

**Order No. 130/19**

**MOTION BY CONSUMERS' ASSOCIATION OF CANADA (MANITOBA) INC.  
FOR AN ORDER COMPELLING CERTAIN RESPONSES TO INFORMATION  
REQUESTS IN THE 2020/2021 GENERAL RATE APPLICATION**

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**September 4, 2019**

**BEFORE: Irene A. Hamilton, Q.C, Panel Chair  
Robert Gabor, Q.C., Chair  
Robert Vandewater, Member  
Carol Hainsworth, Member**

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## 1. SUMMARY

By this Order, The Public Utilities Board (Board) grants, in part, the motion of Consumers' Association of Canada (Manitoba) Inc. (CAC) to compel Manitoba Public Insurance (MPI or the Corporation) to provide responses to certain Information Requests (IRs) made by CAC in the 2020/2021 General Rate Application (Application or GRA).

### 1.0 Overview

MPI filed the Application on June 20, 2019. On July 5, 2019, the Board issued Procedural Order 92/19 granting CAC intervener status in the 2020 GRA and establishing a timetable, which included two rounds of IRs.

Order 92/19 also established a Final Issues List for the 2020 GRA which included Claims Forecasting, including PIPP (the Personal Injury Protection Plan) as an issue to be considered in the normal course of the GRA. The following issues were also included as requiring more detailed consideration:

18. *Proposed Capital Management Plan, the proposed Basic capital build or release provisions, and the proposed mechanisms for capital transfers from other lines of business, including but not limited to the results of the Capital Management Plan Technical Conference directed in Order 159/18;*

*In the event that notice is provided to the Attorneys General of Manitoba and Canada pursuant to The Constitutional Questions Act:*

a. *Is the Reserves Regulation invalid;*

*If the Reserves Regulation is not determined to be invalid:*

b. *Must the Board ensure that approved rates for service comply with it;*

*If compliance is not required:*

c. *does it remain a relevant factor to be considered when setting rates for service;*

*If compliance is required:*

d. *does the Proposed Capital Management Plan comply with the Reserves Regulation;*

*If the Reserves Regulation is determined to be invalid:*

e. *target capital analysis and the target Basic total equity threshold levels.*

19. *Asset Liability Management Study, including the implementation thereof, comparison to the shadow portfolios directed by the Board in Order 159/18, the disposition of the existing portfolio to fund new investment classes, interest rate risk exposure changes, investment income reporting changes including the allocation methodology for balance sheet, investment income and Investment Policy Statement changes.*

## 1.1 *Reserves Regulation*

The Reserves Regulation (the Regulation) was registered on April 12, 2019. It sets out the manner in which the amount to be maintained by MPI in certain reserves is determined. It also restricts the use of any surplus reserve funds. The Regulation states that, for the purposes of section 18 of *The Manitoba Public Insurance Corporation Act*, for the Basic Rate Stabilization Reserve (RSR) MPI must maintain a minimum of the amount determined by using a Minimum Capital Test (MCT) ratio of 100%. For the Extension RSR, the minimum is set at a ratio of 200% MCT.

Prior to this GRA, the amount of Basic total equity to be held by MPI was not prescribed by regulation and was set by the Board as a range (with a lower and upper threshold) rather than a single target. Historically, an adaptation of the Dynamic Capital Adequacy Test (DCAT) has been used for the target capital analysis. Most recently, in Order 159/18, the Board ordered that the lower threshold for Basic total equity be \$140 million and the upper threshold be \$315 million, based on the target capital analysis prepared by MPI.

## 1.2 *Asset Liability Management Study*

The Board has reviewed the issue of MPI's Asset Liability Management over a number of previous GRAs. Most recently, in the 2019 GRA, the Board received the Asset Liability Study (ALM Study) prepared for MPI by Mercer Canada (Mercer), and received evidence in the public hearings from a representative of Mercer, who spoke to the ALM Study. In the 2019 GRA, MPI reported that the implementation of the recommendations from the Mercer ALM Study would result in the separation of the Corporation's commingled investment portfolio into five unique portfolios: Basic, RSR, Pension, Extension and Special Risk Extension. The transition into five unique portfolios was planned to commence at the end of the 2018/19 fiscal year, with the transition expected to be completed by 2019/20.

In Order 159/18, the Board acknowledged that its oversight role does not extend to directing the Corporation as to the particulars of its portfolio management. The Board also found that it appeared the Corporation had selected from a range of reasonable options for its portfolios; however, to test the reasonableness of the portfolio, the Board directed that MPI set up and run certain shadow portfolios and report on the returns of the shadow portfolios in this GRA. In particular, Order 159/18 required MPI to do as follows:

*11.17 The Corporation shall run shadow portfolios for the Basic and Pension portfolios, effective March 1, 2019, with the inclusion of Real Return Bonds as part of an optimal bond portfolio mix. The Corporation shall consult with the Board on the selection and management of the assets chosen for the shadow portfolios.*

*11.18 In the 2020 GRA, the Corporation shall file a report comparing the returns of the shadow portfolios as set out in Directive 11.17, with those implemented by the Corporation.*

*11.19 The Corporation shall immediately engage Mercer to run shadow portfolios for Basic and Pension effective March 1, 2019, without the constraints imposed by the Corporation, and file Mercer's report in that regard in the 2020 GRA.*

In response to Directives 11.17 - 11.19, in the Application, MPI filed a report from Mercer and information on the returns of both of the shadow portfolios required by Directive 11.17 and 11.19.

### **1.3 Information Requests Refused**

On July 15, 2019, CAC filed and served its First Round IRs. On August 12, 2019, MPI filed and served responses to the First Round IRs in which it refused to respond to a

number of CAC IRs (attached as Appendix A to this Order). In summary, the refused IRs fall into three categories:

1. The target capital levels for Basic and Extension in the Reserves Regulation (CAC (MPI) 1-8, 1-14 and 1-15);
2. The design and returns of the Shadow Portfolios (CAC (MPI) 1-23 and 1-24(e)); and
3. The review of PIPP entitlements and coverage (CAC (MPI) 1-29).

MPI's principal reasons for the refusal were that:

1. With respect to CAC (MPI) 1-8, 1-14 and 1-29, the information sought relates to the creation of a regulation, which is subject to Cabinet privilege and cannot be disclosed;
2. With respect to CAC (MPI) 1-15, it required MPI to complete a new DCAT analysis at a new risk tolerance, which is unreasonable and unnecessary; and
3. With respect to CAC (MPI) 1-23 and 1-24(e), MPI has already complied with Order 159/18, and the information required to answer the IRs does not exist and cannot reasonably be obtained.

CAC filed the within motion on August 15, 2019, seeking an Order compelling MPI to answer the refused IRs. On August 20, 2019, MPI filed its response to the motion and on August 21, 2019, CAC filed a reply to MPI's response.

The Board did not require an oral hearing on the motion.

## 2.0 PARTIES' POSITIONS AND BOARD FINDINGS

### 2.1 CAC

With respect to CAC (MPI) 1-8 and 1-14, CAC stated that it anticipates filing a Notice of Constitutional Question on the validity of the Reserves Regulation. CAC expects the information requested (specifically, MPI's internal briefing materials or information on the rationale for the MCT ratios for Basic and Extension) would assist it in determining the scope and content of the Notice. The information would also relate to the question of whether the Board must ensure that approved rates comply with the Regulation and whether the Regulation is a relevant factor for setting rates.

With respect to CAC 1-15(d) (which asked MPI to provide any DCAT analysis undertaken for the test year, assuming a 1-in-40 risk tolerance), CAC took the position that if the Board were to determine that the Reserves Regulation is not valid, is not a relevant factor for rate-setting, or if the Board determines that approved rates do not need to comply with the Regulation, then the DCAT analysis would be relevant for setting capital targets.

With respect to CAC (MPI) 1-23 and 1-24, CAC advised that the intent of the questions was to obtain information as to the key considerations taken into account in the development of the shadow portfolios as well as the approach to the shadow portfolios, and whether they are consistent with Order 159/18. In order for value to be gained from the shadow portfolios, CAC stated that they need to be made as transparent as possible, as soon as possible.

With respect to CAC (MPI) 1-29(a), CAC stated that the presumption by PIPP of full-time income loss determined at 180 days for non-earners and part-time earners without demonstrated intent of employment, full-time or otherwise is significant in terms of financial implications for claims incurred relating to PIPP claims, and that MPI should be compelled to provide all of its internal briefing materials on this area of review.



## **2.2 MPI**

MPI took the position that, with respect to CAC 1-8 and 1-14, MPI is required to comply with the Reserves Regulation and therefore any briefing materials regarding the merits of the Regulation are not relevant. MPI also took the position that, because CAC had not yet served its Notice of Constitutional Question as to the validity of the Regulation, it would be premature to review this issue. With respect to these IRs and CAC (MPI) 1-29(a), any internal MPI briefing materials would form part of a Cabinet submission and therefore would be subject to Cabinet privilege.

With respect to CAC (MPI) 1-15, MPI stated that information regarding the DCAT for target capital purposes would be irrelevant as the Reserves Regulation now sets target capital levels. Further, producing an alternative DCAT is resource-intensive and, as that the Regulation now determines capital targets, it would be unreasonable for MPI to be required to do the work involved.

Finally, with respect to CAC (MPI) 1-23 and 1-24(e), MPI stated that there are many possible shadow portfolios that might be prepared in comparison to MPI's actual portfolio, but shadow portfolios are retrospective and do not reflect the principles and risk tolerance adopted by MPI. The work required in order to respond to these IRs would be uneconomical and of limited value to the Board's rate-setting function.

## **2.3 CAC Reply**

CAC submitted that the refused IRs relate to matters that have short and long-term implications for Basic ratepayers. For those IRs that relate to the Reserves Regulation, CAC advised that it intends to comply with the statutory service requirements for the Notice of Constitutional Question, and it has already prepared a draft Notice. The information sought, according to CAC, is likely to assist the Board and the parties in understanding how the Reserves Regulation fits into the regulatory framework for Basic rates. Further, if the Board were to determine that the Regulation is not relevant for the

purposes of rate-setting, the alternative DCAT information might be necessary for the Board to make a decision on Basic target capital levels.

CAC stated that the IRs related to the shadow portfolios should be answered, because the methodology used to develop the shadow portfolios affects their utility in the assessment of MPI's investment portfolio. Further, if MPI's investment strategy is not reasonable, the cost to ratepayers over the long term will be much more significant than the cost of the additional work required to answer the IRs.

## **2.4 Board Findings**

Rule 14(1) of the Board's Rules of Practice and Procedure provides that IRs are to be directed to a party for the purpose of a satisfactory understanding of the matters to be considered. IRs must be relevant to the proceeding.

Rule 15(1) provides, among other things, that where an IR has been directed to a party and served on that party in accordance with the Board's directions, the party shall provide a full and adequate response to the IR.

Pursuant to Rule 16, a party who is unable or unwilling to provide a full and adequate response to an IR (referred to as an "interrogatory" in the Rule) shall file and serve a response:

- a) Where the party contends that the interrogatory is not relevant, setting out specific reasons in support of that contention;
- b) Where the party contends that the information necessary to provide an answer is not available or cannot be provided with reasonable effort, setting out the reasons for the unavailability of such information, as well as any alternative available

information in support of the response that the party considers would be of assistance to the party making the information requests;

- c) Where the party contends that the information sought is of a confidential nature, setting out the reasons why it is considered confidential and any harm that would be caused by making it public; or
- d) Otherwise explaining why such a response cannot be given.

The objective of every GRA is to obtain Board approval for rates that are just and reasonable. Just and reasonable rates are those which strike the appropriate balance between the interests of ratepayers to pay no more than necessary for the services they receive and ensuring that the applicant, in the case of a public service provider, is financially able to fulfill its statutory mandate. The onus is on MPI, as applicant, throughout to demonstrate that the rates requested are just and reasonable. Within this context, the IR process serves to assist the Board and interveners by developing the record and an understanding of the issues in the GRA.

The Board has considered the positions of CAC and MPI on this motion and will require MPI to provide responses to CAC (MPI) 1-15(d) and 1-29(a). The Board will not require MPI to answer any of CAC 1-8, 1-14, 1-23 or 1-24(e).

The Board's reasons for its decision are as follows.

#### **2.4.1 CAC (MPI) 1-15(d) and 1-29(a)**

First, with respect to CAC (MPI) 1-15(d), the Board points out that CAC has not requested of MPI that it perform any additional DCAT analysis. The specific wording of this IR was for MPI to provide any DCAT analysis undertaken for the test year assuming a 1-in-40

risk tolerance. If, in fact, MPI has undertaken this work, it should be in a position to provide the information. If it has not undertaken the work, the Board expects that MPI will so advise and, accordingly, there will not be any analysis to provide. The Board accepts that any such analysis, if it exists, would be relevant to the issues in this GRA. In particular, in Order 92/19 the Board accepted within Issue 18 the question of whether the Reserves Regulation is invalid. The Board has not, and will not, make any determination in that regard until a full hearing has taken place and the requisite notice has been given pursuant to *The Constitutional Questions Act*. Nevertheless, the Board accepts CAC's position that, should the Board find the Regulation to be invalid, the DCAT may be relevant for the Board to make a decision with respect to Basic target capital levels.

With respect to CAC (MPI) 1-29(a), the Board accepts that the information requested is relevant to Issue 10 in this GRA and, in particular, the financial implications for claims incurred related to PIPP claims. MPI refused to answer this IR by claiming Cabinet privilege, making the general statement that any internal MPI materials sent to Cabinet as part of MPI's Cabinet Submission are captured by the privilege. The Board finds this IR has not requested that MPI specifically disclose information provided to Cabinet. In response to this IR, MPI should be able to provide a financial analysis of the cost consequences of the presumption of full-time income loss as set out in the IR, and elaborate thereon as necessary.

Without making a specific finding on the validity of the claim for Cabinet privilege invoked by MPI, the Board makes the following general comments. While Cabinet privilege (also known as public interest immunity) may be invoked by someone other than the Minister responsible, it is not an absolute privilege. Further, procedurally, a claim for Cabinet privilege must be supported by affidavit material that specifically addresses the basis of the claim for privilege and the nature of the public interest to be protected. General statements, such as those provided by MPI, will not suffice.

### **2.4.2 CAC (MPI) 1-8, 1-14**

These IRs requested MPI's internal materials regarding the merits of or rationale for the 100% MCT RSR target for Basic and 200% MCT target for Extension. In refusing to provide a response, MPI claimed Cabinet privilege. MPI also took the position that the request was premature.

In dismissing CAC's motion on this IR, the Board makes no finding on the merits of the claim for privilege. Rather, the Board is not persuaded that the information sought is relevant. It is not clear that the materials requested would contain any factual information that would assist in an inquiry into the issue of the validity of the Reserves Regulation. The Board fails to see how MPI's internal analysis on the merits of certain target capital levels will assist the Board in making its own determination as to whether the Reserves Regulation is invalid. The Board would point out, however, that if it had found that the IR requested relevant information, the request is not premature. The Reserves Regulation is included in the Final Issues List approved by the Board in Order 92/19, and in that Order the Board specifically commented that it was being included so that the record could be fully developed prior to the public hearings for this GRA.

### **2.4.3 CAC (MPI) 1-23, 1-24(e)**

The Board commented in Order 159/18 that MPI may have foregone an opportunity to hedge against long-term risks by rejecting Real Return Bonds (RRBs) and reducing real assets in its new portfolio.

The Board directed MPI to undertake the shadow portfolio exercise in order to assess the reasonableness of MPI's portfolio and, in particular, to determine how the inclusion of RRBs or the removal of constraints might affect the portfolio. An examination of the composition and design of the shadow portfolios necessarily follows; however, that examination must be proportional to and reflective of the purpose of the exercise, which was to provide the Board with a general sense of the performance of portfolios without constraints imposed by MPI. The design of the shadow portfolios can be tested through cross-examination. Rather than requiring MPI to provide responses to CAC (MPI) 1-23 and 1-24, MPI should produce the representative from Mercer principally responsible for the report on the shadow portfolios as a witness in the public hearings. This will result in a more proportional and efficient examination of the issue.

Accordingly, the Board requires MPI to provide responses to CAC (MPI) 1-15(d) and CAC (MPI) 1-29(a). CAC's motion with respect to the balance of the IRs is dismissed.

### 3.0 IT IS THEREFORE ORDERED THAT:

- 3.1 The Motion filed by the Consumers' Association of Canada (Manitoba) Inc. (CAC) for an Order requiring MPI to file responses to Information Requests CAC (MPI) 1-15(d) and CAC (MPI) 1-29(a) is hereby granted.
- 3.2 The Motion filed by CAC for an Order requiring MPI to file responses to Information Requests CAC (MPI) 1-8, CAC (MPI) 1-14, CAC (MPI) 1-23, and CAC (MPI) 1-24(e) is hereby dismissed.
- 3.3 MPI shall file and serve responses to CAC (MPI) 1-15(d) and CAC (MPI) 1-29(a), on or before **September 9, 2019**.
- 3.4 CAC shall file and serve any Second Round Information Requests arising out of the responses to IRs CAC (MPI) 1-15(d) and CAC (MPI) 1-29(a) on or before **September 11, 2019**.
- 3.5 MPI shall file and serve responses to Second Round Information Requests arising out of the responses to IRs CAC (MPI) 1-15(d) and CAC (MPI) 1-29(a) on or before **September 18, 2019**.

Board decisions may be appealed in accordance with the provisions of Section 58 of *The Public Utilities Board Act*, or reviewed in accordance with Section 36 of the Board's Rules of Practice and Procedure. The Board's Rules may be viewed on the Board's website at [www.pubmanitoba.ca](http://www.pubmanitoba.ca).

THE PUBLIC UTILITIES BOARD

"Irene A. Hamilton, Q.C."  
Panel Chair

"Darren Christle, PhD, CCLP, P.Log., MCIT"  
Secretary

Certified a true copy of Order 130/19  
issued by the Public Utilities Board



Secretary



## APPENDIX A

### **CAC (MPI) 1-8**

Please provide all briefing materials within MPI regarding the merits of a 100% MCT target for MPI which address the merits of asking Basic ratepayers to contribute to a target imposed by regulation rather than an independently determined target.

### **CAC (MPI) 1-14**

Please provide any analysis, report or other information that provides a rationale (other than the Regulation) for maintaining the Extension reserve at a MCT ratio of 200%.

### **CAC (MPI) 1-15(d)**

Please provide any DCAT analysis undertaken for the test year assuming a 1-in-40 risk tolerance.

### **CAC (MPI) 1-23**

a) Efficient Frontier: Why was an Efficient Frontier for Basic not shown on page 1,693? Can the Efficient Frontier be provided?

b) Basic.5 Portfolio Construction: Please explain i) the rationale for constructing the Basic.5 portfolio, ii) the process for constructing its asset mix composition (e.g. an optimization), and iii) the basis for its construction (i.e. in nominal or real terms)?

c) Optimal RRB Allocation: Based on the Efficient Frontier above, what would the optimal asset allocation to RRBs be at the actual level of real surplus risk that MPI selected (i.e. ~4.3% real surplus volatility for Basic.3)?

d) Principles: What principles or other considerations guided the process for developing the composition of the various Shadow Portfolios? Were these principles applied consistently across the four Shadow Portfolios? If not, why not?

e) Risk Components: Why was credit risk, rather than surplus risk, a specific consideration in the selection of Basic Shadow Portfolio 1, noting that credit risk is only one component of surplus risk? (Other components of surplus risk may include inflation risk, real interest rate risk, currency risk, active risk or tracking error, and liquidity risk.

f) RRB Market Considerations: PUB Order No. 159/18 says “it would be beneficial for the Corporation to inform itself and the Board as to how the Basic and Pension portfolios would perform had the Corporation not imposed those constraints.”

- i. Why are the “RRB Market Considerations” in Mercer’s Appendix relevant in determining the composition of the Shadow Portfolios (as distinct from determining the returns of the Shadow Portfolios)? Isn’t this inconsistent with the objective underlying PUB Order No. 159/18?
- ii. Instead of constraining the RRB weight in Shadow Portfolios (e.g. to 24% in the case of Basic Shadow Portfolio 1), wouldn’t it be more appropriate to make an adjustment to the RRB Index returns to account for any market impact acquisition costs that MPI/Mercer believe would be incurred to establish the policy weights in the Shadow Portfolios?
- iii. Wouldn’t any cost adjustment or penalty, noted above, be relatively small (measured on an annualized basis), given the one-time nature of any RRB

acquisitions and the very long holding period over which any such cost could be “amortized” (i.e. decades)?

- iv. While Mercer’s Appendix regarding considerations mentions daily volumes (~ \$20M), was the size of periodic RRB auctions also considered, noting there have been two auctions of RRBs so far in 2019 (February and May) totaling \$1.1 billion?

g) Basic.3 and Policy Portfolios: Why are there differences between the Basic.3 portfolio “selected during the AL Study” (per page 1,692) and the Policy portfolio for Basic in the Investment Policy Statement (page 1,635)? e.g. Did the MPI Board approve an asset mix for Basic that has a longer duration than was reflected in the Mercer Study?

h) Basic.5 vs Fixed Income Mixes (for Shadow Portfolio 1):

- i. On page 1,692, what is the difference between Basic.5 and Fixed Income Mixes (for Shadow Portfolio 1) in terms of asset mix?
- ii. On page 1,666, do the asset mix weights represent those for Basic.5 or Fixed Income Mixes (for Shadow Portfolio 1)? (It appears that the weights for Basic.5 were used in calculating the returns.)

i) Basic.5 as Shadow Portfolio 1: On page 1,692, Mercer said “BASIC.5 is a variation of Basic.3, if the Real Liability Benchmark is selected and similar credit risk is taken”.

- i. Why was BASIC.5 chosen to represent Shadow Portfolio 1 when it has significantly less real surplus volatility than Basic.3 (i.e. 3.2% compared to 4.5%, on page 1,692, or a difference of 29%)?
- ii. Isn’t the approach for developing Shadow Portfolio 1 inconsistent with MPI’s surplus risk tolerance, given the 29% lower risk in real terms noted above,

and 69% higher risk in nominal terms on page 1,695 (i.e. 2.2% surplus risk for Basic.5 and 1.3% for Basic.3)?

- iii. If Mercer's return assumptions are realized, on average, won't Basic Shadow Portfolio 1 have the same average return as MPI's Policy portfolio (i.e. 3.1%) over a reasonably long period of time?
- iv. Shouldn't Basic Shadow Portfolio 1 be constrained to have the same surplus risk that MPI actually selected during the AL Study (i.e. 4.5% real surplus risk for Basic.3), rather than having the same expected return (i.e. 3.1% for Basic.3)? i.e. Wouldn't the performance of a Shadow Portfolio based on the same risk tolerance/level actually selected by MPI better measure the difference in returns underlying PUB Order No. 159/18?

j) "Middle (C)" as Shadow Portfolio 2: On page 1,697 Mercer said "Middle (C) modestly increases return and decreases risk".

- i. Why was a different approach used to develop Shadow Portfolio 2 ("Middle (C)"), compared to the approach used for Shadow Portfolio 1, where neither expected return nor risk were kept constant in Shadow Portfolio 2?
- ii. Wouldn't the selection of B (Same Return) for Shadow Portfolio 2 have been more consistent with the approach used for developing Shadow Portfolio 1?
- iii. Why was the "Current" portfolio used as an "anchor" for defining "Same Risk (D)" and "Same Return (B)"? Doesn't the Current portfolio represent the pre-Mercer asset allocation (3.8% real risk), rather than the portfolio selected by MPI as a result of the Mercer Study (4.5% real risk)? i.e. Shouldn't any "anchor" be related to "Basic.3 (E)", not "Current"?
- iv. Would Mercer/MPI agree that if the Shadow Portfolio 1 approach for Basic were used to develop the Shadow Portfolio 2 for Basic, the risk of Shadow

Portfolio 2 would be significantly different (i.e. < 1% real risk, rather than the 4.5% for the Basic.3 portfolio)?

- v. Would Mercer/MPI agree that if risk (rather than return) were kept constant in developing the Shadow Portfolios, the expected return premium (over Basic.3) would be > 110 bps for Basic Shadow Portfolio 1 and ~ 220 bps for Basic Shadow Portfolio 2?

k) Updated INV Attachment A: Please provide an updated INV Attachment A, reflecting any changes arising from the information requests and questions related to it.

**CAC (MPI) 1-24(e)**

Updated INV Appendix 10: Please provide an updated INV Appendix 10, reflecting any changes arising from the information requests and questions related to it.

**CAC (MPI) 1-29(a)**

Please elaborate and comment in detail on the PIPP entitlement and coverage review including the claims incurred impact of "the presumption by the plan of full-time income loss determined at 180 days for non-earners and part-time earners without demonstrated intent of employment, full-time or otherwise."