

**NEWFOUNDLAND AND LABRADOR
BOARD OF COMMISSIONERS OF PUBLIC UTILITIES**

ORDER NO. A.I. 12(2015)

1 **IN THE MATTER OF** the *Automobile*
2 *Insurance Act*, RSNL 1990, c. A-22, (the
3 “*Act*”), as amended and regulations
4 thereunder; and
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6 **IN THE MATTER OF** an application by
7 Facility Association for approval to
8 implement a revised rating program for its
9 Motorcycles and Mopeds class of business.
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11
12 **The Application**
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14 On May 12, 2014 the Board received a Category 2 filing from Facility Association (“Facility”) requesting approval of a revised rating program for its Motorcycles and Mopeds class of business (the “Application”). The Application initially proposed an overall rate level change of +2.6%. Facility subsequently revised its overall rate level indication to correct an error found during the filing review. The revised Application proposes an overall rate level change of +0.6%.
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20 Facility also proposes to remove rate capping for age, gender and marital status that has been set at 0% since 2005. Without this capping Facility’s average rates for Third Party Liability and Collision would increase by +41.3% and +11.6%, respectively. To maintain revenue neutrality with the removal of the capping for age, gender and marital status Facility proposes to reduce the Third Party Liability and Collision base rates by 31.4% and 14.0%, respectively. Facility also proposes minor changes to its underwriting rules.
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27 **Application Review**
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29 The Application was forwarded to the Board’s actuarial consultants, Oliver Wyman Limited (“Oliver Wyman”), for review. On August 7, 2014 the Board approved an extension to the 90-day review timeline. On August 27, 2014 Oliver Wyman filed a report of findings with the Board. On August 28, 2014 the Oliver Wyman report was forwarded to Facility, and Facility filed comments on the report on September 15, 2014.
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35 In its report Oliver Wyman identified issues and considerations for the Board in respect to Facility’s assumptions and methods used for: i) the loss trend rates, ii) the complement of credibility for Comprehensive, iii) the Health Levy, and iv) the return on investment provision.
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1 The assumptions and methods used for all other parameters were found to be reasonable on the
2 basis proposed and/or in accordance with the Board's Filing Guidelines.

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4 Based on its review Oliver Wyman found that Facility's indicated and proposed overall rate level
5 changes are higher than the rate level changes calculated based on the Filing Guidelines and
6 alternate assumptions, as shown below:

Coverage	Facility's Indications	Facility's Proposed Rate Change	Oliver Wyman's Indications ¹
Third Party Liability	-3.1%	-3.1%	-6.6%
Accident Benefits	+22.0%	+22.0%	+14.3%
Uninsured Auto	+2.3%	+2.3%	-4.3%
Underinsured Motorist	+5.6%	+5.6%	-1.7%
Collision	-4.0%	-4.0%	-6.8%
Comprehensive	+7.0%	+7.0%	+0.0%
Specified Perils	+0.4%	+0.4%	-2.9%
Total	+0.6%	+0.6%	-3.7%

9
10 Oliver Wyman also noted that Facility has made a number of changes in its approach and
11 assumptions used to calculate its rate level indications from those it used in its prior application
12 in 2005.

13 14 **Board Findings**

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16 In its review of rate filings, where an insurer has proposed an increase in a rate previously filed,
17 the Board is required by legislation to determine whether the proposed rate is too high. The
18 Board makes this determination following a thorough review of all information including the
19 reports and findings of the actuarial experts. In exercising its jurisdiction the Board reviews the
20 base rates on a coverage basis and a determination is made as to whether or not the rates are too
21 high. In accordance with the legislation, and as set out in the Filing Guidelines, an insurer is
22 required to provide detailed justification of any proposed rate increase. The Filing Guidelines
23 state that the insurer is required to provide the Board with sound reasoning and justification for
24 the proposed rates based on the most recently available data.

25 26 i. Loss Trend Rates

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28 Since the industry experience for motorcycles is too limited for use in selecting loss trend rates
29 Facility bases its selected loss trend rates on Newfoundland and Labrador (NL) Industry Private
30 Passenger Automobile loss experience through to December 31, 2012. Oliver Wyman stated that,
31 as the Board has no guideline on the data to be used to select trend rates for motorcycles and

¹ Using Facility's proposals with alternate assumptions for the Complement of Credibility for Comprehensive coverage, Health Levy and pre-tax return on investment.

1 Facility's choice is limited to using either Industry Private Passenger Automobile or Commercial
2 Vehicle experience for determining loss trend rates, use of Industry Private Passenger
3 Automobile experience is reasonable. Oliver Wyman notes however that this adds to the
4 uncertainty of the findings.
5

6 Facility did not use the Board's guideline loss trend rates but rather selected its loss trend rates
7 based on its own loss trend regression model. Oliver Wyman notes that this model determines
8 reform factors for the change in product and that these factors are intertwined with the calculated
9 loss trend rate. Oliver Wyman also notes Facility's position that the reform factors do not affect
10 the rate level indications in this Application. Oliver Wyman does not agree with Facility's
11 reform factors but, because the reform factors do not affect the calculation of the rate level
12 indications, does not discuss the issue further.
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14 Oliver Wyman also questioned Facility on why they did not select loss trend rates based on
15 Industry data as of June 30, 2013, which was available at the time of the filing. Facility provides
16 the following as support for use of Industry data as of December 31, 2012:
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18 *FA updates trend selections annually for the Atlantic provinces, unless it is determined*
19 *under special circumstances that a more frequent review is needed. As there were no*
20 *deemed special circumstances, an updated trend analysis based on industry data as at*
21 *June 30, 2013 was not completed.*
22

23 In its report Oliver Wyman provided a summary of Facility's selected past and future loss cost
24 trend rates and the Board's December 2012 and June 30, 2013 past and future loss cost trend
25 rates. Facility calculated that, assuming no other changes in assumptions, its overall rate level
26 indication would reduce from +0.6% to +0.3% using the Board's June 2013 loss trend rates.
27 Given the similarity in rate indications determined by Facility based on its selected loss trend
28 rates and the Board's loss trend rates using Industry Private Passenger Automobile data as June
29 2013, and the uncertainty associated with the data used, Oliver Wyman accepts Facility's loss
30 trend rates as reasonable in this circumstance.
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32 The Board accepts Facility's loss trend rates in this filing on the basis of Oliver Wyman's
33 opinion that the loss trend rates are reasonable and will not result in rates that are too high.
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35 ii. Complement of Credibility for Comprehensive Coverage
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37 To the extent that Facility determines its own loss experience is not statistically credible it
38 assigns the balance of credibility to its estimate of current permissible loss ratio adjusted for the
39 net loss/premium trend over a period of one year.
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41 In its report Oliver Wyman notes that, as there have been no claims under the Comprehensive
42 coverage in the experience period, Facility assigns 0% credibility weight to its own experience
43 and 100% credibility weight to its complement – which is essentially the Private Passenger
44 Automobile net trend rate of +7.0%. Oliver Wyman also notes that, over the past ten years

1 (2003-2012), Facility's Comprehensive coverage loss ratio has been 1.2% and the reported
2 Industry Comprehensive coverage loss ratio for the last five years (2009-2013) is 3%.

3
4 Facility supports its complement of credibility for Comprehensive coverage by stating:

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6 *FA uses a consistent approach to determining credibility across all jurisdictions and all*
7 *rating classes. While we understand the rationale provided, this would suggest that the*
8 *application of credibility is subject to actuarial judgement, in which case we would*
9 *assume that should the Board find this approach reasonable, it would likewise find it*
10 *reasonable in situations where a ten year loss ratio was found to be significantly higher*
11 *than a level associated with a loss ratio associated with a target return.*

12
13 Oliver Wyman finds that, given the very favourable Comprehensive coverage loss experience for
14 both Facility and the Industry, no rate increase for the Comprehensive coverage is reasonable at
15 this time.

16
17 The Board finds that Facility's assignment of 0% credibility weight to its own experience and
18 100% credibility weight to its complement for Comprehensive coverage would result in rates
19 that are in excess of those justified in the circumstances. As there have been no claims under the
20 Comprehensive coverage for the experience period and given the very favorable Comprehensive
21 loss experience of both Facility and the Industry, the Board finds that a rate change no higher
22 than 0% for Comprehensive coverage is reasonable at this time.

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24 iii. Health Levy

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26 Facility selects a provision of \$21.21 per vehicle for the Health Levy based on 2012 information
27 published in the GISA exhibits. Oliver Wyman notes that the current Health Levy rate is
28 estimated at \$26.44 per vehicle. According to Oliver Wyman the inclusion of a Health Levy
29 provision of \$26.44 per vehicle, with no other changes in assumptions, would increase the
30 overall rate level change from approximately +0.6% to approximately +2.6%.

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32 The Board finds that Facility's proposed Health Levy of \$21.21 per vehicle will not result in
33 rates that are too high.

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35 iv. Return on Investment Provision

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37 In its Application Facility assumes a pre-tax return on investment (ROI) of 1.19% on cash flow.
38 Oliver Wyman notes that Facility's selected ROI rate of 1.19% is outside the Board's Guideline
39 range of 2.8% to 4.0%, and is considered a current "risk-free" rate. Oliver Wyman estimates the
40 Industry average ROI for 2013 (the latest available full year data) was 2.8%, a decline from 4.0%
41 in 2012. If the ROI is increased to 2.8%, and assuming no other changes, Facility calculates its
42 overall rate level indication would reduce from +0.6% to -5.2%.

1 Facility provided the following as rationale for its 1.19% ROI selection:
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3 *We believe the return on investment should be a forward looking exercise, rather than*
4 *backward. We contend that the risk free return assumption is appropriate, and that such*
5 *return in the current environment is aligned with the assumption we selected, and we do*
6 *not anticipate a significant shift in the yield curve in the immediate future. As such, we*
7 *believe our assumption, while lower than the Guideline level, is appropriate.*
8

9 The Board acknowledges Facility's position that the ROI rate should be forward looking but
10 finds that Facility has not provided sufficient justification to support a pre-tax 1.19% ROI to be
11 included in its provision for profit. In the absence of this justification the Board will require
12 Facility to use a pre-tax ROI of 2.8%, consistent with the Board's Filing Guidelines.
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14 **Summary of Findings**

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16 The Board accepts Facility's assumptions and methods used to calculate and select the
17 parameters included in the proposed rates for its Motorcycles and Mopeds class of business, with
18 the exception of the complement of credibility for Comprehensive coverage and the pre-tax ROI.
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20 Facility may submit a revised rate proposal for its Motorcycle and Mopeds class of business
21 proposing rates which are no higher than the rate level changes indicated reflecting the
22 following:
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- 24 • A Health Levy no higher than \$26.44;
 - 25 • A rate indication of 0% for Comprehensive coverage; and
 - 26 • A pre-tax ROI of 2.8%.
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28 **Costs**

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30 As set out in the Filing Guidelines, pursuant to section 57 of the *Automobile Insurance Act* and
31 section 90 of the *Public Utilities Act*, Facility will be required to pay the costs of the Board
32 associated with this filing, including the costs of the actuarial review.

1 **IT IS THEREFORE ORDERED THAT:**

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1. The application is denied.
2. Facility Association will be required to pay the costs of the Board associated with this filing, including the costs of the actuarial review.

DATED at St. John's, Newfoundland and Labrador, this 16th day of April 2015.

Andy Wells
Chair & Chief Executive Officer

Darlene Whalen, P.Eng.
Vice-Chair

Dwanda Newman, LL.B.
Commissioner

James Oxford
Commissioner

Cheryl Blundon
Board Secretary