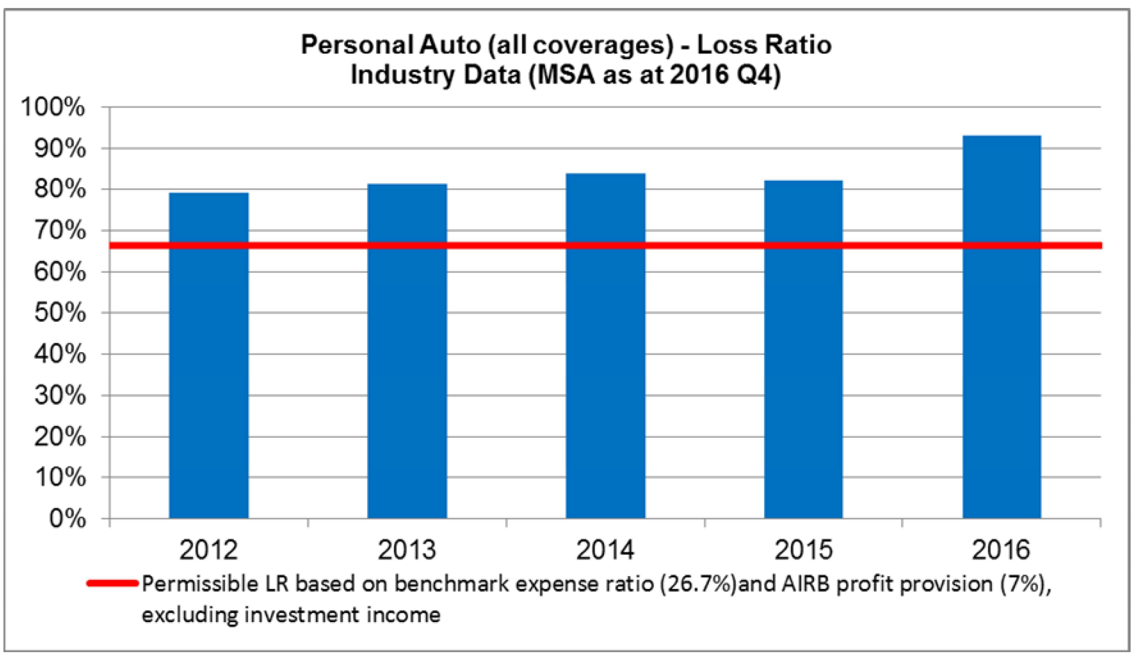
Intact Financial Corporation ("Intact Financial") helps people, businesses and society prosper in good times and be resilient in bad times. With over $1 billion in written premiums in 2016, we are the largest provider of property and casualty insurance in Alberta, offering automobile, property and liability insurance to individuals and businesses through Intact Insurance, Novex Insurance and belairdirect. We employ more than 1,400 people and support over 525,000 customers in Alberta, both directly and through a vast network of 500 brokerages that are active in their respective communities. Automobile insurance is an important segment of our business, making up approximately 65% of our sales in the province.

SUMMARY OF EXPECTATIONS AND CONSIDERATIONS

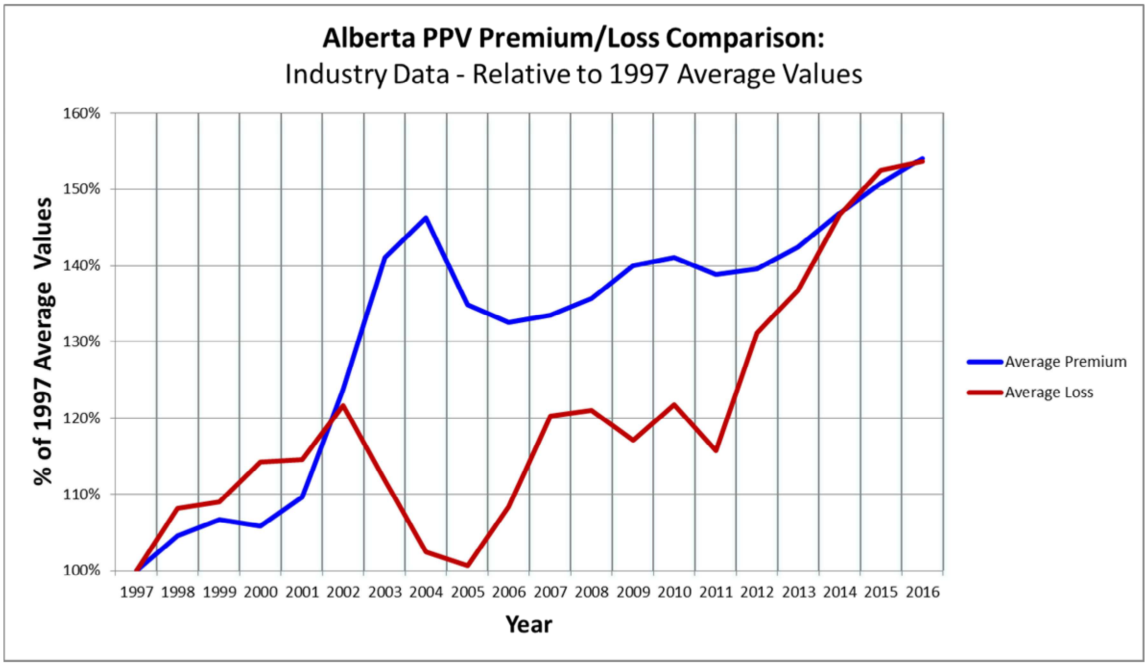
Intact Financial would like to reiterate that a reform of the Minor Injury Regulation ("MIR") is important to ensure an affordable and sustainable automobile insurance product is provided in Alberta.

In 2016, the industry loss ratio was 93%, demonstrating a continued high level of rate inadequacy in Alberta. This loss ratio implies a premium deficiency of around 40% (or $476 per vehicle on average), based on a low interest rate environment, with benchmark profit and expense ratios of 7% and 26.7%, respectively.

In Q1 of 2017, the industry loss ratio remained high at 84%. Given this high premium deficiency, significant premium increases are expected in the short to medium term.



The seriousness of the current level of rate inadequacy is also highlighted by the following graph which shows how industry premiums have responded to changing levels of losses. It is clear that premiums will need to increase to catch up to the rapidly growing losses experienced over the past several years.

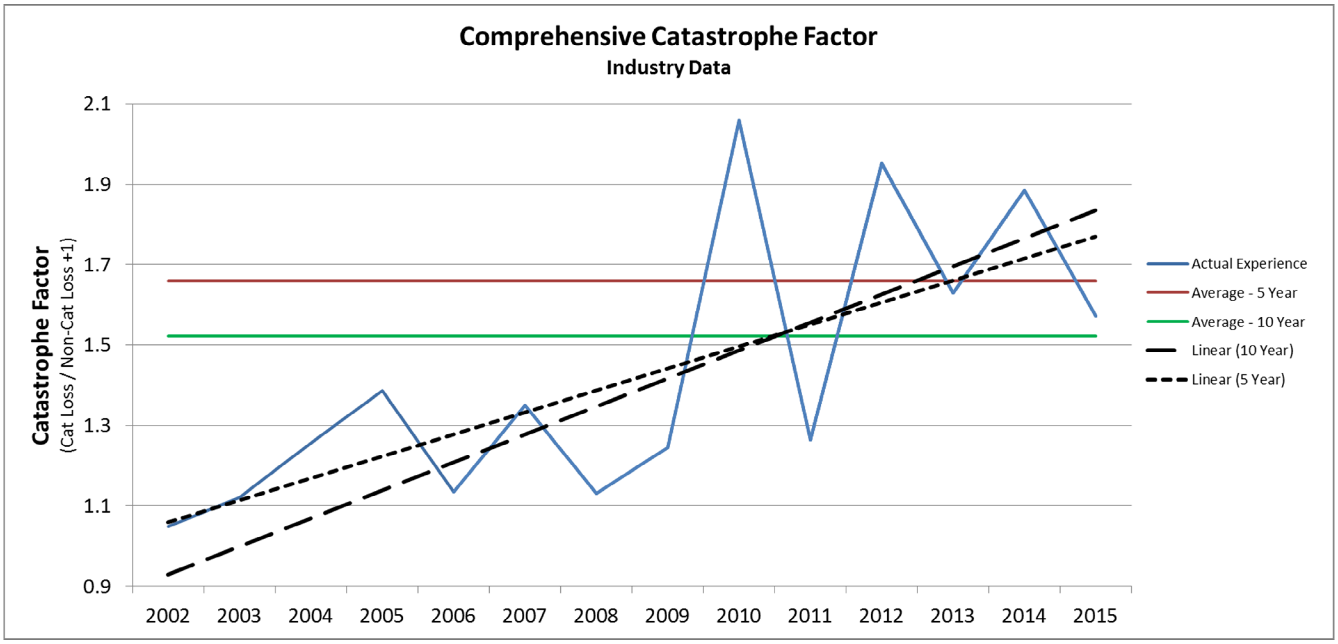


In our submission, we will focus on:

- Catastrophe load
- Loss trends
- Causes for increasing severity of bodily injury claims resulting from increased incidence of claims being settled outside the MIR.

I. Comprehensive Catastrophe Provision

When compared to recent catastrophe experience, we maintain that the 55% catastrophe provision adopted as a benchmark by the AIRB is low. The frequency and severity of these weather-related catastrophic events have increased in recent years and, until proven otherwise, it should be assumed that this trend will continue. The following graph shows how the industry catastrophe factor has trended upwards over the past decade.



We suggest that a provision of 70% is a more appropriate catastrophe assumption, though the 10 year trend line would suggest an even higher loading. Catastrophe losses continued to be high in 2016 with the Fort McMurray wildfires and the significant hail losses. Intact Financial's internal catastrophe factor was over 1.75 in 2016.

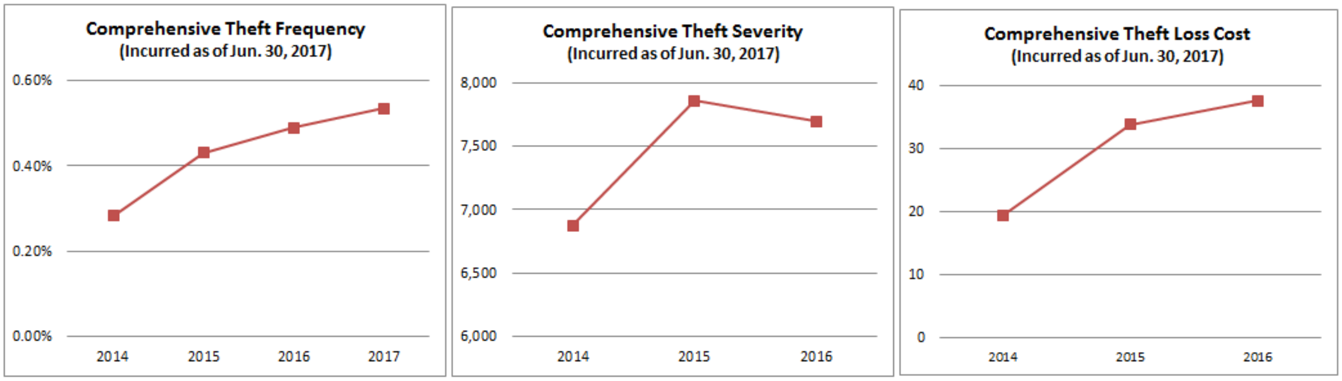
II. Loss Trends

After reviewing Oliver Wyman's report entitled *Annual Review of Industry Experience – Preliminary Report as of December 31, 2016* and analyzing our internal data, we found that our trends were generally consistent with the findings of this report, with the exception of comprehensive and collision coverages.

Comprehensive – Theft

As noted by Oliver Wyman, the industry loss cost for comprehensive - theft has increased significantly since the end of 2014. This is due to large increases in both the frequency and severity of theft claims.

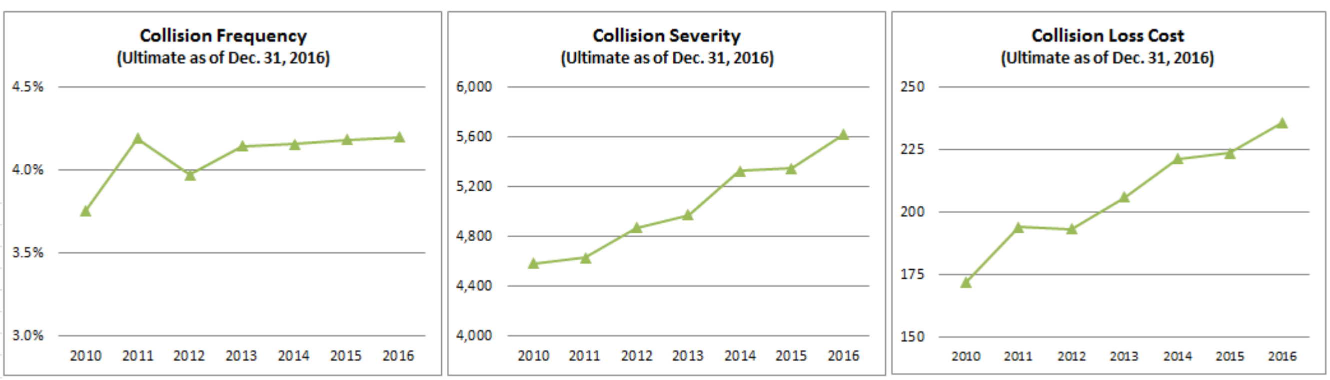
The industry experience is reflective of Intact Financial's experience, as per the graphs below:



Between 2015 and 2016 we have observed an increase in theft loss cost of over 10%. To date in 2017, we continue to see a significant increase in theft frequency. The increase in theft claims is likely associated with the current economic downturn Alberta and as such, we reasonably expect this trend to continue until the economy recovers. Therefore, we believe a future trend of at least +7% for comprehensive loss cost is appropriate (versus the +5% noted in Oliver Wyman's report). This is still conservative given the observed 2015-2016 loss cost increase.

Collision

We have observed a steady increase in collision loss cost over the past several years, as shown in the following graphs:



We have not observed the same flattening in loss cost trend between 2015 and 2016 that Oliver Wyman noted using the industry data. Instead, we have found that collision loss cost increased by +5.1%, driven mainly by an increase in severity in 2016 that continued a fairly steady trend upwards in loss cost since 2010.

We suggest that the +2% collision loss trend selected by Oliver Wyman may be overly sensitive to the sharp decline in 2016-1, which appears to be an outlier rather than the start of a trend. As noted by Oliver Wyman, the snow precipitation level measured at the Edmonton and Calgary airports during the first half of 2016 was the lowest recorded level for the first half of a year since at least 1995, and was around 70% below average. This is in contrast to the first half of 2017 when snow precipitation rebounded to roughly double that of the first half of 2016[1]. Intact's position is that the more severe winter conditions experienced in the first half of 2017 are more representative of expected conditions in the future. With this in mind, we believe a collision loss cost trend closer to +3% may be more appropriate.

Third Party Liability – Bodily Injury ("TPL BI")

Recognizing the rising costs of TPL BI costs, we agree with the future trend selection of +7.75% as noted by Oliver Wyman and the AIRB. This trend poses affordability risks for automobile insurance in Alberta and as such, reinforces the need for legislative reform to reverse the observed trends.

For all coverages combined, the future loss trends selected by Oliver Wyman would add an extra 4.9% per year (or $58 per vehicle on average) in the future. This is in addition to the current 40% (or $476 per vehicle on average) premium deficiency, based on 2016 industry results mentioned on page 1.

III. Causes for increasing severity of bodily injury claims

Following the Court of Queen's Bench Sparrowhawk decision, the behaviours we highlighted in our last submission have continued in recent months. This decision interpreted the scope of the MIR narrowly. If a motorist suffers from an injury that is not a sprain, strain or WAD I or II, the cap does not apply. Furthermore, if an injury is affecting a person for more than 6 months, it can be deemed chronic and is also outside the cap. This interpretation was confirmed in another decision of the Court of Queen's Bench in McLean v. Parmar.

As a result of this narrow interpretation of the MIR, we continue to experience an evolving presentation of injuries by plaintiff counsel arguing that their clients are suffering from multiple and/or chronic injuries that are not covered by the MIR.

Since 2012, we have observed an approximate 20% increase in the occurrence of bodily injury claims presented with chronic pain, head injuries (concussions, headaches, etc.) and/or psychological conditions such as post-traumatic stress disorder. We have also seen an increase in claims involving temporomandibular joint dysfunction ("TMD") with chronic pain often as the overriding issue.

This has influenced the pursuit of general damage awards, in addition to other heads of damages, i.e. loss of future income, housekeeping, etc. In addition, this strategy often keeps claims open longer, increasing pressure on BI and Accident Benefits coverage as injured motorists are encouraged to seek treatment to evidence their injuries. This issue is aggravated by an overly generous pre-judgement interest ("PJI") rate environment. We will comment on the PJI issue later in the submission.

[1] Based on average of data collected at Calgary, Edmonton, and Peace River airports.

In addition, the current Certified Examiner ("CE") process is adding upward pressure on bodily injury coverage. When the MIR was introduced, the CE process was expected to be used by insurers to settle more claims more efficiently by determining the nature of the injury. According to the MIR, the opinion of the CE is sufficient evidence that the injury is or is not minor. In other terms, it is supposed to be sufficient evidence unless rebutted.

In the last few years, we have seen a significant erosion of the value of this process; in addition to the time required to deliberate the nature of injury and the CE (particularly if disagreements arise), certified examinations usually take place in the months following the accident. With more allegations of chronic pain affecting claimants over a long period of time, the relevance of these examinations is greatly diminished. If a claimant can prove that he/she has continued experiencing pain and/or other symptoms for months or years after the examination, either by producing a medical expert and/or medical records, the courts will tend to conclude that the opinion of the CE is rebutted and the injury is not minor. This is often by way of subjective self-reporting of continued pain.

PJI awards are another source of cost pressure for bodily injury claims. PJI is meant to compensate for the loss of use of money and not as a punishment on the at-fault party. Since 1984, the PJI rate has been set at 4%, which is nearly 3% higher than the current bank rate. This increases claims costs and provides an incentive to keep files open longer. In January 2015, Ontario passed legislation linking the PJI rate to the bank rate in the province (currently at .8%). By following the fluctuations in the bank rate, the PJI appropriately compensates for the loss of use of money. If a similar change were introduced in Alberta, we estimate savings on BI loss costs to be around 6.0% annually. While more will be required to reform the automobile product and claims procedures in Alberta, a reduction in the PJI interest rate to reflect today's interest rate environment will almost immediately improve the affordability of automobile insurance in the province. We also feel such a change will appeal to the logic and intuition of all industry stakeholders.

The ongoing changing dynamics of bodily injury claims is not only adding indemnity pressure, but also additional claims handling expenses as we continue to manage bodily injury claims relative to the original intent of the MIR.

Intact Financial is actively involved in the current regulations review and presented these arguments to the Superintendent of Insurance in August last year.

CONCLUSION

As you embark on your review process, we respectfully request that the Board:

- Reflect recent weather related events by adopting a 70% catastrophe provision;
- Adopt a comprehensive future loss trend benchmark of at least +7% to reflect that comprehensive claims costs are increasing due to the downturn in the Alberta economy;
- Adopt a collision future loss trend benchmark of at least +3% to avoid too much sensitivity to data outliers; and,
- Support legislative reform to reverse the high BI loss trend that is currently at +7.75% based on Oliver Wyman's latest analysis.