

## **Introduction**

1. In its September 16, 2016 motion to the Public Utilities Board ("PUB" or "Board") the Consumers' Association of Canada (Manitoba) ("CAC"), seeks an Order from the Board:
  - a. determining that MPI is not in compliance with rule 25(3) of the Rules of Practice;
  - b. determining that the failure of MPI to comply with the Rules of Practice is causing ongoing prejudice to the public;
  - c. directing MPI to provide and update Public Notice to ensure consumers are aware they are at risk of a significant Interest Rate Forecasting Risk Factor ("IRFRF") rate increase over and above the proposed 2% general rate application; and
  - d. such further and other relief as the Board in its discretion deems appropriate.
2. These are the reply comments of Manitoba Public Insurance ("MPI" or "the Corporation").
3. The public has had appropriate notice of the Application and the order that MPI is seeking. The Application, which has been publically available since June 17, 2016, is clear, concise and in compliance with Board Order 128/15 on how the Application must consider interest rate forecasting. The PUB's public notices issued on June 25th, 2016, and the reminder notice issued on September 10th, 2016, accurately identify the nature of the relief sought. MPI submits that CAC's motion is really an objection to the nature of the relief MPI is seeking, which is a substantive issue for determination at the conclusion of the hearing. MPI submits that the motion should be dismissed.

## **The Application Describes the Order Sought and Rationale Supporting It**

4. MPI's Application laid out in detail what MPI are requesting and the rationale for it. The order sought is set out on page 2 of the Application. It states in part:

In the 2017 Basic Autopac GRA the Corporation is requesting that the Board approve:

  - The premiums charged with respect to compulsory driver and vehicle insurance (rates for service) effective March 1, 2017.

- A 2.0% overall Basic insurance rate change effective March 1, 2017.
- **An Interest Rate Forecast Risk Factor (IRFRF), effective March 1, 2017, the form and magnitude of which will be developed through a collaborative process with the PUB and interveners.**
- No Rate Stabilization Reserve (RSR) rebuilding fee on Basic Autopac premiums effective March 1, 2017.
- A minimum (lower) RSR total equity target of \$181 million, based on a 1-in-40 probability Dynamic Capital Adequacy Test (DCAT) scenario from the 2016 DCAT report.
- A maximum (upper) range RSR total equity target of \$404 million, based on a 100% Minimum Capital Test (MCT) value.

(emphasis added)

5. The Application Overview, starting at page 3, summarizes the issue presented by the standard interest rate forecast that MPI was ordered to use:

“The IRFRF is a critically important element of Manitoba Public Insurance’s requested approvals in this Application. The Corporation is facing interest rate forecasting risk, as a result of the underperformance of third party interest rate forecasts. These forecasts have consistently overstated the interest rate forecast relative to actual results, creating both a persistent and significant risk to Basic’s financial health, and an increased prospect of future rate shock. It is no longer within the Corporation’s ability to manage this risk with capital transfers, and no other means of internally mitigating this risk is available to the Corporation. Therefore, in order to mitigate interest rate forecast risk in the best interests of ratepayers, the Corporation is applying for an Interest Rate Forecast Risk Factor (IRFRF). The Corporation has identified practical upper and lower range limits on interest rate forecasting risk, and is proposing a pre-hearing technical conference, involving the PUB and interveners, to explore the possibility of reaching 16 consensus on the form and magnitude of the IRFRF.”

6. Further, at page 5 the Corporation identifies the risk and potential consequence of such risk, created by the standard interest rate forecast:

“Stable and predictable rates are key to the success of the public auto insurance model over the long term. Significant rate increases in a short span of time will result in rate shock that can compromise the public’s confidence in Manitoba Public Insurance and the public auto insurance model.

In 2015/16, the Corporation transferred \$72.7 million in retained earnings from the competitive lines of business, saving Basic ratepayers from an 8% RSR rebuilding fee in this application. This transfer combined with a \$75.5 million transfer in 2014/15 has effectively depleted the ability of the competitive lines' total equity to subsidize Basic Autopac rates in the future.

Going forward, the Corporation faces a significant risk from the interest rate forecast, which could result in as much as a 7% increase in Basic Autopac rates being required for Basic to breakeven. Had the Corporation not transferred capital to avoid an 8% RSR rebuilding fee, together with the possibility of a 7% increase related to the interest rate forecast, customers might have been faced with significant rate shock of 15%."

7. At page 13 of the Overview, MPI describes how the requested IRFRF involves a rate increase on top of the 2% increase that is based on the mandated approach:

**"Unmitigated interest rate forecasting risk is unsustainable and represents a serious challenge to the financial health of Basic over the longer term. In order to mitigate this risk of deficiency in premiums and potential future rate shock, the Corporation is applying for approval of an Interest Rate Forecast Risk Factor, in addition to the 2% increase required to address other cost drivers.**

The Corporation is proposing a technical conference involving the PUB, interveners and MPI to address the form and magnitude of an Interest Rate Forecast Risk Factor to mitigate the risk of a deficiency in premiums resulting from the non-ALM impact of an inaccurate interest rate forecast. The Corporation is hopeful that a collaborative process of this nature will produce a consensus on the form and magnitude of the Interest Rate Forecast Risk Factor that is sufficient to manage the risk that the actual interest rate trajectory materializes somewhere lower than the Standard interest rate scenario and above the Flat interest rate scenarios. The long-term interests of the Corporation and customers are aligned in the desire to maintain the health of Basic insurance and avoid the need for large rate increases in future years." (emphasis added)

8. The Investment Income section of the Application includes further discussion on the risk factor on pages 15 to 24.

### **Public Notice Reflects What MPI is Seeking**

9. The PUB has issued two public notices in this proceeding. The PUB's public notices both reflect what MPI has requested; in the form that MPI requested it. It is accurate notice of the requested relief.

10. Both notices stated:

**RATE IMPACT:** The Corporation is requesting approval for Basic Autopac vehicle and drivers licence insurance rates and premiums effective March 1, 2017, which, if approved, will result in 2% overall change in MPI's Basic premium revenue (excluding the impact of vehicle upgrades and an increased overall driver and vehicle population). **The Corporation is also requesting an Interest Rate Forecast Risk Factor, effective March 1, 2017, to be developed collaboratively through the General Rate Application process.**

Actual vehicle and driver premiums would vary depending on claim and driving experience, insurance use, territory and vehicle rate group. **Full particulars, including the rate impact and application, can be found on the Manitoba Public Insurance Website: [www.mpi.mb.ca](http://www.mpi.mb.ca).**

Persons seeking further information as to MPI's application, or with respect to the Board's process, and/or wishing to address the public hearing in French should notify the Board Secretary by August 26, 2016. **As well, interested parties may examine MPI's application and supporting materials, either at the offices of the Corporation or on its website, or the Board's office.**

(emphasis added)

11. Public notice provides abbreviated content, with the practical objective being to notify individuals of the filing and forthcoming process. It is reasonable to expect that the details of requests must be ascertained and understood with reference to the Application itself. The Notices expressly refer people to the Application to inform themselves further, as reflected in the above quoted passages. As detailed above, the Application spells out in detail the request, the rationale for it, and the implications of it.
12. CAC has cited media articles that reference the 2% increase (although one also refers to the IRFRF). MPI's media release, which is included in Volume 1 of the Application, also referred to the Interest Rate Forecast Risk Factor:

In addition to an overall 2% increase in Basic Autopac rates for 2017, the corporation has requested that the Public Utilities Board consider introducing an Interest Rate Forecast Risk Factor, effective March 1, 2017, the form and magnitude of which would be developed through a collaborative process with the Board and interveners. The purpose of the Risk Factor would be to mitigate the risk of a significant premium increase in the future, due to year-over-year underperformance of interest rates against the forecasts established by the major Canadian banks, and which

has an ongoing affect on the Corporation's ability to achieve investment income forecasts.

13. In short, MPI has been transparent about its requests from the outset, and the public was well equipped to make further inquiries about them.

### **MPI Has Acted Consistently With What it Proposed**

14. MPI has proceeded in a manner consistent with what it requested in the Application. At the Pre-hearing conference, MPI proposed a September date for the Technical Conference on the IRFRF, and in response to feedback from the Board Panel, advanced the scheduled Technical Conference to August 16th, 2016. No party objected to the proposed process and Technical Conference at that time. On August 9<sup>th</sup>, 2016 PUB counsel circulated a draft agenda for the Technical Conference to all parties for comment. On August 15th, 2016, the Corporation circulated materials to be presented by the Corporation at the Technical Conference.
15. Following the Technical Conference, the Corporation prepared a detailed response to the PUB's second round Information Request ("IR") PUB(MPI)2-25. In that IR response, the Corporation:
  - a. provided a summary of the collaborative process to the current point in time,
  - b. identified the salient issues that emerged through the collaborative process that could inform a solution, and
  - c. presented a scenario, based on the outcome of the collaborative process, which in the Corporation's opinion will alleviate the issues around interest rate forecasting risk.

For ease of reference, the complete response to PUB(MPI)2-25 is enclosed as **Attachment A**.

### **CAC is Characterizing a Substantive Argument as a Procedural Issue**

16. CAC's motion is, in reality, an objection to the nature of the relief that MPI is seeking. Its objection is a substantive issue for determination at the conclusion of the hearing, not a procedural fairness issue. MPI submits that the procedural approach taken is a reasonable one.
17. In this Application the Corporation is facing a situation without precedent in that:
  - i) the Corporation does not believe the interest rate forecast it is required to use

is a best estimate, and ii) has limited ability to address the anticipated shortfall in revenue outside of an IRFRF rate increase.

18. Instead of waiting to the Hearing, where the reasonableness of forecasts are normally challenged, the Corporation raised this issue to the forefront in the Application, and in the Public Notice of Hearing.
19. The Corporation requested that it, the Board and the Interveners work collaboratively to address the issue of accurately predicting future interest rates. The Corporation believes there is benefit in collaborating with the Board and Interveners to find solutions to complex issues.
20. The Corporation's approach in this Application is consistent with CAC's own recommendation for addressing the complex issue of consistently overstated interest rate forecasts. At 2016 GRA Pre-Hearing Conference, the CAC had stated:

"...these are uncertain times for interest rate forecasters. And – and certainly with the panel's invitation, in—in the Hydro general rate application, we did go through evidence that addressed how interest rate forecasts have consistently overstated the interest rate expectations as compo—as—compared to—as compared to actual interest rate costs.... It's – it's a little more complex in –in terms of how it affects MPI....

One (1) of the recommendations our client made in the Hydro GRA was that there might be value – because it's an issue that historically has affected both of our – our major Crowns, that there might be some value in – in having some sort of technical conference or dialogue in terms of trying to have a – a common approach to interest rate forecasting and an exchange of views."

21. CAC's discussion of the merits of a collaborative approach was longer than the quoted passages above. Although the CAC was contemplating involving Manitoba Hydro in those discussions as well, MPI's proposal reflects the essence of CAC's discussion. Specifically, CAC was acknowledging:
  - a. that interest rate forecasting is an exercise that is inherently uncertain, and
  - b. a collaborative approach, incorporating a technical conference, is an appropriate approach to addressing the issue of interest rate forecasting.
22. The complete portion of transcript from the 2016 GRA pre-hearing conference is enclosed as **Attachment B**.

23. MPI submits that: i) the uncertainty around the problem of interest rate forecasting and ii) the very nature of a collaborative process, require that the specific magnitude of the IRFRF be the substantive issue for resolution through the hearing process.
24. As detailed above, the Corporation's public notice has met the test at issue in rule 25(3), that:
- "Notices ... shall contain a clear and concise statement of the substance of the application, including any proposed rate changes in sufficient detail and in plain language for the public's clear understanding of the substance of the application."
25. Accordingly, the Corporation has complied with Section 25(3) of the Rules of Practice in the current circumstances.

### **Conclusion and Order Sought**

26. MPI respectfully submits that CAC's motion should be dismissed. The nature of the Corporation's requested relief in the Application is clear. The PUB's two public notices issued on June 25th, 2016 and September 10<sup>th</sup>, 2016, accurately identify the nature of the relief sought. CAC will have an opportunity to argue at the conclusion of the proceeding that there is a better way to address interest rate risk than the approach MPI has taken, which appears to be the essence of its objection.

ALL OF WHICH IS RESPECTFULLY SUBMITTED

  
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Michael Friggs  
Director, Legal Services