CANADIAN DIRECT INSURANCE
Canadian Western Bank Group

IN THE MATTER OF
THE *UTILITIES COMMISSION ACT*
R.S.B.C. 1996, Chapter 473, as amended
and the
INSURANCE CORPORATION ACT
R.S.B.C. 1996, Chapter 28, as amended

and

AN APPLICATION BY THE
INSURANCE CORPORATION OF BRITISH COLUMBIA ("ICBC")
FOR APPROVAL OF REVENUE REQUIREMENTS FOR
UNIVERSAL COMPULSORY AUTOMOBILE INSURANCE
FOR THE POLICY YEAR COMMENCING NOVEMBER 1, 2013

and

FOR APPROVAL OF A NEW BASIC INSURANCE
CAPITAL MANAGEMENT PLAN

SUBMISSIONS OF

CANADIAN DIRECT INSURANCE INC.

March 6, 2014

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MANAGEMENT PLAN

WRITTEN FINAL ARGUMENT OF

CANADIAN DIRECT INSURANCE INC.

A. INTRODUCTION

1. Canadian Direct Insurance ("CDI") is an intervener on the application filed by the Insurance Corporation of British Columbia ("ICBC") on August 30, 2013 in respect of its 2013 revenue requirements for Universal Compulsory Automobile Insurance and the proposed New Basic Insurance Capital Management Plan. These submissions address the two components of the rate indication: Chapter 3, Actuarial Rate Level Indication Analysis and Chapter 4, The New Basic Capital Management Plan for the Rate Smoothing Framework of ICBC's application.

2. CDI's submission, discussed in more detail below, is summarized as follows:

(a) This Panel should be cautious in approving the rate increase sought by ICBC.

(b) As required, ICBC prepared its application based upon the information available as at May, 31 (and/or June 30) 2013. That application makes certain assumptions regarding trends and increases.

(c) Despite ICBC's "gloom and doom" Application, and the negative testimony at the hearing, the evidence put forward has established that ICBC's "Minimum Capital Test ("MCT") was at 129% as at September 30, 2013. ICBC has undertaken to provide the Panel with the MCT as of December 31, 2013.

Transcript Ref. Volume 5, p. 676, Line 5

(d) For the reasons set out below, it is submitted that ICBC's future projections, as contained in the Application, should be scrutinized very carefully.

B. 2013 REVENUE REQUIREMENTS FOR BASIC INSURANCE: INTRODUCTORY COMMENTS

3. On August 16, 2012, the Commission granted ICBC an increase of 11.2% in ICBC's Basic insurance rate for PY 2012, commencing February 1, 2012.

4. This increase in ICBC's Basic Insurance rate was the first it had applied for since PY 2007. The 2007 application resulted in a 3.3% rate increase.

5. Special Direction IC2 directs the Commission to ensure that increases or decreases in Basic insurance rates are phased in in such a way that these rates remain relatively stable and predictable.

Special Direction IC2, BC Reg. 307/2004 as amended, S. 3(e)

6. In its current application, ICBC notes that the indicated rate change for PY 2013 would be 11.5% to cover its costs and to make up a basic insurance revenue deficiency of $266,697,000, but for Special Direction IC2 and the 2013 government directive which requires, for rate smoothing purposes, that the Loss Cost Forecast Variance be excluded when arriving at the indicated rate change for PY 2013.

Exhibit B-1, Chapter 3, Figure 3.2, and paras. 12 and 13, pps. 3-4 and 3-5

7. In essence, what ICBC is saying is that its costs have risen for PYs 2012 and 2013 to such an extent that a cumulative rate change for the two year period would have amounted to an increase of +22.7% but for the government directive mandating that the PY 2012 Lost Cost Forecast Variance, which had a +6.6% impact on costs, be excluded from the PY 2013 indicated rate change.

8. It is submitted that the proposed rate increase of 4.9% for PY 2013 taken with the rate increase of 11.2% for PY 2012 exceeds the allowable rate fluctuation warranted under the concept recognized by all parties of relative rate stability and predictability.

C. ACTUARIAL RATE LEVEL INDICATION ANALYSIS (CHAPTER 3)

9. The two components which comprise the bulk of the PY 2013 indicated rate change of 11.5% are PY 2012 Lost Cost Forecast Variance of +6.6 percentage points and Loss Trend to PY 2013 of +4.4 percentage points for a total of +11.0 percentage points. We know, however, that for the PY 2012 rate application, the total of those two components was 7.4 percentage points.

Exhibit B-1, Chapter 3, p. 3.4, Figure 3.2

See Exhibit B-1, Chapter 3, p. 3.3, Figure 3.2 of 2012 ICBC Rate Application (PY 2012 indicated rate change)

(i) <u>PY 2012 Loss Cost Forecast Variance</u>

10. As in ICBC's projections for PY 2012 (a Loss Trend to PY 2012 of +1.9% was forecast and now the Loss Trend forecast for PY 2013 is +4.4%), ICBC seems to have difficulty in forecasting its claims experience for the following policy year. This is borne out by its comment that this forecast is "due to higher than expected emergence of BI claims frequency" and that benefits, rehabilitation frequency and severities have emerged higher than expected.

11. Following on that point ICBC, in Chapter 3 of its application and the testimony at the hearing, noted that it had not forecast the increased expenses in the following areas:

    (a) In 2013, ICBC introduced a program to approve insureds for treatments (physiotherapy and massage) on a streamlined basis. As a result of this new program:

        (i) The frequency of insureds using the treatment modalities increased;

        (ii) The amount of money that was spent on each insured's treatment ("medical rehab severity") also increased;

        (iii) The program applied to older claims, as far back as 2008 (not just new claims incurred in 2013)

    (b) ICBC intends to continue to focus on the "proactive management of customers' injuries, it is expected that these costs will continue to

increase...in line with the inflation inherent in the cost of medical treatment and other therapeutic services."

Exhibit B-1, Chapter 3, p. 3-15, para. 40

12. In answer to these claims CDI says:

(a) The fact that Medical Rehabilitation claims frequency and severity increased in 2013 is not at all surprising. It is a direct result of ICBC's decision to switch to the new proactive management structure.

Transcript Ref. Volume 3, p. 471, Lines 4-8

(b) Because the new proactive management structure was introduced in 2013 and back-dated to claims as old as 2008, this would have adversely impacted prior years' severity development and, potentially, frequency. In 2014, the proactive management structure will not be asked, yet again, to pay for treatments incurred due to 2008 accidents. Those claims have been taken care of. Hence, in 2014 the new proactive management structure will only apply to new claims, such that the severity should stabilize.

Transcript Ref. Volume 3, p. 473, Lines 18-23

(c) Since the one-time introduction of the proactive management structure, the severity should now, as compared with PY 2013, stabilize. However, ICBC projects that it will increase.

Exhibit B-1, Chapter 3, Figures 3.9 and 3.10, pps. 3-15 and 3-16

(d) The new proactive management structure was designed to reduce the "representation rate" and to reduce the overall "BI Severity". There is no indication that ICBC has taken the expected reduction in severity into account in its projections.

(e) Paragraph 40 of Chapter 3 closes with the sentence: "The expected increases are in line with the inflation inherent in the cost of medical treatment and other therapeutic services." That statement is patently incorrect. The vast majority of Medical Rehabilitation payments made by ICBC are paid to Physiotherapists, Massage Therapists and Chiropractors. Those payments are made under Part 7 of the Regulations. ICBC's obligation is not subject to inflation. ICBC pays at a prescribed rate. There is no inflation.

Exhibit B-1, Chapter 3, para. 40, p. 3-15

13. We note that ICBC undertook to and did provide the BI Claims Frequency as at the end of 2013. The chart at page 2 of 4 of 2013 RR BCUC.UT.1 indicates that BI Frequency for 2013 was 1.30% which was a drop from 2012 (1.37%). ICBC then adjusts that figure upward to indicate that the correct figure should be 1.35%. However, we note that both of these figures are significantly below the "BI Basic Frequency" figures used in Figure 3.6 of Chapter 3 and Exhibit D.0, para. 13 which show the projected frequency at 1.50%.

Exhibit B-29, 2013 RR BCUC.UT.1, pps. 2 of 4 and 3 of 4
Exhibit B-1, Chapter 3, Figure 3.6, p. 3-12 and Exhibit D.O, p. 4, para. 13

(ii) **Events Impacting BI Frequency**

14. ICBC indicates there have been certain significant developments which have had a favourable impact on BI frequency, those events being safer vehicles, safer roads and an increasing number of drivers in their safest driving years. ICBC then suggests there were other developments that have had an adverse impact on BI frequency. Those developments are the following:

(a) mass adoption of smartphones

(b) fewer new vehicles; and

(c) vehicles per household no longer increasing.

These topics are discussed in order below

(a) Mass Adoption of Smartphones

15. ICBC suggests that the increasing market penetration of smartphones and the percentage of drivers who admit to using such a device when driving, are factors likely to lead to a collision, thus resulting in increased BI frequency as depicted in Figure 3.6. ICBC says the illustration "intuitively supports the logical conclusion" to be reached that the use of smartphones while driving is causing upward pressure on frequency.

Exhibit B-1, Chapter 3, para. 34 and Figure 3.6, pp. 3-11 and 3-12

16. A number of responses by ICBC to BCUC and Intervener Information Requests in the first round of those requests shows that there is no real evidence, merely conjecture, about increasing frequency.

17. For example, in response to BCUC's Information Requests on the use of smartphones, ICBC makes these points:

- statistics on market penetration of smartphones represent the proportion of drivers who could **potentially** use the devices while driving (emphasis added);
- consumers are using smartphones "in increasing numbers in their daily lives";
- "there is consistent and converging evidence that handheld smartphones are being used in vehicles ...".

2013.1 RR BCUC 13.1 to 13.5

2013.1 RR BCUC 14.1 to 14.3

2013.1 RR BCUC 15.1 to 15.2

18. ICBC then, on the basis of some of the above indicators, states that it is "confident that smartphone use is contributing to the upward pressure on frequency" (response to 2013.1 RR BCUC 13.4). Yet at the same time, it casts doubt on this conclusion in responses to other Information Requests. For example:

(i) BCUC 13.4 – "Data on PED [Personal Electronic Devices] use while driving, as well as PED involvement in crashes has indeed been difficult to obtain, particularly for smartphones".

(ii) BCUC 13.5 – "While the reliability of data regarding personal electronic data is so far inconclusive with respect to the effectiveness of BC's distractive driving laws ....";

(iii) CDI 5.3 – "ICBC cannot provide a list of accidents involving the use of a smartphone as it does not have that data in order to do so".

2013.1 RR BCUC 13.4 and 13.5

2013.1 RR CDI 5.3

19. In testimony, it became clear that ICBC does not collect statistics on the number of accidents caused, or contributed to, by smartphone usage.

20. Further, the following exhibits demonstrate that the only available statistics prove that fatalities caused by distracted drivers have declined since 2008. ICBC actually used those statistics in its "Safe Driving" campaign in February, 2014. This hard evidence goes against the "intuitive" statements of ICBC.

Exhibit C2-4 Article "Police Targeting Distracted Drivers in February"

Exhibit C2-5 Paper with Statistics "2008 TO 2012, Motor Vehicle Fatalities in British Columbia: Statistics"

21. It is submitted that there is no specific evidence about the impact on frequency with respect to smartphone use from these responses and testimony, only conjecture and "intuition". While CDI does not, in any way, condone the use of smartphones while driving, it does say that there is no evidence to support ICBC's contentions that smartphones are having an upward effect on frequencies. CDI submits that any increase in rates that is based on ICBC's "intuition" should be removed.

22. It is hard to understand ICBC's assertion at paragraph 26 of its submission that while data linking smartphone use to crashes is not available, there is "ample evidence from police statistics" to conclude distracted driving makes a significant contribution to accidents. The only evidence from police statistics is found in Exhibit C2-5 introduced in evidence by CDI. Table 11 of that exhibit does not support the contention made in paragraph 26 of ICBC's submission.

23. Given ICBC's focus on accepted actuarial practice, CDI questions how such speculation in paragraph 26 of the ICBC submission can qualify as an unbiased best estimate to accord with accepted actuarial practice. (See paragraph 17 of the ICBC submission which indicates "that the estimate of costs must be an unbiased 'best estimate'".)

ICBC final submission of February 25, 2014, pps. 11 & 16, paras. 17 & 26

(b) Fewer New Vehicles

24. ICBC uses one paragraph in Chapter 3 to identify this as a significant event resulting in a flattening of BI frequency as a result of depressed new vehicle sales.

Exhibit B-1, Chapter 3, para. 35 and Figure 3.7, pp. 3-12 and 3-13

25. ICBC refers to a favourable influence trend experienced on BI frequency as a result of safer vehicles in operation before the recession, but says the trend has now been impacted because of fewer sales of new vehicles. However, there is no reference to any evidence put forward to confirm how that favourable influence has been affected by fewer sales.

(c) Vehicles Per Household No Longer Increasing

26. ICBC is not able to make much of an argument to show that no growth in the number of vehicles per household has had a negative (ICBC describes it as a "dampened") effect on BI frequency and the favourable influences listed in paragraph 32.

Exhibit B-1, Chapter 3, p. 3-11, paras. 32 and 33

27. The figure that affects ICBC is the total number of vehicles insured in the Province. BI Basic Frequency is discussed at 2013 RR BCUC.UT.1. However, the table at page 2 of 4 in that undertaking response shows that the total number of policies issued in 2013 increased by 45,000 vehicles over 2012. Similarly, in 2012 there were 40,000 more insured vehicles than in 2011.

2013 RPI BCUC.UT.1, p. 2 of 4

Exhibit B-1, Chapter 3, paras. 33 and 36, Figure 3.8, pp. 3-11 and 3-14

28. The Commission requested evidence to support higher usage per vehicle in a given household to support ICBC's contention on frequency. In response, ICBC admitted that data was not available to provide evidence of such higher usage, but noted it was reasonable to assume this was so. It provided an example of how a vehicle may be driven more, resulting in a greater chance for the vehicle to be in an accident. However, this "intuitive" approach is not supported by any evidence.

2013.1 RR BCUC.17.2

29. Then, in paragraph 37 of Chapter 3, ICBC appears to back off its contention that these three "significant events" or "three new upward forces" (those terms being used in ICBC's submission at paragraph 21) are really impacting BI frequency, noting there is some "softening" impact on BI frequency regarding smartphone adoption with the other two events having "little or no change in their effects on frequency". While this contention regarding the two events is not clearly worded, it is assumed ICBC means these events had no discernible impact or effect on frequency.

Exhibit B-1, Chapter 3, p. 3-14, para. 37

30. In summary, while ICBC refers to these three events as having a significant impact on BI frequency, it cannot offer any evidence or proper data to support its theory. In fact evidence tendered by CDI and referred to in paragraph 20 of this submission suggests otherwise.

(iii) Change in Average Premium

31. At page 3-4 of Chapter 3, Figure 3.2 shows at line 7 that the "Change in Average Premium" is causing a 1% impact for the PY 2013 indicated rate change. That trend is further explained in paragraphs 22 – 24.

Exhibit B-2, Chapter 3, Figure 3.2, p. 3.4 and paras. 22-24, pps. 3-7 and 3-8

32. The fact is that ICBC is charging a lower premium to the vehicle owners in BC, because they are becoming safer drivers. One would therefore expect that claims frequency would continue to decline. ICBC's Application is based upon a "flattening" of the frequency levels. As discussed in paragraph 13 above, ICBC's projection in this regard is questionable.

33. CDI further submits that in any private insurance company, if the overall insured risk was decreasing (due to, for example, drivers becoming more experienced and safer) the insurer, knowing that premiums would be decreasing, would take steps to reduce overall operating costs. It is unclear whether ICBC has made the necessary changes to reflect the decrease in overall premium or whether, in fact, cost allocation issues should be pursued.

D. THE NEW BASIC CAPITAL MANAGEMENT PLAN FOR RATE SMOOTHING FRAMEWORK

34. The Capital Management Target ("CMT") being proposed by ICBC arises from the new rate smoothing framework established by amended *Special Direction IC2* and the 2013 Government directive regarding Rate Smoothing.

35. *Special Direction IC2* provides for CMT to be the total of three components. The first two are the following:

    (i) MCT of 100% as mandated in *Special Direction IC2;*

    (ii) a percentage margin reflecting ICBC's risk profile, which the Commission accepted previously as 30% for an overall MCT of 130%, often described as the solvency target.

36. The third component of the CMT in the Government directive allows for an additional margin to be consistent with relatively stable and predictable Basic rates.

37. The Government directive provides that a revised Basic capital management plan should continue to "protect the solvency of Basic insurance while also improving ICBC's ability to use Basic capital to promote more stable and predictable Basic rates."

Government directive of March 18, 2013 (OIC 153/13)

38. ICBC has chosen an increase of 20% to the target of 130% MCT, such that the new CMT would be 150% MCT.

39. ICBC and its actuary Mr. Weiland agree that based on a recent DCAT analysis, the 130% solvency target continues to be appropriate "given the volatility in the Basic insurance business".

ICBC final Submission of February 25, 2014 p. 60, para. 110

40. ICBC suggests in its submission that there is a "compelling rationale" for the additional 20% of MCT to cover rate smoothing as this increase is needed based on past forecast variances. ICBC suggests the effect of the additional 20% will not constitute a great burden on insureds.

41. At the hearing, Mr. Miller, counsel for the Commission, challenged Ms. Minogue on using an additional 20% for MCT when an additional 10% might well be a sufficient margin for rate smoothing. In her response to that proposition, Ms. Minogue, in her exchange with Mr. Miller, was forced to conclude the following:

> **Ms. Minogue - A**: ".... So it depends on what the risk is and how much capital the Commission wants to have available for smoothing for rate volatility. So I would suggest that there's no one right answer and it really has to do with the Commission's preference ultimately on how much available they want for rate smoothing to smooth through these periods of volatility.

42. Mr. Miller then followed this answer with the following questions on volatility:

> **Mr. Miller - Q**: When we talk about volatility, the last two years have been I guess, some of the worst for lost forecast variance, correct? In years prior to that, you weren't so far off in your estimation.
>
> **Ms. Minogue - A**: That's correct. The flattening of the frequency has created a lot more forecast variance than we've seen.
>
> **Mr. Miller – Q**: So rather than planning for what's being based on the last two years, perhaps an unusual variation in the forecast estimations, why not base it on more historical numbers where you are much closer. Wouldn't that bring us down closer to requirement of only 10 points for rate smoothing, rather than 20?

Ms. Minogue – A: One could do that. However, we don't have alot of historical data points for that. ICBC hasn't set rates for basic alone since its been regulated by the Commission, so that's since 2003. So there is not a lot of data points. What we did do, just for informational --- information request is look at another jurisdiction that similar to B.C., namely Alberta, because they make rates in a tort jurisdiction, and looked at the forecast variance that they have experienced in that jurisdiction and I would suggest to you that even in light of the volatility that we've seen lately, our estimate of 3.4 standard deviation is very reasonable in terms of what one would expect going forward."

Transcript Ref. Vol. 5, p. 692, lines 23-26, p. 693, Lines 1-26 and p. 694, Lines 1-8

43. CDI also notes that despite periods of volatility, ICBC's MCT to Q3 of 2013 was still a solid 129%.

Transcript Ref. Volume 5 p. 676 line 5

44. One further element in ICBC's proposed rate smoothing is to change the current 20 year capital maintenance plan to a 10 year plan running from 2013 to 2023. The current 20 year capital maintenance plan runs from 2006 to 2026.

45. In an Information Request, CDI asked why ICBC was shortening the transition period to a 10 year period when the current 20 year capital maintenance plan was meant to ease the impact on rates.

2013.1 RR CDI.10.3

46. In response, ICBC referred to a response it had filed to a BCUC Information Request seeking an answer to a similar question. The response to BCUC was that the new 10 year transition period was to "maintain similar timing of when the full maintenance provision will be captured in rates". This response acknowledges this new transition period is three years earlier than the prior capital management plan, but would have little impact on the policyholder (less than 0.1% of the indicated rate change).

2013.1 RR BCUC 71.2

47. In response to a request by CDI on the cost impact to a policyholder, ICBC indicated that the cumulative 10 year impact for the proposed change would be an extra $28 per policy, $18 attributable to the capital management plan and $10 attributable to the change in transition period.

2013.1 RR CDI 10.4-6

48. In a followup Information Request, CDI questioned why ICBC could not adhere to the current 20 year capital management plan or was the adoption of the 10 year plan based on convenience. In response, ICBC admitted the rate impact on the two periods and the construct was not easy to explain to or be understood by stakeholders. It suggested this be left to the Commission to decide whether it is worth maintaining "this complex construct" until 2026.

2013.2 RR CDI 1.1-2

49. To comment on all of the above, it is hard to see that the current 20 year plan is any more of a complex construct than the 10 year plan now being proposed by ICBC.

50. And even though ICBC suggests adopting this 10 year plan will have only a minimal impact on the indicated rate change and its impact on premium over 10 years is slight, nevertheless if ICBC is concerned about the cost to its policyholders, wouldn't it stand to reason that it at least keep the balance of the 20 year period in place up to 2026 to provide some relief to policyholders, however small?

E. CONCLUSION

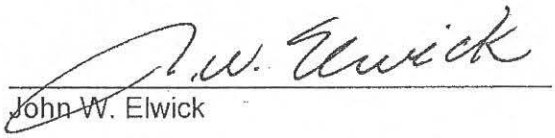
51. While the strictures placed on ICBC by Amended Special Direction IC2 and the 2013 Government Directive on rate smoothing, particularly the exclusion of the loss cost forecast variance, have left ICBC with an indicated rate indication of 4.9%, nevertheless, there are factors that might temper that number to some extent.

52. For example, when calculating the loss trend to policy year 2013 of 4.4%, ICBC places a certain amount of weight on the impact of specific factors affecting frequency, such as the mass adoption of smartphones, the drop in new vehicle sales and the end of growth in the number of vehicles per household to account for no downward trend of frequency. Yet ICBC has had to admit that it does not have solid data on these factors and is relying on intuition. ICBC appears to either have overlooked or ignored the statistics contained in exhibits filed, which are referred to in paragraph 20 of this submission.

53. As to the New Basic Capital Management Plan, it is submitted that there are some areas – using only an additional 10% for rate smoothing and extending the plan's proposed new period for another three years – which would reduce the +0.9% capital maintenance provision in the indicated rate change. The statistics show that ICBC's MCT is not in any danger. However, as ICBC's Corporate MCT has exceeded the 2012 plan of 175%, as noted in the ICBC 2012 Annual Report page 20, it should be questioned as to whether Basic policyholders should incur a premium increase to further build or maintain the capital allocated to Basic, as opposed to government reallocating existing capital to meet the capital requirements ICBC has included in its application.

54. To conclude, for the reasons set out in paragraph 2 of this submission, CDI suggests that careful scrutiny needs to be applied to the facts and projections underpinning ICBC's application for a 4.9% rate increase.

ALL OF WHICH IS RESPECTFULLY SUBMITTED.



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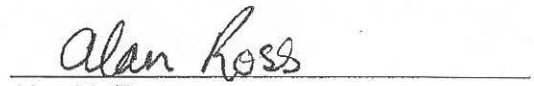

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March 6, 2014