

NEWFOUNDLAND AND LABRADOR
BOARD OF COMMISSIONERS OF PUBLIC UTILITIES
120 Torbay Road, P.O. Box 21040, St. John's, Newfoundland and Labrador, Canada, A1A 5B2

Hearing Transcript

2017 Automobile Insurance Review

September 13, 2018

PRESENT:

The Board:

Darlene Whalen, Chair and CEO
Dwanda Newman, Vice-Chair
James Oxford, Commissioner

Board Counsel/ Staff:

Ryan Oake, Regulatory Analyst
Peter O'Flaherty, Q.C., Hearing Counsel

Parties (Alphabetical Order)

Atlantic Provinces Trial Lawyers Association
Ernest Gittens

Presenters:

Dr. Fred Lazar
Presenting on behalf of the Campaign

Campaign to Protect Accident Victims

Colin Feltham
Jerome Kennedy, Q.C.

Consumer Advocate

Dennis Browne, Q.C.
Andrew Wadden

Insurance Bureau of Canada (IBC)

Amanda Dean
Kevin Stamp, Q.C.
Trevor Foster

Spinal Cord Injury NL

Thomas Fraize, Q.C.
Lara Fraize-Burry
Michael Burry

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1 (9:15 a.m.)
 2 CHAIR:
 3 Q. Good morning, everybody. I guess we're
 4 going to go right to the Campaign. You can
 5 introduce your presenter.
 6 MR. FELTHAM:
 7 Q. Thank you, Chair. Good morning, Chair and
 8 Commissioners. This morning we have Dr.
 9 Fred Lazar with us, and Dr. Lazar is here to
 10 review or present, I guess, his report which
 11 has been supplied to the Board entitled,
 12 "Estimated Overpayments of Automobile
 13 Insurance Premiums in Newfoundland and
 14 Labrador 2012 to 2016", which has already
 15 been filed with the Board. I'll note that
 16 the report is co-authored with Dr. Eli
 17 Prisman, and Dr. Prisman could not be here
 18 today, only Dr. Lazar was available, given
 19 we were only working with a small set of
 20 dates. I did, and I hope it was received,
 21 supply two CV documents; one for Dr. Lazar
 22 and one for Dr. Prisman to the Board. So
 23 the CV of Dr. Prisman, it is available, even
 24 though he isn't present. Good morning, Dr.
 25 Lazar?

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1 DR. LAZAR:
 2 A. Good morning.
 3 MR. FELTHAM:
 4 Q. Thank you for agreeing to be here today, and
 5 to share your thoughts with the Board. I
 6 know it was a late arrival for you, or early
 7 morning arrival, I guess, really, with some
 8 flight issues. I'd like to begin, Doctor,
 9 with just reviewing your CV a little bit,
 10 some of your background, credentials, and
 11 qualifications and that sort of thing. Dr.
 12 Lazar, you're a professor at York
 13 University?
 14 DR. LAZAR:
 15 A. Yes.
 16 MR. FELTHAM:
 17 Q. And how long has that been the case?
 18 DR. LAZAR:
 19 A. It seems like forever. I've lost track,
 20 45/46 years.
 21 MR. FELTHAM:
 22 Q. And your CV indicates that you're in the
 23 Department of Economics?
 24 DR. LAZAR:
 25 A. Department of Economics, cross-appointed

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1 between the Faculty of Liberal Arts and
 2 Applied Professional Studies, and Schulich
 3 School of Business.
 4 MR. FELTHAM:
 5 Q. And in terms of your role as professor, what
 6 sort of – what do you teach there, what are
 7 your areas?
 8 DR. LAZAR:
 9 A. My economics area, used to be the Department
 10 of Arts, taught just about every course, but
 11 primarily international trade and finance,
 12 industrial organization which deals with
 13 competitive behaviour strategy, and in the
 14 business school a course called Economics
 15 for Management. It's really the application
 16 of economic concepts to decision making.
 17 MR. FELTHAM:
 18 Q. And competitive behaviour strategy, what is
 19 that?
 20 DR. LAZAR:
 21 A. That's looking at market structures, how
 22 firms compete in different market
 23 structures, how those market structures
 24 evolve, and discussions of how should
 25 companies develop strategies to gain an

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1 advantage in the marketplace.
 2 MR. FELTHAM:
 3 Q. And I note from your CV just in terms of
 4 formal education, you graduated from
 5 University of Toronto in 1969, went on to
 6 complete post-graduate degree at Harvard
 7 University, the last of which was a PhD in
 8 1978. What's the PhD in?
 9 DR. LAZAR:
 10 A. It's in economics. My dissertation was on
 11 male racial unemployment rate differences in
 12 the US, so I started in the labour economics
 13 field.
 14 MR. FELTHAM:
 15 Q. And I won't belabour this, but you've listed
 16 in your CV a number of books and journal
 17 publications and that spans – the ones
 18 you've listed here in terms of the journal
 19 work runs into about 2015, I believe, and I
 20 note that one of the journals referred to
 21 is, if we look at the bottom of page two,
 22 risk management and insurance review?
 23 DR. LAZAR:
 24 A. Yes.
 25 MR. FELTHAM:

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1 Q. And the title of the article is,
 2 "Regulator's Determination of Return on
 3 Equity in the Absence of Public Firms: The
 4 Case of Automobile Insurance in Ontario".
 5 DR. LAZAR:
 6 A. Yes.
 7 MR. FELTHAM:
 8 Q. And that was in 2015?
 9 DR. LAZAR:
 10 A. Yes.
 11 MR. FELTHAM:
 12 Q. And that's a peer review journal?
 13 DR. LAZAR:
 14 A. All of these are.
 15 MR. FELTHAM:
 16 Q. Okay, and that was co-authored with Dr.
 17 Prisman as well.
 18 DR. LAZAR:
 19 A. Yes.
 20 MR. FELTHAM:
 21 Q. Is that of a similar nature to what you've
 22 done here in terms of the subject matter?
 23 DR. LAZAR:
 24 A. No, it really is an extension of the work
 25 that we did for FSCO, where, you know,

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1 traditionally in applying the capital asset
 2 pricing model, one uses data for public
 3 companies. In this particular case, we were
 4 dealing with largely a mix of public and
 5 private companies. Even the public
 6 companies, there was really no public data
 7 available, so we had to resort to use of
 8 accounting data rather than publicly
 9 reported financial data.
 10 MR. FELTHAM:
 11 Q. And if I go to page three of your CV, I note
 12 you've listed quite a number of instances
 13 when you've worked as expert witness?
 14 DR. LAZAR:
 15 A. Yes.
 16 MR. FELTHAM:
 17 Q. In different types of hearings. It appears
 18 largely regulatory type hearings?
 19 DR. LAZAR:
 20 A. Yes.
 21 MR. FELTHAM:
 22 Q. And the last one, I guess, this is what
 23 you're referring to work with FSCO,
 24 indicates Financial Services Commission of
 25 Ontario, calculating the return on equity

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1 for automobile insurance companies in
 2 Ontario. When you mentioned you worked for
 3 FSCO, is that what you were talking about?
 4 DR. LAZAR:
 5 A. Yes. Eli and I were retained by FSCO
 6 because they had to respond to the Auditor
 7 General of Ontario's comment that they
 8 hadn't reviewed the return on equity in
 9 about 15 years, so we were retained to
 10 examine how they would determine what might
 11 be an appropriate return on equity for
 12 automobile insurance companies.
 13 MR. FELTHAM:
 14 Q. And then if we move on to your professional
 15 consulting activities, and it says in
 16 brackets over 40 years, I guess, there
 17 appears to be - you've done a mix of public
 18 and private in that regard?
 19 DR. LAZAR:
 20 A. I started basically in the public sector,
 21 more idealistic at the time, and I don't
 22 think it really have changed, just learned a
 23 lesson of how the system works, and then
 24 sort of evolved into the private sector, and
 25 then more recently combining the two.

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1 MR. FELTHAM:
 2 Q. And in terms of the work that you've done
 3 here that we're going to discuss today, have
 4 you done work of a similar nature before?
 5 DR. LAZAR:
 6 A. Again the original work was for FSCO. Prior
 7 to that, Eli and I did comparable work for
 8 the Ontario Energy Board with regards to
 9 local electricity distribution companies,
 10 and following that work for FSCO, that's
 11 when the Ontario Trial Lawyers contacted us
 12 and asked us just to apply a methodology to
 13 the experience in Ontario, so that's sort of
 14 the history in this particular area.
 15 MR. FELTHAM:
 16 Q. And I'll get to the Ontario Trial Lawyers
 17 piece in just a second. Before I do, the
 18 Ontario Energy Board work, can you explain
 19 what was done there? Who was the client, I
 20 guess, and what was - more specifically what
 21 you were doing?
 22 DR. LAZAR:
 23 A. It was again the Ontario Energy Board, the
 24 regulator, and I believe in their case as
 25 well it was the Auditor General that had

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1 suggested that they review their
 2 determination of rate of return on equity
 3 rules for the local electricity
 4 distributors. So it was similar work that
 5 we did with FSCO, but a different sample,
 6 different group of companies.
 7 MR. FELTHAM:
 8 Q. And then you mentioned for the Ontario Trial
 9 Lawyers Association. A couple of those
 10 gentlemen were here yesterday. When did you
 11 – I guess, what did you do for the Ontario
 12 Trial Lawyers Association and when?
 13 DR. LAZAR:
 14 A. I'm trying to remember the original one,
 15 2014, 2015, they asked Eli and me to look at
 16 what had been the experience in Ontario to
 17 try to assess whether consumers of
 18 automobile insurance were paying the right
 19 price, paying too much, too little, and
 20 they've come back to me on two other
 21 occasions, 2016 and this year, to update the
 22 reports, which I have done. Again I've
 23 taken the original report and just
 24 incorporating more recent data into the
 25 analysis.

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1 MR. FELTHAM:
 2 Q. Same methodology, just changing the data to
 3 update?
 4 DR. LAZAR:
 5 A. Methodology is not going to change, just the
 6 data have changed.
 7 MR. FELTHAM:
 8 Q. Dr. Lazar, at a high level, what were the
 9 results in Ontario from this study?
 10 DR. LAZAR:
 11 A. At the high level, again what sort of
 12 underlied our methodology, so the original
 13 work, and then the follow up work was to
 14 look at the estimates of the actual realized
 15 returns on equity of the individual
 16 insurance companies, and then collectively,
 17 and compared that to what should have been
 18 an appropriate return on equity. Also
 19 looking at what might have been a more
 20 appropriate expense ratios over time in
 21 light of technological developments.
 22 MR. FELTHAM:
 23 Q. And what was found in Ontario in terms of
 24 the results?
 25 DR. LAZAR:

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1 A. Again the realized returns on equity have
 2 for most companies far exceeded what would
 3 have been appropriate levels, and the gap
 4 had risen, at least up until las year, so
 5 that there seemed to be an indication that
 6 there were significant overpayments for
 7 automobile insurance.
 8 MR. FELTHAM:
 9 Q. And you describe it as overpayments. What
 10 do you mean by that?
 11 DR. LAZAR:
 12 A. Again if the regulator in Ontario's FSCO, if
 13 they had gone with the recommendations we
 14 made and incorporated those return on
 15 equities in their rate determinations, then
 16 the premiums that would have been awarded or
 17 permitted, and this is really sort of a
 18 maximum the insurance companies could have
 19 always charged less for competitive reasons
 20 or for other reasons, that those premiums
 21 would have been less than the premiums that
 22 are actually charged inferred from their
 23 realized returns on equities.
 24 MR. FELTHAM:
 25 Q. So in terms of the return on equities or the

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1 return on equity was in excess of what, in
 2 your opinion, the appropriate target return
 3 on equity would have been?
 4 DR. LAZAR:
 5 A. Yes.
 6 MR. FELTHAM:
 7 Q. Okay.
 8 DR. LAZAR:
 9 A. I mean, the correct analysis, and because of
 10 lack of data, we had to use this
 11 methodology, would have been to look at,
 12 okay, what were the premiums that were
 13 actually awarded based on the information
 14 available when the premiums were permitted,
 15 and compare those premiums to what they
 16 should have been with different return on
 17 equities, you know, Eli and my estimates,
 18 and what would have been more reasonable
 19 expense allowances, and the gap between
 20 those two would have been a measure of the
 21 overpayments.
 22 MR. FELTHAM:
 23 Q. And I gather then the – I mean, we've talked
 24 about Ontario thus far and the work that you
 25 did there with respect to return on equity

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1 in automobile insurance companies. In terms
 2 of this report, your report, July, 2018,
 3 you've now at the request of the Campaign to
 4 Protect Accident Victims, taken that
 5 methodology and applied it to Newfoundland
 6 and Labrador data, is that correct?
 7 DR. LAZAR:
 8 A. The difference is that we had to apply the
 9 capital asset pricing model to those
 10 insurance companies operating in
 11 Newfoundland in determining what would have
 12 been, based on that model, appropriate
 13 returns on equities, and they differed from
 14 those in Ontario largely because if you
 15 applied the capital asset pricing model,
 16 there was a different data, a different risk
 17 factor, slightly higher one for Newfoundland
 18 than for Ontario.
 19 MR. FELTHAM:
 20 Q. Okay, and we'll get a little bit more into
 21 that. I'll get you to explain it somewhat
 22 further in the report, but if we start at
 23 the top here, I guess, and look at page four
 24 of your report, here we have your executive
 25 summary. So you've laid this out in four

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1 points. You've indicated that you've looked
 2 – well, it's done in a question form, but
 3 number one, "Are the conclusions of the
 4 report by Oliver Wyman for the Board of
 5 Commissioners of Public Utilities for
 6 Newfoundland and Labrador valid", and I'm
 7 going to change the order a little bit and
 8 I'm going to deal with that issue last as we
 9 go through the report, or I'd like you to
 10 deal with that issue last. Going to number
 11 two, "What has been the real experience of
 12 auto insurance companies in Newfoundland and
 13 Labrador"? What do you mean there when you
 14 say, "What has been the real experience"?
 15 DR. LAZAR:
 16 A. Okay, again Eli and I used data provided by
 17 MSA Research, and they use – they rely on
 18 GISA data and other data. So we had, I
 19 think, 15/18 companies, somewhere in that
 20 range. I apologize, I do not remember the
 21 exact number. I can look in the appendix
 22 and see the exact number. What we did was
 23 let's estimate what their actual return on
 24 equity for their operation in Newfoundland
 25 and Labrador had been, and compare those to

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1 our estimates of what should have been the
 2 regulated return on equity, and whenever
 3 they were greater, obviously that was an
 4 indication that, you know, the premiums that
 5 were allowed were greater than what they
 6 would have been or should have been if our
 7 return on equity numbers had been used.
 8 (9:30 a.m.)
 9 MR. FELTHAM:
 10 Q. And you mentioned MSA Research. Let's just
 11 deal with that for a second. I guess, what
 12 is that and why was that necessary to do
 13 that, to use them?
 14 DR. LAZAR:
 15 A. We originally approached GISA for data on
 16 individual companies. In the absence of
 17 having data on individual companies, you
 18 can't apply the capital asset pricing model.
 19 The data don't exist. Again Eli was
 20 conducting sort of negotiations. For
 21 whatever reason, GISA was either unwilling
 22 to provide us with the data in the format we
 23 required, or the cost proved to be
 24 excessive, so we then resorted to MSA, whom
 25 we had used for the work we did for FSCO.

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1 So we were familiar with them, and they were
 2 able to format the data for us so that we
 3 could input it into the model very quickly,
 4 and we could do it on schedule and at much
 5 lower cost.
 6 MR. FELTHAM:
 7 Q. I mean, what is MSA Research, what are they?
 8 DR. LAZAR:
 9 A. I've got it here, the official name. Okay,
 10 MSA Research, they work with what's called
 11 the National Insurance Conference of Canada
 12 and they essentially – I'm not sure if
 13 they're an independent group or – they do
 14 work with GISA, they do get data from GISA,
 15 as well as from the insurance companies, and
 16 I know in the work we did for FSCO, FSCO
 17 relied considerably on this group for data
 18 for rate determinations.
 19 MR. FELTHAM:
 20 Q. So number two, "What has been the real
 21 experience of auto insurance companies in
 22 this province". Number three, "How does
 23 this experience compare to what would have
 24 been considered a fair return on equity for
 25 these companies", and we'll get into this in

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1 some more detail, and I think you've sort of

2 already mentioned this, but what are we

3 talking about there?

4 DR. LAZAR:

5 A. Essentially, again the gap between the

6 realized returns on equities, and the return

7 on equities that Eli and I estimated would

8 have been appropriate in light of financial

9 market developments.

10 MR. FELTHAM:

11 Q. Okay. Finally, the fourth item, "What are

12 the implications for the aggregate premiums

13 paid by drivers in Newfoundland and

14 Labrador", what does that mean?

15 DR. LAZAR:

16 A. Which one is this?

17 MR. FELTHAM:

18 Q. Sorry, number four, "What are the

19 implications for the aggregate premiums paid

20 by drivers in Newfoundland and Labrador".

21 I'm just wondering what are we talking about

22 there?

23 DR. LAZAR:

24 A. Okay, I thought you were referring to point

25 four here.

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1 MR. FELTHAM:

2 Q. Oh, no, sorry.

3 DR. LAZAR:

4 A. The implications, again depending on what

5 sample of companies you use, that there

6 seemed to have been over this period of 2013

7 to 2016, overpayments that ranged, I

8 believe, depending on the methodology,

9 somewhere between 4 or 5 percent, and 9

10 percent.

11 MR. FELTHAM:

12 Q. Before we leave your executive summary

13 because it's expanded upon a little bit in

14 terms of summary answers, I guess, to the

15 issues, I'd like to review that and then

16 we'll get into a little bit more detail

17 about how you got there. So if we start

18 with, and again I mentioned I'm going to

19 skip over number one here, which is the

20 conclusions of Oliver Wyman, we'll get back

21 to that, I want to focus first on the work

22 that you did and your own estimations. So

23 number two, "ROE's for auto insurance

24 companies in Newfoundland and Labrador", and

25 you note here, "When we exclude the TD

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1 subsidiaries, Primmum and Security National,

2 and three other companies with average

3 negative ROE's over the entire period, 2011

4 to 2016, the weighted average ROE's for the

5 remaining companies increased 12.2 percent

6 over the period, 2011 to 2016. Obviously,

7 the companies that have been profitable have

8 been very profitable". So, I guess,

9 essentially then you determined once you

10 took certain, I'll call them under

11 performing companies from the analysis, that

12 the results were positive ROEs?

13 DR. LAZAR:

14 A. Yes, but they were positive for the entire

15 sample. They were just much larger when you

16 excluded those particular companies.

17 MR. FELTHAM:

18 Q. And then, I guess if we look at the next

19 step here, if we go over to page 5 and item

20 3, "How much have consumers in Newfoundland

21 and Labrador overpaid?" And this I guess is

22 the answer to the comparison of the realized

23 ROEs versus what the targets ought to have

24 been?

25 DR. LAZAR:

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1 A. Yes.

2 MR. FELTHAM:

3 Q. And you note there that, "For the companies

4 with average positive ROEs, the estimated

5 upper limit for aggregate overpayments is

6 \$92 million. For the companies with

7 positive ROEs, the estimated overpayments

8 represent about 8.6 percent of the total

9 premiums paid between 2011 and 2016." And

10 there's smaller print in italics below that.

11 DR. LAZAR:

12 A. Right.

13 MR. FELTHAM:

14 Q. Which notes that, "For all companies,

15 excluding Primmum and Security National, the

16 upper limit for aggregate overpayments

17 during the period 2011 to 2016 is 54 million

18 dollars." So, let me see—I want to make

19 sure we understand this. So, I gather that

20 you're giving us a range here, depending on

21 whether we just exclude the two TD companies

22 or also exclude a couple of others who have

23 had similar negative performance and that

24 for that five-year period, 2011 to 2016, I

25 guess it's five years, anyway 2011 to 2016,

Page 21

1 the overpayment estimate is somewhere
 2 between 54 million dollars and 92 million
 3 dollars for consumers in this province?
 4 DR. LAZAR:
 5 A. Yes, but as we point out, that's sort of the
 6 upper limit.
 7 MR. FELTHAM:
 8 Q. Yes.
 9 DR. LAZAR:
 10 A. Were there over the entire period
 11 overpayments? Most likely. What was the
 12 value? As I said, the only way to determine
 13 that with greater certainty is if one had
 14 access to sort of other data. What were the
 15 aggregate premiums that were permitted to
 16 the insurance companies? And two, what
 17 would have been the aggregate premium
 18 permitted to the insurance companies with
 19 lower return on equity assumptions, lower
 20 operating expense assumptions? And the gap
 21 between the two would have reflected the
 22 overpayments regardless of what the
 23 insurance company—the actual performance of
 24 the insurance companies.
 25 MR. FELTHAM:

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1 Q. And Dr. Lazar, I want to pick up on a phrase
 2 that you've used there. You say, "If one
 3 had access to the data," and we've also
 4 talked a lot about estimating. You know,
 5 why is it that we're estimating, and you
 6 know, why it is that we don't—you know, if
 7 one had access to the data? What is it—what
 8 are you telling us?
 9 DR. LAZAR:
 10 A. You know, Eli and I don't have access to the
 11 decisions made by the Board, at least we
 12 didn't have it when we did the report, don't
 13 have it now. They might be available. So,
 14 we don't know. Here, so the aggregate
 15 premiums that were awarded which would have
 16 been different from the actual premiums that
 17 were paid, you know, if the Board sets an
 18 upper limit, it's up to the insurance
 19 companies—they can set rates below that for
 20 various reasons. In addition, we wouldn't
 21 have access to the claims, so expectations
 22 that were built into these decisions. So,
 23 in the absence of having—not having those
 24 data, even though we have return in equity
 25 assumptions, we can—I'll have expense

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1 assumptions, there is no way that we could
 2 determine what the premiums could have been
 3 with a different set of assumptions, so as
 4 to be able to simply calculate the
 5 differences.
 6 MR. FELTHAM:
 7 Q. And if we go to your report, page 24 next.
 8 And so, I gather here what we have is—and
 9 you can take us through the explanation, but
 10 these are the results in terms of the return
 11 on equity calculations for the various
 12 insurers over the period examined?
 13 DR. LAZAR:
 14 A. Yes.
 15 MR. FELTHAM:
 16 Q. You earlier mentioned that a couple of
 17 companies were excluded, Security National
 18 and Primmum Insurance. I gather that's TD
 19 Insurance? It's my understanding.
 20 DR. LAZAR:
 21 A. Yes.
 22 MR. FELTHAM:
 23 Q. Yes. And if I look at those, since--well in
 24 the case of Security National, since 2013,
 25 every year recording a negative ROE, and

Page 24

1 ranging from--you know, in 2015 it was
 2 negative 247 down to negative 20 I guess in
 3 2013. And Primmum similarly, but from 2014
 4 consistently negative. So, because--you
 5 note that some companies were excluded from
 6 the analysis. Can you tell us I guess why
 7 that was done? What's the economic
 8 rationale for doing that and why is it
 9 reasonable to do it in your view?
 10 DR. LAZAR:
 11 A. Now, with the case of the TD companies we
 12 found similar results in Ontario. That—
 13 again, if you apply standard economic
 14 reasoning, if a company is consistently
 15 losing money then in one particular line of
 16 business and this is part of a much broader
 17 line of business, they're doing so because
 18 they're using that line of business as a
 19 lost leader for their other financial
 20 services. So, that's what we concluded with
 21 TD. I mean, if you look at RBC, they were
 22 losing money. I think they've exited from
 23 the insurance, auto insurance industry.
 24 There are a couple of other companies in
 25 Ontario that when they were acquired by

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1 other companies, Fairfax acquired some
 2 insurance companies that were doing poorly,
 3 within a year or two, Fairfax turned them
 4 around. So, if a company is losing money,
 5 it's going to either exit the industry if it
 6 is not a lost leader, or if it continues in
 7 business, it's using this to promote other
 8 lines of business. So, they're willing to
 9 tolerate a loss here. It's an investment in
 10 order to generate profits in other lines of
 11 business. Another possibility is that again
 12 firms that for one or two years experience
 13 negative results, negative returns on
 14 equity, losses, they're doing so perhaps to
 15 increase market share. So, they're
 16 competing more aggressively. They'll cut
 17 price to increase market share. If they
 18 succeed, then one should expect the prices
 19 to sort of rise up. The return in equity is
 20 to improve. If that doesn't happen, chances
 21 are they'll exit the industry. Then there's
 22 a third possibility and this is using
 23 transfer pricing to shift around profits
 24 from higher tax jurisdictions to lower tax
 25 jurisdictions. And if you look at corporate

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1 tax rates at a provincial level, chances are
 2 quite good that most of the automobile
 3 insurance companies are doing this, trying
 4 to perhaps understate their profits in
 5 Newfoundland and Labrador because the
 6 corporate tax rate is what, 15 percent at
 7 the provincial level, and shifting them to
 8 lower tax regimes, in particular Ontario and
 9 Alberta that have rates, I think what--
 10 Ontario is about 11½ percent, Alberta is 12
 11 percent. Even BC has a lower rate. So,
 12 some of the cases might simply be, you know,
 13 shift the profits, diminish your profits,
 14 perhaps even generate some losses for one
 15 reason or another. And again, all of these
 16 legitimate reasons for companies to behalf
 17 in this way, but that tends to sort of muddy
 18 the waters when it comes to trying to figure
 19 out, have consumers in this province ended
 20 paying too much of the proper amount or too
 21 little as a result?
 22 MR. FELTHAM:
 23 Q. Like trying to determine the real experience
 24 I guess as you put it?
 25 DR. LAZAR:

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1 A. Yes.
 2 MR. FELTHAM:
 3 Q. If I go to the bottom of page 25, and right—
 4 well, I guess it is sort of the last full
 5 paragraph that starts with “Furthermore.”
 6 This is--right above that you reviewed what
 7 you just talked about in terms of the
 8 experience with TD Insurance and companies
 9 of a similar nature, but in—here you say,
 10 “Furthermore, the reported or estimated ROEs
 11 might be quite misleading with regards to
 12 the ability of a company to attract capital
 13 to a particular line. As well, without
 14 detailed information about the intricacies
 15 of intra-corporate transfer pricing and
 16 other accounting practices, it is very
 17 difficult to measure the real profitability
 18 of any one line of business for a P&C
 19 company.” What are we talking about there?
 20 DR. LAZAR:
 21 A. Okay, and if you look at the major
 22 automobile insurance companies that operate
 23 in this province, most of them operate
 24 automobile insurance in most if not all of
 25 the other provinces, and most of them also

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1 operate in other line of business. In the
 2 case of the TD subsidiaries, TD also
 3 operates in many lines of financial
 4 services. So, you're going to have sort of
 5 at the corporate level, you're going to
 6 aggregate sort of the performance, the
 7 revenues, the cost of all of these companies
 8 to come up with consolidated statements.
 9 And then, you're going to sort of try to
 10 establish what the profitability is of your
 11 separate business units, but there you have
 12 under the accounting rules a certain degree
 13 of flexibility and even in the tax rules you
 14 have a certain degree of flexibility with
 15 regards to transfer pricing. So, transfer
 16 pricing refers to what cost can you charge.
 17 For example, your automobile insurance
 18 operation of Newfoundland and Labrador, that
 19 might be provided from their corporate head
 20 office or from some other business unit, and
 21 can you perhaps increase this cost
 22 marginally, again, with the accounting rules
 23 and tax laws? Should you reduce this? So
 24 that flexibility—here is our real cost which
 25 you will report in order to determine

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1 internally what's the profitability of the
 2 different business units and to determine
 3 the performance bonuses for the people
 4 running these. And then, from a tax point
 5 of view, you'll have different cost
 6 allocations in order to try to minimize your
 7 tax liability. I don't have privy to those
 8 data. Unless you happen to be the tax
 9 authority, CRA, nobody else has access to
 10 that information other than the companies
 11 and a possibility of CRA.
 12 (9:45 a.m.)
 13 MR. FELTHAM:
 14 Q. And if we go over to page 26, Dr. Lazar,
 15 table 14, and I'll just—I'll to the
 16 paragraph below the table to give us some
 17 background here. So, it says, "It is quite
 18 clear that the annual returns on investments
 19 in equities fluctuate widely from year to
 20 year. Therefore, it is not surprising that
 21 the annual ROEs of auto insurance companies
 22 also fluctuated from year to year. The net
 23 investment returns were relatively more
 24 stable than the S&P TSX total returns.
 25 Furthermore, our estimates of the aggregate

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1 ROIs exceed the ROI assumptions of OW,"
 2 which is Oliver Wynman, "reinforcing our
 3 earlier comments that Oliver Wynman likely
 4 has underestimated the profitability of
 5 automobile insurance companies in the
 6 province and overestimated their premium
 7 deficiencies during the period 2012 to '16."
 8 Can you take us through—I mean what we
 9 seeing here? What's the relevance of this
 10 table?
 11 DR. LAZAR:
 12 A. Okay. Now, the P&C companies are going to
 13 use sort of the reserves to invest them.
 14 You want to earn something on them, and
 15 that's sort of a major driver of the
 16 profitability. I mean, you look at two
 17 classic examples. Warren Buffett with
 18 Berkshire Hathaway, really what underlies
 19 that operation is insurance, and he's got a
 20 phenomenal track record obviously with this
 21 team of investing those reserves to generate
 22 you know remarkable returns. In the case of
 23 Canada, we have Fairfax Financial which
 24 again largely a P&C company, and their
 25 returns are driven primarily by the ability

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1 of the team, Prem Watsa and his team, to
 2 generate superb returns from their
 3 investment activities. So, the insurance
 4 companies have access and they have to look,
 5 how are we going to invest this to sort of
 6 generate returns, boost our profitability?
 7 And you've got a whole range of financial
 8 assets. To simplify them, you know, invest
 9 in real estate, you can invest in a whole
 10 range of bonds, government to corporate,
 11 different sort of ratings, or you can invest
 12 in equities. And every insurance company
 13 has their own sort of investment strategy.
 14 Most, if not all, are going to invest part
 15 of this portfolio in equities. And you
 16 know, if you invest in bonds, the returns
 17 there tend to be more stable. Real estate,
 18 less stable than bonds, but more stable
 19 likely than equities. Equities are going to
 20 be the most variable component.
 21 MR. FELTHAM:
 22 Q. And what are you showing us in the table?
 23 DR. LAZAR:
 24 A. In this particular table, essentially
 25 showing that, you know, returns on equity

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1 year to year can bounce around. You can
 2 have losses, you can have extremely good
 3 returns. The performance of the auto
 4 insurance companies, the greater stability I
 5 think is the reflection of the fact that
 6 they haven't invested 100 percent in equity.
 7 There is a mix with a considerable
 8 allocation to more stable bonds, but
 9 nevertheless, the returns are going to be
 10 driven in part by what happens in the equity
 11 markets.
 12 MR. FELTHAM:
 13 Q. And if we move down on page 26 to the last
 14 paragraph, I'm going to just read that to
 15 you. "The auto insurance companies with
 16 positive ROEs throughout the 2011-2016
 17 period accounted for about 75 percent of
 18 total premiums over the entire period,
 19 ranging from a low of 66 percent of total
 20 premiums in 2016 to a high of 82 percent in
 21 2011. When Primmum and Security National
 22 are excluded, the companies with positive
 23 ROEs accounted for 84 percent of the total"—
 24 "of the remaining total premiums over the
 25 period 2011 to 2016." What's the

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1 significance of that? What -
 2 DR. LAZAR:
 3 A. Oh, just pointing out that the companies
 4 that were profitable for this entire period
 5 were major players in the market in
 6 Newfoundland and Labrador. They weren't a
 7 small, you know, relatively insignificant
 8 component of that market.
 9 MR. FELTHAM:
 10 Q. Okay. And then, if we go over to page 27,
 11 at the bottom, page 27. There we go. I
 12 guess there and onto page 28 you explain how
 13 you estimated potential overpayments, and
 14 you say, "Using these data, we estimated
 15 potential premium overpayments as follows.
 16 Whenever the realized ROEs exceeded the ROEs
 17 we estimated for the auto insurance
 18 industry, it is likely that premiums were
 19 too high, and as a result, drivers in
 20 Newfoundland and Labrador paid too much for
 21 auto insurance. In table 16 we report the
 22 gaps," and you talked about the gaps
 23 earlier, "when they are positive between the
 24 realized pre-tax ROEs and the CAPM ROEs for
 25 two groups of companies, all companies

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1 excluding Primmum and Security National, and
 2 only the companies that reported average
 3 positive ROEs over the entire period." So,
 4 when the realized ROEs exceeded the ROEs
 5 that were estimated to be appropriate, that
 6 equals overpayment?
 7 DR. LAZAR:
 8 A. Yes.
 9 MR. FELTHAM:
 10 Q. Okay. And then, page 29, that brings us to
 11 your sort of final results, if you will.
 12 And if we look at the chart at the top, I
 13 guess there's sort of two options, I'll call
 14 them options. You either—you have the
 15 results with the all companies excluding
 16 only Primmum and Security National or all
 17 the positive ROE companies? Am I reading
 18 that correctly?
 19 DR. LAZAR:
 20 A. Yes.
 21 MR. FELTHAM:
 22 Q. Okay. So, I mean we look at that and you
 23 know insurance companies are suggesting
 24 private passenger automobile is not a
 25 profitable venture in Newfoundland and

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1 Labrador. Are they likely correct about
 2 that?
 3 DR. LAZAR:
 4 A. Well, again from an economic theory point of
 5 view, if an activity is not profitable, and
 6 it's consistently not profitable, you exit
 7 that line of business. You leave. You do
 8 not stay in it unless it's a lost leader to
 9 generate business in other financial or
 10 insurance services in that particular
 11 jurisdiction. So, if you're not in
 12 automobile insurance, you're not going to be
 13 a player or you're going to be a smaller
 14 player in those other fields. So, you'll
 15 take the losses in this activity because
 16 you're more than making up for it with
 17 profits in other activities. So, it's one
 18 or the other. So, you know, the argument is
 19 that the auto insurance in Newfoundland and
 20 Labrador is not profitable, well, if that
 21 were the case, then you look at the
 22 committed equity to this industry, the
 23 capital. If that argument is correct, you
 24 would expect the equity allocated to this
 25 business to have declined over time. The

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1 data show otherwise. So that tends to
 2 dismiss that argument. So, could it be
 3 still unprofitable and your allocation of
 4 equity of capital could have increased?
 5 Possibly, if this is now being used as a
 6 loss leader. But it appears, based on the
 7 individual insurance companies, that this
 8 might be the case only for the TD
 9 subsidiaries, not for the others.
 10 In the case of Intact, which had
 11 negative returns on equity I think the last
 12 two years, maybe three years, it appears in
 13 their case that Intact has been quite
 14 aggressive in competing for market share in
 15 all lines of business and has been quite
 16 successful in doing that, especially when
 17 you look at their aggregate profitability
 18 and the – while I haven't followed their
 19 share price that closely, they seem to have
 20 done quite well over different periods of
 21 time. So that strategy seems to be working
 22 for them, and I suspect if you look at the
 23 allocation of capital to this line of
 24 business in Newfoundland and Labrador, it
 25 has also been increasing, which suggests

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1 they expect this business to be profitable
 2 in the future and this is part of their
 3 strategy. They believe they have an
 4 advantage in insurance in general across the
 5 country and they're simply trying to expand
 6 their market share, become a more prominent
 7 player to grow more rapidly and then use
 8 whatever internal advantages they have to
 9 make it more profitable.
 10 But it boils down to if it's
 11 unprofitable, you're exiting the business
 12 unless it's a loss leader and the data do
 13 not support that argument that it's
 14 unprofitable and you're exiting.
 15 MR. FELTHAM:
 16 Q. And if we look at page 30, Dr. Lazar, that's
 17 where I was going next, which is the capital
 18 availability piece that you're speaking of.
 19 DR. LAZAR:
 20 A. Yeah.
 21 MR. FELTHAM:
 22 Q. So, here specifically what were the
 23 findings?
 24 DR. LAZAR:
 25 A. Again, there was some decline again for all

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1 companies 2012 to 2013, but since then, it's
 2 been increasing steadily, even during those
 3 years like 2014, 2015 where profits eroded
 4 quite substantially because of significant
 5 increase in claims. Excluding the TD, subs
 6 again decline from 2011 through to 2013 but
 7 a significant recovery. So, there does not
 8 appear to be any indication from these data
 9 that there has been any sort of continuous
 10 long term decline in the allocation of
 11 capital to this line of business in
 12 Newfoundland and Labrador.
 13 MR. FELTHAM:
 14 Q. And Doctor, I'd like now to turn to look at
 15 little bit at your assessment of some of the
 16 Oliver Wyman conclusions in their
 17 profitability study. To start, we can go to
 18 page nine of your report, and I guess we'll
 19 just confirm, but you reviewed as part of
 20 the work that you did, and this makes its
 21 way into some of your report, the Profit and
 22 Rate Adequacy Review, March 29 2018, that
 23 Oliver Wyman has done for this Board?
 24 DR. LAZAR:
 25 A. Yes.

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1 MR. FELTHAM:
 2 Q. Okay. And okay, on page nine, this is your
 3 review of the Oliver Wyman key assumptions
 4 and one of the issues that is raised in –
 5 that you raise and that makes its way into
 6 the Oliver Wyman report as well is the use
 7 of the ten percent ROE target, and I gather
 8 Oliver Wyman is using that as their
 9 benchmark. They've accepted that that's
 10 what it ought to be, not to have been. And
 11 the figure, as I understand it, comes from
 12 benchmark setting process that this Board
 13 engaged in in 2005 and it's been that way
 14 ever since.
 15 But you – I'll put it this way. You
 16 take issue with just simply using that ten
 17 percent from 2005 as the benchmark. I
 18 guess, firstly, I mean, could Oliver Wyman
 19 have examined whether a ten percent target
 20 was appropriate? Is that something they
 21 could have done?
 22 DR. LAZAR:
 23 A. Yeah, I mean, they have access to or could
 24 have – yeah, could have easily obtained
 25 access to individual company financial

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1 information, their accounting information.
 2 The capital asset pricing model is widely
 3 known. It's been around for a long time.
 4 Anyone doing any work related to finance
 5 would know how to use it, how to apply it,
 6 and Oliver Wyman does have experts in that
 7 field in their consulting operations. Also,
 8 it would not have been a difficult exercise
 9 if they had been asked, and I suspect they
 10 weren't asked, but if they had been asked to
 11 look at was the ten percent return on equity
 12 still appropriate in light of financial
 13 market developments from 2005 to the present
 14 time.
 15 (10:00 a.m.)
 16 MR. FELTHAM:
 17 Q. And if I just go to that under "Key
 18 Assumptions" on page nine, the bottom
 19 paragraph says "The key assumptions involve
 20 claim costs, operating costs and ROI".
 21 That's Oliver Wyman's key assumptions you
 22 refer to there, right?
 23 DR. LAZAR:
 24 A. Yes.
 25

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1 MR. FELTHAM:
 2 Q. And “OW, Oliver Wyman, should have included
 3 ROE, but apparently they were not asked
 4 whether the ten percent after tax ROE
 5 introduced in 2005 was appropriate
 6 throughout the period 2007 to 2017.” And
 7 you just referred to that. “We do examine
 8 this question for if the target ROE should
 9 have been set at a different level each
 10 year, the premium adequacy, the estimates of
 11 Oliver Wyman would be misleading.” So, how
 12 so? Why might they have been misleading
 13 then? What do you mean?
 14 DR. LAZAR:
 15 A. I mean, if Oliver Wyman was simply
 16 presenting here are the facts over this
 17 period of time, this is what happened,
 18 without commentary whether premiums were
 19 adequate or not, whether there’s
 20 overpayments or underpayments, say “here are
 21 the data; here are the facts” without
 22 commentary, I mean, I would have had no
 23 problems with it. But they then proceeded
 24 to try to estimate what the under or
 25 overpayments of insurance premiums might be

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1 in 2017 based on the data that they used and
 2 that’s where we begin to take issue.
 3 If they’re going to now look at the
 4 adequacy of premiums, then you have to start
 5 with the following: one, is the return on
 6 equity that’s permitted by the Board
 7 appropriate in light of what’s happened in
 8 financial markets? You know, going back
 9 2009-2010, people have said well, the
 10 interest rate – interest rates sort of
 11 normally low. This is really an aberration.
 12 They’re going to pop back up to historical
 13 levels. We’ve been hearing that now for
 14 nine years and it hasn’t changed much. So,
 15 what’s an aberration? When will interest
 16 rates return to those levels? So, one had
 17 to look at this is not a short term
 18 aberration in having historically low
 19 interest rates. This seems to have been a
 20 fundamental change. And that should then
 21 translate into what might have been
 22 appropriate return on equities, just plain
 23 common sense.
 24 Second, expense ratio. Why use
 25 historical values? Why not look at best

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1 practices? Look at technology and how this
 2 will affect how the insurance market should
 3 operate, could operate, and build those into
 4 the analysis.
 5 And then return on investment, well,
 6 you look at the GISA data or MSA data and
 7 you look at the accounting data that Oliver
 8 Wyman used and you say, well, you know, the
 9 differences are too large. They should have
 10 then examined why and adjusted accordingly.
 11 So, if they’re going to use the past to
 12 try to estimate what is – you know, what’s
 13 the nature of the under or overpayments of
 14 premiums going forward, then you have to
 15 address these questions and that’s where Eli
 16 and I took issue with her analysis.
 17 MR. FELTHAM:
 18 Q. And if I can take you to page 16 of your
 19 report under 3.0. I gather this is the
 20 portion of your report where you provide
 21 some detailed consideration of what the
 22 appropriate ROE target level ought to be is
 23 where this begins I believe?
 24 DR. LAZAR:
 25 A. Yes.

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1 STAMP, Q.C.:
 2 Q. What page are you at? I’m sorry.
 3 MR. FELTHAM:
 4 Q. Page 16.
 5 DR. LAZAR:
 6 A. Yes.
 7 MR. FELTHAM:
 8 Q. So, firstly, I note that you refer here and
 9 you quote fairly extensively to some
 10 decisions of this Board. You refer to
 11 those. Can you take us through that a
 12 little bit and why – give us some context of
 13 why are you making those references? What
 14 does that help us understand?
 15 DR. LAZAR:
 16 A. As you say that this Board, like regulatory
 17 boards not only dealing with auto insurance
 18 but with other areas, electric utilities,
 19 gas utilities, et cetera, across Canada and
 20 across Canada US, have recognized
 21 increasingly, probably over the past 10-15
 22 years, that the capital asset pricing model
 23 is the tool to use to try to determine what
 24 is an appropriate return on equity for these
 25 regulated entities. And I’m just using the

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1 Board's decision here. So, they acknowledge
 2 that this is the case. They accept this and
 3 they believe going forward this is the model
 4 that should be used.
 5 MR. FELTHAM:
 6 Q. And I gather this kind of work, estimating a
 7 benchmark ROE like this, this is not the
 8 work of an actuary? It's not who typically
 9 does that?
 10 DR. LAZAR:
 11 A. It's finance. This is sort of the area of
 12 expertise of a Professor Prisman. I teach
 13 this as well, but it's, you know, really the
 14 workhorse of finance. Every first year
 15 finance course, this is how you determine
 16 the risk profile of companies. This is how
 17 you determine what should be their target
 18 return on equity and that's get based –
 19 built into what should be the weighted
 20 average cost of capital for companies.
 21 MR. FELTHAM:
 22 Q. And explain a little bit, if you could, --
 23 and you know, I know it's pretty elementary,
 24 but the capital asset pricing model, that's
 25 what was utilized in this case to come up

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1 with what the appropriate target or
 2 benchmark, whatever -
 3 DR. LAZAR:
 4 A. Yes.
 5 MR. FELTHAM:
 6 Q. - ROE ought to have been over time. Give us
 7 a little overview of how that works.
 8 DR. LAZAR:
 9 A. Essentially what you're trying to do for a
 10 company is a risk-free rate of return.
 11 That's usually taken as interest rate on
 12 some government bond. It could be short
 13 term government bond. It could be sort of a
 14 medium term government bond. But we find an
 15 asset class that we can agree the return on
 16 that asset class has little risk. Never
 17 going to be a zero risk, but it's little
 18 risk. It's almost impure risk.
 19 Then the question becomes for a
 20 particular company. For a company's equity,
 21 for example, what should be the return?
 22 Well, the return should be over time, the
 23 company should do better than that risk-free
 24 return. If it can't be better, don't be in
 25

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1 business. You might as well use your
 2 capital and invest it in that government
 3 bond. So, what's the risk that the company
 4 undertakes for which it expects to be
 5 compensated and hence earn a return on its
 6 equity investment over and above that risk-
 7 free asset. So, that's the starting point.
 8 And you then sort of look at the actual
 9 profitability of that company, relate it to
 10 the sort of return of a market portfolio.
 11 In Canada, you use the S&P TSX. If you're
 12 doing the US, probably would use the S&P.
 13 So, you run a relationship to find out
 14 how risky is this particular company
 15 compared to the market in total and you
 16 estimate as a result what's called beta.
 17 That's an estimate of a risk profile. If
 18 this company is as risky as the market, the
 19 beta will be equal to one which means that
 20 the return on equity should be that risk-
 21 free return plus what has been the excess
 22 return of investing in a market portfolio of
 23 equities less that risk-free return. That's
 24 your premium, your risk premium. If the
 25 beta is less than one that means this

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1 company's investment opportunities have
 2 proven to be somewhat less risky than the
 3 market in total and therefore the risk that
 4 you add to the risk-free rate will be
 5 somewhat less than for the market as a
 6 whole.
 7 MR. FELTHAM:
 8 Q. And I'll take you through a little bit then
 9 on the findings here, but before we get
 10 there, and I don't want to belabour this
 11 point too much, but I mean, I guess, why is
 12 it important – why is it important to know
 13 the appropriate estimated target ROE versus
 14 assuming one from 2005 is appropriate?
 15 What's the pitfalls if we use that 2005
 16 figure? What do we run the risk of?
 17 DR. LAZAR:
 18 A. The pitfalls, you could both ways.
 19 Financial markets change, year to year, over
 20 time, and the risk premium that you're
 21 adding to that risk-free rate will also
 22 vary, as will the risk-free rate. So, from
 23 a regular regulatory point of view, you want
 24 to ensure that you're giving the companies
 25 the opportunity to earn what's an

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1 appropriate return on equity for their
 2 investment class. There'll be some
 3 companies that'll do better. They're more
 4 efficient. They do better on their
 5 investment portfolio. They get lucky on
 6 their claims. Some will do poor. But what
 7 you want to do is here's the average that
 8 you're going to use for the industry. That
 9 then sets a maximum for the premiums. What
 10 the company has set, they can set lower
 11 premiums for various reasons.

12 If financial markets are stable,
 13 interest rates remain constant, the market's
 14 risk premium remains constant, using
 15 historically determined return on equity for
 16 regulatory purposes is fine. But since
 17 financial markets aren't stable, then it's
 18 appropriate to take these changes into
 19 account.

20 The work we did for FSCO, we argued
 21 there that we don't want to change return on
 22 equity year to year because you get too much
 23 variability in the markets. What you want
 24 to do, our preferred suggestion for them --
 25

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1 you know, we didn't have enough data here to
 2 do it for Newfoundland and Labrador, but our
 3 preferred suggestion for them was to take a
 4 ten-year rolling average. So, new year data
 5 become available. You add that into your
 6 average. You drop the data ten years ago.
 7 That gives you more stability in that return
 8 on equity over time, but it also will allow
 9 that return on equity to track what is
 10 actually happening in financial markets.

11 MR. FELTHAM:
 12 Q. And at the bottom of page 18, last
 13 paragraph, there you say "As noted in
 14 Appendix 2, there are three key variables
 15 required to estimate the ROE", and I think
 16 you've gone over those, "risk-free interest
 17 rate, risk premium and an estimate of beta".
 18 And so, take us then through here the rest
 19 of your estimation process in this instance.
 20 You've identified the key variables.

21 DR. LAZAR:
 22 A. Okay. So, the risk-free rate we basically
 23 used sort of the average of the expected
 24 spot rate going forward five years and we
 25 can derive that from the term structure of

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1 interest rates. So, that's a straight
 2 forward calculation. Calculating the beta
 3 requires having data on individual
 4 companies, looking at their profitability
 5 and what we call in economics and finance,
 6 running the regression, running – using that
 7 as your dependent variable and running that
 8 against your independent variable which is
 9 simply the realized return on a market
 10 portfolio. So, you run that statistical
 11 relationship. You come up with an estimate
 12 of beta which is a measure of the risk,
 13 riskiness of this particular line of
 14 business in this province.

15 So again, straightforward procedure.
 16 The Excel file has the ability to do this
 17 type of statistical analysis. But what's
 18 required, again, three pieces of
 19 information. The data for companies, that's
 20 what we relied on MSA to provide us with
 21 that information. Some measure of the risk-
 22 free rate, there are different
 23 possibilities. According to Eli, the one
 24 that we use is most appropriate and most
 25

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1 widely used and again it's derived from Bank
 2 of Canada data. So, that's widely
 3 available. And then a market return, the
 4 TSX, the S&P TSX index with a return from
 5 year to year, again widely available. So,
 6 those data there simply run that
 7 relationship to come up with an estimate of
 8 beta that we then use to determine the
 9 return, what should be the return on equity
 10 for the individual companies and for the
 11 industry as whole.

12 (10:15 a.m.)
 13 MR. FELTHAM:
 14 Q. And, Doctor, in that regard, if we go to
 15 Table 11 on page 19, these are the results,
 16 I'll say, so you got the risk adjusted, what
 17 you've calculated the risk adjusted
 18 competitive ROEs say, ought to have been, I
 19 guess, for 2011 to 2016, and we've got
 20 numbers from a low of 5.85 up as high as
 21 7.84—sorry, no, a low of 3.75 in 2016. I
 22 guess what strikes me about these is that
 23 none of them are 10.

24 DR. LAZAR:
 25 A. And one would not expect them to be 10. At

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1 the time 10 was set, you know, interest
 2 rates were significantly higher than they
 3 are at this time, and that would account for
 4 the difference, you know, were interest
 5 rates 3 or 4 percentage points higher,
 6 that's all that would be required to get to
 7 your 10 number. Most likely, they were.
 8 The other factor, I think, was the beta that
 9 was used was 1, ours was about .8, .83, so
 10 that would tend to move the return on equity
 11 somewhat lower, but the key driver was that
 12 risk-free rate.
 13 MR. FELTHAM:
 14 Q. And so, I'm trying to explain this in a
 15 simple manner, I guess, or summarize this in
 16 a simple manner, but instead of utilizing a
 17 10 percent figure, as a ROE in these years,
 18 if we were looking at premium sufficiency
 19 relative to rate inadequacies, instead of
 20 using 10, you would say we should be using
 21 these numbers?
 22 DR. LAZAR:
 23 A. Again, subject to the proviso I said before,
 24 that our preference would have been if you
 25 had historical data, do 10-year rolling

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1 averages.
 2 MR. FELTHAM:
 3 Q. Right.
 4 DR. LAZAR:
 5 A. When we did the work for FSCO, we had data
 6 going back to about 1993, '94 so we could do
 7 that. That's not the case here, but if you
 8 take just a five-year average, six-year
 9 average, six percent, that would have been
 10 much more appropriate than a 10 percent
 11 number, that would be your starting point.
 12 MR. FELTHAM:
 13 Q. And if we go to the next page, page 20. And
 14 here this gets into the return on investment
 15 portion and I'll start at the top, you say,
 16 "The comparisons in Table 9"—which is, just
 17 for reference purposes, is back on page 15,
 18 you say, "The comparisons in Table 9 make it
 19 clear that Oliver Wyman's assumptions for
 20 ROI", return on investment, "are
 21 unrealistically low." And I guess I'm
 22 trying to break this down as much as I can.
 23 Why is the ROI important?
 24 DR. LAZAR:
 25 A. Again, that enters into trying to estimate

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1 the profitability of these companies and it
 2 would factor into the rate setting process,
 3 again, familiar with what happens in Ontario
 4 and their ROI is a key variable in that rate
 5 determination process.
 6 MR. FELTHAM:
 7 Q. And why do you say Oliver Wyman's assumption
 8 on it were unrealistically low?
 9 DR. LAZAR:
 10 A. Again, you know, we derive the ROIs from the
 11 GISA data, sort of at the aggregate industry
 12 level, and the reported returns on equity
 13 for the companies and we use equity as a
 14 proxy for sort of the reserves they had
 15 available. The reason we made that
 16 assumption, and that was the assumption
 17 built into FSCO's rate determination
 18 process, so we just sort of extrapolated it
 19 to the case in Newfoundland and Labrador,
 20 and the numbers generated from those
 21 aggregate data were well above the Oliver
 22 Wyman data. I think the difference and
 23 again, I haven't done any sort of detailed
 24 analysis, is that Oliver Wyman is using as
 25 returns dividends and interest cash

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1 received. At the GISA data level, what's
 2 included there are capital gains and losses
 3 recorded from year to year. Mostly likely
 4 because that's required for tax purposes,
 5 and there is trading in these assets that's
 6 not a matter of they'll buy an asset and
 7 stick with it. And the gap tends to reflect
 8 the fact that most, if not all insurance
 9 companies, invest a significant part of that
 10 portfolio in equities and they do so because
 11 of the higher expected returns on equity
 12 over time and the capital gains to be
 13 received, that's why that earlier table
 14 looked at the returns on the market
 15 portfolio to look at how that's bounced
 16 around and the importance of that for the
 17 ROI calculations.
 18 MR. FELTHAM:
 19 A. And below this paragraph at the top of page
 20 20, there are some more references, quotes
 21 from the Board's 2005 benchmark decision and
 22 I want to refer you to the sort of second
 23 paragraph, it begins with "The Board agrees
 24 with the evidence of Dr. Kalymond and Ms.
 25 McShane"—I gather they were experts

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1 testifying in that hearing at the time.
 2 “The ROI should reflect to the extent
 3 possible the actual investment practices of
 4 Canadian automobile insurers and should bear
 5 an internal consistency to ROE in the
 6 benchmarking process.” So I gather you’ve
 7 directed us to that because that’s what that
 8 is telling us, it’s the same thing. This is
 9 the manner in which you should—you should
 10 actually look at actual investment
 11 practices.
 12 DR. LAZAR:
 13 A. Yes, I mean that’s what is built into the
 14 GISA data and you would expect the return on
 15 investments to track the ROEs and the gaps,
 16 don’t know how small or large they might be,
 17 but again if you think of it logically,
 18 you’re an insurance business and you’re
 19 investing a certain amount of equity, there
 20 are going to be regulatory tax reasons for
 21 doing so, and you’re going to expect a
 22 certain return on this investment. And a
 23 significant return is going to be generated
 24 by the cash you have available for a period
 25 of time and it appears, according to Oliver

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1 Wyman the cash generated by the premiums
 2 available for about 2.3 years on average, so
 3 you’re going to invest that to generate a
 4 return to boost your profitability, which
 5 says that you can run this business and your
 6 underwriting profits might be zero or close
 7 to zero and it’s still profitable because
 8 you got that cash that you can invest. Well
 9 if you’re simply breaking even on the
 10 underwriting side and you have a target ROE
 11 of 10 percent, you’re going to expect to do
 12 10 percent or better on your investment
 13 portfolio. You will tolerate a slightly
 14 lower return on the investment portfolio if
 15 you’re actually operating with some
 16 underwriting profit. So that would boost
 17 your overall return on equity.
 18 MR. FELTHAM:
 19 Q. And, Doctor, staying on this page for a
 20 moment, a little further down in the third
 21 paragraph, there’s the third sentence, “In
 22 Ontario, the regulator, FSCO, has been using
 23 an ROI assumption of 6 percent to set
 24 premiums.” So I want to ask you about that,
 25 Mr. Stamp, counsel for the IBC, was asking

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1 Paula Elliott, who was here on behalf of
 2 Oliver Wyman, the actuary, he asked her
 3 about that and both seemed to take issue
 4 with the notion of 6 percent being used by
 5 FSCO. Can you explain that? I mean, how
 6 did that get in there?
 7 DR. LAZAR:
 8 A. That was the number given to Eli and myself
 9 by FSCO when we did the original work, what,
 10 I think 2013? So it’s not a number that we
 11 made up, it was a number they gave us, they
 12 showed us how they incorporated into the
 13 formula. When I did the first update for
 14 the Ontario Trial Lawyers in, I think 2016,
 15 I’m trying to remember the time period
 16 again, I went back to some contacts at FSCO
 17 and asked them what ROI are you using now?
 18 And they informed me that it was still 6
 19 percent, so again, it’s a number that came
 20 directly from FSCO. I’m not aware of their
 21 publishing it anywhere, but that’s the
 22 number they used in the rate determination
 23 process, that’s the number they gave Eli and
 24 me when we did the work, that’s the number
 25 they gave to me in 2016. Has it changed in

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1 the past year or two? Possibly, maybe, I
 2 don’t know, but up to 2016 that was the
 3 number.
 4 MR. FELTHAM:
 5 Q. Okay. And then carrying on down the page,
 6 the next section in the report is “General
 7 Operating Expenses of the Insurers”. I’d
 8 like to get into that a little bit. What
 9 was your assessment here of the operating
 10 expenses and what were your findings?
 11 DR. LAZAR:
 12 A. Those are two issues. One, from a
 13 regulatory point of view what you want to do
 14 is create incentives for companies to be
 15 efficient. If you set an industry average
 16 and you’re going to base that average on
 17 one, if not two factors. One, what are the
 18 best practices in this industry, whether
 19 it’s across Canada, whether it’s across
 20 Canada and the US. Do the investigation,
 21 find out who is doing the best, what is the
 22 most efficient cost structure, and then you
 23 can probably say, well, okay, you’d like all
 24 insurance companies to trend towards that,
 25 but you’ll set an operating expense ratio

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1 slightly above it, which will tend to be
 2 lower than what's currently in practice.
 3 And that was an argument we also made with
 4 FSCO, they had used 25 percent for a long
 5 period of time and we asked them have you
 6 actually explored those practices? And they
 7 said, yeah, we know there are companies that
 8 do much better than that, but we haven't
 9 changed it. So that's the first, you know,
 10 you want to lower this to provide incentive
 11 to become more efficient and those that are
 12 extremely efficient will have a higher ROE,
 13 those that are less efficient, a lower ROE,
 14 but that's what you want to do. The second
 15 is take into account technology. What I've
 16 read in the Oliver Wyman report, commissions
 17 are 12 percent, I look at the technology in
 18 this industry and say, going forward,
 19 commissions are going to be driven down
 20 towards zero. The technology exists today
 21 and it's only a matter of time until they
 22 essentially disrupt the current brokerage
 23 system for better, for worse. All of this
 24 can be done on-line, the information is
 25 available. We see a number of US companies

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1 doing this, we even begin to see some
 2 Canadian companies, say you want a
 3 comparison of rates, that's easy to do. If
 4 you look at automobile insurance, it's
 5 largely a commodity. The only differences
 6 are really on the service side and from a
 7 consumer point of view how quickly,
 8 thoroughly, does an insurance company deal
 9 with a claim and individuals might pay a
 10 premium for better service; otherwise, the
 11 basic insurance policy, a commodity. So
 12 from an expense point of view what are the
 13 best practices, so let's adopt an expense
 14 ratio slightly above it and try to reduce it
 15 over time to encourage companies to become
 16 more efficient; and second, let's take into
 17 account the role of technology, how that
 18 will impact costs.
 19 MR. FELTHAM:
 20 Q. And I'll say this, I gather, at least in
 21 this province, a lot of insurance companies
 22 have got into the business of buying
 23 brokerages, so they may not want the
 24 commission to trend towards zero.
 25 DR. LAZAR:

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1 A. Yeah, but again, we have sort of a history
 2 of companies and industries that are
 3 overtaken by technology and, you know, it's
 4 one thing if that technology did not exist,
 5 was not developed, but it's quite a simple
 6 matter to do a quick cost comparison of
 7 insurance and it's a simple matter for, you
 8 know, an uber type, amazon type platform to
 9 be created for consumers to be matched up
 10 with the lowest cost suppliers, taking into
 11 account that service element.
 12 (10:30 a.m.)
 13 MR. FELTHAM:
 14 Q. And, Dr. Lazar, just to wrap up on the
 15 Oliver Wyman examination, on page 22, this
 16 is your conclusion in this area and you note
 17 here four times that you say lead to Oliver
 18 Wyman reaching a conclusion of premium
 19 inadequacy. You say, "Oliver Wyman's
 20 estimates of the supposed inadequacy of the
 21 premiums for auto insurance resulted from
 22 the following key assumptions: excessive
 23 ROE of 10 percent"—and we've talked about
 24 that, but it's not been calculated, it's
 25 just assumed from 2005—"unrealistically low

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1 pre-tax investment income returns", you've
 2 talked about that, but using investment
 3 income returns and their calculations that
 4 you say are too low, "the claims ratio being
 5 out of line with the GISA estimate", and
 6 finally, "the operating expenses being in
 7 the 25 percent range", rather than being
 8 more competitively placed, I guess. And
 9 then, so what did those assumptions lead to
 10 on the part of Oliver Wyman? What was the
 11 outcome as a result of those things?
 12 DR. LAZAR:
 13 A. Well, again, given the assumptions they made
 14 that would sort of bias sort of their
 15 premium as they estimated a premium,
 16 underpayments, you know, bias results in
 17 that direction, bias re: their estimated
 18 return on equities, again, towards a
 19 negative number. You know, I did some
 20 simple calculations using basically, okay,
 21 here's how we measure profits, return and
 22 equity, what are the implications? So if
 23 you were to set premiums related to the
 24 claims expected in the following year, how
 25 much higher, you know, how much higher

<p style="text-align: right;">Page 65</p> <p>1 should the premiums be over those expected</p> <p>2 claims? And it varies considerably,</p> <p>3 depending on the assumptions, and I use some</p> <p>4 assumptions with regards to the expense</p> <p>5 ratio, return on investment, return on</p> <p>6 equity, and what you get is premiums should</p> <p>7 be anywhere from the low end assumptions,</p> <p>8 about 23 percent above the expected claims</p> <p>9 for the year, upwards to, I think 42 percent</p> <p>10 higher. So depending on the sets of</p> <p>11 assumptions, how you set the premiums,</p> <p>12 there's a substantial differential. So if</p> <p>13 you use more realistic assumptions, premiums</p> <p>14 are going to be set at a much lower ratio to</p> <p>15 claims expected than if you use the type of</p> <p>16 assumptions that Oliver Wyman used.</p> <p>17 MR. FELTHAM:</p> <p>18 Q. Thank you, Doctor. I don't have any</p> <p>19 additional questions and concludes the</p> <p>20 presentation portion, Madam Chair, and,</p> <p>21 Doctor, there may be some questions for you</p> <p>22 from other parties.</p> <p>23 DR. LAZAR:</p> <p>24 A. Pleasure to entertain them.</p> <p>25 O'FLAHERTY, Q.C.:</p>	<p style="text-align: right;">Page 67</p> <p>1 June of 2017.</p> <p>2 STAMP, Q.C.:</p> <p>3 Q. And how were you contacted?</p> <p>4 DR. LAZAR:</p> <p>5 A. I'm sorry, you will have to speak a little</p> <p>6 louder.</p> <p>7 STAMP, Q.C.:</p> <p>8 Q. How were you contacted?</p> <p>9 DR. LAZAR:</p> <p>10 A. I don't think it was Colin's, Colin's</p> <p>11 colleague contacted I think Eli Prisman</p> <p>12 initially and asked if he was interested in</p> <p>13 sort of trying the work that he and I had</p> <p>14 done for FSCO and the Ontario Trial Lawyers</p> <p>15 Associate to explore, to examine the case in</p> <p>16 Newfoundland and Labrador.</p> <p>17 STAMP, Q.C.:</p> <p>18 Q. Okay, and when did you actually become</p> <p>19 engaged to do that very thing?</p> <p>20 DR. LAZAR:</p> <p>21 A. I think it was I that period, May, June.</p> <p>22 STAMP, Q.C.:</p> <p>23 Q. So you began to do—the paper we're looking</p> <p>24 at here is dated July 2018?</p> <p>25 DR. LAZAR:</p>
<p style="text-align: right;">Page 66</p> <p>1 Q. Madam Chair, Mr. Gittens advised me that he</p> <p>2 would have to leave at 10:00, so he won't be</p> <p>3 asking any questions of Dr. Lazar.</p> <p>4 CHAIR:</p> <p>5 Q. Okay. That's fine, thank you. Mr. Fraize,</p> <p>6 I guess.</p> <p>7 FRAIZE, Q.C.:</p> <p>8 Q. We have no questions.</p> <p>9 CHAIR:</p> <p>10 Q. Okay. Mr. Stamp.</p> <p>11 STAMP, Q.C.:</p> <p>12 Q. Dr. Lazar, just to clarify, can you tell me</p> <p>13 when you were engaged for this work, please?</p> <p>14 DR. LAZAR:</p> <p>15 A. Well the exact date?</p> <p>16 STAMP, Q.C.:</p> <p>17 Q. If you have that.</p> <p>18 DR. LAZAR:</p> <p>19 A. Well if you bear with me, I'll open up this</p> <p>20 file and try to get some sense of this. It</p> <p>21 appears sometime June—May of 2017.</p> <p>22 STAMP, Q.C.:</p> <p>23 Q. Did you say June or May of 2017?</p> <p>24 DR. LAZAR:</p> <p>25 A. It appears to be based on this file, May,</p>	<p style="text-align: right;">Page 68</p> <p>1 A. Yes.</p> <p>2 STAMP, Q.C.:</p> <p>3 Q. Are you saying you spent more than a year</p> <p>4 doing that?</p> <p>5 DR. LAZAR:</p> <p>6 A. No. The original report was essentially</p> <p>7 what would have been Sections 3 and 4,</p> <p>8 whatever, and in this current report, let me</p> <p>9 just go back and be exact, my conclusions,</p> <p>10 referred to as Sections 2, 3, and 4 and then</p> <p>11 Oliver Wyman's report was made public and we</p> <p>12 were re-approached to examine that report</p> <p>13 and make comments on that. So the report</p> <p>14 you have is essentially our original report,</p> <p>15 including the section of our commentary on</p> <p>16 the Oliver Wyman report.</p> <p>17 STAMP, Q.C.:</p> <p>18 Q. All right, so when you say Sections, 2, 3,</p> <p>19 4, I'm just trying to make sure I'm clear,</p> <p>20 what are Sections 2, 3, 4 in this report?</p> <p>21 DR. LAZAR:</p> <p>22 A. Yeah, here it's just looking at the ROEs for</p> <p>23 auto insurance companies in the province,</p> <p>24 looking at –</p> <p>25 STAMP, Q.C.:</p>

<p style="text-align: right;">Page 69</p> <p>1 Q. What page is that at, Mr. Lazar, please, I'm 2 just trying to make sure I'm clear. 3 DR. LAZAR: 4 A. Sorry, it would be—so the original report 5 focussed on looking at the ROEs for 6 automobile insurance companies operating in 7 Newfoundland and Labrador, determining the 8 appropriate return on equities, looking at 9 the question of premium overpayments and 10 capital adequacy. So our original report 11 dealt strictly with those issues. Obviously 12 the Oliver Wyman report was not available at 13 that time and our report did not include any 14 commentary, any discussion about the Oliver 15 Wyman report. 16 STAMP, Q.C.: 17 Q. So what was the date of that first report? 18 DR. LAZAR: 19 A. I'm sorry? 20 STAMP, Q.C.: 21 Q. What was the date of the first report? 22 DR. LAZAR: 23 A. Again, let me go back. First report, it 24 would look sometime, sort of mid July 2017. 25 It appears to be the case, yes.</p>	<p style="text-align: right;">Page 71</p> <p>1 issue, was that Mr. Prisman's work 2 essentially? 3 DR. LAZAR: 4 A. Sorry? 5 STAMP, Q.C.: 6 Q. Was the ROE essentially Mr. Prisman's? 7 DR. LAZAR: 8 A. Again, Eli did sort of the statistical of 9 calculations. I'm fully capable of doing 10 that, but you know, he assisted in doing it, 11 so I had no difficulty, and then the writing 12 of the report, based on those results, was a 13 joint effort. 14 STAMP, Q.C.: 15 Q. You said in your evidence earlier, 16 "estimating ROE is Prisman's, is a workhorse 17 of finance." 18 DR. LAZAR: 19 A. Yes. 20 STAMP, Q.C.: 21 Q. So Prisman did that work? 22 DR. LAZAR: 23 A. He calculated the beta I the capital asset 24 pricing model and the risk-free rates. 25 STAMP, Q.C.:</p>
<p style="text-align: right;">Page 70</p> <p>1 STAMP, Q.C.: 2 Q. And that was a former report, like this one 3 submitted to Mr. Feltham or to who? 4 DR. LAZAR: 5 A. I think Colin was our liaison at the time 6 and I apologize, I forget the name of your 7 colleague, and it was submitted to them and 8 we said thank you. And then many months 9 later, they came back to us, I guess because 10 these hearings were announced and there was 11 the Oliver Wyman report. 12 STAMP, Q.C.: 13 Q. So this first report you prepared was, you 14 think, submitted, dated and submitted in 15 around July, 2017? 16 DR. LAZAR: 17 A. Yes. 18 STAMP, Q.C.: 19 Q. And one of the focusses was ROE, you say? 20 DR. LAZAR: 21 A. It was essentially everything in this report 22 except a discussion, commentary on the 23 Oliver Wyman report. 24 STAMP, Q.C.: 25 Q. And in that report, particularly the ROE</p>	<p style="text-align: right;">Page 72</p> <p>1 Q. Okay, that wasn't your work, that was his 2 work? 3 DR. LAZAR: 4 A. Yes, but again, I'm fully capable of doing 5 that, it's not something that is foreign to 6 me and it's not something I haven't used 7 myself. 8 STAMP, Q.C.: 9 Q. Right, but you didn't do it in this case, he 10 did it? 11 DR. LAZAR: 12 A. No. 13 STAMP, Q.C.: 14 Q. So then when were you contacted—you did that 15 report in July of 2017, submitted it to 16 either Mr. Feltham or one of his colleagues, 17 and then what happened after that? 18 DR. LAZAR: 19 A. Silence until sometime early in 2018. 20 STAMP, Q.C.: 21 Q. Right. 22 DR. LAZAR: 23 A. And again – 24 STAMP, Q.C.: 25 Q. When in 2018 would that have been, Mr.</p>

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1 Lazar?
 2 DR. LAZAR:
 3 A. It would probably have to be, what's the
 4 date of the Oliver Wyman report? Oliver
 5 Wyman report is March 29th, so it was
 6 probably sometime in April.
 7 STAMP, Q.C.:
 8 Q. Okay, and so you had between April, sometime
 9 and April you were contacted, you think, do
 10 you know when that was?
 11 DR. LAZAR:
 12 A. When exactly in April?
 13 STAMP, Q.C.:
 14 Q. Yes.
 15 DR. LAZAR:
 16 A. I'm just going by some of these dates here,
 17 all I can say is sometime early April.
 18 STAMP, Q.C.:
 19 Q. And then your report is dated July, when was
 20 it actually submitted? What date in July?
 21 DR. LAZAR:
 22 A. The report, I think early July, July 12th
 23 thereabouts, again just going by the dates
 24 that I have here.
 25 STAMP, Q.C.:

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1 Q. So should I take it from this that you spent
 2 about three months doing the report?
 3 DR. LAZAR:
 4 A. No.
 5 STAMP, Q.C.:
 6 Q. Okay, how long?
 7 DR. LAZAR:
 8 A. How long? It was over that period of time,
 9 but I don't know the exact number of days.
 10 Five days, eight days, over that period of
 11 time, somewhere in that range.
 12 STAMP, Q.C.:
 13 Q. All right. In your report you suggest that,
 14 and I'm not sure if I—I will try and locate
 15 the exact—in your report and you spoke about
 16 this this morning, you estimated premium
 17 overpayment and you referred to the 92, 54
 18 to 92 you said was the upper limit?
 19 DR. LAZAR:
 20 A. Yes.
 21 STAMP, Q.C.:
 22 Q. 54 to 92 as an upper limit. Why is there
 23 such a significant range in the upper limit?
 24 DR. LAZAR:
 25 A. It's a function of what companies were

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1 included for the calculation and the
 2 differences were for the higher limit we
 3 excluded, not only the TD subsidiaries, but
 4 I think there were three other companies
 5 that were excluded, personal insurance, I
 6 think Intact and there was there another
 7 one? I believe that's it, yes.
 8 STAMP, Q.C.:
 9 Q. And if you looked at the upper limit, what
 10 was the lower limit?
 11 DR. LAZAR:
 12 A. The lower limit –
 13 STAMP, Q.C.:
 14 Q. For comparison to 54 to 91 being the upper
 15 limit, what would be the lower limit?
 16 DR. LAZAR:
 17 A. The lower limit would be from zero upwards,
 18 the only way we could ever determine the
 19 actual number, as I said before, is if we
 20 knew what the premiums that were permissible
 21 aggregated overall companies were in each
 22 year, and what the premiums could have been
 23 using different sets of assumptions.
 24 STAMP, Q.C.:
 25 Q. On that very point that premiums that are

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1 permitted each year, did you make any
 2 inquiry of the Public Utilities Board to
 3 determine what premiums were permitted?
 4 DR. LAZAR:
 5 A. No.
 6 STAMP, Q.C.:
 7 Q. Why didn't you do that?
 8 DR. LAZAR:
 9 A. Just using public data, we weren't going
 10 into any sort of detailed analysis. Our
 11 original, sort of, position was to look at
 12 the return on equity, what should it have
 13 been. A second was to look at the
 14 reasonableness of the expense ratios.
 15 STAMP, Q.C.:
 16 Q. Yes, I know, I got that.
 17 DR. LAZAR:
 18 A. Yes.
 19 STAMP, Q.C.:
 20 Q. I heard that. I'm trying to understand why
 21 you didn't look at available data the Public
 22 Utilities –
 23 DR. LAZAR:
 24 A. Okay, I -
 25 STAMP, Q.C.:

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1 Q. - Board has all the rates available that are
 2 approved for insurers, you didn't choose to
 3 look at that?
 4 DR. LAZAR:
 5 A. No, because again, we were studying from a
 6 different, not mandate, but a different sort
 7 of approach. Even if we had looked at it,
 8 we would then still have had to go back to
 9 the regulator and say, okay now for each of
 10 these insurance companies tell us what were
 11 their expected claims year by year. And
 12 then we could come up with an estimate of
 13 what would be more reasonable permitted
 14 premiums. That, I think, is a task for the
 15 Board to do or to decide whether they want
 16 that done to come up with an accurate
 17 measure.
 18 (10:45 a.m.)
 19 STAMP, Q.C.:
 20 Q. You talked about companies shifting income –
 21 DR. LAZAR:
 22 A. Yes.
 23 STAMP, Q.C.:
 24 Q. to the most favourable location. If
 25 companies have an obligation to pay taxes in

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1 this jurisdiction, for example, that's a
 2 legal obligation, is it not?
 3 DR. LAZAR:
 4 A. That's legal, but you still have flexibility
 5 with regards to how you allocate
 6 expenditures.
 7 STAMP, Q.C.:
 8 Q. So, you're not asserting that somebody has,
 9 sort of, cheated one province or another.
 10 DR. LAZAR:
 11 A. I made it clear at the outset that transfer
 12 pricing is legal. There are limitations
 13 imposed and companies would fully take
 14 advantage of the rules to minimize their tax
 15 liabilities. They're not doing anything
 16 illegal. It's all legal; it's all
 17 permissible.
 18 STAMP, Q.C.:
 19 Q. Okay. I want to come back to your table 17,
 20 it's at page 29 of your report.
 21 DR. LAZAR:
 22 A. Yes.
 23 STAMP, Q.C.:
 24 Q. So, do I understand that's what's happened
 25 here is that you took certain companies in

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1 the top line and more companies in the
 2 bottom line, is your—if what is done here is
 3 added 15 and 9 and 3 and 26?
 4 DR. LAZAR:
 5 A. Yes.
 6 STAMP, Q.C.:
 7 Q. To 54?
 8 DR. LAZAR:
 9 A. Yes.
 10 STAMP, Q.C.:
 11 Q. And added 42 and 19 and 6 and 24 to 92?
 12 DR. LAZAR:
 13 A. Correct.
 14 STAMP, Q.C.:
 15 Q. Right. Now, you also said—I just want to
 16 try and find this for you. I can't put my
 17 fingers right on it, but my recollection,
 18 Mr. Lazar, was that you said, there were
 19 significant losses in '14 and '15.
 20 DR. LAZAR:
 21 A. Yes.
 22 STAMP, Q.C.:
 23 Q. I think you said the profits—when profits
 24 eroded substantially, I think you might have
 25 said, in '14/'15.

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1 DR. LAZAR:
 2 A. Yes.
 3 STAMP, Q.C.:
 4 Q. Were the profits in '14/'15 that would go
 5 into Table 17 negative?
 6 DR. LAZAR:
 7 A. They weren't included in Table 17.
 8 STAMP, Q.C.:
 9 Q. No, that's what I'm wondering; where are
 10 they?
 11 DR. LAZAR:
 12 A. I just ignored them. I was asked to redo
 13 this, taking those into account.
 14 STAMP, Q.C.:
 15 Q. Taking, asked to take what into account?
 16 DR. LAZAR:
 17 A. The negative results in 2014/2015 and if
 18 they're negative results, the argument that
 19 was posed to me was well, does that mean
 20 that there were premium underpayment and
 21 shouldn't that be factored out? That was
 22 the presumption and I reported to that
 23 question and said okay, I'm quite happy to
 24 throw them in here are the results.
 25 STAMP, Q.C.:

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1 Q. Okay, I'm confused. We got to back up a
 2 bit. You said somebody asked you to take
 3 them out?
 4 DR. LAZAR:
 5 A. No, no. Someone asked, posed a question to
 6 Eli and myself, okay, you didn't include
 7 those negative results. Shouldn't you have
 8 included them to refine your estimates of
 9 the upper limit of the premium overpayments
 10 assuming that if there were these losses
 11 that therefore there were premium
 12 underpayments and that should have been
 13 deducted from the premium overpayments to
 14 come up with a more reasonable number? That
 15 question was posed to us and we responded
 16 and said, that's fine, we'll throw these in
 17 and we'll show you what the numbers are and
 18 you can judge what that means for you, but
 19 I'll have a different position on that.
 20 STAMP, Q.C.:
 21 Q. Where are those numbers thrown in?
 22 DR. LAZAR:
 23 A. In a response to questions submitted by the
 24 Public Utilities Board, I'm not sure if it
 25 was the Board that asked that question or if

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1 it was your organization that asked the
 2 question. We responded and submitted those
 3 to Colin and I just presumed that he
 4 forwarded them to everybody who is
 5 participating here.
 6 STAMP, Q.C.:
 7 Q. Sure, and so for '14/'15, if you have
 8 plugged in numbers in both lines, all
 9 excluding Primmum and Security National –
 10 DR. LAZAR:
 11 A. Yeah.
 12 STAMP, Q.C.:
 13 Q. - and then the second line, all positive
 14 ROEs, if you'd plug numbers in there for
 15 those two years, for those two groupings,
 16 what would the numbers be?
 17 DR. LAZAR:
 18 A. The resulting total over the period?
 19 STAMP, Q.C.:
 20 Q. No, the numbers for '14 and the numbers for
 21 '15.
 22 DR. LAZAR:
 23 A. Okay. Roughly, again slightly different
 24 methodology, but the numbers will be
 25 reasonable, -21,000,000 by both years and

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1 one can then –
 2 STAMP, Q.C.:
 3 Q. Negative twenty one million?
 4 DR. LAZAR:
 5 A. Negative twenty one million.
 6 STAMP, Q.C.:
 7 Q. In which line?
 8 DR. LAZAR:
 9 A. 2014/2015.
 10 STAMP, Q.C.:
 11 Q. Which line of 2014/'15?
 12 DR. LAZAR:
 13 A. All excluding Primmum and Security National.
 14 STAMP, Q.C.:
 15 Q. Twenty one, twenty one million?
 16 DR. LAZAR:
 17 A. Yes.
 18 STAMP, Q.C.:
 19 Q. Negative?
 20 DR. LAZAR:
 21 A. Yes. And then the question becomes, does
 22 this reflect premium underpayments?
 23 STAMP, Q.C.:
 24 Q. Well, it affects a poor result in '11, '12,
 25 '13 and '16, does it not?

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1 DR. LAZAR:
 2 A. Yes, however, as I pointed out, the complete
 3 analysis would have been here are the
 4 premiums and aggregate that were permitted.
 5 Here are the premiums that should or could
 6 have been permitted under different set of
 7 assumptions. ROE assumptions, expense
 8 assumptions, ROI assumptions. And you take
 9 that differential which means in 2014/2105
 10 it still would have been a positive number.
 11 STAMP, Q.C.:
 12 Q. Hold on a second now. When you did 2011,
 13 did you use a number that actually occurred,
 14 you say –
 15 DR. LAZAR:
 16 A. Yes.
 17 STAMP, Q.C.:
 18 Q. - a number that—is it a number that you
 19 created or that's published somewhere?
 20 DR. LAZAR:
 21 A. That number, that's a number we created. We
 22 took the actual performance and we compared
 23 it to what would have been a more
 24 appropriate ROE for that year.
 25 STAMP, Q.C.:

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1 Q. Right, okay, so you took your theory of
 2 what's more appropriate and generated a
 3 number for 2011 of 15.4, is that right?
 4 DR. LAZAR:
 5 A. Yes.
 6 STAMP, Q.C.:
 7 Q. And you did the same for '12 and so on?
 8 DR. LAZAR:
 9 A. Correct.
 10 STAMP, Q.C.:
 11 Q. And when you took your appropriate approach
 12 on '14, what did you get?
 13 DR. LAZAR:
 14 A. When you're referring to appropriate
 15 approach –
 16 STAMP, Q.C.:
 17 Q. No, I don't think it's appropriate. I'm
 18 saying it's your approach.
 19 DR. LAZAR:
 20 A. Okay, which one are you referring to?
 21 STAMP, Q.C.:
 22 Q. The one that gave you 15.4.
 23 DR. LAZAR:
 24 A. For that, again since the gap was negative,
 25 we just zeroed it out.

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1 STAMP, Q.C.:
 2 Q. Hold on now. You used an approach you told
 3 me.
 4 DR. LAZAR:
 5 A. Yes.
 6 STAMP, Q.C.:
 7 Q. I want to understand this. You used an
 8 approach to get 15.4.
 9 DR. LAZAR:
 10 A. Okay, let me backtrack.
 11 STAMP, Q.C.:
 12 Q. Sure.
 13 DR. LAZAR:
 14 A. When the gap between the actual ROE and our
 15 estimate of what would be an appropriate
 16 ROE, again subject to the fact that we're
 17 using annual numbers rather than a moving
 18 average, when the gap was positive, that
 19 produced an estimate of an upper range for
 20 possible premium overpayments. When the gap
 21 was negative, which was the case in
 22 2014/2015, we just zeroed it out. We did
 23 not include that.
 24 STAMP, Q.C.:
 25 Q. But why did you zero it out? Why not show

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1 what your similar approach would have been
 2 for '14 rather than leave it blank?
 3 DR. LAZAR:
 4 A. Because our arguments would be that the
 5 losses that were incurred might have been
 6 the result of misestimating, misjudging the
 7 actual realized claims for the year, might
 8 have been the result of competitive pricing.
 9 There may have been a whole host of other
 10 factors that drove those losses. These are
 11 ex-post losses compared to what was
 12 anticipated at the beginning of that period.
 13 STAMP, Q.C.:
 14 Q. But everybody anticipates at the start of
 15 the period, I guess, that they're going to
 16 make some money.
 17 DR. LAZAR:
 18 A. Yes, that's the essence of risk.
 19 STAMP, Q.C.:
 20 Q. Sure. But I got to tell you, Mr. Lazar, you
 21 got me baffled because I'm looking at this
 22 and saying, okay, you leave out some years
 23 because it could be explained by some bit of
 24 back luck and planets lined up badly. This
 25 is what would have happened, but you don't

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1 tell me the numbers.
 2 DR. LAZAR:
 3 A. We did present the numbers in response to
 4 the question.
 5 STAMP, Q.C.:
 6 Q. Can I ask you to take a look at your, I
 7 guess these came from you, responses to
 8 questions submitted by Public Utilities
 9 Board.
 10 DR. LAZAR:
 11 A. Yes. The numbers are there.
 12 STAMP, Q.C.:
 13 Q. Okay. Do you have that? I don't know if
 14 you have that up there.
 15 DR. LAZAR:
 16 A. I have it.
 17 STAMP, Q.C.:
 18 Q. Thank you, okay. So, tell me, the question
 19 I guess—I can probably get the questions for
 20 you too so that we won't be confused, just
 21 give me a second there.
 22 DR. LAZAR:
 23 A. What you're suggesting is, if we throw those
 24 in, that gives a better estimate, possibly
 25 of premium overpayments over the entire

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1 period.
 2 STAMP, Q.C.:
 3 Q. Mr. Lazar, the Public Utilities Board
 4 question number 6 was this, “Please explain
 5 why the years 2014 and 2015 are left blank
 6 in Table 16, 17 and ‘18”? And your answer
 7 which was on the board a moment ago—I’m
 8 sorry we just shifted off that again, but
 9 your answer was there.
 10 DR. LAZAR:
 11 A. Because the gap was negative.
 12 STAMP, Q.C.:
 13 Q. Yeah, your answer--sorry, just to come back
 14 to your answer--is “the years 2014 and ‘15
 15 are left blank because in both years the
 16 aggregate ROEs were negative and thus
 17 obviously below our estimates of appropriate
 18 ROEs for this industry in Newfoundland and
 19 Labrador”. So, where are the numbers? You
 20 said you gave the numbers, where are the
 21 numbers?
 22 DR. LAZAR:
 23 A. They’re in point 7 on that same document.
 24 STAMP, Q.C.:
 25 Q. Is that “ROE gaps” that you’re talking

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1 about?
 2 DR. LAZAR:
 3 A. Yes, yes.
 4 STAMP, Q.C.:
 5 Q. So, when you said 21,000,000 –
 6 DR. LAZAR:
 7 A. That’s point 8.
 8 STAMP, Q.C.:
 9 Q. Hold on now, I’m trying to understand.
 10 DR. LAZAR:
 11 A. I thought it was clear in what we did and
 12 how we responded.
 13 STAMP, Q.C.:
 14 Q. Not to me.
 15 DR. LAZAR:
 16 A. Sorry.
 17 KENNEDY, Q.C.:
 18 Q. I think it should be pointed out, Chair, and
 19 it will be pointed out to members of the
 20 Board later, Mr. Stamp has had this report,
 21 IBC has had this report for quite some time.
 22 They could have had their own expert, they
 23 could have brought expert evidence. I
 24 don’t think the commentary, the gratuitous
 25 commentary “it’s not clear to me” adds

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1 anything to this hearing. Comments like
 2 that—Dr. Lazar is answering the questions,
 3 the questions are being put to him. They
 4 could have had their own expert and we will
 5 be arguing this in our submissions.
 6 STAMP, Q.C.:
 7 Q. The point, Madam Chair, of course is Mr.
 8 Lazar has prepared this report, we’re
 9 looking for clarification, that’s the
 10 purpose of the questions, to inform the
 11 Board on Mr. Lazar’s report and any
 12 questions that arise out of that report.
 13 We’ve done the same thing. I mean, all the
 14 questions that were put to Oliver Wyman,
 15 there were tonnes of questions of the same
 16 sort, explain this and explain that.
 17 There’s nothing different happening here at
 18 all with Mr. Lazar and I’m just trying to
 19 understand it.
 20 DR. LAZAR:
 21 A. Oh no, I have no problem with your
 22 questions.
 23 KENNEDY, Q.C.:
 24 Q. It’s the gratuitous comments that I have—the
 25 commentary “I don’t understand”, “I’m not

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1 clear”, that’s not the purpose of
 2 questioning, ask a question and you’ll get
 3 an answer, can you explain a little bit
 4 further” but we’ve seen this now for two
 5 days with gratuitous comments that I would
 6 suggest, sir, is not appropriate. It’s not
 7 the way it should be conducted, the
 8 questions should be conducted. It’s
 9 disparaging to the witness, “I’m not clear”,
 10 “I don’t understand”.
 11 STAMP, Q.C.:
 12 Q. And I don’t.
 13 KENNEDY, Q.C.:
 14 Q. Well that’s your problem, Mr. Stamp. You
 15 could have obtained an expert witness, you
 16 chose not to do that, you choose to rely on
 17 Oliver Wyman, fair enough, that’s the way
 18 this works out. So I’m suggesting, Madam
 19 Chair, we saw it yesterday with the attack
 20 on the people from Ontario and I don’t think
 21 this thing can deteriorate to that same kind
 22 of questioning today, that’s what I’m asking
 23 you to stop.
 24 STAMP, Q.C.:
 25 Q. Madam Chair, Mr. Lazar was asked about the

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1 gap in his Table No. 17, and he's explained
 2 in some fashion why that gap exists. He
 3 said he provided the numbers in answers to
 4 either IBC or the Public Utilities Board.
 5 So I got the questions and I've read the
 6 question into the record from the Public
 7 Utilities Board, Question No. 6, and I've
 8 asked—because the answer to Question No. 6
 9 is contained in the Answer No. 6 in the
 10 response, but the numbers that were asked
 11 for by the Public Utilities Board are not
 12 given in No. 6. Now I think Mr. Lazar had
 13 explained to us they're in maybe 7 or 8, I'm
 14 going to just try and clarify that because
 15 that's where my confusion lies.
 16 CHAIR:
 17 Q. Just ask your question.
 18 STAMP, Q.C.:
 19 Q. Sure. So, are the numbers for 14 and 15,
 20 Mr. Lazar, that would have gone into Table
 21 17, which were asked for by the Public
 22 Utilities Board, where are they please?
 23 DR. LAZAR:
 24 A. They're in Point 9.
 25 STAMP, Q.C.:

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1 Q. And they're percentages, are they?
 2 DR. LAZAR:
 3 A. Sorry?
 4 STAMP, Q.C.:
 5 Q. Are Point 9 percentages?
 6 DR. LAZAR:
 7 A. Oh, sorry, Point 8.
 8 STAMP, Q.C.:
 9 Q. Point 8 has the numbers?
 10 DR. LAZAR:
 11 A. Yes, sorry about that.
 12 STAMP, Q.C.:
 13 Q. Okay, so Point 8 is dollar amounts?
 14 DR. LAZAR:
 15 A. Yes. Point 9 is percentage amounts, as you
 16 correctly pointed out.
 17 STAMP, Q.C.:
 18 Q. Right, and so the 14 number is minus 29
 19 million now?
 20 DR. LAZAR:
 21 A. No, the one that is comparable to Table 17
 22 in our report is 21 million, minus 21
 23 million number.
 24 STAMP, Q.C.:
 25 Q. I thought—and you can clarify this for me,

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1 when I was asking what numbers would have
 2 gone into the lines on 14 and 15 of Table
 3 17, I thought you had told me the top line?
 4 DR. LAZAR:
 5 A. No, it's again to be equivalent the first,
 6 well the second row there is all excluding
 7 Primmum and Security National. This is
 8 where the minus 21 million comes in.
 9 STAMP, Q.C.:
 10 Q. Okay.
 11 DR. LAZAR:
 12 A. Second is all positive ROEs where it's
 13 approximately minus 20 million.
 14 STAMP, Q.C.:
 15 Q. So if you included those minus, for example
 16 all companies is minus 61 million.
 17 DR. LAZAR:
 18 A. Okay, now I want to point out that in
 19 responding we did just a short cut, just
 20 took the gap, multiplied it by the equity.
 21 For the report, we did an iterative process,
 22 the only reason we did the short cut here
 23 was just time constraints. If you compare
 24 the results in the response Point 8 to our
 25 Table 17, what you find is the iterative

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1 process actually produced larger estimates
 2 of the overpayments.
 3 STAMP, Q.C.:
 4 Q. So when I look at your answer No. 8.
 5 DR. LAZAR:
 6 A. Yes.
 7 STAMP, Q.C.:
 8 Q. Looked at the question, but the answer,
 9 because this is what you're explaining to
 10 me, is that the total 11 through 16, all
 11 excluding Primmum and National Security and
 12 all companies, it's just that those two—the
 13 two things are flipped around from the Table
 14 17. Table 17 has all positive ROEs on the
 15 bottom and you have all companies on the top
 16 in this table at No. 8, is that right?
 17 DR. LAZAR:
 18 A. Is that first row, all companies, is nowhere
 19 in Table 17.
 20 STAMP, Q.C.:
 21 Q. Okay.
 22 DR. LAZAR:
 23 A. Only the next two rows are the equivalent to
 24 what's in Table 17.
 25 STAMP, Q.C.:

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1 Q. Which two rows, I'm sorry?
 2 DR. LAZAR:
 3 A. The last two rows. Would it be easier if I
 4 just came there and pointed it out? I mean,
 5 I'm sorry, I just can't make it any clearer.
 6 I'm not sure what the confusion is.
 7 STAMP, Q.C.:
 8 Q. Well when I look at Table 17, all positive
 9 ROEs.
 10 DR. LAZAR:
 11 A. Yes. That is the equivalent of the last row
 12 in our Point 8.
 13 STAMP, Q.C.:
 14 Q. Right, which is 92 million, the total 92
 15 million?
 16 DR. LAZAR:
 17 A. Yes.
 18 STAMP, Q.C.:
 19 Q. And that becomes 2 million?
 20 DR. LAZAR:
 21 A. No, it becomes 35.
 22 STAMP, Q.C.:
 23 Q. I'm sorry, in –
 24 DR. LAZAR:
 25 A. You have got to compare the same groupings.

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1 STAMP, Q.C.:
 2 Q. Where do I find 35 in the—Oh, over here,
 3 over in the other positive ROEs.
 4 DR. LAZAR:
 5 A. Yes.
 6 STAMP, Q.C.:
 7 Q. I see. Okay, so there's all companies and
 8 all positive ROEs.
 9 DR. LAZAR:
 10 A. And the number in Point 8, the 35 million,
 11 if we had used the same methodology we used
 12 in the report, that number would actually be
 13 higher, approximately about 15 – 20 percent
 14 higher.
 15 STAMP, Q.C.:
 16 Q. So, this in this response you gave to the
 17 Public Utilities Board, the 54 million in
 18 Table 17 becomes two in estimated, in Number
 19 8 answer.
 20 DR. LAZAR:
 21 A. Yes, but again –
 22 STAMP, Q.C.:
 23 Q. And the 92 becomes 34.
 24 DR. LAZAR:
 25 A. But both of those are underestimated

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1 because we use a simple methodology for the
 2 responses as compared to the more
 3 appropriate iterative methodology in our
 4 report.
 5 CHAIR:
 6 Q. Mr. Stamp, might this be a good time for us
 7 to take a break?
 8 STAMP, Q.C.:
 9 Q. Yes, Madam Chair.
 10 (BREAK – 11:06 a.m.)
 11 (RESUME – 11:36 a.m.)
 12 CHAIR:
 13 Q. Back to you, Mr. Stamp.
 14 STAMP, Q.C.:
 15 Q. Thank you, Madam Chair. Mr. Lazar, I'm just
 16 going to go back to your Table 17 in your
 17 report for a moment, at page 29.
 18 DR. LAZAR:
 19 A. Okay.
 20 STAMP, Q.C.:
 21 Q. I want to note for a moment, the top line
 22 “All except”—I guess—“Primum and Security
 23 National”, do you see 15.4, 9.5, 3.4 and
 24 then two spaces and the 26 and 54. And if I
 25 can now turn to the answers or responses to

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1 the questions from Public Utilities Board
 2 and at page, there's no page number, I'm
 3 sorry, answer Number 8, I guess, at the
 4 bottom of the page. Yeah, that's right
 5 there, that's fine. Do you have that Mr.
 6 Lazar?
 7 DR. LAZAR:
 8 A. Yes.
 9 STAMP, Q.C.:
 10 Q. Now, you don't have the other numbers in
 11 front of you again, but if you need, I can –
 12 DR. LAZAR:
 13 A. Which table were you –
 14 STAMP, Q.C.:
 15 Q. The bottom of—it's marked Number 8.
 16 DR. LAZAR:
 17 A. No, no, what was the table in the report you
 18 referred to?
 19 STAMP, Q.C.:
 20 Q. Seventeen.
 21 DR. LAZAR:
 22 A. Okay, I've got that here.
 23 STAMP, Q.C.:
 24 Q. So, what I'm noting is that the line for
 25 “all excluding Primum and Security

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<p>1 National” in the table, in response Number 8 2 puts numbers in there, of course, 21 million 3 or -20.7 or whatever, -20.7 and 20.7. 4 DR. LAZAR: 5 A. Yes. 6 STAMP, Q.C.: 7 Q. But why have you changed the other numbers 8 as well? 9 DR. LAZAR: 10 A. Okay, as I explained, there are two possible 11 approaches. The simple approach which is 12 what was used for Point 8 here in the 13 response was to simply take the gap, the 14 difference between the actual ROE and/or 15 estimate of what should be an acceptable ROE 16 and multiply that times the total equity. 17 So, that’s the methodology, the simple 18 methodology that we employed in the 19 response, less time consuming. 20 STAMP, Q.C.: 21 Q. Okay. 22 DR. LAZAR: 23 A. In the report, we went through an iterative 24 process because once you start making 25 adjustments for differences in equity, you</p>	<p>1 A. No, the premium is part of the—two parts of 2 it. I believe there’s legal obligation to 3 hold a certain amount of reserves against 4 future claims. And the premiums provide the 5 claims will be paid in the future. You 6 going to have net of your expenses some cash 7 available to you for a period of time that 8 you can that you can invest. 9 STAMP, Q.C.: 10 Q. So, reserves for the purposes of this, when 11 you made this comment, reserves are 12 essentially equity that’s maintained in the 13 company? 14 DR. LAZAR: 15 A. We equated it to primarily because of the 16 work we did with FSCO where they simply used 17 the particular ratio of premium to equity 18 which FSCO claimed and we have no reason to 19 question them on this, they said was a 20 measure of, sort of, the reserves, the 21 investable funds that the companies had. 22 STAMP, Q.C.: 23 Q. But when I asked you what reserves were, I 24 thought you said it’s the amount retained to 25 provide protection for claims. Did you say</p>
<p>1 have to factor that back into return on 2 investment, et cetera. So, we use the more, 3 sort of, complicated with more appropriate 4 approach in the report than we did in the 5 response. And again, the only reason we did 6 that for the response was to save time. 7 STAMP, Q.C.: 8 Q. Okay. I want to just come back to your 9 evidence earlier today. At one point you 10 said, and hopefully I got this generally 11 accurately recorded, reserves are invested 12 by insurers and it’s a major driver of 13 profitability. Now, I may not have that 14 exactly right, but something to that effect. 15 DR. LAZAR: 16 A. Yes. 17 STAMP, Q.C.: 18 Q. And what are reserves? 19 DR. LAZAR: 20 A. The reserves that have to hold against 21 future claims. 22 STAMP, Q.C.: 23 Q. And so is that—that’s not the premium for 24 investment, is it? 25 DR. LAZAR:</p>	<p>1 that – 2 DR. LAZAR: 3 A. For future claims, yes. 4 STAMP, Q.C.: 5 Q. Future claims, yes. And so that’s the—is it 6 essentially the equity in the company? 7 DR. LAZAR: 8 A. We use them as being equivalent. 9 STAMP, Q.C.: 10 Q. That may be, but essentially is what you’re 11 referring to, essentially is the equity in 12 the company. 13 DR. LAZAR: 14 A. The equity committed for this line of 15 business. 16 STAMP, Q.C.: 17 Q. Right. And would that be all the equity in 18 the company or limited amount of equity? 19 DR. LAZAR: 20 A. Again, we used it as the entire equity 21 committed to this line of business in this 22 province. 23 STAMP, Q.C.: 24 Q. Okay. Now, you also spoke about reserves, I 25 think, in a different context. You said,</p>

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1 most if not all insurers invest significant
 2 part of reserves in equity. Do you recall
 3 that discussion?
 4 DR. LAZAR:
 5 A. Yes.
 6 STAMP, Q.C.:
 7 Q. And so when you speak that way, are you
 8 speaking about the same reserves that you
 9 spoke about earlier?
 10 DR. LAZAR:
 11 A. Yes.
 12 STAMP, Q.C.:
 13 Q. Okay. And what part, you say a significant
 14 part, what part does each insurer invest?
 15 DR. LAZAR:
 16 A. I don't know.
 17 STAMP, Q.C.:
 18 Q. But you said it was significant.
 19 DR. LAZAR:
 20 A. If you'll look at the returns they've
 21 generated on their investments and
 22 essentially on this pool of funds, then you
 23 know, you compare it to returns on investing
 24 in a bond portfolio, one can infer from that
 25 as we did, that there has to be, don't know

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1 what the number is, 40, 50 percent on
 2 average that might be invested in equities
 3 in order to generate those returns.
 4 STAMP, Q.C.:
 5 Q. I just noticed that one of the pieces of
 6 information that IBC has on their—they have
 7 a facts book which records or discloses how
 8 insurers, P & C insurers invest—how they
 9 actually—what they invest in. And the
 10 investment on the equity side, this is I
 11 think part of the data is from MSA and I
 12 think some from Provincial authorities.
 13 That investment in shares which I take it to
 14 be equities is 11.2 percent as of the end of
 15 the December 2017.
 16 MR. FELTHAM:
 17 Q. Madam Chair, Mr. Stamp is—we've had this
 18 theme reoccurring here. Again, we're
 19 referring to documentation which hasn't been
 20 provided to the Board, hasn't been provided
 21 to the parties, that witness has not had an
 22 opportunity to review what he's being
 23 referred to. It's very unfair.
 24 STAMP, Q.C.:
 25 Q. Madam Chair, let me just try and see if we

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1 can get past some of this complication. Mr.
 2 Lazar came this morning and he testified
 3 that more, if not all insurers invest
 4 significant part of reserves in equity.
 5 Now, I don't know where that would be in
 6 this report. I haven't seen it and so he's
 7 testified or spoken about or presented it as
 8 part of this information this morning. I'm
 9 happy to let that go in, but I'm happy to
 10 question him about it as well. I can't
 11 anticipate what he will say and come armed
 12 with a library. I had to come and listen to
 13 Mr. Lazar give his presentation and then ask
 14 him about that presentation. This is just
 15 one aspect of that presentation.
 16 (11:45 a.m.)
 17 MR. FELTHAM:
 18 Q. Madam Chair, it's not library. He's the one
 19 who is bringing up the document and
 20 referring to it. It's an IBC document. It
 21 would be so difficult to provide that
 22 document in advance, if he's going to
 23 question the witness about it.
 24 STAMP, Q.C.:
 25 Q. Madam Chair, I didn't hear the comment until

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1 I heard Mr. Lazar speak. I didn't come
 2 with, you know, all the GISA and FSCO and
 3 IBC documentation in my back pocket. I
 4 can't do that. I listened to Mr. Lazar
 5 explain what he thought was the investment,
 6 I don't know, agenda or style for P&C
 7 insurers and said that a significant part
 8 and I think he went on to say, I don't know
 9 if he said 40 percent. I'm sorry, Mr.
 10 Lazar, I can't remember what you said there,
 11 significant part, 40 percent maybe I think
 12 he said and according to the IBC and
 13 information I've just been passed, it's more
 14 like 11.1 or 2 or whatever I said that
 15 percent I said was.
 16 CHAIR:
 17 Q. Yes, yes –
 18 STAMP, Q.C.:
 19 Q. So, I can't come—my friend is critical of me
 20 not coming with information. I can't come
 21 with that information. I can only try to
 22 deal with it as it arises.
 23 CHAIR:
 24 Q. I agree, Mr. Stamp. When information arises
 25 in the course of cross-examination I

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1 appreciate that information is not in the
 2 report. It would be helpful to the Board
 3 though if you're referring to something
 4 that's different than what Mr. Lazar would
 5 have said to put it on the record.
 6 STAMP, Q.C.:
 7 Q. Madam Chair, yes, what I can do is I can
 8 tell you, if you can just—I can ask what
 9 that document actually is so Mr. Lazar can
 10 then refer to it if he wishes or –
 11 CHAIR:
 12 Q. Well, it's going to be difficult for him to
 13 refer to it now, so.
 14 STAMP, Q.C.:
 15 Q. Yes, I know. It is a –
 16 CHAIR:
 17 Q. Can you just make a copy of the –
 18 STAMP, Q.C.:
 19 Q. Well, I can send—maybe I could just send
 20 that information to maybe Ms. Glynn or
 21 somebody and it could get printed or
 22 something. Is that possible? Can you send
 23 that to—one page? Does that explain where
 24 it came from? We'll do our best, Madam
 25 Chair to –

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1 CHAIR:
 2 Q. Yes, well, it would have to put on the
 3 record for us to be able to take note of it
 4 in any event.
 5 STAMP, Q.C.:
 6 Q. That's fine, sure. We'll let that unfold
 7 and I'll come on to –
 8 DR. LAZAR:
 9 A. Can I just ask one thing and then you can
 10 comment? The 11 percent, that's for all P&C
 11 companies in Canada?
 12 STAMP, Q.C.:
 13 Q. I gather so.
 14 DR. LAZAR:
 15 A. And what time period?
 16 STAMP, Q.C.:
 17 Q. At the end of December 2017, but I don't
 18 know any –
 19 DR. LAZAR:
 20 A. Okay, but it could vary from year to year?
 21 STAMP, Q.C.:
 22 Q. Oh, I'm sure it would.
 23 DR. LAZAR:
 24 A. And secondly, you don't know what that
 25 number is for the auto insurance companies

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1 that operate only in Newfoundland and
 2 Labrador.
 3 STAMP, Q.C.:
 4 Q. I don't think so.
 5 DR. LAZAR:
 6 A. Could be plus or minus for that. You don't
 7 have those data? Okay, so my, sort of,
 8 question, my comment then, if you look at my
 9 Table 14 in my report, where I compare the
 10 S&P TSX Annual Return and Net Investment
 11 Return on Equity for the Auto Insurance
 12 Companies in Labrador and Newfoundland,
 13 assuming it's 89 percent in bonds, 11
 14 percent in equities. Now, of course the 89
 15 percent, it could be another asset
 16 (phonetic) classes. You know, Eli and I can
 17 sort of do quick calculations what the
 18 returns on a bond portfolio would be and at
 19 89 percent, 11 percent split, you're not
 20 going to get numbers anywhere near this.
 21 The returns on a bond portfolio were simply
 22 too low given that 89 percent weight to
 23 generate these types of returns. So, that's
 24 why when I said "significant", I'm looking
 25 at these numbers. I know what happened to

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1 interest rates over this period of time, so
 2 there was no much capital appreciation. The
 3 yields on them are quite low and, you know,
 4 applying 89 percent to that 11 percent to
 5 the rest, you're going to get investment
 6 returns on equity that are significantly
 7 lower than these reported numbers. So,
 8 those numbers might be interesting, I would
 9 question them, and in particular how
 10 appropriate are they for the auto insurance
 11 companies operating in this province?
 12 STAMP, Q.C.:
 13 Q. So, on that point, Mr. Lazar, where did you
 14 get 12.12, is that your number?
 15 DR. LAZAR:
 16 A. No, that's from the GISA numbers.
 17 STAMP, Q.C.:
 18 Q. That's a GISA number?
 19 DR. LAZAR:
 20 A. Sorry, should be a GISA number, I believe.
 21 STAMP, Q.C.:
 22 Q. Can you tell me where in GISA we'll find
 23 that, please?
 24 DR. LAZAR:
 25 A. Okay, going back—sorry, this is not GISA,

Page 113	Page 115
<p>1 it's from the individual insurance 2 companies, from the MSA research base. 3 STAMP, Q.C.: 4 Q. So, this is MSA information you're saying? 5 DR. LAZAR: 6 A. Yes. 7 STAMP, Q.C.: 8 Q. Okay. So, they've done some kind of a 9 calculation to break down Newfoundland – 10 DR. LAZAR: 11 A. No, they've just reported, here's the net 12 income from investment, here's the equity 13 and we've allocated it to these companies. 14 They didn't so these calculations. We used 15 their numbers, simply a matter of taking a 16 ratio between two numbers to produce these 17 numbers. 18 STAMP, Q.C.: 19 Q. I'm going to ask if we can bring up the 20 source of the information that I was 21 referring to. Do you see that, Mr. Lazar, 22 it's on the screen now? 23 DR. LAZAR: 24 A. Yes. 25 STAMP, Q.C.:</p>	<p>1 Q. No. 2 DR. LAZAR: 3 A. What's called "other," that 16 percent? 4 STAMP, Q.C.: 5 Q. I don't know. I don't know the answer. 6 DR. LAZAR: 7 A. Okay. 8 STAMP, Q.C.: 9 Q. Okay, in any event, apparently, it's 10 something other than shares. 11 DR. LAZAR: 12 A. Um-hm. It could be investment in, you know, 13 other companies that are essentially 14 investing shares. I—again – 15 STAMP, Q.C.: 16 Q. Okay. 17 DR. LAZAR: 18 A. If I add the two together, 27 percent, it's 19 still not, at least for these companies 20 operating in Newfoundland and Labrador, the 21 splits are going to be different, and 22 remember, we weren't using 2017 data, so 23 what were the data for 2011 to 2016? 24 STAMP, Q.C.: 25 Q. Okay. Mr. Lazar, I'm going to come back now</p>
<p>Page 114</p> <p>1 Q. So this is, I take it, Canada wide, P&C? 2 DR. LAZAR: 3 A. Um-hm. 4 STAMP, Q.C.: 5 Q. I'm assuming—can we just go to the top 6 again, please? Yes, okay, so that's the 7 discussion. It's an IBC document. If you 8 can just go down to the bottom, you'll see 9 there, it's investments and I guess, it's 10 millions of dollars I guess it is, as of 11 December 31, 2017 and at the bottom of that, 12 it's hard to make it out, but it looks like 13 "as of 2016 Q4 Investments reported through 14 OSFI regulatory returns exclude pool funds 15 accounted using equity method, source IBC, 16 MSA, SCOR AMF and you'll see shares are 17 shown both as a dollar amount and as a 18 percentage. 19 DR. LAZAR: 20 A. What's the other category? 21 STAMP, Q.C.: 22 Q. Well, it looks like mortgages. 23 DR. LAZAR: 24 A. No, no, no, the - 25 STAMP, Q.C.:</p>	<p>Page 116</p> <p>1 if I can to the early part of your report. 2 Get myself organized. At page 5 of your 3 report, please. 4 DR. LAZAR: 5 A. Yeah. 6 STAMP, Q.C.: 7 Q. And you get into a discussion here about the 8 exclusion or inclusion of various companies? 9 DR. LAZAR: 10 A. Yes. 11 STAMP, Q.C.: 12 Q. And then, we go to page, I think it's 24. 13 So, you list 15 companies right there on 14 that chart at page 24? It's table 13. 15 DR. LAZAR: 16 A. I believe so. 17 STAMP, Q.C.: 18 Q. I just did a quick count. 19 DR. LAZAR: 20 A. It sounds right. 21 STAMP, Q.C.: 22 Q. And I'm just going to go a little further 23 over. I think there was a further 24 discussion on this point a little further 25 along. Yes, at page 32, Mr. Lazar.</p>

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1 DR. LAZAR:
 2 A. Um-hm.
 3 STAMP, Q.C.:
 4 Q. I think this is the same 15 companies, but
 5 you mention two others. Is that Tokio
 6 Marine or Tokyo Marine? How do you say
 7 that, do you know?
 8 DR. LAZAR:
 9 A. I would assume –
 10 STAMP, Q.C.:
 11 Q. Anyway, Tokio Marine.
 12 DR. LAZAR:
 13 A. Yes.
 14 STAMP, Q.C.:
 15 Q. And Zurich are two mentioned companies. Do
 16 you see that in the paragraph below the
 17 list?
 18 DR. LAZAR:
 19 A. Yeah.
 20 STAMP, Q.C.:
 21 Q. Yes. And what you said was, “We excluded
 22 both.”
 23 DR. LAZAR:
 24 A. Yes.
 25 STAMP, Q.C.:

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1 Q. And if I’m saying it right, “Tokio Marine
 2 was a marginal player at best in the
 3 industry in the province with an average of
 4 \$8,833 in written premiums during the period
 5 2011 to 2016.”
 6 DR. LAZAR:
 7 A. Correct.
 8 STAMP, Q.C.:
 9 Q. That’s why it was excluded?
 10 DR. LAZAR:
 11 A. We excluded them in order to calculate the
 12 beta, so that would could calculate the
 13 return in equity.
 14 STAMP, Q.C.:
 15 Q. But what you say is that it appeared to me a
 16 marginal player?
 17 DR. LAZAR:
 18 A. Yes.
 19 STAMP, Q.C.:
 20 Q. With what I take it you mean to be a small
 21 average written premium?
 22 DR. LAZAR:
 23 A. That’s right.
 24 STAMP, Q.C.:
 25 Q. Is that right?

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1 DR. LAZAR:
 2 A. Yes.
 3 STAMP, Q.C.:
 4 Q. And by “average written premium,” does that
 5 mean ‘11 through ‘16, six years, six times,
 6 you know, eighty-eight—six times nine,
 7 \$54,000 or so is what we’re talking about?
 8 DR. LAZAR:
 9 A. Yes.
 10 STAMP, Q.C.:
 11 Q. That’s why they are a small and marginal
 12 player?
 13 DR. LAZAR:
 14 A. Yes.
 15 STAMP, Q.C.:
 16 Q. And you excluded Zurich because they only
 17 operated in ‘11, ‘15 and ‘16?
 18 DR. LAZAR:
 19 A. According to the data we were given, yes.
 20 STAMP, Q.C.:
 21 Q. And this is MSA data in both cases?
 22 DR. LAZAR:
 23 A. Yes.
 24 STAMP, Q.C.:
 25 Q. Okay. So, what would be—I mean, where Tokio

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1 was excluded because, you know, \$8,833 on
 2 average in 2011 through 2016, but what would
 3 be the cut-off? If they had been \$20,000,
 4 would they have stayed?
 5 DR. LAZAR:
 6 A. That would be 20,000. Looking at what—200-
 7 plus million. Probably the cut-off would
 8 have been, figure it out, on tenth of one
 9 percent would have been reasonable.
 10 STAMP, Q.C.:
 11 Q. Well, how does that translate into a number,
 12 you know, per month or something or –
 13 DR. LAZAR:
 14 A. Roughly 200,000.
 15 STAMP, Q.C.:
 16 Q. Two hundred thousand.
 17 DR. LAZAR:
 18 A. Again –
 19 STAMP, Q.C.:
 20 Q. So, 8,000 is way too low for you. Two
 21 hundred thousand would have been –
 22 DR. LAZAR:
 23 A. Yeah, again, if you throw that in, that
 24 wouldn’t have affected our estimate of the
 25 beta.

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1 STAMP, Q.C.:

2 Q. Okay.

3 DR. LAZAR:

4 A. In the case of Zurich, if you were throwing

5 that in, that would have affected it because

6 it was in and out, and you want consistency,

7 you wanted companies that were in this

8 industry throughout this period.

9 STAMP, Q.C.:

10 Q. Okay, okay. So, on that note, I want to

11 bring up the material from the

12 superintendent who was the regular, one of

13 the regulators in Newfoundland, the

14 Superintendent of Insurance. He publishes a

15 report showing insurance premiums and claims

16 and so on. And if we turn to that, that's

17 been—I think it's on the system now. We've

18 provided the table 1 chart from the

19 Superintendent's Report from 2011 through

20 2016. Okay? So, if we can bring up 2011,

21 please. And with '11 I'll turn first to ACE

22 INA Insurance. That's the first one on the

23 second page, the first company. This is a

24 published document by the Public Utilities—

25 by, I'm, sorry, by the Superintendent of

Page 122

1 Insurance. This one is published for 2011,

2 and if you turn to the last page, just to

3 have the—we have that last page just to show

4 you how it's—how they're focusing on it,

5 there's some totals on that last page which

6 is page 14 of this document at the bottom of

7 the page. So, you'll see that in—under the

8 columns for automobile insurance they have a

9 number of categories, but total earned

10 premiums is the middle line. And you'll see

11 the total earned premiums in, I guess, in

12 thousands of dollars. So, the total earned

13 premium for liability, 245 million, plus;

14 for personal accident, 29 million; for

15 other, 106 million. Okay? So, that's what

16 they—that how they do it, and then you go

17 back to the front, to the second page of the

18 exhibit, you'll see that they, for each

19 company, they provide a similar breakdown,

20 and in the second row in each case it's the

21 total earned premium, and in the third row

22 it's total direct claims. That's what the

23 Superintendent reports. So, here we have

24 ACE INA Insurance. They weren't included in

25 your study, were they?

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1 DR. LAZAR:

2 A. No, we didn't get data on that company.

3 STAMP, Q.C.:

4 Q. Okay. I can tell you that if we looked at

5 all the charts, my understanding that they

6 provided insurance coverage or wrote premium

7 2011 through 2015, but not in '16, and the

8 total premium was about 1.7 million dollars,

9 would that be a number that should have been

10 included in some fashion in your analysis?

11 (12:00 p.m.)

12 DR. LAZAR:

13 A. You said they weren't in there in 2016?

14 STAMP, Q.C.:

15 Q. They were not there in '16.

16 DR. LAZAR:

17 A. Well, we would have excluded them because we

18 would not have consistency.

19 STAMP, Q.C.:

20 Q. Okay.

21 DR. LAZAR:

22 A. Remember the purpose of the companies are

23 included here were for estimating for

24 incorporating them into the capital asset

25 pricing model to estimate a measure of the

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1 risk profile.

2 STAMP, Q.C.:

3 Q. Let me jump down, Mr. Lazar, to the next

4 page, the top of the next page, Atlantic

5 Insurance. Do you see that entry?

6 DR. LAZAR:

7 A. Um-hm.

8 STAMP, Q.C.:

9 Q. I can tell you that in this year, they have

10 of course as you can see, 2.9 million and 98

11 thousand and then 994 million in coverages,

12 but I've taken the trouble of going through

13 the—all of these reports from '11 through

14 '16. And Atlantic Insurance premium in 2011

15 was 3.9 million; 3.6 plus in 2012; 3.4

16 million plus in 2013; just shy of 3.5

17 million in 2014; just over 3 million in

18 2015; and 2.4 million in 2016. An

19 approximate total of 20 million dollars in

20 earned premium in the six-year period. Why

21 would they be excluded?

22 DR. LAZAR:

23 A. Again, if they're not on our list, the only

24 three we excluded were those three that we

25 mentioned. If we didn't get data for them,

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1 then we did not incorporate them into our
 2 analysis.
 3 STAMP, Q.C.:
 4 Q. Did you ask, or did you look, at the
 5 Superintendent's Reports to see what other
 6 data would be available?
 7 DR. LAZAR:
 8 A. No, we went strictly to MSA.
 9 STAMP, Q.C.:
 10 Q. So, if MSA didn't have Atlantic and you're—
 11 and you say they don't —
 12 DR. LAZAR:
 13 A. Right.
 14 STAMP, Q.C.:
 15 Q. - they missed 20 million dollars worth of
 16 premium from an insurer who wrote every year
 17 from '11 through '16?
 18 DR. LAZAR:
 19 A. Okay. Now, let me explain the relevance of
 20 this, if any. If we had this complete set,
 21 and we had an expanded data set, would that
 22 have produced a different estimate for beta
 23 and the risk profile? Maybe. Would the
 24 beta have been higher or lower? Don't know.
 25 Could have been lower which would have meant

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1 the return equity according to the capital
 2 asset pricing model should have been lower.
 3 Could the beta have been higher? Possibly,
 4 which would have biased it upwards. What's
 5 the degree of sort of adjustment in the beta
 6 as a result of having a more complete set?
 7 We don't know. I'm willing to bet that it's
 8 not going to change that much. You know,
 9 our estimate of return on equity might be a
 10 little higher. Now, with regards to the
 11 loss estimates and that's probably what
 12 you're getting to, let me make this clear,
 13 was there overpayment in every year of
 14 premiums? The answer to that is
 15 unequivocally yes, regardless of the actual
 16 performance of the insurance companies.
 17 Now, how can I say this with certainty?
 18 Because the assumptions that were used in
 19 setting the premiums used a return in equity
 20 that too high, used a return in investment
 21 that was too low, and did not look at best
 22 practices with regards to expenses. So —
 23 STAMP, Q.C.:
 24 Q. So, even in the —
 25 DR. LAZAR:

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1 A. No, no, no, please. Please.
 2 STAMP, Q.C.:
 3 Q. Just go ahead.
 4 DR. LAZAR:
 5 A. You know, I think it's important to
 6 understand this. So, here are the premiums
 7 that were set. The premiums that were
 8 charged could have been lower for various
 9 reasons, competitive reasons or whatever.
 10 The actual performance of the insurance
 11 companies would have been—could have been
 12 different from what was anticipated and
 13 could have been different from that ten
 14 percent because the claims experience was
 15 different, their operating expenses
 16 experience were different. Okay? But here
 17 are the premiums that were set. Our
 18 argument based solely on what would have
 19 been appropriate return on equity suggests
 20 even if you use the ROI assumptions, even if
 21 you use the expense assumptions, because the
 22 ROE should have been lower, the permitted
 23 premiums would have been lower. So, you're
 24 going to get that gap year in, year out,
 25 which means you have overpayment of

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1 premiums. Adjusting for the ROE for the
 2 return on investment and expenses expands
 3 that. Now, what happens when insurance
 4 companies lose money? It should matter to
 5 the regulator. There are assumptions made
 6 the beginning. You set the premiums. The
 7 experience is going to vary. Some years the
 8 industry will actually do better than at
 9 regulated return in equity if they got
 10 lucky. Some years they're going to do
 11 worse. They got unlucky for the industry as
 12 a whole. Within the industry in a given
 13 year, some companies do better, some do
 14 worse. So, if you're doing the analysis
 15 correctly, the actual after-the-fact return
 16 on equities from estimating the overpayments
 17 almost becomes irrelevant. What matters is
 18 what were the assumptions used in setting
 19 the premiums. What happens during the year
 20 and the final performance becomes
 21 irrelevant. So if we included a larger
 22 sample of companies, it affects the data, it
 23 would affect our estimate of the return on
 24 equity. Would it push that return on equity
 25 up to 10 percent; no way, wouldn't even come

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1 close. With regards to overpayments, even
 2 in the years when the insurance companies
 3 lost money, the answer to that is there were
 4 overpayments, period, because you used
 5 different assumptions for setting the
 6 premiums than what should have been used,
 7 plain and simple. So you can look at this
 8 data, you can say we did include these, you
 9 should have included these, what about those
 10 negative years, the reality is using logic,
 11 using common sense, using different sets of
 12 assumptions that were more appropriate,
 13 they're overpayments.
 14 STAMP, Q.C.:
 15 Q. We're going to come back to all that, Mr.
 16 Lazar. All of that we'll come back to, but
 17 the first piece –
 18 DR. LAZAR:
 19 A. Yeah, but it's –
 20 KENNEDY, Q.C.:
 21 Q. Is he finished? The witness has to be
 22 allowed to finish his answer.
 23 DR. LAZAR:
 24 A. But again we can go through these tables,
 25 you can go company to company, why didn't

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1 you include it, we didn't have it. You have
 2 to understand what difference would this
 3 have made, and I'm saying the only place it
 4 comes in, it comes in two places; one, how
 5 does it impact the return on equity, and in
 6 my view, without looking at the companies we
 7 missed, without including them, their
 8 impacts, I'm willing to bet, would have been
 9 marginal. The worst case scenario, it would
 10 have increased what would have been
 11 appropriate after tax return on equity, 25,
 12 50, 75 basis points. Averaged over that
 13 period, you go from 6 to maybe 6.75 percent
 14 maybe. Just as likely it could have reduced
 15 it. So that's the worst case scenario for
 16 estimating overpayments, but in terms of
 17 overpayments, premiums too high, I say
 18 unequivocally that was the case in every
 19 year regardless of what data you show me,
 20 regardless of what happens if you include
 21 those negative years. If you're going to
 22 tell me that we've got to guarantee the
 23 insurance companies generate this return on
 24 equity each and every year, then the risk is
 25 being shifted onto consumers and the return

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1 on equity, therefore, should be equal to the
 2 risk free rate, 2.5 percent. So if you want
 3 to spend more time going through this,
 4 that's fine. I no longer see the relevance
 5 of it, but you've got the floor, you can
 6 pursue it.
 7 STAMP, Q.C.:
 8 Q. Sovereign Insurance is not on your list, as
 9 I see it. It wrote insurance every year
 10 just under 20 million dollars, 2.6, 3.6,
 11 2.8, 3.2 or 3.3, 3.2, 3.9. They're not
 12 included.
 13 DR. LAZAR:
 14 A. Okay, but again we can go through it company
 15 by company. I'm not denying any of this.
 16 STAMP, Q.C.:
 17 Q. Okay.
 18 DR. LAZAR:
 19 A. All I'm asking is, what's the relevance of
 20 it?
 21 STAMP, Q.C.:
 22 Q. Right.
 23 DR. LAZAR:
 24 A. And I've answered what the relevance of it
 25 is.

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1 STAMP, Q.C.:
 2 Q. Well, you excluded Zurich, according to your
 3 note, because it didn't write –
 4 DR. LAZAR:
 5 A. Because we had data available on Zurich.
 6 STAMP, Q.C.:
 7 Q. You excluded it?
 8 DR. LAZAR:
 9 A. Because we had data available. These
 10 companies you're pointing out, they're not
 11 on a list, we didn't have the data available
 12 on them.
 13 STAMP, Q.C.:
 14 Q. The data is right here in the
 15 Superintendent's Report published every year
 16 for Newfoundland.
 17 MR. FELTHAM:
 18 Q. Madam Chair, this has been asked now a
 19 number of times. Mr. Lazar has given his
 20 answer. He's indicating, "I've given you my
 21 answer, it's the same answer, you can refer
 22 to each company and go through line by line,
 23 that's my answer". He shouldn't keep – it's
 24 now quarter after 12. How much time are we
 25 going to spend going over and over the same

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1 thing.
 2 STAMP, Q.C.:
 3 Q. Until, I guess, I get my questions answered.
 4 MR. FELTHAM:
 5 Q. The problem is Mr. Stamp doesn't like the
 6 answer that he's getting.
 7 A. But, you know –
 8 O'FLAHERTY, Q.C.:
 9 Q. Excuse me, Dr. Lazar, as hearing counsel, I
 10 just make the observation, Madam Chair, that
 11 Mr. Stamp is entitled to ask what dataset is
 12 relied upon in a presenter's report. Do I
 13 simply turn it back and say, you know, maybe
 14 the fastest way forward is to let Mr. Stamp
 15 ask his questions and then we can take that
 16 information which way it goes. Constantly
 17 interrupting, as I've said earlier, for the
 18 sake of good order in the transcript, it's
 19 not that helpful. So I think in the context
 20 that we're in, Mr. Stamp is simply asking
 21 about data.
 22 DR. LAZAR:
 23 A. If I can say something, I have no problem –
 24 O'FLAHERTY, Q.C.:
 25 Q. Excuse me, Dr. Lazar, just –

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1 CHAIR:
 2 Q. Excuse me, Mr. Lazar, you can respond to
 3 questions from the –
 4 DR. LAZAR:
 5 A. Okay, sorry. Thank you.
 6 CHAIR:
 7 Q. Mr. Stamp, I understand the tenure of your
 8 questions. Are you going to ask the same
 9 question with respect to each of the
 10 companies or is it a general –
 11 STAMP, Q.C.:
 12 Q. I won't do that. We'll capture this, Madam
 13 Chair, I guess, in other materials later on,
 14 but Zurich was specifically excluded we were
 15 told because they only wrote three years.
 16 Is that right, Mr. Lazar?
 17 DR. LAZAR:
 18 A. I can repeat this only one way. We were
 19 given a certain dataset. The companies
 20 you're pointing out were not on that
 21 dataset. With the OSFI data, I suspect all
 22 the detailed other information may or may
 23 not be available. Why MSA did not include
 24 these, go contact MSA. From our
 25 perspective, and as I said, all that

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1 matters, if you want us to include to
 2 broaden this, great, give us the detailed
 3 information, we'll be able – we'll do it on
 4 our time, our expense, to see how it affects
 5 that measure of data, and I suspect it's
 6 going to have a trivial effect on that
 7 estimate of data, and hence on the estimate
 8 of the return on equity, okay.
 9 STAMP, Q.C.:
 10 Q. But, Mr. Lazar –
 11 DR. LAZAR:
 12 A. Now if you want us to do the complete
 13 thorough analysis, and go to the regulatory
 14 data, if you also have the ex anti-claims
 15 numbers, we can run this through. I've done
 16 some simple calculations that suggest the
 17 overpayment on the premiums probably run 8
 18 to 10 percent per year, year in, year out,
 19 regardless of the performance, and I base
 20 this on looking at what the multiple of the
 21 claims should be based on different
 22 assumptions with regards to expense ratio,
 23 the ROE, and the return on investment.
 24 Simple calculations. I can just run through
 25 a few of these and it gives me a number of 8

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1 to 10 percent in premium overpayments year
 2 in, year out. If you want, I'll expand the
 3 dataset, I'm going to expand the premium
 4 number and the overpayments. It's quite
 5 simple. So you want to ask me other
 6 companies that are not on the list, and why
 7 they're not in a list, the answer is the
 8 same, they weren't in the dataset that MSA
 9 sent us. Is it relevant for analysis; yes.
 10 Is it going to significant alter analysis;
 11 I'm willing to say probably not. Does it
 12 affect our conclusions with regards to
 13 overpayments on the premiums? Absolutely
 14 not.
 15 STAMP, Q.C.:
 16 Q. Are you done? Zurich, you report only wrote
 17 a premium or collected premium in '11, '15,
 18 and '16, and yet the Superintendent's Report
 19 shows that they were also here for '12, '13,
 20 and '14. About the same numbers through the
 21 whole piece in those years as well.
 22 DR. LAZAR:
 23 A. That's not what the data that we were given
 24 said.
 25 (12:15 p.m.)

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1 STAMP, Q.C.:

2 Q. Right. So what I'm back to is you had said

3 earlier that you didn't have available the

4 permitted premiums in Newfoundland, which

5 are all published through this Public

6 Utilities Board, you didn't have the data on

7 who wrote insurance, and you just had to go

8 to the Superintendent's information and

9 you'd have every insurance company for every

10 year in the period you're interested in,

11 2011 through 2016. Every single company is

12 here, and you relied on 17 insurers, I

13 guess, that you were provided with data from

14 MSA or MSI, whatever they're called, and you

15 excluded a bunch of those. Is that right?

16 DR. LAZAR:

17 A. Yes.

18 STAMP, Q.C.:

19 Q. Okay, because there's, I don't know, 30 or

20 40 insurers here. Your report at page 12,

21 Mr. Lazar, this is when you're speaking

22 about the ROI, you identify the ROI produced

23 by Oliver Wyman. That's out of their

24 report, is it not, that table?

25 DR. LAZAR:

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1 A. Yes.

2 STAMP, Q.C.:

3 Q. At Table 6?

4 DR. LAZAR:

5 A. Yes.

6 STAMP, Q.C.:

7 Q. And at Table 7, you produce a table that

8 some of it is GISA data, and some of your

9 own calculations, I believe. Is that

10 correct?

11 DR. LAZAR:

12 A. These should all be derived from the GISA

13 data, yes. Some of these ratios.

14 STAMP, Q.C.:

15 Q. Well, let me just make sure I'm clear, first

16 of all, just a couple of point. If you can

17 pop ahead to page 14, and Item 4. I want to

18 make sure we speak the same language. You

19 say in Item 4, "The returns on equity, or

20 ROI, keeping in mind the preceding

21 observations, were in excess of 10 percent".

22 Are you saying both, or is ROE and ROI the

23 same thing?

24 DR. LAZAR:

25 A. No, they're different.

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1 STAMP, Q.C.:

2 Q. Are you referring to both here or just one?

3 DR. LAZAR:

4 A. I'm just referring to one.

5 STAMP, Q.C.:

6 Q. Which one are you referring to?

7 DR. LAZAR:

8 A. The return on their investment portfolio.

9 STAMP, Q.C.:

10 Q. So you're not referring to equity here?

11 DR. LAZAR:

12 A. No.

13 STAMP, Q.C.:

14 Q. Returns on equity is not being referred to?

15 DR. LAZAR:

16 A. No.

17 STAMP, Q.C.:

18 Q. You say that it is, but it's not, I take it?

19 DR. LAZAR:

20 A. Not in that point.

21 STAMP, Q.C.:

22 Q. Okay, and at page 30, if you can just turn

23 to that page, there's a series of bullets

24 there, and again I'm trying to understand

25 what terminology you use, or what you

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1 understand to be the discussion, in the

2 fifth bullet it says, "Expected investment

3 income return on equity". Is that the same

4 thing?

5 DR. LAZAR:

6 A. No, it's the investment, return investment,

7 the denominator we equated with equity, and

8 again if you go to the preceding table,

9 that's how the numbers are calculated, and

10 here investment return on equity, it's not

11 the return on equity, the net profit of the

12 company divided by their equity, but rather

13 their net investment income divided by their

14 investment portfolio, which we equated with

15 equity. This is not the return on equity,

16 it's the return on their investment.

17 STAMP, Q.C.:

18 Q. So, is bullet 15 (sic) properly explained or

19 properly described?

20 DR. LAZAR:

21 A. Bullet? Well, we thought it was properly

22 described, but obviously it was

23 misinterpreted. We said, "Return on

24 equity". We just stated explicitly the

25 "return on equity".

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<p>1 STAMP, Q.C.:</p> <p>2 Q. Okay, all right, just come back to Table 7</p> <p>3 at page 13, please.</p> <p>4 DR. LAZAR:</p> <p>5 A. Which table?</p> <p>6 STAMP, Q.C.:</p> <p>7 Q. Seven.</p> <p>8 DR. LAZAR:</p> <p>9 A. Seven.</p> <p>10 STAMP, Q.C.:</p> <p>11 Q. And three parts of the way down that table,</p> <p>12 there's a net investment income?</p> <p>13 DR. LAZAR:</p> <p>14 A. Yeah.</p> <p>15 STAMP, Q.C.:</p> <p>16 Q. And below that an allocated equity, and then</p> <p>17 you divide the two?</p> <p>18 DR. LAZAR:</p> <p>19 A. Yes.</p> <p>20 STAMP, Q.C.:</p> <p>21 Q. And that gives you 15.08 in '12, 10.9 in</p> <p>22 '13, and so on, up to 6.4 in '16. Is that</p> <p>23 right?</p> <p>24 DR. LAZAR:</p> <p>25 A. Yes.</p>	<p>1 divide that by the equity. That's the</p> <p>2 return on equity. So the return, what we</p> <p>3 call return on investment – a line that</p> <p>4 comes farther up in that table, that's just</p> <p>5 one component of their overall</p> <p>6 profitability.</p> <p>7 STAMP, Q.C.:</p> <p>8 Q. But I'm looking at this line, investment</p> <p>9 income over equity. Now, am I looking at a</p> <p>10 return on investment?</p> <p>11 DR. LAZAR:</p> <p>12 A. Return on investment.</p> <p>13 STAMP, Q.C.:</p> <p>14 Q. I take it -- and this pops up at your Table</p> <p>15 9 as well -- the same numbers show up in</p> <p>16 Table 9?</p> <p>17 DR. LAZAR:</p> <p>18 A. Yes.</p> <p>19 STAMP, Q.C.:</p> <p>20 Q. So, if I take \$1,000 and invest it and earn</p> <p>21 \$100, I do a calculation that says what my</p> <p>22 return on my investment was.</p> <p>23 DR. LAZAR:</p> <p>24 A. Ten percent.</p> <p>25 STAMP, Q.C.:</p>
<p>Page 142</p> <p>1 STAMP, Q.C.:</p> <p>2 Q. And you identify that as return on equity,</p> <p>3 do you not?</p> <p>4 DR. LAZAR:</p> <p>5 A. No, that's return on investment.</p> <p>6 STAMP, Q.C.:</p> <p>7 Q. It's return on investment?</p> <p>8 DR. LAZAR:</p> <p>9 A. Okay, there are two parts here, and they</p> <p>10 both involve equity, so assuming the equity</p> <p>11 that companies commit a certain amount of</p> <p>12 cash, that's equivalent to the reserves that</p> <p>13 are available to invest. So we assume that</p> <p>14 the two are the same. So that pool is</p> <p>15 available and invested in a group of</p> <p>16 financial assets. What we're measuring here</p> <p>17 is what's the return on that investment</p> <p>18 pool, and that will then filter into</p> <p>19 determining the overall profitability of the</p> <p>20 companies. Then you look at – the last line</p> <p>21 there, and the insurance companies, they</p> <p>22 make underwriting profits or losses, they</p> <p>23 make money on all their investments. Add</p> <p>24 the two together, that gives you your</p> <p>25 overall profitability. Profit or loss, you</p>	<p>Page 144</p> <p>1 Q. If I happen to own a house, I don't throw</p> <p>2 that into the discussion to see what my</p> <p>3 return on my investment was. I just take</p> <p>4 the \$1,000 I invested and the income I made</p> <p>5 on that \$1,000, don't I?</p> <p>6 DR. LAZAR:</p> <p>7 A. See that's – if you do that, that's because</p> <p>8 you didn't take a finance course. Because</p> <p>9 finance makes it quite clear, you have to</p> <p>10 look at all your assets, not just pure</p> <p>11 financial assets.</p> <p>12 STAMP, Q.C.:</p> <p>13 Q. Um-hm.</p> <p>14 DR. LAZAR:</p> <p>15 A. For most people, the house is the biggest</p> <p>16 asset.</p> <p>17 STAMP, Q.C.:</p> <p>18 Q. Right.</p> <p>19 DR. LAZAR:</p> <p>20 A. So you throw that into the base and you look</p> <p>21 at what is – so, your capital appreciation.</p> <p>22 I mean there's capital losses on that less</p> <p>23 whatever sort of maintenance expenditures</p> <p>24 you incur.</p> <p>25 STAMP, Q.C.:</p>

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1 Q. But I understood you to say that the return
 2 on equity, ten percent which is the
 3 benchmark, is too high and one of the
 4 reasons it's too high you said, I thought,
 5 was that rates of return on investments,
 6 ROI, was given at a certain amount but it
 7 was actually, in your view, higher than the
 8 insurers said it was. And therefore -
 9 DR. LAZAR:
 10 A. No. Those two are unrelated. The return on
 11 equity that we estimated that would be
 12 appropriate was derived from - okay, what's
 13 the risk profile of this industry? So, you
 14 look at any type of asset class, any type of
 15 company, and you've got here's the risk-free
 16 return. How much more should that asset
 17 generate on average? How much more should
 18 that company earn on average on its equity
 19 investment in that company? And that
 20 depends on the risk profile. The risk
 21 profile is derived from applying the capital
 22 asset pricing model. So, that's what we did
 23 and that generated a return on equity.
 24 Now, we then looked at the actual
 25

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1 returns on equity and they're going to be
 2 influenced in part by the returns the
 3 companies generate on their investments in
 4 their investment portfolio. And again, if
 5 you look at the GISA data and the returns on
 6 investment, at those levels that just
 7 reinforced the point I made earlier that
 8 there's no way you can generate those
 9 returns by investing two-thirds of your
 10 portfolio in bonds during that period of
 11 time.
 12 STAMP, Q.C.:
 13 Q. Well, that's a very long answer.
 14 DR. LAZAR:
 15 A. Yes.
 16 STAMP, Q.C.:
 17 Q. But it did say somewhere in that answer that
 18 return on equity was in part derived out of
 19 ROI.
 20 DR. LAZAR:
 21 A. I didn't say that.
 22 STAMP, Q.C.:
 23 Q. I thought you did.
 24 DR. LAZAR:
 25 A. Well, no, I didn't.

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1 STAMP, Q.C.:
 2 Q. Okay. In any event, you're saying - what
 3 you're saying - let me just make sure we
 4 have this clear, is that return on
 5 investment, you don't take the amount you've
 6 earned on the investment and divide it by
 7 the amount of the investment to get the
 8 return on the investment, to get the rate of
 9 return? That's not how you do it? Is that
 10 right?
 11 DR. LAZAR:
 12 A. No, that's exactly how we did it.
 13 STAMP, Q.C.:
 14 Q. Oh, okay. Oh, that's how you did it?
 15 DR. LAZAR:
 16 A. Um-hm.
 17 STAMP, Q.C.:
 18 Q. That's how you did it?
 19 DR. LAZAR:
 20 A. Yes.
 21 STAMP, Q.C.:
 22 Q. Well, I had just said a few minutes ago I
 23 invest \$1,000, earn \$100 on it -
 24 DR. LAZAR:
 25 A. Right.

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1 STAMP, Q.C.:
 2 Q. - and that tells me what my rate of return
 3 was.
 4 DR. LAZAR:
 5 A. But you then said you had a home and you
 6 didn't include that.
 7 STAMP, Q.C.:
 8 Q. Didn't include that in calculating that
 9 investment.
 10 DR. LAZAR:
 11 A. Right. And that's what I said you're wrong.
 12 STAMP, Q.C.:
 13 Q. So, to have my return on my \$1,000
 14 investment calculated properly, I got to
 15 include the value of my home?
 16 DR. LAZAR:
 17 A. No. If you're looking at what's the return
 18 you've made on your -
 19 STAMP, Q.C.:
 20 Q. On what?
 21 DR. LAZAR:
 22 A. On your assets.
 23 STAMP, Q.C.:
 24 Q. Different thing though.
 25 DR. LAZAR:

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1 A. Your assets will consist of financial assets
 2 plus real estate. It could also consist of
 3 other assets, furniture, jewelry, whatever.
 4 So, when you look at what's the net wealth
 5 position of an individual, it takes into
 6 account all these holdings. That becomes
 7 the denominator and then the numerator
 8 becomes what are your capital gains, what
 9 are you dividends, interest payments you
 10 receive during that period of time.
 11 STAMP, Q.C.:
 12 Q. Well, Mr. Lazar, I'm still troubled by the
 13 confusion because at the bottom of page 15
 14 you talk about the implication of a higher
 15 ROI, which means you have to study – you
 16 have to examine the ROI in order to make
 17 certain conclusions that you have made and
 18 the ROI is different from the ROE, is it
 19 not?
 20 DR. LAZAR:
 21 A. Yes.
 22 STAMP, Q.C.:
 23 Q. So, you have to get the ROI as well. It's a
 24 component you got to get?
 25 DR. LAZAR:

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1 A. It's a component in the rate setting
 2 process.
 3 STAMP, Q.C.:
 4 Q. Right. And so, you pulled a rate of return
 5 by dividing investment income not by the
 6 amount of the investment but by the amount
 7 of equity.
 8 DR. LAZAR:
 9 A. Because we assumed that the two were
 10 equivalent.
 11 STAMP, Q.C.:
 12 Q. Okay. So, you assumed that every company's
 13 investment happens to coincide perfectly
 14 with every company's equity?
 15 DR. LAZAR:
 16 A. Only in this particular case, automobile
 17 insurance. With other companies – let me
 18 think – their investments – okay, so look at
 19 the case of the banks. Well, financial
 20 institutions, if you look at banks, their
 21 investment pool most likely exceeds the
 22 equity invested in the company. Most other
 23 companies, manufacturing companies, they're
 24 going to be sort of comparable. I'm trying
 25 to think of some of the technology

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1 companies, their investment pools likely are
 2 less than the total equity.
 3 STAMP, Q.C.:
 4 Q. Short answer for what you've told me, I
 5 think, is that you treat investment and
 6 therefore how to calculate the rate on that
 7 investment, the rate of return on it, you
 8 treat investment as equal to the company's
 9 equity?
 10 DR. LAZAR:
 11 A. Yes.
 12 STAMP, Q.C.:
 13 Q. Thank you.
 14 DR. LAZAR:
 15 A. For automobile insurance companies; and the
 16 sole reason we did that, that was the
 17 assumption used by FSCO in the rate setting
 18 process.
 19 STAMP, Q.C.:
 20 Q. I'm going to refer you, Mr. Lazar, to Ms.
 21 Elliott's evidence.
 22 DR. LAZAR:
 23 A. Sorry, to what?
 24 STAMP, Q.C.:
 25 Q. Ms. Elliott's evidence, Paula Elliott.

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1 DR. LAZAR:
 2 A. Okay.
 3 STAMP, Q.C.:
 4 Q. She was here with Oliver Wyman testifying.
 5 DR. LAZAR:
 6 A. Yeah.
 7 STAMP, Q.C.:
 8 Q. They're the Board's actuarial consultants.
 9 DR. LAZAR:
 10 A. Yes.
 11 STAMP, Q.C.:
 12 Q. And at page 85, 86, 87, 88, I guess that all
 13 shows up on one page for our technical
 14 assistant.
 15 CHAIR:
 16 Q. What date?
 17 MR. FELTHAM:
 18 Q. Madam Chair, I guess if we could -
 19 CHAIR:
 20 Q. Are you referring to the transcript?
 21 STAMP, Q.C.:
 22 Q. September the 6th, yes.
 23 DR. LAZAR:
 24 A. So, you're not referring to a report?
 25 (12:30 p.m.)

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1 CHAIR:
 2 Q. It'll be a transcript reference, Mr. Lazar.
 3 DR. LAZAR:
 4 A. Oh, okay.
 5 CHAIR:
 6 Q. It should show up there, yeah.
 7 STAMP, Q.C.:
 8 Q. We're discussing with Ms. Elliott this
 9 concept of ROI and at the very top of page
 10 86, my question is "and so, it's a division
 11 of course to get that number parity, but
 12 from 2012-2016, the authors of this report
 13 come up with investment income to equity.
 14 Is that ROI? Is that what they're thinking
 15 about?"
 16 Ms. Elliott's response is "No, this is
 17 not. ROI is return on your investments
 18 which is a ratio of your investment income
 19 divided by your invested assets. What's
 20 presented here in this row is the investment
 21 income divided by the equity and the equity
 22 does not equal the invested assets."
 23 So, you have it as a proxy. Ms.
 24 Elliott says it is not a proxy.
 25 DR. LAZAR:

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1 A. Okay. And did she provide any estimate or
 2 number of the invested assets?
 3 STAMP, Q.C.:
 4 Q. If we just turn to page 90, and at page 90,
 5 Ms. Elliott is speaking about this topic
 6 again, because I explained how your numbers
 7 were fundamentally different from hers and
 8 she said "Right. No, because a return on
 9 investment rate are your investment income
 10 including the realized capital gains and
 11 losses. That's included in the number that
 12 we present and it's taken as a ratio of the
 13 average at the beginning of the year and the
 14 end of the year of your investment assets
 15 that you have. So, all your investments,
 16 your bonds and your stocks and everything
 17 else, these are the actual return on
 18 investment rates that are reported in what's
 19 referred to as a P&C-1, a financial
 20 statement that is audited, and each company
 21 is required to file this annually with the
 22 regulatory OSFI. So, our numbers are
 23 different. What Lazar has presented is a
 24 ratio of the investment income as he has
 25 extracted it from GISA exhibit divided by

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1 equity and equity in invested assets are not
 2 the same." Investment assets are not the
 3 same thing I think she's saying.
 4 So, I asked does it make any sense the
 5 way you did it, and at the top of page 91,
 6 she says "no, because it's not an ROI". And
 7 of course, down at the bottom of page 91,
 8 she says and it would have been a flag. You
 9 see at the bottom, she says "and so, if you
 10 see this measurement as presented by Lazar,
 11 you know, double digit 15 percent, we know
 12 that would be a red flag because we know
 13 that government bonds that companies invest
 14 in are not 15 percent. So, it's different.
 15 Something else, it's not ROI."
 16 Now, Mr. Lazar, you were asked
 17 questions by the Public Utilities Board and
 18 we've gone through some of them and I think
 19 we'll have a look at -
 20 KENNEDY, Q.C.:
 21 Q. Excuse me, Madam Chair. Is there a question
 22 there? He just read from a transcript and
 23 said Ms. Elliott said this and now he's
 24 moving to another area. I mean, if you're
 25 going to do that, there has to be a

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1 question.
 2 STAMP, Q.C.:
 3 Q. I pointed out to Mr. Lazar that Ms. Elliott
 4 has taken a fundamentally different
 5 position; that she does not agree that
 6 investment and equity are the same thing.
 7 Mr. Lazar has said one is a proxy for the
 8 other and she disagrees. That's my point
 9 again.
 10 CHAIR:
 11 Q. To be fair, Mr. Lazar should be able to
 12 respond to it.
 13 STAMP, Q.C.:
 14 Q. Sure. He can respond to that if he wishes.
 15 DR. LAZAR:
 16 A. I'll only have two comments. If I'm not
 17 mistaken, in her work the only return on
 18 investment she included were dividends and
 19 interest payments. She didn't include any
 20 capital gains on any of the financial
 21 assets. And second, I don't recall in her
 22 report any data on what the magnitude were
 23 of these assets, and what's in the response
 24 what the magnitude of these assets. So, if
 25 she says they're in the OSFI filings,

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1 wonderful. What's the number and how does
 2 it differ from the equity number that we're
 3 approximating?
 4 I mean, even if you double the
 5 denominator saying invested assets are twice
 6 the equity, which I seriously doubt is the
 7 case, that still reduces returns to numbers
 8 well above hers.
 9 STAMP, Q.C.:
 10 Q. Mr. Lazar, you were asked by the Public
 11 Utilities Board in questions that they put
 12 to you.
 13 DR. LAZAR:
 14 A. Yeah.
 15 STAMP, Q.C.:
 16 Q. This is Question 2B, and the question is:
 17 "Do Dr. Lazar and Dr. Prisman find invested
 18 assets to be the same as equity?"
 19 DR. LAZAR:
 20 A. Yeah.
 21 STAMP, Q.C.:
 22 Q. So explain why in the audited financial
 23 statements the invested assets, P&C1, page
 24 20.10, are a different value than the
 25 equity, P&C1, page 20.20, for each insurer?

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1 And then your response, I take it it's your
 2 response, is as follows, "As noted, we
 3 assumed invested assets and equity to be the
 4 same. We made this assumption for two
 5 reasons. We did not have any data for
 6 reserves and in our work for FSCO on auto
 7 insurance companies in Ontario, FSCO assumed
 8 that equity closely approximated invested
 9 assets." So now you're telling us here not
 10 only that it's because FSCO does something,
 11 you also tell us you don't have any data for
 12 reserves?
 13 DR. LAZAR:
 14 A. Not in the database that we had.
 15 STAMP, Q.C.:
 16 Q. No, okay.
 17 DR. LAZAR:
 18 A. Is there any documentation from OSFI what
 19 the assets were and compared to the equity
 20 assumptions we made? I'd be curious to see
 21 them.
 22 STAMP, Q.C.:
 23 Q. Mr. Lazar, in your report at page 30, you
 24 have a discussion on operating expense
 25 ratios?

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1 DR. LAZAR:
 2 A. Yes.
 3 STAMP, Q.C.:
 4 Q. And then that discussion is taken out more
 5 fully I think in page 16 of your report?
 6 DR. LAZAR:
 7 A. Page 16?
 8 STAMP, Q.C.:
 9 Q. I believe. So you will see at Table 10 a
 10 comparison of general expense ratios, GISA
 11 and Oliver Wyman, and of course, the purpose
 12 of you including this, is it not, to show
 13 that the Oliver Wyman expense ratios are
 14 higher than GISA, was that the purpose of
 15 it?
 16 DR. LAZAR:
 17 A. Yes.
 18 STAMP, Q.C.:
 19 Q. And the Oliver Wyman column comes right out
 20 of the Oliver Wyman report and I just might
 21 mention for the record it's at page 21,
 22 Table 12 of the Oliver Wyman report, but
 23 your numbers, you say, are, you say they're
 24 GISA numbers?
 25 DR. LAZAR:

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1 A. I think if you go back to Table 7 that's
 2 where they are.
 3 STAMP, Q.C.:
 4 Q. Yes. You're referring to the general
 5 expense ratio?
 6 DR. LAZAR:
 7 A. Yes.
 8 STAMP, Q.C.:
 9 Q. Right. Now, Oliver Wyman's information,
 10 we're told by Ms. Elliott here in her
 11 presentation, came out of the GISA Industry
 12 Expense Report. The industry expense
 13 report, she said, provided the information
 14 for expense ratios for each of the years,
 15 actually only provided for '13, '14, '15 and
 16 '16, I think she had to do a calculation for
 17 '12, but certainly the industry expense
 18 report at Page 20, this is the GISA Industry
 19 Expense Report, has those rates, simply add
 20 the two expense rates to get the 8.2, 7.2,
 21 8.5—not 8.2, sorry, 7.2, 8.5, 7.7 and 9.1.
 22 KENNEDY, Q.C.:
 23 Q. Is this a document we have?
 24 CHAIR:
 25 Q. It's Oliver Wyman's report.

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1 STAMP, Q.C.:

2 Q. This is the one I referred to with Ms.

3 Elliott when she was giving her evidence.

4 We spoke about it then, she spoke about it

5 herself in her evidence or in her

6 presentation and explained where she got her

7 data. So, my –

8 KENNEDY, Q.C.:

9 Q. The witness has got to be shown the

10 document, either put it on the screen or

11 show it to the witness. You just can't

12 simply, Madam Chair, question a witness on a

13 document that you're interpreting the

14 evidence of what someone else said without

15 showing the witness the document.

16 O'FLAHERTY, Q.C.:

17 Q. Madam Chair, it's Table 12 of Ms. Elliott's

18 report.

19 KENNEDY, Q.C.:

20 Q. I don't think so, Mr. O'Flaherty.

21 STAMP, Q.C.:

22 Q. That's where the numbers come, that's where

23 the numbers are. She explained, Mr. Lazar –

24 KENNEDY, Q.C.:

25 Q. That's not the document he's referring to.

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1 STAMP, Q.C.:

2 Q. She explained where she got those numbers,

3 Mr. Lazar.

4 CHAIR:

5 Q. Was that in the transcript, Mr. –

6 STAMP, Q.C.:

7 Q. Oh yes, it's in the transcript. Where she

8 spoke about this you mean, Madam Chair?

9 CHAIR:

10 Q. Yes.

11 O'FLAHERTY, Q.C.:

12 Q. Profit rate adequacy. Just one second, Mr.

13 Stamp, we'll just bring it up for you.

14 FRAIZE, Q.C.:

15 Q. For clarity, what table are we looking at?

16 O'FLAHERTY, Q.C.:

17 Q. 21, page 21, just one second, Mr. Fraize and

18 we will bring it up there for you. I

19 believe this is what we are referring to.

20 STAMP, Q.C.:

21 Q. So I'll take you to this in just a moment,

22 Mr. Lazar, but I just want to make sure your

23 expense ratios, the GISA, 5.7, 4.8, 5.8. 5.6

24 and 6.0, where did you get those?

25 DR. LAZAR:

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1 A. From the GISA document.

2 STAMP, Q.C.:

3 Q. Which document please?

4 DR. LAZAR:

5 A. If I can find it here, make sure I open up

6 the right file. So I'm having difficulty

7 figuring out where it is here on my list,

8 but it was a GISA document. Maybe I shifted

9 it over here. Again, my apologies, I

10 haven't got this organized the best way. So

11 I can't find the exact document here, but

12 it's a GISA document from which my Table 7

13 was extracted.

14 STAMP, Q.C.:

15 Q. Ms. Elliott said it was the Industry Profit

16 and Loss Report that GISA publishes.

17 (12:45 p.m.)

18 DR. LAZAR:

19 A. Most likely that is the case. Here it is,

20 GISA report, automobile insurance financial

21 information, Industry Profit and Loss,

22 that's the report. And footnote give gives

23 the reference.

24 STAMP, Q.C.:

25 Q. I'm sorry, on footnote 5 in your –

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1 DR. LAZAR:

2 A. In my report.

3 STAMP, Q.C.:

4 Q. It's page 25 of the GISA –

5 DR. LAZAR:

6 A. No, page 13.

7 STAMP, Q.C.:

8 Q. No, no, but you're referring in your

9 footnote to page 25 of the GISA report.

10 DR. LAZAR:

11 A. Table on page 25 in the GISA report, yes.

12 STAMP, Q.C.:

13 Q. Right, and Ms. Elliott referred to that same

14 page. When you used the numbers that you

15 used, of course, we know that the total

16 expense ratio that Oliver Wyman produced are

17 set out in Table 12 of the Oliver Wyman

18 reform, of profit review document, right, do

19 you know that?

20 DR. LAZAR:

21 A. I'm sorry, I didn't hear that.

22 STAMP, Q.C.:

23 Q. We have to bring up page 21 of the Oliver

24 Wyman profitability review.

25 CHAIR:

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1 Q. Is that the one that's up, Mr. Stamp?

2 STAMP, Q.C.:

3 Q. Oh yes, sorry, it is up there, sorry. So,

4 Mr. Lazar, the total expense ratio for those

5 years is made up of three components?

6 DR. LAZAR:

7 A. Uh-hm.

8 STAMP, Q.C.:

9 Q. Commissions, premium taxes, general expenses

10 and total expenses, which Oliver Wyman puts

11 at 28, 23, and so on. You have a different

12 total expense ratio because you have a

13 different general expense ratio, is that

14 correct?

15 DR. LAZAR:

16 A. Correct.

17 STAMP, Q.C.:

18 Q. Simple as that.

19 DR. LAZAR:

20 A. Apparently.

21 STAMP, Q.C.:

22 Q. How did you determine that the number they

23 had put in for commissions was correct? Did

24 you check that?

25 DR. LAZAR:

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1 A. No, it wasn't broken down, so I took her

2 numbers.

3 STAMP, Q.C.:

4 Q. It wasn't broken down?

5 DR. LAZAR:

6 A. Not, no, looked at the general numbers, so

7 it was included in acquisition expense

8 ratio.

9 STAMP, Q.C.:

10 Q. So are you aware of whether or not GISA data

11 specifically identifies the commission

12 percentage in the reports it produces?

13 DR. LAZAR:

14 A. I'd have to go look, back and look at the

15 data to answer that question.

16 STAMP, Q.C.:

17 Q. And how did you satisfy yourself that the

18 premium taxes that Oliver Wyman listed in

19 Table 12 were acceptable?

20 DR. LAZAR:

21 A. I had no reason to question that.

22 STAMP, Q.C.:

23 Q. Okay, so the only question that you had was

24 with the general expense piece, is that

25 right?

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1 DR. LAZAR:

2 A. Was the general expense ratio, yes. Now,

3 can I just make a comment?

4 STAMP, Q.C.:

5 Q. I'm just going to ask you questions, please,

6 if I can, Mr. Lazar.

7 MR. LAZAR:

8 A. Okay, I'll be patient.

9 STAMP, Q.C.:

10 Q. One of the things that I can point you to on

11 this discussion is again at Ms. Elliott's

12 evidence, because I asked her about where

13 you got your expense rates that you have in

14 your table, the one we just looked at a

15 moment ago, your expense ratios at your

16 Table 10. I asked her about that and if you

17 can go –

18 CHAIR:

19 Q. Page 97 of that transcript.

20 STAMP, Q.C.:

21 Q. Yes, thank you, Madam Chair.

22 KENNEDY, Q.C.:

23 Q. Sorry, what date is that?

24 STAMP, Q.C.:

25 Q. September 6th. So I asked her about this and

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1 I said, "They suggest that the column that

2 they used, GISA numbers, they pulled that

3 out of, I guess, the same report maybe?"

4 Ms. Elliott says, "No, they pulled that out

5 of 9501. What they're presenting is a

6 subset of the general expenses, so they're

7 both from GISA, but one is a subset of the

8 general expenses, the column labelled "OW"

9 which is GISA 9502, is all general

10 expenses." And I said, "Right, and is that

11 the report you're referring to called the

12 Industry Profit and Loss Report?" And she

13 says, "Under the column, GISA, yes." And I

14 say, "Right, okay, and so they've

15 essentially jumped from one GISA report with

16 the expenses that they show attributed to

17 Oliver Wyman, they actually, they're

18 actually GISA, jumped to a different

19 report?" Ms. Elliott says, "Right, they

20 have used a profit and expense report which

21 presents a subset of the general expenses

22 and didn't use the total general expenses

23 which is available in the report that we

24 used that is specific to private passenger

25 expenses only." I asked then, "So can you

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1 offer any explanation why the authors would
 2 have left the expense report, the industry
 3 expense report that has the data right in
 4 it, and gone to a different report to take a
 5 different set of expense percentages?" Ms.
 6 Elliott says, "I have no idea why, I don't
 7 know." I asked, "Does it make any sense?"
 8 She says, "No, I don't agree with their
 9 number, they are missing a component of the
 10 general expenses." And I say, "You're not
 11 comparing apples and apples?" And she says,
 12 "Right." So her point is, and you can
 13 answer this, Mr. Lazar, you've missed
 14 expenses when you used the percentages that
 15 you used which she says comes from the
 16 Industry Profit and Loss Report and don't
 17 come from the Industry Expense Report.
 18 DR. LAZAR:
 19 A. Okay, I'll answer this as quickly as I can.
 20 I'm sure Ms. Elliott is a great actuary, I'm
 21 not going to question her, I'm sure she's
 22 extremely good. She's not an economist and
 23 she misses the point entirely. So let's
 24 take her expense numbers, use those, and I
 25 believe it's one to put in context, what's

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1 the relevance of all of this if we use a
 2 higher number? There is no relevance for
 3 the question of did consumers of auto
 4 insurance in this province pay too much?
 5 It's not relevant and here's the reason why.
 6 If you accept her expense numbers, let's
 7 take them, so they're going to enter into
 8 the rate setting process. What are the two
 9 key variables that we still disagree upon?
 10 The return on equity and the return on
 11 investment. The return on equity, Ms.
 12 Elliott, that was not her area of expertise,
 13 that's not what she was asked to do. So all
 14 I'm saying is even if we take her expense
 15 numbers for the time being, plug them in and
 16 let's go through the exercise, let's
 17 determine what the maximum premiums would
 18 have been allowed with a 10 percent return
 19 in equity, whatever number you want for the
 20 return on investment, here the premiums
 21 would have been allowed, redo that with a
 22 lower return on equity number, use her
 23 return investment if you want, use her
 24 expense numbers, that maximum allowable
 25 premium is going to be lower, which means

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1 consumers have overpaid. I don't care how—
 2 what numbers you use, how you try to cast
 3 this. Now, even if you use her numbers and
 4 again, she's not an economist, so I can't
 5 blame her for this, you've got to take into
 6 account what are best practice, what are
 7 expense ratios that should be the target for
 8 the Board.
 9 STAMP, Q.C.:
 10 Q. Madam Chair, if I can just interrupt here.
 11 It's not focussing on the question that I
 12 asked, it's focussing on –
 13 DR. LAZAR:
 14 A. Yes, but there's got to be context.
 15 STAMP, Q.C.:
 16 Q. It's giving us a seminar that he gave
 17 earlier in his direct evidence or his direct
 18 presentation.
 19 DR. LAZAR:
 20 A. But again, it's the context, you're asking
 21 me these questions, what the difference is,
 22 so the question is what difference does it
 23 make for the fundamental question, and my
 24 answer is it doesn't, there are
 25 overpayments, regardless of what numbers you

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1 throw in because of the differences in
 2 return on equity that were used and that
 3 should have been used, that's the bottom
 4 line. Then, is her number the right one to
 5 have been used in the exercise, that's
 6 another question. And my answer to that is,
 7 no, it's not, regardless of general expense
 8 number it's the wrong number to use because,
 9 again, not being an economist, you don't
 10 realize that part of the regulatory process
 11 is to incentivize the companies that are
 12 being regulated to achieve the best
 13 practices.
 14 STAMP, Q.C.:
 15 Q. Madam Chair, you know, we're getting a
 16 seminar here. I'm getting a lecture.
 17 CHAIR:
 18 Q. Did you get an answer to your question, Mr.
 19 Stamp?
 20 STAMP, Q.C.:
 21 Q. Well my point was, simply this –
 22 CHAIR:
 23 Q. Did you ask a question first of all?
 24 STAMP, Q.C.:
 25 Q. I asked a question, but first of all I'm

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1 going to go back because Mr. Lazar keeps
 2 going around and around in these long-winded
 3 answers. The fact is he has said the
 4 expense ratio doesn't matter. Now he's
 5 explained it's one of the three, I think,
 6 critical points to why he says the premium
 7 is overpaid.
 8 CHAIR:
 9 Q. I think we're going around in circles here.
 10 I just wanted to know if you got an answer
 11 to the question that I thought you asked.
 12 STAMP, Q.C.:
 13 Q. I'll ask it again, Madam Chair.
 14 CHAIR:
 15 Q. Okay, that's fair enough.
 16 STAMP, Q.C.:
 17 Q. Why would you exclude pertinent expenses
 18 from the expense ratio?
 19 DR. LAZAR:
 20 A. Because the dataset I had and we used didn't
 21 distinguish them.
 22 STAMP, Q.C.:
 23 Q. Okay, so you didn't look at all of the
 24 charts that were available, you looked at
 25 one chart and picked it, is that correct?

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1 DR. LAZAR:
 2 A. That seemed to be the relevant chart because
 3 it's dealing with the profits of the
 4 industry.
 5 STAMP, Q.C.:
 6 Q. Well Ms. Elliott, who is an actuary and
 7 studies this all the time, says you looked
 8 at the wrong chart.
 9 DR. LAZAR:
 10 A. But the issue is what does that have to do
 11 with estimating overpayments?
 12 STAMP, Q.C.:
 13 Q. Well it has this to do, does it not, Mr.
 14 Lazar, doesn't it suggest that the
 15 overpayment that you are contemplating or
 16 advancing has occurred, you're wrong on the
 17 expense ratio, that's one of the critical
 18 points that you've made.
 19 DR. LAZAR:
 20 A. No, my answer is our analysis, whether you
 21 accept it or not, is if you were to have
 22 done the right analysis, to do it thoroughly
 23 you conclude unequivocally and I'll repeat
 24 it again and I hate to repeat things, but
 25 premiums are too high, plain and simple,

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1 regardless of what expense ratio you plug
 2 in, regardless what return on investment you
 3 plug in because you used the wrong return on
 4 equity. And then the other question
 5 becomes, even if you take her number –
 6 STAMP, Q.C.:
 7 Q. So, go ahead, go ahead.
 8 DR. LAZAR:
 9 A. Okay, she used it to try and estimate
 10 premium over underpayment for 2017, but she
 11 never asked the question what are the best
 12 practices, so our criticism of her work was
 13 when she tried to take what she had done and
 14 then try to extend it to deal with what
 15 should be the fundamental question here,
 16 were premiums too high or too low? That's
 17 where our criticism came in and that's my
 18 criticism of her work, period.
 19 O'FLAHERTY, Q.C.:
 20 Q. Madam Chair, earlier this morning we had
 21 discussed perhaps we would check at around
 22 12:45 and I see we are past that, to see how
 23 we were progressing with the examination and
 24 I have spoken with my learned friend, Mr.
 25 Browne, and he indicated that he had a time

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1 estimate he could share with us once we find
 2 out from Mr. Stamp as to how he's
 3 progressing with his questioning to
 4 determine how we move forward.
 5 CHAIR:
 6 Q. Mr. Stamp, I don't want to put you in a
 7 position of having to tell us how long you
 8 are going to be, but –
 9 STAMP, Q.C.:
 10 Q. Madam Chair, we would typically stop at
 11 1:30, but if we kept going, we won't stop at
 12 1:30, so if you wish to take a break,
 13 that's, you know, probably the best thing to
 14 do if you feel that that is –
 15 CHAIR:
 16 Q. Well, yes, let's take a fifteen-minute
 17 break, let everybody get prepared for
 18 another, what appears to be at least an hour
 19 or so, at least.
 20 KENNEDY, Q.C.:
 21 Q. Madam Chair, if we're going to do that, I'd
 22 suggest we take a lunch break. I mean, we
 23 sat here yesterday until 2:30, you know,
 24 this is just—we are sitting from 9:00 in the
 25 morning to 2:30 in the afternoon. It's a

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1 very long time to be sitting here like this.
 2 I mean, we've got the witness, we've got
 3 staff members, we've got all of us. If
 4 we're not going to finish, I'd just as soon
 5 take the lunch break, come back and just
 6 keep going, like we would do as if we were
 7 in a courtroom.
 8 O'FLAHERTY, Q.C.:
 9 Q. I don't think everybody has the
 10 availability. I'm seeing heads being shaken
 11 behind Mr. Kennedy, so I think, I don't
 12 think that's going to be workable, Madam
 13 Chair.
 14 CHAIR:
 15 Q. We're just going to push through to finish
 16 Mr. Lazar and whatever break is going to be
 17 needed here, we'll take, so –
 18 STAMP, Q.C.:
 19 Q. Did you want to take a break now, Madam
 20 Chair?
 21 CHAIR:
 22 Q. We'll take a fifteen-minute break and we'll
 23 come back, is that okay for you, Mr. Browne?
 24 BROWNE, Q.C.:
 25 Q. Yes, that's fine, Chair. We can't go over

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1 the 2:00 mark, there's commitments and I'll
 2 only be 10 minutes at most. My questions
 3 will be quite specific.
 4 CHAIR:
 5 Q. I understood yesterday, I think what we had
 6 agreed to is that we would stay until we
 7 finished Dr. Lazar, so that's what we'll try
 8 to do. Is your flight out today, sir?
 9 DR. LAZAR:
 10 A. 5:30.
 11 CHAIR:
 12 Q. 5:30, okay. Thank you, see you in about
 13 fifteen minutes.
 14 (RECESS – 1:00 p.m.)
 15 (RESUME – 1:15 p.m.)
 16 STAMP, Q.C.:
 17 Q. Batteries recharged, Mr. Lazar?
 18 DR. LAZAR:
 19 A. I think so.
 20 STAMP, Q.C.:
 21 Q. Good. Mr. Lazar, look, on this point
 22 generally that we've been talking about,
 23 what you say is it doesn't matter about the
 24 expenses if they're what Ms. Elliott says,
 25 it doesn't matter if the ROI is what she

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1 says, it all comes down to they've got to
 2 find best practices, is that where you are?
 3 DR. LAZAR:
 4 A. That's one of the issues.
 5 STAMP, Q.C.:
 6 Q. And because, as we have already talked
 7 about, she has said to this panel in her
 8 evidence, in her presentation, that you have
 9 approached the ROI incorrectly. She also
 10 said you've miscalculated the expense ratios
 11 because you left out expenses, and these are
 12 the things that she says lead you where you
 13 have gone, to wrong conclusions. But you
 14 say it doesn't matter because, I think
 15 you're saying best practices have to come
 16 into play?
 17 DR. LAZAR:
 18 A. Okay, well I took advantage at the break to
 19 do some sort of rough calculations, to get
 20 an estimate of what the overpayments were,
 21 and –
 22 STAMP, Q.C.:
 23 Q. No, I don't want to go back to that
 24 overpayment, I want to come back to the
 25 expense ratios.

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1 DR. LAZAR:
 2 A. No, no, but it's –
 3 STAMP, Q.C.:
 4 Q. I want to stay focused on the questions.
 5 DR. LAZAR:
 6 A. Okay, but your question is saying, gee, if
 7 we accepted everything Ms. Elliott said,
 8 then our estimates of the overpayments would
 9 disappear, her numbers that suggest there's
 10 actually been underpayments would be valid.
 11 STAMP, Q.C.:
 12 Q. But you still say to that it's still not
 13 good enough because you've got to find a
 14 better way to do business?
 15 DR. LAZAR:
 16 A. I'm saying that's one variable. I mean, I
 17 was going to say I did some calculations and
 18 –
 19 CHAIR:
 20 Q. Just a second now, did you get an answer to
 21 your –
 22 STAMP, Q.C.:
 23 Q. No, I'm trying to be clear, I don't want to
 24 go back over everything we've done, Mr.
 25 Lazar.

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<p>1 MR. LAZAR: 2 A. No, no, I'm not going to go over it, I'm 3 just wanting to give you some indication of 4 what the differences are. 5 STAMP, Q.C.: 6 Q. Well we have Oliver Wyman's calculations – 7 CHAIR: 8 Q. But Mr. Stamp hasn't asked for that 9 question. 10 STAMP, Q.C.: 11 Q. We have Oliver Wyman's calculations as to 12 the answers that she has provided, what I 13 want to make clear is this, you're saying 14 that if her expense calculations, her 15 expense ratio which she says I took all the 16 expenses and she says you didn't take all 17 the expenses. To that, you say, I took what 18 I had and I didn't know about some other 19 chart and it doesn't matter, you said 20 anyway, I think, did you? 21 DR. LAZAR: 22 A. It doesn't matter in – 23 STAMP, Q.C.: 24 Q. The expenses of what she says or what you 25 say, it doesn't matter, did you say</p>	<p>1 with? 2 DR. LAZAR: 3 A. I would have no reason to sort of challenge 4 them, I might disagree with the numbers, but 5 I'm saying these are the numbers she 6 presented and they're of little relevance 7 for the questions that Eli and I were asked 8 to address. 9 STAMP, Q.C.: 10 Q. Okay, but one of those questions that she 11 has spoken about, or one of the issues she 12 spoke about is ROI, and she says you and she 13 are on a different page when you discuss 14 ROI. She says you're not talking about ROI 15 like she's talking about it, you're talking 16 about something else. That's a difference 17 she has that gives her a different ROI than 18 you give. 19 DR. LAZAR: 20 A. Except the question I have in my response 21 earlier was she only included dividend and 22 interest payments in terms of the return on 23 the investment and in terms of her 24 denominator, I have no idea what numbers she 25 used. We didn't see any number, all we saw</p>
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<p>1 DR. LAZAR: 2 A. In terms of determining the overpayments, 3 yes. 4 STAMP, Q.C.: 5 Q. Right, so how can it be that an important 6 element like expense ratios doesn't make any 7 difference? Why have you spent so much time 8 talking about it if it makes no difference? 9 DR. LAZAR: 10 A. Essentially to sort of cast some doubt on 11 her methodology for trying to determine are 12 the premiums too high or too low for 2017. 13 As I said in my presentation, if she had 14 stopped before that, whatever numbers she 15 has, those are her numbers, you presented 16 the facts as you know them, that's 17 wonderful. But it doesn't address the 18 question that Eli and I were asked to 19 address, have the premiums been too high or 20 too low, that was our question. And until 21 she moved in that direction, we would have 22 had very few comments to make. 23 STAMP, Q.C.: 24 Q. So essentially, then, everything up to her 25 conclusions as to 17, you would not disagree</p>	<p>1 was the ROI percentage. I know I went into 2 the numerator, I don't know what was the 3 denominator and how that differed from what 4 we used. So that was a question that we 5 posed. 6 STAMP, Q.C.: 7 Q. I'm pretty certain she spoke about including 8 capital gains. You turned to page 90 – 9 DR. LAZAR: 10 A. No, no, no, go to her report, forget about 11 what she did in the testimony. We went by 12 her report. I don't know what she testified 13 here, but in her report there are only 14 dividends in interest payments. 15 STAMP, Q.C.: 16 Q. Where are you referring to? 17 DR. LAZAR: 18 A. Sorry? 19 STAMP, Q.C.: 20 Q. Where in her report are you referring to? 21 DR. LAZAR: 22 A. When she defines the returns there. I don't 23 think she mentioned at all capital gains. 24 STAMP, Q.C.: 25 Q. Take us to where you are on that point, Mr.</p>

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1 Lazar, please.

2 DR. LAZAR:

3 A. I'm going to have to, so I believe through

4 her whole report here, claim methodology,

5 expenses, investment income, okay, so we

6 used, the rate that was calculated there was

7 investment income, I guess on her page 8 she

8 doesn't really explain this.

9 STAMP, Q.C.:

10 Q. Are you saying she didn't include it?

11 DR. LAZAR:

12 A. The numbers she had there did not, I'm sure

13 -

14 STAMP, Q.C.:

15 Q. Where are you, Mr. Lazar, I'm sorry, can you

16 tell us where you are?

17 DR. LAZAR:

18 A. I'm looking at page 8 of her report.

19 STAMP, Q.C.:

20 Q. Of the March 29, Oliver Wyman report?

21 DR. LAZAR:

22 A. Table 6, okay, that's where she has the

23 investment rates and she does not discuss

24 what goes into the numerator, what are the

25 returns.

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1 STAMP, Q.C.:

2 Q. So how did you conclude from that that she

3 didn't take that into account?

4 DR. LAZAR:

5 A. I just looked at the low returns, I did a

6 comparison to, I think, what company do I

7 have here? Intact, where Intact reported

8 their investment returns and their

9 investment returns were clearly only

10 dividends and interest payments.

11 STAMP, Q.C.:

12 Q. I don't know about Intact, but I know that

13 Ms. Elliott testified here, page 90, that

14 she took into account, I think it was here

15 that she said -

16 DR. LAZAR:

17 A. She didn't state that at all in her report

18 and given the values here, the low values,

19 that could only suggest that what was

20 included were dividend and interest

21 payments.

22 STAMP, Q.C.:

23 Q. Mr. Lazar, you talk about, let me just make

24 sure I've got the right report here in front

25 of me now, at page 11 of your report, it's

Page 187

1 above Table 5, you see that Oliver Wyman did

2 disaggregate the operating expenses in the

3 three categories.

4 DR. LAZAR:

5 A. Yes.

6 STAMP, Q.C.:

7 Q. I asked Ms. Elliott about all that and

8 you'll find that discussion, or we can find

9 that discussion at page, I think it starts

10 at 104, but primarily at 105, I point out at

11 the top of page 105, this is all the

12 September 6th hearing date again that we're

13 referring to, and I'm referring to a table.

14 I say, "The authors say"—this is at line 4,

15 5, "The authors say that Oliver Wyman did

16 disaggregate the operating expenses into

17 three categories and describes those

18 categories and the breakdown is presented in

19 Table 5." And I'll skip down, she says,

20 "That's correct." I say, "So it wasn't the

21 case that Oliver Wyman broke the numbers

22 down as we have in this table, the GISA

23 numbers are broken down that way?" She

24 says, "That's correct, yes." And a little

25 further down on the page 106 at line 8, she

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1 says, "It's all clearly that I'm just taking

2 the numbers from the chart and putting them

3 in the table for our report." "So it wasn't

4 Oliver Wyman that disaggregated, it was GISA

5 had done this?" "Uh-hm, yeah." So the

6 point that she's making is she's taken the

7 expenses and the point that she's making, of

8 course for your purpose, is that she took it

9 all from the Industry Expense Report and she

10 says I don't know why Mr. Lazar went to the

11 Industry Profit Report to take a subset of

12 those expenses. So I'm going to leave this

13 topic, but if you have anything to say on

14 that point before I go, by all means, this

15 is the time to say it.

16 DR. LAZAR:

17 A. I'm trying to remember in her report she

18 referred to GISA's—okay, what was it? Yeah,

19 Financial Information Industry Profit and

20 Loss Report for Private Passenger

21 Automobiles, she referred to that and she

22 made some comparisons.

23 STAMP, Q.C.:

24 Q. She used two reports.

25 DR. LAZAR:

<p style="text-align: right;">Page 189</p> <p>1 A. Well, that's what's referred to here on her 2 page 11, and that the report we went to and 3 used and took those numbers. Up to that 4 point, again her original report, that had 5 nothing to do with Oliver Wynman. We used 6 the MSA data. We only went to the GISA data 7 after we got the Oliver Wynman Report and 8 her reference here is strictly to this 9 report, Financial Information Industry 10 Profit and Loss Report for Private Passenger 11 Automobiles. That's the report we used. 12 Now it seems that she claiming she used a 13 different report. If so, I don't see any 14 reference to it. Perhaps I missed it, but I 15 don't see that Eli and would both have 16 missed that. 17 STAMP, Q.C.: 18 Q. That's fine. 19 DR. LAZAR: 20 A. Okay. 21 STAMP, Q.C.: 22 Q. Her presentation is here on that point, so 23 we have all that already. 24 DR. LAZAR: 25 A. Okay.</p>	<p style="text-align: right;">Page 191</p> <p>1 DR. LAZAR: 2 A. That's going back to table 7 in our report. 3 STAMP, Q.C.: 4 Q. Right, and I'm going to suggest to you 5 that's right out of that same GISA Industry 6 Profit and Loss Report? 7 DR. LAZAR: 8 A. Yes. 9 STAMP, Q.C.: 10 Q. But Oliver Wynman of course as you know, has 11 generated and they've calculated the loss 12 ratios based on accident year? 13 DR. LAZAR: 14 A. Yes. 15 STAMP, Q.C.: 16 Q. And there's a focus on that issue in her 17 presentation that you don't—you say over 18 time it'll all be a wash, I think you said 19 maybe? 20 DR. LAZAR: 21 A. Yeah, it should average out. 22 STAMP, Q.C.: 23 Q. Yes. 24 DR. LAZAR: 25 A. Whether it's three years, five years, eight</p>
<p style="text-align: right;">Page 190</p> <p>1 STAMP, Q.C.: 2 Q. I'm going to turn, Mr. Lazar, to the claims 3 ratio, and this—again, you picked this up 4 at, in your report, at—again, picked up or 5 mentioned again in that group of bullets at 6 page 30. 7 DR. LAZAR: 8 A. Yeah. 9 STAMP, Q.C.: 10 Q. You'll see in the second bullet 79 percent, 11 approximately halfway between the GISA for 12 2016 and Oliver Wynman's assumption for '17. 13 So, what, you just did an average? Is that 14 right, or an approximate average? 15 DR. LAZAR: 16 A. Yeah, just an average, a simple average. 17 STAMP, Q.C.: 18 Q. Sure. Okay. And you point out in your 19 report, I think it's table 12 that you got 20 your claims ratios from a GISA FII PNL 21 Report or ratios from that report? 22 DR. LAZAR: 23 A. Yes. 24 STAMP, Q.C.: 25 Q. Is that right?</p>	<p style="text-align: right;">Page 192</p> <p>1 years, I don't know the exact timeframe, but 2 it should wash out. 3 STAMP, Q.C.: 4 Q. Yes, yes. So, if you wait long enough, 5 it'll all sort itself out, but she uses the 6 accident years for a particular reason she 7 explains. Did you know what she had said 8 about that? 9 DR. LAZAR: 10 A. I read it, but again, the data we had 11 available were only available on a calendar 12 year basis. 13 (1:30 p.m.) 14 STAMP, Q.C.: 15 Q. So, would you agree that the question of the 16 calculation of accident year loss ratios is 17 an actuarial exercise? 18 DR. LAZAR: 19 A. Yes, but you know, it can all be put on 20 computers. I mean, yes. 21 STAMP, Q.C.: 22 Q. You don't need actuaries any more, is that 23 right? 24 DR. LAZAR: 25 A. It's an actuarial exercise.</p>

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<p>1 STAMP, Q.C.:</p> <p>2 Q. Okay.</p> <p>3 DR. LAZAR:</p> <p>4 A. Okay.</p> <p>5 STAMP, Q.C.:</p> <p>6 Q. Yes, I can't put it on the computer and make</p> <p>7 it happen.</p> <p>8 DR. LAZAR:</p> <p>9 A. There's no reason to disagree.</p> <p>10 STAMP, Q.C.:</p> <p>11 Q. I'm going to turn to the questions asked to</p> <p>12 you, are put you, or put the Campaign for</p> <p>13 you I guess by IBC. And I'm going to turn</p> <p>14 to question 1a. And essentially the</p> <p>15 question—I don't know if that needs to be</p> <p>16 brought up, but we can, I guess, have it</p> <p>17 brought up if it's best.</p> <p>18 DR. LAZAR:</p> <p>19 A. Yeah.</p> <p>20 STAMP, Q.C.:</p> <p>21 Q. This is IBC questions to the Campaign for</p> <p>22 Dr. Lazar, and 1 –</p> <p>23 MR. FELTHAM:</p> <p>24 Q. The questions or the answers?</p> <p>25 STAMP, Q.C.:</p>	<p>1 A. The MSA data.</p> <p>2 STAMP, Q.C.:</p> <p>3 Q. Oh, it's MSA again, is it? Okay.</p> <p>4 DR. LAZAR:</p> <p>5 A. And the GISA data we looked up ourselves.</p> <p>6 STAMP, Q.C.:</p> <p>7 Q. Okay.</p> <p>8 DR. LAZAR:</p> <p>9 A. I believe, or it was a document sent, but</p> <p>10 it's—you know, the report that Ms. Elliott</p> <p>11 referred to in her report.</p> <p>12 STAMP, Q.C.:</p> <p>13 Q. I want to turn for a moment to PUB, Public</p> <p>14 Utilities Board Questions, and question</p> <p>15 number 3. And that question 3 at the bottom</p> <p>16 of the page I think. Yes, thank you. "As</p> <p>17 reported by GISA, its accident year 2016</p> <p>18 estimate ultimate loss ratio is 87 percent,</p> <p>19 and as of December 31st, 2017, AUTO 1005. As</p> <p>20 presented in the Oliver Wyman report, the</p> <p>21 estimated ultimate loss ratio for accident</p> <p>22 year 2016 is 85 percent. On page 22, Dr.</p> <p>23 Lazar and Dr. Prisman state Oliver Wyman's</p> <p>24 estimate of the ultimate loss ratio for</p> <p>25 accident year 2016 is out of line with</p>
<p>Page 194</p> <p>1 Q. I'm going to get to both I guess, but I just</p> <p>2 want to get the question first if we—in case</p> <p>3 people want to see it. I don't want Mr.</p> <p>4 Kennedy mad at me. So, I'm sorry, is this</p> <p>5 IBC? I'm not sure. Yes, here we are.</p> <p>6 MS. KEAN:</p> <p>7 Q. Yes, sorry.</p> <p>8 STAMP, Q.C.:</p> <p>9 Q. Thank you. That's right, thank you. So,</p> <p>10 the question is essentially, "Could you</p> <p>11 please explain financial year data and</p> <p>12 accident year data, and why differences in</p> <p>13 the financial year data should affect an</p> <p>14 analysis based on accident year data?"</p> <p>15 That's the question that was asked of you at</p> <p>16 question 1a, and I can tell what the answer</p> <p>17 is that you gave. It can be brought up,</p> <p>18 too, if you wish, but it says, "We relied"—</p> <p>19 this is 1a. "We relied on financial year</p> <p>20 data because these were the data provided to</p> <p>21 us. Over a period of time, any year-to-year</p> <p>22 differences should net out to zero." When</p> <p>23 you say, "It was provided to us," who do you</p> <p>24 say it was provide to you by?</p> <p>25 DR. LAZAR:</p>	<p>Page 196</p> <p>1 GISA." And then the question is, "Given</p> <p>2 that GISA's and Oliver Wyman's accident year</p> <p>3 2016 ultimate loss ratio are quite close,</p> <p>4 explain the basis for this statement."</p> <p>5 That's 3a. And if I can turn to your</p> <p>6 response to question 3a, you don't appear to</p> <p>7 answer the question, Mr. Lazar. You simply</p> <p>8 refer back to your 74 percent again, don't</p> <p>9 you?</p> <p>10 DR. LAZAR:</p> <p>11 A. Yes.</p> <p>12 STAMP, Q.C.:</p> <p>13 Q. They've asked for an explanation, but all</p> <p>14 you did was repeat the 74 percent.</p> <p>15 DR. LAZAR:</p> <p>16 A. Well, our comment was there was a</p> <p>17 significant gap; 74 percent compared to her</p> <p>18 number of 85 percent.</p> <p>19 STAMP, Q.C.:</p> <p>20 Q. But they had asked you to explain the</p> <p>21 difference when it came to this 85 percent</p> <p>22 versus 87 percent, and you just repeated the</p> <p>23 74 percent, is that right?</p> <p>24 DR. LAZAR:</p> <p>25 A. Well, we interpreted that question to refer</p>

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1 to the difference between the GISA number
 2 and this 87 percent number.
 3 STAMP, Q.C.:
 4 Q. I think they were drawing your attention to
 5 the fact that the 85 and 87 percents were so
 6 close. Were they not doing that?
 7 DR. LAZAR:
 8 A. That's not how I interpreted the question.
 9 STAMP, Q.C.:
 10 Q. Okay. In 3b you are asked by the Public
 11 Utilities Board, "In comparing loss ratio
 12 findings, explain what consideration Dr.
 13 Lazar and Dr. Prisman gave to the
 14 differences in accident year versus calendar
 15 year definition of loss ratios." And
 16 there's an answer to that given –
 17 DR. LAZAR:
 18 A. We did not answer that.
 19 STAMP, Q.C.:
 20 Q. Oh, you did.
 21 DR. LAZAR:
 22 A. Uh?
 23 STAMP, Q.C.:
 24 Q. You give an answer. It's at—in your
 25 responses.

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1 DR. LAZAR:
 2 A. I refer to the answer to 1a.
 3 STAMP, Q.C.:
 4 Q. Yes, but I'm looking at your response to
 5 question 3 –
 6 DR. LAZAR:
 7 A. I don't know what the difference would be
 8 between calendar and financial year, year by
 9 year, since we didn't have sort of the
 10 calendar and accident year because we didn't
 11 have the accident year data. So -
 12 STAMP, Q.C.:
 13 Q. I'm sorry, what did you say again? I'm
 14 sorry, Mr. Lazar.
 15 A. Okay, I think your question was—sorry, I'm
 16 going to refer back to your—"In comparing"—
 17 yes. "What consideration"—"gave to the
 18 differences"—we did not give any because we
 19 did not have the accident year data. Okay.
 20 You said the data we used was annual data?
 21 DR. LAZAR:
 22 A. Yes.
 23 STAMP, Q.C.:
 24 Q. And do you not accept that there's an
 25 important distinction between annual year,

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1 calendar year, versus accident year?
 2 DR. LAZAR:
 3 A. Undoubtedly, there will be timing issues.
 4 There will be differences, you know. Can I
 5 predict what they might be from year to
 6 year; no, I can't, I don't know.
 7 STAMP, Q.C.:
 8 Q. I'm going to just ask you to – we're going
 9 to turn to page 109 in Ms. Elliott's
 10 presentation on the 6th of September, please.
 11 I'm sorry, September 6th, Ms. Elliott's
 12 transcript. Sorry about that.
 13 MS. KEAN:
 14 Q. Page?
 15 STAMP, Q.C.:
 16 Q. Page 109. Can you see that, Mr. Lazar?
 17 DR. LAZAR:
 18 A. Yes.
 19 STAMP, Q.C.:
 20 Q. So Ms. Elliott says, "The information that's
 21 provided where we do our analysis of
 22 estimating what the ultimate losses will be
 23 is provided by coverage on an accident year
 24 basis, and we also as part of the review
 25 process wanted to review the coverage

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1 information that is only available by
 2 accident year, and it would be the standard
 3 way to review pricing review work is on an
 4 accident year basis. So when companies
 5 submit rate applications, it's using
 6 accident year data, and so this review was
 7 looking at a hindsight review of the return
 8 on equity that was achieved and measuring
 9 that against is a 10 percent target that
 10 would be allowed in rates, and that is all
 11 done on an accident year basis. So the
 12 detailed data is available by accident year.
 13 If you look at the calendar year data, it's
 14 done on a higher level, so it's third party
 15 liability accident benefits and all other
 16 coverages combined. It doesn't have the
 17 same detail as the accident year data does,
 18 and also the calendar year data is net of
 19 reinsurance arrangements, whereas when we're
 20 looking at pricing, it's all done before any
 21 financial reinsurance, and that's done kind
 22 of after the fact by the financial
 23 departments in insurance companies". Can you
 24 respond to that? Do you have anything to
 25 say to that observation that Ms. Elliott has

<p style="text-align: right;">Page 201</p> <p>1 made about why it's important to use 2 accident year and not calendar year? 3 DR. LAZAR: 4 A. Again my response will be two-fold. One, 5 I'll accept there are going to be, 6 obviously, differences in whatever analysis 7 you want to undertake, and, you know, I have 8 no reason to quarrel with this, and my 9 second comment is, I refer you back to my 10 dissertations that I've repeated several 11 times before, and no need to repeat it now. 12 STAMP, Q.C.: 13 Q. Thank you. I'm going to turn for one moment 14 to a report that you prepared for the 15 Ontario Trial Lawyers. 16 DR. LAZAR: 17 A. Yeah. 18 STAMP, Q.C.: 19 Q. It was done April, 2018. You may recall all 20 of that. 21 DR. LAZAR: 22 A. Yeah, well, you're assuming my memory is 23 better than it is, thank you. 24 STAMP, Q.C.: 25 Q. It's just April.</p>	<p style="text-align: right;">Page 203</p> <p>1 you could tell of any jurisdiction that used 2 that model to do ROE for auto insurance? 3 DR. LAZAR: 4 A. Other jurisdiction? 5 STAMP, Q.C.: 6 Q. That used that model for automobile 7 insurance? 8 DR. LAZAR: 9 A. I can sort of go back to the work we did for 10 the Ontario Energy Board, and when we looked 11 at other jurisdictions, Canada, US, there 12 were several in the US that were using this 13 model for regulating electrical utilities. 14 STAMP, Q.C.: 15 Q. Okay, electrical utilities, sure, but I'm 16 asking whether you – 17 DR. LAZAR: 18 A. For the automobile insurance, FSCO never 19 asked us to do this, so we never did it for 20 them. I've never followed up and looked at 21 it. 22 STAMP, Q.C.: 23 Q. But were you asked by the Board here whether 24 that approach was followed by any other rate 25 regulator?</p>
<p style="text-align: right;">Page 202</p> <p>1 DR. LAZAR: 2 A. Um? 3 STAMP, Q.C.: 4 Q. It's only just April. 5 DR. LAZAR: 6 A. Thank you for giving me the benefit of the 7 doubt. 8 STAMP, Q.C.: 9 Q. When that shows up, turn to page six, if I 10 can, please. This is a discussion on ROE, 11 as you'll see in a moment when it comes up, 12 page 6, the bottom of the page, please. 13 Thank you, and you'll see this last full 14 paragraph. It says, "Several years ago my 15 colleague at the Schulich School of 16 Business, Professor Eli Prisman, and I, were 17 retained by FSCO to determine whether the 12 18 percent benchmark continued to be 19 appropriate in light of the changed 20 financial and economic environments. In our 21 study for FSCO, we estimated ROE caps for 22 2013 ranging between 4.2 percent and 5.3 23 percent based on capital asset pricing 24 model". Now were you asked by the Public 25 Utilities Board in their questions whether</p>	<p style="text-align: right;">Page 204</p> <p>1 DR. LAZAR: 2 A. That was one of the questions. 3 STAMP, Q.C.: 4 Q. And did you have an answer? 5 DR. LAZAR: 6 A. I don't know. 7 STAMP, Q.C.: 8 Q. Of any? 9 DR. LAZAR: 10 A. No, no, I don't know if any are using it. 11 STAMP, Q.C.: 12 Q. Thank you, okay. Now to come back to what 13 you said here, you recommended to FSCO – I 14 take it this is a recommendation to FSCO, is 15 that what you were saying? 16 DR. LAZAR: 17 A. At that time, yes. 18 STAMP, Q.C.: 19 Q. And when I look at this paragraph, we saw on 20 your CV some reference to a 2015 report. Is 21 that what you mean by several years ago? 22 DR. LAZAR: 23 A. Where is this several years ago? 24 STAMP, Q.C.: 25 Q. In the part – you said several years –</p>

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1 DR. LAZAR:
 2 A. Oh, FSCO.
 3 STAMP, Q.C.:
 4 Q. I'm just wondering if you –
 5 DR. LAZAR:
 6 A. I think we did the work 2013.
 7 STAMP, Q.C.:
 8 Q. You had a report or something in your CV
 9 that spoke about a 2015 rate of return
 10 equity discussion for, I thought, FSCO. I'm
 11 wondering is what you're referring to –
 12 DR. LAZAR:
 13 A. There was a publication in 2015.
 14 STAMP, Q.C.:
 15 Q. Okay, is that the one?
 16 DR. LAZAR:
 17 A. No, but this FSCO is the work we actually
 18 did for FSCO.
 19 STAMP, Q.C.:
 20 Q. All right.
 21 DR. LAZAR:
 22 A. It wasn't published. It was internal to
 23 FSCO.
 24 STAMP, Q.C.:
 25 Q. Thank you. So in any event, you

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1 recommended, is that right, to FSCO that it
 2 be capped between 4.2 and 5.3?
 3 DR. LAZAR:
 4 A. No, we said those are the numbers we
 5 generated. What we recommended to FSCO is
 6 if they're going to use this model, then
 7 start it off as a ten year rolling average,
 8 so either you can go back and correct it, or
 9 use your 12 percent, which fell to 11
 10 percent, and then just adjust annually from
 11 that point onwards.
 12 STAMP, Q.C.:
 13 Q. And do I understand from your paragraph
 14 above that FSCO did not adopt your
 15 recommendations?
 16 DR. LAZAR:
 17 A. Well, they didn't.
 18 STAMP, Q.C.:
 19 Q. I just want to read your answer to the
 20 question I put to you a moment ago about the
 21 methodology, CAPM. Your answer at number
 22 five is, "There are no jurisdictions in
 23 Canada that rely on the methodology that we
 24 have used, which is the core of finance
 25 courses around the world. We can speculate

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1 as to the reasons for this, but based solely
 2 on our experiences with FSCO and the Ontario
 3 Energy Board, where we were retained to
 4 estimate appropriate ROE's for the regulated
 5 local electric utilities, the regulators
 6 succumbed to the pressures of the regulated
 7 industries". I take it that means you don't
 8 know of any where this is done for auto
 9 insurance?
 10 DR. LAZAR:
 11 A. I don't know.
 12 STAMP, Q.C.:
 13 Q. Thanks, Mr. Lazar.
 14 DR. LAZAR:
 15 A. But I know what happened in Ontario.
 16 STAMP, Q.C.:
 17 Q. Thanks very much. That's all the questions
 18 I have, thank you.
 19 DR. LAZAR:
 20 A. Okay.
 21 CHAIR:
 22 Q. Consumer advocate.
 23 BROWNE, Q.C.:
 24 Q. Thank you, Chair. Thank you, Dr. Lazar.
 25 Dr. Lazar, can we go to page 17 of your

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1 evidence.
 2 STAMP, Q.C.:
 3 Q. Evidence? Report?
 4 BROWNE, Q.C.:
 5 Q. Yeah, the report of July, 2018.
 6 DR. LAZAR:
 7 A. Yeah.
 8 BROWNE, Q.C.:
 9 Q. Okay, at page 17, and we see here sort of
 10 the genesis of where the rate of return
 11 comes from, which we're referring here, and
 12 we see down below in the 2005 decision for
 13 automobile insurance, PUB stated, and this
 14 is our PUB, Dr. Kalymon, I assume that's
 15 "Dr. Basil Kalymon, recommended a target ROE
 16 for setting automobile insurance of 9 to 10
 17 percent. "According to Dr. Kalymon, current
 18 30 year Canada Bond rates were at around 5.3
 19 percent, and 10 year Canada Bond rates were
 20 at 4.5 percent. Given that the long term
 21 market risk premium based on previous
 22 studies is around 4.6", that's combined the
 23 two, I guess, "and that the beta risk of
 24 insurance operations is around 1, Kalymon
 25 stated that the cost of equity capital for

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1 setting automobile insurance rates should be
 2 at 9.63 percent.
 3 BROWNE, Q.C.:
 4 Q. “And in considering the issue of the
 5 appropriate ROE for automobile insurance
 6 benchmark rates in the Province, the Board
 7 found Dr. Kalymon’s evidence and testimony
 8 most instructive and compelling” and went
 9 on, “the Board finds that an ROE of ten
 10 percent is reasonable for the use in
 11 determining the 2005 benchmark rates for
 12 automobile insurance.”
 13 Now, what are – this was 2005. Can you
 14 give us generally what happened to the 30-
 15 year Canada bond rate after that period and
 16 indeed the ten-year Canada bond? Can you
 17 give us some history of that?
 18 (1:45 p.m.)
 19 DR. LAZAR:
 20 A. Let me just go to – what rate did we use
 21 here. Okay. We wouldn’t use either of
 22 those, but nevertheless what happened from
 23 2005 to onwards, especially following
 24 September 2008 with the financial market
 25 collapse in prices, that interest rates,

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1 short, medium and long term collapsed. They
 2 all declined very sharply. And only in the
 3 past two or three years, the ten-year and
 4 the 30-year bond rates in Canada have edged
 5 upwards. They’ll still well below the five
 6 percent level in that period, you know, pre-
 7 2005. Short rates are still at historically
 8 low levels and somewhere in the one, one and
 9 a half percent range.
 10 BROWNE, Q.C.:
 11 Q. So, therefore, if these are the benchmarks
 12 for establishing the ROE and these factors
 13 are lower now, certainly you apply them,
 14 should we be having an ROE of ten percent?
 15 Would that be reasonable in the current
 16 environment? Just roughly.
 17 DR. LAZAR:
 18 A. Not at all. Even if you accept Professor
 19 Kalymon’s estimate of the beta, take his
 20 one, he never sort of calculated that. He
 21 just assumed that was the right value. We
 22 actually did calculate and came up with a
 23 lower value. But if you accept that, a
 24 value of one, and we’ve got in our Table 11
 25 what the risk premium has been averaged over

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1 the period 2011 to 2016, it’s 5.5 percent,
 2 so slightly higher than his number, and if
 3 you take the average of the risk-free rate
 4 that we use, which is about one and a half
 5 percent, add those two together and it gives
 6 you an upper limit of seven percent, which
 7 is -
 8 BROWNE, Q.C.:
 9 Q. So, the rate of return should have been
 10 closer to seven percent based on those
 11 values if you were to find -
 12 DR. LAZAR:
 13 A. Just on those values. If you take into
 14 account our calculations and that beta, it’s
 15 closer to six percent.
 16 BROWNE, Q.C.:
 17 Q. Now, there’s a general criticism of utility
 18 boards across the country, regulators across
 19 the country in reference to not accepting
 20 the new values of the new economy. I see
 21 you’re smiling there. In that rates of
 22 return seem to be set minus consideration of
 23 the long term Canada bonds and the ten-year
 24 bonds and indeed the interest rates. Do you
 25 have any comments on that?

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1 DR. LAZAR:
 2 A. Yeah. Both in the Ontario Energy Board case
 3 and the automobile insurance case with FSCO,
 4 the regulated companies argued quite
 5 vociferously this would be disastrous,
 6 they’ll pull out. They’re going to leave
 7 the industry. They’re going to leave the
 8 country. And the boards, in both cases,
 9 wasn’t really willing to challenge them,
 10 thinking “what if they do? Then we look
 11 rather stupid.” So, in both those cases,
 12 they capitulated, you know.
 13 Did they do the right thing or not?
 14 I’m not going to speculate on that. But
 15 that’s what happened. Those are the same
 16 argument in both cases, different types of
 17 companies, different industries, but with a
 18 threat that they were going to exit if the
 19 returns were too low. I personally didn’t
 20 think that would happen, but I didn’t offer
 21 that opinion. I’m not the one that had to
 22 make the final decision. And I didn’t have
 23 to report to political masters. So, it’s
 24 easy for me to say this is what it should
 25

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1 be.
 2 BROWNE, Q.C.:
 3 Q. And there's some thought that follows that
 4 that ratepayers haven't got the full value
 5 of this changing financial economy because
 6 boards have been reluctant to lower rates of
 7 return consistent with that economy. Is
 8 that a fair comment?
 9 DR. LAZAR:
 10 A. Absolutely, and that was the point I was
 11 trying to make in my repeated dissertations
 12 why we can quibble the numbers, but at the
 13 end of the day, there's a difference between
 14 the ROE that was allowed and the ROE that
 15 should have been allowed. That's one of the
 16 major issues.
 17 BROWNE, Q.C.:
 18 Q. And I know in this particular jurisdiction,
 19 at one point, at least for the energy
 20 utility, there was an automatic adjustment
 21 formula in place back – requested by the
 22 utility actually and brought evidence of how
 23 it would be more beneficial to us all, in
 24 1998, I do believe, 1999, and indeed, the
 25 Board implemented an automatic adjustment

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1 formula based on the long term Canada and
 2 the ten-year, an average of those, and plus
 3 put three percent on top of that which
 4 became the rate of return for the company.
 5 It set the range for the rate of return.
 6 And I remember anecdotally, the first
 7 year in which it was implemented, there was
 8 press releases from the utility saying how
 9 pleased they were because their rates went
 10 up. Well, lo and behold, then we got the
 11 new economy and all of a sudden, the
 12 automatic adjustment formula was no longer
 13 applicable to the utility. They said “we
 14 can't make any money like this”, when
 15 actually if it had to stay in place, we
 16 probably wouldn't be talking about the
 17 overcompensation and the rate of return of
 18 the insurance industry and perhaps, no
 19 doubt, of the utilities.
 20 Do you have any comment on the
 21 implementation of an automatic adjustment
 22 formula as opposed to going through these
 23 processes, based on the long term rate or
 24 the short term rate? Because the Canada
 25 bond really is what is the distinguishing

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1 feature.
 2 DR. LAZAR:
 3 A. I'm a firm supporter of simplicity.
 4 BROWNE, Q.C.:
 5 Q. Yes.
 6 DR. LAZAR:
 7 A. Hearings, there are times when they have
 8 values. Most often they're a monumental
 9 cost burden to everybody and simply a waste
 10 of time. I'm not a fan of meetings. I
 11 think issues can be resolved very quickly.
 12 So, is an automatic formula the way to go?
 13 Yes. You're going to need a hearing to
 14 determine what that formula should look
 15 like, what should go into it, and then it's
 16 on auto pilot.
 17 BROWNE, Q.C.:
 18 Q. Yes.
 19 DR. LAZAR:
 20 A. Period.
 21 BROWNE, Q.C.:
 22 Q. Because it seems to me that the regulators
 23 across the country have kowtowed to the
 24 regulated by compensating them more in this
 25 particular economy. Is that fair comment?

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1 DR. LAZAR:
 2 A. That's been the net result and it's not just
 3 Canada, but you see the same thing in the US
 4 as well.
 5 BROWNE, Q.C.:
 6 Q. Is there a role for the legislature in this?
 7 That the legislature should take note of the
 8 situation as it is and that rates could be
 9 set based on long term bonds and percentages
 10 and for them to give more direction to the
 11 regulator when setting rates of return in
 12 the interest of consumers generally?
 13 DR. LAZAR:
 14 A. Well, the government appoints the board,
 15 gives the board the mandate. Should the
 16 legislature pass a law saying there should
 17 be a set formula and then it should be on
 18 auto pilot thereafter? I think that they
 19 should. Then it would be up to the board to
 20 again have a hearing and determine the
 21 formula and the inputs into it.
 22 BROWNE, Q.C.:
 23 Q. Thank you, Dr. Lazar.
 24 CHAIR:
 25 Q. Any questions?

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1 COMMISSIONER OXFORD:
 2 Q. No.
 3 CHAIR:
 4 Q. Anything -
 5 MR. FELTHAM:
 6 Q. Just one to go back to – I’m not sure we
 7 have a fulsome answer on one question that
 8 was put to you by Mr. Stamp, Dr. Lazar, with
 9 respect to – the questions concerning can we
 10 take the numbers from Oliver Wyman, you
 11 know, and put those in; that that’s somehow
 12 going to change your opinion with respect to
 13 what the overpayment looks like. And you
 14 indicated “well, I’ve looked more closely at
 15 that and I’ve done some calculations to kind
 16 of get a sense of what that might be”, and I
 17 think it’s important that the Board hear
 18 from you on that point.
 19 DR. LAZAR:
 20 A. Okay. Again, there’s a simple formula for
 21 how you define profits, underwriting profits
 22 plus whatever investment returns there are.
 23 Simple formula for then determining what the
 24 return on equity, can play around with it,
 25 and what you get then is premiums depending

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1 upon key assumptions, such as operating
 2 expense, return investment, return on equity
 3 equals some multiple of whatever the claims
 4 are expected for that year. So, it’s a
 5 straightforward exercise. I’m quite happy
 6 to sort of write out the formula and send it
 7 along to you.
 8 But nevertheless, plugged in that
 9 formula and I just did some rough
 10 calculations and I said, okay, what if we
 11 take the Oliver Wyman assumptions as a
 12 starting point this is how premiums should
 13 have been set, and I used their expense
 14 ratio of 26 percent on average, four percent
 15 return on investment, ten percent return on
 16 equity. So, that would give us some
 17 multiple of premiums to whatever the claims
 18 are.
 19 And so, okay, now let’s adjust those.
 20 Let’s adjust – let’s take the 26 percent
 21 expense ratio, four percent return on
 22 investment and only change the return on
 23 equity. What difference does this make?
 24 And the difference is three percent of
 25 premium overpayments each year. So, just by

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1 changing return on equity from ten to six
 2 percent, accepting everything else in the
 3 Oliver Wyman report, we get overpayments of
 4 three percent year in year out.
 5 Now, what if we change – reduce the
 6 expense ratio? Take the four percent return
 7 on investment, the six percent return on
 8 equity, but we’re also reducing the expense
 9 ratio. What is the result? Now you get
 10 overpayments of five and a half percent per
 11 year. So, change that assumption. Well,
 12 now what if we go one step further, change
 13 expense ratio, change return on investment
 14 to six percent, the return on equity to six
 15 percent, what does this do? It increases
 16 the overpayments each year by six percent.
 17 So, ranges from three to six percent
 18 per year. What are the premiums on average
 19 here? They’re running around 300 million.
 20 Apply these numbers. So that means
 21 overpayments of 9 to 18 million per year at
 22 the current premium rate. Plain and simple.
 23 Doesn’t matter what the end profitability is
 24 of the insurance companies. If you plug in
 25 different expense ratios, different return

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1 on investments, more importantly different
 2 return on equity, you’re going to get
 3 overpayments. Everything else just becomes
 4 irrelevant noise.
 5 MR. FELTHAM:
 6 Q. Thank you.
 7 CHAIR:
 8 Q. Thank you, Mr. Feltham. Thank you very
 9 much, Dr. Lazar.
 10 DR. LAZAR:
 11 A. Oh, my pleasure.
 12 CHAIR:
 13 Q. Wish you safe travels home this evening.
 14 We’re back here tomorrow morning at nine
 15 with Dr. – please help me with his
 16 pronunciation.
 17 MR. FELTHAM:
 18 Q. Madam Chair, I think 9:00 we’re going to
 19 begin with the Consumer Advocate presenter.
 20 CHAIR:
 21 Q. Oh, we switched?
 22 MR. FELTHAM:
 23 Q. Yeah.
 24 CHAIR:
 25 Q. Okay. All right.

<p style="text-align: right;">Page 221</p> <p>1 MR. WADDEN: 2 Q. Yeah, if that's okay, Madam Chair. What 3 we'll do is we'll start with Mr. Donaher at 4 nine. I know the Campaign was interested in 5 knowing how long that would take. 6 CHAIR: 7 Q. Absolutely. 8 MR. WADDEN: 9 Q. But I mean, Mr. Donaher is not putting 10 forward any contentious information or 11 evidence, I don't anticipate, so I think by 12 the time we're finished with him, assuming 13 there's some questions from around the room, 14 including yourselves, I suspect an hour 15 would be find for Mr. Donaher, if they want 16 to give Mr. Blidook some idea of when to 17 come in. 18 CHAIR: 19 Q. Will that be enough time to deal with Dr. 20 Blidook? 21 MR. FELTHAM: 22 Q. I understand Professor Blidook will be here 23 at 9:30. 24 CHAIR: 25 Q. Okay.</p>	<p style="text-align: right;">Page 223</p> <p style="text-align: center;">CERTIFICATE</p> <p>I, Judy Moss, hereby certify that the foregoing is a true and correct transcript in the matter of the 2017 Automobile Insurance Review heard before the Board of Commissioners of Public Utilities, 120 Torbay Road, St. John's, Newfoundland and Labrador and was transcribed by me to the best of my ability by means of a sound apparatus.</p> <p>Dated at St. John's, Newfoundland and Labrador this 13th day of September, 2018</p> <p>Judy Moss</p>
<p style="text-align: right;">Page 222</p> <p>1 MR. FELTHAM: 2 Q. So, he has some flexibility. 3 CHAIR: 4 Q. That does give us time to finish? 5 MR. FELTHAM: 6 Q. I hope so. 7 CHAIR: 8 Q. Okay. All right. Have a nice evening 9 everyone. 10 UPON CONCLUSION AT 2:00 P.M. 11 12 13 14 15 16 17 18 19 20 21 22 23 24 25</p>	

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