Newfoundland & Labrador

BOARD OF COMMISSIONERS OF PUBLIC UTILITIES

IN THE MATTER OF AN

APPLICATION BY FACILITY ASSOCIATION FOR APPROVAL OF REVISED RATES AND RULE CHANGES FOR ITS NEWFOUNDLAND AND LABRADOR PUBLIC VEHICLES – TAXIS AND LIMOUSINES CLASS OF BUSINESS

DECISION AND ORDER OF THE BOARD

ORDER NO. A.I. 11(2015)

BEFORE:

Andy Wells
Chair and Chief Executive Officer

Darlene Whalen, P. Eng.
Vice-Chair

Dwanda Newman, LL.B.
Commissioner

James Oxford
Commissioner

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BOARD OF COMMISSIONERS OF PUBLIC UTILITIES

AN ORDER OF THE BOARD

NO. A.I. 11(2015)

IN THE MATTER OF the *Automobile Insurance Act*, RSNL 1990, c. A-22, as amended; and

IN THE MATTER OF an application by Facility Association for approval of revised rates and rule changes for its Newfoundland and Labrador Public Vehicles – Taxis and Limousines class of business.

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TABLE OF CONTENTS

1. The Application

Facility Association ("Facility"), as operator of the residual market mechanism for automobile insurance in the Province, filed a Category 2 application on March 6, 2014 seeking approval of increased rates for its Newfoundland and Labrador Public Vehicles – Taxis and Limousines ("Taxis") class of business (the "Application"). The Application proposes rate increases for Third Party Liability, Accident Benefits and Uninsured Automobile coverages, to be effective no earlier than August 1, 2014, as follows:

Facility Association Proposed Taxi Rate Increases[1]			
	Third Party Liability	**Accident Benefits**	**Uninsured Automobile**
Proposed % Increase	+50.0%	+294.3%	+329.3%
Proposed Average $ Increase	+$1,417	+$235	+$46

Facility estimates that its Application proposals, if approved, will result in an increase of 54.1% in its overall rate level for all coverages combined, including Physical Damage. The Application also proposes a number of additional changes, including increased limits for Third Party Liability and Physical Damage coverages, elimination of certain discounts, rating amendments and other rule changes.

2. Procedural Matters

Notice of the Application was provided directly to policyholders and published in newspapers beginning March 26, 2014. Copies of the Application and supporting documentation were made available on the Board's website.

The Board's actuarial consultants, Oliver Wyman Limited ("Oliver Wyman"), filed a report on May 9, 2014, which was finalized on May 16, 2014, outlining its review of the actuarial justification provided in the Application. Facility responded to Oliver Wyman's report on May 14, 2014.

On May 1, 2014 Thomas Johnson notified the Board that, pursuant to his appointment under section 61 of the *Automobile Insurance Act*, he would be acting as Consumer Advocate in the proceeding, representing the interests of automobile insurance customers.

A Notice of Hearing was published in newspapers throughout the Province starting July 9, 2014 inviting intervenor submissions, comments and presentations.

On July 24, 2014 Thomas Johnson filed an intervenor submission as Consumer Advocate.

[1] Proposed average increase as shown in Facility's cover letter to the Application. Individual policyholder increases will vary depending on coverage level and driving record

As a result of the direct and published notices the Board received 14 written comments on the Application proposals, primarily from taxi operators and/or drivers.

A number of information requests were issued by the Board and the Consumer Advocate, all of which were responded to by October 29, 2014.

A Notice of Hearing Date was published starting on October 13, 2014. The hearing of the Application was scheduled to begin on Wednesday, November 5, 2014 at the Board's office in St. John's. The public hearing was held over a five-day period November 5-7, 2014 and November 17-18, 2014.

At the hearing Facility was represented by counsel, Kevin Stamp, Q.C. and Jennifer Newbury. The Board was assisted by its counsel, Jacqueline Glynn, and Cheryl Blundon, Board Secretary. The Consumer Advocate, Thomas Johnson, Q.C. was assisted by his counsel Thomas Williams, Q.C.

Shawn Doherty, FCAS, FCIA, Facility's Senior Vice President of Actuarial Services and Chief Financial Officer, and Paula Elliott, FCAS, FCIA, Oliver Wyman's Principal Actuary, provided expert testimony.

The Board also heard presentations from Doug McCarthy of St. John's Taxi Co-operative Society Limited and Todd Edmunds of Star Taxi in Corner Brook.

Written submissions were filed by Facility and the Consumer Advocate on January 9, 2015 and reply submissions were filed by both on January 14, 2015.

3. Background

i) Legislation

Facility was established under section 97 of the *Insurance Companies Act* as an unincorporated non-profit association of insurers. Under subsection 98(2) Facility is required to establish a Plan of Operation: a) to provide automobile insurance to owners and licensed operators of automobiles who would otherwise be unable to obtain that insurance; and b) to provide, in accordance with sections 45.1 and 45.21 of the *Automobile Insurance Act*, payment with respect to claims for damages made by persons who are not insured under a contract within the meaning of section 33 of the *Automobile Insurance Act* and who have no other insurance or who have other insurance that is inadequate with respect to the damages claimed.

Pursuant to section 102 of the *Insurance Companies Act* Facility is required to file automobile insurance rates with the Board and the Board is required to address the rate filing as set out in the *Automobile Insurance Act* and the regulations thereunder. The legislation sets out how the Board is required to assess a proposed rate, and specifically the grounds upon which the Board is required to assess a rate increase. Section 8 of the regulations requires the Board to determine if a proposed rate is too high:

8. (1) Where a rate filed by an insurer under section 51 of the Act constitutes an increase in a rate previously filed, the board shall determine if the proposed rate is too high.

(2) The board shall vary or prohibit a rate that it determines is too high.

(3) A rate approved by the board comes into effect on the date approved by the board.

Section 11 of the regulations states:

11.(1) For the purpose of subsections 7(1), 8(1) and 10(1), the board shall determine if the insurer's proposed rate is in excess of that which is required or justified on the basis of the insurer's projected loss experience, expenses and investment income for its automobile insurance business for the province and other elements considered appropriate by the board.

(2) The board shall in its determination under subsection (1) ensure that the projected loss experience takes into account the insurer's loss experience in the province where that experience is relevant, adequate or otherwise reasonable for use in establishing rates.

(3) Where the board determines that an insurer's loss experience in the province is not relevant, inadequate or otherwise unreasonable for use in establishing rates, the board shall determine the elements and information upon which an insurer shall file its projected loss experience with the board.

ii) Filing Guidelines and Directives

The Board issues Filing Guidelines for automobile insurance rates in the Province, setting out the information requirements that must accompany all filings for Private Passenger, Commercial and Miscellaneous automobile insurance rates. The Filing Guidelines are made available to all insurers currently writing or planning to write automobile insurance in the Province.[2]

As part of the Filing Guidelines the Board also publishes guideline loss trend rates that may be used by insurers in rate filings without the need for further actuarial supporting analysis. These loss trend rates are developed by the Board's consulting actuaries and are updated by half-year as new Industry Newfoundland and Labrador data is made available by the General Insurance Statistical Agency ("GISA"). The Board forwards the new loss trend rates to the Industry for comment and, upon acceptance by the Board, the loss trend rates are issued in a Directive and may be used by insurers in rate filings. If an insurer wishes to use alternate loss trend rates other than those provided by the Board the Filing Guidelines state that it must provide "*satisfactory data supporting their chosen factors and rationale why their selected factors are more appropriate for use by the insurer*."

The Filing Guidelines set out that, where a filing contemplates changes to base rates or other factors that result in an increase in any rate for any coverage for any insured, the filing is considered a Category 2 filing and prior approval is required. In order to satisfy the legislative provisions, a Category 2 rate filing must include an actuarial memorandum that provides a general description of the rate indication methodology as well as a discussion of each

[2] The most recent Filing Guidelines were issued September 1, 2011 and are available on the Board's website at http://www.pub.nl.ca/down/2011FilingGuidelines.pdf

consideration in the rate indication methodology. The rate analysis must include a clear explanation of the approach and data used, the rationale for each key assumption made and the reasons for any changes in methodology or judgements from those in the company's last approved rate filing. In no case does the Board accept a rate proposal for a coverage that is higher than the supported rate level need for that coverage.

The Filing Guidelines are intended to support efficiency and consistency in the regulation of automobile insurance rates in the Province. The Newfoundland and Labrador loss experience can be limited due to the small number of insureds, and particularly when looking at the experience of individual companies. Issuing acceptable trend rates based on Industry data provides an option for those insurers without company specific experience to justify a filing proposal and for insurers who may wish to avoid the costs associated with conducting a full loss trend analysis.

iii) Facility's 2013 Application

The last Category 2 application by Facility for its Taxis class of business was made on January 24, 2013, requesting approval of increased rates for Third Party Liability, Accident Benefits and Uninsured Auto coverages. In that application Facility proposed an increase of 50% in rates for Third Party Liability, and an increase of 100% in rates for both Accident Benefits and Uninsured Automobile. While the review by the Board's actuaries identified some issues for the Board's consideration, Facility's proposed rates were not found to be too high based on the justification provided. In Order No. A.I. 9(2013) the Board approved the rate proposal from Facility for its Taxis class of business, with new rates effective August 1, 2013.

4. Review of Application

Facility's rate indications and proposed rate changes are shown below:[3]

Coverage	Facility Rate Indication[4]	Facility Proposed Rate Changes
Third Party Liability	+67.3%	+50.0%
Accident Benefits	+294.3%	+294.3%
Uninsured Automobile	+329.3%	+329.3%
Physical Damage[5]	-9.1%	0%
Total	+69.7%	+54.1%

Facility proposes to limit the Third Party Liability rate change to +50.0%. The Physical Damage coverage is rated as a percentage of Facility's Private Passenger Physical Damage rates. This multiplier is currently set at 225% and is not proposed to change.

In its report Oliver Wyman identified issues and considerations for the Board with respect to Facility's methods and assumptions used for: i) the loss trend rates; ii) the full credibility standard for Third Party Liability; iii) the basis for the complement of credibility; iv) the Health

[3] Facility's Actuarial Memorandum, Section 2, page 31

[4] Assuming 2.8% ROI and 0% ROE

[5] Includes Collision, Comprehensive, Specified Perils and All Perils

Levy; and, v) the return on investment provision (ROI). The assumptions and methods used for all other parameters were found to be reasonable on the basis proposed and/or in accordance with the Filing Guidelines.

Based on its review Oliver Wyman found that Facility's indicated and proposed rate level changes for Third Party Liability, Accident Benefits and Uninsured Automobile are higher than the rate level changes calculated using the Board's Filing Guidelines and alternate assumptions. By substituting alternative assumptions within the Board's Filing Guidelines Oliver Wyman estimates a rate level need of +21.5% as shown below:

Coverages	**Facility Rate Indication**[6]	**Oliver Wyman's Indication**[7]
Third Party Liability	+67.3%	+19.8%
Accident Benefits	+294.3%	+125.4%
Uninsured Auto	+329.3%	+132.8%
Independently Rated Coverages Total	+73.5%	+21.5%[8]

Oliver Wyman also noted that Facility made a number of material changes in the approach and assumptions used in its prior rate application filed in 2013 which affect the rate level indications. These relate primarily to the loss trend rate selection process, the standard for full credibility and the complement of credibility. Other changes relate to the treatment of certain expenses such as service carrier fees, excess legal fees and unallocated loss adjustment expenses.

5. Public Presentations and Comments

At the start of the hearing on November 5, 2014 the Board heard presentations from Doug McCarthy on behalf of the St. John's Taxi Co-operative Society Limited and Todd Edmunds of Star Taxi in Corner Brook.

Mr. McCarthy explained that he represents the majority of the industry in St. John's as their spokesperson. Mr. McCarthy stated that, if the rate increase proposed by Facility is approved, it would have a dramatic impact on the overall industry, as well as the economy of the Province. Mr. McCarthy explained that the rate increase granted last year was a surprise to the industry and was enough to force some marginal operators to retire from the industry. He questioned the factors that are driving the cost increases, such as claims settling costs, and whether the taxi industry was being fairly treated. He acknowledged that the taxi industry is a high risk business but suggested that his insurance rates should be based on him as an individual and not what he does for a living. Mr. McCarthy states that, as a taxi operator, it doesn't matter if he has not had an accident or a claim for 25 years since he will still be classified as high risk, which he queried

[6] Assuming 2.8% ROI and 0% ROE

[7] Assuming Board's Guideline Commercial Vehicle loss trends, ROI of 2.8%, ROE of 0%, a Health Levy provision of $26.44 per vehicle, and Facility's standard of full credibility and complement of credibility selections from its 2013 Taxi application

[8] Indication reduced by approximately 1% due to error discovered – CA-FA-01 and Transcript, November 17, 2014, page 3

was just another form of discrimination. Mr. McCarthy agreed that increased costs have to be passed on but concluded:

> Facility has failed to cover their losses in the past and now they seem to want to play catch up at our expense. If it is because of a management issue, then Facility should get their own house in order before they burden the industry with rates that may force many of us from the business and have an overall impact on the provincial economy. Thank you very much.[9]

Mr. Edmunds represented Star Taxi in Corner Brook and spoke to the impact of the last Facility rate increase, stating that it drove the insurance cost for his cars from $1,206 per car to $3,021 per car. According to Mr. Edmunds this resulted in him having to remove seven cars from his fleet and three independents also removed their cars. He questioned Facility's commitment to keep costs down. He closed by stating that his expenses keep going up and, with no way to get his money back, another rate increase is *"probably going to put us out of business, that's all I can say."*

The Board also received several written comments, generally from taxi operators expressing concerns regarding the negative impacts that the proposed rate increase would have on the taxi industry in the Province.

6. Board Findings

The Board is cognizant that there are a wide range of possible outcomes in any prospective ratemaking exercise. The Board must be satisfied that the proposed rate changes are supported based on the information filed. This does not necessitate that Facility's proposed rate changes be in-line with those calculated by Oliver Wyman, but the Board does consider the findings of Oliver Wyman in assessing whether the proposed rates are too high. The Board will look to the professional judgement of the actuaries, as well as the support and explanation for their respective positions, to determine if the proposed rates are too high in the circumstance. The Board notes that neither Mr. Doherty of Facility nor Ms. Elliott of Oliver Wyman took the position that each other's work was unreasonable or contrary to actuarial practice standards.

The Consumer Advocate submits that the central theme in this proceeding and indeed the central reason for the differences between the estimates of rate level need offered by Oliver Wyman and Facility involves the exercise of "actuarial judgment".[10] The Board agrees with this assessment and accepts that actuarial analysis is not an exact science but instead relies on the experience and training of the actuary to apply judgment to the results of any analysis. This is the foundation of insurance ratemaking.

The Board has reviewed the record of the proceeding, including Facility's Actuarial Memorandum, Oliver Wyman's report on its review of the Application, Facility's responses to Oliver Wyman's report and the information requests, as well as the hearing transcripts and submissions. The issues to be addressed are : i) data limitations; ii) loss development factors; iii) loss trend rates; iv) full credibility standard; v) complement of credibility; vi) Health Levy; vii)

[9] Transcript, May 5, 2015, page 15
[10] Consumer Advocate Submission, January 9, 2015, page 11

expense provision; viii) Physical Damage coverages; ix) territorial differentiation; and, x) proposed rule changes. These issues, along with the Board's findings on each, are discussed in the following sections.

6.1 Data Limitations

A key issue for the Board in this Application relates to the data used as the basis for the analyses and determination of indicated rate levels. The legislation directs that the Board's determination in relation to a proposed rate increase is to be made on the basis of the insurer's projected loss experience, expenses and investment income. Where the Board determines that the insurer's loss experience is inadequate the Board is required to determine the basis upon which an insurer shall file its proposal. The Board's Filing Guidelines set out trend rates based on Industry data which may be used by insurers without the requirement for additional supporting data or justification.[11]

Given the small number of taxis insured in Newfoundland and Labrador,[12] both Facility and Oliver Wyman used alternative data sources in addition to the Taxis experience in the analyses and determination of indicated rate levels. Facility acknowledged the data limitations, stating:

> We relied on industry data because a sufficient volume of stable and credible historical experience does not exist for FA for the purpose of selecting trends by sub-coverage. We believe it is reasonable to assume that the factors that affect industry loss costs similarly affect FA, and therefore that trend structures estimated for the industry are applicable to FA.[13]

In its report Oliver Wyman addresses the data limitations:[14]

1. Facility's Taxis experience is not statistically credible due to the low number of data points.
2. The loss development factors selected by Facility are based on its non-Private Passenger Vehicle[15] experience through December 31, 2012, as opposed to Taxis-only experience. This requires an assumption that the split between Bodily Injury and Property Damages losses for non-Private Passenger Vehicles for each accident year is the same as for Taxis, which Oliver Wyman suggests is unlikely to be the case.
3. The claim count development factors used by Facility to estimate the ultimate number of claims for its Taxis class of business for each of the accident years in the experience period are based on Industry Commercial Vehicle data as of December 31, 2012, which does not include Taxis experience. Oliver Wyman notes that the claim count development pattern for Industry Commercial Vehicles may be different than for Facility Taxis.

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[11] As per the Board's Filing Guidelines, page A-3

[12] Facility reports 816 written Taxi exposures as of December 31, 2012 (Actuarial Memorandum, Exh-C1, line 1)

[13] Facility Actuarial Memorandum, Section 2, page 11

[14] Oliver Wyman Report, May 16, 2014, pages 20-22

[15] Non Private Passenger Vehicle includes all vehicles except private passenger (e.g. commercial, motorcycles, taxis, etc.). Mr. Doherty suggest that 2/3 of these claims are probably taxis (Transcript, November 7, 2014, page 114)

4. Loss trend rates are developed using the Industry Commercial Vehicle experience through December 31, 2012 rather than Industry Taxis experience. As with the loss development factors the selected trend rates for Bodily Injury and Property Damage based on this data must be combined since the Third Party Liability loss experience for Taxis is not available separately for Bodily Injury and Property Damage.

During the hearing Ms. Elliott further described the impact of the data limitations on the statistical analyses undertaken by both actuaries to determine loss development factors and loss trend rates used to predict future costs and therefore premium requirements:

> ...Any of the statistics that are presented by anybody, FA or Oliver Wyman, are not strong statistics. We're dealing with very few claims. So the statistics presented by FA for its models are not strong, and I can assure you if I presented statistics for any of the runs that we do, they're not going to be strong either. We only have a few claims every year. There is no way you're going to get strong statistics.[16]

During the hearing, in responding to a question from Facility's counsel on the subject of data exclusions in selecting trend rates, Ms. Elliott commented:

> Here with this commercial data in Newfoundland it is the most challenging data that we look at. Of all the reviews for lost trend rates, it is the most challenging. It is the most limited data. And so this is the approach that we've taken to try to account for this volatility in this limited database that we have work with.[17]

In discussing the issue of the credibility standard Ms. Elliott commented:

> The standard for determining whether data is sufficient for credibility, the credibility standard is much higher than just for the regular experience that's used. This data would not meet the standard that we see in other provinces. And I'm repeating myself, the data is very thin, very volatile and not reliable in terms of the estimate that is provided. So if you're asking me do I think this data is fully credible and reliable, that whatever trend result pops out of the XL *[sic]* model, is the right number? The answer is no. It is not fully credible, absolutely not.[18]

The Board believes that data limitations are a significant factor in its evaluation of Facility's rate proposal.

6.2 Loss Development Factors

Facility uses its Newfoundland and Labrador experience for non-Private Passenger Vehicles to select loss development factors which are then applied to Facility's reported incurred losses for Taxis in Newfoundland and Labrador. Loss development factors were calculated as the ratio of the valuation selected ultimate indemnity amount to the recorded indemnity amount as of December 31, 2012 for each different year.

[16] Transcript, November 18, 2014, page 153
[17] Transcript, November 17, 2014, page 177
[18] Transcript, November 17, 2014, pages 178-179

Although Facility's approach was based on different assumptions and methodologies the Oliver Wyman report confirms that Facility's selected loss development factors are reasonable, except in relation to Accident Benefits. Oliver Wyman suggests that Facility's Accident Benefits selections for periods 18-24 months and 48-54 months are higher than suggested by historical data.[19] During the hearing Ms. Elliott explained the impact of the use by Facility of higher selected loss development factors on Accident Benefits loss trend rates and rate indications:

> ...although accident benefits is a small coverage, there are some larger differences there. And in this case here, I believe that these larger factors that FA is selecting, that are generally larger than if they had used their own experience, it's leading to higher loss development factors that are leading to higher loss trend rates and a higher rate indication, yeah.[20]

Facility states that there is no evidence to suggest that the loss development factors used in Facility's rate indications are unreasonable or that using only Taxis data as the basis for loss development factor selection would reduce the overall level of uncertainty of Facility's rate indication. In addition Facility submits that there is no evidence to suggest there is an available set of data that would produce more suitable loss development.[21] The Consumer Advocate did not make submissions on Facility's selected loss development factors.

The Board accepts that Facility's Accident Benefits selections for two periods are higher than suggested by historical data. Facility explained the basis for these selections as being the result of combining the experience of the Atlantic Provinces to improve the credibility of the estimates.[22] The Board is satisfied that Facility has justified its approach in the circumstances.

The Board finds that Facility has justified the proposed loss development factors.

6.3 Loss Trend Rates

Loss trend rates are applied to the experience period incurred losses to adjust for the cost levels that are anticipated during the policy period covered by the proposed rates. The selection of the appropriate loss trend rate by coverage is a matter of actuarial judgment in the statistical analysis of the underlying data. In this Application the issue of the selection of the appropriate loss trend rate accounts for a significant variation in the rate indications of Facility and Oliver Wyman. While both Oliver Wyman and Facility use the same Newfoundland and Labrador Industry Commercial Vehicle data the trend rates selected by each are different, as shown below:[23]

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[19] Oliver Wyman Report, May 16, 2014, pages 10-11

[20] Transcript, November 17, 2014, page 49

[21] Facility Submission, January 9, 2015, page 9-10

[22] Undertakings #11 and #12

[23] Facility's Actuarial Memorandum, Section 2, page 12; Oliver Wyman's May 16, 2014 report, May 16, 2014, page 9

Loss Trend Rate Selections		
Coverage	**Facility Selected Loss Trend Rate**	**Oliver Wyman Selected Loss Trend Rate**
TPL Bodily Injury	+4.4%	-1.5%
TPL Property Damage	+2.4%	0.0%
Accident Benefits	+7.6%	+1.0%

Facility separately determines its frequency and severity trend rates for each coverage based on its regression analysis of the Industry Commercial Vehicle ultimate losses and claim counts by accident half-year over the 20-year period ending December 31, 2012. Based on the regression analysis results Facility split the data into two line periods, changing at 2004-H2 to reflect a change in trend. The selected frequency and severity trend rates for each of the coverages are then combined to produce loss cost trend rates for Bodily Injury, Property Damage and Accident Benefits.

Oliver Wyman uses the Board's Guideline loss trend rates as published in Board Directive A.I. 2013-02. The Board's Guideline loss trend rates are based on a loss trend analysis completed by Oliver Wyman using the Industry Commercial Vehicle experience data as of December 31, 2012.

In its report Oliver Wyman identifies several areas of difference in Facility's selected loss trend rates and the Board's Guideline loss trend rates.[24] Two specific areas highlighted by Oliver Wyman include the use by Facility of a 20-year time period in its loss trend rate analysis and the finding by Facility of a reform factor in the 2004-H2 data period.

Facility uses a 20-year period (1993-H1 to 2012-H2) for its regression analyses in selecting its loss trend rates to be applied to its 2008-2012 experience period to arrive at rate indications for each coverage. Ms. Elliott expressed her opinion that a 20-year time period is too long to select loss trend rates to apply to the 2008-2012 period:

> There is a point in time where you begin to question what am I measuring back from 1993 to 1998--that's sort of the first of the five of the 20 years that is presented by FA. You know, I'm sure I said yesterday there's no harm in looking at it, that's fine, but when you go back to 1993 and 1998 and you have to ask yourself is what's happening there relevant to 2015--like where do you draw the line? We could go back 25 years, and is that really relevant? And so the actuary has to make some judgment where you draw the line of what you're going to include in your loss trend model, and if we had 20 years of really solid, stable data, yeah, you could run that and you could run five years and say, gee, I get the same answer, you know, I'm getting a really good fit. That's not the case here, and I had presented--we went through with the yellow highlights yesterday how it went up and down and up an *[sic]* down, and having more of that noisy data, volatile data, am I really going to get an answer over 20 years? I'm not certain of that. I'm not certain you get a better answer using more data that's highly uncertain.[25]

[24] Oliver Wyman Report, May 16, 2014, page 10

[25] Transcript, November 18, 2014, pages 60-61

Mr. Doherty explained Facility's reasoning for the use of a 20-year time period in its loss trend regression analysis:

> ...The reason we use a 20-year period is because if there is one trend over that 20-year period, you're going to get a better estimate of that trend if you use all 40 data points as opposed to using only the most recent 16 or 20 or 10 data points. That's the nature of the statistical process that we go through. Using a 20-year period allows us not only to identify through statistical analysis areas where or periods where potential trend rates have changed over that period, it also at times gives us insight into our ability to identify where things are changing and test for those.[26]

Mr. Doherty explained that, while 20 years of data was used for the trend analysis, the trend period used for rate indications is actually an eight-year period post-2004.[27]

The second area highlighted by Oliver Wyman with respect to Facility's selected loss trend rates relates to the bifurcation by Facility of the data trend starting at 2004-H2. In its Actuarial Memorandum, when describing the selections of the past and future loss trends for Bodily Injury severity and frequency, Facility states: "*...we believe the best split to be two time periods (changing at 2004-H2) to reflect the product reform, with the "past trend" ending 2012-H2 and "future trend" starting 2013-H1.*"[28] A similar statement attributing the data split to product reform is included with Facility's descriptions of the trend selections for Property Damage, Accident Benefits and Uninsured Auto.

In its report Oliver Wyman states that Facility's regression model estimates the August 2004 reforms resulted in a reduction in Industry Commercial Vehicle loss costs for Bodily Injury, Property Damage and Accident Benefits. With respect to the trend selection for Bodily Injury Oliver Wyman stated:

> *From the regression model selected by FA, FA estimates the August 2004 reforms resulted in a reduction in Industry CV loss costs for BI of 37.1% (split between frequency at -27.2% and severity at -13.6%). We do not find this estimate to be reasonable. We observe that frequency began its decline well before the 2004 reforms were introduced, and we do not find evidence that the $2,500 deductible on non-pecuniary loss amounts introduced in August 2004 had a measurable impact on Industry CV loss costs (but possibly contributed to reducing the loss trend rate). In its prior filing FA did not include a parameter in its regression model for the August 2004 reforms, so this represents a change from the prior filing - although FA states this reform estimate is not important to its findings.*[29]

Oliver Wyman makes a similar finding with respect to Property Damage and Accident Benefits, where Facility estimates reductions in loss costs of 17.2% and 72.6% respectively. As a result of these reductions Facility applies a bifurcation to its selected trend line starting at the second half of 2004.[30]

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[26] Transcript, November 6, 2014, pages 135-137

[27] Transcript, November 6, 2014, page 65

[28] Facility Actuarial Memorandum, Section II, pages 13-14

[29] Oliver Wyman Report, May 16, 2014, page 11

[30] Oliver Wyman Report, May 16, 2014, pages 11-14

In its response to the Oliver Wyman report Facility states:

The decrease noted is determined from the fitted regression above and we believe it is reasonable (given our selected periods, the regression fit of the data itself determines the drop at 2004-H2; we are not able to specify the extent to which this is directly related to the reform or to any other cause). [31]

Facility further states in the same response:

As the major component of the 2004 reform was the introduction of a deductible, we believe it not only reasonable, but should be expected, that a one-time impact would manifest itself (as we believe it does). A deductible where one did not exist before will take claims dollars out of the loss costs.

Mr. Doherty explained Facility's conclusion that there was a change in 2004-H2 and how he approached the analysis of the data to arrive at a bifurcation due to a change in trend post-August 2004, stating:

I think I can see something that perhaps other people aren't seeing, but I still believe that there are two different periods that are reflective of trends in this loss cost data, and we'll get into that in a minute, but maybe we'll just slide up for the frequency for a second. Now when we were looking at this, and I think it will become more evident if you start looking at the other piece, there appears, in my mind, to be two distinct periods, and we know that there is a reform that occurred in 2004. [32]

Mr. Doherty also commented:

I'm just looking at the data, and so I see a bifurcation occurring at a point in time. It may be because of the 2004 reforms, maybe not. Oliver Wyman may have done a study that focused – like, maybe a closed claim study or something like that that says we actually looked at the claims settlements related to non-pecuniary losses and the application of deductible pre and post the 2004 reform, and we've determined based on a separate study that there is, in fact, no change in the outcomes. I don't know, they may have done something like that. Maybe that's how they determined that for their view the 2004 reforms had no impact on loss cost, and that's fine, I don't know, I'm not aware of any study like that. We certainly did not do a study. All we did was said, look, we're looking at the data, and it appears that they agree at least in terms of frequency, there was a change in frequency. So we're attributing that change in frequency as initial estimate due to the reforms, so it was going up. If frequency continued to go up, you would have been up here, but it started to go down, so we measured the gap between those two and that gap, as they point out here, was 27.2 percent drop, and then it continues to go from there. On the severity, we saw the same thing. Severity was going up and it went up more, and so again we looked at where it was going to go, and then compared along one trend line and then the other trend line, and just compared the values to come up with that. Is it because of the change in deductible; I don't know. Does it have anything at all to do with the reforms or was it just coincidental; maybe, I don't know. All I know is the

[31] Facility's response to the Oliver Wyman Report, page 9
[32] Transcript, November 5, 2014, pages 100-101

data is telling me something happened, there's a change, you should reflect the change, it's valid, so I did.[33]

According to Mr. Doherty Facility's selected trend rates, using the bifurcated data, better reflect the Newfoundland and Labrador experience:

> ...So our assessment of the Newfoundland industry commercial, using our bifurcation of periods and coming up with our estimates of what was happening with loss cost over that period, it seemed to look something like what we were seeing happen with the taxis, and I'm looking at that and it seems – to me, it seems to fit better....Certainly, for me, it looks like a heck of a lot more like the commercial experience for the industry, which is why we picked it, and doing the same thing for each of the other coverages, you get the same result. I believe our trend better reflects the experience for taxis, I think it better reflects the experience of the commercial vehicles in Newfoundland.[34]

Ms. Elliott explained how Facility's selected trend rate was affected by the inclusion of a bifurcation:

> It's my opinion that FA's selected loss trend rate of +4.4 percent is premised on using the period 2004-2 to 2012-2. There's an exclusion of a very high point in there, which I believe is 2012--2011-2, a high point, but they derive this 4.4 percent starting with 2004-2 and it's my view that because they use that time period, and because the first two accident half years in that time period are quite low, it drives up--so they start at a low point and end up here, and they end up with this +4.4 percent.[35]
>
> If FA had used one less year of data and started with 2005-2, they would get a couple of point percentage drop in their trend rate. And if they bought into the common acceptance that the reforms did not affect cost to a material or measurable degree, if they had used a ten-year period, if they had used the modified loss adjustment expenses--sorry, loss development factors that I refer to, they would have a much lower loss trend rate.[36]

Ms. Elliott also explained why she considered Facility's findings with respect to a reform factor to be not fully supported:

> Well, we have—we review the rate filings on behalf of the Board and we have not seen that in other rate filings. In FA's own rate filing last year for taxis, they assume that the reforms had no impact on the cost. So this is a complete turnabout by FA, that it now sees these reform savings from the 2004 reforms, or something in 2004, and you know, saying—and I'm repeating what I said earlier, but saying that there's this sustained drop from these reforms moving forward, that everything shifted down, we don't find that to be intuitively reasonable. I can't explain to anyone why that would be the case, it doesn't need—the reforms were for two hundred and fifty—sorry, $2,500 deductible on all BI claimed and some other minor changes. I can't think of any other event in the second half of 2004 that

[33] Transcript, November 6, 2014, pages 72-73
[34] Transcript, November 6, 2014, pages 61-62
[35] Transcript, November 18, 2014, pages 159-160
[36] Transcript, November 18, 2014, pages 160-161

> would cause AB cost to decrease by 73 percent; the reforms weren't for AB. I just don't find it intuitively reasonable, no.[37]

In relation to whether the reforms resulted in a reduction in loss costs, Ms. Elliott stated:

> That's not evident in the private passenger data at all. We're not seeing that. You know, in any of the tests that have been run, it is not there...what's being provided with significant savings in commercial of 37 percent on BI and 73 percent on AB, there's a flaw in the model.[38]

Ms. Elliott further stated:

> ...with private passenger auto experience, the severity, the P-tests and T-tests show you there was no impact, and so you have to say with a larger body of data in Newfoundland, the same cars on the same roads in Newfoundland, and there's no savings on private passenger data which is more stable, not as volatile as the commercial data, we're not seeing it there. Then you look at a small volume of commercial data, which is very volatile, and here is says there's a 37 percent savings. That just doesn't make any intuitive sense at all.[39]

With respect to the statistical measures Facility provided as support for it's loss trend rate selections, Ms. Elliott stated:

> You can look at statistics all you like. I'm an actuary, I look at statistics and they have value, but you have to look at it: are they reasonable? And a really good case in point is you look at the P-test and the T-test for the reform factor that FA has presented—we're not going to pull those up on the screen and look at them, but FA is saying that these P-tests and T-tests are statistically, you know, significant, and I'm going to accept that, and I don't agree with that approach. I look at it and say does this make intuitive sense? Is it reasonable? Can I really tell a consumer that your costs reduced by 73 percent of the reforms in AB? And they're going to say to me, well, did you reduce my premium by 73 percent because the cost went down? Well, the answer is no. Nobody came in – no rate filer came in with a reduction in cost for AB, anywhere near or at all. Nobody came in with a reduction for BI of 37 percent. Nobody for private passenger, commercial, nobody, but FA is saying that the P-tests and T-tests are strong and reliable, and that's what the data says. I disagree with that approach. It's flawed. It's not intuitively reasonable that this occurred. So you can look at any P-test and T-test you want and say it's significant and it's perfect, but does it make sense? And I think you have to look at it and ask yourself does it make sense, and I say it doesn't.[40]

Facility submits that the *"issue for consideration by the Board, therefore, is the extent to which the Facility Association's Loss Cost Trend Rates or those of the Consulting Actuary are representative of Facility Association taxi experience in Newfoundland and Labrador."*[41] According to Facility it has shown that its selected past trends do reflect the underlying patterns that occurred during the experience period with respect to Taxis, while Oliver Wyman acknowledged that its trend rates do not. In its submission Facility reproduces its graphs showing

[37] Transcript, November 17, 2014, page 34
[38] Transcript, November 18, 2014, page 66
[39] Transcript, November 18, 2014, pages 67-68
[40] Transcript, November 18, 2014, pages 62-64
[41] Facility Submission, January 9, 2015, page 10

selected loss trends based on Industry Commercial Vehicle data and the actual loss costs for Taxis, stating, that in its opinion, its selected Industry Commercial Vehicle loss trends reflect the Facility Newfoundland and Labrador Taxi experience. Facility goes on to state:

> *The Consulting Actuary suggested that the taxi experience is not "credible", when attempting to explain why her selected trend rates show decreases from 2003 to 2012 and yet actual NL taxi ultimate indemnity values have generally been increasing since 2003. However the concept of "credibility" is applied to ascertain whether the trends in a particular data set (i.e. taxi experience) are adequate enough in size to make predictions for the future. Even if the amount of data was not considered to be sufficient to be relied upon exclusively to predict the future, this does not detract in any way from the historical measures. We are still left with the incongruous position of the Consulting Actuary claiming not only that it is reasonable to apply the Consulting Actuary's Commercial Vehicle TPL declining trend from 2003 onward to taxi loss costs, when the taxi experience quite clearly demonstrates the opposite to be true, but the equally perplexing position that this is more reasonable than using Facility Association's trend selections which, in contrast, do align with the taxi experience.*[42]

According to Facility, not only do Oliver Wyman's trends fail to represent changes in Facility Taxis loss costs over time, they also fail to represent the underlying Industry Commercial Vehicle trends.[43]

The Consumer Advocate submits that Facility has not justifiably demonstrated its use of non-approved trend rates and that Facility should be required to use the Board approved trend rates in calculating its rate changes for Taxis. On the issue of the data and Facility's loss trend rate selection the Consumer Advocate states:

> *In assessing the actuarial judgment of Facility Association in this filing, the Consumer Advocate is struck by the fact that the Facility Association's approach to determining a loss trend rate does not appear to take into consideration the fact that the parties to this Application are dealing with exceedingly challenging experience data.*[44]

Facility responds that it does not believe the above statement of the Consumer Advocate is an accurate representation of Facility's position with respect to the data limitations "*as Facility Association recognizes this explicitly in its modeling approach via statistical analysis of the results, explicitly reviewing model fits and residuals.*"[45] Facility acknowledges that, in its 2013 filing, Private Passenger data and not Industry Commercial Vehicle data was used to select the Bodily Injury severity trend, primarily because of data volatility. According to Facility the inclusion of accident year 2012 has enabled Facility to find a statistically significant model for Bodily Injury severity based on Industry Commercial Vehicle data.

The Board accepts that the selection of loss trend rates is a matter of actuarial judgment and also that, in this Application, the loss trend rate selections have a significant impact on the rate indications. As noted by Oliver Wyman, if Facility had selected the Board's Guideline

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[42] Facility Submission, January 9, 2015, page 15-16
[43] Facility Submission, January 9, 2015, pages 12, 17
[44] Consumer Advocate Submission, January 9, 2015, page 14
[45] Facility Reply Submission, January 14, 2015, page 3

Commercial Vehicle loss trend rates, and with no other changes in assumptions, its Third Party Liability indication would be reduced by approximately 25.4%.[46]

In relation to the 20-year time period selected by Facility in its loss trend analysis the Board notes the issue raised by Oliver Wyman as to the relevancy of the older data and the consideration of the data limitations in selecting loss trend rates based on the longer data set. Ms. Elliott comments that there is no harm in looking at the older data but notes that the data is highly uncertain and questions whether you can get a better answer using more data. The Board notes Mr. Doherty's explanation that, while the 20 years of data was used for the regression analysis, the selected trend period is actually only eight years because of the finding of a change in trend in the data at 2004-H2. The Consumer Advocate did not comment on Facility's use of a 20-year time period. In the Board's view, while the use of a longer data period may be justified in some circumstances, a better answer may not be achieved by using more data in this case, given the Commercial Vehicle data uncertainty and volatility. The issue of whether the older data continues to be relevant is a concern for the Board. While the Board is not satisfied that looking at a 20-year period leads to a better result in this case, the Board does not reject Facility's proposals on the basis that a 20-year period was used.

The Board notes that Facility's loss trend selection relies on Mr. Doherty's judgment that a distinct change in loss trends happened in 2004-H2. The Board notes that, in its 2013 Taxis filing, Facility did not find evidence of a change in trend in 2004-H2 nor did it find the reform variable to be statistically significant. In addition, Facility's 2013 Private Passenger filing did not find evidence of a change in loss trend in 2004-H2. The Board also notes that, in the Industry Commercial Vehicle loss trend rates published in Board directives since 2007,[47] there was no indication of a trend bifurcation at 2004-H2, either for Private Passenger or Commercial Vehicle experience. The loss trend rate reports were provided to Industry for feedback prior to acceptance by the Board and there was no indication from any insurer, including Facility, that the loss trend rates should reflect a trend bifurcation as of 2004-H2.

On the issue of why a trend change would now be justified when it was not present in Facility's 2013 Taxi filing, or its 2013 Private Passenger filing, the Board notes Mr. Doherty's statement that he did not question why the change occurred but accepted the model output, saying he let the data speak for itself. Mr. Doherty acknowledged that he doesn't know if the change was the result of the reforms and that it may be coincidental. Facility did not provide any other explanation for what may have happened in 2004 to cause this change in trend at 2004-H2. An explanation would be especially important in this circumstance since Facility's finding of a change in trend in 2004 represents a departure from Facility's 2013 Taxis and Private Passenger filings, and from the Board's Guideline loss trend rates.

The Board notes Ms. Elliott's comment that the commercial data in Newfoundland *"is the most challenging data that we look at. Of all of the reviews for loss trend rates, it is the most challenging."* The Board also notes that in its 2013 Taxis filing Facility was unable to find a statistically sound trend rate from the Industry Commercial Vehicle data for Bodily Injury severity or Accident Benefits frequency and severity, and that it selected its trend rates based on

[46] Oliver Wyman Report, May 16, 2014, page 15

[47] The Board first implemented guideline loss trend rates following the publication of data through June 30, 2007

its estimate of Private Passenger Industry experience.[48] Facility explained that the inclusion of accident year 2012 enabled Facility to find a statistically significant model for Bodily Injury severity based on Industry Commercial Vehicle data. Ms. Elliott comments that, had Facility used one less year of data and started with 2005-H2, the trend rate would decrease by a couple of percentage points.

The Board finds that the data is highly volatile. This volatility is a significant factor in the Board's evaluation of the proposed rates. While the Board acknowledges Facility's statistical measures supporting a reform factor, the Board notes that Facility's test statistics are not strong, especially in light of the significant data limitations, and finds that these statistics do not justify the proposed loss trend rates in the circumstances. Facility has not demonstrated why a product reform impact (or some other impact) would show up in Facility's trend analysis some 10 years later, when no intervening analysis showed such an impact. In the Board's view the finding of significant reductions in loss costs for all coverages, based on the reforms introduced in the second half of 2004, is not supported based on the nature and type of reforms introduced.

The Board finds that Facility has not justified the proposed selected loss trend rates.

6.4 Full Credibility Standard

The standard of full credibility determines the weight given to the latest Facility Taxis experience in the rate change indication. In this Application Facility has changed its full credibility standard for Third Party Liability coverage to 3,264 claims from 5,410 claims used in its 2013 Taxis filing, which increases the rate change indication by approximately 7%. The credibility standard for Comprehensive and Specific Perils also changed from 3,246 claims in the 2013 filing to 1,082 in this filing. In both filings Facility references its 2003 Atlantic Commercial Study as the basis for its selected standard. Oliver Wyman notes that Facility has not provided an explanation as to why the full credibility standard was changed from its 2013 filing and, as a result, found that Facility's new full credibility standard for Third Party Liability was not fully supported.[49]

Mr. Doherty explained and corrected the basis for the current credibility standard used in this filing, stating that the reference to the 2003 Atlantic Commercial Study in this filing is incorrect and that the credibility standards used in this filing were based on his judgment.[50] Mr. Doherty described an ongoing review by Facility of the credibility process, but confirmed that this review has been pushed forward to 2015. He confirmed that the credibility standard could change again and that the manner in which the credibility standard is determined could also change.[51]

Facility submits that a full explanation for its choice of full credibility standard has been provided to support the change from the previous year's filing. Facility also submits that Oliver Wyman has failed to provide any particular criticism of Mr. Doherty's actuarial judgment in selection of the full credibility standard other than it is changed from the previous year's filing.

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[48] Information #5

[49] Oliver Wyman Report, May 16, 2014, page 16

[50] Transcript, November 7, 2014, pages 120-121

[51] Transcript, November 7, 2014, page 123

Facility states that *"there is nothing inherently wrong in adopting a change in actuarial approach where the change is properly explained and supported."*[52]

The Consumer Advocate submits that he does not believe that Facility should have elected to decrease its full credibility standard, and thus increase its rate change indications, at a time when taxi drivers and owners are already struggling to absorb the rate increases from its 2013 filing.[53] Facility responded that its 2013 requested rate increase was significantly less than the rate indication and that the position of the Consumer Advocate has no actuarial foundation.[54]

The Board believes that there is value in taking a consistent approach from filing to filing, but agrees with Facility that changes in actuarial approaches between filings are acceptable where the proposed change is properly explained and supported. It appears the change in this filing was the result of the decision to update the full credibility standards used by Facility to be consistent at the coverage level across all jurisdictions based on Mr. Doherty's judgement.[55] The impact of this decision is that the full credibility standard decreased for all coverages from the 2013 rate filing, resulting in an increase of approximately 7% in the rate indication for Third Party Liability. Facility did not provide an explanation of how the full credibility claim counts were established for each coverage. The Board finds that Facility has not adequately justified a change in the full credibility standard for Newfoundland and Labrador. The Board also notes that the ongoing review by Facility of its credibility metrics in 2015 may result in further changes to the full credibility standard.

The Board accepts that the choice of full credibility standard is a matter of actuarial judgment but any resulting rate increases must be fully supported and justified. In the Board's view Facility has not demonstrated that a change in the full credibility standard is justified in this Province.

The Board finds that Facility has not justified the proposed change to the standard of full credibility.

6.5 Complement of Credibility

Facility changed its basis for the complement of credibility in this Application from that used in its 2013 Taxis filing. A one year loss cost trend rate was previously used as complement of credibility for the indicated rate change, which reflected the anticipated frequency of rate reviews. In this filing Facility has changed its approach to the complement of credibility to start with one of the following estimates for the "loss ratio underlying current rates":

- *where we have recently filed for a rate change, we would use the previous filings estimate of loss ratio assuming no rate change, then adjusted for subsequent actual (approved) rate changes; or*
- *where we have not recently filed for a rate change, we assume the current rates are "adequate" on a basis consistent with expenses underlying the current "expiring" term*

[52] Facility Submission, January 9, 2015, page 39
[53] Consumer Advocate Submission, January 9, 2015, page 18
[54] Facility Reply Submission, January 14, 2015, page 6
[55] Transcript, November 6, 2014, page 92

> *(that is, the term that will end at the point where our new proposed rates would take effect) and use a loss ratio consistent with this assumption.*[56]

As a result of this change Facility now adjusts its loss ratio for the inadequacy it believes exists due to the difference between its 2013 Taxis filing rate indication and the rate change approved by the Board in Order No. A.I. 9(2013). Mr. Doherty confirmed that the impact of this adjustment is an increase in the rate indication of 24%, assuming all of Facility's remaining proposals are accepted.[57]

Oliver Wyman states that they do not find it appropriate for Facility to make an adjustment in this Application for rate inadequacy carried over from its 2013 Taxis filing.[58] Oliver Wyman notes that, in its 2013 Taxis filing, Facility estimated its needed rate level change at +70.7% but proposed a rate change of +51.1%. In Order No. A.I. 9(2013) the Board approved the proposed increase of 51.1%, which was in-line with the rate increase indicated using the Board's Filing Guidelines. Ms. Elliott stated:

> So in the prior filing, we had done our analysis and we estimated the rate indication for FA could support a +50 percent change. FA proposed a +50 percent increase, and the Board approved a +50 percent increase, so in our view there was no rate inadequacy.[59]

The Consumer Advocate submits that the choice by Facility of one year of trend plus the inadequacy in the current rates implied by the rate change indication in its 2013 filing is not an appropriate basis for the complement of credibility. He argues that the indicated rate change in the 2013 filing was not approved by the Board and is significantly higher than the 2013 rate change that was calculated by the Board's actuary. The Consumer Advocate submits that Facility should be directed to recalculate the complement of credibility underlying its rate change indications, excluding the Facility estimated inadequacy in the approved rates.[60]

In its submission Facility restated its view that a rate deficiency remained of approximately 13% based on the difference between the rate level indication and the approved 2013 change. Facility points to the projected and actual results for 2012 as support for this position, stating that the results show that the deficiency was actually higher than previously thought. Facility states:

> *Clearly, if the +50.1% rate increase asked for and approved in 2013 was a "true best estimate", it stands to reason that the accident year 2012 loss costs would have been at a level no higher than $2,219.*[61]

On the matter of rate adequacy and the timing of rate filings Facility stated:

> *Mr. Doherty also noted that if Facility Association had not filed for a rate change within the past two or three years, they would have started from the position that the current rates were "adequate" (i.e. they would not have alerted the Board to the apparent deficiency in the*

[56] Facility Actuarial Memorandum, Section 2, page 8
[57] Transcript, November 6, 2014, page 155
[58] Oliver Wyman Report, May 16, 2014, page 17
[59] Transcript, November 17, 2014, pages 58-59
[60] Consumer Advocate Submission, January 9, 2015, pages 19-20
[61] Facility Submission, January 9, 2015, page 42

> *rates). Mr. Doherty believes that it would not be fair in those circumstances to start with the assumption that rates are inadequate, even if the experience suggests that such rates are indeed inadequate. However, in this particular case, Facility Association did file for a rate change in the immediately prior period, and that rate application clearly alerted the Board to existing rate inadequacy.*[62]

The Board does not accept that there was rate inadequacy at the time of the approval of the 2013 Taxis filing. In the 2013 Taxis filing Facility requested approval of an increase of +50.1% and the Board approved an increase of +50.1%. While some of the underlying assumptions between Facility's and Oliver Wyman's indications for that filing were different, in Order No. A.I. 9(2013) the Board accepted the level of rate increase proposed by Facility as justified. The Board does not accept that there was rate inadequacy at the time. In addition, in the Board's view, recovery in future rates of a deficiency from a prior period based on a difference between rates approved in 2013 and Facility's indications at the time is inconsistent with the prospective nature of rate setting.

The Board finds that Facility has not justified the proposed complement of credibility.

6.6 Health Levy

The rate indications provided by Facility do not include a provision for the Health Levy, which is a set dollar amount fee per vehicle as determined by the provincial Government's Department of Health and Community Services. This is a change in approach by Facility as a Health Levy provision was included in its 2013 Taxis filing.

Oliver Wyman explains that it understands the reason for the exclusion of the Health Levy from the rate level calculation is because the GISA exhibits do not include the Health Levy in the published exhibits for Taxis and that Facility's understanding is that the Health Levy fee for Taxis is not paid by insurers to Government. The current Health Levy fee is estimated at $26.44 per vehicle. Oliver Wyman states that it is their understanding that Taxis should be subject to the Health Levy fee and therefore a provision should be included in the rates.[63]

Mr. Doherty confirmed that Taxis are not included in the Health Levy assessed in the Province and, as a result, Facility does not include in the indications for this filing a provision for the Health Levy. If it was included in the rates the amount would be collected from the taxi industry but not remitted to Government, and would instead go to the members of Facility.[64]

The Board finds that exclusion of the Health Levy is justified.

6.7 Expense Provision

The total expense provision of 23.6% incorporated in Facility's rates includes a component for service carrier compensation. Facility's current contractual arrangement with its servicing carriers provides for a 10% variable expense provision for underwriting and processing and 6%

[62] Facility Submission, January 9, 2015, page 44

[63] Oliver Wyman Report, May 16, 2014, page 15

[64] Transcript, November 6, 2014, pages 76-77

for commissions. Oliver Wyman notes that, if Facility's current average premium increases are approved as proposed in its filing, its servicing carriers will receive significant increases in this compensation, stating:

> *...Hence, if FA's current average premium for (TPL, AB and UA) of $2,928 increases as proposed to $4,626, its servicing carriers will receive an average increase of $170 (from $293 to $463) per Taxi for underwriting and processing. Similarly, with FA's contractual arrangement of 6% commission expense, its average commission for TPL, AB and UA combined will increase from $176 to $278 per taxi.* [65]

Oliver Wyman finds the expense provision is accurately included in the calculation of the rate level change need presented by Facility but suggests that the Board may wish to confirm the reasonableness of these amounts.

Facility notes that it makes payments to its brokers and servicing carriers as set out in the Plan of Operation. This Plan is approved by the Superintendent of Insurance in the Province and applies to all industry Commercial, non-Private Passenger and Private Passenger business in the Province. Facility submits that, as approval of the Plan falls within the jurisdiction of the Superintendent of Insurance, any attempt to suggest that the Board should approve revised rates with expense provisions different than those prescribed by the Plan would be inappropriate and would encroach upon the jurisdiction of the Superintendent of Insurance.[66]

The Consumer Advocate submits:

> *It is, in any event, difficult to accept the proposition that a servicing carrier should be entitled to receive more for claims expense solely because of a premium increase. Mr. Doherty agreed that the formula is meant to be a proxy for fair and reasonable compensation for these services. (Transcript, November 7, 2014, page 36) The difficulty is that in order to be confident that the proxy is producing fair and reasonable results it would be necessary to know the actual expenses incurred. That information is not available.*[67]

The Consumer Advocate refers to Ms. Elliott's testimony in which she suggested that Facility take the initiative to review the costs for underwriting, claims handling and commissions to explore ways to bring down the premium. The Consumer Advocate recommends that the Board require Facility to do this prior to its next rate filing in this Province.

In its reply submission Facility submits that the recommendation made by the Consumer Advocate seems to implicate all rate classes and would impose a significant work effort by Facility. Facility also submits that the main issue is that loss costs, primarily Bodily Injury, and not expenses drive the rate need. Facility states that indemnity amounts for Taxis over the 10 accident year history provided in Facility's filing have surpassed premium levels by more than 58%. Facility states that *"This has placed a significant burden on the insurance industry and represents a de-facto subsidy from the insurance industry to the taxi industry."*[68]

[65] Oliver Wyman Report, May 16, 2014; page 22
[66] Facility Submission, January 9, 2015, pages 45-46
[67] Consumer Advocate Submission, January 9, 2015, page 21
[68] Facility Reply Submission, January 14, 2015, page 8

The Board notes that neither Oliver Wyman nor the Consumer Advocate suggest that the expense provision is calculated incorrectly or is not in accordance with the existing Plan of Operation. Rather it is proposed that the actual costs associated with claims handling for Facility's Taxis class of business be reviewed in advance of the next filing to ensure that the percentage approach produces a reasonable amount to be recovered from insureds.

The Board is responsible for ensuring that the rates to be charged are not too high. The rates for Taxis were increased by 50% following Facility's 2013 Taxis filing and Facility is proposing another 50% increase with this filing. The percentage approach means that the compensation to brokers and servicing carriers will increase significantly as a result but it is not clear whether there is actually any increase in the level of effort or work required to process and handle claims. The Board notes that the dollar increases in the servicing carrier payments are significant and that this amount is reflected in the proposed rates. The Board finds that it is not clear that the proposed expense payments to servicing carriers accurately reflects the costs of writing the business. However, the Superintendent of Insurance approves the expense provision in the Plan of Operation and Facility is obliged to pay these expenses. The Board finds that the expense provision is calculated correctly according to the Plan of Operation and the Board will accept the amount to be reflected in rates.

With respect to the suggestions by Oliver Wyman and the Consumer Advocate that Facility should take the initiative to review the costs for underwriting, claims handling and commissions to explore ways to reduce these costs for insureds, the Board agrees that this would be of benefit to insureds. In addition, the Superintendent of Insurance for the Province may wish to review the provision for expenses in the Plan of Operation.

The Board finds that Facility has justified the inclusion of the proposed expense provision.

6.8 Physical Damage Coverages

Facility determines rates for Physical Damage coverages by applying a physical damage multiplier, currently set at 225%, to Private Passenger Automobile rates. Oliver Wyman reports that the indications in this filing shows a 9% decrease for the Physical Damage coverages but no change in the physical damage multiplier is proposed.

Facility's 2013 Taxis filing indicated a rate decrease for Physical Damage coverages but no change in the multiplier was proposed at the time. In Order No. A.I. 9(2013) the Board found that Facility's proposed physical damage multiplier for Taxis may result in rates for these coverages that are too high. As a result the Board directed Facility to review its physical damage multiplier and to provide further criteria in relation to its proposed multiplier for Physical Damage coverages. Facility advised by letter dated June 12, 2013 that it had reviewed the physical damage multiplier for Taxis and, while the factor was not actuarially justified, the multiplier was reduced by approximately 10% from 250% to 225% "as a good faith gesture". Facility also advised that this move would bring the multiplier in line with that of Nova Scotia and Prince Edward Island and that it would be reviewed again later. The Board accepted this proposal with the caveat that a further review be conducted in 18 months.

The Board notes that, while the physical damage multiplier is not actuarially justified based on Newfoundland and Labrador Taxis experience due to limited data, based on Oliver Wyman's report the proposed multiplier may be too high. The Oliver Wyman report states that the indications in the filing show a 9% decrease. Facility has advised that it plans to review this multiplier but did not advise whether this review has been completed. The Board finds that, based on the Oliver Wyman report, and in the absence of actuarial evidence to support the approval of the existing multiplier, Facility has not justified the proposed physical damage multiplier.

The Board finds that Facility has not justified the proposed Physical Damage multiplier.

6.9 Territorial Differentiation

Facility's current Third Party Liability base rates for its Taxis class of business are not broken down by territory in the same manner as the rates for Private Passenger. The optional Physical Damage coverages are subject to separate base rates for the statistical rating territories since they are derived based on Private Passenger rates.

The Consumer Advocate raised the issue of territorial distinction in the Province and questioned whether there was sufficient data to permit the distinctions to be drawn for separate rating for Taxis within the four territories. The Consumer Advocate submits that, based on Facility's responses to PUB-FA-16 and PUB-FA-18, there appears to be marked differences in the reported pure loss ratios in Territories 005 and 006 (Bonavista/Burin and Labrador) and Territories 004 and 007 (Avalon and rest of Island). While noting that, according to Undertaking #8, the only jurisdictions in Canada where Facility has different taxi rates by territory are Alberta and Ontario, the Consumer Advocate submits:

> *Nonetheless, there does appear to be a concern about the level of subsidization in favour of taxi insureds on the Avalon and the rest of the Island by insureds in Labrador and Bonavista/Burin. In Facility Association's next taxi rate filing, the Consumer Advocate would recommend that Facility Association provide together with its normal filing an alternative for the consideration of the Board which takes into account the experience in the territories.*[69]

In its submission Facility recognizes that territorial rating would not impact its overall rate requirements but suggests that, by reason of the extremely small taxi population in the Province, and the even smaller group outside the Avalon, it would be challenging to attempt to separate those territories for rate setting. Facility also submits that the breakdown of the Taxis experience by territory would also likely increase expenses for Facility and its servicing carriers.[70]

The Board notes that both Mr. Doherty and Ms. Elliott confirmed that having different rates for each of the four statistical territories does not impact Facility's overall rate requirements. This is because the overall rate requirements would still be collected from the total pool of insureds. If rates for one territory are reduced the difference will be collected from the remaining insureds. The existing statistical territories recognize the different risk exposures in the Province. It seems

[69] Consumer Advocate Submission, January 9, 2015, pages 23-24
[70] Facility Submission, January 9, 2015, pages 46-47

reasonable to assume that there may be a risk-based reason to separate Taxis into territories for rate setting. However the Board agrees with Facility that the Taxis experience may not be a sound basis on which to establish differentiated rates for Taxis in the Province. The Board is concerned that the Industry Commercial Vehicle and Taxis experience in the Province may not be sufficient to establish actuarially justified territory differentials.

There is not sufficient evidence in this proceeding to enable the Board to make any finding on whether territorial differentiation for Facility's rates for Taxis may be reasonable or actuarially justified. The Board is satisfied that Facility should address the issue of territorial differentiation for Taxis in the Province as part of its next rate filing for Taxis.

The Board finds that Facility has justified its approach in relation to territorial differentiation.

6.10 Proposed Rule Changes

Facility has proposed a number of rule changes[71] to become effective with the implementation of new rates, including but not limited to:

- Offering a $2,000,000 Third Party Liability limit and up to $5,000,000 where required for a contract of work;
- Increasing the available limit for physical damage coverage to $1,000,000;
- Changes to the definition of convictions;
- Removing All Perils and replacing it with Collision and Comprehensive;
- Minor amendments to the minimum deductible tables to provide for lower limits and where there have been 5 or more losses;
- Adding requirements for valid vehicle registrations to verify ownership and for branded vehicles;
- Eliminating the discount for owner driven taxis;
- Amending the U.S. exposure surcharge;
- Including requirements for imported and right hand drive vehicles under Homemade/Reconstructed vehicles;
- Amending the rating for more than one use to use the highest rated class (based on premium) regardless of the percentage of exposure; and
- Changing the approach for vehicles used in other jurisdictions.

For each of the proposed rule changes Facility provides the revised wording for its Rules and Rates Manual along with the reason for the change and whether there is an impact on premiums as a result of the change. Oliver Wyman observes that, since Facility provides no information as to the rate level impact of these changes, which it understood to be due to data limitations, it does not offer any comment on the proposed changes.[72]

During cross-examination the Consumer Advocate questioned Mr. Doherty on the rule changes associated with removal of the discount for owner driven taxis and the rating for more than one

[71] As set out in Section 3 of Facility's Actuarial Memorandum
[72] Oliver Wyman Report, May 16, 2014, page 3

use, which were identified by Facility as having a possible impact on premiums. No other rule changes were canvassed during the hearing or in submissions.

Owner Driven Discount

Facility currently provides a 10% premium discount for taxis that are owner driven. This discount has been in place for at least 15 years.[73] The decision to remove this discount was based on a review by Facility of its current underwriting manual. Facility submits that the owner driven discount is incongruous with its position as a market of last resort, suggesting that *"like the provision for rating for more than one use, the owner driven taxi discount is open to mischief."* Facility argues:

> *The owner driven taxi discount allows for a reduction in premium that would otherwise be collected by Facility Association, based largely on the honor system. However, based on the insurance system in Newfoundland and Labrador, an owner driven vehicle being operated with the permission of the owner by another operator does not relieve Facility Association of its obligations under the policy to pay third party claims up to the statutory minimum, notwithstanding that the insured vehicle is being operated by other than its owner. Accordingly, a breach by the owner/operator of the assurance in the application for insurance that the vehicle is driven only by the owner, does not relieve Facility Association of liability under the policy, at least to the extent of the statutory minimum for third party liability coverage amounts.*[74]

In relation to the question of whether there is a basis to differentiate between vehicles that are owner-driven versus employee driven from a risk perspective, and whether that risk would be lower for an owner driven vehicle, Mr. Doherty stated that he believed this would make sense. Mr. Doherty explained why he believed the discount should be removed:

> I can't speak specifically to the rationale because I'm more on the numbers side than the underwriting rule side, but as I understand it, it's more that presenting things as a discount we don't think is the tone we would want to set. It would be better to surcharge people who are not owners than to give owners a discount. It's semantics more than anything else, but from our perspective giving discounts seem to be counterintuitive. You would usually use discounts as a way of marketing so that you can attract business that you want by offering them discounts, but it amounts to the same thing. I don't recall, though, that we're actually proposing to put a surcharge on non-owners.[75]

The Consumer Advocate notes that Facility was not able to identify how insureds would be affected by the loss of this "*long-standing, apparently risk-based discount*" and, as a result, its removal should not be permitted. The Consumer Advocate submits:

> *Facility Association is practically the only insurance option for taxis in this jurisdiction. Keeping the discount in place will not attract Facility Association more business – it already has it all.*

[73] Undertaking #9

[74] Facility Submission, January 9, 2015, pages 47-48

[75] Transcript, November 7, 2014, page 44

> *Finally, while Facility Association is a "last resort", it should not follow that therefore its insureds should be deprived of risk-based differentiation such as owner driven discounts.*[76]

Facility responds that, while it agrees with the Consumer Advocate's statement that keeping the discount will not attract more business to Facility, removing the discount may make such drivers more attractive to the regular market and therefore entice other insurers to enter the market.[77]

The Board notes that Facility has not provided actuarial evidence to justify the removal of this discount, nor did it provide information on how the removal of the owner driven discount will impact insureds and how many insureds would be affected. The Board also notes that the removal of a 10% premium discount on an average Facility premium of approximately $3,000 is a significant impact in dollar terms. Mr. Doherty's suggestion that removing this discount may make such drivers more attractive to the regular market seems inconsistent with his comments that he is not aware of any other insurers that would offer coverage for Taxis in the Province. The Board is not prepared at this time to approve the proposed rule change to remove this discount in the absence of supporting documentation to justify the rule change.

The Board finds that Facility has not justified the proposed rule change to remove the owner driven discount.

Rating for More Than One Use

The Consumer Advocate also questioned Mr. Doherty on the proposal to change the manner in which vehicles are rated where there is more than one use. The existing rule provides that if a vehicle is being used for more than one purpose the rating is done on the basis of the highest percentage of exposure. Facility is proposing to change this rule so that the rating is done on the basis of the highest rated class (based on premium) regardless of exposure. Facility states that this rule has been in place in this Province since 2005, but that records from 2004 appear to show that the proposed dual usage rating was in place prior to then.[78]

Mr. Doherty agreed that this was a potentially significant rule change, particularly for an operator who would currently have less than 50 percent taxi usage. Mr. Doherty explained that the rationale behind this proposed rule change was related to the risk of the taxi business itself and that, even with a lower percentage of taxi use, the risk of being involved in an accident was higher.[79] Facility did not provide actuarial evidence to justify the proposed change.

Facility confirmed that the proposed rating rule is in place in the Northwest Territories, Nunavut, Yukon, Alberta and Prince Edward Island and that Facility is in the process of filing in Ontario, New Brunswick and Nova Scotia.[80] No information on the number of affected insureds or the dollar impact of this proposal was provided.

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[76] Consumer Advocate Submission, January 9, 2015, pages 22-23
[77] Facility Reply Submission, January 14, 2015, pages 8-9
[78] Undertaking #9
[79] Transcript, November 7, 2014, pages 49-50
[80] Undertaking #10

In the absence of supporting documentation to justify the rule change the Board is not prepared at this time to approve the proposed rule change to amend the rating for more than one use to use the highest rated class (based on premium) instead of the percentage of exposure.

The Board finds that Facility has not justified the proposed rule change related to the manner for rating for more than one use.

Remaining Rule Changes
The Board has reviewed the remaining proposed rule changes as set out in Section 3 of Facility's Actuarial Memorandum. Many of the rule changes appear to be housekeeping and/or policy enhancements and will not impact premiums for insureds. Where Facility has indicated that the rule changes may result in premium changes the Board is satisfied that the impact is not significant and mostly relates to optional or enhanced coverages, such as increased liability levels and higher limits for Physical Damage coverage.

The Board finds that Facility has justified the proposed rule changes, other than the removal of the owner driven discount and the change to the manner for rating for more than one use.

6.11 Conclusions

The Board finds that Facility has not justified its proposals in relation to:

i) the loss trend rates;
ii) the full credibility standard;
iii) the complement of credibility;
iv) the physical damage multiplier;
v) the removal of the owner driven taxi discount; and
vi) the manner of rating for more than one use.

Facility's proposals result in an average overall rate level increase for all coverages combined of 54.1%. The Board notes that Oliver Wyman calculated an indicated increase of 21.5% for independently rated coverages using the Board's Guidelines parameters, including the Board's commercial loss trend rates as set out in the Board Directive A.I. 2013-02.[81] The Board notes that Facility proposes no rate changes for the Physical Damages coverages but Oliver Wyman reports that the indications show a 9% decrease for these coverages. The Board finds that the rates proposed by Facility are too high in the circumstances.

As set out in section 8 of the *Automobile Insurance Act*, where the Board determines that an insurer's proposed rates are too high, the Board must either vary or prohibit the proposed rates. Based on the Oliver Wyman indications the Board accepts that a rate increase for Facility's Taxis class of business appears to be justified. The Board notes however that Facility raised several concerns in relation to Oliver Wyman's review of its filing and, in particular, with respect to Oliver Wyman's methodology for its selection of loss trend rates. These include the

[81] Indication reduced by approximately 1% due to error discovered – CA-FA-01 and Transcript, November 17, 2014, page 3

time period selected, the consideration of "stability" over "fit" and their treatment of statistical outliers.[82]

The Consumer Advocate submits that the proposed rate increases as presented and recommended by Oliver Wyman are within reason particularly in light of the large rate increases approved in 2013.[83] In particular, the Consumer Advocate supports the approach used by Oliver Wyman in its loss trend analysis, which the Consumer Advocate submits is more reasonable and responsive to the data limitations and extreme variability.

The Board believes that Oliver Wyman's approach to selecting loss trend rates strikes a reasonable balance between stability and responsiveness in view of the acknowledged data limitations and volatility. In selecting loss trend rates Oliver Wyman uses an averaging approach rather than attempting to determine the best "fit" over a single time period. Oliver Wyman takes the data volatility and uncertainty into consideration through the use of averaging in an attempt to create a model which is stable, responsive and consistent. The Board notes Ms. Elliott's comments in relation to the data limitations:

> ... The data is not credible, it's very limited. So I don't think that anyone can stand up in good conscience and say I've got the perfect fit, mine is great, mine is wonderful, I've got the right answer. That's not the case with this data. It's very limited and volatile, and that is the point that we're trying to make. By drawing in averages, we take a wider range of possibilities. By picking just one number and saying that's it, got the right number, I think it's not—it's not the approach that we want to take, it's not what we've done. In our judgment we've taken a different approach.[84]

The Board is satisfied that the use of the Board's Guideline loss trend rates and the rate indications developed by Oliver Wyman using these loss trend rates would not result in rates which are too high in the circumstances. Further the Board accepts the approach set out in Oliver Wyman's report with respect to the full credibility standard, the complement of credibility, and indications in relation to the physical damages multiplier. Based on the Oliver Wyman indications the Board accepts that a rate increase is justified for Facility's Taxis class of business and, while Facility has not justified the proposed increase, it may revise its rate proposal to reflect the findings of the Board in this Order. In particular the rates proposed in the revised filing should be no higher than indications developed using:

i) the Board's Guideline Commercial Vehicle loss trend rates in Directive A.I. 2013-02;
ii) the standard of full credibility consistent with its last approved filing;
iii) the complement of credibility consistent with its last approved filing;
iv) a physical damages multiplier that reflects the indications; and
v) proposed rule changes excluding the removal of the owner driven taxi discount and changes to the manner of rating for more than one use.

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[82] Facility Submission, January 9, 2015, page 18
[83] Consumer Advocate Submission, January 9, 2015, page 3
[84] Transcript, November 18, 2014, page 139-140

Pursuant to sections 57 and 61(2) of the *Automobile Insurance Act* and section 90(1) of the *Public Utilities Act*, Facility will be required to pay the costs of the Board associated with this filing, including the costs of the actuarial review and the costs of the Consumer Advocate.

7. Order

<u>IT IS THEREFORE ORDERED THAT:</u>

1. The Application by Facility Association is denied.

2. Facility Association will pay all costs of the Board, including the cost of the actuarial review and the costs of the Consumer Advocate.

DATED at St. John's, Newfoundland and Labrador, this 2nd day of April 2015.

Andy Wells
Chair & Chief Executive Officer

Darlene Whalen, P.Eng.
Vice-Chair

Dwanda Newman, LL.B.
Commissioner

James Oxford
Commissioner

Cheryl Blundon
Board Secretary

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