IN THE MATTER OF

INSURANCE CORPORATION OF BRITISH COLUMBIA

REVENUE REQUIREMENTS
FOR UNIVERSAL COMPULSORY AUTOMOBILE INSURANCE
FOR THE POLICY YEAR
COMMENCING EFFECTIVE FEBRUARY 1, 2012

DECISION

August 16, 2012

Before:

A.W.K. Anderson, Commissioner/Panel Chair
M.R. Harle, Commissioner
R.D. Revel, Commissioner

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EXECUTIVE SUMMARY

This Decision relates to an application to the British Columbia Utilities Commission (Commission) by the Insurance Corporation of British Columbia (ICBC) for an increase of 11.2 percent in the rates for universal compulsory automobile insurance (Basic Insurance), for the policy year commencing February 1, 2012.

ICBC states that the rate increase it seeks in the Application is based on two primary factors:

- First, declining interest rates in a period of global economic uncertainty has significantly reduced the yield that ICBC is obtaining on invested premiums collected and Basic equity. Therefore, there is relatively less investment income available than in past years to offset rising claims costs;
- Second, lCBC's bodily injury claims costs continue to increase, with the main change from past years being higher claims frequency.

On November 30, 2011, the Lieutenant Governor in Council issued Order in Council No. 560 approving the November 25, 2011 Letter of Direction issued by the Minister of Public Safety and Solicitor General to ICBC regarding ICBC's use of Basic capital to bring greater stability and predictability in Basic Insurance rates. The Letter of Direction requires ICBC to modify its determination of the Minimum Capital Test (MCT) ratio and alter its Basic Insurance Capital Management Plan. The Commission is required to recognize and accept government directives to ICBC when regulating and fixing Basic Insurance rates. These changes had to be fully considered in the Panel's deliberations and findings regarding the Application.

Several key issues emerged during the proceeding. These are addressed in the Decision and include:

- The selection of the most appropriate forecasting model to use for determination of the updated loss cost variance for the 2010 policy year;
- Forecasting the appropriate New Money Rate to use for estimating investment income and premium financing plan revenue; and
- Consideration of the impact of *Special Direction IC2* and the MCT ratio requirements.

After considering the evidence and arguments of all parties, the Commission Panel approves an 11.2 percent Basic Insurance rate increase for the Policy Year 2012, commencing February 1, 2012.

1.0 INTRODUCTION

1.1 The Application and Approvals Sought

On December 1, 2011, Insurance Corporation of British Columbia (ICBC) applied for approval of an 11.2 percent increase in universal compulsory automobile insurance (Basic Insurance) rates for the policy year commencing February 1, 2012 (PY 2012) pursuant to sections 59 to 61 of the *Utilities Commission Act*, R.S.B.C. 1996 c. 473, as amended, and the *Insurance Corporation Act*, R.S.B.C. 1996, c.228, as amended (the Application). ICBC states that the proposed Basic Insurance rates were developed in accordance with accepted actuarial practice (AAP) and reflect the forecasted increase in costs of providing Basic Insurance in PY 2012. ICBC states that the proposed rates are just and reasonable and that they should be approved as sought. (Exhibit B-1, Chapter 1, p. i) As set out in Order G-221-11 (Exhibit A-3), the Application seeks the following three approvals:

1) Approval for a permanent 11.2 percent increase in Basic Insurance rates, to apply:

    i. to all new and renewal policies with an effective date on or after February 1, 2012 that have: (i) premiums determined through the use of the Schedule of Basic Insurance Premiums (Schedule C) as filed with the Commission, excluding rate classes 800 and 900 – 906 and excluding policies relating to vehicles located on isolated islands; and (ii) premiums determined under a Fleet Reporting Policy, (together the Plate Owner Basic and Fleet Reporting Policies);

    ii. to all new and renewal policies other than the Plate Owner Basic and Fleet Reporting Policies effective on the first day of the first month that is at least 60 days following the Commission's final decision on the Application;

2) Interim relief, pursuant to section 89 of the *Utilities Commission Act* and section 15 of the *Administrative Tribunals Act*, to allow a rate increase of 11.2 percent to apply on an interim basis for all new and renewal Plate Owner Basic and Fleet Reporting Policies with an effective date on or after February 1, 2012, pending the hearing of the Application and orders subsequent to that hearing;

3) If the Commission's final decision determines that a portion of the interim increase should be refunded, any refunds be dealt with in the manner set out in Appendix A to the Application.

1.2 Key Participants

The proceeding was initiated as a combined written and oral hearing, subsequently changed to a written hearing only. In addition to the Applicant, ICBC, there were fifteen registered Interveners, of which two withdrew. ICBC and the following seven Interveners filed Final Argument:

- Automobile Insurance Committee of the Canadian Bar Association (AIC);
- Canadian Direct Insurance (CDI);
- Insurance Bureau of Canada (IBC);
- Pemberton Insurance Corporation (Pemberton);
- Frank Duck;
- Voice for Economic Justice (VEJ); and
- British Columbia Old Age Pensioners Organization (BCOAPO).

ICBC also filed Reply Argument.

1.3 Overview of the Decision

Section 2 of this Decision overviews the legislative authority and legal context of the Decision. It also addresses issues related to the attempted introduction of new materials into the proceeding through Arguments.

Section 3 discusses the eight components comprising the PY 2012 Indicated Rate Level Change:

- PY 2010 Loss Cost Forecast Variance;
- Loss Trend to PY 2012;
- Investment Income and Premium Financing Revenue;
- Impact of International Financial Reporting Standards;
- Operating Expenses;

- Capital Provision;
- Trend in Average Premium;
- Other.

Section 4 describes Claims Initiatives;
Section 5 addresses Performance Measures;
Section 6 discusses Road Safety;
Section 7 discusses Other Matters;
Section 8 provides the Panel's Conclusion.

The Panel has considered and weighed the evidence and arguments of all parties participating in the Proceeding. The Panel has concluded that the requested increase is needed to enable ICBC to have the best opportunity to meet two competing requirements of *Special Direction IC2*: (1) achieving or maintaining its required MCT ratio, and (2) phasing rates in a way that they remain relatively stable and predictable for PY 2012.

2.0 APPLICABLE LEGISLATIVE AND LEGAL CONTEXT

2.1 Legal Context

ICBC is governed by the *Insurance Corporation Act* and Regulations. ICBC is also subject to specific sections of the *Utilities Commission Act*. As a Crown corporation, ICBC is subject to legislation applicable to all Crown corporations, such as the *Budget Transparency and Accountability Act*, the *Financial Information Act*, the *Financial Administration Act*, and the *Freedom of Information and Protection of Privacy Act*. In addition, ICBC has administrative and other duties and obligations under various motor vehicle related acts and regulations, such as the *Motor Vehicle Act*, the *Commercial Transport Act*, the *Motor Vehicle (All Terrain) Act*, and the *Social Service Tax Act*.

Basic Insurance rates must be determined within the legislative context applicable to Basic Insurance. *Special Direction IC2* to the BC Utilities Commission*, BC Regulation 307/2004*, as amended, (*Special Direction IC2*) is particularly relevant. (Exhibit B-1, Letter, p. ii)
Among the provisions of *Special Direction IC2* that are relevant to this Application are:

- Subsection 3(1)(b) provides that the Commission must set rates for Basic Insurance that allow ICBC to maintain capital available in relation to its Basic Insurance business equal to at least 100 percent of the Minimum Capital Test (MCT) ratio.
- Subsection 3(1)(c) provides that subject to paragraphs (c.1) and (e), for each year that the Commission fixes Basic Insurance rates, the Commission must fix those rates on the basis of accepted actuarial practice so that the rates allow ICBC to collect sufficient revenue to pay certain identified costs and to achieve or maintain the capital required.
- Subsection 3(1)(c.1) provides that the Commission must, when regulating and fixing Basic Insurance rates, regulate and fix those rates in a manner that recognizes and accepts actions taken by ICBC in compliance with government directives issued to ICBC.
- Subsection 3(1)(e) provides that the Commission must ensure increases or decreases in Basic Insurance rates are phased in in such a way that those rates remain relatively stable and predictable.

The Lieutenant Governor in Council approved Order in Council No. 560 on November 30, 2011 approving a government directive of November 25, 2011, regarding ICBC's use of Basic Insurance capital and to bring greater stability and predictability in Basic Insurance rates (the 2011 government directive). The 2011 government directive is important in the context of this Application for two reasons:

(1) it requires "… for the purposes of applying the terms of the May 2010 direction letter, ICBC is to hereafter use the most recent quarter Basic insurance MCT level to determine the Basic insurance revenue requirements, rather than using the MCT at the end of the previous calendar year"; and

(2) it directs that "… notwithstanding the May 2010 letter, ICBC is directed to alter its Basic insurance Capital Management Plan to exclude any capital build provision in Basic insurance rates from February 1, 2012 to January 31, 2015, provided that Basic capital remains above the regulatory minimum." (100 percent of the MCT ratio)

The impact of the 2011 government directive is discussed in following sections of this Decision.

2.2 The Introduction of New Materials through Final Submissions

In the course of this proceeding, issues arose with respect to the admissibility of late evidence which AIC requested permission to file. The AIC request was rejected by the Commission for the reasons given in Exhibit A-10. The matter has resurfaced in the form of AIC's Argument and ICBC's Reply Argument.

ICBC's Reply Argument submits that "It is apparent that AIC has included in its Submission the evidence that the Commission recently ruled was to be excluded from the record. The AIC Submission provides new analysis of data that was never put to ICBC in IRs. It quotes selectively from academic writings that are not in the record, and in some cases the quotes have been taken out of context. It quotes from, and cites, evidence from prior applications that is not in the evidentiary record of this proceeding. The author's qualifications to opine on actuarial matters have not been established. The Commission's rationale for excluding the AIC evidence had included the potential prejudice to ICBC from admitting intervenor evidence so belatedly. The introduction of that evidence "via the backdoor" in counsel's submissions only magnifies the prejudice. ICBC disagrees with much of what AIC has stated, but is hamstrung in responding at this stage by the fact that ICBC never had an opportunity to see AIC's arguments during the proceeding and file evidence in rebuttal. ICBC submits that the Commission should disregard significant portions of the AIC Submission on that basis alone." (ICBC Reply, p. 14)

ICBC does address a number of the points raised in AIC's argument, but concludes with the submission that "The Commission should disregard, or alternatively give no weight to, AIC's submissions on loss cost forecasting generally." (ICBC Reply, p. 16)

2.2.1 Commission Determination

As ICBC notes in Reply, the Commission rejected AIC's request to submit late evidence for the reasons set out in Exhibit A-10. The Panel concurs with ICBC's submissions in response to AIC's attempt to introduce new evidence through its argument. In the interests of natural justice and fairness, the Panel gives no weight to AIC's submissions with respect to loss cost forecasting which are based on the attempt to introduce new evidence.

3.0 PY 2012 INDICATED RATE CHANGE

ICBC's PY 2012 Indicated Rate Change of 11.2 percent represents the increased Basic Insurance revenue that ICBC states it requires in order to pay for expected future costs. In terms of premium, it is the average percentage change to the current Basic Insurance policy premium that is needed to generate the required revenue for PY 2012.

ICBC states that in order to cover its forecast costs, it will require total premium revenue for PY 2012 (commencing February 1, 2012) of $2.232 billion, $234 million more than it expects to receive based on the rates in effective prior to February 1, 2012.

The required revenue for PY 2012 is determined by ICBC in accordance with accepted actuarial practice in Canada (AAP), and is certified by the Filing Actuary and a Reviewing Actuary that it is in accordance with AAP. (Exhibit B-1, pp.3-1 – 3-3)

Chapter 3 of the Application describes the Actuarial Rate Level Indication in substantial detail, and was the subject of extensive Information Requests by the Commission and Interveners.

The impact of the primary components of the indicated rate change, expressed as percentage point(s) of the total 11.2 percent rate increase are summarised in the following table.

Table 3.1

Line No.	Components	Impact (percentage points of PY 2012 indicated) rate change)
1	PY 2010 Loss Cost Forecast Variance	+5.5
2	Loss Trend to PY 2012	+1.9
3	Investment Income and Premium Financing Plan Revenue	+2.5
4	Impact of IFRS changes	+0.4
5	Operating Expense (excluding IFRS changes)	+0.0
6	Capital Provision	+0.3
7	Trend in Average Premium	+0.4
8	Other	+0.2
9	**PY 2012 Indicated Rate Level Change**	**+11.2**

(Source: Exhibit B-1, Figure 3.2, p. 3-3)

The first three components account for 9.9 percentage points of the total Indicated Rate Change of 11.2 percent:

• PY 2010 Loss Cost Forecast Variance	5.5 percentage points
• Loss Trend to PY 2012	1.9 percentage points
• Investment Income and Premium Financing Revenue	2.5 percentage points
Total of three components	9.9 percentage points

In order to determine the approved level of rates for PY 2012, in addition to examining the various components of the actuarial analysis and related forecasts, the Commission must consider legislative and regulatory requirements, including the recent Order of the Lieutenant Governor in Council No. 560 approving the November 25, 2011 Letter of Direction issued by the Minister of Public Safety and Solicitor General to ICBC. The Commission is required to recognise and accept the Letter in accordance with *Special Direction IC2*. The impact of that Letter is discussed in Section 3.5.3 of this Decision.

The following parts of this Section 3 discuss the components comprising the 11.2 percent average Basic Insurance rate increase.

3.1 PY 2010 Loss Cost Forecast Variance

The PY 2010 Loss Cost Forecast Variance of +5.5 percentage points represents the difference between the originally expected PY 2010 loss costs and the updated forecast based on actual costs being incurred with respect to that Policy Year. (ICBC Final Argument, p. 16) ICBC states that main factors contributing to the rate increase are lower interest rates and rising Personal Bodily Injury (BI) claims costs, mainly due to higher than forecast BI frequency. (Exhibit B-1, pp. 2-1, 3-7)

The 2010 Personal BI loss cost forecast comprises frequency and severity elements, with the frequency element having the largest impact on the PY 2010 Loss Cost Forecast Variance. ICBC states that increased variability of historical data, attributed to the impact of the recent economic recession and precipitation levels, has added uncertainty in future forecasts.

ICBC submits that the exercise undertaken by the actuaries is one of forecasting claims costs for the future policy year, not of finding a trend that best describes or fits past data. In statistical terms, a model used for forecasting must necessarily be a predictive model, as opposed to merely a descriptive model, in order to estimate future costs according to AAP. An actuary applying AAP must select appropriate methods, techniques and assumptions, giving consideration to changes in the social and economic environment, trends over time, and the distribution of the business, among other relevant factors. Reliance on simple statistical measures, without sufficient regard for relevant social and economic factors, can lead to poor results. (ICBC Final Argument, pp. 22, 23)

While the Interveners took no issue with this assertion itself, the methods, techniques and assumptions, including the selection of an appropriate model used by ICBC in developing its prediction for PY 2012 have been questioned by Interveners, particularly with respect to Personal BI frequency.

ICBC also states:

> ICBC's actuaries have applied accepted actuarial practice (AAP) to arrive at a best fit trend line for loss costs. The loss cost trend to PY 2012 was based on detailed analysis by coverage and separately for frequency and severity. (ICBC Final Argument, p. 21)

and:

> ICBC also submits that as actuaries are required to exercise judgement in the development of models for forecasting purposes, two different actuaries may develop different but equally valid models that accord with AAP. Models that do not reflect the more normal conditions expected in the forecast period will, in ICBC's submission, produce estimates for PY 2012 that are biased, and are not consistent with AAP. (ICBC Final Argument, p. 24)

3.1.1 Personal BI Frequency Models

ICBC's evidence includes testing the selected model for Personal BI Frequency. ICBC selected a 12-year exponential model using 48 data points up to 2008 Q1, but excluded data points beyond that date. (Exhibit B-6, 2012.1 RR AIC.12.1 – Attachment C)

ICBC submits that BI frequency has returned to the long-term trend line after more favourable experience in 2008 and 2009 and that the use of long-term pre-2008 trend line for BI frequency is justified based on:

- The causes of the favourable experience in 2008 and 2009; and
- The fact that frequency returned to the long-term trend in 2010, and has since remained at levels higher than the long-term trend.

  (ICBC Final Argument, p. 25)

ICBC's Application was based on its determination that a 12-year exponential model (1997 – 2008-Q1) for Personal BI Frequency was the best fit trend line for the purpose of forecasting based on the data.

ICBC states that it "...responded to a number of IRs that proposed the use of a variety of other models for determining BI frequency and loss costs. The suggested models have in common that they give weight to 2008 and 2009 data to reduce the actuarial rate indication. These models are either not consistent with AAP, or do a poor job in describing the claims experience since 2010. ICBC is in its third year of experiencing claims frequency near or above the pre-recession long-term trend line. Selecting a model for BI frequency that gives weight to anomalous data points will result in a trend that may represent a plausible outcome, but is not a reasonable estimate for the expected value." (ICBC Final Argument, pp. 28, 29)

An alternative 11-year econometric model of Personal BI Frequency, based on ICBC's approved Streamlined Revenue Requirements Application (SRRA) 2010 model, was requested through

Information Requests. The explanatory variables in the 2010 SRRA model were GDP growth, the proportion of the BC population aged 55 to 74, and total precipitation. The 11-year econometric model uses the same explanatory variables and starts from the first quarter of 2000, but ends in the fourth quarter of 2010. The 11-year econometric model would have an impact of -3.7 percentage points on the Basic Insurance actuarial rate indication. (Exhibits B-7, 2012.2 RR BCUC.150.1; Exhibit B-13, 2012.CP RR BCUCP.5.1)

The Personal BI frequency issue was further explored through Panel Information Requests. In its responses, ICBC introduced evidence to demonstrate that the key issue of the increase in the number of injury claims in 2010 was not limited to BC but is prevalent across the country. ICBC also provided information from the State of Washington where some insurers are using shorter term trends starting in 2008 to forecast BI frequency to capture higher premiums to offset increasing costs. (Exhibit B-13, 2012.CP RR BCUCP.4.2.3)

Panel IR 2012.CP RR BCUCP.5.2 further explored the 11-year econometric model and its -3.7 percentage point impact on the Application's 11.2 percent Basic Insurance Indicated Rate Change.

ICBC's response contends that the 11-year econometric model does not describe well the most recent accident year 2011 and it produces a forecast that is significantly lower than the pre-recession trend line despite the evidence that frequency levels have returned to the long-term trend line. The ICBC response also states that the application of accepted actuarial practice based on the data and circumstances at hand led ICBC actuaries to propose the selected model.

ICBC's response further discusses the impacts of the 11-year econometric model, and concluded with the statement: Even with the adoption of an 11.2% Basic Insurance rate increase, ICBC is expecting an adverse forecast variance to emerge for PY 2012, which has implications for the actuarial rate indication for PY 2013. The low end of the estimated 2012 range for BI claims frequency suggests an adverse forecast variance of about 3%, while the high end of the range suggests an adverse forecast variance of about 9%. Even the forecast variance of 3% that would occur at the low end of the range would put ICBC very near to the statutory minimum capital requirement of 100% MCT. (Exhibit B-13, 2012.CP RR BCUCP.5.2)

3.1.2 Personal BI Severity Models

The Application explains that, in addition to claims frequency, the other potential source for the PY 2010 loss cost forecast variance impact is claims severity and notes that the severity of BI claims is rising over time, but the PY 2010 severity has emerged near to the levels forecast in the 2010 Application. ICBC comments that the emergence of claims costs in 2010 resulted in a slight increase to the Basic BI severity which has an unfavourable, but modest, impact on the PY 2012 rate indication. (Exhibit B-1, p.3-12)

ICBC has selected a 6.25 year exponential model to keep the experience period starting year at 2005. (Exhibit B-1, Exhibit D.0, p. 9)

3.1.3 Intervener Submissions on ICBC's Forecast Models

3.1.3.1 AIC

AIC's argument with respect to loss cost forecasting is based upon new evidence that AIC sought to introduce through Final Argument. In Section 2.2 of this Decision, the Panel notes that in Exhibit A-10 it had previously rejected AIC's request to submit late evidence and concludes it will give no weight to that evidence for reasons of natural justice and fairness.

3.1.3.1.1 ICBC Reply

Notwithstanding its position on AIC's argument in general, ICBC addresses what it describes as the " 'five key points' made by AIC to the extent it is possible to do so within the proper parameters of the evidentiary record." ICBC's description of and responses to AIC's 'five key points' are summarized as follows:

1. AIC: complex models with explanatory factors are preferable to simple models with time.
   ICBC: many different factors may influence claims frequency or severity, and the relationships among the factors are often too complex for the types of models advocated by AIC to yield better results than simple exponential models;

2. AIC: ICBC's adjustments have increased forecast variance.
   ICBC: Making predictions, as opposed to undertaking descriptive modelling, demands that models be updated, revised, and refined as new data and information become available;

3. AIC: ICBC's models produce point estimates rather than a range of values, making it difficult to assess uncertainty and reliability.
   ICBC: AIC's argument is based on one author's view, which has not been shown to be authoritative within the domain of AAP. Only the estimate of the theoretical mean - a point estimate - is the best estimate of the quantity being estimated;

4. AIC: ICBC's models do not appear to have been tested.
   ICBC: AIC's statement is wrong. For example, ICBC has tracked the variances of its Basic loss cost forecasts;

5. AIC: ICBC's claim costs are to a large degree within ICBC's control . . . the increase could be caused by management edicts.
   ICBC: There is no evidence to support AIC's speculation.

   (ICBC Reply, pp. 15, 16)

3.1.3.1.2 Commission Determination

The Panel finds ICBC's responses to AIC's 'five key points' to be supported by ICBC's actuarial evidence which has been calculated in accordance with accepted actuarial practice in Canada, as certified by both the filing and reviewing actuaries. (Exhibit B-1, pp.3-33, 34) The Panel further finds that there is no actuarial or other evidence on record to which any weight can be given with respect to AIC's submissions on loss cost forecasting, for the reasons given in Section 2.2.

3.1.3.2 BCOAPO

BCOAPO submits that "The largest single component of the of the proposed 2012 rate increase (+5.5%) arises out of ICBC's AAP-compliant, yet clearly inaccurate forecast in its 2010 Streamlined Revenue Requirement Process. The large forecast variance for 2010 was apparently "not unexpected" because of the higher-than-usual amount of uncertainty associated with the BI frequency trends emerging in 2008/2009. With the greatest of respect, this position seems at odds with the insurer's position in 2010, when there was no hint of uncertainty in their Revenue Requirements Application." (BCOAPO Argument, p. 4)

3.1.3.2.1 ICBC Reply

ICBC takes issue with BCOAPO's submission that loss cost variance was 'not unexpected' and notes that "Variances are inevitable when forecasting." ICBC also notes in reply that the Commission, in its 2010 SRRA Decision stated '[t]he actuarial rate indication is based on estimates of future costs, and accordingly there will likely be a variance between forecast and actual costs in a test period' and noted that ICBC's Basic Insurance operates in a closed system. ICBC states "In the 2010 SRRA, ICBC was comfortable that the approach it had taken to forecast loss costs was the right approach for reducing the chance of significant variances in PY 2010 ICBC has used a similar approach in the current Application to minimize the potential forecast variance in 2013." (ICBC Reply, p. 8)

3.1.3.2.2 Commission Determination

The Panel acknowledges BCOAPO's concern in questioning the accuracy of ICBC's forecasting for its 2010 Application. The Panel concurs with the Commission's view in its 2010 SRRA Decision (Section 3.1.3.2.1 above) that, by their very nature, variances between forecast and actual costs are expected. The quantum of the variance in this instance is disturbingly high, even taking into account the extended period between Applications.

3.1.3.3 IBC

IBC submits that, while the requested rate increase may be justified on an actuarial basis, ICBC has done a poor job of explaining what factors are driving claims costs and the associated rate increase. IBC submits that ICBC is focused on economics and weather in the 2012 filing, but is aware of the numerous other factors that affect frequency as in the response to 2012.2 RR IBC.35.1 and should have access to data regarding these other factors. IBC's view seems to be that ICBC should access and use the available data to provide clearer explanations regarding what is driving claims costs. IBC also submits that ICBC's statements regarding the impact of economics and weather are not properly supported. (IBC Final Argument, pp. 2, 3)

3.1.3.3.1 ICBC Reply

ICBC responds to IBC's submissions respecting how ICBC uses its internal data to explain historic trends with examples of the use of internal data such as increased injury frequency to cyclists and pedestrians, and notes that it had to rely on external data on weather, vehicle traffic and economic forecasts to provide support for historical analysis and selecting trends. (ICBC Reply, pp. 7, 8)

3.1.3.3.2 Commission Determination

The Panel considers that the evidence respecting the use of internal and external data provided by ICBC through its Application and responses to Information Requests adequately supports the Application. The Panel does encourage ICBC to seek effective ways to improve the transparency of information in order to assist external stakeholders in understanding the reasons for its rate changes.

3.1.3.4 CDI

CDI submits, with respect to ICBC's loss cost variance component, that ICBC's projections seem to have been overly optimistic in applying an indicated rate change impact of -5.2 percentage points from the PY 2007 Loss Cost Forecast Variance to PY 2010. This appears to have been based primarily on a perceived flattening of Basic loss costs over previous years, even though these included rate increase years. (CDI Argument, p. 3)

3.1.3.4.1 ICBC Reply

ICBC says that it does not understand CDI's statement (above), and submits that the PY 2007 loss cost forecast variance that was included in the PY 2010 rate indication was primarily a comparison between a past (2007) forecast and updated estimates to 2010 based on known claims data that had emerged since the 2007 revenue requirements application. CDI's references to "optimism" and "perceived flattening" make little sense in the context of an assessment of a loss cost forecast variance based primarily on known claims data. (ICBC Reply, p. 10)

3.1.3.4.2 Commission Determination

The Panel agrees with ICBC's Reply to CDI, and finds that the CDI comments are not supported by any evidence relevant to the determination of the PY 2010 Loss Cost Variance in this Application.

3.1.3.5 Pemberton

Pemberton argues that

- "...the issue [in the Application]...is not whether a prior year variance was incurred, but instead how that amount is accounted for, and how the incidence of variance is borne";
- "retrospective rating is not a normal practice in the general insurance industry. General insurers practice prospective premium rating principles"; and

"...this PY 2010 Loss Cost Forecast Variance (+5.5 percentage points) portion of the Applicant's application is neither just nor reasonable to the rate payer, and that it be denied by the British Columbia Utilities Commission." (Pemberton Argument, pp. 2, 3)

3.1.3.5.1 ICBC Reply

ICBC replies that including a loss cost forecast variance in the rate indication is a normal part of actuarial ratemaking and is consistent with AAP and not an exercise in retroactive rate making, ICBC states that the PY 2012 rate indication does not include any provision to recoup the shortfall for PY 2010 and is set at the cost level expected for the PY 2012 policies only, which is arrived at by starting with the re-estimated PY 2010 loss costs and increasing them by the estimated increase in claims costs of 1.9 percent, in essence an adjustment to the starting point for the trend. (ICBC Reply, pp. 9, 10)

3.1.3.5.2 Commission Determination

Pemberton's argument seems to suggest that ICBC is seeking to recover the shortfall for additional premiums that should have been charged for PY 2010 had ICBC been able to accurately forecast the future loss costs to date for the 2010 Policy Year. The Panel understands ICBC's explanation in Reply to mean that, had the PY 2010 rates been set to reflect what is now considered the trend in loss costs based on 2012 forecasts, the rates would have reached the level now requested by the implementation of the 5.5 percentage point increase to the rates put into effect for PY 2010. The shortfall in PY 2010 premiums has been funded from capital and has been a factor in the significant decrease in the MCT ratio since 2010. The PY 2012 premiums will be set to recover only the loss costs, based on current forecasts, for loss claims incurred in the PY 2012 premium duration period. The Panel rejects the Pemberton submission as it is based on a misunderstanding of the purpose and use of the PY 2010 Loss Cost Forecast Variance component of the PY 2012 Indicated Rate Change.

3.1.4 Summary Commission Discussion and Determination: PY 2010 Loss Cost Forecast Variance

The key issue surrounding the determination of the PY 2010 Loss Cost Variance is ICBC's selection of a 12-year exponential model for computing Personal BI frequency. The model selected by ICBC uses data for a period ending Q1, 2008 rather than, for example, using an 11-year econometric model based on the years 2000 through 2010. (Exhibit B-7, 2012.2 RR BCUC.150.1)

Resolving the selection of an appropriate PY 2010 Loss Forecast Variance factor requires careful consideration, particularly with respect to the alternative BI Frequency models brought forth in evidence. The Loss Cost Forecast Variance factor selection must also be considered in concert with the need to balance it with other necessary and in some cases competing factors, including the legislative and regulatory requirements to ensure that rates are relatively stable and predictable, determined in accordance with Accepted Actuarial Practices, and comply with the Minimum Capital Test limit.

The Panel is concerned about the volatility of the major components of the Indicated Rate Change. The most current evidence on record in this Application indicates a +1.1 percentage point higher PY 2010 Loss Cost Forecast Variance and Loss Trend factors than that used in the Application. The latest New Money Rate and Yield on Basic Equity indicates an additional +1.9 percentage points over the rate used in the Application. Taken in isolation, this updated evidence suggests a need for an even higher rate increase than the 11.2 percent requested in the Application.

If the updated forecast indications prove to be accurate, and the Application is approved as originally requested at 11.2 percent, there will be another revenue shortfall and a corresponding drop in the MCT ratio. The result will likely be a need for a further rate increase in the near future in order to mitigate the risk of ICBC's MCT ratio falling below the regulatory minimum and jeopardising the financial solvency and stability of the Basic Insurance business.

On the other hand, a further increase above the rates requested in the Application would further challenge the requirement to phase rate changes in such a way that the rates 'remain relatively stable and predictable.'

The Panel has considered the question of the selection of an appropriate model for the purposes of forecasting Personal BI frequency. ICBC's evidence is that the 12-year exponential model used in developing the 11.2 percent rate increase underestimates recent experience. Even with the 11.2 percent increase, ICBC is expecting an adverse forecast variance for PY 2012. Even the low end of the updated forecast range would put ICBC very near the minimum 100 percent MCT ratio. (Exhibit B-13, 2012.CP RR BCUCP.5.2) Determining the PY 2012 Indicated Rate Change by using the 11-year econometric model scenario, indicating a 3.7 percentage point decrease in the requested rate change would increase the risk of falling below the 100 percent minimum MCT ratio requirement. The Panel considers that the use of the 11-year econometric model, including the 2008 and 2009 recession years inappropriately distorts the recent claims cost experience of ICBC, and should not be used for the PY 2012 Indicated Rate Change.

The Panel concludes that ICBC's use of the 12-year exponential model for the period ending first quarter 2008 provides an appropriate base for estimating the BI Frequency sub-component of the PY 2010 Loss Cost Variance. There were no issues raised by Interveners with respect to use of the 6.5 year exponential model to forecast the BI Severity sub-component of the PY 2010 Loss Cost Variance. The Panel considers the use of that model to be appropriate as it fairly represents recent experience in BI Severity.

The Panel further finds that, at a minimum, the 5.5 percentage point Loss Cost Forecast Variance component, incorporating the use of ICBC's 12 and 6.25 year exponential models respectively for Personal BI frequency and severity, is acceptable for use in determining the forecast of loss costs components of the PY 2012 Indicated Rate Change.

3.2 Loss Trend to PY 2012

3.2.1 Model Selection and Loss Costs

The second major component of the required rate increase of +11.2 percent is the Loss Trend to PY 2012. The +1.9 percentage point loss trend impact to the indicated rate change is the difference between where loss costs for PY 2010 emerged, and what they are expected to be in PY 2012. The forecast of loss costs for PY 2012 is based on actuarial modelling. (ICBC Final Argument, p. 22)

ICBC has selected a 12 year exponential (1997 to 2008) model and a 6.25 year exponential model starting at 2005 to forecast 2012 personal BI frequency and severity losses respectively.
(Exhibit B-1, Exhibit D.0, pp. 4, 9)

BI claims account for over 70 percent of the Basic Insurance loss costs. The increasing trend in BI loss cost is driven by ongoing upward pressure on the severity of BI claims. The selected severity trend reflects the trend that has emerged since 2005, which is lower than the trend that was experienced in the years leading up to 2005. ICBC has implemented a number of claims cost management initiatives since 2006, and believes that they have contributed to this lower trend. These efforts are expected to continue to be effective, so that this lower trend in severities is forecast to continue. (Exhibit B-1, pp. 3-14-15)

ICBC states that its "... selection of a BI frequency trend reflecting a return to the long-term trend that was present before 2008 was in part due to ICBC's determination that the low frequency experienced in 2008 and 2009 was the product of unusual events, specifically unusually dry weather and a declining amount of travel during the recession." (ICBC Final Argument, p. 26)

3.2.2 Intervener Submissions

3.2.2.1 CDI

CDI made a number observations and submissions in its Argument with respect to PY 2010 Loss Cost Forecast Variance and Loss Cost Trend to PY 2012, including references to ICBC's use of 2008 Personal BI severity and frequency data, the direction and rate of change indicated by the data and the conclusion to be drawn from the 8.7 percent rate increase hypothetical scenario.

CDI's submission suggests that the +5.5 percentage point change in the PY 2010 Loss Cost Forecast Variance 'does not add up' because the graph illustrating the Basic BI claims frequency shows that the trend line for frequency will continue to decline. (CDI Argument, p. 4)

ICBC responds that the BI frequency trends do not (as CDI appears to assume incorrectly) have to be upward sloping, . . . in order to adversely affect the rate indication. A change in the downward slope of the BI frequency trend is what is affecting the rate indication for PY 2012. (ICBC Reply, p. 11)

CDI submits that "... it is hard to understand that there has been a lower trend in severities when one looks at Figure 3.8 and at paragraph 33 of Chapter 3 [of the Application}. Instead of indicating that the lower trend in severities is forecast to continue, ICBC indicates the severity continues to increase." (CDI Argument, p. 7)

ICBC responds that a "lower trend in severities" is not synonymous with saying that the severity trend is depicted on a graph as angled down and to the right. A "lower trend in severities" means that the upward severity trend is less steep now than it was before 2006. (ICBC Reply, p. 11)

CDI submits that "In reviewing the chart prepared by ICBC showing Basic Bodily Injury Count Personal as of May 31, 2011 (six months before filing this Application), the Ultimate Count indicating claims frequency from 1994 through to 2010 shows Ultimate Bodily Injury claim counts at record lows for the last three years of that period. In fact, there is a difference or increase in claim count between 2008 and 2010 of only 18 (Exhibit B-1, Chapter 3, Exhibit C.1.2.1)."
(CDI Argument, p. 4)

ICBC responds that CDI is overlooking the very significant leverage that BI frequency has on the rate indication. As frequency is a measure of claims per 1000 policies, and there are 2.9 million Basic policyholders, it only takes a very small change in BI claims frequency to have very large ramifications for the revenue requirements. (ICBC Reply, p. 12)

CDI submits that "(t)aking a balanced approach, as ICBC indicates it has done (see Submission of ICBC, pp. 27-28, para. 55), and notwithstanding ICBC's various projections, BCUC's Scenario 1, which results in a rate increase of 8.7%, appears reasonable, in that such an increase would not cause the MCT ratio to change, a point on which ICBC agrees." (CDI Argument, p. 8)

ICBC responds that "CDI is incorrect in stating that the Basic MCT is not affected if a rate change of 8.7% is approved. CDI has misquoted 2012.CP RR BCUCP.8.1. ICBC was responding to a hypothetical scenario in which ICBC was asked to assume that the actuarial rate indication is 2.5 percentage points lower than 11.2%. ICBC did not accept that the hypothetical scenario is reasonable, and qualified its response accordingly." (ICBC Reply, p. 13)

3.2.2.2 BCOAPO

In its submission, BCOAPO notes that "The most significant contributor to the PY 2012 loss trend (+1.9%) is said to be the return of BI frequency to the long term trend line or higher. However, ICBC has acknowledged that there is significant uncertainty in the direction of the BI frequency trend. It is entirely possible that 2010/2011 will prove to be aberrant years, with 2008/2009 marking the beginning a long term downward trend in BI frequency. This may be particularly likely given the correlation identified between precipitation and BI frequency, and the general trend toward warmer, drier weather arising from climate change." (BCOAPO Final Argument, p. 4)

3.2.2.2.1 ICBC Reply

ICBC states "ICBC explained in paragraph 57 of its June 8, 2012 Submission why the scenario that "2010/2011 will prove to be the aberrant years" is increasingly unlikely. ICBC is now in its third year of experience that either reflects a return to, or a further deterioration from, the long-term frequency trend that existed prior to 2008. ICBC continues to see higher frequency and low interest rates in 2012, which supports ICBC's rate indication. ICBC's forecasts are based on historic data, not weather forecasts, as BCOAPO appears to assume. In any event, precipitation to date in 2012 is tracking quite close to the long-term average." (ICBC Reply, pp. 13, 14)

3.2.2.3 Commission Determination

The Panel has reviewed CDI's Argument and ICBC's Reply Argument to the matters raised by CDI. The Panel finds that CDI has not accurately understood and/or represented the ICBC evidence in its submissions, and further finds that ICBC has adequately refuted the CDI Argument. Accordingly, the Panel gives no weight to the CDI submissions.

The Panel finds the BCOAPO Argument with respect to the Loss Trend to 2012 to be speculative opinion not supported by any evidence, and is accordingly given little weight.

The Panel has addressed the issues surrounding the selection of an appropriate model for use in developing the PY 2010 Loss Cost Forecast in Section 3.1 above and has accepted ICBC's use of the BI frequency and severity models used in arriving at the best fit trend line for loss costs. The Panel accordingly accepts the extension of those models for the purpose of determining the Loss Trend to PY 2012. The Panel notes that the ICBC update of the PY 2010 Loss Cost Forecast Variance and Loss Trend to PY 2012 suggest a further +1.1 percentage point increase to the PY 2012 indicated rate change.

The Panel finds that, at a minimum, the +1.9 percentage point Loss Trend to PY 2012 component, incorporating the use of ICBC's 12 and 6.25 year exponential models respectively for Personal Bodily Injury frequency and severity, is acceptable for use in determining the forecast of loss costs components of the PY 2012 Indicated Rate Change.

3.2.3 Prospective Adjustments

ICBC describes prospective adjustments as occurring "When a future event that will influence claims costs is not accounted for within the loss trend models, a specific adjustment is made to the estimated claims costs for the prospective policy year in order to reflect the impact of this event. This is known as a prospective adjustment." (Exhibit B-1, p. 3-28)

ICBC states that it "... has made a prospective adjustment for the expansion of the ISC [Intersection Safety Camera] Program, which represents a net savings of $7.9 million for PY 2012. The ISC Program expansion qualified for a prospective adjustment under AAP because (a) the timing of the ISC Program improvements coincides with PY 2012, (b) the improvements to the ISC Program are expected to yield benefits that are not captured in the existing trend, and (c) the impact of the improvements can be reliably estimated based on past data available from the ISC Program." (ICBC Final Argument, p. 31)

ICBC uses five criteria to determine whether a prospective change with an impact on future claims costs have a meaningful and quantifiable effect in the prospective policy year:

- Timing,
- Causal relationship to costs or savings,
- Incremental costs or savings,
- Estimable costs or savings,
- Significant impact.

The five criteria are described at Exhibit B-1, pp. 3A-1 to 3A-5.

ICBC discusses a number of possible prospective adjustment candidate projects in its direct evidence and in response to Information Requests, as summarised below.

<u>Sea-to-Sky, Canada Line and Personal Electronic Device (PED) ban</u>

ICBC's evidence provides the results of studies conducted to assess the potential impacts of the Sea-to-Sky Highway Improvement Project, Canada Line project, and the PED ban. While all three projects satisfied the first three criteria, ICBC found that in each case specific effects are not currently estimable and insufficient data exist to establish a stable model plus other factors resulting in ICBC's determination that they do not meet criteria 4 and 5. (Exhibit B-1, p. 3A-6)

<u>Evergreen Line Rapid Transit Project</u>

In response to a request to discuss the merits for future prospective adjustments attributable to the Evergreen Project, scheduled for completion in 2016, ICBC states that it does not believe there are any merits to including a prospective adjustment for a future event which does not meet the five criteria which at best, doing so would result in a biased estimate to produce a forecast variance that would affect future years' rates. (Exhibit B-7, 2012.2 RR BCUC.140.1-2)

Impaired Driving

In response to a request related to impaired driving laws, ICBC states that it "... has not assessed any prospective adjustments to the actuarial rate level indication for policy year 2012 for reductions in alcohol-related collisions as no estimate was available for the amount of these costs. ICBC notes that any impact the new impaired driving strategy might be having on claims would have begun to occur in 2010 and 2011 and that by the end of 2011, the updated loss trend models would include consideration of any changes in claims frequency observed as a result of the new penalties for impaired driving." (Exhibit B-6, 2012.1 RR BCUC.110.1.2)

ICBC submits it has employed accepted actuarial practices in the selection of appropriate models to determine an unbiased loss trend to PY 2012. ICBC's systematic application of its criteria for prospective adjustments ensures that impacts of events are captured where appropriate and based on credible evidence, and not double-counted. (ICBC Final Argument, p. 33)

3.2.3.1 Intervener Arguments

While ICBC noted that "Participants in this proceeding identified a number of candidates for prospective adjustments in future rate applications," none of the Interveners made submissions concerning prospective adjustments in their Arguments.

3.2.3.2 Commission Determination

The Panel agrees with ICBC that prospective adjustments should be made based on sufficient data and the use of accepted actuarial practice and determines that the prospective adjustment made with respect to the ISC Project is appropriate in calculating the Loss Trend to PY 2012.

The Panel is concerned that ICBC's framework for assessment of large projects with significant potential may be inadequate to reflect prospective changes in a timely manner. That said, the Panel does recognise that cost effectiveness must be considered in cases where the rate impacts may be transitory due to ICBC's closed system.

The Panel notes that ICBC acknowledges that the Sea-To-Sky the project was a major road improvement to one of BC's most dangerous highways, and also acknowledges the likely causal relationship of safer highways to reduced frequency and severity of crashes and that ". . . claims savings could reasonably be expected to occur as a result of the types of improvements . . ." (Exhibit B-1, pp. 3A-8, 3A-15 et. seq.) ICBC also states that it ". . . continues to review and develop its framework for the application of prospective adjustments to new highway improvement projects, and other events.", and notes that " . . . as observed with the Sea-to-Sky . . .Project, early involvement in the planning process is crucial; it is often too late to find ways to obtain essential data or to control for confounding factors once a project has been completed." (Exhibit B-6, 2012.1 RR BCUC.24.3)

The Panel is concerned that the combined effects of a lack of pre-planning to acquire useable data and the threshold of proof required by ICBC to meet its fourth criterion, Estimable Effects, may result in projects failing to pass the initial screening under criteria 2, Causal Relationship to Claims Savings.

The Panel encourages ICBC to continue its development of an appropriate framework that responds to potential prospective adjustments in a pragmatic and timely manner. Co-ordination of data gathering capability with other agencies should be pursued as part of this initiative.

3.2.4 Summary Commission Discussion and Determination: Loss Trend to PY 2012

The Panel has considered the evidence and arguments of ICBC and the Interveners, and concludes that, at a minimum, the +1.9 percentage point Loss Trend to PY 2012, including the treatment of prospective adjustments, should be approved as requested in the Application.

3.3 Investment Income and Premium Financing Plan Revenue

3.3.1 ICBC's Evidence

ICBC summarizes investment income and premium financing revenue component of the rate increase as follows:

> The third major component of the required rate increase of +11.2% is the change in the expected amount of investment income and premium financing plan revenue, relative to the 2010 Application. Expected rates of return on investments for PY 2012 are significantly lower than was forecasted for PY 2010 in the 2010 Application due to historically low interest rates. Rates of return on investment are discussed in further detail in Chapter 5 [of the Application]. Overall investment income and premium financing plan revenue was expected to contribute $120 per policy to the PY 2010 rate level. It has been reduced to a contribution of $103 per policy in the PY 2012 rate level. This change has an impact of +2.5 percentage points of the PY 2012 indicated rate change.
> (Exhibit B-1, p. 3-15)

The forecast of income from investments and premium financing from incoming premium revenue is based on a formula for the New Money Rate (NMR) which is determined from data averaged from the financial forecasts of six financial institutions (the multi-dealer survey). ICBC's Application used forecast information for calculating the NMR that was available in mid-September 2011, whereas the Yield on Basic Equity used was calculated based on the investment portfolio profile at June 30, 2011. (Exhibit B-1, p. 5-4)

ICBC states that the most current assessment of the NMR and Yield on Basic Equity would be the most appropriate for Basic Insurance rate setting if ICBC were planning to re-file a revenue requirements application based on the most current information at this time. However, ICBC does not plan to re-file this Application in order to use updated information, and is still proposing an 11.2% Basic Insurance rate increase. (Exhibit B-7, 2012.2 RR DUCK.5)

ICBC demonstrates that NMR of 3.13% and Yield on Basic Equity of 4.00% (Updates as of yearend 2011) would have an impact on rate indication of +2.1 ppt. The NMR and Yield on Basic Equity at

"Most Current" rates as of March 31, 2012, would have an impact on rate indication of +1.9 ppt. (Exhibit B-7, 2012.2 RR BCUC.133.1 – Attachment A)

3.3.2 Intervener Submissions

Mr. Duck submits that the timing of when an inventory of market interest rates is to be taken is an issue for the New Money Rate and Yield on Basic Equity. Mr. Duck proposes to blend an average of all the observations as follows. First, the average of the 4 observations of the NMR in the table above is 3.78 percent. ICBC calls for an estimate of 4.15 percent in 2013. Mr. Duck suggests that a reasonable best estimate of the NMR taking all the information into account would be 4 percent, slightly higher than ICBC's application, but more representative of the economic environment of the next few years.

The VEJ submission can be summarized as proposing that ICBC should not engage in asset-liability duration matching in the management of its investment portfolio.

BCOAPO submits that ". . . the volatility in the global economy and the low yields currently available suggest that future trends will most likely be upward. In any event, the risk surrounding ICBC's investment income is less than in recent years, since increased investment income is more likely in the future because current, historically low interest rates weight the likelihood toward favorable rate changes." (BCOAPO Argument, p. 4)

3.3.3 ICBC Reply

In response to Mr. Duck, ICBC states that it has articulated a sound rationale for basing the rate indication in response to the very significant interest rate shift that occurred in Q3 2011. ICBC also submits that there is no principled basis to give weight to the interest rate scenarios from March 2011, prior to the interest rate shift, nor is it appropriate to use a forecast for PY 2013 to calculate the PY 2012 rate indication. (ICBC Reply, pp. 16, 17)

ICBC notes in Reply to VEJ that holding a fixed income portfolio that approximates the duration of its claim liabilities is an important feature of ICBC's investment management in the current context. It reduces ICBC's exposure to interest rate risk and submits that VEJ's approach is a very high risk strategy in the current circumstances with the lowest interest rates in decades. (ICBC Reply, p. 17)

3.3.4 Commission Determination

The Panel acknowledges Mr. Duck's concern about the volatility of the NMR. However, the Panel considers that recent NMR and Yield on Basic Equity data is most indicative of expected returns on investments as it is prospective, rather than an averaging of prior data. BCOAPO's contention that increased investment income is more likely in the future, while hopeful, is not supported by any evidence and is contrary to the forecast evidence on the record.

The updated evidence points to continued volatility and declining trends in the NMR and Yield on Basic Equity. This in turn may point to an indicated rate change even greater than the 11.2 percent increase requested in the Application if ICBC is to achieve its revenue requirement based on updated investment income forecasts. Any revenue shortfall will have a negative impact on ICBC's MCT ratio but may be recoverable in the future due to ICBC's closed system of operations. The magnitude of any negative forecast variance will have to be monitored to ensure that the MCT ratio does not fall below the 100 percent minimum requirement of *Special Direction IC2.*

The Panel therefore finds ICBC's evidence respecting its methodology of determining the impact of the New Money Rate and Yield on Basic Equity to be persuasive, and accordingly approves, at a minimum, the use of the +2.5 percentage point Investment Income and Premium Financing Revenue component of the Indicated Rate Change as requested in the Application.

3.4 Operating Expenses

3.4.1 Operating Expenses Are Not Adding to the Indicated Rate Change

ICBC indicates that it "initiated a suite of cost control measures which has had the short term impact of reducing corporate operating expenses for 2011 by $26 million in comparison to the original plan as represented in ICBC's 2011-2013 Service Plan. For the 2012 forecast, these cost control measures are expected to contain operating expense increases below the level of inflation.

As a result of these cost control measures, operating expenses do not contribute to the rate increase requirement for the 2012 policy year." (Exhibit B-1, p. 7-1) Also, "for the 2002 to 2010 period, ICBC was able, on average, to maintain year to year operating expenses at about the rate of inflation." (Exhibit B-1, p. 7-5) And, "… on a per policy basis there is no dollar difference [between 2010 operating expenses after adjustment, and 2012 operating expenses excluding IFRS change] representing a net zero percentage point impact on the actuarial rate indication." (Exhibit B-1, pp. 7-29, 7-30)

Further, in its Final Argument ICBC indicates that "Since 2001, ICBC has maintained average year to year operating expense increases at about the rate of inflation. Operating expenses do not contribute to the actuarial rate indication for PY 2012." (ICBC Final Argument, p. 39)

ICBC makes the following points:

a) ICBC implemented cost control strategies in mid-2011 that generated significant operating expense savings, and the results are reflected in the 2012 forecast used for the PY 2012 rate indication;

b) The base operating expense increase for the 2012 forecast is largely the product of higher depreciation expense, higher project spending, and compensation increases in line with inflation; and

c) Costs relating to the Transformation Program ("TP") have been appropriately allocated 100% to Optional insurance."

(ICBC Final Argument, p. 40)

Key cost control measure initiated in 2011 included:

- Detailed budget reviews;
- Strategic prioritization of projects;
- Management of staffing vacancies (only vital positions are being filled);
- Functional review of the efficiency of delivering corporate support functions; and
- New guidelines to contain discretionary spending within inflation.

ICBC indicates that the “2012 forecast increase in compensation costs is within inflation and reasonable based on ICBC’s business needs … the FTE’s per policy is flat. Compensation level increases are limited to those approved by the Public Sector Employers’ Council (“PSEC”). The change in employee mix to include more M&C employees is driven by business imperatives.” (ICBC Final Argument, p. 43)

3.4.1.1 BCOAPO has Raised Concerns Related to Compensations Costs and Management and Confidential (M&C) Employees

BCOAPO indicates that “Between 2007 and 2011, ICBC virtually doubled the number of its employees receiving combined salary and bonus compensation from 200 to 395. BCOAPO also notes a significant increase in the number and cost of M&C employees occurring during relatively low claim years when the value of such additions is questionable … In this Application, as in ICBC’s last, BCOAPO does not find that ICBC has justified the increases to M&C FTE’s that has occurred in recent years.” (BCOAPO Final Argument, p. 5)

It further submits “Between 2007 and 2011, the average compounded compensation increase for the Bargaining Unit (hereinafter ‘BU’) employees was a modest 0.749%. During the same time period, ICBC’s M&C employees saw an average annual compounded increase in compensation of 8.74%. Coupled with the fact that during the same time period the number of M&C FTE’s ballooned from 855 to 1070, and increase of just over 25% in ICBC’s most expensive employee group, and it becomes clear from a ratepayer perspective the Utility's decision to continue to develop its top heavy corporate structure is problematic." It also makes reference to "this disproportionate corporate structure." (BCOAPO Final Argument, p. 6)

BCOAPO also raises a concern that "ICBC's short term incentive program (hereinafter 'STIP') appears to provide an incentive to M&C employees to underestimate revenue. If ICBC's net income exceeds its forecast, the surplus revenue is distributed to the same salaries responsible for producing the forecasts and in direct proportion to the variation from the expected revenue. A more appropriate structure may be to link the size of the bonuses to how closely forecast revenue matches actual revenue: the greater the deviation, the less the distribution." (BCOAPO Final Argument, p. 6)

ICBC responds to BCOAPO's reference "to ICBC as 'top heavy' based on the fact that the number of M&C FTEs has increased while the number of BU FTEs has decreased … ICBC submits that it is not possible to assess the efficiency of ICBC's corporate structure by counting the number of FTEs in this manner …. ICBC has provided evidence on the importance of adding M&C FTEs in certain areas of the Corporation to address span of control, improve claims handling quality, and manage risks effectively. ICBC's evidence is referenced in paragraph 98 of ICBC's June 8, 2012 Submission." (ICBC Reply, p. 21) ICBC provided a detailed explanation of the change in employee mix by Division. (Exhibit B-6, 2012.1 RR BCUC.78.4.1)

ICBC further submits that "The evidence is that ICBC's cost reduction initiatives have been very successful. ICBC reduced 2011 operating expenses by $26 million. The efficiencies were captured in the 2012 budgeting cycle. There is no evidentiary basis to support further operating expense reductions." (ICBC Reply, p. 21)

Finally, ICBC makes the following submission in response to BCOAPO's assertion that ICBC's STIP appears to provide an incentive to M&C employees to underestimate revenue, and that a compensation system based on revenue forecasting accuracy might be preferable. "The volatility

ICBC is experiencing relates to costs; revenues are capable of fairly accurate forecasting. Moreover, STIP is paid based on a variety of corporate objectives. ICBC's PSEC-approved M&C compensation system, which aligns employees with corporate objectives, is most appropriate and beneficial for policyholders." (ICBC Reply, p. 21)

3.4.1.2 IBC has Raised Concerns With The Amount Of Information Regarding Operating Expenses

In its Submissions, IBC raises concerns with the amount of information provided in the proceeding regarding operating expenses. "The 2012 Application provides very limited information regarding operating expenses. This means that neither the interveners not the Commission can properly assess the operating expenses." (IBC Argument, p. 3) Further, "Absent more detail, the Commission, the interveners and the public cannot assess whether the various elements that comprise the operating costs are reasonable, whether further savings are possible, what changes have been made in ICBC's structure and how these affect operating costs, and how changes in the operating structure and operating costs may affect the allocations." (IBC Argument, p. 4)
"IBC urges the Commission to require that ICBC provide more complete information regarding its operating costs on future full revenue requirement applications and require ICBC to provide the information in a consistent format."

IBC also comments that ICBC's Information Request response "... fails to recognize Commission's continuing obligations under section 45 of the *Insurance Corporation Act* to oversee the manner in which Basic insurance is made available and under section 49 to ensure that revenue from the Basic business is not used to subsidize the Optional business. There can be no oversight without adequate information." (IBC Argument, p. 3)

In its Reply, ICBC disagrees with IBC assertions regarding the level of detail of operating expenses.

It "submits that the present Application

- provides greater financial detail; and
- is organized in a better format for year –over-year comparisons."
  (ICBC Reply Argument, p. 18)

ICBC argues that "Organizing costs with reference to relevant cost drivers … permits a more meaningful year-over-year comparison. The presentation of costs by cost driver is also unaffected by organizational structure changes. ICBC's current presentation also segregates items that ICBC can control … from those that ICBC cannot control." Furthermore, "ICBC did provide divisional [organizational] presentation overview in this proceeding in response to IBC's request. ICBC also conducted a more detailed divisional analysis for FTEs and compensation, which accounts for the most significant base operating component." (ICBC Reply, pp. 18, 19)

3.4.1.3 IBC has Raised Concerns Regarding the Allocation Of Performance-Based Pay Between Basic and Optional Insurance

IBC expresses concern on the allocation of performance-based pay between Basic and Optional given that Basic faces a revenue deficiency. It states that "ICBC may perceive itself as an integrated business, but requiring Basic to contribute to performance-based pay when it is incurring a loss is in effect a double penalty and may actually encourage a focus on Optional (the profitable part of the integrated entity) at the expense of Basic (the unprofitable part of the entity)." (IBC Argument, p. 5)

ICBC indicates that "ICBC applies the Commission approved financial allocation methodology and percentages in the allocation of compensation costs to the Basic and Optional insurance." (Exhibit B-7, 2012.2 RR BCUC.168.3) Also, ICBC challenges IBC's assertion that "requiring Basic to contribute to performance-based pay when it is incurring a loss is in effect a double penalty and may actually encourage a focus on Optional." It submits that "In fact, the converse is true. IBC's approach to basing STIP on the performance of Optional insurance alone would mean that employees of ICBC are incented to focus only on the Optional insurance business. This is not in the interests of Basic Insurance customers." (ICBC Reply, p. 20)

Except for BCOAPO and IBC, no other Interveners made submissions regarding ICBC's Operating Expenses and their impact on the actuarial rate indication.

3.4.2 Commission Determination

For the following reasons the Panel determines that Operating Expenses are not adding to the Indicated Rate Change. The Panel finds that forecast operating expenses for the 2012 year are in line with inflation, given the cost management programs that ICBC has implemented and described in the Application. No Intervener has provided evidence to suggest that these cost management programs will be ineffective in maintaining costs within inflation, nor insufficiently contribute to efficient operations.

The Panel finds that ICBC's evidence regarding the mix of M&C and BU FTEs supports the rationale for the changes made to support operational needs. The Panel also accepts that tying STIP to corporate business objectives is a superior incentive program than to tying it to revenue forecasting accuracy, especially in view of ICBC's operational volatility being tied more to cost management than to revenue forecasts.

The Panel is satisfied with the amount of detail provided regarding operating expenses throughout this Proceeding, for the review of the Application and the requirements of Sections 45 and 49 of the *Insurance Corporation Act*. The Panel is particularly satisfied with the evidence demonstrating cost information reflecting on cost drivers, including costs ICBC can control and those it can't control. With two rounds of Information Requests, in addition to the Application itself, the Panel was able to obtain the necessary information to properly evaluate ICBC's operating expenses. However, ICBC should be mindful of past Commission direction regarding the filing of operating expense information under Order G-65-10 and its Decision dated April 6, 2010, which states "The Commission Panel directs ICBC to include the historical information as outlined in Exhibit B-4, 2009 ST BCUC.19 as part of the operating expense filing" only applies to streamlined applications. **In full**

revenue requirements applications, ICBC is directed to file full operating cost details, including divisional information.

Finally, the Panel accepts that allocating performance-based pay between Basic and Optional insurance is appropriate as it incents ICBC employees to direct adequate attention to both businesses.

3.4.3 Transformation Program (TP)

The Commission asked a number of Information Requests (Exhibit B-6, 2012.1 RR BCUC.71, 78.8; Exhibit B-7, 2012.2 RR BCUC.165) in order to determine the benefits of the TP that would flow through to the Basic Insurance portion of the business. Although the funding of the TP is entirely from Optional insurance, ICBC has indicated that benefits will flow through to both Optional and Basic Insurance policyholders. ICBC indicated that the TP benefits would flow through in subsequent policy years and ICBC will report to the Commission regarding any implications for Basic Insurance rates in future filings. (Exhibit B-6, 2012.1 RR BCUC.71.2) Based on the current planning, ICBC expects to implement the final components of the TP in the fall of 2016. (Exhibit B-6, 2012.1 RR BCUC.71.3)

The benefits that could be provided by the TP were shown in the attachments to Exhibit B-6, 2012.2 RR BCUC.165.1 where the document entitled "Our Journey" indicates "For example, we know that as a result of the implementation of new Claims systems and processes, the Claims division will be reduced by about 350 positions by the end of 2014. This includes about 70 management positions."

ICBC was asked to identify the timing of the 350 reduction in positions and responded that planned workforce reduction relating to TP will be achieved through natural attrition, beginning 2014 and continuing through 2016, but precise details are not yet known. (Exhibit B-6, 2012.1 RR BCUC 78.8.1)

ICBC also notes "At the conclusion of TP, internal TP resources will return to core positions, and the temporary backfilled resources will be released." (Exhibit B-6, 2012.1 RR BCUC.78.8.2)

3.4.4 Commission Determination

ICBC was asked to identify quantifiable benefits of the TP that would flow through to the Basic Insurance policyholder. ICBC provided evidence only in qualitative format that does not show the financial implications of the TP. **ICBC is directed to provide a comprehensive qualitative and quantitative analysis of the TP benefits anticipated to flow through to the Basic Insurance business. This analysis should be provided prior to the commencement of the 2014 policy year** and preferably within the next ICBC Revenue Requirements application, be it a streamlined or a full application.

The Panel also cautions ICBC to ensure that FTEs hired for the TP should have a smooth transition without increasing staff levels when it concludes in 2016, as indicated in Exhibit B-6, 2012.1 RR BCUC.78.8.1.

3.5 Capital Provisions, MCT and IFRS

Discussions of ICBC's Basic Insurance capital requirements, capital maintenance and capital build provisions, MCT and in this instance, impacts of the IFRS conversion, are inter-connected and are combined in this Section.

3.5.1 ICBC's Basic Capital Evidence

ICBC states that it "requires sufficient Basic capital on hand to ensure that liabilities are covered in the event of adverse circumstances. The level of capital that is considered adequate, and how ICBC builds, releases, and maintains that capital, is dictated in large measure by regulation. Consistent with the regulatory framework, the rate indication includes only a capital maintenance provision and does not include a provision to build capital." (Exhibit B-1, p. 4-1)

The current regulatory regime is described in Exhibit B-1, Chapter 4, and can be summarized as follows:

- *Special Direction IC2* establishes a minimum regulatory level of capital of 100 percent of the MCT ratio;
- The Commission approved Capital Management Target (CMT) is 130 percent of the MCT ratio;
- The Capital Management Plan (CMP) provides for a capital build component to be included in the rate indication when the MCT ratio falls below the 130 percent Capital Management Target, and for a release of capital in excess of the CMT, as modified by the 2010 Government Directive;
- The 2011 Government Directive comprises two elements:
  - In determining revenue requirements, the MCT ratio calculation is to be made as at the most recent quarter; and
  - The Basic CMP is to be altered to exclude any component building capital from February 1, 2012 to January 31, 2015, provided that Basic capital remains above the regulatory minimum.
- The Basic MCT ratio as at the third quarter 2011 was 120 percent, thus the Application's Indicated Rate Change reflected neither any capital release nor, in accord with the 2011 Government directive, any capital build provision.
- ICBC includes a capital maintenance provision in its PY2012 Indicated Rate Change, which is required to account for growth in the Basic Insurance portfolio.
- The Basic Insurance forecast MCT ratio for December 31, 2012 is 108 percent, reflecting the new OSFI guidelines effective January 1, 2012.

  (Exhibit B-1, Chapter 4; Exhibit B-7, 2012 RR.156.1)

3.5.2 Intervener Submissions

3.5.2.1 CDI

CDI pointed out that ICBC updated its forecast for the MCT ratio as at December 31, 2012 to 108 percent compared to 102 percent forecast at the time of the January 23, 2012 workshop and commented that this illustrates the elusive nature of such forecasting. (CDI Argument, p. 10)

In its conclusion, CDI submits that the increase of 8.7 percent will allow the MCT ratio to remain above the mandated 100 percent and suggests that this is supported by a response to a Panel Information Request. (CDI Argument, p. 13, para. 49(b))

3.5.2.1.1 ICBC Reply

ICBC agrees that the MCT ratio is difficult to forecast, but points out that the change in the year end 2012 MCT ratio forecast from 102 percent to 108 percent is due to the new OSFI guidelines rather than forecasting error. (ICBC Reply, p. 9)

ICBC also submits that CDI is incorrect in stating that the Basic MCT is not affected if a rate change of 8.7% is approved and has misquoted 2012.CP RR BCUCP.8.1 in which ICBC was responding to a hypothetical scenario in which ICBC was asked to assume that the actuarial rate indication is 2.5 percentage points lower than 11.2%. ICBC did not accept that the hypothetical scenario is reasonable, and qualified its response accordingly. (ICBC Reply, p. 13)

3.5.2.1.2 Commission Determination

The Panel agrees that CDI is incorrect in stating that MCT will not be affected if a rate increase of 8.7 percent is approved. CDI has overlooked or misunderstood the hypothetical underlying condition in the Panel's Information Request, that if a minus 2.5 percent reduction in the indicated rate change were to be actually realised, there would be no change to the MCT ratio. If ICBC's realised revenue falls short of that required by the indicated rate change, a decrease in MCT will result, all else equal. The Panel has determined that the updated evidence supports a minimum increase of at least 11.2 percent.

3.5.2.2 Frank Duck

Mr. Duck submits that the MCT objective (target) is too high and should be set at 110 percent not 130 percent.

3.5.2.2.1 ICBC Reply

ICBC points out that a change in the MCT management target would have no effect on the PY 2012 rate indication, as there is no capital build provision in the components of the rate indication. ICBC also observes that the Government directive, subject to the recent OIC, remains in effect, and that the Commission has recognised in previous decisions that adequate capitalization of Basic Insurance is fundamental to ensure viability of Basic Insurance over the long-term.

3.5.2.2.2 Commission Determination

ICBC correctly points out that there is no effect on the PY 2012 Indicated Rate Change due to the Government directed absence of a capital build provision. The Commission has previously accepted ICBC's Capital Management Plan, and has not been persuaded by Mr. Duck's submission that that there is a need for any changes to the Plan.

3.5.2.3 BCOAPO

BCOAPO submits that ". . . our clients would generally not like to see premiums increase when the economy is weak,. . ." and suggests that ICBC investigate ". . . a model in which some additional capital build is undertaken when the economy is doing well - with the express purpose of smoothing any rate increases during a downturn by a capital release."

BCOAPO also submits that "ICBC's own preliminary actuarial analysis indicates that there is sufficient capital to absorb a 3.3% deficiency in the recommended PY2012 rate." and ". . . respectfully urges the Commission to reduce [to +7.9 percent] ICBC's revenue requirement accordingly." (BCOAPO Argument, p. 8)

3.5.2.3.1 Commission Determination

BCOAPO's suggestion to build capital when the economy is doing well in order to smooth rates during a downturn is effectively embedded in ICBC's Capital Management Plan. The Panel notes that the combined impacts of a significant changes in the PY 2010 Loss Cost Variance and the Investment income has caused a rapid decrease in the capital available for capital release, to the point where there is now a risk that ICBC will have to introduce a capital build component into its rate indication in order to maintain the minimum 100 percent MCT ratio.

As indicated in the Panel's comment on CDI's submission, any reduction of the requested +11.2 percent increase would increase the risk of falling below the minimum MCT requirement. While the Panel would be sympathetic to BCOAPO's suggestion if ICBC's forecast MCT ratio was significantly higher than 100% MCT, given ICBC's current financial condition, a release of capital to smooth rates, even if permitted, would not be prudent.

3.5.2.4 AIC

AIC comments on ICBC's [corporate] transfer of funds to the Provincial Government, and concludes by submitting that "From a public policy standpoint, the BCUC should not accept a basic insurance rate increase, and the Corporation and Government should instead focus on offsetting losses and profits through fiscally sound balancing of the basic and optional insurance income and expenses", and "While it is recognized that this may not be within the mandate of the BCUC, this committee suggests that some inquiry be made into the practice of large transfers of capital (profit) to the Government to determine if, under certain circumstances, more capital can be retained in the corporation to better stabilize insurance premium rates for basic insurance."
(AIC Argument, pp. 13-15)

3.5.2.4.1 ICBC Reply

ICBC responds that Transfers to Government from Optional capital are the subject of legislation; the Commission has jurisdiction over Basic rates, not Optional rates; Basic capital and rates are unaffected by the transfers of Optional capital to Government; transfers of Optional capital to Basic Insurance can only occur by direction from Government and the Commission should reject AIC's submissions on these points. (ICBC Reply Argument, p. 26)

3.5.2.4.2 Commission Determination

The Panel expects that AIC is or ought to be well aware that there have been Government directives for significant transfers of capital from Optional Insurance in recent years to support the capital requirements of Basic Insurance. The Panel accepts ICBC's submission that AIC's points on this matter be rejected as they are clearly beyond the jurisdiction of the Commission, as recognized by AIC. Matters of public policy should be directed elsewhere.

3.5.3 Commission Determination on Capital Provisions and MCT

Subsection 3(1) of *Special Directive IC2* provides, among other things:

> "3(1) With respect to the exercise of its powers and functions under the [Insurance Corporation Act] in relation to the corporation generally, the commission must do the following:

. . .

> (b) set rates for the corporation's universal compulsory [Basic] insurance business in a way that will allow the corporation to maintain capital available in relation to its universal compulsory insurance business equal to at least 100% of MCT;
>
> (c) subject to paragraphs (c.1) and (e), for each year for which it fixes universal compulsory vehicle insurance rates, fix those rates on the basis of accepted actuarial practice so that those rates allow the corporation to collect sufficient revenue,

. . .

(iii) for 2005 and each following year for which rates are set, to achieve or maintain, as the case may be, the capital available required by the capital available target established for that year under paragraph (b)";

(c.1) when regulating and fixing universal compulsory vehicle insurance rates, regulate and fix those rates in a manner that recognizes and accepts actions taken by the corporation in compliance with government directives issued to the corporation;

. . .

"(e) ensure that increases or decreases in universal compulsory vehicle insurance rates are phased in in such a way that those rates remain relatively stable and predictable."

The November 25, 2011, Government Direction precludes the Commission, even if it were so inclined, from requiring a capital build component for the Indicated Rate Change if the MCT ratio is at or above 100 percent. The Panel's concern is whether the MCT ratio will continue to decrease to a point below 100 percent, thus requiring a capital build provision as part of the Indicated Rate Change. The introduction of a capital build component to the rate indication would further challenge the requirement to set rates which are 'relatively stable and predictable' as mandated by *Special Direction IC2*.

ICBC's Capital Management Target ratio of 130 percent, accepted by the Commission in an earlier decision, is intended to provide a cushion to absorb the impact of 'adverse events', a number of which have been and/or continue to be experienced by ICBC, including increasing loss costs, and fluctuations in interest rates, yields, portfolio and asset values. The forecast December 31, 2012 MCT ratio of 108 percent, based on the 11.2 percent rate increase, is uncomfortably low, with little 'cushion' left to protect the minimum capital requirement.

ICBC's latest forecast in evidence illustrates a revised Indicated Rate Change of +14.2 percent, (11.2 + 1.1 + 1.9) resulting in a further decrease of the MCT ratio of some 7 percent, placing the ratio virtually at the 100 percent minimum. ICBC states that despite the updates rate indication, management has decided not to re-file the Application. (Exhibit B-7, 2012.2 RR BCUC.129.1-3)

ICBC states that the MCT ratio at March 31, 2012 was 120 percent, but that by the end of April 2012 the ratio had decreased to 114 percent. (Exhibit B-13, 2012.CP RR BCUCP.9.1-2)

The Panel understands the dilemmas facing ICBC, including forecasting the dynamic and volatile components of the rate indication. The Panel's view is that the primary concern for ICBC's policyholders should be the financial health and solvency of the Basic Insurance business, as expressed by the Commission in previous decisions, and implicit in the regulatory requirement for the Commission to set rates which permit ICBC to earn revenue sufficient to maintain the MCT ratio at or above 100 percent.

The Panel finds that while the evidence points to a continued decline in the MCT ratio to December 31, 2012, that evidence does not conclusively support a finding that the MCT ratio will decline below 100 percent by December 31, 2012.

The Panel concludes that the Commission should monitor the trend in the MCT ratio on a regular basis. ICBC is directed to file year-to-date MCT ratio calculations, estimated as described in Exhibit B-13, 2012.CP RR BCUCP.9.1-2, not later than 30 days following the end of each calendar month, together with MCT ratio estimates for the following two calendar quarters. In the event that any of the estimates indicate a MCT ratio of less than 100 percent, ICBC is further directed to file with the Commission an application for a rate change to ensure that the MCT ratio is maintained at or above the 100 percent regulatory minimum. ICBC is directed to continue the monthly filings until otherwise directed by the Commission.

3.5.4 International Financial Reporting Standards (IFRS)

The transition from Canadian Generally Accepted Accounting Principles (CGAAP) to IFRS has had a +0.4 percentage point impact on the PY 2012 actuarial rate indication. ICBC has confirmed that it is required to adopt IFRS effective January 1, 2011 in accordance with directions from the Treasury Board under the *Budget Transparency and Accountability Act* and the Public Sector Accounting

Board of Canada. ICBC also confirms that the transition to IFRS conforms to the basis of accepted actuarial practice in Canada. (Exhibit B-6, 2012.1 RR BCUC.44.1, 44.2)

3.5.4.1 Commission Determination on IFRS

There were no submissions from Interveners with respect to ICBC's determination of the impact of the transition IFRS. **The Panel finds that ICBC's evidence adequately supports the determination of the +0.4 impact of IFRS Changes in the PY 2012 Indicated Rate Change.**

3.6 Trend in Average Premium and Other

3.6.1 ICBC's Evidence

ICBC forecasts the average premium of the policies expected to be written in PY 2012 if the current premium rates continue to be charged. The average premium is trending lower due to a combination of shifts in rate classes as the proportion of seniors increases, and shifts in discount levels as existing customers migrate to greater levels of discount on average. This has the effect of reducing the expected revenue and therefore contributes to the increase in the rate level. The impact of reflecting the trend in the average premium is +0.4 percentage points on the PY 2012 indicated rate change.

The Other component to the rate indication includes miscellaneous revenue, broker fees, unallocated loss adjustment, expenses, and rounding differences. (Exhibit B-1, p. 3-5)

3.6.2 Commission Determination

There were no issues raised by Interveners with respect to either the Trend in Average Premium or Other components of the Indicated Rate Change. The Panel accepts the +0.4 percentage points impact on the Indicated Rate Change. The Panel takes note of ICBC's comments (above) with respect to increasing proportion of seniors and the migration to greater levels of discount on average, and anticipates that these demographic trends will continue, with a corresponding increase in the trend in average premium.

ICBC is directed to prepare and submit to the Commission a report illustrating a five year forecast of the impact of these trends on the Basic Insurance Trend in Average Premium. The report should also address any rate design and or discount initiatives ICBC might take to mitigate the impact of the increasing average trend in premiums. The report should be submitted to the Commission by May 31, 2013.

3.7 Conclusion – PY 2012 Indicated Rate Change

Interveners were virtually unanimous in directly or indirectly expressing concern about the size of ICBC's Application for an average 11.2 percent rate increase. The Panel shares that concern.

In reaching its determination respecting the appropriate rate change, the Panel is confronted with competing requirements. The Commission is required to set rates for ICBC that will allow it to maintain a Basic Insurance MCT ratio of at least 100 percent. The Commission is also required to ensure that increases (or decreases) in Basic Insurance rates are phased in such a way that the rates remain relatively stable and predictable. In the case of this Application, these two requirements are competing: the continued downward trend in the MCT ratio suggests a possible requirement for an even higher rate increase than that indicated in the Application in the interests of protecting ICBC's solvency, yet such a further increase above the already unprecedented 11.2 percent increase would clearly challenge the requirement for relatively stable and predictable rates.

The Panel has addressed and reached conclusions with respect to the various components of the 11.2 percent Indicated Rate Change in Section 3 of the Decision. The primary drivers of the requested rate increase are the PY 2010 Loss Cost Variance, the Loss Trend to PY 2012 and the Investment Income and Premium Financing Plan Revenue. The latest updates of the evidence indicate that the PY 2010 Loss Cost Variance could possibly be 1.1 percentage points higher than the 5.5 percentage point indication in the Application. The latest update of the New Money Rate indicates that the Investment Income component of the Indicated Rate Change could possibly be 1.9 percentage points higher than the +2.5 percentage point indication in the Application.

The combination of these two updates suggests a possible PY 2012 total Indicated Rate Change (increase) of +14.2 percent, 3 percentage points higher than the 11.2 percent increase requested in the Application. If a 14.2 percent rate increase is actually required for PY 2012, an even further decline in the MCT ratio will occur to a point at or very near the 100 percent regulatory minimum, absent some combination of further increased insurance rates and/or increased investment income.

In its Decision respecting ICBC's 2007 Revenue Requirements, the Commission reinforced its view that achieving appropriate financial targets, such as appropriate MCT ratios, is a critical factor in ensuring that ICBC will have the ability to achieve and maintain the satisfactory financial strength necessary to meet its obligation to its policyholders in an orderly fashion and to comply with its regulatory requirements. In that Decision the Commission Panel also expressed the view that it would be important for ICBC to replenish its capital as quickly as possible following an adverse scenario occurrence and recognized that the severity of such an occurrence and consequential impact on rates can affect the relative stability and predictability of the rates. On balance, and giving consideration to *Special Direction IC2*, the Commission in that Decision determined that the financial strength and stability of the Basic Insurance business should be given more weight than maintaining relatively stable and predictable rates.

This Panel continues to hold those views. However, adverse scenarios are being experienced to an unforeseen degree, and the regulatory regime has been modified.

The Panel finds that the 11.2 percent rate increase, while unusually large, does meet the test of being relatively stable and predictable, in the context of ICBC's current circumstances, and the increase that might otherwise have been necessary had the requirement for a capital build provision in the rate indication not been removed by Order in Council No. 560 which approved the Government's November 25, 2011 Letter of Direction.

In Section 3.5, the Panel concludes that, while there is a continuing decline in the MCT ratio and continued volatility and a declining trend in the New Money Rate, the evidence does not conclusively support findings that the MCT ratio will decline below 100 percent by December 31, 2012.

The Panel has considered and weighed the evidence and arguments of all parties in the Proceeding. The Panel determines that, based on the foregoing reasons, the requested increase is needed to enable ICBC to have the opportunity to best balance the competing requirements to (1) achieve or maintain its Minimum Capital Test solvency ratio of 100 percent, and (2) phasing rates in a way that they remain relatively stable and predictable for PY 2012.

The Panel determines that, in the aggregate, ICBC's evidence with respect to the various indicated rate change components adequately supports a PY 2012 Indicated Rate Level Change of at least +11.2 percent.

4.0 CLAIMS INITIATIVES

The Application includes a discussion of ICBC's Claims Initiatives which provides an overview of factors affecting BI claims costs, along with information on ICBC's claims cost management initiatives that are helping to manage the growth in BI claims costs. ICBC explains that while there has historically been a long-term trend of declining BI claims frequencies which partially offset the impact of a long-term trend of rising BI claims severities, this is not currently the case. (Exhibit B-1, Chapter 6, p. 6-1)

ICBC notes that the most significant factor in determining Basic Insurance rates, and the majority of Basic loss costs incurred are BI related. There are a number of factors that affect BI claims costs. Some are within and others are beyond ICBC's control. BI claims severities are impacted by the type and complexity of injuries reported, which in turn drive payments for general damages and the costs of litigation. Claims handling initiatives do not affect claims frequency.

ICBC indicates that since late 2005 it has developed and implemented a number of initiatives aimed at managing the growth in BI claims costs. ICBC believes that its claims handling initiatives have contributed to lower BI severity trend that has emerged since 2005. Claims cost management initiative strategies fit broadly into three categories:

- Improvements to claims handling, including establishing the centralised litigation claims handling centre;
- Increased focus on BI claims and a revised management accountability strategy;
- Introduction and development of key business indicator reports and data analysis.

Information Requests for claims initiatives examine, among other matters, BI litigation costs. The following table shows ICBC's average BI claims loss costs and average costs of litigation for closed claims.

Table 4.1

Line #	Year (a)	Average BI Claims Loss Costs for Closed Claims		Average Costs of Litigation for Closed Claims		Average BI Paid Severity All (f)	Annual Change % (g)
		Total Average (b)	% Annual Change (c)	Total Average (d)	% Annual Change (e)		
1	2006 Actual	$21,730	-	$7,643	-	$24,957	-
2	2007 Actual	$23,205	6.8%	$9,527	24.7%	$27,330	9.5%
3	2008 Actual	$22,932	-1.2%	$10,240	7.5%	$27,563	0.9%
4	2009 Actual	$23,819	3.9%	$11,286	10.2%	$29,256	6.1%
5	2010 Actual	$26,488	11.2%	$12,021	6.5%	$32,072	9.6%
6	2011 Actual	$28,967	9.4%	$12,533	4.3%	$34,929	8.9%
7	2012 Forecast	n/a	n/a	n/a	n/a	$36,179	3.6%

(Exhibit B-7, 2012.2 RR BCUC.162.4)

ICBC submits that the costs of litigation are driven in large part by the amounts awarded under the Supreme Court Civil Rules tariff of costs as third party taxable costs, and the amount of disbursements incurred by the parties for items such as expert reports. Factors that increase the average costs of litigation include the extent of the legal process and the stage at which a claim is resolved, with claims resolved after trial generally resulting in the highest costs of litigation. ICBC states that it does not have jurisdiction over the courts in BC and consequently cannot drive reductions in court awarded damages in BI tort claims.

In terms of strategies, initiatives, or efforts to reduce court awards for BI litigation, ICBC seeks to settle BI claims through fair and reasonable settlement offers and prompt payment of benefits. In evaluating BI claims and determining fair and reasonable settlement offers, ICBC considers the BI tort claim case law precedents. In the event that a fair and reasonable BI claim settlement cannot be reached through negotiation by the parties, the case will proceed to court. (Exhibit B-6, 2012.1 RR BCUC.62.5; Exhibit B-7, 2012.2 RR BCUC.162.3)

ICBC has not conducted any studies on the relationship between BI severity and BI claims handling processes since 2002 although there have been significant changes in claims handling and the types of claims made since that year. ICBC's states that past attempts to investigate the relationship between operational factors and cost outcomes did not produce results useful for making program evaluations or prospective adjustments. (Exhibit B-7, 2012.2 RR BCUC.163.2)

4.1 Intervener Submission

BCOAPO notes the portion of premiums attributable to Part 7 claims (medical and rehabilitation, weekly and death benefits) has been dropping since 2007 while the portion of premiums attributable to third party claims has been increasing over the same time frame. BCOAPO acknowledges that the Commission does not have the jurisdiction to alter ICBC's claims handling procedures, but states that it does have the ability to question whether ICBC is, in fact, in a position to reduce BI severity by providing more rehabilitative services. BCOAPO questions whether the trend to increasing BI severity noted by ICBC is a result of its own claims handling procedure. (BCOAPO Final Argument, p. 6)

4.2 Commission Determination

The Panel notes that the 2011 rate of increase in average costs of closed claim litigation is lower than the rate of increases in previous years and acknowledges that ICBC does not have any control over court awards. ICBC is expected to manage its BI claim settlement procedures and its BI litigation costs as efficiently as possible for the benefit of all Basic Insurance policyholders. The Panel also notes BCOAPO's concerns.

BI losses and related litigation and other costs are of continuing interest and concern to the Commission, notwithstanding the recent decrease in the rate of increase in litigation costs. The Panel considers that the discussion and direction in Section 3.4 of this Decision (Operating Costs) respecting the systems Transformation Project will also impact ICBC's Claims Initiatives.
ICBC is directed to specifically include anticipated benefits for its Claims Initiatives in the Transformation Program analysis directed in Section 3.4.4.

5.0 PERFORMANCE MEASURES

As agreed in the May 2004 Negotiated Settlement Agreement and modified in the July 2006 Decision, ICBC has provided 2010 actual and 2011 forecast data for the agreed performance measures. It has also provided reference data for 2008 and 2009. The measures have used the Commission-accepted allocated methodology where performance measures are presented for Basic Insurance. The measures cover four areas: Service, Financial, Efficiency, and Directional.

Service related performance appears to be fairly constant since 2008, with some minor gains being made, and no significant deterioration in any one area. Explanations for variances in Financial and Efficiency measures are largely addressed in earlier sections of this Decision, particularly related to the higher frequency and severity of BI claims, investment returns, and operational costs including the introduction of cost control measures introduced in 2011. It is noted that cost per policy in force is trending upward, with significant increases as a result of higher claim cost trends, partially offset by the internal cost control measures in 2011 and lower external costs associated with legal counsel, medical and dental, private investigator, independent adjusters, and towing fees.

ICBC does not set targets for its Directional indicators which include New Driver Comparative Crash Rate, Crash Rate, and Injured Person Rate. It considers these as indicators of effectiveness of Road Safety programs and not as measures.

There were no submissions from Interveners related to the adequacy or effectiveness of ICBC's Performance Measures.

5.1 Commission Determination

The Panel is satisfied that the measures are not showing significant deterioration. All of the performance measures remain relevant and provide a valuable tool to monitor overall ICBC performance. Such measure should continue to be provided in future filings. The Commission will continue to monitor the ongoing impact of the cost control programs introduced in 2011 and will look with interest on the intended improvements to overall corporate performance when the TP is fully implemented in 2016.

The Panel encourages ICBC to further develop its Directional measures, including the linking of Road Safety programs and other strategic initiatives impacting traffic within British Columbia to the claims factors affecting actuarial rate indications. The Panel also believes that further assessment, analysis, and explanations of the interrelationships between the Service, Financial, Efficiency, and Directional measures would be helpful. It would be useful to have measures that reflect on how ICBC will sustain its ability to change and improve for the benefit of its customers. The Panel recognizes that this may require further investments in data collection and analysis, but would expect that the ultimate outcome would be enhanced corporate effectiveness and performance.

6.0 ROAD SAFETY

In a letter addressed to IBC dated September 15, 2010, the Commission responded to a request from IBC concerning ICBC's Road Safety programs. The Commission's response included the following:

> The Commission considers that the next full revenue requirements application by ICBC would be an appropriate time to review ICBC's Road Safety programs for operational efficiency and effectiveness education and awareness program costs, and cost allocation matters.
>
> By this letter, ICBC is advised to address road safety matters in its next full revenue requirements application. (Exhibit B-1-1, Chapter 10, Appendix 10-A)

ICBC has responded in this Application by including Chapter 10, Exhibit B-1-1 which addresses Road Safety, together with responses to Information Requests related to Road Safety.

IBC was the only Intervener to address Road Safety in its Argument, and addressed a number of matters it considers to be of concern with respect to Road Safety.

6.1 Road Safety Process

6.1.1 <u>IBC Submission</u>

IBC submits that "(i)t would appear that the Commission is encouraging ICBC to avoid scrutiny on contentious issues, by filing something less than the Commission has requested in the course of an application and subsequently making a "compliance filing." And that ". . . IBC notes that the Commission, further to its Order G-21-12 declined to include Road Safety as part of the oral public hearing. Road safety and the associated allocations have been and continue to be important issues for IBC, but the length of time it has taken to address the issues and the limited scrutiny afforded interveners are not satisfactory." (IBC Argument, pp. 6, 7)

6.1.2 ICBC Reply

ICBC submits that "(t)he present Application included a chapter on Road Safety that meets the Commission's requirements. ICBC provided thorough responses to all IRs on this topic. In short, the processes set by the Commission to assess Road Safety programs have been transparent and appropriate. IBC has had ample opportunity to participate and provide feedback." (ICBC Reply, p. 23)

6.2 Road Safety Issues in the 2012 Application

IBC submits that it ". . . is particularly concerned that road safety programs generally, and not simply education and awareness programs, be tied to an enforcement mechanism, particularly in the absence of measureable outcomes. Clear funding tests and the allocation of various current programs are also a concern." (IBC Argument, p.7)

6.3 Education Programs Tied to Enforcement

IBC submits that it ". . .continues to have concerns that not all of ICBC's road safety programs have measurable outcomes, or that appropriate measurable outcomes have not yet been developed." And that "What is most troubling, however, are programs that have no enforceable consequence and no reliable measurable outcome. Thus, the Safer Vehicles Program, listed in Table 10.6 of the Application as a Road Safety Program focused on Vehicles is a particular concern."
(IBC Argument, p. 7)

6.4 Measureable Outcomes

6.4.1 IBC

IBC expresses a number of concerns in its submissions, including:

- The decreased spending on the Intersection Safety Camera Program may not be justified given the results to date, particularly when ICBC is choosing at the same time to increase funding for something like the Safer Vehicles Program. If there is lower spending occurring it should be on those programs that do not provide measurable results.
- ICBC should be strongly encouraged to carry out evaluations of all its programs and to use indicators that are more reliable.
- The Commission should strongly encourage ICBC to develop more reliable measurements.
- ICBC lists a number of other data sources it reviews including observational studies, contraventions data, ICBC claims data and ICBC actuarial data. Use of this data should be encouraged. ICBC, which enjoys a monopoly in respect of Basic insurance, has access to the data, but to date it has not been effective in using that data to measure the effectiveness of its Road Safety programs or, for that matter, its claims handling, as noted above.

6.4.2 ICBC

In its Reply, ICBC's responses include:

- ICBC has explained in the Application that the one-time project expenditures are ramping down because the ISC upgrade and expansion project is complete and the ISC Program is fully operational. However, there are now more cameras in place, and the anticipated claims savings are reflected in the forecasts. (ICBC Reply, p. 23)
- Challenges associated with measuring the traffic safety impacts of certain Road Safety programs are common across jurisdictions because of the difficulty of attributing observed changes to a specific program or tactic when there are so many factors that influence collision outcomes over a given period of time. ICBC is developing a new Road Safety Monitoring and Evaluation Framework, which will review evaluation criteria for programs and tactics. ICBC anticipates filing the results of the review in September 2013. (ICBC Reply, p. 24)

6.5 Allocation of Road Safety Programs

6.5.1 IBC Submission

IBC submits that "ICBC has developed a definition of "road safety," but the definition is sufficiently vague that that any program ICBC deems to be road safety fits within the definition. What constitutes “road safety” is also left entirely to ICBC to determine. (Exhibit B-6, 2012.1 RR IBC.32.2) What is lacking is some objective determination by a third party. (IBC Argument, p. 8)

With respect to the Safer Vehicles Program, IBC states that it “. . . is allocated 100% to Basic since, according to ICBC, “it conforms to the definition of a road safety program.” (IBC Argument p. 9)

IBC also submits, with respect to the Safer Vehicles Program, that:

- There is nothing that establishes a proper link such as to conclude it is a proper road safety expenditure;
- There is no enforcement mechanism;
- Education and awareness was eliminated from the Drivers category but has now been moved to the Vehicles category;
- It is not a proper Road Safety program.

  (IBC Argument, pp.8, 9)

IBC also submits that the Bait Car Program is a concern because of benefits to Optional at Basic’s expense and that ICBC continues to use regulatory schemes such as the MOU [Memorandum of Understanding] to do indirectly what it cannot do directly. (IBC Argument, p. 10)

6.5.2 ICBC

In its Reply, ICBC’s responses include:

- The Commission, an objective third party, approved the definition of “Road Safety.” ICBC has described the process that it follows to determine, in the first instance, whether a program meets the approved definition of “Road Safety.” The Commission oversees the allocation methodology. IBC’s argument should be rejected.
- ICBC submits that the Safer Vehicles Program falls within the approved definition of a Road Safety program, has reliable measureable outcomes, and falls within ICBC’s mandate to “promote and improve highway safety.” (ICBC Reply, p. 9)

ICBC also submits that IBC is correct that there is a benefit to both Basic and Optional associated with IMPACT (as there had been with BAIT Car Program); however, the Commission has no jurisdiction to make the allocation advocated by IBC. *Special Direction IC2* requires that the Commission fix Basic rates so as to cover all costs of the MOU, and IMPACT (unlike BAIT Car) is a program established under the MOU. (ICBC Reply, p. 25)

6.6 Allocation of Other Campaigns

6.6.1 IBC

IBC submits that:

- "ICBC continues to allocate the cost of its advertising campaigns to Basic. The campaigns may not be within the road safety budget, but if they are to be charged to Basic, particularly at a time when Basic requires rate increases, they should be contributing something to Basic." (IBC Argument, p. 10); and
- that two of ICBC's ads "have nothing to do with Basic coverage, but Basic is paying for them. Evidently there is something wrong with the allocator." (IBC Argument, p. 11)

6.6.2 ICBC Reply

ICBC responds that "Advertising is an integral component of the applicable program it supports and the advertising costs are allocated accordingly. The attribution of advertising costs to either Basic insurance or Optional insurance is based on the character of the particular program that appropriately recognizes the line of business that is benefitting from the expenditure and is consistent with *Special Direction IC2*. Corporate initiatives such as the "Share a Wave and Win" campaign, which are not Road Safety, are allocated appropriately between Optional and Basic insurance. (ICBC Reply, pp. 25, 26)

6.7 Commission Determination

6.7.1 Road Safety Process

IBC complains that the Commission is somehow encouraging ICBC to avoid scrutiny on contentious issues and what it describes as the limited scrutiny afforded to address issues which are important to IBC. The Panel notes that IBC devotes a significant part of its Argument with respect to Road Safety to ICBC's Safer Vehicles Program, an initiative ". . . to inform drivers about the availability, effectiveness, and use of new vehicle technologies and safety features, and help support their decision-making when buying a vehicle." (Exhibit B-1-1, Appendix 10-B, p. 32) The Panel also notes that the Safer Vehicles Program has a 2012 planned expenditure of $280 thousand, (Exhibit B-6, 2012.1 RR BCUC.117.1), which accounts for something in the order of one-half of one percent of ICBC's PY 2012 Basic Road Safety and loss management expense.

The Panel has reviewed ICBC's evidence, including the responses to Information Requests, and finds that it is sufficiently comprehensive to meet the Commission's requirements for the purposes of this Application.

The Panel suggests that if IBC has ongoing issues respecting Road Safety, it should more clearly articulate and quantify the nature and reasons for, and significance of its concerns.

6.7.2 Measureable Outcomes

ICBC's development of targets for driver programs has historically been based on police-reported crashes in the Traffic Accident System (TAS) and has been the only source of observation information about human factors that contribute to any specific crash in BC.
(Exhibit B-6, 2012.1 RR IBC.29.2)

The Panel notes impact of the 2008 changes to the TAS and the resulting inability to use the data to track collision changes as was previously the case. (Exhibit B-6, 2012.1 RR BCUC.107.1.1) The Panel shares the concerns that have been expressed respecting the need to obtain and use appropriate data for program evaluations.

The Panel expects that ICBC's Road Safety Monitoring and Evaluation Framework, presently under development, will be a fundamental component in understanding ICBC's Road Safety programs and an important tool for assessing the impact of the programs. **The Panel directs ICBC to file the Road Safety Monitoring and Evaluation Framework with the Commission when it is completed in September 2013.**

6.7.3 Allocation of Road Safety Programs

Special Direction IC2 requires all costs under the Traffic and Road Safety Enforcement Funding MOU to be funded from Basic Insurance, which includes IMPACT's Bait Car program. The Panel considers that the Safer Vehicles Program contributes to highway safety and agrees with ICBC's submission that the Safer Vehicles Program falls within the definition of a Road Safety program.

Since its inception, the bait fleet has been expanded to include ATV's, snowmobiles, various watercraft, motorcycles and manufactured trailers. Only vehicles operated on a highway in BC must be licensed and insured with at least Basic Insurance. Neither watercraft nor manufactured trailers are considered to be vehicles and cannot be licensed and insured under Basic Insurance. (Exhibit B-7, 2012.2 RR BCUC.177.2) The Panel considers that the use of ATV's, snowmobiles, and various watercraft as part of the Bait Car program, funded by Basic Insurance, do not fall within ICBC's definition of a Road Safety program.

The Panel shares IBC's concern that ICBC's Optional Insurance business may benefit at the expense of Basic Insurance due to the operation of the Traffic and Road Safety Enforcement Funding MOU and its required funding from Basic Insurance premiums under *Special Direction IC2.* The Panel also notes ICBC's acknowledgement that there is a benefit to both Basic and Optional associated with IMPACT. The Panel considers that other providers of optional insurance, including IBC's stakeholders, may also benefit from the IMPACT and other Road Safety programs.

ICBC is encouraged to seek amendments to the Traffic and Road Safety Enforcement Funding MOU and or *Special Direction IC2* which enable a fair, equitable and transparent allocation of costs of the Road Safety programs which benefit both the Basic and Optional Insurance businesses. **ICBC is directed to report the results of its efforts to obtain such amendments with its next Road Safety report to the Commission.**

7.0 OTHER MATTERS

7.1 ICBC Autoplan Agency Agreements

ICBC has not issued new Autoplan Agency Agreements (Agreements) since 1992. Since brokers are permitted to sell or transfer an Agreement subject to the approval of ICBC, a market has been created for Agreements that is based on supply and demand. ICBC does not track or regulate the value of Agreements and the value of a transaction is not required to be disclosed to ICBC. Therefore ICBC does not comment on their value. ICBC believes the public is well served by the current number of Agreements and believes that because they are transferable, brokers compete for areas that they perceive to be underserved. ICBC does not take into consideration the value of an Agreement when determining Basic Insurance fee costs for customers. (Exhibit B-6, 2012.1 RR VEJ.6.0)

ICBC also submits that as Agreements are transferable and as brokers compete with one another for business, increases with respect to policy or population growth are typically absorbed by the current number of Agreements. There is no limit to the customer volume growth on an Agreement so brokers are often eager to attract new customers and grow their businesses, thereby mitigating the need to add new Agreements based on population growth. ICBC monitors customer satisfaction and feedback with respect to distribution of Agreements and at present does not see a need to issue additional Agreements; however, ICBC reserves the right to issue new Agreements in the event there is evidence that a community is underserved.

7.1.1 Commission Determination

The Panel believes that the number of Agreements should reflect operational efficiency when serving customers, which would affect Basic Insurance policyholders. The Panel encourages ICBC to consider developing objective criteria, potentially in consultation with existing and prospective brokers, to assess whether existing number of Agreements available is appropriate, seek options to improve broker operations efficiency, and confirm that communities are well served.

The Panel finds that a set of objective criteria and ongoing assessment relating to ICBC's Autoplan Agency Agreements would be useful information to include in the next revenue requirement application.

7.2 Mechanism to Bill Customers

As part of the Application, ICBC had requested approval of an interim rate increase of 11.2 percent for implementation with an effective date on or after February 1, 2012, and stated that ". . . it does not currently have a mechanism to bill customers if the approved permanent rate is higher than the approved interim rate but will work towards developing a system that has this capability by the time of an affected customer's next policy renewal date." (Exhibit B-1 p. 1 of Appendix A)
If the Commission approves a permanent Basic Insurance rate in 2012 that is higher than the interim Basic Insurance rate, ICBC will retroactively bill customers the difference between Basic Insurance rates. The costs to make the required system changes to CCRS are estimated to be $308,000. The impact on policyholders would be minimal. (Exhibit B-6, 2012.1 RR BCUC.4.2-3)

7.2.1 Commission Determination

The Panel notes that the system to deal with refunds was developed in 2007, but did not include the capacity to bill rates higher than the requested interim rates. Now the costs to make such a system changes are estimated to be $308,000.

The Commission's rate determination in this Decision renders this issue moot at this time. **The Panel considers that such capability may be required in the future, and directs ICBC to ensure that such capability will be available in conjunction with any future application for interim rates.**

7.3 Comments on the Regulatory Review Process

CDI submits that ICBC's designation of policy years may cause inconsistency in how the rate is determined for a particular policy year. (CDI Argument, pp. 10, 11)

It suggests that ICBC be required to file a yearly Basic rate application, whether streamlined if it is seeking to reduce, seeking no increase or looking for a slight increase in rates or non-streamlined for a rate increase of over 2.5%. It also suggests that the application be filed by a designated filing date, to be set a period of months in advance of each policy year which would commence on January 1st of each calendar year. In other words, a policy year would equate to a calendar year. (CDI Argument, p. 12)

IBC expresses concern both about the scheduling of ICBC's full revenue requirements applications and the limited opportunity of Interveners to cross-examine and submits that a more consistent timetable may help establish rates that are more stable and predictable. In other words, the full revenue requirements hearings, if required, should be brought into line with the streamlined timetable. (IBC Argument, p. 11)

IBC suggests that there is a need for better timing and reporting of full revenue requirements applications and states that "Ideally, ICBC should be required to advise by May of each calendar year whether no increase, a limited increase or something greater is required and proceed with its filings accordingly." (IBC Argument, p. 11)

7.3.1 ICBC Reply

ICBC submits that it deferred the Application in order to ". . . look for ways to reduce operating expenses and manage growth in BI claims costs; and, explore whether it was possible to develop a better mechanism to apply the (then) Basic excess capital to mitigate the rate increase.", and that ". . . relative stability and predictability of rates encompasses an element of balancing the magnitude of rate increases against subjecting policyholders to frequent rate changes."
(ICBC Reply, p. 4)

7.3.2 Commission Determination

The Panel acknowledges the concerns raised regarding the overall regulatory review process and timing for ICBC revenue requirement applications. The Panel considers that having ICBC indicate the magnitude of a Basic Insurance rate change and a timeframe for such filing would benefit in keeping relatively stable and predictable rates. However, the Panel is also aware that *Special Direction IC2* does not specify the timeframe in which ICBC must file its revenue requirement application before the Commission.

The Panel considers that timely filing of a revenue requirement application could mitigate large fluctuations in Basic Insurance rates, and allow rates to be kept relatively more stable and predictable.

8.0 CONCLUSION

In reaching the determinations and directions in this Decision, the Panel has considered all relevant materials comprising the record of this proceeding, including the evidence of ICBC, and the Arguments and Reply provided by each Party.

References in this Decision to specific parts of the record are intended to assist the reader in understanding the Panel's reasoning relating to a particular matter and should not be taken as an indication that the Panel did not consider all relevant portions of the record with respect to that matter.

All the components of the 2012 Indicated Rate Change which the Panel must consider in setting rates for Basic Insurance have been addressed in this Decision. In the aggregate, the approval of these components supports the Application for the requested 11.2 percent increase to Basic Insurance rates.

The Application's requested 11.2 percent increase in universal compulsory automobile insurance (Basic Insurance) rates for the Policy Year 2012, commencing February 1, 2012, is approved.

DATED at the City of Vancouver, in the Province of British Columbia, this 16th day of August 2012.

Original signed by:

A.W.K. ANDERSON
PANEL CHAIR AND COMMISSIONER

Original signed by:

M.R. HARLE
COMMISSIONER

Original signed by:

R.D. REVEL
COMMISSIONER

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BRITISH COLUMBIA UTILITIES COMMISSION

ORDER NUMBER G-109-12

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IN THE MATTER OF
the Utilities Commission Act, R.S.B.C. 1996, Chapter 473

and

the Insurance Corporation Act, R.S.B.C. 1996, Chapter 228, as amended

and

An Application by the Insurance Corporation of British Columbia
for Approval of the Revenue Requirements for Universal Compulsory Automobile Insurance
for the Policy Year Commencing February 1, 2012

BEFORE: A.W.K. Anderson, Panel Chair/ Commissioner
M.R. Harle, Commissioner
R.D. Revel, Commissioner August 16, 2012

O R D E R

WHEREAS:

A. On December 1, 2011, the Insurance Corporation of British Columbia (ICBC) submitted an application to the British Columbia Utilities Commission (Commission) for approval of the Revenue Requirements for Universal Compulsory Automobile Insurance (Basic Insurance) for the policy year commencing February 1, 2012 (the Application);

B. The Application seeks Commission approval for a permanent 11.2 percent increase in Basic Insurance rates, pursuant to sections 59 to 61 of the *Utilities Commission Act*, and *the Insurance Corporation Act*, to apply:

i. to all new and renewal policies with an effective date on or after February 1, 2012 that have: (i) premiums determined through the use of the Schedule of Basic Insurance Premiums (Schedule C) as filed with the Commission, excluding rate classes 800 and 900 – 906 and excluding policies relating to vehicles located on isolated islands; and (ii) premiums determined under a Fleet Reporting Policy, (together the Plate Owner Basic and Fleet Reporting Policies);

ii. to all new and renewal policies other than the Plate Owner Basic and Fleet Reporting Policies effective on the first day of the first month that is at least 60 days following the Commission's final decision on the Application;

.../2

C. The Application also sought interim relief, pursuant to section 89 of the *Utilities Commission Act* and section 15 of the *Administrative Tribunals Act*, to allow a rate increase of 11.2 percent to apply on an interim refundable basis for all new and renewal Plate Owner Basic and Fleet Reporting Policies with an effective date on or after February 1, 2012, pending the hearing of the Application and orders subsequent to the hearing;

D. By Order G-221-11, the Commission approved the requested 11.2 percent interim refundable rate increase for implementation with an effective date on or after February 1, 2012 for all new and renewal Plate Owner Basic and Fleet Reporting Policies. The Commission also established an Initial Regulatory Timetable for the review of the Application, which included a Workshop held on January 23, 2012 and a Pre-hearing Conference held on February 23, 2012;

E. By Order G-21-12, subsequent to the Pre-hearing Conference, the Commission established a Revised Regulatory Timetable to review the Application. The Revised Regulatory Timetable included: (i) an Oral Public Hearing for actuarial matters only and (ii) ICBC and Intervener Oral Final Arguments, and ICBC Oral Reply Argument;

F. By letter dated May 15, 2012, the Commission invited comments from ICBC and Interveners to amend the Revised Regulatory Timetable regarding the necessity of a limited Oral Public Hearing on actuarial matters only, and potentially replacing the oral argument process with written arguments;

G. By Order G-62-12, subsequent to comments received from ICBC and four Interveners, the Commission established an Amended Regulatory Timetable for the remaining regulatory process. The Amended Regulatory Timetable comprised: (i) Commission Panel Information Requests, if any, on actuarial matters; (ii) ICBC and Intervener Written Final Arguments; and (iii) ICBC Written Reply Argument. The Amended Regulatory Timetable replaced both the limited Oral Public Hearing on actuarial matters and the oral argument process;

H. On June 8, 2012, ICBC filed its Final Argument;

I. Six Interveners filed Final Argument by June 18, 2012: Canadian Direct Insurance, Pemberton Insurance Corporation, the Automobile Insurance Committee of the Canadian Bar Association, Mr. Frank Duck, Insurance Bureau of Canada, Voice for Economic Justice, and BC Old Age Pensioners Organization *et al*.;

J. On June 22, 2012, ICBC filed its Reply Argument; and

K. The Commission has considered the Application, the evidence and submissions all as set forth in the Decision issued concurrently with this Order.

NOW THEREFORE pursuant to sections 59 to 61 of the *Utilities Commission Act*, the Commission orders as follows:

1. A permanent 11.2 percent Basic Insurance rate increase is approved, to apply:

   (i) to all new and renewal policies with an effective date on or after February 1, 2012 that have: (i) premiums determined through the use of the Schedule of Basic Insurance Premiums (Schedule C) as filed with the Commission, excluding rate classes 800 and 900 – 906 and excluding policies relating to vehicles located on isolated islands; and (ii) premiums determined under a Fleet Reporting Policy, (together the Plate Owner Basic and Fleet Reporting Policies);

   (ii) to all new and renewal policies other than the Plate Owner Basic and Fleet Reporting Policies effective on the first day of the first month that is at least 60 days following the date of this Decision;

2. Policyholders who renewed or purchased new policies in the period between February 1, 2012 and the effective date of this Order are to be notified of the permanent increase in the most cost effective manner, which is to be determined by ICBC. The notice must be reviewed by the Commission in advance of its release. For policyholders renewing or purchasing new policies after the effective date of this Order, notice of the permanent increase will be given with the Notice to Renew or other similar form issued by ICBC to Basic Insurance policyholders in the ordinary course of business for renewal policies, and at the time of purchase for new policies.

3. The Commission will accept, subject to timely filing, amended Basic Insurance rate schedules in accordance with the terms of this Order.

4. ICBC is directed to comply with all determinations and directives set out in the Decision that is issued concurrently with this Order.

DATED at the City of Vancouver, in the Province of British Columbia, this 16th day of August 2012.

BY ORDER

Original signed by:

A.W.K. Anderson
Panel Chair and Commissioner

SUMMARY OF DIRECTIVES

This Summary is provided for the convenience of readers. In the event of any difference between the Directions in this Summary and those in the body of the Decision, the wording in the Decision shall prevail.

	Directive	Page
1.	The Commission Panel approves an 11.2 percent Basic Insurance rate increase for the Policy Year 2012, commencing February 1, 2012.	2
2.	ICBC's use of the 12-year exponential model for the period ending first quarter 2008 provides an appropriate base for estimating the BI Frequency sub-component of the PY 2010 Loss Cost Variance.	21
3.	At a minimum, the 5.5 percentage point Loss Cost Forecast Variance component, incorporating the use of ICBC's 12 and 6.25 year exponential models respectively for Personal BI frequency and severity, is acceptable for use in determining the forecast of loss costs components of the PY 2012 Indicated Rate Change.	21
4.	The Panel agrees with ICBC that prospective adjustments should be made based on sufficient data and the use of accepted actuarial practice and determines that the prospective adjustment made with respect to the ISC Project is appropriate in calculating the Loss Trend to PY 2012.	27
5.	At a minimum, the +1.9 percentage point Loss Trend to PY 2012, including the treatment of prospective adjustments, should be approved as requested in the Application.	28
6.	ICBC's evidence respecting its methodology of determining the impact of the New Money Rate and Yield on Basic Equity to be persuasive, and accordingly approves, at a minimum, the use of the +2.5 percentage point Investment Income and Premium Financing Revenue component of the Indicated Rate Change as requested in the Application.	31
7.	Operating Expenses are not adding to the Indicated Rate Change.	37
8.	In full revenue requirements applications, ICBC is directed to file full operating cost details, including divisional information.	37, 38
9.	ICBC is directed to provide a comprehensive qualitative and quantitative analysis of the TP benefits anticipated to flow through to the Basic Insurance business. This analysis should be provided prior to the commencement of the 2014 policy year	39

SUMMARY OF DIRECTIVES

10.	ICBC is directed to file year-to-date MCT ratio calculations, estimated as described in Exhibit B-13, 2012.CP RR BCUCP.9.1-2, not later than 30 days following the end of each calendar month, together with MCT ratio estimates for the following two calendar quarters. In the event that any of the estimates indicate a MCT ratio of less than 100 percent, ICBC is further directed to file with the Commission an application for a rate change to ensure that the MCT ratio is maintained at or above the 100 percent regulatory minimum. ICBC is directed to continue the monthly filings until otherwise directed by the Commission.	46
11.	ICBC's evidence adequately supports the determination of the +0.4 impact of IFRS Changes in the PY 2012 Indicated Rate Change.	47
12.	ICBC is directed to prepare and submit to the Commission a report illustrating a five year forecast of the impact of these trends on the Basic Insurance Trend in Average Premium. The report should also address any rate design and or discount initiatives ICBC might take to mitigate the impact of the increasing average trend in premiums. The report should be submitted to the Commission by May 31, 2013.	48
13.	ICBC's evidence with respect to the various indicated rate change components adequately supports a PY 2012 Indicated Rate Level Change of at least +11.2 percent.	50
14.	ICBC is directed to specifically include anticipated benefits for its Claims Initiatives in the Transformation Program analysis directed in Section 3.4.4 of the Decision.	53
15.	The Panel encourages ICBC to further develop its Directional measures, including the linking of Road Safety programs and other strategic initiatives impacting traffic within British Columbia to the claims factors affecting actuarial rate indications.	55
16.	ICBC is to file the Road Safety Monitoring and Evaluation Framework with the Commission when it is completed in September 2013.	62
17.	ICBC is directed to report the results of its efforts to obtain such amendments with its next Road Safety report to the Commission.	63
18.	The Panel considers that such capability may be required in the future, and directs ICBC to ensure that such capability will be available in conjunction with any future application for interim rates.	65
19.	The Application's requested 11.2 percent increase in universal compulsory automobile insurance (Basic Insurance) rates for the Policy Year 2012, commencing February 1, 2012, is approved.	68

LIST OF ACRONYMS AND ABBREVIATIONS

AAP	Accepted Actuarial Practice
AIC	The Automobile Insurance Committee of the Canadian Bar Association
Application, Exhibit B-1, or Exhibit B-1-1	Revenue Requirements for Universal Compulsory Automobile Insurance for the Policy Year Commencing February 1, 2012
Basic Insurance	Universal Compulsory Automobile Insurance
BCOAPO	British Columbia Old Age Pensioners' Organization *et al.*
BCUC, or Commission	British Columbia Utilities Commission
BI	Bodily Injury
BU	Bargaining Unit
CDI	Canadian Direct Insurance
CGAAP	Canadian Generally Accepted Accounting Principles
CMP	Capital Management Plan
CMT	Capital Management Target
IBC	Insurance Bureau of Canada
ICBC, or Corporation	Insurance Corporation of British Columbia
IFRS	International Financial Reporting Standard
IMPACT	Integrated Municipal Provincial Auto Crime Team
IR	Information Request(s)
ISC	Intersection Safety Camera
M&C	Management and Confidential
MCT	Minimum Capital Test
MOU	Memorandum of Understanding

LIST OF ACRONYMS AND ABBREVIATIONS

NMR	New Money Rate
OIC	Order in Council
OSFI	Office of Superintendent of Financial Institutions
PED	Personal Electronic Device
Pemberton	Pemberton Insurance Corporation
PY 2012	Policy Year 2012, Commencing February 1, 2012
RRA	Revenue Requirements Application
Special Direction IC2, or IC2	Special Direction IC2 to the BC Utilities Commission, BC Regulation 307/2004
SRRA	Streamlined Revenue Requirements Application
STIP	Short Term Incentive Program
TAS	Traffic Accident System
TP	Transformation Program
UCA	Utilities Commission Act
VEJ	Voice for Economic Justice

IN THE MATTER OF
the Utilities Commission Act, R.S.B.C. 1996, Chapter 473

and

Insurance Corporation of British Columbia
2012 Revenue Requirements Application

LIST OF EXHIBITS

Exhibit No.	Description
COMMISSION DOCUMENTS	
A-1	Letter L-92-11 dated December 7, 2011 – Requesting Stakeholder Submissions on Interim Rates
A-2	Letter dated December 7, 2011 – Appointment of Commission Panel
A-3	Letter dated December 16, 2011 – Order G-221-11 Initial Regulatory Timetable
A-4	Letter dated February 8, 2012 – Information Request No. 1 to ICBC
A-5	Letter dated February 20, 2012 – Additional Information regarding Pre-hearing Conference
A-6	Letter dated February 23, 2012 – Revised Commission Staff Draft of Regulatory Timetable Options
A-7	Letter dated February 29, 2012 – Order G-21-12 Revised Regulatory Timetable
A-8	Letter dated March 2, 2012 – Accepting Hans Karow request to Withdraw Intervener status (Exhibit C4-3)
A-9	Letter dated April 2, 2012 – Information Request No. 2 to ICBC
A-10	Letter dated May 14, 2012 – Denied Automobile Insurance Committee Request for an Extension to file Evidence
A-11	Letter dated May 15, 2012 – Oral Public Hearing Request for Comments
A-12	Letter dated May 22, 2012 – Order G-62-12 Amended Regulatory Timetable
A-13	Letter dated May 24, 2012 - Commission Panel Information Request on Actuarial Matters

Exhibit No.	Description
A-14	Letter dated May 31, 2012 – Accepting Don Rosenbloom's request to Withdraw Intervener status (Exhibit C13-3)
A-15	Letter dated June 19, 2012 – Reply Argument Submission Extension

APPLICANT DOCUMENTS ICBC

B-1	**INSURANCE CORPORATION OF BRITISH COLUMBIA (ICBC)** Letter dated December 1, 2011 - 2012 Revenue Requirements Application Volume 1
B-1-1	Letter dated December 1, 2011 - 2012 Revenue Requirements Application Volume 2
B-1-2	Letter dated December 1, 2011 - Actuarial Rate Level Indication Analysis Excel Exhibits (Zip file - 2.35 Mb)
B-2	**CONFIDENTIAL** Letter dated December 1, 2011 – Confidential ICBC Customer Notices
B-3	Letter dated December 13, 2011 – ICBC Reply to Stakeholder Comments on Interim Rate
B-4	Letter dated January 23, 2011 – ICBC Submitting Workshop Presentation
B-5	Letter dated February 10, 2012 – ICBC Submitting Confirmation of Public Notices
B-6	Letter dated March 12, 2012 – ICBC Responses to Information Requests No. 1 on ICBC's Revenue Requirements Application for the 2012 Policy Year
B-7	Letter dated April 26, 2012 - ICBC Responses to Information Requests No. 2 to BCUC, BCOAPO, CDI, IBC and Frank Duck
B-8	Letter dated May 10, 2012 - ICBC Response to AIC Request for Filing Extension
B-9	Letter dated May 17, 2012 – ICBC Submitting Witness Panel and Direct Testimony
B-10	Letter dated May 18, 2012 – ICBC Submitting Comments on Revised Regulatory Timetable Options
B-11	Letter dated May 18, 2012 – ICBC Submitting Errata to the Application and Responses to BCUC, Frank Duck and IBC Information Request No. 1

Exhibit No.	Description
B-12	Letter dated May 22, 2012 – ICBC Submitting witness panel and direct testimony
B-13	Letter dated May 31, 2012 – ICBC Submitting Responses to Commission Panel Information Requests on Actuarial Matters

INTERVENER DOCUMENTS

C1-1	**TRIAL LAWYERS ASSOCIATION OF BC (TLABC)** Online Registration Dated December 16, 2011 – Request for Intervener Status by Carla Terzariol
C1-2	Letter Dated December 12, 2011 – TLABC Submission on Interim Rates
C2-1	**AUTOMOBILE INSURANCE COMMITTEE (AIC)** Letter Dated December 12, 2011 – Request for Intervener Status by Sheane Flewlling and AIC Submission on Interim Rates
C2-2	Letter Dated February 12, 2012 – AIC Submission of Information Request
C2-3	Letter Dated May 10, 2012 – AIC Submission Requesting Filing Extension
C2-4	Letter Dated May 11, 2012 – Confirmation of Expert Witness and Request to file Expert Evidence by May 17, 2012
C2-5	Letter dated May 18, 2012 – AIC Submitting Comments on Revised Regulatory Timetable Options
C3-1	**CANADIAN DIRECT INSURANCE (CDI)** Online Registration Dated December 16, 2011 – Request for Intervener Status by Karen Hopkins-Lee
C3-2	Letter dated February 1, 2012 – CDI Information Request No. 1
C3-3	Letter dated February 1, 2012 – CDI Information Request No. 2 to ICBC
C4-1	**KAROW, HANS (KH)** Letter Dated December 17, 2011 Via Email – Request for Intervener Status by Hans Karow
C4-2	Letter dated January 10, 2012 – Submission of Evidence
C4-3	Letter dated February 29, 2012 – Submitting notification regarding removal of Intervention

Exhibit No.	Description
C5-1	**CANADIAN OFFICE AND PROFESSIONAL EMPLOYEES UNION LOCAL 378 (COPE 378)** Letter Dated January 9, 2012 Via Email – Request for Intervener Status by Jim Quail
C6-1	**MINISTRY OF PUBLIC SAFETY AND SOLICITOR GENERAL (MPS)** Letter Dated January 6, 2012 – Request for Intervener Status by C. Foerstner
C7-1	**INSURANCE BUREAU OF CANADA (IBC) –** Letter Dated January 11, 2012 Via Email – Request for Intervener Status by Lindsay Olson
C7-2	Letter Dated December 12, 2011 – IBC Submission on Interim Rates
C7-3	Letter Dated February 15, 2012 – IBC Submitting Information Request No. 1
C7-4	Letter Dated April 3, 2012 – IBC Submitting Information Request No. 2
C7-5	Letter dated May 18, 2012 – IBC Submitting Comments on Revised Regulatory Timetable Options
C8-1	**LANDALE, RICHARD (LR)** Online Registration Dated January 11, 2012 – Request for Intervener Status
C8-2	Letter Dated January 13, 2012 – LR Submitting comments on the Application
C8-3	Letter Dated June 15, 2012 - LR Submitting comments
C9-1	**PEMBERTON INSURANCE CORPORATION (PEMBERTON)** – Online Registration Dated January 12, 2012 – Request for Intervener Status by Roger Finnie
C9-2	Letter Dated December 12, 2011 – Pemberton Submission on Interim Rates
C10-1	**DUCK, FRANK (FD)** Letter Dated January 17, 2012 Via Email – Request for Intervener Status by Frank Duck
C10-2	Letter Dated December 12, 2011 – FD Submission on Interim Rates
C10-3	Letter dated February 15, 2012 – FD Submitting Information Request No. 1
C10-4	Letter Dated April 3, 2012 – FD Submitting Information Request No. 2
C10-5	Letter dated May 18, 2012 – FD Submitting Comments on Revised Regulatory Timetable Options

Exhibit No.	Description
C11-1	**VOICE FOR ECONOMIC JUSTICE (VEJ)** was **CETERIS PARIBUS COMPANY (CPRC)** Online Registration and Letter Dated January 16, 2012 Via Email – Request for Intervener Status by Jason Strauss
C11-2	Letter dated February 13, 2012 – CPRC Submitting Information Request No. 1 Part 1
C11-3	Letter dated February 17, 2012 – Submitting change of Name for Intervention Voice for Economic Justice
C12-1	**BCAA ROAD SAFETY FOUNDATION (BCAARSF)** Online Registration and Letter Dated January 16, 2012 Via Email – Request for Intervener Status by Allan Lamb
C13-1	**ROSENBLOOM, DON (DR)** Letter Dated January 19, 2012 Via Email – Request for Intervener Status by Don Rosenbloom
C13-2	Letter dated February 15, 2012 – DR Submitting Information Request No. 1
C13-3	Letter dated May 28, 2012 Via Email - DR Submitting withdrawing Intervener Status
C14-1	**BRITISH COLUMBIA OLD AGE PENSIONERS' ORGANIZATION (BCOAPO ET AL)** Letter Dated January 19, 2012 Via Email – Request for Intervener Status by Leigha Worth and James Wightman
C14-2	Letter Dated December 12, 2011 – BCOAPO et al Submission on Interim Rates
C14-3	Letter Dated February 15, 2012 – BCOAPO et al Information Request No. 1
C14-4	Letter Dated April 3, 2012 – BCOAPO et al Information Request No. 2
C14-5	Letter dated April 23, 2012 - BCOAPO et al Submitting Consultant update
C14-6	Letter dated May 18, 2012 – BCOAPO Submitting Comments on Revised Regulatory Timetable Options
C14-7	Letter dated June 15, 2012 - BCOAPO Submitting Request for Filing Extension
C15-1	**YELLOW CAB / VANCOUVER TAXI ASSOCIATION (YC)** Online Registration Dated January, 19, 2012 – Request for Intervener Status by Carolyn Bauer and Sahota Kulwant

Exhibit No.	Description
INTERESTED PARTY DOCUMENTS	
D-1	**FANG, JOASH (FJ)** Online Registration Dated January 6, 2012 – Request for Interested Party Status by Joash Fang
D-2	**CHAMBERS, JEFFREY (CJ)** Online Registration Dated January 6, 2012 – Request for Interested Party Status by Jeffrey Chambers
D-3	**INSURANCE BROKERS ASSOCIATION OF BC (IBABC)** Letter Dated January 16, 2012 Via Email – Request for Interested Party Status by C.J Byrne
LETTERS OF COMMENT	
E-1	**MARSHALL, GORD CANADIAN AVIATION QUALITY CONSULTING INC.** Letter of Comment dated December 3 , 2011
E-2	**MANN, JONATHAN** Letter of Comment dated December 7 , 2011
E-3	**PETER, CARL AND GAIL** Letter of Comment dated December 7 , 2011
E-4	**DESAI, F** Letter of Comment dated December 7 , 2011
E-5	**FOSTER, RUSS** Letter of Comment dated December 2 , 2011
E-6	**MIKE** Letter of Comment dated December 2 , 2011
E-7	**BURLEY, BRUCE** Letter of Comment dated December 8 , 2011
E-8	**LEIPERT, KLAUS** Letter of Comment dated December 8 , 2011
E-9	**SWANSON, JOANN** Letter of Comment dated December 2 , 2011
E-10	**MACDONALD, MURRAY** Letter of Comment dated March 18 , 2012
E-11	**BONA, BYRON M.** Letter of Comment dated March 12 , 2012
E-12	**KAROW, HANS** Letter of Comment dated March 21 , 2012

OIC NO. 560 WITH LETTER OF DIRECTION

PROVINCE OF BRITISH COLUMBIA

ORDER OF THE LIEUTENANT GOVERNOR IN COUNCIL

Order in Council No. 560 *, Approved and Ordered* NOV 30 2011

Lieutenant Governor

Executive Council Chambers, Victoria

On the recommendation of the undersigned, the Lieutenant Governor, by and with the advice and consent of the Executive Council, orders that approval is given to the attached letter of direction, dated November 25, 2011 issued by the Minister of Public Safety and Solicitor General to the Insurance Corporation of British Columbia.

Minister of Public Safety and Solicitor General

Presiding Member of the Executive Council

(This part is for administrative purposes only and is not part of the Order.)

Authority under which Order is made:

Act and section: *Insurance Corporation of British Columbia*, R.S.B.C. 1996, c. 228, ss. 7 and 47

Other: Special Direction IC2 to the British Columbia Utilities Commission, B.C. Reg. 307/2004; s. 3 (1) (c.1)

November 28, 2011 O/858/2011/88

OIC NO. 560 WITH LETTER OF DIRECTION

BRITISH
COLUMBIA

NOV 25 2011

Ms. Nancy McKinstry
Chair
Insurance Corporation of British Columbia
Room 517, 151 West Esplanade
North Vancouver BC V7M 3H9

Dear Ms. McKinstry:

I am writing to provide direction to the Insurance Corporation of British Columbia (ICBC), regarding its use of Basic capital to bring greater stability and predictability in universal compulsory vehicle (Basic) insurance rates. In providing this letter, I respect the fact that responsibility for approving Basic insurance rates rests with the independent BC Utilities Commission.

Government is cognizant of the impact that increases to Basic insurance rates can have on British Columbia drivers and their families. On May 18, 2010, Government issued a directive to ICBC to establish a framework for rate stability while minimizing the need for Basic rate increases by directing ICBC to use Basic excess capital to help moderate future actuarially indicated rate increases.

ICBC has identified that ICBC Basic Capital levels have eroded over 2011, due to lower investment income and higher bodily injury costs. Additionally, ICBC has identified that there is pressure on ICBC Basic insurance rates due to these factors.

The May 2010 direction letter requires ICBC and BCUC to use information on ICBC's Basic capital position from the end of the previous calendar year, which is aligned with ICBC's normal reporting cycle. Using more up-to-date information is important in the present context of a lower interest rate environment, where ICBC's capital position may change significantly between the end of the previous year and the time ICBC files a revenue requirements application to set Basic rates.

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OIC NO. 560 WITH LETTER OF DIRECTION

Ms. Nancy McKinstry
Page 2

Additionally, Government believes that there is an opportunity for ICBC to use more Basic capital to manage Basic insurance rate pressures in the short term than is currently permitted under ICBC's Basic Insurance Capital Management Plan. ICBC's Capital Management Plan is currently based on maintaining a certain amount of capital above the minimum capital requirements specified in *Special Direction IC2 to the British Columbia Utilities Commission,* which is 100 percent Minimum Capital Test (MCT). Government believes that the capital available above the Basic insurance regulatory minimum should be made available to help manage rates.

Consequently, ICBC is directed as follows:

> First, for the purposes of applying the terms of the May 2010 direction letter, ICBC is to hereafter use the most recent quarter Basic insurance MCT level to determine the Basic insurance revenue requirements, rather than using the MCT at the end of the previous calendar year.
>
> Second, notwithstanding the May 2010 letter, ICBC is directed to alter its Basic insurance Capital Management Plan to exclude any capital build provision in Basic insurance rates from February 1, 2012 to January 31, 2015 provided that Basic capital remains above the regulatory minimum. This will have the effect of allowing ICBC to use more Basic capital above the regulatory minimum to reduce a portion of the actuarially indicated rate during these three years than would otherwise be permitted under ICBC's Capital Management Plan.

Government believes that the above framework will bring greater stability and predictability to Basic insurance rates in the face of rising claims costs and investment market volatility, while protecting the Corporation from excessive risk through adequate capitalization.

This letter of direction is a government directive within the meaning of that term as defined in Special Direction IC2 to the British Columbia Utilities Commission.

Sincerely,

Shirley Bond

Shirley Bond
Solicitor General and
Attorney General

SECTIONS 59 TO 61 OF THE *UTILITIES COMMISSION ACT*

Discrimination in rates

59 (1) A public utility must not make, demand or receive

(a) an unjust, unreasonable, unduly discriminatory or unduly preferential rate for a service provided by it in British Columbia, or

(b) a rate that otherwise contravenes this Act, the regulations, orders of the commission or any other law.

(2) A public utility must not

(a) as to rate or service, subject any person or locality, or a particular description of traffic, to an undue prejudice or disadvantage, or

(b) extend to any person a form of agreement, a rule or a facility or privilege, unless the agreement, rule, facility or privilege is regularly and uniformly extended to all persons under substantially similar circumstances and conditions for service of the same description.

(3) The commission may, by regulation, declare the circumstances and conditions that are substantially similar for the purpose of subsection (2) (b).

(4) It is a question of fact, of which the commission is the sole judge,

(a) whether a rate is unjust or unreasonable,

(b) whether, in any case, there is undue discrimination, preference, prejudice or disadvantage in respect of a rate or service, or

(c) whether a service is offered or provided under substantially similar circumstances and conditions.

(5) In this section, a rate is "unjust" or "unreasonable" if the rate is

(a) more than a fair and reasonable charge for service of the nature and quality provided by the utility,

(b) insufficient to yield a fair and reasonable compensation for the service provided by the utility, or a fair and reasonable return on

the appraised value of its property, or
(c) unjust and unreasonable for any other reason.

Setting of rates

60 (1) In setting a rate under this Act

SECTIONS 59 TO 61 OF THE *UTILITIES COMMISSION ACT*

(a) the commission must consider all matters that it considers proper and relevant affecting the rate,

(b) the commission must have due regard to the setting of a rate that

(i) is not unjust or unreasonable within the meaning of section 59,

(ii) provides to the public utility for which the rate is set a fair and reasonable return on any expenditure made by it to reduce energy demands, and

(iii) encourages public utilities to increase efficiency, reduce costs and enhance performance,

(b.1) the commission may use any mechanism, formula or other method of setting the rate that it considers advisable, and may order that the rate derived from such a mechanism, formula or other method is to remain in effect for a specified period, and

(c) if the public utility provides more than one class of service, the commission must

(i) segregate the various kinds of service into distinct classes of service,

(ii) in setting a rate to be charged for the particular service provided, consider each distinct class of service as a self contained unit, and

(iii) set a rate for each unit that it considers to be just and reasonable for that unit, without regard to the rates set for any other unit.

(2) In setting a rate under this Act, the commission may take into account a distinct or special area served by a public utility with a view to ensuring, so far as the commission considers it advisable, that the rate applicable in each area is adequate to yield a fair and reasonable return on the appraised value of the plant or system of the public utility used, or prudently and reasonably acquired, for the purpose of providing the service in that special area.

(3) If the commission takes a special area into account under subsection (2), it must have regard to the special considerations applicable to an area that is sparsely settled or has other distinctive characteristics.

(4) For this section, the commission must exclude from the appraised value of the property of the public utility any franchise, licence, permit or concession obtained or held by the utility from a municipal or other public authority

SECTIONS 59 TO 61 OF THE *UTILITIES COMMISSION ACT*

beyond the money, if any, paid to the municipality or public authority as consideration for that franchise, licence, permit or concession, together with necessary and reasonable expenses in procuring the franchise, licence, permit or concession.

Rate schedules to be filed with commission

61 (1) A public utility must file with the commission, under rules the commission specifies and within the time and in the form required by the commission, schedules showing all rates established by it and collected, charged or enforced or to be collected or enforced.

(2) A schedule filed under subsection (1) must not be rescinded or amended without the commission's consent.

(3) The rates in schedules as filed and as amended in accordance with this Act and the regulations are the only lawful, enforceable and collectable rates of the public utility filing them, and no other rate may be collected, charged or enforced.

(4) A public utility may file with the commission a new schedule of rates that the utility considers to be made necessary by a rise in the price, over which the utility has no effective control, required to be paid by the public utility for its gas supplies, other energy supplied to it, or expenses and taxes, and the new schedule may be put into effect by the public utility on receiving the approval of the commission.

(5) Within 60 days after the date it approves a new schedule under subsection (4), the commission may,

(a) on complaint of a person whose interests are affected, or

(b) on its own motion,

direct an inquiry into the new schedule of rates having regard to the setting of a rate that is not unjust or unreasonable.

(6) After an inquiry under subsection (5), the commission may

(a) rescind or vary the increase and order a refund or customer credit by the utility of all or part of the money received by way of increase, or

(b) confirm the increase or part of it.