This is not normal:

Fairness in extraordinary times!

Closing submissions of the Public Interest Law Centre on behalf of the Consumers' Association of Canada (Manitoba)

November 5, 2020

Two fundamental Challenges – raised by the current GRA

1. We have not "returned to normal" – these are extraordinary times with resultant stresses for consumers, for forecasters and for formulaic capital management plans.
2. New analysis is raising important questions about the fairness of our ratemaking system as it relates to driver safety rating, territories and uses only some of which can be answered by the Public Utilities board.

In the midst of a proposed 8.8% rate change – why isn't this easy?

- Because the MPI "best estimate" for the 20-21 year is palpably wrong amid sadly bright Codes of Orange and Red raising the risk of excess capital beyond the capabilities of a rule bound capital management plan;
- Because the extraordinary events of the past 8 months coupled with statements by MPI which appear to "walk back" its "non-discretionary" commitment to transfer excess capital back to the captive ratepayers they came from, has undermined stakeholder confidence in one of the key philosophical underpinnings of the Capital Management Plan;
- Because the output of the minimum bias examination of territories, uses, rate groups and driver safety rating (DSR) has quantified a stark issue of unduly discriminatory rates for vehicle owners at the upper limits of the DSR scale, while raising critically important issues about the relativities related to territories and uses;
- Because the issue of registered versus primary driver as it relates to the DSR rating system is still outstanding and because the ultimate decision maker on that issue is not in the room;
- Because it is not right for registered owners at DSR level 15 to be paying vehicle premiums that may be more than 20% above their indicated costs and have to wait a decade for just and reasonable equilibrium;
- Because it is troubling to see an important class facing a 4.7% rate increase when MPI is seeking a 8.8% rate change

Just and Reasonable Rates

- The PUB is an independent, quasi judicial administrative tribunal entrusted with approving just and reasonable rates for MPI.[1]
- In approving just and reasonable rates, "(t)he PUB has two concerns when dealing with a rate application; the interests of the utility's ratepayers, and the financial health of the utility. Together, and in the broadest interpretation, these interests represent the general public interest."[2]

[1] The Public Utilities Board, "About the PUB", online: http://www.pubmanitoba.ca/v1/about-pub/index.html; & *Crown Corporations Governance and Accountability Act*, CCSM c C336, s. 25(1)(3); & *Public Utilities Board Act*, CCSM c P280, s. 77(a).
[2] *Consumers' Association of Canada (Man.) Inc et al v Manitoba Hydro, Electric Board*, 2005 MBCA 55, at para 65.

Elements of Just and Reasonable Rates

- ensuring forecasts are reasonably reliable;
- ensuring activities are necessary and prudent;
- assessing the reasonable revenue needs of the Corporation in the context of the overall general health of MPI;
- determining an appropriate allocation of costs between classes and lines of business; and
- setting just and reasonable rates in accordance with statutory objectives.[3]

[3] PUB Order 98/14, at 28.

A heightened focus on forecasting, rate discrimination, price signals and just and reasonable ratemaking

- With 100% MCT accepted on a 2 year pilot project basis and a 8.8% rate change proposed, the focus of debate in this hearing has been less about prudence and financial targets
- And more about:
  - forecasting;
  - potential rate discrimination;
  - appropriate price signals; and,
  - the application of highly uncertain forecasts to just and reasonable rates
- As always, a reasonable and balanced approach to risk in the public interest underlies all considerations of just and reasonable rates

Issue 1: Can we conclude that the MPI best estimates for the 2020-21 year and the 2021-22 year are reasonably reliable?

- **No** - the October 9, 2020 MPI best estimate for the 20-21 year already has been overtaken by the unforeseen duration of the pandemic and its impact on collision frequency (which suggests that the projected excess retained earnings at year end are understated at a time of great need for many Manitobans)

- **No** – it is highly uncertain whether we will "return to normal" for the 21-22 year (which suggests that the PUB should be playing a more assertive monitoring role informed by monthly MPI updates)

- **But** for the 21-22 year, the MPI best estimate may be the best we have even with ongoing uncertainty relating to PIPP (which suggests the proposed AAP rate reduction of 0.8% is reasonable)

Things are not back to normal

- We have gone from Code Orange to Code Red in Winnipeg.
- Manitobans continue to struggle:
    - *DR. BYRON WILLIAMS: Okay. And it would be fair to say that things have not returned to normal economically, socially, or in the personal finances of a number of Manitobans as a result of COVID-19 impacts, sir?*

      MR. LUKE JOHNSTON: That's -- it would be a reasonable assumption, yes.[4]

[4] Transcript from October 19, 2020 at 314 WILLIAMS/Johnston.

Things are not back to normal

- Many Manitobans continue to work at home.
- Google workplace mobility patterns remain lower than pre-pandemic levels and have yet to rebound beyond pre-pandemic levels.[5]

[5] MPI Exhibit 53.

Things are not back to normal

- And they are not going back in the near future;
- For example: roughly 70 percent of MPI employees remain home with no near term prospect of returning to work;[6]
  - *DR. BYRON WILLIAMS: Okay. And, Mr. Giesbrecht, are they going back to work at the office next week?*

    MR. MARK GIESBRECHT: I do not expect so.

    DR. BYRON WILLIAMS: Do you expect them to go back to work at the office before January 1st, 2021?

    MR. MARK GIESBRECHT: Hard to say. We continue to follow guidance from -- from Public Health and -- and, you know, how the pandemic is – is transpiring. But at this point, hard to envision that they'd be back before Christmas. [7]

[6] Transcript from October 19, 2020 at 307-09, WILLIAMS/Johnston.
[7] *Ibid.*

Fewer Manitobans driving to work on a daily basis has material implications on collision frequency and MPI forecasts

- MPI's reported claim counts and Google workplace mobility patterns are very similar, with both remaining lower than pre-pandemic levels and yet to rebound beyond pre-pandemic levels. [8]

[8] MPI Exhibit 53.

The Asymmetric Effect of COVID-19 on Costs, Revenues and Risks

- In reality, MPI has shown that claim costs are tracking significantly below budget in 2020/21, while there has been only minor impacts to premiums.[9]

[9] CAC 2-4 b

The Asymmetric Effect of COVID-19 on Costs, Revenues and Risks

- Pandemic influenced mobility patterns have a material downward effect on costs
- There are closely correlated relationships between:
  - Collision claims incurred frequency and ultimates;
  - Property claims incurred (perfectly correlated); and,
  - Claims expenses – MHSC, towing, medical and chiropractic consults.[10]
- Although not reflected in the COVID19Q3 and Q4 scenarios, there also is a relationship between collision frequency and PIPP which is more challenging to disentangle:
  - *MR. LUKE JOHNSTON**: Yeah. Our – our assumption that if collision goes down 20 percent, PIPP will probably go down 20 percent as well**, I think that continues to be reasonable. It just takes a little longer to figure out the final ultimate PIPP losses.* [11]

[10] PUB 1-45 b
[11] Transcript from October 19, 2020 at 320-21 WILLIAMS/Johnston [emphasis added].

The Asymmetric Effect of COVID-19 on Costs, Revenues and Risks

- To date, the pandemic has had little effect on premiums

  - *DR. BYRON WILLIAMS: In effect, to date, there's been an asymmetrical effect of COVID-19 in terms of claims incurred where those effects have been noticeable, versus those effects in terms of premiums where those effects have not been noticeable.*

    MR. LUKE JOHNSTON: Yeah. Of course, we -- we don't know for sure, but living in Winnipeg, you do tend to need access to your vehicle to get around, and at least to date, it appears that customers are continuing to keep that insurance on their vehicle.[12]

  - *MR. LUKE JOHNSTON: We have not. And just -- just kind of restating, we definitely had a lot of concerns over our -- our premium intake. . . .We made a minor adjustment for volume, but we're tracking very close to -- to target.*[13]

[12] Transcript from October 20, 2020 at 363 WILLIAMS/Johnston.
[13] Transcript from October 20, 2020 at 178-79 MCCANDLESS/Johnston.

The Asymmetric Effect of COVID-19 on Costs, Revenues and Risks

- There continues to be much uncertainty in the forecasts for the remainder of the 2020/21, but MPI believes that these risks are either potentially favourable (i.e. less claims than expected) or adequately modeled in this FCT report (i.e. equity decline risk).[14]

[14] MPI Exhibit 24, 12-13.

The Naïve Forecast is not the Best Estimate for 20-21

- *MR. LUKE JOHNSTON: No. I – the truth is this is unchartered territory. And we, clearly, don't know what the forecast is going to be for COVID.* [15]
- CAC Manitoba concurs

[15] Transcript from October 19, 2020 at 333-337 WILLIAMS/Johnston.

MPI has struggled to forecast the implications of COVID-19 for the 20-21 Year

- In the emergency rebate hearing, MPI forecast: an assumption of a reversion to "normal frequency" of forecasted claims after May 15, 2020. [16]
- *DR. BYRON WILLIAMS: And again, we'll get into this later, but the assumption of normal frequency post-May 15th, 2020 has not borne out to date, correct?*

  MR. LUKE JOHNSTON: It has not, and we're still under budget -- not the same magnitude, but -- but still under budget, yes.[17]

[16] *Order 71-20*, 10-11.
[17] Transcript from October 19, 2020 at 317-18 WILLIAMS/Johnston.

The October 9 Naïve forecast Update assumed a reversion to normal by August 31, 2020

- *DR. BYRON WILLIAMS: Would you assume a return to normal, sir, in the ultimates for September 2020?*

  MR. LUKE JOHNSTON: Yes. . . .

  DR. BYRON WILLIAMS:. . . And if we look at that naive forecast, line 1, and we look at the results for that, sir, in terms of COVID-19 impacts, that assumes a return to normal as of September 1st, 2020 and running all the way out to the end of March 2021. Would that be fair?

  MR. LUKE JOHNSTON: That's right. Really, September 2020 and thereafter.[18]

[18] Transcript from October 19, 2020 at 329-331 WILLIAMS/Johnston.

Current Collision Frequency Patterns Still "Ain't Normal"

- *DR. BYRON WILLIAMS: When you see a collision frequency still tracking at approximately 10 to 15 percent below the five (5) year average in September of 2020, that would suggest to you that there's still an ongoing COVID-19 impact, agreed?*

  MR. LUKE JOHNSTON: That would -- it'd be very likely that that was the case, yes.[19]

[19] Transcript from October 19, 2020 at 341-342 WILLIAMS/Johnston; see also MPI 2-1(b).

The MPI Best Estimate – Pre-dates Code Orange and Code Red for Winnipeg

- Winnipeg went into Code Orange after the MPI Oct 9 Update was filed:
  - *DR. BYRON WILLIAMS: And, Mr. Johnston, where we are in Winnipeg now is a state of code orange. Is that correct?*

    MR. LUKE JOHNSTON: Yes. . . .

    DR. BYRON WILLIAMS: And, Mr. Johnston, we're now in the third quarter of the MPI fiscal year?

    MR. LUKE JOHNSTON: Yes.

    DR. BYRON WILLIAMS: And it would be fair to say that there are ongoing impacts of COVID-19 on the lifestyles, behaviours, and financial circumstances as Manitobans as we speak today?

    MR. LUKE JOHNSTON: True. Yeah. [20]

[20] Transcript from October 20, 2020 at 354-356 WILLIAMS/Johnston.

MPI's Best Estimate Assumes Code Orange Never Happened in Winnipeg in the fall of 2020

- *DR. BYRON WILLIAMS: Just to remind ourselves, that [naïve] scenario assumes no COVID-19 impact in September of 2020 or moving forward, agreed?*

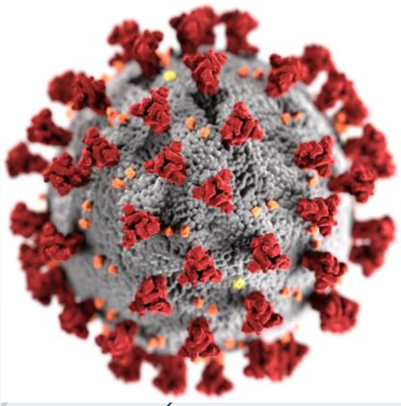
  MR. LUKE JOHNSTON: Agreed.

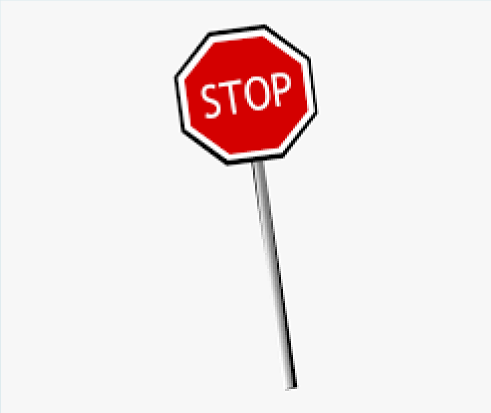
  DR. BYRON WILLIAMS: In essence, it would be as if the code orange in Winnipeg never happened?

  MR. LUKE JOHNSTON: It would – it would be our original pre-COVID forecast, yes. Yeah. [21]

[21] Transcript from October 20, 2020 at 368-370 WILLIAMS/Johnston.

Now we are in Code Red!





Updated Collision Frequency and Mobility Data suggest an ongoing and growing effect in terms of variances from historical averages in mid Sept – Oct as compared to August month end

- Mr. Johnston confirms that as of August 28th, 2020, reported collision claims was between 10% and 20% below the 5 yr average. [22]
- Mr. Johnston confirms that after August 28, 2020 that there were some weeks where the 2020 reported collision claims were between 20% and 30% below the 5 yr average. [23]
- Mr. Johnston confirms that after September 18th, it appears that 2020 reported collision claims are 20% or more than 20% below the 5 yr average. [24]

[22] Transcript from November 3, 2020 at 2186 WILLIAMS/Johnston.
[23] *Ibid* at 2187.
[24] *Ibid* at 2188

There is no “return to normal” in the third quarter

- *DR. BYRON WILLIAMS: And it's also concluding that MPI reported claims counts and Google workplace mobility patterns both remain lower than pre-pandemic levels and have yet to rebound beyond pre-pandemic levels, agreed?*

  MR. LUKE JOHNSTON: Agreed [25]

[25] Transcript from November 3, 2020 at 2188 WILLIAMS/Johnston.

COVID-19 Q4 estimate is the best estimate

- Well into the third quarter with "higher than August" impacts on collision frequency as compared to five year average.
- Zone Red for Territory 1 which is by far the largest territory in terms of registered vehicles.
- Contemplating curfews (judicial notice)
- Significant workforces not contemplating coming back before Christmas (ie MPI)

Recommended finding: that COVID19 Q4 is the best estimate 20-21

Change in Severity Trends During COVID – Reflect in part - the Under-representation of urban, high frequency, lower severity claims

- *MR. LUKE JOHNSTON: Correct. Rural claims are often on the highway and -- and generate a larger severity. **And so, again, it's more -- it's not so much an increase in rural as it is a decrease in the city and -- and change in that distribution**.*

  MS. KATHLEEN MCCANDLESS: And I take it that there was little change in rural driving patterns during the what I'll call to – call colloquially -- colloquially the lock-down period?

  *MR. LUKE JOHNSTON: What I've seen – the latest information I've seen, and it's more – likely more up-to-date than -- than what we filed, we track -- I'm trying to remember the name of it – mobility data. **So, there are different breakdowns provided for people going to work versus people travelling in rural.** And there has been an increase in rural driving and a pretty sharp decrease in commuting to work in the city type of driving, so no surprise that we see more rural claims because of that.* [26]

[25] Transcript from October 19, 2020 at 295-97, MCCANDLESS/Johnston.

There is common ground between CAC Manitoba and MPI in terms of the 21-22 forecast for claims incurred

- Things are highly uncertain due to COVID19
- Standing where we are today – a "return to normal" is the best guess given COVID19 uncertainty but is only a guess!
  - This year in our history is going to be an outlier year. There's no other way to put it. Everything we see in this year, whether it's volume or upgrade or claims experience, is likely going to be unusable for forecasting in a normal situation.

    So our view is that our best estimate of '21/'22 today is that we use the -- the forecast pre -- pre-COVID. But, of course, like, being reasonable, I only think that now. Three (3) or four (4) months from now, it could get worse, and it would be hard to make that statement. But as of today, that's what I -- that's what MPI believes. [27]

[27] Transcript from October 19, 2020 at 272, MCCANDLESS/Johnston.

Recommended findings and orders for 20-21 and 21-22 forecasts

Recommended Findings

The naïve forecast should be rejected as the best estimate for 20-21

COVID19 Q4 estimate should be accepted as the best estimate for 20-21

MPI return to normal forecast for 21/22 should be accepted as best estimate for 21/22 at this time

Recommended Order

MPI should provide regular monthly updates of COVID19 impact on claims incurred until March 2021 with PUB reserving discretion to extend time period

Monthly updates should present both accounting (budget variance) and actuarial world views (variance from 5 year frequency or other)

Consistent with the statutory regime, PUB reserves right to review and vary 21-22 rates if it identifies a material change in circumstances

A COVID19 Q4 or Q3 estimate has a material effect on excess retained earnings

- Projections for 20-21 in initial GRA filing - $78.6 million net income. [28]
- MPI estimates a $29 M positive variance in basic ultimate claims incurred from mid May to Aug 31 in Oct 9 Update. [29]
- Naïve forecast Oct 9 update assumes no pandemic impact beyond Aug 31, 2020.
- If no C19 Impact after Aug 31, MPI expect net income to be $105.4 million can achieve 100% MCT over three year release period with 5% cap. [30]
- If no C19 Impact after Dec 31, expect net income 127,488 20/21 and 88 M over MCT target – - will not achieve 100% MCT over three year release period with 5% cap - would require annual 6.08% release to achieve 100% MCT within 3 years. [31]
- If C19 impact up to March 31, 2021 $147 M net income and $110 in reserves over 100% MCT RSR (after the emergency rebate of $58 million) – 127% MCT - will not achieve 100% MCT over three year release period - would require 6.84% annual release to achieve 100% MCT within 3 years. [32]

[28] MPI Exhibit 27 at 27.
[29] MPI Exhibit 38.
[30] Transcript from October 20, 2020 at 370-72 WILLIAMS/Johnston and Exhibit 29.
[31] *Ibid.*
[32] *Ibid.*

Recommended Finding

- The 5% capping rule is interfering with the timely return of excess capital at a time of substantial hardship for many Manitobans

Do Q3 COVID19 and Q4COVID19 estimates include property or PIPP reduction provision?

- *DR. BYRON WILLIAMS: So to the extent that it does not include property in the COVID-19 third-quarter scenario or COVID-19 fourth-quarter scenario, it would tend to underestimate the COVID-19 impact, sir?*

  MR. LUKE JOHNSTON: That's true. I wouldn't expect property damage to be a -- a very large number, but if it was missing, it – these numbers would be slightly higher, yes.

- CAC Manitoba understands the estimates do not reduce expected PIPP claims and remains uncertain where there is an adjustment for property (which is perfectly correlated with collision).[33]

[33] Transcript from October 20, 2020 at 360 WILLIAMS/Johnston.

What are the implications of COVID-19 for the Capital Management Plan?

- MPI does not anticipate any impacts by COVID-19 on its Capital Management Plan unless significant COVID-19 related claims savings persist much longer than anticipated or unless a second wave of COVID-19 prompts a mass shutdown. [34]

[34] CAC (MPI) 2-1

What is the status of the Capital Management Plan?

- Capital Management Plan accepted by PUB for 2 year trial period
- We are clearly in the trial period as decisions regarding capital adequacy in the emergency rebate were governed by the trial financial target of 100% MCT for Basic

Some key technical elements of the Capital Management Plan

- "Compulsory", "non-discretionary" [35] commitment by MPI to transfer excess reserves (over 200% MCT) to basic program at fiscal year end
- MPI target of 100% MCT for basic accepted for the 2 year trial period
- No more rebates
- Rate stability enhanced by releases of excess capital over 3 years toward 100% MCT (5% cap on releases) or by 5 year rate increases to address capital shortfalls below 100% MCT
- In order to **manage rate volatility**, which is the main purpose of the RSR, the CMP uses a 5% cap on capital release provisions in any given GRA. (RSR 6.4)

[35] Transcript from October 21, 2020 at 697-698 BOARD CHAIRPERSON / Giesbrecht; Mr. Scarfone, in the submission last year, said -- very eloquently, I might say: "The transfers have moved from being discretionary to non-discretionary, and they're automatic.

The Philosophical Underpinnings of the CMP

- Recognition that basic and extension intertwined with an implicit recognition by MPI that extension's dominant position would not exist without basic
- Recognition by MPI that excess capital whether in extension or basic should be returned to basic ratepayers
- <u>in exchange for</u>
  - Significantly more conservative financial targets for basic
  - An end to "disruptive" rate rebates
  - Enhanced rate stability through 5% annual cap on releases

Prospective Best Estimate for Current Year is Central to CPM

- *DR. BYRON WILLIAMS: So the expected MCT level as a -- as of March -- the end of March 2021 was an important factor in the determination of the Corporation's ultimate capital release proposal. Agreed?*

  MR. LUKE JOHNSTON: Yeah. And we're just updating our -- our forecasts as best estimates and letting the Capital Management Plan kind of run its course and produce the indicated -- indicated bill to release.[36]

[36] Transcript from October 19, 2020 at 326-328 WILLIAMS/Johnston. See also Transcript from October 20, 2020 at 374-76 WILLIAMS/Johnston.

Provisional Runs Both Ways

- *DR. BYRON WILLIAMS: And of course, depending on the year, Mr. Johnston, that provisionality could go the other way in the event that only a 2 percent capital release was contemplated and the results were improved. Looking forward to the year end of the current year that you're in, that – that provisionality could be amended with a larger capital release. Correct?*

  MR. LUKE JOHNSTON: Yes. Agreed. And I think what we've learned, even through the interest rate adjustments and such that we've made, that we can reduce the likelihood of either inadequate or excessive rates by updating these forecasts at least for interest rates. And this is kind of new, the Capital Management Plan, but if we're presented with a totally different situation, it would probably make sense to react to that.) [37]

[37] Transcript from October 19, 2020 at 326-328 WILLIAMS/Johnston.

Do these recent developments sound like the Capital Management Plan Approved by the PUB?

- Excess capital in extension at year end 19/20 was not transferred to basic (COVID19 emergency response)
- The first return of excess capital to captive ratepayers took the form of a $110 M rate rebate (COVID19 emergency response) – **not subject to the capping rule**
- The MPI Board now "walks back" its capital management plan commitment by asserting its right to pre-collect excess retained earnings from "captive" extension ratepayers in order to fund capital projects (a prerogative its legal counsel spent much of closing argument defending)

Walking back the "non-discretionary" commitment

- The CMP does not stipulate what accumulated profits generated by the Extension line of business may be used for but rather stipulates that at the end of each fiscal year, capital that remains in excess of 200% MCT is to be transferred to Basic.
- It is conceivable that Extension profits could be utilized for purposes other than transfers to Basic.
- A past example of this was the funding of the Enhanced Drivers Licenses initiative. [38]

[38] PUB (MPI) 1-28 b

No Policy Protecting the Transfer

- DR. BYRON WILLIAMS: And to your knowledge, in seeking Public Utilities Board approval of the Capital Management Plan, did MPI bring to the attention of the Public Utilities Board or others that it was conceivable that Extension profits could be used for purposes other than transfers to Basic?

  MR. MARK GIESBRECHT: I don't recall a discussion specifically. You know, the -- what was brought forward was that any excess profits above 200 percent would be transferred, but I don't believe we got into that exact discussion.

  DR. BYRON WILLIAMS: And, Mr. Giesbrecht, in terms of corporate policy for MPI, would it be accurate to say that MPI does not have a corporate policy which prevents it from using excess capital in Extension for purposes other than transfers to Basic? (BRIEF PAUSE)

  MR. MARK GIESBRECHT: No, I'm not aware of any policy to that effect.[39]

[39] Transcript from October 21, 2020 at 632-635 WILLIAMS/Giesbrecht.

The walk back of the "non-discretionary" extension transfer commitment is a critical factor in the growing concern of CAC Manitoba that excess capital will either be stranded or dissipated in extension

The Battered and Bruised Capital Management Plan - Rate stability when it comes to rebates and releases has (quite properly) become a myth

- *Put another way, MPIC will be seeking $95 million (ninety-five million dollars) less from Manitobans in 2021/'22. And that number is arrived at by simply taking the net premiums written and multiplying it by 8.8 percent. And that -- that's from figure 1 in revenues.*

  If you couple that, Madam Chairperson, with the rebate application, that amounts to over $200 million in favour of the ratepayer. And if approved, this year's rate decrease would represent the largest in thirty (30) years, as Mr. Graham indicated back when the 10.5 indication was first filed. And that would surpass the negative 8 percent that was ordered by this Board in the 2012 GRA. [40]

- Make no mistake – this is a good thing provided it is prudent

- But dramatic rebates and record setting releases do not make for rate stability

[39] Transcript from October 19, 2020 at 85, Scarfone.

The decision to kick rate stability to the curb in seeking rebates and releases is not a failure

- *DR. BYRON WILLIAMS: And recognizing that the premise of the capital release provision under the Capital Management Plan is to manage rate volatility. . . -- would MPI regard this reality as a failure on its part to manage volatility, contrary to the intentions of the Capital Management Plan, or would it consider its actions to be an appropriate response to both the pandemic crisis and to the objective of sharing the benefits of program changes and excess capital with captive ratepayers in an orderly manner?*

  MR. LUKE JOHNSTON: Well, I -- I hope there's no debate on the emergency situation and the position MPI found itself in. . . . We're managing to the situation like -- like everyone else. . . . Those types of models are -- are, I guess, under stress right now -- or whatever you want to call it -- because the situation is so unusual. MPI has shown candour in acknowledging these challenges and is attempting through increased and better trained staff, standardized case management and metrics to address them. [40]

- But it underscores the frailty and inflexibility of the existing CMP if rigidly applied

[40]Transcript from October 21, 2020 at 638-42 WILLIAMS/Johnston.

CAC Manitoba agrees that MPI acted appropriately in the initial wave of the pandemic

- MPI Board Members support this approach as it expedites customers receiving excess capital in a time of need [41]
- CAC Manitoba agrees that the actions of MPI in issuing the emergency rebate and seeking (at least) a further 8.8% rate change for 2020-21 were quite reasonable in light of the pandemic emergency, actuarial evidence and excess capital

[41] PUB1-1, 20-050 Minute

Which makes the failure of MPI to respond to the evidence of ongoing impacts of the COVID19 pandemic in the 3rd Quarter so mystifying

- A commitment to the 5% cap leaves excess capital in the hands of MPI basic at a time of acute consumer need

An Inflexibly Applied Cap to Promote the Myth of Rate Stability

- MPI prefers an inflexibly applied cap to promote a mythical rate stability to proposals better tailored to return excess capital on a timely basis to hard pressed Manitoba ratepayers
- People are unemployed
- Entrepreneurs are closing their doors or laying off staff
- In light of the material "bounce" that MPI is receiving via the pandemic – is it appropriate to ignore the "best evidence" of an ongoing COVID19 impact and to inflexibly apply the 5% cap?

CAC Manitoba has considered 4 options to return excess capital to consumers on a more timely basis at a time of acute need

4 options considered with Q4COVID19 as best estimate (also would apply to Q3COVID19 best estimate):

1. Accept MPI release proposal with 5% cap (status quo) –too long to return excess capital to Manitobans at time of need
2. Follow CMP process but release cap constraint in order to return excess capital over 3 years (relaxed cap constraint) – respects spirit and intent of CMP – slightly better than 5% cap at responding to need to return excess capital on a timely basis – less costly than rebate – but does not meet the objective of returning excess capital at time of need as well as rebate
3. Order second COVID19 rate rebate by cheque (rebate by cheque) leaving it open for MPI to propose creative ways to return rebate other than cheque – more timely than rate release – best option to return excess capital on a timely basis – mailing costs are a drawback[42]
4. Order second COVID19 rate rebate to be credited to consumers at time of renewal (rebate at renewal) – may be questions of technical feasibility – second best way to return excess capital on timely basis (within the renewal year rather than over three years) – saves on mailing if technologically feasible

[42] MPI should be encouraged to test the market for the least cost alternative (see if financial services marketplace can be more efficient than the mail room). MPI should consider demand-pull approach i.e. credit on account, and let consumers elect to pay out the negative balance, or leave it on account until renewal.

Recommended Order with regard to the treatment of excess reserves

- CAC Manitoba rejects options 1 (status quo) and 2 (relaxed cap constraint)
- While it feels option 4 is reasonable if technically feasible, it strongly prefers option 3 (second COVID19 rebate)
- CAC Manitoba recommends a 2nd COVID 19 rebate by cheque of $70 M approximated by taking the difference between Q4COVID19 best estimate of $147 M net income projected at the time of the GRA filing of ($78.6 million)
- While such an estimate is still projected to leave excess capital over the 100% MCT target at 20-21 year end, it best meets the objective of sharing the COVID19 “bounce” in net income with hard pressed Manitoba consumers.

Analytic Considerations in Making the second COVID rebate recommendation

CAC MB acknowledges that:

- Collision frequency variance is not at -50% as it was in March but points out that it appears to be at -20% in recent weeks (Exhibit 52) and Winnipeg is in Code Red
- Excess capital estimate is prospective (not in the bank yet) but notes that its approach is consistent with the “best estimate” of the current year approach contemplated under the CMP and that the provisional approach should apply in good and bad years

Analytic Considerations in Making the second COVID rebate recommendation

In addition, CAC Manitoba observes that:

- MPI continues to enjoy lower than expected claims incurred at a time of tough personal circumstances for many Manitobans
- The CMP inflexibly applied is ill suited to these times as Mr. Johnston noted
- The 100% MCT is already a highly conservative capital target

Analytic Considerations in Making the second COVID rebate recommendation

A 3 year release plan is untenable when MPI is vigorously defending its prerogative to “walk back” its “non-discretionary” CMP commitment of extension transfers to Basic. [43]

[43] PUB (MPI) 1-28 b)

Issue: How do we address issues of fairness regarding our ratemaking system flowing from recent analysis of the relativities between driver safety rating, territories, uses and rate group?

Issue: How do we address the primary v registered driver issue recognizing the respective roles of the PUB, MPI and Government?

The Importance of reasonably reflecting risks and costs in rates

In setting just and reasonable rates, while we always must be mindful of other policy considerations including accessibility for higher risk drivers:

- we want a rating system and rates that reflect the risk that vehicle owners and drivers bring to the system because it is generally regarded as fair;[44]
- people are prepared to pay for the risk they bring to the system but tend to be unhappy if they are also asked to cover part of someone else's costs or risks (their fair share);[45] and,
- rates that reflect the risk that one brings to the system sends an important message about the value of risk-reducing behaviour.[46]

[44] Transcript from October 27, 2020 at 1529-1530, WILLIAMS / Johnston
[45] *Ibid.*
[46] *Ibid.*

Focus on Issues Relating to DSR, Territories and Use

CAC Manitoba will focus on four critical issues of fairness from the perspective of the private passenger class:

- findings arising from Driver Safety Pricing Review Minimum Bias review regarding DSR levels;
- issues relating to registered v primary drivers;
- findings arising from Driver Safety Pricing Review Minimum Bias review relating to other relativities including territory and use; and,
- the need to address the outcomes of the pricing review on a timely basis in a manner that reflects the entirety of its insights while insuring that the PUB, MPI and Government can have an orderly dialogue on the issue of registered v primary drivers.

Later it will address matters related to:

- investment issues including their implications for motorcyclists; and,
- the allegations of unduly preferential pricing of private passenger vehicles for hire.

Key excerpts from the record flowing from the DSR Pricing Review – DSR

- Discounts and surcharges do not reflect the relative risk of drivers with different DSR levels; [47]
- Relative to the risk their registered vehicles bring to the system, DSR level 15 registered owners are paying 20% too much; [48]
- There appears to be a material cross subsidy of other vehicle owners by DSR levels 11 -15 registered owners, [49]
- Addressing the cross subsidy in 1 year would require significant increases. [50]

[47] Exhibit 25, 11/14.
[48] Exhibit 25, Figure 5, 12/14
[49] Exhibit 25, Figure 5,12/14
[50] Exhibit 25, Figure 5, 12/14

Key excerpts from the record regarding DSR and Primary Driver v Registered Driver

- The provision of discounts to the registered owner of vehicles is a long standing approach of MPI dating to the bonus malus system (ie 1980s);
- The registered owner model encourages policyholders to register all household vehicles in the same name of the household driver with the best DSR rating; [51]
- MPI is concerned that the primary driver approach may be difficult to difficult to enforce for MPI in the same way as all purpose versus pleasure;[52]
- But assuming that most people are honest in responding to the primary driver question (which CAC Manitoba does), if the primary driver is truly the primary driver, then the shortcomings with respect to the registered owner model should be reduced under a primary driver model; [53]
- The primary driver model would have to be considered more fair in that somewhat better information, which would allow MPI to more accurately price the product and do a better job of relating premium level to risk level; [54]
- The ultimate decision maker on whether to amend the registered model is government which has shown reluctance in the past.

[51] Transcript from October 27, 2020 at 1489, MCCANDLESS / Johnston
[52] Transcript from October 27, 2020 at 1511-13, MCCANDLESS / Johnston
[53] *Ibid.*
[54] Transcript from October 27, 2020 at 1517-18, MCCANDLESS / Johnston

Key excerpts from the record flowing from the DSR Pricing Review – Territories, Uses, Groups

- Territory 1 and 2 are much more similar than implied by the current relativities underlying the rate application with the reasonable inference that territories involving more highway driving may have been undercharged for PIPP; [55]

Uses

- When consideration of DSR is included in the minimum bias procedure, the relative rates between different uses such as All Purpose and Pleasure become less volatile or more similar;[56]

Ultimate Conclusion

- Findings from DSR Pricing Review cannot be reviewed or understood in isolation from revised relativities especially as they relate to territories and uses
- In Mr. Johnston's view, "*the sensible thing to do would be to* ***adjust the relativities for all of these variables with the same timing to ensure the correlations between them are accounted*** *-- counted for*" [57]
- This can be done for the next GRA [58]

[55] Transcript from November 3, 2020 at 2197-98, WILLIAMS / Johnston
[56] Transcript from November 3, 2020 at 2199, WILLIAMS / Johnston
[57] Transcript from November 3, 2020 at 2200, WILLIAMS / Johnston
[58] Transcript from November 3, 2020 at 2201, WILLIAMS / Johnston

Significant Overpayment for the best drivers who are registered owners

- *DR. BYRON WILLIAMS: Relative to the risks they bring to the system, this would suggest that those vehicle owners at DSR level 15 are paying 20 (twenty) percent too much?. . . MR. LUKE JOHNSTON: -- on a purely actuarial basis, that -- those are the numbers. Yes. DR. BYRON WILLIAMS: And is it consistent with accepted actuarial practice to have certain vehicle owners paying 20 percent too much, sir?*

  MR. LUKE JOHNSTON: On an actuarial basis, that would not be appropriate. But every jurisdiction would have rules on -- on -- policy-based rules on, perhaps, the maximum discounts that are allowed or the maximum additional surcharge that are — are required. So, there would be different rules in each jurisdiction. But that wouldn't affect the actuarial calculation of indicated risk. So I -- I'm just saying that there may be other steps beyond what I do that could influence that outcome. [59]

[59] Transcript from October 27, 2020 at 1549-50, WILLIAMS / Johnston

The magnitude of the overpayment by DSR Level 15 Registered Owners is likely understated

- *MR. LUKE JOHNSTON: That's right. And-- and maybe just so I don't lose my opportunity to say this, the -- the discount at DSR plus 15 is really the minimum possible discount, and the reason is because, if you're a DSR plus 15 driver, the only type of driver you can add to your policy is somebody higher risk than you, so a zero, minus 5, a plus 10. Since this is the collective experience of everybody that drives in vehicles registered by that owner, the discount is not as big as it would have been if we just said only plus 15 people can drive it, no one else on the policy, et cetera. So the -- this, again, it's the -- it's really, if -- if this was done in isolation just for plus 15 drivers, the discount rate would be even – even larger.* [60]

[60] Transcript from October 27, 2020 at 1487-88, MCCANDLESS / Johnston

Beginning to address the cross subsidy in the current system will not undermine a recommendation to proceed to primary driver system

- *DR. BYRON WILLIAMS: And, Mr. Johnston, in the event a decision was made to make some changes to the system, including the DSR -- let's say the vehicle discounts within the current model, while moving towards, for example, a primary driver system, would any interim changes prejudice ultimate changes to a primary driver system?. . ..*

  MR. LUKE JOHNSTON: Sure. My comments before -- this isn't exactly what you asked, but there's a lot of similarities between primary driver and registered owner. I did state that by definition, really, primary driver has to -- would be an informational improvement over registered owner. Directionally, they should produce similar results. So if we were to move on the – this information directionally towards targets, I don't think that that -- doing so would prohibit us from implementing primary driver, for example, effectively. And it wouldn't create, you know, a massive rate shock if we were to move to primary driver, if that's – if that's the question. [61]

[61] Transcript from October 27, 2020 at 1553-1558, WILLIAMS / Johnston

Government approval is not required to begin to address the cross subsidy of the best drivers who are registered owners

- Reality is that while changes to the DSR level are in the hands of government, regulatory changes are not required to change the driver premiums and vehicle premiums discounts in the existing DSR model.[62]

Plus – there does not appear to be the risk of Project Nova delay

- MPI intends to use the current Registered Owner model in the near term and find ways to move the premiums closer to the actuarial target, independent of Project Nova. [63]

[62] PUB (MPI) 1-89 (2792) b)
[63] CAC 1-30, CAC 2-12

Addressing the overpayment by the best drivers who are registered owners will have consequences for others

- *MR. LUKE JOHNSTON: So, in this case, in order to provide that discount at the top of the scale, we would have to increase our level zero base rate by 23 percent.* [62]

[64] Transcript from October 27, 2020 at 1461-62, JOHNSTON.

The Move to Address the DSR level cross subsidy issue should be measured but not glacial

- *DR. BYRON WILLIAMS: Okay.*

  MR. LUKE JOHNSTON: -- if we were to move to this approach, is there are certain rules in the rating model that describe how we should move to target when we're different. So if you have lots of data, move faster; if less, move slower. . . Whether those rules appropriately handle this situation or not I think is an important discussion. So we know, as you've mentioned earlier, DSR 15 has lots of drivers, lots of credibility. That may say minus 15 percent on the day -- day 1 based on our remaking methodology. Is that appropriate in this situation? I would struggle to say that it is, but that is what our rate-making model would do. So my current position is that we should really think about, you know, if we are moving, how to do that in a appropriate way that allows the Corporation this information on a more gradual basis.

  DR. BYRON WILLIAMS: So you gave me a really good example of drastic. In terms of gradual, sir, are you thinking, for example, of the pace when Manitoba Public Insurance sought to implement clear -- or, in those days, VICC in the last 1990s and early 2000s?

  *MR. LUKE JOHNSTON: Yeah, noth -- nothing specific comes to mind. I -- I did state earlier that those discussion should really be had with our management and board in terms of creating a recommendation, right? So let's -- and this is purely hypothetical, not my recommendation, but **let's say that we set a target in the future that, you know, we would like to get to the targets within ten (10) years** and -- and we always moved one-tenth (1/10th) of the way. That's an example of a potential gradual approach that doesn't create major swings. That's not my recommendation, but just -- just as a -- as an example of how something might have been implemented in the past with major dislocation.* [65]

[65] Transcript from October 27, 2020 at 1553-1558, WILLIAMS / Johnston

A 20% overpayment is not a token thing

- Dislocation is inevitable – it should not be shocking (and moderate during COVID-19) – but just because the registered vehicle owners with the best records have endured significant overpayment without complaint does not mean that concerns about dislocation should lead change to proceed at a glacial pace

- PUB may wish to review approach to implementing the CLEAR group rating system undertaken during the 1990s as a potential precedent

PUB also may wish to consider accelerating the pace of change at times when a rate decrease is mandated

- *DR. BYRON WILLIAMS: And in the context of the current Application, MPI may be hamstrung in terms of an approach such as that given the commitment that -- that the change in deductible coverage might be revenue neutral, agreed?*

  MR. LUKE JOHNSTON: Yeah, there's –if, in a -- DR. BYRON WILLIAMS: Rate – rate impact neutral, excuse me. MR. LUKE JOHNSTON: Yeah, in a normal year without deductible changes or capital releases, we're talking about a small rate decrease, less than 1 percent, as high as negative 2 percent based on interest rates. That's, I believe, what you'd be talking about playing with. And if -- if that adjustment is made exclusively kind of on the DSR basis, giving more of that quicker to the people that deserve it the most and -- and collecting that from those that need to increase, you could consider doing that.[66]

[66] Transcript from October 27, 2020 at 1559, WILLIAMS / Johnston

Territory would be important to review even without results of DSR Pricing Study

- Location is a significant driver of a difference in risk most jurisdictions; [67]
- ICBC recently updated its territorial data to better reflect different regions in the province; [68]
- Longer term trend where the vehicle population in Winnipeg and as well as territory, the commuter, is increasing relative to the other rural populations;[69]

[67] Transcript from October 29, 2020 at 1951 WILLIAMS / Johnston
[68] Transcript from October 29, 2020 at 1956-1957 WILLIAMS / Johnston
[69] Transcript from October 29, 2020 at 1948-49 WILLIAMS / Johnston

MPI did not appear overly enthusiastic about reviewing territories at the start of the process

- *"MPI has not conducted a territory review since their introduction."* [70]
- MPI initially suggested in this hearing that the territorial review might have to come behind other priorities such as DSR because "Driver Safety Rating is --really affects almost everybody." [71]
- MPI agrees that modifying territories under the new system will be relatively simple because it's such a common thing. [72]

[70] CAC 1-17
[71] Transcript from October 29, 2020 at 1963-64 WILLIAMS / Johnston
[72] Transcript from October 29, 2020 at 2011-12 GABOR / Johnston

Learnings from review of relativities related to Territories (Exhibit 82)

- *MR. LUKE JOHNSTON: So today's DSR discounts would be reflected in there. The other piece that is new in the DSR analysis is the actual splitting out and creating separate analyses for PIPP and non-PIPP. . .but what you're seeing here, once all those adjustments are made, does appear that* ***territory 1 and two 2 are much more similar than implied by the current relativities. And what seems to be driving that is a much higher relativity in -- for PIPP****. . . . .* ***This analysis basically is saying that we've potentially undercharged for PIPP in territory 2, and if that's properly accounted for, they're much more similar in risk.***[73]

- *MR. LUKE JOHNSTON: Well, in the chart in front of us here, Figure 3, you can see that territory 3 and 4 are suggesting a lower relative rate. We're still seeing a -- a commuter – additional commuter charge, and that also seems to be driven by PIPP. So it's -- there seems to be a relationship with additional driving on the highway would be my -- my guess, the -- more likely to get into more serious claim versus city-only driving.* [74]

- ***What seems to be happening when DSR is included in the analysis is all of these relative rates are less volatile, so if you -- or more similar,*** *I guess. If you -- if you go to the far right, you'll see the variation between the lowest and the highest is considerably less. So what this tells me is the – the information gained from including DSR in the relativity analysis has changed what we would attribute to use or territory when calculating the other relativities.* [75]

[73] Transcript from November 3, 2020 at 2198 Johnston [emphasis added]
[74] Transcript from November 3, 2020 at 2198-2199 Johnston
[75] Transcript from November 3, 2020 at 2199 Johnston [emphasis added]

DSR Pricing Model Relativities can only be understood in conjunction with other relativity change

- The model results for the DSR relativities in isolation are impacted by the lift or impact of the other fitted relativities that came out of the model, territory use and group. [76]

[76] Transcript from October 27, 2020 at 1543, WILLIAMS / Johnston

It is not analytically defensible or sensible to adjust DSR based on the pricing review without adjusting other relativities flowing from the pricing study

- *Dr. Williams: From this analysis, sir, does MPI plan to* ***adjust the relativities for all of these variables with the same timing to ensure the correlations between them are accounted*** *-- counted for?*

  MR. LUKE JOHNSTON: ***Yes, that would be the sensible thing to do, yeah.***

  DR. BYRON WILLIAMS: And do you have a sense of the timeline for that plan, sir?

  MR. LUKE JOHNSTON: . . . But once that is -- is done, we – we ***could run this analysis as -- as shown here, and I – I have no concerns that we could do that for next year's GRA.*** [77]

[77] Transcript from November 3, 2020 at 2200-2201, WILLIAMS / Johnston

There may be a claims frequency bonus from moving to better pricing signals

- There may be a substantial opportunity to send a stronger safe driving system with changes to DSR given the relative stability[78] of DSR impacts on driving behaviour over recent years

[78] Transcript from October 26, 2020 at 1307 WILLIAMS / Johnston

Recommended Findings, Orders and Recommendations

- The findings of the DSR pricing review demonstrate a material cross subsidy. The best drivers with registered vehicles including those from DSR levels 11-15 are paying rates that appear to be unduly discriminatory;
- Using the transition to the CLEAR rating group as one example and considering the existing MPI ratemaking rules as well as the current hardship from the pandemic, MPI should present options at the next General Rate Application which consider addressing the existing subsidy in a time period of three and of five years indicating its plan to mitigate against excessive dislocation and allow for orderly planning by those who will pay more (if MPI considers the dislocation excessive, it could present other options);
- As recommended by Mr. Johnston on November 3, 2020, any such process should be coordinated with adjustment to the relativities for all of these variables with the same timing to ensure the correlations between them are accounted for; [79]
- MPI is asked to recommend for the government's consideration replacing the existing registered owner approach with a primary driver model or a blended model (identify primary and secondary)
- The PUB also may wish to remind parties that in the event of proposed rate decreases in the future related to rates set in accordance with Accepted Actuarial Practice, it reserves the right to differentiate any relief ordered to address longstanding issues of cross subsidization. [80]

[79] Transcript from November 3, 2020 at 2200, Johnston.
[80] Transcript from October 27, 2020 at 1559, WILLIAMS / Johnston.

Issue: what is the level of risk posed to Manitoba Public Insurance and its ratepayers by Project Nova?

Overview of Comments - A High Risk and Extremely Important Project

- Little doubt that 20 year old systems such as CARS and AOL are nearing cost effective end of life and that is essential that MPI cost effectively address these technology challenges in a way that mitigates risk
- Given the importance of the project and risk of the project, it may be overly ambitious to expect a positive NPV upon final evaluation. [81]

[81] Transcript from October 26, 2020 at 1366-1368 GABOR / Wennberg

This remains a high-risk project

- Projects of this scale such as these are inherently risky – relying to a significant degree on technological experts to "get" the business and the business to be flexible enough to incorporate the technology without undue customization – then have a robust culture [82] to manage the disruptive transition
- Internal Capacity Concerns - performance of MPI on major projects over the last decade on projects such as Physical Damage Re-engineering and BI3 has demonstrated major challenges both in delivering cost-effective projects [83] but also in delivering promised benefits without material adverse consequence [84]

[82] Transcript from October 22, 2020 at 909-10, WILLIAMS / Mitra / Remillard; Transcript from October 22, 2020 at 972-73 WILLIAMS / Mitra. PUB (MPI) 1-62.
[83] Impairments - PUB (MPI) 1-71. PDR negative NPV PUB (MPI) 1-51. 48 Fineos Customizatons, CAC (MPI) 1-56 b).
[84] Mitchell 8 percent severity spike, CAC 2-11 c). Also Transcript from October 26, 2020 at 1325-29 WILLIAMS / Wennberg. Capping of EAL, PUB (MPI) 1-50. Also Transcript from October 26, 2020 at 1318-1322 WILLIAMS / Wennberg. Permanent impairment backlog and unintended consequences of centralized reserving, PUB 2-8 a).

This remains a high risk project

- Scope of Project is unprecedented – no analogous programs involving both a complex P and C line of business and a complex DVA line of business has been identified [85]
- Evidence that MPI business plan underestimated:
  - a) the complexity of the project; [86]
  - b) the costs of the project; [87] &
  - c) and the governance challenges of the project. [88]

[85] Transcript from October 22, 2020 at 825, Mitra.
[86] Transcript from October 22, 2020 at 880-83, MCCANDLESS Mitra/ Remillard. Transcript from October 22, 2020 at 911-13, WILLIAMS / Remillard / Dessler.
[87] Adverse cost variances, PUB (MPI) 1-73. $12 M miss relating to COTS, CAC (MPI) 1-60
[88] Transcript from October 22, 2020 at 833-35, Mitra

This remains a high risk project

- Significant residual risk remains for over 50% of the benefits related to equivalent full time positions and broker commissions[89]
- Delays out of the gate are worrisome
- Risk that Project Nova will overshadow, delay or serve as an excuse for other necessary projects[90]

[85] Transcript from October 22, 2020 at 945-48, WILLIAMS / Remillard. CAC (MPI) 1-60. CAC 1-56 b).
[86] PUB (MPI) 1-79. CAC 1-17. CAC 1-32.

Other Observations

- Business plan and initial analysis appears more careful than for PDR but no independent evaluation of business case.[91]
- There may be value in having PWC undertake an independent evaluation of the business plan at some point in time.

[91] Transcript from October 22, 2020 at 915-18, WILLIAMS / Remillard

Recommended Findings Project Nova

- The PUB observe that Project Nova remains a high risk project
- The PUB request an update for the next GRA based upon the revised business case including updates on the status of projected savings related to EFTs and Brokers
- The PUB reserve the right to direct that MPI retain an independent party to conduct an independent evaluation of the business

Potential Sources of Funding on Capital Projects

- MPI currently funds capital projects through cash and then amortizes the capital expenditure in rates. This may have implications for the MCT ratio (and releases under the CMP); [92]
- MPI has speculated about using extension excess retained earnings to fund capital projects which would reduce future releases under the CMP; [93]
- At a time of record low interest rates, MPI has not considered the option of debt financing major capital projects.
- MPI has not evaluated the relative merits of these options from the perspective of its own financial well being or the interests of ratepayers [94]

[92] Transcript from October 22, 2020 at 1168-1170 WILLIAMS / Giesbrecht. See also CAC 2-20.
[93] PUB 1-28
[94] Transcript from October 22, 2020 at 1171-1172 WILLIAMS / Giesbrecht

Recommended Findings

- PUB advise MPI that using pre-collected excess retained earnings from extension is inconsistent with the understanding of the PUB when it approved the CMP on a 2 year trial basis
- MPI be asked to review the relative merits of cash and debt funding options from the perspective of its own financial well being and the interests of ratepayers and report back

Issue: Allegations of “unduly preferential” pricing for Private Passenger Vehicle For Hire

If it walks like a subsidy and the actuary calls it a subsidy

- Comment during MPI closing - suggestion made that high PP VFH loss ratio was not a subsidy because it came out of retained earnings

- The logic of this escapes CAC Manitoba which concurs with Mr. Johnston:

  - *MR. LUKE JOHNSTON: . . .* ***But I'm quite willing to say that with consecutive loss ratios in this neighbourhood, the -- the likelihood that there's some subsidization is high.*** *But we still have to appreciate the volatility of a -- a small vehicle group like this can have in such a short time frame.* [95]

[95] Transcript from October 28, 2020 at 1715-18 WATCHMAN / Johnston

Its a subsidy

- All other things being equal, if the rates more closely approximated risk then retained earnings and excess capital would be higher and potential "releases" would be higher under the capital management plan
- This walks, talks and costs other ratepayers like a subsidy
- Retained earnings are not some magic pot of money to absorb or mitigate the effects of cross subsidy (or questionable capital spending decisions for that matter). To the extent they exceed appropriate financial targets, they represent excess funds which should be repaid to captive ratepayers

Considerations in addressing the subsidy

- The question becomes how does one address the likely cross subsidy being alive to:
  a) Data limitations;
  b) The respective competitive interests of the market disruptors PP VFH and the established industry (the Taxi Coalition);
  c) The interest of other ratepayers;
  d) The interests of the living breathing humans who may be affected by these rates.

Neither the 10 year plan or the 1 Year Plan are recommended

- Given low credibility, the "*slow and steady*" approach of MPI "*would take something like ten (10) years to get to the indicated rate*"[96]
- The Taxi Coalition independent witnesses, mindful that "*major players are only now showing up. This is still our chance to fix a problem,*"[97] rejects the idea of a pricing signal of a 15% rate increase as not a strong enough "*to send the signal that we* ***know*** *is needed*"[98]
- Its experts proposes a 56% rate increase on this relatively new class based upon quite limited data
- Neither the 10 year or the 1 year plan are recommended

[96] Transcript from October 28, 2020 at 1726-31 WATCHMAN / Johnston
[97] Transcript from October 29, 2020 at 2142-44 WILLIAMS / Bowman

[98] Transcript from October 29, 2020 at 2138- WILLIAMS / Bowman

Recommended finding

- The PUB is in a difficult position being asked to address a rating issue affecting disruptive new entrants into the marketplace and indirectly their competitors
- A directional pricing signal sufficient to address the issue within a five year period may be appropriate recognizing that an additional year of data may give better insight

The Issue: Transparency, Coverage Changes and the Negative Option

A Comment on Terminology – This is not an 8.8 percent rate decrease

- The 0.8% rate change in accordance with AAP is appropriately described as a rate decrease
- A 3% percent price reduction relating to a diminished insurance product is not a rate decrease – it is the unilateral creation of a new product – which is sold for a lower price
- A five percent CMP release is simply a return of excess capital over-collected from basic and extension consumers over time reflecting a number of factors including:
  - very positive developments in collision frequency in 2019/20; [99]
  - the benefits of market dominance in extension;
  - the compounding, cumulative impact of roughly 8 percent in rate increases flowing from Board Orders in 2016, 2017 and 2018; [100]
  - the combined efforts of the regulator, MPI and intervenors to eliminate prior MPI speculation on interest rate duration mismatches; and
  - assertive efforts by MPI in terms of its relationships with the trades and service providers
- Ratepayers can always celebrate pricing relief but this is hardly a 8.8% rate decrease

[99] CAC (MPI) 1-29
[100] Order 162/16, 3.7%, Order 130/17, 2.6% increase, 159/18, 1.8%.

Negative Option Marketing

- Negative option marketing turns the sales transaction backwards
- Instead of the merchant having to "sell" you a product or service, it starts with the assumption that you've already bought it
- Its up to the consumer to contact the merchant and cancel the order if they don't want to complete the transaction
- Mr. Williams bought a lot of very bad cassette tapes that way in the 1980s

A Living Breathing Example

- Customers who currently have a five hundred dollar ($500) deductible Basic (which means they have not previously purchased extension insurance to buy down their deductible) will have the five hundred (500) deductible level Extension for the MPI Extension Product put on their renewal invoice(or maybe "sold to them") without their prior consent. [101]

  - *DR. BYRON WILLIAMS: And so, Mr. Johnston, we talked before about . . . the 14 percent of captive Basic customers who don't currently purchase MPI Extension, for those customers is it your understanding that they will be assigned to the five hundred (500) deductible level in Extension?*

    MR. LUKE JOHNSTON: Yes.

    DR. BYRON WILLIAMS: And so those customers will have 45 days to visit a broker or the MPI service centre if they want to change their assigned coverage. Agreed?

    MR. LUKE JOHNSTON: Correct. . .

    DR. BYRON WILLIAMS: . . . to the extent that those customers had Extension insurance with another service provider, would they also be assigned to the five hundred (500) deductible level for Extension?

    MR. LUKE JOHNSTON: They would. MPI wouldn't -- wouldn't know, necessarily, what they have with other providers.

    DR. BYRON WILLIAMS: . . .the vast majority who are at that $500 cap, they don't have a prior contractual relationship with MPI Extension with regard to deductibles. Agreed?

    MR. LUKE JOHNSTON: Most of them wouldn't, yes. Yeah. [102]

[101] Transcript from October 20, 2020 at 671-72 WILLIAMS / Johnston.
[102] Transcript from October 20, 2020 at 672-73 WILLIAMS / Johnston.

This is Negative Option Marketing

- This is concerning treatment of captive MPI customers including those who have relationships with other competitive service providers
- This can only harm the competitive marketplace and place burdens on customers who either did not wish to lower their deductible or chose to lower their deductible with another insurer

Recommendations

- Let's call what MPI is doing by its true name – negative option marketing
- That in directly communicating with consumers of the responsibility to "opt out" of MPI coverage, that MPI consider advising consumers that there are competitive options with regard to the extension product
- In the event that MPI customers who are assigned by MPI to an extension product as a result of the unilateral product change and transfer to the extension line of business wish to amend their coverage within a one year period (whether within the 45 day opt out period) that MPI choose to waive any processing fees
- That MPI share its consumer information package and advertising materials with stakeholders including CAC MB and CMMG for comment

Issue: Fairness and Risk Issues Associated with MPI Investment Portfolios

MPI Investment Portfolio – Fairness and Risk Issues - Background

- PUB cannot tell MPI how to invest but questions of the prudence and reasonableness of MPI's management of its investment portfolio are relevant to the determination of the revenue requirement
- To the extent that MPI has not reasonably managed its investment portfolio, incurred undue risk or unreasonably prejudiced certain ratepayers, the PUB can reflect that in its ultimate rate approval determinations

MPI Investment Portfolio – Fairness and Risk Issues - Background

- MPI is committed to a basic insurance portfolio exclusively comprised of nominal bonds at a time of record low interest rates,[103] significant volatility in the equity markets during COVID19 and at a time when the Bank of Canada is reviewing its focus on a low inflation target – the record low interest rates are part of a long-term pattern of decline; [104]
- Reflecting the absence of competitive options for those seeking return, the equity markets are challenging at present, given valuations and growth concerns (e.g., P/E ratios)

[103] Transcript from October 28, 2020 at 1683-85 SCARFONE / JOHNSTON (see - it keeps falling, falling)
[104] CAC MB – exhibit 6

MPI Investment Portfolio – Fairness and Risk Issues - Background

- Unlike the private passenger class, motorcyclists will experience a significant rate increase due in large part to the relative large representation of PIPP claims and the extremely modest new money rate that underlies the setting of AAP rates
- MPI undertook a significant portfolio review,[105] addressing some, but not all, of CAC Manitoba's concerns (e.g., adopted segregated portfolios for long tail files such as pensions, changed the basis of optimizing the portfolio and relaxed minimum Canadian equity constraint)
- MPI has only recently fully implemented the portfolios flowing from its portfolio review

[105] Mercer ALM Study in 2018, filed in 2019 GRA

What MPI basic portfolio does well

- Largely escaped the short-term volatility associated with equities during the shortest bear market in global economic history.[106]
- Interest rate duration matching of liabilities and assets has significantly mitigated **nominal** interest rate risk

[106] Transcript from October 20, 2020 519-521, WILLIAMS/ Bunston.

Where MPI portfolio comes up short

- Opportunity cost (lower expected returns) of basic, given 100% fixed income (no equity risk premium)
- Sacrifices the interests of those whose risk is driven by long-term claims with resultant adverse consequences on rates at a time of low interest rates as real purchasing power of bonds diminishes (PIPP claims – noting that motorcyclists are particularly vulnerable)

Where MPI portfolio comes up short

- Lack of inflation protection given a focus on managing **<u>nominal</u>** interest rate risk, rather than the **<u>real</u>** interest rate risk and inflation risk that comprise it
  - No RRBs or other real assets (e.g., real estate, infrastructure) in Basic portfolio
  - Lower real assets in **<u>non-Basic</u>** portfolios, following most recent ALM Study
- Potentially on the wrong side of history at a time when the Bank of Canada is reviewing its current inflation targeting practice and considering other policy objectives (i.e., increased long-term inflation risk)
- Lower diversification contrary to portfolio theory and policies implemented by other funds
  - Canadian Equity less constrained after removing 10% minimum allocation (pre-Mercer ALM Study), but home bias remains with ~ 30% of public equities of **<u>non-Basic</u>** portfolio invested in Canada, or 10X higher than Canada's ~ 3% global market cap)
  - Canadian sector/stock concentration risk higher than other markets
- Lack of flexibility

Conclusions and Recommendations

- The lack of inflation protection in the basic portfolio given a focus on managing **nominal** interest rate risk, rather than the **real** interest rate risk and inflation risk is concerning at a time when the Bank of Canada is reviewing its current inflation targeting practice and considering other policy objectives (i.e., increased long-term inflation risk).
- MPI should monitor and report back on the Bank of Canada deliberations in terms of long-term inflation risk including the expectation that Governments carrying heavy debt loads may see inflation as a partial remedy.
- While CAC Manitoba has serious concerns with the short term fixation of the MPI investment decisions, it recognizes that MPI has only recently established its new segregated portfolios therefore a portfolio review or redesign is premature.[107]
- While CAC Manitoba has considerable sympathy with the concerns of CMMG, the equity markets are challenging at present, given valuations and growth concerns (e.g., P/E ratios).

[107] Transcript from October 20, 2020 517, WILLIAMS/ Bunston .

Investment Income Forecasting

- For the purpose of setting AAP rates for the test year, MPI reviews the new money rate for bonds (Provincial and Corporate) at a certain point in time (naïve forecast)
- MPI's expectations of its investment returns for the purposes of forecasting net income for the current year (and consequently for the expected level of retained earnings) is based upon investment return forecast methodologies, many of which, have not changed for many years, and have not been tested for predictive power. [108]
- High level evaluations of MPI demonstrates that a number of asset classes have proven to have forecasts that understate actuals or are highly variable, based on a simple back test (against historical actuals).[109]
- This calls into question the reasonableness of the investment forecast, and demands that MPI conduct a more thorough effort to test the forecast.
- MPI has agreed to do so for the next GRA.

[108] CAC (MPI) 1-50. Transcript from October 20, 2020 536-540, WILLIAMS/ Bunston
[109] *Ibid.*

Recommendation

- CAC Manitoba appreciates the MPI responsiveness on this issue and recommends the PUB direct that MPI undertake a review of the predictive power of its investment income forecasts and to propose amendments to that forecast for the next GRA.

Claims frequency

- The major driver of revised claims incurred forecast for 21/22 is $26 M reduction in frequency which is part of a longer term trend. [110]
- A major driver of collision frequency in recent years appears to be the adoption of collision avoidance technology in the market place which has been demonstrated to play a role in reducing accident frequency and severity. [111]
- It is estimated that over 60 percent of the Manitoba market **has not** adopted this technology. [112]
- While MPI has reflected the past five year average of collision frequency into its estimate of claims incurred it has not assessed the implications of increased adoption of this technology on claims incurred frequency and severity

110 CAC (MPI) 1-26. Transcript from October 26, 2020 at 1302-1304 WILLIAMS / Johnston

111 CAC 2-9 b) and CAC 2 10 b). Transcript from October 26, 2020 at 1302-1304 WILLIAMS / Johnston
112 CAC 2-9 b) and CAC 2 10 b)

Observation (but not a recommendation)

- As noted by Mr. Wennberg and Mr. Johnston, the pace of adoption of driver safety technology in vehicles has potentially important implications for claims frequency and may represent an opportunity for claims saving in the future that is not yet (quite appropriately) represented in claims incurred forecasts.

PIPP

While MPI should be commended for actions relating to its strategic review of PIPP in 2017,[113] it is apparent there are ongoing challenges with the reserving and management practices of PIPP including:

a) Whether the increase of case reserves for WI should be met with a commensurate reduction in IBNR or whether that judgement is premature given the lack of evidence to date in terms of favourable development;[114]

b) Ongoing challenges with the volatility of AB O indexed notwithstanding the favourable developments that are being gradually being recognized;[115]

c) Delays in paying AB other non-index personal impairment benefits Brief discussion of principles of statutory interpretation;[116]

d) Over-reserving in that centralized reserving was treating delays as adverse developments rather than delays in payment.[117]

113 CAC 1-6, CAC 2-6
114 PUB (MPI) 1-12, Transcript from October 26, 2020 at 1335-36 WILLIAMS / Johnston
115 PUB (MPI) 1-12, 1-13
116 CAC 1-22 and CAC 2-6
117 Transcript from October 26, 2020 at 1342-47 WILLIAMS /Wennberg, Transcript from October 26, 2020 at 1342-47 WILLIAMS / Johnston; PUB 2-8 a) d), CAC 1-22 and CAC 2-6.

Findings and Recommendations

- Potential future IBNR releases from Accident Benefit WI and Accident Other Indexed may be a source of future positive development to set off against adverse indications potentially flowing from change in methodology related to severity trend recommended by PUB and accepted by MPI
- MPI should be directed to report back on the outcomes flowing from its strategic review of PIPP in 2017 in terms of successes, challenges and uncertainties and whether it is delivering on the improvements in claims management and reserving expected

Thank you to the PUB and its staff

- CAC Manitoba has had the opportunity to appear before the PUB in independent, evidence based regulatory processes for over 30 years on issues relating to Manitoba Hydro, Pay Day Lending, Centra Manitoba and Manitoba Public Insurance
- Since the passage of what was then the Crown Corporations Public Review and Accountability Act in the late 1980s, the PUB, its staff and its independent advisors have delivered outstanding service to Manitoba in the public interest
- Our clients truly appreciate the rigour, independence, courage and compassion brought to their task by all individuals associated with the PUB