DECISION **2017 NSUARB 59**
M07862

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 modify its rates for Snow Vehicles and its rating rules for Snow Vehicles and other Miscellaneous Vehicles

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

APPLICANT: **FACILITY ASSOCIATION**

FINAL SUBMISSIONS: April 18, 2017

DECISION DATE: **April 26, 2017**

DECISION: **Application is approved.**

I INTRODUCTION

[1] Facility Association ("Facility" or "Company") filed supporting documents and materials ("Application") with the Nova Scotia Utility and Review Board ("Board") for approval to modify its rates for Snow Vehicles and its rating rules for Snow Vehicles and other Miscellaneous Vehicles. The Application was filed electronically on February 1, 2017, and the original documents were received on February 3, 2017.

[2] Information Requests ("IRs") were sent to the Company on March 1, 2017, and responses dated March 13, 2017, were received on March 14, 2017.

[3] As a result of a review by Board staff, a staff report dated April 5, 2017, ("Staff Report") was prepared. The Staff Report was provided to the Company for review on April 5, 2017. The Company's response was received on April 18, 2017, indicating that it had reviewed the Staff Report and, other than reiterating comments made in its Application, had no additional comments.

[4] The Board did not deem it necessary to hold an oral hearing on the Application.

II ISSUE

[5] The issue in this Application is whether the proposed rates and changes to the rating rules are just and reasonable and in compliance with the *Insurance Act* ("*Act*") and its *Regulations*.

III ANALYSIS

[6] The Company sought approval to change its rates and rating rules for Snow Vehicles. The Application was made in accordance with the Board's *Rate Filing Requirements for Automobile Insurance – Section 155G Prior Approval* ("*Rate Filing Requirements*"). The Company's mandatory filing date was February 1, 2017.

[7] The Company also proposed several changes to rating rules which apply to other Miscellaneous Vehicles insured by Facility.

[8] The proposed effective date for both new business and renewal business is 100 days after the Board's issuance of an Order approving the rates.

Rate Level Changes

[9] The Company proposed to change its rates and rating rules. The proposed changes represent an overall rate level increase of 14.4%.

[10] In considering the Company's Application, Board staff reviewed all aspects of the ratemaking procedure, including the following:

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

[11] Based upon Board staff's review of the Application, the only issues that arose concerning the Facility analysis of its rate level needs where additional review is required are:

a. the selection of loss trends;
b. the profit or cost of capital; and
c. finance fee revenue.

[12] All other concerns that were raised in the Information Requests were resolved satisfactorily through that process.

Loss Trends

[13] Because Miscellaneous Vehicles lack sufficient experience to develop trends directly, Facility used Private Passenger Vehicle loss trends. This use of Private Passenger loss trends as proxies for Miscellaneous Vehicle trends is common in the industry due to the lack of data.

[14] When industry claims experience data was released by the General Insurance Statistical Agency ("GISA"), Board staff requested Oliver Wyman ("OW"), the Board's consulting actuaries, to develop assumptions for loss trends for Private Passenger Vehicles. At the time of the filing, Facility had access to the OW report based on data through December 2015. Subsequently, OW published a report based on data through June 2016.

[15] In developing its selections, OW examined trends for the industry loss costs, frequency and severity before making its selections. OW considered both 5 and 10 years of data. After selecting past loss cost trends, OW selected future trends to match the selections for past trends. It is important to note that OW uses industry data that reflects both indemnity costs and allocated loss adjustment expenses.

[16] Facility selected loss trends that differ from those selected by OW. Facility based their selected loss trend rates primarily on a review of industry experience in Nova Scotia through December 31, 2015. Facility reviewed loss experience excluding Allocated Loss Adjustment Expense from 1996-2015 to develop its "indemnity only" loss cost trend selections. The timeframe is longer than that used by OW.

[17] For some coverages Facility varied its selections for past and future trends. It also changed the starting point of the future trend based upon its analysis.

[18] Board staff produced for the Board's review a chart comparing the Facility and OW selections.

[19] The OW selections produce higher indicated changes for all coverages except for Accident Benefits. The largest difference was for Specified Perils where Facility developed its own trend while OW uses the Comprehensive trend.

[20] Although the results are reasonably close for most coverages, with the exception of Specified Perils, Board staff recommended the Board should require the use of the OW trends when developing the indications. This recommendation was made despite the fact it would lead to higher indicated rates for most coverages. The recommendation is consistent with past Board staff recommendations for other Miscellaneous Vehicles. The Board agrees with the use of the OW trends.

Return on Equity

[21] Facility included a 12% after tax return on equity ("ROE") and a 2:1 premium to surplus ratio. Using the investment returns on surplus assets, which Facility sets based on current market yields, the profit provision expressed as a percentage of premiums is

about 8.5%. Board staff believes Facility's assumed investment return on surplus assets should be higher based on the fact that the companies holding surplus to back Facility's assets are not investing at current market yields.

[22] In recent decisions, the Board has required companies to lower the target ROE to 10%. This action was taken as a result of Board concerns that, as evidenced in part by the release of the 2012 and 2013 GISA Financial Information report, the industry appeared to be earning ROEs well in excess of the 12% the Board was approving.

[23] The 2014 and 2015 version of these reports show negative ROEs for the industry for Private Passenger Vehicles. This is likely a result of many companies not taking full indicated rates coupled with some deteriorating experience that is possibly related to inclement weather at the start of 2015, as opposed to the result of the Board forcing companies to the lower end of its profit range. As such, the Board has continued to require the 10% ROE for most companies.

[24] In past filings the Board has required Facility to reduce its 12% assumption to 11% which is higher than that ordered for other companies.

[25] Facility provided indications using the 11% ROE as an alternative and Board staff recommended that the Board continue to require Facility to use the 11% ROE instead of its selected 12%. The Board agrees.

Finance Fee

[26] In a number of recent Facility applications, the Board has required Facility to reduce its variable expenses by 1% to reflect the finance fees that are charged by the servicing carriers. To be consistent, Board staff recommended the Board should require Facility to reduce its variable expenses by 1% to reflect finance fees. The Board agrees.

Staff Indications

[27] Based upon the recommendations to use the OW loss trends, an 11% ROE, and the 1% reduction in variable expenses, Board staff then compared the staff indications to the proposed changes which equal the original Facility indications.

[28] The overall proposed change is for a lower increase than indicated in the staff indications and results in an ROE below the Board's allowed range.

[29] While the proposed rates result in a small subsidy from the mandatory coverages to Specified Perils, Board staff do not view this as being a reason to change the rates and, accordingly, recommended the Board should approve the rate changes as filed. The Board agrees.

Rating Rules

[30] Facility proposed several changes to its rating rules some of which, as noted, apply to vehicles insured by Facility other than just Snow Vehicles. The proposed changes are as follows:

List Price New: ATV and Snow Vehicles

[31] Facility proposed a change to allow rating of these vehicles by actual cash value in certain circumstances. If an ATV or Snow Vehicle has a value of $15,000 or more and the insured provides an acceptable appraisal, performed at his/her own expense, and the appropriate endorsement is included, then the vehicle can be rated on actual cash value as opposed to list price new. This represents a change in risk-classification system and the change seems reasonable and is approved.

Motorhomes

[32] Facility proposed a change where a commercial/public vehicle is converted to a Motorhome. The change deals with physical damage. If the value of the vehicle is up to $15,000, the rate group can be based upon the limit selected by the insured, but for higher valued vehicles the list price new must be used. This change seems reasonable and is approved.

Off Road Vehicles

[33] Facility proposed a change for Off Road Vehicles, except for Pickups, 4x4s and similar vehicles that are designed for road use, that will allow the use of actual cash value for determining rate group in certain circumstances. If the vehicle value is less than $15,000, either list price new or a value selected by the insured may be used. For higher value vehicles, list price new is used unless the insured provides, at his/her expense, an acceptable appraisal. In that case, actual cash value can be used. This change seems reasonable and is also approved.

Mopeds

[34] Facility proposed to change its definition of Moped to remove the reference to maximum speed and to focus solely on engine size. The revised approach is similar to other insurers and seems reasonable.

Motorcycles Converted to Ski Bikes

[35] Facility proposed a number of changes to handle situations where a Motorcycle has been converted for use on snow or ice (as a Ski Bike). The first change includes this type of vehicle under the Motorcycle definition so they are treated as such and not as Snow Vehicles. The second change confirms that since these vehicles are to

be rated as Motorcycles and given the normal exposure is expanded outside the usual May to November period an additional premium will be required. However, if the Ski Bike is used only in the winter, no premium would apply for the May-November period. The final change details how to calculate the premium using short rate tables for the additional exposure. These changes seem reasonable and are approved.

Rating Algorithm

[36] Facility proposed to change its rating algorithm. The change involved the determination of premiums for differing liability limits for Bodily Injury and Property Damage. The current approach uses a constant amount that is added to the base rate for each available liability limit. Facility proposed to change this to a multiplicative factor. These new factors were determined so that the premiums under the current and the proposed method were the same.

[37] This change seems reasonable and Board staff recommended that the Board approve the change to the rating algorithm and the resulting differentials, as filed. The Board agrees.

Rate Manual Review

[38] Board staff have reviewed the current Rate Manual that is posted on the Company website, as well as the list of changes proposed by Facility in section 7 of the Application and have found no areas where the Company appears to be in violation of the *Regulations*.

IV FINDINGS

[39] The Board finds that the Application complies with the *Act* and *Regulations*, as well as the *Rate Filing Requirements*.

[40] The Board finds the proposed rates are just and reasonable. The Board also approves the changes to the rating rules as proposed.

[41] The Application included full actuarial indications and the required territorial analysis; therefore, it qualifies to set the new mandatory filing date for Snow Vehicles for the Company to February 1, 2020.

[42] The Board approves the effective date for both new business and renewal business at 100 days after the Board's issuance of an Order approving the rates.

[43] The Company is required to file an electronic version of its updated Rate Manual within 30 days of the issuance of the Order in this matter.

[44] An Order will issue accordingly.

DATED at Halifax, Nova Scotia, this 26th day of April, 2017.

Peter W. Gurnham