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 504 to 700

APPEARANCES

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

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--- Upon commencing at 9:27 a.m.

THE CHAIRPERSON: I wonder if we couldn't start immediately. Maybe the first time in recorded history that we've started early. But since everybody is here, I guess congratulations are in order, Ms. McLaren, for the initiative that you took on last night. So congratulations for being such a success -- successful fund raiser. So congratulations to -- to a very worthwhile initiative.

So we -- do we have any business to attend to before -- no. I'll turn it over back to you --

MS. CANDACE GRAMMOND: Yeah.

THE CHAIRPERSON: -- you, Ms. Grammond, for the continuation of the cross-examination.

MS. CANDACE GRAMMOND: Thank you, Mr. Chairman. Yeah, there's no housekeeping that I'm aware of so I'll resume cross-examination with respect to actuarial matters.

MPI PANEL, RESUMED:

MARILYN MCLAREN, Resumed

HEATHER REICHERT, Resumed

LUKE JOHNSTON, Resumed

CONTINUED CROSS-EXAMINATION BY CANDACE GRAMMOND:

MS. CANDACE GRAMMOND: Mr. Johnston, my first set of questions deal with the interest rate margin for adverse deviation. So what I'd ask you to do to start is to discuss the three (3) components of the provision for adverse deviation.

(BRIEF PAUSE)

MR. LUKE JOHNSTON: Sorry, I was just checking if -- if you happen to have a reference in your book of documents, and I think you do under Tab 17, page 46.

MS. CANDACE GRAMMOND: Yes, thank you. So that's at Tab 17 of the book of documents. There's an excerpt of the external actuary's report from October of 2011. When you open the tab, you'll see page 22.

There are a few pages there, but then if you -- if you keep flipping, it's actually the fourth page from the back. You'll see page 46. And the title there is, "Discount Rate and Provision for Adverse Deviation."

So that -- is that what you were referring to, Mr. Johnston?

MR. LUKE JOHNSTON: That's correct. As mentioned, there are three (3) different categories for the provision for adverse deviation, and these are provisions that are required under actuarial standards of practice.

The first is the claims development provision, and this is a provision that's applied to the unpaid claims for potential variability in the development or ultimate value of those claims. And the -- the standards of practice require a range between 2.5 percent and 15 percent, with some exceptions in exceptional circumstances.

The idea is that the margin selected should reflect the variability of the coverage that they're being applied to. These margins that we have selected in our report are -- are judgmental. And you'll see on page 47 the -- the selections there. I won't -- I won't read them. But you will notice just in general that PIPP coverages with -- that are fairly uncertain and very long payment patterns have a higher margin, whereas shorter -- shorter-tailed coverages, like collision, have a lower margin.

The interest rate PFAD, similarly it's -

- provide for variability in the realized return, assumed return in the calculation of the claims liabilities. And what we do is basically we -- we first calculate the present value of our liabilities using the prevailing interest rate of our -- of our bond portfolio.

We then adjust that rate by -- like lower it, for example, and then recalculate the present value at a lower rate. The difference between those two (2) calculations is the interest rate margin. And currently, in this report, we're using a 1.25 percent interest rate margin.

And finally, there is a margin for adverse deviation on the recov -- coverability of reinsurance. And we don't have a large significant amount of -- of ceded claims but, again, there is some risks that -- that those could not be paid if a reinsurer was to default.

MS. CANDACE GRAMMOND: Thank you. So just to summarize -- and I appreciate the explanation of each of the three (3) components, the three (3) components then of the provision for adverse deviations are the claims development margin, the reinsurance recovery margin, and the interest rate margin?

MR. LUKE JOHNSTON: Yes, as -- as per

the second paragraph on page 47.

MS. CANDACE GRAMMOND: Thank you. Now, the claims development margin is unchanged from last year. Is that right?

MR. LUKE JOHNSTON: That's correct. We didn't make any changes to those assumptions.

MS. CANDACE GRAMMOND: And you mentioned that the margin for the interest rate was a hundred and twenty-five (125) basis points. And that's up from a hundred basis points previously.

Is that right?

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

MS. CANDACE GRAMMOND: And was this new margin for interest rates applied uniformly to all lines of business -- or, lines of coverage?

MR. LUKE JOHNSTON: Yes, the same interest rate before and after the margin was supplied to all coverages.

MS. CANDACE GRAMMOND: And is it the case that the estimated impact of this change in assumption was an increase in the claims liabilities of about 34 million?

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

MS. CANDACE GRAMMOND: Now can you discuss the rationale for the increase in the interest rate margin from a hundred basis points to a hundred and twenty-five (125) basis points?

MR. LUKE JOHNSTON: Yes. So the -- the range of the interest rate PFAD is from -- per -- per actuarial standards is 0.25 percent to a maximum of 2 percent. And there's no -- or at least we haven't used a scientific method to -- to come up with the assumption, it is judgmental. However, there are educational notes on the topic that guide the actuary in how to select this assumption.

And in -- I'll just go through a few of the considerations. One -- one consideration is obviously the -- the length of the cashflows that -- for the claim liabilities. So if it's a very long period where the cashflows are paid out, like -- like for the PIPP program, for example, there's obviously more risk of interest rate impacts.

So MPI would -- would definitely be at the higher risk range in terms of the length of our -- our claims liability duration. Other property casualty insurers tend to settle much more quickly than -- than MPI.

Another consideration would be the

quality of the assets that are backing the liabilities. And MPI is generally backing the liabilities with government bonds. There's some -- there's some corporate bonds there but not -- not any significant amount.

So the -- the risk of asset default is -- is fairly low. So MPI would -- in MPI's case, that would justify moving towards a lower margin. The -- another consideration is, of course, the -- the variability of the -- the claim payment pattern.

And, as you've seen, there is -- there is definitely some variability in the PIPP program, especially in the early stages and the -- the unknown stages where we have no -- no experience yet of how claimants are going to -- how claims are going to close in the tail period.

Finally, another -- another consideration would be current economic conditions. If -- if you are in the middle of a recession or a very uncertain economic period, that may justify a higher margin, the opposite for a fairly strong economy or economic period.

So those are -- there's a whole list of considerations that -- that are -- are used. In the past, I've -- I've always found the selected -- our selected margin, which was -- has been 1 percent up until this time, to be in the middle of the minimum and maximum provision. And I found that reasonable, because we -- as I've stated, we have a very long, risky cashflow stream from PIPP. However, we do have fairly strong asset base supporting those liabilities, with a fairly low risk of default.

If I could turn to -- let me just find the reference, please.

(BRIEF PAUSE)

MR. LUKE JOHNSTON: Sorry, it's right in front of me, actually. In the same Tab 17, page 48, if you could turn there, please.

As I mentioned yesterday, we pre -- the internal actuarial department prepares the valuation internally first, and then the -- the initial results are presented to our appointed actuary. And then we go through various discussions on whether the assumptions are appropriate, et cetera.

In regards to the interest rate provision, our appointed actuary was concerned with the -- the combination of significantly declining yield on our fixed income portfolio, combined with higher inflation rate at the time of the valuation.

So if you -- the middle table on page 48, you'll see the expected return on MPI's bond portfolio at various points in time. Net of the -- and then the second column has Manitoba inflation, and then last column has the real return, which is essentially the -- the nominal or the first-column return net of inflation.

So you can see that the real return has declined very significantly in the last several reviews, and it was this that drawed (sic) the attention of our appointed actuary. And this was his rationale for -- for seeing increased risk and, therefore, an increase in the interest rate provision for adverse deviation.

MS. CANDACE GRAMMOND: So, Mr. Johnston, then would it be fair to say that the -- sort of the two (2) things that the external actuary observed that led to the recommendation were higher inflation and lower-trending interest rates?

MR. LUKE JOHNSTON: That's correct. And -- and the -- yeah, as -- as we've shown in the table here, the combination of those two (2) essentially leading to a real return of 0.6 percent and clearly -- yeah. In relatively short period of time, the real return dropped by basically 1 1/2 percent almost.

MS. CANDACE GRAMMOND: Now, in the context of non-indexed coverages, considering that a fixed interest rate margin represents an increasing proportion, as interest rates decline, of the assumed interest rate, why would declining interest rates call for an increase in the interest rate margin?

(BRIEF PAUSE)

MR. LUKE JOHNSTON: I apologize. I know that was a long question, but could I -- could I hear it one more time?

MS. CANDACE GRAMMOND: Yes, definitely.

So in the context of the non-indexed coverages and considering that a fixed interest rate margin represents an increasing proportion, as interest rates decline, of the assumed interest rate, why would declining interest rates call for an increase in the interest rate margin?

(BRIEF PAUSE)

MR. LUKE JOHNSTON: So if -- I just

want to make sure again I understand the question correctly. The question being: Why does the interest -- increased interest rate provision, why is that applicable to non-indexed lines given that the -- our appointed actuary's concern appears to be with a decline in the real return -- the real -- yield?

MS. CANDACE GRAMMOND: Yes, roughly.

MR. LUKE JOHNSTON: There is -- there is an IR discussing this. We -- we don't -- we do not select different interest rates by coverage, we do it on an overall basis.

There is -- it is possible we could consider having different interest rates, and different interest rate provisions by coverage. The vast majority of our claim liabilities are for inflation indexed benefits. So I believe we have stated this in an IR that we will consider looking at that. But the -- the magnitude of such a change I -- I believe is fairly small. I'll try to find a reference.

(BRIEF PAUSE)

MS. CANDACE GRAMMOND: We think, Mr. Johnston, the reference is at Tab 26 where there are actually two (2) IRs, 1-17 and 2-10. It may be 2-10 that you're thinking about.

(BRIEF PAUSE)

MR. LUKE JOHNSTON: Yes, thank you for that. So as it -- as it states in Part D of this question, the -- I'll -- I'll just read it in rather than trying to summarize it. Quote:

"The Corporation agrees that the use of different interest rate MFADs for different coverages is a possibility, and will consider such for future valuations. However, the impact of such a change is minimal. For example, if the interest rate MFAD for non-indexed coverages were left unchanged from that using the previous valuation, i.e., one hundred (100) basis points instead of one hundred and twenty-five (125) basis points, the unpaid claim liabilities will decrease by less than 0.5 million."

End quote. So I'm not -- I'm not trying to use this to indicate that -- that the approach you're recommending isn't reasonable. We'll consider it. We are indicating that the -- the impact is fairly minor and is something we could consider in the next valuation in our discussions with our appointed actuary.

(BRIEF PAUSE)

MS. CANDACE GRAMMOND: I -- I think really what we're asking, Mr. Johnston, is why for the non-indexed lines there wasn't a consideration of actually dropping the number rather than increasing it.

MR. LUKE JOHNSTON: Yeah, I -- I think I answered that, but I -- the -- really the -- the main reason right now is that we -- we decided to just select one (1) interest rate and one (1) interest rate provision for all coverages combined.

Again, I -- I do see your point that -- that maybe a different view is possible. And -- and we're definitely open to reviewing that with our appointed actuary. The impact is minimal but -- but maybe a better method could be used.

(BRIEF PAUSE)

MS. CANDACE GRAMMOND: Would -- would you agree that if, after consideration, the Corporation did agree to change the rate downward for non-indexed lines, that the impact could be more significant because it affects the indexed lines as well, or the indexed coverages as well?

(BRIEF PAUSE)

MR. LUKE JOHNSTON: Yeah, I'm sorry for the delay there. I -- I'm just -- I'm having trouble understanding the basis for -- for the question. So I -- I do understand the piece about using a different rate for non-indexed coverages. However, I -- I'm not understanding how that change would lead to a change in the overall margin and then any impact on indexed coverages.

MS. CANDACE GRAMMOND: Okay, fair enough, Mr. Johnston. Maybe I'll ask my next question, which is for an undertaking. And then once we get the result of that, maybe it'll become a little more clear for both of us.

MR. LUKE JOHNSTON: Thank you.

MS. CANDACE GRAMMOND: So here's the question by way of undertaking. And this is to illustrate the sensitivity with respect to these margin assumptions.

Can you provide the estimated impact on the net Basic claims liabilities as at February 28th, 2012, by component, subject to discounting, and in total arising from the adoption of the interest rate margin of a hundred basis points and seventy-five (75) basis points for indexed and non-index -- non-indexed coverages, respectively?

MR. LUKE JOHNSTON: Okay, so I -- I understand your request. So the first piece, if I understand, is that -- to see the impact of using an interest rate provision of one hundred (100) basis points. And earlier in your questioning, I -- I believe you stated for the Board that the impact was approximately $34 million.

So I'm wondering if we've already provided that piece of information.

(BRIEF PAUSE)

MR. LUKE JOHNSTON: And -- sorry, and I -- I don't want to oversimplify the -- the calculations, because they're -- they're not simple. But I would expect a additional quarter point reduction would be possibly a little bit larger but in the same magnitude of the first quarter point.

So if you -- if you -- if it was a $34 million impact for the -- for a quarter point, another quarter point, I -- it won't be identical, but I would assume probably in the 30, $40 million range.

MS. CANDACE GRAMMOND: So you would agree then that it would be a material change if it would be roughly in the same order of magnitude as the -- the change from a hundred to one twenty-five (125)?

MR. LUKE JOHNSTON: Absolutely the -- the -- a change in the interest provision is material. Thirty-four (34) million dollars is -- is very material. And we've -- we've noted in the report why the appointed actuary felt that that change was necessary.

If we come back in October, we review the information again, it's possible that our appointed actuary may decide that the provision that was added last year is -- is no longer required. I'm not going to say that that's what he's going to do. But, of course, I know I'm going to expect our appointed actuary to provide evidence for why the margin needs to remain at 1.25 percent. And -- so that -- that's all -- that's all I can really say.

I don't know -- I've talked earlier in -- in -- in my remarks about why I thought 1 percent was reasonable and I -- I do think it's reasonable for such a long-tailed business as MPI's. But again it -- it is -- it is -- it is judgmental, I -- I agree to that.

(BRIEF PAUSE)

MS. CANDACE GRAMMOND: Okay, Mr. Johnston, based on your evidence we're satisfied with respect to the undertaking that was requested, in terms of the -- the sensitivity piece. So you don't need to provide that detailed information. But we do appreciate the evidence that you gave with respect to considering a different approach and having that discussion with the external actuary.

MR. LUKE JOHNSTON: Yes, and I thank you for though -- those comments. We'll definitely consider it at the October review.

MS. CANDACE GRAMMOND: Okay. Now with respect to the indexed coverages, can you tell us the authority for the assumed future inflation assumption of 2 percent?

(BRIEF PAUSE)

MR. LUKE JOHNSTON: Again, I -- I believe there's a reference. I'll just try to find it.

MS. CANDACE GRAMMOND: Yeah, we couldn't find one, so. But please -- please tell us.

THE CHAIRPERSON: TI.18, Section 1.3.

MR. LUKE JOHNSTON: Thank you.

(BRIEF PAUSE)

CONTINUED BY MS. CANDACE GRAMMOND:

MS. CANDACE GRAMMOND: We understand that that reference -- thank you, Mr. Chairman -- that that reference reflects that the assumption is 2 percent.

What we were hoping to learn was where that was -- stemmed from or what the basis was for that assumption or the authority for it.

MR. LUKE JOHNSTON: Okay. So I'm looking at TI.18, page 3, and there's a table on that page under the title "Summary of Economic Forecast Variables." And in that table there is a history along with a projection for inflation. And underneath of that table there is a list of multiple sources: Global Insight, TD Bank, Royal Bank, BMO, Scotiabank.

And the -- these are the -- we've -- you know we've -- and my understanding is we take all these forecasts from the bank and we -- we use the median forecast with -- and some cases around it and that's -- that's the basis for the -- for the forecast of 2 percent.

(BRIEF PAUSE)

MR. LUKE JOHNSTON: This is -- this is a similar approach we follow with interest rates as well. We don't believe that we have better information than the banks or the professional forecasting agencies to forecast interest rates or inflation rates. We rely completely on them and generally select a median forecast from those -- those banks and forecaster agencies.

(BRIEF PAUSE)

THE CHAIRPERSON: You talked about the -- the impact of a change in -- of interest rate on the claims liabilities. But leaving the changes to interest rate in isolation and looking at inflation rate, what impact does it have on your liab -- on your liabilities?

In other words, assume that interest rates don't change but inflation increases, which is one of the concerns of your actuary, if that was to change in isolation of the interest rate what happens to liabilities? Say it goes up 1 percent, what happens?

MR. LUKE JOHNSTON: Yeah, it would be similar. We talked about a quarter point being about $33 million. So if -- if we had assumed a quarter point higher inflation, you'd get approximately the same impact, an -- an increase of about 33 million.

(BRIEF PAUSE)

MR. LUKE JOHNSTON: A 0.1 percent change, or a ten (10) basis point change, in our interest rate for any reason, whether we were to increase the inflation rate or -- or just the yield dropped, is about $12 million on the total -- total value.

And we -- clear -- clearly given that rates have declined so significantly, if we did not have our, what we call our asset liability management program, we would have saw very significant increases in claim liabilities. However, we have -- we essentially attempt to match the duration of our assets or the -- the approximate average cash flow of our assets to our liabilities, so when interest rates change you get an impact on claims. And we hope to get a fairly sig -- similar impact on asset values.

And it -- it's proven to work fairly effectively in the past. It's never perfect but -- but it's approximately equal. So I don't have numbers in front of me but it's -- it -- the assets are believed to cover about 80 percent of the -- any changes in liabilities that you have from interest rates.

THE CHAIRPERSON: You know, the -- the -- I hate to interrupt here but I just want to under -- give you my understanding of -- last year Mr. Palmer testified that, if I remember correctly, that you were covered approximately 80 percent for the swings in -- in interest rates and so on. In other words, you -- your portfolio was designed such that there was only 20 percent that was uncovered, I guess.

Now, I guess what I'm -- I'm currently struggling with, like a lot of other individuals, is this issue of a -- of an interest rate shock where suddenly we have a tremendous increase in interest rates, and what impact that'll have on your portfolio. And I guess the other side of it is what -- what impact it has on your claims liabilities, so.

(BRIEF PAUSE)

MR. LUKE JOHNSTON: I -- I believe there's a reference. I'll try to find it quickly. If -- if I can't I'll -- I'll let you know, and get back to you. Let me just have a look.

(BRIEF PAUSE)

MS. MARILYN MCLAREN: Mr. Chairman, while we're searching I can tell you that unlike the people at MPI who worry about our claims liabilities, our bond manger is hoping for one of those big spikes in interest rates that you talk -- talked about.

And one of the things he's thinking about is, you know, the extent to which it makes sense to continue to sit on more cash than we would normally have in anticipation of an upward move in interest rates.

It's -- it's a difficult question and something that, you know, we do talk about and consult with because we really take great comfort from the fact that we have this matching to, you know, about the 80 percent that you mentioned. So one could take the position that well, you know, if you're matched to that extent don't -- don't even worry about what return you're going to get on the bonds that you purchased because, you know, they're matching your liabilities.

But -- but Mr. Gibson is -- is, you know, still the investment fund manager, he's responsible for it, and he really wants to balance that perspective with really trying to anticipate how to possibly get the best returns.

Corporately, you know, we're -- we're comfortable with the matching, but there -- there's always that kind of dual side of it.

MR. LUKE JOHNSTON: And I do have a reference that -- that may be helpful, PUB-1-11. And I can just talk to it.

Basically, the -- the response indicates that the average yield on the bond portfolio dropped from 4.10 percent in February to 3.55 percent in February of -- the following February, 2012. That was a $75 million increase to claim liabilities. The equivalent change on the assets, the fixed income assets, was a $65 million -- $65.8 million impact, so approximately 88 percent of the liability change.

And the reason the asset impact is lower now is because the -- our -- Mr. Gibson has flexibility to keep the duration of assets within two (2) years of liabilities. He may have different reasons for being above or below that -- that target. Right now he happens to be below. It's probably fairly difficult to have an average duration of bonds in excess of ten (10), which is close to what our basic liabilities duration is.

(BRIEF PAUSE)

THE CHAIRPERSON: Go ahead, sorry.

CONTINUED BY MS. CANDACE GRAMMOND:

MS. CANDACE GRAMMOND: Thank you. No, it's fine.

Mr. Johnston, I just want to clarify something that you said a couple of minutes ago. We're not sure if we heard it correctly.

Did you say that the impact of a -- of a 1 percent change in interest rates would be 12 million, or what -- what was -- what was it with the 12 million that you said?

MR. LUKE JOHNSTON: Point 1 (.1) of a percent, so ten (10) -- ten (10) basis points is approximately 12 million. As the changes get larger, that ceases to be true depending on which direction you go. But for -- for a small change, it's about 12 million. For multiples of that, it's approximately equal to that, but, yeah.

MS. CANDACE GRAMMOND: Okay, so if -- if point one (.1) of a percent is 12 million, then 1 percent would be about 120 million?

MR. LUKE JOHNSTON: Yeah. Unfortunately, it doesn't work out quite that way because the -- something called convexity. I won't go into that. But the -- the incremental change increases or -- or decreases depending on which direction you're going.

Again, I -- I do believe we have an IR showing the -- the two (2) -- two (2) different directions, half a point up, half a point down. They're definitely not equal. But for -- for a small change, it's -- it's about 12 million. And -- yeah.

(BRIEF PAUSE)

MS. CANDACE GRAMMOND: Mr. Johnston, is that change in interest rate or change in inflation that we're speaking of?

MR. LUKE JOHNSTON: That would be a change in the -- the real interest rate. Ju -- as a way of example, I was just indicating that a change in the -- the real interest rate could be caused if you change the inflation rate by point one (.1), for example, all things equal. But, yeah, any -- any change of -- of point one (.1), rather inflation or just the nominal rate.

(BRIEF PAUSE)

MS. CANDACE GRAMMOND: Okay. Mr. Johnston, you spoke about part of the Corporation's response at 2-10. So this is at Tab 26 of the book of documents, the second IR that we see there. And you had commented about (d). I'd ask you now to tell us about what we see at (b), if you can describe and interpret that information for the Board.

MR. LUKE JOHNSTON: Sorry, at -- at what subsection?

MS. CANDACE GRAMMOND: 2-10(b). This is at Tab 26.

MR. LUKE JOHNSTON: So (b), where the answer being the assumed inflation rate is based, et cetera, that -- that --

MS. CANDACE GRAMMOND: No. No, you're looking at something different. Oh, okay, you're looking at 1-17. So if you just continue on in that tab you'll find 2-10 is right behind it. And that would be the (b) that I'm asking about.

(BRIEF PAUSE)

MR. LUKE JOHNSTON: Yes, so the -- the question in (b) is addressing the impact between the indexation -- the actual indexation adjustment of one point o-o-eight (1.008), or .08 percent, versus our assumed inflation rate of 2 percent in our -- in our valuation. And part (b) provides the answer to that.

And I -- I don't -- I don't think it's necessary to go through all the numbers. But the -- the impact of the actual being .8 percent instead of two (2) was, I guess, a savings or -- or a lower number, by 12.7 million. If the adjustment had been 2 percent instead of .8 percent, the impact would have been 12 million higher. And that would have flowed through net income.

MS. CANDACE GRAMMOND: Thank you. I'm going to move then into questions with respect to the Dynamic Capital Adequacy Testing, or DCAT.

Mr. Johnston, when you gave direct evidence on Tuesday regarding your work with respect to the DCAT, you stated that you're guided by the profession's actuarial standards of practice.

Is that right?

MR. LUKE JOHNSTON: That's correct.

MS. CANDACE GRAMMOND: Now, I understand that actuaries also get guidance from sources other than the standards of practice, such as educational notes.

Is that right?

MR. LUKE JOHNSTON: Yes, that's correct. In -- in the case of the DCAT, there -- there is an educational note.

MS. CANDACE GRAMMOND: And you had guidance from that educational note in your work on the DCAT?

MR. LUKE JOHNSTON: Yes, I did. The -- the educat -- educational notes go into a lot more detail than the -- the standards, which are more general in nature.

MS. CANDACE GRAMMOND: Now, I'm advised that the scope of the DCAT standards of practice reads as follows in Section 2510.01, quote:

"This Section 2500 applies to the appointed actuary of an insurer when preparing a report on the insurer's final (sic) condition pursuant to law."

End quote. Sorry, not final condition; financial condition pursuant to law, pardon me.

Would you agree with that, subject to check if you wish?

MR. LUKE JOHNSTON: I see that. I agree.

MS. CANDACE GRAMMOND: Now, strictly speaking, would it be correct to conclude that this standard of practice is not binding guidance for the DCAT that you've prepared, since it's not pursuant to law?

(BRIEF PAUSE)

MR. LUKE JOHNSTON: Sorry, I -- I just -- just thinking about that a little bit. So clearly, as an actuary, I'm -- I'm -- I should follow, and do follow, accepted actuarial practice.

Is the DCAT report in this province pursuant to law? No, it's not. Have I followed actuarial standards of practice in preparation of this report? Absolutely.

MS. CANDACE GRAMMOND: So -- just so that I understand you correctly, you followed the standards, even though doing so was not strictly required, given the task?

MR. LUKE JOHNSTON: It's -- it's -- the DCAT is not required by law in this province, so, yeah.

(BRIEF PAUSE)

MS. CANDACE GRAMMOND: At the end you said, "So, yeah." Yes?

MR. LUKE JOHNSTON: My apologies, yeah. Not a professional answer. The --

MS. CANDACE GRAMMOND: I -- I'm not criticizing your semantics. I just want to make sure that I understand that you're agreeing that you did follow the standards, even though you didn't strictly have to, in the DCAT. That -- that's all I'm trying to ask. I'm not trying to accuse you of anything.

MS. MARILYN MCLAREN: If -- if I can attempt -- a bit of an explanation, I think, is likely what Mr. Johnston is struggling with. It -- again, you know, the un -- uneducated non-actuary here is speaking.

It kind of sounded like you were saying that his professional standards don't really require him to follow professional standards, because DCAT is not the law in Manitoba. And I don't think that's what you were -- that's what you were trying to get at. I mean, I think it's important to Mr. Johnston that he says he did follow the standards, and the fact that this is not a regulated requirement here in Manitoba, unlike it is with OSFI and others, right.

That -- that's -- that's, I think, maybe just the terminology of the question. It -- he comp -- followed the standards and, no, it's not the law. But that doesn't imply that he somehow didn't need to follow the standards, because as a professional actuary he feels very bound by his requirement to follow standards.

MR. LUKE JOHNSTON: So I can confirm your previous question.

MS. CANDACE GRAMMOND: Okay. Now, I'm advised that the term "financial condition" is defined in the actuarial standards of practice as follows, quote:

"Financial condition of an entity at a date is its prospective ability at

"...that date to meet its future obligations, especially obligations to policy owners, members, and those to whom it owes benefits."

End quote. Would you agree, again subject to check?

MR. LUKE JOHNSTON: I would agree with that statement.

MS. CANDACE GRAMMOND: I'm advised that the purpose of the DCAT, as outlined in the Standards of Practice -- and this is in Section 2520.08 -- is as follows, quote:

"The purpose of Dynamic Capital Adequacy Testing is to identify plausible threats to satisfactory financial condition, actions that would lessen the likelihood of those threats, and actions that would mitigate a threat if it materialized."

Again, would you agree with that, subject to check?

MR. LUKE JOHNSTON: I agree, and I've checked it. Thanks.

MS. CANDACE GRAMMOND: So what is, in

your view, the phrase -- or, what is the meaning, I guess, of the phrase "satisfactory financial condition," as used in that definition of DCAT -- or, purpose of DCAT?

(BRIEF PAUSE)

MR. LUKE JOHNSTON: I'm just turning to AI.11 part 2, the amended DCAT report, on page 12.

And, again, sorry, that's Volume 3, AI.11, part 2.

(BRIEF PAUSE)

MR. LUKE JOHNSTON: In -- on page 12, under the -- under the heading, "Definition of Satisfactory Future Financial Condition," I've defined the -- this -- this term as follows, quote:

> "The Corporation's financial condition is satisfactory if throughout the forecast period it is able to meet all its future obligations under the base scenario and all plausible adverse scenarios, and under the base scenario it meets

the minimum regulatory capital requirement."

MS. CANDACE GRAMMOND: Now, that language about meeting its future obligations, does that stem from language in the standards that talks about assets being greater than liabilities?

MR. LUKE JOHNSTON: Yes. And in this case where assets greater than liabilities or an RSR greater than zero.

MS. CANDACE GRAMMOND: So would you agree that a consideration of that analysis, assets versus liabilities, implies a focus on solvency?

(BRIEF PAUSE)

MR. LUKE JOHNSTON: Yeah. In regards -- in regards to solvency for a private insurer, having assets less than liabilities could be -- or, is described as perhaps insolvency. That's not what -- we're not assuming MPI is going to go insolvent if RSR falls below zero.

This is -- however, as -- as I've just read, this is the -- the definition we're using for defining "satisfactory financial condition." However, we believe that this purpose is -- is very consistent with the stated purpose of the rate stabilization reserve in that it significantly prevents rate shock. If we do fall to a negative RSR position, we will be required to rebuild or recover our retained earnings, and that'll require rate increases or rate surcharges.

So I -- yeah, I agree that that particular definition seems to indicate a solvency basis but we believe the considerations related to the purpose of the RSR are -- are similarly addressed through that definition.

(BRIEF PAUSE)

MS. CANDACE GRAMMOND: So, Mr. Johnston, following on that evidence and the -- the solvency piece that's included in the DCAT, and given MPI's situation and that it is what it is, what, if any, steps ha -- has MPI taken to adapt the DCAT process, as outlined in the Standards of Practice and the related educational note, to make it relevant to the determination of the target for MPI's RSR?

(BRIEF PAUSE)

MR. LUKE JOHNSTON: So I -- I did talk

a little -- a little bit about this in direct but I'll -- I'll go through it because it is important.

As you'll see again on that page 12, we are using -- we're not using private sector regulatory capital requirements to determine satisfactory future financial condition. We are looking at the regulatory rules in this province. That's one.

The scenarios described in the report are definitely MPI specific; they are specific to our particular risks and situation, our -- our coverages, our program.

Third, the -- a -- the reasonable period to which the Corporation could react to the adverse scenarios is considered. Generally we assume we could put in a rate change or a rate surcharge within a couple of years of the adverse scenario occurring. We -- we don't, of course, assume that we're going to lose any business or anything like that that would be a consideration for a private insurer.

(BRIEF PAUSE)

MR. LUKE JOHNSTON: I'm sure I've listed other reasons in the evidence, they're not coming to my mind at the moment, but those are the main ones I believe.

(BRIEF PAUSE)

MS. CANDACE GRAMMOND: So, Mr. Johnston, if we've heard you correctly you've talked about changing the assumptions appropriately for MPI. You've also talked about changing the -- the reference point with respect to the supervisory target. Are there any other changes that -- that derive from the standards -- or that -- sorry, that depart from the standards that MPI implemented in its work?

(BRIEF PAUSE)

MR. LUKE JOHNSTON: I guess one thing I'm concerned about with the question is that it seems to be implying that I've already departed from the standards.

(BRIEF PAUSE)

MS. CANDACE GRAMMOND: Mr. Johnston, maybe I can rephrase a little bit so that I'm getting -- getting our point across. It -- it's our view that, given other circumstances in which the DCAT is used as compared with what MPI is proposing, that there could be changes that would be made, given that MPI does not have solvency issues.

We -- we're hearing that one of the changes that was made was with respect to the reference point for the supervisory target. And we're trying to get at whether there were any other changes that MPI has incorporated in its analysis because of the fact that MPI is a Crown Corporation and so on.

(BRIEF PAUSE)

MR. LUKE JOHNSTON: So the -- there's definitely a change in the DCAT, not -- not deviating from standards. Simply, the DCAT should reflect the regulatory rules of the -- the jurisdiction that you're operating in. The -- outside of that, the -- the risks to MPI are -- were assessed as they would be expected to occur for the Corporation.

We went -- I went through the entire spectrum of risks in the DCAT educational note along with any others that I thought were applicable. These are Manitoba impacts. They're not private sector impacts. They're in no way related to risks in the private sector.

The -- the impacts that occur are -- and -- and what MPI does after that is reflective of what will actually happen in this province. It has the expected regulatory actions in this province.

So, yeah, I don't -- I wouldn't say I've deviated at all from standards but merely just reflected the -- the Manitoba situation as accurately as possible.

(BRIEF PAUSE)

MS. CANDACE GRAMMOND: Now, MPI describes the adverse scenarios used in the DCAT as "plausible". How would you define "plausible"?

MR. LUKE JOHNSTON: I used the guidance from the DCAT educational note. And the goal is to have the scenarios within 1 percent to 5 percent probability of occurrence. That also includes the assumed management and regulator actions. So I can't put in a plausible equity scenario and then assume no response whatsoever from MPI or the Board. So the combination of a -- of appropriate assumptions in the scenario and, of course, appropriate management and regulatory actions.

MS. CANDACE GRAMMOND: Now, just in terms of the language, when you talk about an event with a 1 to 5 percent change of occurring is that the same as saying an event that's in the 95th to 99th percentile?

MR. LUKE JOHNSTON: Roughly, or you could say the -- depending on the -- it could be the first fifth percentile depending on what side of the -- the bell curve you're looking at.

MS. CANDACE GRAMMOND: And if -- if we're talking about the percentile, can you explain how that set of language is -- or that set of language corresponds with some of the other language that we sometimes see in the -- in the documents that's a one (1) in twenty (20) year, or a one (1) in one hundred (100) year event.

MR. LUKE JOHNSTON: The fifth percentile would mean, for example, that 5 percent of observations would be expected to fall below that number. Similarly for the 95th percentile, you would expect 95 percent of -- of observations to fall below that -- that number.

Those assumptions are easier to make when you have something like stock return data where you have lots of history and you can say that you actually know what -- what number -- what the number is where 5 percent of the observations are below that point.

The -- a 5 percent probability of occurrence would be equivalent to say a one (1) in twenty (20) year event, just basically the reciprocal. A 1 percent similarly would be a one (1) in a hundred (100) year event.

MS. CANDACE GRAMMOND: Thank you. Now, I'm advised that the DCAT educational note includes the following provision. Quote:

> "When stochastic models with reasonable predictability are available, an adverse scenario would be considered plausible if it reflects the 95th to 99th percentile of outcomes. Generally a 95th percentile or greater result would be required for a scenario to be deemed adverse, but less than or equal to a 99th percentile for the scenario to be deemed plausible."

End quote. Did you consider that guidance in carrying out the DCAT?

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

that's the point we've been discussing. That's -- that's where I got that guidance, yeah.

MS. CANDACE GRAMMOND: And did all of the adverse scenarios that you tested fall within the range of 95th to 99th percentile outcomes?

MR. LUKE JOHNSTON: Yes, that's essentially what is trying to be shown in the reports. In some cases, I have a lot more support to -- to make those judgments in some cases. There's other scenarios where it's a lot more difficult to -- to assess that.

So the -- the basis of the -- the report, the key scenarios, the equity scenario, and the combined equity and claims incurred scenario, I do believe we have a very significant amount of historical evidence for me to confidently state that -- that -- you know, or to make a reasonable judgment that the scenarios I produced are in the 1 percent of 5 percent probability of occurrence.

Of course, other people may have different judgments on that but I provided as much evidence as possible to support those judgments.

MS. CANDACE GRAMMOND: And did you vary the plausibility level -- plausibility level between adverse scenarios?

(BRIEF PAUSE)

MR. LUKE JOHNSTON: The -- not all scenarios were picked at the -- the same plausibility level. The equity scenario we used all history since 1919. And we found that the 5th percentile was approximately 43 percent, I believe. We judgmentally selected a 40 percent decline. For the claims scenario, we -- we ran a one (1) in a hundred (100) year event.

So there -- so -- sorry, to answer your question, no, we didn't use the exact same probability in every scenario.

MS. CANDACE GRAMMOND: And why did you chose different levels of plausibility among the scenarios?

MR. LUKE JOHNSTON: Although there is, as I've mentioned for these particular scenarios, a significant amount of evidence, there is still some judgment required in -- in this tail period. It is -- it does reflect more extreme values.

For -- for claims, I believe it's -- we can feel more strongly about -- about the output. For equities, we have had some discussions on the -- during the direct about other views on equity returns.

We -- looking at the history, we selected 40 percent as reasonable, recognizing that, you know, a more recent period hasn't had as many significant declines as maybe a longer period, as -- as discussed by Professor Simpson.

THE CHAIRPERSON: Since we're talking about the -- that scenario, I guess I'm struggling with the -- you know, the -- the fact that you wouldn't sell any stock if you had a drop of 40 percent. I mean, you don't -- you don't -- I don't perceive that MPIC would need the cash immediately. So you would just hold your position and wait for a few years and then you'd sell that stock if you needed it. So I guess, you know, a lot of people lost money because they sold their stock at a time when they shouldn't have sold it and those that kept their stock saw their values return.

So you -- so in -- in -- in the Panel making its decision, would -- why would you expect us to believe that you would sell that position out after a 40 percent drop?

(BRIEF PAUSE)

MS. MARILYN MCLAREN: I'll ask Mr. Johnston to speak to his assumptions in the DCAT. But

I can tell you back in '08 and '09 we were a little bit surprised when we saw the extent to which the different equity investment managers that -- that are hired for our fund continued to sell and buy and continue, even with significantly depreciated value of, you know, some of the stocks in their portfolios. They were -- we recognized, you know -- I mean, the way the accounting rules work, we have to recognize in net income actual sales where -- where there is a loss from book value.

And then we also, you know, through the year-end audit process we -- the external auditors take a very hard look. And we -- and every year, even in a good year, there are some stocks that it's recognized that they are now being held for less than we paid for the and we have to recognize that, and that goes into net income as well.

So the activity continued in '08/'09, and -- and from that I would expect that that would happen again in the future. And even if they do hold it, waiting for it to recover, if the auditors believe that it's not likely to, we have to recognize that loss, right, in the net income as well.

MR. LUKE JOHNSTON: So just -- just to follow on that. The -- the DCAT has assumed that the regular turnover rate of the equity portfolio is about one-third (1/3) a year, based on internal information. We've also assumed in that first year that, given the significant level of the decline, we'd also write down about a third of the equity investments.

(BRIEF PAUSE)

CONTINUED BY MS. CANDACE GRAMMOND:

MS. CANDACE GRAMMOND: Thank you. So just continuing to talk about the plausibility levels. If a plausibility range of the 95th to 99th percentile outcome is appropriate for a solvency-focussed DCAT, what would you suggest is an appropriate plausibility level for an RSR-target-level-focussed DCAT?

In other words, how severe of an event should be tested for the purposes of setting the RSR target range?

MR. LUKE JOHNSTON: This -- this is -- clearly involves some judgement. And there is -- I will point to Professor Simpson's evidence where he provided some historical insight about the Board's risk tolerance. And -- for example, the risk analysis uses a 95 percent to 97.5 percent confidence interval. So the -- the DCAT plausibility or probability range is approximately in line with that.

It does consider, perhaps, scenarios that are a little bit less plausible than the Board has indicated that its risk tolerance level if -- if you assume that 97.5 percent is the Board's risk tolerance level. I don't want to assume that, but.

So we believe that the DCAT kind of falls within that same range. At the same time, if -- if the Board does have a risk tolerance level of one (1) in forty (40), that's something that can be modelled in the DCAT, and, yeah, we can definitely show the Board what the one (1) in forty (40) year event is to the best of our ability for -- for every scenario.

THE CHAIRPERSON: Could I ask you a question in respect of risks, specifically with the regulatory risk. In other words, provincial government decides that it will enrich the PIPP program, and what -- what had been a practice in the past when the government has modified the PIPP program? Did it make the benefits retroactive?

MS. MARILYN MCLAREN: Actually, even well before PIPP, right from 1971 when we had limited no-fault benefits and also tort opportunities for non-responsible parties to recover, the no-fault benefits every few years -- the weekly indemnity, the salary compensation piece -- every few years that would increase.

A few times during that period the medical expense coverage increased. The medical expense coverage increases did not necessarily apply to existing claimants, but the income protection improvement always did. So there are sometimes rare examples of when benefit improvements are not provided to existing claimants, but that tends to be the exception with -- with programs like this.

It's very, very hard, I think, for governments to recognize that, you know, the -- the legislative standard of benefits is -- is not sort of meeting the test of what people require and then only give it to claimants going forward and not -- not the existing claimants. So for the most part, it has generally been retroactive more than not.

THE CHAIRPERSON: Can you give us a scale of, you know, what -- what's been the impact financially of perhaps a major change -- an example of a major change to -- to the PIPP program?

MS. MARILYN MCLAREN: The changes that were made in 2009, I believe, were the most extensive ever. And -- and we estimated at that time that it would be about a $90 million impact on the -- the cost of existing claims. So that would be $90 million on at that time would have been about a billion dollars of liabilities at that time. So fairly significant impact in year, but -- but in terms of the overall liability, still a reasonably smaller portion.

And we tend to be a little bit conservative when -- when we estimate the impact of things like that. It's new territory. We don't know for sure what it will cost. And I think we're sitting at about 70 or 75 million now in terms of what we think that 90 million has been reduced somewhat. So that -- that's the -- that was the most extensive -- some significant improvements there.

Things like -- one of the most costly, one of the most extensive is -- is we always -- part of the legislation had always said people who -- kids. If kids are catastrophically injured and are never, ever able to enter the workforce, they would always receive an income indemnity for the rest of their lives based on the average industrial wage.

If someone had been injured fairly early in their career, maybe they were only making slightly more than minimum wage, they would have that salary they were earning at the time they were severely injured indexed for the rest of their life, but it would always be anchored to what they were earning when they were injured.

The changes in '09 allowed for anyone who meets the test of catastrophic injury, which really means there's no expectation that these people will ever reenter the workforce. No matter what they were earning before they got hurt, they will receive a minimum of the average industrial wage.

So that -- that was one of the most fundamental changes at that point. And in my memory, there hasn't been another extensive change like that in pre-PIPP or during PIPP.

CONTINUED BY MS. CANDACE GRAMMOND:

MS. CANDACE GRAMMOND: Mr. Johnston, just following up on the -- the last answer, what I'm going to ask you to do is just leave aside the -- the risk analysis and what the Corporation thinks the Board might think and just ask you -- and -- and even leave aside what's in the educational note, because that relates to sort of a solvency-based test -- what do you think -- what -- what do you/the Corporation think the -- the percentile range should be?

(BRIEF PAUSE)

MS. MARILYN MCLAREN: Rather than have -- rather than have us ask Mr. Johnston to sort of leave all those standards and educational notes aside and have a personal opinion, I'll -- I will give this my shot.

The Corporation is -- is very comfortable with the approach of the DCAT. I mean, that's, in large -- in large part, for all the reasons we've talked about, why we are really recommending this -- this approach to this Board.

We're very comfortable with those, remembering that this is really an attempt to provide rate stability for Manitobans; remembering that, you know, there's all kinds of things that can happen to have negative net income in any given year and chew up the RSR, other than the scenarios that met the test in the DCAT, so that those are not, you know, the only potential two (2) bad things that can happen.

We can have several years of the kind of hail we had last year or the year before, and it will be significantly chewing up net income. So we're -- we're very comfortable with that approach.

I think that -- the fact that there is any number of things that can happen and with this structured, disciplined approach of identifying sort of the -- the worst-case plausible scenarios, we -- we stand behind that.

THE CHAIRPERSON: I think it's an opportune time to take a few minutes. Let's take ten (10) minutes and back in this room at 11:00. Thank you.

--- Upon recessing at 10:51 a.m.
--- Upon resuming at 11:06 a.m.

THE CHAIRPERSON: Ms. Kalinowsky, ready to go?

MS. KATHY KALINOWSKY: Yes.

CONTINUED BY CANDACE GRAMMOND:

MS. CANDACE GRAMMOND: Okay. So, Mr. Johnston, I do have some more questions about the DCAT, and I'll start off just by following on some of the discussion that went on before the break.

When -- when we talk about the equity decline scenario, can you clarify whether it's the drop in the value of the equities in that scenario or the realization of the consequent loss that affects the RSR level?

(BRIEF PAUSE)

MR. LUKE JOHNSTON: Yes, it's the -- it is the -- it's the combination of the -- the total return being negative 40 percent and then the subsequent recognition of -- of those losses as the equity portfolio is -- is turned over.

MS. CANDACE GRAMMOND: And that's either through sale or a write down?

MR. LUKE JOHNSTON: That's correct.

MS. CANDACE GRAMMOND: Now, you had mentioned, Mr. Johnston, a reference to one-third (1/3) in terms of that loss or the -- the realization of that loss.

Is that -- were you referencing one-third (1/3) of the whole of the equity portfolio, or one-third (1/3) of the 40 percent decline?

(BRIEF PAUSE)

MR. LUKE JOHNSTON: That is roughly the historical turnover rate of our -- of our total equity portfolio, one-third (1/3).

MS. CANDACE GRAMMOND: So what is that roughly in dollars?

(BRIEF PAUSE)

MR. LUKE JOHNSTON: Roughly one-third (1/3) of 450 to $500 million, so 150 million.

MS. CANDACE GRAMMOND: Now, can you tell us about the historical experience of the Corporation with respect to permanent impairments?

Do you know what the -- the most significant permanent impairment has been, historically?

MR. LUKE JOHNSTON: Like equity asset impairment?

MS. CANDACE GRAMMOND: Yes.

MS. MARILYN MCLAREN: The most significant year of write downs was -- it would have been the '08/'09 fiscal year.

MS. CANDACE GRAMMOND: Do you remember what the number was roughly? We think it might have been 24 million.

MS. MARILYN MCLAREN: That sounds about right, but we'll -- subject to check.

MS. CANDACE GRAMMOND: Mr. Bunston nodded his head in the back, so...

MS. MARILYN MCLAREN: That probably counts as a check.

(BRIEF PAUSE)

MS. CANDACE GRAMMOND: Okay. Now, we know that the Corporation is recommending a minimum RSR target level of 200 million, and we believe that that's based primarily on the -- the adverse scenario which you have found to be the most significant, which is the equity, the client scenario.

Is that fair to say?

MR LUKE JOHNSTON: That's fair.

MS. CANDACE GRAMMOND: Now, looking at the table of results for that scenario -- and this is on page 19 of the DCAT, in AI.11, part 2.

(BRIEF PAUSE)

MR. LUKE JOHNSTON: I'm there.

MS. CANDACE GRAMMOND: Can you confirm that the $200 million target recommendation is based on the difference from forecast -- or, sorry, difference from base forecast and retained earnings for 2014/'15? And that's in the lower table on the page.

MR. LUKE JOHNSTON: That's right. That's the expected impact, assuming the -- the stock market decline occurs in '13/'14, and that's the -- the total impact by the end of the '14/'15 year.

MS. CANDACE GRAMMOND: And so why is it that '14/'15 is the critical year with respect to the recommendation?

(BRIEF PAUSE)

MR. LUKE JOHNSTON: If the decline occurred in '13/'14, the -- the rates for '13/'14 would already be set. It's -- it's also quite possible that we would not know the full extent of the magnitude, in terms of setting the '14/'15 rates. So the assumption here is that no significant rate action would occur until the '15/'16 year, based on, obviously, the knowledge of the decline that we have when we're setting that year's rates.

MS. CANDACE GRAMMOND: So would it be fair to say, then, that the expectation is there would be action taken to try to mitigate the results that are shown here for 2015/'16 and 2016/'17? That's the 229 million and the 260 million lost, respectively?

MR. LUKE JOHNSTON: Yes. The assumption, of course, is that we'd continue to set rates to break even, of course. We also know that -- the Board's existing RSR targets, and this would be substantially below -- below those amounts.

Clearly, I don't know the -- the actual actions that the Board will take, but I'd assume that something will occur, a rate change and/or a surcharge.

MS. CANDACE GRAMMOND: And -- but those changes have not been modelled in the DCAT - that is, a rate change or a surcharge?

MR. LUKE JOHNSTON: Correct. So -- yeah. As I -- I didn't feel appropriate to just assume what I think the Board would do, but I assume that there will be action that will make the 229 million impact, for example, in '15/'16 not -- not plausible. And we would reduce that impact, I would assume.

MS. CANDACE GRAMMOND: Okay. Now, you've indicated that if the Board were to adopt the 200 million minimum RSR target level, that you would find the Corporation's financial condition to be satisfactory.

Is that right?

MR. LUKE JOHNSTON: A target based on this report of $200 million or greater would lead to satisfactory financial condition.

MS. CANDACE GRAMMOND: Now, since the definition of "satisfactory financial condition" in the DCAT report applies the relevant tests throughout the forecast period, which extends to 2016/'17, why would adoption of the 200 million minimum target level lead the Corporation to a satisfactory financial condition?

(BRIEF PAUSE)

MR. LUKE JOHNSTON: So basic -- basically as of the date of this report, $200 million or more in RSR would allow the Corporation to maintain RSR balance above zero in all of these scenarios through the entire forecast period. Again, with the assumption of management and regulatory action occurring in the '15/'16 year and -- and thereafter.

(BRIEF PAUSE)

MS. CANDACE GRAMMOND: So I -- I assume that you would agree that reasonable stability is a desirable attribute for the RSR target level?

MR. LUKE JOHNSTON: I agree you -- we -- we'd want the -- the target to remain fairly stable.

MS. CANDACE GRAMMOND: Now over the last three (3) GRAs the Corporation's DCAT-based recommendation for the minimum target level has varied from 185 million two (2) years ago to 210 million last year and then to two hundred (200) this year.

Assuming that those numbers are correct would you characterize those changes as reasonably stable?

(BRIEF PAUSE)

MR. LUKE JOHNSTON: Yes, I -- I'm -- I'm fairly comfortable with that level of stability, recognizing the -- that we are -- we do have an excess of $2 billion of assets, and those allocations do change and forecasts do change. We will continuously improve our -- our models as well. In some cases there are model changes that result in differences. But if -- if a target range was able to stay within 10 to 20 million, given the significant risks that we do have, I'd be happy with that level of variability.

MS. CANDACE GRAMMOND: And would you attribute the -- the changes that I've described over the last few years in -- in what has been recommended as a reflection of changing ris -- risk levels within the Corporation or just improvements in the modelling process?

MR. LUKE JOHNSTON: I haven't -- I definitely haven't quantified the specific impacts. We do know that the higher RSR target was generated by a forecast -- forecasted higher equities than we have today. So yeah, again, clearly if the Corporation's risk profile changes the DCAT has to change, and should change.

The -- but again, continual model improvements should refine some of the numbers. I would actually hope that again that would make things more stable as we improve and refine these models.

(BRIEF PAUSE)

MS. CANDACE GRAMMOND: Okay, can you tell us whether the type of variability over the last couple of years that we're talking is something that may -- we may expect to continue to see, going forward?

(BRIEF PAUSE)

MS. MARILYN MCLAREN: Referring back to what we talked about in terms of what is the purpose of the target, I think -- I think this Board should be very comfortable with a target that moves, you know, 5 to $10 million from year to year, reme -- remembering that the purpose of the target is, you know, is a rebate warranted, is a surcharge warranted.

If it's at one ninety-five (195) instead of two hundred (200), if it's at two ten (210) instead of two hundred (200), you're not going to have a surcharge, in all likelihood, unless there's some serious indicative negative trends going forward.

So we're very comfortable in suggesting that the Board ought to find comfort in that kind of an annual movement around a number of two hundred (200).

MS. CANDACE GRAMMOND: On Tuesday, Ms. McLaren, you made it very clear in your direct evidence that control over the Corporation's investments does not reside with the Corporation.

Given that the composition of the investment portfolio has a significant bearing on the results of the DCAT, does this lack of control by the Corporation represent a further risk to it? And, if so, does the DCAT capture this risk?

And this may be a question for Mr. Johnston. I'll leave it up to you as to who wants to answer.

(BRIEF PAUSE)

MS. MARILYN MCLAREN: I -- I think I'm

confident in saying that -- that -- confident enough in my knowledge of the DCAT that it really -- it's based on forecasts that -- that reflect the Corporation's forecast, particularly starting with the base forecast.

So, no, I don't think that's a risk, because what we're dealing with here, and if -- you know, if -- we are dealing with the administration of and the financial stability of a legislated automobile insurance program under the statutes of Manitoba.

So under the Act, we -- we, at MPI, as administrators, do not have responsibility for investments. Neither do we have responsibility for coverage, you know. So I think you -- we, as participants -- and as I talked about, as well, in my direct -- you know, there are three (3) players in this, essentially.

The government, the legislature passes the Act and -- and passes the regulations. We administer. PUB reviews and approves rates. We -- we, in this room, have -- have to believe that the government, with the -- the first and primary responsibility of establishing the program, has some sort of vested interest in a stable automobile insurance program for Manitobans.

So if you don't believe that, then I

guess all of this could be a risk, right, because we don't have anything to say about coverage. We don't have anything to say about, you know, any number of aspects of the program. And we don't manage our own investments.

So I do not think that's an inordinate risk. I think we have to look at the program in its entirety and in terms of the overall objective of the program. We have legislation. We have a monopoly in this province because the province wanted -- wants to provide guaranteed access to good, quality automobile insurance. There's a vested interest at -- with the legislators of -- of making that work, as well.

(BRIEF PAUSE)

MS. CANDACE GRAMMOND: Thank you, Ms. McLaren. I -- I guess then if -- if we have your answer correctly, the DCAT does not specifically reflect as a risk the fact that the Corporation does not have control over the equity portfolio.

MS. MARILYN MCLAREN: That's true.

MS. CANDACE GRAMMOND: Okay. Mr. Johnston, you had testified on Tuesday that a peer review of the DCAT is being undertaken by Mr. Cheng, the Corporation's external appointed actuary, and that his report will be forthcoming soon.

Can you give us an idea of the scope and level of intensity of that peer review?

(BRIEF PAUSE)

MR. LUKE JOHNSTON: I'm sorry, I'm -- I'm struggling a bit with describing the details of -- of the scope, but I can tell you what -- some examples of -- of the level of detail that -- that Mr. Cheng goes into.

So obviously he's provided the report and the statements from the DCAT, and all -- all those underlying details. He was provided with a detailed listing of all our asset holdings, so he can -- he can review those assumptions. It's clearly not as detailed of an analysis as the one that -- that we perform internally, but Mr. Cheng should have all of the underlying data that he needs to -- to verify our assumptions in that report and, you know, provide a fair peer review on the DCAT.

MS. CANDACE GRAMMOND: Can you tell us whether there are aspects of the DCAT that he will just take as a given in his review, as opposed to different pieces that he may test rigorously?

MR. LUKE JOHNSTON: I haven't -- the DCAT is in the process of being peer reviewed, so I'm -- I'm really in the process of providing Mr. Cheng with everything that he needs to be com -- comfortable in those assumptions. I will -- I expect that we'll go through every main assumption in detail and make sure that -- that he's comfortable with -- with those.

Obviously, as well, as Mr. Christie did in the past, I -- I fully expect there to be recommendations for improvement as well.

(BRIEF PAUSE)

MS. CANDACE GRAMMOND: Can you tell us if there are defined terms of a review that have been put in place in an engagement letter? We're -- we're trying to get a sense of the -- the level of -- or the degree of -- of review and intensity that Mr. Cheng is going to be going into.

(BRIEF PAUSE)

MR. LUKE JOHNSTON: I know we filed the -- the engagement letter for Joe Cheng as our appointed actuary. I -- I'm trying to find the reference at the moment. But I can say that we haven't -- we haven't put any restrictions on Mr. Cheng in his -- in his peer review. And it is largely his discretion as to what he feels is important to -- to look into in further detail and what he believes he can take at face value.

But again, I expect, as an actuary, Mr. Cheng will make those judgements appropriately and get whatever he needs to -- to issue a peer review with his name on it.

(BRIEF PAUSE)

MS. CANDACE GRAMMOND: Mr. Johnston, can you give us an idea of the level of formality that we can expect in terms of his response? Like, is it going to be assigned opinion or something less formal?

(BRIEF PAUSE)

MR. LUKE JOHNSTON: The specific wording in the engagement letter to Mr. Cheng is, quote:

"On an annual basis, the vendor will
peer review the Dynamic Capital

Adequacy Testing, DCAT, and issue a separate report for each line of business."

End quote. I would expect that -- Mr. Cheng to sign an opinion on that report. It doesn't specifically say that in here. I'd also expect, of course, for -- that he follow the -- the standards of actual practice in regards to peer reviews.

MS. CANDACE GRAMMOND: And you had indicated on the first day that that is expected at some point during the course of the Hearing?

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

MS. CANDACE GRAMMOND: And is there an indication of what the budget is with respect to the DCAT review, in terms of fees?

(BRIEF PAUSE)

MS. CANDACE GRAMMOND: If the answer's not readily available, do you want to take it as an undertaking?

(BRIEF PAUSE)

MR. LUKE JOHNSTON: I think we have it. I'm just finding the page.

(BRIEF PAUSE)

MR. LUKE JOHNSTON: Perhaps I can -- the -- the fees are in one of the attachments. Perhaps I can provide that after the -- the break?

MS. CANDACE GRAMMOND: Sure. Thank you.

MR. LUKE JOHNSTON: Thank you.

(BRIEF PAUSE)

MS. CANDACE GRAMMOND: Okay. Just a -- a couple more questions with respect to actuarial matters, and then we'll move on to another area.

Mr. Johnston, at Tab 42 of the book of documents we have the answer at PUB/MPI-2-32, Tab 42 of the book of documents.

MR. LUKE JOHNSTON: Yes.

MS. CANDACE GRAMMOND: With regard to this answer, can you tell us: What would the recommended DCAT-based minimum RS -- RSR target level be if it was agreed that a 35 percent decline in equity markets was the appropriate equity decline scenario for the purposes of DCAT, everything else being equal?

MR. LUKE JOHNSTON: The -- there's -- there's a couple of things to consider here. If this scenario was deemed exceptial -- acceptable as per the -- the guidelines -- the plausibility guidelines we discussed for the DCAT, it would also still have to be the most significant scenario. We do have a combined scenario right now that is higher than this. And I would assume, if -- if we agree on a different equity model, that it would change the results of the combined scenario as well.

Let's just assume that this is the most significant scenario, which I think is where you're going, and so yeah, the -- the DCAT target would be lowered to approximately 182 million if 35 percent decline was considered the most severe scenario.

(BRIEF PAUSE)

MS. CANDACE GRAMMOND: Okay. Thank you, Mr. Johnston, I appreciate that. Last question, I think, on -- on the DCAT, just coming back to Mr. Cheng's review for a minute.

Is there a particular reason why the

review is being conducted in this time frame rather than being done maybe a little bit earlier, sort of after the DCAT was actually completed?

(BRIEF PAUSE)

MR. LUKE JOHNSTON: No. No particular reason. The -- the preference would have, of course, been to have the peer review done before the hearings. This -- the situations around the amended DCAT and having to provide a revised version to Mr. Cheng create -- created the delay. We don't have a -- you know, we're still waiting for official Board approval as well. So that -- that is -- that's the main reason.

MS. CANDACE GRAMMOND: So would you expect then that in the future, for future hearings and DCATs, that perhaps the peer review would be available a little bit sooner, maybe before the hearing?

MR. LUKE JOHNSTON: Absolutely. And in -- in -- in regards to the comments that Professor Simpson made in his evidence as well, we do feel there's a need to bring forward the DCAT process in -- in time a little -- a little bit to, again, allow the -- the Board and the Intervenors have this information a little bit earlier so we -- we can discuss the scenarios in detail and possibly make changes.

MS. CANDACE GRAMMOND: Thank you. Okay, I'm going to move then --

THE CHAIRPERSON: Before you --

MS. CANDACE GRAMMOND: Of course.

THE CHAIRPERSON: -- change subjects, I wonder if I could explore something with Mr. Johnston. And this is in respect of your determination that -- that MPI's -- MPIC's financial condition would not be -- is not considered satisfactory, because your RSR level is not where it should be.

Now, without stealing any of Mr. Williams' future thunder on this subject, I just wonder about, say, for example, the external actuary comes in and suggests to you that you should have used data after the World War -- first -- second World War as opposed to 1919.

Would that cause you to vary your opinion, your qualified opinion, about the condition of MPIC?

MR. LUKE JOHNSTON: Well, you're -- you're definitely -- I'll start that over. The -- the DCAT -- the clear benefit of the DCAT that we're -- we're seeing here is that we're actually discussing the risks of -- of MPI and, in this particular case, equities.

So this is really one of the key benefits that -- that we see. We -- we have, obviously, insight from the Board, Intervenors, and expert witnesses to improve these scenarios.

I think in -- in the particular case of the peer review, that -- for this particular year, that peer review report would be provided for information. I -- I wouldn't refile the DCAT report, but the Board would -- would know that this actuary -- or, a different actuary has a different opinion on the risks of that scenario. And that would obviously guide some of my judgments in -- in future reviews, as -- as with all other information that we debate at the -- at the hearings.

(BRIEF PAUSE)

CONTINUED BY MS. CANDACE GRAMMOND:

MS. CANDACE GRAMMOND: Thank you. Okay, I'm going to move then to some questions dealing with investments.

We've already heard evidence, and I think we all know that investment income is quite critical to MPI's operations; I think, Ms. McLaren, you had said that on Tuesday?

MS. MARILYN MCLAREN: Yes.

MS. CANDACE GRAMMOND: And we have a document in the book of documents that reflect the composition of the Corporation's investment portfolio. That's at Tab 23 of the book of documents. This is 1-9 and, in particular, 1-9(b), Attachment A.

So if we go to Tab 23 and flip past the narrative and then flip past the list of equity holdings, we get to some tables that show us what is included, in terms of dollar amounts and different investment categories.

If we're all there, it -- it would seem that for the last fiscal year that ended the 2011/'12 year the portfolio was just over 2.2 billion.

That's for the Corporation as a whole?

MS. HEATHER REICHERT: Yes, that's correct.

MS. CANDACE GRAMMOND: And it's projected to increase as -- according to this table, to about 2.9 billion by the end of the outlook period that's shown, which is 2015/'16?

MS. HEATHER REICHERT: Sorry, yes, that's correct.

MS. CANDACE GRAMMOND: And I gather

that when the Corporation prepares these projections, it does so assuming no rate changes in the future and no further rebates being issued?

MS. HEATHER REICHERT: The forecasted investment income would be based on anticipated levels of the -- of the investments. So in the modelling it -- it would assume that there were some increases in the investment levels; based on -- based on what's happening with premiums and claims, there -- there would be.

But because we run a break-even operation, for all intents and purposes -- but that is why you are seeing the increase in the value from the 2.2 billion to the 2.9 billion.

MS. CANDACE GRAMMOND: But there's no assumptions built in with respect to increases in rates charged to motorists or Board issuing rebates or anything like that?

MS. HEATHER REICHERT: Sorry, that's correct.

MS. CANDACE GRAMMOND: Okay. Now, we know that -- and I'm not going to take you through the -- the list here of how much is in bonds and how much is -- is in equities. But we know that, in the past, the composition of the portfolio has been different than it is today, and that some of the -- what we see here derived from a report that was done by Aon back in 2009. Is that right?

MS. HEATHER REICHERT: Yes, that's correct. The different allocations within the type of investment is established -- targets are established within the investment policy. And so the changes year over year reflect trying to maintain those targeted allocations, or get to them, as the case might be.

MS. CANDACE GRAMMOND: Okay. And some of what we see today did flow from the Aon report in 2009.

MS. HEATHER REICHERT: Yes, I believe that to be the case.

MS. CANDACE GRAMMOND: Now, I'd like to talk a little bit about that 2009 time frame when the Aeon report came -- and I know that, Ms. Reichert, you weren't with the Corporation so I'm not sure who's best to answer this, but my question is, In that time frame when the Aon report was provided who at the Corporation analyzed or reviewed what Aeon was proposing.

What is -- was it one of the working groups, or -- or how did that happen?

MS. MARILYN MCLAREN: The investment committee working group, which is comprised of both members from the provincial Department of Finance and from MPI, really led the entire RFP process: getting the report, reviewing the report, preparing information to the Corporation's board of directors on the contents of the report.

MS. CANDACE GRAMMOND: And so in that time frame obviously Ms. Reichert would not have been on the working group.

MS. MARILYN MCLAREN: That's right.

MS. CANDACE GRAMMOND: Were you on the working group, Ms. McLaren?

MS. MARILYN MCLAREN: I -- I'm not formally part of the working group but I attend most of the meetings and I -- I stay in pretty close touch with its work.

MS. CANDACE GRAMMOND: And just for the purposes of the record, when we're talking about the investment committee working group that's the one, I think, Ms. McLaren, on the first day you said is co-chaired by Ms. Reichert and Mr. Gibson from the Department of Finance.

MS. MARILYN MCLAREN: Yes, exactly.

MS. CANDACE GRAMMOND: So I gather then that in this 2009 and following time frame when the Aon report was being reviewed that members of the

Department of Finance were involved in that through the working group.

MS. MARILYN MCLAREN: Oh, absolutely.

MS. CANDACE GRAMMOND: Now, we have in one of the other IR responses, 1-8, which is in the book of documents at Tab 22, a summary of what the Aon recommendations were. This is at the -- the second page. So if you go to Tab 22, and first page, second page, we've got a chart that's sideways that reflects the Aon recommendations, how the Corporation responded, and then what their progress has been.

We see at the first item that a recommendation was made by Aon with respect to bonds. And just -- just to clarify, I see the notation here is March 2008. I think I said earlier March 2009.

Was I wrong in my year, Ms. McLaren? It -- it was 2008?

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

MS. CANDACE GRAMMOND: Thank you. So the Corpor -- or the -- Aon made a recommendation with respect to bonds, and we see in the second column that the Corporation adopted a 10 percent allocation to long-term bonds.

And it appears from what -- what we see

here that the Corporation is continuing to increase its allocation in -- in that regard.

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

(BRIEF PAUSE)

MS. CANDACE GRAMMOND: And in the second row we see that Aon made a recommendation with respect to illiquid asset classes, which would include real estate, private equity, and infrastructure.

And that is also something that the Corporation has undertaken and we see the percentages here with respect to progress in that regard.

MS. MARILYN MCLAREN: Yes.

MS. CANDACE GRAMMOND: And just for a moment while we're on infrastructure, can you comment on what the infrastructure investments are that the Corporation is in at present?

(BRIEF PAUSE)

MS. MARILYN MCLAREN: The...

(BRIEF PAUSE)

MS. MARILYN MCLAREN: We have two (2) infrastructure investments at this point. We have one (1) direct investment. We have, I don't know, maybe a foot or two (2) of the -- the 407 Freeway north of Toronto. Relatively small investment, but that is our -- our -- our sole direct infrastructure investment at this point.

We are also -- have become part of an infrastructure coalition -- infrastructure investment coalition of sort of like-minded, largely public sector investment funds. And that is really just in the earliest, earliest stages of getting off the ground. And there is one (1) small investment through that process. I'm not personally aware of even what it is exactly.

MS. CANDACE GRAMMOND: Thank you. Now, just turning back to the Aon recommendations briefly, it's also referenced, I believe, in the third row that one of -- the recommendation to go into real estate and infrastructure and so on would eliminate the need for real return bonds, which were something that the Corporation held previously. And this has to do with exposure to foreign currency changes.

Is that right?

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

MS. CANDACE GRAMMOND: Okay. Now, we had asked a question about the Corporation getting an updated Aon report, because as -- as I corrected myself, it was from 2008. So we're in that four (4) to five (5) year time frame from when that report was done, and the Corporation has advised that the Department of Finance considers it to be premature to get an updated report at this point.

Can you comment on -- on why that view is held?

MS. MARILYN MCLAREN: Sure. There was a really significant change in the direction for the Corporation's investments that the Assistance Deputy Minister and the Minister of Finance adopted flowing from the 2008 report. Until -- at -- at that time, remembering -- sort of take a step back even earlier than that -- until 1998, the only investments that the Corporation's insurance fund had were bonds. So from 1998 to 2008 and -- and a little bit later than that, moved into the world of equities.

The decision to go into the alternative classes was, you know, really quite different, and the allocation within the bond portfolio was really quite different. So we are continuing to move in those directions, and it would be really in the view of Mr.

Gibson too -- too preliminary, too early at this point since we are still moving in the direction of the work that we did at that point.

I mean, it -- it takes time. It takes time first to, you know, educate, you know, the fund manager and his staff on these various classes and to decide how exactly they choose to move into those classes. Often, there is regulation changes, in terms of the Financial Administration Act for the province. So it -- it -- it takes time. There's -- he continues to have strong support for the allocations that kind of float -- flow through that, but to repeat the process at this point, he -- he would just see as too soon.

MS. CANDACE GRAMMOND: And do I take from your answer that the Corporation shares his view?

MS. MARILYN MCLAREN: Absolutely. We have no concerns with that -- with that direction at all.

MS. CANDACE GRAMMOND: Okay. Coming back to some of the composition of the portfolio, I'll ask you to turn back to Tab 23, which we had looked at just at the very beginning of this part of the questioning. So Tab 23, again, flip past the narrative, flip past the list of equities, we get to 1-9B, Attachment A, which reflects some detail with respect to the composition of the portfolio.

We see that the allocation in bonds -- and I'm looking at the bottom table which reflects the percentages for each investment category, and we see the line "Total Bonds," which is where that -- the horizontal line appears. We see that 2010/'11 the composition of bonds -- and again, this is corporate investment portfolio was about 71 percent, 70.9, and then it drops to 62.2 in 2011/'12. That decrease was -- I -- if I understand it correctly, not due to a decision to -- specifically to drop the bonds in the portfolio but that was due to the premium rebate that was ordered by the Board of some 300 million and change?

MS. HEATHER REICHERT: Yes, that's correct.

MS. CANDACE GRAMMOND: And that rebate that was ordered by the Board was funded primarily by Government of Canada bonds, the thinking being that there was a fairly low yield there.

Is that right?

MS. HEATHER REICHERT: Yes, that would be correct.

MS. CANDACE GRAMMOND: Now we also see a drop -- and -- and sorry, just to -- so -- for the purposes of following in the document we see that very first line in the table that we're looking at is the Government of Canada bond line, we see the allocation changed from about 15 percent to five (5). And I'm rounding. We also see on the third line, under "Other provincial bonds" that the allocation dropped from about 18 percent to about 14 percent.

Was that the same reason, the funding of the rebate? Or was that changed due to something else?

MS. HEATHER REICHERT: That would be for the same reason.

MS. CANDACE GRAMMOND: Still, though, looking through current year, year of application, certainly bonds are by far the biggest component of the investment portfolio for the Corporation?

MS. HEATHER REICHERT: Yes, that's correct.

MS. CANDACE GRAMMOND: Now we see that equities, which is a little bit farther down on that table, are projected to decrease over time. And the -- the first two (2) columns for 2011 -- or 2010/'11 and 2011/'12 we see over 20 percent, around twenty-two (22). And then that's projected to decline as -- as we read to the right to nineteen (19) and even under nineteen (19) by the end of the outlook period.

And -- and can you tell us if there's anything specific driving that change?

(BRIEF PAUSE)

MS. HEATHER REICHERT: There's no particular reason, it's just still hovering around the target of 20 percent.

MS. CANDACE GRAMMOND: Thank you. Now we know, and -- and it's not reflected here, but it is on the record that the Corporation has dropped equities outside of Canada and US, what we used to call "EAFE," the Europe, Asia and the Far East. Can you explain the -- the thinking behind that decision?

MS. HEATHER REICHERT: I can. My understanding is that, as we have said, the Minister of Finance is ultimately responsible for the investment decisions for MPI. And it was a decision of the Minister of Finance that we not invest in EAFE-type investments.

MS. CANDACE GRAMMOND: Leading up to that decision being made by the -- the Department of Finance as you say, did the investment committee working group make any recommendations or take part in discussion?

MS. MARILYN MCLAREN: Investment committee working -- I mean, you can see that EAFE was there and now it's not, right. So that -- that's kind of the context of what we're talking about. The investment committee working group was not at all uncomfortable including EAFE as it was part of the Aon recommendations back from '08.

Given the way the world has evolved since that time, certainly the MPI members of the investment committee working group are not at all uncomfortable with its removal. I'm not party to or even if I was would -- would not be talking public about any conversations between the fund manager and the minister. But, you know, on its face, EAFE was there as an outcome of the Aon, and we are not all uncomfortable with the fact that it's not there anymore.

MS. CANDACE GRAMMOND: Ms. McLaren, when you refer to the market evolving can you be a little bit more specific in what those evolutions have been that gives the Corporation the comfort that it has on this issue?

MS. MARILYN MCLAREN: The economic stability of Europe, whi -- which comprises a big chunk of the EAFE market, is questionable at this point. I -

- you know, if it was up to me, I certainly wouldn't be recommending that this insurance investment fund move into an area for the first time at this point in time.

MS. CANDACE GRAMMOND: Okay, thank you. Now, looking at the composition of the bond portfolio here on this bottom table, we do see -- and -- and I appreciate that it's -- it's not on a single line, but the MUSH bonds -- municipalities, universities, schools and health organizations -- do appear to be growing somewhat.

We see that specifically on the school line and -- and a couple of the others. What's the thinking behind an -- an increase in composition of MUSH bonds?

MS. HEATHER REICHERT: Actually, I believe if you look at the -- the MUSH bonds in their -- in totality, you'll see that over the forecast period they are actually declining to about 26, 27.2 percent. Well, actually staying about the -- about the same as what they are in '11/'12.

So really they're holding relatively steady during the forecast period. And that -- that again is a decision of the assistant deputy minister on how much is invested within MUSH bonds versus the other -- other types of bonds.

MS. CANDACE GRAMMOND: Is there a change -- you -- you mentioned between 2011/'12 and -- and outward. What about a change from 2010/'11 to 2011/'12? As I say, I'm looking at the school line, in particular, where there's a change of a couple of percent, and does appear that some of the other MUSH lines are changing as well.

MS. HEATHER REICHERT: Again, I think that that may just be, honestly, a factor the -- of the -- the fact that government of Canada and other provincial bonds decreased so significantly from '10/'11 to '11/'12 that the calculation looks like we're increasing the actual value.

The -- the actual dollar value increased somewhat, but -- but, in total, again, I think it's just the -- what was happening with the government of Canada and the other provincial.

MS. MARILYN MCLAREN: It --

MS. HEATHER REICHERT: Thank you.

MS. MARILYN MCLAREN: It could also be a timing issue. We're aware of no policy considerations that would have changed any of this.

MS. CANDACE GRAMMOND: Mr. Chairman, I have a few more questions about this IR. I can ask those now or we can take the break. It's up to the panel.

THE CHAIRPERSON: I think we should take a break right now and resume after lunch. So let's meet again at 1:15.

MS. CANDACE GRAMMOND: And just as a reminder, we will have Ms. Ruth here to give her presentation that she was not able to give on Tuesday. So we'll just lead off with that. And then I'll resume here. Thanks.

--- Upon recessing at 12:03 p.m.

--- Upon resuming at 1:18 p.m.

THE CHAIRPERSON: I believe we are ready to resume the proceedings. I think you have a few exhibits to enter, Ms. Kalinowsky?

MS. KATHY KALINOWSKY: Yes, I do. I've got two (2) exhibits to enter, and then I have a question of -- to let Mr. Johnston respond to one of Ms. Grammond's earlier questions. But I have Undertaking number 1, which is the mean and median of the stochastic modelling. And that can be marked as MPI Exhibit number 7, I would suggest.

--- EXHIBIT NO. MPI-7: Response to Undertaking
number 1

MS. KATHY KALINOWSKY: And then Undertaking number 4, which is the accident better -- benefits other indexed comparison which is Undertaking number 4, that can be marked as MPI Exhibit number 8.

--- EXHIBIT NO. MPI-8: Response to Undertaking
Number 4

MS. KATHY KALINOWSKY: And with that, I'd also ask Mr. Johnston now to provide a response to an earlier question from Ms. Grammond.

MR. LUKE JOHNSTON: Yes, thanks. The question was in regards to the costs of the DCAT peer review, and I -- I couldn't find the reference at the time. If you go to CAC-1-57, Attachment A -- I don't know if you need to go there but that's where it's located, and that's page 23.

And that shows that the -- in the first year of the agreement with our appointed actuary the expected costs of the DCAT peer review is twenty-three thousand three hundred dollars ($23,300). That includes approximately forty-five (45) hours of review time. In the second year, the cost is fifteen thousand four hundred dollars ($15,400) with thirty (30) hours of review time.

This is just recognizing the fact that the --the first year will be the first time that our appointed actuary is looking at this information.

MS. CANDACE GRAMMOND: Thank you. And I'll just state for the record that the presenter that we were expecting in the end was not able to attend, so I don't know at this point whether she'll be coming -- asking to come back at a later time or not. So we'll just continue with the cross-examination. And if that arises later, we'll address it.

THE CHAIRPERSON: Is it possible that she might give something in -- in writing in lieu of having to come to the...

MS. CANDACE GRAMMOND: We don't expect that. Mr. Simonsen is shaking his head. So, yeah, as I say I don't know whether she'll ask to come next week, but we'll see.

CONTINUED BY MS. CANDACE GRAMMOND:

MS. CANDACE GRAMMOND: Okay. So, Ms. Reichert, we were speaking about 1-9(b), Attachment A, which is at Tab 23 of the book of documents. And we had talked about some of the bond investments, some of the equity composition. I'm going to move on now to real estate.

We see that -- and again, I'm looking at the bottom table which is in percentages; the top table is in dollar amounts. We see a significant increase in the real estate piece of the portfolio from 4.2 percent in 2010/'11, increasing in -- in each of the -- the subsequent years.

Is -- is that increase something that's flowing from the Aon recommendations, or is there another factor that's coming into play with respect to that allocation?

MS. HEATHER REICHERT: No, I believe that's also flowing from the Aon recommendations.

MS. CANDACE GRAMMOND: And the Corporation's real estate investments at this point, if I have this correctly, consist of the CityPlace property as well as a number of surrounding parking lots, and the -- there was also an investment in the Greystone real estate pooled fund.

Is that right?

MS. HEATHER REICHERT: That's correct.

MS. CANDACE GRAMMOND: And the increase in real estate investments then that we see through the outlook period is still a continuation of Aon recommendations?

MS. HEATHER REICHERT: Yes, that's correct.

MS. CANDACE GRAMMOND: Now, we know, as it's reflected on the record, that the Corporation has sought out expressions of interest relative to the development of some of the properties around the MTS Centre and, in fact, around the building that we're in and has granted a one (1) year exclusive option to the Artis/Longboat Group with respect to that?

MS. HEATHER REICHERT: Yes, that's right.

MS. CANDACE GRAMMOND: And is that development a driver behind the expected -- or, pardon me, the increase in investment income anticipated?

MS. HEATHER REICHERT: No, it is not.

MS. CANDACE GRAMMOND: Now, just so that we're clear, we've talked about some of the -- the different pieces of the portfolio and the continuation of implementation with respect to the Aon recommendations.

Are there any other factors at play with respect to what we're seeing, in terms of changes in the -- the composition of the -- the portfolio, or are the -- the changes in allocations pretty much strictly related to the implementation of Aon recommendations?

MS. HEATHER REICHERT: My understanding is that the -- the changing allocations are a reflection of an implementation of the Aon recommendations.

MS. CANDACE GRAMMOND: And that would include the decision for the high concentration in bonds that we're seeing?

MS. HEATHER REICHERT: Yes, I believe so.

MS. CANDACE GRAMMOND: Okay. Thank you. I'm going to ask you to turn to the next tab in the book of documents, Tab 24. We have here another IR that was asked by the Board. And in particular, we have attached to this IR the investment policy statement for the Corporation, or what I refer to as the IPS.

And what we had asked for was a blackline version of the IPS, meaning that any changes from the way that the IPS was written last year be underlined. So we see as we -- and this is the attachment at that tab. We see some changes that are underlined or struck through that represent the revisions.

Is that right?

MS. HEATHER REICHERT: Yes, that's correct.

MS. CANDACE GRAMMOND: Now, I'm going to go into some of the specifics in the IPS. But first I just wanted to ask some more general questions. Ms. McLaren, you had indicated on the first day of the hearing that the Investment Committee Working Group is actively involved in educating itself, learning about other investment classes. And I have the -- the transcript reference if -- if you want it.

But my question is: What does the Investment Committee Working Group do with that information that it obtains?

MS. MARILYN MCLAREN: Excuse me. It uses it to discuss changes to the investment portfolio that -- that might be possible. It's -- really the Investment Committee Working Group is a resource to the fund manager.

MS. CANDACE GRAMMOND: And you had talked about education on Tuesday. And then I -- when I went back and read the transcript, I saw that you did say that the committee educates itself. But I also gathered from your evidence that it -- it also educates, perhaps, the Corporation as well as the

Department of Finance with its work.

Would that be fair to say?

MS. MARILYN MCLAREN: Yeah, the -- the key -- as I understand it, the key staff in the Treasury Branch of the Department of Finance are members of the Investment Committee Working Group. So I don't know that there would be very many people that they would further educate back at their office.

And -- and most of the key players from the Corporation are -- are on that committee as well. There are a few people in our small four (4) person investment department that -- that don't attend the meetings, but they would certainly be asked to do some of the research. And they would also certainly share in the information gleaned from it.

MS. CANDACE GRAMMOND: Thank you. And I'm -- I'm glad you brought up the four (4) people, because you had referenced that on Tuesday as well, that there were four (4) staff people that provide a resource, I think you had said, for monitoring the activities of the investment managers, providing research and that -- the -- these individuals are a resource to the Investment Committee Working Group.

And one of the questions that I had was whether all four of them sat on the Investment

Committee Working Group or not?

MS. MARILYN MCLAREN: No, generally there's two (2) that -- that are sitting as members on the Investment Committee Working Group.

MS. CANDACE GRAMMOND: And who are they?

MS. HEATHER REICHERT: I can an -- I can answer that. Glen Bunston, who is the manager of the investment department, is the actual member on the Investment Committee Working Group. And he is supported by Wes Springer (phonetic), or Springer, who is there to provide secretarial support if -- and coordination support of the ICWG.

MS. CANDACE GRAMMOND: Is there anyone else from MPI on the -- the ICWG besides yourself, Ms. Reichert, Mr. Bunston, and Mr. Springer?

MS. HEATHER REICHERT: I can actually refer you to an IR in one moment.

(BRIEF PAUSE)

MS. HEATHER REICHERT: Okay, I have the list here. So the current members of the -- if you want to refer to the specific IR, it's PUB-2-3, part B. But I can just read into the record the members of the

ICWG.

The current members of the Investment Committee Working Group are the Vice President and CFO, Manitoba Public Insurance; the Assistant Deputy Minister of Finance, Province of Manitoba; the Manager of the Investment Department, Manitoba Public Insurance; Executive Director and Corporate Controller, Manitoba Public Insurance; the Manager of Financial Services, MPI; Assistant Manager of Financial Services, MPI; and then three (3) members from the Province of Manitoba: the Director Capital Markets, the Director of Treasury Services, and the Director or Risk Management and Banking.

MS. CANDACE GRAMMOND: Okay. Thank you. Let's just go through that list one more time if you would, and let's talk names. Like I know obviously you're the VP of Finance and CFO. Mr. Bunston, I take it, is the Manager of the Investment Department.

Who's the Executive Director and Corporate Controller?

MS. HEATHER REICHERT: Just started with us in September, that would be Cynthia Campbell (phonetic).

MS. CANDACE GRAMMOND: Can you give me the names of the other MPI people?

MS. HEATHER REICHERT: The Manager of Financial Services is Diane Hopkins (phonetic). And the Assistant Manager of Financial Services is Audrey Gertzen (phonetic).

MS. CANDACE GRAMMOND: And I know, Ms. Reichert, that you're a CA. Can you give us an indication and -- and -- I don't know if we need necessarily to go person by person off that list, but I want to try to get a sense of the -- the designation of some of the other individuals of MPI that represent MPI on that committee with respect to investments, you know, qualifications that kind of thing.

MS. HEATHER REICHERT: Okay. Yes, I am a CA. Glen Bunston, the Manager of the Investment Department, is a CFA. The Executive Director and Corporate Controller is also a CA. The Manager of Financial Services is a CMA and the Assistant Manager of Financial Services I believe is a CGA.

MS. CANDACE GRAMMOND: Thank you. And do you know about the designations of the representatives of the Department of Finance that sit on that committee, or would that be a better question for me to ask Mr. Gibson when he comes?

MS. HEATHER REICHERT: That would be a question for -- for Mr. Gibson.

(BRIEF PAUSE)

MS. CANDACE GRAMMOND: Ms. Reichert, just for the purposes of the record, what does a "CFA" stand for?

MS. HEATHER REICHERT: CFA is a Certified Financial Analyst -- Chartered Financial Analyst, I'm sorry.

MS. CANDACE GRAMMOND: Thank you. Okay. I'm going to ask you then to turn to page 10 of the investment policy statement. This is where we see a description of the role of the Investment Committee Working Group.

So we see at the -- about halfway down page 10 a portion that's been struck through. So that's what's been removed. And what it read was that the Investment Committee Working Group provides information and advise to the Investment Committee relating to the investment policy, investment council mandates, investment council selection, performance evaluation, and assorted investment management issues.

That piece has been replaced with the seven (7) subparagraphs that we see immediately above that portion that's struck through.

Is that right?

MS. HEATHER REICHERT: Yes, that's correct.

MS. CANDACE GRAMMOND: And obviously we can see what the -- the seven (7) new subparagraphs provide, and we -- we will talk about some of them, but can you tell us from the Corporation's perspective whether this change was made to the IPS to improve upon semantics or whether there was an actual functional change in the role of the ICWG?

MS. MARILYN MCLAREN: The former. There's been no change in the role.

MS. CANDACE GRAMMOND: And since we're talking about the Investment Committee as opposed to the Investment Committee Working Group in this section of the IPS, I'll just ask you to confirm that the Investment Committee is a subcommittee of the board of directors of the Corporation.

Is that right?

MS. HEATHER REICHERT: If I -- if I can, this is -- this section is talking about the Investment Committee Working Group that -- on page 10, but I can confirm that the Investment Committee is a subcommittee or a committee of the board of directors of MPI.

MS. CANDACE GRAMMOND: Yes, I know that this refers to the working group, but we -- I also referenced in the part that I read in the Investment Committee, so I just wanted to be clear of who that is that we were speaking about.

(BRIEF PAUSE)

MS. CANDACE GRAMMOND: Now, we talked a few minutes ago about recommendations that may be made by the ICWG to the Department of Finance. And, Ms. McLaren, you said, Well, there's representation of the Department of Finance on the working group, so, you know, really there's not much educating that goes on from that working group to -- to the Department of Finance.

Some of the -- the items on the new sublist do refer to communication with the -- the Department of Finance. Can you tell us a little bit about, practically speaking, how that unfolds?

And that can be answered by either one of you, whoever's better -- better suited to answer.

(BRIEF PAUSE)

MS. MARILYN MCLAREN: Is the language in 'G', would that be an example of -- of the question in terms of preparing reports for the department? Is that -- is that the kind of thing that you're looking for?

MS. CANDACE GRAMMOND: Sure. 'G' would be an example. 'E' talks about preparation of policy strategies parameters for review and approval of the Investment Committee, but -- and of the department, which is obviously the Department of Finance. 'C' talks about supporting the Assistant Deputy Minister. I appreciate that he's -- or that he's on the committee.

But I -- I'm trying to get a sense of, in practical terms, if -- if it doesn't unfold in the way of the Investment Committee Working Group coming up with things and then passing that information on, if -- if it's really more of a collaborative approach, then I just want to try to understand that.

MS. MARILYN MCLAREN: There's a good deal of contact that would go on between Mr. Gibson and Mr. Bunston, for example, outside Investment PD Working Group. There's collaboration between the three (3) -- Mr. Bunston, Mr. Reichert, and Mr. Gibson -- with respect to agendas for the Investment Committee Working

Group meetings.

What -- what happens in practicality often is that, based on those discussions, written material will be provided by the investment department of MPI to the Investment Committee Working Group. In discussions, at the meetings -- at the meetings, occasionally offline, but often at the meetings, in discussion, the group will suggest changes to the documents that have been prepared.

And, ultimately, they are prepared as directed by Mr. Gibson and then finalized, formalized, and become part of his -- his action or -- or part of the formal sort of documentation of the committee.

MS. CANDACE GRAMMOND: So there could be situations where a new idea wherever -- or whatever that may be, that relates to investments as suggestion for some type of change could originate within the working group. It could originate between -- in a separate conversation between Mr. Bunston and Mr. Gibson or whatever.

And then it -- it evolves among those involved from there?

MS. MARILYN MCLAREN: That's right, with the ultimate decision as to whether it becomes part of the investment practice or not, up -- up to Mr.

Gibson.

MS. CANDACE GRAMMOND: Okay. I'm going to ask you to go to page 5 of the IPS. We were just looking at page 10, so I'll just ask you to go back a little bit. On page 5 is where we find the statement of investment beliefs. And based on the black lining, I believe this is a new section that we -- we see in the IPS here for the first time.

Is that right?

MS. HEATHER REICHERT: Yes, that's correct.

MS. CANDACE GRAMMOND: And I gather that the statement of investment beliefs is what governs the philosophy or strategy that's followed to manage the Corporation's investment portfolio.

Would that be fair to say?

MS. HEATHER REICHERT: Yes, that would be fair.

MS. CANDACE GRAMMOND: And I understand from one of the IR responses that this statement of investments beliefs was developed internally by the Investment Committee Working Group.

So I appreciate that includes representatives of the Department of Finance, as well?

MS. HEATHER REICHERT: Correct.

MS. CANDACE GRAMMOND: But it wasn't something that was done with external reports from anyone beyond the Investment Committee Working Group?

MS. HEATHER REICHERT: I believe that in the IR we indicated that we looked at or -- or reviewed other statement of investment beliefs from other Investment Committees that we were aware of. But we developed this as our statement of investment beliefs within the ICWG and forward to the Investment Committee.

MS. CANDACE GRAMMOND: And if you want to look at that answer, I can give you the reference. It's not -- I don't think it's in the book of documents. It's 2-7. But my question was going to be why the decision was made that the statement be developed without consulting any external advisor.

Is it just because it was felt that the Investment Committee Working Group had all of the necessary knowledge and skill and just wasn't needed, or was there some other reason?

MS. HEATHER REICHERT: I would say that it was felt that, as was MPI with the Assistant Deputy Minister's statement of our investment beliefs, that -- that we didn't need to have external consultation.

MS. CANDACE GRAMMOND: Now, if we look

at the -- the statement of investment beliefs. And again, I'm not going to go through every one of them. But I would ask to -- to discuss a couple of them.

Item 4 on the list speaks about the success of active management and -- and that that success can vary, and then item 5 talks about passive management. Number 4, just to go back to that for a minute, basically says that the success of active management can vary in efficiency or on -- depending on the efficiency of the market.

And what we were wondering was: Is that thought process of what's reflected at item 4, and specifically that active managers maybe underperform net of fees over the long term, is something that was behind the move -- to move towards passively managed US equity investments?

MS. MARILYN MCLAREN: I guess first of all I'd like to just say, for the record, that, you know, there's nothing particularly surprising or uncommon, anything you wouldn't find in -- in any other sort of investment funds statement of beliefs. This is pretty standard, textbook stuff, as I understand it, for the most part. And we were really trying to sort of -- that was the intention, was to sort of get that -- that stated -- pretty much noncontentious statement of beliefs that you would find pretty consistently, we understand, about investment activity.

So, no, I don't think deciding that we believed these things caused the fund manager to change the course in the US necessarily. You know, I mean, I think the fund had some pretty unsatisfactory returns with active management in the US. And again, I think some of this is fairly self-evident.

I think that, you know, you -- you probably find any number of funds that somehow make a decision upfront to go with passive or active and stick with it and -- and ride that out of the long term, but others will have some version of moving back and forth.

But I think probably more than anything, Mr. Gibson would have decided that, you know, it -- it's the -- the big key to success in choosing active or passive, and if you're going to go with active, the key is the manager, right? And I don't know that there was any real sense that the MPI fund would have any better success the second or third time out of choosing an active manager in the US market. And he made the decision to -- that -- that -- that passive approach was -- was in our best interest.

MS. CANDACE GRAMMOND: And with respect to the Canadian equities, which I understand are -- are

still managed actively, is there any consideration being given to a change, or is it because of the fact that the Corporation is
-- is happy with what's going on there that there's no change to passive management in Canadian equities?

MS. MARILYN MCLAREN: We have a small contribution to passive in the Canadian market now, and I -- I'm not in a position to say whether that might grow in the future. I don't know.

MS. CANDACE GRAMMOND: One of the other items on the list here, item 7 in the statement of investment beliefs, speaks to the idea that over the long term you'll do better with equities than with bonds. And I -- I understand your point about this being a fairly standard set of -- of ideas.

Is -- is the Corporation thinking about an increase on the equity side, or is the Investment Committee Working Group thinking about an increase on the equity side?

MS. MARILYN MCLAREN: The -- the allocation, I believe, is expected to pretty much stay as it is un -- unless we had some other compelling evidence, like a new asset/liability study, to really determine a different course of action.

I -- I think it was this general belief, as stated here in this -- in this page 5, that likely led the Minister of Finance to move from total investment and bonds into equities back beginning in 1998, as the Department of Finance and MPI began to understand the differences in the liabilities of the Corporation in a no-fault world versus the tort world with -- with much longer liabilities, a longer investment horizon, than would have become more appropriate.

So I think it would reflect that as much, and I don't know of any -- any intention on -- on the manager's part to be changing the allocations that -- that we've got at this point.

MS. CANDACE GRAMMOND: At item 7 here, in addition to the -- the piece about returns that I mentioned, there's also reference to the naturally higher expected volatility on the equity side.

Can you tell us a little bit about how the Corporation balances its weighting and equities to capture the increased returns but to try to mitigate against the higher volatility?

(BRIEF PAUSE)

MS. MARILYN MCLAREN: The -- the

overall weighting in equities derived from the asset/liability study, which is all intended to balance risk and return, but within the equity portfolio itself it is a diversified portfolio with small caps as lar -- as well as mid to large cap US as well as Canadian. So there's diversification within the equities, as well, to try -- to try to mitigate some of that.

MS. CANDACE GRAMMOND: And we did speak a little bit earlier today about the decision to remove the non-North-American equities from the portfolio.

And so I gather that the -- the reasons that the Department of Finance had to make that decision outweighed the benefits of continuing that piece of diversification in the portfolio?

MS. MARILYN MCLAREN: Yeah, that's fair. And just -- just for the record, we never had any of those investments in the portfolio. It was -- if you go back in time when you did see the EAFE was there, it was always zero percent allocation. We never actually had any investments.

So it was there as a possibility and has now been removed as a possibility, and never actually had any investments in that category.

MS. CANDACE GRAMMOND: I'm going to ask you to go to page 8 of the investment policy statement.

This is where we see the responsibilities of the Investment Committee, which we spoke about a minute ago as distinct from the working group. And I just want to ask about these changes a little bit.

But before we do that, Ms. McLaren, you testified that you're not technically a member of the Investment Committee Working Group but that you -- you try to attend the meetings, or attend most of them, or whatever your words were.

Are you a member of the Investment Committee?

MS. MARILYN MCLAREN: Ex officio.

MS. CANDACE GRAMMOND: Okay. So we see here on page 8 there have been some changes with respect to the responsibilities of the Investment Committee. And again we see some provisions that have been struck through, meaning that they've been removed, and new provisions that have been added and -- and are underlined.

Can you tell us generally why these changes were made?

MS. MARILYN MCLAREN: The same reason as the Investment Committee Working Group changes. Really trying to better articulate the roles and responsibilities. As -- as I think some people have heard me say in the past, I -- personally, I really have a great belief that words really matter, that language matters.

And in -- in all honesty, some -- some of the awareness that we need to work harder, the language probably came through these proceedings that it -- it is important. We understand that it's important to this Board, this panel, to understand the relationship between the Department of Finance, the Investment Committee, the -- the Corporation.

And so we're really trying to do the best job we can to really art -- articulate what is the practice in these different groups that are -- that share some involvement in the MPI investment fund. Again, no -- no change in role, no change in function; just language.

MS. CANDACE GRAMMOND: Thank you. I do want to go through a couple of them a little bit more specifically.

In the preamble of the paragraph, you can see on the third line, it used to say that the Investment Committee is responsible for overseeing the direction of the investments of the fund, and that's been taken out.

So does that mean that the investment

committee is no longer responsible for overseeing the direction of investments or that it -- that it is? I guess I -- I just want the panel to be clear about that.

MS. MARILYN MCLAREN: Well, it's -- it's really just cleaning up the language. And -- and you can see that when that -- when that language was there, it didn't align particularly well with the sub-bullets that used to be there, and it certainly doesn't align now with the sub-bullets that we have changed and im -- improved upon.

MS. CANDACE GRAMMOND: Okay, so your evidence is not that the role has actually changed, but that the language has been revised to be more accurate?

MS. MARILYN MCLAREN: Absolutely correct.

MS. CANDACE GRAMMOND: Let's turn to sub item 1. It used to read that the Investment Committee was responsible for or maintained an active role in formulation of the statement and investment counsel mandates, and -- and that's come out.

Is -- is the same true for that piece, that it's just changed -- the semantics have changed, but in reality the practicalities have not?

MS. MARILYN MCLAREN: That's right, the

practicalities have not changed.

MS. CANDACE GRAMMOND: So just so that we're clear -- when it used to read that the Investment Committee was formulating mandates, who is it then now that would be said to be doing that?

MS. MARILYN MCLAREN: In -- in practice it would be at the direction of the Investment Committee Working Group, brought forward for consultation with the Board. But ultimately the formulation which, I guess in my -- "formulation" can mean either preparation or adoption. So the Investment Committee Working Group works together on formulating.

The Investment Committee of the Board has -- has full opportunity and responsibility to provide input and perspective on it, and the Assistant Deputy Minister adopts what he sees fit.

MS. CANDACE GRAMMOND: Okay. If we look at number 2 -- sub item 2, it used to talk about the Investment Committee recommending investment counsel, agents, and advisors to the Board, who would in turn communicate with the -- the Minister of Finance. That's been changed to:

"Review matters relating to investment activities of the fund."

Do you have any specific comment about

that change?

MS. MARILYN MCLAREN: I've been directly involved with the Investment Committee -- Investment Committee Working Group since 2004 now. And at -- and at no time did the Investment Committee or the Board recommend investment counsel, agents, and advisors who would then communicate with the Minister. It never happened. So this is really just clarifying and -- and correctly language that had been in the IPS.

MS. CANDACE GRAMMOND: And just so you know where -- where I'm coming from. I can tell you when I read this it really -- as somebody that's not involved in this, it really gives the reader the impression that things have really changed. So I -- I want to go through it in some level of detail with you and have you comment on -- on each.

You know, and -- and I -- I hear your evidence that that's not the case, but honestly that's not necessarily what I was expecting you to say, based on the language because it really seems that -- that -- that it's different.

Okay, so number 3, it used to talk about the Investment Committee evaluating performance. It now reads:

"To provide oversight and monitor

performance."

So can you comment on that piece?

MS. MARILYN MCLAREN: Well, this is probably not as significant as the change in number 2 that we just reviewed. But others evaluate performance in terms of actually the running the matrix and -- and writing reports about the performance of, for the most part, equity or real estate managers. You know, external managers hired by the department.

The -- the Board -- the committee of the Board does, in fact, you know, provide oversight and -- and monitoring that performance, but they don't evaluate and they don't act on the results of the evaluation.

MS. CANDACE GRAMMOND: And then item 4 is a new one:

"To monitor the implementation of investment decisions consistent with policies and strategies through direction to the joint working group."

And -- and I -- again, I assume that the working group referenced here is the ICWG that we've been talking about?

MS. MARILYN MCLAREN: Yes, that's

right.

MS. CANDACE GRAMMOND: So would this piece of monitoring implementation be, again, something that was added to reflect what was already ongoing, or was this actually something new?

MS. MARILYN MCLAREN: No. That -- that would be actually what has been happening and reflects the sort of long -- long-standing activities of the investment committee. For example, you know, modern -- monitoring the results of a move from active to passive in the US, right, that that would be an example. So that was something that happened that was a change in the fund, and they would monitor the implementation and -- and sort of the downstream results.

MS. CANDACE GRAMMOND: Okay. Now, the -- there used to be a rebalancing policy attached to the IPS at the end. This is at page 28 -- or -- yeah, twenty-eight (28) and on. And that's been removed. And what the Corporation has advised us in response to our question about why the rebalancing policy is gone is that, Well, that's a policy of the working group, not a -- a -- you know, doesn't need to be in the IPS.

Is that fair to say?

MS. HEATHER REICHERT: Yes, it is.

MS. CANDACE GRAMMOND: So is the

rebalancing policy, then, still in use by the Investment Committee Working Group, or has it been done away with?

MS. HEATHER REICHERT: No, it is still in use by the ICWG.

MS. CANDACE GRAMMOND: And can you tell me in general terms whether it's changed a lot in substance from what was here?

MS. HEATHER REICHERT: No, it has not.

(BRIEF PAUSE)

MS. CANDACE GRAMMOND: So is there, then, a separate IPS-type document for the Investment Committee Working Group?

(BRIEF PAUSE)

MS. MARILYN MCLAREN: Is your question as to whether there is another similar document like a policy statement that would include a rebalancing policy as part of it? The answer is no, we have the rebalancing policy, which has really not changed much. It's just the rebalancing policy. We -- there's only one (1) investment policy statement for the MPI investment fund.

MS. CANDACE GRAMMOND: And so does the Investment Committee Working Group, then, have any other documents or any other policies that it works under or follows in addition to the written rebalancing policy?

MS. MARILYN MCLAREN: No, nothing that any of us can think of off hand. I mean, the rules and responsibilities are documented here. We have the rebalancing policy and, you know, other things like monitoring manager performance and expectations of managers to be, you know -- compliance with manager expectations are all really embedded in the manager contracts that are between the individual managers and the Department of Finance. There's no other policy documents that are coming to mind.

(BRIEF PAUSE)

MS. CANDACE GRAMMOND: Okay. I'm going to move to some questions then about investment income. And if you need a -- a document reference from me, let me know; but probably the questions are high level enough that -- that you may not need it.

My understanding is that in 2011/'12

investment income was higher than expected, by about 20 million, because of large gains in the fixed income portfolio, which was due to lower interest rates and resulted in gains in the bond portfolio that were not forecasted.

Does that sound right?

MS. HEATHER REICHERT: Yes, that sounds right.

MS. CANDACE GRAMMOND: And as well, there was income from real estate that was higher than expected. It was about 17 million instead of 9 million. And this was because of a higher level of investment in real estate.

Is that right?

(BRIEF PAUSE)

MS. HEATHER REICHERT: In fact, I believe it was a combination of both. It was a growth in our investments in real estate as well as doing better on those investments than we were anticipating.

(BRIEF PAUSE)

MS. CANDACE GRAMMOND: Now, in terms of

benchmarks, the -- the Corporation has provided us with benchmarks by investment category and has compared actual performance with that. The real estate return was about 15 percent -- or 14.9, and the benchmark was about 15.1. So it was very, very close to that benchmark.

Is that right?

MS. HEATHER REICHERT: Can I just get you to tell me what the reference is that you're looking at?

MS. CANDACE GRAMMOND: For sure. PUB/MPI-1-14, so the IR we were just looking at on the investment policy statement. It's just at the beginning. It's the second page in, right before the -- the IPS at that tab.

(BRIEF PAUSE)

MS. HEATHER REICHERT: So, yes, I can agree that it was 14.9 percent and then the benchmark was 15.1.

MS. CANDACE GRAMMOND: Okay. Now, the funds that the Corporation has available for investment, as I understand it, are primarily unearned premiums and unpaid claims, although there are other funds in there as well.

Is that right?

MS. HEATHER REICHERT: Yes. Generally, the biggest contributors would be the two (2) that you named.

MS. CANDACE GRAMMOND: And the Corporation's lines of business don't have separate investment portfolios; rather, the Corporation invests in one (1) portfolio and then allocates income across the lines of business?

MS. HEATHER REICHERT: Yes, that is correct.

MS. CANDACE GRAMMOND: And Basic's share is typically right around the 85 percent mark, in terms of that allocation?

MS. HEATHER REICHERT: Yes, that's correct.

MS. CANDACE GRAMMOND: So when the Corporation forecasts investment income -- and I believe for the year of the Application the -- the forecast for the Corporation is about 88 million, eighty-five (85) of that -- or -- or, sorry.

When -- when the Corporation forecasts 88 million for Basic for the year of the Application, that's 85 percent of the overall corporate forecast?

MS. HEATHER REICHERT: Yes, you're correct.

MS. CANDACE GRAMMOND: Okay. Now, we have a document in the book of documents at Tab 16, which is an excerpt from AI-9 of the filing. And this provides a fair level of detail about the investment income of the Corporation.

(BRIEF PAUSE)

MS. CANDACE GRAMMOND: Just a moment, Mr. Chairman.

If we look at the -- the first page at Tab 16 -- so this is AI-9, Schedule 1 -- we see that most of the investment income for last year, 2011/'12, was from the bond part of the portfolio.

Would that be fair to say?

MS. HEATHER REICHERT: Yes, that would be fair.

MS. CANDACE GRAMMOND: Of course, that's the highest weighting, allocation-wise within the portfolio, is bonds?

MS. HEATHER REICHERT: That's correct.

MS. CANDACE GRAMMOND: We see an equity gain of about $2.1 million in 2011/'12?

MS. HEATHER REICHERT: Yes, that's correct.

MS. CANDACE GRAMMOND: And would it be fair to say that the reason for the high bond returns relative to overall returns would be the high weighting of bonds in the portfolio that we've spoken about, and, as well, realized gains on what I call the FVTPL bonds -- and I'll read in what that stands for -- due to declining interest rates?

Is that right?

MS. HEATHER REICHERT: The -- both realized gains and unrealized gains on bonds, yes.

MS. CANDACE GRAMMOND: And FVTPL for the court reporter, stands for "fair value through profit and loss", which is way too much of a mouthful.

Now, I also understand that the unrealized gains reflected here were due to a reevaluation of the bond portfolio that was required under the international financial reporting standards?

MS. HEATHER REICHERT: Yes, that is correct.

MS. CANDACE GRAMMOND: And under those standards, or IFRS, unrealized gains will be recognized as income each time the portfolio is revaluated -- reevaluated?

MS. HEATHER REICHERT: Correct. The unrealized gains are recognized through other comprehensive income each -- each year.

MS. CANDACE GRAMMOND: Now, in terms of investment income looking forward, if we look across to the right side of the page through the outlook period, we see that significant bond income relative to equities income is a common expectation.

Would that be fair to say?

MS. HEATHER REICHERT: Yes, that would be fair to say, based on the weighting that we have being so highly weighted towards bonds versus equities.

MS. CANDACE GRAMMOND: And we see -- if we look at the equity gain and loss line, which is the fourth line down, we see in '07/'08 a fairly significant income relative to the other numbers we see here. That was about 42 1/2 million. In '11/'12 it was two point one (2.1) as you've said. And through the outlook period it's in the range of 16 to 18 million a year.

MS. HEATHER REICHERT: Yes, that's correct.

(BRIEF PAUSE)

MS. CANDACE GRAMMOND: Now, we see as well at the lower part of the table, a line item called "management fees", which are all in brackets so that's obviously a charge against the income.

Can you tell us to whom those management fees are paid?

MS. HEATHER REICHERT: The management fees would be paid to the different fund managers, so that would be the government of Manitoba, and the other fund managers that we -- that -- not "we", but that the government of Manitoba engages.

MS. CANDACE GRAMMOND: And we see just underneath the "management fee" line there's a line called "pension fund transfer", which is also a deduction from investment income.

Can you tell the Board a little bit about why the Corporation does not segregate its pension investment assets?

(BRIEF PAUSE)

MS. HEATHER REICHERT: I understand that when the Aon review was done it was looked at, whether or not it made sense to segregate the -- the pension investment separate from the other corporate investments. And it was determined that because of the relative size of the -- of the pension investment there was no overall benefit to the Corporation, and it actually is more beneficial to keep it in a larger pool. So that's what we did.

MS. CANDACE GRAMMOND: We see --

THE CHAIRPERSON: Excuse me, could I ask a question there?

MS. CANDACE GRAMMOND: Of course.

THE CHAIRPERSON: So -- so in respect of the pension fund, is the responsibility for managing the fund the responsibility of the Department of Finance, or is it -- is it the responsibility of -- of MPIC?

In other words, could you decide to make investment choices for the pension fund that you couldn't make for the -- the regular reserves that you have managed by MPIC -- managed by the Department of Finance?

MS. MARILYN MCLAREN: The Act doesn't differentiate. The Act says that -- that any of the Corporation's funds for investment are given to the Department of Finance to invest -- to the Minister of Finance to invest.

CONTINUED BY MS. CANDACE GRAMMOND:

MS. CANDACE GRAMMOND: Ms. Reichert, we see on the schedule here at AI-9 under the 2011/'12 year, that the pension fund transfer was about 27 million in change, which is higher than the previous years shown on this table and higher than the subsequent years.

Can you just explain to the Board why it was particularly high last year?

MS. HEATHER REICHERT: Yes, I can. Unfortunately, the discount rate used to value the pension assets decreased significantly. The decline in interest rates that occurred last year resulted in a loss in the value of the -- of the pension fund, which is what you're seeing reflected in 2011/'12.

On the outlook periods, on the go-forward basis, we -- we do not speculate what will happen with -- with the interest rates as it relates specifically to the -- the value of that pension fund. And so that's why what you see here as being the reductions are the contributions that make to the Civil Service Superannuation Board directly on behalf of employees.

MS. CANDACE GRAMMOND: Thank you.

THE CHAIRPERSON: Before you move on

from that page, could I ask a question?

I'm looking at the results for equity dividends '10 -- 2011 and '12, which appears to be an outlier relative to the historical experience in equity dividends. And surprising piece of data that -- I wonder what was going on there?

What would have happened that caused a negative value for equity dividends?

(BRIEF PAUSE)

MS. HEATHER REICHERT: On -- on the page that you are -- are looking, if you referred down to -- you'll notice beside "equity dividends" there's a Note 2. And Note 2 indicates that it:

"Includes foreign exchange gain/loss on US equities, write-downs, and gain/loss on Canadian and US equities."

So my understanding is the reason that it seems -- seems to be an outlier in '11/'12 is because of the write-downs that were taken on equities.

THE CHAIRPERSON: Now, is there a reason why you would be taking the write-down on that line as opposed to the next line, which is the equity gains and losses?

MS. HEATHER REICHERT: I don't think that there's any particular reason. I think that's just the categorization of where we decided to group the write-down.

CONTINUED BY MS. CANDACE GRAMMOND:

MS. CANDACE GRAMMOND: Now, Ms. Reichert, the Corporation has provided evidence, as well, with respect to the -- the yields in some of the various investment categories. And I -- I can provide you with the reference if you would like, but I understand that the long-term bond yield is forecasted to drop from the 4.5 percent that it was last year in '11/'12, to 2.6 percent in 2012/'13.

Can you explain what's behind that anticipated change? And as I say, if you want the reference, just let me know.

MS. HEATHER REICHERT: Yes, please, could I get the reference from you?

MS. CANDACE GRAMMOND: For sure. It's AI-9, Schedule 2, page 1, which is actually not in the excerpt from AI-9 at the book of documents, so we'd have to go to Volume III of the filing.

(BRIEF PAUSE)

MS. CANDACE GRAMMOND: So it's AI-9, Schedule 2, page 1.

(BRIEF PAUSE)

MS. CANDACE GRAMMOND: And it's right arou -- along the bottom of the page.

(BRIEF PAUSE)

MS. HEATHER REICHERT: Okay. If I could refer -- refer the Board to 'T' -- I'm sorry, TI.18, which is the revenue forecast book on page 21. If you wanted to refer to that; if not, I can just talk to it.

Within the revenue forecast book, what we do for interest -- the interest rate forecast is we do a survey of all of the various banks and what they are projecting for the upcoming year to do with the interest rates, and then use the -- okay.

And so then the interest rate forecast for the government of Canada ten (10) year bond, we get that from the various institutions. I'm looking here at the table that's on page 21. And it's, like Scotiabank, CIBC, Royal Bank, TD, BMO, Global. We look at that. We take the -- the averages and the medians of those and calculate the average that they're anticipating for the '12/'13 year. And that is how we derive the two point six (2.6) that you see at the bottom of -- of the Schedule 2, page 1.

MS. CANDACE GRAMMOND: Thank you. I want to get into a bit of a discussion then about the equity yields that the Corporation is -- is looking for, or expecting. We know that the Corporation has previously calculated equity -- or anticipated equity yields by using the five (5) year average long-term bond rate, plus a 1.5 percent equity risk premium?

MS. HEATHER REICHERT: Yes, that's correct.

MS. CANDACE GRAMMOND: And I understand that for the year of the application, the result of that calculation was 4.8 percent, which the Corporation considered to be unreasonably low, comparing that return with the TSX numbers, which has never seen over a twenty (20) year timeframe a percentage below 5.2.

Is that right?

MS. HEATHER REICHERT: Yes, that's correct.

MS. CANDACE GRAMMOND: So as a result of this, the Corporation has changed the methodology that it uses, and it's now using a minimum return on equities of 6.1 percent for the year of the application, and that's based on the ten (10) year return of the TSX?

MS. HEATHER REICHERT: Yes, that is correct.

MS. CANDACE GRAMMOND: And as a result of this change, the Corporation's investment income forecast for the year of the application has increased by about 6.1 million?

MS. HEATHER REICHERT: Can you give me the reference for that, please. Sorry.

MS. CANDACE GRAMMOND: I was scared you were going to ask me that. I don't have it right at my fingertips. Just give me a minute.

MS. HEATHER REICHERT: Oh, I think I can help out on this one. I think on Schedule 1 of AI-9 --

MS. CANDACE GRAMMOND: Yes.

MS. HEATHER REICHERT: -- page 1, if you look at -- where are we here? If you look at -- where was it? Actually, the better reference is SM-3 in Volume -- whatever volume. Volume I. I can just --

I can read it in.

MS. CANDACE GRAMMOND: Sure.

MS. HEATHER REICHERT:

"Using -- [excuse me] using a forecasted annual equity return of six point one (6.1) instead of six point one (6.1) instead of 4.8 percent results in additional investment income of approximately 6 million per year."

MS. CANDACE GRAMMOND: Thank you for that. And I understand that with respect to the anticipated yields in real estate and infrastructure -- and these are shown on Schedule 2 of AI-9, what the -- what the numbers are -- that in the case of real estate, the Corporation is using CPI at 2 percent plus a 4 percent addition, which would be how it arrives at its anticipated 6 percent yield, and that's unchanged from previous years?

MS. HEATHER REICHERT: Yes, that's correct.

MS. CANDACE GRAMMOND: And with respect to infrastructure, again the Corporation is using CPI at 2 percent, and then it's added a 5 percent...

MS. HEATHER REICHERT: Yes, that is

correct.
MS. CANDACE GRAMMOND: Okay. So that the total expected yield then in infrastructure is 7 percent, which is also unchanged from the past?
MS. HEATHER REICHERT: Yes, that -- that is correct. It's unchanged.
MS. CANDACE GRAMMOND: Can you tell us whether these yield estimates -- that is, the 6 percent for real estate and the 7 percent for infrastructure -- are common in the marketplace?

(BRIEF PAUSE)

MS. HEATHER REICHERT: So it is my understanding that it's fairly common, when doing a forecast, to take a CPI plus a factor. So I -- I can't speak to the plus factor that other organizations may use in their forecast, but we believe it was a -- is a reasonable forecast for those two (2) types of investments.
MS. CANDACE GRAMMOND: Thank you. And just to ask a bit of a more detailed question about the CPI component to those two (2) yields, or anticipated yields, we were wondering: Given the change that the Corporation made on the equity yield side and the

concern that it had about the 4.8 percent relative to what the TSX provides, is there a basis to be concerned about the estimated yields for real estate and infrastructure if the 2 percent for CPI is unrealistically low?

(BRIEF PAUSE)

MS. HEATHER REICHERT: I'm sorry, may I get you to repeat the question, please?

MS. CANDACE GRAMMOND: Yeah, definitely. We talked about the fact that when the Corporation calculated its equity yield for this application year on the basis that it used to use, it was concerned that the outcome was too low. So it changed the calculation method, and now it's obviously satisfied with -- with the outcome there.

So our question is: Did the Corporation do a similar kind of review, I guess, with respect to the anticipated yields for real estate and infrastructure, and on the basis that the 2 percent CPI component might be too low?

MS. HEATHER REICHERT: If -- if I'm understanding your question, when we adjusted the equity yield to six point one (6.1), that was based on the fact that the previous method of calculating that yield generated something that -- four point eight (4.8), I believe you -- you had said, which we have not see that low of a -- of an equity -- equity yield in the past twenty (20) years.

So we -- we decided to use the ten (10) year -- ten (10) year average equity yield and came up with the six point one (6.1). So that wasn't related in any way to where we saw inflation or CPI.

So when we calculated the return, or the -- the forecasted return to use for real estate and infrastructure, we continued to use CPI plus four (4) and CPI plus five (5).

And we're comfortable that the CPI rate that we're using has been low, continues to be low, and is -- is forecasted to -- to stay low. So we did not view that we needed to increase the returns for real estate and infrastructure on the basis of the -- of deeming that the CPI was an inappropriate amount.

(BRIEF PAUSE)

MS. CANDACE GRAMMOND: I -- I don't want to spend too much more time on this, but I just want to -- to make sure that we're communicating the --

where we're trying to -- to go or what it is that we're trying to ask.

In the case of the equity yield, the calculation has been done on the basis of historical information. But as we understand it, with respect to real estate and infrastructure, the calculation is in part based on what -- what we might call a proxy for a historical record.

Does that difference, in the view of the Corporation, give any cause for a concern, in terms of accuracy?

MR. LUKE JOHNSTON: Maybe I can jump in here. Is the question -- like, we've talked about inflation earlier today, and I -- about how it being fairly consistent, both the recent history averages about 2 percent, our forecast averages about 2 percent.

So you had said something about inflation being unrealistically low, so I don't -- I don't think our inflation forecast is low or high. I think it's about the average. It's two (2) in the past, and it's two (2) going forward.

Is your question: Have we, given the economic environment right now, have we analyzed the -- the spread that we're assuming overinflation for this year's Application?

(BRIEF PAUSE)

MS. CANDACE GRAMMOND: Is there a way for the Corporation to look at historical returns for real estate and infrastructure within the marketplace that could assist it when calculating its anticipated yields in those categories?

MS. HEATHER REICHERT: Yes. In -- in conferring with -- with my colleague, we in fact do check, like, while we calculate it at CPI plus 4 percent and CPI plus 5 percent, we are checking with -- with investors in those markets to see what their -- what their spread is that they're looking for above inflation. And so we're comfortable that we are using something that is reasonable in the current market.

MS. CANDACE GRAMMOND: Thank you. Okay. I'm going to move, then, into a bit of a --

THE CHAIRPERSON: Can I ask a question --

MS. CANDACE GRAMMOND: Oh, of course, of course.

THE CHAIRPERSON: -- before you move on to something else?

Staying with -- with the table that

we're looking at, you've been able to capture gains in bonds by selling bonds over the last few years. You know, you -- interest rates have come down, bond value have gone up. You sold bonds, captured some gains there.

Now, what will we -- have you talked about your strategy if the market interest reverse themselves? In other words, interest rates at increasing while values start falling, what would be your strategy in that case? I mean, that's a common discussion amongst investment managers nowadays.

Have you thought about what the -- what your strategy will be at the Investment Committee Working Group level?

MS. MARILYN MCLAREN: Not to sound too much like a broken record, but -- but we wouldn't have the strategy. Wouldn't be our strategy.

I talked a little bit the other day about the fact that Mr. Gibson is holding more cash than we normally would right now. So as -- as -- as much as I can comment just on that fact, I think he's -- he is -- has indicated he is holding that cash in anticipation that, some point, interest rates would come up. And therefore, we would be in a position to buy more bonds at that point because we have foregone buying them today at the lower interest rates.

THE CHAIRPERSON: Now, ultimately, you know, investment allocation decisions are a big driver of -- of returns, both on income and in capital gains. And I guess, you know, at the heart of this there's the 10 percent allocation to real estate, 20 percent to equities, 20, 25 percent equity in the balance to -- to bonds.

In terms of the long-term horizon that MPIC is facing, what go -- what is the logic behind that particular allocation?

You know sitting from the outside, without being responsible for the -- for the management decisions, it seems to me that the allocation needs to be lower to bonds, more to equities. And infrastructure obviously is -- is all -- already being taken into account.

So what's the underlying logic for the particular mix that you're -- you're -- you have at the moment?

MS. MARILYN MCLAREN: To feel comfortable providing an answer to that, I would really like to go back to the Aon asset/liability study. So if we can take that as an undertaking, we will provide that answer.

--- UNDERTAKING NO. 5: MPI to provide the underlying logic for the particular mix of investment allocations

CONTINUED BY MS. CANDACE GRAMMOND:

MS. CANDACE GRAMMOND: Thank you. Okay.

(BRIEF PAUSE)

MS. CANDACE GRAMMOND: Okay, Ms. McLaren, you just mentioned a minute ago, and -- and I know you mentioned it before over the last few days, that MPI is at present holding extra cash balances within the cash and short-term investment class.

And -- and just to put some specifics on that, I understand that the target weight within that class is about 1 percent, but the Corporation is sitting at about 7.3 over that; so it's at about 8.3 percent right now?

MS. HEATHER REICHERT: Can I just get the reference? I'm sorry. Your -- is it the -- an IR or one of the tables?

MS. CANDACE GRAMMOND: Just give me a

minute, please.

(BRIEF PAUSE)

MS. CANDACE GRAMMOND: The reference is 1-8(f), which is at Tab 22. So this is -- there's a colour PowerPoint presentation there. And if we look at the bottom of the first slide -- sorry, bottom of the first page, it's actually the second slide, it reads, at the second bullet:

"The cash and short-term asset class is 7.3 percent over its target weight and 5.3 percent over the maximum allowable weight."

It doesn't actually say it here in the narrative part, but it does say in the chart above it that the target weight for that class is 1 percent.

MS. HEATHER REICHERT: Yes, that's correct.

MS. CANDACE GRAMMOND: And I believe that the amount that's being held is approximately 188 million? I don't -- yeah, it's reflected there as well in the chart -- the numerical chart above the narrative.

Do you see that?

MS. HEATHER REICHERT: Yes, that's correct.

(BRIEF PAUSE)

MS. CANDACE GRAMMOND: Now, it's reflected here at the bottom of that second slide in the second paragraph that the funds are being held for tactical purposes and will be considered to be part of the fixed-income portfolio.

When we asked some further questions about that, the Corporation advised that the cash is being held in anticipation of a rising interest environment. And I think that's consistent with what Ms. McLaren has said here.

Is that right?

MS. HEATHER REICHERT: Yes, that's correct.

MS. CANDACE GRAMMOND: Now, I understand that the percentage return on this amount at present is less than 1 percent?

MS. HEATHER REICHERT: That makes sense to me, yes.

MS. CANDACE GRAMMOND: So what would

the Corporation consider the implications to be of holding on to such a large cash balance?

(BRIEF PAUSE)

MS. HEATHER REICHERT: Maybe I could get you to -- to restate the question. I'm not sure, when you say "implications", what -- what exactly you want.

MS. CANDACE GRAMMOND: What is the opportunity cost if the funds are held for about a year?

MS. HEATHER REICHERT: I mean, we could -- we would -- could take as an undertaking to do the calculation, but the opportunity cost would depend on what you would be investing it in if not in -- if not in holding it as cash or short-term investments.

(BRIEF PAUSE)

MS. CANDACE GRAMMOND: If the yield and the bond portfolio was about 3 percent and if what the funds are earning in the current cash and short-term category is -- is one (1) or a little bit under one (1), wouldn't the difference be about 2 percent?

MS. HEATHER REICHERT: That's fair, and, again, assuming that you held it for an entire year.

MS. CANDACE GRAMMOND: Thank you.

(BRIEF PAUSE)

MS. CANDACE GRAMMOND: Mr. Chairman, may I suggest we take the break at this point?

THE CHAIRPERSON: Let's do that. Return at approximately ten (10) -- ten (10) to 3:00.

--- Upon recessing at 2:40 p.m.

--- Upon resuming at 2:54 p.m.

THE CHAIRPERSON: Ready to resume.

MS. CANDACE GRAMMOND: Thank you. And I think Ms. McLaren has an answer to the question that you had asked, Mr. Chairman.

MS. MARILYN MCLAREN: Thank you. The asset/liability study really is just that. It's not an asset allocation study in isolation. Like it -- it -- actually the Corporation's liabilities are a huge input to the process. And it's intended to match assets and liabilities.

And at the beginning of the process the corp -- the -- the client, Aon's client -- you know, MPI, Department of Finance, Investment Committee Working Group -- has to answer the question: What are your two (2) main objectives, the first and second objective of -- of this investment fund?

And the first is -- is always strongly match the liabilities, you know, make sure that our liabilities are fully funded and protected. And second is to gain additional return with an appropriate risk profile that -- that the manager's comfortable with. So it really does match the liabilities.

I mean, we've talked here about the extent to which our liabilities are interest rate sensitive, right? The -- the discounting that happens on -- on the vast majority of our claims' liabilities in -- inflation sensitive, they -- the best fit to truly fully protect and match our liabilities are bonds. And the allocation policy that's been adopted really hopes to improve return over historic levels when it was really bonds and not much else sort of around -- around the edges of that with the primary focus being on matching those liabilities.

And again, it's things like real estate and infrastructure which really align very well to inflation sensitive and -- and those other considerations that have an alignment with the Corporation's liabilities. The kinds of volatility that are possible with a heavy weight to equities would -- would really create extensive year-to-year volatility.

And -- and I would ask Mr. Johnston to just talk a little about that sort with a -- a window to the recent past for us.

MR. LUKE JOHNSTON: Yes, we -- I really should stress the importance of matching the -- the claim liabilities to the fixed income portfolio. The -- as we talked about before, this really allows us the base that we have, the 80 to 90 percent matching, when interest rate changes occur. If we did not have this strategy in -- for example, the recent huge decline in interest rates, it's not totally clear it would have happened, but we do know that the hundred -- probably hundred to $200 million increase in claim liabilities that occurred with the interest rate drop was largely offset by gains on the asset side and went largely unnoticed because of that matching.

If we had a different strategy, we likely would see an increase in those liabilities because of interest rates, but we would have experienced more of the equity decline we've -- we saw recently. And I don't -- I don't know this for sure, but I believe equities have essentially returned something close to zero in the last decade as well. So we would have had the hit on the claim liabilities from declining interest rates; the hit from poor equity returns; and no -- or only a partial offset on the asset side.

So the -- the -- the matching strategy really limits our variability in net income considerably. And again, we talked about how sensitive those liabilities are just -- even a ten (10) basis point change in interest rates.

CONTINUED BY MS. CANDACE GRAMMOND:

MS. CANDACE GRAMMOND: Thank you. And I'm going to get to some more questions about the matching and what we call the "immunization strategy". But before we do that, Ms. Reichert, before the break we were talking about the sum that is being held as cash, the 188 million that's shown on the document that we were looking at, that's as of May 31st of 2012.

Can you give the Board an idea of when it was that the Corporation really started to accumulate this large amount of cash, relative to what it usually holds?

(BRIEF PAUSE)

MS. HEATHER REICHERT: We don't have that specific information here. We can get back to you on when that balance started to increase above the -- above the target weight.

MS. CANDACE GRAMMOND: That would be appreciated. Thank you. We'll take that as an undertaking.

--- UNDERTAKING NO. 6: MPI to indicate when it began to accumulate this large amount of cash, 188 million, relative to what it usually holds

CONTINUED BY MS. CANDACE GRAMMOND:

MS. CANDACE GRAMMOND: Okay. So coming back then to this -- to the concept of matching. And just again for the purposes of the record, this is also what we've referred to in the past as the "immunization strategy."

Is that right?

MS. HEATHER REICHERT: Yes, that's correct.

MS. CANDACE GRAMMOND: Now, the Corporation has said in the record -- or on the record in this proceeding, that a hundred point bases shift in interest rates would affect its fixed income portfolio by about $58 million. And the reference for that is in AI-7, the Basic annual report page 36. If you -- if you wish to turn there, please do so.

So AI-7, Basic annual report, page 36. You'll see there a section entitled, "Interest Rate Risk." And then there's a table. And just underneath the table there's a paragraph that reflects what I had indicated about the change of 58 million flowing from a hundred basis point change in interest rates.

MS. HEATHER REICHERT: Yes, I -- I'm there.

MS. CANDACE GRAMMOND: Thank you. Can you tell me whether today, so say the end of September of 2012, there's a more current number to that 58 million, either one that the Corporation has prepared, or can you give me a ballpark of what that number might be today?

MS. HEATHER REICHERT: We could take that as an undertaking. We don't have anything readily available that gives us that number.

MS. CANDACE GRAMMOND: I don't think I -- I'll need to take the undertaking. But can you tell me even directionally whether that fifty-eight (58) would be higher or lower today?

(BRIEF PAUSE)

MS. HEATHER REICHERT: I believe it would be in and about the same. The -- the impact of the hundred basis point change would be -- being 58 million, would be related to the size of the fixed income portfolio, which I think, I mean, has grown a bit. But that would be really what we would need to look at, which we can -- I'll ask folks here to look to see what the size of that portfolio is today, and it would be ten (10) -- or a hundred basis points of that.

MS. CANDACE GRAMMOND: Okay. Thank you.

--- UNDERTAKING NO. 7: So AI-7, Basic annual report, page 36. You'll see there a section entitled, "Interest Rate Risk." And then there's a table. And just underneath the table there's a paragraph that reflects what I had indicated about the change of 58 million flowing from a hundred basis point change in interest rates. To advise whether today, so say the end of September of 2012, there's a more current number to that 58 million, either one that the Corporation has prepared, or provide a ballpark of what that number might be today.

CONTINUED BY MS. CANDACE GRAMMOND:

MS. CANDACE GRAMMOND: Now, this paragraph speaks to the effect of an interest rate change on the fixed income portfolio. But obviously an interest rate change would also affect the Corporation un -- the Corporation's unpaid claims liabilities?

MS. HEATHER REICHERT: Yes, that's

correct.

MS. CANDACE GRAMMOND: And I know it's the view of the Corporation that such an impact would largely offset the effect on the investment portfolio?

MS. HEATHER REICHERT: Not precisely, but you -- yeah, generally offsets -- the two (2) generally offset with not that significant of a difference between...

THE CHAIRPERSON: Could you give us a reference, please, for the document you're reading?

MS. CANDACE GRAMMOND: Oh, I'm sorry, Mr. Chairman. Yeah, it's AI-7, the basic annual report. So AI-7 has the basic annual report, which is the black and white one, and then it has that bound glossy one. It's not the bound glossy one I'm looking at; it's the black and white, and it's page 36.

(BRIEF PAUSE)

MS. CANDACE GRAMMOND: So, Mr. Chairman, Ms. Reichert was just looking at the first full paragraph that appears under that table that's in the middle of the page. That's where the 58 million comes from.

CONTINUED BY MS. CANDACE GRAMMOND:

MS. CANDACE GRAMMOND: And so I -- I think it's been said on the record here, but, basically, this matching strategy, or an immunization strategy, is based on the idea that the -- the time frame for claims liabilities or the generation time claim -- time frame for claims liabilities is about equal to the bond portfolio maturity time frame.

Is that fair to say?

MS. HEATHER REICHERT: Yes. Generally, we try to match the duration of the bond portfolio to the estimated duration of the outstanding liabilities.

MS. CANDACE GRAMMOND: Does the Corporation also try to match the cash flows within -- fro -- from one (1) to the other?

(BRIEF PAUSE)

MS. HEATHER REICHERT: The -- the management is to the overall duration of the liabilities to -- to the fixed-bond portfolio. We don't match cash flow to cash flow, per se.

MS. CANDACE GRAMMOND: Has the Corporation considered doing that, matching cash flow to cash flow?

MS. MARILYN REICHERT: The reality is that some of our liabilities are forty (40) or fifty (50) years in duration, and there are, as far as we know, no bonds that are of a forty (40) or fifty (50) year duration. So for that reason, that's why we're saying we aren't matching cash flow to cash flow.

THE CHAIRPERSON: Since we're on that topic, and this stems back to the discussion that Mr. Johnston and I just had, I'm going back to my economics course analogy of a bathtub. You know, the liability is coming in and then being paid out, and there's a nut that is always there, you know? Like, so in other words, you know, as years progress, you've got this middle nut that will always be there, respective (sic) of who comes in, who comes out of the pool.

And I guess the question that I have is: Knowing that -- if you start from the premise that long-term returns on the equity markets are higher than they will be on the bond market over time, you would think that that would cause you to have enough equity to cover that nut that will continue in the future, a nut of liabilities.

And that's -- that's where I was going with the equity questions, is at some point you would want to make sure that you capture the maximum returns in perpetuity, because you'll always have that nut going forward, that middle nut that will always be present. And that's where my question was coming from, is: Wouldn't it make sense to have an equity portion present in your portfolio to cover the bulk of that -- that -- that significant liability that will always be there going forward?

(BRIEF PAUSE)

MR. LUKE JOHNSTON: Any -- any increase in that equity allocation will -- will definitely increase the variability of -- of net income. So, for example, if we went to the unrealistic, extreme side and invested 100 percent in equities, you could imagine what a -- what a DCAT on equities would look like in that scenario, right?

So when the asset liability study is -- is done, the -- the variability of the net income is -- is also calculated, and -- and you're right. There has to be a certain risk tolerance level that you're willing to accept the variability of equities.

The -- as you know, there's -- we have about 20 percent of equities and other assets, and we've matched the liabilities completely to fixed income. So we are getting extra return from a fairly substantial portion of equities, while almost completely offsetting net-income risk on the -- on the liability side.

So it's, of cour -- as we've discussed, we do -- we are very concerned about rate stability, so there is that balance rate. You can get a little bit extra return and have very, very unstable rates and -- and -- and net income, or you can select kind of a balance that -- through that -- what was done in the asset allocation study.

(BRIEF PAUSE)

CONTINUED BY MS. CANDACE GRAMMOND:

MS. CANDACE GRAMMOND: Just on the issue of matching cash flows, I -- I understand your evidence, Ms. Reichert, that that's not what the Corporation shoots for.

But having said that, does the Corporation track it?

(BRIEF PAUSE)

MR. LUKE JOHNSTON: Is the question

whether -- are you asking whether we actually know what our expected payment pattern is on claim liabilities and bond cash flows?

MS. CANDACE GRAMMOND: Yeah. I mean, does the Corporation look from time to time at the two (2) cash flow categories to see how they relate to one another at a given point in time?

MR. LUKE JOHNSTON: Well, we -- we do definitely know the cash flows that we're using when we're calculating the duration of -- of the two (2) -- of the assets and liabilities. Yeah -- but again we -- we don't attempt to match one (1) to one (1) those cash flows.

The -- sorry, the -- the liability cash flows are -- are fairly unique, and as we said, they kind of -- they start off fairly large and tail off into the far distant future, and happen to produce a -- a duration of about eight (8) or nine (9) years.

But yeah, we -- we haven't made any attempt to try to match that cash flow pattern.

MS. CANDACE GRAMMOND: I understand, Mr. Johnston, that you're saying that the -- the Corporation isn't trying to match the cash flows, but does the Corporation have numbers, you know, even over the first ten (10) years, or the first twenty (20) years, that reflects a comparison of the two (2)?

MR. LUKE JOHNSTON: Are you just asking if -- if we -- if you're asking if we have the expected cash-flow patterns from both sides in the first ten (10) years: yes.

MS. CANDACE GRAMMOND: Is that something that the Corporation can provide for us to review by as an undertaking?

(BRIEF PAUSE)

MR. LUKE JOHNSTON: I'm not sure how long that can take -- or how long that takes, pardon me. The -- the claim liability duration analysis obviously has all the cash flows underlying that analysis available, as of the last time it was done. Perhaps, we can -- I can talk with Mr Bunston and -- and just see how long this would take to get those cash flows. I think it's possible, but I -- I don't know the magnitude of time so I don't want to commit him to anything.

MS. CANDACE GRAMMOND: Fair enough. If you could have that discussion offline and let us know that would be great.

--- UNDERTAKING NO. 8: MPI to talk with Mr. Bunston regarding the providing of cash flows

CONTINUED BY MS. CANDACE GRAMMOND:

MS. CANDACE GRAMMOND: Okay. So going back to the discussion about the -- the immunization strategy that the Corporation has in place. We know that last year the evidence was that the level of immunization was about 80 percent and this year in one of the IR responses that we got the Corporation has said it's up to about 88 percent.

MS. HEATHER REICHERT: Yes, that's correct. That's IR-PUB-1-11.

MS. CANDACE GRAMMOND: Yes. So it would be fair to say then that the Corporation is substantially immunized as against interest rate risk?

MS. HEATHER REICHERT: Yes, I would consider that to be substantially immunized.

MS. CANDACE GRAMMOND: Okay. Now we had looked at the excerpt from the basic annual report which reflects that a hundred basis point shift would have an effect of about 58 million on the investment portfolio at a specific date, that being the end of February of 2012.

(BRIEF PAUSE)

MS. CANDACE GRAMMOND: Sorry. So with that in mind, what's reflected at AI-7, given the extent of the immunization strategy that's in place, would the Corporation agree that in -- in that scenario from page 36 it would be about $7 million of exposure or 7 million that would not be covered off pursuant to the immunization strategy in place?

(BRIEF PAUSE)

MS. CANDACE GRAMMOND: All that we tried to calculate with that is that basically 12 percent, which would be the exposed part of the fifty-eight (58), is -- is about 7 million.

MR. LUKE JOHNSTON: Yeah, I think, on average, we'd expect 80 to -- to 90 percent would be immunized. There may be reasons why it's above or below that, but on average.

MS. CANDACE GRAMMOND: And -- and I do want to -- want to talk about the -- the range of that percentage and -- and how stable it is. And I'm -- I'm going to come to that in a minute.

But if we accept the February 29th,

2012, date, the hundred basis point shift in interest rates that's referenced on page 36 and that giving rise to a drop in the portfolio -- or a change in the portfolio, I should say -- of 58 million, it would be about 7 million, or 12 percent of that, that would not be covered off at this point.

Is there something in that logic that -- that the Corporation disagrees with?

MR. LUKE JOHNSTON: I think that's fair, again recognizing that it's not always going to be exactly 85 percent or something like that, but it should be ballpark in that range, I'd hope.

MS. CANDACE GRAMMOND: And I appreciate again that the percentage can change. But if -- as per one of the IR responses and the 88 percent that -- that was put forward at a particular point in time, it's just a simple cal -- calculation on those numbers?

MR. LUKE JOHNSTON: Yeah, that's the calculation. I just -- I just wanted to make sure that I didn't -- I didn't want to commit and say the -- exactly such a number, because that's not how it works; yeah, just approximately that number.

MS. CANDACE GRAMMOND: Okay. And so the range then, I gather, Mr. Johnston, that you would suggest would be between eighty (80) and ninety (90).

Is that fair? Or would it be between eighty-five (85) and ninety (90)?

Or what -- what would your thought be about the range within which that percentage might fluctuate?

MR. LUKE JOHNSTON: Yeah, it -- assuming the duration is -- is constant, again, I think eighty (80) to ninety (90) is reasonable. There could be that -- those percentages could start to differentiate more as the interest rate changes get larger.

And that, I -- that, I can't tell you exactly wha -- how -- how that relationship's going to be once we start talking a hundred, a hundred and fifty (150) basis point type changes.

MS. CANDACE GRAMMOND: And how likely would you say it is that the im -- immunization percentage will change from year to year?

(BRIEF PAUSE)

MR. LUKE JOHNSTON: So I believe the question was: How likely is that immunization percentage to change? The -- as you know, the Department of -- of Finance manages the fixed-income portfolio. The investment policy statement, I believe, has a plus or minus two (2) year duration matching to the claim liabilities.

Based on what Mr. Gibson believes is the best investment strategy for bonds, he may choose to be bang on the duration, over or under. So that -- that will change over time. And -- and you've seen it change over time.

At times, we've been really close to the same duration. Other times, we've been a little bit lower. And that's, again, based on what Department of Finance feels is the best way to manage their money, given the constraints of the investment policy statement.

MS. CANDACE GRAMMOND: So is it...

(BRIEF PAUSE)

MS. CANDACE GRAMMOND: Is it fair to say then that Mr. Gibson considers the immunization strategy when he's making selections with respect to investments?

(BRIEF PAUSE)

MR. LUKE JOHNSTON: Well, he's -- he's constrained to that -- that two (2) year window of -- two (2) year window, pardon me, two (2) year up or down duration. So I -- I don't have the numbers in front of me, but I believe we are basically almost at the -- the bottom, I guess, of the two (2) year difference there right -- currently.

So we're about at the lowest we can be right now. So any increase in that duration will only improve the matching, going forward.

MS. CANDACE GRAMMOND: And so just so that we're clear, the -- the -- at the end of the day, if interest rates go up, there will be an upward pressure on rates, because bond values would go down; and correspondingly, unpaid claims liabilities would also go down, but not by as much because of the immunization strategy that's in place?

MR. LUKE JOHNSTON: The -- you definitely have the idea right. I -- I would expect, because currently claim liabilities have a longer duration, that the decline in claim liabilities would be greater than the -- the decline in the asset values. Yeah.

(BRIEF PAUSE)

MS. CANDACE GRAMMOND: Now, does the Corporation have knowledge about the practices with respect to these issues that are carried on at SGI in Saskatchewan?

Sorry, this is for the Saskatchewan auto fund.

MS. MARILYN MCLAREN: No, I don't believe we do.

MS. CANDACE GRAMMOND: Okay.

(BRIEF PAUSE)

MS. CANDACE GRAMMOND: Okay. I'm going to move into a different area then, and this is to do with benchmarking with respect to other provinces, in terms of insurance rates.

We know that the Corporation has as a Corporate goal that it charge average rates that are lower than the rates charged by private insurance companies for comparable coverage and service. That comes right out of the annual report.

What about public insurers? Does the -- would it be fair to say that that goal, as well, applies to other jurisdictions with public insurers?

MS. MARILYN MCLAREN: I think I would

agree with that im -- implicitly, because we have covered the entire country in -- in our rate comparison.

MS. CANDACE GRAMMOND: Okay. And, yeah, in that rate comparison, I -- I do have some questions, so let's maybe go to that. It's found at tab 35 of the book of documents, which is PUB/MPI-1-44. We've got it as an attachment. So tab 35 of the book of documents, and it's the third page in.

Perhaps you can explain for the Board sort of how this study is conducted and by whom.

(BRIEF PAUSE)

MS. MARILYN MCLAREN: For quite some time, and I believe it's still true, that we've used a company called Compu-Quote to get auto insurance rate quotations from private insurers across the country. And I believe we go direct to the public auto insurers.

MS. CANDACE GRAMMOND: Thank you. And that's -- the compilation of the data, I assume, is done in house at MPI?

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

MS. CANDACE GRAMMOND: So how are the -

- the vehicles selected? Like we see here there is a series of driver profiles, and then within each profile there's a series of vehicle makes, models, years.

How are those selected?

MS. MARILYN MCLAREN: For the most part both the selection of vehicles and the driver profiles are some of the most common vehicles in Manitoba, some of the most common driver profiles in Manitoba.

MS. CANDACE GRAMMOND: And is there a particular reason behind the Corporation's approach of using Compu-Quote and doing the work internally, as opposed to having an analysis done by an outside party?

MS. MARILYN MCLAREN: I don't -- I don't know that we've ever looked for a third party to do the whole thing. I mean, we -- it -- it -- there's a -- there's a cost associated with using Compu-Quote. We do have relationships. We can go direct to the public insurers. To have someone do the entire thing would be more costly, for sure.

I think the -- the process has been pretty standard, and we're pretty comfortable with the -- the speed with which we can do it, and the cost effectiveness.

MS. CANDACE GRAMMOND: And does this comparison, in terms of rates, take into account differences in coverage from jurisdiction to jurisdiction?

MS. MARILYN MCLAREN: The only -- I mean, this is a standard set of coverage for the most part with respect to deductible levels and so on, third-party liability. It does not -- it -- it's a rate comparison. So, no, it doesn't directly, explicitly try to take rates that are charged in other locations and then change those rates in some fashion, based on some determination about the comprehensiveness or quality of the coverage that -- that's available in different locations.

For example, like we've said a number of times, you would -- the no-fault accident benefits that are guaranteed to Manitobans injured in automobile accidents are really second to none in Canada. They're extremely comparable to the benefits available in Saskatchewan and pretty darn close the benefits that are available in Quebec. They are far in excess of the no-fault benefits available anywhere else.

So we didn't see any need to somehow deal with that other level of complexity of somehow arbitrarily changing the true rates that are charged elsewhere when we know the coverage is, if not second to none, pretty darn close to second to none here in

Manitoba.

MS. CANDACE GRAMMOND: And I -- I think I heard you say that the coverage in Manitoba is very comparable to the coverage in Saskatchewan?

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

MS. CANDACE GRAMMOND: Okay. And does this rate comparison take into account differences in population densities in the different urban centres that are listed?

MS. MARILYN MCLAREN: These are simply the rates that are charged. There are some differences, definitely. I mean, you're comparing Charlottetown with Toronto and Montreal, but -- but these are the rates that are charged.

MS. CANDACE GRAMMOND: And just on that, is there a particular reason why, for example, the comparison is done with Montreal rather than Quebec City, which is arguably more similar to Winnipeg or, you know, Edmonton instead of Calgary?

Or are you just trying to pick one (1) city in each province?

MS. MARILYN MCLAREN: I'm not aware of any reason. I think for the most -- for the most part these are provincial capitals. Quebec City would certainly fall into that category as opposed to Montreal, having had a look at this.

MS. CANDACE GRAMMOND: I think Edmonton does, too.

MS. MARILYN MCLAREN: Maybe they're the largest. I don't honestly -- yeah, I'm scrambling. Maybe they're the largest ones. Yeah, okay, we can find all the mistakes in what I just said.

MS. CANDACE GRAMMOND: You slept on the street last night. It's okay.

MS. MARILYN MCLAREN: I slept on the street last night. And this is the first mistake I've made, ever.

MS. CANDACE GRAMMOND: Okay, so --

MS. MARILYN MCLAREN: No rationale.

MS. CANDACE GRAMMOND: No. Fair enough. And the -- the rate entries that we see here -- the rate entries that we see here that are shaded represent the ones that are lower than Manitoba?

MS. MARILYN MCLAREN: I believe that's true.

MS. CANDACE GRAMMOND: The -- the shading is kind of light on the first page, and I think that's just a function of the photocopying. But if you -- if you look closely, you can see that there are some shaded squares on each of the three (3) pages.

And I see that on the first page we see some shading under Saskatchewan, some under Montreal, and some under Charlottetown. But as we turn to the subsequent two (2) pages, there's an awful lot of shading under Saskatchewan and -- and not elsewhere.

What can you tell us about why the rates in Saskatchewan seem to be pretty consistently lower than ours?

MS. MARILYN MCLAREN: I -- I suspect really the sole reason is that they have one (1) rating territory in Saskatchewan. The rates, if -- if we had used Brandon instead of Winnipeg, our rates probably would have been the lowest in the entire country. But Regina -- you know, Saskatchewan has a number of fairly similarly sized, you know, smaller/mid-sized urban centres, right. Regina is significantly smaller than Winnipeg, but they also got Saskatoon and, you know, the Battlefords and Swift Current and Moose Jaw. And they have number of -- of urban centres like that that Winnipeg -- Manitoba doesn't really have.

So if we had compared this in our lowest-rated territory that would be enough to really wipe out any lower rates in Saskatchewan, I believe.

MS. CANDACE GRAMMOND: And I -- I think

we've had discussions before at these hearings about one (1) rating territory for Manitoba. And I recall that that was something that the Corporation probably wasn't excited about.

Can you just comment on that a little bit?

MS. MARILYN MCLAREN: Yeah. We have statistical evidence that risk varies according to the territories that we have here in Manitoba, and it would really -- to -- to move to one (1) rating territory would fail the test of -- of, you know, fair and equitable rates sort of based on loss costs.

I don't know whether they have one (1) territory in Saskatchewan for some sort of a provincial policy reason or whether they don't have the same statistical data. I mean, it is a very different -- the -- the population is dispersed very, very differently in Saskatchewan than it is in Manitoba. They may very well have as compelling data that they should not have more than one (1) territory as we have that we should.

But the reality is here in Manitoba the -- the territories that we have embedded in the regulations really do reflect the risk across the province.

MS. CANDACE GRAMMOND: Now, as I had stated, and -- and we can see on the first page, there's also some shading relative to Montreal and Charlottetown. I appreciate that there isn't really any shading under either of those except for one (1) on the last page.

Can you comment on why we're seeing some rates in Montreal and Charlottetown that are lower than ours?

MS. MARILYN MCLAREN: Not really. I -- I suspect Charlottetown, it has something to do with both the less-dense population. It's a very, very small centre. I believe the no-fault accident benefits that are -- are required -- the legislation in that province are -- are a fraction of what they would be in some other parts of the country, including Manitoba.

Quebec, the government runs through a very similar mandate as MPI, runs only the injury compensation portion of automobile insurance. So the no-fault benefits are administered by a -- a Crown corporation, a government plan in Quebec. But it is a very competitive market for the -- the TIN (phonetic) as -- as we say, the -- the actual coverage on the vehicles.

So, you know, there's ten (10) or $40 or so difference. I think that's really just sub -- subject to some of the marketplace realities in -- in that province.

MS. CANDACE GRAMMOND: So when the Corporation gets the results of this rate comparison back, does it do any further analysis to try to get to the bottom of where other cities are lower, or is -- is this just compiled for the purposes of filing at the Board?

MS. MARILYN MCLAREN: Directionally, we pay a lot of attention to it. We don't -- we don't dive into individual rating differences and individual profiles in -- in different provinces. But if we -- if we continued to see -- for the most part, in a significant majority of situations in every province, we are the lowest. And where the one (1) exception would be Saskatchewan, we understand sort of the base rationale why there would be differences. And we're still within the ballpark that that's pretty much where we leave it.

MS. CANDACE GRAMMOND: Now, you commented on if Brandon were used here instead of Winnipeg, Manitoba would for sure be the lowest.

Have you ever thought, or would there be any value in conducting comparisons of Brandon to similarly sized cities in other provinces just to sort of take the analysis down to a different level?

MS. MARILYN MCLAREN: Sure. And we've had some conversations recently about the extent to which we might want to have another look at how we do this. And really one of the things that really important to us is that we have some consistency from year to year. But -- but, also, we need to make sure that it is relevant, that it resonates with Manitobans. So there's always some things like that that we can tweak now again -- now and again.

MS. CANDACE GRAMMOND: Okay. Now, we had some back and forth in the IRs with respect to this issue of the corporate goal being to have the lowest rates and, you know, this -- this analysis and -- and coverage differences.

And the -- the Corporation made the statement in one of its responses that it didn't believe that it was within the jurisdiction of the Public Utilities Board to be testing the Corporation's assertion that its premiums are -- are the lowest in the country. If you need a reference for that, I've -- I've got it.

My question was: So who is responsible for -- for testing that?

MS. MARILYN MCLAREN: I might wish that I had asked you for the reference. But I -- I believe what we were -- that sort of the full context of that was that the interrogatory had -- had referenced sort of the -- the rate comparison in relation to the coverage.

And that's -- you know, I mean, the -- the coverage is the coverage, right. I mean, whatever the legislature chooses to make part of the mandatory compulsory coverage, we have to find a way to charge rates to cover the costs.

So I think -- I don't think it's at all unreasonable for this panel -- for the PUB to ask questions. I mean, when -- when, you know, we publish information about our rates and how they compare and how we think that aligns with the initial mandate of the Corporation, I think rates -- anything to do with rates are -- are relevant to this Board.

So I think it's -- it's muddied the water, in my thinking, when I look back at the IR, because of the added complexity of in relation to the coverage. So asking questions about the rates when we hold ourselves out to sort of have a certain goal and compare ourselves to others, I think that -- that's fair game.

MS. CANDACE GRAMMOND: Mr. Chairman, I'm just going to need a moment. I'm -- I'm at a break where I'd be going into a new area, which is cost allocation. And I know I'm not going to finish that today, so I probably am just going to skip. I just need a minute to find a short area that I can cover in twenty (20) minutes.

Oh, yeah, of course, please.

THE CHAIRPERSON: I just would like to ask a few questions, and this is really for my education. I -- I know that the government was considering adopting affordability legislation, in respect of the public utilities.

Now, this was an election promise made during the last election. Now, I -- does MPIC get affected by that potential legislation or...?

(BRIEF PAUSE)

MS. MARILYN MCLAREN: We understand that le -- legislation has been passed. It has not yet been proclaimed. We're scrambling a little bit, remembering the exact name of it. It -- it does include Autopac rates in that. I can't say a whole lot more. But it's not so much about affordability as --

as it is -- it's a compare -- it's sort of a national comparison concept, that sort of the basket of utilities would be lower in Manitoba than elsewhere. So it's similar to what we've done here.

Directionally, my intention would be to try to align whatever else we do publically with whatever we're obligated to do under that legislation, because it would -- just wouldn't make sense to have -- you know, do -- do something one way over here and then contribute to sort of this legislative imperative over -- in a -- in a different way, so.

If this changes next year, it would likely be in response to trying to align what we do in this regard with what that legislation speaks to.

THE CHAIRPERSON: Now, the data collected for the -- the legislation -- pursuant to the legislation, comes from MPIC, or it comes from some other source?

MS. MARILYN MCLAREN: I -- I think the answer is probably yes. I think the -- both. I think there will be some sort of third party involvement in, you know, collecting most of the data from across the country. I think the MPI rates are -- are in regulation, and they would probably come straight from the actual act and regulations in Manitoba. I don't think they'd pay a third party to collect the data for Manitoba, is all I'm saying, really.

The Bill is called the Affordable Utility Rate Accountability Act.

CONTINUED BY MS. CANDACE GRAMMOND:

MS. CANDACE GRAMMOND: Thank you. Okay. I have a few questions on some areas that relate from the Board's perspective to the DSR scale and people's driving records. And I know that these are all areas that have been touched on in the past, in past proceedings, where the Board has expressed concerns about essentially the ability of a driver to avoid the full consequences of his or her actions in terms of the DSR scale. And the first of those areas is the intersection safety cameras, or red light camera. And I know Board Member Botting had some questions about those either yesterday or Tuesday.

So we have a little bit of evidence about it. And we talked about the fact that these types of tickets are issued under the legislative framework, there are demerits that are attached to them. And I know I -- Ms. Mclaren, in response to the question, you had advised that the Corporation doesn't have information with respect to the frequency of the convictions that are taking place with respect to those tickets.

Is that all correct?

MS. MARILYN MCLAREN: Yes, that's all correct.

MS. CANDACE GRAMMOND: Does the Corporation have any statistics on what we might call "problem intersections" relative to the intersection safety cameras? In other words, intersections where there's a high frequency of collisions taking place.

MS. MARILYN MCLAREN: I believe we collect data when -- when it is available from claimants with respect to where accidents occurred. Wherever possible, we -- you know, we've -- we've tried to implement some software that actually has some consistency; that it's, you know, Grant at Pembina every time, as opposed to not Pembina at Grant half the time, and Grant to Pembina the other half, and so on. We try to do some of that.

We -- I would have to come back with specific information as to sort of the -- the extent of that report, how often it's published and so on, but leave it as something that we do under the Drivers and Vehicles Act responsibility.

And I -- I can tell you that the -- the

crash locations are very, very dispersed. There's certainly not any one (1) location in Winnipeg that would account for even 5 percent of all of our crashes, or all of our claims costs, you know? So it is -- it is -- it's not -- not a densely populated city in terms of its geographic footprint, and -- and the accidents are quite dispersed.

MS. CANDACE GRAMMOND: I would take you up on that offer if you could report back to us about that.

--- UNDERTAKING NO. 9: MPI to provide report regarding problem intersections

THE CHAIRPERSON: I clearly recall articles in the free press about locations in this city, or intersections in this city that had high incidents of accidents. I mean, that data would have come from -- from what source? Would it have come from MPIC or...?

MS. MARILYN MCLAREN: I -- I believe so. Sometimes that data comes from traffic accident reports, which would therefore come from the police.

But I -- I think for the most part sort

of the -- the comprehensive body of data about where accidents happen, you know, reg -- only -- as we talked about the other day, only the most serious accidents are reported to police, so I think we do have some form of a report that we produce about all the claims that come to us in terms of -- and we do our best to sort of track locations on that basis.

CONTINUED BY MS. CANDACE GRAMMOND:

MS. CANDACE GRAMMOND: Thank you. The -- the second area in addition to the -- the red-light camera tickets where the -- the Board has expressed concerns about individuals not taking the consequences on their DSR rating of their actions, is in the area of -- of buying back claims. We know that that's something that does occur from time to time.

Is the Corporation in a position to give us some numbers, either now or by way of undertaking, about how many claims are generally bought back annually, and the corresponding dollar value to those?

MS. MARILYN MCLAREN: I'm not sure. We can have a look. And it -- it's really kind of the -- a compliment to the conversation that -- that the Chairman and I had the other day. We -- we would certainly have no idea about how many people would chose not to use their coverage, but people who have and then had to rethink that decision for whatever reason they would chose to, we -- we can see -- we can have a look at what we've got.

MS. CANDACE GRAMMOND: Thank you. And the -- the Corporation does agree that the net effect of a claim that's bought back is that whatever consequences would have otherwise flowed to a person's DSR rating are not going to be flowing at that point?

MS. MARILYN MCLAREN: Yeah, it puts them in the position as if they had not reported the claim.

MS. CANDACE GRAMMOND: Now having said that, if associated with the collision there was some kind of a ticket issued to the person for which they were convicted, that would obviously stand on its own, irrespective of the insurance claim?

MS. MARILYN MCLAREN: Absolutely.

MS. CANDACE GRAMMOND: Okay. And then the third area that the Board has expressed concern in with respect to this idea of the -- the accuracy of an individual's DSR rating is in the family transfer piece. So this is the concept, just for the record, of two (2) drivers within the same household, all of the vehicles in one (1) of the driver's name that has the -

- the better DSR rating.

Does the Corporation have numbers on transfers within households that would be from an individual with a lesser DSR rating to one with a better DSR rating? And I'm asking in terms of the number of times that this is going on, and if there's any indication of a corresponding dollar loss to the Corporation?

MS. MARILYN MCLAREN: We could go back and provide the information that we filed with this Board a couple or more years ago that answered that question at that time. I mean, you -- you can never predict why people are doing that, and -- and some of them may very well have been reasons that absolutely had nothing to do with trying to get a particular discount.

Having said that, the number therefore is as automatically assumed to be overstated, and even on that basis it was -- it was a low number; It was not material to the overall insurance fund. But we can pull that out and bring it forward again. We have not done anything new on that since that time.

MS. CANDACE GRAMMOND: If you could, I'd appreciate it.

--- UNDERTAKING NO. 10: MPI to indicate the number of transfers within households that would be from an individual with a lesser DSR rating to one with a better DSR rating, and if there's any indication of a corresponding dollar loss to the Corporation

CONTINUED BY MS. CANDACE GRAMMOND:

MS. CANDACE GRAMMOND: And can you just explain to the Board, you know, why it is or on what basis that these transfers are permitted?

MS. MARILYN MCLAREN: People are allowed to sell or give their vehicles to anybody they want. Within the -- the family situation, it also has nothing to do with household that -- that has been referenced either. I mean, it -- one (1) of the considerations of the difference between giving and selling is for tax payment purposes. And the -- the Retail Sales Tax Act has a list of family members that someone can gift their vehicle to and not have to pay tax. If you give your vehicle to someone who's not on that list, that recipient still has to pay tax on the actual cash value of the vehicle.

So -- but people can give or sell their vehicles to anybody they want, so there's no real way to restrict that. We really believe that our -- our plan is fundamentally in a better position to get the right rate because of the DSR scale that we have on the driver's side of the equation.

Bad drivers can hide, you know. And particularly, you know, back in the day when we had a maximum ninety-nine dollar ($99) surcharge for nineteen (19) demerits, that -- that was one (1) thing, but now we're talking as much as, you know, potentially twenty-five hundred dollars ($2,500). The DSR scale is a driver-based system and I think we are well positioned to negate any potential impact. And -- and as Mr. Johnston talked about earlier, since we've got DSR in place we've seen no indication that there's any sort of nefarious manipulation going on.

MS. CANDACE GRAMMOND: And is the Corporation in a position on a case-by-case basis to weed out those situations in with -- in which someone is making a transfer to get a -- a better premium or a -- a better discount as opposed to those that may be for completely unrelated reasons?

MS. MARILYN MCLAREN: No, we're in absolutely no position to do that. I can only imagine the public backlash if we were to start, you know, questioning people as to why they were giving up ownership of their vehicle.

MS. CANDACE GRAMMOND: Thank you. Mr. Chairman, that's the end of what my predecessor would have called the "short-snapper section." So I can start a longer section and I'm happy to do that or --

THE CHAIRPERSON: No, I think we should concentrate on any other short snappers that might be wanting to come out in the open.

I have a question in relation to the policy debate, at least the media policy debate, about speed limits in proximity of schools. Now, I'm wondering would MPIC have any data that would demonstrate increased or decreased costs -- injury costs related to lowering the speed limit in proximity of a school?

MS. MARILYN MCLAREN: No, we don't have such robust data collection mechanisms that -- you know, we would have to somehow find a way to plot the location of schools into this framework that we have with the different intersections and -- and streets and so on. That -- that's not part of the system that we have.

But in terms of just our general understanding of where -- I -- I guess really for the most part what we would be concerned about around schools would be injuries. Injuries to pedestrians, children. We don't have a lot of incidents of that. It is not something that -- that we would be flagging as a -- a high-risk area that -- that we think would deserve attention.

Now, having said that, I'm talking about sort of anecdotal narrative information from our injury case managers. We don't have the data that would help us prove or disprove.

(PANEL RETIRES)

THE CHAIRPERSON: I think that's all for the short questions, so I -- I think we should adjourn the proceedings and resume them on 9 -- at 9:30 on Monday morning.

Do we have any other business to attend to before we adjourn? Okay, have a good weekend everyone. Thank you very much.

--- Upon adjourning at 3:53 p.m.

Certified correct,

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Wendy Warnock, Ms.

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