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May 28, 2009

Mr. Del Dyck
Executive Director
Alberta Automobile Insurance Rate Board
200 Terrace Building
9515 – 107 Street
Edmonton, Alberta T5K 2C3

*Delivered via email airb@gov.ab.ca
Original to follow by courier*

Re: Annual Review of Automobile Insurance Premiums for Basic Coverage

Dear Mr. Dyck,

Please find enclosed the required signed original and twelve copies of the Facility Association submission to the Alberta Automobile Insurance Rate Board's Annual Review of Automobile Insurance Premiums for Basic Coverage.

Attending at our presentation on behalf of Facility Association will be:

David Simpson, President & CEO

Please also find enclosed a signed disclosure form.

With respect to our presentation needs, we will be using a laptop-driven PowerPoint presentation to highlight facts and themes from our submission. A projector (with USB cable connectivity) and screen are all that we need. We will email the presentation to you a week before the Hearing as requested in your letter to me of May 9th.

If you require anything further in the interim, please let me know directly.

Yours truly,

A handwritten signature in black ink, appearing to read 'David J. Simpson', written over a light blue horizontal line.

David J. Simpson, M.B.A., FCIP
President & CEO

c.c.: Martin Beaulieu, FA Board Chair

Alberta Automobile Insurance Rate Board

Annual Review of Automobile Insurance Premiums for Basic Coverage

June 17, 2009



Submission

A handwritten signature in black ink, appearing to read 'David J. Simpson', written over a horizontal line.

David J. Simpson, M.B.A., FCIP
President & CEO

1 **EXECUTIVE SUMMARY**

2

3 This submission provides the Alberta Automobile Insurance Rate Board (AIRB) with an
4 updated overview of the size of the Alberta Risk Sharing Pools and their financial
5 performance since inception.

6

7 We also highlight the financial impact on member companies and include a brief discussion
8 of the impact of the Minor Injury Regulation (MIR) strike down on the Risk Sharing Pools.

9

10 **SIZE**

11

12 Our view is that residual market mechanisms should be as small as possible. This stems from
13 the belief that consumers are best served by companies competing directly for their business
14 in an environment where those companies do not have to frame their business decisions based
15 on impacts from residual markets.

16

17 In 2008, we saw an overall decrease in written premiums transferred to both the Grid and
18 Non-Grid Risk Sharing Pools (RSP) combined as volume dropped from \$382M to \$348M.
19 There was a decline in premium written through each pool as the Grid RSP declined by
20 \$19.6M and the Non-Grid RSP declined by \$14.1M. Written premiums transferred to both
21 RSPs together represent 15.1% of all private passenger automobile insurance premiums
22 written in Alberta in 2008.

23

24 Please see Table 1 for a summary of Risk Sharing Pools written premiums and market share
25 data for the last three years.

26

Table 1						
Alberta Risk Sharing Pools – Market Share (Written Premium Basis)						
Year	Total		Grid RSP		Non-Grid RSP	
	W. Prem	Mkt Share	W. Prem	Mkt Share	W. Prem	Mkt Share
2006	\$380,543,231	18.5%	\$309,538,332	15.1%	\$71,004,099	3.5%
2007	\$382,378,719	17.6%	\$302,904,752	14.0%	\$79,473,967	3.7%
2008	\$348,642,315	15.1%	\$283,278,774	12.3%	\$65,363,541	2.8%

27

28 On a written exposure count basis (exposure is defined as one car insured for one year) a total
 29 of 193,191 exposures were transferred to both RSPs in 2008, down from 221,455 exposures
 30 in 2007 and 230,568 in 2006. As with written premium, written exposures declined in each
 31 RSP as the number of exposures transferred to the Grid RSP decreased by approximately
 32 18,950 to 134,700 and exposures transferred to the Non-Grid RSP decreased by
 33 approximately 9,300 to 58,491.

34

35 Please see Table 2 for a summary of Risk Sharing Pools written exposure and market share
 36 data for last three years.

37

Table 2						
Alberta Risk Sharing Pools – Market Share (Written Exposure Basis)						
Year	Total		Grid RSP		Non-Grid RSP	
	W. Exp	Mkt Share	W. Exp	Mkt Share	W. Exp	Mkt Share
2006	230,568	11.5%	164,643	8.2%	65,925	3.3%
2007	221,445	10.5%	153,649	7.3%	67,796	3.2%
2008	193,191	8.8%	134,700	6.2%	58,491	2.7%

38

39 On a written exposure basis, the combined Alberta RSPs remain among the largest residual
 40 market mechanisms in North America, behind only Nunavut, the Northwest Territories and
 41 North Carolina. In fact, there are only six North American jurisdictions (five out of which are
 42 in Canada) where residual market mechanisms have over 5% market share.

43

44 **FINANCIAL PERFORMANCE**

45

46 Table 3 summarizes the financial performance of the Risk Sharing Pools since inception. The
 47 data in the table is taken directly from our audited financial statements.

48

Fiscal Year	Grid RSP	Non-Grid RSP	Combined
2005 (13 months)	\$(93,902)	\$(28,038)	\$(121,940)
2006	\$8,498	\$(30,562)	\$(22,064)
2007	\$93,357	\$(9,422)	\$83,935
2008	\$(73,490)	\$(29,955)	\$(103,445)
Total	\$(65,537)	\$(97,977)	\$(163,514)

50

51 Last year, we were unable to include a provision for the strikedown of the Minor Injury
 52 Regulation (MIR) in our financial statements. This year's statements **do** include such a
 53 provision. A summary of the derivation of the estimates underlying that provision was
 54 circulated to all member companies in a member bulletin that may be found as Appendix 2.

55

56 On an undiscounted basis as at March 2009, provisions for the MIR increase the claims
 57 liabilities in the Grid RSP by approximately \$90 million and increase the claims liabilities in
 58 the Non-Grid RSP by approximately \$22 million. One of the key assumptions underlying the
 59 estimates of the liabilities for the MIR strikedown is the assignment of a 50% probability that
 60 the appeal of the Court of Queen's Bench will be successful. That assumption is not based on
 61 a legal evaluation of the case but simply reflects that the decision of the Alberta Court of
 62 Appeal is unknowable in advance. Therefore, the court's decision will have a material impact
 63 on the financial results of the RSPs one way or another, and that underscores the highly
 64 uncertain operating environment Alberta's automobile insurers are working within. If, as has
 65 been speculated, the decision of the Alberta Court of Appeal is appealed to the Supreme Court
 66 of Canada, the dollar amount reflecting that uncertainty will only continue to grow in
 67 magnitude until an ultimate legal decision is reached.

68

69 Automobile insurance is a business based on estimates – the true results of a given accident
 70 year cannot be known until many years in the future. Deriving estimates for the RSPs is
 71 especially challenging from an actuarial perspective as it involves taking into account the
 72 independent decision making of member companies with respect to what types of risks they
 73 will transfer to a given pool. The estimated ultimate loss ratios for the RSPs by accident year
 74 and how these estimates have evolved since the inception of the RSPs are shown in Table 4.

75

Table 4					
Alberta Risk Sharing Pools – Undiscounted Estimated Ultimate Loss Ratio (ELR)					
Period	----- Accident Year -----				
Grid RSP	2004	2005	2006	2007	2008
As at Oct 31 2005	82.3%	82.5%			
As at Oct 31, 2006	69.2%	73.7%	76.3%		
As at Oct 31, 2007	51.7%	57.3%	65.5%	69.1%	
As at Oct 31, 2008	54.7%	60.0%	69.0%	75.1%	75.6%
Non-Grid RSP	2004	2005	2006	2007	2008
As at Oct 31 2005	173.7%	123.4%			
As at Oct 31, 2006	204.2%	107.8%	103.8%		
As at Oct 31, 2007	210.5%	94.0%	89.8%	100.0%	
As at Oct 31, 2008	242.4%	93.2%	88.8%	101.7%	107.2%

77

78 **FINANCIAL IMPACT ON THE INDUSTRY**

79

80 Because we must prepare our financial statements according to Generally Accepted
81 Accounting Principles, our statements can only show the results of our own operations. As
82 member companies incorporate their share of Risk Sharing Pool premiums and results into
83 their own statements, they have to reflect items such as health levies, premium taxes,
84 investment income, income tax effects and their cost of capital on those premiums and results.
85 Table 5 illustrates what an adjusted operating result might look like from the industry's
86 perspective.

87

88 **Table 5**

ALBERTA RISK SHARING POOL
SUMMARY OF OPERATIONS - INDUSTRY IMPACT FOR ILLUSTRATION PURPOSES
ADJUSTED OPERATING RESULT
(Amounts in \$000's)

	GRID RSP					NON-GRID RSP				
	Total	Oct-08	Oct-07	Oct-06	Oct-05	Total	Oct-08	Oct-07	Oct-06	Oct-05
Net Operating Result <i>(per Financial Statements)</i>	(\$65,537)	(\$73,490)	\$93,357	\$8,498	(\$93,902)	(\$97,977)	(\$29,955)	(\$9,422)	(\$30,562)	(\$28,038)
Adjustments :										
Premium Taxes Paid Directly by Members	(39,253)	(8,566)	(9,291)	(9,264)	(12,132)	(8,094)	(2,094)	(2,134)	(2,674)	(1,192)
Health Levies Paid Directly by Members	(39,142)	(9,172)	(13,495)	(10,291)	(6,184)	(7,974)	(1,878)	(2,789)	(2,741)	(566)
Discounting of policy liabilities	31,809	(1,945)	(1,533)	15,117	20,170	8,420	(1,282)	169	6,379	3,154
Association Dues paid directly by members	(5,234)	(1,142)	(1,239)	(1,235)	(1,618)	(1,079)	(279)	(285)	(357)	(159)
Investment Income	69,566	26,880	21,495	15,250	5,941	10,179	4,059	3,459	2,095	566
Net Adjustment	17,746	6,055	(4,063)	9,577	6,177	1,452	(1,474)	(1,580)	2,702	1,803
Adjusted Net Operating Result	(47,791)	(67,435)	89,294	18,075	(87,725)	(96,525)	(31,429)	(11,002)	(27,860)	(26,235)
Income Tax on net Operating result	(14,646)	(19,893)	28,663	6,077	(29,493)	(31,806)	(10,089)	(3,531)	(9,366)	(8,820)
Operating Result Before Cost of Capital	(33,145)	(47,542)	60,631	11,998	(58,232)	(64,719)	(21,340)	(7,471)	(18,494)	(17,415)
Deemed after tax Cost of Capital	77,713	19,841	20,617	23,774	13,481	15,661	4,698	5,342	4,296	1,325
Combined Net Operating result	(\$110,858)	(\$67,383)	\$40,014	(\$11,776)	(\$71,713)	(\$80,380)	(\$26,038)	(\$12,813)	(\$22,790)	(\$18,740)

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The net operating result between 2005 and 2008 shown above is taken from Audited Alberta Grid Financial Statements.

The "impact on member companies" illustrates the effect on member companies of, in addition to sharing in Risk Sharing Pool's Net Operating Result, also having to pay income and premium taxes, health levies, association dues and incur a cost of capital due to their compulsory participation in Facility Association as described in Note 2 of the Audited Financial Statements. Member impact also includes investment income earned on funds held by members and the effect of discounting.

Minor Differences may occur due to rounding.

Assumptions:

<u>Adjustments</u>	<u>Source</u>	<u>Assumption</u>
Premium Taxes Paid Directly by Members	Insurance Bureau of Canada	n/a
Health Levies Paid Directly by Members	Alberta Finance, Tax and Revenue Administration	n/a
Discounting of policy liabilities	Eckler Ltd.	Risk free rate of return used is based on a portfolio of Government of Canada bonds, for which the dates and amounts of maturities were matched to the expected payout of policy liabilities. 2008 discounted rate 2.93%
Investment Income	Eckler Ltd.	Investment Rate 3.5% Estimated industry investment yield
Income Tax on net Operating result	Facility Association	Published income tax rates.
Association Dues	Facility Association Accounting Committee	0.40005% of Written Premium
Deemed after tax Cost of Capital	Facility Association Accounting Committee	Deemed after tax Cost of Capital 10% Surplus based on 1.5:1 ratio

98
99

100 As the AIRB has requested, we have calculated “break even” loss ratios for both RSPs from
101 the industry’s perspective. These loss ratios are shown in Table 6.
102

Fiscal Year	Grid RSP	Non-Grid RSP
2005	51.32%	-19.27%
2006	65.55%	57.63%
2007	69.86%	62.04%
2008	66.78%	66.90%

103
104 Of course, it is unlikely that the loss experience of any one particular company will be
105 identical to that of the industry as a whole, as each company’s loss experience will depend on
106 the loss experience of risk transferred to the RSPs, relative to the loss experience of the RSPs.
107

108 One could look at the overall financial results of the Risk Sharing Pools (especially the Grid
109 RSP) in the context of the Minor Injury Regulation ultimately being upheld and conclude that
110 the presence of the Grid RSP has, and will continue to be, relatively benign. For those that do,
111 we would provide the following notes of caution:
112

- 113 - The Grid RSP loss experience compares poorly to that of the overall market. To the
114 extent that the overall market loss performance deteriorates, we would expect the Grid
115 RSP loss experience to deteriorate as well.
116
- 117 - Competitive enterprises need to generate a competitive level of return. To the extent
118 that companies are not generating a competitive level of return on approximately 15%
119 of revenue, that return must be generated from those paying the remaining 85% of
120 premium in the marketplace
121
- 122 - Taken together, the Risk Sharing Pools represent a large volume of premium likely to
123 behave in a more volatile way than of most individual companies. Although this
124 volatility impacts all companies in a similar way, smaller companies with limited
125 financial resources very probably find those impacts more difficult to absorb. As well,
126 the presence of such large RSPs with their inherent volatility may act as a barrier to

127 entry to insurers who would otherwise seek the opportunity to serve Alberta
128 consumers.

129

130 **CONCLUSION**

131

132 We stated near the beginning of this submission our belief that consumers are best served by
133 companies competing directly for their business in an environment where those companies do
134 not have to frame their business decisions based on impacts from residual markets. So we
135 were heartened to read in the Chair's remarks in the 2008 annual report of the AIRB the
136 Board's support of increasing competition in Alberta automobile insurance:

137

138 "The Board continued to play a key role in the Government's Premiums
139 Regulation review and is in the process of forwarding to the Minister a
140 recommendation that if accepted will change the current industry-wide process
141 to a file and approve system. The Board believes that this new system, will
142 reduce uncertainty in the market and, thereby, support greater competition
143 resulting in improved premiums for consumers over the longer term."

144

145 Simply stated, maximizing insurance availability for consumers can be achieved in an
146 environment of product stability and pricing flexibility. We therefore believe that a move
147 away from a rigid industry-wide process to a more flexible company-specific approach to rate
148 review would not only lead to improved premiums but smaller residual market mechanisms as
149 well. In a similar vein, we suggest, as we did last year, that steps be taken to ensure the
150 protection afforded by the premium grid remains as tightly focused as possible on the group
151 of consumers it is intended to protect and that insurers be allowed to charge adequate rates for
152 risks not targeted by the grid.

153

154 **APPENDIX I: RISK SHARING POOLS BACKGROUND, AUTHORIZATION &**
155 **OPERATION**

156

157 **BACKGROUND**

158

159 Facility Association is an administrative mechanism that administers involuntary residual
160 market automobile insurance on behalf of the voluntary/private sector automobile insurance
161 industry across Canada. Created by the industry and empowered by statute, Facility
162 Association’s mission is to guarantee the availability of automobile insurance coverage for
163 consumers who require it to legally operate their vehicles. Facility Association has a full-
164 time staff of twenty-five people and fulfils its mandate via a network of outsourcing
165 arrangements.

166

167 In Alberta, Facility Association administers the Alberta RSP (in reality, two Pools – one for
168 Grid and the other for Non-Grid risks) for private passenger vehicles. It also administers the
169 traditional Residual Market for non-private passenger vehicles and a very small “Residual
170 Market Segment” (with very tightly defined risk criteria) for private passenger vehicles.

171

172 Because all licensed automobile insurers must participate in the residual markets
173 administered by Facility Association according to specified sharing formulas, their financial
174 results are subject to greater volatility and uncertainty than would otherwise be the case.
175 Participation in the Residual Market also imposes additional costs on Facility Association
176 member companies for such expenses as premiums taxes, health levies, and the cost of
177 capital members must maintain to support residual market premiums.

178

179 **THE RESIDUAL MARKETS - AUTHORIZATION**

180

181 In Alberta, Facility Association administers the RSPs and Residual Market as authorized by
182 its Plan of Operation, which is approved by the provincial Superintendent of Insurance. (The
183 Plan may be viewed and downloaded at www.facilityassociation.com.) All companies
184 licensed to sell automobile insurance in Alberta are required to abide by the provisions of
185 the Plan.

186

187 For risks ceded to the Alberta RSPs, the Plan requires Facility Association to maintain and
188 report separate financial results for those risks that are subject to the premium grid and those

189 that are not. This creates the need for two RSPs, commonly referred to as the Grid RSP and
190 the Non-Grid RSP. Both are for private passenger automobiles only. All financial results of
191 the Alberta RSPs and the traditional Residual Market are assigned to member companies
192 based on their participation in the Alberta automobile insurance market. That is, they are not
193 spread across the other jurisdictions Facility Association serves.

194

195 THE RISK SHARING POOLS - OPERATION

196

197 Essentially, a RSP is a residual market that acts as an industry-wide reinsurance mechanism
198 that is largely invisible to consumers and intermediaries. A consumer buys insurance in the
199 normal way, and the application is forwarded to a company underwriter. The underwriter
200 assesses the risk, decides whether to keep it on the company's own books or to transfer the
201 risk to the RSP, subject to the operational rules and eligibility guidelines of the Pool.

202

203 For both Alberta RSPs, companies receive an expense allowance to cover costs such as
204 those incurred for acquisition, policy issuance, policy administration and claims servicing.
205 That expense allowance is set annually by the Facility Association Board of Directors in
206 consultation with the Superintendent. For both Pools, companies are required to submit
207 100% of all premiums for all coverages on a policy and are eligible for 100%
208 reimbursement of eligible claims and related expenses. Financial results (top **and** bottom
209 lines) of the Pools are shared among companies based on the proportion of a company's
210 private passenger automobile exposures not ceded to a RSP divided by the number of
211 industry private passenger automobile exposures not ceded to a RSP. As Facility
212 Association is simply an administrative mechanism, all companies receive a monthly report
213 reflecting the operations of the Pool, providing them with the amounts they are then required
214 to book into their own financial statements.

215

216 The two Pools differ primarily in the number of risks companies can transfer to each. For
217 the Grid RSP, companies can transfer eligible risks without limit. This lack of limit is based
218 on the philosophy that companies are required to accept risks for which they have no control
219 over price and, therefore, little or no control over the financial results of that business. In a
220 general way, the size of the Grid RSP will be a function of how companies view the
221 adequacy of the grid premium for a given risk. If the grid premium is approximately the
222 same as the company's own risk-based premium, the company might prefer to keep the risk

223 on their own books. The upper limit to the size of the Grid RSP is, of course, a direct
224 function of how many risks in the province are impacted by the grid.

225

226 For the Non-Grid RSP, companies can transfer up to 4% of written exposures not transferred
227 to the Grid RSP. This Pool is designed to help companies cope with the “take-all-comers”
228 environment in the province.

229

230 In a competitive market, most insurers tend not to target the entire universe of private
231 passenger automobile risks. Insurers generally each have their areas of expertise and a
232 healthy competitive marketplace tends to allow a proper mix of generalist and
233 specialist/niche private passenger automobile writers. Moreover, because it is a practical
234 impossibility to have a perfect price for every risk, most insurers choose to have risk
235 eligibility rules to complement and protect their respective pricing structures. An
236 underwriter faced with a requirement to accept a greater degree of risk than that
237 contemplated by the company’s classification system and rates can transfer that risk to the
238 Non-Grid RSP. The Non-Grid RSP has a relatively low limit to ensure that it does not
239 become used as a marketing tool. That is, without such a limit, companies could deliberately
240 adopt a strategy of under-pricing certain risks to attract new customers. Because these risks
241 could then be transferred to the Non-Grid RSP, and because of the way all insurers share in
242 the results of the Pool, this would amount to companies growing their businesses at the
243 expense of their competitors.

244

245 The key point here is that RSPs are designed as mechanisms to promote stability in the
246 marketplace by making it possible for companies to accept risks they believe are not
247 adequately priced. Therefore, the general expectation is that RSPs by their very nature will
248 operate at a financial loss. It is also important to note that because the RSPs also act as a
249 cross-subsidization mechanism across the industry, at any given point in time, companies
250 will have their own, unique, financial results vis-à-vis the Pools.

251

252 **APPENDIX II: RISK SHARING POOLS - PROVISION FOR THE ALBERTA MIR**
253 **DECISION**

254
255 **BULLETIN NO.:** F08 – 079

256
257 **DATE:** OCTOBER 9, 2008

258
259 **SUBJECT:** ALBERTA RISK SHARING POOLS – PROVISION FOR THE
260 ALBERTA MIR DECISION

261
262 *A copy of this bulletin should be provided to your Chief Financial Officer and to your*
263 *Appointed Actuary.*

264
265 The purpose of this bulletin is to provide members with information about an additional
266 provision for IBNR and Development that will be included in Monthly Member Operational
267 Reports, beginning with the September 2008 Reports. The information included with this
268 bulletin is sufficiently detailed to allow a member company to estimate its share of the
269 additional provision, and to reflect it in advance of the release of the September 2008
270 Reports, should the member so choose.

271
272 **Background**

273
274 On 8 February 2008, the Alberta Court of Queen’s Bench released its decision striking down
275 as unconstitutional the October 2004 Minor Injury Regulation (“MIR”) in that province,
276 which limited awards for non-economic loss on minor personal injuries as defined by a
277 verbal injury threshold. The matter is currently before the Alberta Court of Appeal, and
278 ultimately may be decided by the Supreme Court of Canada.

279
280 Due to the uncertainty this created for the valuation of policy liabilities, and the data and
281 time limitations encountered in trying to address that uncertainty, the financial statements as
282 of 31 October 2007 for the Facility Association Residual Market, the Alberta Grid Risk
283 Sharing Pool, and the Alberta Non-Grid Risk Sharing Pool were each released containing
284 qualifications by both the auditor and the actuary.

285
286 The Operational Reports released to date (i.e. up to and including the August 2008
287 Operational Report) have not included an explicit provision for the effect of the MIR
288 decision, except in the form of a loss ratio “freeze” described below. Pending the
289 development of an explicit MIR provision, the ultimate loss ratios for the Alberta Risk
290 Sharing Pools were frozen at the level estimated at 30 September 2007. Elimination of the
291 loss ratio freeze is a one-time change, to be made coincident with the introduction of the
292 MIR provision.

293
294 The provision described in this bulletin is based on estimates derived in the course of the
295 most recent quarterly valuation of the Risk Sharing Pools (i.e. as at 30 June 2008), as well as

296 members' responses to a recent survey conducted by Facility Association. The underlying
 297 assumptions will be reviewed in light of any significant information and events as they arise,
 298 including the results of quarterly valuations, additional information from member
 299 companies, and any changes in the status of the appeal process.

300
 301 **Provision for Member Sharing Purposes**

302
 303 The September 2008 Operational Reports are due to be released to members at the end of
 304 October. The reports will include a provision for IBNR and Development made up of two
 305 parts:

- 307 • A provision for IBNR and Development prior to consideration of the Alberta MIR
 308 decision, and
- 309 • A provision reflecting the estimated effect of the Alberta MIR decision.

310
 311 The latter provision is summarized below. Minor changes may be made to these estimates
 312 prior to the release of the September 2008 Operational Reports, but such changes are not
 313 expected to be significant. The effect of this provision will be offset to some extent by the
 314 elimination of the loss ratio freeze described above. The extent of the offset is estimated to
 315 be about \$16 million for the Grid RSP and about \$6 million for the Non Grid RSP, and will
 316 be reflected in the provision in first bullet, above.

317

PROVISION FOR ALBERTA MIR DECISION					
(Assumes a 50% Probability that the Court Decision Will be Upheld)					
	Held at 31/Aug/08	ESTIMATED FOR SEPTEMBER 2008 OPERATIONAL REPORTS			Target to 31/Dec/08
		As at 30/Sep/08	As at 31/Oct/08	As at 30/Nov/08	
<u>Alberta Grid RSP</u>					
2004	0	2,017	2,017	2,017	2,017
2005	0	14,377	14,377	14,377	14,377
2006	0	20,237	20,237	20,237	20,237
2007	0	22,439	22,439	22,439	22,439
2008	0	20,153	22,391	24,631	26,870
Total	0	79,223	81,461	83,701	85,940
<u>Alberta Non Grid RSP</u>					
2004	0	115	115	115	115
2005	0	1,895	1,895	1,895	1,895
2006	0	5,890	5,890	5,890	5,890
2007	0	6,284	6,284	6,284	6,284
2008	0	5,377	5,974	6,572	7,169
Total	0	19,161	19,758	20,356	20,953

318 (Amounts in \$000's)

319

320 The provisions for accident year 2008 will be adjusted each month based on the actual
321 earned premium to date. The amounts shown in the table reflect an assumption that the
322 premiums estimated for accident year 2008 will be earned evenly throughout that year.

323 The provision includes an estimate of the total effect of eliminating the minor injury cap,
324 reduced to reflect an assumption that there is a 50% probability of the February 2008
325 decision being upheld upon appeal. The 50% probability assumption is consistent with
326 Facility Association's assessment that there is no clear indication of the ultimate outcome of
327 the case, whether decided by the Alberta Court of Appeal or the Supreme Court of Canada.

328

329 If a member's assessment of this probability is significantly different from 50%, the member
330 may wish to make an adjustment to its share of the provision. This is addressed in more
331 detail under the heading "Member's Share of Provision".

332

333 For member reporting purposes, the provisions for the Alberta MIR Decision shown in the
334 bulletin reflect the time value of money based on a discount rate of 3.14% per annum, and
335 include explicit provisions for adverse deviations ("PFAD"), in accordance with the
336 standards of practice of the Canadian Institute of Actuaries. The PFAD includes a provision
337 for claims development based on a margin of 15%. The discount rate will be revised
338 periodically, in conjunction with quarterly valuations.

339

340 Additional information and assumptions are outlined in Appendices 1 and 2, attached.

341 **Member's Share of Provision**

342 A member's share of the Alberta RSP MIR provisions can be computed by applying share
343 ratios to each of the amounts shown in the preceding table. Share ratios vary by RSP (Grid
344 and Non Grid) and by accident year. Current share ratios can be found in the August 2008
345 Operational Report. Please refer to Page 3 of that report.

346

347 A member's share may be adjusted to reflect a probability of other than 50% that the
348 February 2008 court decision will be upheld. The following table illustrates the calculation
349 of a member's share, as well as the calculation of an adjusted share reflecting the member's
350 own assessment of the probability that the decision will be upheld. For illustrative purposes,
351 the member's share has been adjusted to reflect a probability of 33%, i.e. an adjustment of
352 $0.66 = 33\% / 50\%$.

353

354

ALBERTA GRID RSP – MIR PROVISION AT 31 DECEMBER 2008					
SAMPLE MEMBER SHARING CALCULATION					
Accident Year	Grid RSP Target to 31/Dec/08 (1)	Member's Share Ratios (2)	Member's Share of Provision (3)=(1)x(2)	Member's Probability Adjustment (4)	Adjusted Member's Provision (5)=(3)x(4)
2004	2,017	3.50%	70.6	0.66	46.6
2005	14,377	4.00%	575.1	0.66	379.6
2006	20,237	4.50%	910.7	0.66	601.1
2007	22,439	4.00%	897.6	0.66	592.4
2008	26,870	4.00%	1,074.8	0.66	709.4
Total	85,940		3,528.8		2,329.1

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(Amounts in \$000's)

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A similar calculation may be used to determine the amount of the Alberta MIR decision included in a member's share of the provision for IBNR and Development in the September 2008 and subsequent Operational Reports.

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Although more complex, an adjustment might also be made to the assumption regarding the extent to which the elimination of the minor injury cap might affect claims closed prior to February 2008, as indicated on line (6) of Appendix 2.

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Premium Deficiency Reserve (DPAC)

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The premium deficiency reserve is an amount which, when added to the unearned premium, is expected to make proper provision for the future costs expected to arise on the unexpired portion of in-force policies. In this context, future costs include losses adjusted to reflect the time value of money, claims expenses and administrative expenses.

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Prior to the release of the September 2008 Operational Reports, the estimated future costs will be revised to reflect the estimated effect of the Alberta MIR Decision.

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Measurement Uncertainty

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The establishment of provisions for the unpaid and unreported claims is based on both known facts and the interpretation of current and anticipated circumstances. It is a complex and dynamic process influenced by a large variety of factors. These factors include the experience of the Residual Market and the experience of the voluntary market, involving claim payment patterns, loss payments, pending levels of unpaid claims, claims severity and claim frequency patterns.

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384 The process of determining the provisions necessarily involves risks that the actual results
385 will deviate, perhaps substantially, from the best estimates made.

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387 Should you require any further information, please call Norm Seeney, Vice President,
388 Finance & Chief Financial Officer, Facility Association at (416) 644-4914.

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391 David J. Simpson, M.B.A., FCIP

392 President & CEO

393

394 Attach.

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APPENDIX 1 (Attached to Bulletin F08-079)
FACILITY ASSOCIATION
ALBERTA

ESTIMATED EFFECT OF THE FEB/08 DECISION
REGARDING ALBERTA MINOR INJURY REGULATIONS (“MIR”)

General Comments

- Prior to the August 2008 Operational Report (or July 2008 FARM Participation Report), the provisions for IBNR and Development reported to members made no explicit provision for the effect of the MIR decision, except in the form of a loss ratio freeze described below.
- Pending the development of an explicit MIR provision, the ultimate loss ratios selected for the FARM and RSP’s in Alberta were “frozen” at the level estimated at 30 September 2007, notwithstanding the favourable development observed during the first part of fiscal year 2008.
- Elimination of the loss ratio freeze is a one-time change, to be made coincident with the introduction of the MIR provision.
- Information gathered from member companies was used as the basis for assessing the reasonableness of certain key assumptions.

Key Assumptions

- Estimates were derived as a percentage of the FARM and RSP ultimate incurred losses for accident years 2004 through 2008.
- The FARM estimates are based on the valuation at 31 March 2008.
- The RSP estimates are based on the valuation at 30 June 2008.

With respect to the February 2008 MIR decision, we assumed the following:

- Reported incurred losses used in the latest valuation (FARM at Mar/08; RSP’s at Jun/08) do not reflect any significant changes in case reserving or payment patterns as a result of the February 2008 decision.
- The October 2004 product reforms in Alberta resulted in a reduction in Bodily Injury losses of about 50% as compared to pre-reform levels.
- About 30% of the reduction to Bodily Injury losses is attributable to reforms other than the Minor Injury Cap.
- There is a 50% chance that the February 2008 decision will be upheld upon appeal.

- 436 • If the decision is upheld, there is a 25% chance that the effect of the decision (i.e.
437 elimination of the cap) would apply to claims closed prior to February 2008.
- 438 • For member sharing purposes, the provision will be discounted at the rate of 3.14%
439 per annum for the Risk Sharing Pools and 3.31% per annum for the FARM. The
440 discounted MIR provisions will include a provision for adverse deviations based on a
441 claims development margin of 15%.

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443 **Future Estimates**

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445 The MIR provision will be revised in the future to reflect the following as applicable:

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- 447 • Revised estimates of the starting point, i.e. the ultimate incurred losses resulting
448 from quarterly valuations.
- 449 • Additional exposure corresponding to the time elapsed from the date of the decision.
- 450 • Consideration of decisions arising from the current appeal or subsequent appeals, if
451 any.
- 452 • Additional information that might be forthcoming from member companies
453 regarding changes in claims handling, claims reserving and claims payment practices
454 pertaining to the MIR decision.

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**APPENDIX 2 (attached to Bulletin F08-079)
FACILITY ASSOCIATION
ALBERTA**

**ESTIMATED EFFECT OF THE FEB/08 DECISION
REGARDING ALBERTA MINOR INJURY REGULATIONS
(Amounts in \$000's)**

	<u>Residual Market</u>	<u>Grid RSP</u>	<u>Non Grid RSP</u>	<u>Total</u>
<u>Open Claims at 31/Dec/08 - Prior to Discounting</u>				
[1] "Gross" Provision on Open Claims at 31/Dec/08	30,608	144,128	35,894	210,630
[2] Probability that Feb/08 Decision is Upheld	50.0%	50.0%	50.0%	50.0%
[3] Net" Provision on Open Claims at 31 Dec/08 = [1] x [2]	15,304	72,064	17,947	105,315
<u>Closed Claims at 31/Dec/08 - Prior to Discounting</u>				
[4] "Gross" Provision on Closed Claims at 31/Dec/08	19,474	58,355	11,320	89,149
[5] Probability that Feb/08 Decision is Upheld	50.0%	50.0%	50.0%	50.0%
[6] Probability that Decision Applies to Closed Claims (25% prior to February 2008, and 100% thereafter)	26.6%	28.3%	29.5%	28.0%
[7] "Net" Provision on Closed Claims at 31 Dec/08 = [4] x [5] x [6]	2,591	8,243	1,668	12,502
<u>Open & Closed Claims at 31/Dec/08</u>				
[8] Total "Gross" Provision Prior to Discounting = [1] + [4]	50,082	202,483	47,214	299,779
[9] Total "Net" Provision Prior to Discounting = [3] + [7]	17,895	80,307	19,615	117,817
[10] Effect of Discounting (Including PFAD) at 31/Dec/08 (The Claims Development PFAD is based on a margin of 15%)	1,190	5,633	1,338	8,161
[11] Total Net Provision, Discounted for Member Sharing = [9] + [10]	19,085	85,940	20,953	125,978
<u>Offset for Elimination of Loss Ratio Freeze</u>				
[12] Approximate Offset for Elimination of Loss Ratio Freeze	-1,727	-16,055	-6,069	-23,851
[13] Effect of Implementation of Explicit Provision = [11] + [12] (Based on Target to 31/Dec/08)	17,358	69,885	14,884	102,127

Note: The "gross" provision is prior to consideration of the probability that the February 2008 decision will be upheld upon appeal.

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The "net" provision reflects consideration of the probabilities identified in rows [2], [5] and [6].

Information Disclosure Statement

The Automobile Insurance Rate Board (the Board) is mandated to annually determine and set premiums for basic coverage. Basic coverage for private passenger vehicles means the insurance coverage statutorily mandated or provided for under sections 627 (third party liability coverage) and 629 (e.g. Section B benefits) of the *Insurance Act*. To enable the Board to do this, it needs to collect or receive information under the authority of section 656 of the *Insurance Act* and sections 4 and 11 of the *Automobile Insurance Premiums Regulation*. The Board is committed to making its rate setting process as open and transparent to the public as possible.

Therefore, this is to notify you that subject to section 816 of the *Insurance Act*, any information (including personal or business information) that is submitted to the Board for consideration in the rate setting process, will be considered made in the context of a public hearing, whether made as a written submission or an oral presentation will be made available to the public upon request to the Board.

I acknowledge that I am submitting the attached information to the Board in the context of an open public hearing in the rate setting process and that, subject to section 11 of the Automobile Insurance Premiums Regulation, A.R. 124/2004, I am not required by law or by the Board to provide this information, that I do so on my own account at my own instance. For these reasons, I understand that the attached information will be routinely made available to the public upon request and I am submitting the information to the Board on that basis.

If you have any questions concerning the management or disclosure of Board information, you may contact the Executive Director of the Board at (780)415-1126.



Signature

May 28, 2009

Date

David J. Simpson, M.B.A., FCIP
President & CEO
Facility Association

Print Name