New Brunswick Insurance Board

DECISION

IN THE MATTER:
Of a rate revision application for **THE INSURANCE COMPANY OF PRINCE EDWARD ISLAND**
With respect to automobile insurance rates for
COMMERCIAL VEHICLES

Written Hearing
Heard at Saint John, New Brunswick

PANEL:	Ms. Marie-Claude Doucet	Chair
	Ms. Francine Kanhai	Member
	Ms. Heather Stephen	Member

Date of Written Hearing: November 30, 2018

Decision Rendered: January 8, 2019

Summary

[1] Pursuant to subsection 267.51(1) of the *Insurance Act,* R.S.N.B., 1973 c. I-12, (the "Act") the New Brunswick Insurance Board (the "Board" or "NBIB") convened a Panel of the Board to conduct a written hearing (the "Hearing") on November 30, 2018 at the offices of the Board, in Saint John. The purpose of the Hearing was to consider the rate revision application (the "Filing") submitted by the Insurance Company of Prince Edward Island (the "Applicant" or "ICPEI") with respect to automobile insurance rates for commercial vehicles in New Brunswick. ICPEI is an insurance company duly licensed to write automobile insurance in New Brunswick.

[2] In compliance with subsection 19.71(2) of the *Act,* the Board notified the Office of the Attorney General ("OAG") and the Consumer Advocate for Insurance ("CAI") of a hearing to be held in this matter. On October 30, 2018, the OAG and the CAI advised the Board that they would not intervene in this matter.

[3] For the purpose of the written hearing the Panel accepted the following exhibits as part of the Record as shown below:

EXHIBIT	DESCRIPTION	DATE
1	ICPEI Original Rate Filing (2018-144)	May 22, 2018
2	Amended Rate Filing	June 18, 2018
3	Questions from KPMG Round 1	June 19, 2018
4	Questions from NBIB Round 1	June 20, 2018
5	ICPEI Responses to KPMG and NBIB Round 1 and Amended Rate Filing	June 27, 2018
6	Questions from KPMG Round 2	August 2, 2018
7	ICPEI Responses to KPMG Round 2	August 10, 2018
8	Questions from KPMG Round 3	Sept. 10, 2018
9	ICPEI Responses to KPMG Round 3	Sept. 14, 2018
10	Amended Rate Filing	Sept. 18, 2018

11	Questions from NBIB Round 2	Sept. 25, 2018
12	ICPEI Responses to NBIB Round 2	Sept. 28, 2018
13	Questions from KPMG Round 4	Oct. 25, 2018
14	Questions from KPMG Round 5	Oct. 29, 2018
15	ICPEI Responses to KMPG Round 4 and 5 and Amended Rate Filing	Nov. 6, 2018
16	Questions from KPMG Round 6	Nov. 8, 2018
17	ICPEI Responses to KMPG Round 6 and Amended Rate Filing	Nov. 14, 2018
18	Questions from KPMG Round 7	Nov. 15, 2018
19	ICPEI Responses to KMPG Round 7	Nov. 19, 2018
20	Actuary Review	Nov. 28, 2018

[4] The Panel, after examining the evidence in its entirety, requested the Applicant to bring the following changes to its Rate Application:

1) For each coverage, modify the calculation of the territorial ultimate losses and expenses (Exhibit 17 of the Record, ICPEI Responses to KMPG Round 6 and Amended Rate Filing dated November 14, 2018, Section 4: Actuarial Justification, Exhibit 2, Sheets 1 and 2, Column (b) Ultimate Loss & Exp.) to be consistent with the approach used in the provincial indication to arrive at the "developed ultimate loss" (Exhibit 17 of the Record, ICPEI Responses to KMPG Round 6 and Amended Rate Filing dated November 14, 2018, Section 4: Actuarial Justification, Exhibit 5, Sheets 1 through 8, Column (T) Developed Ultimate Loss). Specifically, apply the following steps at the territorial level for each coverage:

    a. Calculate the selected ultimate losses for each accident year by taking into account the respective indicated ultimate losses from both the loss development and the Bornhuetter-Ferguson methods;

    b. Apply the appropriate trend factor to each accident year's selected ultimate losses reflecting the respective trend period;

    c. Apply the appropriate Harmonized Sales Tax (HST) factor to each accident year's selected trended ultimate losses; and

d. Apply the appropriate Minor Injury Regulation (MIR) factor to each accident year's selected trended ultimate losses adjusted for the change in HST.

2) For each coverage, re-calculate the credibility weighted territorial relativities and indicated change using the ultimate losses and expenses calculated using the same steps as detailed under 1).

3) Apply the capping selected by ICPEI such that the final proposed territorial relativity change will be capped at 10%, at the territorial level for each coverage after rebalancing.

[5] Further to the above amendments, the Panel approves the average rate level change of **+7.19%** proposed by the Applicant.

[6] The approved rates will be effective on March 1, 2019 for new and renewal business.

1. Introduction

[7] The Board is mandated by the Legislature with the general supervision of automobile insurance rates in the Province of New Brunswick. In order to fulfill that mandate, the Board exercises the powers prescribed by the *Act*. One responsibility for the Board is to ensure that rates charged or proposed to be charged are just and reasonable. Under the *Act*, each insurer carrying on the business of automobile insurance in the province must file with the Board the rates it proposes to charge once every 12 months from the date of its last filing. An insurer must appear before the Board when :

a. The Insurer files for a rate change more than twice in a 12-month period, or

b. The Insurer files rates where the average rate increase is more than 3% greater than the rates charged by it within the 12 months prior to the date on which it proposes to begin to charge the rates, or

c. When the Board requires it to do so.

Procedural History

[8] The Applicant filed a rate revision application for the commercial vehicles (CV) category on May 22, 2018, proposing an overall average rate increase of 7.40% with an indication of 7.40%. Amendments to the rate filing were subsequently filed with the Board, on June 18, 2018, June 27, 2018, September 18, 2018, November 6, 2018 and November 14, 2018. In its final Rate Filing amendment, ICPEI proposed an overall average change of +7.19%, based on an indication of +7.19%.

[9] The Board issued a Notice of Hearing on October 25, 2018 and convened a Panel of the Board to conduct a hearing on the matter. The Office of the Attorney General and the Office of the Consumer Advocate both confirmed to the Board that they would not act as intervenors in this matter.

[10] The Panel held the written hearing on November 30, 2018.

2. Evidence and Positions of the Applicant

[11] The Applicant's Filing forms the main portion of its submission and the evidence before the Panel.

[12] Pursuant to its mandate, the Board, upon receipt of the rate application, proceeded to investigate the Filing in order to determine whether the proposed rates are "just and reasonable".

[13] ICPEI presented a Rate Filing to the Board with an overall indication of +7.40% and proposed to select an average rate change of +7.19% based on its amended indication of +7.19%. Following are the changes proposed to the existing rates by coverage:

Bodily Injury (BI)	-3.32%
Property Damage (PD)	+28.03%
Direct Compensation – Property Damage (DCPD)	+15.72%
Accident Benefits (AB)	-2.20%
Uninsured Auto (UA)	+1.69%
Collision (CL)	+14.23%
Comprehensive (CM)	+1.91%
Specified Perils (SP)	N/A
All Perils (AP)	N/A
SEF 44	-0.16%
Total	***+ 7.19%***

[14] The rates contained in the Filing are produced assuming a target return on equity (ROE) of 13.92%, a 5.00% target return on premium (ROP) and a 3.39:1 premium to surplus ratio. The proposed overall average rates would increase from the current average of approximately $840 to approximately $901.

[15] As a result of the Board's and its consulting actuaries' review of the filing, the following amendments were made by the Applicant to its Rate Application prior to the hearing:

a. Revision of the indication to exclude the MIR conversion factor applied to AB.

b. Revision of the frequency trend applied to Comprehensive to ensure that the selection matched the basis described in the actuarial justification text.

c. Revision of the indication to apply the MIR conversion factors only for accident periods prior to July 2013.

d. Revision of the indication to apply the HST adjustment only for the accident periods prior to July 2016.

e. Revision of the indication to exclude Unallocated Loss Adjustment Expense (ULAE) in the calculation of company indicated loss cost but to include it as a variable expense due to the specific situation of the Applicant.

f. Revision of the average in-force policy effective date to October 23, 2017 in the calculation of premium and loss trend for the in-force policies.

g. Revision of the earned premium used in the premium trend analysis to on-level premium.

h. Revision of the selected investment yield to reflect the investment yield for the most recent P&C 1 for ICPEI instead of Echelon Insurance.

i. Revision of the methodology and correction of the data used to determine the territorial differentials indications.

j. Revision of the effective date for new and renewal business from October 1, 2018 to March 1, 2019.

[16] With the amendments, the Applicant submits that the provincial indication in the Filing was prepared utilizing sound actuarial methods and practices and that the assumptions contained therein are reasonable and that the Filing has been prepared in accordance with the filing guidelines issued by the Board.

3. Analysis and Reasons

[17] A review of the Record (Exhibits 1 to 20) led the Panel of the Board to identify issues with respect to some of the approaches and methodology used by the Applicant in its Filing. The Panel addresses each issues individually as follows:

1) Unallocated Loss Adjustment Expenses

[18] In its original Rate Filing, ICPEI calculates ULAE as a percentage of incurred losses, based on the percentage used by their parent company (Echelon Insurance). In its response to round 1 of questions by the Board's consulting actuaries, KMPG, the Applicant explains that (Exhibit 5, page 301 of the Record):

> The Appointed Actuary does not hold a ULAE provision as all of ICPEI's claims are handled externally. Due to indirectly paying these costs, we kept the same ULAE provision as the parent company (Echelon).

[19] In its response to KPMG's questions, the Applicant provides the following excerpt of the December 31, 2017 Appointed Actuary's Report for ICPEI (Exhibit 5, page 317 of the Record):

> All of ICPEI's claims are handled externally and have therefore never held an Unallocated Loss Adjustment Expenses provision. Although ICPEI would incur a minor internal Unallocated Loss Adjustment Expenses provision to handle general overhead and information technology related to the handling of losses, it was deemed to be immaterial and has been excluded.

[20] Further to a detailed investigation with its Finance team, the Applicant provided the following additional information on the ULAE (Exhibit 9, page 404 of the Record):

> At ICPEI all claims are handled externally. The costs of hiring the firm are based on premium and vary by jurisdiction. For New Brunswick, these costs are 2.6% of the premium. As such, a variable expense of 2.6% will be added to the rate indication and the indicated rate change will be different from what we submitted last time.

[21] ICPEI therefore changed its methodology to include in its model a factor of 2.6% of premium as a variable expense instead of calculating the ULAE using a percentage of incurred losses. Further to this change, the Panel is satisfied that the ULAE allocation methodology utilized by the Applicant is reasonable.

2) Profit Provisions

[22] In the calculation of its overall rate level change need, ICPEI includes a profit provision targeting return to premium (ROP) of 5%, resulting in a target return on equity (ROE) of 13.92% and a premium to surplus ratio of 3.39 to 1.

[23] To date, the Board has not issued benchmarks with respect to profit provision and will continue to monitor and assess such issue on a case-by-case basis, in light of the current market conditions.

[24] The Panel finds that the selections adopted by the Applicant with respect to profit provision are reasonable in light of current market conditions and accepts the Applicant's selection of profit provision.

3) Estimation of Projected Ultimate Loss Amounts for Territorial Indications

[25] In arriving at ultimate loss estimations, experts in actuarial science can consider various estimation methods including but not limited to, the Incurred Loss Development method, the Expected Loss Ratio method and the Bornhuetter-Ferguson method (BF). Each of these methods has its own strengths and weaknesses, hence the reason for actuaries adopting different methods in calculating the ultimate losses.

[26] In estimating its ultimate CV losses for the provincial indications, ICPEI uses the average of ultimate losses calculated using the Incurred Loss Development method (based on actual claim experience that has emerged) and the BF method (based on both actual and expected claim experience). However, when estimating ultimate CV losses for the territorial indications, the Applicant selects a different methodology and opts to rely solely on the Incurred Loss Development method. As a result, ICPEI does not assign any weight to the expected claim experience at the territorial level. This difference in approach creates inconsistencies between the estimates of ultimate losses calculated for the provincial and territorial indications at the coverage level.

[27] In estimating its projected ultimate CV losses for the provincial indication, ICPEI applies loss cost trends, HST adjustment and MIR adjustment factors that are appropriate for each accident year in the experience period. In estimating the projected ultimate CV losses, ICPEI uses a gross up approach instead of applying the appropriate factors for each accident year. Although, this process ensures consistency of the overall projected ultimate losses at the coverage level between the territorial and provincial indications, it does not properly reflect effect of the adjustments for trends, HST and MIR at the territorial level.

[28] In light of the above, the Panel finds that the Applicant's exercise of judgement in calculating projected ultimate losses not to be reasonable in the circumstances, and requests that the following amendments be made:

1) For each coverage, modify the calculation of the territorial ultimate losses and expenses (Exhibit 17 of the Record, ICPEI Responses to KMPG Round 6 and Amended Rate Filing dated November 14, 2018, Section 4: Actuarial Justification, Exhibit 2, Sheets 1 and 2, Column (b) Ultimate Loss & Exp.) to be consistent with the approach used in the provincial indication to arrive at the "developed ultimate loss" (Exhibit 17 of the Record, ICPEI Responses to KMPG Round 6 and Amended Rate Filing dated November 14, 2018, Section 4: Actuarial Justification, Exhibit 5, Sheets 1 through 8, Column (T) Developed Ultimate Loss). Specifically, apply the following steps at the territorial level for each coverage:

    a. Calculate the selected ultimate losses for each accident year by taking into account the respective indicated ultimate losses from both the loss development and the Bornhuetter-Ferguson methods;

    b. Apply the appropriate trend factor to each accident year's selected ultimate losses reflecting the respective trend period;

    c. Apply the appropriate HST factor to each accident year's selected trended ultimate losses; and

    d. Apply the appropriate MIR factor to each accident year's selected trended ultimate losses adjusted for the change in HST.

2) For each coverage re-calculate the credibility weighted territorial relativities and indicated change using the ultimate losses and expenses calculated using the same steps as detailed under 1.

3) Apply the capping selected by ICPEI such that the final proposed change is capped at 10% at the territorial level for each coverage after rebalancing.

4. Decision

[29] For the reasons set out above, the Panel determines that ICPEI does not meet the burden of establishing that the actuarial methodology underlying the territorial analysis is reasonable and appropriate and in accordance with accepted actuarial practice. The Panel accordingly orders the Applicant to make the following changes to its Rate Application:

1) For each coverage, modify the calculation of the territorial ultimate losses and expenses (E Exhibit 17 of the Record, ICPEI Responses to KMPG Round 6 and Amended Rate Filing dated November 14, 2018, Section 4: Actuarial Justification, Exhibit 2, Sheets 1 and 2, Column (b) Ultimate Loss & Exp.) to be consistent with the approach used in the provincial indication to arrive at the "developed ultimate loss" (Exhibit 17 of the Record, ICPEI Responses to KMPG Round 6 and Amended Rate Filing dated November 14, 2018, Section 4: Actuarial Justification, Exhibit 5, Sheets 1 through 8, Column (T) Developed Ultimate Loss). Specifically, apply the following steps at the territorial level for each coverage:

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2) For each coverage re-calculate the credibility weighted territorial relativities and indicated change using the ultimate losses and expenses calculated using the same steps as detailed under 1).

3) Apply the capping selected by ICPEI such that the final proposed change is capped at 10**%** at the territorial level for each coverage after rebalancing.

[30] The Applicant is ordered to incorporate changes to the rate application as set out in paragraph 29.

[31] The above noted requested changes have no impact to the overall provincial rate indications.

[32] The Applicant is therefore **approved to adopt the proposed average rate change of +7.19%.**

[33] The approved rates will be effective on March 1, 2019 for new business and renewal business.

Dated at Saint John, New Brunswick, on January 8, 2019

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Marie-Claude Doucet, Panel Chair
Chair, New Brunswick Insurance Board

WE CONCUR:

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Francine Kanhai, Board Member

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Heather Stephen, Board Member