*(9:15 a.m.)*

MR. SAUNDERS, PRESIDING CHAIRMAN: Good morning, Mr. Simpson.

MR. SIMPSON: Good morning.

MR. SAUNDERS, PRESIDING CHAIRMAN: How are you this morning?

MR. SIMPSON: Very well, thank you, Mr. Chairman.

MR. SAUNDERS, PRESIDING CHAIRMAN: Good. Ms. Newman, are you ready to resume or are there any preliminary matters?

MS. NEWMAN: I understand there are no preliminary matters and I am prepared to proceed.

MR. SAUNDERS, PRESIDING CHAIRMAN: Okay.

MS. NEWMAN: Oh, wait now, there are a few things here that we do have to file, I forgot about. Yes, there have been three items that were presented by Facility Association in response to some undertakings yesterday. I have two of them here, one is being re-copied, and what I'll do is just introduce them now and have Mr. Simpson speak to them briefly since I have them here. That would probably be the easiest thing to do. The first item is the Facility Association brochure that was requested yesterday.

MR. SIMPSON: Yes, that's the one we discussed yesterday, yes.

MS. NEWMAN: Okay. That was Undertaking No. 5. The next item is the binder control registry sheet that was requested yesterday as well, I believe, Mr. Simpson.

MR. SIMPSON: Yes. That's the item we discussed yesterday.

MS. NEWMAN: And Undertaking No. 3, I believe. And the other I will deal with when we have the copy.

MR. WHALEN, Q.C.: Sorry, Undertaking?

MR. STAMP, Q.C.: No. 3 for the binder control, was it, Ms. Newman?

MS. NEWMAN: Yes.

MR. STAMP, Q.C.: And No. 6 for the ...

MS. NEWMAN: 5.

MR. STAMP, Q.C.: 5, is it?

MS. NEWMAN: 5 for the brochure.

MR. STAMP, Q.C.: Brochure.

MR. WHALEN, Q.C.: I wonder if we could get a copy of No. 3? I think ...

MS. NEWMAN: Are you going to circulate those now? The Clerk will circulate those now.

MR. WHALEN, Q.C.: We don't, but I've given copies to other counsel but I've given them, I didn't keep any for us, so. I thought we had extras. I just have one of these, so, and I just need the back one. That's good, thank you.

MR. SAUNDERS, PRESIDING CHAIRMAN: So the brochure is Undertaking No. 5?

MS. NEWMAN: Yes.

MR. SAUNDERS, PRESIDING CHAIRMAN: And the other document we have is Undertaking No. 3?

MS. NEWMAN: 3. Good morning, Mr. Simpson. I guess we'll get started here. I have three or four major headings that I'm going to go through today and ask you questions on. The first is the structure of the industry. I think your counsel indicated to you that somebody may wish to take you into more detail on how Facility interacts with the servicing carriers and the brokers and such, so I'll ask you a few questions about that. I've got one or two general questions on the application itself and then some specifics on particular aspects of the application, not too much there, and finally on the implementation, a few questions there. I hope to be finished by break time, so we'll give it our best shot.

MR. SIMPSON: Alright, thank you.

MS. NEWMAN: So I guess the starting point for me is to sort out how the various aspects of the industry interact, and you went through some detail on how Facility Association operates. I wonder if you could maybe give us your understanding of what the role of

Facility Association is vis-a-vis the brokers and the servicing carriers, and I'll give you some idea of the level of detail that I'm looking for. I'm wondering how the money progresses through this system, I'm wondering how the risk progresses through this system, who pays expenses, you know, the premium tax and the health levy, those sorts of things, so that we get an idea of how it all interacts. I understand that you are only one piece of the puzzle but so is everybody else, so if we could have your understanding of it to the best of your ability, I'd appreciate it.

MR. SIMPSON: Yeah, I'll do my best and I'm not a finance or an accounting person so how all the money flows through, the broker or agent writes the application for the, you know, with the applicant, submits it to a servicing carrier, the broker agent collects a premium, submits that to the servicing carrier, the servicing carrier processes the business, issues the policy, and does all the usual service aspects that most of us as consumers are familiar with, handling claims, billing, policy changes, things of that nature, and in terms of the financial results, those are reported monthly to the Association. We publish what we call a Member's Participation Report once a month, and typically that will follow by about six or eight weeks at the close of the month, so I would expect to see the August participate, Member Participation Report, sometime in late October, for example, and that indicates on a month by month basis the member's share of the business and it has some detail in that well, total premiums written, expenses, things of that nature, reserve changes and that sort of thing and also actuarially based projections for the two months forward. In terms of how we interact with the members in terms of the sharing that's dictated by the plan of operation, that requires the Board at the end of every fiscal year to make a determination as to whether or not, based on the year end financial, based on the year's financial results, whether or not there'll be an assessment or distribution in a jurisdiction.

MS. NEWMAN: Okay. So just so that I understand it here, an insured walks into the broker's office, the broker places insurance with FA, the insured writes a cheque.

MR. SIMPSON: Typically that's my understanding.

MS. NEWMAN: Provides cash.

MR. SIMPSON: Cheque or cash.

MS. NEWMAN: And does a broker then take all that money in and distribute it to the appropriate places or does that then go whole scale to the servicing carrier?

MR. SIMPSON: As I understand it, the money goes to the servicing carrier along with the application. In terms of how the servicing carrier and the broker commission detail works, I don't know.

MS. NEWMAN: Okay, alright. Somehow the broker gets a commission.

MR. SIMPSON: Somehow the broker gets a commission as prescribed by the plan of operation.

MS. NEWMAN: Okay. And then the servicing carrier would write a policy.

MR. SIMPSON: That's correct, would ...

MS. NEWMAN: And send it directly to the insured or would it all be done through the broker then?

MR. SIMPSON: It really depends on the nature of the operation of the business, but usually it's through the broker or the agent.

MS. NEWMAN: And then the servicing carrier reports to Facility Association of the money that's coming in and the insurance that's been placed.

MR. SIMPSON: That's correct. There's two systems reporting, one is financial, one is statistical.

MS. NEWMAN: And then Facility Association would manage that pool of funds.

MR. SIMPSON: That's right, all the premiums and then our board has an Investment Committee of Board which is responsible for investing the money that's collected but not needed today to pay claims, I think as Mr. Pelly indicated, because liability claims, they can have quite a long time frame, so that money is invested in what I would describe as a conservative investment portfolio as mandated by the investment guideline to the Association as approved by the Board.

MS. NEWMAN: Okay. So the money that the servicing carrier gets is sent to Facility Association and it manages it.

MR. SIMPSON: In a manner of speaking, yes. I mean, they need some money for their day to day operations and it's my understanding that it's zero balance between the servicing carrier and the Facility Association at the end of every day, but I'm really, I'm sorry, I'm out of my depth on this one in terms of, you know, I'd have to touch base with my accounting people to talk about how the mechanics of it day to day work.

MS. NEWMAN: But I guess in effect the insurance funds are sent somehow to Facility Association to be managed by Facility Association. Is that correct?

MR. SIMPSON: That's correct, but it's also my understanding that, you know, every day the servicing carrier has operational expenses as well as claims to be paid.

MS. NEWMAN: Right.

MR. SIMPSON: So it's my understanding that they don't send everything to Facility Association and we send some back. The accounts have a zero balance, as I understand it, at the end of every day so that there's nothing remaining with the servicing carrier. Now, I may be contradicted by the servicing carrier representative, but ...

MS. NEWMAN: But that's your understanding ...

MR. SIMPSON: That's my understanding.

MS. NEWMAN: ... and that's fair enough. So Facility Association wouldn't do any of the claims handling or any assessment of how much is to be paid other than to accept what the servicing carriers are telling you, is that correct?

MR. SIMPSON: That's correct. We're not an insurer so we don't do the day to day insurance functions. On that basis though, on behalf of the membership at large we have two auditors on staff and one is responsible for what we'll call an operation audit which deals primarily with risk classification, premium collecting and well described as underwriting, although, because we're a take all comers organization, the underwriting that is done on behalf of Facility is different than what a voluntary company would do, and also we have a claims auditor as well and in the Atlantic Provinces we out source that to a major adjusting firm to make sure that claims are being handled in accordance with our prescribed practices, the company's own standards and industry standards generally. We also have a working group, a claims committee, it's not an advisory committee, it's a working committee that reviews large losses as defined either by the dollar amount of the loss or the severity of injury typically, and so there's a review there, several review processes that are conducted on behalf of the membership and to make sure that business is being conducted appropriately, and also because there's historically been a concern in some regulatory sectors that somebody insured through Facility Association might not receive the same level of service for their claims or whatever, from an individual company as they would for, say, their own customers, if you will, and part of the audit process is to make sure that doesn't happen.

MS. NEWMAN: So do the servicing carriers provide you details of the claims that are paid then or do you actually go into the servicing carriers and periodically audit?

MR. SIMPSON: The short answer is both.

MS. NEWMAN: Okay.

MR. SIMPSON: Okay. The details of the claim are provided on the large losses as identified by dollar amounts or by injury severity. The volume of claims, it's impractical to take a second look at every one so that's done on an audit basis and the auditor is required to go in and select a certain volume of claims and review those and report back to the servicing carrier those audits, the findings from those audits, reviewed by the Board of Directors, and are forwarded to the CEO of the servicing carrier.

MS. NEWMAN: So that's the relationship with the servicing carriers in a nutshell, and then FA would also have a relationship with the member companies which you spoke of in terms of the assessments to the members and from the members. Is that ...

MR. SIMPSON: Yes, and the relationship between the members and Facility Association is primarily financial because of the sharing. As I say, we send a participation report every month to let them know how things are trending because presumably they have to make provision on their own books for the financial results of the Association, and as well from our committee structure in terms of the operations of the Association. As I mentioned yesterday, most of our committees have representation from servicing carriers and non-servicing carriers right up to the Board level.

*(9:30 a.m.)*

MS. NEWMAN: So it sounds like FA doesn't have a lot of involvement with the brokers themselves.

MR. SIMPSON: Not directly, no.

MS. NEWMAN: An application is made by a broker to become a broker for purposes of FA?

MR. SIMPSON: We do a certain administration of broker contracts. You know, if a broker enters into the business they need a contract through their servicing carrier and our role is to assign those contracts. You know, if we've got three or four servicing carriers in a given jurisdiction, we don't want 70 percent of them to be with one servicing carrier. We try to balance that out, so my staff administers that aspect of things in terms of broker contracts and assignment to a servicing carrier. A broker may be or have a Facility Association contract with a servicing carrier that they have no other relationship with. They may have contracts in the voluntary market with three or four other companies, but their only contract may be with the servicing carrier, so the servicing carrier may or may not be one of the voluntary companies that they deal with outside the residual market arena.

MS. NEWMAN: So a broker would apply to FA to become a broker to service FA.

MR. SIMPSON: Through the servicing carrier, yes. Pardon me, through the local operating committee.

MS. NEWMAN: Through the local operating committee. And then that local operating committee would sign a contract or simply refer them ...

MR. SIMPSON: They forward that to Facility Association. The contract is actually between a broker and a servicing carrier and the administration is done at our head office in terms of assigning a broker the servicing carrier.

MS. NEWMAN: Okay. So FA would assign the broker to a particular servicing carrier and then a contract would be signed between the two, the broker and the servicing carrier. Would FA participate in that contract execution or do they simply just assign them and leave the two ...

MR. SIMPSON: I'd have to look at the contract.

MS. NEWMAN: Okay.

MR. SIMPSON: Okay. I don't have the recollection of the detail on that.

MS. NEWMAN: And FA actually keeps a copy of these contracts?

MR. SIMPSON: We do keep a copy of the contract and I can certainly undertake to provide a blank copy of the contract if you'd like to have one.

MS. NEWMAN: If you could do that, that would be helpful.

MR. SIMPSON: Yeah.

MS. NEWMAN: Now, similarly for the servicing carrier, does FA enter into a contract with the servicing carrier?

MR. SIMPSON: Yes.

MS. NEWMAN: Can we get a copy of that as well, a blank copy?

MR. SIMPSON: I'll undertake to provide that.

MS. NEWMAN: In terms of servicing carriers, can any insurer apply to be a servicing carrier?

MR. SIMPSON: If they're licenced to write automobile insurance in the jurisdiction, yes.

MS. NEWMAN: And in terms of FA's relationship with members other than statutory structures and plan of operation and things like that, there's no individual relationship, I think you said, with each of the members and FA, between each of the members and FA.

MR. SIMPSON: Not beyond what I've described.

MS. NEWMAN: So no contract, no day to day ...

MR. SIMPSON: The predecessor organization, there was contracts because participation was not compulsory in all jurisdictions, but because, as the

Consumer Advocate mentioned yesterday, in the Act companies are required by law to be members of the Association. There's not, presumably not a need for a contractual arrangement between the member and the Association.

MS. NEWMAN: I want to take you to the plan of operation. I don't know if you have a copy of that there. I've got a couple of small questions on the plan of operation itself.

MR. SIMPSON: Okay. I don't have a copy in front of me. Thank you.

MS. NEWMAN: Page 18.

MR. WHALEN, Q.C.: Page 18, was it?

MS. NEWMAN: 18. It's Article 9.

MR. SIMPSON: Yes.

MS. NEWMAN: Okay. In No. 1, I just want to have you clarify for me, in the last sentence there's a reference there to marketing methods. "It is desirable to designate one or more servicing carriers from each of the types of marketing methods providing each is qualified to handle servicing carrier responsibilities in an efficient manner." I'm just wondering if you could explain to me what is meant there by marketing methods? It's referred to throughout the plan of operation.

MR. SIMPSON: Yeah, I'm sorry, I don't ... I'm on page 18 here but I don't have that.

MS. NEWMAN: You must be on ... you're probably on the old plan of operation, are you? There was two that were filed.

MR. SIMPSON: Okay. It's ... I've got the one revised June 2002, so I'm on page 18. If you could just help me out, I'm sorry.

MS. NEWMAN: Yeah, Article 9.

MR. SIMPSON: Yeah, and what sub point?

MS. NEWMAN: No. 1, and the last sentence.

MR. SIMPSON: Oh, I'm sorry, I have it now. I beg your pardon. In terms of marketing methods, there's two predominant marketing methods, well, now I'll say three, in automobile insurance. Companies that market through independent brokers and companies that are known as direct writers, they'll market through a captive agency force. An example of that would be the Cooperators where the agent does not write business for a number of companies. A broker may have one, two, three, five, seven companies that they can place business with, an agent, and sometimes they only write for one company so they're commonly known sometimes as captive agents, will write for just one company so that's a direct writer, an example. Another example, they don't operate in Newfoundland and Labrador, but would be State Farm Insurance. It's another direct writer. And then a third category that's arisen in the last number of years largely due to advances in technology, telephone and internet, is what's come to be known as a direct response type of marketing method and that's where somebody does business not through an intermediary but directly with the company and presumably through the phone or through the internet. So in this jurisdiction it's my understanding Unifund and Cooperators use the direct marketing method and Royal and Sun Alliance and Insurance Corporation of Newfoundland market through brokers. We don't have any servicing carriers that are, that use the direct writing method, pardon me, the direct response method, the people who do business over the phone or over the web.

MS. NEWMAN: Okay. I wonder if you could look at No. 2 on that same page, and it flows over onto the next page. It's, "Servicing carrier shall be reimbursed for servicing Association business on the following basis." I wonder if you could sort of summarize how that works. Do you have any understanding of how that works?

MR. SIMPSON: Just a very broad high level understanding, and the operating cost is based on written premiums, as it says there, Ontario, 9.9 percent, other jurisdictions, 9, and plus a service fee equal to the following percentage of written premiums, Ontario, .9 percent, other jurisdictions, 1 percent. That's the fee for writing and servicing the business on an ongoing basis and it's based on a written premium, and just in terms of how the timing of that works and the flow of that fund works, I don't know the detail. I'd have to get that from my accounting people.

MS. NEWMAN: So it'd be 9.9 percent of the written premium.

MR. SIMPSON: In this jurisdiction it would actually be 10, other jurisdictions, 9 plus a service fee of 1 percent, so 10 percent.

MS. NEWMAN: Okay. And then the next item there for claims expenses.

MR. SIMPSON: Yeah, and this is claims expenses both allocated and unallocated, the following percentage of earned premium, so it's a little bit different here, it's based on earned premium rather than written premium, Ontario, 9.1 percent, other jurisdictions, 10 percent, and the rates of reimbursement are predicated with an earned income loss ratio of, as follows, Ontario, 61.7, other jurisdictions, 67.5, and then there's provision for a retroactive claims adjustment based on the loss ratio, and that's specified in the accounting and statistical manual. It's briefly highlighted there, which on average increases or decreases the rate by .5 percent for each 5 percent of increase or decrease in that loss ratio, and it's my understanding from my recollection of the accounting and statistical manual that that is banded, capped at the low end at 9 percent, the high end at 16 percent, so, and my understanding for the reason for that is that the loss ratio serves as a proxy for the amount of claims work that servicing carriers are required to perform.

MS. NEWMAN: Okay. So this is a reimbursement for the work they have to do when adjusting a claim, so to speak, is that ...

MR. SIMPSON: Right. A reimbursement applies, you know, a dollar for dollar cost exchange, I think as Mr. Pelly highlighted. It's a general formula so it's not a direct dollar for dollar reimbursement but it's, this portion is designed to cover the costs of the servicing carrier that they incur to adjust and handle claims.

MS. NEWMAN: And those are the two, those are the only two aspects of the fee that's paid to the servicing carrier that you're aware of?

MR. SIMPSON: There are provisions for reimbursements for specific expenses, motor vehicle abstracts would be one example. In Ontario until very recently there was a vehicle pre-inspection requirement and that involved a specific cost so they were eligible for specific reimbursements for ... and that is a dollar for dollar reimbursement process, but, and then as the next section said, there is provision for reimbursement of extraordinary expenses as well.

MS. NEWMAN: Okay. I'd like to take you to page 40 now.

MR. SIMPSON: Four zero?

MS. NEWMAN: Four zero, 40.

MR. SIMPSON: Thank you.

MS. NEWMAN: Section 2 of the Servicing Carrier, Part 2, Article 20. Have you found it?

MR. STAMP, Q.C.: Section 2?

MS. NEWMAN: Article 20 and then Operating Principles, Part 1, and then Part 2, Servicing Carriers. Got the Operating Principles? So Part 1, Part 2, Servicing Carriers, and then there's, of the Servicing Carriers there's a Section 1. We're at Section 2. There's a section, a little subheading there, (h), goes from (a) to (i). We're on (h). I wonder, Mr. Simpson, if you can just familiarize yourself with (h).

MR. SIMPSON: Yes.

MS. NEWMAN: I wonder if you could just briefly explain to me what the purpose of that section is or what the reason for it is, if you have any familiarity with it at all?

MR. SIMPSON: I don't have any familiarity with it. I'm sorry, but my understanding just from a reading of it is that, you know, and part of it, I think, goes to philosophy of our goal to depopulate Facility Association, keep the population in it as small as possible, and that if a policy is insured through Facility Association with a servicing carrier and subject to these prescribed procedures, if they want to take that policy on their own book of business, they may solicit it.

MS. NEWMAN: And can a broker work with more than one servicing carrier or is he simply assigned to one?

MR. SIMPSON: There are cases and they're not too many where a broker may have more than one servicing carrier. I don't recall the name of the broker or the servicing carrier but I do recall one instance where we had a broker apply to have the personal lines automobile business with one servicing carrier and the commercial lines with another primarily due to the, as I understand the history of it or recall the history of it, the amalgamation of the brokerage, separate computer systems and just from a cost standpoint made it totally impractical, but that would be an unusual event. Most brokers are with one servicing carrier.

MS. NEWMAN: Those are all my questions on the plan of operation for now. I'd like to refer you to DJS No. 2. It looks like ...

MR. SIMPSON: Yes, thank you.

MS. NEWMAN: We've gone through this on a couple of different occasions with respect to a few different topics, I suspect. I simply wanted you to explain how it is that the amount in the assessment column, that is the money that might be paid out to or that was in fact paid out to the member companies in a particular year, which is the last column over, gets determined. So how is it that Facility Association decides that, for example, in 1990, $87,000 is to be paid out to the member companies when I thought that maybe it would be a direct relationship between the excess and a deficiency that is set out in the previous column, but it's not, so I wonder if you could explain to me how that last number, the assessments, are determined?

*(9:45 a.m.)*

MR. SIMPSON: And that's changed through time so I can only give you my recent knowledge, and in terms of why the excess or deficiency is not identical to the assessment to/from members, it's my understanding that those are largely due to timing differences. If we were to wind up the Association and once all the bills and outstanding claims were paid so many years down the road, those two columns ought to be the same when you total them all out. In a practical way then, the assessment or distribution to the members and, is based on accident year results and as at a certain point in time, and it's my recollection that for the assessment that took place in October of 2002, well it is based on accident year, accident years 2001 and prior, results from accident years change from year to year as a claim experience matures, and I think Mr. Pelly discussed that a little bit, and so it's for accident years 2001 and prior and, as I recall, that was determined as at June of 2002.

MS. NEWMAN: You had said that the method of, the way in which this is calculated has changed over the years. When was the last change that you're familiar with?

MR. SIMPSON: The last change would have been, relative to this jurisdiction, would have been in 2002, and that was to bring it in line with the other jurisdictions briefly for at least a few years in the other jurisdictions. The results were determined based on the immediate, the accident year and prior, immediately prior to the calendar year, to the fiscal year. So, for example, just this last year the assessment or distribution that took place in October 2002 for all other jurisdictions was based on 2001 and prior. In 2001 it was similar. October 2001 would have been accident year 2000 and accident years prior for all jurisdictions aside from, except for Newfoundland and Labrador.

MS. NEWMAN: I actually have a few documents here that might help you in explaining this. It's, and I'll have the Clerk circulate it, it's, I believe, a notice that's sent out to all the members of Facility Association, and the subject is, "The Distribution and Assessment of Funds." That's an annual thing, but I will have the Clerk circulate copies of it.

MR. SIMPSON: Perhaps before we get to that, I would just finish up what I was going to say in terms of the change that was made relative to this jurisdiction in 2002, and prior to that the immediate accident years three years old, if I can put it that way, and prior, were *(sic)* incorporated into the settlement of accounts, the distribution assessment process.

MS. NEWMAN: They weren't incorporated, sorry?

MR. SIMPSON: The immediately preceding three accident years were not incorporated, and that was, I don't know the history on that, I only know it's different, and I believe the rest of the Association at one time was, the distribution assessment process was handled on a similar basis, but since my tenure, since I began it's always been for the immediately preceding accident year and prior years and a decision was made by the Board in 2002 to bring this jurisdiction in alignment with the other jurisdictions that we serve.

MS. NEWMAN: When was that decision made?

MR. SIMPSON: I believe it was, well, certainly in 2002 and I believe it was either in September or October. I'd have to look at the Board calendar, the Board meeting in the fall of 2002.

MS. NEWMAN: Around the time that your rates were filed.

MR. SIMPSON: I think it would have been ... I believe the Board meeting was in October, so it would have been a month or so after these rates were filed.

MS. NEWMAN: Okay. So again, as I said, what I'm circulating here is for the years 2002 back to 1998, I believe, and you can clarify this for us, what would be an annual notice to the members showing distribution, the distribution of funds that is proposed, I guess, if that's a proper word, and the years upon which they're based. Is that fair?

MR. SIMPSON: Yes, this is distributed to CEOs of all member companies as well as the regulatory authorities in the jurisdictions we serve.

MS. NEWMAN: I guess we could label this Consent No. 3 and again that would have the years 1998 to 2002, for the record. So the first item on top of everybody's package should be the 2002 year and it shows, I guess, are those all of the jurisdictions in which FA operates?

MR. SIMPSON: Yes.

MS. NEWMAN: And can you just briefly describe that chart there, what's going on with respect to Newfoundland only?

MR. SIMPSON: Newfoundland, this gives a summary of the net operating results based on an accident year basis and, it seems my memory has served me correctly, as at June 30th of 2002 for accident years 2001 and prior for all jurisdictions, so for Newfoundland and Labrador the net operating result for accident years 1997 and prior is given as a positive, $479,007, for 1998 a positive, $4,760,106, and for 1999 a negative, $168,627, for 2000 a negative result of $2,632,521, and for 2001 a negative result of $3,965,209, for an overall total, negative, or the total assessment to the members in the province of $1,527,244.

MS. NEWMAN: And that total amount reflects back to your chart, which is DJS No. 2, in the assessment column for 2002, I see.

MR. SIMPSON: There's a discrepancy, and I don't know why, of, as I make it out to be, $12, between DJS No. 2 and Consent No. 3. Other than that, that's the number referred to.

MS. NEWMAN: So in effect that is the amount that was paid out to the members.

MR. SIMPSON: That was assessed from the members.

MS. NEWMAN: Sorry, assessed from the members. Now, you had said that this year in October approximately the decision was made to, and correct me if I'm wrong, I'm paraphrasing here, to base the assessment on all the years prior, so previous to that the last three years would not have been reflected in the assessment to or from the members, is that true?

MR. SIMPSON: That's my understanding, yes.

MS. NEWMAN: Okay. So in this case then, in 2002, the assessment would have been based on 1997 and prior and 1998 only.

MR. SIMPSON: That's correct. As in the prior year, in 2001, and I see you've included that bulletin, the most recent three years would have zeros in those columns.

MS. NEWMAN: Yes, so we can just look to the next item down, which is October 17th, 2001, that's the next double (phonetic) sheet, and we can look at Newfoundland there and we see that it was 1996 and prior and 1997 and zero was included for 1998, '99 and 2000.

MR. SIMPSON: That's correct.

MS. NEWMAN: Okay. And that's the way it had been done, I think if you look back through all of these particular years, it had been done consistently with that approach back to '98. Is that fair?

MR. SIMPSON: As I say, I have no direct knowledge of it but that seems to be the case from the bulletins, yes.

MS. NEWMAN: And you said that you didn't know why that was done, simply that it had been done in the past in Newfoundland and in other jurisdictions.

MR. SIMPSON: Why it had been ...

MS. NEWMAN: Why that was done, why three years, the last three years ...

MR. SIMPSON: I don't have any direct knowledge of it. I think, you know, anything I would have to offer would be speculation.

MS. NEWMAN: So I'd like to take you back to 2002 now, and the decision was made in the fall to include those latest three years. Can you please tell me what the impact of that was on, what the impact was on the assessment itself?

MR. SIMPSON: I don't have a calculator with me, if that's the answer that you're looking for.

MS. NEWMAN: Well, I guess we can approximate it. If those three years had not been included, as had been done in the past, what would the assessment to or from the members have been?

MR. SIMPSON: Well, there would have been a 1997 and prior, 1998 then would have been included and there would have been a distribution in excess of $5 million.

MS. NEWMAN: And so therefore by including these latest three years, rather than making a distribution to the members, you've actually sought a payment from the members of $1.5 million.

MR. SIMPSON: That's correct, and the change was made to bring it in alignment with the methodology used in other jurisdictions.

MS. NEWMAN: And are you aware why that was done this year?

MR. SIMPSON: No. It's just one of those things that had been outstanding for a while and the Board decided to follow the same procedures in all jurisdictions.

MS. NEWMAN: No, but it had been for some number of years, the same procedures had been in other jurisdictions, I see.

MR. SIMPSON: Yeah, in terms of just why it was done beyond a desire to generally harmonize things across most jurisdictions, which is part of our general philosophy.

MS. NEWMAN: Did it have anything or are you aware of any discussion around the possibility that it could have been caused in part at least by the fact that FA was coming to this Board looking for a significant rate increase and it would have a poor appearance to be having such a large surplus?

MR. SIMPSON: Well, we'd still have, the fiscal results would be the same in the middle column on DJS No. 2, I think that's important to note, and the decision to file in Newfoundland was in fact, as I recall, made in August, the decision around the distribution and assessment that's reflected in this bulletin was, I believe, made at an early October board meeting. Like I say, I'd have to check my calendar. So this distribution assessment of funds decision was made, I would approximate, about two months after the decision to file in this jurisdiction.

MS. NEWMAN: So you're not aware then of that being part of the reason for that change?

MR. SIMPSON: No, that's not my understanding.

*(10:00 a.m.)*

MS. NEWMAN: I'd like to take you now, and we're moving on to the second major topic, which is the application itself and some general questions with respect to that. I believe you said yesterday, and you can again correct me if I'm misinterpreting what you said, that for our purposes here, for the purposes of rate setting, purposes of the Board's decision making, the rates are determined on loss experience or loss costs. Is that accepted by FA and proposed by FA?

MR. SIMPSON: That's my understanding of the basis for the filing as prepared by Mr. Pelly's firm, yes.

MS. NEWMAN: Okay. So these other issues that have arisen throughout this proceeding, and I'm summarizing, I guess, one of them is, you know, whether there should be room in the market for grey market insurers so that the rate should be set significantly above the regular market rate, so a grey market insurer can squeeze in there, that issue, the issue of trying to keep FA participation low, the issue of trying to minimize competition between FA and the regular market insurers, all of those issues do not pertain to the rate proposals of FA, is that fair?

MR. SIMPSON: Those kind of issues that you're talking about are the sort of follow on consequences of rate inadequacy for Facility Association that you would expect to see in the marketplace, so the goal of the Board is to pursue rate adequacy for the Facility Association book of business on the basis of the filing as submitted.

MS. NEWMAN: So when you say pursue rate adequacy, you think that the rates that you proposed are adequate.

MR. SIMPSON: That's what Mr. Pelly's firm tells us, we need to get to that zero percent profit provision rate to generate enough premium to cover the losses and the expenses of the Association and the expenses incurred by the member companies as a result of their participation in the Association.

MS. NEWMAN: So but FA thinks that the rates proposed in its application are adequate, that FA's proposal is ...

MR. SIMPSON: That's the mandate to Mr. Pelly, is to develop rates that will generate rate adequacy on the basis of the mandate I've described.

MS. NEWMAN: I wanted to ask you to clarify for me something that you said yesterday, and I think you said that you felt the primary factor causing the higher participation in FA in Newfoundland is the lower rates in comparison to the regular market. Is that your belief?

MR. SIMPSON: By and large, yes. It is a belief based on what we observe in other markets. Basically we see a relationship as outlined in the (inaudible), I forget what the number is, I think it's BGP-4, of a relationship between our market share and the rate relativities, premium levels, between the voluntary market and Facility Association.

MS. NEWMAN: I just want to explore that. When you say there's a relationship, that's quite different than there being a cause and effect, and I'm wondering if, if you see a relationship, that's one thing, but if you're telling us that you believe that the lower rates relative to the other jurisdictions is causing the increased participation, then I'd like to know which of the two you ...

MR. SIMPSON: I would lean more honestly towards correlation in that, you know, but it's a pretty consistent one. As that chart highlights, we observe pretty much in all jurisdictions, through time, we've been looking at it since 1996 as an association, but a direct causal relationship, no, I wouldn't say that but I'd say there's a strong correlation that's observable.

MS. NEWMAN: And we have gone through to some extent the fact that there are many other factors, and I think you spoke of one yesterday in Ontario, the two tiers residual market. That's a significant factor in Ontario, isn't it?

MR. SIMPSON: The total residual market there, risk sharing pool, as I recall from the chart that distributed, I think was about 2 percent including the risk sharing pool on the residual market, I call the traditional residual market as it existed in other jurisdictions, so a significant impact, I'm not sure that when we're talking about a total residual market, less than 2 percent, I'm not sure that I would term it significant. It obviously has an impact.

MS. NEWMAN: And we spoke yesterday in New Brunswick, and I think you said in Nova Scotia to some degree, there's this binder control registry system and that dramatically reduced participation in FA as well.

MR. SIMPSON: That was one of the goals, is my understanding. As I indicated, I wasn't around at the time. That's my understanding, but there's a number of other causal factors that I would say would pertain there. From what I've read, there's a causal, there's a correlation, and this is American experience, between prior approval of rate regulation and the size of residual market. In other words, in jurisdictions ... US is an interesting laboratory because they have individual state regulations, we have individual province regulations, so there's a lot of different things you can observe, so from what I've read and so we've got a de-regulation of rates happening in Nova Scotia and New Brunswick presumably opening up, there's no filing requirement, to my knowledge, for rate filings in Nova Scotia, New Brunswick, it's pretty much a file and use type of system since about 1996, I think, so you see ... that's one factor. You see a heightened sense of competition in the Canadian automobile insurance industry generally and favourable factors giving companies a large appetite for risk in the latter half of the 1990s, unexpected investment incomes for private companies, so there's a lot of factors that impact the size of the residual market.

MS. NEWMAN: And that's why you said that, you know, correlation, yes, cause and effect ...

MR. SIMPSON: I couldn't draw you a ... like I say, we observe that pretty much at all times in all places, but in terms of the causal relationship for that, for the decline in a residual market population, is part economic and part regulatory.

MS. NEWMAN: Okay. I'd like to refer you now very briefly to BGP No. 5 and the series of bar graphs that were provided to us. I'm looking at the bar graph for New Brunswick and then Nova Scotia and Prince Edward Island and I see an upswing in the last three years. Is that fair?

MR. SIMPSON: Residual market market shares started increasing from historically low levels in 2000 in New Brunswick and similarly in Nova Scotia and PEI as well.

MS. NEWMAN: And do you have an explanation for that?

MR. SIMPSON: Well, I go back to the, as I say, there's a variety of causal mechanisms, but I will say that to my knowledge rates have been increasing significantly in the voluntary market in those provinces. Our rates are becoming closer to those and so we start, on BGP No. 4 we start moving up into the left on that graph, and that presumably, I'm going from memory now, we were awarded in Nova Scotia a rate increase of 7.1 percent in November ... that would have been January 2002. It took effect, I think, in June of 2002. So our rate increase activity has been lagging the market so I assume that there would be classes of risk where it would be increasing the price competitive.

MS. NEWMAN: Alright. Can you please look at the filing, Eckler Partners Report, page one? So at page one of the report, that's the Summary of Findings, and it shows those, three on that page and one more table on the next page, and I understand that the first two tables relate to private passenger, the first being the indicated. I understand from your testimony as well as that of Mr. Pelly that he indicated the number is calculated by Mr. Pelly's firm.

MR. SIMPSON: In consultation with our Actuarial Committee.

MS. NEWMAN: Right, through the committee ...

MR. SIMPSON: Yeah.

MS. NEWMAN: ... through that process that we've gone through. And that the proposed are those rates that are proposed by FA, having gone through the further process of having it reviewed by the Rules and Rates, Rates and Rules Committee, and then gone through the Board of Directors for approval.

MR. SIMPSON: Yes.

MS. NEWMAN: Okay. I just want you to explain to me if you are aware of the reason for the differences between the two in each particular circumstance, so if we look at private passenger, accident benefits, there's a very minor difference of, instead of 13.9 in the indicated, the proposed rates by FA are 13.8. Do you know the reason for that?

MR. SIMPSON: No, I'm sorry, I don't.

MS. NEWMAN: Okay. And then uninsured auto, instead of 46.7 the proposed are 45.8. Do you know the reason for that?

MR. SIMPSON: No, I don't. Mr. Pelly would have that information, I don't.

MS. NEWMAN: Specified perils, instead of negative 27.3 it's negative 20.5. Do you know the difference ...

MR. SIMPSON: No.

MS. NEWMAN: No, okay. So you can't speak to any of these in respect of the private passenger. How about ...

MR. SIMPSON: Not in any level of specific detail other than there may have been some capping decisions proposed by the Rates and Rules Committee, that sort of thing. That's not unusual, but in every specific instance, no, I don't have any direct knowledge of it or direct recollection of why it would move a few percentage points.

MS. NEWMAN: I assume that you do have some knowledge though in respect of the commercial and the decision with regard to the uninsured auto.

MR. SIMPSON: No, I'm sorry.

MS. NEWMAN: I understand, and correct me, that have to do with FA utilizing the $19 base premiums that was proposed in New Brunswick? Is that ...

MR. SIMPSON: That's what's on page two of the filing there ...

MS. NEWMAN: Yes.

MR. SIMPSON: ... about four paragraphs down.

MS. NEWMAN: Yeah.

MR. SIMPSON: I don't have any additional information other than what's in the filing document.

MS. NEWMAN: With respect to that $19, Mr. Pelly spoke about the fact that it wasn't an actuarially justified figure. It was a figure that they, that FA chose. Can you speak to why that number was chosen and why the Board should adopt it here?

MR. SIMPSON: No, I'm sorry, I can't, other than if, and it would be speculation on my part, but it would ... if insufficient information was available to develop a rate level in that coverage in this jurisdiction, they may look to another jurisdiction as a proxy, and that may have been done here but I don't know that for sure.

MS. NEWMAN: Alright. There would have been a rate for this particular coverage prior to this filing.

MR. SIMPSON: That's my understanding.

MS. NEWMAN: But there was no, not enough evidence to suggest what the change should be or if there in fact should be change, is that what you're saying?

MR. SIMPSON: That may have been the case. It wouldn't be unlikely. I don't know that for sure.

MS. NEWMAN: We spoke a bit yesterday about the fact that there are some drivers in FA, a significant number of drivers in FA who have clean driving records, and I think ...

MR. SIMPSON: Yes.

MS. NEWMAN: ... I think we may want to refer to DJS No. 3, which was that illustration that was provided in evidence in Nova Scotia.

MR. SAUNDERS, PRESIDING CHAIRMAN: DJS No.?

MS. NEWMAN: 3.

MR. SAUNDERS, PRESIDING CHAIRMAN: 3.

MS. NEWMAN: And there's a package of material, a letter on Facility Association letterhead and I'm looking at the Illustration No. 5.

MR. SIMPSON: I have a terrible propensity to lose paper, so I appreciate Ms. Blundon helping me out here. Yes.

MS. NEWMAN: We have Illustration 5.

MR. SIMPSON: Yes, I do, thank you.

MS. NEWMAN: Okay. And that's headed up, "Facility Association, Percentage of Private Passenger Applications." We saw yesterday that with respect to new business in Newfoundland Labrador, 62.6 percent of the insureds in FA have no accident or convictions, and with respect to renewal business 60.9 percent of the insureds have no accidents or convictions.

MR. SIMPSON: That refers to no at fault accidents in the last five years and no convictions in the last three.

MS. NEWMAN: And you had said yesterday, and it's fair enough, that there are sometimes other factors that might impact upon risk that aren't, you know, beyond simply whether they have at fault accidents or convictions.

MR. SIMPSON: Yes.

MS. NEWMAN: Fair enough. There are some presumably insureds in here that are here not because of risk related issues but other issues, and we've seen reasons for this, for example, poor payment history, those sorts of things that don't impact upon risk but they're there because no other insurer wants them.

MR. SIMPSON: In terms of the detailed underwriting practices of the member companies, I don't have direct knowledge of that but that's my general understanding.

MS. NEWMAN: Yeah. There is a Consumer Advocate information request, CA-9.2. I'm looking at Response 9.2, several pages into the responses.

MR. SIMPSON: I've made it as far as the CA tab in the information request binder. If you could provide me with a little further direction on that, I'd sure appreciate it.

MS. NEWMAN: Okay, you're in responses. Have you got ... one of the responses, should be the next tab, should be.

MR. SIMPSON: There is ...

MS. NEWMAN: And you're probably already in the response. It should be ... the first page should be Response to Consumer Advocate Information Request.

MR. SIMPSON: Yes.

MS. NEWMAN: Okay. So you're probably 10 or 15 pages in, in Response CA 9.2.

MR. SIMPSON: Yes. 9.2?

MS. NEWMAN: Yeah, and the second paragraph there, "Facility Association (inaudible) business."

MR. SIMPSON: Yes.

MS. NEWMAN: And it sets out some examples, this is not a comprehensive list, but examples of reasons that the regular market might consider somebody to be unacceptable.

MR. SIMPSON: Right.

MS. NEWMAN: Some of these don't have much to do with the risk that they pose, for example, payment history problems, that sort of thing.

*(10:15 a.m.)*

MR. SIMPSON: I'm not sure that I agree with that statement ...

MS. NEWMAN: Okay.

MR. SIMPSON: ... in the sense that, one, I'm prompted to assume that underwriters in the voluntary market know what they're doing, the role of the underwriter generally being to say yes to the profit, to the risk being presented, and also in terms of the experience for drivers with payment history problems, I do not know whether there's a correlation between somebody with payment history problems and a higher than average accident record. I do know that it's common practice in the United States automobile insurance industry to use credit history as an underwriting variable, so it may have some validity, so to say that it's not predictive of risk is not a statement that I can agree with. To the extent that it is predictive of risk, I don't know.

MS. NEWMAN: So if we look back to the percentages on the Illustration 5 that we just looked at, our 62.6 and our 60.9, to some extent you must admit these drivers must pose a lesser risk than people with four accidents or three convictions or ... in your view do you feel that those people pose the same risk as ...

MR. SIMPSON: I haven't seen any data to support that one way or another. Like I say, there's other variables other than accident conviction records that presumably are predictive of risk, so in terms of what that relationship is more or less, I don't know, but there was a sense from the Rates and Rules Committee supported by the Board and regulators in a couple of other jurisdictions I mentioned yesterday, Ontario, New Brunswick, that for a variety of reasons there should be a greater attention paid to those drivers and to develop a more gradual surcharge schedule and provide a discount to those that might be in, insured through Facility Association for reasons other than accident and convictions and hence our application for a 10 percent clean driver discount. You know, in terms of the extent, I haven't seen any empirical data in terms of the predictive reliability of these other factors relative to accident and convictions.

MS. NEWMAN: Okay. But there's some inherent acceptance that these people should be rewarded somehow with this discount and the others who have accidents and convictions should be somehow punished. I guess there's some reference to behaviour modification aspects to this particular item, the discount and the surcharge.

MR. SIMPSON: Yeah, there's a couple of aspects to it. One is because of what you say, there is, you know, an assumption that at some level that somebody with a number of at fault accidents and convictions pose a higher risk, and also that's a behaviour that they have a control over, their driving behaviour, and the more gradual approach we're proposing to the accident and surcharge schedule here and the fact that we do require servicing carriers to order abstracts on a renewal is to let the driver out there know that we are monitoring their behaviour and encouraging them to clean up their driving record and to hopefully enhance their eligibility for the voluntary market. As well it's my understanding that our Rates and Rules Committee in conjunction with staff did a survey of the voluntary market and the voluntary market has moved towards this more gradual approach, especially to conviction surcharges, in the last number of years.

MS. NEWMAN: So I understand that in New Brunswick the Board there felt that the ten percent didn't go far enough and they ordered 15 percent.

MR. SIMPSON: I think I mentioned that yesterday, that's correct, yes.

MS. NEWMAN: That's one thing that this board could do here as well if it felt that it wanted to further reward these drivers, it could also order a higher discount.

MR. SIMPSON: I would assume that's within the Board's authority, yes.

MS. NEWMAN: And would you have any particular comment as to problems that might be associated with doing that?

MR. SIMPSON: Well, I think too steep a discount puts us in direct competition with our members, so I see that as being a potential pitfall, and also in terms of the overall rate level need, a discount beyond ten percent reduces, if you don't change anything else, reduces the overall rate level, and so presumably the, I think Mr. Pelly called the off balance factor calculation, would need to be re-done.

MS. NEWMAN: So that the discount that you're giving to these good drivers, the money you're losing there would have to be collected from the rest of the drivers. Is that what you're saying?

MR. SIMPSON: That's correct, yes.

MS. NEWMAN: And there's another way that this could be handled, there's probably two actually, one is you could change the differentials that are applied to the base rate, is that true as well? Do you ...

MR. SIMPSON: I'm not sure I understand that question.

MS. NEWMAN: What you have is a base rate that's charged to consumers and then better drivers than people in this class of the driving, this certain driving record, get a discount off of this base rate, the differential is applied to it?

MR. SIMPSON: Yes.

MS. NEWMAN: So another thing is you could adjust those differentials, if you call it that, to reflect more favourable rates to people with better records.

MR. SIMPSON: Presumably, yes.

MS. NEWMAN: Any problems with doing that?

MR. SIMPSON: I don't know offhand. We're trying to maintain a harmonized approach across jurisdictions in the interest of operational efficiency for servicing carrier and ourselves, so to the extent that we have different accident and surcharge programs in different jurisdictions, there's bound to be a cost from a programming standpoint with that sort of thing.

MS. NEWMAN: So you've got 15 percent now in New Brunswick. Are you going to ...

MR. SIMPSON: There goes that part of the harmonization approach, but happily the surcharges are still, so that's, you know, there is one change there.

MS. NEWMAN: Okay. But you're not changing the discounts in other jurisdictions, you're leaving ...

MR. SIMPSON: We're applying for this accident and surcharge schedule in every jurisdiction.

MS. NEWMAN: Okay. And the discount is ten percent in other jurisdictions ...

MR. SIMPSON: Ten percent, yes.

MS. NEWMAN: ... except for New Brunswick.

MR. SIMPSON: That's what we're applying for, yes.

MS. NEWMAN: What about the driving record, how many driving records are there in FA?

MR. SIMPSON: I don't know offhand. Mr. Pelly, I think, would be able to address that. I think we go to Driving Record 5 but I'm not positive.

MS. NEWMAN: Okay. And are you familiar with the regular insurance industry, what their ...

MR. SIMPSON: No, I'm not. I've never been an auto insurance underwriter, so in terms of the details of it ...

MS. NEWMAN: So if I told you that, you just assume this is correct, that FA has a Driving Record 5 and that the regular insurance market has up to a Driving Record 6, which is, you know, a better record even then, what would be the problems associated with the Board ordering FA to add an extra driving record so that people with even better records get rewarded?

MR. SIMPSON: Well, certainly, you know, we're into those programming issues again for one thing, but I'm not knowledgeable about ... I'd have to go back to my staff and to Mr. Pelly and ask them about what the impact of such a change would have.

MS. NEWMAN: Alright. I have one other small thing to ask Mr. Simpson on this subject area and then I guess I'm not going to be finished by break. I'll have to come back after and discuss implementation, but if you indulge me for another minute or two, then we can ...

MR. SAUNDERS, PRESIDING CHAIRMAN: Carry on.

MS. NEWMAN: With respect to the CLEAR system that you spoke about in quite a lot of detail yesterday, I wanted to ask you, you'd made a couple of comments throughout the day about the CLEAR, if the implementation of the CLEAR system would cause drivers to migrate back to the regular market. Is that what you said and what did you mean by that?

MR. SIMPSON: Well, what I was trying to get at is the potential for adverse selection if we don't use the CLEAR system, so that's one aspect of it, because if we maintain manufacturer suggested retail price groups, as we have now, if we didn't go to the CLEAR system, which I understand has been embraced by this Board, then we would presumably be somewhat more attractive rate-wise for low priced high powered cars, muscle cars, with high accident experience, so, and then in terms of ... so that goes one way. I think what I was getting at in terms of the dislocation, and I think that's where I made those remarks, in the context of dislocation that is presumably a concern of the Board, is that there, if somebody is going to be dislocated presumably because of CLEAR, there's a few things, one, they may not be insured through Facility anymore as they were at the time of the analysis due to the high level of turnover, through the Facility Association, and the other, two other alternatives are they would remain insured through Facility Association and experience a dislocation, but a third alternative that distinguishes a competitive market from a monopolistic situation is that if their rate were to go up due to the implementation of CLEAR, they may find themselves in a position where they can find a more competitive price in the voluntary market.

MS. NEWMAN: I just want to clarify, CLEAR, the changes that flow from CLEAR only relate to own damages, that is they don't relate to a liability coverage, is that correct?

MR. SIMPSON: It's my understanding it's just the car coverages, yeah.

MS. NEWMAN: Okay. And the bulk of a premium, I guess, would relate to the liability.

MR. SIMPSON: In Facility Association typically, yes.

MS. NEWMAN: 80 percent of people don't even have own damage coverage, I understand.

MR. SIMPSON: Well, I don't know that it's premium ... as I understand, the premium volume collected through Facility is about 80 percent liability. Whether, how that translates to number of cars and vehicles and coverages, I don't know.

MS. NEWMAN: So the relatively favourable rate that might be given to some insureds under the manufacturer's retail program versus CLEAR is probably going to be offset by the liability, the increase in the liability premium ...

MR. SIMPSON: In terms of a net effect ...

MS. NEWMAN: Yes.

MR. SIMPSON: ... in this application ...

MS. NEWMAN: Yeah.

MR. SIMPSON: ... and we've got three things going on. We've got an overall rate level change, we've got the implementation of CLEAR, we've got the accident and surcharge schedule changes, so how those all interplay will depend on the individual risk.

MS. NEWMAN: But I would think that it'd be fairly easy to say, and you can correct me if this is wrong, I think it'd be fairly easy to say that the liability costs for premiums are so much higher than the own damages, that changes in the CLEAR aren't going to impact upon choices of insurance vehicles.

MR. SIMPSON: Well, the liability premium is the dominant coverage and the dominant ...

MS. NEWMAN: Right.

MR. SIMPSON: ... cost in the product, that's for sure.

MS. NEWMAN: Okay, alright. I'm going to move into, when we come back, if that's alright, to the implementation section, and I expect probably that'll take 10 or 15 minutes and then I'll be finished.

MR. SAUNDERS, PRESIDING CHAIRMAN: Okay. We'll return in 15 minutes, at about quarter to. Thank you.

*(break)*

*(10:50 a.m.)*

MS. NEWMAN: Sorry, Mr. Chairman, we're trying to work on this undertaking number four, which hopefully by the end of the hearing we'll have sorted it out (inaudible).

MR. O'FLAHERTY: And Mr. Chairman, before my friend recommences with her examination, I just wanted to raise a procedural matter with you. I do note that this morning we've been presented with, or documents have been presented, either in evidence or have been left on our desk which are new documents that we haven't yet seen, and I'm wondering if the Consumer Advocate would have an opportunity to question this witness about some of the aspects of these new documents, and secondly, how the timing of that should be handled, if the Board were inclined to allow us to ask some brief questions concerning matters, you know, that were just placed before us this morning.

MR. SAUNDERS, PRESIDING CHAIRMAN: Any comment, Mr. Whalen?

MR. WHALEN, Q.C.: No, I think that's reasonable.

MR. SAUNDERS, PRESIDING CHAIRMAN: It seems fair enough.

MR. WHALEN, Q.C.: For Mr. O'Flaherty to be able to ask some questions, perhaps after Ms. Newman is finished, if that's appropriate, I think that's only fair.

MR. SAUNDERS, PRESIDING CHAIRMAN: Okay.

MR. O'FLAHERTY: Thank you, Mr. Chairman.

MR. SAUNDERS, PRESIDING CHAIRMAN: Sounds good.

MR. SIMPSON: Mr. Chairman, before Ms. Newman recommences her questions, I wonder if I might address a couple of earlier matters.

MR. SAUNDERS, PRESIDING CHAIRMAN: Sure.

MR. SIMPSON: One that came up yesterday from the Consumer Advocate was whether or not Facility Association had filed for a decrease in rates in this jurisdiction. I spoke to Mr. Pelly yesterday, given his history with the organization, he seemed to be the best resource on that, and his records reflect that we filed for a decrease in private passenger, an overall decrease of minus 1.3 percent in a rate change that took effect in February of 1996, so I don't have the date of the filing. There was, I believe, about a two year period where the IAO, the Insurers Advisory Organization, was preparing filings for Facility Association, and apparently this filing falls into that timeframe, so Mr. Pelly's direct knowledge of the details of it are ... apparently 4.6, an increase of 4.6 percent was approved, even though an overall decrease of minus 1.3 percent was filed for, and why a decrease was filed for, and an increase approved, I don't know, I don't have the background on that and neither does Mr. Pelly. The other thing that he highlighted was that there have been numerous occasions where within individual coverages, that we had filed for decreases, but the liability coverage is the dominant coverage and as we've heard, we'll take 80 percent as the number of the premium, and that the trends throughout the last decade or so on that coverage has been upwards, and that's the additional background there. I hope that that's helpful.

Also, when I spoke to our Vice-President of Finance and Operations on the break to get a copy of the broker contract and the servicing carrier contract faxed down, as I undertook to do before the break, I did ask her about the agreement with the member companies, and I was mistaken. We do ask our member companies to sign an agreement with Facility Association, so I apologize for that error. One of the drawbacks, I suppose, of starting at the top of an organization rather than working your way up through the ranks is the level of detailed knowledge I have of the day-to-day operations is not as in-depth as I would like it to be, and I work pretty hard trying to remedy that, but I'm still on a learning curve. She did highlight that in her consideration, that was something of a formality because the statutory requirements of being a member of the Association would presumably take precedence over any agreement, pardon me, we would enter into with our member companies, so I just wanted to clear that up.

MS. NEWMAN: Thank you, Mr. Simpson. Before we proceed with my questions, I did want to have this undertaking number four entered into the record, Mr. Simpson. Is this a copy of an application for insurance that would have been requested under undertaking number four?

MR. SIMPSON: Yes, it is.

MS. NEWMAN: I would comment for the record that the Board will keep the original application here, but it is, you may be aware, it's somewhat difficult to copy because of the size of it and the size of the print, so if any ... we've provided copies and people can have those, however, we'll keep the original. If any of the parties or anyone else needs to have a better copy or a view of it, it's certainly on record for them to look at.

MR. STAMP, Q.C.: We have two copies now (inaudible).

MS. NEWMAN: Yes.

MR. STAMP, Q.C.: One shows the best copy of the top and one shows the best copy of the bottom. Together they work.

MS. NEWMAN: Right, so together you can see it all, but if you'd rather see the original. It's all the same document, it's simply ... it seemed to be the only way we could actually show the document in its entirety. I apologize. Now, Mr. Simpson, before I move on to the implementation, I did have a chance to review some of the, one of the undertakings in particular and consider some of your responses, so I do have three things I'd like to go back to.

The first one is the uninsured motorist coverage for commercial, that $19.00 that we spoke of from the New Brunswick ...

MR. SIMPSON: Yes.

MS. NEWMAN: I'm wondering if you're aware of what the proposals were for Nova Scotia, and what the rate is in PEI?

MR. SIMPSON: No, I'm not.

MS. NEWMAN: Can you find that out for us, please?

MR. SIMPSON: I'm sorry, the rate in Nova Scotia for uninsured motorist coverage?

MS. NEWMAN: Yeah, the equivalent to that $19.00 that's being proposed here for commercial.

MR. SIMPSON: For commercial?

MS. NEWMAN: Yeah, in Nova Scotia and PEI, and I guess in Nova Scotia, that would be the rate proposed in your application because you don't have a decision on that, I understand.

MR. SIMPSON: Not as yet, we had our hearing in the first week in November.

MS. NEWMAN: Okay, also I wanted to go back over to a small degree the decision making process within FA. I think that the last step for major decisions, you said was a board meeting.

MR. SIMPSON: Yes.

MS. NEWMAN: Okay, so on two issues, one would be this application, the Eckler Partners report, the difference between the indicated and the proposed.

MR. SIMPSON: Yes.

MS. NEWMAN: Would that decision have been made at a meeting?

MR. SIMPSON: Yes.

MS. NEWMAN: And would you have been present at that meeting?

MR. SIMPSON: Yes.

MS. NEWMAN: Who would have chaired the meeting?

MR. SIMPSON: The chair of our board is Bob Kirk. Our deputy chair is the senior vice-president for State Farm in Canada, the chief agent in Canada for State Farm Insurance, and our deputy chair is Mr. Larry Simmonds *(phonetic)*, who is the CEO of Royal and Sun Alliance, and so whether Mr. Kirk or Mr. Simmonds was actually in the chair of the meeting, I'm not sure, but it would have been one of the two.

MS. NEWMAN: And you would have been at that meeting?

MR. SIMPSON: Yes.

MS. NEWMAN: Would there have been minutes?

MR. SIMPSON: Yes.

MS. NEWMAN: Can you undertake to provide for us an excerpt from the minutes of the board of directors meeting relating to the decision with respect to the indicated versus the proposed rates?

MR. SIMPSON: Yes.

MS. NEWMAN: And similarly with respect to the decision to change the way in which the assessments are made, were you at that meeting?

MR. SIMPSON: I was at the meeting where the assessments and distributions were determined, yes.

MS. NEWMAN: And the decision to change the method in which those assessments were made, yes, you were at that meeting?

MR. SIMPSON: Yes.

MR. O'FLAHERTY: Okay, and were there minutes?

MR. SIMPSON: Yes.

MS. NEWMAN: And can we please have an excerpt of the discussion relating to that change?

MR. SIMPSON: Yes.

MS. NEWMAN: And the assessment itself. Okay, we discussed earlier this morning about factors that may cause a person to be placed into Facility Association.

MR. SIMPSON: Yes.

*(11:00 a.m.)*

MS. NEWMAN: And following up on that, I guess, I wanted to refer you to the binder control register sheet that was undertaking number three.

MR. SIMPSON: Yes.

MS. NEWMAN: I wonder if you could just, undertaking three, it's a single page that was provided this morning. I wonder if you could just take us through this sheet so that we all understand what's going on.

MR. SIMPSON: Okay, it's a single page form with Facility Association at the top, binder control register, for completion by the agent or broker, and Facility Association risk codes, and it requires the broker or agent to enter column one, class, and it identifies various classes of vehicles, private passenger, commercial vehicle, public vehicle, recreational, garage, non-owned, drivers, fleet, or the last code is a combination of vehicles. Column two is for the broker or agent to indicate the reason of risk, why the risk is written through Facility Association, and it says to enter the alpha code, and it provides a variety of alpha codes, and I could note here that this is the second edition, if you will, of the binder control registry. The first one offered a much lengthier list of codes, but it was found to be very cumbersome for the agent and broker to use and not all that helpful, as I understand, so beginning with alpha code "A" and reading in sequence, at-fault losses or conviction record, material misrepresentation or insurance fraud, premium payment history, any combination of A, B, or C, new driver to Canada, age of driver under age, age of driver senior, vehicle age and condition, vehicle use and type, location, vehicle domicile used, insurance history not available, any combination of E, F, G, H, I, J, or K ... "M", premium lower than other available markets. "N", other, please specify.

In column three, asking the agent or broker to indicate was the reason for placing in Facility Association revealed to the applicant, yes or no, and there's a place to indicate the province. As we've talked about before, this is in use in New Brunswick and Nova Scotia, and there's a form there of lines and columns to enter the codes I've just outlined, and the bottom notation on the form is the Facility Association ... I see we need to correct a typo there ... Facility Association and servicing carrier copy must be returned to your servicing carrier after this form is full.

MS. NEWMAN: Okay, so this is a mandatory step that the servicing carrier must do with every placement of insurance.

MR. SIMPSON: The broker or agent.

MS. NEWMAN: Okay, so this has to be completed?

MR. SIMPSON: We require them to do that and submit it to the servicing carrier when it's completed.

MS. NEWMAN: In both New Brunswick and Nova Scotia it's mandatory?

MR. SIMPSON: Yes.

MS. NEWMAN: Okay, and how long has this been in use?

MR. SIMPSON: It's my understanding that it was implemented in March of 1997 in New Brunswick and May of 1997 in Nova Scotia.

MS. NEWMAN: And what does Facility Association do with this information?

MR. SIMPSON: My staff compiles it, typically prior to a rate hearing in either of those jurisdictions because the boards in ... I'd like to say we do it annually, I'm not sure staff is that diligent, but certainly before we go to a rate hearing we compile the results and share them with the boards in those jurisdictions.

MS. NEWMAN: Okay, so you just had a rate hearing for Nova Scotia?

MR. SIMPSON: In Nova Scotia and New Brunswick in the first week of November, 2002.

MS. NEWMAN: Okay, so there would have been a document that compiled these statistics for the previous year?

MR. SIMPSON: As I recall there was.

MS. NEWMAN: Has that been provided to this Board?

MR. SIMPSON: Not to my understanding. We don't have a binder control registry for Newfoundland and Labrador so ...

MS. NEWMAN: No, but the particular documents in relation to both Nova Scotia and New Brunswick haven't been submitted as part of the record, I haven't seen it.

MR. SIMPSON: The compiled results, I don't believe anybody submitted them to my knowledge.

MS. NEWMAN: Can I get an undertaking for those, please? What does this ... I don't have the benefit of having it in front of me here, what would this summary sheet look like?

MR. SIMPSON: I'm going from recollection here.

MS. NEWMAN: Yes, yeah, I understand.

MR. SIMPSON: But essentially, and it will look a little bit different because as I said, this is a revised form, and as I recall, the summary dealt with the results as they were compiled on a previous form.

MS. NEWMAN: Okay.

MR. SIMPSON: So as I recall, it's basically a spreadsheet of the totals in each category as received by us.

MS. NEWMAN: Okay, alright, and when was the revision made to the form that you spoke of?

MR. SIMPSON: I believe it was sometime in 2002.

MS. NEWMAN: Okay, and can you generally describe how it was revised, now that we have the new one in front of us? What did the old one look like?

MR. SIMPSON: I think I mentioned, the old one had more codes on it, and I think perhaps originally the motivation might have been to capture a level of detail through the rates and rules committee and staff, but it didn't seem to be doing that, so it was thought that to make the form easier to use, but at the same time capture the essential information, that some of the codes were consolidated to capture the information in a more comprehensive way.

MS. NEWMAN: But there is here on this new code a column two, which is the reason that the risk was placed with FA.

MR. SIMPSON: Yes.

MS. NEWMAN: And that would have been on the old code *(sic)*, the old form.

MR. SIMPSON: Well, there was, I think that's one of the key differences, is that the old form had a greater number of reason codes.

MS. NEWMAN: Okay.

MR. SIMPSON: Some of which were duplicative, etcetera, and this was done as a streamlining exercise as I understand.

MS. NEWMAN: Okay, so I want to take you to, under the reason section, "F".

MR. SIMPSON: Yes.

MS. NEWMAN: And so that's saying there that the reason, if "F" is put under the reason code, it would be that the reason that an insured is put in FA is because he's under age.

MR. SIMPSON: Under age, as defined as being under 25, yes.

MS. NEWMAN: Yes.

MR. SIMPSON: It was in the right *(phonetic)* manual, yes.

MS. NEWMAN: And then similarly then it must be that for "G", it's possible that the reason that a person will be put in FA is that they're senior.

MR. SIMPSON: That's correct, and it's my understanding that this is a new code and it was included on this form because of concern by the regulatory authorities, and society generally, it's reflected in the media that the availability of automobile insurance for senior drivers, and that's a concern that's raised here obviously, was becoming an issue for society and an attempt to capture that information.

MS. NEWMAN: So that wouldn't be in the other information that I've requested.

MR. SIMPSON: I believe that's a new addition to the form.

MS. NEWMAN: Okay, and then the next item, vehicle age and condition.

MR. SIMPSON: Yes.

MS. NEWMAN: So therefore that would capture those insureds that are placed there because of the condition, if their vehicle is old, for example.

MR. SIMPSON: Old, prior damage, that sort of thing, that's my understanding, yes.

MS. NEWMAN: Okay, and "J", the location of the vehicle, what would that be intended to capture?

MR. SIMPSON: I'm not really sure on that one, I'd have to follow up on that one.

MS. NEWMAN: Okay, and "K", insurance history not available, why would that be?

MR. SIMPSON: It's my understanding that generally people with no prior record of insurance generally have higher loss experience, so that goes to the risk profile.

MS. NEWMAN: Okay, and I note here, "M", premium lower than other available markets, was that on the other form?

MR. SIMPSON: I don't know.

MS. NEWMAN: Okay, alright, is there an obligation in New Brunswick and Nova Scotia for the insureds to be told that they're placed in FA?

MR. SIMPSON: Can you clarify for me what you mean by obligation, please?

MS. NEWMAN: Well, I'm just looking at column three here, was the reason for placement in Facility Association revealed to the applicant, is there any obligation for the broker or the servicing carrier to explain to them?

MR. SIMPSON: It's my understanding that there's not a legal obligation to do that.

MS. NEWMAN: Okay.

MR. SIMPSON: We certainly encourage brokers and agents, and I believe that the summary form in both provinces shows that somewhere well over 90 percent of applicants are informed that they're being insured through Facility Association, and that's coupled with the changes to the application and the brochure we've talked about, the efforts we're making to make sure that people are not insured through Facility Association unaware of it.

MS. NEWMAN: Okay.

MR. SIMPSON: At one time there was a desire presumably in the regulatory community to make sure the consumer was not aware they were insured through Facility Association, so things change with history and we've gone 180 degrees away from that.

MS. NEWMAN: And it sounds like an improvement for sure.

MR. SIMPSON: It does to me too.

MS. NEWMAN: Okay, finally, we'll move on to the implementation section of questions, and I only have a few. The first one being, clearly we're not going to get a decision that would allow implementation for February 1, I think everybody has accepted that. How much time does Facility Association need from the date of the Board order, so whatever that date may be, to the actual implementation?

MR. SIMPSON: Commonly, that's 105 days, our servicing carriers tell us they need three months to implement a rate change. We've tried to get them to speed that up from time to time, but with all the programming that's involved, the printing of manuals, the preparation of manual pages, things of that nature, just from a practical matter, and then that 105 days also incorporates time for Facility Association staff and Mr. Pelly to do any final preparation or changes for those rates and rate pages to hand them over to the servicing carriers so that they can begin their work.

MS. NEWMAN: Okay, so 105 days would be the proposal of FA for the lag time from the date of the order to the implementation.

MR. SIMPSON: Yeah, I should clarify ... yes, that is true, and I should clarify that's calendar days, it's not working days.

MS. NEWMAN: If the Board orders changes to the FA proposal, will you need extra time for that implementation phase?

MR. SIMPSON: That's certainly possible. It would depend entirely on the nature and extent of the changes but we'd want to make sure everybody at the Association, my staff and our servicing carriers were making their very best efforts (inaudible) to do things as quickly as possible.

MS. NEWMAN: Will changes need to be made to the proposal to reflect this delayed implementation? I have put this question to Mr. Pelly, and I think he effectively deferred it to you, as the CEO of FA to advise the Board as to whether you would require, or FA would require changes to the proposal if the date is no longer February 1.

MR. SIMPSON: Changes to the rate level?

MS. NEWMAN: Proposed rates, yes.

MR. SIMPSON: Yeah, I believe that we would look for a reflection of the trend factor changes as we did with our last filing, the filing that was submitted in May 2001. As I recall the decision from the Board reflected that and I believe we would seek that again.

MS. NEWMAN: Okay, that's the only change that you would see would be necessary?

MR. SIMPSON: That's the only one that I can think of at present.

MS. NEWMAN: I wanted to leave it to you to make any comment that you feel hasn't been made to date on the changes that are either set out in the Mercer report, or changes to the proposal that have been raised throughout this hearing, that you feel require your comment because they might pose such a big impact upon FA, or because some piece of evidence hasn't been brought forward. Is there anything that has been suggested to be changed that you feel just hasn't been talked about enough, or something should be said about, because the Board has got to make a decision here and, you know, we don't want there to be some major gap.

MR. SIMPSON: I appreciate that opportunity and I respect those responsibilities of the Board. This has been a thorough hearing thusfar, and I can't think of any significant topic that hasn't been covered so far, but if anything comes to mind, perhaps I can drop you a note.

*(11:15 a.m.)*

MS. NEWMAN: Certainly, one last point, and that has to do with the level of the rate change that would be affected by these proposed rates. You know, we have accident and conviction surcharge, we have the CLEAR system, and we have just the rate changes themselves, and there's going to be some significant rate changes for insureds. Do you think that it is wise for the Board to implement some sort of cap or some other mechanism to delay the implementation of the extent of these rates upon the insureds? Should the Board be concerned about rate shock effectively?

MR. SIMPSON: Other than a decision on the ... perhaps I'll approach it this way, other than a decision on the rate level itself, New Brunswick, the filing was very very similar to this one, and the Board there did not impose such caps, so ... and given the high turnover of the Facility Association book, I'm told that it's about 50 percent a year, which is significantly higher than you'd experience in an individual company, I would be, and given the cost that would be incurred as a result of that, the benefits that would flow through to anybody as a result of that, and given that the changes, aside from what I've already described as a very significant change to the base rate level, the CLEAR implementation and the accident surcharge schedule are designed to be consumer friendly, if you will. I would be opposed to capping the rates. There's also the impact on the voluntary market if the rates are capped and are the non-standard writers restricted in their ability to write business in this province ... I would assume they would be, so the Board has a challenging decision before it, and has to balance off a number of factors, but no, I would not support capping of the implementation.

MS. NEWMAN: Those are all my questions, Mr. Chairman.

MR. SAUNDERS, PRESIDING CHAIRMAN: Okay, thank you, Ms. Newman. Anything on redirect, Mr. Whalen?

MS. NEWMAN: Um ...

MR. SAUNDERS, PRESIDING CHAIRMAN: Oh, I'm sorry, we did promise the Consumer Advocate another ...

MR. O'FLAHERTY: Thank you, Mr. Chairman, I just have a couple of questions. Perhaps we can turn to the last document, undertaking number three, first, and my friend has asked a number of the questions that I would have wanted to ask you, in any event. That's the binder control register.

MR. SIMPSON: I'm sorry, yes.

MR. O'FLAHERTY: It's your understanding, under the section which is headed "alpha codes".

MR. SIMPSON: Yes.

MR. O'FLAHERTY: Do these represent actual reasons for placement in Facility Association?

MR. SIMPSON: How do you mean, actual reasons?

MR. O'FLAHERTY: You know, are there persons who fall under each of these particular categories? Well some of them are combinations of categories, but the ones that represent just a category.

MR. SIMPSON: And I don't think that they are mutually exclusive either. They could be ...

MR. O'FLAHERTY: Exactly, yeah.

MR. SIMPSON: You know, somebody could fall into one, and I think by asking for the code, we're asking for the dominant reason, if you will, or there may be more than one, and this, the only thing I can give you really in response to that is that this was developed by underwriting staff in conjunction with rates and rules, so presumably it's a reflection of (a), market practices, and (b), concerns that have been noted in the regulatory and the public sector ... the issue of senior drivers that I mentioned earlier. That's why these categories are here.

MR. O'FLAHERTY: Okay, so you don't know, and at this stage, unless we have that undertaking regarding the compiled results, you don't know if there are persons who are placed in Facility Association as a result of, as one of the factors being that they are senior.

MR. SIMPSON: That's correct.

MR. O'FLAHERTY: Okay, I want to ask you a couple of questions about the Consent No. 3, which is a series of documents, distribution assessments. Can I ask you if these figures, these appear to be a publicly filed document or filed pursuant to a regulatory requirement, is that your understanding?

MR. SIMPSON: I'm not sure of a regulatory requirement, to be honest with you, when I joined Facility Association, this memo was being distributed to all superintendents of insurance, and I asked staff to include the various boards on the distribution of this memo as well as to the CEO's, if you will, the CEO community of our members.

MR. O'FLAHERTY: Yes, I noted in the legislation, it did require that the Superintendent be provided with whatever information he or she saw fit. Can I ask you if this information represents audited results of Facility Association, and by that I mean by your outside auditors?

MR. SIMPSON: The financial statements of Facility Association are audited by an independent auditing firm. The participation reports would be a review as a part of that audit process, but the participation reports themselves do not have an audit letter on top, but they flow into the audit process that culminates in the letter that accompanies the financial statements, so these are based on our participation reports which are part of the annual audit process, but are they independently audited and provided with a separate cover letter, the answer to that would be no.

MR. O'FLAHERTY: Okay, now these are separate from ... yesterday you referred to a monthly distribution report or memorandum that gets sent out to the members, is that correct?

MR. SIMPSON: I think I was talking about the monthly participation report, and I think that was this morning.

MR. O'FLAHERTY: Okay.

MR. SIMPSON: I may have mentioned it yesterday as well, but that is provided to all members and that is to allow them to track month by month for their own accounting purposes, the impact of Facility Association on their financial results. How they use that participation report is a matter for their decision.

MR. O'FLAHERTY: Sure, but that's not this document. This is an annual report, or a series of annual reports.

MR. SIMPSON: This is based on the net operating result as of June 30th, 2002, as reflected in our participation report.

MR. O'FLAHERTY: Okay, now, can I just look at the figure in, the first one right on the top, because yesterday you will recall, I was asking you a series of questions about how the 1997 filing and the increase that was requested for 1997, how the financial results of FA had worked out afterwards. Does this figure of $4 million, and I'm looking in the column 1998 for Newfoundland ... does this figure for $4,760,106 represent a final total for that accident year?

MR. SIMPSON: The short answer to that would be, I believe, no, because the long, the colloquial term for liability claims is long-tail.

MR. O'FLAHERTY: Right.

MR. SIMPSON: They can go on for a long period of time, years and years, certainly more than three or four, so that is accident year 1998, I think the actuarial word is "developed" as of June 30, 2002. We may see further development from outstanding claims still from that year.

MR. O'FLAHERTY: But there's provision made for those claims as well?

MR. SIMPSON: Through the valuation actuarial work there is provision made for those, that's correct.

MR. O'FLAHERTY: So that's the amount that's been paid out to date based on that year in this jurisdiction.

MR. SIMPSON: For 1998, yes.

MR. O'FLAHERTY: Okay, now that particular, and I think the document I was trying to make this point with was DJS-2, which is obviously a much blunter tool than this one. Can I just bring you to that for a second?

MR. SIMPSON: Yes.

MR. O'FLAHERTY: Now DJS-2 does deal with the issue of the distributions, which is this particular document, and that's the far column to the right?

MR. SIMPSON: Yes.

MR. O'FLAHERTY: But it also deals with the net premiums for that given year. Now is that number a solid number, or will that change?

MR. SIMPSON: To my knowledge that's a solid number.

MR. O'FLAHERTY: Okay, so the premiums in that year were $13,287,000?

MR. SIMPSON: For what year, I'm sorry?

MR. O'FLAHERTY: 1998, I'm sorry, and then the, if we go back to this chart, return to members so far for that year is $4,760,106.

MR. SIMPSON: Okay, the premiums written are based on the fiscal year, and the accident ... or pardon me, the assessment and distribution is based on an accident year.

MR. O'FLAHERTY: Okay, and what's the difference, is it one is an actual calendar year, is it?

MR. SIMPSON: You're asking me to define accident calendar year, and it's my understanding that the definition very briefly is accidents that occurred in 1998.

MR. O'FLAHERTY: No, no, I understand that, but I think we understand from the evidence that accident years close off as of a December 31st date?

MR. SIMPSON: Yes.

MR. O'FLAHERTY: And when do the premiums written close off as of, the same December 31st date?

MR. SIMPSON: I'm not sure they close off but the premium is written today, so ... and then it starts, and one 365th of it is earned today, and the second 365th will be earned tomorrow. That's briefly, you know, what's written, and what eventually ... written and earned eventually match up, but there are some timing issues in there, and that's about the extent of my insurance accounting knowledge right there.

MR. O'FLAHERTY: And I'm certainly not trying to be obtuse here, and I don't think I understand your point then. We have $13,286,000 in premiums written in 1998.

MR. SIMPSON: Yes.

MR. O'FLAHERTY: And then when we look over to the 1998 AIX, there's a $4,760,000 return to the members. Now, you were, you're indicating that perhaps those, there's a timing issue between those two numbers?

MR. SIMPSON: Well, I'm just saying that there is ... this is based on accident year and the premiums written is based on the fiscal year, so there very could very well be a timing difference. I don't have intimate knowledge of how the numbers interrelate.

MR. O'FLAHERTY: Is your fiscal year based on a December 31st year end?

MR. SIMPSON: No, it's not, it's October 31st is the year end.

MR. O'FLAHERTY: Okay, so when you calculate premiums for 1998, you're not talking about the premiums that are in November and December of 1998?

MR. SIMPSON: Under this net written premiums, it's the, as the column indicates, it's at the end of the fiscal year, as of October 31st ... at the top of the premiums written (inaudible).

MR. O'FLAHERTY: Can you indicate to me where that says that on the form?

MR. SIMPSON: I'm sorry, I'm on DJS-2.

MR. O'FLAHERTY: Yes.

MR. SIMPSON: And for fiscal year, on the top of the column where it gives all the years, it says fiscal year, October 31st.

MR. O'FLAHERTY: Okay, thanks.

MR. SIMPSON: Yeah.

MR. O'FLAHERTY: Okay, so still then, it's not possible really to match up these figures then identically one to the other.

MR. SIMPSON: Well, I don't think so. Mr. Pelly, I think, would have been able to provide more assistance in this matter. I believe our audit partner *(phonetic)* gave a pretty thorough understanding of how the

Facility Association accounting works at the last hearing. A review of that transcript might be helpful but we're beyond the depth of my knowledge here.

MR. O'FLAHERTY: Okay, the last document that I wanted to ask you about today was this document, Facility Association, undertaking number five.

MR. SIMPSON: Yes, the consumer information brochure we've been discussing?

MR. O'FLAHERTY: Yes, and is this document sent out to consumers in this province?

MR. SIMPSON: Yes, it is. It's sent out, as I mentioned yesterday, well, we've directed our servicing carriers to send it out. I have not conducted any kind of audit to ensure that it is being sent out, but I'll take it on faith that they're doing what they're supposed to, and they're sending it out with new and renewal business to people insured through Facility Association insured in Newfoundland and Labrador, and the three other Atlantic Provinces.

MR. O'FLAHERTY: Okay, I just have a, I just have a question about the fifth question and answer, why is it important for me to know about Facility Association.

MR. SIMPSON: Yes.

MR. O'FLAHERTY: A couple of questions about that. Yesterday we spoke at some length about the statement that's contained in the third sentence of the answer, which is the cost ultimately will be reflected in higher insurance premiums for all drivers in that jurisdiction.

MR. SIMPSON: Yes.

MR. O'FLAHERTY: Now, I'm not looking to go back over that topic again, I want to follow it ... and then it follows into another statement. Conversely, if Facility Association generates a surplus, those funds can be distributed to all automobile insurance companies, helping them to control costs. I'm wondering if you can explain to me the last phrase in that sentence, helping them to control costs. What is your understanding of what's meant by that?

MR. SIMPSON: I'm not sure that, it's been a while since I've had a look at this.

MR. O'FLAHERTY: Uh hum.

MR. SIMPSON: If they receive a distribution from Facility Association, presumably they can use that in their business if they so choose.

MR. O'FLAHERTY: Are there any restrictions based on the distributions that are sent by Facility Association to the member companies?

MR. SIMPSON: Restrictions in what sense?

MR. O'FLAHERTY: Well, that they must be applied to control costs, for example?

MR. SIMPSON: No, I think relying on the competitive market is the ultimate reliance for cost control to consumers.

MR. O'FLAHERTY: Okay, so the money is just sent to the member companies, but there are no strings attached with that money.

MR. SIMPSON: The members either receive a cheque or they receive a letter of assessment, and the cheque is accompanied by a cover letter describing the basis in very brief form as to why they're receiving a cheque. They don't just get an envelope with a cheque in it.

MR. O'FLAHERTY: Okay, but there are no strings attached to the funds.

MR. SIMPSON: That's correct.

MR. O'FLAHERTY: Okay, and which brings me back to DJS-2. When we spoke yesterday about this document, I had asked you whether all of these amounts which were indicated as assessments were paid out amounts. Now, when I, when you were testifying this morning, I had the sense that the September 2002 results were somehow not a full year's results. They were, you know, perhaps a ... you know, a partial result for 2002, am I correct on that?

*(11:30 a.m.)*

MR. SIMPSON: This is based on our, every month our accounting staff prepares draft financial statements on an unaudited basis for internal use. This number here in the excess deficiency of revenue over expenses, net premiums written is based on those interim financial results. The assessment to/from members that's identified there, and I don't know why the number is out by $12.00, but that is based on Consent No. 3, Facility

Association bulletin *(phonetic)*, FO2-017, as actual dollars paid out.

MR. O'FLAHERTY: Okay, so I see the distinction, so the 1.527232 figure is, relates to the annual document which was just placed in evidence this morning.

MR. SIMPSON: That's correct.

MR. O'FLAHERTY: And the $5,761,000 is based on unaudited internal review on a year to date running total basis.

MR. SIMPSON: That's 11 months of experience, yes.

MR. O'FLAHERTY: Okay, alright, I think those are all my questions. Just let me just quickly look back through. Yes, one of the other questions, and it doesn't really arise from the documents, but I just wanted to understand this because I had reviewed some of the material before as well. I thought you testified this morning that the servicing carriers were cutting the cheques for settlements and, you know, that, out of the funds that they had in their possession, but I had some understanding that all of the cheques were being actually written by Facility Association, which would then allow them to do these running totals. Do you have any indepth understanding of how the banking system works for Facility Association?

MR. SIMPSON: The short answer is no, but is your question a cheque to ...

MR. O'FLAHERTY: To a law firm who represents a claimant, for example.

MR. SIMPSON: The cheques there that would be written by, to my understanding, which as I've said is limited, for the uninsured automobile fund that we administer on behalf of the province, those are Facility Association cheques.

MR. O'FLAHERTY: Okay, so I may be confused about that.

MR. SIMPSON: I'm not going to testify as to your mental state, Mr. O'Flaherty, but I don't believe that routine claims payments made by servicing carriers are ... those are ...

MR. O'FLAHERTY: So those are made by Royal and Sun Alliance or whoever.

MR. SIMPSON: Those aren't mailed out through our office, yes.

MR. O'FLAHERTY: Okay, and then the net balancing that you have done takes into account those payments that are made locally, let's say on a claim here by ICON or whoever.

MR. SIMPSON: That's my understanding, yes.

MR. O'FLAHERTY: And finally on the servicing carrier fees issue, if I have this correct now, the servicing carrier receives ten percent of the written premium.

MR. SIMPSON: I believe that's what's in the plan of operation, yes.

MR. O'FLAHERTY: Plus at least nine percent of the earned premium for claims expenses.

MR. SIMPSON: Yes.

MR. O'FLAHERTY: Plus the cost of the driver abstracts which are out of pocket dollar amounts.

MR. SIMPSON: There's certain direct (inaudible) reimbursements, and it's my understanding that would be one example, yeah.

MR. O'FLAHERTY: Plus what you called extraordinary expenses which could come up.

MR. SIMPSON: Well, they have the opportunity through the plan of operation to apply to the board of directors for reimbursement of extraordinary expenses. Whether those expenses are, in fact, reimbursed, of course, is a matter for the board to decide.

MR. O'FLAHERTY: So that's the total of the payments that are made to a servicing carrier, or can be made to a servicing carrier?

MR. SIMPSON: I think you omitted the one percent service fee, I believe it's one percent, .9 percent.

MR. O'FLAHERTY: I had actually had that under the ten percent, because the servicing carriers in Newfoundland are nine percent, I think, plus one percent.

MR. SIMPSON: There we go. I stand corrected, thank you.

MR. O'FLAHERTY: And the, the cap (inaudible) is nine percent and 16 percent of the claims expenses.

MR. SIMPSON: That's my recollection from the accounting and statistical manual *(phonetic)*, which is on the website, and we could check that but ...

MR. O'FLAHERTY: So it can go as high as 16 percent but can never go below nine percent.

MR. SIMPSON: That's correct.

MR. O'FLAHERTY: Okay, thank you once again for your patience.

MR. SIMPSON: Thank you.

MR. SAUNDERS, PRESIDING CHAIRMAN: Thank you, Mr. O'Flaherty.

MR. O'FLAHERTY: Thank you, Mr. Chairman.

MR. SAUNDERS, PRESIDING CHAIRMAN: Mr. Whalen, redirect?

MR. WHALEN, Q.C.: Thank you, Mr. Chairman, just to tidy up a couple of points. Mr. Simpson, Consent 3 and BJS-2, I just want to deal with those to see if I understand how they work. First of all, Consent 3, as I understand it from your evidence, it's a report that has been sent annually to the regulators and is now going to not just the regulators, but also ... I'm sorry, to the Superintendents, and is now also going to the regulators.

MR. SIMPSON: Yes.

MR. WHALEN, Q.C.: And the, you might ... did I understand you to say, or did you intend to say that this figure in Consent 3 are the operating results, or is this a settlement of account based on net operating results?

MR. SIMPSON: I'm sorry, the latter part is more precise. It is a settlement of account based on the net operating results as the correspondence indicated, as of June 30th, 2002.

MR. WHALEN, Q.C.: Okay, and the figure for Newfoundland in that column on Consent 3 really gets us to the right hand column in DJS-2.

MR. SIMPSON: That's correct, yes.

MR. WHALEN, Q.C.: So those figures actually match up, other than the small error in numbers.

MR. SIMPSON: Yes.

MR. WHALEN, Q.C.: Okay, now, I just want to deal briefly, if I may, with the undertakings that were provided and the number two, which is ... sorry, number three, which is the Facility binder control registry concept, which I think we reference in our earlier hearing and the evidence will show that it was kind of encouraged to be done here in this jurisdiction, but it hasn't been, but the point I want to deal with you is, these categories, do I understand you to have said that, that this is an attempt to capture what the market practice is for assigning insureds to Facility.

MR. SIMPSON: That's correct, we have to take all that come to us. We don't determine how or when or why people come to us.

MR. WHALEN, Q.C.: Yeah.

MR. SIMPSON: They do and we have to take them, and this is an attempt to ascertain in a broad outline the reasons they do.

MR. WHALEN, Q.C.: Yes, because there is a number of questions about this, and sometimes the implication almost seems to be that Facility creates these designations, Facility uses these reasons somehow, but really this is a reflection of what the industry does.

MR. SIMPSON: Well, it's been developed at the committee level by representatives with some pretty senior underwriting experience, so around the table there's a pretty good general wisdom about industry practice, and that's reflected in the codes.

MR. WHALEN, Q.C.: Now, so as I understand it, you don't accept or reject coverage on the basis of any of these categories.

MR. SIMPSON: No.

MR. WHALEN, Q.C.: You're just trying to ascertain, like why are you coming here?

MR. SIMPSON: It's, from our standpoint it's for the purpose of gathering information that others, including the regulators, have indicated they find helpful, and as I indicated yesterday, so that the broker or agent when placing business through Facility, does so, if I may say so, in a conscious and thoughtful manner, and gives it some thought. Is this really, am I ... the thought process that we would hope would occur in the broker/agent's mind is really to apply their best expertise and say to themselves, is this really a risk that belongs in Facility Association, or is there another market for it.

MR. WHALEN, Q.C.: Exactly, but once a broker or an agent concludes that, for whatever reason, that they can't find coverage, or for some ... you have one category here which is, you have a lower premium, whatever that might be, that's not your choice. You can't reject, you must accept everyone who comes.

MR. SIMPSON: That's absolutely correct, that's our statutory mandate.

MR. WHALEN, Q.C.: And you cannot, you cannot refuse somebody coming in because the form is not filled out, or it's filled out incorrectly, or you don't like the reason.

MR. SIMPSON: No, that's correct as well, that's true.

MR. WHALEN, Q.C.: And you were taken by Ms. Newman to, and I don't want you to go necessarily there again, to the information request 9.2, where it listed a number of reasons why people may be in Facility, which is the response, and to illustration number five in the, in DJS-3, and again, there's a reference to 62.6 percent of new business having no accident or convictions, but again, you have no control over that in Facility.

MR. SIMPSON: No, we don't, and as I've discussed, the underwriting community has indicated that there's other reasons that are predictive of risk, are predictive of loss beyond accident and conviction record.

MR. WHALEN, Q.C.: Now, given those reasons in terms of percentages, that's a percentage of what's in Facility, 62 point something percent. There's another percentage which is how big the market is in Newfoundland, where it's ... I think it's around four percent now, compared to how big that percentage is in Ontario where it's ... even with a combined, two *(sic)* system, below two percent.

MR. SIMPSON: That's correct.

MR. WHALEN, Q.C.: Okay, now, there's been some discussion of price as a component of that, and we talk about that exhibit, we've moved to the right and moved to the left.

MR. SIMPSON: Yes.

MR. WHALEN, Q.C.: And you've indicated in this list that premium and availability of market is a factor.

MR. SIMPSON: Yes.

MR. WHALEN, Q.C.: So if we're in a jurisdiction, and I don't want to beat this horse to death, because everybody has touched on it, I think, if there's a limited market and a proximity of price, do you see that as being a factor of why Facility may have a greater population, that is a higher percentage of the market?

MR. SIMPSON: Very definitely and I think that one thing that's important is that it's been noted that our prices are among the higher in the marketplace, and risk being commensurate with ... and premium being commensurate with the risk, they should be at the highest end, and one follow on from that, that I think from a common sense standpoint is that the person that's buying that insurance is going to be pretty price conscious if they're paying, you know, a very significant dollar for their insurance, one would assume that unless they're extremely wealthy or extremely unintelligent, they're going to be shopping the market for a lower price than the one we offer, or the lower price than the one they're paying, so they could be with a non-standard writer who is, in fact, priced above us, and then move to us as they find out we offer a lower price.

MR. WHALEN, Q.C.: So the non-standard market, that's the grey market that we also refer to.

MR. SIMPSON: Yeah, I prefer non-standard market, but grey market is another term for it as well, but it's the same thing, yes.

MR. WHALEN, Q.C.: And generally speaking, do I understand you correctly that these are for-profit insurance companies that write in that high risk area, which is above the regular market, and in some jurisdictions below Facility?

MR. SIMPSON: Yes, that's correct.

MR. WHALEN, Q.C.: But if there isn't a big enough gap between Facility and the regular market, there is no opportunity for those people?

MR. SIMPSON: Well, that's correct, and just to elaborate on that, I think that there is a ... and especially in a time when costs, and therefore premium levels are rising, the person or the company that's taken the entrepreneurial risk to serve the customer in the non-standard market stands a real chance of being significantly squeezed out of that niche in the market that they've targeted, either through a delay in getting the adequate rate level, or the rates in the Facility Association being inadequate.

MR. WHALEN, Q.C.: Now, I think both Mr. O'Flaherty and Ms. Newman identified a concern, and particularly Ms. Newman, that Mr. Pelly has filed rates which he says this is what we require for rate adequacy.

MR. SIMPSON: Yes.

MR. WHALEN, Q.C.: And there has been the other concern expressed, and we may hear someone talk about it later, some of the independent people, that even with rate adequacy there may still be a very close proximity between Facility and the regular market, even if Facility were to get the rate that it has applied for, and even if Facility were to get somewhat of an increase because of the delay in implementation, and the normal market operates as anticipated, for instance, by Mr. Pelly, then the gap will not spread between Facility and the regular market, it will stay at that same proximity that we see in the chart that was put in showing the comparison of the percentages in the provinces, and that's a concern, and my question to you is could the difficulty there be caused because the regular market has into, componented into its (inaudible) cost recovery when it comes for a benchmark, and the non-standard writer also has when it comes to this Board for a benchmark, they have a profit component right in there, but Facility does not.

*(11:45 a.m.)*

MR. SIMPSON: Well, I think that's a, I would assume that to be a very real issue, particularly for the non-standard writers. In other words, if I was a non-standard writer thinking about taking that entrepreneurial risk I mentioned by servicing and serving that market niche of high risk drivers and vehicles, I have to be cognizant of the fact, I would assume very much so, that I am at risk of competing with what is in effect the cooperative entity with the full weight and financial strength of the insurance industry behind it, operating on a breakeven prospect, so I've got issues of solvency concern, being able to compete effectively, how do I compete with an entity that's operating on a not-for-profit basis, and generate a reasonable return to my shareholder. I would suspect that the way they do that is to hope that, you know, by applying underwriting techniques, they'll be just under where we are, but it can be a close run thing.

MR. WHALEN, Q.C.: And just two quick little points to clear up. One is with the implementation of CLEAR, and as I understand it, Mercer's have recommended caps for Newfoundland.

MR. SIMPSON: Yes, that's my understanding as well.

MR. WHALEN, Q.C.: And my understanding is that Mercer's are also the actuarial advisors for Ontario.

MR. SIMPSON: For the Financial Services Commission of Ontario, yes.

MR. WHALEN, Q.C.: Yes, and that you filed a similar proposal in Ontario for implementation.

MR. SIMPSON: Yes, we did.

MR. WHALEN, Q.C.: And are there any caps imposed in Ontario?

MR. SIMPSON: There are in the voluntary market, that level as I understand it is 35 percent, but no caps were imposed on the implementation of CLEAR for Facility Association.

MR. WHALEN, Q.C.: Now, do you know whether Mercer's recommended the implementation of caps in Ontario for the Facility market?

MR. SIMPSON: No, I don't. One of the advantages we have in a forum like this is it gets everything out in the open. The kind of discussions that FISCO has with their consulting actuary are not necessarily available to us. I guess, I suppose maybe we could explore freedom of information requests, or something of that nature, so I don't know whether FISCO had any conversation with Ms. Elliott or not regarding caps regarding the CLEAR implementation in Ontario. They certainly had every opportunity to do so. Whether that conversation took place or not, I don't know.

MR. WHALEN, Q.C.: So you don't know where she recommended not at all, or whether she recommended no caps, but in any event, there are no caps in Ontario.

MR. SIMPSON: That's correct.

MR. WHALEN, Q.C.: Now, there is one other brief area I just want to touch on and Mr. O'Flaherty asked you yesterday about the Suchar report, and I think it's on page 41 of the transcript, and he was ... this is before he had the document, and I think he was reading from his notes, and that may have been where the error that I suggest he made came from. He says on line 14 of page 41, "So when I look at the report, the Board's actuary concluded that the loss costs were, and I'm quoting now from the report, quote, consistently and significantly lower." And when he actually got the report, I think the report, which is on the next page, page 42, "Now the question I have ..." ... no, I'm sorry, it's up above, it's on line 4, and he's quoting again, and the words are, "appear to have significantly overestimated the loss cost", so do you know if there was anything in this report where they used the word "consistently overestimated, or consistently underestimated?

MR. SIMPSON: Going from recollection from Mr. Pelly's testimony, as I recall the statement was that the filings prepared and submitted by Mr. Pelly and his firm had not exhibited a bias towards consistent over or underestimation. I'm paraphrasing from memory.

MR. WHALEN, Q.C.: Yes, and if I could just read ... maybe I could give you that.

MR. O'FLAHERTY: I don't have a copy of that document here.

MS. NEWMAN: We have a copy here, what page reference is it?

MR. WHALEN, Q.C.: Page 15, and now when I give that to the witness I won't have a copy. I'm trying to reference there that you ...

MR. SIMPSON: Yeah, this is the report that the Consumer Advocate directed me to yesterday, and asked me to read a certain paragraph, so perhaps I could just start there and then continue on a little bit. So the paragraph that I was asked to read yesterday begins, "With the benefit of hindsight we have found that the filings made in 1992 through 1995 appear to have significantly overestimated the loss cost for private passenger, third party liability (see previous section). The 1996 filing may have overestimated as well, but the loss experience that stems from that filing is not mature enough to evaluate this as yet."

The next paragraph goes on to say, "The methodologies used in all the filings reviewed were generally accepted sound approaches. We did not detect any source of systematic bias in this area."

MR. WHALEN, Q.C.: Thank you, and in terms of the suggestion that Mr. Suchar has been consistently in any direction, my understanding that your last filing, he made a recommendation and I believe that even Mr. O'Flaherty will concede to this that it has proved not to be sufficiently adequate for events as they have transpired.

MR. SIMPSON: You mentioned Mr. Suchar, I believe you meant to say Mr. Pelly.

MR. WHALEN, Q.C.: Oh, I'm sorry, Mr. Pelly, yes.

MR. SIMPSON: But that's ...

MR. O'FLAHERTY: Yes, the Consumer Advocate that Mr. Pelly has been wrong on both sides.

MR. WHALEN, Q.C.: Yes, so he's been high and low, and I think if we look at, if we look at this report, and if you'll give me a moment I'll try to find the reference. (inaudible) the bottom of page 15. Maybe I'll have you read it, the bottom of page 15, Mr. O'Flaherty.

MR. O'FLAHERTY: Yes, thank you.

MR. WHALEN, Q.C.: And that's, this is the Board's actuary here now commenting specifically, the bottom paragraph. I apologize, Mr. Chairman, it's difficult to do this when we're passing around the same copy, but ...

MR. SAUNDERS, PRESIDING CHAIRMAN: You're talking about page 15 of Suchar's report?

MR. WHALEN, Q.C.: Suchar's report, the last paragraph in terms of ...

MR. SAUNDERS, PRESIDING CHAIRMAN: Yes.

MR. SIMPSON: Okay, "Many readers of this report will already be aware of this, but it bears repeating. Most actuarial projections will turn out to be incorrect to some degree because of the uncertainty inherent in projecting future results based on past experience. The best that can be done is to minimize the uncertainty by using the best methods and data available and try to avoid any hidden biases that would make it more likely for actual results to be higher or lower than projected." And then it gets into some technical description of loss development factors, etcetera.

MR. WHALEN, Q.C.: And in ... I guess in conclusion, Mr. Simpson, one would intuitively, or in a common sense way conclude that the more actuaries you have giving you opinion, the more likely you are to find common ground, but they could all be wrong.

MR. SIMPSON: I think it's almost certain that they'll all be wrong, but, you know, hopefully with a larger group, some sort of consensus would emerge, yes.

MR. WHALEN, Q.C.: Thank you, that's all I have.

MR. O'FLAHERTY: Mr. Chairman, could I suggest that we mark this document as an exhibit because we've all referred to different portions of it, and we've already got the executive summary in and it seems a little bit unusual to ...

MR. SAUNDERS, PRESIDING CHAIRMAN: Good idea.

MR. WHALEN, Q.C.: It's probably a good idea.

MR. SAUNDERS, PRESIDING CHAIRMAN: Where are we with the numbers.

MS. NEWMAN: We probably would call that an information item, wouldn't we, as it's a report that's filed with the Board sometime in the past, it would be information number six.

MR. SAUNDERS, PRESIDING CHAIRMAN: Six.

MR. WHALEN, Q.C.: This might be an easier one to copy because it's not ... are we going to mark that as a certain number?

MR. SAUNDERS, PRESIDING CHAIRMAN: Information six.

MR. O'FLAHERTY: Thank you, Mr. Chairman.

MR. WHALEN, Q.C.: That's all I have, Mr. Chairman.

MR. SAUNDERS, PRESIDING CHAIRMAN: Okay, it's not almost 12:00. We will proceed on with panel questions, but we'll do that after the break and we'll come back in fifteen minutes to conclude the morning, thank you.

MR. O'FLAHERTY: Mr. Chairman, I'm sorry, I know you've just gotten up, but before you go, we have four witnesses waiting outside, and I'm wondering if we might possibly be able to estimate how long the next phase will take so that we can perhaps send some of them on on their way.

MS. NEWMAN: Perhaps I'll deal with counsel on that during the break, if that's alright?

MR. O'FLAHERTY: Thank you very much.

*(break)*

*(12:20 p.m.)*

MR. SAUNDERS, PRESIDING CHAIRMAN: You had finished your redirect, Mr. Whalen.

MR. WHALEN, Q.C.: Finished, thank you, Mr. Chairman.

MR. SAUNDERS, PRESIDING CHAIRMAN: Okay. Commissioner Powell, do you have any questions?

COMMISSIONER POWELL: Yes, I have a few items to talk to Mr. Simpson about. Hopefully I won't be too long, all the various schedules and things that, hard to keep it in some sort of order so you don't duplicate too much. What I'd like to get at, when I look at this, I look at it as, if you take the high view, it's a relatively simple process at least from my perspective, and you can tell me how I got it wrong and I better go back and do my reading. Setting the rate, they're forecasted. You hire actuarial people who's experts, they do the forecasting based on the, certain historical data based on trends, and we had all that information explained to us, and as counsel said just before break, if you had enough of them you'd probably, all different opinions, but you'd probably get into a more focused rate setting process, and I guess to use some words that were put out when we were talking to actuaries, that maybe one of the two actuaries we had presenting evidence to us, they may be an outlier, if you had ten, and one of the challenges that we're going to have to look at eventually is the evidence, the judgements, the differences between the two actuaries we did have, but they do the forecasting and they say this is what the rate should be. The forecasting rates, my understanding, it's made up of various components, the largest cost built into the rates are the claims that people will make on those premiums that everybody paid to cover everybody's cost, and then there's the element put in for the overhead and less return that the insurer will be able to earn on the money they invest while they're holding these premiums, waiting for the claim process to work itself through, and there's, in the normal course of events, there's a small portion put in for rate of return for the insurance industry itself. I think Ms. Elliott sort of went, took the 20,000 (inaudible), and that's my understanding of how the rates are set. The profit element that is actually put into the actuary rate, my understanding, is relatively a small percentage of the rates themselves, anywhere from one to maybe upwards of five percent, so in terms of the total premium cost that you would pay, it's the, if the model followed through, as the actuary said, that the return for the industry would be relatively (phonetic) lowest percentage of the total premium paid. The challenge in the business is to get enough of them. Of course if enough people pay $1, you end up with a lot of dollars. But that's essentially the setting of the rates, am I sort of correct there?

MR. SIMPSON: In a general sense that's my understanding as well, and, you know, you reference it to being a relatively low margin business, yeah, I think that's true also.

COMMISSIONER POWELL: Yes. So the fact that FA do not build any profit into their rates or not, I mean, really from a dollar point of view, really not immaterial but it's not a big money thing in itself.

MR. SIMPSON: The Board did ask Mr. Pelly to recast some rates with a profit provision with a return on equity provision, and I don't have those numbers here in terms of what it would do to the rate that's been applied for here. It's my recollection that it would take the rate from the filed 41 to about 50 percent, and I think that was on a 10 percent ROE basis, but I could follow up with Mr. Pelly and provide an illustration of a rate with an ROE target, he's done that work, versus a rate without a profit provision built into it.

COMMISSIONER POWELL: That would be nice to have that. But once these rates are set, actuarial decided ... the challenge for the industry is to sort of develop a business model to manage the risk associated with these? I mean, that's the challenge for the industry, an actuary come in and say here are your rates, here's how things are going to be, here's how the future is going to unfold from our perspective, so the challenge from the industry, not (phonetic) FA but just the industry, say, is to manage that, this is the rate you're going to receive and to manage all the elements that's built into them, the claim costs, there's the overhead costs to the return on their investments. Their challenge is to put in the rate model to manage that.

MR. SIMPSON: That's correct, yes.

COMMISSIONER POWELL: Okay. And the biggest uncertainty in the insurance industry is the length of time before you're actually, results are really known, because we've seen, we have a number of these triangular charts in terms of I pay my premium in 1992 but if I happen to have an accident or claim in that year, based on that premium, could be up to ten years before it finally gets settled for a whole bunch of reasons, from a ... and these are built into their actuarial projection based on ... this is where the past comes in to help ... am I correct there?

MR. SIMPSON: The longer (unintelligible), as I understand, is particularly associated with the injury coverages ...

COMMISSIONER POWELL: Yeah.

MR. SIMPSON: ... liability and accident benefits.

COMMISSIONER POWELL: So the only thing that the industry would have to see how well the actuary did a projection is the historical financial data they get. Your financial statement is prepared, are actually what happened in that time frame, and so to see how an, how accurate an actuary was in their forecasting is to take that historical data and look at it and, in theory if, in a perfect world, if they had built in a three or four percent return on equity as a component, you look back over and do your triangular thing down and you say, oh yeah, great, great, great, the rates were good, but from a practical point of view that doesn't really work that way, but all these financial historical data is put there and somebody, if nothing more than to pass judgement, how good our actuaries are, because that's their ultimate test is that when they project the rates they built in these returns, and the industry must look and say is the fault our managing of those or our actuary was really on the low side, his or her projections. Would that be a true ...

*(12:30 p.m.)*

MR. SIMPSON: I think that's true. I think in a theoretical sense, if you will. In a practical sense sorting out those things that you talked about, how well the business was managed, these types of things, from the actuarial, which is more based on the loss costs, I think would be challenging, but theoretically I would agree.

COMMISSIONER POWELL: The thing that really having trouble getting my handle on, my mind around, is that the concept is great and I'm sure within the industry itself the large carriers or providers of insurance, they must do this internal analysis because everybody from the CEO to the person at the bottom, they all get managed (phonetic) on how well they perform, and so the actuarial component of the industry who's giving this advice, they must feel under pressure from time to time and some measure to be able to justify what they rejected in terms of what actually turns out, so they must have tools to manage that. I mean, the insurance industry, you get the impression they're well managed and well functioning part of our market, so I'm sure these tools must be there just the same as Loblaw's do the same thing to manage all the different components of their business, make sure they get their one or two percent return on their sales. Well, when I look at the financial statements, and trying, that are produced by FA, and trying to relate it to projection, it's just every time you try to look at it, you're always given a reason that something is not included. I wonder why would FA, I mean, they in Newfoundland had roughly four percent of the market, and they're based, and these rates are based on some actuarial device, why the financial statements don't reflect all the components that the actuary build into the rate forecasting, so historically we can look back and say, okay, they did manage their rates well and they did have a reasonable rate of return, but it seems like not all the elements that are built into the FA rates are reflected in the FA financial statements, so how can FA effectively manage that they're not there in the historical document?

MR. SIMPSON: I've not heard a direct concern expressed that way previously and I'm far from being an expert on financial statements, but there is certainly concern voiced at the Board level, and I think I alluded to that. When you start to see the financial results emerge as they do and when you're targeting a break even result and you're headed under water, that's when concern typically is expressed, you know, about the adequacy of the rate level and discussions are held, but in terms of putting something in the financial statements to go back so that you could look at each accident year as it's developed, I don't know if that's practical. That's something I would have to explore. The bulletin that we looked at earlier, Consent No. 3, gives a sense of on an accident year basis, how the experiences has unfolded through time, but beyond that I don't know of the tools that you speak of. It's something I could certainly explore with our financial people, with our Accounting and Statistical Committee, with our auditor, to see if there's a way that we can provide more detailed information through the financial statements. I know that or I'm led to believe that through time various notes have been developed for the financial statements to provide more explanation to what is a pretty unique entity in terms of the way that we operate, so in terms of developing that on a going forward basis, that's something I'd be more than willing to explore.

COMMISSIONER POWELL: I wasn't concerned going back and identifying all the costs, say, in the 1997 year, with all the revenue, but each year, as Mr. Pelly, there's a provision put in your balance sheet showing, I forget what the exact terminology, it's like accrual for unpaid claims, and it's actuary best estimate, and he suggested that you have another actuary do the same analysis, it would be a different figure, I appreciate that, but given over a period of time they're all using the same method, the claims are what the claims are and, you know, that'll work itself through. But I notice there in the, one of the schedules we saw, and I don't think it's really important we look at it, Superintendent of Insurance had taken the data and they had adjusted the, I think the figures are shown in DJS No. 2, showed the excess rate and took a deduction for health and levy tax off and came up with a figure, and I think he used the suggestion that over this period of time we've had a return of two and a half percent, which actuarially results based on projection, you thought was very good. I have no problem and probably that's accurate as you'll ever get, but my thought was when I saw it, I said, why, why aren't you doing this on a regular basis, the estimates ... we got ... we have an estimate on a financial statements for the unpaid claim, you hire an expert, an actuary, they give their best estimate doing it. The other components that are missing each year that really reflect what went on, that the FA, based on the best information we're going to lose our shirt this year or we're going to make a lot of money, whichever way it turns out, are not incorporated in the statements, so they're more transparent, and rather than showing up at a hearing and saying, well, here's our figures but they're not our figures because this is missing and that's missing, I can't understand why an industry like the insurance industry would want to be in a public domain apologizing for whether it's made a profit. You didn't project to have, didn't plan to have a profit, but based on the best information we are going to have a profit this year because this is our revenue and these are our actual costs and our projected costs based on the best science we have available. Isn't everybody better off, even though you forecast your best rates, that the industry through a marketing campaign, a public relations campaign, through involvement of the brokers, the insurance providers, the customers, the claims are down, that we do have a profit, so therefore on a forward going basis we can almost anticipate that we should have lower rates? I mean, wouldn't that be a more proactive approach as opposed to the customer looking, saying, well, you know, 1998 you made $10 million, why do you want to, you haven't used all that profit up yet, why increase my rates this year, you know? The message, I get the feeling that, you know, there's, the cart and the horse is mixed up. I mean, do you want ...

MR. SIMPSON: I've been in the industry for 15 1/2 years and I find it tough to understand, so I think there's always improved, room for improvement in how we talk about information and how we display that information, and I think the financial statements, as I say, I'm led to believe they've evolved over time to disclose more information. In terms of how, what Mr. Pelly has describe to me as a financial paradigm and the actuarial paradigm, his words, interrelate, is somewhat mysterious to me and I hope to learn more about it as time goes along, but in terms of, you know, claims experience leading to lower rates, we had a period following some product change in Ontario, 1996, where, according to the regulator there, rates went down for 11 straight quarters, 33 months, and the industry and the regulator were trying to do a pretty good job of publicizing that and lower claim frequencies, and there are public relations campaigns being done by the IBC about increase in claiming behaviour and what a person can do to help lower their own insurance costs and things of that nature, but certainly these matters are not easy to understand. I don't have a detailed explanation, as I say, of how the actuarial and the financial paradigms interrelate. That's more for someone of Mr. Pelly's expertise, but to the extent the Board would like to see more of that type of information on the financial statements, I'm happy to carry that message back.

COMMISSIONER POWELL: It just seems to me you shouldn't have to be apologizing or, that's my words, or trying to explain financial data. They should be self-explanatory. I realize, an accountant, I find it a lot easier, but I look at a financial statement as a good novel and it should be an easy read, but when you get the situation that this is it but, the first but, but then the second but, then you ... I hesitate to say this in a public forum but when I was listening to some of the comments about the financial statements, the last time I heard a large entity trying to explain so many off balance sheet items was the largest bankruptcy in North America, Enron. That was their biggest problem, they had too many things off their balance sheet and nobody really knew where they stood. So FA financial statements almost seems like there's so many things off, and I haven't seen (phonetic) why. They shouldn't be. As Mr. Pelly says, the facts are facts, results are results, and in theory the last dollar in got to pay the last dollar out and it balances out, and so the financial statements should reflect that, which I don't get a sense they do now. DJS No. 3, I wish I had that, Illustration No. 5, when Mr. Pelly was here, and BGP No. 4, the one where I asked Mr. Pelly how we can get to the lower right-hand corner as opposed to the upper left-hand corner. The DJS No. 3, that's the Facility one, put into the Nova Scotia hearing. Illustration No. 5, that's the one with the percents, and the other is BGP No. 4. That's the comparison of the written premium chart ...

MR. SIMPSON: I have both of them now, thank you.

*(12:45 p.m.)*

COMMISSIONER POWELL: When Mr. Pelly gave his evidence I asked him about the BGP No. 4 and how we can get ourselves over to the lower right-hand corner and I asked him for more information to be turned out that in Ontario they, I think by legislation, they have another category other than FA and when you put those figures back in, gets sort of Ontario closer to where we are, but when we looked at BJ (phonetic) No. 3, it gave the explanation that something around 60 percent of our, FA insured population don't really have any accidents or convictions and really are not the cause (phonetic) it would appear, not the cause (phonetic) of the high claim, and since we have, my quick math, that if we got 4 percent of the population and 60 percent of them do not have any claim, that would mean there's probably about 1 1/2 to 1.6 percent of our population, are costing (phonetic) most of the claims in FA, and so that percentage then would get fairly close to the Ontario one as shown on BGP No. 4. So my question, and I don't know if you can answer this or not, but has FA run any models on what the premium would be for those 40 percent of FA clients that let their premium (inaudible) if they were the only ones in FA?

MR. SIMPSON: No, we haven't. I'm not sure that, you know, in terms of the availability of the detailed statistics to do that, but I would just say that these are people insured through FA that have no, as I mentioned earlier, at fault convictions or, pardon me, at fault accidents, the prior five years, and convictions, convictions in the last three years, and that I don't believe it's just the 40 percent that have had a conviction or an accident prior to being insured through Facility Association that are having the claims in FA. I have to assume, as I said earlier, that the underwriting community is doing its job and that there are other factors that are predictive of risk as well beyond driver behaviour, type and use of vehicle for example, so to really get at that we'd have to slice down through the existing book and take a look at who's making the claims, who's having the losses and what was their prior history to being insured through Facility Association.

COMMISSIONER POWELL: But assuming that, and I can appreciate you may not have, from Facility's point of view having all that data, but if we assume that DJS figure, the 60/40 number, I'm using it, it's reasonably accurate, but, and if we assume that 40 percent was (unintelligible), that would get us over to the right corner if there's only 1.4 percent, and the premium rate then would be roughly between 3 and 350 percent of the normal rate versus the low percentage, 150 percent or ...

MR. SIMPSON: And I think that's, to some extent that's what the changes to the accident and surcharge schedule that are proposed are designed to do so that those with more prior accidents, at fault accidents and convictions are paying a higher premium relative to the overall four percent of the population that's insured through Facility Association, so we might see some movement in the direction of that chart as a result of that.

COMMISSIONER POWELL: Looking at that, there was some question about the increase in surcharge and the discount, and again these figures, got to be careful because they can distort and you really actually got to get down into the actual ... when FA did their analysis for the surcharges and that, were these type of figures here taken in? I mean ...

MR. SIMPSON: The ones illustrated in BGP No. 4?

COMMISSIONER POWELL: BJS *(sic)* No. 3. This is the first ... up here, I didn't realize he had a breakdown of the BG 4 and knowing that roughly 40 percent of those are population more likely to have convictions or accidents or claims. These are actuarial questions I'm asking you now.

MR. SIMPSON: Yeah, they are and I'm having a tough time with them. I apologize, Commissioner Powell.

COMMISSIONER POWELL: Okay. Looking at this here, I get the impression that surcharge should be higher and the discount should be higher.

MR. SIMPSON: In the ... and that may be, and as we go forward, we're working with the IBC ... I've got a voice mail since coming down to St. John's from one of their people. We were trying to get together before Christmas but that didn't happen, on how we can get more detailed information about the FA population in terms of what may be available now. They're going to a new technology platform over the next two to three years, which apparently is, IT people promise a lot of things but their promise is it provides more detail in a more timely fashion and we're working with them to work to obtain that, so the accident and surcharge schedule, I think we regard that as an initial step with incomplete information that we do have but we believe that it's a step in the right direction and as more detailed information becomes available and we develop more experience with it, it's not something that we intend to be cast in stone, but because of the ... we have a sense that this is a good way for us to move. From a public policy standpoint, from a risk standpoint, it's a good way for us to move and other regulators in other jurisdictions have agreed with us, but it's not necessarily the be all and end all of accident and surcharge schedules. As we develop a more detailed information, that we're working to do with the IBC, and as we develop more experience with it, we expect in fact that we'll see it shifting somewhat over time based on our experience as it develops, but we wanted to get things started moving in the right direction and that's the best way I could sum that up.

COMMISSIONER POWELL: As a person who is insured under FA and the broker gives me the good news, is the fact that not only I'm in FA but I'm in the higher end of FA because, conviction, because of accident or whatever, that ...

MR. SAUNDERS, PRESIDING CHAIRMAN: Because of your age.

COMMISSIONER POWELL: Oh, because of my age, but the ...

MR. SIMPSON: Pardon me, I think ...

COMMISSIONER POWELL: There's our two step approach. First of all I got to get myself in the lower end of FA before I can get out of FA or do that not necessarily ...

MR. SIMPSON: That depends on the voluntary market. In other words, we may have rates at the lower end, as you describe it, of FA, where if you qualify for something, our clean driver discount or our base rate or whatever, and you may have opportunities in the non-standard market, you may have opportunities in the standard market, depending on the extent of the range of rates available through individual companies, because in addition to non-standard writers, some of the standard mass market companies have rates to accommodate non-standard business for various business reasons. In other words, they may insure a whole household. You know, they've got a home, a few cars, at one risk and one thing and another, and one risk, driver or vehicle in the household is looked at in isolation, might be an FA risk, but it's one that because of the client profile with the company, they would desire to keep, they would have a rate for that, so I would hope that as we move things in this direction, we get more and more to really the residual end of the market, you know, the one or two percent, and that we're creating mechanisms, if you will, to encourage people to move back to the voluntary market.

COMMISSIONER POWELL: Schedule DJS No. 2 ...

MR. SIMPSON: Yes.

COMMISSIONER POWELL: ... what struck me when I looked at this schedule, I know net premium is written there, September 2 is not complete data for the fiscal year, but it's about a 50 percent increase in the net premium. There was a rate increase, I think, supposed to be reflected in 2002 of I think ten percent, I think was mentioned. I presume the other increase is just population?

MR. SIMPSON: The increase in premium?

COMMISSIONER POWELL: Premium ... yeah. For instance ...

MR. SIMPSON: We're seeing our premium volumes increase in all jurisdictions in Canada with the possible exception of the territories, and 50 percent increase is pretty significant although at a relatively small premium base relative to the overall industry, but on our own base it's a significant increase, and it's a much more dramatic increase in Nova Scotia, New Brunswick. It would be over 100 percent for sure, I don't have the exact numbers with me here, in that same time frame, and it can be a reflection of a number of things that we've been discussing through the hearings, companies tightening their underwriting guidelines so that there is more of an availability issue, more rate activity on behalf of the companies that would move on this chart, still closer together to the voluntary market on an average premium basis. The Board would have those premiums presumably as a result of the filed rates for the companies, probably more recent information than we have, but we're seeing the volumes increase in all jurisdictions and certainly on a percentage basis more dramatically in other provinces in Atlantic Canada than Newfoundland and Labrador.

COMMISSIONER POWELL: You may or may not be able to answer this but I'll ask the question anyway, is that our rate benchmark insurance across the board the last two years essentially is flat, on the average the base, no increase at all, so when you see this 50 percent increase in Facility business you sort of wonder why should there be such a tremendous increase here now.

Are you familiar with the other provinces, Nova Scotia, New Brunswick, has their benchmark across the board increased significantly or anything or ...

MR. SIMPSON: Nova Scotia doesn't have rate regulation as such of voluntary market companies. We're the only insurance entity that the UARB down there deals with. New Brunswick has a file and use, in other words, the companies have to, as I understand the system, provide their rates to the PUB there and if they don't hear back from the PUB within 30 days they're free to use them, and what we hear and what we see, you know, just in the marketplace there is that the rates have been rising very, very rapidly in some voluntary companies within 12 month time frame, within 30 or 40 percent, so they're closing up to, getting closer to where we are. I'm not familiar with the, that familiar with the benchmark system here in this province because of course all our filings are non-benchmark filings pretty much by definition, but it's my understanding some of the companies have been filing for increases within those benchmarks within the last year or two even though the, because there is a certain bandwidth, as I understand it, within the benchmark, and even though that the benchmarks themselves have not changed.

COMMISSIONER POWELL: So it's difficult to try to compare apples and apples.

MR. SIMPSON: I would expect, Commissioner Powell, and, you know, I don't have that much detail level of what's going on on the ground in the marketplace, but I would hope that the broker representatives you're going to hear from would be able to provide you some valuable insights into that.

MR. SAUNDERS, PRESIDING CHAIRMAN: You made a comment in your testimony, you mentioned something about FA tend to have a higher participation in rural areas. Is there any reason for that?

*(1:00 p.m.)*

MR. SIMPSON: The only thing that I would suggest is because we're there to deal with availability and ...

COMMISSIONER POWELL: Lack of competition?

MR. SIMPSON: I can just go to my own experience. My folks lived in rural British Columbia for 17 years and all the goods and services are just harder to get and harder to get to, even though there it's a monopoly insurance market, so it doesn't translate into insurance necessarily but, you know, everything from groceries to TV channels are harder to get in rural areas, and I would not expect insurance, auto or home, to be any different.

COMMISSIONER POWELL: So actually one of those ... you were talking about three types of insurance that's been provided. Yeah, direct response provided. They probably ... there's an option now for the rural drivers that wasn't there before, if I fitted that ...

MR. SIMPSON: I would certainly hope so and I would certainly hope that the advances in technology would make that true of other goods and services, people living in more remote areas would have greater access to things than they've had, goods and services they've had prior to this. I'd be optimistic about that.

COMMISSIONER POWELL: So the challenge for consumers, making him and herself aware that there are other options other than the local insurance agent down the street who tells you where to go, when to go.

MR. SIMPSON: Well, I'm not going to make myself popular as an agent or a broker by saying somebody should go to a direct response company, but there is a wider range of choices available to the consumer and I think competition and choice benefits the consumer, so the more of that there is the better.

COMMISSIONER POWELL: Because I was just wondering whether experience wise that rural area drivers are more accident prone because they're thinking about things they shouldn't be thinking about, which would be the opposite of what you think in a busy city driving and the way they drive in cities.

MR. SIMPSON: Yeah, I think the rates in the territories outside of where we are right now are somewhat lower than the city, so hopefully that's not the reality.

COMMISSIONER POWELL: Now, I was wondering, one other question, sort of may not be any correlation to this at all, but I made a note here that your Schedule DJS No. 1, you talked about taxi cab, jitneys and liveries. Jitneys I understand. I grew up in a city that most all our transportation was done by jitney drivers. But I notice that the accident years, that the number of, 1998, that was the lowest year, the number of taxi cabs that were in FA.

MR. SIMPSON: Okay. So I've got ... I'm sorry, I've got for Newfoundland and Labrador?

COMMISSIONER POWELL: Yeah, the Province of Newfoundland, 1997, $790,000.

MR. SIMPSON: Yeah, here we are. I'm sorry, I have it now.

COMMISSIONER POWELL: And in 1998, 710, and the percentage down below of 62 percent, percentage market share ... am I reading this right, 62 percent of taxi drivers were covered by FA?

MR. SIMPSON: Well, it's on a premium volume basis, so how that translates to vehicles as such, I'm not sure.

COMMISSIONER POWELL: Okay. The thing that struck me when I saw it, and there may not be any correlation, but the 1998, there's another schedule, that was the best year the FA had in the province, according to the financial data, one of the schedules, yeah, your DJS No. 2. I think we've got it a number of times. Excess of revenue over expenses, $10 million, forgetting that that's not the true but assuming it's consistent with other years. Is there any correlation between one and the other?

MR. SIMPSON: I really don't know.

COMMISSIONER POWELL: It just struck me as funny. You didn't have many cabs or premium wise but you made a lot more money, so ...

MR. SIMPSON: You've got me curious as well now. I'd like to follow up with Mr. Pelly on that, if I may, and see if he's got that information and what kind of impact that would have on our financial results.

COMMISSIONER POWELL: It just sort of struck me and we'll be talking to people from the taxi industry and ... I think that's all the questions I have for you, sir. Thank you very much.

MR. SIMPSON: Okay, thank you, sir.

MR. SAUNDERS, PRESIDING CHAIRMAN: Thank you, Commissioner Powell. Commissioner Martin?

COMMISSIONER MARTIN: I have no questions.

MR. SAUNDERS, PRESIDING CHAIRMAN: Okay. I have a few questions which I hope I'll be able to finish in a few minutes, mainly on follow up, questions that were asked earlier, but I wanted to make a comment first, if I could, to give you some feel for some of the frustration, I guess, that I feel in terms of trying to analyze Facility's results that were touched on to some extent by Mr. Powell, but, and I think he forgot to ask a question that I thought he was going to ask you, but I'll ask it to you anyway. Why is it that Facility doesn't put up a statement showing the actual results of your own in-house operations and then to show the operations of the body, if you like, the agency or facility acting for the industry, because nowhere in the statements that I've seen put forward do you separate that. Am I wrong or am I right?

MR. SIMPSON: I want to make absolutely sure that I understand the question and is the first part referencing the administrative expenses?

MR. SAUNDERS, PRESIDING CHAIRMAN: Yes. Like, since we started to regulate insurance, well I shouldn't say that, since I became involved with the Board in my second reincarnation, I guess, the question that I have very much difficulty answering for members of the public who ask me questions from time to time about how we regulate utilities, how we regulate the auto insurance industry, the question that's very difficult to describe or to answer is what Facility is and how it functions as a part of the industry. Now, there's a time when I thought I knew it, there's a time when I got involved in the surplus hearing we had in 1997 or some such time in the past, and I participated in the writing of the order to try and address the question of what Facility was and whether or not it was a profit making organization, but my question to you is ... I guess I should make one more point before I ask the question. You don't do a lot as an organization to separate, if you like, your day to day administrative function from your function as a investment agent, if you like, of the industry, because that's what you are, aren't you?

MR. SIMPSON: Well, we do manage funds on behalf of the industry, that's true, and the investment ...

MR. SAUNDERS, PRESIDING CHAIRMAN: Yeah, and what else do you do on behalf of the industry besides manage the funds, the industry funds?

MR. SIMPSON: We make sure that the plan of operation is executed, if you will.

MR. SAUNDERS, PRESIDING CHAIRMAN: No, of a financial nature, managing the funds.

MR. SIMPSON: Managing the funds, pull in your results and ...

MR. SAUNDERS, PRESIDING CHAIRMAN: And in order to manage the funds you incur certain expenses, which are the 14 people you have in your employ, plus yourself, plus the rent on your office, and your photocopier and all these things.

MR. SIMPSON: I'm included in ...

MR. SAUNDERS, PRESIDING CHAIRMAN: But you never attempt to show that as a separate statement, you don't bring that forward to say here's the FA operation, the non-profit operation of FA right here in this statement.

MR. SIMPSON: I believe, Mr. Chairman, that would be captured under administrative expenses.

MR. SAUNDERS, PRESIDING CHAIRMAN: Yes, but not as a separate statement. I have never seen a separate statement. It may be that you have such a document.

MR. SIMPSON: Not to my knowledge, sir.

MR. SAUNDERS, PRESIDING CHAIRMAN: You don't, no, but would it help, do you think, to relieve some of the confusion that exists to say, yes, FA is performing two functions here ... one is that we have an administrative function and to do that we have to employ people and rent space, and then we have a function that we perform for the industry, which is to manage the funds that end up in an account called Facility Association. The funds are owned by the industry members that participate.

MR. SIMPSON: Yes.

MR. SAUNDERS, PRESIDING CHAIRMAN: Not by you.

MR. SIMPSON: That's correct.

MR. SAUNDERS, PRESIDING CHAIRMAN: You merely perform the task of managing the funds and all of that, and all that that entails, right?

MR. SIMPSON: Yes, sir.

MR. SAUNDERS, PRESIDING CHAIRMAN: Yes, think about that, would you?

MR. SIMPSON: I certainly will.

MR. SAUNDERS, PRESIDING CHAIRMAN: Okay, because that may help in trying to explain what it is that this, this body called FA actually is.

MR. SIMPSON: I'll take that message back to my board of directors.

MR. SAUNDERS, PRESIDING CHAIRMAN: I still think I don't have a lot of difficulty with it, but there are times when I doubt myself, because of the confusion that exists and surrounds this statement filing, the statement preparation, if you like, okay. Commissioner Powell and I had a long discussion about this and I thought he was going to ask that question.

COMMISSIONER POWELL: I apologize to you, sir.

MR. SAUNDERS, PRESIDING CHAIRMAN: That's alright. I'll get rid of some of these binders, it's less confusing. I want to draw your attention to a letter that, I'm not sure if you saw the letter, but I wanted to read you a couple of sentences in the letter. The letter comes from Mr. Tisdale, who is the President and CEO of (inaudible), I think it is, yes. Are you familiar with him?

MR. SIMPSON: He's on our board, yes.

MR. SAUNDERS, PRESIDING CHAIRMAN: Yes, and have you seen the letter he wrote to us which has been distributed to all the parties to my knowledge, and it's an October 3rd, 2002 letter in which ... have you seen it, or is it available for ...

MR. SIMPSON: I believe that I have, Mr. Chairman.

MR. SAUNDERS, PRESIDING CHAIRMAN: I just wanted to draw your attention to a statement there and it's in relation to what's been discussed this morning, and that is the gap, if you like, between Facility and the regular market, the voluntary market, and I understand Mr. Tisdale has indicated he's going to be coming forward himself to make a presentation, is that correct? No, he hasn't, okay.

MR. SIMPSON: Thank you.

MR. SAUNDERS, PRESIDING CHAIRMAN: Does everyone have a copy of Mr. Tisdale's letter.

MR. WHALEN, Q.C.: We've seen it earlier.

MR. SAUNDERS, PRESIDING CHAIRMAN: Okay, if you need a copy, I'm sure we can make one available, but I just wanted to make a reference here to a statement that he makes in the letter, and it's at the top of the second page, Mr. Simpson, the second paragraph where he says, "Offering an alternative market to the FA is challenging. It means charging the right price for the right risk. In an efficient market this challenge is lower as market segmentation is easier to identify. However, in Newfoundland and Labrador today the market is not efficient", and I'm not sure what he means by that but I'm not going to ask you what he means. "This is because the higher risk drivers are being cross-subsidized by the lower risk drivers.", and I guess that's what he means by being not efficient. "This has created an artificial lower price ceiling on the higher risk market segment. This lower ceiling and cross-subsidization are currently hampering our ability to offer an alternative market to the FA." Okay?

MR. SIMPSON: Yes.

MR. SAUNDERS, PRESIDING CHAIRMAN: Now, my question is, is it the intention of FA through this rate filing to create that gap that's referred to?

MR. SIMPSON: The intention of the rate filing is to get the rate to an adequate level on that zero percent profit provision that we described. That's the intent of the filing.

MR. SAUNDERS, PRESIDING CHAIRMAN: Okay, and if it so happens ...

MR. SIMPSON: One of the follow on effects we would expect to see is that gap being created, but that's not the intention of the filing.

MR. SAUNDERS, PRESIDING CHAIRMAN: Alright then, do you agree that if we base the voluntary market rates and FA's rates on actuarial analysis and science and loss costs, that if the gap takes place, if it happens, it's more by accident than by design?

MR. SIMPSON: I'd say it's in the way of the nature of the market's function, Mr. Chairman.

MR. SAUNDERS, PRESIDING CHAIRMAN: Okay.

MR. SIMPSON: But that's what we would expect to see.

MR. SAUNDERS, PRESIDING CHAIRMAN: Alright, do you believe that the gap should be, let's say, promoted by this Board so as to create an opportunity for the grey market insurers?

*(1:15 p.m.)*

MR. SIMPSON: Well, I would say that I believe the competition in choice for the consumer benefits the consumer, whether it's in auto insurance or anything else, and in terms of the impact of the decision of the Board, anything that would enhance the level of competition, the number of competitors, and the amount of choice available for the consumer, whether they are a high risk driver or not, is something that I would believe to be a good thing for the people of this province.

MR. SAUNDERS, PRESIDING CHAIRMAN: But isn't the choice there now?

MR. SIMPSON: There is a level of choice there now. I think there would be a greater level of choice if we achieved the adequate rate that we've applied for in our application.

MR. SAUNDERS, PRESIDING CHAIRMAN: And getting back to Mr. Powell's question on, I think it was on DJS-2, which I'll find in a minute ... where we talked about ... oh, this one, what is it, DJS-3, or DSJ, is it?

MR. SIMPSON: DJS, yes.

MR. SAUNDERS, PRESIDING CHAIRMAN: The 62 percent or the 60 percent approximately that shows up in there as being accidents, no accidents or convictions, would they normally end up in the grey market insurer's book of business?

MR. SIMPSON: I really don't know. It would depend on the selection, on the writing selection criteria used by the non-standard or the grey market insurers, you know, and the criteria that they use in addition to driving record, if you will.

MR. SAUNDERS, PRESIDING CHAIRMAN: Yeah.

MR. SIMPSON: To determine the risk profile of what they have in front of them.

MR. SAUNDERS, PRESIDING CHAIRMAN: Okay.

MR. SIMPSON: I would certainly hope that these people would wind up somewhere else other than FA.

MR. SAUNDERS, PRESIDING CHAIRMAN: Yes, that's desirable.

MR. SIMPSON: Yes, sir.

MR. SAUNDERS, PRESIDING CHAIRMAN: As far as FA is concerned.

MR. SIMPSON: Yes.

MR. SAUNDERS, PRESIDING CHAIRMAN: The plan of operation that we have here dated June of '02, is the final, or is the last approved plan by the Superintendent, the one we referred to this morning, because you mentioned the date of June '02. That's the last on that ...

MR. SIMPSON: To my knowledge, the latest changes that were made were of a housekeeping nature.

MR. SAUNDERS, PRESIDING CHAIRMAN: Yes, I saw those changes, they didn't really impact the ...

MR. SIMPSON: To incorporate Nunavut and things of that nature.

MR. SAUNDERS, PRESIDING CHAIRMAN: Right, right.

MR. SIMPSON: That would be the latest version.

MR. SAUNDERS, PRESIDING CHAIRMAN: Okay, you mentioned that in Nova Scotia the procedure before the Board there was a tribunal hearing, no lawyers, and no sworn evidence.

MR. SIMPSON: I'm sorry, if that's what I said, I have to correct myself. There were no lawyers to the best of my knowledge, unless members of the panel had a legal background, but we are sworn.

MR. SAUNDERS, PRESIDING CHAIRMAN: Is that a ... but you have a choice to have a lawyer, do you, it's just not a requirement of the Board.

MR. SIMPSON: It's not a requirement of the Board, and when the chair says I see there are no lawyers present, he smiles. No disrespect to members of the legal profession present.

COMMISSIONER MARTIN: And he's a lawyer.

MR. SAUNDERS, PRESIDING CHAIRMAN: Well, I don't know, that was interesting. I'm not suggesting that we follow that practice here, by the way.

MS. NEWMAN: Well, you'll note that counsel in the room were rather quiet, Mr. Chairman.

MR. SAUNDERS, PRESIDING CHAIRMAN: No, actually, I find that when lawyers are present that matters move along more expeditiously. I don't prefer hearings where there's no lawyers involved for all kinds of different reasons. Usually it's not easy to get through the process.

You mentioned there were seven different service carriers, this is in response to Mr. Whalen's direct examination, across Canada.

MR. SIMPSON: Yes, sir.

MR. SAUNDERS, PRESIDING CHAIRMAN: And we have four of them as service carriers in Newfoundland.

MR. SIMPSON: Yes.

MR. SAUNDERS, PRESIDING CHAIRMAN: Are there more than four in any jurisdiction?

MR. SIMPSON: Not to my knowledge, no.

MR. SAUNDERS, PRESIDING CHAIRMAN: Four is the maximum that there would be in any jurisdiction.

MR. SIMPSON: Yes.

MR. SAUNDERS, PRESIDING CHAIRMAN: The binder control, and this was talked about at some length at our last hearing, and my question is, has there been any further discussions between FA and the Superintendent in respect of implementing the binder control in Newfoundland since the last hearing?

MR. SIMPSON: Yes, there has been and the Superintendent has not expressed an interest in implementing a binder control in this province.

MR. SAUNDERS, PRESIDING CHAIRMAN: I see.

MR. SIMPSON: But we're certainly willing to do so.

MR. SAUNDERS, PRESIDING CHAIRMAN: Have you been told why?

MR. SIMPSON: No sir, not to my knowledge.

MR. SAUNDERS, PRESIDING CHAIRMAN: Some of my questions have already been dealt with so I'm just picking on those that haven't been dealt with. Would you explain the risk sharing pool that exists in Ontario and its function as opposed to FA and the regular market, just briefly. I just want to get a better understanding of what the function of the risk sharing pool is.

MR. SIMPSON: I'll try to do that, and briefly.

MR. SAUNDERS, PRESIDING CHAIRMAN: Okay.

MR. SIMPSON: It was set up, I believe, around 1993, in response to a growing FA population which had, in turn, been growing presumably because of the price constraints in the voluntary market in the late 1980s, so a little bit of history. Members, and all companies in Ontario, auto insurance companies, are members, write insurance at, what I'll call their street rates, the rates that they filed with the Superintendent in the province. In Ontario we also have a take all comers rule which says that you have to file your underwriting guidelines, your underwriting rules with the Superintendent, and if something comes to you that is within those rules, that take all comers parlance means you have to take that risk, so presumably what happens at the company level is a piece of business or risk comes in to an underwriter and they took a look at it, and say well when we drew up that rule, I didn't contemplate that I'd be looking at this. You can't have a rule that encompasses every factual reality up there presumably, so they have an opportunity to, and it works very much like a reinsurance mechanism, what I'll call a quota share reinsurance mechanism, so an individual company can seed up to five percent of the risks on its book to the reinsurance pool, and there is an expense allowance, and they retain 15 percent of the premium, seed 85 percent of the premium, and if a loss occurs, the pay 15 percent of the loss, and the pool pays 85 percent of the loss, and this is subsidized by the whole market. The formula is roughly based on 50 percent market share, 50 percent usage, so you've got competitors subsidizing one another, about ... companies representing about 15 percent of the market don't use the risk sharing pool, but because they have a market share, they're required to subsidize those risks. It's a cross-subsidization mechanism, I'd be very hesitant to recommend in the event that we ever get beyond a take all comers market in Ontario, and that's the industry's goal. We would presumably look to wind down the risk sharing pool. Drivers in that pool, the last time that our accounting folks looked at it was about a year ago, are being subsidized to the tune of about $500 per year per vehicle. In other words, for the risk that they represent, on average across the whole pool, so obviously that average can give you a lot of numbers above and below, to whatever degree. And so it's a large cross-subsidization mechanism. We talked about our administrative budget, last year we spent about $3.5 million to administer the residual markets across Canada and about a million of that was for the risk sharing pool in Ontario alone, so it's a relatively costly endeavour to run. In the Nova Scotia piece, I'm not sure what it went in here as but we've been going to ... here it is, DJS-3, I think at the back of that there's an article on false kindness and it talks about issues of when you cross-subsidize high risk drivers, as the risk sharing pool does, and the monopoly provinces do through social pricing, one of the unintended consequences you seem to arrive at is that bad drivers drive ... I shouldn't say bad drivers, high risk drivers drive more, cause more accidents, and more grief and misery, so it builds not only costs into the system when you subsidize people in this category, but there is a very human cost as well, so the risk sharing pool is something that we administer as efficiently as we can. It's not a mechanism that I would recommend. It's the only two-tier residual market in Canada, and to the best of my knowledge, probably the only two-tier residual market in North America, and the United States, the various states operate a variety ... there are different ways of operating residual markets. England doesn't have one at all. The United States has half a dozen ways of administering them, so Ontario has arrived at kind of a unique solution. Forgive me a little editorial comment, but ...

MR. SAUNDERS, PRESIDING CHAIRMAN: When you refer to Ontario residual market, you always use, or you most times use the term "all comers rule", and what's the difference in that and the way in which

Facility operates in Newfoundland where you're in a situation where you have to take everything that comes at you from your servicing carriers?

MR. SIMPSON: We're in the same ... the all comers rule in Ontario is different in that it applies to the voluntary market.

MR. SAUNDERS, PRESIDING CHAIRMAN: Okay.

MR. SIMPSON: Where if they filed a guideline, an underwriting rule, and the risk that comes across the underwriter's desk, vehicle, driver, what have you, through that application, falls within the boundaries of a filed rule.

MR. SAUNDERS, PRESIDING CHAIRMAN: Uh hum.

MR. SIMPSON: They must take that risk.

MR. SAUNDERS, PRESIDING CHAIRMAN: Okay, oh yes, when you were listing the servicing carriers in Newfoundland, I missed on ... Unifund, Co-op, Royal Sun Alliance ...

MR. SIMPSON: And the Insurance Corporation of Newfoundland.

MR. SAUNDERS, PRESIDING CHAIRMAN: Yeah, right, when Mr. Pelly was giving evidence, I was looking for it in my notes but I couldn't find it, but I didn't take a lot of time, maybe someone can recall it, but I think he was referring to FA and not to the industry, that as far as age of a driver is concerned, FA has no, no say in that. That determination as to whether he ends up in FA is made at the broker level.

MR. SIMPSON: The broker and company level.

MR. SAUNDERS, PRESIDING CHAIRMAN: Right, and so the fact that he ends up in FA, he meaning the over age, or the senior driver that's referred to in one of your exhibits, I think it was senior was the word used, ends up there because the member industry, or the industry members, the industry servicing carriers and brokers put him there, not because of anything you did, and he shows up as a statistic because that's the way in which the industry wanted that binder, what do you call it, binder form completed. This wasn't done by FA, this form.

MR. SIMPSON: This was done by ...

MR. SAUNDERS, PRESIDING CHAIRMAN: This is undertaking number three.

MR. SIMPSON: Yes, this was developed by my staff in conjunction with industry people, and because of the concern, you know, I had a reporter from Halifax call me up and say, so I guess once you're over 65 FA is your only alternative, is that right? That kind of challenging.

MR. SAUNDERS, PRESIDING CHAIRMAN: And that's not the case.

MR. SIMPSON: That's not the case, and that's what the evidence shows.

MR. SAUNDERS, PRESIDING CHAIRMAN: Yeah.

MR. SIMPSON: But it is a concern so it's something that the committee decided they wanted to monitor through this and obviously it's of interest here as well, so to monitor whether, in fact, that is going on, so we've got various ways to monitor it and get the agent or broker thinking about it on the front end when the business is written, and through statistical analysis on a follow on basis as we submit it to the Board.

MR. SAUNDERS, PRESIDING CHAIRMAN: Okay, this is probably a question I should ask the industry people, but I'll ask you and if you don't know the answer then I'll ask the industry people. There aren't any rates in the rate schedules that are designated as rates for seniors, are there?

MR. SIMPSON: For individual companies, I don't know for Facility ... after 25 everybody is the same.

MR. SAUNDERS, PRESIDING CHAIRMAN: That's right, and that's what Mr. Pelly said, after 25 everyone is the same. Okay, that's all the questions I had. Anything coming out of the Board questions, Mr. Whalen?

MR. WHALEN, Q.C.: I just have a brief few things, Mr. Chairman.

MR. SAUNDERS, PRESIDING CHAIRMAN: I'm hoping we can finish up with Mr. Simpson this morning. What's your schedule?

MR. O'FLAHERTY: I'm just wondering in terms of timing if you'd like me to go first, because I know that in the past Facility has wanted to go last.

MR. WHALEN, Q.C.: That's fine.

MR. SAUNDERS, PRESIDING CHAIRMAN: Okay.

MR. O'FLAHERTY: I only, I have a couple of matters.

MR. SAUNDERS, PRESIDING CHAIRMAN: Okay, so we're okay to go until we finish with Mr. Simpson?

MR. WHALEN, Q.C.: Well, I don't know if we'll finish him or not.

MR. SAUNDERS, PRESIDING CHAIRMAN: Okay.

MR. WHALEN, Q.C.: You're going to be five or ten minutes, and I'm going to be five or ten minutes, so maybe if we have a half hour in the morning we can ...

MR. SAUNDERS, PRESIDING CHAIRMAN: Okay, so Mr. Simpson wasn't planning to return home today.

MR. WHALEN, Q.C.: No, he's here.

MR. SAUNDERS, PRESIDING CHAIRMAN: That's what I was anticipating.

MR. WHALEN, Q.C.: Thank you, Mr. Chairman.

MR. O'FLAHERTY: Thank you, Mr. Chairman.

MR. SAUNDERS, PRESIDING CHAIRMAN: Okay, we'll resume at 9:00, thank you.

*(hearing adjourned to January 10, 2003)*