

August 13, 2021

Tim Bzowey
Executive Vice President, Auto/Insurance Products
Financial Services Regulatory Authority of Ontario (FSRA)
Auto Insurance Sector
25 Sheppard Avenue West, Suite 100
Toronto, ON M2N 6S6

Re: Consultation on Loss Trend Benchmarks based on Industry Data as of December 31st, 2020

Dear Mr. Bzowey,

The Co-operators General Insurance Company (CGIC) has reviewed Oliver Wyman's Preliminary Ontario Selected Private Passenger Vehicles Loss Trend Rates and Reform Factors based on data through December 31, 2020 and is providing the feedback detailed below.

Investment Yield Benchmark

CGIC supports FSRA's consideration in replacing its current minimum investment yield benchmark of 2.25% with a rate selected by each individual insurer that reflects their own investment strategy.

Profit Provision

In Section 4.6, Oliver Wyman asserts that when insurers consider their total profits when setting rates, they should include investment income on capital along with the 5% of premium profit provision explicitly allowed by FSRA. It is worth noting that a contrary perspective is taken by Charles L McClenahan in his article titled 'Insurance Profitability'¹ in which he says the following:

"Most importantly, the calculation should be made at a risk-free rate of return. It must be understood that the insured has not purchased shares in a mutual fund. The existence of an opportunity cost (paying premiums in advance of losses and expenses being paid, when the funds could have been invested in some alternative) does not give the policyholder a claim on some

¹ McClenahan, C.L., "Insurance Profitability," Actuarial Considerations Regarding Risk and Return in Property- Casualty Insurance Pricing, Casualty Actuarial Society, 1999, Chapter 8.
(https://www.casact.org/sites/default/files/2021-03/9_McClenahan.pdf)

part of the actual earnings of the insurer. Should the insurer engage in speculative investments resulting in the loss of policyholder supplied funds, the company cannot assess the insureds to make up the shortfall. By the same token, investment income over and above risk-free yields should not be credited to the policyholders in the ratemaking process.

Finally, investment income on surplus should be excluded from the ratemaking process. Policyholders' surplus represents owners' equity which is placed at risk in order to provide the opportunity for reward. While it provides protection to policyholders and claimants, the surplus does not belong to them. In fact, the inclusion of investment income on surplus creates a situation in which an insurer with a large surplus relative to premium must charge lower rates than an otherwise equivalent insurer with less surplus. In other words, lower cost for more protection. This, in my opinion, does not represent equitable or reasonable rate regulation."

We would be interested to understand Oliver Wyman's perspective on this viewpoint.

Future Trends

For all coverages, the Future Loss Trends begin in 2016 at the *latest*. In other words, the same trend rate is assumed from 2016 and onwards. Oliver Wyman acknowledges that future trend rates should "consider the same historical patterns that are the bases for the past trend rate, *as well as the likelihood that those patterns may change*". While this report does not include speculation about the likelihood of patterns changing, insurers will attempt to understand and anticipate changes in trends so it is not uncommon to have future trends that differ following the experience period.

Individual company experience

Related to the above point, we would like to reiterate the fact that each insurer has a unique mix-of-business and unique claims handling and reserving practices. As a result, one cannot expect the loss trends for an individual insurer to align with the overall industry selections. There is value in understanding the trends in the overall industry. However, we also believe that internal data and insights are valuable for loss trend selections.

Bodily Injury and Accident Benefits

We address Bodily Injury and Accident Benefits together as they are treated similarly. There are a couple general comments we want to address:

Chain Ladder Development method

CGIC has undergone significant reserving practice changes in recent years, as well as many other insurers. Using chain ladder development directly without properly adjusting for historical claims triangles may distort the ultimate claim projection. We acknowledge that this would be challenging for Oliver Wyman to properly account for, so this represents a limitation when using industry data. Given that these two

coverages are long-tailed the less developed years are sensitive to inaccuracies in the selected loss development factors.

Impact of Reform

The future trend rate is based on post-reform (ie 2016 and onwards) data. Regardless of whether 2020 is included or excluded, this represents a relatively short period on which to base reliable long-term trends. Further to the earlier section about Future Trends, we feel it is prudent to consider these limitations (immature, short history) along with the likelihood that historical patterns may change. For instance, it has been historically observed that a few years following reform changes that we tend to see frequency start to increase.

COVID-19 Loss Adjustment Factors

We have reviewed Oliver Wyman's methodology regarding accounting for COVID-19 and support the approach that the historical claims experience should be first adjusted to fully remove the impact of the pandemic and if the proposed rate program is to be in effect during the pandemic, an adjustment should be applied for the impact the pandemic is expected to have on the loss experience during the proposed rating program.

First, it is worth noting that even in a post-pandemic state, there may be some long term impacts that should be taken into account that could affect claim frequency and severity. For example, there is the possibility that there will be fewer commuters with some individuals continuing to work from home which could make future frequency different from pre-pandemic levels.

Second, Oliver Wyman considers the use of the mobility composite metric published by the Institute of Health Metrics and Evaluation (IHME), which represents the decline from typical mobility levels. We agree that this would have an intuitive relationship with claims frequency, but feel that this fails to account for factors associated with the impact that would particularly affect severity, including:

- Pandemic lockdowns orders which hinder the availability/convenience of injury treatments and health care
- Mental health and reduced resiliency of claimants

The inclusion of these factors would be important to bring impacted losses back to its assumed "normal" state or to project the cost level of the proposed rating period.

Third, one limitation of relying on the IHME data is that it only projects through to October 1, 2021. For an insurer using data as of December 31, 2020 for ratemaking purposes, they will likely have much of the risk earned in 2022 and 2023. This means that for ratemaking, insurers are forced to project farther into the future any pandemic-related impacts to rating.