MANITOBA PUBLIC UTILITIES BOARD

Re: MANITOBA PUBLIC INSURANCE
2010 GENERAL RATE APPLICATION

Before Board Panel:

Graham Lane - Board Chairman
Eric Jorgensen - Board Member
Len Evans - Board Member

HELD AT:

Public Utilities Board
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Pages 573 to 781

APPEARANCES

Walter Saranchuk, Q.C.	)Board Counsel
Candace Everard	)
Kathy Kalinowsky	)Manitoba Public Insurance
Raymond Oakes	)CMMG
Byron Williams	)CAC/MSOS
Nick Roberts (np)	)MUCDA
Donna Wankling (np)	)CAA
Jerry Kruk	)
Robert Dawson	)CBA/MBA

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THE CHAIRPERSON: Okay, good morning, everyone. Welcome to week 2.

Ms. Kalinowsky, do you want to introduce your witness and then we'll have him sworn in?

MS. KATHY KALINOWSKY: Yes, good morning, Mr. Chairman and others, Members of the Board. Here today, I'm pleased to present Mr. Richard Olfert, chartered accountant at -- managing partner at Deloitte, and he is prepared to testify with respect to cost allocation methodology as requested by the Board.

THE CHAIRPERSON: Thank you very much.

Mr. Gaudreau...?

MPI PANEL 2:

RICHARD OLFERT, Sworn

THE CHAIRPERSON: Thank you, sir. Welcome, Mr. Olfert.

MR. RICHARD OLFERT: Thank you.

THE CHAIRPERSON: Ms. Kalinowsky, do you want to begin?

MS. KATHY KALINOWSKY: Yes, sir. I'd also like to introduce to the Board, Mr. Olfert brought with him, his own back row specialist, Mr. Steve Martens who's seated directly behind him. Also a chartered accountant from Deloitte who assisted in the report.

THE CHAIRPERSON: Very good.

MS. KATHY KALINOWSKY: For ease of reference later on, I have already handed out copies of page 30 of the Cost Allocation Report, it's a coloured chart and I thought that it might be helpful just have -- people have that at their fingertips for later on. There's no need to mark it as an exhibit.

I spoke to Mr. Saranchuk about that earlier today because it's just a page that's taken directly from the report, but it's handy for people to have that available and at their fingertips, so to speak.

THE CHAIRPERSON: Yes, that's a very good idea. Thank you.

EXAMINATION-IN-CHIEF BY MS. KATHY KALINOWSKY:

MS. KATHY KALINOWSKY: Mr. Olfert, I'm looking at PUB-1-38, which is a copy of your curriculum vitae. I'd like you to explain your experience as a chartered accountant in cost allocation.

MR. RICHARD OLFERT: I was admitted as a member of the Institute of Chartered Accountants of Manitoba in 1988, and since my commencement in the profession I've been involved as -- in the auditing profession since 1995 as a partner with Deloitte, including audits of several of Manitoba's largest corporations.

With respect to cost allocation, there are a number of elements to that experience. First, all of our financial statement audits, of course, deal with the verification of costs.

With respect to cost allocation for regulatory or legal purposes, there are a couple of specific assignments that I have been involved in. Some years ago, I was involved on behalf of, then, Manitoba Telecom Services when it was regulated by the CR -- as it was regulated by the CRTC. And, at that time, it had Phase 2 filing requirements that required costing across several lines of business between its competitive and utility elements, and our responsibility was to audit their cost allocation calculations in accordance with the methodology what had -- which had been approved by the CRTC.

The other, particularly relevant example, relates to some work also some years ago done for -- in combination for the Government of Manitoba and the Government of Canada to audit the claims which Manitoba filed with Canada in relation to costs which were recoverable under the Canada Assistance Plan. Again, verifying that costs which were submitted were in cor -- in accordance with the definition of eligible costs which had been provided by the Federal Government.

MS. KATHY KALINOWSKY: Thank you for that. You're here to testify today on the cost allocation report, which is found at AI.19 of Manitoba Public Insurance General Rate Application filing?

MR. RICHARD OLFERT: Yes, I am.

MS. KATHY KALINOWSKY: And the report was prepared under your direction and control?

MR. RICHARD OLFERT: Yes, it was.

MS. KATHY KALINOWSKY: I understand there's a couple of very minor comments that you would like corrected in the report.

Is that correct?

MR. RICHARD OLFERT: That's correct. There's one (1) set of editorial changes which I will draw everyone's attention to, and they occur on page 39 of our report under Section 5.5, which is entitled, "Business Process Review Projects." In the middle of that page there's a list of numbered and lettered items. I'm referring to Item 2(a). And in the second line it says "Insurance LOB." That should in fact say "COB."

And, similarly, in the very last line of that paragraph, the last -- second last word should be "COB" instead of "LOB." And that, I might also point out one (1) additional item which was in the Corporation's cover to our Expense Allocation Methodology Report, and that would be on the second page of that cover note, the very last bullet point.

And the very last line of that bullet point should terminate after the COB parentheses, the words "and line of business LOB" can be stroked.

MS. KATHY KALINOWSKY: And, Mr. Palmer, you adopt those -- that change with respect to the AI.19 filing which was prepared -- the -- the preface which was prepared by Manitoba Public Insurance?

MR. DONALD PALMER: Yes, I do.

CONTINUED BY MS. KATHY KALINOWSKY:

MS. KATHY KALINOWSKY: This report was also pre -- presented to the Audit Committee of the Manitoba Public Insurance Board of Directors, by yourself.

Is that correct?

MR. RICHARD OLFERT: Yes, it was, at a meeting in late June of this year.

MS. KATHY KALINOWSKY: Can you explain to this Board, the Public Utilities Board, how Deloitte gathered information from Manitoba Public Insurance to make this report and also explain the interaction between MPI and Deloitte in preparing this report?

MR. RICHARD OLFERT: The work to which you're referring began in mid March of this year and concluded with the submission of the final report at the end of June. Allow me to take you chronologically through that period of time in order to answer your question.

So, in mid March we began with a kickoff meeting which involved all of the members of the Deloitte team, together with members of MPI's senior management. And at that meeting we were provided with a good deal of information which was background on the Corporation, information about its ongoing strategies with particular emphasis on the strategies to integrate the various services provided to MPI's customers.

After that meeting, our work basically followed two (2) streams of activity. First, there was a block of activity related to gathering information that would allow us to do the work, that's internal MPI information, and there was a stream of activity related to research on comparative corporations and other costing situations. So allow me to give you some detail on each of those.

First, in terms of gathering information, we began with a series of meetings with MPI's Director of Finance and Controller as well as his staff in the budgeting and planning area. And the purpose of those discussions was to gather information related to MPI's systems and its processes to understand better its process for establishing cost centres, as well as, how costs were aggregated within MPI's systems.

We then worked through at a -- we obtained and worked through a detailed description of the cost centres that MPI currently has and we sought a great deal of, I'll call it general information with respect to the Corporation, its activities and the activities within individual cost centres.

So we received documents on those topics in addition to the discussions which we had with a number of MPI staff. And we also gathered information with respect to the budget for the 2010 year. The budget, at -- at its status at that point in time and we reviewed it to understand how the cost centres, which had been identified to us, were accounted for in that budget.

And we worked through the budget in order to establish the nature of the types of costs that were being incurred. For instance, salary or other administrative costs or claims costs et cetera. And we also studied those -- that budget to try and understand which costs related to which part of the business. Concurrent with that information gathering activity, we had other members of our team involved in research activities. And, that research activity was principally focussed on gathering information from the web sites of various utilities, various regulators, research of various publications.

And we also engaged in discussions with the manager of financial reporting at SGI, the controller at ICBC and individuals on behalf of the Financial Services Commission of Ontario and New Brunswick Insurance Board and the Insurance Bureau of Canada.

Those activities each progressed until about mid April, at which point in time, we had an update meeting with senior management of MPI. That meeting consisted essentially of a number of questions that we had and discussion related to the cost centres that MPI has established. And it also gave us an opportunity to provide information on the research that we had done to date. That meeting also gave us an opportunity to clarify some of the costs that were in different accounting units and which line of business or category of business they might relate to.

And we then proceeded after that meeting to follow up on those various discussions and to continue taking our analysis to greater depths and that consisted of ten (10) to fifteen (15) or so meetings with a variety of people inside MPI related to specific types of costs incurred in specific cost centres.

In some cases it was clear to us that certain cost centres related specifically to a category of business or a line of business. Others, there was more question and it was those areas in which there was more question that we made sure that we had conversations with people from inside of MPI. That work continued to approximately the end of April and at that time we met with several of MPI's executives for two (2) purposes.

The first, was to outline our early conclusion that when there was -- there was a choice between accepting the pro rata approach to cost allocation or the incremental approach and our conclusion was that the pro rata approach should be adopted.

We presented that, discussed that, and that was concurred. In addition, we also outlined in broad terms our view that a methodology could be structured to create a decision tree type of logic, which is the decision tree that's presented on page 30 of our report, which is also the page that was handed out in advance.

There was also concurrence that that was a logical and reasonable approach to take, and so our work continued through the month of May. And in May we had continuing discussions with individuals within MPI, continuing to refine our knowledge of different cost centres and accounting units.

We also, at that point, began to work through the analysis, and calculations, and application of our evolving methodology proposal against the 2010 budget. And we also took opportunity, in the month of May, to visit the Winkler Service Centre so that we could understand specifically what was going on inside the first service centre, so that we would be in a position to understand what would occur, more broadly, as the service centre concept was put into place with the construction and development of an increasing number of service centres.

By the time we had reached the end of May we had worked through the methodology in a fair degree of detail and had a solid proposal for that. And so we again met with management to describe how we saw the decision tree methodology, if I can call it that, applied against the cost centres.

We described what would occur at each of Levels 'A', 'B', and 'C'. That discussion, I anticipate, we'll spend more time on later this morning. We discussed the challenges that occurred, for us, with respect to those costs which needed to be allocated because they were general corporate wide costs, those costs that are ultimately captured at Level 'C' of the methodology.

And then we also discussed in those conversations with management the alternatives that would exist for allocation at both Level 'C' and Level 'D'. And then, throughout the balance of the time at which we did our work, which was the month of June, there was ongoing work to finalize the allocation process at Level 'C' and Level 'D' of our approach.

And that also forced us, as we refined those allocators, to spend a little bit more time with certain individuals who were involved in those accountings units and cost centres that had the most challenge attached to them, and then we also drafted our report during the month of June.

That draft was distributed to the Audit Committee. And while the Audit Committee had it for a couple of weeks, we completed our internal reviews, which meant that we had a number of changes to make, principally editorial in nature.

And so, when we presented that report to the Audit Committee at its late June meeting we walked them through the material that had been distributed. We also provided them with an updated draft which reflected the editorial and other minor changes which we had made and described those to them.

And after we had heard word that the Audit Committee had no further questions of us, we finished our internal quality assurance processes, and the report was issued at the end of June, of this year.

MS. KATHY KALINOWSKY: Thank you very much for that. The report categorizes MPI as a service industry. Why is that important for cost allocation study and how would that differ as compared to MP -- MPI being classified, let's say, as a utility, for instance?

MR. RICHARD OLFERT: The objective of a cost allocation study is of course to determine which costs relate to which portion of the business. And when two (2) businesses are substantially different, one would anticipate that, while the principles of cost allocation might remain the same, the way in which they are applied could be quite different.

And so we, in doing our research, we obviously saw the work that was done by many capital intensive energy based utilities, the work that they did with respect to cost allocation. And while those principles were useful for us, the detailed parts of their methodology were of less relevance because of the fundamental difference in the business. There are a couple of significant differences that create that situation. The first is the degree to which those two (2) types of businesses depend on capital infrastructure for the delivery of services.

Obviously, in a utility -- or energy based utility, for example, the dependence on capital infrastructure is very high. For instance, if one -- if one compares the extent of long serving assets, for instance, of Manitoba Hydro, its balance sheet shows that almost 80 percent of its assets are long serving assets. In the case of MPI there's about 3 percent of the assets are capital long serving assets. And so the allocation process, with respect to capital infrastructure, does not need to occur in a service based industry as it does in a capital intensive one.

On the flipside, the preponderance of costs in a service based business like MPI, the preponderance of costs, or annual costs incurred annually, or costs related directly to serving specific customers, such as claims costs for instance.

And in the case of the capital intensive businesses that preponderance is obviously lower.

And so again, if you -- if you compare for instance, Manitoba Hydro and MPI, you can see that in the case of -- of MPI, the operating costs are substantially higher. If you look at the claims and the administrative costs are substantially higher than the annual operating costs of Manitoba Hydro.

A third difference would be in -- a third difference occurs because of those two (2) features and that has to do with the extent of annual costs which relates to depreciation and amortization. In the case of a capital intensive business that would be the -- a very large part of the cost to be allocated, and again in the case of Manitoba Hydro, those costs are in the range of 50 percent of the annual costs in the income statement, whereas at MPI depreciation and amortization would be less than 1 percent.

The last difference that I will draw will relate to the -- relate to the extent to which the costs to be allocated are comprised of administrative or corporate support costs, because of the large preponderance of capital in a capital intensive utility. That type of organization would have the majority of its costs -- majority of its benefits to customers delivered by that capital. And so in the case of -- in the case of Manitoba Hydro, the supporting costs are well in the range of a quarter. In the case of MPI, the administrative costs are much lower, in the range of 10 percent of the organization.

So there are substantial differences. What does that mean for cost allocation? Well in terms of what makes MPI unique compared to an energy related industry, is that in MPI's case virtually all of the costs to be allocated are annual costs, as comparison -- as compared to a capital intensive industry in which the costs are principally the allocation of expenses, investments, over a period of years.

Secondly, in MPI's case the allocation of costs that we're preoccupied with is across lines of business that are generally provided to the same customers. In the case of the energy utilities the focus of the cost allocation is more on the costs of serving different classes of customers. And then the preoccupation for regulatory purposes, I would expect, in the energy related industry relates to the allocation of costs between customers. And in the case of a service industry, the allocation is between those services which are regulated as part of the basic insurance, and those costs which are competitive. And what's regulated and what's competitive obviously differs by jurisdiction, as it relates to the service industries.

MS. KATHY KALINOWSKY: Thank you. I'd like to have you take a look at page 25 of the study at AI.19. And page 25 of the study that is a section dealing with the guiding principles and approach.

Deloitte indicates that it established five (5) guiding principles. Can you elaborate on each of those guiding principles and explain how each informed you in your development of the cost allocation methodology.

MR. RICHARD OLFERT: The first of those principles is the one identified at 4.2.1 which we identified as fair and reasonable. The principle objective of the cost allocation study is based on the need to identify costs with a line of business at MPI, and so costs ultimately need to be assigned to tho -- those lines of businesses.

And the concept of fair and reasonable would suggest that the costs which are assigned to individual lines of business should fairly reflect the cost of delivering those services. In addition, when the allocation process is completed, the results which come at the end of the process should yield reasonable results.

So, in some respects, the guiding principle of fair and reasonable is a bit of a common sense test that really has two (2) key dimensions. The first is whether the costs that are occurred have a causal relationship with the line of business to which they are allocated. So does the -- does the incur -- does the existence of that line of business require that cost to be incurred. The second dimension of that common sense test is is it transparent, can it be understood, and so that causality must be apparent for the allocation to be fair and reasonable.

In terms of how that was applied, that concept of fair and reasonable led us to our objective to ensure that we could maximize the costs which could be directly assigned to individual lines of business rather than -- so we chose to -- we -- our intent was to maximize costs which could be directly assigned rather than having them be caught in places where they would need to allocated on some basis.

A second example of fair and reasonable might be, when costs are captured for employee benefits as a whole, how does one allocate those? Well, a fair and reasonable basis, a common sense basis would be to say, How are the salaries allocated, and it would make sense for the employee benefits to follow the similar pattern.

The second guiding principle is noted at

4.2.2 as the -- as the principle of being practical and efficient. Now, in the context of our cost allocation methodology, that means, from our point of view, that the methodology should be suited to the environment or the business for which it's been developed and it should be able to be applied with relative ease.

And so that means, from our perspective, the allocation must be an -- understandable. It means that the allocation process itself needs to balance complexity. And getting to the greatest level of detail, that needs to be balanced with accuracy. What's the tradeoff between complexity and accuracy? It also needs to be workable, something that can be put in place and remain in place for a period of time. And notwithstanding the interest in balancing practicality and complexity, we would want to make sure there's no undue sacrifice of accuracy for the sake of ease of application of the methodology.

So where did that inform our process? First, you will note that we spoke about the purification of accounting units. That was in an effort to make the methodology practical and efficient. We were careful in terms of how the accounting units, being the lowest level of detail at which costs are aggregated, the aggregation of those costs into cost categories; that was done so that the methodology could be practical and efficient.

And we also endeavoured, where possible, to stay away from allocators that were based on work effort because those generally in -- involve a significant effort on behalf of the Corporation and can become very complex. And so if there was another which, in our view, didn't undermine accuracy or detail, we stayed away from work effort allocators where possible.

The third principle of flexible and adaptable, at 4.2.3, was a principle that said:

> "As the methodology is developed, it's important that it be developed in a way that it can be adapted into the future and take into account or handle ongoing changes to the operations, or ongoing changes to processes, or ongoing changes to the business model."

And so, from our point of view, the methodology needed to, first of all, anticipate those changes which we knew were coming, like the increased use of service centres. And -- and it also needed to be one that provided a framework, like the one that we will describe on page 30, the decision tree, it needed to provided a framework that could continue to be applied as the business evolved.

And so our design of cost categories and our construction of the decision tree that we will go through was an example of how we worked for the methodology to be flexible and adaptable.

The fourth guiding principle was that it be acceptable in a regulatory context, which, from our point of view, was quite simply that it needed to be acceptable to the regulator.

Now, why is that important? Well, some cost allocation that's done only for internal purposes within an organization probably lacks the rigour and may not be able to withstand the scrutiny that would come as it will -- as it does in this form. And so it was important to us that the methodology be done in a way that it was rigorous and that it was able to withstand that scrutiny.

So examples of how that informed our approach was that the potential use of the incremental approach to cost allocation was dismissed early on in the process. We spent a great deal of time and attention focussed on the budgeted costs at the accounting-unit level, so that when we ended up with the final accounting units into cost categories into the methodology, we had confidence that the trail of those costs would support the ultimate allocation. And we worked where allocators were needed to allocate costs. We worked to use allocators that have been used in other jurisdictions and have been found acceptable in those jurisdictions.

The last guiding principle at 4.2.4 was that consistency with industry standards would be important. These guiding principles were set at the very beginning of our work. And as we continued through the research phase of the assignment that I described earlier it became clear to us that this guiding principle was perhaps less instructive than we had hoped. The research that we did into industry standards demonstrated that the approach which we had adopted would be -- was generally accepted and it reinforced those fundamental choices that we made.

However, when we went searching for definitive guidance that was difficult to find, in part, because most of the other regulated situations are capital intensive energy utilities, and for the reasons described earlier those allocation methodologies were of less relevance.

And then, secondly, in the -- as I expect we'll also discuss later with respect to ICBC, there are some differences in the coverage provided at ICBC that make the allocation basis there less instructive than we might've originally hoped. However, industry standards was also a key element of our recommendation and ultimate conclusion that the pro-rata approach to cost allocation should be applied at MPI.

MS. KATHY KALINOWSKY: It's my understanding that two (2) options were available for the cost allocation study. Can you -- namely the incremental approach and the full -- or the pro rata full cost approach.

Can you explain each of these and then advise why Deloitte chose the full cost pro rata option?

MR. RICHARD OLFERT: The -- the incremental approach was considered for MPI as it was for ICBC, but in both cases ultimately rejected. The incremental approach essentially says there's one (1) business that exists, which in MPI's case would be the insurance business that it has historically been in since its inception, and then another business is added to it, in this case the driver vehicle licensing. And so the incremental approach would say let us establish what the costs are of providing that initial business, and then identify what additional costs are incurred in order to provide the incremental service.

The challenges in that methodology were two-fold. First it would require the establishment of the baseline or the base case for the existing business, which in itself is a challenge but as that business evolves and changes over a period of time, establishing that base would be an exceptionally difficult effort.

The second thing is that that methodology would have a bias to have costs remain with the original business, as opposed to being allocated to the business that was added on, which, in our view, was going to be problematic opposite the guiding principle of fair and reasonable.

The pro rata approach is one that simply says let's look at the costs and try and determine how those costs are incurred in the provision of the services. And where there needs to be allocation of costs to services that are supported by -- that are both supported by those costs, then let's find an acceptable way to split those costs between the two (2). So it's a look at the existing cost structure and allocation to the existing business.

The conclusion was that the pro rata approach should be selected and that's a conclusion that was consistent with the guiding principles that had been established. It's also a conclusion that's consistent with the one that was adopted by ICBC, and it's also consistent with the conclusion in virtually every cost -- every other cost allocation process which we reviewed where that cost allocation process had been employed for regulatory purposes.

MS. KATHY KALINOWSKY: On page 29 of the report under Section 5.2, Methodology and Approach, you mention that there's two (2) objectives. Can you please elaborate on those two (2) objectives you used in developing the methodology.

MR. RICHARD OLFERT: The two (2) objectives flowed from the guiding principles that I described earlier. The first one was that we would maximize what we'd call the assignability of costs. And so that is it was important to us wherever possible to identify where costs were incurred, specifically and exclusively in support of a single line of business or a single category of business. Because if costs could be so identified then no allocation process would required, they could simply be assigned to a particular line of business or category of business.

Examples of those would be the cost of claims, the costs of managing personal injury situations. Those costs are associated with the insurance line of business. That would differ from costs which require allocation. So for instance the cost of a receptionist at a service centre or administrative staff in the executive offices, it would be impossible to assign the costs of those salaries to individual lines of business. And so our first principle was where possible let's identify those costs that can be assigned.

The second principle was where allocation would be required. Then we would work to identify allocators that were practical and which were fair so that the basis of allocation would meet the criteria of the guiding principles. So that meant, where possible we would use actual operating information from within the organization or measures of activity, and we also wanted to use information which by it's nature was more objective than subjective, so that there would be less judgment applied rather than more, in the determination of the application of the allocators.

And that process of establishing practical fair allocators again required us to balance precision and suitability of the allocator with the effort and the extent of the analysis that would be required to develop and to quantify that allocator. Those were the two (2) objectives.

MS. KATHY KALINOWSKY: Thank you for that. Would you like to walk through a bit of the report and identify and explain the steps undertaken to develop the methodology starting with the identification of services offered, the identification of the category of business, the line of business, accounting units, cost categories, et cetera.

MR. RICHARD OLFERT: Sure. When we looked at the MPI system by which costs were captured, we identified that the greatest level of detail at which they were captured was the accounting unit level. And so a list of accounting units is provided in Appendix 'B' on pages 48 and 49 of our report.

We looked at each of those accounting units and sought information as to the nature of costs that was incurred in each of them. So that set of questions about the nature of the costs concerned itself first with: Is it salaries? Is it depreciation? Is it costs of managing a claim? Is it property costs? What is the type of expenditure being made?

And secondly, we sought information on the nature or -- sorry, we sought information on that part of the business and services to customers which was being supported. And so the intent of that effort was to be able to identify cost centres which were similar in nature.

So as an example, if you look on page 48, you can see that Accounting Units 13 through 17 are all claims centres. The nature of those costs are the same. The only difference is at which location they are incurred. So from our perspective those costs together with a host of other claims centre costs could be grouped together in a single cost category.

And so, our effort was to take the cost -- sorry, the accounting units that are listed on pages 48 and 49 and to group them into cost categories. And the intent of that was simply to take a large number of accounting units and reduce them to a smaller number of accou -- of cost categories which would be easier to work with.

And so Appendix 'C' which follows on pages 50 through 54 identifies the thirty (30) odd cost categories which were established and it describes the individual accounting units which are each included in those cost categories. It also describes the description of the costs and the nature of the costs that are incurred.

As we worked through that process, of that aggregation, we wanted to make sure that, to uphold our principle of maximizing assign ability, that where it was possible to make accounting units assignable by a simple revision to the type of cost which was charged to them we identified a series of recommendations for what we call purifying the accounting units, which would mean looking at the types of costs in an accounting unit and then extracting those costs which made that particular accounting unit not assignable. So as an example, in the regulatory and appeal accounting unit, that would be an accounting unit that we would anticipate should be allocated to the provision of Basic insurance.

However, prior to the recommendations that we made, that accounting unit also included the Crown Corporation counsel levy. That levy should be in our view, reflected across a number of -- across -- across the categories of business. And so by extracting that cost from that accounting unit, the remaining costs in the accounting unit could be assigned and then it would be important to have the Crown Corporation counsel levy placed into an accounting unit with similar types of costs that should be allocated across categories of business.

So the basic level of -- of captured information is the accounting unit, purify those accounting units so that they have the most like costs possible, group them into cost categories and then the cost categories would be used in the -- in the decision tree approach that we had identified.

Another key concept in that decision tree approach relates to line of business versus category of business. And here, I might already draw your attention to page 30 which was distributed that includes the decision tree.

The objective of the cost allocation methodology in its most basic form is to take the total costs of normal operations which would be a number that would appear in the top black box, and ultimately those costs need to be split up into four (4) specific landing points. And those are the four (4) across the bottom. Basic insurance, Extension insurance, SRE and the non-insurance. So each of those four (4) items has been referred to -- I'm sorry, those -- the three (3) insurance items each are referred to as a line of business.

In addition there are several lines of business within non-insurance including DVL and Identification Cards for purposes of the Cost Allocation Study. The direction, which we received, was that as long as those costs were captured together as non-insurance, that was sufficient and the methodology did not need to break them into further line of business costs. So there are a number of lines of business, the three (3) insurance ones are Basic, Extension and SRE and non-insurance has several.

Another concept, which we developed as part of the methodology, was the concept of the category of business. And so a category of business came about as a result of our efforts to maximize the assign ability of costs.

So as an example, when one looks at the costs of a claims centre it is not possible to identify from the accounting units what of that cost should go to Basic, to Extension, or to SRE. However, those costs quite clearly relate to the insurance operations and not the insurance operations -- sorry -- they relate to insurance and they do not relate to non-insurance.

So in order to assist in the assignability of those costs the concept of a category of business was developed so that costs like claims centres could be assigned to a category of business with allocation then occurring within that part of the decision tree. And there would be no risk that any of those direct insurance costs would by virtue of some allocation process be allocated to the non-insurance part of the business.

So those are the concepts which were used in the development of the methodology and that methodology is summarized in the decision tree on page 30.

MS. KATHY KALINOWSKY: You've summarized some of the methodology used in the decision tree at page 30 but I'd like you to walk through level by level the recap of the levels and identify that in a fairly significant amount of detail recognizing that this really is the nuts and bolts of the cost allocation methodology.

MR. RICHARD OLFERT: One (1) overall comment before we look at the chart itself was that when we looked at the budgeted information for the 2010 year there were two (2) types of costs in there. There were the normal operations costs of some 976 million and there were business process re-engineering costs, BPR costs.

This methodology has been designed to deal with the normal operations costs and the report speaks separately to how BPR costs should be handled. That was done on the basis that BPR costs by their nature are project-specific and should merit specific attention. And also in the accordance with the guiding principle of being flexible and adaptable in time the BPR projects will have wound down and represent a much smaller portion of MPI costs. And so in the long term, the normal operations costs are what will require allocation. So this deals with normal operations costs. BPR costs are dealt with separately in our report.

So as I mentioned, the methodology, which is reflected in this decision tree if you will, is designed to have the total normal costs, ultimately, allocated or assigned to four (4) final destinations:

Basic insurance, Extension insurance, SRE insurance, and non-insurance. And this was done using the aggregation of costs at the cost category level.

So the first thing that would happen in the methodology is what we called the Level 'A' decision point, which is to ask, when one looks at those cost categories, which of them are directly linked to a line of business, one (1) of the four (4) at the bottom of the chart?

So, examples would be the cost of provider -- providing driver licensing, driver examination services included. Another example would be broker commissions which are paid based on a schedule for a commission for a particular type of transaction. Premium taxes and claims are all examples of items that can be assigned to a line of business.

About 82 percent of those budgeted normal operations costs are assigned directly at Level 'A' into each of the four (4) final destinations. The remaining 17 percent and change of the costs are costs which cannot be so alloc -- so assigned into individual lines of business or the non-insurance category of business. And so, the Level 'B' part of the decision tree is designed to begin taking those costs apart so that they can ultimately be placed into the appropriate place.

And so at Level 'B', we begin to look for a certain cost that, while they cannot be assigned to a particular line of business, are costs that relate to a particular category of business. And so, for example, the management of injury claims, the operation of claims centres, loss prevention activities, insurance support operations. These are all costs that support the insurance category of business, exclusively. And so they are assigned at Level 'B' to the box that reads, "Signable to the Category of Business - Insurance." And there's approximately another 7 percent and change of costs that are assigned directly into that box.

So that means between the Level 'A' assignment and the Level 'B' assignment either to line of business or category of business just under 90 percent of costs can be directly assigned into one (1) of the three (3) insurance lines of business or the overall insurance category of business.

At Level 'B' there are no additional costs that are assigned to the non-insurance category of business because, of course, that's the same level of aggregation as the box at the very bottom of the chart. And so Level 'A' would have picked up all such costs which means that in the middle box of Level 'B' these are costs that are incurred by the Corporation in support of both categories of business, insurance and non-insurance.

So for example, this would be things like costs of property, it would include non-assignable information technology costs, it would include employee benefits, it would include customer support et cetera. And so just over 10 percent of the normal operation costs are identified as "subject to allocation."

Then at Level 'C' the question is how should those costs which are "subject to allocation" be split between the insurance and the non-insurance lines of business And at Level 'C' is where a series of allocators are required. So at Level 'C' is where there's application of some of the principles as the allocators are established to split costs between the insurance and the non-insurance category of business.

Once those allocators are applied to the cost centres for which they have each been identified, that total amount of costs, subject to allocation, which using the figures in the report which were based on the then 2010 budget, amounted to just over $100 million. Those are then split between the cate -- the insurance and non-insurance categories of business.

And then at Level 'D' there would be certain costs that are -- that relate to the insurance category of business. So this would be those costs which were directly assigned like injury claims, management, and claim centres. And those costs which were allocated, which would be the insurance portion of senior management, support time, corporate IT and so on, those costs are grouped together, that amounts to about $160 million using the numbers in the study.

And then at Level 'D' there again a series of allocators that are established for each of the -- a series of allocators were established, one (1) for each of the cost categories so that the costs which have been allocated are assigned to the insurance category of business can then be desegregated and assigned to each of Basic, Extension and SRE. That would a summary of the decision tree methodology.

MS. KATHY KALINOWSKY: Thank for that level of detail, Mr. Olfert. Not to belabour the point but I'd like you to also walk through Sections 5.3.1 which is located on page 33 and then 5.4.1.

And perhaps direct the Board Members to the actual use of the different levels.

MR. RICHARD OLFERT: The table on pages 33 and 34 under 5.3.1 lists each of the cost categories. So again to recap, each of the hundred and twenty-nine (129) accounting units have been aggregated on the basis of like costs into the cost categories identified as 'A' through 'GG'.

The table then identifies how those cost categories are handled in the methodology. So for instance, Cost Category 'D' is assigned at Level 'A' to the non-insurance category of business, in the same way that Cost Category 'X' is assigned at Level 'A' to the Basic line of business.

A variety of costs, as I described earlier, are assigned at Level 'B', and you can see those costs identified with Xs under the column that reads, "Insurance." So at Level 'B' costs are allocated between insurance, and so cost categories 'A', 'B', and 'C' would each be assigned to the insurance category of business. Whereas Categories 'E' and 'F', for instance, could not be assigned to a specific category of business and hence were identified for allocation. All of the costs which have an 'X' under the Allocation column are those costs which must be allocated at Level 'C' and those are the ones for which allocators must be developed.

And Section 5.4.1 identifies what the suggested allocators are for each of those cost categories. If we review them one-by-one, Category 'E', approximately $3 million in amount, relates to the maintenance of driver records. So there is a single set of efforts used to track information on convictions, on court processes, on accident reports, on suspensions, et cetera, and that single set of processes drives information uses by both the court system and law enforcement, related to non-insurance DVL activities, and it drives information that's used by MPI in its merit program in the establishment of insurance rates.

And so our suggestion is that the allocator be estimated work effort, and in that case because there's one (1) process that yields two (2) -- supports two (2) purposes, the estimated work effort suggestion is a 50/50 split.

Cost Category 'F' on vehicle registration, about $1.8 million, relates to personnel who are principally providing vehicle registration services, but there are certain classes of commercial vehicles for which insurn -- insurance services are provided. And so our suggestion is that work effort be analysed so that an allocator can be developed based on that work effort. That analysis to determine precisely what the percentage allocation would be has yet to be completed, but we would anticipate that that work effort basis would have most of those costs allocated to the non-insurance line of business.

Cost Category 'I' on service centres is allocated on the basis of what we've called, "Category of

Business Salary Ratio." So let me describe that one in a bit more detail, and a bit of background is required in that description.

When one enters a service centre it is a facility that is designed to provide MPI customers with both ins -- both insurance and non-insurance services. When one analyses the effort that goes on inside the service centres a large part of that effort by individuals has each individual's effort specifically attached to either insurance or non-insurance activities. So, for instance, the claims adjusters and those who assess vehicles brought in for damage are clearly focussed on the insurance line of business, whereas those who are present in the service centre to provide driver testing are clearly for non-insurance purposes.

And so by analyzing the costs within a service centre, the salaries that are directly related to insurance services can be identified, and salaries that are directly related to non-insurance services can also be identified. There are some costs of -- there are some salary costs that cannot be assigned in that fashion, for instance, the receptionist who would be at the front desk, however, the majority of the costs can be assigned.

And so when one takes the ratio of those dedicated insurance costs, versus the dedicated non-insurance salary costs and compares that two (2) sets of salary, that's the category of business salary ratio that we are referring to, and that would be the basis for allocating service centre costs.

Category 'L' on physical properties, would be the allocation of just about $19 million. And the basis of allocation would be what we're calling the enterprise-wide per square foot basis. That would essentially require that each location which MPI has would need to have its square footage analyzed and assigned to a cost category.

Concurrently, work would be done to determine the aggregate cost of property and the aggregate number of square feet, so a corporate-wide per square foot amount could be calculated. And then having allocated the square feet for each location to individual cost categories, and having a per-square foot amount that would then allow the square feet attached to each cost category to be calculated and allocated in the same proportion as that cost category is for other purposes within the methodology.

Item 'T', Employee Benefits, which is almost $13 million, is a percentage of base salary costs. Mechanically, that works basically the same as the enterprise-wide per-square foot basis. How are the salaries? What is the ratio of employee benefits to salaries so that one can calculate what I might call a burden? That burden is then allocated to categories of business on the same basis as the salaries are in each and every cost category.

Category 'V', Identification Verification and Data Integrity, costs of about half a million dollars. Again, a single block of activities occur that serve both insurance and non-insurance activities. Our suggestion is that estimated work effort be used, and given the nature of the work that goes on there, that estimated work effort in our view would be 50/50.

Category 'U', for Legal, which is just over $2 million would require a basis of work effort to be established for the legal department, so that the costs could be allocated based on that study between insurance and non-insurance.

Customer Service and Support Costs, Category 'W'. Approximately $9 1/2 million are the costs associated with MPI's interactions with its customers. And the basis of allocation which being -- is being recommended there is the weighted customer call centre contact ratio, which I'll simply call a "customer contact ratio" for the balance of the day. And that is a measure of the inbound customer call activity into the organization by type of call and duration of call, so that the costs that are spent serving customers by MPI can be allocated in accordance with the subject matter of the calls coming into the call centre.

Cost Categories 'K', 'M', 'N', 'O', 'P', 'Q', double 'AA', double 'BB', and double 'DD', are all costs associated with, I'll call them "Corporate Support Functions." This would have been an area of significant challenge because these are the costs which have the least assignability to individual cost categories -- sorry, the least assignability into individual categories of business or lines of business. And so after considerable reflection and evaluation of alternatives our recommendation is that those costs too, be allocated on the basis of the customer contact ratio.

The application of all of those allocators listed on pages 34 and 35, under 5.4.1, that's the sum total of the allocators that would be used at Level 'C' which are all of the -- all of the cost categories designated for allocation on the initial table that was referred to at 5.3.1.

MS. KATHY KALINOWSKY: Can you perhaps elaborate a little bit more on the weighted customer call centre contact ratio, elaborate on it and explain how the tracking of calls works, to the best of your knowledge.

MR. RICHARD OLFERT: The assignment of costs at Level 'C' for this group of costs was among the largest challenges that we had, as I mentioned earlier. And that's because these costs are not assignable and there's no particular causality between any individual dollar that's spent here in a particular line of business, and the costs that are incurred in those cost categories support services to customers in both of the categories of business.

And so several options were considered and the key features that we believed were required in an allocator for those costs was that they reflected the inherent higher complexity of the insurance operations, versus the non-insurance operations.

And we debated whether or not the allocator for this block of costs was better suited to be an allocator based on an internal view of MPI, or whether it was better based on an external view of MPI's support activities. And our conclusion was that the pers -- all of the service -- all of those costs support services to customers, and so the external view of the customers should be the guiding light in terms of how they should be allocated, and so the customer contact ratio was selected.

The way it works, in terms of the

mechanics, is that, when a customer calls into MPI's call centre, the automated voice menu requires the individual to designate what the nature of their call is, looking at it from a customer's perspective: Is it a new claim? Is it a glass ca -- claim? Is it a question about driver's licence? And so on.

And based on that categorization by the customer, the call is then categorized into a number of categories which we have aligned with insurance and non-insurance. Those calls are then measured in terms of length, and then the aggregate number of minutes spent on each type of call, which can then be aggregated to the number of minutes on - insurance versus non-insurance calls can also be aggregated. And it's ultimately that proportion of minutes of customer calls that determines the customer contact ratio.

MS. KATHY KALINOWSKY: Thank you. And you -- you had provided a dollar figure for the various different other cost categories. Do you have an aggregate dollar figure for the corporate support functions?

MR. RICHARD OLFERT: Yes, the corporate support functions allocated using the customer contact ratio amounted to approximately $52 million.

MS. KATHY KALINOWSKY: And can you just

clarify to the Board that the weighted customer call centre contact ration is only done at the Level 'C', which is the allocation between insurance and non-insurance.

MR. RICHARD OLFERT: That is correct.

MS. KATHY KALINOWSKY: And you're not proposing that the weighted customer call centre contact ratio is between -- allocation of costs between Basic, and Extension, and SRE?

MR. RICHARD OLFERT: That is also correct.

MS. KATHY KALINOWSKY: Thank you. You've explained how the cost allocation methodology operates it.

Did you apply it to the MPI costs, and, if so, how and what were the results?

MR. RICHARD OLFERT: As I described, we did indeed apply that methodology to MP -- MPI's 2010 budgeted costs. And to demonstrate how that application worked, I will direct your attention to Appendix 'D', which begins on page 55 of our report. On page 55 one can see all of the cost categories listed, with the aggregate of normal operations costs being just over $976 million.

The first step in our recommended process would be the purification of those cost units. I'm sorry, the clar -- the -- the purification of those cost categories, a couple -- and you see the impact of the adjustments in the middle column. As an example, you can see there's an alloca -- a reallocation or a re -- an adjustment of costs between Categories 'CC' and 'DD', that would represent our recommendation that Crown Corp. levy be moved out of regulatory appeal and into a place that will be allocated, which then leaves regulatory and appeal as a pure cost which can be assigned later on in the methodology.

Similarly, if you look at cost Category 'M', Corporate Information Technology, costs that can be specifically identified as costs related to the operations of the CARS system, which is in place for managing claims. Those costs could go to a cost category that is assigned directly to insurance.

And so where information technology application costs could be specifically attached to a category of business activity, they were reclassified. And, in this case, the four million six twenty-seven (4,627,000) had been allocated -- has been adjusted into Category 'B' where it's part of the six million three forty (6,340,000).

As a result of those adjustments, and

these adjustments represent the aggregate impact of the purification recommendations contained within the report.

The $976 million of costs are reset into what we've called, "The Purified Normal Costs." And those purified normal costs are carried forward to the first column on pa -- on Table 2, which is on page 56.

The first step in the methodology is the Level 'A' assignment to ask which of these cost categories relate exclusively to an individual line of business within insurance or to the non-insurance category of business. And then you can see in those middle four (4) columns from basic LOB through to non-insurance COB, that there are about $800 million of costs that are directly assigned at Level 'A' into the four (4) final landing places in the methodology, which as I mentioned earlier is about a little over 80 percent of the aggregate costs.

That leaves the costs in the right-hand column of just over $172 million, as costs which must be further considered in the methodology because they could not be assigned to an individual line of business.

That number of one seventy-two four eighty-two (172,482) carries forward to the first column of figures on page 57 in Table 3. And this table identifies those -- those costs that are assigned to --

those costs which can be assigned to a category of business. And so Injury Claims Management for instance at Level 'A' -- sorry, Cost Category 'A', relates to provision of insurance services and so it is allocated to the insurance category of business, similarly with all of the other items that are under the insurance category of business column, and then you can see that that leaves one hundred million eight hundred and thirty-three thousand (100,833,000) of costs which are still subject to allocation.

And that's the same hundred million that I referred to earlier as needing to be allocated at Level 'C'. That $100 million of costs which represents just over 10 percent of aggregate normal operations, needs to be allocated between the insurance and the non-insurance category of business. And that allocation is done of page 58 in Table 4.

And so in keeping with the allocators that I've described earlier, Categories 'E' and 'F' are allocated on work effort. Category 'I' is based on COB salary ratio. Category 'L' and physical properties uses the per square foot amount and so on, with the largest number of cost categories done using the customer contact ratio, again amounting to approximately half of those costs at $51 or $52 million.

Having completed Level 'C' there are -- there is still one (1) step left which is the Level 'D' allocation, and that occurs on page 59. The first column on page 59, or Table 5, shows those costs which were assigned or allocated to the insurance category of business. So just to be clear, coming out of Level 'B' on page -- sorry, coming out of Level 'B' on Table 3, two (2) pages back, there was seventy-one million six hundred and forty-nine (71,649,000) of costs that were assigned to the insurance category of business. And then on level -- at Level 'C' there was eighty-seven million nine hundred and seventy-three thousand ($87,973,000) million of costs al -- sorry, allocated to the insurance category of business.

So between Level 'B' and Level 'C' an aggregate amount of one hundred and fifty-nine million six twenty-two (159,622,000) was assigned or allocated to the insurance category of business. And then Level 'D' uses the allocators set out in the report to split those costs between the Basic, Extension, and SRE lines of business.

So after completion of those steps in the methodology, Table 6 on page 60 demonstrates the final allocation of each cost categories dollar amounts into the four (4) final landing spots on the methodology. And you can see the totals on page 60 with just over 800 million being allocated to Basic line of Business and so on with just -- just under 26 million being allocated to the non-insurance category of business.

MS. KATHY KALINOWSKY: Thank you very much for that detailed explanation of the methodology that you developed for Manitoba Public Insurance.

I want you to move back a little bit, in terms of the chronology, and I understand that you looked at Saskatchewan Government Insurance, SGI, and the Saskatchewan Auto Fund.

Could you perhaps give a bit of comparison to the Board in any kind of lessons derived from your study of SGI and SAF?

MR. RICHARD OLFERT: In looking at the SGI/SAF comparator it's important in the first instance to understand the organization of SGI and SAF. SGI is owned by Saskatchewan investments. It's got a broad P&C product mandate, so it offers a variety of insurance products beyond auto. It provides insurance in seven (7) provinces and it also provides the Extension products for the coverage which I'll describe in a moment, which is provided by Saskatchewan Auto Fund or SAF. SGI also provides certain claims and administrative services for SAF.

SAF, on the other hand, is owned by the Province of Saskatchewan. It's regulated by the Saskatchewan Rate Review Panel and it provides, on a monopoly basis, personal injury coverage, core collision coverage, and third party liability coverage to Saskatchewan drivers. It also provides driver licensing and vehicle registration function. And all of those activities, whether it's DVL related or related to the insurance coverage, are all covered by the Basic rates.

So the second area of interest to our process when we looked at SGI/SAF, was what is the need for or the basis of cost allocation that's done in that environment? And the purpose of the allocation is a little different in that environment because all of the costs that are captured within SAF are recoverable through Basic rates, and so there is no need to allocate costs within SAF. The allocation that is required in the SGI/SAF environment goes back to the fact that SGI provides certain claims and administrative services to SAF, and so SGI needs to bill SAF for those amounts. And so then the question of course is at what amount should that billing take place?

There's no information available publicly on how that is done. We requested information and it was not provided to us on the basis that that information was not public. And so through review of the financial statements of the respective organizations, it's apparent that there is an annual amount calculated and a charge levied from SGI to SAF. It also appears that there's a target range in which that -- that costing amount should fall, though it's unclear to us precisely how that's established.

And so while it was interesting to compare the SGI/SAF situation to Manitoba, the fact that there was no allocation within SAF was not particularly helpful, and an inability to see the SGI calculation of allocated costs left us without any learnings from that particular effort.

MS. KATHY KALINOWSKY: And what about ICBC?

MR. RICHARD OLFERT: Considerably more information was available on ICBC, and so let me provide you with our perspective on that information in a couple of categories.

First, let me describe for you sort of our overview of the situation, and then I can take you through their cost allocation methodology and then I can provide you with some observations on the regulatory process and ultimately with some lessons that we learned from that process.

So ICBC is a provincial Crown corporation in British Columbia. It is a monopoly provider of Basic coverage and it's regulated by the BC Utilities Corporation. And it too has responsibility for driver and vehicle licensing and its responsibilities in that area actually extend beyond those which MPI has in Manitoba, because some of the functions that today in Manitoba rest with the Government of Manitoba, in fact rest with ICBC in British Columbia, so that would include the collection of fines, for example, and another example would be the operation of commercial vehicle compliance facilities, like weigh scales. That's done by ICBC in British Columbia.

In looking at ICBC's coverage, insurance coverage, again, an important difference to note to Manitoba, the Basic compulsory coverage in British Columbia is made up of the third party liability coverage and it's made up of personal injury coverage.

The optional coverage which ICBC provides includes collision coverage, which, of course, in Manitoba is included with in Basic, and it includes Extension products similar to the way Manitoba offers Extension products.

And so, when we reviewed all of the ICBC material, it was exceptionally important to us to remember that every time in that material we read "Basic" versus "Competitive," that was a different comparison than in Manitoba when we say "Basic" versus "Competitive," because in BC that means personal injury and third party liability versus collision and extension, and in Manitoba it means collision, and liability, and personal injury versus extension.

So the placement of collision in a different spot is exceptionally important in making that "Basic" versus "Competitive" comparison. In terms of the operations, ICBC, as I mentioned, has responsibility for DVL operations, and ICBC's material will describe that as an integrated offering of DVL services.

What they mean by integrated is it's provided by the same corporation. When one looks at the method by which the DVL services are delivered, they are actually delivered at separate standalone facilities, unlike Manitoba, where integrated means the direction of providing those services from the same facilities.

And the second significant difference is that, in British Columbia, all of the DVL costs, including those for the services -- sorry, including those for the DVL aspects of operations, like fines and commercial compliance facilities, which in Manitoba rests with the government, all of those costs of DVL services are covered by Basic premiums in British Columbia.

And so, when one looks at the purpose of cost allocation in British Columbia, our sense was that the principle concern is the allocation of costs between Basic, being third party and injury coverage, and Competitive, being collision and extension.

Now that's significantly different from Manitoba in two (2) respects. First, in terms of quantity, in Manitoba that competitive piece would be less than 20 percent of revenue, in BC it would be more than 40 percent of revenue.

And it's also a significant difference in terms of nature, because, as I mentioned before, in British Columbia the Competitive business includes collision coverage, which is considerably different from simply providing extended insurance coverage, as MPI does, in its Extension services.

The other interesting aspect of MPI's -- sorry, ICBC's cost allocation was that there -- while there is a requirement to split costs between insurance and non-insurance, the level of concern or attention to that appears to be relatively low because, ultimately, those non-insurance costs are scooped back into Basic for the determination of rates.

So if we then shift from sort of an

overview of the ICBC situation to an overview of their cost allocation methodology, ICBC also began its Cost Allocation Study with the comment that there's a significant difference between capital intensive energy related utilities, where the most significant amount of guidance is available, and an insurance based services entity.

Then, as it rolled out its cost allocation methodology, ICBC began with a guiding principle. And by guiding principle, they meant the selection of the pro rata approach over the incremental approach, because, as ICBC's methodology states, it views the pro rata approach as more objective, and more reasonable, and more reflective of economic reality, and that is the same conclusion that we reached with respect to MPI's cost allocation.

In ICBC's case the next thing they did was to establish the allocation criteria which are in many respects serve a similar process as what we call guiding principles in our report. They highlighted four (4) allocation criteria.

The first, was that they would follow generally accepted accounting principles for information, that is, it should be understandable and relevant and reliable and comparable. And those elements are akin to fair and reasonable and practical and efficient, which we identified as guiding principles in our report.

Their second allocation criteria was that their approach should be consistent with the North American Assurance Commissioner's Guidelines that speak to this -- that speak to cost allocation. And those guidelines essentially say that where possible, costs should be specifically identified with the business that they undertake, which is another way of saying assignability should be maximized, a key part of our underlying principles. And where that can't be done then a fair and reasonable allocator should be selected, again, which was a significant part of our process.

The third criteria which ICBC used was that material that was available at that time, being an expense allocation program guidance from the Insurance Bureau of Canada, that that be complied with. That material has since been withdrawn by the Insurance Bureau of Canada and so we were not able to consider that in our approach.

And lastly, the final allocation criteria for ICBC was that their methodology should be consistent with method -- methods that were used in Canada's public auto insurance. And so that is an approach that we also followed by drawing on SGI and principally on ICBC.

So in terms of ICBC's guiding principle and its allocation criteria, we see them as lining up with the guiding principles and the basic objectives which we established. Their allocation process was designed around three (3) steps.

The first was to identify where costs could be directly linked with parts of the business, something they called directly attributable, which in brackets meant, not allocated, exactly the same concept as we were working with when we said maximizing assign -- assignability which on our chart shows up at Levels 'A' and 'B'.

Their second step in the process was to attribute claims incurred to the line of business to which it related, which is the same concept which we applied at Level 'A' and then where allocation was required there be an allocator determined based on work effort, premiums written, claims incurred, or shared services.

Those are the same kinds of considerations we went through at Level 'C' and Level 'D' and in fact, similar types of allocators are used at MPI -- or are suggested for MPI as are used at ICBC, with the single difference being that there was a significantly higher emphasis on premiums written in the ICBC case, but that principally had to do with splitting up certain costs of providing insurance like underwriting. Where, the fact that collision is in a separate category means that there needs to be more analysis of the costs to obtain that Basic versus Competitive split.

In ICBC's scenario we were unable to obtain the numbers in terms of how everything flowed through from the total costs into the final allocated amounts but our sense is that in excess of 80 percent of their costs were directly attributable, which compares in Manitoba's case to about 90 percent of the costs being directly attributable.

If I can make a couple of observations that factored into our work, as a result of the regulatory process that has gone on in BC, their chronology is that their costing methodology was filed in 2003. Since then they've had a number of developments with respect to that when the costing methodology was filed. It was filed with a professional report suggesting that the provider's view was that the methodology was appropriate and reasonable.

They have since engaged another firm to work together with them as they resolve some of the BCUC's questions. That firm also, again, indicates that the methodology is appropriate and reasonable. And BCUC has agreed with the methodology and concept though it continues to have questions on some of the allocators.

So with respect to those allocators there -- that -- on which there are questions, there are principally two (2) groups of questions that have occurred. Early on there was one (1) group of seven (7) allocators that was questioned. More information was sought about those allocators. That information was provided and after that, five (5) of those were accepted and BCUC required refinements on two (2) of those seven (7) allocators principally having to do with the split between Basic and Competitive, again, third party and injury versus collision.

And then there was a second set of seven (7) allocators that has resulted in an extended process. That process has included a series of questions from the regulator and negotiated settlement process, updated work effort studies and now there's an independent third party review been sought.

Fundamentally, the issue on those seven (7) allocators, is that they relate to work effort allocators and what is the basis for calculating them?

And then secondly, all of the questions related to those work effort allocators are designed to get at the appropriate allocation of costs between Basic and Competitive again trying to make sure that the right costs are attributed or allocated to the competitive or collision line of business.

So after all of that analysis of ICBC, what were our learnings or our take-aways? The first, was that the broad framework which we provided is consistent with the approach that ICBC has employed.

Secondly, our approach of maximizing allocation of costs -- sorry, maximizing assignability of costs and minimizing allocation is again consistent.

And lastly, it would be our view that the principle sources of ongoing discussion about those parts of the ICBC methodology that are continuing in process they relate principally to circumstances that don't exist here which is an interest on the part of the Intervenors and making sure the costs of insurance provision between third party and injury versus collision are appropriately handled. That would summarize the ICBC learnings.

MS. KATHY KALINOWSKY: Thank you for that.

Mr. Chairman, I'm -- I'm looking at the time, but I only have two (2) more questions, so with your indulgence, I'd like to proceed, if that's possible?

THE CHAIRPERSON: Please.

CONTINUED BY MS. KATHY KALINOWSKY:

MS. KATHY KALINOWSKY: Mr. Olfert, can you also provide a comparison with in lessons derived from other regulated utilities or organizations?

MR. RICHARD OLFERT: With the exception of the two (2) that we've already talked about, ICBC and SGI, SAF, all of the other information that was available to us came from energy and infrastructure based utilities.

And so for the reasons I described earlier that information was of limited use. Nonetheless, that analysis supported the use of the pro rata approach which was employed in all of those situations that we looked at. And all of them had significant guiding principles. So that left us with the view that our approach for MPI was conceptually consistent with those -- with that used in other scenarios.

And the detailed methodology that was developed for those other situations was of less relevance because of the significant difference between the capital intensive utilities and the service based monopoly situation.

MS. KATHY KALINOWSKY: And the final question that I have, Mr. Olfert, is that the Public Utilities Board had identified eight (8) areas to be addressed in a Cost Allocation study.

Can you identify the eight (8) different areas and explain how each was factored into the development of your methodology?

MR. RICHARD OLFERT: That question is specifically addressed in Section 6 of our report which starts on page 40. Allow me to go through the eight (8) areas individually.

The first question related to the Driver Licence Service Delivery Model with the reflection on the fact that the integrated service offering was being provided through brokers on behalf of MPI and there was an interest in assuring the appropriate allocation between driver licensing, Basic, Extension and SRE.

In terms of the methodology, there are two (2) components to the broker cost that we would be concerned about in relation to that question. The first and the largest would be the broker commissions themselves and these are payments that are provided to the brokers for actually performing individual transactions. There is a schedule that exists which provides detail on how much compensation is to be provided to each broker for each transaction undertaken.

As those transactions are undertaken the cost of each is identified and tracked into an accounting unit and so those broker commission costs can, through the process I described earlier, be directly assigned into insurance line of business and the non-insurance category business.

The second type of cost is what we've called "Broker Network Support Costs." It amounts to $2.3 million or so, virtually all comprised of salaries, and this is the salaries of MPI personnel who work together with the brokers, to assist them, to teach them, and to support them. And, in our view, that effort relates to the broader mandate of the brokers to serve and support MPI's customers, and so that accounting unit of costs is included in those group of costs that are allocated based on the customer contact ratio.

The second area of question related to service centres, and it reflected on the transition from claim centres to service centres with a question about how the appropriate apportionment of costs between lines of business and category of business would occur.

Our focus on the handling of service centre costs came as a result of our review of what service centres are designed to do, as well as our visit to the Winkler Service Centre, so we could actually see what went on inside of a service centre.

And I think I described in a fair amount of detail earlier that, within the service centre, while there are integrated -- while a customer can have an integrated service experience, the provision of service by individuals is done by individuals whose individual functions are largely dedicated to one (1) category of business or another.

And so within the integrated facility, with the appropriate purification of accounting units, a large part of those costs can be assigned directly to insurance and non-insurance categories of business, with the remaining costs needing to be allocated, and our suggestion is on the basis of the category of business salary ratio.

The third area of question related to the main frame decommissioning, in contemplation of the intended decommissioning of the former DVL system. In thinking about that question, from our perspective, there are two (2) elements to a direct response to it.

The first is with respect to current operations. Today those costs are underta -- the current operational costs are undertaken in a couple of specific accounting units. Those have been tracked through the system and end up in cost categories that are assigned at Level "C" based on work efforts, so that the costs are indeed allocated to each of insurance and non-insurance.

In the future, when that mainframe is decommissioned, that will be part of a discreet BPR Program. That program has not yet commenced, and so the -- the recommendations we make with respect to the handling of BPR costs would be followed at that time with respect to the actual costs of decommissioning themselves.

The fourth question highlighted at 6.4 on page 42 has to do with ensuring that the judgment -- that the judgments that are made in the cost allocation methodology have some external evaluation and have been tested for reasonability and accuracy.

Through our involvement, our approach, as I've described, in establishing the methodology was to achieve several objectives. One (1) was to reduce and isolate the number of places where a judgment is required. So, through the Level 'A' and Level 'B' assignment processes, almost 90 percent of the costs can be assigned without any judgment about where they should be allocated. And then, at Level 'C', where the allocations must be done on the remaining 10 percent of costs, the guiding principles were used to establish allocators, which we believe are fair and reasonable.

The fifth question had to do with BPR costs and seeking information about how they would be captured and handled within the proposed allocation methodology. The approach which we've identified would separate out BPR costs for specific analysis for each of the projects.

The principles would be that, in assessing each B -- each BPR project, the same decision tree should be employed, to consider projects one(1) by one (1) so that, based on the essence of what is being accomplished through the project, it can be determined to be either exclusively insurance, exclusively non-insurance, or a project that must be allocated on some basis. And our proposed methodology would have that analysis, that's initially done, applied consistently to that BPR project over the course of its life.

The sixth question has to do with the allocation of B -- of BPR -- I'm sorry, the allocation of -- the allocation of DVL costs in the post BPR environment, which, in our view, is most significantly impacted by the development of the service centres, and so the guiding principles which we had identified included flexible and adaptable.

And in looking at the purification recommendations which we've made, as well as the way in which service centres should be handled on an ongoing basis, we believe that the methodology accomplishes the appropriate allocation of those costs of service centres over the long-term as those costs continue to grow and dedicated claim centre costs go down.

The other area for the need for application of flexible and adaptable is in the BPR cost area, the question I've just responded to.

And the third observation we would have with respect to the ongoing use of the methodology is that there will be a requirement for MPI to continue to remain vigilant and update its accounting units into costs categories. And make sure that that process of purifying accounting units is done on an ongoing basis so that the methodology continues to allow for maximum assignability.

The seventh question related to activity based costing and what place it might have in the methodology. You will note that activity based costing does not come up in our proposal or our proposed methodology. From our experience, activity based costing is principally used by organizations when they seek to do an internal assessment of the costs of providing a particular business process from end to end.

It potentially could be a way to look at some of the work effort type of allocators. However, activity based costing is generally preoccupied with a single point in time and it would be difficult and costly to maintain on an ongoing basis.

And we've also found limited reference to activity based costing in a regulatory environment, and it's not something that was used by ICBC, and so activity based costing is not part of the proposal that we're making.

And, finally, the eighth question had to do with te -- obtaining jurisdictional comparis -- comparisons between SGI and ICBC, and I've answered questions on those already.

MS. KATHY KALINOWSKY: Thank you very much for that, Mr. Olfert. That concludes my direct examination of Mr. Olfert. Mr. Olfert will now be ready to testify alongside with the MPI panel, which I think is a first for Manitoba Public Insurance.

Usually it's, if anybody is provided, they -- externally to the Corporation, they've testified on their own behalf, but at the request of Board counsel, he will be testifying with the MPI panel on matters of cost allocation.

THE CHAIRPERSON: Thank you, Ms. Kalinowsky, and thank you, Mr. Olfert. We'll take a short break now. We'll be back in fifteen (15) minutes. Thank you.

--- Upon recessing at 10:47 a.m.

--- Upon resuming at 11:08 a.m.

THE CHAIRPERSON: Okay. Welcome back, everyone. Just to let everyone know, we have something else we have to attend to at noon, so we're going to have to break at noon, sort of regardless of where we stand at that point, so there's nothing you've said, Mr. Olfert, that's causing to shut down early, or anything like that.

Ms. Everard...?

MS. KATHY KALINOWSKY: If I could just -- Mr. Chairman, just prior to the break advisors to the Board asked if we could re-file page number 30, the decision tree, with a breakdown of dollar figures and percentages, and it doesn't look very pretty, but we have it here and it's photocopied.

It's, unfortunately, not a colour photocopy, but it does have the dollar figures and percentage figures just drawn -- or written in by hand. If we could file that as MPI Exhibit Number 17.

THE CHAIRPERSON: Very good. Thank you very much.

--- EXHIBIT NO. MPI-17: The decision tree, with a

breakdown of dollar figures
and percentages

MPI PANEL 1 RESUMED:

MARILYN MCLAREN, Resumed
DONALD PALMER, Resumed
OTTMAR KRAMER, Resumed

CONTINUED CROSS-EXAMINATION BY MS. CANDACE EVERARD:

MS. CANDACE EVERARD: Thank you, Mr. Chairman. Mr. Olfert, I just have a few general questions with respect to the work that Deloitte undertook, so we'll -- we'll start with those, and then we'll get into more specifics from there.

In the course of the research that Deloitte performed did it review any previous orders of this Board regarding MPI?

MR. RICHARD OLFERT: Yes.

MS. CANDACE EVERARD: Can -- do you recall which ones?

MR. RICHARD OLFERT: Not by number. They would have been the -- in particular, the December '08 and the December '07 rulings.

MS. CANDACE EVERARD: Which would have been on the GRA's for --

MR. RICHARD OLFERT: Yes.

MS. CANDACE EVERARD: -- those years --

MR. RICHARD OLFERT: Correct.

MS. CANDACE EVERARD: -- or the following years? And did you or any of the Deloitte representatives have occasion to meet with any parties external to the Corporation such as any representatives of Government, Intervenors to this process, staff of the Public Utilities Board, Crown Corporations counsel, anything like that?

MR. RICHARD OLFERT: None of those folks, no.

MS. CANDACE EVERARD: What about the auditor for MPI? The external auditor?

MR. RICHARD OLFERT: We had no discussions with him.

MS. CANDACE EVERARD: Over the course of the work that Deloitte did and the conclusions that it came to, did it find that any costs incurred by the Corporation should be charged to a third party like the Provincial Government, for example?

MR. RICHARD OLFERT: We didn't set out to identify such costs nor did anything that we saw lead us to believe that anything was inappropriately charged to MPI.

MS. CANDACE EVERARD: So even though that question wasn't part of the original mandate, it wasn't something that to your knowledge came up over the course of Deloitte's analysis?

MR. RICHARD OLFERT: No, but as I said, we did not search in any way for such costs.

MS. CANDACE EVERARD: Over the course of the work that Deloitte did and its -- its analysis, did any occasions arise where there were differences of opinion and approach between Deloitte and the Corporation?

MR. RICHARD OLFERT: There were a number of occasions when, in the course of the discussions which I alluded to when I responded to the question about process, where we met to discuss for instance the pro rata approach, Level 'C' allocators and so on.

There would have been good discussion and some challenge of some of the assumptions that we had made. Those challenges were in the nature of providing additional information or asking whether we had considered any particular factor appropriately after having considered all of those items and come to our conclusion.

We are of the view that management concurs with the methodology.

MS. CANDACE EVERARD: So the extent that there was any discussion arising those issues were resolved through additional discussion analysis.

Is that fair to say?

MR. RICHARD OLFERT: Yes.

MS. CANDACE EVERARD: You spoke about perhaps some of the assumptions being questioned by the Corporation.

Can you point us to which assumptions those may have been?

MR. RICHARD OLFERT: There were two (2) areas where we had extended conversations. The first would have been in making sure we had a thorough conversation about the conclusion on the pro rata approach versus the incremental approach.

And the reason for that would have been that intuitively the incremental approach offered a great deal in terms of being consistent with MPI's approach of saying DVL will be added on to what we're doing and will become an incremental part of our integrated service operation.

So that was an extended conversation simply to be sure we had thought through all of the various perspectives that could be brought to that question.

The second occasion would have been for all of what I'll call "the Level 'C' Allocators" which take costs, which must be allocated between the insurance and non-insurance categories of business and assessed which -- and the process was to assess what the appropriate basis of allocation was, there was discussion on each of them. And there was likely the most extended conversation with respect to the, I'll call them the general support costs which are ultimately allocated on the basis of the customer contact ratio.

(BRIEF PAUSE)

MS. CANDACE EVERARD: Can you give us a general overview of how the proposed approach under the report will change the allocation methodology that's been used by the Corporation up until this point?

MR. RICHARD OLFERT: That's a difficult question for me to answer because we did not spend a significant amount of time reviewing the former methodology. The principle time that we spent on the old methodology would have been by members of our team who sought to understand how costs were accumulated.

Our view going in which was also part of the original discussion we had with management about why cost -- new cost allocation study was required, was that circumstances had changed dramatically since it was prepared and so our view going in was that the past methods would be of little relevance because they did not reflect the integrated operations which this one by definition needed to.

(BRIEF PAUSE)

MS. CANDACE EVERARD: Thank you. Now, we know that -- and -- and this may be a question more for the MPI panel than for you, Mr. Olfert, but we know that there was some correspondence exchanged with the Board and the Corporation, that is the Public Utilities Board and the Corporation, back in January of 2009, which was of course before Deloitte was formally retained and -- and work began, and that discussion was in an exchange of letters and it -- it centred around the scope of what the review would be.

And just to refresh memories there's a letter -- and this is referenced in -- in one (1) of the IRs, it's Number 1-39, there was a letter to Ms. McLaren from the Board about the RFP that -- that the Corporation had issued on January the 13th and it was noted that the RFP appeared to be limited to an expense allocation review and asked about whether the review would include a method to allocate assets for the preparation of financial statements for the Basic program. And then Ms. McLaren replied on January 30th, 2009 and agreed that the Corporation must continue to be able to produce separate audited financial statements for Basic and that this would be drawn to the attention of the successful bidder.

Ms. McLaren, can you comment on that exchange relative to the scope of the work that Deloitte actually undertook as 2009 unfolded?

MR. DONALD PALMER: The Cost Allocation Study that -- and other allocations, asset allocation and revenue allocation that you had mentioned, really it's the cost allocation piece that's -- that's really the only -- only part of that that really is relevant in terms of the MPI operations. Mr. Olfert talked at some length about the capital or other utilities being capital intensive, that doesn't apply to -- to MPI.

In terms of our revenues and our assets, are far and away majority direct -- directly allocated. Our liabilities are all direct. Our revenues are all direct. I guess when you talk in terms of allocation of investment income there's maybe one (1) piece of the assets which would be allocated, that would be our employee benefits, our pension liabilities, but again, those are -- are allocated based on salary and there's really very little choice in -- in what you can allocate those based on, so in our opinion, those items of revenue allocation and -- and asset allocation were really not material.

(BRIEF PAUSE)

MS. CANDACE EVERARD: It is the case though that the Basic financial statements are prepared on an allocation or are based on allocation?

MR. DONALD PALMER: Investments and expenses. The -- all the liabilities would be direct, assigned, not allocated.

MS. CANDACE EVERARD: I'll -- I'll just let everyone here know, especially the -- the panel members, obviously a lot of what we had prepared was -- been covered in direct and so there's going to be some pauses in between the questions; that's just because I'm scanning and making sure I'm not missing anything that I -- that I need.

(BRIEF PAUSE)

MS. CANDACE EVERARD: Mr. Olfert, one (1) of the pieces of evidence that you gave in direct was with respect to the non-insurance COB or category of business, and the fact that the report didn't include any analysis of allocation among the -- what would be notionally the lines of business within the non-insurance COB, and your evidence was that Deloitte was not asked to do that or was told that they didn't need to do that.

Was -- did I hear you correctly?

MR. RICHARD OLFERT: We concluded in discussion with the management that there would be four (4) ultimate landing spots for costs in this methodology and there would be no differentiation between costs in the non-insurance category business.

MS. CANDACE EVERARD: For the MPI panel, has the Corporation looked at allocation among the non-insurance category of business?

MR. DONALD PALMER: Not specifically. In terms of our overall lines of business, I think I've alluded here before, that we have five (5) lines of business, the three (3) insurance ones that we've talked about, the amin -- administration of the DVA Act, and discontinued lines. So it's the administration of the DVA and those various component pieces that we have not specifically tried to separately se -- or to separate those costs because for any sort of financial reporting purposes there -- there's no need to at this point.

MS. CANDACE EVERARD: Mr. Palmer, when you speak of the DVA, that's the Driver and Vehicle Act of Manitoba?

MR. DONALD PALMER: That's correct.

(BRIEF PAUSE)

MS. CANDACE EVERARD: Mr. Olfert, you testified that Deloitte reviewed the Corporation's budget for the 2010/'11 fiscal year. How does that budget, if at all, differ from what's been put forward in the GRA?

MR. DONALD PALMER: It was actually the comparison of the 2009/'10 budget that was provided to Deloitte for comparison purposes. When Mr. Olfert talked about the 2010 year that would've been referring to year ending February 28th, 2010.

MS. CANDACE EVERARD: Just so that we're clear, so Deloitte's work was based on '09/'10 numbers, not year of application numbers?

MR. DONALD PALMER: Yes, those are the completed budgets that we had. We have not formally set our budgets for 2010/'11 and beyond.

MS. CANDACE EVERARD: If we turn to page 7 and 8 -- or pages 7 and 8 of the report, this is under

Section 2.2.3 relating to "Broker Commissions," and it's provided that -- this is -- I'm reading from the last sentence on page 7:

"MPI's 2009 budget -- 2009/'10 -- [pardon me] budget for broker commissions broken down by insurance LOBs and non-insurance COB as presented in the following table."

And if we go over the page, it would appear that the majority of broker commission some 58.9 percent is Basic.

Is that right?

MR. RICHARD OLFERT: Correct.

MS. CANDACE EVERARD: And the non-insurance component is less than 1 percent or 0.9 percent?

MR. RICHARD OLFERT: Correct.

(BRIEF PAUSE)

MS. CANDACE EVERARD: And the next Section 2.2.4 of the report, deals with internal operating costs, and it's provided there that salary and benefits comprise some 64.2 percent of those costs, I'm still on page 8.

Is that right?

MR. RICHARD OLFERT: Correct.

MS. CANDACE EVERARD: And the physical properties represent some 8.8 percent of internal operating costs?

MR. RICHARD OLFERT: Correct.

MS. CANDACE EVERARD: And it's, I believe, the case that that would represent the cost of properties throughout the province, including head office for the Corporation.

Is that right?

MR. DONALD PALMER: That's correct.

MS. CANDACE EVERARD: And is the -- or does this analysis or these numbers incorporate the new head office, the Cityplace purchase?

MR. DONALD PALMER: The budgets were set pre the purchase of Cityplace, so -- although the -- the overall costs were not significantly different in -- in terms of the operating -- once you change some of the investment income, the -- the foregone investment income, I think in the quarterly we have said that the purchase of Cityplace saves us about $3 million a year, so those savings would not be incorporated into...

(BRIEF PAUSE)

MS. CANDACE EVERARD: Now it's the case, I believe, that MPI operates about thirty-three (33) different properties in the province.

Is that right?

MR. DONALD PALMER: Sounds very --

MS. CANDACE EVERARD: Subject to check?

MR. DONALD PALMER: Subject to check, it sounds very close, yes.

MS. CANDACE EVERARD: And is it the case that the operating costs for each of those properties are captured in a separate accounting unit in MPI's general ledger?

MR. OTTMAR KRAMER: Yes, that would be correct.

MS. CANDACE EVERARD: Now, it's my understanding that there are nine (9) properties, the primary use of which is driver testing, and those are operating locations of the former DVL and they existed when the merger took place.

Does that sound about right?

MR. OTTMAR KRAMER: Subject to check, yes.

MS. CANDACE EVERARD: Now is it the intention of the Corporation that these facilities will be closed once all of the new service centres are up --

up and running?

MR. DONALD PALMER: Yes.

(BRIEF PAUSE)

MS. CANDACE EVERARD: Just continuing on in Section 2.2.4 of the report on page 8, we've spoken a little bit about physical properties. The third line item under that chart, 2.2.4, is other costs. And it's indicated there that that represents about 27.1 percent of the internal operating costs.

Is that right?

MR. RICHARD OLFERT: Correct.

MS. CANDACE EVERARD: And the items that comprise other costs or what would be included there is listed in a bulleted list at the bottom of page 8.

Is that right?

MR. RICHARD OLFERT: Correct.

MS. CANDACE EVERARD: Now, the next section of the report, 2.2.5, is entitled "Future Intentions for Operating Expenses". Can either you, Mr. Olfert, or one (1) of the panel members, just summarize for a high level what those future intentions are, as set out in that section?

MR. RICHARD OLFERT: We would have

identified several key trends in that area. The first would be the continuing efforts to consolidate human resources and processes to provide integrated services to customers on both DVL and insurance functions.

The second would have been regarding a similar concept with respect to physical properties and the anticipated decommissioning of claim centres and the ongoing process of bringing new service centres online.

And then there would have probably -- there will be a third one (1) picked up under BPR projects in the future which is the decommissioning of significant DVL systems as those first two (2) items are concluded.

(BRIEF PAUSE)

MS. CANDACE EVERARD: Now, Section 2.2.6 as you've mentioned, Mr. Olfert, relates to the business process review or BPR and as we know, MPI is in the process of integrating DVL functions into the Corporation. You've commented generally on 2.2.5 and I thank you for that.

In the second paragraph of that section there's a -- a bit of an update of specifically what integration activities the Corporation has or is in the process of undertaking, the first one (1) being -- and I'll -- I'll just read the first sentence or part of the first sentence of that second paragraph. It says, quote:

"To date integration activities have included MPI integrating all management functions, for example, finance, administration, human resources, et cetera."

Is that an integration process that's now been completed?

MR. DONALD PALMER: Yes.

MS. CANDACE EVERARD: The next item on the list is eliminating duplicate customer record keeping, databases, and systems. Which are the record keeping databases that have been eliminated?

MS. MARILYN MCLAREN: By virtue of the move to the new driver licence system I guess three (3) years ago now and the integrating of the driver licence renewal notification and -- and renewal process into Autopac online aligned with vehicle registration and insurance we have one (1) address for every customer who has a driver licence and a vehicle now. So that duplicate administration of driver records and vehicle owner records who most of the time are the same person has been amalgamated into one (1) database now.

MS. CANDACE EVERARD: The paragraph here on 2.2.5 also references customer record keeping systems. Is that anything distinct from the databases that you've just described or is that just a further descriptive word for the same systems or databases?

MS. MARILYN MCLAREN: It's really the same thing. The renewal system is for both drivers and vehicles.

MS. CANDACE EVERARD: And is this something that's been completed at this point?

MS. MARILYN MCLAREN: With the exception of, I guess, for lack of better terminology what we would call sort of the prime version of the driver record itself, that is still a mainframe system, a mainframe database. We have to add convictions from other jurisdictions onto the driver record in the mainframe so that has not yet happened. Mainframe decommissioning has not happened.

MS. CANDACE EVERARD: The next item referenced in this paragraph is:

> "Aligning driver's licence and insurance and vehicle registration and insurance renewal processes."

And that is something that is coming, is that correct?

MS. MARILYN MCLAREN: It's done, that was what happened in '06.

MS. CANDACE EVERARD: And next there's a reference to combining all direct customer contact into a single call centre. Is it the case that all DVL inquiries are now handled by the same call centre that handles claims?

MS. MARILYN MCLAREN: Mostly. There is still a small group responsible for booking driver road test appointments. In the next several months that will be largely rolled out for the administration of the brokers.

So people will be able to go to any broker location, book their appointment in our online system with the broker, pay for that road test right then and there. So that, rather than amalgamating that with a large call centre it will be a -- a direct service handled that way.

MS. CANDACE EVERARD: And the last item listed in that second paragraph under 2.2.5 is:

> "Eliminating separate driver licensing functions by integrating this work into procedures undertaken by the insurance broker network."

So you've just given us an example of

that. Would that also include things like taking photos for driver's licences and issuance of driver's licences?

MS. MARILYN MCLAREN: Sure, that would be an example because before '06 brokers in the larger centres in the province were not able to do that work, you had to go to DVL directly.

MS. CANDACE EVERARD: Thank you. The next paragraph or the third paragraph under 2.2.5 references integration activities that are still in the process.

And the first one (1) on the list there is:

> "The closure of dedicated DVL facilities in favour of new service centres which will host both insurance and driver licensing operations."

Are there any of the DVL facilities that have been closed at this point? Keeping in mind this is something that you're saying is still in process.

MS. MARILYN MCLAREN: Two (2) DVL offices in Winnipeg have been closed. Earlier, 1075 Portage was closed as a customer service outlet, as well, so that would be a third one.

And -- well I guess there's been four (4) that have been closed so far. The only one still operating in Winnipeg is the one (1) of Nairn.

Brandon is now part of the claim centre. The claim centre on 1st Street and Brandon has become a service centre. Winkler we've talked about a number of times, Steinbach as well.

And, you know, I mean from the -- from a customer -- from a motorist's perspective Winkler and Steinbach have onsite access to service. It just didn't exist in those communities before.

So it's not like we closed a facility. We introduced new onsite services that weren't there before.

MS. CANDACE EVERARD: And 1075 Portage is being used for BPR work, is that right?

MS. MARILYN MCLAREN: In part. There are also DVL departments there still, as well.

MS. CANDACE EVERARD: And once the conversion to the service centres are -- or is complete, how many will there be in the province? Can you give us a -- a rough number?

MS. MARILYN MCLAREN: I think we usually talk in terms of nineteen (19) claim centres. So for the most part, they will all become service centres. Maybe not every last one (1).

MS. CANDACE EVERARD: Thank you. In this same paragraph, the third paragraph under 2.2.5, there's reference to:

"The development of a new drivers record system that will serve both insurance risk rating and driver licensing purposes."

And we're familiar with that.

You spoke a minute ago, Ms. McLaren, about the de-commissioning of the DVL former mainframe. Do you know when that's slated to occur?

MS. MARILYN MCLAREN: No, we don't have a comprehensive business plan or project planned for that yet, no.

MS. CANDACE EVERARD: I'd like to move down on this page to Section 2.3, we're still on page 9 of the report. This is under the heading of, "Transfer of Driver Licensing and Vehicle Regulation to MPI."

Can you just give us a brief summary of what occurred here in 2004 for the record?

MS. MARILYN MCLAREN: Well I guess in general terms, I think it was announced in the spring of '04. Like has happened in every other of the three (3) jurisdictions in Canada with public auto insurance systems, the Government decided to amalgamate some core driver vehicle licensing functions with the public insurer.

MS. CANDACE EVERARD: And what is set out on page 10 of the report, still under Section 2.3, is a list of items pursuant to this change that the Corporation would assume responsibility for and a list of items that the Province would retain responsibility for?

MS. MARILYN MCLAREN: Yeah, exactly. In short form, we administer programs that they determine. The context of the programs, the regulations within which those programs are conducted continue to be the responsibility of the government. We administer them.

(BRIEF PAUSE)

MS. CANDACE EVERARD: And just on the -- the transfer, we've heard evidence in other Proceedings before this Board, and it's -- it's detailed in 2.3, first paragraph that:

> "Pursuant to this change, the Province pays MPI an annual payment of $21 in perpetuity."

MS. MARILYN MCLAREN: Yes, that's right.

MS. CANDACE EVERARD: Mr. Olfert, obviously, when this report was prepared by your office, you, at some point, learned about that arrangement, the $21 million a year that MPI receives from the government?

MR. RICHARD OLFERT: Yes.

MS. CANDACE EVERARD: Did you consider or draw any conclusions about that payment and whether there should be a renegotiation between the Corporation and government on that point?

MR. RICHARD OLFERT: We did not assess the $21 million in any way.

MS. CANDACE EVERARD: So you have no opinion or evidence to share with the Board on that score?

MR. RICHARD OLFERT: No.

(BRIEF PAUSE)

MS. CANDACE EVERARD: Mr. Olfert, do you have a sense of the amount of cost that was borne by the non-insurance category of business up to this point, that is prior to taking into account Deloitte's analysis?

MR. RICHARD OLFERT: As I said earlier, we did not look at the past allocation methodology. I do not know what that number is. If I have a recollection, it may have been referred to in a response to an IR that the Corporation put forward, but I couldn't tell you what the numbers.

MS. CANDACE EVERARD: According to

Exhibit 17, the version of page 30 with the handwritten notes, the allocation to the non-insurance category of business under Deloitte's analysis is about just under $26 million, or 25.9.

Is that right?

MR. RICHARD OLFERT: Based on the '09/'10 numbers, that's correct.

MS. CANDACE EVERARD: For Ms. McLaren or Mr. -- Mr. Palmer, just following up on the question to Mr. Olfert about the amount of the non-insurance category of business costs that he wasn't able to -- to give us a number on, can either of you provide us with that at this point?

MR. DONALD PALMER: I would refer you to Information Request PUB-53, where it was stated the operating expense difference for Basic under the current methodology is $3.9 million less than the outcome of the methodology probo -- proposed by Deloitte.

Those costs wouldn't be completely transferred from DVL. There may be costs that were reallocated from the other lines of business, but most of them would be from the DVL line of business.

MS. CANDACE EVERARD: So, Mr. Palmer, if we look at the -- the 26 million or so that would be allocated under the Deloitte's analysis and add the 3 or

4 million that you mentioned, we'd be around 30 million.

Is that correct?

MR. DONALD PALMER: I don't have that information handy for the '09/'10 year. For the '08/'09 year it is disclosed in our annual report in the management discussion and analysis at page 27 where it says:

> "The loss due to driver and vehicle licensing operations was $8.3 million with the remaining seven point seven (7.7) due to project costs."

So from an operating perspective that would be $21 million plus the eight point three (8.3) so twenty-nine point three (29.3), so your $30 million is -- is quite accurate.

MS. CANDACE EVERARD: Is that figure available for '09/'10 to date?

MR. DONALD PALMER: No.

(BRIEF PAUSE)

MS. CANDACE EVERARD: Mr. Olfert, you spoke about the guiding principles that were developed with respect to Deloitte's study and the third one (1) that you commented on was the principle that the process should be flexible and adaptable. That's under 4.2.3 of the report, which is at the top of page 26?

Can you tell us about the adaptability or the use of this methodology for the point in time that will come to the Corporation when the BPR or the business process review is finished? Does that -- will that in any way affect this methodology?

MR. RICHARD OLFERT: It would not. One (1) of the reasons that we concerned ourselves with normal operating costs for the bulk of the analysis and segregated the BPR costs was that we believed that BPR costs are fundamentally of a different nature, would be for a limited period of time, and would be project-by-project and so they should be isolated for separate treatment.

When the BPR projects are completed, they will have had some impact on normal operations. We believe those impacts can be accommodated within the methodology.

MS. CANDACE EVERARD: So it's not the case that the Corporation will have to go through another exercise when the BPR is finished?

MR. RICHARD OLFERT: I would expect not.

MS. CANDACE EVERARD: And in terms of a framework for the Corporation to use when the BPR is complete you mentioned a moment ago those costs being fit in. Is that something that the Corporation will have, that it can -- it can do or is it your expectation that further analysis and work at your end would be needed?

MR. RICHARD OLFERT: It's less a question of further analysis and more a case of ensuring that the process of taking the basic level at which costs are accumulated and then the process by which they're aggregated for use in the methodology. There will need to be ongoing vigilance to ensure that that is appropriate.

So, because we anticipated that the transition to service centres would be among the most significant of those changes, we recommended purification steps to handle that particular item. But if a BPR project introduces a new type of cost or a new process, then the Corporation will need to assess that process to determine how those costs are accumulated, trying to protect the principles of maximizing assignability and making sure that allocated costs are allocated fairly and reasonably.

(BRIEF PAUSE)

MS. CANDACE EVERARD: Mr. Chairman, I

know it's only ten (10) to 12:00, but I think Mr. Cathcart and I are going to do some pretty significant review over the lunch hour and we'll probably be able to save some time if we just break now, maybe come back a little bit earlier than we otherwise might, and then we can be a little bit more pointed with our questions, and, as I say, probably save some time overall.

THE CHAIRPERSON: Will you be ready to begin at one o'clock or 1:15 or...?

MS. CANDACE EVERARD: One o'clock should be fine, Mr. Chairman.

THE CHAIRPERSON: Ms. Kalinowsky, are you all right with that?

MS. KATHY KALINOWSKY: Yes, we are.

THE CHAIRPERSON: Mr. Williams...? Mr. Oakes...?

MR. BYRON WILLIAMS: Yes, Mr. Chairman.

MR. RAYMOND OAKES: That's fine.

THE CHAIRPERSON: Very good. We'll come back at 1:00.

--- Upon recessing at 11:50 a.m.

--- Upon resuming at 1:00 p.m.

THE CHAIRPERSON: Okay, good afternoon,

everyone.

Ms. Everard...?

MS. CANDACE EVERARD: Thank you, Mr. Chairman.

CONTINUED BY MS. CANDACE EVERARD:

MS. CANDACE EVERARD: Mr. Olfert, we've had a chance to go through our questions and we've -- we're going to have some specific areas to ask you about. I know that you testified in your direct evidence about the purification process that Deloitte used in its analysis.

Can you just give us a little bit more information about that and maybe just review, in general terms, what that is for the Board's benefit? They'd just like to hear a little bit more detail on that.

MR. RICHARD OLFERT: Perhaps the easiest way to do that is to point you to pages 31 and 32 of our report. As I mentioned, the most basic level of cost accumulation within MPI is the accounting unit, of which there are a hundred and twenty-nine (129).

And we wanted to go through a process of aggregating like accounting units into cost categories, so we had a smaller number of discreet blocks of costs to concern ourselves with when working through the methodology. So, through that process, we were able to go from a hundred and twenty-nine accounting units to thirty (30) odd cost categories.

In order to be able as -- to assemble like accounting units into cost categories, we needed to have certainty that those accounting units were, indeed, sufficiently similar that they could be aggregated.

So in the case of some of the cost centres, so, for instance, a long list of claim centres, it's fairly straightforward that those would be uniformed costs and they could be aggregated together into a single cost category.

In other cases, it was not possible prior to the purification process to group accounting units together into like cost categories, or it was not possible to have an accounting unit as part of a cost category assigned to either a line of business or a category business because it contained costs which supported both insurance and non-insurance operations.

And so the intention of the purification process was after having spent considerable time analysing those accounting units that had blended activities was to -- was to determine whether there were -- whether there was an easy way to extract certain costs out of accounting unit so that the remaining costs would be exclusively assignable to a specific line of business or a category business.

So, a simple example was, if an accounting unit would have fifty (50) people's salary in it and it was quite clear that forty-five (45) of those people supported insurance and five (5) were potentially insurance and non-insurance, if we could take those five (5) out and put them in another cost cat -- another accounting unit, that would leave the original accounting unit with forty-five (45) people pure and assignable within the methodology.

MS. CANDACE EVERARD: Thank you. Now, we've heard evidence and we -- the record reflects that the Winkler Service Centre was looked at by Deloitte, and it being the first cen -- centre that was up on running.

Is it as simple for the Corporation, as you just described, with respect to the new service centres going forward?

MR. RICHARD OLFERT: It may be advisable to obtain some comments from Mr. Kramer in addition to mine. The purification process that we identified was based on the fact that, today, all of the service centre costs are included in a single accounting unit. So Winkler Service Centre's one accounting unit.

We believe it's quite doable to identify which people within that service centre are providing dedicated insurance or non-insurance services and, so, you might split that accounting unit into three (3) for insurance, Winkler services, non-insurance Winkler services, and shared Winkler services.

In our discussions with the Corporation as the methodology was prepared that was seen to be workable and so there may be additional accounting units introduced as a result of that purification process but if there was one (1) before, there are now three (3) that allow two (2) of them to be directly assigned and a smaller dollar value to be allocated.

MS. CANDACE EVERARD: Thank you. Mr. Kramer, do you want to add anything to that?

MR. OTTMAR KRAMER: I -- I don't think I have a whole lot to add. What Mr. Olfert's described to me is -- is something that, you know, we understand and is entirely doable. We've got numerous accounting units in capacity in our system that we can add as many as are needed and we can do it through accounting units and we've also got something called sub-accounts that perhaps we could use that methodology but the -- the approach would be the same.

MS. CANDACE EVERARD: And is it the Corporation's intention to review any aspect of the cost allocation and methodology annually?

MR. OTTMAR KRAMER: Currently, the -- the process that we use currently for allocating costs is reviewed annually and, again, this would be updated annually, approved by our audit committee.

MS. CANDACE EVERARD: So would any analysis of purification be done as part of the annual review or in the case of the service centres, would it be done as they open?

MR. OTTMAR KRAMER: Both. As -- as changes are being introduced in the business, we'd have to identify them during that time when they're being introduced and then annually our policy and our approach would have to be updated.

(BRIEF PAUSE)

MS. CANDACE EVERARD: Is it fair to say with respect to the service centres that the Corporation at this point would have a form of template created that it can use for each service centre going forward?

MR. OTTMAR KRAMER: Currently, our -- our methodology is not the same as -- as is being introduced by the -- the Deloitte report but we do have a template for what we're doing currently and under the Deloitte report, yes, there absolutely would be a template and that would be followed consistently.

MS. CANDACE EVERARD: Thank you. Okay, I just want to get into some questions about the Level 'C' allocations.

Now, it's our understanding that there are two (2) types of costs that would be allocated at Level 'C' and tell me if I'm wrong. One (1) would be those costs under the insurance category of business which must be allocated among the insurance lines of business at Level 'D', and then there are the others which were indicated under the allocation category in the report which must be allocated between the insurance COB and the non-insurance COB; is that correct?

MR. RICHARD OLFERT: I would say it a little bit differently. The Level 'C' allocation is designed to deal exclusively with those costs that must be split between the insurance and non-insurance categories of business. So, if I can refer back to the exhibit that was distributed earlier with the numbers on it, the Level 'C' allocation would be of the $100.8 million which using the '09/'10 numbers is split eighty-seven point nine (87.9) to insurance and twelve point eight (12.8) to non-insurance.

The allocation of costs between the three

(3) insurance lines of business actually occurs at Level 'D' and that is done for both those costs that were directly assigned at Level 'A' -- sorry, at Level 'B', the seventy-one point six (71.6) and those assigned at -- allocated at Level 'C' eighty-seven point nine (87.9).

MS. CANDACE EVERARD: Thank you for clarifying that, it's appreciated.

I'll ask you to have a look at page 34 of the report for a moment. This sets out the allocation between categories of business at Level 'C' and you did comment on the chart there at 5.4.1 in your direct evidence.

The cost categories of driver records and vehicle registration that are reflected here show a basis of allocation of estimated work effort. And you spoke about that a little bit and I believe your evidence was that Deloitte actually tried to stay away from that allocator because it does have a -- an element of subjectivity.

Can you comment on that in -- in terms of the -- the ultimate recommendation that that allocator be used for these cost categories?

MR. RICHARD OLFERT: The broader context is exactly as you describe, that our objective was to try and minimize the number of places where work effort was required. Having said that, there are some cost categories where an effort to fairly and reasonably allocate the costs between the two categories of business can really only be done by assessing the work which goes on there.

And so while our overall objective would have been to minimize work effort instances, we have, I believe four (4) of them in the course of the thirty (30) odd cost centres. So I would say we've achieved the objective of minimizing it but it would be, in our view, unwise to not use them at all.

MS. CANDACE EVERARD: So there are just some instances in which it's still the best, even though it's not preferred?

MR. RICHARD OLFERT: That's correct.

MS. CANDACE EVERARD: Now, you testified that the allocation in the driver records costs category would be 50/50? How did Deloitte come to that conclusion?

MR. RICHARD OLFERT: When one employs the work effort allocator, there needs to be a study of the nature of the work that goes on to assess which line of business it supports. And so, in some situations you might be able to look at number of pieces of paper handled or the number of claims that are processed or some measure of activity which enables you to use that measure as a way of proportionally allocating.

In the case of the driver records, this one is difficult to do on that basis because there's a single database of costs which are being managed. It gathers information from a variety of sources and when people are doing the work, it is really independent of what purpose it will ultimately be used for.

Having said that, once the database is maintained, it is used to support the DVL operations and it's used to support the insurance operations and so the simple conclusion was, one (1) consistent uniform set of activities that feed two (2) purposes where you can't attach individual efforts to outcomes would simply be split 50/50 to acknowledge that there are two (2) places where the information is used.

(BRIEF PAUSE)

MS. CANDACE EVERARD: With respect to the allocation of 50/50 that you just described for the driver records, it would be fair to say then that there was no time study conducted?

MR. RICHARD OLFERT: That is correct.

And our -- our view in terms of the advisability of time study was when someone is updating a database for a piece of information that's used for two purposes, it would be impossible to assess for what purpose that activity was undertaken, and so the question of what activities would be measured for what time period was so difficult to answer that that was an unworkable solution.

MS. CANDACE EVERARD: Now I see on the next page of the report, page 35, where the chart of Level 'C' allocations is continued, that there is a line item which is 'U', referring to legal, the cost category of legal, which also has -- is one (1) of the ones that has an estimated work effort as the basis for allocation, that's correct?

MR. RICHARD OLFERT: Indeed it is.

MS. CANDACE EVERARD: And do you know what the percentage allocation is with respect to that cost category? Is it also 50/50 like driver records or is it something else?

MR. RICHARD OLFERT: Let me answer that question in two (2) ways: The first is that for the actual application of the methodology MPI will still need to do some work to assess what the basis of that estimated work effort might be.

In the extreme, some organizations would use time sheets, for instance; in other organizations as may be the case here, there's an opportunity to look at the staff compliment and say, well, these five (5) people are dedicated to managing insurance claims and these do such and such and there may be some method other than time sheets by which a reasonable allocation can be made.

So that -- the determination of precisely how that work effort ratio will be established and the work to do the analysis to come up with a percentage has not yet been done.

Having said that, based on the discussions which our team had with individuals within the legal department, we've made an assumption as to how that might turn out for purposes of doing the calculations. But that assumption should in no way be seen as a definitive indication of how the ultimate analysis will turn out.

MS. CANDACE EVERARD: And do you know when that analysis is going to be done?

MR. RICHARD OLFERT: I do not. I presume it would follow the adoption of this methodology by the Corporation.

MS. CANDACE EVERARD: Just so that we're clear, is that an analysis that Deloitte would be involved in or would it be done by the Corporation on its own?

MR. RICHARD OLFERT: The way the methodology's been designed, it would be something that the Corporation could do. It could seek assistance if it chose but it would be something the Corporation could do independently.

MR. DONALD PALMER: Just if I may add some clarification to that. In AI.19 on page 2 we have identified three (3) areas that the Corporation is going to have to undergo some significant work and study to implement this particular cost allocation. And that work's -- work effort is certainly one of those items that has been identified.

MS. CANDACE EVERARD: Thank you, Mr. Palmer. While we're still looking at page 35 and the chart that's set out there, can it be confirmed for the record where it is that costs associated with general management of the Corporation are covered?

Is -- is that under management committee which is on the very last row of the chart or is it somewhere else?

MR. OTTMAR KRAMER: Yes, the management committee cost centre would be primarily the -- the executive team.

MS. CANDACE EVERARD: And as reflected here, the proposed basis of allocation for those -- or for that cost category, together with all these other ones listed, is the call centre ratio.

MR. RICHARD OLFERT: That is correct.

MS. CANDACE EVERARD: Okay, I'm going to ask you to have a look at one of the IRs posed by the Board in the First Round, it's Number 40 and in particular 40(c). This question comes back to shared cost of the service centre.

I'll just read the question in and then we'll come to the answer. The question was:

> "Please provide the pros and cons of allocating service centre shared costs based on COB salary ratio versus other allocators considered based on the five (5) guiding principles outlined in Section 4.2.
>
> Please elaborate on the alternative bases of allocation."

And if we turn to the response Deloitte has provided a narrative and, Mr. Olfert, whether you wish to read it in or just discuss the answer, I'll -- I'll leave to you.

But if you could speak to that it would be appreciated.

(BRIEF PAUSE)

MR. RICHARD OLFERT: Perhaps for ease and completeness I'll simply read it in.

"MPI has currently established one (1) service centre which is located in Winkler and this location was formerly a claims centre which handled only the insurance category of business. However, with the introduction of the full service centre concept, both categories of business services are provided.

Analysis of the operating costs incurred in the Winkler service centre indicate that approximately 75 percent are salary and benefit costs, 18 percent are physical property operating costs and 7 per cent are miscellaneous supporting costs such as travel, postage, stationery supplies, et cetera.

In the service centre the majority of the staff can be identified as devoted to the provision of either insurance or non-insurance services and assigned directly to that category of business. There is a small compliment of staff which supports service provision in both categories of business.

We identified two (2) potential approaches in the development of an appropriate allocator. The first approach was to identify and utilize a measure of business transactions such as number of claims managed and driver tests taken.

This approach was abandoned as the business transactions of the two (2) categories of business are very different and thus not comparable for purposes of creating a meaningful allocator.

The second approach was to identify and utilize measures related to the people providing services as all costs related to the provision of services by people; those -- those costs being, salary, physical space, and miscellaneous supporting costs.

Three (3) indicators were considered: First, direct category of business, salaries, and benefit dollars; second, direct category of business FTE positions; and third, direct category of business square feet of space. Our assessment of these potential allocators resulted in the following: First, all three potential allocators met the criteria of practical and efficient, flexible and adaptable, and acceptable in a regulatory context. With respect to consistency with industry standards all three (3) could be considered consistent, depending on what type of cost is being allocated. Third, with respect to fair and reasonable, the suitable of square feet was questionable given that people's compensation represents the majority of the costs and, finally, category of business salaries and category of business FTEs could both be considered reasonable as they related to people, however, category of business salaries was considered more fair as it better reflected the different level of complexity of the two (2) categories of business."

MS. CANDACE EVERARD: Thank you. Just with respect to that last bullet and the comment that the category of business salaries was considered fairer as it -- as it better reflected the different level of complexity of the two (2) categories of business, why is that the case or why would Deloitte say that was the case?

MR. RICHARD OLFERT: Our view was that the -- if -- if -- our -- our view was that if "people" was to be used as an allocator, it made sense to understand what those people did. It made sense to understand how qualified those people needed to be. It made sense to understand the skill level that was required in the work that they did.

It was our belief by comparing the relative salary dollars, it would allow us to, by inference, be comparing the relative salaries of individual positions. So, if a position required more skill, was more complicated, more complex, that would be reflected in a higher salary.

And so, we would have expected

differentials in salaries between those dedicated to insurance and those dedicated to non-insurance and by using the salary dollar ratio that difference in complexity would be reflected which it would not be had it been done simply using head count.

MS. CANDACE EVERARD: And is it your view that there would be any difference in terms of transparency between the number of positions and the salary dollars?

MR. RICHARD OLFERT: If by "transparency" you mean would there be any difference in the ease with which those could be calculated or the ease with which someone could follow how they could be calculated, we would anticipate they would be the same.

(BRIEF PAUSE)

MS. CANDACE EVERARD: Thank you. Just getting into a couple of questions with respect to the call centre ratio and -- and we have on page 35 the two (2) cost categories: customer service and support and then the -- the group of other cost categories for which that basis of allocation is proposed.

And I don't know if this will be for you, Mr. Olfert, or for the MPI panel, but, does the

Corporation or Deloitte, as the case may be, have an indication of how often people phone in with questions relating to DVL versus relating to the insurance side and also how often or, sorry, how often that occurs and then what kind of questions do they ask that are related to DVL? Can you speak to that?

MS. MARILYN MCLAREN: By far, most of the calls we get are related to insurance. The single greatest number of calls is probably related to windshield claims, but things related to driver licence surcharges which is an insurance question and so on are -- are the majority.

I -- I don't want to guess off the top of my head but, certainly, less than -- far less than a quarter of the calls would be related to DVL.

And again, you know, part of the purification -- not -- not purification, part of the analysis that still needs to be done is a more careful look at the category of calls that, up until today, we've called DVL.

People reporting an address change, clearly, has an insurance component as well as a driver licencing component, so that would be shared, you know, in -- in this new world, things like that.

I've just been identified a reference here of PUB/MPI-1-48A, which talks about the weighted call centre ratio. This is a combination of calls and -- and minutes spent responding to the calls, and 13 percent are DVL related in this response to the P -- PUB/MPI-1-48A.

The kinds of calls that the 13 -- probably -- I would tell you, probably, right now, some of the 13 percent is made up of things that would both have an insurance and -- and a licencing component.

But more the pure kinds of DVL calls, it would somebody calling in response to a letter they got about having to get a medical for their -- before they have to renew their driver licence, questions about the Private Vehicle Inspection Program, questions about transfer of ownership documents. Things like that would be pure DVL kinds of calls.

MS. CANDACE EVERARD: Thank you, and we appreciate the reference to 1-48, which does have that information for a variety of months throughout 2007 and 2008, and it looks like the percentage varies from 6 to 13 or 5 to 13 but, definitely, in the under 25 percent range that you suggested.

(BRIEF PAUSE)

MS. CANDACE EVERARD: Ms. McLaren, is it

the case that those kinds of inquiries may also be made of brokers, and if that is true, would -- that would not be captured by the call centre ratio; is that correct?

MS. MARILYN MCLAREN: I think, in general terms, it's far, far more likely that brokers would be asked to respond to insurance-related questions. They can't respond to questions about driver improvement and control. They can't respond to questions about a request from a medical report before someone can renew their driver licence. The Vehicle Inspection Program brokers would never an -- if they got a question, they wouldn't answer it.

So, I think, for the most part, it's -- it's highly likely that a preponderance of DVL focussed questions come directly to the Corporation, unlike insurance ones.

MR. RICHARD OLFERT: And to the second part of your question, contact with brokers is not factored into the call centre -- the customer contact ratio.

MS. CANDACE EVERARD: Thank you. Mr. Olfert, just coming back to page 35 in the -- the two (2) groups of cost categories, if you will, that -- that are proposed to be allocated on the basis of the -- the call centre ratio, can you tell us a little bit about the rationale?

I appreciate there is a rationale listed here for each row item, but just to give the Board an idea of what other allocators were considered for these cost categories and why the call centre ratio was preferred in the analysis.

MR. RICHARD OLFERT: Let me start with the first of the two (2) categories that you described, which is cost Category 'W', customer service and support. This is a group of accounting units that effectively relate to responding directly to customer inquiries, providing support to the broker network, and so on.

And so it seemed quite logical to us to seek an allocator which was tied as closely as possible to the interaction with customers. And so, as we searched for such an allocator, given that the principle sources of contact with the customers are either through the brokers or through the call centre, and looking at the allocation of broker costs based on the -- which is based on the negotiated per transaction amount, that seemed to us to be a function of negotiation rather than a function of interaction with clients -- or customers rather.

It seemed to us then that the call centre ratio was the most effective way to deal with those customer support costs.

With respect to the large block of costs which we might call corporate support costs -- allow me just a moment to consult one (1) of the IRs.

MS. CANDACE EVERARD: Might be 48.

MR. RICHARD OLFERT: Thank you.

MS. CANDACE EVERARD: 'F'.

(BRIEF PAUSE)

MR. RICHARD OLFERT: So with respect to that group of costs, the first key determination in that was that they would all be treated alike as opposed to trying to treat them separately and our view was that they shared one (1) key common significant trait which was that they fundamentally represented services to the entire Corporation, hence, they were treated all as one (1).

A number of alternatives were evaluated in terms of how they might be allocated. We, for instance, looked at a number of ratios between -- a number of possible ratios between, for instance, going back to Level 'A' or Level 'B' and saying what's the ratio of directly assigned costs; could we use the category of business ratio that for instance -- or an equivalent to the category of business ratio that came out of service centres but something tied to people.

One (1) of the significant flaws we believed with that approach is that while it is, indeed, true that the services are provided principally through people, a substantial portion of the service to customers is also accomplished through the information systems and the investment in information systems we believed intuitively is much higher for insurance operations because there's underwriting functions, there's claims functions, there's a whole host of complicated functions as part of insurance which differed from the information system requirements of DVL which is principally database-type of applications.

And so we sought an -- we -- we believe an indicator based on people, numbers, or accounts, or some average using earlier information in the decision tree would be inadequate in that regard. So then we said, How do we best identify a measure that takes into account the inherent complexity of the insurance business but not use those people-based accounts -- those people-based measures?

We searched internally for quite a while to say looking from inside the Corporation what might the perspective be and we had a difficult time identifying something that would be other -- something that would be straightforward and something which would be other than some amalgam of the previous ratios.

And then we began to say to ourselves, well, fundamentally, MPI is a customer service organization providing services to customers and perhaps the customer view on the Corporation's activities is a valid and appropriate measure for the organization's activities which, in turn, require those support activities.

And on that basis we said that customer contact ratio, which reflects what customers are obtaining from MPI would be an appropriate basis on which to allocate those combined corporate services costs included in that -- in that group of cost categories.

(BRIEF PAUSE)

MS. CANDACE EVERARD: Okay. So, Mr. Olfert, just commenting on the salaries, when we spoke a moment ago about the service centres, we talked about the consideration of the FTE numbers but, ultimately, it was the recommendation that salaries be used and if I understood your -- your evidence correctly just now with respect to these cost categories, it was the -- the thought that the ratio of call centre usage was preferred over salaries.

Can you explain that, how salaries or why salaries were viewed differently in those two (2) contexts?

MR. RICHARD OLFERT: In the case of the service centres, the vast majority of the costs which were to be allocated were themselves salary dollars and they were for activities that occurred within one (1) location for the purpose of serving customers on either insurance or non-insurance matters.

On that basis, we believed it made sense to say, What other salary activity's happening around those salary dollars and apply that to that -- on that basis.

In the case of the Corporate support costs, our view was that those costs included costs beyond salaries and so it wasn't automatic to go look at salaries.

And it was also our view that looking at salaries was -- was reflective of the input by people but it did not consider -- did not in any way consider the fact that a significant amount of the services provided at a Corporate support level are driven by investments and information technology which take complex functions that might otherwise have to be done by people and they're done by the -- obviously by the systems.

And so there was a need, in our view -- or the shortcoming in our view of the salary was that with the insurance operations being supported by information technology applications that supported the most complex functions of the organization. And in -- that ratio did not appropriately factor in enough weighting to the insurance side of the business for those Corporate support costs.

MS. CANDACE EVERARD: Thank you. Now, if I heard your earlier evidence correctly and I think this was on direct examination, you testified that the cost or the amount that were being allocated under these two (2) rows, that is, item 'W' the customer service and support and then the -- the grouping of a number of other cost categories immediately below was about 52 million?

Did I -- did I note that correctly?

MR. RICHARD OLFERT: The 52 million is a reference to the Corporate support services. The category 'W' customer service and support was an additional $9.4 million. Again all using '09/'10 numbers.

MS. CANDACE EVERARD: So the total for Level 'C' that's being allocated on the basis of the call centre ratio was about sixty-one (61) million? Does that sound about right?

MR. RICHARD OLFERT: Sixty point three (60.3), yes.

(BRIEF PAUSE)

MS. CANDACE EVERARD: Mr. Olfert, you commented a moment ago about the reason why Deloitte has recommended the grouping of these cost categories, the last row on the table on page 35.

And you said that I believe that the main reason was that they were Corporate wide or words to that effect. At the answer to the Information Request posed by the Board at Number 48, there were a couple of other details or three (3) bullet points that Deloitte referenced with respect to that grouping.

Can you just give us a little bit more detail on that? I'm looking at page -- well, I guess it's the second last page of -- or third last page of the answer to Number 48 after all the tables?

MR. RICHARD OLFERT: So just to be clear, you're looking at the paragraphs beneath the table that ends with 51.9 million, $30 million and so on?

MS. CANDACE EVERARD: I'm looking at the

answer to 48 --

MR. RICHARD OLFERT: Yes.

MS. CANDACE EVERARD: -- and it's the first I guess -- part of the narrative of the response where it says "B & F we will respond --"

MR. RICHARD OLFERT: Yes.

MS. CANDACE EVERARD: Yeah. And you'll see in the middle there, there are three (3) bullet points --

MR. RICHARD OLFERT: Oh, I'm sorry.

MS. CANDACE EVERARD: -- and this was --

MR. RICHARD OLFERT: Okay.

MS. CANDACE EVERARD: -- my understanding with this was this was the explanation as to why the various cost categories were lumped together in the way that they were and I -- I -- as I say, I appreciate your earlier evidence that basically they're all Corporate wide.

But this is just a little bit more detail on that.

MR. RICHARD OLFERT: The aggregation of all of those accounting units into a single cost category stems from these three (3) common attributes. The first one is that none of those costs are incurred directly -- or are required directly by the provision of any line of business.

The second one is, if you look at the activities that go on in any one of those, for instance, internal audit, it's hard to say that any particular thing that internal audit does is directly a cost or is caused by any particular line of business.

And, finally, those costs together are all supports to the overall management effort by which services are provided to customers. So, those three (3) attributes are further elaboration on my earlier comments about why those were grouped together.

(BRIEF PAUSE)

MS. CANDACE EVERARD: Thank you. Getting into some questions then about the Level 'D' allocation and the discussion of that, for the purposes of the record, starts at page 37 of the report.

Now Level 'D', and we've heard this a couple of times but just for clarity, this is the allocation of the assigned and allocated insurance COB costs, is that correct?

MR. RICHARD OLFERT: That is correct.

MS. CANDACE EVERARD: And Section 5.4.2 here on page 37 sets out the various cost categories that it's suggested be allocated at Level 'D', that's right?

MR. RICHARD OLFERT: That is also correct.

MS. CANDACE EVERARD: The first row item is cost Category 'A', which is injury claims management, and it's suggested that the basis of allocation is claims under management ratio.

And there is an explanation here as to the rationale for that allocator. Can you comment on that for the purposes of the record?

MR. RICHARD OLFERT: The intent was to have the injury claims management costs allogated -- allocated to a line of business in proportion to the activity which sustained those -- that claims management function.

And so our view was that the most appropriate way of doing so was to determine the number of claims of each type, that is, each line of business. And having seen -- or having established the ratio of those claims, one to the other, then that same ratio would be used to allocate the injury claims management cost.

MS. CANDACE EVERARD: Thank you. The next row item there at cast -- or cost Category 'E' is driver records, and it's reflected that the basis of the allocation be simply to the -- the basic line of business, and the rationale is that the efforts of personnel are to establish and maintain the driving record used for basic driver and vehicle insurance rating purposes.

Are the driving records that are referenced here used for any purpose other than basic driver and vehicle insurance rating purposes, and this may be a question for the panel?

MS. MARILYN MCLAREN: No. I think we've discussed this here and we've put on the record before that, basically, our rate determination for the extension line of business is the same as any other insurer selling Extension, is what con -- what -- what basic insurance discount do you qualify for. SRE, a totally separate matter.

MS. CANDACE EVERARD: Thank you. The next row in the table relates to vehicle registration cost category and, similarly, that one is reflected as being assigned solely the basic, and the rationale reflects that the efforts of personnel include the sale of basic insurance products to certain classes of commercial vehicles.

Is Extension coverage available to commercial vehicles?

MS. MARILYN MCLAREN: No. I'm trying to think whether there may be some very, very limited exceptions, but for the vast majority, no.

MS. CANDACE EVERARD: Would you mind having a looksee and let us know if there are any exceptions that you're -- that are -- just aren't coming to your mind at the moment?

MS. MARILYN MCLAREN: Sure.

MS. CANDACE EVERARD: Thank you.

--- UNDERTAKING NO. 11: To advise if Extension coverage is available to commercial vehicles

CONTINUED BY MS. CANDACE EVERARD:

MS. CANDACE EVERARD: Now, the next line item relates to:

> "Investments and the basis of allocation is listed as the percentage of claims reserves and unearned premiums by insurance line of business."

Can you comment on whether it's you, Mr. Olfert, or Mr. Palmer or any of the other members of the MPI panel comment on the -- the rationale for that allocator as reflected here and perhaps in a bit more detail?

MR. RICHARD OLFERT: The intent with the allocation of investments was to recognize the fact that the pool of investments is supported by the need to hold those investments for particular purposes. The two (2) primary purposes would be claims reserves and secondly, premiums paid in advance.

And so, it seemed logical to us, that if one determined the dollars of claims reserves by line of business and the dollars of unearned premiums by line of business, summed those amounts for each of Basic, Extension, and SRE, that that ratio would represent a reasonable basis of saying these are the reasons for which that block of investments is held.

(BRIEF PAUSE)

MS. CANDACE EVERARD: Thank you. Now, like we say at Level 'C' the last grouping on the chart is a -- a multitude of cost categories.

Can you comment maybe, firstly on, why these particular cost categories were grouped together?

MR. RICHARD OLFERT: In reviewing each of these accounting units to form a single cost category unlike the previous cost -- cost categories that we talked about, there was an inability to look at the dollars spent in any one (1) of these areas and say that dollar relates to Basic or that dollar relates to Extension.

And so, because there was an inability to say there is some basis for figuring out how each cost relates to the different lines of insurance business, the view was they should be aggregated together for purposes of a consistent allocation across the lines of business of insurance.

MS. CANDACE EVERARD: Thank you. Now, the basis of allocation for that group of cost categories as indicated here is net claims incurred percentage and there's a rationale reflected. Do you want to maybe comment on the rationale and then we'll get into some further detail on that?

MR. RICHARD OLFERT: All of those individual types of costs are incurred for the purposes of managing the claims activity and so, it was our view, that the relative proportion of the claims was a reasonable basis on which to allocate the costs which supported the management of those claims.

MS. CANDACE EVERARD: Thank you. On the top of page 38 there's some narrative on that rationale that -- that we've just been discussing and it's reflected in the second line of that paragraph that Deloitte considered a number of options including claims volumes, insurance premiums, and claims incurred.

Is that correct?

MR. RICHARD OLFERT: Yes, it is.

MS. CANDACE EVERARD: And it's reflected on the fifth line of that paragraph in the first full sentence that premiums as a basis for allocation were rejected as Basic insurance reflects no profit component, yet Extension and SRE premiums are competitive lines which reflect a profit component.

Is that right?

MR. RICHARD OLFERT: Yes, it is.

MS. CANDACE EVERARD: If you can for a moment, just keeping that statement in mind, turn your mind to the guiding principles set out in the report that have been discussed today, can you comment on how the allocation of these costs, on a net claims incurred basis, compares to the premiums-earned basis?

MR. RICHARD OLFERT: Could you please --

MS. CANDACE EVERARD: Sure.

MR. RICHARD OLFERT: -- restate your question?

MS. CANDACE EVERARD: Sure. What I'm

getting at is if we -- if we focus on the -- the sentence here indicating why the -- the premium approach was rejected because Basic doesn't have a profit component, whereas the Competitive lines do, the Basic insurance program as we're all aware is regulated by this body. And probably everyone in the room would agree that the reason why the Basic program is regulated the way it is is because it is a monopoly and compulsory program.

So would it be fair to say that the main reason why the premium approach was rejected by Deloitte was because of the profit margin that is built into the Extension and SRE lines?

MR. RICHARD OLFERT: I think in the final analysis that was a point on which the conclusion turned, however, prior to thinking about that point and going back to the guiding principles which you referred to in your earlier question when -- with the objective of coming up with fair and reasonable, our view would be, that it would be best if the measure that's used for each of the lines of business to which the costs are to be allocated, if those bases were determined in a similar fashion based on similar principles.

And so when we considered the premiums alternative it seemed to us that on the Basic insurance, which operates on a cost-recovery basis with rates set by this Board, that the premiums were influenced by different factors than they would be for either Extension or SRE where the Corporation is free to do as it sees fit with respect to profit element.

And so the inclusion of a Corporation determined profit element in the measure for two (2) of the lines of business, but not in the first line of business where it's determined by the Board, our view was, that it was more fair and more reasonable to go to a basis on which they were similar and uniform, which was the basis -- which is the basis that was chosen, being that of claims incurred.

MS. CANDACE EVERARD: Now, we asked the Corporation to rerun some of the dollar numbers on the premiums-written basis. This is at sub (d) to question 50, which we posed in the First Round. I'll just give you a moment to get there.

(BRIEF PAUSE)

MS. CANDACE EVERARD: This chart sets out a comparison between the analysis that the question asked be conducted versus the original allocation dollars set out in the Deloitte report, which are at Appendix 'D' to that report on page 59.

Can you summarize for the Board the -- the differences in dollar amounts set out across the -- or across the bottom of the table?

MR. RICHARD OLFERT: Certainly. The detail which is provided for each of the cost categories is how the Level 'D' allocation would have turned out had the premiums-earned basis been used, and had that basis been used the costs assigned to the Basic line of business would have been reduced by $8.7 million from the method that was recommended in our report. And the costs of -- allocated to Extension and SRE would have been $6.8 and $1.8 million higher, respectively.

(BRIEF PAUSE)

MS. CANDACE EVERARD: Thank you for reviewing those dollar amounts, Mr. Olfert.

Just speaking about the -- the thinking behind these two (2) approaches that this chart reflects, can you comment on each of the five (5) guiding principles and why with respect to each of them it's Deloitte's view that the claims incurred approach is better than the -- the premium approach?

(BRIEF PAUSE)

MR. RICHARD OLFERT: With respect to the first guiding principle of fair and reasonable, I believe my earlier comments addressed that item. With respect to practical and efficient, I'm not sure that I would differentiate between the two (2). Both are relatively straightforward to obtain the figures to do that allocation on either basis. In terms of flexible and adaptable, I would consider them to be equal given that this guiding principle was more about parts of the operation that would evolve significantly over time.

Acceptable and regulatory context, from our research particularly as it relates to ICBC, both allocators are used and I should say that in the ICBC situation where premiums written are used, its principally on those allocators which differentiate -- sorry -- it's principally on those allocators where there's an effort to split costs associated with particular elements of the underwriting -- particularly elements of the insurance process like underwriting where there's an effort to split it between third party and insurance as part of Basic and collision as part of Competitive.

So given that that's not the Competitive /Basic split that we're looking at here, we thought it was less relevant in this scenario than to ICBC.

So both -- both have been acceptable in a regulatory context and the same comments would apply with respect to consistent with industry standards where I would view the ICBC cost allocation methodology as the principle source of reference.

MS. CANDACE EVERARD: Mr. Olfert, when you gave your direct evidence this morning, you commented on the review that Deloitte did of other jurisdictions, SGI and ICBC and the research that was conducted.

With respect to SGI just specifically for the moment, is it -- or are you aware that the Saskatchewan Rate Review Board, which of course deals with SGI, only provides recommendations as opposed to actually setting rates?

MR. RICHARD OLFERT: We were not aware of that, no.

MS. CANDACE EVERARD: Similarly with respect to that Review Panel in Saskatchewan, was Deloitte aware that it does not actually hear evidence from sworn witnesses nor does it contemplate cost awards to Intervenors?

MR. RICHARD OLFERT: We had not studied the process to know those things by virtue of fact. Having said that, our inability to find anything on the public record with respect to cost allocation led us to believe it was a substantially different process.

MS. CANDACE EVERARD: Thank you. Now with respect to Saskatchewan and BC the jurisdictions reviewed, did Deloitte look at the underlying legislation in those provinces as compared with what we have in Manitoba?

(BRIEF PAUSE)

MR. RICHARD OLFERT: The background information we gathered was principally publicly available information like annual reports, and so on, and anything we could find on cost allocation.

We did not review the constituting legislation of either case.

MS. CANDACE EVERARD: Okay. Mr. Olfert, you gave evidence with respect to what Deloitte was able to glean from British Columbia and there's some commentary on that in a Response Number 42 that the Board posed in the First Round.

And I'll just read in the question at 42(a) which was:

"In the Deloitte Expense Allocation Methodology Study, the full cost pro rata allocation method is chosen as being the best suited for the Corporation. This method, although seemingly simple in its initial implementation holds the risk of becoming increasingly cumbersome in its use over time as experienced by ICBC. What steps can be taken to mitigate this from happening at the Corporation?"

And if we look at Deloitte's answer there's a -- a narrative in response and there are six (6) bullet points in the middle of that narrative.

Can you comment on Deloitte's response to that particular question and -- and tell us about the -- the six (6) bullet points which reflect the attributes to mitigate the risk?

MR. RICHARD OLFERT: Our assessment of the risk associated with that approach considered the interaction that ICBC had in its regulatory proceedings and our observation was that those interactions were based principally -- sorry, the -- the -- not only were those interactions but the continuing points of question or the continuing points of investigation related almost exclusively to work effort allocators. And they related almost exclusively to work effort allocators that endeavoured to apportion costs between liability and injury versus collision on the other hand.

So in assessing the risk that the ICBC experience was a signal that there could be undue complexity for MPI, we thought about the six (6) items that are listed in response to that question. If we work our way through them individually, we believe first that the focus on maximizing assignment of costs and minimizing the requirement for allocation puts some distance between that risk and this methodology. And I will remind you that on our -- on the exhibit that was distributed earlier, 90 percent of the costs of the Corporation are done by way of assignment leaving only 10 percent subject to allocation.

That objective was achieved in part because of the activity described by the second bullet point which is the purification process which allowed the assignment of costs to be maximized. An element which is not part of the report because it by definition will follow the adoption of the methodology is that there must be ongoing vigilance and monitoring on the part of the Corporation to ensure that as streams of costs or natures of costs evolve that they are treated correctly in their -- in their original point of entry into the accounting system, that becomes an important feature to remain that -- to -- to continue having accounting units remain pure.

We did, as I described earlier, adopt a reluctance to use work effort measured allocators and, hence, the fact that there are only four (4) amongst the thirty (30) odd categories. Where work effort was selected, our effort was to ensure that the pieces of information that were used to establish work effort were object -- were objective where possible.

And lastly, where work effort was contemplated we thought, is there a better one (1), and we weighed that in terms of cost benefit to determine whether a better measure could be derived without undue additional cost and those considerations are reflected in the conclusions that we reached which minimized the number of work effort allocators.

(BRIEF PAUSE)

MS. CANDACE EVERARD: Mr. Olfert, do any the four (4) cost categories for which, work effort are being used for the Corporation, include aspects of subjectivity?

(BRIEF PAUSE)

MR. RICHARD OLFERT: In short the answer would be, yes. Each time work effort is applied there's a judgment in terms of the most appropriate way to do that.

For those that we've ident -- for those that we've suggested that a work effort analysis results in a 50/50 allocation, that's fairly objective to apply, but that conclusion reflects a judgment.

MS. CANDACE EVERARD: And as we discussed before, while the -- the work effort approach isn't preferred for the four (4) cost categories that we've discussed it was still the -- the best way to go in the analysis of Deloitte?

MR. RICHARD OLFERT: Our conclusion was that, in each case that would be the best. Perhaps another way of looking at those four (4) allocators is the total dollars allocated, again using nine (9), ten (10), figures is the range of $7 million out of almost a billion dollars of expenditures.

MS. CANDACE EVERARD: Thank you. Mr. Olfert, thank you taking us through 42 Sub 'A', and the list of the -- the six (6) bullet points being the -- the attributes that Deloitte tried to incorporate to avoid the ICBC experience.

I note, in the last sentence of the

narrative at (a), there's a comment that the revisions that had to be done to ICBC's methodology came as a result of requests from Intervenors in their regulatory process, presumably to develop more detailed data to support the bases of determining allocators.

Obviously in the process that the Corporation is involved in through this Board there are Intervenors that participate.

Does Deloitte have any comment, with respect to that similarity in terms of issues arising in the future for the Corporation and it's methodology?

MR. RICHARD OLFERT: Let me answer your question in this way. This sentence could perhaps have been more complete by indicating that the interests of the Intervenors when they asked those questions was in seeking a different way of allocating costs between collision, as Competitive, and Basic -- which includes injury and third party liability, we would not anticipate any questions of that nature in these Proceedings.

MS. CANDACE EVERARD: And Part 'B' of this question, Number 42, posed by the Board in the first round, asked for an outline or explanation of the negotiation between ICBC and the British Columbia Utilities Commission. And the response from Deloitte is -- is quite lengthy but does provide information, with respect to that.

I'd ask you to go to the chart that appears on Page 2 of the answer, which sets out the issues that were present in the negotiations and the resolution of those issues.

Can you just comment on those at a high level for our Board, please?

MR. RICHARD OLFERT: Can you be a bit more specific in terms of comment in what respect?

MS. CANDACE EVERARD: Why don't you tell us what each issue was and -- and then, in brief terms, how it was resolved.

If you just want to read in those two (2) columns, that would be fine, the issue column, and the resolution column. If you'd rather read them in than comment on them, that's fine.

(BRIEF PAUSE)

MS. CANDACE EVERARD: Mr. Olfert, I can maybe save you a little bit of work. If you want to take a look see through the issue list, and if there are any that you can foresee arising in the Manitoba context, comment on those.

If you don't have any understanding at

this point, or inclination at this point that they may arise in Manitoba, then you just need to tell us that.

MR. RICHARD OLFERT: Perhaps the most important distinguishing feature of these items is that the fundamental allocation that's being challenged in each of them is the allocation between Basic and Competitive and I go back to my point again, that Competitive includes collision in BC. And so that is a point -- or that allocation to Competitive collision in BC in part turns on these.

And so the relevance of these to that proceeding because it relates to that question is significantly higher than I would anticipate here because that's not a differentiation that would need to be made.

I would also make the observation that following review of virtually all of these, there was either a fine tuning made to a work effort allocator which goes back to the discussion and points we've made earlier or the -- additional information was accepted and the allocator was continued to be used, as was originally proposed.

MS. CANDACE EVERARD: Thank you. Mr. Olfert, I just want to have you turn quickly to page 39 of the report. This is where we find Section 5.5 which deals with the business process review projects.

I think, I heard your evidence earlier today and tell me if I'm wrong, that, in essence, the allocation process that's reflected here for the BPR project is the same as the decision tree that we looked at on page 30. That was a note that I thought I -- or that I had made as to what I thought you had said, is that correct?

Or are there any differences between the page 30 decision tree and the allocation of BPR cost analysis?

MR. RICHARD OLFERT: Your statement is correct and I'll add one (1) sort of proviso at the end. The logic by which the decision tree works is intended to be exactly the same logic by which decisions are made on the allocation of BPR costs.

The difference would be, obviously, that the decision tree would need to be worked through annually with the costs that are incurred each year.

In the case of BPR we would expect a significant effort at the commencement of a BPR project to determine how it should be allocated. And then that determination would be used consistently over the life of the BPR project. And so I would envision more of a one (1) time effort with checks for consistency across BPR, whereas there would be an ongoing annual process on normal operating costs.

MS. CANDACE EVERARD: Has any of that work been done with respect to the BPR projects to date in terms of the cost allocation?

MR. RICHARD OLFERT: I would invite additional comment from MPI. We are aware that for the current methodology process there's been consideration given to how BPR projects should be allocated.

I would anticipate that that thought process would be incorporated into the application of this. Whether or not this has been commenced on yet, in terms of the new methodology, I would defer to MPI.

MR. DONALD PALMER: The BPR costs were allocated before this particular report was -- was issued. But it was the same sort of decision tree where -- where do those costs belong, for what purpose is that project being undertaken?

So it was on that same basis that we would have allocated those costs.

MS. MARILYN MCLAREN: But I can give you an example of a potential difference. We haven't done the work. As I think we've said in these Proceedings a number of times, the mainframe decommission's been identified as a BPR/DVL project. Clearly, you know, a heightened awareness through this process that the driver record held on the mainframe has significant value to the insurance program.

Whether that means we would contemplate changing what we said about allocating the mainframe decommission cost, probably not, but it would certainly inform the allocation of the cost going forward when the project is done. Maybe the project too, I'm not sure, but -- but that's an example of having to go back and revisit previous decisions in the context of a new methodology.

(BRIEF PAUSE)

MS. CANDACE EVERARD: Does the Corporation anticipate -- does the Corporation anticipate that there will be any changes in the methodology prior to next year's GRA that will be apparent in the filing?

MR. DONALD PALMER: Changes from that proposed in the report, you mean?

MS. CANDACE EVERARD: A difference between what's in the current application as to how BPR costs are to be treated.

MS. MARILYN MCLAREN: Probably not. That's what I intended to say. I think that's what I said a few minutes ago. Probably not to the extent of going back and making different decision about the projects themselves, but certainly this report, once adopted, will inform the allocation of ongoing expenses into the future.

MS. CANDACE EVERARD: Thank you. Mr. Olfert, when you gave your direct evidence this morning you did make some comments with respect to Manitoba Hydro as an example, for comparative purposes.

Have you had occasion in your work to undertake a cost allocation review of Manitoba Hydro?

MR. RICHARD OLFERT: I have not.

MS. CANDACE EVERARD: And you commented in one (1) of the sections of the report dealing with questions that the Board had posed, and that is specifically the section on activity based costing.

I believe your evidence was that there wasn't a lot of examples out there of utilities using that type of costing. Were you aware that Manitoba Hydro does use activity based costing?

MR. RICHARD OLFERT: We were not aware of that, no.

MS. CANDACE EVERARD: Thank you.

(BRIEF PAUSE)

MS. CANDACE EVERARD: If I could turn you to MPI Exhibit 17, which is the decision tree with the handwritten notes that was entered into evidence this morning.

We see across the bottom the -- the three (3) dollar amounts of 801.5 million, 103.4 million, and 45.7 million, of course, pertaining to Basic, Extension, and SRE respectively.

What are the relative net written premiums for those three (3) lines corresponding to these budgeted cost allocations?

(BRIEF PAUSE)

MR. RICHARD OLFERT: I don't have that information at this point in time.

MS. CANDACE EVERARD: Mr. Palmer, do you want to take an undertaking, or do you think you can put your fingers on it?

MR. DONALD PALMER: The only one (1) that I could definitely put my finger on is the Basic number. We don't have the other numbers ha -- handy.

MS. CANDACE EVERARD: Can you give -- give us the Basic number now then, if you don't mind?

(BRIEF PAUSE)

MR. DONALD PALMER: The total earned revenues would be 742.9 million, and that's made up of motor vehicle premium, driver's premium, less reinsurance ceded premium, and adding service fees and other revenues, and I got that number from TI.15.

MS. CANDACE EVERARD: Thank you. That's appreciated. I'm just going to move then to AI.19 just for some summarizing and wrap up with respect to cost allocation. So I'll ask the -- the panel to go there.

(BRIEF PAUSE)

MS. CANDACE EVERARD: Are you with me, Mr. Palmer? The third paragraph of AI.19 provides that the methodology outlined in Section 5 of the report has been accepted in principle by the Corporation's Board of Directors, to be implemented on March 1st, 2011.

Is that right?

MR. DONALD PALMER: That is correct.

MS. CANDACE EVERARD: Is there any aspect of the report that the Corporation does not intend to adopt at this point?

MR. DONALD PALMER: No, we -- we are

looking to adopt a -- the program as it has been proposed. Certainly there's a lot of flushing out of details. These are sort of broad concepts, not accounting policies per se. So there will be certainly a -- going into some of the details of some of the specific allocations that we'll have to -- to flesh out.

Of course there's additional work, as I mentioned, with regard to the -- the purfi -- purification of costs. The estimated work effort, as Mr. Olfert has described, will take some extra analysis as well. And again into the -- the call centre ratio, we'll review that to ensure that we're collecting the right data, that we have the -- the right categories that are coded in.

So there is certainly work that will have to be undertaken to properly implement the spirit of this study, if I can use the -- those terms.

MS. CANDACE EVERARD: And just for the purposes of the record, those three (3) items of study or analysis that you've identified are listed on page 2 of AI.19?

MR. DONALD PALMER: That's correct.

MS. CANDACE EVERARD: And it's also reflected on -- at the bottom of page 2 of AI.19, that the Corporation recognizes that this Board will review the study of the current GRA and may have comments leading to possible changes, insofar as it is accepted for rate setting for the next GRA, the 2011/'12 GRA?

MR. DONALD PALMER: That is correct. We would expect to have our 2011 GRA with the new cost allocation methodology.

MS. CANDACE EVERARD: Thank you. Mr. Palmer, with respect to these three (3) items that are listed as the -- the to-do list, so to speak, for the Corporation, can you give us any idea of the timing with which these items will be completed? Or is it too early for you to say?

MR. DONALD PALMER: I'll just say that they'll be completed by the time we get the 2011 GRA. We are, in terms of -- of some of the, like the -- the sub-accounting units, it's a feature in our accounting system, financial system, that we currently don't utilize, so that's -- there's certainly some setup required from that standpoint. But certainly we -- we think all these three (3) are doable by the next GRA.

MS. CANDACE EVERARD: Thank you. And I'm just going to take you back in AI.19 for a moment. There is a -- a bulleted list that spans from page 1 and spills over onto page 2. This is a -- a list of points setting out the differences or the primary differences between the new methodology and the current methodology that the Corporation uses.

Can you just highlight those, I believe there are four (4) on the list, those four (4) differences for the Board?

MR. OTTMAR KRAMER: I'll take that. The first bullet, being purification of cost within accounting units, and as indicated, we do some purification currently, but the new proposed methodology does -- does additional purification beyond what we currently do.

The second bullet discusses the recognition of the insurance work that's performed by what was previously called DVL, the -- the current methodology -- under the current methodology that work was charged to DVL, and under this proposed methodology it is allocated to the categories or business that it's applicable to.

The third category is the overall allocation of non-direct costs. Currently, when -- when DVL was taken on, the allocation of what was DVL versus what was non-DVL was done on a departmental -- department-by-department basis. That was increasingly difficult as the Corporation was -- was more or less becoming one so.

(BRIEF PAUSE)

MR. OTTMAR KRAMER: And then, so what that meant is it -- we were really losing the distinction between what was a DVL function, and what was non-DVL. And so was -- it done, more or less, on an incremental basis, which was dismissed under the Deloitte review.

The fourth bullet is allocation of non-direct insurance costs. Under the current methodology some operating expenses are allocated based on direct premiums written. The current methodology, as Mr. Olfert has discussed, allocates some of those non-direct insurance costs under -- using the claims incurred basis, which, again, we support.

MS. CANDACE EVERARD: So, if we understand at least the second and third of these points correctly, there -- the net result will be that some of the costs that were previously born by DVL are going to shift to Basic?

MR. OTTMAR KRAMER: Yes, some of that would be what -- what we are saying here. But I think what it does is -- is -- there's shifting of costs throughout. There's some costs that Basic was bearing that now non-Basic will be bearing, and visa-versa. So, I -- think things have went both ways.

MS. CANDACE EVERARD: Sure, on an overall basis I understand that. I just meant with respect to these two (2) bullets it -- these are comments on costs going in the other direction, things that DVL, in the Corporation's eyes, has been paying for that it shouldn't have been.

MR. OTTMAR KRAMER: Yes.

MS. CANDACE EVERARD: Mr. Chairman, I took a little longer than I thought I was going to. I think I'm done, but maybe with the Board's indulgence we can take the break now. I can just confirm that I'm done, and then Mr. Williams can have at 'er when we get back.

THE CHAIRPERSON: Very good. I'll just ask, Mr. Williams, do you have questions for Mr. Olfert and the panel?

MR. BYRON WILLIAMS: I have some, but not an overwhelming amount.

THE CHAIRPERSON: I don't see Mr. Oakes. Mr. Dawson...?

MR. ROBERT DAWSON: No questions, Mr. Chairman.

THE CHAIRPERSON: Mr. Charran, I presume you're just maintaining your watching brief? Okay. Thank you.

Okay, we'll take the break now.

--- Upon recessing at 2:27 p.m.
--- Upon resuming at 2:51 p.m.

THE CHAIRPERSON: So, Ms. Everard, do you have any more questions for Mr. Olfert?

MS. CANDACE EVERARD: No, I do not, Mr. Chairman. I just want to clarify one (1) thing with the panel though.

CONTINUED BY MS. CANDACE EVERARD:

MS CANDACE EVERARD: Mr. Palmer, you and I had a discussion. I had asked a question about the -- the net premiums written for the three (3) lines of business, and I had said if you wanted to answer it by way of undertaking that would be okay. You gave me the number for Basic, at your fingertips, but I didn't actually confirm an undertaking for the balance of the question.

So, I just wanted to confirm that we do have that undertaking from you.

MR. DONALD PALMER: Yes, I'll take that undertaking.

--- UNDERTAKING NO. 12: What are the relative net written premiums for Basic, Extension and SRE corresponding to the budgeted cost allocations.

MS. CANDACE EVERARD: Thank you. Now the record's clear. So, I have no further questions, Mr. Chairman. I believe Mr. Williams does have some questions for Mr. Olfert.

THE CHAIRPERSON: Thank you. Mr. Williams...?

CROSS-EXAMINATION BY MR. BYRON WILLIAMS:

MR. BYRON WILLIAMS: Good -- excuse me. Good afternoon, Mr. Chairman, Members of the Board. And good afternoon, Mr. Olfert, and in -- yeah, in your massive back row of, I believe, Mr. Martens.

I hope you're not too insulted. I don't have a lot of questions for you this afternoon. Are you okay with that, Mr. Olfert? He's nodding his head, so.

Mr. Olfert, just in terms of the -- my understanding is that you conducted some literature review in -- in preparing for this report, is that correct, Sir?

MR. RICHARD OLFERT: Our team did, yes.

MR. BYRON WILLIAMS: And I just wonder, in -- in your literature review of regulatory principles relating to cost allocation, did your team come across the concept of -- or the guiding principle of stability or predictability?

Was that something that you came across in your research?

(BRIEF PAUSE)

MR. RICHARD OLFERT: No, we did not.

MR. BYRON WILLIAMS: And, as you may be aware, Mr. Olfert, I work with other regulated utilities where cost allocation hearings tend to take three (3) weeks, not four (4) hours, so I'm really glad that this is a short one.

But in -- in that context, I'm going to suggest to you that the concept of stability may -- may refer to the idea that you don't want your allocators to be ones that may be subject to material variation, in that if they're ones that are more inclined to change, they may lead to instability, in terms of rates, on a year-to-year basis.

Is that -- is that helping at all, in

terms of that concept?

MR. RICHARD OLFERT: The explanation of the concept is helpful. As I reflect on it in light of the work that we've done, I go back to the initial -- one of the initial objectives which we established, which was to maximize assignability and to minimize the occasions when allocators would be required.

And so the risk that you identify exists by definition. But in the case of the methodology that's been designed here, that would -- that -- that risk by definition, separate and apart from whether it would actually turn out that way, would apply to roughly 10 percent of the costs because 90 percent are assigned based on causal activity.

MR. BYRON WILLIAMS: And accepting that as an -- as an answer, and I appreciate that answer, you wouldn't disagree with the fact that when we look at allocating costs, rather than assigning costs, that one factor that you may want to keep in mind, in terms of a principled approach, would be that concept of stability?

Would you agree with that, sir?

MR. RICHARD OLFERT: I think it's a -- a useful concept to have in mind. I also think that in some cases, if the allocator is appropriately chose and it reflects the underlying activity on a proper causal basis, fluctuations in an allocator from year to year may indeed be the best representation of how a cost is allocated.

MR. BYRON WILLIAMS: Fair enough. I just wand to ask you a couple of questions about the scope of your retainer.

Am I correct -- and again, Ms. Everard, has -- has dealt with some of this, so I may be tip toeing over her area. You'll accept my apology for that.

In terms of your -- your retainer, my understanding is you were engaged to perform a cost allocation review and to develop a cost allocation methodology.

Has that got it in broad strokes, sir?

MR. RICHARD OLFERT: Yes.

MR. BYRON WILLIAMS: You were not asked to provide advice on the allocation of revenues between various lines of business.

Would that be fair, sir?

MR. RICHARD OLFERT: We were not asked to do that.

MR. BYRON WILLIAMS: And indeed you did not provide any advice, in terms of the allocation of revenues between various lines of business.

Is that right, sir?

MR. RICHARD OLFERT: We did not.

MR. BYRON WILLIAMS: And it would be fair to say that you, certainly in -- in the course of this retainer, have not explored possible methodologies relating to the allocation of revenue, in the context where you've got a -- a monopoly line of business and a -- and a competitive line of business.

Is that fair, sir?

MR. RICHARD OLFERT: We have not studied the issue of allocation of revenues.

(BRIEF PAUSE)

MR. BYRON WILLIAMS: I'm going to turn to the area of BPR costs, and some of these questions may be directed to Mr. Olfert and -- and some to your panel members.

As I understand your methodology -- and again you'd testified to this this morning, but I just want to confirm it -- the -- in your work the BPR costs were not considered as part of normal operations, and as a consequence the cost allocation methodology addresses these costs independently from normal operating costs.

Would that be fair?

MR. RICHARD OLFERT: That is correct.

MR. BYRON WILLIAMS: And I'll come back to you in a second, Mr. Olfert. To the MPI panel, and I'm not sure which one, but the Interrogatory that I'd like to refer you to, is PUB-2-25.

(BRIEF PAUSE)

MR. BYRON WILLIAMS: Do you have that, Mr. Palmer?

MR. DONALD PALMER: We have it.

MR. BYRON WILLIAMS: And I just want to direct your attention to the -- the second page of that response, which presents a table headed at the top, "PUB Corporate Total Percent Basic Average" and then "Basic Share."

Do you see that table, Mr. Palmer?

MR. DONALD PALMER: I see it.

MR. BYRON WILLIAMS: And as I understand it, this table details certain BPR costs, including PIPP Phase 2 and 3, Driver Safety Ratings, Streamlined Renewal, Enterprise Data Warehouse, and Program Management.

Is that right, sir?

MR. DONALD PALMER: That's correct.

MR. BYRON WILLIAMS: And what the -- the

column -- the first column -- or the second column being PUB-1-58D, Corporate Total, does is sum the -- or layout the estimated total cost of these BPR initiatives.

Is that correct, Mr. Palmer?

MR. DONALD PALMER: Yes.

MR. BYRON WILLIAMS: And the next column over sets out the -- how much of these costs have been assigned to Basic on a percentage basis, sir, correct?

MR. DONALD PALMER: Yeah, that's correct.

MR. BYRON WILLIAMS: And then the third column sets out the -- the numerical result of the first -- the two (2) previous columns, in terms of Basic share after a certain amount of costs has been allocated.

Is that right?

MR. DONALD PALMER: That's correct. And -- and I would say for PIPP Driver Safety Rating, it's not allocation but assignment.

MR. BYRON WILLIAMS: Fair enough. And I -- I appreciate that correction. And what you mean by that, Mr. Palmer, is that 100 percent of the costs related to PIPP Phase 2 and 3 have been assigned to Basic, as well as 100 percent of the Driver Safety Rating cost.

Is that correct?

MR. DONALD PALMER: Yes, that's correct.

MR. BYRON WILLIAMS: And I'm assuming, although it's not on this table, that Phase 1 of PIPP, 100 percent of those costs would also be -- have been assigned to Basic?

MR. DONALD PALMER: That's correct too.

MR. BYRON WILLIAMS: And then the -- the bottom there, you'll agree that -- with me though that there has been an assignment of cost to Basic from BPR initiatives, such as Streamlined Renewal, Enterprise Data Warehouse, and Program Management.

Is that right?

MR. DONALD PALMER: Yes.

MR. BYRON WILLIAMS: And just where I was trying to -- to get at Mr. Olfert, in -- in terms of your work, have you reviewed the specific assignment of a certain percentage of costs related to these BPR projects, sir?

MR. DONALD PALMER: We did not.

(BRIEF PAUSE)

MR. BYRON WILLIAMS: So you have not considered the -- the validity of these assignments from -- from a principle basis.

Would that be fair?

MR. DONALD PALMER: We have not, which is -- we have not.

MR. BYRON WILLIAMS: And, Mr. -- Mr. Palmer, just to -- to MPI, it's probably on the record somewhere, my understanding of allocation is when -- when you're allocating costs there has to be an allocation methodology or an allocator that goes with it.

Would that be fair, sir? Your understanding, as well?

MR. DONALD PALMER: Yes, that's correct.

MR. BYRON WILLIAMS: And can you point me to where on the record -- record the -- the allocators for Streamlined Renewal, Enterprise Data Warehouse, and Program Management are.

I just need a reference, sir.

(BRIEF PAUSE)

MR. BYRON WILLIAMS: I probably have the one for Enterprise Data Warehouse.

MR. DONALD PALMER: That reference is PUB/MPI-152D.

MR. BYRON WILLIAMS: And does that cover all three (3), Mr. Palmer?

MR. DONALD PALMER: Program Management is one of those allocated costs, so it's not a project within itself; it's allocated to the other projects. So that would not be in that chart.

MR. BYRON WILLIAMS: Thank you for that.

MR. DONALD PALMER: It -- it's allocated on the basis of deferred development costs of each of those other projects.

MR. BYRON WILLIAMS: Mr. Olfert, you spoke earlier today in your direct evidence of -- in -- I'm putting quotations around this word, "challenges," you experienced in the allocation of corporate wide costs.

Do -- do you remember that, sir?

MR. RICHARD OLFERT: I do.

MR. BYRON WILLIAMS: And you also spoke of, I believe, again I'm putting quotations, at least in my note taking, around these words, "significant challenges," in terms of allocations related to the call centre.

Is that your recollection as well, Sir?

MR. RICHARD OLFERT: I believe I was making reference to the fact that those cost categories that are ultimately allocated using that call -- the customer contact ratio did -- there was significant challenge in coming to that conclusion, yes.

MR. BYRON WILLIAMS: And because you speak accounting, and I just speak lawyering, when -- when you use the word "challenges," what do you mean by that Mr. Olfert?

MR. RICHARD OLFERT: It meant that the most appropriate way to allocate those costs was not easily apparent, because there was not a direct causal relationship between the costs in any particular line of business.

There were a number of alternatives that were identified and each had advantages and disadvantages to them. And so, there was a considerable amount of judgment that needed to be applied in coming to a conclusion.

MR. BYRON WILLIAMS: And I thank you for that answer. And -- and in applying you -- you've identified the need for applying judgment. And you'll agree with me that when it comes to applying judgment, reasonable people may disagree in terms of applying -- in -- in the decision they ultimately make.

Would that be fair?

MR. RICHARD OLFERT: It is possible.

MR. BYRON WILLIAMS: And -- and just on a going forward basis, to the extent that judgment is -- is required, I take it you'd agree that it -- and I think you've testified to this, that it's important to regularly review the -- the cost allocation methodology of the Corporation?

MR. RICHARD OLFERT: I think there are a number of level of reviews that must occur. We've endeavoured to recommend a methodology which will stand the test of time and not need to be revised itself.

Having said that, the application of that methodology requires numerous ongoing determinations about new costs that are introduced, how accounting units are aggregated into cost centres and so on.

And so, when there are changes in the operation of the organization, there will need to be ongoing effort to ensure that the methodology continues to be appropriately applied.

MR. BYRON WILLIAMS: And I'll divide your -- and thank you for that thoughtful answer. I'll just divide your answer into to two (2) parts.

In terms of the second part of your answer, seeing that the -- the proposed methodology is appropriately applied, in your view that would -- would tend to be an ongoing activity.

It's -- although with BPR you might suggest that maybe a lot of effort at the start, and then -- and then after that just monitor it.

Would that be fair?

MR. RICHARD OLFERT: I'm not sure I understand your reference to BPR, but with respect to the need for an ongoing monitoring, I would indeed expect that there would need to be, at a minimum, an annual process to ensure continued appropriate application of the methodology, and that exercise should be done annually.

MR. BYRON WILLIAMS: And I'll come back to BPR in a second. In terms of the -- in terms of the methodology itself, assuming it's accepted by -- by MPI and approved by -- by the regulator for rate setting purposes.

If you were giving advice to the -- to the regulator, in terms of reviewing it, would you see any need to review it at a certain point in the future, not the application of the methodology, but the actual methodology itself?

MR. RICHARD OLFERT: It would seem to me that if the nature of the business changed dramatically, if new lines of business were added or there were some other significant development in the operations of the corporation, the corporation would have the same interest as the Board in ensuring that the methodology's appropriate.

(BRIEF PAUSE)

MR. BYRON WILLIAMS: If you could turn, for just a couple minutes, Mr. Olfert, to AI.19, I believe Appendix D, page 58, please, sir.

(BRIEF PAUSE)

MR. BYRON WILLIAMS: Now, Mr. Olfert, and you've testified about this a few times so I won't go over it, but this is the Level 'C' allocation in -- in which you assign a certain cost to -- based upon allocators to insur -- the insurance category business and others to the non-insurance category business, would that be fair, sir?

MR. RICHARD OLFERT: That is correct.

MR. BYRON WILLIAMS: And at this level we start to get into that challenging environment you spoke of before in that -- in that it requires judgment and -- and the choice between various potential allocators, correct, sir?

MR. RICHARD OLFERT: This is indeed where the most judgment was required.

MR. BYRON WILLIAMS: And as I understand the outcome of this judgment, about 12 percent --

actually closer to 13 percent of these costs were assigned to the non-insurance category of business with the remaining, let's say, about 87 percent being insi -- assigned to the insurance category business.

Would that be correct, sir?

MR. RICHARD OLFERT: Yes.

MR. BYRON WILLIAMS: And then just to turn to the next -- the next page, that 87.973 million, which has gone through one (1) level of allocation consideration on -- on this page, goes through a subsequent level on -- on the next page.

Is that right, sir?

MR. RICHARD OLFERT: Yes, the allocation identified on page 58 identifies those eighty-eight (88) odd million dollars of costs as being related to the insurance category business, but from there they must still be allocated between Basic, Extension and SRE.

MR. BYRON WILLIAMS: So for that particular 88 million there's two (2) steps of judgment or consideration required: One (1) at the Level 'C' level and then one (1) at the Level 'D' level, is that right, sir?

MR. RICHARD OLFERT: I would say there's two (2) sets of allocation required.

MR. BYRON WILLIAMS: And then, of course, it's added to some additional monies and that's where we get to the allocation at Level 'D' between the Basic, Extension and SRE, is that right?

MR. RICHARD OLFERT: Yes, it is.

MR. BYRON WILLIAMS: If you turn again for just a moment to, again, AI.19, page 29, sir?

I'll direct your attention to par -- under -- under the overu -- Overview Section 5.1, the second and third sentences, and you state there, Mr. Olfert, do you not, that:

"Even though MPI has in recent years become a provider of other services, MPI is at its core a provider of insurance products to Manitobans. Other services provided are complimentary in that they leverage existing MPI customer records and customer points of contact."

Did I state that -- read that correctly, sir?

MR. RICHARD OLFERT: Yes.

MR. BYRON WILLIAMS: I wonder if you would agree with me one (1) step further, that the Extension insurance line of business is complimentary to -- to the Basic line in that it -- it levers existing MPI customer records and customer points of contact that flow from that monopoly.

Would you agree with that, sir?

MR. RICHARD OLFERT: Could I ask you to repeat that, please?

MR. BYRON WILLIAMS: I'm not sure I can repeat it but let's -- let's try.

Let's take that -- I wonder if you'd agree with me one (1) step further? If I suggested to you that the extens -- Extension insurance line of business levers -- is -- is complimentary in that lt levers the existing Basic customer records and customer points of contact, that -- that it benefits from leverage that -- that flows from the Basic program itself, sir?

MR. RICHARD OLFERT: Both product offerings would draw on the same customer information in the same processes, that's correct.

MR. BYRON WILLIAMS: And to that extent there may be material benefits to the Extension program, you'd agree with me, whether in terms of keeping costs lower or -- or in -- in enhancing revenue potential, sir?

MR. RICHARD OLFERT: I'm not sure I follow your question.

MR. BYRON WILLIAMS: But for the Basic monopoly, the Extension line of business would look very different from -- from -- or may -- might look very different from what it does, fair enough?

MR. RICHARD OLFERT: I think that's fair.

MR. BYRON WILLIAMS: And in fact it's -- it's potential to obtain revenues is materially enhanced from its relationship with the Basic program and the Basic monopoly, sir.

MR. RICHARD OLFERT: As the activities are undertaken frequently at the same time, I would agree with that.

MR. BYRON WILLIAMS: As well, from the cost perspective, Extension has the opportunity to benefit materially from the Basic monopoly as compared to what it would otherwise do as a standalone operation, correct?

MR. RICHARD OLFERT: I think you're -- the point you make is fair, although I'm not sure that, considering that circumstance, it is other than sort of thinking about a speculative business because I'm not sure that's a business that one would be in on its own.

MR. BYRON WILLIAMS: I'll accept that answer. You had a -- an interesting discussion with Ms. Everard relating to, I believe it's page 37 of your -- your evidence, Mr. Olfert, if you could turn there please. Page 37 of the report.

And directing your attention to Section 5.42 you'll recall, Mr. Olfert, that you had some discussion regarding the relative merits of allocating that cluster of cost categories at the bottom of the page using net claims incurred as compared to written -- written premiums or premiums earned.

Do you recall that discussion, sir?

MR. RICHARD OLFERT: Yes.

MR. BYRON WILLIAMS: And I don't want to follow it through in too great a detail. But would it be fair to say that the -- from your perspective the net premiums earned or written would not be an unreasonable allocator with regard to this area, sir?

MR. RICHARD OLFERT: I would say that it's one (1) that we considered and we concluded that there was a better allocator.

MR. BYRON WILLIAMS: But it was -- you didn't consider it was unreasonable?

MR. RICHARD OLFERT: We certainly considered it less reasonable that the one that was selected.

MR. BYRON WILLIAMS: And that's a matter of course of judgment and reasonable people can disagree, sir?

MR. RICHARD OLFERT: That's conceivable.

MR. BYRON WILLIAMS: In -- in looking at the two (2) allocators, did you consid -- look at it all and -- and by the two (2) potential allocators I mean premiums earned or written versus claims incurred.

Did you look at the -- the -- their relative volatility in terms of results on a year to year basis, sir?

MR. RICHARD OLFERT: We did not.

MR. BYRON WILLIAMS: And so you wouldn't be in a position to comment on whether or not claims incurred would tend to be more volatile than premiums written or earned.

Would that be fair?

MR. RICHARD OLFERT: Not without further analysis, no.

MR. BYRON WILLIAMS: Without trying to get into -- and Ms. Kalinowsky may want to pay attention to this question. But without trying to get into too many details of the business model for Extension or SRE, you -- you talked about the built-in profit margin for Extension/SRE, can -- can you give me some sense of the magnitude of that built-in profit margin and the -- and the pricing, sir?

MR. RICHARD OLFERT: We did not calculate or gather information on that. Our differentiation between the two (2) was based on the principle that the allocator chosen should be on a consistent basis, which we believe the net claims is.

MR. BYRON WILLIAMS: So you didn't analyse for example, sir, the materiality of that -- that built-in profit margin to the calculations?

MR. RICHARD OLFERT: We were concerned with the fact that the Corporation was able to assess -- or determine profitability -- or determine premiums in one (1) line which included a -- a profit component and the premiums were established for the other line of business in a similar fashion -- sorry, were established by the Board.

MR. BYRON WILLIAMS: And that's fair enough. But, would you like to answer my question, sir?

MR. RICHARD OLFERT: Could you repeat the initial question?

MR. BYRON WILLIAMS: Certainly. You didn't consider the materiality of the -- the profit margin?

MR. RICHARD OLFERT: We did not.

MR. BYRON WILLIAMS: In terms of -- you again chatted with Ms. Everard, I think it was this morning, it seems so long ago now, about the process that -- that Deloitte engaged in with Manitoba Public

Insurance in -- in reviewing your work as it evolved. Do you recall that conversation, sir?

MR. RICHARD OLFERT: Yes.

MR. BYRON WILLIAMS: And you identified, at least, two (2) areas where, to use your words, extensive discovery -- excuse me, extensive discussions took place. One (1) of them being the pro rata versus the incremental. And the other being the Level 'C' allocation.

Do you remember that discussion, sir?

MR. RICHARD OLFERT: Yes.

MR. BYRON WILLIAMS: And just in terms of, my -- my question flowing from that is just, in terms of whether or not there were any elements of the Deloitte methodology or assumptions that were materially changed as a result of your discussions with MPI?

MR. RICHARD OLFERT: There were not. Information and input was provided, which we were glad to consider, but, our conclusions were ours and consistent with the initial thought processes we brought into those discussions.

MR. BYRON WILLIAMS: Mr. Chairman, and Mr. Olfert, I want to thank you for your -- your assistance today, it was very helpful. Thank you, Mr. Chairman.

THE CHAIRPERSON: Thank you, Mr. Williams.

So, Mr. Oakes, I don't think you were here at the time. You don't have any questions?

MR. RAYMOND OAKES: Mr. Chairman, I do not. I advised Board counsel at the end of the morning session that I wouldn't have any.

THE CHAIRPERSON: I already canvassed the other Intervenors.

So, Ms. Everard, if you want to return to your other line of questioning we can excuse -- do you have any re-direct, Ms. Kalinowsky?

MS. KATHY KALINOWSKY: No, I have no further -- no re-direct.

THE CHAIRPERSON: Thank you very much, Mr. Olfert. We appreciate you taking the time, and your participation today. Thank you.

(MPI PANEL 2 STANDS DOWN - RICHARD OLFERT)

MS. MARILYN MCLAREN: Ms. Everard, while we have a little bit of a lull. I can tell you that there's one (1) insurance use in the commercial major class. And this information, in terms of the insurance uses themselves are in AI.4, Part 1.

The common carrier local passenger vehicle insurance use is able to buy Extension insurance. There is less than two thousand (2000) of those vehicles in the fleet.

And we believe also Artisan Trucks of which there -- no Artisan Trucks, sorry. So, we have less than two thousand (2,000) common carrier local passenger vehicles that can buy Extension insurance, and the heavy farm trucks, of which there are more. They can buy down their deductable, increase their liability, that's pretty much it. A tiny fraction of the overall category.

CONTINUED CROSS-EXAMINATION BY MS. CANDACE EVERARD:

MS. CANDACE EVERARD: Just as a follow up question then. Would it fair to say that the -- the amount is not material enough to warrant looking any adjustments to those cost allocations?

MS. MARILYN MCLAREN: You know, I do know there are a lot of large farm trucks. So, we might want to have a look at the actual percentage. But, certainly on the basis of the common carrier local passenger vehicle it wouldn't be worth the effort, no.

MS. CANDACE EVERARD: Would you be able to provide the percentage on the --

MS. MARILYN MCLAREN: We'll do that.

MS. CANDACE EVERARD: -- other one, please?

MS. MARILYN MCLAREN: We'll do that.

--- UNDERTAKING NO. 13: To provide the percentage on cost allocations for farm trucks

CONTINUED BY MS. CANDACE EVERARD:

MS. CANDACE EVERARD: Thank you. Okay, when we ended for the day on Wednesday, I had, had some questions on IFRS. And Mr. Chairman, I've got about two (2) more pages so we should be just ending about the right time and wrapping up on the IFRS topic.

We had left off at Tab 27 of the book of documents which is the Deloitte report on IFRS and we had gone through pages 12 and 13 and I'll just wait for the panel to get there.

This was the section of the report that dealt with the first time adoption of IFRS-1 and we had gone through the elective exemptions, the mandatory exceptions, et cetera and what the next steps would be for the Corporation.

So we left off at the bottom of page 13.

And if we turn over the page to page 14 we get into the section of the report that deals with insurance contracts and IFRS-4.

If we look at the row relating to accounting differences, the first bullet, this is the fourth row of the table on page 14 heading "Accounting Differences".

The first bullet reads:

> "Insurance contracts need to be assessed to determine if they meet the definition of an insurance contract or financial instrument in order to determine whether accounting is required under IFRS-4 or IAS-39."

And we had previously defined last Wednesday what those acronyms stand for. Did I read that bullet incorrectly?

MR. OTTMAR KRAMER: No, that's correct. Double negative question, funny answer.

MS. CANDACE EVERARD: Fair. I did read it incorrectly. Just the word --

MR. OTTMAR KRAMER: You -- you read the -- the response correctly.

MS. CANDACE EVERARD: Now that we all know for sure that I can read, we'll move onto the final row on page 14, the same chart, the row entitled "Impact to MPI".

The first bullet reads:

"MPI will be required to review its accounting, specifically IFRS-4 impacts to MPI, in the following ways."

And then there are a list of four (4) bullet points. Mr. Kramer, maybe I'll have you read those into the record for the Board if you would.

MR. OTTMAR KRAMER: Okay on page 14 the four (4) bullet points are as follows:

"Requirement to verify if current insurance products meet the definition of insurance contracts under IFRS-4. Requirement to review insurance contracts for imbedded derivatives and standalone [typo obviously] fair value accounting if certain criteria are met. Requirement to demonstrate compliance with the liability adequacy testing methodology identified in IFRS-4 for insurance liabilities."

And the last one:

"Disclosure enhancements related to significant assumptions, risk management objectives and policies for mitigating insurance risks, sensitivity and concentrations of an insurance risk, claims development information et cetera."

MS. CANDACE EVERARD: Thank you. Now if I have you turn the page to page 16 of the report this is the section which -- which deals with the preliminary views on insurance contracts, so the -- the section that we were just looking at.

It's reflected here that the discussion papers with respect to the insurance contracts issue will be forthcoming. And that is reflected under the section entitled "Accounting Differences".

It says:

"Discussion paper is currently out for comment with the final standard not expected until 2011 or 2012."

Is that correct?

MR. OTTMAR KRAMER: That -- that is the understanding when that was written I believe it's -- it's still 2011 or '12 but it could even be, perhaps, more delayed.

MR. DONALD PALMER: And may I also say that that's when the standard will be released, not the effective date of that standard.

MS. CANDACE EVERARD: That was going to be my next question because we are speaking about IFRS-4 here rather than IFRS-1. It's my understanding that the actuarial standards with respect to insurance contracts are still under discussion and development.

Is that right?

MR. DONALD PALMER: That's correct.

MS. CANDACE EVERARD: And I believe the earlier evidence from the panel was that those may be coming down by about 2014.

MR. DONALD PALMER: I think I said '13 or '14 or '15, so right now it's -- it's up in the air for sure. And that's certainly timing that's beyond the control of MPI.

MS. CANDACE EVERARD: Yes. Thank you. The next page of the report, page 17 deals with financial instruments, recognition and measurement, in particular IAS-39.

What I'd ask the panel to do with respect to this is just provide rather than reading in a specific portion although you certainly can if you wish but just provide the Board with a -- a flavour of what IAS-39 relates to and -- and how it may affect the Corporation.

(BRIEF PAUSE)

MR. OTTMAR KRAMER: There's -- there's not a whole lot of differences between when we adopted 3855 several years ago the section related to the mark to market process.

There are a few differences. Those have been identified in the accounting differences and one that I'll draw your attention to is the impairment we -- as we probably may understand it there are some impairment rule differences between IAS-39 and 3855.

MS. CANDACE EVERARD: Mr. Kramer, when we're speaking about impairment that's -- in terms of an impairment of an investment?

MR. OTTMAR KRAMER: Yes, that's an impairment of investment. Again, based on preliminary analysis, I believe that impairments of -- of debt instruments are -- are reversed through profit and loss whereas under 3855 they are not.

It's a minor difference but it is a difference that's discussed here.

MS. CANDACE EVERARD: And is there anything else that you wish to comment on with respect to IAS-39 at this point?

MR. OTTMAR KRAMER: This also touches to

the -- the issue of what we'd call the start over provision, where we've got financial instruments designated between held to maturity, available for sale, or held for trading.

And -- and that's something that has been discussed here at the -- at the Board previously.

MS. CANDACE EVERARD: Yes. And I was actually just going to ask a couple of questions about that. We know from looking at AI.21 which relates to IFRS and that's at Tab 13 of the Board's book of documents the Corporation is considering reclassifying financial instruments as part of IFRS and this is on page 2 of AI.21 in the chart the row -- that is Item Number 2 relating to financial instruments.

And this would have been already read into the record previously but where there's a reference to the transition for IFRS providing for an opportunity for a quote, "do-over" end quote, on the classification of financial instruments.

You're with me?

MR. OTTMAR KRAMER: Yes, I see that.

MS. CANDACE EVERARD: And the reclassification of financial instruments is further detailed in the Deloitte report if we go back to that which is at Tab 27.

Still in the same section, the IAS-39 section but just a few pages from where we were, in particular, I'm looking at page 20.

There's -- the second full bullet on page 20 speaks about:

> "IFRS-1 permitting an entity to designate financial assets as available for sale as of the date of transition to IFRS.
>
> IFRS-1 also permits a first time adopter to designate any financial asset or liability as at fair value through profit and loss provided the criteria for using the fair value option are met.
>
> This provides an opportunity to change the designation of certain financial instruments on transition to IFRS."

Now what we looked at, at AI.20, said that the Corporation was considering this, is there potential here for financial impact to the Basic ratepayers relating to this issue?

MR. OTTMAR KRAMER: As -- as we've discussed I would believe it was at last year's Hearing, what -- what this re-designation would be if -- if it's taken would -- would allow for better matching on the -- on the income statement or the profit and loss statement.

By -- by re-designating some of the held -- or, available for sale, bonds, any interest rate fluctuations by -- by designating them as held for trading, any interest rate fluctuations would then also go through the -- the P&L.

So -- so ideally if interest rates rise or fall the effect on the P&L would be immediate, and not on -- on any future disposition.

MR. DONALD PALMER: We -- we were looking -- and we have already taken this step partially under 3855. And the reason we did that was to have more stability in the P&L. So, from that standpoint for the -- offering the rate payer more stability.

Now, we have not yet made the policy designation with regard to this one (1) time do over. That's something that will be going to the Board of Directors within the next three (3) to six (6) months, before the end of this fiscal year.

But, certainly our view as the -- the adoption of -- or, classifying newly purchased bonds is one of stability, I would expect that same consideration to be in any of the policy adoptions.

MS. CANDACE EVERARD: Mr. Palmer or Mr.

Kramer, can you comment on what, if any, affect these changes may have on the Corporations retained earnings?

MR. OTTMAR KRAMER: If the -- that do-over provision was taken, the accumulated comprehensive income associated with those available for sale financial instruments would be moved over into the retained earnings and a piece of that, of course, would -- would hit the RSR.

MS. CANDACE EVERARD: So, the effect would be an increase in retained earnings?

MR. OTTMAR KRAMER: Not necessarily. It's dependant on what the AOCI balance is, that is associated with those financial instruments.

If we would have done it a year ago, it was probably negative. If we would have done it at year end, off the top of my head I don't know what it is. But, it fluctuates based on market conditions. So, it's not an automatic up, it's not an automatic down. It's dependant on the market forces that are applicable at that point in time.

MR. DONALD PALMER: May I just add to that just a little bit. There -- that's very true on the asset side of the business because the fixed -- fixed income securities are dependant on interest rates.

There is the offset on the liability side as well. So, there maybe some change in retained earnings, but overall to the whole net equity of the Corporation it's a net wash.

(BRIEF PAUSE)

MR. OTTMAR KRAMER: Just for some clarification, when we submitted, I think it was Exhibit No.16 on Wednesday and -- and that shows the accumulated other comprehensive income for the last two (2) quarters, the May 31st and August 31st, we -- we submitted that, I think, towards the end of day, Wednesday.

And you can see the opening AOCI associated with the bonds that are in available for sale category on March 1st, 2009, which is the same as February 28th, 2009, the AOCI was in a negative position at that point in time, a negative $10.7 million.

Hypothetically speaking, if the election was triggered at that point in time, which we couldn't do, but if -- if we were right at IF -- IFRS cut-over date we would have had a negative impact on retained earnings and on RSR.

At May 31st, it was five hundred and eighty two thousand (582,000), or .6 million. So it would net almost negligible. And at August 31st it was $15.8 million.

So it does fluctuate, so that's why my comment was that there is not a -- an automatic increase or decrease. It's dependent on -- on the market forces which are driven primarily the -- the long term interest rates.

THE CHAIRPERSON: Correct me if I misunderstand you. But with the preponderance of bonds that you hold in your portfolio and if interest rates rose, market values would decrease, correct?

MR. OTTMAR KRAMER: Did you say decrease?

THE CHAIRPERSON: Decrease.

MR. OTTMAR KRAMER: Yes, that is correct.

THE CHAIRPERSON: So run by me if you don't mind for a minute, this do-over business. You've got most of the bonds now and held for trading, correct? Other than the MUSH?

MR. OTTMAR KRAMER: No, most of our bonds are still unavailable for sale. Some are -- some -- and held for trading and yes, the MUSH are in a -- held to maturity.

THE CHAIRPERSON: Okay. We'll reflect on this for a while.

CONTINUED BY MS. CANDACE EVERARD:

MS. CANDACE EVERARD: Okay. Now some of the evidence that we had today on IFRS and some of the evidence that we had last Wednesday lets us know that as a result of IFRS there are several accounting elections that are going to be made in the current year and that some of those may have implications on rates.

MR. DONALD PALMER: On rates, because rates are set prospectively we -- and we have our assumptions on investment income that all of those are that ultimately we will get some return which on an accounting basis could be through AOCI, it could be through the P&L but eventually we'll realize that income.

So we -- that's what we include as our assumptions on investment income. So, regardless of these particular elections, on an ultimate basis at the time you're going to realize them that could change from year to year but the ultimate value would be the same.

So on a rate setting perspective I would say that these particular elections would not have an effect on the rates. What these elections could have an effect on is the RSR balance, not -- not the prospective rates.

So to the -- to the extent that there could be an RSR surcharge or an RSR refund or rebate, then there could be some effect. But on the actual rates themselves that are set on a prospective basis, there would be no impact.

MS. CANDACE EVERARD: Is the answer that you just gave restricted to the elections that would be made for IFRS-4 or was your question taking into account IFRS-1 as well, because I -- I meant it to include everything and maybe I didn't state that clearly?

(BRIEF PAUSE)

MR. DONALD PALMER: We're -- we're still preliminary with -- with all of those. Again, the elections will be -- certainly there will be always an eye on stability when any of those recommendations with regard to elections are made.

So at this point in time the effect on rates would be minimal in my estimation. But again, that's preliminary.

MS. CANDACE EVERARD: And -- and I know from the discussion that we had last Wednesday that there's still some work to be done with respect to the options that are going to be put forward to your Board of Directors.

And I asked about implications on rates

and -- and your evidence was, Mr. Palmer, that, you know, you didn't know what the -- the magnitude of any effect would be.

But in speaking about the five (5) elective exemptions for IFRS-1 I had asked whether any of them or all of them would have financial implications. You said that likely leases and insurance contracts would not have an effect, but the other three (3) elective exemptions under IFRS-1 could.

And so I took that to mean that to be determined at some point in the future will be a more certain answer, but, at this stage, it's possible that the elections to be made will have financial implications for the Corporation, and Basic, which, in turn, is relevant to rates. That's simply what I'm getting at.

MR. DONALD PALMER: And -- and just to clarify on that, yes, the elections could have an impact depending on what election is taken. And -- but, again, what we -- our goal through all of these Proceedings will -- is stability, will continue to be stability and I would suspect that any elections that may -- would be made under IFRS-1 would be with stability in mind.

MS. CANDACE EVERARD: I understand that. And -- and, as we also discussed on last Wednesday, before the Board of Directors is going to make any decisions with respect to elections, they'll have some financial information before them about what the various options would materialize into, in terms of dollars.

MR. DONALD PALMER: Absolutely.

THE CHAIRPERSON: Mr. Palmer, if I recall properly, you also indicated that your Board would decide, without any prior consultation, for example, with PUB.

So, potentially, PUB could take a different rate regulated view than the Corporation would, is my understanding correct? If you want stability, that's what I'm coming back to.

MS. MARILYN MCLAREN: I'm sorry, can you repeat the last part?

THE CHAIRPERSON: Well, coming to this. It sounds to me like you've got a number of different potential options. And if I understood what Mr. Palmer said the other day, your Board would make its decisions in which options it wanted to take, okay, without any consultation with, for example, this process.

If you want stability, I'm just posing to you whether or not that approach is the most effective one (1) because the problem that you could have is you could select a particular approach, and then, for rate purposes, you could have the regulator taking a different position.

I'm not saying it would or it wouldn't because I don't know what your Board would do, but just on the surface of it, there seems to be an argument for consultation rather than determination.

MS. MARILYN MCLAREN: As I recall, Mr. Chairman, we had a longer version of this conversation last week. Mr. Palmer didn't say that the Board of the Corporation is intending to make decisions without consultation.

There was a question posed about, I think, somewhere in some document we used the word "stakeholder" and there was questions about stakeholders. I said that in -- in every eventuality with respect to financial reporting our stakeholders must include the Provincial Comptroller, the Auditors, the Auditor General.

And after the comments that you made with respect to regulatory accounting, and so on, I had said that we may need to take a broader view with respect to consultation in this matter.

THE CHAIRPERSON: Thank you for reminding me. That brings me back up to date.

(BRIEF PAUSE)

CONTINUED BY MS. CANDACE EVERARD:

MS. CANDACE EVERARD: This is for Mr. Palmer probably, or perhaps for Ms. McLaren. Following on the Chairman's questions about the role of this Board, or what, if any, role it may have in -- in IFRS elections, at page 57 of the Deloitte Report that we've been looking at, this is under the heading of "Wider Business Considerations," there is reference -- I'll -- I'll just wait for you to get there.

I'm still at Tab 27 of the book of documents, page 57 of the Deloitte Report.

MR. DONALD PALMER: Yes, I have it.

MS. CANDACE EVERARD: Deloitte says, at the second row in the chart, with respect to regulatory matters, that:

"Changes to the RSR that result from the adoption of IFRS may impact MPI's compliance with legislative requirements."

I'm not sure if that should be "of the PUB," or "or the PUB." But then it goes on to say:

"The PUB is focussed on the RSR as this determines the level of rebates authorised by PUB. Accordingly, a regulatory strategy will need to be developed once the effects of IFRS on MPI's financial statements have been quantified."

Are you with me?

MR. DONALD PALMER: Yes, I am.

MS. CANDACE EVERARD: And then, the Board posed a question following on that statement, which is at the same tab, Tab 27. If you just flip to the very end of Tab 27, we have Question 24, posed by the Board in the Second Round, where we asked that -- the Corporation to ask Deloitte to elaborate on what should be included in the reference to regulatory strategy.

And can I have you read in Deloitte's reply, Mr. Palmer.

MR. DONALD PALMER:

"The implementation of IFRS can result in either or both of retroactive changes to MPI's financial statements and future accounting policies -- changes that would effect reported earnings. These changes could be caused by required changes to accounting policies mandated by IFRS. The selection of different accounting policies that are permitted by IFRS, or the application of IFR 1 -- IFRS 1 standards that govern the transition to IFRS.

These changes could result in changes to MPI's reported equity level as at March 1st, 2011, the date of transition, and/or to reported net income thereafter. Changes to either MPI's equity or reported earnings will impact MPI's Rate Stabilization Reserve, RSR. The level of the RSR is of ongoing interest to the PUB. Accordingly, the term "Regulatory Strategy" simply refers to the need to anticipate and appreciate the impact that any resultant changes to RSR levels might have on the regulatory rate setting process."

MS. CANDACE EVERARD: Thank you. Now, does the Corporation read that as a suggestion by Deloitte, that perhaps the Corporation consult with this Board, with respect to IFRS decisions?

MR. DONALD PALMER: I don't read that into this, no.

MS. CANDACE EVERARD: What is the

Corporation's position with respect to Deloitte's advice on a regulatory strategy, as set out in the references that we've looked at?

MR. DONALD PALMER: Not necessarily only because of IFRS, but certainly we do our pro formas, our forecasts, on a go-forward basis from both a pro forma P&L perspective, and a projected RSR balance. We do that every year, and then make decisions as to what our application will consist of, to this Board.

So this would be in that same context. So, once we've got what the effect of the IFRS will be, we project those further and then that will affect, obviously, what we apply to this Board for, in terms of rates and RSR levels, or rebates, or surcharges, or whatever.

MS. CANDACE EVERARD: It is agreed though, that the implications of IFRS will carry forward into future years and future rate applications?

MR. DONALD PALMER: Yes.

MS. CANDACE EVERARD: Mr. Chairman, that wraps up the questions that I have on IFRS. I see it's ten (10) to 4:00. Do you want me to start in another area, or just wait until tomorrow morning?

THE CHAIRPERSON: No, I think we've dealt with enough weighty issues for the day. Thanks, Ms.

Everard.

We'll see you all tomorrow at 9:00.

(MPI PANEL NO. 1 WITNESSES RETIRE)

--- Upon adjourning at 3:53 p.m.

Certified Correct,

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Cheryl Lavigne, Ms.