

NOVA SCOTIA UTILITY AND REVIEW BOARD



IN THE MATTER OF THE INSURANCE ACT

- and -

IN THE MATTER OF AN APPLICATION by **WAWANESA MUTUAL INSURANCE COMPANY** for approval to modify its rates and risk-classification system for commercial vehicles

BEFORE: Richard J. Melanson, LL.B., Member

APPLICANT: **WAWANESA MUTUAL INSURANCE COMPANY**

FINAL SUBMISSIONS: February 1, 2018

DECISION DATE: **February 12, 2018**

DECISION: **Application is approved.**

I INTRODUCTION

[1] Wawanesa Mutual Insurance Company (Wawanesa or Company) filed supporting documents and materials (Application) with the Nova Scotia Utility and Review Board (Board) for approval to modify its rates and risk-classification system for commercial vehicles (CV). The Application, dated November 24, 2017, was filed electronically on December 6, 2017, and the original documents were received on December 8, 2017.

[2] An Information Request (IR) was sent to the Company on December 22, 2017, and a response was received on January 12, 2018. An additional IR was issued on January 25, 2018, to which the Company responded on January 26, 2018.

[3] As a result of a review by Board staff, a staff report dated January 31, 2018, (Staff Report) was prepared. The Staff Report was provided to the Company for review on the same date. The Company responded on February 1, 2018, indicating it had no comments to add to the Report.

[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 risk-classification system 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 its risk-classification system for CV. 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 March 1, 2019.

[7] The proposed effective date is May 1, 2018, for both new business and for renewal business.

Rate Level Changes

[8] The Company proposed changes to its base rates and risk-classification system, that are not uniform by territory. The proposed changes represent an overall rate level increase of 4.6%. This is less than the increase suggested by Wawanesa's actuarial indications.

[9] In addition, the Company proposed:

- Changes to territorial differentials;
- New deductibles;
- Increased liability limits;
- Class changes;
- Driving Record Changes; and,
- Endorsement Changes.

[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;
- Expense provisions, including unallocated loss adjustment expenses;
- Credibility standards and procedure;
- Premium (rate group drift) trends;
- Experience period and weights;
- Premium-to-surplus leverage ratio; and,

- Target and proposed return on equity (ROE).

[11] Board staff advise that two issues arose as a result of its review of the Application where more discussion was warranted: the profit provision, specifically the target ROE; and, expenses, specifically the Health Services Levy. All other issues identified during the review by Board staff were resolved through the IR process.

Return on Equity

[12] Wawanesa uses a 12% target ROE and a premium-to-surplus ratio that varies by coverage but averages to 2:1 overall. This ratio is lower than in the Company's last application. Wawanesa explains that it revised its approach based on feedback from a review of pricing by a third party. It based its selection on the ratio observed in other filings.

[13] The selection of 12% ROE puts Wawanesa at the top of the Board's range of reasonable return on equity (i.e., 10%-12%).

[14] In recent decisions, the Board, concerned about the level of ROE/profit observed for the industry, forced some companies to use a 10% ROE. When asked why Wawanesa should not be required to make a similar adjustment, the Company responded:

Wawanesa is a mutual company and is very well capitalized. Our premium to surplus ratio is established by looking at other benchmarks within the industry rather than on operating constraints as with other public companies. Our target ROE of 12% is similarly set by comparing what other companies have done in similar business segments across Canada.

...

With the changes as proposed our ROE will only be 7.835% which is lower than 10%.

[Response to question 5 of IR-1]

[15] Wawanesa provided indications using a 10% ROE. The largest impact relates to Bodily Injury. It is clear, however, that the process of reducing the ROE has relatively little impact on the indications. This appears to be due in part to the low level of credibility of the Wawanesa experience, which forces more reliance on the complement of credibility, which is independent of the ROE selected.

[16] Given the relatively small impact of a change to a 10% ROE, Board staff recommend allowing the use of a 12% ROE in assessing whether the proposed changes will result in just and reasonable rates.

[17] The Board accepts the recommendation, noting that the Company had used the upper end of the range.

Expenses

[18] In its indications, Wawanesa includes a provision for the Health Services Levy. The value used was \$24.69 and was based upon a value provided by the Board for a review in 2016. The Superintendent of Insurance published a revised value for 2017 of \$33.09. The Company indicated it was unaware of the new level.

[19] When reflected in the indications, the change raised the overall indications by + 0.5%. The Board notes this impact approximates the reduction that would be required if the 10% ROE were used.

[20] Board staff recommends Wawanesa not be required to reflect the higher Health Services Levy in this filing. Given Board staff's analysis, the Board accepts this recommendation. This recommendation alleviates any concerns about the selected ROE being too high in the circumstances of this Application.

Staff Indications

[21] Based on the recommendations, the Staff Indications, which are the target against which the Wawanesa proposal should be assessed for reasonableness, would equal the Wawanesa indications. These indications would be a reasonable approximation to those if the 10% ROE adjustment and the Health Services Levy adjustment were required.

[22] The Board agrees with Board staff's assessment that there is no reason to require changes.

Proposed Rate Changes

[23] Where changes are proposed, the proposed rate changes are in the direction of the Staff Indications. Only the magnitude is different. Except for PD-Tort, Collision, and SEF#44, the proposal results in lower rates than indicated rate changes would produce. The overall proposed change is for a much smaller rate increase than indicated.

[24] The proposed rates produce a ROE of 7.84%. This result is well below the target of 12% and the lower bound off the Board's range (i.e., 10%). The deviations for Bodily Injury and Accident Benefits are the source of most of the shortfall. When Board staff questioned this result, the Company responded:

If Wawanesa were to take the full indication for both TPL and AB, we would likely lose a significant number of policy holders, which would have a large effect on our current book. Wawanesa is focused on long term growth, by taking the full indication this would not coincide with the company's objectives. The company would rather take smaller rate increases over time than [*sic*] one large rate increase.

[Response to question 3 of IR-1]

[25] Taking a smaller rate increase than indicated for these two coverages, and a larger rate increase than indicated for Collision, creates a small subsidy among the coverages. While this should be monitored in future filings, the Board agrees with Board staff that it does not warrant any change at this time.

[26] As a result, the Board finds that the proposed changes will result in just and reasonable rates, and approves them.

Other Proposed Changes

Territorial Differentials

[27] Rather than conducting an analysis of territorial differentials, Wawanesa developed indicated rates directly for each of its coverages for each territory. Based upon these indications, the Company selected changes that were in the direction of the indicated change but were tempered based upon Wawanesa's perception of its market position in those territories. The Board accepts the recommendation of Board staff and approves the proposed territorial differentials.

New Deductible

[28] Wawanesa proposed the introduction of several new deductible levels for Collision, Comprehensive and Specified Perils. The new levels are \$2,500; \$7,500; \$10,000; \$15,000; \$20,000; and \$25,000.

[29] The Company interpolated between the differentials for \$2,000 and \$3,000 to derive the \$2,500 differentials. For levels \$7,500 and above, Wawanesa rebased the differentials for those levels in Ontario to reflect the Nova Scotia levels.

[30] Wawanesa supported the proposed changes to deductible offerings. The Board approves the new deductible levels and the proposed differentials, as filed.

Increased Liability Limits

[31] Wawanesa proposed to add liability limits up to \$9,000,000 for Bodily Injury, PD-Tort, and SEF#44. The limits and differentials for these items are the same as those filed for use in Ontario. The differentials are based on those published by IAO Actuarial Consulting Services Inc. (IAO) for Bodily Injury and PD-Tort. For SEF#44, the premiums for limits exceeding \$5,000,000 are based upon adding \$10 to the previous premium amount, beginning at \$5,000,000. The Board approves the increased limits and proposed differentials/premiums, as filed.

Class Changes

Class 42 Light Sand & Gravel

[32] Wawanesa proposed the doubling of the class factor for Class 42 to compensate for the increased exposure associated with light sand and gravel hauling commercial vehicles. Wawanesa only has a very small number of these risks insured. With this small volume, an exact surcharge cannot be determined. The IAO manual imposes a factor of 2.0 to Class 42 for only Collision and Direct Compensation Property Damage (DCPD) for these risks. A systems limitation requires Wawanesa to apply the factor to all coverages (Bodily Injury, PD-Tort, DCPD and Collision) and not just Collision and DCPD.

[33] Wawanesa explained that because the Bodily Injury indication is highly positive, combined with the higher risk for Bodily Injury claims with these vehicles, the 2.0 factor is appropriate. As well, these vehicles will be heavier and could cause larger property damage claims. The Company also believes it would be overly competitive for these vehicles without the 2.0 differentials.

[34] Board staff recommends the Board approve the doubling of the Class 42 factor, as filed. The Board accepts this recommendation.

Class 43C Mobile Canteens

[35] Wawanesa proposed to start writing mobile canteens using Class 43C. The Company will apply a 50% surcharge to Comprehensive, Specified Perils, and the Comprehensive portion of All Perils, due to the increased risk of exposure under these coverages.

[36] An additional surcharge will apply to all coverages if the mobile canteen operates within a radius that exceeds 80 kilometers. The Company seeks to write those canteens with minimal distances driven, but the surcharge allows them to provide the coverage if the insured wants to travel longer distances without being so competitive that the Wawanesa rates become attractive to the long range canteen market. The surcharge varies by distance traveled beyond the 80-kilometer mark.

[37] The surcharges were based upon industry knowledge. There is little data to develop experience related surcharges so Wawanesa selected some conservative surcharges to reflect their risk appetite for these vehicles.

[38] Board Staff recommend the Board approve the introduction of this class and the two surcharges, as filed. The Board accepts the recommendation.

Class 43W Tow Trucks

[39] Wawanesa also proposed to begin providing coverage to tow trucks under this class. To reflect the additional risk (e.g., driving in all weather), Wawanesa proposes to apply a 50% surcharge for all tow trucks. For trucks operating in a radius larger than 40 kilometers, the surcharge increases to 100%. As with mobile canteens, the surcharges were based upon industry knowledge. There is little data to develop experience related surcharges so Wawanesa selected some conservative surcharges to reflect their risk appetite for these vehicles.

[40] The Board accepts Board staff's recommendation and approves the introduction of this class and proposed surcharges, as filed.

Class 49 – Heavy Sand & Gravel

[41] The Company will apply a radius of operation surcharge of 200% for all coverages. The surcharge applies to compensate the Company for the increased exposure to risk. While Wawanesa will collect information on the radius of operation to allow for the gathering of future experience data, the surcharge will remain 200% across all radii. Wawanesa explains that this is the only way the surcharge could be implemented in the current system. The surcharge applies to Bodily Injury, PD-Tort, Accident Benefits, DCPD, Collision, and the Collision portion of All Perils.

[42] Board staff recommends approval of the proposed radius of operation surcharge, as filed. The Board accepts this recommendation.

Class 61 – Truckmen Operating within 160 Km

[43] Wawanesa proposed to begin writing these risks. The Company proposed to offer discounts based on the radius of operation. Three bands will be used. The 81 km to 100 km band receives the larger discount. The next band, 101 km to 130 km, sees the first band discount almost halved. The discount disappears for the 131 km to 160 km band.

[44] The Company based the discount on interpolation between the Class 49 (Truckman with a radius under 80 km) and the Class 61 midpoints. Wawanesa provided details of the calculation in response to an IR.

[45] The Board approves the introduction of Class 61 and the proposed discounts, as filed.

Driving Record

[46] Wawanesa currently uses a scale of 0-3 for driving records. This is primarily driven by the number of years free from at-fault claims. Wawanesa proposed to extend this scale to make it 0-6. The new driving records 4, 5 and 6 will have the same definition as driving record 3, but will have correspondingly higher at-fault accident free requirements (i.e., four years, five years, and six years respectively, instead of three years). A requirement to have owned/operated/leased a commercial vehicle for at least 3 years will likewise be extended to four, five, and six years in the new driving records.

[47] Premiums for the new driving records will be determined by applying a factor to the driving record 3 rate. The factor will become smaller, with a resulting lower premium, for each higher driving record.

[48] Wawanesa will also offer accident forgiveness for the first at-fault accident for driving record 6 risks. The Company proposed to offer this feature with no additional premium.

[49] Wawanesa did not directly increase the premiums for driving record 3 to reflect the fact that those risks will now be riskier, as the best drivers have been removed from that category. Wawanesa provided a table that showed most of the driving record 3 risks will move to driving record 6 after the change. Wawanesa off-balanced the impact of the change within the territorial rates so that the change is revenue neutral.

[50] Wawanesa supported the proposed new driving record, the proposed discounts from the driving record 3 premium and the off-balancing. The Board approves the introduction of the new driving records and the discounts and off-balancing, as filed.

Endorsements

[51] Wawanesa proposes the introduction of four new endorsements. Three will be added with no premium associated with them. Wawanesa will use the standard wording for these three new endorsements. The Company recently began offering these three endorsements in New Brunswick and wishes to do so here. The three are:

- NSEF#8 – Property Damage Reimbursement Endorsement;
- NSEF#8A – Property Reimbursement for Operation by Named Person (Section A); and
- NSEF#21B – Blanket Basis Fleet Endorsement.

[52] Wawanesa will also offer NSEF27B – Legal Liability for Damage to Non-Owned Automobile Endorsement, Business Operations for Non-Owned Automobiles In Your Care, Custody, or Control. The Company wants to offer this coverage to commercial vehicles, including trailers. The premiums will be reduced to the approved premium level for private passenger vehicles for this endorsement. This approach ensures the premium is the same for the same class of vehicle (e.g., pick-up truck, artisan van).

[53] The Board accepts Board staff's recommendation to approve the proposed changes to the endorsements, as filed.

Automobile Insurance Manual Review

[54] Board staff reviewed the revised Automobile Insurance Manual included in the Application. After some modifications made during the IR process, Board staff did not find any areas where the Company is in violation of the *Regulations*. The Company proposed no changes to its Automobile Insurance Manual other than those necessary to effect the changes noted in this Decision.

IV FINDINGS

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

[56] The financial information submitted by the Company satisfies the Board, pursuant to Section 155l(1)(c) of the *Act*, that the proposed changes are unlikely to impair the solvency of the Company.

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


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

[59] The Board approves the effective date of May 1, 2018, for both new business and for renewal business.

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

[61] An Order will issue accordingly.

DATED at Halifax, Nova Scotia, this 12th day of February, 2018.



Richard J. Melanson