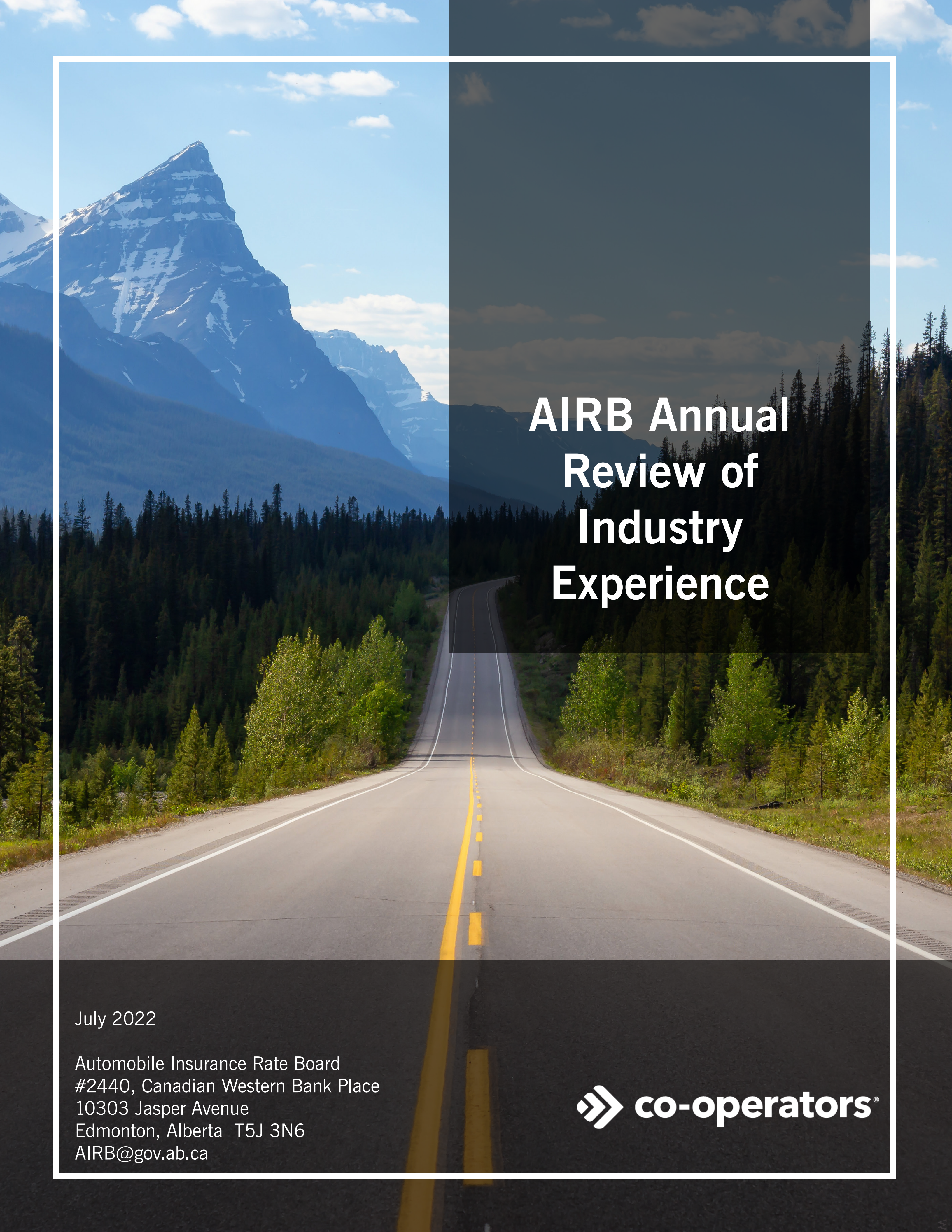

AIRB Annual Review of Industry Experience

July 2022

Automobile Insurance Rate Board
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co-operators

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INTRODUCTION

The Co-operators Group Limited (“Co-operators”) is a leading Canadian, diversified, integrated, multi-line insurance and financial services organization. As a co-operative, our 46 members include co-operatives and credit union centrals representing a combined membership of millions of Canadians. Operating in Alberta, we have 10 member organizations, including the Alberta Federation of Agriculture, the Federation of Alberta Gas Co-ops Ltd., and UFA Co-operative Ltd.

We have a strong footprint in Alberta, insuring approximately 261,000 private passenger vehicles and 57,000 commercial vehicles across our group of companies, ranking fourth in market share by direct written premium. We employ over 680 staff in addition to having independent distribution contracts with 95 financial advisors who in turn operate their own agencies, employing over 500 staff across 126 offices. Guided by our co-operative principles, we are committed to the communities in which we work and, in 2021, we invested over $567,000 in various charities, non-profits and co-operatives throughout the province.

We are proud to provide insurance and financial services to more than two million Canadians. We take even more pride providing financial security to these Canadians and their communities while staying true to our co-operative values.

Co-operators is pleased to participate in the Automobile Insurance Rate Board’s (AIRB) annual review of industry experience for private passenger vehicles (PPV) again in 2022, which provides us with the opportunity to share feedback in response to Oliver Wyman’s industry loss experience analysis.

We commend the AIRB for continuing to modernize rate regulation in Alberta with transparency and through collaboration, specifically the transition to a more principles-based approach. We are pleased with the recent amendments to the filing guidelines for both PPV and other than PPV, which expand the opportunities for insurers to utilize the file-and-use filing guidelines. These changes are positive for Albertans because the reduction of regulatory red tape creates a more responsive and competitive market and they support the accessibility of the product and sustainability of the industry. Additionally, the framework allows the AIRB to maintain significant oversight, ensuring all rating programs are evidence based. Lastly, with respect to the filing guidelines, combining the prior approval and file-and-use filings into one comprehensive guideline is also a step forward given the improved clarity and, therefore, efficiency.

We look forward to continued collaboration with the AIRB on additional rate regulation items that benefit both parties and, more importantly, Alberta drivers.

FINANCIAL CONTEXT & OUTLOOK

After several challenging years, there is a favourable outlook for the sustainability of the Alberta automobile insurance market in the short term. The expiry of the second rate cap in 2019 and the rate increases approved by the AIRB shortly thereafter were catalysts for the turnaround. Additionally, the COVID-19 pandemic impacted profitability significantly in both 2020 and 2021. Government lockdowns and other protective measures, along with personal responses to the pandemic in general, influenced a change in driving habits and behaviour and led to impactful reductions in vehicle collision frequency.

Many Canadians refer to the current period as “post pandemic” and are living as such but new variants, as well as new vaccines, remain in the conversation as we approach the fall and winter seasons once again. In the workforce, many organizations have invited their employees to return to physical office locations. However, new employee preferences identified during the pandemic, the current competition for talent and other factors are adding complexity as many insurers attempt to define the “new normal”. Adding to the complex environment, our country is experiencing economic pressures from persistent supply issues, labour shortages and historic inflation. In short, there is a significant amount of uncertainty both in the near future and beyond. It is important for the AIRB, insurers and industry partners to continue their open communication to identify new and emerging trends. The uncertainty underscores the expansion of file-and-use filings as a significant and positive step. Insurers have a tool to adjust rates, as needed, more responsively ensuring accessibility and sustainability of the product. Provided these tools remain in place, the recent challenges faced by the automobile insurance industry in Alberta are likely to be avoided.

Albertans must carry mandatory coverages for automobile insurance, so the affordability of the product also remains a top priority. **We believe there is an opportunity to achieve more affordable premiums through comprehensive product reform and, if that opportunity is not pursued, we are concerned rates will continue to increase**. Recent rate regulation changes have paved the way to more equitable premiums, and the pandemic has likely changed driving behaviour and habits moving forward, but product reform is required to lower average premiums more permanently. We encourage the AIRB to advocate with Co-operators for these product reform changes.

REVIEW OF INDUSTRY BENCHMARKS

LOSS TRENDS

Bodily Injury

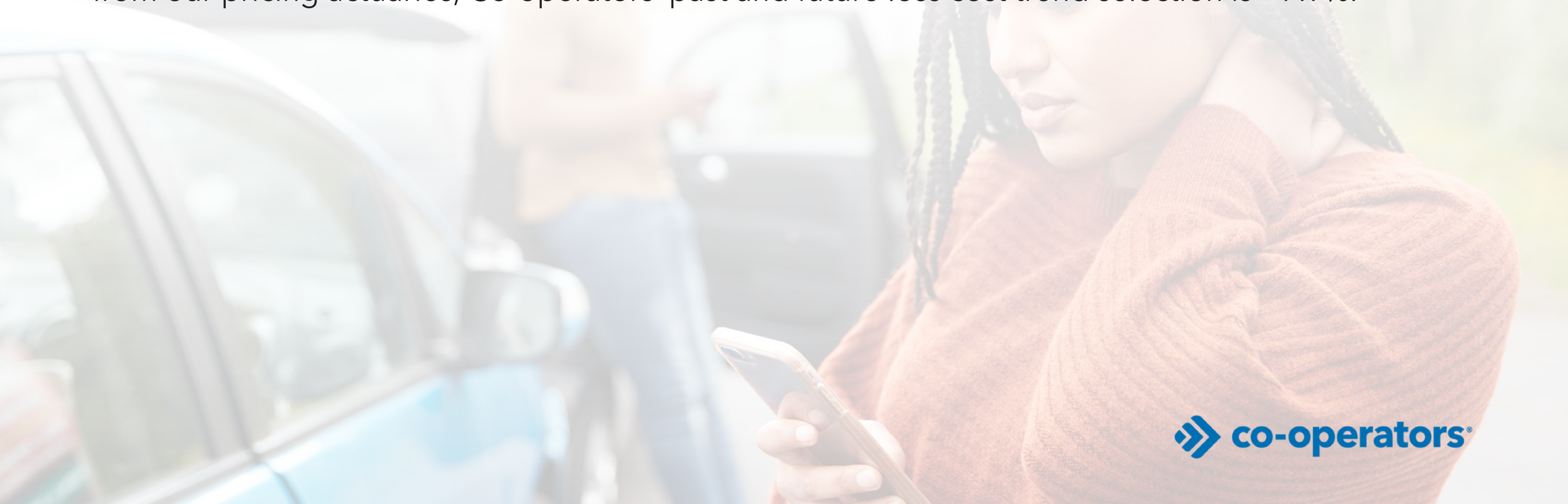
For Bodily Injury (BI) coverage, we observe that the analysis and commentary from Oliver Wyman's 2022 preliminary report is relatively unchanged from their 2021 Annual Review Report. A preliminary past loss cost trend of +7.0% has been selected, which appears to be the average of four separate indicated loss cost trends. Each of these indicated trends use the same end period (2019.75) with four different starting periods ranging from 2014.75 to 2016.25. Notably, these are the four shortest periods from Oliver Wyman's loss cost analysis. Oliver Wyman notes in their preliminary report they considered estimated loss cost trends, rather than making selections directly from the frequency and severity trends, due to GISA reporting issues that "increase the uncertainty associated with (their) ultimate claim amounts and claim counts." The loss development data is, of course, the primary input into the loss trend analysis. Oliver Wyman also notes in their report, with respect to their loss cost analysis, that "since 2017, (they) observe early signs of a slight flattening and large decrease during 2020 and 2021 coincident with the COVID-19 pandemic." The observations from these two years, 2020 and 2021, were excluded from the indicated loss cost trends considered for their selections. Consistent with their approach from last year's annual review, Oliver Wyman selected a future loss cost trend 2% lower than their past loss cost trend, at +5%. However, they repeat that "uncertainties related to ultimate claim amounts – particularly for more recent accident years" render "the selection of the future loss trend rate more challenging".

Co-operators' pricing actuaries analyze frequency, severity, and loss cost trends separately, using Co-operators' internal data only, prior to making trend selections. We are not impacted by the claims amount and claims count challenges from the GISA data discussed by Oliver Wyman, which allows us to evaluate the individual components of the loss cost first. Additionally, if we modify our claims handling and/or reserving practices, the knowledge of our data combined with the available expertise from our Claims and Reserving teams, equips us to make appropriate adjustments. Following our most recent loss trend analysis, we selected past frequency and severity trends from 10 years of data, excluding 2020 and 2021. These individual selections resulted in a loss cost trend of +7.9%. Upon review of our internal data, we did not observe a flattening of the loss cost curve starting at 2017, so there is no evidence to suggest our future loss cost trend selection should be lower than our past loss cost trend selection.

We appreciate the transparency within Oliver Wyman's preliminary report and commend their consistently professional work. That said, we do not agree with their BI loss cost trend selections, past or future. The slight flattening of the loss cost curve starting in 2017 is visible from the industry data, in the third image of Figure 9 from the report, but there were no significant external environment events (i.e. reform) between 2014.75 and 2016.25 to justify the selection from a shorter period. From both our internal data and the industry data, there are no other observations supporting the selection of an indicated loss cost trend from a period shorter than 10 years. The flattening of the curve is not observed in our internal data and we believe the shorter period is overly responsive for a long-tailed coverage like BI. From the BI Loss Cost Heatmap provided by Oliver Wyman as Figure 12 in their report, it is our position that a past loss cost trend at or above +8.2% is more appropriate because it relies on a longer period and is supported by higher adjusted R-squared values. A selection at this level aligns more closely with our selection of +7.9% and achieves the balance between responsiveness and stability.

At this time, we do not believe there are external changes that support a future loss cost trend selection below the past loss cost trend selection. There is no evidence that the number of minor injuries pushed outside of the cap is stabilizing over the last few years and we continue to experience an increase in the number of claimants with legal representation. As we noted in our previous two annual review written submissions, although the changes to the minor injury regulation wording in 2018 and Bill 41 were important steps, it will take years before we can assess whether there has been a resulting reduction in BI loss costs given the long-tailed nature of BI claims. This remains our position. With respect to Bill 41 the *Insurance (Enhancing Driver Affordability and Care) Amendment Act, 2020* we agree with Oliver Wyman that there is insufficient claims experience at this point to update the expected cost impact with these changes. Insurers are unlikely to realize any benefits from a loss cost perspective until at least 2024. Additionally, also noted by Oliver Wyman, the COVID-19 pandemic may create an additional time lag before an accurate measure of changes from Bill 41 can be completed.

BI is a long-tailed coverage and loss cost trend selections should strike a balance between responsiveness and stability, which is why we believe BI loss trend selections based on 10 years of data are most appropriate in most situations. There should also be sound evidence to support future trend selections that differ from one's past trend selections, otherwise the two selections should be aligned. Based on Figure 12 from Oliver Wyman's preliminary report and the reasons presented in this section, we believe the past and future loss cost trend selections from the industry analysis should both be +8.2% at a minimum. Using Co-operators' internal data and the analysis from our pricing actuaries, Co-operators' past and future loss cost trend selection is +7.9%.



Accident Benefits

In both the industry data and Co-operators' internal data, there is a steep upward trend or increase in the Accident Benefits (AB) severity trend and loss cost trend beginning in 2015 or 2016. The increase starts slightly later in our internal data, which is likely a dataset or mix of business difference, but the patterns are similar. We've identified the likely drivers of this upward trend. Similar to BI, we are observing increased legal involvement on AB claims. The retroactive reform changes effective November 2020, also noted in Oliver Wyman's report, are most certainly leading to the increasing severity. Additionally, cycle times (i.e. the time it takes to cycle through a claim, from the initial report until the claim is closed) began to increase in 2020 and 2021. We observed the start of this pattern pre-reform and then the pattern emerged more clearly following the reform, combined with the impacts of the COVID-19 pandemic.

Our observations of the AB frequency, severity and loss costs trends are reasonably consistent with those shared by Oliver Wyman and, as a result, we support Oliver Wyman's preliminary loss cost trend rate selection of +12.0% beginning January 1, 2015.

Collision

Record inflation and persistent supply chain issues are among the hot topics facing our industry today and we are monitoring both from an automobile insurance physical damage perspective. With new car production slowing for an extended period, and car lots sitting with far less than capacity as a result, there has been inflation on total losses. From our internal, country-wide data, we have seen significant growth on total loss amounts the last three quarters and are confident this growth applies to Alberta specifically as well. A trusted industry partner with additional access to industry data has confirmed for us the significant growth in total loss actual cash value payments over the last couple of years. We have also experienced an increase in cycle time on repairs due to delays with parts supplied. Consequently, our policyholders need their rental vehicles for longer periods. Our preferred rental vehicle provider has shared related data with us, which confirms this impact for Co-operators as well as the industry overall. We expect these two phenomena, the inflation on total losses and the increased cycle time on repairs, to be temporary. As new car production continues to grow and inventory levels return to a normal level, we expect to see a reduction in rental vehicle costs and an associated reduction in actual cash value estimates on total losses.

In addition to the inflation on total losses, we are also experiencing inflation on vehicle replacement parts. We have not specifically quantified the amount of the inflationary increase but, relying on high-level comparisons, can confidently state that it is not as significant as the inflation experienced on some property lines of business. At some point in the future, without speculating on the specific timing, we expect the parts inflation to level out but we do not believe the cost of vehicle parts will retreat to prior levels.

Within our Collision loss cost trend analysis to date, similar to Oliver Wyman's analysis, we have not made adjustments to our models or selections to account for economic conditions; specifically, the effect of inflation. This allows us to compare our preliminary loss cost trend selection with those from Oliver Wyman's report and we have confirmed they are consistent. We will continue to monitor inflation, and its impact on physical damage severity, and will reconsider the need for inflationary adjustments within our loss trend analysis on an ongoing basis.

We support Oliver Wyman's preliminary loss cost trend rate selections for the Collision coverage.

THEFT CLAIMS

The AIRB's website notes that Alberta has the highest incidence of vehicle theft in all of Canada and this number continues to increase. From 2017 to 2019, Co-operators General Insurance Company spent over $1.2M per month in auto theft losses, and then in the first quarter of 2020, we experienced the largest number of first quarter auto theft claims over the four previous years. From the second quarter of 2020 forward however, during the COVID-19 pandemic specifically, our auto theft loss counts dropped significantly from 2019 levels. We believe this was a pandemic effect, a result of Albertans staying home more and therefore driving less. With the province open and "return-to-office" programs in flight for many employers, we have not observed an increase in vehicle thefts yet.

Presently, there is no deductible on auto theft claims for policyholders in Alberta. We continue to recommend that the comprehensive deductible should apply to claims for theft of the entire vehicle to provide policyholders more financial incentive to prevent vehicle theft. We also support regulatory action to prevent fraudulent registration of stolen vehicles.

APPLICATION OF INDUSTRY BENCHMARKS

We appreciate the opportunity to participate in the AIRB's annual review process and acknowledge the amount of work to prepare the preliminary report, to gather and incorporate industry feedback and to host the open meeting. The industry benchmarks are an important tool for all insurers and their pricing actuaries. For larger insurers such as Co-operators, the Annual Review Report and the benchmarks offer another qualified point-of-view that may challenge an actuary's thinking or confirm what the actuary is observing in their internal data and/or their selections. In some cases, with the proper rationale, it may be appropriate for the pricing actuary to adopt an industry benchmark as an input into their rate level indication.

That said, when an actuary's internal data is sufficiently or fully credible, we encourage the AIRB to continue to allow the actuary to rely on that internal data and apply the selections or inputs derived from that data within the rate level indication calculation. An actuary has intimate knowledge of their internal data, they have access to the insurer's internal experts to explain shifts or anomalies in the data and they partner with qualified internal personnel who make appropriate adjustments to the data or analysis as needed prior to the pricing actuary's selection. Additionally, internal data reflects the mix of business of the insurer, which may be different or poorly represented by the industry data. It is our position that a qualified actuary should be given the flexibility to determine the appropriate dataset and to make selections for the rate level indication calculation. This represents the spirit of principles-based regulation.

CONCLUDING COMMENTS

We have reviewed Oliver Wyman's proposed methodology to adjust for the pandemic period within the rate level indications and we are aligned with this methodology. To be more precise, the effects of the COVID-19 pandemic must be removed from 2020 and 2021 data and then all years in the experience period should be adjusted to reflect the expected "new normal." The timing of the shift to the "new normal" is an important input to this methodology and we continue to actively monitor our data to identify this timing, which is likely to be gradual. Given rate level indications are sensitive to loss trend selections, we believe these selections must continue to balance stability and responsiveness as the shift towards the "new normal" occurs.

We would like to thank the AIRB for allowing Co-operators, and our industry peers, to provide written submissions in response to Oliver Wyman's preliminary report. We look forward to more opportunities to work collaboratively with the AIRB along its transition to a more principles-based approach and as additional rate regulation amendments are considered. **We are aligned with the AIRB in that all solutions must provide Alberta drivers with an accessible, affordable and equitably priced automobile insurance product — a product that provides security, is simple to understand and meets their needs**.

As noted in previous years, we are not members of the Insurance Bureau of Canada (IBC) and prefer to contribute to the policy development process directly. As a co-operative financial services organization, we believe we bring a unique perspective to public policy consultations.

If you have any questions or require clarification with respect to any of the topics in this written submission, please do not hesitate to contact me at **todd_saunders@cooperators.ca**.

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Co-operators