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Ms. Laurie Balfour  
Executive Director, Automobile Insurance Rate Board  
#2440 Canadian Western Place  
10303 Jasper Avenue  
Edmonton, AB T5J 3N6

**RE: AIRB 2023 Annual Review**

Dear Ms. Balfour;

Thank you for the opportunity to participate in the Automobile Insurance Rate Board's (AIRB) annual review of auto insurance trends and rates for basic and additional coverage. We will provide our view on Oliver Wyman's (OW) selected trends including the impact of inflation and the 2020 reforms on the trends.

After several years of dynamic changes of how people live, work, and drive, as well as significant macro-economic factors such as inflation, we are not yet in a place to define a "new normal". The past will not be a reliable indicator of the future so it will be important for the AIRB to look beyond past trends and indications, give more weight to insurers' actuaries and be forward looking. There are still uncertainties about inflation, the impact of reforms and individual insurers will have different claim experience. There is no one-size-fits-all approach. Companies should integrate actuarial adjustments into their projections, tailoring to their claim experience. AIRB should consider the approval of filings based on their reasonableness and not only OW's suggestions.

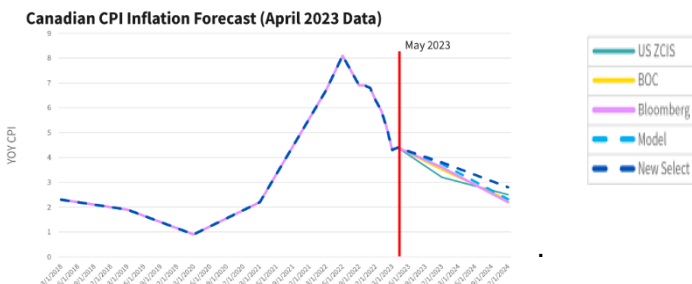
**Oliver Wyman's Loss Costs Trends**

Aviva agrees with Oliver Wyman's 2022-2 Industry loss trends selection and believes that these are appropriate at the aggregate level. We were pleased that OW acknowledged the significant increase in Property Damage and Collision severity that occurred in 2021 and the need to adjust historical accident years (2021-2 and before) to account for elevated inflation.

Claim inflation shock is expected to persist until at least 2024, so adjustment for elevated inflation is also needed for the initial years following late 2021.

We do not agree with Oliver Wyman that 2022-2 frequency is a “new normal”. It may be the start of a new normal but the 2022-2 frequency alone is not reliable enough to conclude we are at a “new normal”. More time is needed to determine a “new normal”.

## Inflation



Inflation is likely to be structurally higher over the longer term. We are unlikely to return to pre-pandemic levels of inflation anytime soon. As can be seen in the graph, experts predict that inflation will continue to be above 3% through 2024.

Inflation affects many aspects of insurer’s operation. Any premium growth will be offset by inflation-driven increases in claims costs. Rising costs will continue to erode profit margins for insurers that are unable to achieve sufficient rate. Inflation will also drive-up wages as insurers seek talent.

The impact of inflation is already seen in auto physical damage claims. This is driven by more expensive technology in vehicles and supply chain issues which have impacted the availability of parts. Rental vehicle costs have increased with longer repair times. Auto parts and used car inflation are good indicators of Physical Damage inflation. Aviva has been modelling Physical Damage/ Collision claims inflation using the Parts Price and Used Car Prices Indexes. Parts Price inflation continues above 5% which is up from the pre-pandemic inflation rate of 2-3%. Aviva believes that Parts Price Inflation will continue between 5-6% through 2024. Used car inflation increased dramatically during the pandemic but is now declining. Aviva expects it to return to pre-2021 level in 2024.

Wage inflation is both a key predictor for claims cost inflation and impacts claims cost inflation. Wage inflation continues to be high and has not returned to the pre-2021 level. Aviva has been modelling Physical Damage, Collision, Accident Benefits and Bodily Injury claims inflation with Canadian wage data.

Considering the changing inflationary environment, insurers should have flexibility to adopt a different trend for post-2021 or include an inflation adjustment factor for the early periods after 2021.

## Inflation Shock Impact

Insurers’ pricing must also account for the impact of continuing Inflation Shock. (Inflation shock is the difference between the CPI Rate Projection and the normal average CPI in the historical years). Inflation shock represents the increase we expect to see above regular inflation/loss trend. Oliver Wyman estimated a one-time severity increase at 2021-2 for Physical Damage and

Collision. Aviva believes that the impact of inflation shock will continue beyond 2022 and insurers must be able to account for the additional costs in their indications.

Using data and expert opinion, we have estimated the degree to which the inflation shock will impact each coverage on a year-over-year basis.

### Inflation Shock by Coverage (Year-over-Year)

	Baseline	2022	2023	2024	2025	2026
Auto Physical Damage	1.74%	11.50%	2.50%	2.00%	0.75%	0.75%
Auto Accident Benefits	1.80%	2.50%	1.50%	1.00%	0.75%	0.75%
Auto Bodily Injury	2.07%	3.50%	2.00%	1.50%	1.10%	1.10%
Personal Property	1.77%	4.00%	2.00%	1.00%	0.75%	0.75%

The impact of inflation shock on Physical Damage claims costs is 11.5% higher than the regular inflation in 2022. We expect inflation shock to continue but it will start to decline.

The impact of inflation and reforms on Bodily Injury and Accident Benefit claims costs remain uncertain. Bill 41 included a reform to the calculation of pre-judgment interest, which now fluctuates with the interest rate. As current interest rates are high, pre-judgment interest in Bodily Injury claims has increased accordingly. As a result, partly due to pre-judgment interest, Bodily Injury severity has increased in 2022. Aviva agrees with OW that inflationary pressures on health care costs have lagged physical damage. A flexible approach is needed from the AIRB when assessing insurers' projections for Bodily Injury and Accident Benefits severity. We recommend that the AIRB allow room for actuarial judgment and consider adjustments that are backed by additional information or the insurer's data.

## **“New Normal” Claim Frequency Level**

Aviva agrees with OW’s recommended adjustment to historical accident years to reflect the change in claims frequency expected as a result of the reforms and the general shift toward a hybrid workplace. OW considered 2022-2 to be the starting point of the “new normal” and suggests a prospective adjustment to the historical accident years based on the 2022-2’s trended frequency level. Aviva believes that 2022-2 may be a starting point, but it is premature to say that 2022-2 is the new normal. Physical damage claim frequency in 2022-2 is even higher than the pre-pandemic level. Aviva does not believe the increased frequency is due to a shift from collision to DCDP claims. Data suggests that total km driven is increasing despite hybrid work and employers continue to encourage employees to spend more days in the office, which may continue to increase km driven and claim frequency. Lastly, it is still too early to conclude the full impact of reforms on frequency. The AIRB should recognize the limitations of relying solely on the 2022-2 frequency level and allow insurers to apply actuarial judgment which draws upon ongoing trends, vehicle usage patterns, economic factors, driving behaviour expectations etc.

## **Auto Theft Crisis**

Auto theft has hit crisis levels across Canada. Theft claims frequency and severity have increased significantly especially in Ontario due to organized crime. Although Alberta has not experienced the same increase in auto theft as Ontario, the AIRB should be aware of the trend in Ontario particularly as Ontario government clamps down on auto theft. We should watch for criminal organizations to move their operations to other provinces.

Aviva thanks the AIRB for the opportunity to comment and would be pleased to answer any questions arising from this submission.

Yours very truly,

**Aviva Canada Inc.**

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