DECISION

2018 NSUARB 171
M08547

NOVA SCOTIA UTILITY AND REVIEW BOARD

IN THE MATTER OF THE INSURANCE ACT

- and -

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

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

APPLICANT: **TD INSURANCE GROUP**

FINAL SUBMISSIONS: July 19, 2018

DECISION DATE: **September 11, 2018**

DECISION: **Application is approved as modified.**

I INTRODUCTION

[1] TD Insurance Group (TD/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 for the three companies within the TD Insurance Group of Companies: Security National Insurance Company, Primmum Insurance Company, and TD Home and Auto Insurance Company. The Application, dated February 8, 2018, was filed electronically on February 9, 2018, and the original documents were received on February 23, 2018.

[2] Given the extent of the indicated changes in the Application, Board staff engaged Oliver Wyman (OW), the Board's consulting actuaries, to complete the review of the application. Board staff provided access to the electronic application to OW on February 27, 2018.

[3] On March 14, 2017, OW sent its first information request (IR) to TD. The Company responded on April 10 and 18, 2018. In the interim, on March 20, 2018, TD amended the Application to include the adoption the 2018 Canadian Loss Experience Automobile Rating (CLEAR) to assign rate groups to Accident Benefits and physical damage coverages. At the request of OW, TD also provided supporting loss development data on April 23, 2018. OW sent follow-up questions to TD on May 1, 2018. After amending the Application on May 24, 2018 to change the overall proposed rate change, TD provided its response to the second IR on May 30, 2018. OW sent a final IR on June 11, 2018 and received the TD response on June 12, 2018. At that point, there was

sufficient information to allow OW to complete its report. OW provided its report to Board staff in its final form on June 26, 2018.

[4] Board staff also prepared IRs which were sent to the Company on March 16 and June 28, 2018. Responses were received by the Board on April 3 and June 28, 2018.

[5] As a complement to the OW report, and as a result of a review by Board staff, a staff report dated July 4, 2018 (Staff Report), along with the OW report, dated June 26, 2018, was prepared and provided to the Company for review on July 4, 2018. The Company provided comments on July 16, 2018. OW and Board staff responses to the TD comments, including a revised Staff Report, were provided to the Company on July 18, 2018. TD provided its final comments on July 19, 2018.

[6] The Board did not deem it necessary to hold an oral hearing on the Application.

II ISSUE

[7] 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

[8] 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*). While the Company had a mandatory filing deadline of October 1, 2018, the Application included full actuarial indications and the required analysis of its territorial indications that a mandatory filing must include. It qualifies, therefore, to reset the mandatory filing deadline for these vehicles to February 1, 2020.

[9] The original proposed effective date was changed to December 1, 2018, for both new business and January 1, 2019, for renewal business.

Rate Level Changes

[10] The Company proposed to change its rates and risk-classification system, which are uniform by territory but not by coverage, that results in an overall all-coverages combined increase of 7.5% for the group. Board staff advises that the proposed rate changes are before the application of a premium dislocation cap. The application of the cap reduces the overall change to an increase of 7.3%, instead of the uncapped 7.5% increase. The different volumes of business of the three respective companies give rise to different uncapped changes.

[11] The Company proposed the adoption of the 2018 CLEAR Table approved by the Board for use in the Province. The Company also proposed the introduction of the new Client Assessment rating variable.

[12] OW reviewed the rate level indications developed by TD Insurance Group, and in doing so, examined all aspects of the rate-making procedure. The following are the changes to the key assumptions in TD Group's rate Application that OW suggested:

- Selection of loss development factors excluding Unallocated Loss Adjustment Expense (ULAE);
- Use of the Board Guideline trends using December 2016 based report;

- Use of equal weights for the five accident years in the experience period;
- Use of ULAE provision based on Nova Scotia, not country-wide, experience;
- Treatment of Health Services Levy as fixed expense, instead of variable;
- Use of a 10% after-tax return on equity instead of the selected 12%;
- Use of expense provision based on TD experience instead of industry average; and
- Use of net trend rate as the complement of credibility.

Loss Development Factors

[13] When determining the factors used to bring reported losses to their expected ultimate level, TD uses an approach that includes a provision for unallocated loss adjustment expenses (ULAE) with its losses and allocated loss adjustment expenses.

[14] OW requested TD to provide rate indications by selecting its estimate of ultimate losses without including a ULAE provision, as is normal practice. These indications produced an overall indicated change that was almost 5 percentage points lower than the TD indications.

[15] The Board accepts the OW recommendation to remove the ULAE provision when selecting the ultimate loss amounts.

Loss Trends

[16] TD selected its loss trends based upon its own experience through October 31, 2016. These loss trends are higher than those selected by OW using data through December 2016 for Bodily Injury and Accident Benefits. For remaining coverages, the trends are close or below the OW selections.

[17] OW expressed concerns that:

- the TD trend selections were based upon ultimate losses that reflected a ULAE provision, as discussed earlier;

- the TD data may not be sufficiently credible for determining loss trends, particularly for the two coverages with the large differences (e.g., Bodily Injury and Accident Benefits); and
- the TD loss trend selections implicitly include a provision for the changing mix of business that is mismatched with the premium trend rates that do not include such a provision.

[18] TD explained that one of the reasons for the higher loss trends is that its volume of business is growing and changing in nature. Loss trend rates implicitly include changes in the portfolio mix of business. For the industry, whose data OW uses, there is little such impact on loss trend rates as the change in mix is relatively small year to year. However, for TD, the Company portfolio has been changing materially over the last few years and the impact is, therefore, more material. OW argues however, that not including a similar change in mix within the premium trend assumptions results in a mismatch that should not exist.

[19] TD further argued that it has written a large portion of its business within a specific territory and for a certain driving experience group that results in higher claims experience. Not being able to reflect this experience in its indications via trends would jeopardize the Company's ability to properly charge for its risks.

[20] TD implemented changes in its last application to address the concerns with the concentration of risks in a specific driving experience group. These changes would account, in part, for some of the changing nature of the portfolio mix and should direct the mix closer to that of industry.

[21] TD did provide indications using the OW loss trend selections based upon its report using data through December 2016. The indication declined by almost 7 percentage points.

[22] The Board accepts the OW recommendation to use its industry-based loss trends, using data through December 2016.

Experience Period Weights

[23] TD selected experience period weights that were based upon adjusted earned premium. This approach implies increasing weights for the most recent accident years.

[24] OW expressed concern about the reasonableness of this approach for a growing portfolio. Given the uncertainty over the ultimate loss amounts for more recent years, OW recommended the use of equal weights to each of the five accident years used by TD. This approach would be more balanced in the circumstance.

[25] The Board accepts the OW recommendation and requires TD to use equal weighting of the five accident years when developing its indications.

Unallocated Loss Adjustment Expense

[26] TD based its assumption for ULAE on the ratio of its country-wide all lines of business (including personal property) paid ULAE to paid loss data for 2016.

[27] OW objected to the use of the country-wide all lines basis for ULAE and instead suggests the Board require the use of the ratio for Nova Scotia (NS) private passenger automobile ULAE as reported to the General Insurance Statistical Agency (GISA) for the Financial Information Reports for the years 2014-2016. While the NS factors are more volatile, they are consistently lower than the country-wide all lines based ULAE.

[28] The Board requires TD to use the NS private passenger automobile ULAE for 2016 instead of the country-wide all lines ULAE when developing its indications.

Health Services Levy

[29] TD treats the Health Services Levy (including the volunteer fire fighter levy) as a variable expense.

[30] The Board, on advice of OW, and after reviewing other jurisdictions' approaches, requires the Health Services Levy to be treated as a fixed expense. The Board, therefore, requires TD to treat the levy as fixed expense when developing its indicated rate level needs.

Expense Provision

[31] TD uses an expense provision based upon the industry-wide 2016 average expense (28.3%) as reported by GISA. The Company then splits this between variable and fixed expense, with the fixed expense portion being assigned solely to Bodily Injury.

[32] OW argues the Company should include a provision for expenses that reflects its own expense costs and not those of the industry. TD expenses are much lower than the industry average reflecting how the Company conducts business, and this should be included in the premiums TD charges. OW also suggests the fixed expenses should be allocated across all coverages.

[33] After correcting the Company's own expense ratio to reflect the proper 4% premium tax, the use of the lower expense provision with fixed expenses allocated to all coverages results in an overall indicated increase that is nine percentage points lower than the TD indications. If the fixed expenses were allocated solely to Bodily Injury as is TD practice, the revised indications are only six percentage point lower (instead of nine).

[34] The Board requires TD to reflect its own actual expense costs when developing its indicated rate level needs. It will however allow the Company to apply the fixed costs to Bodily Injury only as it has done in the past.

Profit Provision

[35] TD uses an after tax-return on equity of 12% and premium-to-surplus ratio of 2:1 in its indications. When combined with the tax rate and the Company's return on surplus assets, the profit provision is about 7.6%.

[36] In recent decisions, the Board required companies to lower the target ROE to 10%. This action was taken because of Board concerns that, as evidenced in part by the release of the 2012 and 2013 General Information Statistical Agency Financial Information report, the industry appears to be earning ROEs well in excess of the 12% the Board believed it was approving.

[37] The 2014 through 2016 versions of these reports show negative ROE for the industry for private passenger vehicles. 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 the 10% ROE for most companies.

[38] Consistent with the last application, the Board requires TD to use a 10% target return on equity, instead of 12%, when developing its indications.

Complement of Credibility

[39] When its claims data is not fully credible, TD assigns the balance of credibility to its prior filing estimate of the projected credibility-weighted loss ratio, adjusted

for the approved rate change. In this manner, TD reflects any rate inadequacy (i.e., difference between indicated rates and approved rates).

[40] OW expressed concerns over the use of this complement of credibility because, in large part, OW did not conduct the review of the last filing. OW uncovered several issues in its review of the current filing that result in a lower overall indicated change. OW observes that had it reviewed the previous filing, similar issues may have been found. The rate inadequacy reflecting the TD indications and approved rates from the last filing, therefore, may be overstated.

[41] OW suggested the Board require TD to use net trend as the appropriate complement of credibility to address the concerns. The use of this approach would significantly reduce the indicated rates. OW noted, however, that despite the OW preference for the use of net trend approach as the basis for the complement of credibility, the Board may find it reasonable to give some consideration of the TD position regarding rate inadequacy from the prior application.

[42] TD expressed concern with the net trend approach, during the IR process, and in its comments on the advisor reports. TD believes there was a large rate inadequacy because it took lower rates than indicated. Use of the net trend method, would ignore this inadequacy and would lead to an underestimation of the indicated rate. It also would not reflect what TD believes to be an ongoing profitability issue, which may lead to affordability and availability concerns.

[43] In the last application, TD proposed, and the Board approved, rates that were much lower than the TD or the Board Staff indicated rates. Based on these observations, the rates were inadequate. If OW had reviewed that application, it may

have found similar issues to those found in this Application. The Board may have viewed such lower indications as appropriate, reducing the rate inadequacy,

[44] The Board recognizes that TD believes the full level of rate inadequacy as measured against its own indications or the Board's indication should be reflected in the complement. Faced with the OW assessment of this Application, the Board accepts, however, that while there may be some level of rate inadequacy in the approved rates, it likely would be lower if OW had reviewed the last application.

[45] The Board, therefore, will allow TD to reflect a level of rate inadequacy in its complement of credibility. That level, however, will be one-half the level of that TD originally included. In the circumstances of this Application, the Board finds this to be a reasonable compromise between the two differing opinions.

Comparison of Proposed Rates to Indicated Rates

[46] Board staff prepared a chart showing the differences between TD and OW indications, noting that the overall proposed increase, before capping, is still well below the OW indicated level.

[47] While the proposed change for Collision is higher than the indications, the opposite is true for all other coverages. In some cases, the difference is quite large. The smaller than indicated overall increase will result in a return on equity that is well below the 10% required in the indications and, possibly, is negative.

[48] Given the Board ordered changes that differ from the OW recommendations for complement of credibility and expense provision (i.e., allowed fixed expenses to be assigned to Bodily Injury only), the Board indications would be higher overall than the OW indicated level and the differences from those indications will be larger.

[49] The Board has concerns about companies taking much smaller increases than indicated. This concern was particularly heightened given the TD indications but is somewhat alleviated with the Board indications being lower than the TD indications. TD has demonstrated this pattern for several filings. Despite this observation, however, Board staff does not believe the Board should step in and force a higher rate change than TD proposed.

[50] Board staff recommended approval of the proposed base rate change, as filed. The Board concurs.

[51] The Board advises TD that it will re-examine this concern in future filings and expects that future increases will move gradually towards indicated levels, rather than moving abruptly to that indicated level, but perhaps in larger increments, if needed.

Other Changes

Territory and Territorial Differential Changes

[52] TD conducted a loss ratio analysis by territory. This approach produces indicated changes for the various territorial relativities for each coverage. TD chose to leave the territorial differentials unchanged despite some indications suggesting changes should be made.

[53] The Board finds that TD has supported the proposal for no changes to its territorial differentials. The Board approves the proposal, as filed.

Adoption of 2018 CLEAR Table

[54] TD currently uses the 2017 CLEAR table to assign rating groups for Accident Benefits and physical damage coverages. The Company uses the CLEAR (AB Alberta & Atlantic) - Collison, DCPD and Comprehensive Separated version of the table.

[55] In this Application, TD proposed the adoption of the 2018 version of this table, which the Board approved for use earlier this year. TD off-balanced the impact of the change of table for Accident Benefits to make it revenue-neutral, as required, but let the impact flow through for physical damage coverages. The Board allows this approach.

[56] TD proposed to continue its Board approved practice of making adjustments for the most recent model years. TD proposed no change to this practice.

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

New Rating Variable

[58] TD proposed the introduction of the new rating variable, Client Assessment which, based on information provided by the client, allows for a different level of discount to be applied to eligible individuals.

[59] OW reviewed the actuarial support provided for this new variable and the proposed differentials. OW found the proposed differentials to be supported.

[60] Board staff also reviewed the new variable and confirmed that it does not involve any prohibited risk classification factors.

[61] Based on the OW and Board staff reviews and recommendations, the Board approves the proposed introduction of this new rating variable, as filed.

Premium Dislocation Cap

[62] TD currently uses a Board approved premium dislocation cap that limits both increases and decreases for each vehicle to +/-15% unless an at-fault accident

occurs. In such a case, the upper bound increases to 40% to allow some impact of the accident to be observed in premium. TD proposed to continue the use of this cap.

[63] TD provided the number of vehicles subject to the cap both before and after it makes the proposed changes. The proposed changes result in a small increase in the number of vehicles with capped premiums. TD believes the vast majority of capped cases will reach true premium at either the first or second renewal, leaving only a few rare cases that will be capped longer (assuming all vehicles stay with TD).

[64] To use negative capping (i.e., limiting the reductions a policy is entitled to), the Board requires that the impact of the negative capping on premium must be less than or equal to the impact on premium of the positive capping. TD indicates that the proposed overall "uncapped" increase of 7.5% becomes an overall increase of 7.3% when the proposed cap is applied. As a result, TD meets the Board negative capping constraint.

[65] Board staff recommends, and the Board approves, the proposed capping, as filed.

Automobile Insurance Manual Review

[66] Board staff reviewed the Automobile Insurance Manual on file, as well as the manual pages provided in the Application. Apart from the concern that will be described below, and after an agreed correction to one of the declination rules (to add a missing "not"), Staff uncovered no areas where the Company appears to be in violation of the *Regulations*.

[67] However, there is an area of concern surrounding the restriction of coverage under Comprehensive, Specified Perils, and All Perils for three or more thefts, which are not at-fault incidents. This appears to violate the *Automobile Insurance Underwriting*

Practice Regulations that prohibits the use of "unsatisfactory claims record if the claims were non-at-fault" as a reason to decline or refuse to renew a coverage.

[68] When asked about this, TD provided the following response:

> The SOI stated, in AutoInsRegsFAQs-20130814, that comprehensive claims are not considered accidents and therefore; the rule mentioned above is not in violation of the prohibited practice 4(2)(d)(iv) "has an unsatisfactory claims record, if the claims record includes any claim resulting from an accident for which the insured, applicant, or other person was not at fault" of the Automobile Insurance Underwriting Practices Regulations.
>
> [Response to question BS-11 of Staff IR-1]

[69] Given this response, Board staff confirmed, with the Superintendent of Insurance's office, that it views theft as a comprehensive claim arising from a not-at-fault incident, and therefore, cannot be used to decline (deny) coverage. As such, the rule violates the *Regulations* and the Board requires TD to remove that rule from the manual.

[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.

IV FINDINGS

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

[72] The financial information submitted by the Company in the original applications 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.

[73] The Board accepts indications reflecting all of the OW suggested changes, modified to allow TD to reflect half of the rate inadequacy in the last application and to allow fixed expenses to apply to Bodily Injury alone, as the target against which to judge

the appropriateness of the TD proposal. These indications will fall between the TD indications and the "Oliver Wyman Indications" as shown on page 13 of the OW report."

[74] The Board approves the proposed changes to base rates, as filed.

[75] The Board approves the proposal to leave territory differentials unchanged, as filed.

[76] The Board approves the proposed introduction of the Client Assessment rating variable, and its associated differentials, as filed.

[77] The Board approves the proposed adoption of the 2018 CLEAR table, and the off-balancing of the impact for Accident Benefits, as filed.

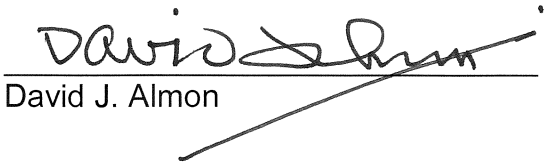
[78] The Board approves the proposed continuation of the premium dislocation cap, as filed.

[79] The Board requires TD to remove the rule restricting coverage based upon the number of thefts to avoid the violation of the *Regulations*.

[80] The Board resets the mandatory filing deadline to February 1, 2020, for these vehicles. The Board approves the proposed effective date of December 1, 2018, for new business and January 1, 2019, renewal business.

[81] An Order will issue accordingly.

DATED at Halifax, Nova Scotia, this 11th day of September, 2018.



David J. Almon