DECISION **2019 NSUARB 37**
M09087

NOVA SCOTIA UTILITY AND REVIEW BOARD

IN THE MATTER OF THE INSURANCE ACT

- and -

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

BEFORE: Stephen T. McGrath, LL.B., Member

APPLICANT: **THE WAWANESA MUTUAL INSURANCE COMPANY**

FINAL SUBMISSIONS: March 6, 2019

DECISION DATE: **March 19, 2019**

DECISION: **Application is approved.**

I INTRODUCTION

[1] The 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 for commercial vehicles. The Application was filed on February 12, 2019.

[2] Information Requests (IRs) were sent to the Company on February 27, 2019, and responses were received on March 1, 2019.

[3] As a result of a review by Board staff, a staff report (Staff Report) was provided to the Company for review on March 4, 2019. The Company responded on March 6, 2019, 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 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 for commercial 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 December 1, 2020.

[7] The proposed effective date is June 1, 2019, for both new business and renewal business.

Rate Level Changes

[8] The Company proposed to change its rates and risk-classification system. The proposed change to the Company's rates for commercial vehicles represents an overall rate level increase of 11%. The base rate changes are uniform by territory but vary by coverage.

[9] To support these changes, Wawanesa provided actuarial indications, which are calculations of the changes to the current premium that the Company should make in order to achieve its target return on equity, assuming its actuarial assumptions prove correct. These actuarial indications suggest that Wawanesa should increase its overall rate by a higher amount than proposed.

[10] The Company did not propose any capping on its requested increase, and proposed no changes to discounts, surcharges, endorsements, rating rules or underwriting rules.

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

- Loss trends and the effects of reforms;
- 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 and proposed return on equity (ROE).

[12] Board staff report that the only issue surrounding the Wawanesa analysis of its rate level needs where more discussion is warranted is the profit provision. All other issues were resolved through the information request process.

Profit Provision

[13] In its model, Wawanesa uses a 12% target ROE and a premium to surplus ratio that varies by coverage but averages to 2:1 overall. There are minor differences in the ratios for the coverages in the Application compared to Wawanesa's last application for rates for commercial vehicles, but the overall result is the same. Board staff have determined that Wawanesa's assumptions result in a profit provision of 6.93% of premiums.

[14] The *Rate Filing Requirements* note that the Board generally finds ROEs between 10% and 12% to be reasonable. This level presumes the use of a premium to surplus ratio around 2:1. The Board also allows for the use of a return on premium approach to be used to reflect profit, and generally views a range of 5.5%-7% as reasonable. Wawanesa's selection of a 12% ROE puts the Company at the top of the Board's range of reasonable ROEs and at the high end for profit as a percentage of premiums.

[15] In recent decisions, the Board has required companies to lower their target ROE to 10%. This action was taken because of Board concerns that the industry appears to be earning ROEs well in excess of the 12% the Board believed it was approving, as evidenced in part by the release of the 2012 and 2013 General Insurance Statistical Agency (GISA) financial information reports. Later versions of the GISA reports show negative ROEs. The Board considers this outcome is likely more 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 a 10% ROE for most companies.

[16] The standard forms provided by the Board for use under the *Rate Filing Requirements* note that if recent Board decisions suggest the industry should use a lower target ROE (e.g., 10%) or profit provision, the Company should explain why it is different from the industry if it selects a higher ROE (or profit provision).

[17] In response to an IR about its target ROE, Wawanesa stated:

> While we use 12% ROE generated indication in the initial filing, our selection of proposed changes is well below the indication resulting when using a 10% ROE. Therefore, Wawanesa is not asking the board to treat us differently. Conversely, the proposed increase will put us in a ROE position that is much lower than 10%.
>
> [IR-1, Q.3]

[18] Wawanesa also provided indications using a 10% ROE. Although the difference in the indicated change in the rate for coverage for bodily injury is somewhat larger than the differences for the other coverages, the indicated overall rate level change is only a few percentage points lower, and still higher than the Company's proposed rates.

[19] Board staff also noted that financial information for 2013-2017, provided by the Company in the Application, shows that Wawanesa earned an overall ROE below 10% in all five years. The Company's loss ratios for Nova Scotia were also worse than those for all provinces combined for the last four years suggesting that, at least recently, its returns from its business in Nova Scotia may have been well below the 10% level.

[20] Board staff concluded that it appeared that Wawanesa's experience may be different from the industry. Board staff recommended that the Board accept the profit

provision included in the Wawanesa indications as filed and not force the Company to use a lower ROE. The Board agrees.

Proposed Rate Changes

[21] Having accepted the Board staff recommendation, the indications against which the proposed changes are to be assessed to determine their reasonableness are the Wawanesa indications. For all coverages, the proposed changes are all in the direction of the indications, but neither indicated increases nor indicated decreases have been fully recognized in the proposed rates.

[22] For mandatory coverages, other than PD-Tort, the proposed rates are well below the indicated rates. This result is partially offset by proposed rates for optional coverages that are higher than indicated. Board staff observed that the rates for coverages where Wawanesa is proposing to recover more than is indicated slightly subsidize those coverages where the Company is proposing to recover less than what is indicated. Board staff recommends that the Board monitor this in future filings but did not recommend any changes at this time. The Board accepts this recommendation.

[23] The proposed rates produce an ROE of 5.76%, which is well below the range of ROEs in the Board's *Rate Filing Requirements*. The Company was asked in an IR why it was proposing smaller increases than indicated, to which it responded:

> Wawanesa is a proud company with a long history dating back to 1896. Our mutual ownership structure both allows us and requires us to take a steady and prudent approach to balancing growth and financial strength. As a policyholder-owned mutual insurance company, we will continue to earn trust by providing quality products and services at the lowest pricing which supports long-term growth and financial stability. Due to the nature of our ownership structure, we decided to take less than indicated and continue to monitor closely on this book of business in the meantime to see if there are underwriting actions that we can take to improve the result of this segment.
>
> [IR-1, Q.1]

[24] Board staff submits that the Company supported its proposed rate changes and, despite the low ROE, recommends that the Board approve the Wawanesa proposal, as filed. The Board is generally concerned when companies choose to seek approval for rates that are much less than indicated; however, the Board accepts that the Company will monitor its financial results closely and agrees with the recommendation from Board staff.

Territorial Differentials

[25] The Company proposed no changes to its territorial differentials, and thus it is not required to undertake a territorial analysis, pursuant to the Board's recent change in filing requirements (2018-2 revised November 30, 2018).

Automobile Insurance Manual

[26] Wawanesa proposed no changes to its Automobile Insurance Manual. Because Wawanesa is only changing rates, and the Manual does not include rates, the Company does not need to file an updated Manual with the Board.

[27] Board staff reviewed the manual on file and did not find any areas where the Company appears to be in violation of the Regulations.

IV FINDINGS

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

[29] 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.

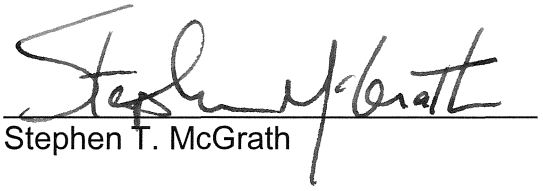
[30] The Board finds the proposed rates are just and reasonable.

[31] The Application included full actuarial indications and qualifies to set the new mandatory filing date for commercial vehicles for the Company to February 1, 2022.

[32] The Board approves the effective date of June 1, 2019, for both new and renewal business.

[33] An Order will issue accordingly.

DATED at Halifax, Nova Scotia, this 19th day of March, 2019.



Stephen T. McGrath