DECISION **2019 NSUARB 47**
M09097, M09098 & M09101

NOVA SCOTIA UTILITY AND REVIEW BOARD

IN THE MATTER OF THE INSURANCE ACT

- and -

IN THE MATTER OF APPLICATIONS by **INTACT INSURANCE COMPANY, TRAFALGAR INSURANCE COMPANY** and **NOVEX INSURANCE COMPANY** for approval to modify their rates and risk-classification systems for private passenger vehicles

BEFORE: Peter W. Gurnham, Q.C., Chair

APPLICANT: **INTACT INSURANCE COMPANY**
TRAFALGAR INSURANCE COMPANY
NOVEX INSURANCE COMPANY

FINAL SUBMISSIONS: April 1, 2019

DECISION DATE: **April 8, 2019**

DECISION: **Applications are approved.**

I INTRODUCTION

[1] Intact Insurance Company, Trafalgar Insurance Company and Novex Insurance Company applied to the Nova Scotia Utility and Review Board for approval to modify their rates and risk-classification systems for private passenger vehicles. On February 20, 2019, the Board received applications from Novex and Trafalgar to adopt the changes proposed in an application submitted by Intact. Novex used the exact Intact rates and risk-classification system apart from a group discount it offers that Intact does not. Trafalgar rates, while not matching, are based on the Intact rates. The proposal to adopt the same changes as Intact (apart from one additional change for Trafalgar only) maintain these relationships.

[2] The Board, however, had not received an application from Intact. On February 27, 2019, Intact contacted the Board to determine the status of its application. The Board informed Intact that no application was received. After determining a technical issue concerning file size prevented the transmission of the electronic files to the Board, Intact was finally able to provide the application, dated February 6, 2019.

[3] Although Intact, Trafalgar and Novex filed separate applications with the Board, because the applications are quite similar the Board addresses all three applications in this Decision.

[4] All three applications complied with the Board's "*Rate Filing Requirements for Automobile Insurance – Section 155G Prior Approval*".

[5] Intact, Novex and Trafalgar had mandatory filing deadlines of April 1, 2019. Because the Intact application included the required actuarial analysis, the applications qualify to reset the mandatory filing deadlines to February 1, 2021.

[6] After they filed their applications, Intact, Novex and Trafalgar received and responded to Information Requests (IRs). Board staff also reviewed the applications and prepared a report (Staff Report). The Staff Report was given to Intact, Novex and Trafalgar. All three told the Board that they had no comments on the Staff Report.

[7] During the IR process, Intact separately filed an amended application on March 20, 2019. The revisions slightly changed the indications but the proposed rates remained unchanged. After the Board shared the Staff Report with Intact, each company provided further amendments on March 29, 2019. These amendments included a proposal to adopt the most recently approved version of the Canadian Loss Experience Automobile Rating (CLEAR) tables to assign rating groups for determining premiums for several coverages.

[8] The Board did not consider it necessary to hold an oral hearing. The Board finds that the proposed rates and risk classification systems are just and reasonable in the circumstances and approves the applications.

II ISSUE

[9] The issue in these applications is whether the proposed rates and changes to the risk-classification systems are just and reasonable and follow the *Insurance Act* (*Act*) and its *Regulations*.

III ANALYSIS

[10] Intact proposed changes to its base rates that varied by coverage but, not by territory. While Intact's rate level needs or indications suggested rates should increase overall by 13%, Intact applied for an overall rate level increase of only 7.6%.

[11] Applying Intact's changes results in an increase of 7.1% for Novex and 8.6% for Trafalgar.

[12] The Companies also proposed the adoption of the 2019 CLEAR Table and certain changes to their premium dislocation caps.

[13] Board staff reviewed rate level indications developed by Intact and in doing so looked at the following:

- Loss trends and the effects of reform;
- Loss development;
- Credibility standards, procedure and complement of credibility;
- Premium (rate group drift) trends;
- Expense provisions, including Unallocated Loss Adjustment Expenses;
- Experience period and weights;
- Premium to surplus leverage ratio; and
- Target and proposed return on equity (ROE).

[14] Board staff advised that all but two issues raised in the IR process were successfully resolved in that process. The issues requiring further analysis were (1) loss trends selections and (2) profit provision.

Loss Trends

[15] Intact based their loss trend selections on their own Nova Scotia experience through June 30, 2018. Intact believes its large number of policies represents a sizeable share of the industry and warrants the use of its own data to determine the loss trends. Intact considered industry data through December 31, 2017, for certain coverages

including Bodily Injury and Accident Benefits, when making its selections. While Intact reviewed experience from 2006 to 2018, it believed the more recent 2012-2018 data deserved more weight. Intact set its future trend rates equal to its past trend rates.

[16] The Board consulting actuary, Oliver Wyman, also made loss trends selections for private passenger vehicles. Oliver Wyman examined trends for frequency, severity and loss cost information after examining both five and ten years of data on a half-yearly basis. For future trends Oliver Wyman selected the most recent past trends which they assumed would continue.

[17] Board staff compared the loss selections made by Intact and Oliver Wyman. Board staff advised that for all coverages the Intact selections are lower than the Oliver Wyman trends. Therefore, the Intact selections would produce lower indicated rates. Board staff advised that the differences are not that large.

[18] Given that Intact represents a sizeable segment of the Nova Scotia market, Board staff advised that Intact's experience is large enough to allow it to use its own data to develop trends and, in the circumstances, recommended the Intact loss trends are the appropriate ones to use in determining the indications to assess the appropriateness of the Intact proposal. The Board accepts this recommendation.

Profit Provision

[19] Intact used a financial model that projects cash flow for a policy using assumptions about expenses, losses, and investment income. The model also included a 12% target return on equity and a level of capital of 200% of the Office of the

Superintendent of Financial Institutions (OFSI) minimum capital test (MCT). If all the Intact assumptions prove correct, it will achieve its target of 12% return on equity.

[20] OSFI is the federal regulator of property and casualty insurers. OSFI developed the MCT. The test applies a set of capital requirements that reflect the riskiness of a company's assets and liabilities to determine a consistent level of capital. OSFI requires each company to hold additional capital above the MCT level to ensure the company's ongoing solvency. This additional capital is expressed as a percentage of the MCT. The required percentage of MCT varies by company and reflects OSFI's concern about the company's unique characteristics (e.g., size, concentration of risk, etc.). If the company's actual capital level drops below this OSFI target, the company will attract greater scrutiny from OSFI and may face further regulatory actions to address the shortfall. To avoid this additional scrutiny, a company holds an even higher level of capital to avoid random fluctuations in experience dropping the actual level of capital below the OSFI target.

[21] The 200% of MCT used in the pricing model is higher than the OSFI target for Intact. The question is whether Nova Scotia drivers should cover the full costs of this additional capital in the pricing model. The Board determined previously that 185% of MCT was the appropriate level of capital to include. This level addresses the concern about random fluctuations in experience forcing capital below the OSFI target for Intact. This level is also the reasonable amount of capital for Nova Scotia clients to cover. With no new information presented in the application, the Board requires Intact to use 185% instead of the Intact selection of 200%.

[22] In recent years, the Board has required companies, including Intact, to lower the target return on equity to 10%. The Board based these reductions on concerns that the industry appeared to be earning returns on equity that were higher than the 12% the Board was approving.

[23] In its last three decisions, the Board required Intact to use 185% of the MCT and a 10% return on equity. These assumptions produced a profit provision which falls within a range the Board considers satisfactory.

[24] When given the opportunity to explain why the Board should not use a similar adjustment in this application, Intact expressed concerns about the assumptions not being suitable in current market conditions. Intact also suggested its experience in Nova Scotia was not as good as in the rest of Canada. These are arguments Intact has made in past applications.

[25] The Board notes that in each of the past complete filings (2014, 2015, 2016 and 2017) Intact proposed changes to rates that were lower than both its indications and the Board approved indications. The Board believes the lower Intact returns on equity and poorer Nova Scotia loss ratios are more likely caused by Intact taking smaller than indicated increases rather than the result of the Board forcing Intact to change its assumptions for return on equity and percentage of minimum capital. Board staff recommended the Board require Intact to use a 10% return on equity and 185% of the MCT as inputs to the model to produce indications to be used as the target to assess the proposal. The Board accepts this recommendation.

Staff Indications

[26] The Staff indications, which are recommended as the target against which the Intact proposal should be assessed, are those calculated using all of the Intact assumptions except the use of a 10% return on equity and 185% of the MCT. Board staff compared the Staff indications to the proposal and found that the proposed rate changes followed the direction of the Staff indications although the size is different. Apart from one of the coverages examined, the proposed rates are lower than the indicated rates.

[27] Because the proposed increases are smaller than the staff indicated increases, the likely return on equity falls below the 10% target. In the circumstances Board staff recommended the Board approve the proposed rate changes as filed.

Other Proposed Changes

Territorial Differentials

[28] Intact did not propose any changes to territories or territorial differentials.

Conviction Free Discount

[29] Intact asked to remove its current Conviction Free Discount and instead will move the discount into its rating variable “Number of Minor Convictions in Last 3 Years”.

[30] Board staff advised this change will have no impact on existing customers as the differentials for the rating variable will produce the same effect as the discount produces. Intact also requested it be allowed to remove the requirement that a principal operator be licensed for six or more years. This change will make the conviction-free benefit available to more clients. Board staff recommended the Board approve the removal of the Conviction Free Discount and placing its impact in the rating variable

"Number of Minor Convictions in Last 3 Years", as well as the change to the eligibility criteria.

Group Discount (Trafalgar Only)

[31] Trafalgar proposed the introduction of a Group Discount. Intact does not offer a group discount while Novex does.

[32] Trafalgar explained that it wishes to offer this discount when it has a contract with a group with a national presence. Trafalgar sees the discount as a marketing tool to help grow its business through partnerships with eligible groups. Board staff recommended the Board approve the Group Discount, for Trafalgar, as filed.

Premium Dislocation Capping Change

[33] To manage the rate impact, which is called dislocation, experienced by its clients, Intact currently applies a 20% premium dislocation cap on premium increases at renewal. As a partial offset, Intact also applies a 20% cap on premium decreases at renewal. If there is no material change in the risk that a vehicle poses at renewal, the premium will not increase or decrease by more than 20%.

[34] Where there has been a new minor conviction during the policy period, the cap is increased to 30% to allow the impacts of any minor conviction (i.e., loss of conviction free discount or conviction surcharge) to pass through. The cap returns to 20% if, in the next policy period, there are no new minor convictions.

[35] Intact explains when the rates proposed under this application are effective, all policies will have renewed under the risk-classification changes made in the last application. Intact believes that its current capping restrictions will no longer be required to manage dislocation.

[36] Intact proposed removing the cap on premium decreases and to increase the cap on premium increases to 35%. As well, the second-tier cap when there is a new minor conviction will increase from 30% to 45%. These changes will move clients to their true premium faster. Intact estimates most policies will achieve their true premium at the second renewal. Intact expects to remove capping entirely in a future filing.

[37] The Board has concerns over rate capping. Given the rate inadequacy in the industry resulting, in part, from companies taking less than indicated increases, a cap would further hamper getting to the indicated rates. The Board prefers caps, if required, to be removed quickly. The Intact proposal does that.

[38] Novex and Trafalgar will make similar changes to their premium dislocation caps. The current caps are the same as those used by Intact.

[39] Board staff recommended the Board approve the proposed changes to the premium dislocation caps, as requested.

Adoption of 2019 CLEAR Table

[40] To assign rate groups for physical damage coverages and Accident Benefits, Intact uses the 2018 CLEAR (Canada, Collision and DCPD Combined, with extended Vehicle Code (21 years) for Alberta & Atlantic Canada) Table. In the amended application, Intact proposed to adopt the 2019 version of this table. The Board approved this table for use in Nova Scotia on February 15, 2019. Intact off-balanced the impact of the adoption of the table to make the change revenue-neutral.

[41] Board staff recommended the Board approve the proposed adoption of the 2019 CLEAR table and the associated off-balancing, as filed in the amended application.

Other Observations on the Application

Automobile Insurance Manual Changes

[42] Intact proposed a few changes to its rating/underwriting rules in its Automobile Insurance Manual. These changes are in addition to those required to implement the changes described earlier.

[43] The changes addressed the types of risks Intact will write. For example, rather than requiring a principal operator to be licensed four or more years, Intact will now require the operator to be licensed five or more years. This change will align Nova Scotia underwriting with Ontario.

[44] Intact will also increase the minimum deductibles in several special cases with specific loss histories. The increases are in keeping with the increases to the minimum physical damage deductibles (now $500 for All Perils and Collision and $250 for Comprehensive and Specified Perils).

[45] Intact will also split its current speeding minor conviction into a minor conviction for speeding less than 31 km/h over and a major conviction for speeding more than 30 km/h over. These changes align Intact with Facility Association and other competitors.

[46] None of the proposed changes violate the *Regulations*.

[47] Novex and Trafalgar will make the same changes.

[48] Board staff reviewed the current and proposed Manuals and found no areas where the Companies appear to be in violation of the *Insurance Act* or its *Regulations*.

[49] Board staff recommended the Board approve these proposed changes to the Automobile Insurance Manual, as filed

Other Sections

[50] Board staff reviewed the remaining sections of the applications and found that they comply with the Board's *Rate Filing Requirements*.

Effective Dates

[51] Intact, Novex, and Trafalgar in the original applications proposed effective dates of May 14, 2019, and June 14, 2019, for new business and for renewals, respectively. In the cover note for the final amended application, these dates were changed to June 5, 2019, for new business and July 5, 2019, for renewals.

IV FINDINGS

[52] The Board finds that the applications follow the *Act* and *Regulations*, as well as the *Rate Filing Requirements*.

[53] The financial information supplied by Intact, Trafalgar or Novex satisfies the Board, under Section 155I(1)(c) of the *Act,* that the proposed changes are unlikely to impair the solvency of the Companies .

[54] The Board finds the proposed rates are just and reasonable.

[55] The Board approves:

- the requested changes to the Conviction Free Discount;
- the introduction of a Group Discount for Trafalgar only;
- the proposed changes to the Premium Dislocation Cap;
- the proposed changes to Rating and Underwriting Rules in the Automobile Insurance Manual; and
- the proposed adoption of the 2019 CLEAR Tables.

[56] The Board resets the mandatory filing date of February 1, 2021 for all three Companies for private passenger vehicles.

[57] The Board approves the proposed effective dates of June 5, 2019 for new business and July 5, 2019 for renewals.

[58] Each of Intact, Trafalgar and Novex are required to file an electronic version of its updated Automobile Insurance Manual within 30 days of the issuance of the Order in this matter.

[59] An Order will issue accordingly.

DATED at Halifax, Nova Scotia, on April 8, 2019.

Peter W. Gurnham