DECISION **2018 NSUARB 111**
M08589

NOVA SCOTIA UTILITY AND REVIEW BOARD

IN THE MATTER OF THE INSURANCE ACT

- and -

IN THE MATTER OF AN APPLICATION by **ALLSTATE INSURANCE COMPANY OF CANADA** for approval to modify its rates and risk-classification system for private passenger vehicles

BEFORE: Murray E. Doehler, CPA, CA, P.Eng., Member

APPLICANT: **ALLSTATE INSURANCE COMPANY OF CANADA**

FINAL SUBMISSIONS: April 18, 2018

DECISION DATE: **May 22, 2018**

DECISION: **Application is approved.**

I INTRODUCTION

[1] Allstate Insurance Company of Canada (Allstate 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 private passenger vehicles. The Application was filed electronically on March 16, 2018.

[2] Information Requests were sent to the Company on April 3, 2018, and responses were received on April 13, 2018.

[3] As a result of a review by Board staff, a staff report dated April 16, 2018 (Staff Report) was prepared. The Staff Report was provided to the Company for review on April 17, 2018. The Company responded on April 18, 2018, indicating that it had reviewed the Staff Report and had no 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 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 private passenger 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 March 1, 2019. As this Application included full actuarial indications, it meets the requirements of a mandatory filing resulting in a reset of the mandatory filing date to March 1, 2020.

[7] The proposed, subsequently revised, effective dates are July 1, 2018, for new business and September 1, 2018, for renewal business, for all changes except the usage based insurance program and the endorsement. The revised effective dates for the usage based insurance program are July 24, 2018, for new business and September 24, 2018, for renewal business.

Rate Level Changes

[8] The Company proposed to change its rates and risk-classification system. The proposed change represents an overall rate level increase of 9.9%, although the indicated overall rate level change is much higher.

[9] Due to lack of data for the individual components (e.g., Bodily Injury, Property Damage-Tort and Direct Compensation Property Damage (DCPD)), Allstate determined indications for Third Party Liability combined, and applied that change to all three coverages. Until the General Insurance Statistical Agency publishes DCPD experience, the Board finds this to be an acceptable approach.

[10] Allstate proposed changes to several of its differentials (e.g., territory, liability limit, inexperienced operator) as well as to its rating rules and changes to its endorsements.

[11] In addition, the Company proposed changes to its usage based insurance program, to allow for the use of a Smartphone, for monitoring purposes, in place of its current dongle-based program.

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

- Loss trends (uses Oliver Wyman selections from its December 2016 based report);
- Effects of Reform (Minor Injury Cap in 2010 and AB reform in 2012);
- Loss development;
- Premium (rate group drift) trends;
- Expense provisions, including Unallocated Loss Adjustment Expenses;
- Experience period and weights;
- Credibility standards, procedures, and the complement of credibility;
- Premium to surplus leverage ratio; and
- Target and proposed Return on Equity.

[13] Based on the staff review of the filing, the only issue that arose surrounding the Allstate analysis of its rate level needs, where the Board might consider alternate assumptions, was the profit provision. Any other issues raised were successfully resolved in the information request process.

Profit Provision

[14] Allstate uses a target return on equity of 12% in its indications. Based upon its selection of a premium-to-surplus ratio of 1.7:1 (consistent with the prior application although the ratio by coverage has changed slightly) and the investment return on surplus assets, the 12% return on equity results in a profit provision of 9.6%. Using a more common 2:1 ratio and the Board range of 10%-12%, along with the Allstate investment income of surplus assets assumptions, the Board range for reasonable profit provision

would be 6.7%-8.1%. By using a high end of the return on equity range, along with a lower premium-to-surplus ratio, the Allstate profit provision is outside this range.

[15] The Board, in recent decisions, expressed its concern, echoed in both the 2012 and 2013 General Insurance Statistical Agency Financial Information Reports, that the industry appears to be earning profits in Nova Scotia that exceed the level the Board approved. To address this concern, the Board forced other companies to use a 10% return on equity.

[16] The 2014, 2015 and 2016 version of these reports show negative returns on equity for the industry for private passenger vehicles. This result is likely more a result of many companies not taking full indicated rate changes coupled with some deteriorating experience, including that related to inclement weather at the start of 2015, rather than the result of the Board directing companies to the lower end of its profit range. As such, the Board continues to require the use of a 10% return on equity for companies, unless they can demonstrate they are different from the industry.

[17] The financial information in the Application shows the Allstate loss ratios for Nova Scotia automobiles were mixed, relative to the all Canada result for the Company. Three years were better, one was worse and the other was close to the All Canada result. For the five years combined, the Nova Scotia loss ratio of 65.8% compares favourably to the All Canada result of 72.3%.

[18] Because Allstate uses industry loss costs, adjusted to reflect its own mix of business, one can see that the Company experience was better than that of the industry. Allstate noted:

> Loss experience in general has been favourable due in part to the pricing and underwriting initiatives to focus on obtaining and retaining lower cost business. The industry loss ratio

> is adjusted for Allstate's mix of business. The adjustment is lowering the industry loss ratio, which is a testament to Allstate's better mix of business.
>
> [IR-1, Question 10]

[19] Allstate appears to acknowledge that its experience in Nova Scotia has been good relative to the industry. When asked why the Board should treat Allstate differently than those companies it has ordered to use the 10% return on equity level, the Company explained:

> Our primary capital provider, our parent company requires us to make 13% ROE, which means the cost of capital for each province and line should attain that level, else it shows a sign that the province is not profitable enough to operate in. Comparing against other financial institutions such as banks, which are making a much higher ROE with comparable risks, forcing such low returns may lead to withdraw of capital and threaten coverage availability in the province.
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> [IR-1, Question 1]

[20] While the Company may not be like the industry when all Canada results are examined, when the focus is placed on Nova Scotia only, it appears that Allstate is enjoying higher profits. As such, Board staff recommend the use of a 10% return on equity.

[21] Allstate selects an investment return on surplus assets that is much lower than the response to question CONF-7b in the Application seem to suggest would be earned. Allstate indicates that it based its selection, in part, upon new money rates (i.e., rates that they could achieve investing in risk-free assets today) using logic consistent with prior filings.

[22] In past Allstate applications, the Board accepted the additional information provided by the Company that justified the logic used to select the investment on surplus assets. Board staff recommends the Board continue to allow the use of this logic.

[23] Using a 10% return on equity along with all other Allstate assumptions, the profit provision becomes 7.8%. This level falls into the Board range, albeit closer to the higher end.

[24] Allstate provided indications with all its original assumptions except for the use of a 10% return on equity. The result was an indicated increase that was 3% lower than the original indicated increase.

Comparison of Proposed Rates to Indications

[25] The Indications with a 10% return on equity are used as the target against which the Allstate proposal is assessed for reasonableness.

[26] The Allstate proposal compared to these indications shows that the proposed changes are in the direction of the indicated changes, only the magnitude is much smaller. Allstate explains this decision, as follows:

> Due to our overall proposed rate level change being only a fraction of the overall rate indicated rate level change, we are unable to take the full indicated rate level change for coverages. We are concerned with potential dislocation and therefore only proposing a fraction of the overall indicated rate level change.
>
> Keeping its competitive position in mind, Allstate's plan is to gradually take the full increase over a succession of filings in order to minimize disruptions. Allstate will consider filing for rate changes more frequently than the mandatory schedule and has already been doing so.
>
> [IR-1, Questions 2 and 3]

[27] Because the proposal is for a smaller overall increase than indicated, the proposed rates will produce a return on equity that is lower than the recommended 10%. Given the large differences, the return on equity is actually negative (-5.21%) for this proposal.

[28] The Company states the 12% ROE target is not achievable in one rate change without some large dislocation. Allstate plans to gradually implement rate increases to achieve its target and may approach the Board before its next mandatory filing to accomplish this goal.

[29] In the last application, Allstate made a similar argument, also stating it may approach the Board before its next mandatory filing deadline to keep the process moving. This Application is a year in advance of the mandatory filing deadline established with that application, confirming the Allstate commitment to gradually move towards the indications. This approach, in part, alleviates concerns that the Board had about not taking the full indicated change.

[30] In that last application, the Board cautioned Allstate that if the indications were for double digit increases again, the Board would ensure the proposed increases moved the rates closer to the indications. The proposed change in this Application is almost double that in the previous application. The Board accepts that this condition has been met.

[31] Board staff state that Allstate has provided sufficient support for its proposed rate change.

Other Changes

Territorial Differentials

[32] As part of its indications, Allstate undertook an analysis of indicated rate changes for each of its ten territories. Allstate is addressing those territories where the indications suggest the relativities should change by more than 2%, in either direction.

The proposed changes, however, are only partway towards the indicated change. Allstate explains:

> We wanted to avoid larger dislocations for customers in Territories 8 and 10, given that each of these territories represent more than 25% of the book and we proposed an overall base rate increase of more than 10%. By the same token, we decided to take roughly half of the indicated rate decreases for Territories 1 and 9, as taking the indicated rate decrease in full would mean a higher base rate offset for other territories.
>
> [IR-1, Question 11]

[33] Rather than off-balancing the impact of the changes to the territory differentials through the base rates, Allstate considered this small impact, when it made its selection of the overall change.

[34] Board staff state that Allstate provided sufficient support for its proposal.

Liability Limit Differentials

[35] While the minimum liability limit in Nova Scotia is $500,000, Allstate offers both a one and two million dollar limit. The Company proposed changes to its differentials for these higher limits. The proposed changes match the indicated changes. Allstate did not explicitly off-balance the small impact, but rather considered it as it made its overall change selection.

[36] Board staff state that Allstate supported its proposed changes to the liability limit differentials for private passenger vehicles and for Motorhomes.

Occasional Operator Differential

[37] Based upon an analysis of its occasional operator differentials, Allstate proposed to increase all of these differentials by 10%. The differences between Urban

and Rural and between Male and Female differentials will be unchanged, as a result. This proposal closely follows indications.

[38] Board staff support the proposed changes to the occasional operator differentials, as filed.

Rating Rule Changes

[39] Allstate proposed several changes to its rating rules. The first change involves adding time limits to how the Company assigns risk points for someone who has had a policy cancelled for material misrepresentation or for someone who has been convicted of auto insurance fraud. Allstate will only assign points if the policy was cancelled for material misrepresentation in the last seven years. For fraud, the limit will be ten years. These additions allow more people, who are long past the material misrepresentation or fraud incidents, the opportunity to receive fewer risk points.

[40] Allstate is also making changes about newcomers to Canada. For those drivers coming to Canada from a jurisdiction where there exists a reciprocal driver licensing agreement with the province, they will be credited with the equivalent amount of Canadian experience if they can provide proof of licensing and at-fault free driving in their country of origin. Such proof is referred to as a Letter of Experience (LOE).

[41] For those drivers coming from jurisdictions without the reciprocal licensing agreement, if proof of non-Canadian or US license experience is available, such as an LOE, the driver will receive credit for experience equal to the sum of the time licensed in Canada plus actual experience in the country of origin to a maximum of four years.

Without an LOE, there is no credit for the experience in the country of origin. Only the time since first licensed in Canada will count.

[42] Allstate explains the changes serve to harmonize the treatment of newcomers to Canada in Nova Scotia with other provinces and will support profitable growth given the increased demand for insurance for newcomers by granting them some credit for prior experience, when eligible.

[43] Board staff state that Allstate has provided sufficient support for the proposed changes, and they do not violate the *Insurance Act* or its associated *Regulations*.

SEF#43 Limited Waiver of Depreciation Premium Changes

[44] Allstate offers this endorsement, which waives the depreciation on a vehicle in the event of a total loss, if that loss occurred within 36 months of the date the vehicle was first delivered to the insured. The premium, which is a percentage of the Collision and Comprehensive premiums, varies by the age of the vehicle. The premium increases as the age increases to reflect the greater amount of depreciation that Allstate must waive.

[45] The proposed percentages, by vehicle age, of the sum of the Collision and Comprehensive used to determine the endorsement premium, are increasing 2% from the current rate. There is a minimum premium of $50.

[46] Allstate provided an analysis that showed the current average premium of about $46 should be closer to $54. The proposed changes bring the average premium to $53.40. Allstate also observes the change brings the premium more in line with its competitors.

[47] Board staff state that Allstate provided sufficient support for the proposed change as filed.

Changes to Usage Based Insurance Program

[48] Allstate has approval to offer a usage based discount based on an initial six month monitoring period. The Company uses a telematics device, or dongle, to gather the driving experience data over the monitoring period. Once the monitoring period is complete, the Company scores the driving experience and offers a discount between 0-30% based on this score.

[49] Allstate proposed to replace the dongle-based version of the usage based discount program with one based upon the use of a Smartphone to gather the monitoring data. This new program will be branded under the same Drivewise™ name but will use the Drivesight™ model from Arity.

[50] The Smartphone will measure the same risky driving behaviors currently monitored by the dongle. The new methodology, however, will map drivers to a more granular discount grouping. Drivers will receive a score ranging from 1-100 based upon their experience during the monitoring period. This score will be mapped to the discount that ranges from 0% to 30%.

[51] All other elements of the program (enrollment discount (10%), "Try Before You Buy Discount" (5%), additional monitoring criteria, etc.) will apply to the replacement program.

[52] The use of Smartphone technology will reduce the cost of the program. Allstate estimates the savings to be about half of the current dongle costs. Allstate also

asserts that the dongles use a specific wireless network that will be disconnected in the future, rendering the dongles useless. The switch to Smartphone technology will allow the program to continue into the future. The Smartphone approach will also work for drivers of vehicles where the dongle cannot be used, granting such drivers access to the discount.

[53] Board staff commented that Allstate has provided sufficient support for the change to the Smartphone based application and the revised, more granular, scoring system and the conversion factors to get to a usage based discount.

Minor Conviction Surcharge Waiver Endorsement

[54] Allstate currently applies a 15% surcharge when a client is convicted of a first minor traffic violation (for example, speeding (but not at a high enough level to trigger treatment as major or serious)). For subsequent such violations, within a three-year period, the surcharge increases.

[55] Allstate proposed to introduce a Minor Conviction Surcharge Waiver endorsement that can be purchased where all operators on the vehicle are conviction free for the last three years. The endorsement would forgive the first minor conviction, and no surcharge would apply. If a second conviction occurred within three years of the first, the surcharge that applies would not reflect the first conviction. Furthermore, once three years have passed from the time of the first conviction, the second conviction, if there is still less than three years since that conviction occurred, would then receive forgiveness from the surcharge.

[56] To continue to receive the protection offered by the endorsement, the premium must continue to be paid. If the premium ceases, any minor conviction waived would then be used in the surcharge calculation (if still applicable).

[57] The endorsement will apply to the vehicle (or its replacement) upon which it was purchased. Any other vehicle must have its own endorsement purchased to receive the benefits.

[58] Allstate will offer the endorsement by itself or in a package with the Claims Forgiveness endorsement. The premium for a 12-month policy is $20 if purchased separately. There is a $5 discount if purchased as part of the package. For a six-month policy, the premium is $10 when purchased by itself, and $8 as part of the package. The package premiums are for this endorsement only, and does not include the cost of the Claims Forgiveness endorsement.

[59] To establish the premium, Allstate used the relationship between the average premium in Ontario and the cost of this endorsement there. The Company applied that relationship to the average premium in Nova Scotia. That calculation suggested a premium of about $17 which Allstate rounded to $20.

[60] Allstate also provided evidence that a competitor offers a similar endorsement for $25. In this light, Board staff stated that the Allstate proposed premium is reasonable.

Automobile Insurance Manual

[61] Board staff have reviewed the Automobile Insurance Manual on file and found no instances 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

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

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

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

[65] The Board finds the proposed changes to the Territorial Definitions and Differentials, Liability Limit Differentials, Occasional Operator Differential, Rating Rule and SEF#43 Limited Waiver of Depreciation to be just and reasonable.

[66] The Board finds the proposed replacement of the dongle based program with the Smartphone based program, for the usage based insurance program, to be just and reasonable.

[67] As of the date of this Decision, the Superintendent of Insurance has not approved the non-standard wording of the Minor Conviction Surcharge Waiver endorsement. The Board does not approve this endorsement or effective date. The Company will have to file a simplified application for approval once the wording has been accepted.

[68] The Application included full actuarial indications and the required territorial analysis; therefore, it qualifies to set the new mandatory filing date for private passenger vehicles for the Company to March 1, 2020.

[69] The Board approves the effective dates of July 1, 2018, for new business and September 1, 2018, for renewal business and July 24, 2018, for new business and September 24, 2018, for renewal business for the usage based insurance program.

[70] 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.

[71] An Order will issue accordingly.

DATED at Halifax, Nova Scotia, this 22nd day of May, 2018.

Murray E. Doehler