DECISION

2018 NSUARB 128
M08667

NOVA SCOTIA UTILITY AND REVIEW BOARD

IN THE MATTER OF THE INSURANCE ACT

- and -

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

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

APPLICANT: **COSECO INSURANCE COMPANY**

FINAL SUBMISSIONS: June 7, 2018

DECISION DATE: **June 19, 2018**

DECISION: **Application is approved.**

I INTRODUCTION

[1] COSECO Insurance Company (COSECO or Company) filed supporting documents and materials (Application) with the Nova Scotia Utility and Review Board (Board) on April 30, 2018, for approval to modify its rates and risk-classification system for private passenger vehicles.

[2] Information Requests (IRs) were sent to the Company on May 2, 2018, and responses were received on May 10, 2018.

[3] As a result of a review by Board staff, a staff report dated June 7, 2018 (Staff Report) was prepared. The Staff Report was provided to the Company for review on June 7, 2018, and the Company responded on the same date, 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 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.

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

Rate Level Changes

[8] The Company proposed to change its base rates and differentials that are uniform by territory but vary by coverage that result in an overall all-coverages combined increase of 7.5%. These changes are based upon a much larger all-coverages combined rate increase indications that also varied by coverage.

[9] Board staff provided a chart showing changes by coverage comparing the proposed change to the indicated change.

[10] Due to the lack of data, the indications shown for Bodily Injury, Property Damage-Tort and Direct Compensation Property Damage are for Third Party Liability combined. The combined indication, however, was developed by breaking down the Third Party Liability experience into Bodily Injury and Property Damage (i.e., Property Damage-Tort and Direct Compensation Property Damage combined).

[11] The Application also contains a premium dislocation cap.

[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 based on data to June 2017);
- 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
- Profit provision including the target and proposed Return on Equity (ROE).

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

Return on Equity

Profit Provision

[14] COSECO used a target ROE of 12% in its indications and a premium to surplus ratio of 2.05:1 to reflect profit in its rates. The resultant profit provision is 5.6% of premiums. This is down slightly from the last application due to a small change in the premium to surplus ratio.

[15] The Board has grown concerned over the level of profit observed in the industry as a whole, as evidenced by the 2012 and 2013 Financial Information Reports, produced by the General Insurance Statistical Agency (GISA), despite its approving of ROEs around 12%. To address this, it has ordered some companies to lower the target ROE to 10%.

[16] The GISA Reports for 2014-2016 show negative ROEs 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 a 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 companies unless they can demonstrate they are different from the industry.

[17] Board staff asked COSECO why the Board should treat it differently than the companies that were required to use 10%. COSECO responded:

> COSECO has a relatively small volume in Nova Scotia, making its actual ROE quite volatile. ROE is not readily available for a specific province or line of business. When we look at auto claims ratios and combined ratios for Nova Scotia compared to those for the whole country, we can see that NS results are more volatile and significantly higher in average. We can conclude that, most of the time, other provinces subsidize for NS lack of profitability. This proves that, even if overall ROEs are good, automobile line of business in Nova Scotia is not profitable. Not allowing the use of a 12% ROE would encourage the continuance of this subsidization across provinces and lines of business. Also, using a 10% ROE would not change our proposal.
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> [Response to Question 13 of IR-1]

[18] With the exceptions of 2014 and 2017, the Nova Scotia loss ratios for automobiles are much higher than those for Canada as a whole. Over the five years, the NS loss ratio of 92.2% is well above the countrywide loss ratio of 75.2%.

[19] Board staff indicated that it seems, therefore, that the COSECO experience may be different from the average industry results. Board staff concluded that it does not appear that COSECO is overearning and the financial information suggests the results in Nova Scotia have also been very volatile. Board staff recommended, as it did in the previous application, that the Board allow COSECO to use the 12% ROE in the indications rather than replacing it with 10%, in the circumstances of this Application.

[20] The Board agrees.

Comparison of Proposed Rates to Indications

[21] Board staff prepared a chart showing the proposed changes compared to the staff indications. In all cases, except SEF#44, the proposed changes result in lower rates than would be produced if the indicated changes were taken.

[22] For SEF#44, the indicated change would move the current higher premium closer to the industry average premium of approximately $20. Given the Company is taking much lower than indicated increases for other mandatory coverages, forcing the small reduction for this mandatory coverage does not seem appropriate.

[23] Board staff notes that because the proposal is for a smaller overall all-coverages-combined increase than indicated, the proposed rates produce an ROE that is well below the low end of the Board's 10-12% range of reasonability. The proposed ROE is 2.5%. Despite the small ROE, Board staff does not believe the proposed rates, by themselves, would create any solvency concerns for COSECO.

[24] In the last two applications, COSECO proposed, and the Board approved, rate changes that were much lower than indicated.

[25] The Board has some reservations about companies proposing much smaller than indicated changes as COSECO did in the last two filings. The proposed change in this application is closer to the indicated level than in the past applications and is being made a year earlier than the mandatory filing deadline. The proposed change, as Board staff suggests, may be viewed as COSECO moving closer to the indicated level while continuing to wait to see if previously approved revisions to the risk-classification system, or segmentation, will improve the experience

[26] Board staff recommends, and the Board approves, the proposed changes to the base rates, as filed.

Other Proposed Changes

Territorial Definitions and Differentials

[27] COSECO proposed an analysis of its territorial differentials. Rather than the "generalized linear model" analysis of its territorial differentials used in a recent application, COSECO used a "one-way" analysis to determine indicated differentials. To increase the credibility of the data, the COSECO data was combined with that of sister companies, Cooperators General Insurance Company and CUMIS General Insurance Company.

[28] While the analysis shows that the differentials could change, COSECO did not propose any changes. Where significant changes were indicated, the territory generally had limited data. As well, in most cases, the change would result in higher premiums. Board staff recommended the Board approve the proposal to leave territorial differentials unchanged, as filed. The Board agrees.

Adoption of 2018 CLEAR Tables

[29] COSECO currently uses the 2017 Canadian Loss Experience Automobile Rating (CLEAR) table to assign rating groups for Accident Benefits and physical damage coverages. COSECO uses the CLEAR (AB Alberta & Atlantic) - Collison, Direct Compensation Property Damage and Comprehensive Separated version.

[30] In this Application, COSECO proposed the adoption of the 2018 version of this table, which the Board approved for use earlier this year. COSECO off-balanced the impact of the change of table to make that component revenue-neutral.

[31] Board staff recommends, and the Board approves, the proposed adoption of the 2018 CLEAR table, along with the off-balancing of the impact, as filed.

Premium Dislocation Cap

[32] In prior applications, COSECO imposed a premium dislocation cap that limited increases to +15% and decreases to -5%, at renewal. The cap applies at the vehicle level. For example, if the vehicle were to have a 20% increase applied, the cap would be applied to reduce the increase to 15% with the premium for each individual coverage reduced by 5% to get to the capped level. The Company proposed to continue this cap.

[33] Board staff advises that should there be a material change in risk, the client does not lose all the benefits of the cap. Instead, the reference point for the cap is changed, that is, the maximum and minimum premium will reflect the occurrence of the material change in risk.

[34] COSECO indicated that a limited portion of those risks that are currently capped may still have some residual cap amount after the first renewal. However, most of the current non-capped risks would reach true premium after first renewal under the proposed rates.

[35] The Board has in the past allowed negative caps in such a situation but only if the extra premium collected under the negative cap does not exceed the premium foregone. COSECO provided the information that demonstrated this constraint was met.

[36] Board staff recommended the Board approve the premium dislocation cap, as filed. The Board agrees.

Automobile Insurance Manual Review

[37] Apart from the changes required to implement the proposed revisions to rates and the adoption of the 2018 CLEAR table, COSECO is not making any other changes to its manual. Board staff reviewed the manual on file and uncovered no areas where the Company appears to be in violation of the *Regulations*.

IV FINDINGS

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

[39] The Board accepts the COSECO indications as the target against which to judge the appropriateness of the COSECO proposal.

[40] The Board approves the proposed base rate changes, as filed.

[41] The Board approves the proposed adoption of the 2018 CLEAR table, as filed.

[42] The Board approves the proposed continuation of the premium dislocation cap, as filed.

[43] 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.

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

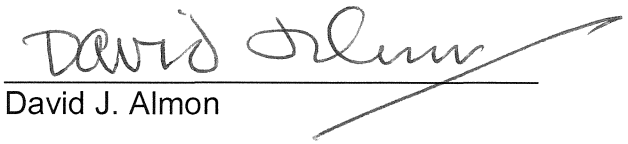
[45] The Application included full actuarial indications and the required territorial analysis; therefore, it qualifies to set the new mandatory filing date for private passenger vehicles for the Company to May 1, 2020.

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

[47] 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.

[48] An Order will issue accordingly.

DATED at Halifax, Nova Scotia, this 19th day of June, 2018.



David J. Almon