DECISION

2018 NSUARB 127
M08675

NOVA SCOTIA UTILITY AND REVIEW BOARD

IN THE MATTER OF THE INSURANCE ACT

- and -

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

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

APPLICANT: **CUMIS General Insurance Company**

FINAL SUBMISSIONS: June 12, 2018

DECISION DATE: **June 18, 2018**

DECISION: **Application is approved.**

I INTRODUCTION

[1] CUMIS General Insurance Company (CUMIS 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 received on May 2, 2018.

[2] Information Requests (IRs) were sent to the Company on June 4, 2018, and responses were received on June 8, 2018.

[3] As a result of a review by Board staff, a staff report dated June 11, 2018 (Staff Report) was prepared. The Staff Report was provided to the Company for review on the same date. The Board received the Company's response dated June 11, 2018, on June 12, 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 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 in the Application is October 1, 2018, for new and renewal business.

Rates and Risk-Classification System

[8] CUMIS proposed changes to base rates and differentials that are uniform by territory, but vary by coverage. The Company also proposed to make changes to its risk-classification system. The proposed changes result in an overall, all-coverages combined, increase of 7.5%. These changes are based upon an indication for a larger all-coverages combined rate increase.

[9] The proposed changes to the risk-classification system relate to the adoption of the 2018 Canadian Loss Experience Automobile Rating (CLEAR) table.

[10] Board staff reviewed the rate level indications developed by CUMIS and in doing so examined all aspects of the rate-making procedure, including the following:

- Loss trends (using Oliver Wyman selections based on data to June 2017);
- Effects of Reform (Minor injury cap in 2010 and Accident Benefits (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 and target and proposed Return on Equity (ROE).

[11] Board staff advised that the only issue that arose surrounding the CUMIS analysis of its rate level needs was the profit provision, where the Board might consider

alternate assumptions or require additional information. Any other issues raised were successfully resolved in the IR process.

Profit Provision

[12] CUMIS uses a target return on equity 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 6.0% of premiums. This is down slightly from the last application due to a small change in the premium-to-surplus ratio.

[13] 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 approving returns on equity around 12%. To address this, it has ordered some companies to lower the target return on equity to 10%.

[14] The 2014 to 2016 version of these reports show negative returns on equity for the industry for private passenger vehicles. This outcome 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.

[15] When asked about using a 10% ROE, CUMIS responded:

> CUMIS 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.
>
> [Response to Question 9 of IR-1]

[16] The Company provided a summary of financial data which is supportive of the statements made in the IR response.

[17] CUMIS has provided sufficient information to show its experience may be different from the average industry results. It does not appear that CUMIS is overearning and the financial information suggests the results in Nova Scotia have also been very volatile. In the circumstances of this Application, Board staff recommends the Board allow CUMIS to use the 12% return on equity in the indications rather than replacing it with 10%. The Board agrees with this recommendation.

[18] Based upon this recommendation the Staff Indications, (i.e., the target against which the CUMIS proposal should be assessed for reasonableness), would equal the CUMIS indications.

Comparison of Proposed Rates to Indications

[19] CUMIS proposed changes that generally follow the direction of the indicated changes, with only the magnitude being different.

[20] The lone exception was SEF#44, where the indicated change would be a small decrease. CUMIS proposed no change. While the indicated decrease would move this premium closer to the industry average, given the Company is taking much lower than indicated increases for other mandatory coverages, the Board agrees with Board staff that CUMIS should not be ordered to reduce the SEF#44 premium to the indicated level.

[21] Because the proposal is for a smaller overall, all-coverages combined, increase than indicated, the proposed rates produce a return on equity that is well below the low end of the Board's 10-12% range of reasonability. The proposed return on equity is 2.5%. Despite the low return on equity, Board staff does not believe the proposed rates, by themselves, would create any solvency concerns for CUMIS. The Board agrees.

[22] The Company explained, its deviation from the indications, as follows:

> The proposed rate level changes were selected balancing our goal to move toward profitability and the importance of limiting the impacts on clients. This gradual approach allows for monitoring how the book reacts to theses changes and analyzing how our results will develop.
>
> In our previous rate reviews, the Board has made the comment that our deviation from indications could set up the potential for having to take even larger increases in the future and we took this recommendation seriously. Although we aim to move toward profitability in a progressive manner, we recognize the importance of ensuring that our rate increases are sufficient to allow us to get there eventually.
>
> Toward that end, as part of the selection exercise, we have compared our current and previous indications against the implemented rate changes to assess whether those changes were allowing us to improve the indication over time. In cases where we observed that the indicated rate level change did not decrease despite having taken an increase in the previous year, we have decided to select a higher rate change than last year.
>
> [Response to Question 1 of IR-1]

[23] The Board had some reservations about the smaller than indicated proposed changes in the last application. Filing for a rate increase now, coming before the mandatory filing deadline, shows CUMIS is taking some steps to move closer to the indicated level.

[24] Board staff recommends that the Board approve the proposed changes, as filed.

Other Proposed Changes

Territorial Definitions and Differentials

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

[26] While the analysis shows that the differentials could change, CUMIS 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 recommends the Board approve the proposal to leave territorial differentials unchanged, as filed.

Adoption of 2018 CLEAR Tables

[27] CUMIS currently uses the 2017 CLEAR table to assign rating groups for Accident Benefits and physical damage coverages. CUMIS uses the CLEAR (AB Alberta & Atlantics) - Collision, DCPD and Comprehensive Separated version.

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

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

Premium Dislocation Cap

[30] In prior applications, CUMIS 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.

[31] Should there be a material change in risk (e.g., an at-fault accident occurs), 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.

[32] CUMIS 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 the first renewal under the proposed rates.

[33] 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 foregone premium. CUMIS provided the information that demonstrated this constraint was met.

[34] Board staff recommends that the Board should approve the continued use of the premium dislocation cap, as filed.

Automobile Insurance Manual Review

[35] Apart from the changes required to implement the proposed revisions to rates and the adoption of the 2018 CLEAR table, CUMIS is not making any other changes

to its Automobile Insurance Manual. Staff reviewed the manual on file and uncovered no areas where the Company appears to be in violation of the *Regulations*.

IV FINDINGS

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

[37] 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.

[38] The Board is satisfied the Company's Application is adequately supported. Its proposal to amend its rates and risk-classification system is just and reasonable. The Board approves the Application, as filed.

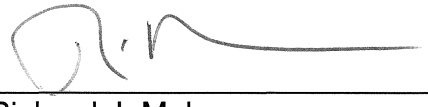
[39] Given that the Application included the required actuarial analysis, the Board finds the Application qualifies to set a new mandatory filing deadline for private passenger vehicles for the Company to May 1, 2020.

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

[41] 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.

[42] An Order will issue accordingly.

DATED at Halifax, Nova Scotia, this 18th day of June, 2018.



Richard J. Melanson