MANITOBA PUBLIC UTILITIES BOARD

Re: PUBLIC HEARING

RE: MANITOBA PUBLIC INSURANCE

GENERAL RATE APPLICATION

FOR THE 2013/14 INSURANCE YEAR

Before Board Panel:

Regis Gosselin - Board Chairman

Karen Botting - Board Member

Anita Neville - Board Member

HELD AT:

Public Utilities Board

400, 330 Portage Avenue

Winnipeg, Manitoba

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Pages 898 to 1018

APPEARANCES

Candace Grammond	)Board Counsel
Kathy Kalinowsky	)MPI
Byron Williams	)CAC
Raymond Oakes	)CMMG
Liz Peters (np)	)CAA

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--- Upon commencing at 9:33 a.m.

THE CHAIRPERSON: Good morning, everyone. I believe we're ready to begin today's proceedings. We have some matters to attend to before we start. I believe we have an exhibit from MPI.

MS. KATHY KALINOWSKY: Yes, I've handed out Undertaking number 9, which is a report regarding the problems intersections in the city. And there's a list there that I'm sure that Board member and others will be looking at as -- before they drive home from the hearing today. But I would suggest that it be marked as MPI Exhibit number 12.

--- EXHIBIT NO. MPI-12: Response to Undertaking number 9: report regarding the problem intersections in the city

MS. CANDACE GRAMMOND: Thank you, Mr. Chairman. I think we can turn it over to Mr. Williams. I know he has some exhibits as well that he'll enter, and then I assume he'll start his cross.

MPI PANEL, RESUMED:

MARILYN MCLAREN, Resumed
HEATHER REICHERT, Resumed
LUKE JOHNSTON, Resumed

CROSS-EXAMINATION BY MR. BYRON WILLIAMS:

MR. BYRON WILLIAMS: Yes. Good morning, Mr. Chair, and members of the panel. And with -- with me again is Ms. Desorcy. She's found her way over from the Bipole 3 hearing and, I think, is very glad to be at the Public Utilities Board.

We have four (4) exhibits to -- to introduce. One should be the -- and does the panel have them be -- yes. One should be a fairly thick document titled, "MPI 2013 General Rate Application Excerpts from the Record," and we would ask that that be marked as Exhibit number 5.

--- EXHIBIT NO. CAC/MANITOBA-5: Document titled, "MPI 2013 General Rate Application Excerpts from the Record"

MR. BYRON WILLIAMS: And those are excerpts from the record, so I -- I certainly have not sought the -- I don't see any issue with these. Next, there is a one (1) page sheet to -- to teach both Ms. Desorcy and Mr. Williams about discount rates, and it's called, "The Simple Illus -- Illustration of the Effect of a 1 Percent Increase in Interest Rates."

We would suggest this is -- this be marked as CAC/Manitoba exhibit number 6. We've shared it with My Learned friend, Ms. Kalinowsky, and I do not believe she has any objections, although not -- she -- she may be looking -- okay.

(BRIEF PAUSE)

MR. BYRON WILLIAMS: I believe we've shared some copies, but some may have disappeared.

(BRIEF PAUSE)

MR. BYRON WILLIAMS: Ms. Kalinowsky, I -- I apologize for my inaccurate counting. So we'd suggest that be marked as Exhibit number 6, Mr. Chair.

--- EXHIBIT NO. CAC/MANITOBA-6: Document titled, "The Simple Illustration of the Effect of a 1 Percent Increase in

Interest Rates."

MR. BYRON WILLIAMS: The -- the next document should be titled, "Addendum to MPI Rate Risk Management in the RSR." This is actually a document prepared by doc -- Professor Simpson. We shared it with MPI and -- and Board counsel quite some time ago.

It's really an addendum to Mr. -- Professor Simpson's evidence. It will be used to assist the discussion either today or -- or tomorrow as well and we would suggest that be marked at CAC Exhibit number 7.

--- EXHIBIT NO. CAC/MANITOBA-7: Document titled, "Addendum to MPI Rate Risk Management in the RSR"

MR. BYRON WILLIAMS: And finally, there should be a document which in the upper left-hand corner is titled, "Accident Benefits Others Indexed." Again, it's a document we've shared with -- with MPI and we would suggest that be marked as CAC Exhibit number 8.

--- EXHIBIT NO. CAC/MANITOBA-8: Document titled, "Accident Benefits Others Indexed"

MR. BYRON WILLIAMS: And I -- our clients do appreciate the -- the cooperation of Manitoba Public Insurance in introducing those documents.

Mr. -- Mr. Chairman, and members of the Board, just a quick outline today of some of the things we're discussing. I -- I realize we have a short day. A -- a lot of them will -- will relate to the -- the work of Mr. Johnson. Some will go to Mr. -- Ms. Reichert, and few may go to Ms. McLaren. I'm sure she'll -- she'll have her say before the -- the day is over.

Our client is part of her -- their organization's ongoing work with both focus groups and their advisory groups, has a number of questions about road safety, some of which she woul -- she would like me to ask today. So we are going to go a bit out of order of the -- perhaps the -- the logic of the cross-examination.

And finally, Mr. Chair, we're mindful we sat through the excellent cross-examination of My

Learned Friend Ms. Grammond. We're always mindful of avoiding duplication. There will be times when we do cover some of the same area, but hopefully to a -- to a different end or to enrich the record rather than to merely duplicate it.

CROSS-EXAMINATION BY MR. BYRON WILLIAMS:

MR. BYRON WILLIAMS: Mr. Johnston, perhaps we'll start with you. And I'd like to start by discussing with you the relationship between the review of claims liabilities and the Corporation's forecast of claims incurred for the purpose of -- of rate setting.

Sound okay, Mr. Johnston?

MR. LUKE JOHNSTON: Yes, that's -- that's fine.

MR. BYRON WILLIAMS: It's kind of what you do.

MR. LUKE JOHNSTON: That's true. We did -- we touched on this a little bit last week. But in the review of claims liabilities, we are looking at prior years' claims and we're making an estimate on the ultimate cost of those claims in prior years.

Of course, when we're forecasting, a -- a very important, if not the most important aspect, is the history of claims. So if we are forecasting PIPP, for example, a -- a good starting point is the historical PIPP experience. And then we'll, of course, supplement that with field information from the bodily injury division.

There may be reasons why we expect different trends than in the past or different claims settling patterns, et cetera. But again, the historical expe -- experiences, I would say, carries the most weight in forecasting.

MR. BYRON WILLIAMS: Thank you, Mr. Johnston, and -- and certainly from your answer, I take it that the -- you would agree that the evaluation of policy liabilities really serves as the groundwork for the financial forecast.

Is that correct, sir?

MR. LUKE JOHNSTON: Yeah, I think that's -- that's fair. It's -- it's -- as I mentioned, it carries the majority of the weight, the -- our historical experience.

MR. BYRON WILLIAMS: And to take that one step further, if we look at the estimations of incurred but not rela -- not reported, IBNR, really, your forecasts are inextricably linked to the IBNR review of liabilities.

Would that be fair, sir?

MR. LUKE JOHNSTON: Yeah, I would -- I would say that's -- that's fair, if -- if there was an assumption knowingly -- perhaps not knowingly overstated in the liability review, that would flow through, a large extent, into our forecast.

So if -- if we had an assumption that, for example, PIPP claims were going to grow by 2 percent a year, and then we later changed that to 1 percent a year, that would obviously flowthrough to our PIPP forecast.

MR. BYRON WILLIAMS: To put it in terms that even a humble lawyer can understand, if your basis overstated, you'll -- there's a material risk you'll also overstate the forecast going forward?

MR. LUKE JOHNSTON: Yes, that's true. If -- if we have a forecast coming out of the liability review it only makes sense to -- to follow the -- the same pattern. If -- if say the -- say the Corporation didn't agree with every aspect of the appointed actuaries review. It likely wouldn't be appropriate for us to make a forecast much lower than -- than the assumptions that -- that he's used in his report.

MR. BYRON WILLIAMS: Now, this question can go to anyone on the panel, so, Ms. Reichert or Ms. McLaren, if you're feeling left out, no worries, pop right in.

But wi -- without asking you to elaborate in particular, I would ask the MPI panel to confirm that you recall that there was considerable discussion on day 1 of the hearing regarding the role of both the external actuary and the external auditor.

Do you recall that in your -- in your direct evidence?

MR. LUKE JOHNSTON: Off -- off the top of my head I -- I don't recall, but there's -- there's definitely a role between those -- those two (2) individuals or bodies.

MR. BYRON WILLIAMS: Well, I'll suggest to you, Mr. Johnston, that whether it was in your evidence or -- or in Ms. Reichert's, and indeed in both, that one of the important messages you were sending was that there are in -- checks and balances in the forecasting process, and that those checks and balances include both the external actuary and the external auditor.

Would that be fair?

(BRIEF PAUSE)

MR. LUKE JOHNSTON: Yeah, that's --

that's fair. With respect to the liability review, there's involvement of the auditors and the appointed actuary. And then the DCAT also includes the appointed actuary review.

MR. BYRON WILLIAMS: And I'm just trying to recall, but perhaps even the cost allocation methodology?

MS. HEATHER REICHERT: Yes, that's correct. The external auditor does -- does do an audit of the Basic financial statements, which embodies the cost allocation. And we did ask the external actuary to do additional work this year to provide more comfort to the PUB.

As well, the external auditor does have their own actuary that looks at, in the process of auditing, our corporate and Basic financial statements, looks at what we are establishing for -- for actuarial estimates in the financial statements.

MR. BYRON WILLIAMS: I thank you for that, Ms. Reichert. And the panel, I do not believe, needs to turn there, but if you're ever bored and are looking for a helpful description of what the -- the roles of the external actuary and the external auditor perform, PUB-1-18 is really a very good description.

And, Mr. Johnston or -- or Ms. Reichert, probably to you, Mr. Johnston, in terms of the -- the role of the external valuation actuary, would it be fair to say that a central document prepared in support of this Rate Application is the review of the assumptions and methodologies underlaying the review of policy liabilities based on figures as of October 31st, 2011?

MR. LUKE JOHNSTON: I believe the question was: Was that an -- the key role of the appointed actuary? Sorry.

MR. BYRON WILLIAMS: The question wasn't very well asked, Mr. Johnston, so let's try that one again. Hopefully I'll do better. In terms of the Rate Application -- let's leave the external actuary out of this for a second.

In terms of the Rate Application, a -- a central foundational document is the actuarial report on MPI, the -- the universal compulsory automobile insurance as of October 31st, 2011, correct?

MR. LUKE JOHNSTON: Yes, and what makes that one more important than February's is the -- we do the October -- the as at October 31 review in advance of year end, so we have more time to review the assumptions prior to year end. Once -- once year end comes, we need to literally just produce a report within a few weeks. So we want more time, which is why we do that earlier in the year.

MR. BYRON WILLIAMS: And that report is prepared by the external actuary, using analysis provided by the Corporation's internal actuarial department, as well as his own -- own staff, correct?

MR. LUKE JOHNSTON: Yes, the actual report is prepared by the external actuary. The -- the work is largely done in house, and we send an initial draft to the appointed actuary. And then discussions ensue on all the assumptions. The appointed actuary also has their own software in house that they use, but I don't review the -- that -- the output from -- from their software.

MR. BYRON WILLIAMS: I apologize to the court reporter. You mentioned, as well, the actuarial report on universal compulsory insurance as of February 29th, 2012.

And, again, that report is prepared by the external actuary with the assistance of MPI, correct?

MR. LUKE JOHNSTON: Yes, that's correct.

MR. BYRON WILLIAMS: And as Ms. Reichert may have already mentioned, both of these documents -- the review of policy liabilities as at October 31st, 2011, and the review of policy liabilities as at February 28th or 29th of 2012 -- are given to the external auditors, KPMG, to be reviewed by their consulting actuary, correct?

(BRIEF PAUSE)

MR. LUKE JOHNSTON: Yes, that's correct. They -- they review those reports and they often have interactions with the appointed actuary, which I don't know the nature of all of them, but they -- they do.

MR. BYRON WILLIAMS: So, in essence, the review of policy liabilities, which forms such a central el -- element of the forecast of claims incurred, is signed off on by both the external actuary and the auditor, correct?

MR. LUKE JOHNSTON: Yeah, that's correct.

MR. BYRON WILLIAMS: And if I were to go back any year in recent history, I would find that -- that same pattern repeating, with the review of policy liabilities being prepared by the external actuary and reviewed by the external auditor, with the assistance of his actuarial consultant, correct?

MR. LUKE JOHNSTON: Yes, that's correct.

MR. BYRON WILLIAMS: For the be -- benefit of the MPI witnesses and also for the panel, CAC-5 is excerpts from the record. And you'll see some messy handwriting up in the right hand -- numbering in the top right-hand corner. So we'll try and work off of that pagination for these documents.

Mr. Johnston -- and again, you have had some discussion with Ms. Grammond, in terms of forecasts of claims incurred, so we're not going to spend a long time here. But we are going to spend a bit of time on this document, which is at page 1, in the top right-hand corner of CAC Exhibit 5.

And you'll agree with me that a -- that it appears to be an attachment to CAC-1-56, the First Round Information Request, correct?

MR. LUKE JOHNSTON: Correct.

MR. BYRON WILLIAMS: And if were to try and to describe verbally what we see as we move in this document from left to right, I'll suggest to you that on the left-hand side we'll see a table titled, "Claims Incurred."

Do you see that, Mr. Johnston?

MR. LUKE JOHNSTON: Yes, I do.

MR. BYRON WILLIAMS: In the middle, we have a -- a table titled, "Statistical Measures Original Projected." Do you see that, sir?

MR. LUKE JOHNSTON: Yes.

MR. BYRON WILLIAMS: And on the right-hand side we see a table, "Statistical Measures Revised Forecast." Is that correct, sir?

MR. LUKE JOHNSTON: Correct.

MR. BYRON WILLIAMS: Now, Mr. Johnston, just for a couple of seconds I'd like you to -- direct your attention to the left-hand side, which is "Claims Incurred." And just as we again try and familiarize -- orient -- orient ourself to the table, the first column under claims incurred is simply the insurance year, correct?

MR. LUKE JOHNSTON: That's correct.

MR. BYRON WILLIAMS: And the next column over would be the actual claims incurred in that particular insurance year. Is that -- is that so, sir?

MR. LUKE JOHNSTON: That's correct.

MR. BYRON WILLIAMS: And the next column over is the original projected, correct?

MR. LUKE JOHNSTON: Correct. So the -- the original projected in the GRA, so again that would be the 2013/'14 year in this -- this case of this Application.

MR. BYRON WILLIAMS: And then there's the revised forecast is the fourth column, sir?

MR. LUKE JOHNSTON: Correct. And -- and that would be the '12/'13 year in this GRA.

MR. BYRON WILLIAMS: And thank you. You -- you made quite an important point. If I was trying to look at what -- what the -- the General Rate Application was based upon I would focus on the original pro -- projected column.

Is that correct, sir?

MR. LUKE JOHNSTON: That's correct.

MR. BYRON WILLIAMS: So let's just take an example of that if -- if we might, just to -- to familiarize ourself with this -- this table. And let's go down to the insurance year 2009/'10. And we'll see that the -- moving two (2) columns over, the original projected claims incurred for that particular year was roughly 625 million.

Would that be correct, sir?

MR. LUKE JOHNSTON: Correct.

MR. BYRON WILLIAMS: And we see that the actual was about five hundred and fifteen (515) -- somewhere between 515 and 516 million, correct?

MR. LUKE JOHNSTON: Yes, that's correct.

MR. BYRON WILLIAMS: So we see a difference between the projection used for rate setting and the actual of about $109 million.

Is that correct, sir?

MR. LUKE JOHNSTON: Yes, that's approximately correct.

MR. BYRON WILLIAMS: And just ballpark, roughly a variance of roughly 17.5 percent of the original projection?

MR. LUKE JOHNSTON: That's correct.

MR. BYRON WILLIAMS: So in essence when we look at the claims incurred table, it's comparing forecast claims to actual claims for two (2) forecasts: the original projection and the revised forecast.

That's what it's telling us, correct?

MR. LUKE JOHNSTON: That's correct.

MR. BYRON WILLIAMS: We're going to ignore the revised forecast table, but I just want to make sure that we're on common ground, in terms of the middle table being statistical measures original projected.

Mr. Johnston, I'll suggest to you that this table summarizes the forecast errors for the original projection under -- that's essentially what it does.

Would that be fair?

MR. LUKE JOHNSTON: That's correct. There's various measures that are used to -- to summarize the -- the deviation.

MR. BYRON WILLIAMS: And let's take, as an example, the most recent year of 2011/'12. That's the -- the bottom year in -- in terms of insurance years, and focussing again on the middle col -- the middle table statistical measures of the projected we see the fourth column over is titled "Prediction Error."

Do you see that, Mr. Johnston?

MR. LUKE JOHNSTON: I do.

MR. BYRON WILLIAMS: And for the 2011/'12 year, we -- we can see that MPI has calculated the prediction error for that particular year to be minus $35 million.

Is that correct, sir?

MR. LUKE JOHNSTON: Correct.

MR. BYRON WILLIAMS: And essentially that's the difference between the projection of claims incurred used for rate setting and the actual results.

MR. LUKE JOHNSTON: Yes, that's

correct.

MR. BYRON WILLIAMS: Moving just one (1) column over you'll see a heading "Percentage Prediction Error."

Do you see that, Mr. Johnston?

MR. LUKE JOHNSTON: I do.

MR. BYRON WILLIAMS: And again focussing on the 2011/'12 year we see the figure of minus 5.46 percent -- minus five point four-six-one (5.461).

MR. LUKE JOHNSTON: That's correct.

MR. BYRON WILLIAMS: You were going to catch me, weren't you, Mr. Johnston?

MR. LUKE JOHNSTON: I was going to say that's approximately correct, whether the last three decimals were accurate or not.

MR. BYRON WILLIAMS: I could see you smiling, sir. If we look at the percentage prediction error, going up to the 2004/'05 year and then essentially running down to 2011/'12, would you agree with me that the pattern of signs have -- have been all negative since 2004/'05?

MR. LUKE JOHNSTON: Yes, and -- and I -- I'm glad you reference 2004/'05 in -- in your question, because in -- in 2005/'06 is -- is when we made a -- a very significant change to our reserving practices.

In predict -- in particular we created new reserving guidelines on -- on large claims and we introduced reserving -- a reserving calculator for case managers. And it really -- it really drastically changed our -- how our claims were reported.

And pri -- prior to '05/'06, and we don't have the entire history here, but you'll notice that at least there were some -- some positive deviations and -- and with the -- with the best-estimate forecast, you'd -- you'd expect that sometimes you'd be above or -- or sometimes you'd be below the forecast.

Aft -- after '05/'06, the results of our new reserving methodology were showing much more favourable development than we had estimated in the liability review, and it -- it took a few years for the Corporation to recognize this favourable experience.

Obviously, you have to be careful with one (1), or two (2), or three (3) years of data, whether you're going to assume that that is exactly the way the new world -- the new state of the world is going to be when you make a big change in -- in reserving.

But you will notice that the assumptions that we were using, in particular to PIPP, were overstating the forecast fairly consistently. And it took some -- some fairly substantial changes in those assumptions to -- to bring the forecast back down to the -- the smaller deviations that you're seeing now in '11/'12, both revised and the original forecast.

MR. BYRON WILLIAMS: Thank you for that thoughtful answer, Mr. Johnston. In terms of the -- you mentioned particular challenges in terms of PIPP, being P-I-P-P, capitalized. And -- and the -- the challenges were in both the accident benefit weekly indemnity line as well as the accident benefit other.

Would that be fair, where the major challenges were?

MR. LUKE JOHNSTON: Yes, that's fair. The -- these, as we -- we talked earlier, are the longer-tail lines, where we're -- where we're dealing -- although the majority of the claims will close fairly quickly there are a -- a large dollar portion of claims that are -- are a result of serious accidents, and they extend for the life of the claimant.

So these assumptions are obviously difficult to make, because we don't -- we don't know exactly what is going to happen with them. And they're

-- they're also very sensitive to changes and assumptions, interest rates, development patterns. So, yes, we -- weekly indemnity and accident benefits other indexed, which is mostly personal care, those are the -- the two (2) key issues with the -- that -- that were affected by this reserving change I spoke of.

MR. BYRON WILLIAMS: And we'll come back to this point in just one second, Mr. Johnston. You describe both accident benefits WI and accident benefit other as longer-tail claims.

Did I -- did I hear you correctly, sir?

MR. LUKE JOHNSTON: Yes.

MR. BYRON WILLIAMS: And one of the particular challenges that Manitoba Public Insurance experiences with claims of a longer duration is you don't have as much evidence, in terms of -- in terms of evaluating your experience or -- or projecting from your experience, correct?

MR. LUKE JOHNSTON: That's correct. For these lines, it's -- it's similar to like a long-term disability type plan, except we really don't have data on the expected life -- lifetimes of quadriplegics or brain-injured people, or -- so we're relying a lot on our own data, and we do have to make assumptions about the future in terms of how long these -- these claimants are going to live and -- and what type of payments they're going to receive over their lifetime.

MR. BYRON WILLIAMS: So you're talking about judgments with fairly limited data?

MR. LUKE JOHNSTON: Definitely in the early years of PIPP we had very limited data. When -- when we look at these reports now we're talking about a tail period, being claims that have open more than ten (10) years. And we -- we believe that this is the point in time where all claims are -- are -- all of the remaining open claims are on for life. There's not really a significant probability of recovery at that point.

And so we have -- we're starting to get some experience in this tail period. But, of course, having fifteen (15) to eighteen (18) years experience is -- is nowhere close to the potential of thirty (30), forty (40), fifty (50) years experience that we'll eventually get.

MR. BYRON WILLIAMS: Mr. Johnston, has Manitoba Public Insurance inquired of its brother or sister Crown corporations involved in no-fault schemes in terms of sources of data that -- that they may rely upon over and above their own internal data?

Do you need an example, Mr. -- Mr.

Johnston, or are you...?

MR. LUKE JOHNSTON: Yeah, I've -- I -- I do meet with SGI fairly regularly. And we have talked about perhaps trying to combine our experience and improve on our estimates. Of course, one of the difficulties is we don't really re -- necessarily reserve the same way. And that can make it a little bit difficult to -- to compare the output.

We haven't looked in -- at a great deal at changing our mortality table or -- or our mortality table is essentially our -- our life expectancy table. We haven't looked at changing that. We believe the table we're using does a pretty good job of -- of estimating lifetimes.

And we -- we now have a process in place that essentially adjusts our tail experience towards the table over time, so we're -- we're happy with that. But to answer your question, I haven't done a lot of work with Quebec or Saskatchewan in terms of what they use for their long-term claimants.

MR. BYRON WILLIAMS: And just in -- thank -- again, thank you for that answer. In -- in terms of -- and recognizing that you haven't done a lot of work in this area, are you aware whether or not, in terms of its accident benefit -- although the -- the categories are slightly different in Saskatchewan, clearly, but in terms of their personal care costs and that, whether or not Saskatchewan relies upon experience from the Workers' Compensation system, sir?

MR. LUKE JOHNSTON: No, I'm -- I'm not aware of -- of what they do in that regard.

MR. BYRON WILLIAMS: Have you made any inquiries?

MR. LUKE JOHNSTON: None, other than discussions I spoke of, of possibly looking at the -- the mortality patterns of our -- our two (2) claimant pools.

MR. BYRON WILLIAMS: And I think I know the answer to this one already, but just to -- to cross my -- my 'T', in terms of their weekly indemnity, are you aware whether or not they rely upon informa -- information from Quebec?

MR. LUKE JOHNSTON: No, I'm not aware of this.

(BRIEF PAUSE)

MR. BYRON WILLIAMS: Mr. Johnston, in areas where these long tail -- tail claims where there is still such material uncertainty, do you have any opinions on the value of seeking data from -- from other sources, whether it is another public auto insurer or a workers' compensation system?

Do you have any opinions on that, sir?

(BRIEF PAUSE)

MR. LUKE JOHNSTON: As -- as I mentioned before, we believe the mortality table that we're using is doing a good job. And we'll likely also see, in some of the evidence, that the -- the new reserving guidelines we're using produce a fairly consistent pattern that we're -- we're happy with.

I -- however, to -- to answer your question, I suspect that getting more data in -- in this regard could -- could add value. I don't know -- I don't know to what extent and if it would really result in any change at all to the way we're -- we're forecasting our long-term claims right now.

MR. BYRON WILLIAMS: Mr. Johnston, when my -- when my client looks to a line of business like accident benefit other, you'll agree with me that they see a -- a -- still a pretty substantial tail factor?

MR. LUKE JOHNSTON: Other -- actually, I should probably explain a -- a tail factor. The --

the tail factor basically is, we -- we talked about the -- these claimants over ten (10) year -- that have been open for more than ten (10) years as being our lifetime claimants.

And not having any experience for these claimants beyond about eighteen (18) years, we, of course, have to be very careful with how we forecast these claimants. If -- if you look at personal care, for example, there -- there still is significant risk there that claim payments could increase as claimants age.

So we have a tail factor, but to describe it as significant or -- I don't know your exact words -- I don't -- I don't believe that to be true. Is it very difficult to estimate? Absolutely. Is it the best estimate that I have right now? Again, I -- it wouldn't be in there if I didn't believe it to be the case. But highly uncertain, I would agree with that.

MR. BYRON WILLIAMS: I might have used the words "pretty big", Mr. Johnston. But I didn't think you were going to go -- go along with that. Let's go back to -- to CAC-1-56, the attachment. And we were focussing on the percentage pre -- prediction error column and the -- the consistent pattern of -- of negative from 2004/'05 on, Mr. Johnston.

You -- you recall that, before I sidetrack the conversation?

MR. LUKE JOHNSTON: I do recall that.

MR. BYRON WILLIAMS: And in your earlier statement you would say that normally with estimates you would expect to be sometimes above, sometimes below.

But here at least, and again recognizing the introduction of the reserving calculator, we've got -- we -- we've had a fairly consistent pattern of negative, since '04/'05, correct?

MR. LUKE JOHNSTON: That's correct.

MR. BYRON WILLIAMS: And although we -- we hope the worst is past, that suggests, to date, that there has been, over the last few years, a systematic over-prediction of actual claims.

Fair enough?

MR. LUKE JOHNSTON: Yeah, I -- I have -- I have to be careful with that, because the -- my predecessors and the previous appointed actuary did not have the data that I have today. So those were the -- they used the information that -- that they had at -- at the time to make their assumptions.

Clearly, looking at where we're sitting

today and the magnitude of the reductions we've made to the liabilities over the last, you know, three (3) to four (4) years, you can say that, yes, we've -- we overstated those claims initially. And we now have better data and -- to make better assumptions and a -- and a improved forecast.

MR. BYRON WILLIAMS: Now, Mr. -- now, Mr. Johnston, in that time period between '04/'05 and 2010/'11, at any time did MPI receive a report from its external auditors suggesting that it would be unreasonable to rely on the final overall estimate of claims liabilities produced by the external actuary?

MS. MARILYN MCLAREN: No, we did not.

MR. BYRON WILLIAMS: Thank you. Directing again in CAC Exhibit 5, the excerpts from the record, just to page -- pages 2 through 6, Mr. Johnston. I'm going to suggest to you that this is a excerpt from last year's transcript of a discussion I had with the former external actuary, Mr. -- Mr. Christie.

And certainly, Mr. Johnston, I didn't show it to you till shortly before the hearing, so I'll try and take you to the right sentences. But if you feel at any time that I'm making you jump around or not giving you time to read the para -- the sentences, just stop me and take the time you need.

But, Mr. Johnston, the purpose is -- I just want to clarify the role that the external auditor plays in assessing the reasonableness of the final overall estimate of claims liability produced by the external actuary. And you and I are both aware that Mr. Christie was the external actuary but I'll suggest to you that in this conversation he was really talking about the role of the auditor.

And -- and if you need a couple minutes to -- to assure yourself of that, please take that opportunity.

MR. LUKE JOHNSTON: And this is in regards to page 2 and 3 of -- of the transcripts that I have here?

MR. BYRON WILLIAMS: Yes, and -- and if you're looking for some -- if you're looking for some references, Mr. Johnston, just on page 1,180 near the bottom, line 22, you can see he's speaking about the -- the audit -- the audit role. And likewise at the top of page 6, again you'll see speaking of the -- of the...

(BRIEF PAUSE)

MR. BYRON WILLIAMS: And, Mr. Johnston, if this is making you feel uncomfortable in this way, I can actually ask the questions a different way, and maybe that would -- and maybe I'll try it a different way if -- if that -- if that works better. Go ahead.

MR. LUKE JOHNSTON: Yeah, I apologize, I just want to, of course, feel comfortable reading through the material and understanding it before I give an answer.

MR. BYRON WILLIAMS: Well, let me try it a different way and then we may come back to it or -- or we may not.

Maybe we'll try it -- the -- the simplest way, Mr. Johnston, is for you to describe in terms of the review of claims liabilities what -- what you understand to be the role of the external auditor and -- and the consulting actuary. And really are they comment -- the question I'm putting to you, Are they commenting on the reasonableness of the overall estimate? Is -- is that what they're opinion is ultimately grounded in? That's the type of in -- insight I'm seeking from you, sir.

(BRIEF PAUSE)

MR. LUKE JOHNSTON: Sorry, can you -- can you repeat the question, please?

MR. BYRON WILLIAMS: I can't, because it was a poor question, but we'll try -- we'll try again. Within -- you -- you spoke the first day of the Hearing and again this morning of the role of the auditor in terms of a check and balance.

In terms of the actuarial liabilities and the report of the external actuary, what is the role of the auditor? Is it to comment on the overall reasonableness, is it to dissect line-by-line?

What does that auditor's signature mean, sir?

(BRIEF PAUSE)

MS. KATHY KALINOWSKY: I'm sorry, we're having a little bit of difficulty in -- in responding to this question. Over the past, I believe it's two (2) years, both KPMG -- KPMG attended and they provided evidence, particularly Mr. Neil Parkinson (phonetic) provided evidence as to what the role of the auditor is in that state -- in preparing the financial statements. And in -- particularly the role of the ex -- the -- the auditor's actuary in auditing Guideline 43, I think the number is.

That's been put on the record two (2) years now. And if Mr. Williams would like me to produce those documents I certainly could again for the -- the Board.

MR. BYRON WILLIAMS: Recognizing we have a new panel, or a -- a newer panel, I would ask Manitoba Hydro to undertake to just provide a -- a summary of -- of those documents. I'm not looking for anything particularly extensive. I --

MS. KATHY KALINOWSKY: Sure, we can provide something then which will outline Mr. Parkinson's evidence on that.

MR. BYRON WILLIAMS: And for the court reporter, the -- the undertaking then is to outline Mr. Parkinson's evidence in terms of his role and the role of the consulting actuary.

--- UNDERTAKING NO. 15: MPI to outline Mr. Parkinson's evidence in terms of his role and the role of the consulting actuary

MS. KATHY KALINOWSKY: Yes.

(BRIEF PAUSE)

CONTINUED BY MR. BYRON WILLIAMS:

MR. BYRON WILLIAMS: Mr. Johnston, let's -- let's hope I don't stretch anyone's memory too much here, although Ms. Kalinowsky clearly has a better one than I do.

Would it be accurate to say that to your knowledge there is at least one (1) occasion where the external auditor for MPI found that the overall estimate of claims liabilities of the external actuary to be reasonable, even while finding certain specific estimates for particular lines of business to be beyond the range of reasonableness?

(BRIEF PAUSE)

MR. BYRON WILLIAMS: And if you're -- if -- if MPI is looking for a -- a reference, I'm referring to the consulting actuary's April 2010 report.

MS. MARILYN MCLAREN: Which the consulting actuary provided to KPMG, which the Corporation learned about when KPMG agreed to make it public for the proceedings two (2) years ago. So I --

I believe that that's a reasonable characterization of what that KPMG internal letter, which became public though these processes, said.

MR. BYRON WILLIAMS: Okay. So thank you. That's a yes. I appreciate that. Your head nodding, I guess, means a "yes," Ms. McLaren?

MS. MARILYN MCLAREN: Well, I think I used the words "I believe that's a reasonable characterization," so that's --

MR. BYRON WILLIAMS: Fair enough.

MS. MARILYN MCLAREN: -- pretty clear.

MR. BYRON WILLIAMS: Mr. Johnston, it probably goes to you and if it should go to Ms. Reichert, you'll just steer me the other way. I -- I want to chat with you about the Corporation's forecast for inflation and for interest rates in just a moment.

But before I do, I wonder if you can indicate whether you or any of your actuarial colleagues are aware of or have had the opportunity to review the PowerPoint presentation to the Canadian Institute of Actuaries dated September 27th, 2012, titled -- by Jonas Fisher of the -- F-I-S-H-E-R of the Federal Reserve Bank of Chicago on the topic of whither, W-H-I-T-H-E-R, US growth.

Are you aware of that document or have

you -- have you had occasion to see it, sir?

MR. LUKE JOHNSTON: I have not seen that document yet.

MR. BYRON WILLIAMS: So for the time being we'll restrict ourselves to whither Manitoba CPI or whither Canadian interest rates.

Mr. Johnston, you probably know this off by heart, but if you're looking for a reference in CAC Exhibit 5, it's page 7 in the top -- top right-hand corner.

MR. LUKE JOHNSTON: I'm there. Thanks.

MR. BYRON WILLIAMS: And again, I don't want to -- to walk too far down the path my Learned Friend, Ms. Grammond, walked upon last week.

But in terms of forecasting CPI or interest rates, my understanding of your evidence last week, Mr. Johnston, is that neither you or the Corporation profess to have any particular expertise as compared to the major banks or professional forecasting agencies in forecasting inflation rates, for example?

MR. LUKE JOHNSTON: Perhaps my words were not the greatest description. But I -- I think we -- we definitely have forecasting expertise in -- internally. But to believe that -- that we have better information or -- or can do a better job of forecasting inflation than the banks and pro -- professional forecasting agencies would probably be a stretch.

MR. BYRON WILLIAMS: So, essentially, for the purposes of forecasting interest rates, you rely on the major banks or -- or professional forecasting agencies?

MR. LUKE JOHNSTON: That's correct.

MR. BYRON WILLIAMS: And you...

And I'll get to Ms. McLaren's question. And that goes for inflation, too, Mr. Johnston?

MR. LUKE JOHNSTON: Yes, that's correct.

MR. BYRON WILLIAMS: And generally, without trying to get into too many details, you select a median forecast from these banks and forecasting agencies, correct?

MR. LUKE JOHNSTON: Yes, that's correct.

MR. BYRON WILLIAMS: Now, if we look at inflation as measured by year-over-year change in the consumer price index, last year was a -- to -- being 2011, was a bit of a tough year in Manitoba, with inflation at -- in the range of 3 percent.

Is that correct, sir?

MR. LUKE JOHNSTON: Yes, that's correct, as per the page 7 in your re -- in your reference material.

MR. BYRON WILLIAMS: And that, of course, was driven by high energy prices, coupled with high food prices, correct?

MR. LUKE JOHNSTON: I believe that's a reasonable explanation as, again, per that paragraph.

MR. BYRON WILLIAMS: And going out in time, the Corporation, for -- for the entire forecast period presented in this Rate Application, the Corporation is -- is forecasting more moderate CPI at 2 percent per annum.

Is that right, sir?

MR. LUKE JOHNSTON: Moderate relative to the -- to the last year, but basically completely in line with the last twenty (20) years before that -- pardon me -- on average.

MR. BYRON WILLIAMS: Thank you for that, Mr. Johnston. As compared to 2011, your inflation forecast is about 33 percent lower for the foreseeable future, correct, compared to the actuals for 20 -- 2011, sir?

MR. LUKE JOHNSTON: Yes. So two (2) relative to three (3) is about 33 percent lower, yeah.

MR. BYRON WILLIAMS: You didn't trust my math, did you, Mr. Johnston? I'm just teasing. Go ahead.

(BRIEF PAUSE)

MR. BYRON WILLIAMS: Just again, if you're trying to follow along in the excerpts from the record, just looking at pages 8 through 11 from the CAC book of documents, Exhibit number 5, we've discussed the methodology.

And -- and really starting at page 9, if I were to -- to -- you'll agree with me, Mr. Johnston, that presented in the -- the middle of this page are the interest rate forecasts for the government of Canada, ten (10) year bonds?

Do you see that, sir?

MR. LUKE JOHNSTON: Yes, I do.

MR. BYRON WILLIAMS: And recognizing that the Corporation tends to rely upon the median -- M-E-D-I-A-N -- if I were to looking at the Corporation's interest rate forecast for the Government of Canada ten (10) year bonds, I would see the Corporation expects an increase in interest rates going forward.

Would that be fair?

MR. LUKE JOHNSTON: That is what we're forecasting. But again, it's -- it is the expectation of the banks listed in -- in the table.

MR. BYRON WILLIAMS: And you rely upon that -- those -- those expectations for the purposes of your forecast?

MR. LUKE JOHNSTON: Yes, we do.

MR. BYRON WILLIAMS: And, likewise, we see a -- when we focus on Treasury bills at the bottom of that page again, we see a expectation presented in the Corporation's forecast of an increase in interest rates going forward, correct?

MR. LUKE JOHNSTON: Correct.

MR. BYRON WILLIAMS: And, not needing to go into the details, but when we look farther out in time, again, we see the Corporation forecasting, over time, a fairly robust growth in interest rates, correct?

MR. LUKE JOHNSTON: Yes, I -- I won't pretend to have knowledge of the -- how they set their forecasts at the banks, but the tendency is that as the -- we go longer into the future, it reverts closer to the historical long -- longer-term average.

MR. BYRON WILLIAMS: This may go to Ms.

-- excuse me -- Ms. Reichert or to Mr. -- Mr. Johnston. And I do want to understand, again without trespassing too much where my friend Ms. Grammond went, the impact of higher interest rates on both the income and costs of MPI. But before I get there, I -- I'd like to use a simplified example to assist both my client and -- and myself in understanding.

So I -- I'd like you to turn to CAC Exhibit number 6. And, Ms. Reichert, before we go into the -- the nitty gritty of this simplifized (sic) illustration, I wonder if we can agree on a definition of "discount rate"?

If I suggested to you that for the purposes of this discussion, a discount rate represents the interest rate used in discounted cash flows analysis to determine the present value of future cash flows, is that something you could agree with?

MR. LUKE JOHNSTON: I can agree with that.

MR. BYRON WILLIAMS: Essentially, the discount rate takes into account the time value of money?

Would that be fair?

MR. LUKE JOHNSTON: That's fair.

MR. BYRON WILLIAMS: And when we think

of the time value of money, we mean the idea that money available now is worth more than the same amount of money in the future?

Would that be fair?

MR. LUKE JOHNSTON: That's fair.

MR. BYRON WILLIAMS: And it means more for, I'm going to suggest to you, Mr. Johnston, for a couple of reasons: A) it could be earning interest; and B) there's always risk or uncertainty associated with anticipated future cash flows.

Fair enough?

MR. LUKE JOHNSTON: That's fair.

MR. BYRON WILLIAMS: Now, we're going to be moving to the absolute limits of my mathematical ability. Let's say one expects a thousand dollars in one (1) year's time, Mr. Johnston.

Could you assume that for me, just for the purpose of -- of an example?

MR. LUKE JOHNSTON: Expects one thousand dollars ($1,000) in a year's time?

MR. BYRON WILLIAMS: Yes. To determine the present value of that one thousand dollars ($1,000), what it's worth today, you'd need to discount it by a particular rate of interest.

Would that be fair?

MR. LUKE JOHNSTON: That's fair.

MR. BYRON WILLIAMS: And, for the panel, we're not yet at the -- at the table, obviously. I'm just trying to make sure Ms. Desorcy and I are on the same page as Mr. Johnston.

So assuming a discount rate of 10 percent, the one thousand dollars ($1,000) in a year's time would be the equivalent of nine dollars ($9.00) -- nine (9) -- nine hundred and nine dollars ($909), excuse me, and nine (9) cents today.

Would you agree with that, sir?

MR. LUKE JOHNSTON: I'd agree with that. So, yeah, if -- if you -- if you put nine hundred dollars and nine cents ($900.09) in your bank account right now, and are fortunate enough to get 10 percent interest, that'd be a thousand dollars ($1,000) by the end of the year.

MR. BYRON WILLIAMS: Well, I said it was Mr. -- simplified, Mr. Johnston. Why don't we talk about 2 and 3 percent interest rates instead. And let's look at this simple illustration. And, Mr. Johnston -- we probably -- we should have done it in larger font for Ms. Desorcy, but hopefully she can read it. I'm having to raise my glasses here.

I'm going to ask you to make two (2)

assumptions. One is at -- at the top we're going to assume that we're purchasing a bond that's under -- beside the number 1 on January 1st, 2012, for 100 million at par with the coupon rate of 2 percent paying semi annual interest payments, and that this bond will mature in three (3) years.

Do you see that, Mr. Johnston?

MR. LUKE JOHNSTON: Yes, I do.

MR. BYRON WILLIAMS: Okay. And again we're not suggesting this is the reality of Manitoba Public Insurance, we're just doing this for illustrative purposes.

So if we see under the -- this bond trading at par, would -- I'll suggest to you that -- Mr. Johnston, that -- that this is the status quo with a value of 100 million, a coupon rate of -- of 2 percent, a time to maturity of three (3) years, and a current yie -- yield of 2 percent with the price allowing for some vicissitudes in supply and demand of $100 million.

Do you see that, sir?

MR. LUKE JOHNSTON: I do. So the -- the price is again the same because in this case the -- the amount of interest you're receiving is equivalent to the -- the yield rate of two (2) and 2 percent.

MR. BYRON WILLIAMS: And just before we leave the status quo for the bond, I'd ask you to direct your attention to the -- the right side of the table, and you'll see a headline, "Payment Pattern."

Do you see that, Mr. Johnston?

MR. LUKE JOHNSTON: Yes, I do.

MR. BYRON WILLIAMS: And this is essentially how the semi-annual interest payments are being paid out. That's what this is intended to -- to represent.

Is that correct, sir?

MR. LUKE JOHNSTON: That's right. The -- the semi-annual payments, and then one (1) large payment of a coupon and principle at the -- on the last day.

MR. BYRON WILLIAMS: Thank you for that. Going now to kind of the num -- or to the number 2, again we're asking the reader to assume an unpaid claim reserve of $100 million -- of $100 million was incurred on January 1st, 2012, and will be paid in three (3) years, and that the unpaid claims liability will be discounted based on the bond rates.

Do you see that, Mr. Johnston?

MR. LUKE JOHNSTON: Yes, I do.

MR. BYRON WILLIAMS: And going to the

discounted at 2 percent column. Again you see the undiscounted value of $100 million, you see the interest rate of 2 percent, the years to payment of three (3), and the discounted value calculated, for illustrative purposes, to be just a bit over $94 million.

Do you -- do you see that, Mr. Johnston?

MR. LUKE JOHNSTON: Yes, I do, and similar to your above calculation where we talked -- or pardon me, not your above calculation, but the calculation where we talked about the thousand dollars ($1,000). In this case, $94 million today growing at 2 percent a year will equal the approximately $100 million by the third year.

MR. BYRON WILLIAMS: Thank you for anticipating my question. I appreciate that. So when we move to the trading -- or to the trade net discount, or the discounted at 3 percent column, let's go up -- back up to the bonds.

And again we're asking the reader to assume that there's been a 1 percent increase -- increase in interest rates on the market value of a bond, and a discounting effect on unpaid claims reserves.

So, Mr. Johnston, looking at the trading in discount, if we compare the -- that column to the trading at par we see two (2) different -- two (2) differences. One is the current yield which is 1 percent higher, and one is the price which is lower, suggesting the bond is -- is less valuable.

Do you see that, sir?

MR. LUKE JOHNSTON: Yes, I do, and now we're in a situation where the required yield is higher than the coupon payment interest rate. So in order to achieve that 3 percent yield, the bond needs to be priced a lower amount. Calculations are a bit more complicated now with all the cash flows, but that's the idea.

MR. BYRON WILLIAMS: And if we go down to the unpaid claim discounted at 3 percent, we again see that the interest rate is different and that the discounted value is somewhat lower than it was before.

Do you see that, Mr. Johnston?

MR. LUKE JOHNSTON: That's right. Now, you -- you don't need as -- as much money put aside today now that you're expecting a higher interest rate.

MR. BYRON WILLIAMS: So there's good news on the claims liability side from the 1 percent increase in interest rates and not as good news on the -- the bond side.

Would that be fair, sir? Flowing from the 1 percent increase.

MR. LUKE JOHNSTON: That's fair.

MR. BYRON WILLIAMS: And it doesn't come out perfectly in the -- the wash in that in this simplified illustration, the -- there -- there's a sixty-eight thousand dollar ($68,000) decrease in net income.

Is that right, sir?

MR. LUKE JOHNSTON: Yes, and we -- we talked -- actually, I'll just say yes for now. I'll let you ask a question.

MR. BYRON WILLIAMS: You were doing better than my -- my questions, Mr. Johnston, and I'm not trying to burden you much farther. But -- so there's a rough matching, but there's not certitude in -- in terms of the bottom line.

The -- the impacts are -- are still somewhat uneven?

MR. LUKE JOHNSTON: That's correct. And all -- all I was going to say is this is essentially the -- a similar idea as we talked about, asset liability matching. And in the -- in our reality it won't be even as clean as this or as accurately matched as this. But again, we hope to get that fairly close.

MR. BYRON WILLIAMS: Mr. Chairman, I can continue or we can take our -- our break. I have a -- I do have some questions I need to ask of my client, so if there's an appropriate time.

THE CHAIRPERSON: Is fifteen (15) minutes enough? Let's take fifteen (15) minutes, so back in this room at, say, five (5) to -- five (5) to 11:00.

--- Upon recessing at 10:38 a.m.
--- Upon resuming at 10:55 a.m.

CONTINUED BY MR. BYRON WILLIAMS:

MR. BYRON WILLIAMS: Mr. Johnston, we're -- Mr. Johnston -- oh, sorry.

MS. KATHY KALINOWSKY: If Mr. -- prior to the cross-examination, Mr. Johnston just wants to make a comment with respect to one of the responses that he gave just prior to the break, if that's all right with you, Mr. Williams.

MR. BYRON WILLIAMS: Absolutely.

MR. LUKE JOHNSTON: Thank you. I didn't -- on -- on CAC Exhibit 6, I -- I didn't notice the -- the wording used, but it says it characterizes the difference in the -- in the asset and liability matching here as immunization ineffectiveness.

I don't know if that wording is intentional, but the -- this cash flow pattern shown here is fairly simplified. We could match this 100 percent and be 100 percent immunized if we purchase the right type of bond.

But I -- I don't want to understate -- I don't want in any way for this to understate the importance of our asset and liability matching program. We have evidence that -- that shows that our program matches about 80 to 90 percent of -- of these changes.

And if you think about changing these numbers here to amounts in billions, and you think about the impact of interest rates increasing and massive changes in asset values you can -- you can see the importance of having the -- the offset on the liabilities side to match that even if it's not perfect.

Eighty (80) to 90 percent is, you know, clearly better than some -- some number much lower than that or not matched at all. So I just wanted to make sure that was clear. And I didn't want our -- our asset liability program in any way to be seen as ineffective.

CONTINUED BY MR. BYRON WILLIAMS:

MR. BYRON WILLIAMS: And, Mr. Johns -- Mr. Johnston, I think those words escaped my attention too, so I don't think there was a plan. The -- I do want to talk about your asset and liability management program. Before I get there I do want to make sure I understand your definition of "actuarial present value".

As I understand it, actuarial present value is:

> "A sum of future payments discounted at an interest rate determined from the balance sheet yield of the Corporation's portfolio with provisions for adverse deviation, for example, claims development, uncollectible reinsurance, and investment return rate."

Would that be fair, sir?

MR. LUKE JOHNSTON: That's fair.

MR. BYRON WILLIAMS: And flowing from that definition and in terms of how assumptions relating to interest rate levels might aflect -- affect claims liabilities, would I be correct in suggesting that one way would be in the assumed discount rate?

MR. LUKE JOHNSTON: Can you rephrase that, please, sorry, or simply repeat it?

MR. BYRON WILLIAMS: If we're trying to understand how assumptions relating to interest rates might affect claims liabilities, and going back to that definition of actuarial present value, one (1) way in -- in which that might occur is in -- in terms of the assumpt -- the dis -- the interest rate in -- at which it is dis -- discounted.

Fair enough?

MR. LUKE JOHNSTON: Yes, sorry. Yeah, a very -- a very key factor is the discount rate assumed in that calculation.

MR. BYRON WILLIAMS: Yes. And, Mr. Johnston, you don't have to apologize for my poor questions. The -- another factor in -- in which investment -- expectations in terms of investment return rate might affect the assumption in terms of -- or the estimate in terms of claims liability would be in terms of the provision for adverse deviation of the investment return rate, correct?

MR. LUKE JOHNSTON: That's correct.

(BRIEF PAUSE)

MR. BYRON WILLIAMS: And, Mr. Johnston, you were so -- so keen to talk about your asset management plan. If the Board is following around in -- along in CAC Exhibit number 5, there's an excellent information request at page 11, or the response is excellent even if the request was not so much. That's CAC-2-74 in the top right-hand corner.

But, Mr. Johnston, the point you made right after the break was that as -- as interest rates change in future years, to a significant extent the -- the Corporation's assets and liabilities will -- and their management program will result in offsetting changes to assets and liabilities. That's the intent of the program?

MR. LUKE JOHNSTON: Yeah, significantly off -- offset impacts. I -- I spoke last week, I believe, that the Department of Finance has some leeway in how they match assets to the liabilities, that being to keep the asset duration within plus or minus two (2) years.

MR. BYRON WILLIAMS: And, essentially, the goal of this program is to reduce volatility in -- in the changes -- in the relative changes of the value of assets and liabilities. Would that be fair -- due to interest rate cho -- changes?

Let me try that again. Essentially, the goal of this program is to reduce the volatility due to interest rate changes in the relative value of assets and liabilities. Would that be fair?

MR. LUKE JOHNSTON: That's fair.

MR. BYRON WILLIAMS: And if we look at this specific example, we're starting with the premise at the top, in the preamble, of unpaid claims in the range of $1.49 billion and a fixed income portfolio valued at $1.5 billion. And what this response outlines is that a hundred basis point decrease in the market yield results in a increase in the present value of the bou -- bond portfolio by about $78 million, and an increase in the present value of the liabilities by some 58 million, correct?

MR. LUKE JOHNSTON: That's correct.

MR. BYRON WILLIAMS: In this case, the Corporation's a bit better off with the hundred basis point decrease, in that the value of the bond portfolio's increase outweighed the increase in the present value of the liabilities, correct?

MR. LUKE JOHNSTON: That's true. I won't -- I'm not sure if the -- why a hundred basis point decrease was used. That's maybe not that realistic, but if -- if that particular impact happened, that would -- that would be the expected impact on -- on both assets and liabilities, yes.

MR. BYRON WILLIAMS: In this particular example, there certainly is a -- a mitigation of the impact, but there's -- given, perhaps, the size of the basis point change there still is a fairly material impact in terms of volatility, though, some 20 million?

MR. LUKE JOHNSTON: Yes, that's fair. Twenty (20) million dollars, of -- of course, would be considered material to -- to me. Again, we -- we don't expect to be fully immunized, but significantly.

MR. BYRON WILLIAMS: And just going the other way, Mr. Johnston, if we could -- and I don't need a -- a calculation from you, but directionally a hundred point basis -- a hundred basis point increase in the yield on the Corporation's marketable bond portfolio, would result in a decrease in the present value of the bond portfolio and a decrease in the present value of the liabilities.

Is that correct?

MR. LUKE JOHNSTON: Directionally, yes, that's correct.

MR. BYRON WILLIAMS: And just for the clarification of -- of my client, just because the decrease made a -- a twenty (20), or 19.7 million difference one way, we wouldn't necessarily expect the same proportionate change the other way? Is that correct, Mr. Johnston?

MR. LUKE JOHNSTON: No, you wouldn't. The -- the larger the changes in interest rates, the more they -- they deviate. We are looking at a particular point in time, of -- of course. The Corporation wouldn't stand still as interest rates gradually rise. We would expect it to, you know, manage our -- our asset -- assets and liabilities appropriately. But the -- the changes aren't necessarily the same for a -- a plus fifty (50) or a hundred basis points, or -- or minus fifty (50) to a hundred basis points.

(BRIEF PAUSE)

MR. LUKE JOHNSTON: I -- I'm just looking for a reference where I think I actually answer that question. One second.

(BRIEF PAUSE)

MR. BYRON WILLIAMS: It's not CAC-1-73. Shall I wait, Mr. Johnston?

(BRIEF PAUSE)

MR. LUKE JOHNSTON: Yes, please.

(BRIEF PAUSE)

MR. BYRON WILLIAMS: It may well be...

(BRIEF PAUSE)

MR. LUKE JOHNSTON: In PUB-1-17 Part C, we were asked to basically show a plus or minus 0.5 percent change in the discount rate for liabilities. And when interest rates decrease by half a percent, the liabilities went up by about $50 million. And when the rate increased, the liabilities went down by about 75 million.

So the changes are not uniform on each side but keeping in mind that it's also the -- the percentage change in the -- in the yield, like on an absolute basis, is not the -- the same either. Dropping from two (2) to one and a half (1 1/2), for example, is not necessarily the same percentage change as going from two (2) to two and a half (2 1/2).

MR. BYRON WILLIAMS: Thank you, Mr.

Johnston, and I'm sorry I misdirected you on the response. Just in terms of conceptually, the asset management strategy stands separate and apart from the actuarial calculation of the provision for adverse deviation. There's no mathematical relationship.

A change in one won't affect -- affect the other?

(BRIEF PAUSE)

MR. LUKE JOHNSTON: To -- I -- I believe you're asking, correct me if I'm wrong: Was the effectiveness of our actu -- asset and liability matching program a consideration in the selection of the interest rate PFAD? No, it was not.

(BRIEF PAUSE)

MR. BYRON WILLIAMS: Mr. Johnston -- and I'm going to ask the -- your indulgence and the indulgence of the Board -- directing your attention to, in the top right-hand corner, page 15 of the CAC Exhibit 5, which is an excerpt of a transcript and, really, a very interesting conversation you had with Ms. Everard -- or, Ms. Grammond, excuse me, about the -

- the impact -- well, excuse me, in terms of the decision-making relating to the decision to increase the PFAD for the interest rate margin by twenty-five (25) basis points.

Without asking you to remember the details as -- as of yet, Mr. Johnston, you remember the conversation?

MR. LUKE JOHNSTON: Yes, I do.

MR. BYRON WILLIAMS: And I want to -- to walk you through some of the highlights of that conversation from my perspective.

And just directing your attention to the -- again to page 15, in the top right-hand corner page 45 of the transcript, we -- we see a -- a conversation in which you indicate that in terms of the pre -- PFAD provision, you didn't go to the new appointed actuary and ask for an increase in the provision for the interest rate margin.

Is that correct, sir?

MR. LUKE JOHNSTON: That's correct.

MR. BYRON WILLIAMS: He presented a case to you which you considered fairly compelling. The change was made with a -- roughly a $33 million impact.

Would that be fair?

MR. LUKE JOHNSTON: Yes, that's fair.

MR. BYRON WILLIAMS: And just directing your attention, Mr. Johnston, to -- to page 16 at the bottom now of the transcript, lines 23, 24, and 25, then moving on to the next page, I'll suggest to you here that, notwithstanding the move to one hundred and twenty-five (125) basis points, you're suggesting in -- in this passage a significant fondness for the one hundred (100) basis points perspective, in that you found that very reasonable.

Does that sound fair, sir?

MR. LUKE JOHNSTON: Yes, that's fair.

(BRIEF PAUSE)

MR. BYRON WILLIAMS: And, Mr. Johnston, why I found the conversation so intriguing is you -- you just kept going on and going on. And I direct your attention to page 18 at the bottom, where you're suggesting that you're going to go back -- line 17 to 25, that you're -- that -- that when you -- when the actuary goes back in the -- in October, he may decide that this $33 million adjustment is no longer required and that you're going to expect your appoint -- the appointed actuary to provide evidence for why the margin needs to remain at 1.25 percent.

Do you see that, sir?

MR. LUKE JOHNSTON: Yes, that's correct. I -- clearly, this is a -- a fairly significant change, in terms of dollars. So I just wanted the Board to understand the process of how we got to that assumption change, how it was brought forth, why I -- I believe that our -- our prior assumption was reasonable, and -- and why I was convinced by the evidence from our appointed actuary that the margin should -- should increase.

Again, and if -- if -- all I was stating in this section was that if -- it would be my expectation that if -- if our appointed actuary was to use the -- the evidence that they did to support increase in that margin, if that evidence no longer existed, I wouldn't -- it wouldn't be my expectation that that margin would remain at that level.

Again, that is the -- that's the judgment from our appointed actuary, but those are my comments.

MR. BYRON WILLIAMS: And, Mr. Johnston, you kind of finished off that same passage saying, line 25: "That's all I can really say."

Do you see that?

MR. LUKE JOHNSTON: I -- I don't remember the exact contents -- context, but I was in a discussion about -- that -- that again, this assumption is -- is somewhat reasonable and -- and, as I've just described, those are my expectations on how I would expect the process to go at the -- at the next -- at the next review. So that's all I can really say about -- about that issue.

MR. BYRON WILLIAMS: And then just directing your attention to the next page, Mr. Johnston, because it wasn't all you could really say. You had to say more. And you're back there defending that 1 percent and -- and offering the perspective that you think it's reasonable for such a long-tailed business as MPI.

Do you see that?

MR. LUKE JOHNSTON: Yes, I do.

MR. BYRON WILLIAMS: Mr. Johnston, you strike me as a very confident and eloquent person.

But would I be correct in suggesting to you that you're not very confident that the one hundred and twenty-five (125) basis point PFAD should be maintained?

(BRIEF PAUSE)

MR. LUKE JOHNSTON: I -- I think I've stated why I'm confident in -- in the -- the new selection. I don't, of course, want to say that I thought of it, because I didn't. And, yeah, as I've -- as I've mentioned, I thought the -- our appointed actuary made a strong case to change it and -- and I wa -- I was okay with that approach.

All I'm saying is that, to be confident again, I'll expect that same level of -- of detail from our appointed actuary and the same -- same rationale.

MR. BYRON WILLIAMS: And you stated previously that you -- you'd expect that same level of detail or -- or evidence.

And, in essence, the -- the evidence that the external actuary relied upon was higher inflation and lower trending interest rates, correct?

(BRIEF PAUSE)

MR. LUKE JOHNSTON: Tha -- that's correct. I just wanted to have the reference. And that's the appointed actuaries report from October, AI-11. And in -- on page 48 we see the -- the real return at 3.3 percent in October. My apologies, I'll let you get to that spot.

MS. CANDACE GRAMMOND: I think it's actually AI-10. I think you said AI-11, Mr. Johnston.

MR. LUKE JOHNSTON: Thank you.

MS. CANDACE GRAMMOND: Mr. Pelly pointed that out, so I'm not taking credit for it either.

(BRIEF PAUSE)

MR. LUKE JOHNSTON: So that again is the -- the middle table in -- on page 48 of AI-10, the October review. So in this -- in this table, like, well, you see the -- the real return ranging from a high of about 4.02 percent in October, '09, to a low of 0.67 percent in October, 2011.

My understanding of the appointed actuary's view is that both the variability in these numbers and the very significant low number as of October 2011, are the -- the main rationale for increase in the PFAD.

CONTINUED BY MR. BYRON WILLIAMS:

MR. BYRON WILLIAMS: And just to go back, and I belie -- in -- in terms of my question and -- and recognizing the nuance you put onto it, but the

-- the drivers of that, his concern were volatility coupled with high inflation and lower trending interest rates.

Fair enough?

MR. LUKE JOHNSTON: I think that's fair, yeah.

MR. BYRON WILLIAMS: And it would be accurate to say that when MPI surveys current forecasts of leading banks it can -- it can see that they are forecasting significantly lower inflation for Manitoba than last year?

(BRIEF PAUSE)

MR. LUKE JOHNSTON: I -- I haven't looked at the -- in detail at the latest inflation forecasts from the bank. We will, of course, get a -- get an update on these numbers in October. But I haven't -- haven't reviewed an updated interest rate forecast as -- as you -- of -- you -- you would see in our evidence in -- in TI.18, for example.

MR. BYRON WILLIAMS: Even the -- the Corporation's forecast is significantly lower than the actuals for last year, sir?

MR. LUKE JOHNSTON: The Corporation's

forecast has been at or very close to 2 percent for a while now. The -- there has been very signif -- significant variability in recent years, ranging from almost no inflation - zero point six (0.6) or four (4), I believe, up to 3 percent in -- in the latest year.

Throughout that whole period, the forecasts that the Corporation has received from the banks generally indicated about 2 percent in -- in all cases. So the -- that's what we're forecasting, based on the information we have. But it -- it can still definitely be variable, as we've just seen over the last few years.

MR. BYRON WILLIAMS: And we may resume this conversation tomorrow, Mr. Johnston. Certainly, it's also fair to say that the banks are generally forecasting a modest growth in -- in interest rates, correct?

MR. LUKE JOHNSTON: Yes, I believe you have evidence there showing that, in particular. But a modest growth in interest rates in the short term, accelerating more in the -- in the longer term.

MR. BYRON WILLIAMS: Moving on, Mr. Johnston, and to -- for the panel, to page 20 in the top right-hand corner of CAC Exhibit number 5.

Mr. Johnston, I don't know if I scrawled over your copy like I -- I did in mine, but I am directing your attention -- this is an excerpt you'll see from your pre-filed evidence of June 15th, 2012, correct?

MR. LUKE JOHNSTON: That's correct.

MR. BYRON WILLIAMS: And in particular, I want to direct your attention to the -- the second paragraph and the discussion beginning, "As of February 29th, 2012." And without meaning to read it all to you, you see the Corporation was concerned about a relatively low equity return forecast. And then I do want to read this sentence:

"The Corporation believes that such a forecast is inapp -- inappropriate, given the average annual return of the Toronto Stock Exchange brackets] (TSX) over any rolling twenty (20) year [in brackets] (i.e., long term) period has never been below 5.2 percent."

Do you see that, Mr. Johnston?

MR. LUKE JOHNSTON: Yes, I do.

MR. BYRON WILLIAMS: You see the Corporation is proposing to add a minimum equity return. And then again drawing your attention to the next sentence:

"The proposed minimum is based on the 5th percentile of annual returns on the TX -- TSX, over all rolling twenty (20) year periods."

Do you see that, sir?

MR. LUKE JOHNSTON: Yes, I do.

MR. BYRON WILLIAMS: And the Corporation is making some -- some powerful statements, in terms of the -- the average annual return never being below 5.2 percent and -- and the proposed minimum being based on the 5th percentile of annual returns on the TSX, over all rolling twenty (20) year periods.

We're agreed on that?

MR. LUKE JOHNSTON: Yes, that -- that's what it says in that paragraph.

MR. BYRON WILLIAMS: In terms of the -- the basis -- and if you need a reference, Mr. Johnston, it's the next page.

But in terms of the basis for those -- those statements that it had never been below 5.2 percent and it was over all rolling twenty (20) year periods, so focus -- am I correct in suggesting to you that those statements were based upon an analysis of the Standard and Poor's TSX composite to -- composite total return index from 1956 to February 29th, 2012?

Is that right, sir?

MR. LUKE JOHNSTON: Yes, that's correct. And my understanding is that is the available range for that index in -- in the Bloomberg investment system that we use. I -- I don't pull the data, but perhaps I could get the details of that for you. I -- I don't know the -- the details.

MR. BYRON WILLIAMS: I'm not sure it's particularly necessary. Mr. Johnston, I'm just wondering -- and perhaps you've already answered that.

The Corporation went back to 1956; why not go back to 1919?

(BRIEF PAUSE)

MR. LUKE JOHNSTON: I'd have to get back to you on the -- like to confirm that the -- that was indeed related to the Bloomberg system, but I -- I can do that.

(BRIEF PAUSE)

THE CHAIRPERSON: Do you mind if I ask a few questions here? And I think I understand where

Mr. Williams is coming from. I guess here the -- the statement -- or, pardon me, the document seems to suggest that, you know, we've never seen anything below 5.2 percent. And the apparent dichotomy here is between what you're using for DCAT and what's being -- what -- what's included in this statement. In other words, we never got below 5.2 percent and then on the DCAT we're saying we could go as low as 40 percent loss on the -- so there's a bit of a dichotomy there.

And -- and I guess the other dichotomy that I can see is that you're using return -- index returns for this statement but you're using portfolio managers who are not using index returns. They're -- they're using their own results, I guess, which -- which on the face of it appear to be lower than what the index has been generating over -- over the years.

So two (2) -- two (2) places where I see a bit of a dichotomy, and I just what to understand your thinking there.

MR. LUKE JOHNSTON: I'll talk first on the -- on your first question which relates to the -- the issue between the DCAT assumptions and -- and the assumptions used to set our equity return forecast.

So the issue around our equity return assumption is to get a reasonable long-term equity return forecast in -- in our -- in our GRA. We -- we don't attempt to -- there's -- there's a wide variety of opinions on what equities are going to do next year or the year after, and there's no -- at least to my knowledge, no reasonable method of taking the average of a bunch of peoples different assumptions and including that in our forecast.

So we -- when we looked at our existing method for equity forecasting we used a equity risk premium of the -- of 1 1/2 percent above the Canadian ten (10) year bond yield. And recognizing that these yields are at some of their lowest levels in history, we looked at the output from that exercise and said, Is it -- is it really reasonable for the Corporation to -- to forecast a 4.8 percent equity return in the GRA.

So we went through an exercise of saying, What is a reasonable long-term return based on the data we had available. And we judgmentally selected twenty (20) years as a -- as a reasonable period of time. And it's over that -- over rolling twenty (20) year periods we've seen that the return as the -- again, the never falling below 5.2 percent compounded return, and the 5th percentile at six point one (6.1).

So that piece was the evidence we needed to say that, you know what, four point eight (4.8) -- we could just blindly apply our existing way of forecasting but that wouldn't really, you know, relate to the history that's -- that -- that we have. So we -- we made a proposal to change that to use this minimum equity return, and -- and so we got a much more reasonable forecast in there.

Relating to the -- the DCAT, there's a -- very different reasons for the -- the two (2) assumptions. So one -- one we're looking at a -- the long-term equity return. And we see that we have some fairly consistent results over longer terms.

For the DCAT we're looking at shocks, significant declines over the period that's applicable to MPI's rating. So that's -- that's great if we can earn a 5.2 percent return over twenty (20) years. And this -- this data is suggesting that it's -- it's likely. But there are ups and down -- significant ups and downs in there. And we're trying to protect in the RSR is the impact on ratepayers from those significant increases and -- and decreases.

So if we were to look at, as we've done in the DCAT, shorter snapshots of equity returns, you'll see periods where it's been down forty (40) and periods where it's been up forty (40), all working out to this 5.26 percent or so average yield over time. So I think two (2) very different -- different purposes. And that -- that, hopefully, explains where we're coming from there.

I just need a moment to respond to your second question.

(BRIEF PAUSE)

MS. MARILYN MCLAREN: Maybe if I could, Mr. Chairman, different -- come at the same information a little bit different perspective while Mr. Johnston gathers his thought on the second question.

If I can paraphase -- paraphrase the question, it's: Why are you making such fundamentally different assumptions about equities in these two (2) different processes? Because they are fundamentally different processes, right. I mean, the first is forward-looking rate-making. And I think -- I don't think we'd have any credibility; it wouldn't be appropriate if we came here and said, Well, we think next year is really going to be the really bad year.

And we -- we always forecast and do our rate-making based on the average. The -- within the rate-making methodology, we average serious losses over a very long period of time. We average -- when looking at the past, we average investment income over a period of time. We look at the forecast of inflation and in -- and interest rates, like we've told. But we always forecast rates based on a normal year.

Trying to make -- trying to determine how much capital we need to protect ratepayers from rate shock is a fundamentally different process. You're purposely looking for plausible adverse scenarios: What are the things out there that can risk that capital?

As -- and if -- and if you don't think there are any, if you think we'll always, for the foreseeable next fifty (50), hundred years we'll just have normal results, then we probably don't need an RSR. So they're fundamentally different purposes and you come at them differently. What do we normally expect in a normal year is a question we're answering for rate-making.

In term -- determining the size of the RSR, what are plausible risks that could destroy the capital and cause rate shock for ratepayers to recover the capital?

MR. LUKE JOHNSTON: In -- in regards to your second question, I -- I believe it was about that we have some evidence that -- that -- indicating that our equity managers perhaps performed slightly below the index. We did not go forward with that assumption that that would continue. That's -- we assume basically the same, they'll maintain the index for the -- for forecasting purposes.

CONTINUED BY MR. BYRON WILLIAMS:

MR. BYRON WILLIAMS: Thank you. Mr. Johnston, I -- I want to, just in terms of your response to the chairman -- and we'll get more into the equity assumption tomorrow -- but you seem to be suggesting that since 1956 there had been a cumulative four (4) year return period with negative results on the range of minus 40 percent.

Can you point to a single cu -- cumulative four (4) year return on the TSX since 1956 of negative 40 percent, sir?

MR. LUKE JOHNSTON: I don't believe I made that reference; but if I did, I apologize. The -- I -- I may have said that they're -- that equities could have shown to swing either way; sometimes negative forty (40), sometimes plus forty (40) might -- may have been my -- my reference.

Four (4) -- four (4) year periods since

1956, no, there's not a negative four (4) -- 40 percent cumulative return over four (4) years. How -- however, the -- let me find my reference here...

Three (3) years ago we had a two (2) year return of more than negative forty (40). That's essentially the -- the same period that I'm assuming the DCAT -- the recogni -- recognization of equity losses occurs.

We also saw approximately a 38 percent decline as early as '02 over a two (2) year period, and again in 1982. So no four (4) year periods over a -- over the last -- or, since 1956 but several two (2) and -- and three (3) year for cumulative returns.

MR. BYRON WILLIAMS: But, sir, of course the -- the heart of your DCAT analysis was that cumulative four (4) year analysis, correct?

(BRIEF PAUSE)

MR. BYRON WILLIAMS: That's the methodology you chose, sir, because you wanted to partially account for the impact of declined recovery scenarios. That's why you chose it.

MR. LUKE JOHNSTON: Yes. The -- so as a -- as evidence to support a selection of negative 40 percent, we looked at four (4) year periods to try to have an understanding of a prolonged equity decline events. And so you'll notice in -- in the report, as well, I -- I don't chose the -- the 5th percentile is approximately negative 43 percent. I don't select negative 43 percent. The -- the 1st percentile is -- is approximately negative 70 percent. I haven't selected that either.

The -- the issue here is not that I don't recognize Professor Simpson's evidence that there's a difference in the variability of equity losses after 1956, but rather whether I should do what is suggested by Professor Simpson and completely ignore all the data prior to 1956.

So in my selection, I think it's evident that I've given some weight to the lack of very significant declines over that period since 1956, but I don't think it's right to just completely ignore that history.

MR. BYRON WILLIAMS: I thank you for that, and we'll revisit this tomorrow. In terms of a small matter, directing your attention to CAC Exhibit 5, page 23 -- and we've discussed this off -- offline, you'll recall, Mr. Johnston.

Under, "Scenario Justification," you see the -- the description of the 5th percentile event as being minus 43.2 percent. Do you see that, sir?

MR. LUKE JOHNSTON: Yes, I do.

MR. BYRON WILLIAMS: And if you flip to the next page, being page 24, in the top right-hand corner, you're going to see a description which appears to be of a similar event, being minus 42.75 percent.

Do you see that, sir?

MR. LUKE JOHNSTON: Yes, I do.

MR. BYRON WILLIAMS: And first of all, are we talking about the same event there?

MR. LUKE JOHNSTON: Yes. As you -- as you can see, these are -- are, of course, very -- very close, in terms of the impact. I'm investigating to see exactly how the particular number was quoted.

For example, there's -- we build a model of equity returns, and that -- the quoted number here may be the -- the model result versus the actual 5th percentile. If that's the case, they are also -- they -- they are fairly close.

Another issue may have to do with -- with timing. And that's unfortunate that these numbers don't -- don't match. But that -- partic -- particularly in the IRs, if we're asked to evaluate a certainly percentile, I -- my -- our investment department likely did that as of that particular point in time.

So I'll investigate those numbers for you and -- and let you know what the -- the reason for the differences are.

MR. BYRON WILLIAMS: Just for my clarification, you'll recall that in the response to PUB-1-60, the Corporation provided the historical analysis on -- on which it relied for its identification of the 5th percentile event.

Do you recall that, sir?

MR. LUKE JOHNSTON: I'm just going to go to that question.

(BRIEF PAUSE)

MR. LUKE JOHNSTON: Are you referring to Part D, where we provide the history?

MR. BYRON WILLIAMS: Yes, sir.

MR. LUKE JOHNSTON: I am there.

MR. BYRON WILLIAMS: Should I expect to see one (1) or both of those figures, whether it's forty-three (43) point minus -- forty-three point two (43.2) or minus forty-two point seven-five (42.75), in that -- in that information?

MR. LUKE JOHNSTON: Likely not. If you -- if -- if we're modelling this history, then the output is likely the percentile from the model. I -- yeah, I -- I can do the calculations offline and let you -- let you know what I get from that. I would expect it to be, again, very close to -- to negative 43 percent.

MR. BYRON WILLIAMS: Mr. Chairman, just in terms of a time frame, I have many questions yet to go. But I'm just wondering the Board's intention for today?

THE CHAIRPERSON: Well, I was thinking we would go right to one o'clock, unless people want a break. Let's keep going, I think, is my view.

MR. BYRON WILLIAMS: Sir, Mr. Chair, if I could suggest that we stand down for cosmetic reasons for roughly three (3) minutes. And while we do so if, Mr. Johnston, you may just want to have at hand pages 542 through 544 of the transcript.

Would that be permissible, Mr. Chair?

THE CHAIRPERSON: Absolutely. Three (3) minutes, then.

--- Upon recessing at 11:44 a.m.

--- Upon resuming at 11:51 a.m.

CONTINUED BY MR. BYRON WILLIAMS:

MR. BYRON WILLIAMS: Yes, thank you for the -- the break, Mr. Chair. Mr. Johnston, I had directed your attention to the transcript pages 542 through 544. I haven't put them in the materials for the -- the tribunal.

(BRIEF PAUSE)

MR. BYRON WILLIAMS: In the six (6) minutes that we've given you, Mr. Johnston, you have no doubt memorized this material. But as you review it, I'm sure you will recall a -- a discussion you had with My Friend, Ms. Grammond, at -- when she was probing you on your definition of "satisfactory financial condition".

Do you recall that conversation?

MR. LUKE JOHNSTON: Yes, I do.

MR. BYRON WILLIAMS: And just to refresh everyone's memory, as I understand it, for the purposes of your DCAT analysis:

"The Corporation's financial
condition is satisfactory if,
throughout the forecast period, it is
able to meet all of its future

obligations under the base scenario and all plausible adverse scenarios, and -- and under the base scenario it meets the minimum regulatory capital requirement."

Is that the definition you employed, sir?

MR. LUKE JOHNSTON: Yes, it is.

MR. BYRON WILLIAMS: And you'll recall as well, My Friend, Ms. Grammond, suggesting to you that that type of question and that type of analysis sounded a lot like you were focussing on solvency.

Do you recall that suggestion?

MR. LUKE JOHNSTON: I recall the solvency discussion, yes.

MR. BYRON WILLIAMS: And I'm going to say you conceded, but -- you -- you may not accept that. But you -- you agreed that the -- that while -- the particular definition seemed to indicate a solvency basis.

Do you recall that, sir?

MR. LUKE JOHNSTON: In terms of the requirement to keep the rate stabilization reserve above zero, I had indicated that that may appear to look like a solvency test.

MR. BYRON WILLIAMS: And we'll come to the -- the other part of your -- your answer, sir. But just focussing on private-sector companies, I'll -- I'll suggest to you that you would not disagree that when employed by private-sector companies in a competitive marketplace, the primary purpose of the DCAT is to determine if there is a plausible risk of a solvency issue.

Would that be fair?

(BRIEF PAUSE)

MR. LUKE JOHNSTON: Yeah, that -- the -- the primary purpose of the -- the DCAT would of course be to understand the risks of the -- the enterprise, how the future financial condition compares to the regulatory targets of OSFI, not necessarily a -- the company going insolvent, but falling below those -- those targets. And it's -- it's, of course, important to know if there are plausible adverse scenarios that could put the Corporation into a -- a negative retained earnings position.

And the -- the DCAT requires that all -- understandably, all those scenarios are laid out in detail in the report so it can be understood why such a scenario could occur for -- for that company.

MR. BYRON WILLIAMS: And that indeed is a central element of -- of the DCAT analysis.

(BRIEF PAUSE)

MR. LUKE JOHNSTON: My apologies. Could you repeat your last question? Or ask a new question if you didn't have one.

MR. BYRON WILLIAMS: Just so I understand, first of all, you're -- you're not changing your answer to the last -- last question, are you, Mr. Johnston?

MR. LUKE JOHNSTON: No, I'm not changing the -- the substance to my -- my last question. I -- I didn't want to imply that it was purely just a solvency test.

MR. BYRON WILLIAMS: And I certainly never understood that to be. But you certainly would not deny that, in the context of a private-sector corporation in a competitive environment, that's certainly one outcome and one important element of that examination?

MR. LUKE JOHNSTON: Yeah, solvency is a -- is a important element, yes.

(BRIEF PAUSE)

MR. BYRON WILLIAMS: And the nature of DCAT, in terms of its design and the range of plausibility outcomes, it has certainly been designed with that -- with recognizing that -- that the solvency issue is one of the issues in play for private-sector companies in the competitive marketplace?

(BRIEF PAUSE)

MR. BYRON WILLIAMS: Mr. Johnston, I'm going to have to have the court reporter repeat that question, because it was a while ago.

MR. LUKE JOHNSTON: Thank you.

(BRIEF PAUSE)

MR. BYRON WILLIAMS: I'll -- I'll take another shot at it. Inherent in the DCAT design and the plausibility range is a recognition that one of the aspects of this analysis is a consideration of its impacts on solvency of private-sector companies in a competitive marketplace?

MR. LUKE JOHNSTON: I'm unclear how to draw that comparison between the DCAT performed for Basic, Autopac, MPI, and -- and the private sector regulatory capital requirements.

The RSR of greater that zero is a target used in the DCAT. The definition of "satisfactory financial condition" is as per the regulatory re -- capital requirements of this Board, not private sector.

The -- the DCAT is recommendation -- recommended risk level is no different than the -- the risk analysis asking for 190 to 300 million excess retained earnings. Here we're adding -- we're essentially adding a risk margin above an assumed RSR level of zero and asking what -- how much do we need above zero to maintain satisfactory financial condition in all scenarios.

The -- the Corporation is not suggesting in any way that this is a solvency test for us, or that we've somehow become insolvent. It's -- it's about the stated purpose of the RSR and preventing rate shock for policy holders.

MR. BYRON WILLIAMS: Mr. Johnston, my question may have been unclear, so let me -- let me try it again.

We agree that -- under the DCAT approach an adverse scenario would be considered plausible if it reflects the 95th to 99th percentile of outcomes, agreed?

MR. LUKE JOHNSTON: Agreed. This would be the -- the risk tolerance of the DCAT similar to other methods.

MR. BYRON WILLIAMS: And I'm suggesting to you that in the inherent -- in the design of that range of risk tolerance is a recognition that when this is being used by a private-sector company in a competitive marketplace, solvency is an issue. It's the DCAT range I'm focussing on, sir, not your Application here.

(BRIEF PAUSE)

MR. LUKE JOHNSTON: If you're asking does the DCAT show in which scenarios with a one (1) in twenty (20) to one (1) in a hundred (100) probability of occurrence could push the private company below the regulator's capital requirements, or potentially push them into insolvency position, then that is what the -- the DCAT would show for a private company. That's not -- that's not the requirement in this province, and it's -- we're not comparing ourselves to that.

MR. BYRON WILLIAMS: And I won't belabour the point, Mr. Johnston, but I'm going to suggest to you that that one (1) in one hundred (100) scenario is, in terms of the breadth of the plausibility range, is a reflection of the fact that the DCAT is designed to -- in contemplation of that solvency issue.

MR. LUKE JOHNSTON: I would disagree with that. I -- if the -- if you're suggesting that the Board's one (1) in forty (40) risk tolerance level has anything to do with solvency of MPI, I don't think that does any more than the risk tolerance level we're selecting in the DCAT. It's about the -- the level of risk that you're willing to accept and how MPI would have to respond if those scenarios occurred.

MR. BYRON WILLIAMS: Now, Mr. Johnston, when we were talking -- chatting about your discussion with Ms. Grammond a few moments ago while you acknowledge that -- that the DCA -- DCAT -- and I'll -- I'll be careful with my language here -- seemed to indicate a solvency basis, without asking you to elaborate, you also indicated that in your view its purpose is very consistent with the purpose of the RSR in that, to quote you:

"It significantly prevents rate

shock."

Do you recall that?

MR. LUKE JOHNSTON: I don't recall those exact words, but the -- the DCAT, we've -- we've stated multiple times in the evidence is -- explicitly measures the risk of MPI and ties in almost perfectly, in my opinion, if not perfectly, with the purpose of the RSR. That is to prevent rate changes from significant events, such -- such as the ones we're outlining in the report.

MR. BYRON WILLIAMS: And you went on to -- to say, at page 543, if you're looking, sir, that if we do fall to a negative RSR position, we will be required to rebuild to recover our retained earnings.

And that -- that will require rate increases or rate surcharges, correct?

MR. LUKE JOHNSTON: I would assume, based on the past precedent and how we set rates in this province, that we would not run at a negative retained earnings position for a prolonged period. I would expect that we would have rate surcharges or rate increases in -- in whatever way necessary to get to the Board's capital requirement, be it DCAT or any other method.

MR. BYRON WILLIAMS: And we'll come to

that in just a moment, sir. Turning to page 25 of CAC Exhibit 5, you'll see the response to CAC-1-3.

(BRIEF PAUSE)

MR. LUKE JOHNSTON: Page 25?

MR. BYRON WILLIAMS: Page 25, in the top right-hand corner, Mr. Johnston.

MR. LUKE JOHNSTON: Thanks.

MR. BYRON WILLIAMS: Now, this -- (c) sets out the adverse scenarios. And, Mr. Johnston, we'll leave the discussion of the decline in equity markets till tomorrow.

But of the three (3) other adverse scenarios, the -- amongst the top four (4) -- those being the combined incurred/equities, a high loss ratio, and a large hail storm -- MPI describes all of these as one (1) in one hundred (100) year probability levels, correct?

MR. LUKE JOHNSTON: That's correct.

MR. BYRON WILLIAMS: And it is your professional judgment that in order to significantly protect ratepayers against rate shock, you have to set up reserves that protect them from the possibility of one (1) in one hundred (100) year events?

Is that your view, sir?

MR. LUKE JOHNSTON: Well, we -- we do have to select -- again, we have to select a risk tolerance. And this is the risk tolerance used in the DCAT. The occurrence -- the event that occurs does not have to be one (1) in one hundred (100). A eighty (80), $90 million decline produced by some of these other scenarios, or through -- for any combination of reasons would also be something that could generate a -- a rate surcharge.

There's obviously the full spectrum of possible outcomes between our best estimate and the 99th percentile.

MR. BYRON WILLIAMS: I -- I may not have asked my questions clearly. So I'll just ask it again, and then you can choose to answer it if you wish.

Is it your professional judgment that in order to significantly protect ratepayers against rate shock, you have to set up reserves that protect them from the possibility of one (1) in (100) year events?

(BRIEF PAUSE)

MR. LUKE JOHNSTON: Just to make sure

I'm clear, would you mind repeating the -- the question?

MR. BYRON WILLIAMS: Mr. Johnston, you're asking a lot of me to repeat it three (3) times, but I think this one I can handle.

Is it your professional judgment that in order to, using your words, "significantly protect ratepayers," end your words, against rate shock, you have to set up reserves that protect them from the possibility of one (1) in (100) year events?

MR. LUKE JOHNSTON: Yes, I believe that to be true. This, and -- this in -- as you've shown on this page, this is the -- essentially the -- the risk tolerance level that I've selected.

MR. BYRON WILLIAMS: Has the Corporation tested that proposition with Manitoba seniors, namely that they would like to keep their money in -- in the Corporation's retained earnings to protect them against one (1) in one hundred (100) year events?

(BRIEF PAUSE)

MR. LUKE JOHNSTON: No, I did not consult -- I -- I believe you quoted them, "Manitoba

Society of Seniors." No.

MR. BYRON WILLIAMS: I couldn't have done that. I don't think they exist anymore, Mr. Johnston. I'm just wondering: Has -- has the Corporation put this to seniors or other Manitobans, this proposition?

MR. LUKE JOHNSTON: No, I did not -- I -- I did not, and the Corporation did not. As part of this risk based analysis, we did not poll the public for their -- their view on our selected risk tolerance.

MR. BYRON WILLIAMS: Mr. Johnston, in your discussion with Ms. Kalinowsky oh so long ago on the first day of the Hearing, you referred to this DCAT as a made-in-Manitoba solution appropriating the words of -- of, I think, one of my witnesses from some time ago.

Do you recall that?

MR. LUKE JOHNSTON: Yes, I do.

MR. BYRON WILLIAMS: In crafting a made-in-Manitoba solution, would it be permissible to employ the -- a DCAT for range between the 95th and the 97.5 percentile?

MR. LUKE JOHNSTON: We did talk a little bit on that topic, and the one (1) and forty (40) year risk tolerance level, the 97.5 percent --

percentile does fall within the DCAT requirements, and we can model those scenarios.

And we did talk a little bit last week also about a more collaborative approach and have indicated that we're quite willing to work with the Board and Intervenors on developing scenarios that meet the standards required of the DCAT process while also reflecting the -- the concerns of the parties in the room and -- and perhaps, as well, the -- the risk tolerance level of the Board.

Again, I'm trying to -- or, pardon me, not trying -- keeping those -- any assumptions that we make within the actuarial standards of designing the DCAT.

(BRIEF PAUSE)

MR. LUKE JOHNSTON: And perhaps if I -- I could clarify. I also mentioned that as a professional, I have to be able to be willing to accept the assumptions that we're using. It in no way means that I -- we -- the Corporation can't provide the Board with the information that it requires for a particular scenario.

I just will not produce a DCAT if I

believe that the underlying assumptions are flawed or -- or not acceptable.

MR. BYRON WILLIAMS: Thank you, Mr. Johnston. Ms. McLaren, you were -- in your evidence yesterday, you were discussing the contribution of the Gartner Group to Manitoba Public Insurance.

And I don't know if you recall a discussion in which you were discussing the applicability of some of Gartner Group's private-sector-driven analysis. But I'll ask you if you recall stating something to the effect that sometimes the lenses do not always align.

Do you remember a statement to that effect, Ms. McLaren?

MS. MARILYN MCLAREN: I do.

MR. BYRON WILLIAMS: Could it be said that in applying a one (1) in one hundred (100) year event solvency test to a rate shock issue, sometimes the DCAT lenses do not always align?

MS. MARILYN MCLAREN: No, I don't think so, because you have to look at a little bit broader context than that. If we were before this Board -- you know, remembering that part of what we're trying to do is to work with this regulatory framework, right, I mean, I think you can -- you cannot understate the importance of your conversations and your perspectives around solvency without considering the importance of the fact that any private-sector company that gets anywhere close to the 150 percent on the MCT score is automatically under supervision.

I mean, if we were here saying, Well, you know, you need a much, much bigger RSR, according to some private-sector model, even back in the day when we were suggesting that the MCT would be a good basis to select the RSR, we weren't talking 150 percent. We were saying between 50 and a hundred percent might be appropriate for the Basic compulsory program.

So to choose the -- the different features in a -- in a similar actuarial methodology without considering how we truly have used that methodology to the circumstances specific to Manitoba, I -- I don't know that those are -- I -- I just don't agree with the basis of your question in that case.

MR. BYRON WILLIAMS: Thank you for that. Mr. Johnston, just going back to the -- your words -- and, again, if you're looking for a reference, it's page 543, line 2 -- "significantly prevents rate shock."

Do you define "rate shock" to be a rate increase of 10 percent or more within a fiscal year?

(BRIEF PAUSE)

MR. LUKE JOHNSTON: Although significant, I -- I wouldn't classify that as a rate shock.

MR. BYRON WILLIAMS: How high would you go, Mr. Johnston? It's your words.

MR. LUKE JOHNSTON: We do have guidelines that we -- that we use for rating to limit the size of increases after 10 percent, capping experience at fifteen (15) and, as an absolute limit, 20 percent increases to rates.

Again, such increases are clearly not -- not desirable, but that's the approach we've taken if the underlying claims experience indicates that such a rate increase is needed.

MS. MARILYN MCLAREN: Let's -- we can go back the other way, as well, in terms of less than 10 percent, if you're talking about the entire fleet, the entire population of Manitoba vehicles. After a cumulative -- I think it's about 12 percent rate decreases in the last year, if we turned around and said, you know, we need 6 percent more now, that may very well qualify as well. Things like this are -- are situational.

We don't use a lot of hard and -- and fast numerical benchmarks, in terms of those -- some of those definitions. What we're talking about is making sure this compulsory automobile insurance program continues to meet the needs of Manitobans for predictability and stability. That's what we're talking about here.

So what Mr. Johnston has said a number of times and what we believe is the DCAT is the best approach possible to determine the RSR according to the definition of the RSR, which doesn't necessarily tie directly to rate shock, right. It's about protecting Manitobans from one (1) time events.

(BRIEF PAUSE)

MR. BYRON WILLIAMS: I could have sworn that -- that it was the actuary who used the word "significantly prevents rate shock."

Was that -- that was you, Mr. Johnston?

(BRIEF PAUSE)

MR. LUKE JOHNSTON: The -- I do believe that the -- the DCAT methodology will aid in preventing significant rate increases, rate shocks. I -- I don't -- I don't -- I don't -- I haven't defined "rate shock".

But the -- the -- again, the stated purpose of the RSR doesn't specifically address rate shock, but rather rate increases made necessary by unexpected events, such as the ones in the -- in the DCAT.

I believe that an adequate RSR level, as set by the DCAT, would significantly reduce the probability that ratepayers have to have rate increases from these events versus selecting another method, for example, that's significantly lower.

MR. BYRON WILLIAMS: So if I understand your last answer, Mr. Johnston, when we think of the RSR target, we should think of it as pre-collecting money to avoid rate increases arising from unforeseen events, regardless of whether rate shock will ensue or not?

MR. LUKE JOHNSTON: I'm a little bit unclear with your question, so I -- I just -- I just spoke that the stated purpose of the RSR is to prevent -- to protect motorists from rate increases made necessary by unexpected events and losses.

So I've said that that -- that is one of the reasons why the DCAT ties so well with that definition, because, again, we're looking at the specific risks that -- that MPI faces and -- and how those risks would impact policy holders. So I'm not clear on what you're asking.

MR. BYRON WILLIAMS: I'll reflect on that, Mr. Johnston. I do thank MPI for assisting our clients in understanding their position. Ms. McLaren -- and, Mr. Chairman, I will come back to some of these questions tomorrow. But just while Ms. Desorcy is -- is here, I do have some questions about the direction of the -- the road -- road safety initiatives.

And -- and certainly, our clients read with -- with interest your thoughtful commentary in -- in a number of the publications you have.

And I -- I'm going to just start with a -- a lengthy question, in terms of -- it won't be the first or the last, Ms. McLaren, but when -- when one looks at the potential roles that Manitobans have suggested for Manitoba Public Insurance, one of them obviously is a -- and I'm going to go through them one (1) by one (1).

But one obviously is a -- as an investor in road safety programming, similar to what you're doing today?

MS. MARILYN MCLAREN: Sure, that's fair.

MR. BYRON WILLIAMS: And another is a -- as a coordinator of groups working in this road safety role? We've seen that in your documentation?

MS. MARILYN MCLAREN: Yes, that's fair. I -- I don't know that there's complete clarity on what everyone would mean by "coordinator", but that's fair.

MR. BYRON WILLIAMS: There's also been a suggestion that Manitoba Public Insurance should act as a central repository to facilitate sharing of data?

MS. MARILYN MCLAREN: Yes.

MR. BYRON WILLIAMS: That it should promote or support a research centre focussed on Manitoba specific issues and be a coordinator of evaluation of programs, correct?

MS. MARILYN MCLAREN: There was some feedback along those lines, yes.

MR. BYRON WILLIAMS: It was suggested it should be an educator, with more extensive and challenging programming, whether field tests, online delivery of programming, and greater use of technology, such as simulations, correct?

MS. MARILYN MCLAREN: Yes.

MR. BYRON WILLIAMS: Some have

suggested it should be an investor in enforcement, correct?

MS. MARILYN MCLAREN: Some, yes.

MR. BYRON WILLIAMS: Others have suggested infrastructure?

MS. MARILYN MCLAREN: Yes.

MR. BYRON WILLIAMS: And the City of Winnipeg and the MTA seem quite keen on you doing road safety audits in high-collision areas?

MS. MARILYN MCLAREN: That's fair.

MR. BYRON WILLIAMS: So, Ms. McLaren, obviously there's tremendous opportunities for the Corporation and for Man -- Manitobans in this discussion.

I wonder if you could assist my client in identifying what you see as some of the risks for the Corporation?

MS. MARILYN MCLAREN: I guess in the broadest sense my answer to that would really follow on some of the conversation that I had with the Chairman yesterday. This is such a broad area. There are so many terrific ideas. The risk is that the spending can certainly get out of control. You have to be very careful at being clear on what you really believe might be investments versus what might truly be expenditures.

I think there are also risks associated with becoming a bit misaligned with what Manitobans would really see as our role if we were too pervasive or aggressive about moving into this area. There are some really mixed feelings out there in the population about the extent to which we should fund enforcement. There are absolutely strong support in some key risky behaviours, but not so much in others.

So I think overall we are always very, very focussed on -- on working hard to stay aligned with what Manitobans believe is appropriate. And I just think in this area, really making sure the expenditures are prudent, identifying investments where you can, but recognizing that a lot of this is -- is a very, very uncertain and fuzzy area.

MR. BYRON WILLIAMS: Now, in -- in your view, recognizing your -- your concern with keeping expenditures prudent and under control, are you confident that the Corporation's existing road safety expenditure and -- and oversight controls are robust enough to do that?

MS. MARILYN MCLAREN: While acknowledging that there's probably always areas to contin -- to continue to improve, the methodology that we adopted many years ago as -- before you embark on a particular program, whether it's an advertising campaign, whether it's a wildlife pilot, what are your -- what are you hoping to achieve. And, in many cases, reduced claims cost are not one of the objectives.

So if what you're hoping to achieve is enhanced awareness, higher self-reporting that they will do something better in the future, and you can actually measure against those objectives, I think that's about as much monitoring as you can do in some cases.

So that's the framework we use. I believe we use it pretty consistently, and I think for the most part we have -- we've stuck to that program.

MR. BYRON WILLIAMS: In terms of other jurisdictions who MPI may -- may seek to learn from, in terms of just this expenditure control and -- and management, is ICBC the -- the leading jurisdiction or are there others?

(BRIEF PAUSE)

MS. MARILYN MCLAREN: No, I -- I think that's fair to say, that ICBC is certainly recognized as a leader. And for quite some time they have spent money or invested in road safety areas that -- that MPI has not. And we would look to learn from them, particularly in those areas.

(BRIEF PAUSE)

MR. BYRON WILLIAMS: Ms. McLaren, we're going to change gears just a little bit, still in the -- hopefully in the loss-prevention, enhancing safety vein.

Our client is curious about -- about the -- the Corporation's research into the driver safety rating and, in particular, what, if any, insight the Corporation has, and what, if any, research it has, in terms of whether consumers are understanding how it works and what it means?

(BRIEF PAUSE)

MS. MARILYN MCLAREN: I would have to go back to see if we've done anything in terms of quantitative research along those lines.

What I can tell you is that anecdotally the calls that we get to our call centre, the conversations that brokers have with Manitobans is they are very, very much in favour with the new system. The comprehensive but simple and straightforward approach we've taken to explaining the new system with each renewal and reassessment that comes up has -- I think would have to -- the -- the information we have from the sources I talked about demonstrates to me that it's working pretty well.

This is the kind of thing that if people were confused and surprised, we would be hearing about it. And there's nothing along those lines. Instead, they're asking fairly informed questions when they do call or go to the broker to talk about their movement on the scale.

(BRIEF PAUSE)

MR. BYRON WILLIAMS: Ms. McLaren, without putting you to a formal undertaking, if there is -- if there is research that -- that the Corporation had -- has done and -- and at the risk of testifying, flowing from our -- certainly our clients' focus groups, has the Corporation identified any age gap in terms of understanding of DSR?

And by that I mean if it has any surveying, has it looked at whether younger persons who are less mail-orientated and more online, whether --

whether they're grasping the principles of that -- of DSR?

MS. MARILYN MCLAREN: Yeah, if we have anything we'll bring it forward.

(BRIEF PAUSE)

MR. BYRON WILLIAMS: Is the cor -- is the Corporation undertaking or considering any education campaigns in terms of the recent Winnipeg phenomena of traffic circles?

MS. MARILYN MCLAREN: We have. We've done both the sixty (60) second driver spot on them. We've also run some print advertising in the Free Press on them. Both of those are currently available under the driving tip section of our website.

I think -- trying to think. There was one (1) more. Just give me half a second here.

(BRIEF PAUSE)

MS. MARILYN MCLAREN: We've also included it in the dri -- the driver's handbook.

MR. BYRON WILLIAMS: Now, we are jumping around a little bit here, Ms. McLaren. You'll forgive me for this. What, if any, customer research has Manitoba Public Insurance done in terms of the desire of consumers to have better information technology services?

And, I guess, the corollary, is it -- ha -- has any of that research been associated with an explanation of how it will be paid for?

MS. MARILYN MCLAREN: No, we haven't done any customer surveys to find out if Manitobans think we should make sure our IT systems keep running and don't fall over. And I think, by the same token, we have done -- not done customer surveys to say, Do you think we should enhance and expand our IT infrastructure so we can do the kinds of services in the future we don't do today.

We've never done that kind of thing at MPI. We don't believe that is the best way to stay in tune with Manitobans. We didn't ask them if we thought the streamlined renewal process was a good idea. What we have asked, and the way we come at these things is to ask if they, you know, support a broader context of eliminating low-value transactions, making sure we're available to them when and how they need us to be, not that we're forcing them to come in and do things according to our agenda or our schedule. So we come it at a slightly different way.

But back to your original question, no, we haven't done a survey on whether they think we should spend money on IT.

MR. BYRON WILLIAMS: Now, in -- in terms of MPI's consumer education advertising, have they had any external reviews of its effectiveness or benchmarking or comparison against what is working in other jurisdictions?

MS. MARILYN MCLAREN: What was the first part of that, in terms of the safety advertising?

MR. BYRON WILLIAMS: Yeah, consumer education, safety advertising.

MS. MARILYN MCLAREN: Okay. When I talked about the -- the measures that we establish for each program, those are all done according to -- and I don't remember the name offhand, I can get it if it's important to you, but it -- there is the Advertising and Public Information Standards Association that says, Here's how to measure the effective -- we -- we follow those benchmarks. We follow those guidelines. We -- we don't come up with them on our own.

MR. BYRON WILLIAMS: Just a last couple questions flowing from some of the consumer context of our client. I think I know the answer to this question.

But does MPI do renewals at their offices and they -- do they advertise this service?

MS. MARILYN MCLAREN: Do we do renewals at our offices? Yes, our service centres do. And, no, we do not advertise that. We communicate to the public, for the most part, the services that we provide directly to Manitobans that are not available from brokers.

Brokers are the -- the primary source of those Basic insurance and registration related transactions. We certainly would never not provide them, but we focus our information to Manitobans on what -- what we do that brokers cannot do.

MR. BYRON WILLIAMS: Mr. Chairman, I've -- I haven't taken all your time. I can certainly move to another area. I'm not sure that I have anything -- I could probably kill a few more minutes on a couple of other subjects. It's up -- up to you, sir.

THE CHAIRPERSON: Please do.

(BRIEF PAUSE)

CONTINUED BY MR. BYRON WILLIAMS:

MR. BYRON WILLIAMS: Sorry about that,

court reporter. Mr. Johnston, back to you at page 28 of the -- of the CAC number 5.

Do you have that, sir?

MR. LUKE JOHNSTON: Yes, I do.

MR. BYRON WILLIAMS: One of the -- the concerns expressed by MPI, in terms of the operational and investment risk analysis, is that setting the RSR target using a time horizon of two point five (2.5) years may not be appropriate.

Do you recall expressing that concern, sir?

MR. LUKE JOHNSTON: Yes, I do.

MR. BYRON WILLIAMS: And I'll suggest to you that CAC-2-28 asks you to re -- reformulate the value at risk time horizon from two point five (2.5) years to one (1) year.

Is -- is that your understanding of this Information Request as well, sir?

MR. LUKE JOHNSTON: That's correct.

MR. BYRON WILLIAMS: And the result of this analysis is that the required RSR based on the revised analysis is a range of between 170 million and 232 million.

Is that correct, sir?

MR. LUKE JOHNSTON: Yes, that's

correct.

MR. BYRON WILLIAMS: Now, sticking with the -- the risk analysis, the operational investment risk analysis for a moment or two (2), sir, at the direction of the -- the Public Utilities Board, that risk analysis is premised on a -- an investment portfolio of Manitoba Public Insurance comprised of 25 percent equities.

Is that your understanding, sir?

MR. LUKE JOHNSTON: Yes, that's correct and the reference for that would be on -- several places, but AI.11, part 1, page 6.

MR. BYRON WILLIAMS: And the 25 percent equity, sir, if I understand your evidence in this hearing, you'll agree with me that it does not reflect the current reality of Manitoba Public Insurance.

I -- in that your portfolio is roughly 60 percent bonds, 20 percent equities, and -- and roughly another twenty (20) -- 20 percent elsewhere?

MR. LUKE JOHNSTON: I won't -- I don't have in front of me the exact proportions, but you're correct, it is less than 25 percent.

MR. BYRON WILLIAMS: And would I be correct in assuming, sir, that -- that if the risk analy -- if the operational and investment risk analysis was modelled on MPI's current equity portfolio, that the -- the figure and the range would probably be directionally lower?

MR. LUKE JOHNSTON: That's fair. If you have a -- a lower base then you'd expect a similar variability with just a -- a reduced number.

MR. BYRON WILLIAMS: And, sir, in terms of the invest -- operational and investment risk analysis, and the MPI critique of it, would it be fair to say that in terms of a methodology, Manitoba Public Insurance has some fairly positive things to say about value at risk.

Would that be fair, sir?

MR. LUKE JOHNSTON: Yeah, val -- value at risk is moving closer towards what we're trying to do. Again, in the DCAT it's looking at current, or in this case twen -- we assume 25 percent. But it's moving to, you know, today's risks. Approximating the 25 percent is the -- of equities is -- is the target. Unlike the other half of that analysis, it's not based on historical outcomes or anything like that.

In a way, it's -- it's somewhat similar to the -- the equity analysis that we're doing in the DCAT. What it's missing is the -- the financial statement outcomes and management and regulatory action. Yeah, I'll leave it at that.

MR. BYRON WILLIAMS: And certainly, in its own materials -- and if you need a reference it's AI.11 part -- or, it's -- it's in your discussion of value of risk. Manitoba Public Insurance describes it as:

"An increasingly valuable tool in understanding and measuring risks and a best practice within the institutional investment industry."

Would that be consistent with your understanding of this tool?

MR. LUKE JOHNSTON: Do you have a reference?

MR. BYRON WILLIAMS: Yes, it's -- it's from -- it's at page 7 of your discussion of -- of value at risk, sir. Probably right near the con -- the end of it.

MR. LUKE JOHNSTON: I'm not finding it, but I -- I don't disagree that it's a -- it's a valuable tool for the -- the purposes for which it was designed.

If -- if I could add to that, one key aspect of the value at risk that is -- is somewhat overlooked is it's not comparing itself to budget. So it's saying what is the most the Corporation could lose over a certain period at a certain confidence level.

So if it was to indicate $200 million, if we have a budget to make $50 million, we've actually -- we're actually at negative 250 million. So that's one -- one aspect that isn't really discussed much in -- in this analysis.

MR. BYRON WILLIAMS: And in terms of the range -- or in the -- in terms of the risk tolerance and, Mr. Johnston, you'll correct me if -- if I'm wrong on this, but am I correct in -- in suggesting to you that it's -- that it is designed in terms of a 95 percent probability or ...?

(BRIEF PAUSE)

MR. LUKE JOHNSTON: A 95 percent and a 97.5 percent level is produced. I just wanted to make sure we did both.

MR. BYRON WILLIAMS: And I apologize for that, sir. I should have indicated that. Mr. Chairman, I'm -- I'm out of any short snappers.

THE CHAIRPERSON: Unless we have some other business to conduct before we adjourn, let's adjourn now and we'll see each other again tomorrow morning at 9:30. So thank you very much for accommodating the needs of this particular Board member. Thank you.

--- Upon adjourning at 12:52 p.m.

Certified correct,

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Lorraine Douglas, Ms.

D