DECISION **2021 NSUARB 23**
M09949

NOVA SCOTIA UTILITY AND REVIEW BOARD

IN THE MATTER OF THE INSURANCE ACT

- and -

IN THE MATTER OF AN APPLICATION by **FACILITY ASSOCIATION** for approval to change its rates and risk-classification system for miscellaneous vehicles

BEFORE: David J. Almon, LL.B., Member

APPLICANT: **FACILITY ASSOCIATION**

FINAL SUBMISSIONS: January 15, 2021

DECISION DATE: **February 19, 2021**

DECISION: **Application is approved as modified.**

I INTRODUCTION

[1] Facility Association applied to the Nova Scotia Utility and Review Board to change its rates and risk-classification system for miscellaneous vehicles, specifically all-terrain vehicles and snow vehicles.

[2] Facility proposed changes to its rates for each type of vehicle. While having developed its own indications based upon its selected assumptions, Facility selected rate changes that matched an alternate set of indications using an 11% return on equity and using the prior credibility weighted loss ratio the Board approved for the complement of credibility, where needed. The Board required Facility to use these assumptions in past decisions.

[3] The Board must consider whether the proposed rates are just and reasonable and in compliance with the *Insurance Act* (*Act*) and its *Regulations*. The Board does not approve the proposed rates but rather requires Facility to submit revised proposals that produce, under staff assumptions, a return on equity that does not exceed 11%, within 15 business days of the release of the Board's Decision.

II ANALYSIS

[4] Facility applied under the Board's *Rate Filing Requirements for Automobile Insurance – Section 155G Prior Approval* (*Rate Filing Requirements*). Facility received and responded to Information Requests (IRs) from Board staff. Board staff prepared a report to the Board with recommendations on the application (Staff Report). Before providing the Staff Report to the Board, Board staff shared it with Facility. The company reviewed the Report and provided its comments.

[5] Board staff examined all aspects of the ratemaking procedure to make the recommendations in the Staff Report and suggested that the Board further review the profit provisions, including the return on investment, the selected loss trends, and the servicing carrier operating cost provision. Board staff consider that Facility satisfactorily addressed all other aspects of the ratemaking procedure in its application and IR responses.

[6] Board staff acknowledged Facility based its proposal on the use of an 11% return on equity (ROE) and the use of the Board based complement of credibility, or its alternate indications, as the Board ordered in other Facility applications.

Profit Provisions

[7] By using the alternate assumptions, Facility included a cost of capital or profit provision using an 11% after tax ROE and a 2:1 premium to surplus ratio (PSR) in its own indications.

[8] For its return on investment (ROI), Facility used a 0.10% based upon current market yields for risk-free government bonds. In past decisions, the Board did not allow Facility's use of a risk-free method to determine the ROI. The Board instead found Facility should use a 2.5% return on investment in previous applications (e.g., private passenger vehicles and taxi applications, and the most recent miscellaneous vehicle application).

[9] The application provided no new information to support the risk-free approach. Board staff recommends requiring Facility to use 2.5% in place of the 0.10%,

for these vehicles. Lacking any new information, the Board sees no reason to reconsider its previous decisions and approves the Board staff recommendation.

Loss Trends

[10] Because miscellaneous vehicles lack enough claims experience data to develop trends directly, Facility used private passenger vehicle loss trend selections as a proxy. Board staff advises that the use of private passenger vehicle loss trends as a proxy for miscellaneous vehicle trends is a common industry practice.

[11] Board staff provided a table comparing the loss trend estimates from Facility models to the selections made by the Board's consulting actuaries, Oliver, Wyman Ltd. (OW) in its report, based on data through December 31, 2019. Identified in the table are cells where the Facility estimates are more than 1.5% different than OW's selections and the difference would lead to higher indicated rates. Other cells in the table show similar differences, but in these cells, the OW selections would produce higher indicated rates.

[12] Facility provided indications using the OW loss trends along with all other assumptions used in the Facility alternate indications. Board staff provided a table showing the changes in the indications for coverages impacted by the change and overall coverage.

[13] Board staff noted the small differences, and the overall indications were higher when using the OW trends and recommended the Board allow Facility to use its selected loss models and the resulting loss cost trends estimates. Board staff advise that this recommendation would only apply in the circumstances of this application. Should Facility apply for private passenger vehicle rate changes, the Board would follow its

practice of having OW assess the reasonableness of the Facility models and provide recommendations on loss cost trends, at that time. The Board accepts the use of the Facility trend models for the purposes of this application only.

Expenses

[14] In previous private passenger vehicle and taxi applications, the Board required Facility to replace its use of the plan of operation based 9% Servicing Carrier Operating Fee (SCOF) assumption with an 8% value. This level reflected the rounded value of the actual cost for two of Facility's servicing carriers, as identified in an earlier hearing. The Board excluded the result for a third servicing carrier because Facility could not explain why the costs for that carrier were much higher than those for the other two. The Board stated it would reconsider this position in future applications if Facility provided evidence to support or explain the servicing carrier cost levels.

[15] Facility did not provide any new information on the actual costs of servicing carriers to administer the Facility business. Facility did explain, however, that one of its servicing carriers announced it was exiting that role. Additionally, a pending acquisition involving the other two servicing carriers, if approved, would result in Facility having a single servicing carrier for its business. Facility also notes that no other company is lining up to take on the servicing carrier role.

[16] Given the departure, which would result in the highest cost servicing carrier being removed, and the pending acquisition and the lack of companies seeking to take on the servicing carrier role, Board staff advise that the uncertainty surrounding the servicing carrier status gives pause to consider the prudence of forcing a reduction in the

SCOF as had been ordered in previous applications. That is, the impact of the servicing carrier changes on the actual cost of administering Facility business is unknown and assuming the cost remains the same may not be appropriate.

[17] Based on the new information and the small impact observed by the SCOF change in the previous application for these vehicles, Board staff recommends and the Board allows Facility to use 9% for the Servicing Carrier Operating Fee in the circumstances of this filing, for these vehicles only. Board staff further advise that conclusions for a concurrent taxi application may result in a different decision. The Board agrees.

Staff Indications

[18] Board staff recommends and the Board approves the use of the staff indications, calculated using Facility alternate assumptions, except for ROI, where 2.5% replaces the Facility selection of 0.1%, as the appropriate target against which to assess the appropriateness of the Facility proposal.

Comparison of Proposed Rates to Recommended Staff Indications

[19] Board staff provided tables comparing Facility's proposal to the staff indications.

[20] Because the staff indications are lower than Facility alternate indications upon which the proposed rate changes are based, the proposed rates would produce a return on equity in excess of the allowed 11%.

[21] Board staff advises that, in similar situations, the Board would order Facility to make changes so that under the staff indication assumptions, the changes would not produce an ROE that exceeds 11%. Facility generally submits rates that match the staff indications to comply with the order.

[22] Board staff recommended that the Board not approve the proposed rates; but rather, require Facility to submit within 15 business days of the date of its decision, new proposed rates that, under the staff assumptions, produce a proposed ROE of no more than 11%. Accordingly, the Board does not approve the proposed rates and requires Facility to submit revised proposals that produce, under the staff assumptions, an ROE that does not exceed 11%, within 15 business days of the release of the Board's decision.

Automobile Insurance Manual Review

[23] Facility proposed no changes to its underwriting or rating rules. Board staff reviewed the online manuals and found no areas where the company appears to be in violation of the *Act* or its *Regulations.*

III SUMMARY

[24] The Board finds that the application follows the *Act* and *Regulations*, as well as the *Rate Filing Requirements*.

[25] The Board approves the use of the staff indications, calculated with all the Facility alternate assumptions except for ROI, where 2.5% replaces the Facility selection of 0.10%, as the appropriate target against which to judge the reasonableness of the proposed rates.

[26] The Board does not approve the proposed rates but rather requires Facility to submit revised proposals that produce, under the staff assumptions, an ROE that does not exceed 11%, within 15 business days of the release of the Board's decision.

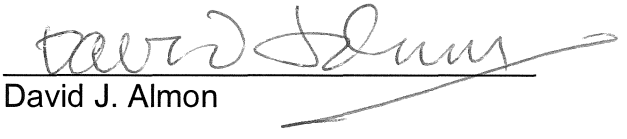
[27] The Board approves the proposed effective date of 100 days after the Board's issuance of the order in this matter, rounded to the first day of the following month, for new business and renewal business. This approach is consistent with past Facility applications.

[28] Facility is not an insurance company, but instead is supported by its member companies who underwrite automobile insurance in Nova Scotia. As a result, Facility is not required to provide financial information to the Board. However, recent examinations of the mandatory filings of the Facility member companies provides comfort that it is unlikely that the changes proposed by Facility, or the recommended changes, will jeopardize the solvency or financial well-being of the Facility member companies.

[29] The application qualifies to set a new mandatory filing date under the *Mandatory Filing of Automobile Insurance Rates Regulations*. The new mandatory filing date for Facility for miscellaneous vehicles is January 1, 2024.

[30] An order will issue accordingly.

DATED at Halifax, Nova Scotia, this 19th day of February, 2021.



David J. Almon