MANITOBA PUBLIC UTILITIES BOARD

Re: MANITOBA PUBLIC INSURANCE CORPORATION (MPI)
GENERAL RATE APPLICATION FOR
2015-2016 INSURANCE YEAR

Before Board Panel:

Karen Botting	- Board Chairman
Regis Gosselin	- Board Member
Anita Neville	- Board Member
Susan Proven	- Board Member
Allan Morin	- Board Member

HELD AT:

Public Utilities Board
400, 330 Portage Avenue
Winnipeg, Manitoba
November 14, 2014
Pages 2173 to 2286

1 APPEARANCES

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3

4 Kathy Kalinowsky)Manitoba Public

5 Michael Triggs)Insurance

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7 Byron Williams (np))CAC (Manitoba)

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1 EXHIBITS

NO.	DESCRIPTION	PAGE NO.
MPI-73	Letter from Byron Williams, dated November 14, 2014	2177

1 --- Upon commencing at 1:01 p.m.

2

3 THE CHAIRPERSON: Good afternoon, and

4 welcome back. This afternoon we're going to have the

5 closing argument of the 2015 MPI GRA by Manitoba Public

6 Insurance, and we'll call upon Ms. Kalinowsky. Thank

7 you also for giving us this exhibit. I believe there's

8 a number attached to this, Ms. Kalinowsky?

9 MS. KATHY KALINOWSKY: Yes, I've been

10 advised by the Board's secretary that it should be

11 marked as MPI Exhibit number 73.

12

13 --- EXHIBIT NO MPI-73: Letter from Byron Williams,

14 dated November 14, 2014

15

16 THE CHAIRPERSON: Okay. Thank you.

17 Did you want to begin your closing argument now?

18 MS. KATHY KALINOWSKY: I'd like to just

19 make two (2) comments first --

20 THE CHAIRPERSON: Okay, sure.

21 MS. KATHY KALINOWSKY: -- on the record

22 prior to jumping into the closing argument. But one --

23 did want to acknowledge on behalf of the Corporation

24 the retirement of Mr. Hollis Singh, and want to thank

25 him very much for a career -- lengthy career devoted to

1 the civil service, whether it was at the United Nations
2 level or indeed at the level at -- in Manitoba, and
3 everywhere in between it seems like.
4 Also want to thank him for the many
5 years of his service at the Public Utilities Board, and
6 I can certainly state that his caring concern has been
7 a hallmark, indeed, of his career. So we did want to
8 wish him the very best for him and his family in
9 retirement, and enjoy. And thank you.
10 I also did note that I received today in
11 my email box was a letter from Mr. Williams dated
12 November 14th, and I believe it has been distributed to
13 the Board now. And I did want to make some comments on
14 that, and it's about using the MCT to set RSR levels.
15 And the position of the Corporation is rather clear on
16 this matter, and it's that no further research is
17 required at this point.
18 The PUB has indicated in its previous
19 order two (2) years ago that DCAT is indeed the
20 preferred approach, and Mr. Williams has made the quote
21 that, and I quote:
22 "The thrust of the deliberations in
23 this proceeding have been on the use
24 of the DCAT."
25 Close quotes. And I'd like to say that

1 that is not completely correct. In fact, MCT has been
2 applied for for the upper level. Of course, it's in
3 the application. It's in Board counsel's opening
4 comments. MCT has indeed been mentioned by all the MPI
5 witnesses in their opening comments, in their
6 presentations. It's been the subject of lengthy cross-
7 examination. There's IRs on the MCT. And there are
8 indeed exhibits on the MCT. And, in fact, his witness,
9 Professor Simpson, was indeed questioned at length in
10 cross-examination by Board counsel.
11 Procedurally, the hearing is over at
12 this point in terms of producing new evidence, and it
13 will be over in a -- a couple of hours as my closing.
14 There's no fur -- further evidence that can be
15 provided. There's no time to prepare materials.
16 Imagine trying to reconvene a hearing so we could ask
17 questions on it, et cetera.
18 And remember that the Board order is
19 required by December 1st. And I'll provide some
20 context for the Board order being required December 1st
21 at the very end of my closing. So at this point, we
22 are indeed asking the PUB to reject this proposal by
23 CAC at this point in the hearing.
24
25 CLOSING COMMENTS BY MPI:

1 MS. KATHY KALINOWSKY: With that, I'd
2 like to go into my closing argument here. And I've
3 reiterated at the beginning the application. So in
4 this GRA, MPI has applied for six (6) specific items.
5 Number 1, premiums charged with respect to compulsory
6 driver and vehicle insurance, which are the rates for
7 service. And that's effective March 1st, 2015.
8 Number 2, it's the 2.4 percent overall
9 Basic insurance rate increase effective March 1st,
10 2015.
11 Number 3, there's an RSR rebuilding fee
12 of 1 percent on each Basic Autopac premium, again,
13 effective March 21st, 2015. There's a minimum or lower
14 RSR target of 194 million in retained earnings based on
15 the result of the 2014 DCAT.
16 Number 5, a minimum or lower RSR target
17 of 213 million in total equity based on the results of
18 the 2014 DCAT.
19 And number 6 is a range above the
20 recommended minimum RSR target. And that's based on
21 the minimum DCAT amount with the upper range based on a
22 hundred percent MCT value. So rates -- that's what
23 we're here for, is the -- this rate application.
24 The Corporation indeed is seeking a 2.4
25 percent increase in premium revenues effective March

1st, 2015. This has been determined by the longstanding PUB-approved rate-making methodology as encompassed in the rate filing. The goal that's accepted by all parties, including the PUB, is for Basic to break even financially.

Break even financially means averaging out the two (2) years of net income for 2015/'16, 2016/'17, and recognizing the effect for the staggered renewal process. Rates are prospectively based on the forecast developed by individuals with an in-depth knowledge of the operational requirements of MPI.

I'll just provide some context around the rate increase, and that was provided at the outset of this hearing. This is only the third time in sixteen (16) -- or sorry, in fifteen (15) years that MPI is applying for a rate increase. Rates have decreased by 14.9 percent over the last ten (10) years. Also, more than $600 million has been rebated to customers in the past fifteen (15) years.

With this year's requested rate increase and the RSR rebuilding fee, MPI is projected to have a net loss of 6.4 million in 2015/'16 but a $17.9 million net income in 2016/'17. This is not the break-even net income for the rating years, because the RSR rebuilding fee needs to generate income to replenish the RSR.

1 There's a following waterfall graph
2 which shows the impact of the various components
3 comprising the 2.4 percent rate indication. And
4 everybody has to have a favourite graph. And, of
5 course, this is Ms. Reichert's favourite graph in the
6 entire application there.
7 So it's a -- a graph that we have
8 utilized for the first time, and it captures a really
9 good visual snapshot of just what is driving the rate
10 increases, which are in red, versus the rate decreases,
11 which are in green. So levelling that all out, it
12 comes out to the 2.4 percent.
13 The important aspect that we spent an
14 awful lot of time dealing with is the very large red
15 block of 3.93 percent, which is the physical damage
16 claims forecast.
17 And the other two (2) areas that we've
18 spent a lot of time discussing are -- in this hearing
19 are the two (2) green blocks, which are the decreases,
20 and that is the impact of interest rate forecast of the
21 2.414 percent and the equity forecast, which is minus
22 1.62 percent. So that would bring down the rates as
23 applied for.
24 So the Corporation continues to
25 demonstrate its commitment to stability throughout the

1 past decade, and it's keeping rates consistently
2 amongst the lowest in Canada for comparable coverage
3 and service.
4 So here's two (2) charts on the history
5 of rebates and rate changes. So the rebate chart,
6 there's the different eras, the GRAs in which the
7 rebates have been provided. And on the right is the
8 applied-for rate increases and the orders given.
9 Of particular note that I would like to
10 draw to your attention are the years twenty (20) -- or,
11 sorry, 2002, in which a 1.2 percent decrease was
12 initially sought and the order granting was zero. And
13 so that's a higher amount. And then 2004, 2.5 percent,
14 and three point seven (3.7) was ultimately granted.
15 Of course, there are other years such as
16 two (2) of the last three (3) years in which a 1.8
17 percent was granted and -- and .9 percent, or it was
18 halved by the Public Utilities Board. In 2012, minus
19 6.8 percent rate decrease was sought, and instead,
20 minus 8 percent rate decrease was granted.
21 So it's important to consider that three
22 (3) times in the past fifteen (15) years, the PUB has
23 ordered a rate lower than applied for, while twice the
24 PUB has ordered a higher rate than applied for. So
25 when compared to the auto insurance rate increases in

1 every other province in Canada, Manitoba has maintained
2 the lowest automobile growth rates in Canada.
3 We have this chart that you might
4 recall from the beginning of the hearing there. The --
5 the light blue line at the top are the unfortunate
6 individuals that live in Alberta, and they have the
7 high insurance rates there.
8 The lowest is dark blue, which is
9 Manitoba, and Saskatchewan and Manitoba are almost
10 right in parallel there together, with Manitoba a
11 little bit less. And the -- the Canada-wide average is
12 the red line with the red squares in it.
13 I can also say that, had MPI rates
14 increased at the same rate as the Canadian average auto
15 insurance rate increases since 2001, Manitoba
16 ratepayers would be paying 60.2 percent more than they
17 are currently paying today.
18 So these three (3) charts, they're
19 really important because I believe it encapsulates one
20 (1) of the challenges that both MPI and the PUB are
21 facing in this rate application, and likely over the
22 next few rate applications.
23 Insurance premiums have decreased by
24 14.9 percent over the past decade, and this does not
25 include the $600 million rebated to Manitobans. So,

1 like freezes in tuitions at universities or civic
2 property taxes, these rate decreases are not
3 sustainable financially over the long term, especially
4 without a negative impact to services, to access, and
5 to coverage by MPI.
6 As always, MPI acknowledges the
7 importance of and the many benefits derived from the
8 public rate-setting process. Basic rates are more
9 fair, more equitable, and rate making at MPI has
10 improved as a result of the PUB process.
11 The Corporation has always supported the
12 need for the PUB to set its Basic rates, and always
13 states that Manitoba ratepayers are much better for it.
14 The financial condition of Basic. Well,
15 vulnerable. That was the word used by Mr. Guimond when
16 Board counsel asked him about how he felt about the
17 financial condition following the second quarter
18 results. And that's transcript page 355. I believe
19 the Board is fully aware of the precariousness of the
20 financial condition of Basic.
21 Basic has experienced two (2) years of
22 losses of 69 and $63 million. The RSR is at $99
23 million, and is projected to decrease to $61 million in
24 the current year. The 2015/'16 indicated break-even
25 rate change deteriorated from 1.7 percent rate decrease

1 that was forecast in the 2014 GRA this year, to the
2 applied for 22.4 percent rate increase in the 2015 GRA.
3 Over the past year, that's a 4.1 percent swing in
4 deterioration.
5 There has been much evidence that with
6 the current interest rates, the 2.4 percent as applied
7 for is not enough. Basic has sustained a two (2) year
8 net loss of $132 million. The further and most recent
9 decline in interest rates only increases the
10 vulnerability of the Basic financial condition.
11
12 (BRIEF PAUSE)
13
14 MS. KATHY KALINOWSKY: So interest rate
15 forecast, the effect. The pivotal question for the PUB
16 to decide in approving rates is, What is the
17 appropriate level of interest rate risk the Board is
18 prepared to embed in the 2015/'16 rates for Manitoba
19 ratepayers? This was laid out in the presentations of
20 Mr. Guimond and Ms. Reichert right at the commencement
21 of the hearing. And it was the subject of extensive
22 cross-examination by Board counsel, questions from the
23 PUB panel members, and of course, the Intervenors.
24 I have -- I have here a definition of
25 interest rate risk, and that's from the

1 PricewaterhouseCoopers report that's provided in the
2 filing and was referred to by Board counsel in her
3 cross-examination. And it states:
4 "Interest rate risk represents the
5 risk of economic loss resulting from
6 market changes in interest rates and
7 the impact on interest rate sensitive
8 assets and liabilities. Interest
9 rate risk arises due to the
10 volatility and uncertainty of future
11 interest rates."
12 Close quote. In general, when interest
13 rates increase, MPI will see favourable financial
14 results. Remember that MPI has approximately $2
15 billion set aside in investments for Basic program,
16 largely for unpaid claims' liabilities of about $1.6
17 billion. The higher the interest rates, the less money
18 that has to be set aside to pay out long-term claims.
19 When interest rates increase, the claims' liabilities
20 decrease.
21 However, when interest rates increase,
22 the value of the marketable bond portfolio decreases.
23 The Basic bond portfolio is approximately $1.3 billion
24 of about which 800 million are marketable. Small
25 changes in interest rates can therefore have a

1 significant impact on investment income. So let me say
2 that again in another way, since it's such an important
3 aspect for the PUB in its rate setting.
4 In a rising interest rate environment,
5 the monies gained from the lower cost of claims more
6 than off sells -- offsets the decreases in the bond
7 portfolio. Thus, the financial results will be better.
8 If interest rates decrease, the Corporation's financial
9 results are worse. Unfortunately, currently we are in
10 a falling interest rate environment.
11 Interest rate forecast and MPI's
12 forecast. Consistently over the past many years, the
13 five (5) major banks and Global Insight have been
14 forecasting increasing interest rates. Generally in
15 each of these years, the forecast has been for interest
16 rates to increase about three hundred (300) basis
17 points over a five (5) year period. Consistently, the
18 forecasts have been higher than what the actual
19 interest rates were, and interest rates have declined
20 even further.
21 It was for this reason that last year
22 MPI changed its forecast from using the average of the
23 five (5) major banks and Global Insight, as was used in
24 previous years, to what the Corporation termed the low
25 interest rate growth, or risk-adjusted interest rate

1 forecast.
2 Based on the direction contained in last
3 year's Board order, the Corporation has reverted back
4 to using the standard interest rate forecast, that
5 being the average of the five (5) major banks and
6 Global Insight. The PUB, in Order 151/'13, reduced the
7 applied for rate from 1.8 percent to .9 percent,
8 partially because of, and I'll quote, the first bullet:
9 "The Board's concern about MPI's new
10 interest rate forecasting methodology
11 which utilized, in part, an in-house
12 adjustment for estimating rates when
13 MPI, by its own admission, does not
14 have any particular expertise in
15 interest rate forecasting."
16 And the second bullet:
17 "Recent changes in interest rates not
18 reflected in the GRA filing that
19 impact favourably on current
20 financial results."
21 End quote. So since then,
22 unfortunately, interest rates have decreased even
23 further, and the financial position of Basic at the
24 second quarter of this year was $14 million worse than
25 budgeted solely due to these lower interest rates.

1 If the PUB choses to use the standard
2 interest rate forecast from March as contained in the
3 filing, then the PUB would be accepting a high level of
4 interest rate risk on behalf of the Manitoba
5 ratepayers. In MPI's opinion, this risk would be too
6 high.
7 If the PUB believes that this time the
8 forecasters will be more accurate than in the past, but
9 they are not, the negative impact on MPI's financial
10 condition and the negative impact on rate stability is
11 just too great a possibility. CAC in its closing
12 argument agrees that the most current forecast be used
13 for the rate application.
14
15 (BRIEF PAUSE)
16
17 MS. KATHY KALINOWSKY: It's important
18 to consider who bears the risk of interest rates not
19 increasing as forecast by the banks. Well, it's
20 Manitoba ratepayers. Mr. Guimond, in his written and
21 oral testimony, referred to the mutual objectives of
22 all of the parties in rate setting.
23 So number 1, provide Basic ratepayers
24 with rate predictability and stability.
25 Number 2, set rates that are just and

1 reasonable.
2 Number 3, offer amongst the lowest rates
3 in Canada.
4 Number 4, ensure the sustainability and
5 financial soundness of the universal Compulsory
6 Automobile Insurance program.
7 Number 5, achieve an actuarial opinion
8 of being in a satisfactory future financial condition.
9 Number 6, provide the ratepayers value
10 for their money paid in rates.
11 And number 7, have a clearly defined
12 process for setting rates publicly.
13 I would strongly suggest to the PUB that
14 those first six (6) objectives are likely unattainable
15 if the PUB sets the 2015/'16 rates based on the
16 standard interest rate methodology in the GRA filing,
17 and then interest rates stay flat or increase only very
18 slightly. One would be very hard-pressed to consider
19 that to be in the best interest of Manitoba ratepayers.
20 So let's take a look now at the details
21 on interest rates. You might recall this graph that
22 Ms. Reichert spoke to at the beginning of the hearing,
23 and this shows the green line is the low growth that
24 MPI submitted in its application from last year. This
25 is from the 2014 GRA. The red line was the standard,

1 and -- from March, and then the black line is the
2 actual. And then the standard was updated in
3 September, so right at the commencement of the hearing,
4 and you can see the red line with the boxes.
5 So what you see is that the forecast was
6 going up for interest rates, and then it's gone down.
7 Since then, of course, it's hovered and even slightly
8 decreased from that point there of the black line.
9 So since the high point of about 2.6
10 percent during last year's rate hearing, interest rates
11 have -- have continued to decrease.
12 So this is for the 2015 GRA. And it's
13 the actual forecasted Government of Canada ten (10)
14 year bond rate until 2016/'17. So again, the black
15 line is the actual. The red line is the standard
16 interest rate forecast. The red line with the boxes in
17 it is the standard that's updated. And the green line
18 is with the load growth as of March 2014. And the
19 green line with the boxes in it is the load growth
20 September 2014.
21 So you can look and see what's hap --
22 happening as at different time points there. And it's
23 a good encapsulation of what has occurred. I'll let
24 Ms. Reichert here explain this, as she did in her
25 testimony. And she stated that:

1 "So if we were filing today, instead
2 of 2.4 percent for the rate increase,
3 this graph, which is slide 45, would
4 indicate that we should be asking for
5 a 3.6 percent rate increase, and
6 that's the difference in what has
7 happened over the last six (6)
8 months. So the reverse of what has
9 happened last year at this time,
10 where we were forecasting lower and
11 interest rates went higher, this
12 year, we forecasted higher and the
13 interest rates are lower.
14 So the impact of that interest rate
15 change is smaller this year than
16 compared to last year, because in
17 order to mitigate the risk of
18 forecasting much higher interest
19 rates instead of dur -- duration that
20 was minus 1.8 in our forecast last
21 year, we are now managing our fixed
22 income portfolio to be at duration
23 one (1) year below our claims'
24 duration.
25 And because of that, it doesn't give

1 us as big a forecast again, but it
2 also protects us a little bit from
3 what -- if the interest rates go
4 down. But regardless, what we're
5 forecasting as a minus one (1) year
6 duration gap, if we use the interest
7 rates that exist today, we would be
8 asking for a 1.2 percent higher rate
9 increase."
10 And that's from transcripts pages 708 to
11 709. So everybody's aware that since the 2015 rate
12 application was filed, interest rates actually have
13 decreased. At the October 31st, 2014, the actual
14 Government of Canada ten (10) year bond rate is 2.05
15 percent. This is ninety-three (93) basis points lower
16 than the 2.9 per -- 8 percent that was being forecasted
17 for October back in March, when the rate application
18 was being filed, and it is lower than any of the
19 forecasters predicted for the end of 2014.
20 We recognize that the PUB is attuned to
21 the risk and to the impact on the Corporation's
22 financial position when the interest rates do not
23 perform as forecasted. As PUB Pre-Ask number 5, the
24 PUB asked how each of the actual interest rates and
25 bank interest rate forecasts have changed since the GRA

1 was prepared.
2 In this timeframe, the Government of
3 Canada ten (10) year bond interest rate had fallen to 2
4 percent, a decrease of eighty (80) basis points from
5 the March interest rate forecast used in the GRA. This
6 results in a forecasted depletion of the RSR to $17
7 million in February 28th, 2015. That's only four (4)
8 months away.
9 During the 1990s, when Basic was in
10 financial difficulties, the RSR was depleted to -- and
11 that should be minus $49 million, so negative $49
12 million. In 1997, the PUB approved a 2.1 percent
13 overall increase in rates and a 5 percent RSR
14 rebuilding fee. And that 5 percent was 2 percent plus
15 2 percent plus 1 percent for the RSR rebuilding fee.
16 And that's in Man -- MPI Exhibit number 31 and from
17 Order 93 of '97. I believe everyone here wants to
18 ensure that we don't repeat that again.
19 The impact to MPI over the two (2)
20 rating years of the application depends on whether the
21 interest rates increase as the banks are forecasting
22 and stay at levels that we have forecasted, or follow
23 historical patterns, staying low and potentially
24 decreasing even more.
25 While the Corporation acknowledges it

1 does not have particular expertise in interest rate
2 forecasting, the Corporation does have significant
3 understanding of the risks facing its rate stability.
4 This understanding of MPI's risk tolerance is something
5 that professional interest rate forecasters cannot
6 claim.
7 Options for the PUB regarding interest
8 rates. What are the options for the PUB as it relates
9 to the interest rate forecast? If actual, interest
10 rates continue to be less for -- favourable than our
11 forecast, and the PUB approves the 2.4 percent rate
12 increase, than the RSR will decrease from its current
13 amount of 108 million as at August 31st, 2014. And
14 that's from MPI Exhibit number 10, which is the second
15 quarter financial report.
16 If interest rates remain at the current
17 actual level and the PUB disallows any rate increase,
18 the RSR will be completely dep -- depleted. And that's
19 MPI Exhibit number 42.
20 Last year, in my closing, I noted,
21 quote:
22 "If interest rates prove to follow
23 the recent financial -- the -- sorry,
24 the recent history of
25 increases/decreases and the PUB

1 disallows any rate increase, the CFO
2 has indicated that she expects that
3 next year, we will be here asking for
4 both a rate increase and an RSR
5 surcharge."
6 Unfortunately, this prediction is the
7 reality of this year's rate application, given even
8 further decreases in interest rates.
9 The following chart provides a snapshot
10 of the different interest rate scenarios and the impact
11 upon net income and the retained earnings. And it's
12 from MPI Exhibit number 69.
13 It provides the seven (7) different
14 scenarios there. And under the shaded components there
15 are what will occur to both net income and to the RSR
16 over the two (2) rating years of this application. And
17 the far right-hand column is the break-even rate
18 requirement, which ranges from 2.4 percent up to 8.6
19 percent.
20 Ms. Reichert spent a fair bit of time in
21 the last day of the hearing explaining this table, and
22 I don't intend to take you through it there. But I
23 thought that would be very helpful to provide that once
24 again and have you reflect upon it in your
25 deliberations.

1 MR. REGIS GOSSELIN: I wonder if I
2 could just interrupt for a second. I just want to get
3 an important clarification. On page 6, the text refers
4 to an RSR of 99 million. And then on page 14, it talks
5 about an RSR of 108 million.
6 MS. KATHY KALINOWSKY: Sure. I can
7 explain that: $99 million was at year end, $108
8 million is at the second quarter financial --
9 MR. REGIS GOSSELIN: Okay. Thanks.
10 MS. KATHY KALINOWSKY: -- six (6)
11 months into the year.
12
13 (BRIEF PAUSE)
14
15 MS. KATHY KALINOWSKY: The 3.4 percent
16 suggestion for the rate increase. At the commencement
17 of this hearing, Mr. Guimond made the suggestion that
18 it was open for the PUB to approve the rate increase of
19 2.4 percent and the RSR rebuilding fee of 1 percent, as
20 combined, 3.4 percent rate increase.
21 This would have the effect of embedding
22 into the rates the 3.4 percent increase, rather than
23 having a separate RSR rebuilding fee of 1 percent.
24 In support of this suggestion that the
25 PUB embed a 3.4 percent increase in rates, Mr. Guimond

1 stated that MPI will meet its mandate and MPI will
2 replenish the RSR. So, quote:
3 "What I'm hoping for is the regulator
4 change their position on the interest
5 rate, that they agree that it's not
6 going to go up, and that they vary
7 the order and put the 3.4 percent
8 towards the Basic rates. I feel that
9 at three point four (3.4), I can meet
10 the mandate. What I'm suggesting is
11 to vary the application and put the
12 3.4 percent towards the Basic rates,
13 and let us take care of the RSR."
14 And that's at transcript pages 362 to 3.
15 And he continues:
16 "And at the end of the day it's a
17 very -- it's a business decision and
18 it's not something that you can go
19 and scientifically determine. It's a
20 judgment call."
21 End quote. Transcript page 365.
22 Furthermore, when questioned by Mr. Williams as to if
23 he was, "correct in inferring that MPI would advise CAC
24 that a 3.4 percent rate increase was desirable?" End
25 quote.

1 Ms. Reichert answered, "Yes". And
2 that's transcript page 1460. And reiterated Mr.
3 Guimond's point that a 3.4 percent rate increase,
4 quote, "looked to be appropriate." End quote.
5 Transcript page 1459.
6 The following table, which is from
7 Volume II rate-making, pages 48 to 50, was updated for
8 a 3.4 percent overall increase and no RSR rebuilding
9 fee. So I'll just leave you, but that -- with that.
10 It just shows by major class the differences that would
11 occur as opposed to what is applied for right now.
12 In summary, in MPI's view, the risk of
13 failing to increase rates by 3.4 percent far outweighs
14 any risk of approving it. There is little risk in
15 approving an increase and significant risk in not doing
16 so, when future interest rates are so uncertain. It
17 really is up to the PUB to determine the risk appetite
18 in approving the rates, and what level of risk they
19 want to pass on to the Manitoba ratepayers.
20 Last year, the PUB used the most recent
21 bank forecast in its decision, and that's certainly
22 open for them to do so once more. Again, I would urge
23 the PUB to reflect back onto those mutual objectives
24 that I mentioned earlier, the seven (7) bullet points
25 for rate-setting, and how these can be accomplished

1 with the PUB's decision on interest rates.
2 So considering the severity of the
3 interest rate risk, the PUB may want to consider
4 providing an even higher rate increase than the
5 suggested 3.4 percent or 3.6 percent, especially in
6 light of the interest rate options chart provided, and
7 noting the highly unfavourable impact on the retained
8 earnings.
9
10 (BRIEF PAUSE)
11
12 MS. KATHY KALINOWSKY: Asset and
13 liability duration matching. The Board members heard a
14 lot on asset and liability duration matching. MPI has
15 a duration matching program that offsets the impact of
16 changes in interest rates on marketable bonds and
17 claims incurred. Since the current forecasted duration
18 gap between income -- fixed income bonds and claims
19 liability is minus one (1) per year -- or minus one (1)
20 year, less than a year, MPI will benefit in a rising
21 interest rate environment.
22 In order to mitigate the impact of
23 changes in interest rates in the past year, the
24 investment policy statement was amended to decrease the
25 gap between the duration of claims liabilities and the

1 fixed income bond portfolio from plus or minus two (2)
2 years to plus or minus one (1) year. This was an
3 intermediate step to reduce the interest rate
4 forecasting and rate-setting risks of MPI. Members
5 will recall that the asset liability management study
6 is expected to be completed by the end of this year,
7 and is to include a recommendation regarding the
8 optimum strategy to manage the interest rate risk of
9 MPI. Our forecast is based on determining the duration
10 of the bond portfolio at one (1) year less than the
11 duration of the claims liabilities.
12 The PUB noted that the interest rate
13 risk could be managed if there was a matching of the
14 assets and liabilities, and then asked why MPI was not
15 proceeding in that direction. I'm not planning to read
16 this lengthy quote in here, but would like it to be
17 part of the record. And I have provided a copy of the
18 filing to the court reporter. But the bold points
19 there are the ones that I'd like the Board members to
20 focus on now, if that's okay for them to read to
21 themselves.
22
23 (QUOTE INSERTED BELOW)
24
25 MS. HEATHER REICHERT: So we are in the

1 process of doing our asset liability management study.
2 We are looking through that study at what the best
3 method to mitigate our risk as it relates to interest
4 rates would be.
5 As we've talked about I think given
6 these just last couple of questions, if in fact
7 interest rates do start to increase, the Corporation
8 does benefit from the fact that, if we have a minus one
9 (1) duration between the assets and the liabilities,
10 and the interest rates are increasing, there is a net
11 benefit to our bottom line.
12 Now, the whole question is: If we see
13 those interest rates going up, we have to make a
14 decision on whether or not we try to capture some of
15 that benefit into our net income, or whether or not the
16 risk of interest rates going up a bit and then dropping
17 more is significant enough for us to say, No, we should
18 be matching more -- more precisely sooner.
19 So it really is a decision that, when we
20 get all the information in front of us on what the best
21 matching strategy might be and what's happening with
22 interest rates at the time that we have all that
23 information, determining whether or not it's
24 appropriate to delay somewhat in order to get the
25 benefit depending on our assessment of the risk at that

1 point in time of whether they're going to go up or if
2 they're going to stay flat or if they might be going
3 down.
4 If we see that they're staying flat and
5 they're going to be going down, then as CFO, I am going
6 to definitely be saying, No, this is unacceptable risk
7 to the Corporation, and we need to be more closely
8 matching as soon as possible.
9 So it will be a determination based at
10 that point in time when we have all the information in
11 front of us.
12
13 (QUOTE CONCLUDED)
14
15 MS. KATHY KALINOWSKY: Okay. Given
16 current increasing interest rate forecasts, if the
17 Corporation had continued to keep fixed income bond
18 durations two (2) years lower than the duration of
19 claims liabilities throughout the two (2) year rating
20 period, the average net income would have been
21 approximately $3.1 million higher. And that's MPI
22 Exhibit number 33.
23 While it may seem foolish of the
24 Corporation not to take advantage of forecasting this
25 higher income and therefore a lower overall rate

1 increase, to do so actually would further increase the
2 risk. If the increasing interest rates as forecasted
3 do not materialize, having a wider duration gap means
4 were are risk of having a more negative result in those
5 years.
6 It was for this reason that while the
7 asset liability management study is underway, the
8 Corporation chose to mitigate some of the interest rate
9 risk. Board counsel inquired on whether MPI intended
10 to manage interest rate risk in asset duration
11 matching.
12 And again, I have a lengthy quote there
13 that I won't read in, but would like to have in the
14 transcript anyways.
15 THE COURT REPORTER: Excuse me, Ms.
16 Kalinowsky. Would you like these two (2) quotes into
17 the transcript?
18 MS. KATHY KALINOWSKY: Yes, I do. I
19 would like them inserted in the transcript.
20 THE COURT REPORTER: Okay. Thank you.
21
22 (QUOTE INSERTED BELOW)
23
24 MS. CANDACE GRAMMOND: And no matter
25 what interest rates do, does the Corporation want to

1 mitigate interest rate risk, or does it want to
2 continue to look for opportunities to take advantage of
3 interest rate shifts?
4 MS. HEATHER REICHERT: As an insurance
5 company, first and foremost we want to be able to
6 mitigate our risk. And to the extent that we can
7 mitigate our risk while potentially looking at
8 opportunities to increase our net income, then we try
9 to do that.
10 But first and foremost, as I said
11 yesterday, as an insurance company, it's about
12 mitigating the risk. As it relates to our investments,
13 first and foremost, is to pay off our liabilities, and
14 then it's to achieve yield. So it's a combination of
15 all of those things that we look at.
16
17 (QUOTE CONCLUDED)
18
19 MS. KATHY KALINOWSKY: Investment
20 income. The investment income forecast is a major
21 component of the rate-setting process. In 2013/'14
22 investment income allocated to Basic was $148 million.
23 Investment income was high in the past year primarily
24 due to $99 million in realized gains from the Canadian
25 and US equity portfolios, which was offset by a $22

1 million loss in the marketable bond portfolio due to
2 rising interest rates.
3 In 2014/'15, Basic investment income is
4 forecasted to be $29 million due to projected losses of
5 $52 million in the marketable bond portfolio. This
6 significant loss is due to even higher increasing
7 interest rates forecasted over the 2014/'15 year. If
8 the impact of increasing interest rates was not
9 included, i.e., the total losses on marketable bonds
10 was zero, then Basic investment income would be
11 approximately $81 million in 2014/'15.
12 Investment income, both the forecast and
13 actual, has fluctuated greatly in the past.
14
15 (BRIEF PAUSE)
16
17 MS. KATHY KALINOWSKY: We have a chart
18 that is so large it can't fit all on.
19
20 (BRIEF PAUSE)
21
22 MS. KATHY KALINOWSKY: It can fit on --
23 now it can fit on, but you can't read it. Sorry about
24 that. You -- you do have copies there. But I did want
25 to take you to the -- the third-bottom line there which

is, "Total investment income." And you can see across that line how it varies over the years, whether it's the actuals or whether it's the forecast.

I would also like to state that this was an exhibit that was filed for this year's rate application. We used the five (5) -- five (5) year actual history. Had we used the six (6) year actual history, total investment income in 2008/'09 was $4 million. Just $4 million, that's it. That's the year that the markets crashed, of course. It just shows you the variability there.

With respect to this year of the application, the big amounts of course are the ones that I mentioned, which affect the actuals, are the Canadian equities realized gains which is $57 million there in -- right in the middle of the page, and US equities realized gains of $58 million. That's the real driver of the good investment income for this past year.

(BRIEF PAUSE)

MS. KATHY KALINOWSKY: It was suggested by Mr. Williams that the investment income forecast does not pass the eyeball test. And I just want to

1 say, Could you imagine if Mr. Johnston said, Yeah, I'm
2 just going to use an eyeball test on something. That
3 simply would not be acceptable.
4 The investment income over the past five
5 (5) years for Basic has indeed averaged $97 million.
6 In the next five (5) years, the investment income is
7 forecast to be an average of $74 million. In the last
8 five (5) years, interest rates have declined, resulting
9 in realized and unrealized gains on marketable bonds of
10 an average $19 million per year.
11 In the next five (5) years, because
12 interest rates are forecast to increase, there is on
13 average a $30 million a year loss on marketable bonds
14 forecasted. So if you remove these gains and losses
15 the last five (5) years would average $78 million and
16 the next five (5) years a $104 million.
17 If MPI had used the five (5) year
18 average as suggested by CAC, then the investment income
19 forecast would have been $26 million lower and the rate
20 increase sought would have to be higher by 3 percent.
21 Six (6) years ago, which is one (1) year
22 away from the five (5) year range of CAC's average, the
23 investment income was $4 million, as I just mentioned.
24 Had this been factored into the average, then it would
25 have dropped to $81 million from 97 million and

1 compared to 74 million for the next five (5) years.
2 These are all reasons why MPI does not
3 utilize a simple five (5) year average in forecasting
4 investment income. Instead, MPI uses a very extensive
5 and sophisticated forecast that's developed by three
6 (3) CFAs within the Corporation and details of that
7 forecast are contained in over a hundred pages in the
8 investment income forecast section.
9 MPI currently has $115 million in
10 unrealized gains. The investment forecast estimates
11 that approximately 20 percent of equities will turn
12 over in a year based on past practice of the equity
13 managers. The PUB questioned MPI on whether the sale
14 of those equities with unrealized gains could trigger
15 sufficient funds to avoid the rate increase sought and
16 partially replenish the RSR.
17 Ms. Reichert explained -- and again,
18 this is a very lengthy quote, and I would like it in
19 the transcript, if the court reporter could do that.
20 I'm not planning to read this in, but I will pause for
21 a moment so the Board members can indeed read this.
22
23 (QUOTE INSERTED BELOW)
24
25 MS. CANDACE GRAMMOND: So could the

1 Corporation realize some additional gains of what we're
2 seeing is available?
3 MS. HEATHER REICHERT: Theoretically,
4 yes, we could. But what we have done and what we have
5 done fairly consistently in the past is let the active
6 equity managers that are hired to manage the equity
7 funds make the determination of when the best time to
8 buy and sell the equities are.
9 As I've already stated, we did make a
10 decision through the investment committee working group
11 to take an actual action with respect to the US
12 equities last year. And then in the case of when we
13 need to rebalance, we take action at that point.
14 So how we've been managing the funds is
15 to allow the -- the equity managers to make the
16 determination. And we monitor. And we will take
17 action if we need to from a rebalancing perspective.
18 MS. CANDACE GRAMMOND: I'd like to
19 learn your views and the Corporation's views on -- on
20 this issue. And appreciating what you've just said, in
21 the context of this particular application, with the
22 Corporation asking for a rate increase, the one point -
23 - or the 1 percent, pardon me, rebuilding fee, because
24 it would appear looking at the ratio of market-to-book
25 value that we see on the screen, and I know that that's

1 May 31st, that there -- if the Corporation took the
2 step to realize some gains, that there could be
3 significant impact to the bottom line in the current
4 year which may mitigate the need for what's being
5 requested.
6 So can -- can you comment about that?
7
8 (BRIEF PAUSE)
9
10 MS. HEATHER REICHERT: So, yes, while
11 it -- it is possible that the Corporation could
12 generate some gains by -- by exercising that particular
13 option within the investment policy statement, by doing
14 that, that will then impact on the possibility of
15 future gains. So it'll -- it would be a one (1) time
16 impact now that would then influence the 20 percent
17 turnover and what we forecasted to the future on a --
18 on an ongoing and a more stable -- stable basis.
19 MS. CANDACE GRAMMOND: So the
20 Corporation has elected not to take that step, but
21 instead to maintain the portfolio and apply to the
22 Board, as it has?
23 MS. HEATHER REICHERT: Yes. I mean, we
24 -- we do anticipate, as I said, and we do forecast to
25 sell 20 percent of equity portfolio every year, and to

1 achieve the gains that -- hopefully, gains that would -
2 - would transpire from that.
3 So we -- we take a longer term view not
4 to sell off a larger portion of our -- of our
5 portfolio, and then limit the ability to achieve that
6 20 percent turnover and -- and gains as a result of
7 that turnover.
8
9 (QUOTE CONCLUDED)
10
11 THE CHAIRPERSON: Ms. Kalinowsky, can
12 you let me know when you need a break? I know you're
13 having to do all this talking, so I'm going to rely on
14 you to let us know when you need to stop.
15 MS. KATHY KALINOWSKY: Okay.
16
17 (BRIEF PAUSE)
18
19 THE COURT REPORTER: Sorry, Ms.
20 Kalinowsky, do you have a page reference?
21 MS. KATHY KALINOWSKY: That would be
22 pages 25 to 26 of the transcript -- or, sorry, of the
23 Exhibit 73.
24
25 (BRIEF PAUSE)

1 MS. KATHY KALINOWSKY: Okay, I'll have
2 to find that then. Sorry. I notice that it says,
3 "TR," which is transcript, and no number. I apologize.
4 It is likely the page bef -- oh, no, the next one
5 doesn't have the page number either. We'll just find
6 it and advise. Thank you.
7 So while it may on the surface appear
8 advantageous to recognize all of the accumulated equity
9 gains currently contained in AOCI, to do so would be a
10 very limited short-term benefit. The AOCI has been
11 accumulating over the past five (5) years, representing
12 the unrealized equity gains from the 80 percent of the
13 portfolio that does not turn over in any given year.
14 If the entire equity portfolio were sold
15 tomorrow the Corporation's net income would increase by
16 approximately $115 million. This would have a positive
17 effect on the RSR for the current year but future rate
18 indications would be negatively impacted.
19 The current forecast relies on
20 approximately 16 to $31 million in realized equity
21 gains each year. This helps keep -- keeps rates lower
22 by at least 2 to 3 percent per year. This longer-term
23 view in managing equities contributes to rate
24 stability.
25 Mr. Johnston also noted that. I have

1 another quote there that I'll just let members look at,
2 I won't read in, and we will find the transcript page
3 for that, too.
4
5 (QUOTE INSERTED BELOW)
6
7 MR. LUKE JOHNSTON: If -- if you look
8 at investment income page 5, kind of that main summary
9 in the investment income section -- I think Diana will
10 probably bring it up -- if you look at the line
11 "Canadian Equities Realized Gains," it's about mid-
12 page.
13 So it's not that -- so you're -- you're
14 correct. We do have unrealized gains, but if you were
15 to realize a significant portion of those gains today,
16 these numbers would reduce significantly.
17 We are -- the -- the rate in -- the rate
18 proposal includes the assumption that you're going to
19 realize a lot of those gains that you have and brings
20 down the rate indication. Like these -- the --
21 particularly in the rating period, you can see the 16.4
22 million and the 31 million of assumed realization of
23 equity gains.
24 If we had nothing in the unrealized
25 gains bucket, so to speak, right now, these numbers

would be much lower or non-existent. So if we were to take more gains now, our rate increase would actually go up because there'd be -- these wouldn't be flowing through. The RSR balance would improve, for sure, right? But it's at the expense of future years' rates.

(QUOTE CONCLUDED)

MS. KATHY KALINOWSKY: So the Corporation or the Department of Finance do not intend to sell off its equity portfolio to realize gains as this is a very short-term outlook.

And with that, I'll take Ms. Botting up on her offer of a break. Thank you very much.

THE CHAIRPERSON: How about if we just take five (5) minutes or so, and then we'll start again. We'll take a few more breaks that way.

--- Upon recessing at 1:50 p.m.

--- Upon resuming at 1:59 p.m.

THE CHAIRPERSON: Okay. I think we're ready to begin again. So thank you very much, Ms. Kalinowsky.

MS. KATHY KALINOWSKY: Thank you. I'll

1 move into the RSR minimum and upper ranges section.
2 The purpose of the RSR is to protect motorists from
3 rate increases made necessary by unexpected events and
4 losses arising from non-recurring events or factors.
5 This has been the accepted purpose for more than a
6 decade.
7 Contrary to the suggestion of CAC in its
8 closing argument, there is no confusion amongst the MPI
9 panel of witnesses regarding the purpose of the RSR.
10 It's important for the PUB to know that the Corporation
11 agrees completely with this stated purpose and sees no
12 need to revisit this.
13 The Corporation has applied for a range
14 in the RSR with the lower level of the DCAT, $194
15 million based on retained earnings, or $213 million
16 based on total equity. The Corporation is recommending
17 the 213 million based on total equity and the higher
18 level of the range at the 100 percent MCT, which is 325
19 million.
20 Two (2) of the mutual objectives cited
21 earlier are, first bullet point, ensure the stability -
22 - or sustainability and financial soundness of the
23 universal compulsory automobile insurance plan. And
24 second bullet point, achieve an actuarial opinion of
25 having a satisfactory future financial conditions. MPI

1 believe that all ratepayers will benefit when these two
2 (2) objectives are reached.
3 The PUB is aware that total equity needs
4 to be in excess of $213 million for Mr. Johnston to
5 state in his opinion that MPI in is -- is in a
6 satisfactory financial condition. Currently, the chief
7 actuary cannot provide such an opinion, and he writes,
8 quote:
9 "In my opinion, the future financial
10 condition of Basic is not
11 satisfactory because (I) Basic does
12 not meet the Regulator's minimum
13 capital target under the base
14 scenario in fiscal years 2014/'15 and
15 2015/'16, and (ii) there are
16 plausible adverse scenarios that
17 caused the statement value of assets
18 to fall below the statement value of
19 liabilities over the forecast
20 period."
21 End quote. And that's from Volume II.
22 The DCAT report is in there at page 4.
23 CAC provided a recommendation yesterday,
24 and that was expanded on today quite extensively on
25 their RSR segregation recommendation. We'd state that

1 it is the Rate Stabilization -- it is a Rate
2 Stabilization Reserve for unexpected and non-recur --
3 non-recurring -- not extremely rare -- events. So it's
4 bad weather, it's falling interest rates, it's market
5 collapses.
6 The RSR is not the same as a rainy-day
7 fund or contingency fund like the province may
8 establish. Accounting standards require that all
9 monies received must flow through the income statement
10 and then into retained earnings. Once the maximum RSR
11 level is reached, any excess is reflected in retained
12 earnings.
13 If investment income is higher than
14 forecast, it too will contribute to the RSR. If there
15 is excess retained earnings, some will be due to
16 interest earned on the RSR balance. So would MPI
17 transfer that to the RSR and keep it higher than the
18 upper limit?
19 It appears to MPI that CAC is
20 misinterpreting the purpose of the RSR. CAC has tried
21 to make the RSR narrower than its stated purpose as
22 evident from the following quote in this latest
23 submission. And he quotes:
24 "The stated purpose of the RSR is to
25 protect motorists from a large

1 premium increase that may otherwise
2 be necessary as a result of
3 unexpected events and losses arising
4 from non-recurring events or
5 factors."
6 Close -- close quotes. Then has another
7 quote:
8 "Going back to the sources of the
9 premium increases, the RSR appears
10 intended as protection against only
11 one (1) of the potential sources of
12 premium increases, the extreme
13 event."
14 Close quotes. CAC correctly states the
15 purpose in the first paragraph, but then misstates it
16 in the second, that it is only for an extreme event.
17 The Board has not said the RSR is so limited. It's
18 just CAC attempting to make it be something that it is
19 not. Therefore, MPI does not find any merit in this
20 recommendation of CAC.
21 Rate Stabilization Reserve and capital
22 adequacy. Since the depletion of the RSR in the mid-
23 1990s, MPI and the PUB and Intervenors have spent
24 almost two (2) decades trying to determine the
25 methodology to calculate the level of capital adequacy

1 and range for the rebates. Approaches reviewed,
2 debated, adopted, improved upon, rejected, and
3 considered include: percentage of premiums, risk
4 analysis, and risk analysis/value at risk, Minimum
5 Capital Test, Dynamic Capital Adequacy Test, and back
6 to the percentage of premiums.
7 Percentage of premiums and the Kopstein
8 approach. The Corporation argues that the percentage
9 of premiums approach be abandoned by the PUB for the
10 following reasons:
11 1. The method assumes that MPI's risk
12 level is a function of its annual prem -- premium
13 level. However, MPI's main risks are from changes to
14 assets and liabilities which are significantly larger
15 than annual premiums.
16 2. It does not assist either management
17 or the PUB in the identification, measurement, and
18 mitigation of key risks.
19 3. The method does not create a clear
20 linkage between the required RSR and the amount of risk
21 faced by MPI.
22 4. The indicated RSR range does not
23 change when MPI's risk profile changes.
24 5. To the Corporation's knowledge, the
25 method is not recognized or used by any other Regulator

1 or professional body.
2 6. The methodology is twenty-five (25)
3 years old, and insurance risk measurement has
4 dramatically evolved since then.
5 7. The PUB has ordered a 10 percent --
6 the PUB ordered 10 percent lower level is less than the
7 Kopstein target of 15 percent.
8 And number 8. The rapidity of recent
9 losses totalling $132 million in two (2) consecutive
10 years dramatically demonstrates the inadequacy of the
11 percentage of premium lower level of $83 million.
12 MPI has recommended the DCAT since 2009,
13 because it explic -- explicitly measures the potential
14 financial impact for the Corporation's key risk factors
15 and produces an RSR target that is directly related to
16 the Corporation's risk level. The DCAT is a process of
17 analyzing and projecting the trends of an insurer's
18 capital position given its current circumstances, its
19 recent past, and its intended business plan under a
20 variety of future scenarios. It allows MPI to determine
21 the implications that its business plan has on capital,
22 and identify the significant risks to which it is
23 exposed.
24 Finetuning of the DCAT and adverse
25 scenarios. Since 2009, the Corporation has revised the

1 DCAT and its adverse scenarios based upon questions and
2 podi -- positions taken in the hearing, exchanges at
3 the technical conferences, and directly between the
4 actuaries and, of course, in Board orders. The
5 consensus that the Board anticipated still has not
6 occurred, though. The Board, in 2012, concluded, and
7 quote:
8 "The Board believes that the DCAT
9 methodology is an improved approach
10 for determining the target for the
11 RSR over the current methodology.
12 However, future analysis and
13 discussion is needed, particularly in
14 relation to the adverse scenarios
15 used in the DCAT, and the methodology
16 construct before such an approach can
17 be utilized for rate-setting
18 purposes. The Board is pleased that
19 the Corporation is willing to be more
20 consensus-based in preparing the
21 DCAT, and that it is receptive to
22 aspects of the adverse scenarios
23 being discussed and revised."
24 And that's from Order 157/'12. The
25 Board then ordered a DCAT technical conference to allow

for further analysis and discussion. At the two (2) technical conferences, the Corporation has been respectful and open to suggestions. The Corporation has not been intransigent in its positions.

When the PUB and the CAC actuaries asked for specific incorporations into the DCAT model, these were done. When it became apparent that the one (1) in one hundred (100) event was of concern to the PUB's actuary, MPI rejusted -- adjusted the risk tolerance down to a one (1) in forty (40) year event.

In addition to the DCAT technical conferences, the chief actuary has maintained an open-door policy of working with the PUB and CAC actuaries, which the former has regularly made use of.

At last year's GRA, the Board expressed concerns about lack of transparency in the DCAT. In addition to having this open door to answer questions from the PUB and CAC actuaries, the Corporation filed over three thousand (3,000) pages of information on the DCAT at this hearing alone.

The response of the CAC witness, which was Professor Simpson, has been to criticize the DCAT for setting an RSR target instead of a range, and criticized the manner in which the DCAT scenarios are constructed. The first criticism is surprising, since

1 the DCAT is the minimum lower range of the RSR as per
2 the Corporation's application.
3 The second criticism appears to be based
4 upon not having the actual 2014 DCAT model at the
5 technical conference to review. The Corporation notes
6 that the Board specifically ordered, in Order 151/'13,
7 that the conference take prior to the filing of the
8 2014 DCAT model.
9 With regard to the position of CAC that
10 a one (1) in twenty (20) year risk tolerance be
11 utilized, MPI notes that the risk tolerances has
12 already been adjusted down from one (1) in a hundred
13 (100) to one (1) in forty (40) based on discussions at
14 previous hearings and technical conferences. This --
15 with the PUB's expectations, we believe.
16 A one (1) in twenty (20) would mean that
17 the RSR could be exhausted every twenty (20) years,
18 certainly not desirable from MPI's perspective. This
19 would not enhance rate stability and predictability.
20
21 (BRIEF PAUSE)
22
23 MS. KATHY KALINOWSKY: CAC has argued
24 that the stagflation years should be removed from the
25 interest rate model. MPI Exhibit number 40 -- 41

1 indicates the results of removing these, and there's no
2 effect on the interest rate scenario this year. This
3 is because the current interest rates are only thirty-
4 eight (38) basis points above the mima -- minimum
5 interest rate floor.
6 Whether the change is made or not, this
7 has no impact on the 2014 DCAT result. The res --
8 result was also run in the response to the super DCAT
9 undertaking, and again shows no material change in the
10 DCAT result. As per MPI Exhibit number 42, which is
11 the flat interest rate scenario, there is a $240
12 million impact to the forecast.
13 We can agree that stagflation can be
14 removed, and there will be no impact because of the
15 extremely low levels of interest rates now. So MPI
16 respectfully submits that this is not a good reason for
17 deferring the implementation of the DCAT.
18
19 (BRIEF PAUSE)
20
21 MS. KATHY KALINOWSKY: Differing
22 theoretical approaches to the DCAT. The evidence
23 submitted by CAC reflects the underlying differences in
24 philosophy to determining the range of the RSR. It is
25 this philosophical difference that prevents the

1 consensus hoped for by the PUB from occurring between
2 the Corporation and the Intervenors.
3 The Corporation relies upon a risk model
4 developed by actuarial science and used throughout the
5 insurance industry. The CAC submits evidence that
6 reflects an economist's perspective, emphasizing issues
7 rather than risks. The differences in the two (2)
8 purported methods for determining the size of the RSR
9 are evident in the chart below.
10 I'll just let you take a look at that
11 chart. How best to protect motorists from the risks of
12 unexpected events and losses?
13
14 (BRIEF PAUSE)
15
16 MS. KATHY KALINOWSKY: The role of the
17 DCAT in achieving rate predictability and stability.
18 At the end of the day, when unexpected events and
19 losses occur, those costs have to be paid by Manitoba
20 ratepayers. The questions are when and how much do
21 they pay?
22 The Corporation has emphasized the
23 importance of rate predictability and stability. This
24 occurs when the RSR is of sufficient size to absorb the
25 costs when the ina -- unexpected nonrecurring events

1 arise.

2 Professor Simpson, for the CAC, espouses

3 the economic theory of taxation upon demand. This is

4 evident in his written evidence at page 5. "The only

5 difference being the" -- and I quote, sorry, quote:

6 "The only difference between the two

7 (2) cases is that motorists must pay

8 higher rates initially to establish

9 the RSR of $200 million in the first

10 case and have less money for personal

11 consumption and investment decisions,

12 which seems like a poor arrangement

13 for both motorists and the economy."

14 Close quote. Furthermore, Professor

15 Simpson's recommendation will not result in rate

16 stability and predictability. And that's MPIC

17 Information Request of CAC number 9.

18 "Does Professor Simpson agree that

19 MPI and the PUB should be striving

20 towards the goals of rate

21 predictability and stability which

22 can be accomplished partially through

23 a range for the RSR?"

24 Response:

25 "Yes, but we should recognize that

1 rate stability provided by the
2 establishment of an RSR comes at a
3 cost to motorists in terms of higher
4 rates than would be necessary in the
5 absence of an RSR. Hence, the
6 benefits of the RSR have to be
7 balanced against the costs, like
8 other economic questions."
9 Close quote. If the Corporation
10 operated with the absence of an RSR, the unprecedented
11 loss of $132 million has occurred over the past two (2)
12 years would have to be recovered in a really short time
13 frame. Assuming that an extra $8 million is generated
14 from each 1 percent increase, a rate shock increase of
15 16.9 percent would be required just to recover those
16 losses.
17 An RSR range established to address
18 risks and the losses that occur from those risks can
19 absorb and be rebuilt over a longer period of time,
20 because there is not the same necessity to replace the
21 losses as quickly. Therefore, this removes rate shock,
22 contributes to better rate predictability and
23 stability.
24 So Manitobans value rate predictability
25 and sta -- stability. In 2005, the Corporation

1 developed its value equation whereby price coverage
2 plus service plus access equals value for all
3 Manitobans.
4 Maintaining stable and fair rates has
5 been consistently the strongest driver of good value as
6 a descriptor of Manitoba Public Insurance. Each of the
7 six (6) years the regression analysis has been
8 conducted on the value equation. This variable has had
9 the greatest impact on ratings of good value.
10 Impressions of the cost of vehicle
11 insurance have been con -- a consistent driver of
12 perceptions of value over time. Although some may
13 argue that there is a cost associated with rate
14 predictability and stability, it is tremendously valued
15 by Manitobans.
16 So here's the regression analysis on the
17 relationship of whether good value describes Manitoba
18 Public Insurance 2013. And you can see there that
19 maintaining fair -- stable and fair rates is right at
20 the top of that access, far above anything else.
21 The table above reinforces that
22 maintaining stable and fair rates is the most important
23 factor for Manitobans in determining whether they
24 receive good value from Manitoba Public Insurance.
25 This is a quantitative analysis of what is important to

1 ratepayers as compared to the focus groups used by CAC,
2 which are of a qualitative nature and not
3 representative of the wider public.
4 External actuary's opinion of DCAT.
5 Just as the auditors provide an opinion on the
6 financial statements, the DCAT is reviewed by the
7 Corporation's external actuary and an opinion is
8 provided. The external actuary provided a clean
9 opinion. Here it is. And this is man -- MPI Exhibit
10 number 14. The Exhibit number 14 isn't signed,
11 unfortunately, but we do have a signed copy, but I used
12 the exhibit that was filed here.
13 So it's important to note that -- that
14 the -- the external actuary, Joe Cheng, provides his
15 opinion:
16 "1) That the work of the chief
17 actuary is within the range of
18 accepted actuarial standards of
19 practice in Canada. 2) The
20 assumptions and methods employed are
21 appropriate. 3) The DCAT report
22 accurately describes the assumptions
23 and methodology employed by the chief
24 actuary. And 4) the procedures and
25 systems relied on by the chief

1 actuary are adequate and sufficient
2 to ensure an appropriate level of
3 data integrity and the accuracy of
4 calculations and results."
5 End quote. This can be contrasted with
6 the evidence of the economist Professor Simpson.
7 Professor Simpson attended the hearing and provided
8 evidence as an economist on behalf of CAC. In my
9 cross-examination, I was able to establish that he is
10 concerned with obtaining the smallest RSR possible.
11 He has changed his position over time on
12 how to calculate the RSR. He chose the 10 to 20
13 percent of premiums methodology because it is
14 incumbent, but the PUB has altered this downward from
15 the Kopstein 15 percent. He has not participated in
16 the most recent DCAT technical conference in trying to
17 improve the DCAT. He did not seem to understand that
18 MPI has applied for a range for the RSR.
19 The economic benefit to ratepayers of a
20 $200 million DCAT is $16 million annually based upon
21 actual investment returns, and if that money were in
22 the ratepayers' pockets, they would likely spend it on
23 other things and then have to pay higher insurance
24 rates in the future.
25 He was unaware that SGI uses 75 to 150

1 percent MCT as its target range, and ICBC uses 145
2 percent. MCT is the minimum RSR. And that's in MPI
3 Exhibit number 25. And he had no knowledge of the
4 Board of Directors transferring significant sums of
5 money to the Basic RSR from the competitive lines upon
6 certain conditions.
7 In response to cross-examination by
8 Board counsel and the Board's questions, Professor
9 Simpson was unable to provide any guidance on the low
10 interest rate scenario, other than to deny its
11 plausibility, given the currently unprecedented low
12 interest rate environment.
13 He appeared to conclude that there was
14 no plausible way to model interest rates -- and that's
15 transcript pages 1,739 to 1,742, greatly abbreviated
16 there -- was unable to justify the 1.6 percent rate
17 increase he recommended for 2015/'16 when there is an
18 actuarially indicated shortfall -- and that's
19 transcript pages 1747 to 1751 -- and showed a lack of
20 understanding of the MCT methodology and how it is
21 different from the DCAT.
22 Through all these items, I would
23 respectfully submit that the PUB should not place any
24 weight on his opinion for purposes of deciding upon the
25 DCAT or the RSR.

1 So conclusion on the DCAT. The
2 Corporation believes that now is the time to approve
3 the use of the DCAT.
4 1. The method is based on MPI's
5 specific risk -- risks resulting from changes to assets
6 and liabilities.
7 2. It assists management in the PUB in
8 the identification, measurement, and mitigation of key
9 risks.
10 Number 3. The method creates a clear
11 linkage between the required RSR and the amount of risk
12 faced by MPI.
13 4. The indicated RSR range will change
14 when MPI's risk profile changes.
15 5. It is a clearly documented process
16 which adheres to professional standards and
17 methodology.
18 6. The recent losses totalling $132
19 million in two (2) consecutive years dramatically
20 demonstrates the need for a DCAT-based minimum.
21 7. It is peer reviewed by the appointed
22 actuary and reviewed in detail at these hearings,
23 including by the PUB's actuarial advisor.
24 Through two (2) technical conferences,
25 there's been almost a dozen areas of agreement between

1 the parties in each -- in each of the technical
2 conference -- technical conferences, sorry, and much
3 consensus has been achieved, resulting in an improved
4 DCAT prepared by Mr. Johnston.
5 MPI respectfully submits that by now,
6 the PUB should have enough evidence on and confidence
7 with the DCAT to determine an adequately funded RSR.
8
9 (BRIEF PAUSE)
10
11 MS. KATHY KALINOWSKY: The MCT is the
12 upper range of the RSR.
13 There is consensus on the purpose of the
14 RSR. The remaining issue is how to determine the range
15 of the RSR. The purpose of the RSR should determine
16 the range of the RSR. If the Board wishes to protect
17 ratepayers from the rate increases made necessary by
18 unexpected events and losses arising from non-recurring
19 events or factors, the Board must establish an RSR
20 range that is adequate to meet the costs of those
21 risks.
22 MPI has applied for an upper range to
23 the RSR to be a hundred percent MCT. In making such an
24 application, the Corporation notes that the MCT is
25 being used as a maximum level for capital adequacy, and

1 not a bare minimum as per the OSFI guidelines.
2 A comparison to the sister Crown
3 corporation insurers is important, though it should be
4 noted that the MCT was chosen by management at SGI and
5 the MCT is mandated by regulation of government for
6 ICBC. And that's from MPI Exhibit number 34.
7 For SGI, the Auto Fund has an MCT target
8 range of 75 to 150 percent based on a twelve (12) month
9 rolling average, though it is currently less than this
10 lower range. Effective August 31st, 2013, the
11 Saskatchewan government approved a 1.23 percent fee to
12 replenish the RSR.
13 ICBC does not make the MCT for their
14 Basic program publicly available. However, ICBC has
15 confirmed that their outlook MCT for 2014 is 145
16 percent. Effective November 2012, if the Basic MCT
17 ratio is below 100 percent, the Corporation must file a
18 plan within sixty (60) days for the restoration of the
19 MCT to or above the hundred percent minimum. And
20 that's from MPI Exhibit Number 34. Again, it is
21 important to reiterate that the two (2) other
22 provincial public insurers use the MCT as a minimum,
23 whereas in Manitoba we are trying to use it as a
24 maximum for capital adequacy.
25 In response to the PUB the Corporation

1 is able to show that the new guidelines for the MCT are
2 to be effective for MPI on February 28th, 2016, and
3 will only impact the score by less than 5 percent. And
4 that's MPI Exhibit 52. Therefore, this should not be a
5 reason for the PUB to fail to adopt the MCT as an upper
6 limit this year.
7 The benefits of the minimum capital test
8 are:
9 1. Although it is a minimum capital
10 test, MPI is proposing to use it as a maximum capital
11 test.
12 2. It is designed to assess the key
13 risks faced by the insurance industry, the majority of
14 which are relevant to MPI.
15 3. It's used by all other insurers,
16 including SGI and ICBC, and it's established by OSFI.
17 4. It assesses the riskiness of assets,
18 policy liabilities, and off balance sheet exposures by
19 applying a consistent set of factors that were agreed
20 upon by a task force of insurance experts.
21 5. It identifies the risk based on
22 MPI's current financial statements or current risk
23 profile.
24 6. The calculation of the MCT score is
25 completely objective, i.e. no judgments required.

1 7. The MCT score is relatively easy to
2 calculate.
3 Given that MPI is proposing to use it as
4 a maximum rather than the industry minimum and is
5 proposing a hundred percent, which is lower than any
6 private insurer has for its capital adequacy, MPI
7 considers that the hundred percent MCT to be a
8 reasonable methodology to calculate the top range of
9 the RSR. Mr. Guimond in his testimony also suggested
10 that MPI would be wiling to revisit the level of the
11 MCT to use as the upper limit in four (4) years.
12
13 (BRIEF PAUSE)
14
15 MS. KATHY KALINOWSKY: The time is now.
16 So, in summary, the Corporation recommends that the
17 DCAT be adopted as the method to calculate the minimum
18 lower level of the RSR. The DCAT explicitly measures
19 the potential financial impact from the Corporation's
20 key risk factors and produces a minimum or lower RSR
21 target that is directly related to the Corporation's
22 risk level and directly responsive to the purpose of
23 the RSR.
24 In other words, it is the only method
25 that truly identifies the risks faced by MPI and

1 produces a minimum target that is directly related to
2 the purpose of the RSR. It's within the Board's
3 jurisdiction to approve what Manitoba ratepayers want:
4 predictable, stable rates. An RSR range established
5 using the 2014 DCAT as a minimum and a hundred percent
6 MCT as the upper limit will ensure predictable and
7 stable rates. Six (6) years ago the Board stated,
8 quote:
9 "The Board finds the divergence of
10 views between the Board and MPI as to
11 what should be the RSR range not to
12 be in the public interest and will
13 attempt to bring about a consensus on
14 an RSR range that can be accepted by
15 all parties, Board, MPI, and
16 Intervenors. While the Board will
17 make the final call on the matter, it
18 nonetheless prefers a consensus on
19 this important issue."
20 And that was Order 157/'08. The
21 Corporation respectfully submits that after six (6)
22 years of working on the DCAT through annual hearings,
23 two (2) technical conferences, and numerous direct
24 communications and exchanges of information between the
25 actuaries, that a consensus has been reached between

1 the Board and MPIC.
2 Unfortunately, based on a different
3 viewpoint held by CAC, based on an economic theory of
4 taxation on demand, the consensus hoped for by the
5 Board will not be achieved. It is respectfully
6 submitted that the Board, to use its words, quote,
7 "make the final call on the manner -- on the matter,"
8 close quotes, in this hearing and approve -- approve an
9 RSR range calculated using the 2014 DCAT as the minimum
10 and a hundred percent MCT as an upper level -- upper
11 limit.
12 Transfer from competitive lines to
13 Basic. The Corporation's board of directors so
14 strongly believe in the DCAT, and noting the vulnerable
15 financial position of Basic compared to the two (2)
16 competitive lines of business, that they are willing to
17 replenish the Basic RSR.
18 As indicated in the pre-filed testimony
19 of Mr. Guimond, once the PUB and MPI have agreed on a
20 satisfactory Basic RSR method and minimum target, MPI
21 will be able to go forward and make other business
22 decisions. Basic has sustained unprecedented, in
23 recent decades, financial losses in the past two (2)
24 years.
25 The Corporation, as it has done in the

1 past when faced with significantly adverse financial
2 results, is willing to rebuild the Basis RSR with a
3 transfer of excess retained earnings from its
4 competitive lines of business. The final amount to be
5 transferred and the rate of transfer is yet to be
6 determined but will be based upon the methodology and
7 minimum target in the order forthcoming from this
8 application.
9 In his testimony, Mr. Guimond provided
10 further context and details regarding the intended
11 transfer from the competitive lines to replenish the
12 Basic RSR. The commitment is that we want to close the
13 gap and get to the minimum amount of retained earnings
14 as quickly as possible and within four (4) years,
15 transcript pages 130 to 131.
16 The amount to be transferred is
17 dependent upon the financial results of the Extension
18 and SRA, transcript page 347. MPI will transfer the
19 lion's share of the hundred million dollars as fast as
20 possible prior to the end of the fiscal year if
21 everything works out, transcript 348. The amount to be
22 transferred will likely be more than is currently in
23 the competitive lines of business, as there will be
24 further profits earned this year, transcript 348.
25 It is imperative to move forward on the

1 DCAT. MPI needs to know where the PUB stands on the
2 DCAT and the range of the RSR before any monies are
3 transferred, transcript page 349. If the RSR falls
4 before the PUB-mandated minimum range of $80 million
5 and the PUB does not approve the DCAT, then there will
6 be no transfer of excess retained earnings and the RSR
7 will remain under the PUB target, transcript page 351.
8 This intended transfer of excess
9 retained earnings from the competitive lines to
10 replenish the Basic RSR is quite extraordinary and is a
11 reflection of concern regarding the current financial
12 vulnerability of Basic.
13 Accumulated other comprehensive income.
14 The PUB has asked what MPI's position is on accumulated
15 other comprehensive income for rate-setting purposes
16 and for capital adequacy. The Corporation's position
17 is that calculating break-even rates based on fiscal
18 year net income provides more rate stability than
19 utilizing total comprehensive income, and therefore we
20 do not recommend changing the current methodology.
21 That's MPI Exhibit number 53.
22 With regard to the RSR range, which is
23 to protect ratepayers from volatility, MPI recommends
24 including AOCI which by its nature is also volatile.
25 Retained earnings plus AOCI equates to total equity and

1 the recommended minimum RSR target of $213 million.
2
3 (BRIEF PAUSE)
4
5 MS. KATHY KALINOWSKY: Collision
6 severity. PUB members will recall the waterfall graph
7 that was shown earlier in my presentation in closing
8 arguments that visually shows that of the two point
9 four (2.4) rate increase sought, three point nine three
10 (3.93), so almost 4 percent, is attributable to the
11 physical damage claims forecast.
12 MPI has experienced higher than normal
13 claims frequency based on historical averages in three
14 (3) of the past four (4) years, which is caused mainly
15 by poor winter driving conditions. The Corporation
16 does not believe that this recent experience is
17 reflective of long-term best estimate assumptions.
18 For example, summer collision frequency
19 was tracking at lower than the most recent five (5)
20 year average during the 2013/'14 fiscal year. It was
21 not until December through February that the collision
22 frequency increased significantly above historical
23 norms. Severity, however, is different.
24 The table below shows the historical
25 average severities and severity growth rates for

1 collision repair, total loss, and overall collision
2 claims as at twelve (12) months. The important points
3 are shaded there of the 7.6 percent change in repair
4 severity in the last year, the 9.7 percent increase in
5 total loss severity, and the 10.17 percent increase in
6 total severity over 2013/'14. It's very, very
7 different from the previous years.
8 In light of the 10.17 percent collision
9 severity growth experienced in 2013/'14, MPI conducted
10 a detailed investigation of the underlying causes of
11 the severity growth by component. The chart below
12 shows the breakdown of the increase in collision repair
13 severity. There you have it.
14
15 (BRIEF PAUSE)
16
17 MS. KATHY KALINOWSKY: The chart below,
18 on the next page, shows the breakdown of the 9.7
19 percent increase in collision total loss severity. So
20 you have the 1 percent decrease in salvage return, 8
21 percent is attributable to increase in Vehicle
22 Valuation Tool, and smaller amounts in tax increase and
23 other.
24 The PUB has heard evidence that the
25 Corporation has mitigated some of this impact by

1 reducing and then eliminating the gap between black
2 book and actual settlement values over the past few
3 years. Here we have a chart with the comparison of
4 average black book values versus the actual average
5 total loss claims settlements, and that was spoken to
6 at some length by both Ms. Reichert and Mr. Johnston.
7 And another graph here, the following
8 graph, shows the historical changes in rates as
9 compared to the average annual growth of collision
10 costs over the past decade highlighting the increasing
11 spread.
12
13 (BRIEF PAUSE)
14
15 MS. KATHY KALINOWSKY: The physical
16 damage incurred forecast increased by $26 million in
17 the 2015/'16 rating period. The majority of that
18 increase is attributable to the significant and
19 unexpected 10 percent severity increase in 2013/'14.
20 The remaining proportion is attributable to an increase
21 in the Corporation's forecasted severity growth trend
22 rate.
23 The portion of the total 2.4 percent
24 rate requirement is 3.9 percent for physical damage.
25 As Mr. Johnston stated, when there's a large increase

1 in severity as per what occurred in 2013/'14, the
2 forecast has to be re-baselined. Simply updating the
3 base collision severity forecast accounts for the
4 majority of the $26 million increase in the collision
5 forecast.
6 Last year's collision severity growth
7 forecast for 2015/'16 and 2016/'17 was also updated
8 from approximately 3 percent per year, and that was at
9 the 2014 GRA, to 4.5 percent per year, and that's in
10 this 2015 GRA.
11 The increased trend rate is reflected of
12 the recent historical experience. The five (5) year
13 average is 4.57 percent per year, per the previous
14 table, and the expectations from the business. And
15 that's from transcript page 671.
16 For many years, the collision severity
17 forecast was very stable. However, this year has shown
18 a quick change in growth and severity. The increase in
19 severity and the changes in the industry when -- will
20 unfold in the next number of years.
21 In the meantime, the frequency and
22 severity forecasts are our best estimate for the
23 2015/'16 rates based on long-term results, short-term
24 large increases, and business insight. There is no
25 evidence on the record to show that this is not the

1 best estimate.

2 Increasing physical damage costs. Mr.

3 Guimond's testimony was clear on the present and future

4 significant increases to the collision side of the

5 insurance industry.

6 This was bolstered by the strong

7 presentation of the Manitoba Motor Dealers Association

8 and Automotive Trades Association representatives who

9 have negotiated automotive repair labour rates with

10 MPI.

11 The PUB heard that US regulation on

12 aggressive new average-mileage standards is resulting

13 in manufacturers reducing vehicle weight while

14 preserving safety and driver amenities. This is

15 happening with the use of complex materials in body and

16 chassis construction. As this trend becomes pervasive,

17 the established repair practices inside MPI and the

18 repair industry in Manitoba will be affected.

19 The scope of the change is on par with

20 the shift to uni-body construction and to electronics

21 two (2) or more decades ago. And that's from MPI

22 Exhibit number 18.

23 Evidence was provided that the market

24 shifts are sustained and pervasive. All OEMs are

25 embracing the use of complex materials into their newer

1 models. This trend will not reverse itself. The
2 industry will see a sustained increase in severity.
3 The anticipated cost increases due to
4 more expensive parts and larger repair jobs when these
5 types of materials are involved will be material and
6 will exceed simple inflation rates for cost of growth
7 for vehicle repairs.
8 The repair industry will need to invest
9 in facility changes, new equipment, and more extensive
10 staff training to handle the advent of these
11 technologies. MPI, working with the repair industry in
12 Manitoba, must find a balanced approach to avoid these
13 very real impacts to the overall collision repair
14 costs, and consequently the rates Manitobans pay for
15 Basic insurance.
16 The Corporation intends to offset
17 savings in other areas in physical damaged based on
18 improving efficiencies and better use of resources to
19 offset this expected cost growth.
20 Cost growth in repairs needs to be
21 mitigated by cost savings in other areas such as --
22 that the overall costs are in line with stable and
23 predictable rates. And that's all taken from MPI
24 Exhibit number 18. Some of this is already manifesting
25 itself in current rates, and it'll be evermore present

in future rate applications.

In his closing argument, CAC argued that:

> "The collision claims forecast is clouded by the change in forecasting methodology."

And then identified an extremely minor anomaly that occurred for two (2) months and was immediately rectified. This appeared to be an attempt to cast doubt on the reliability of the collision forecast.

Evidence shows that the increase in PD is because of the new baseline, including the latest actual of the past year, which had a 10 percent increase in severity.

This is the explanation of the change in the forecast and leads to the majority of the 3.93 percent PD increase in the rate application. The collision forecast is completely solid, and it does include the most up-to-date loss experience.

I would suggest maybe this might be a point for a break, if that's all right.

THE CHAIRPERSON: Yes. Why don't we take a ten (10) minute break. Thank you.

1 --- Upon recessing at 2:42 p.m.

2 --- Upon resuming at 3:05 p.m.

3

4 THE CHAIRPERSON: Well, I think we're

5 all back and ready to move forward. Ms. Kalinowsky,

6 would you like to continue with your closing arguments?

7 Thank you.

8 MS. KATHY KALINOWSKY: Yes, thank you.

9 I'd also like to acknowledge two (2) individuals that

10 are in the audience over there. We have two (2) of my

11 colleagues, vice presidents. Christine Martin is the

12 vice president of Service Operations, and Brad Bunko is

13 the vice president of IT and our chief information

14 officer at the Corporation. So they've come to watch

15 and see what unfolds and what occurs at the PUB. So

16 welcome to them.

17 I did want to go on and speak about the

18 PIPP reserve review. And the prior year -- accident

19 years, weekly indemnity ultimate loss estimates were

20 increased significantly in the October 2013 appointed

21 actuary's report. The increase was caused mainly by a

22 review of all existing PIPP claims reserves, which

23 resulted in significantly more case reserves being

24 added than expected.

25 This was subject of lengthy criticism by

1 CAC. MPI can indicate it is benchmarking and, indeed,
2 the current results are even better. Importantly,
3 since we are here for the 2015/'16 rates, we have not
4 assumed that the negative experience of the PIPP
5 reserve review will be repeated. Instead, the
6 assumptions have rev -- reverted to normal in both the
7 forecast and the claims liability review, which is what
8 is important for prospective rate setting.
9 Rate-making principles. The Corporation
10 states that through twenty-four (24) years of these
11 proceedings, it has established rate making and rate
12 setting on a consistent basis that is actuarially sound
13 and statistically based. Rate making is done on this
14 basis as set out in the actuarial statement of
15 principles. Rates are, and have been predicated, on
16 what is actuarially sound and statistically based.
17 The Corporation would urge the Board to
18 not deviate from this basis after two (2) decades of
19 hard work, effort to achieve rates that adhere to this
20 actuarial standard, and are reasonable, not excessive,
21 nor unfairly discriminatory.
22 Motorcycle rates. MPI has applied for a
23 6.6 percent decrease in motorcycle rates. One (1) of
24 the main drivers behind the observed rate changes is
25 the forecasted increase in interest rates, which lowers

1 forecasted investment income, and forecasted PIPP
2 claims costs. This forecat (sic) res -- forecast
3 results in a more favourable outcome for classes where
4 PIPP is a significant component of the class's total
5 claims costs, like motorcycles, where approximately 85
6 percent of the total claims cost is PIPP. Motorcycles
7 have also experienced a decline in loss costs for the
8 past three (3) years.
9 For rate stability purposes, all
10 motorcycle PIPP claims costs are averaged out over ten
11 (10) years. So even though the past three (3) years
12 have seen favourable loss experience for this class,
13 given its small number of unit holders, accompanied by
14 the volatility in their claims history, MPI strongly
15 believes that a ten (10) year historical period
16 continue to be used for rate setting.
17 There is significant variability in the
18 historical loss ratios for the motorcycle major class,
19 given that approximately 85 percent of the claims costs
20 are for injury claims, and more than half of these
21 costs are from a small number of serious loss
22 incidents. The Corporation sets rates for motorcycles
23 consistent with all other classes of vehicles, in that
24 the historical loss experience of the class is used to
25 determine future rates.

1 The Corporation acknowledges that there
2 was a significant re-evaluation of PIPP claims in 2010,
3 which changed both the projected motorcycle loss costs
4 and motorcycle rate indication on a go-forward basis.
5 However, despite the significant change in the forecast
6 -- in the PIPP forecast, motorcycles still have a
7 historical loss ratio that is slightly higher than that
8 of private passenger vehicles.
9 MPI Exhibit Number 67 was provided to
10 demonstrate how the indicated motorcycle rate decrease
11 of seven point three (7.3) was revised to 6.6 percent
12 after application of the experience adjustment rules,
13 i.e. the rate change capping rules. These long-
14 standing capping rules are part of the PUB approved
15 rate-making methodologies and apply to all vehicle
16 classes. The rules have been put in place to control
17 rate shock.
18 The same rules were in place when
19 motorcycle rates were increasing significantly in prior
20 years. Further, all motorcycles that are affected by
21 the experience adjustment cap are already receiving a
22 rate decrease in excess of 10 percent. The Corporation
23 has seen no evidence to support changing the existing
24 rate capping rules.
25 Deductible. There was quite extensive

1 questioning about the possibility of increasing the
2 dedu -- deductible. This is a decision of the
3 Government of Manitoba, as it's contained in the
4 regulations. And since that decision has not been made
5 by government, it's not relevant for the 2015/'16
6 rates.
7 Operating expenses. The Basic average
8 total expenses for the 2015 rating period are 214.1
9 million, a difference of 7.4 million over the 2014
10 rating period, $206.7 million. It is important for the
11 PUB to note that $4 million of this increase is due to
12 an increase in the overall expense allocation to Basic
13 due to higher claims incurred in 2013/'14 and the
14 balance is due to the mix of improvement initiatives.
15 The increases are not due to higher corporate
16 expenditures.
17 Normal operating expenses are incurred
18 to manage the day-to-day operations of the Corporation
19 and exclude initiatives. The slide below indicates the
20 percentage decrease and increase in normal operating
21 expenses for Basic. Importantly, for the year of the
22 application, 2015/'16, the increase in normal operating
23 expenses is less than inflation, at 1.3 percent.
24 I provided a chart there that shows for
25 the year of the application, 2015/'16, it is indeed 1.3

1 percent, and the following year, 2 percent.
2 Normal operating expenses are not the
3 key driver of the requested rate increase. The Basic
4 average normal operating expenses forecasted in the
5 rating years 2015/'16 and 2016/'17 is two hundred and
6 eight (208) -- or sorry, 200.8 million, representing an
7 increase of 1.3 percent and 2 percent respectively.
8 These year-over-year increases are at or below a CPI of
9 2 percent.
10 You heard Ms. Reichert indicate that MPI
11 is containing overall increases in normal operating
12 expenses despite previously negotiated contractual
13 commitments for salary increases of 4.5 percent. And
14 that's transcript page 689.
15 You have here a slide of the
16 compensation expenses, Basic share. And it shows the
17 increase of five point two-seven (5.27) for the year of
18 the application, followed by three point six-six
19 (3.66), the other year of the rating app.
20 She explained why compensation expense
21 fluctuates. There's four (4) main reasons. There's
22 the general wage increases. These are negotiated based
23 on the mandate provided by the Province of Manitoba.
24 There's changes in the number of staff employed. The
25 changes are due to movement on scale, steps on scale,

1 and job classification changes. And there's changes in
2 benefits, both cost and type.
3 Ms. Reichert testified as to the details
4 of how each component is managed or is due to the
5 collective agreement that's already in place. That's
6 transcript page 690 to 695. While the number of staff
7 may have increased slightly, there is an increase in
8 insured vehicles over this period too, thereby causing
9 more work.
10 We have a breakdown here on this next
11 slide of compensation over the last four (4) years and
12 what it is attributable to. The GWI is general rate --
13 wage increase. It has the dollar amount and the
14 average and compounded amount by percentage. Benefits,
15 mainly pension, are the key driver of the compensation
16 increase as per above.
17 And in the next slide, for the next
18 three (3) years, because those were the past three (3)
19 years, the next three (3) years, so including the year
20 of the application, benefits continue to be the key
21 driver of compensation increases.
22 With respect to the vacancy allowance,
23 Ms. Reichert testified that MPI is forecasting to keep
24 more positions vacant in 2014/'15 as part of the hiring
25 freeze that the Corporation had kept vacant in the

1 previous year. Furthermore, the vacancy allowance will
2 increase again in each of the two (2) years thereafter.
3 Transcript page 924.
4 Over this three (3) year period, the
5 vacancy allowance plus actual reduction in permanent
6 FTEs is a saving of $1.8 million. That's transcript
7 page 925. This is the equivalent of reducing the
8 compensation forecast by an additional thirty (30)
9 positions. And that's transcript page 951.
10 While it is true that the Corporation
11 has not identified the specific positions to eliminate,
12 it has reduced the forecasted compensation expense in
13 the rating period by the thirty (30) FTEs referenced
14 above. The Corporation takes seriously its
15 responsibility to provide excellent service to
16 customers while controlling operating costs. Various
17 cost containment initiatives have been implemented.
18 There's a cost containment initiative in
19 instituting a hiring freeze, excluding front line staff
20 where any other positions that become vacant must be
21 reviewed on a case-by-case basis with justification
22 provided in order to be allowed to fill the position.
23 This has already yielded a savings of $1.1 million in
24 addition to the budgeted vacancy allowance for
25 2014/'15, and that's in MPI Exhibit number 29.

1 The PUB heard evidence that the work of
2 the cost containment committee will be embodied in the
3 budget process for 2015/'16. That committee with
4 representatives from each division identifies areas
5 where they may be able to reduce the requirements from
6 the budget guideline which already is targeting a less
7 than inflationary increase for Basic normal operating
8 expenses of 198.8 million. And that's from transcript
9 page 941 and MPI Exhibit number 37.
10
11 (BRIEF PAUSE)
12
13 MS. KATHY KALINOWSKY: We notice what
14 appears to be a contradiction in the position of CAC
15 with regards to consultants. On the one (1) hand the
16 CAC very strongly objected to the Corporation's use of
17 consultants. It states that:
18 "External consultants appear
19 untouchable."
20 These consultants produce a tangible
21 product for the Corporation, but the CAC finds that not
22 changing the budget for these consultants as difficult
23 to fathom. The CAC criticizes the Corporation for lack
24 of cost containment. However, the CAC wishes MPI to
25 hire consultants to conduct an independent review of

1 the management and oversight of PIPP claims in the wake
2 of BI3 initiative, and wants to hire -- or MPI to hire
3 consultants to follow up in the MNP report.
4 MPI is to hire consultants to update on
5 the cost effectiveness of the driver's education
6 program within a reasonable time period, including a
7 follow up to the 2014 AAA study, even though the
8 current driver education program is going to be
9 substantially changed.
10 These reports cost a significant amount
11 of money, a lot of time, and resources of staff at MPI.
12 Furthermore, these are just a few of the CAC
13 recommendations for review that touch on operational
14 matters, whether road safety, PIPP claims management,
15 or physical damage costs.
16 The Corporation continuously manages all
17 operating, maintenance, and capital expenditures. MPI
18 believes it has shown in the evidence, both written and
19 in oral, that it makes these expenditures with the
20 appropriate degree of fiscal prudence whether it is
21 staff numbers, compensation amounts, benefits, data
22 processing, or postage. The test is whether the
23 expenditure is a positive contributor in the
24 Corporation's value equation.
25 In summary, there is simply no basis for

1 the allegation that the management of operating and
2 claims costs is neither reasonable nor prudent.
3 Operating expenses are not the driver of the requested
4 rate increase.
5 Capital expenditures. There are two (2)
6 key types of capital expenditures incurred by MPI in
7 the delivery of the Basic program. There's the
8 administrative capital, including physical properties,
9 and capital associated with project implementation.
10 The table below shows -- shows Basic's
11 share of capital expenditures over the next five (5)
12 years. If you just look at the bottom line there, the
13 total capital expenditure is 33 to 38 million, and then
14 it starts going down, 32 million, 27, 26, 20 million.
15 The pattern of expenditure confirms
16 MPI's commitment to cost containment. Capital
17 expenditures are forecast to steadily and significantly
18 decline throughout the forecast period. This reducing
19 capital investment will ultimately translate into lower
20 amortization and depreciation costs as related projects
21 perceive -- proceed through their life cycle.
22 The major initiative over the next few
23 years is the physical damage reengineering project that
24 will deliver and orchestrate the improvement of the
25 full cycle of physical damage claims management

1 services in partnership with the extended repair
2 industry to meet the evolving needs for quality,
3 safety, cost control, and service.
4 The claims administration process will
5 strive for a seamless interplay with the various
6 incident touch points by leveraging technology, and
7 staying abreast of new and emerging technologies,
8 tools, and processes, and implementing these when
9 prudent and appropriate, resulting in convenience to
10 the customer. Once completely intimum -- implemented
11 in 2019, the physical damage re-engineering program
12 will contribute more than a $13 million reduction in
13 costs, including almost $10 million directly related to
14 reducing claims costs, which is offset by $5.3 million
15 in increased operating costs.
16
17 (BRIEF PAUSE)
18
19 MS. KATHY KALINOWSKY: The PUB inquired
20 at the hearing why the IT costs of MPI are higher than
21 its comparators. Mr. Guimond testified that: 1) the
22 revenues of MPI are $1.3 billion, a much higher amount
23 than the $1 billion on the financial statements when
24 you include the funds collected on behalf of the
25 province for registration fees and taxes. IT

1 infrastructure is in place to collect and remit such
2 monies to the province.
3 Under the Gartner framework, a company
4 with revenues of around $1.3 billion should not have an
5 IT spend exceeding $60 million. And since MPI's is
6 around $45 million, it's $15 million less than the
7 industry expectations.
8 Number 2. Unlike a private sector
9 insurer, the goal of a Crown Corporation is not to
10 maximize revenues. With the lowest rates in Canada,
11 when IT costs are examined as a percentage of revenues,
12 MPI's score will appear less favourable.
13 Number 3. MPI revenues per employee are
14 approximately two hundred thousand dollars ($200,000)
15 than the industry average. As a break-even
16 organization, MPI has concentrated on keeping claims
17 incurred costs low, and consequently, revenues are
18 lower as well. In order to accomplish this, MPI has
19 utilized an IT-intensive approach.
20 4. MPI has also embraced a distributed
21 estimate -- distributed enterprise model whereby it
22 embeds itself from a technology perspective into its
23 business partners, whether it's brokers, glass repair
24 facilities through eGlass, or auto body repair shops
25 through physical damage reengineering to ensure the

1 lowest rates and highest coverage in Canada. And
2 that's from transcript pages 290 to 295.
3 Gartner Consulting has also been engaged
4 for several years to provide IT reviews and
5 benchmarking. The CIO scorecard shows evidence of
6 improved benchmarking results in two (2) key areas: an
7 increase in the IT spend as a percentage of revenue
8 ratio from 7.6 percent to 7.2 percent; and an increase
9 in the IT maturity ratings from three point zero-two
10 (3.02) to three point two-zero (3.20).
11 Achieving improvements in both these
12 metrics is noteworthy and demonstrates that MPI has
13 adopted the correct approach in managing its IT. The
14 IT maturity ratings act to evaluate the effectiveness
15 of the IT organization to deliver the needs of the
16 business. We've provided there a synopsis of the
17 metric -- some of the metrics from the Gartner report.
18 The increase in the overall maturity
19 ratings demonstrates the effectiveness of MPI's IT
20 organization in both supporting and executing business
21 requirements. Moreover, it confirms that MPI has
22 ensured that IT governance efforts are focussed on
23 capturing benefits realization from its IT investments
24 in the form of lower operating expenses.
25 Remember that Gartner has several years

in a row made the analogy that the IT spend at MPI was high because it was fixing the twenty (20) year-old roof. The roof is now repaired, and the IT forecasts show that MPI is moving into more stable IT capital expenditures.

There are two (2) areas that MPI is improving in: IT FTEs as a percentage of company employees, from 18.4 percent to 17.2 percent; in-house IT employees versus consultants ITE -- or IT FTE, which has moved slightly from 37 to 36 percent.

This higher consultant ratio is reflective of the number of significant IT initiatives undertaken. However, MPI will be monitoring its outsourcing and contractor usage levels, and takes precautions to ensure appropriate knowledge transfer takes place so internal resources can be used once its environment stabilizes.

Similarly, the higher IT FTEs should be considered within the context of the overall enterprise sourcing strategy and future state objectives. Higher IT staffing levels may be required until these initiatives are complete.

Finally, MPI will argue that the claims expense per reported claim is one (1) of the most important benchmarking metrics. In this metric, MPI

1 reports two hundred and sixty-three dollars ($263) of
2 claims expense per reported claim, compared to the
3 Canadian Personal Auto Group of eight hundred and five
4 dollars ($805), the Canadian Benchmark Group at nine
5 hundred and thirty-nine (939), and the US Personal Auto
6 Group of five hundred and forty-five dollars ($545).
7 The bench -- that's taken from the benchmarking, Volume
8 II, page 9.
9 This means that, including expenditures
10 on IT, MPI spends significantly less handling reported
11 claims than others in the industry. All IT
12 expenditures have been necessary, prudent, and
13 reasonable on behalf of the Manitoba ratepayers.
14
15 (BRIEF PAUSE)
16
17 MS. KATHY KALINOWSKY: Road safety and
18 loss prevention. Bike Winnipeg noted the issue of the
19 Corporation's role in road safety has been before the
20 Board for a number of years. I note a difference in
21 how this role was articulated by Bike Winnipeg and CAA
22 (Manitoba). CAA Manitoba appears to understand from
23 last year's hearing that MPI has a road -- role in road
24 safety, but that the body with ultimate responsibility
25 for road safety is the government.

However, Bike Winnipeg appears to believe that by moving -- removing the words, quote, "research or educational," end quote, from Section 6(2)(h) of the MPIC Act, the Corporation now has responsibility for road safety in Manitoba. Bike Winnipeg is concerned that the Corporation is ignoring the social costs of accidents in favour of return on investments. This is not the case.

The Corporation's position has been consistent. It has a role in road safety, and it can contribute to safer roads. But it is not the body ultimately responsible for road safety in Manitoba. As such, the Corporation cannot implement a Road Safety Program as broad as Bike Winnipeg would like. As CAA Manitoba understands, this responsibility rests with government.

MPI does have a role in road safety, of course. Everyone agrees that the Corporation should do what it can within its jurisdiction to improve safety for Manitobans using the roads. Messaging against drinking and driving, speed, distracted driving, and educating young people for safe driving and other safety programs are the right thing to do. Whether there is optimal spending on these and other safety programs is an issue the Board has asked the

1 Corporation to consider. Everyone wants to ensure that
2 the appropriate amount of money is spent on the
3 appropriate programs.
4 Ideally, the Corporation would like to
5 report that 'X' dollars was spent on program 'Y', and
6 the result is 'Z'. And based upon 'Z', an assessment
7 can be made as to whether the money spent was optimal -
8 - optimally used. This is what the Corporation
9 understands the Board was looking for in Order 151/'13.
10 Unfortunately, with respect to road safety, it's not so
11 simple an equation.
12 It is impossible to measure the
13 immeasurable. As Mr. Guimond said, We will never know
14 how many children were not hit by a car on Halloween
15 because they were -- because they were wearing a safety
16 flasher. It would be immensely satisfying to be able
17 to point to a particular child and say that she is
18 alive today because she was flar -- wearing the MPI
19 flasher, but MPI -- but people do not report accidents
20 that do not happen.
21 There is the temptation to measure
22 effectiveness by proxy. Compare the differences in
23 accident numbers and costs that occur after a program
24 is implemented to baseline data. Although this is
25 possible, the measurements may have limited or no value

in assessing the effectiveness of a particular program, given the vast amount of variables that can influence such results.

For example, the number of accidents involving young drivers between the ages of sixteen (16) to twenty-five (25) may go up or down one (1) year to the next, irrespective of the quality of the high school driver ed program. Possible factors affecting the number of accidents could be weather, the price of gas, or the employment rate of young people. One cannot make a direct correlation in the measurements, as the results can be misleading both pos -- both positively and negatively. These numbers should be tracked, but care must be taken in interpreting and relying upon such measurements.

The Corporation is proposing to the Board a two (2) part measurement for assessing whether there is optimal spending on safety programs. The first part will entail measuring the effectiveness of its road safety programs globally under the heading of loss prevention.

Because of our mandate and all the myriad of different reasons causing losses and because of the underlying safety message interconnecting many programs, the Corporation believes that the success of

1 its initiatives should be based upon the global impact
2 of the programs. Therefore, the dollar spent versus
3 dollar saved will be measured at the global level of
4 all loss prevention programs.
5 Individual programs will continue to be
6 measured for whether they met the goals of that
7 particular program. For example, there are people who
8 will never drink and drive, others who do drink and
9 drive, and there's many who might be tempted. A
10 particular 'don't drink and drive' campaign may or may
11 not change a person's behaviour, but over time,
12 cultural change occurs.
13 As such, success of a particular program
14 should be based on si -- specifics about the program.
15 Did it catch people's attention? Did the mess --
16 message resonate? Was it delivered to the appropriate
17 audience? This would be the criteria for determining
18 success.
19 How safely Manitobans use our roads is
20 cultural. Improving the safety culture is a long-term
21 endeavour. Measuring the optimum use of safety program
22 funding must be based upon the understanding that the
23 goal is to achieve societal and cultural change. One
24 (1) program does not change a culture. But globally, a
25 number of programs can shift attitudes which, in turn,

1 can change culture, and that's what needs to be
2 measured. The challenge is how to measure this optimal
3 use. The Corporation has put forward what it believes
4 is reasonable and is seeking the Board's feedback.
5
6 (BRIEF PAUSE)
7
8 MS. KATHY KALINOWSKY: The role of the
9 Intervenors at the PUB hearing. A takeaway for the
10 Board to consider is the future role of some of the
11 Intervenors at GRA hearings and what is the best way
12 for relevant information to be brought before the
13 Board.
14 The Board heard from the Intervenors on
15 numerous occasions of the good cooperative and
16 collaborative relationships that Bike Winnipeg,
17 Recyclers, CMMG, and CAA have with MPI. MPI works with
18 each of the organizations and groups on operational
19 matters. The relationships are good and are valued by
20 the Corporation. But the Board has witnessed cross-
21 examination into operational matters and saw that it
22 was not very effective.
23 The Board also witnessed an alternative
24 approach taken by other Intervenors and presenters.
25 You saw the IBAM, the Manitoba Motor Dealers

1 Association, and the Automative -- Automotive Trades
2 Association. I believe the Board found these
3 presentations very informative and useful.
4 This leads one to ask: Is the nature of
5 cross-examination the proper way to discuss and work on
6 and improve operational matters? Does a cross-
7 examination of operational matters discussed between
8 the Corporation and Intervenors help the Board approve
9 rates?
10 The Corporation submits that the
11 response is, no, and encourages all its business
12 partners to work collaboratively with MPI throughout
13 the year on the operational matters.
14
15 (BRIEF PAUSE)
16
17 MS. KATHY KALINOWSKY: So finally,
18 conclusion. The Corporation stands by its application.
19 First, that premiums charged with respect to compulsory
20 driver and vehicle insurance, rates for services are
21 effective March 1st, 2015.
22 There would be a 2.4 percent overall
23 Basic in -- insurance rate increase effective March
24 1st, 2015.
25 Number 3) an RSR rebuilding fee of 1

1 percent on each Basic Autopac premium effective March
2 1st, 2015.
3 4. A minimum lower RSR target of $194
4 million in retained earnings based on the result of the
5 2014 DCAT.
6 5. A minimum or lower RSR target of 213
7 million in total equity based on the results of the
8 2014 DCAT recommended by MPI.
9 And 6) a range above the recommended
10 minimum RSR target based on the minimum DCAT amount
11 with the upper range based on the hundred percent MCT
12 value.
13 With regard to the second point, MPI
14 reiterates the suggestion made by its CEO that the PUB
15 may wish to allow the 3.4 percent in rates and remove
16 the RSR rebuilding fee.
17 Indeed, given the most recent forecasts
18 as contained in MPI Exhibit number 69, the PUB may see
19 fit to provide an even -- even higher rate increase
20 than 3.4 percent, depending upon their assessment of
21 the interest rate risk that ratepayers are willing to
22 accept.
23 The DCAT is indeed ready to be adopted
24 by the PUB to establish the minimum level of retained
25 earnings. The DCAT will vary somewhat every year,

1 given the underlying adverse scenarios and MPI's
2 financial condition. MPI is willing to review the 100
3 percent MCT in four (4) years to provide the Board with
4 comfort that this upper limit is not cast in stone.
5 This application is unique in that the
6 MPI board of directors has communicated its plan to
7 transfer excess retained earnings from its competitive
8 lines to replenish the RSR. Of course, this is
9 conditional upon knowing that minimum retained earnings
10 are prescribed by the DCAT results. Then the board of
11 directors can be confident in ensuring that Basic is
12 financially viable with adequate levels of capital, and
13 therefore can establish the amount of money to be
14 transferred.
15 Contrary to the CAC recommendation to
16 oppose a -- impose a 2.75 percent overall rate change
17 given their perceived lack of MPI -- their perceived
18 lack of MPI's cost control, MPI has provided strong
19 evidence that the operating expenses are not the main
20 driver of the rate increase, and that MPI is
21 controlling these in any event.
22 MPI has explained that rising physical
23 damage costs attributed to changes in the auto
24 manufacturing industry will be managed over the next
25 number of years to mitigate otherwise likely premium

1 increases.

2 So in closing, I would like to say that

3 MPI submits it has satisfied the onus that its rates as

4 applied for are just and reasonable, and requests that

5 the PUB approve them. The Corporation has placed

6 sufficient evidence on the record for the PUB to

7 approve the rates.

8 It is critical for the Corporation to

9 receive the order by December 1st, 2014. This is due

10 to required system changes, drafting of a new

11 regulation of certificates and rates by Legislative

12 Council, there have to be two (2) approvals by Cabinet.

13 And keeping in mind that the first notices to customers

14 for payment of premiums and the renewals occurs on

15 January 15th, so that's forty-five (45) days prior to

16 the March 1st, 2015, effective dates of the rates.

17 So that's some of the context as to why

18 we need the rates -- the rate order by December 1st.

19 Of course, I didn't put in there that there's holiday -

20 - holiday time, of course, being a very important

21 period for many people at that time of the year.

22 With that, I would like to thank very

23 much the many people that put a lot of effort into this

24 General Rate Application. There are enormous amounts

25 of people back at the Corporation that have spent a lot

1 of time putting together this application. I'd like to
2 thank the witnesses that you see. There's the people
3 that come in for the back row. I'd like to thank Board
4 counsel, the advisors for their help, the court
5 reporter, and the Intervenors always provide a
6 perspective that keeps MPI on its toes, and you can
7 always say that the -- the hearing process improves
8 with the interventions.
9 And I would also like to thank the Board
10 members very much. And now it gets very busy for you
11 guys, so thank you very much.
12 THE CHAIRPERSON: Thank you very much,
13 Ms. Kalinowsky. We have some questions from the panel,
14 and I believe we're going to start with Mr. Gosselin.
15 MR. REGIS GOSSELIN: Yeah, I guess -- I
16 do, and I -- and I -- and maybe just in a formulation
17 of your request, and -- and it has to do with the
18 dichotomy between 3.4 percent of rate increase versus
19 two point four (2.4) rate increase plus 1 percent.
20 So on the one (1) hand you're saying,
21 Approve the rates as applied for, and then on the other
22 hand, Let's go with three point four (3.4). So I --
23 I'm having trouble with that, but I think I understand
24 clearly that -- that MPI is seeking 3.4 percent based
25 on the comments that I heard from Mr. Guimond. And

1 that's -- that's my assumption, notwithstanding the
2 fact that we have a bunch of material before us that --
3 that was based on a two point four (2.4) plus 1
4 percent.
5 So -- so I'm not -- I -- I understand
6 the dilemma you're facing in terms of -- but from our
7 standpoint, am I correct in assuming the request is 3.4
8 percent of a rate increase?
9 MS. KATHY KALINOWSKY: Yes, it is. I
10 was being very technical and very lawyerish by saying
11 2.4 percent as applied for, recognizing that there was
12 no formal amendment to the application.
13 MR. REGIS GOSSELIN: Now -- now the --
14 the discussion around the -- the DCAT, I guess I'm
15 trying to situate the comments -- the -- the offer that
16 was made by MPI of the actuary acting on behalf of PUB
17 to hold the pen. So, you know, the app -- the material
18 before us today suggests, accept the DCAT. But we
19 haven't completed the work that relates to the holding
20 the pen offer.
21 So could you give me your comments about
22 that?
23
24 (BRIEF PAUSE)
25

1 MS. KATHY KALINOWSKY: Thank you. It's
2 always difficult to provide great responses on very
3 technical aspects, but, you know, it's -- you're --
4 you're asking about the pass the pen to Pelly approach
5 versus accept the DCAT now, from what I understand of
6 your question.
7 And I can say that all the requests that
8 were made in that DCAT super-undertaking be --
9 responded to several of the requests already. And Mr.
10 Johnston on the record I believe has made the case that
11 this is the information that's already been provided in
12 the response to this super-DCAT undertaking that the
13 PUB needs to make its decision on the DCAT.
14 There are other items still outstanding
15 that he's acknowledged. And those will be provided
16 over the next year, but they are not going to
17 materially change the result of the 2014 DCAT.
18 We want to very much encourage the
19 adoption this year of the DCAT. It's been five (5)
20 years. You asked the question yesterday of Mr.
21 Williams about, you know, Are we ever going to get to
22 the end of the DCAT, was the thrust of your question.
23 We think that we are there right now.
24 The DCAT is always going to improvements to it.
25 There's adverse scenarios. Those will change every

1 year as new risks are identified, and indeed those
2 risks quantify differently over time. There are --
3 it's based on the financial situation that MPI is
4 currently is.
5 So we think that the pass the pen to
6 Pelly approach is going to be an ongoing approach that
7 occurs over the year, and so that when Mr. Johnston
8 next year is putting forward some adverse scenarios and
9 including different types of -- of data, he can pick up
10 the phone and say, Okay, you know, Brian, what's --
11 what's up with this? What's up with that? and get to
12 more of a finalization and an improvement over time.
13 But at this stage, we're very much
14 thinking that the DCAT is not going to change based
15 upon any of those information that was requested in
16 that DCAT super-undertaking, and that it's very much
17 the time is now to go with the DCAT.
18 MR. REGIS GOSSELIN: Now, there -- I
19 want to challenge one (1) of the statements you have in
20 your -- in your closing arguments, and that's on page
21 42. Page 42, which is the discussion around MCT as the
22 upper range of the RSR. And the statement there is,
23 There is consensus on the purpose of the RSR. And I
24 would venture to say that there isn't consensus, based
25 on what I heard from Mr. Williams yesterday.

1 In other words, he's saying the RSR was
2 designed for a certain set of events, cer -- certain --
3 was a certain construct, and -- but the -- the way in
4 which it's actually performed is that it's been used as
5 the rainy day fund for all kinds of events that
6 influence income of MPI -- the net income of MPI. So,
7 in other words, if you have a bad year, you know, the
8 RSR is taken down to cover off the bad year. So in
9 reality, the RSR functions just like regular retained
10 earnings.
11 And so to what extent are we served by
12 having a -- a RSR construct, particularly in the face
13 of the evidence that we heard from Mr. Williams that
14 consumers don't understand what an RSR is? They
15 understand retained earnings, but they don't understand
16 RSR. So I'd like to hear what you have to say about
17 that.
18
19 (BRIEF PAUSE)
20
21 THE CHAIRPERSON: Excuse me. This is
22 to the MPI panel over there. If you would like to just
23 give us something in writing when -- you know, later,
24 that would be just fine. You don't have to be -- spend
25 a lot of time developing a position at this point. We

1 would appreciate that.
2 MS. KATHY KALINOWSKY: Yes, we'd like
3 to very much realize that this is something extremely
4 important and -- for the Public Utilities Board and for
5 the Corporation. So there's lot of input. You saw a
6 lot of flurry of activity, et cetera, people handing
7 notes and so on like that, so we very much welcome the
8 opportunity to get something in very quickly. Thank
9 you.
10 MR. REGIS GOSSELIN: Now, I wanted to
11 talk about the duration mich mas -- duration mismatch
12 issue. And very specifically, the concern I have is
13 around the continuing position that MPI is in, where
14 you still have a one (1) year mismatch.
15 And based on the evidence that I've
16 seen, you're much more affected by a drop in rates than
17 you are by an increase in rates. In other words, if
18 you're duration mismatched the way you are, you end up
19 losing more money in a drop in -- in a -- in a interest
20 rate environment where rates are dropping than you are
21 if you're in the other environment, where rates are
22 increasing.
23 So -- and I guess the other piece that
24 is related to that is because of the duration mismatch,
25 there was a statement made by Mr. Williams that you've

1 lost hundreds of millions of dollars over the years
2 because of this mismatch, and I think that's a
3 statement that needs to be addressed by MPI. It is on
4 the record, and I'd like to hear what you have to say
5 about that.
6 And I think his statement was related to
7 the fact that we've been in an environment of dropping
8 interest rates, successive drops in interest rates over
9 the last five (5) to six (6) years, and the duration
10 mismatch is not working in favour of MPI.
11 I fully realize that, you know, you
12 weren't tracking this until a few years ago, but now
13 you're in a situation where I heard Mr. Guimond say,
14 you know, Rates are not going to go up, and yet you're
15 saying, Let's wait for a study before we make a
16 decision. So I'd like to know what your -- why you --
17 you're clinging to that duration mismatch issue.
18
19 (BRIEF PAUSE)
20
21 MS. KATHY KALINOWSKY: Thank you for
22 your question. We understand it's with regards to the
23 duration matching and the continuing position of MPI
24 with retaining the plus or minus one (1) year mismatch
25 and, of course, as you stated correctly, that we're

1 more affected by a drop than an increase.
2 We'd would like to state that, yes, in
3 the past when interest rates declined, then we were at
4 plus or minus two (2) in duration. Since that time
5 when we started to analyze it and monitor it, we've
6 gone down to plus or minus 1 percent in our investment
7 policy statement -- one (1) -- one (1) -- sorry, plus
8 or minus one (1) year in the investment policy
9 statement to mitigate this as we do the study.
10 The study is currently being done.
11 We're expecting it. There's testimony from, I believe,
12 Ms. Reichert saying that it's going to be done by the
13 end of this year, meaning calendar year, so it's
14 December. It's within, you know, a -- a month that
15 it's going to be done. We are going to be looking at
16 the entire strategy then, and executing upon it at that
17 point.
18 And finally, we did take a hit, so to
19 speak, when interest -- on the -- on the way down, so
20 to speak, and we'd like to benefit when the interest
21 rates do increase, so we're continuously monitoring it.
22 We think we are on the cusp of having something
23 changed. It's not in time for this hearing,
24 unfortunately.
25

1 (BRIEF PAUSE)

2

3 MS. ANITA NEVILLE: The hour is moving
4 on, so I'll -- I'll try and be brief. I was just
5 reviewing the closing testimony of Bike Winnipeg and
6 Mr. Monnin, and I'm struck by the lack of response by
7 MPI that cited -- to the Board order cited by Mr.
8 Monnin on road safety.
9 You have developed a new construct of
10 loss prevention, which is fair enough in itself, but it
11 strikes me that there's a great deal more that has not
12 been addressed. And it's been put forward in Board
13 orders, and perhaps you're arguing jurisdictional
14 issues with it, but I think that has not yet been
15 resolved, and the fact that MPI has not responded to
16 those Board orders requires some comment.
17 It's rather convoluted, I'm sorry.
18

19 (BRIEF PAUSE)

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21 MS. KATHY KALINOWSKY: Bike Winnipeg
22 preven -- presented a lot of different points in its
23 closing testimony, as did all of the Intervenors.
24 Indeed there was, I believe, six and a half (6 1/2)
25 hours of closing testimony yesterday. And I -- in my

1 closing, I responded to many, many aspects. But you --
2 I would agree that I did not respond directly to that
3 one (1) aspect of Bike Winnipeg.
4 The lack of response is in no way,
5 shape, or form to -- to portray MPI as dismissive of
6 it. And -- but I do want to say that it's our intent
7 as part of this new construct, this loss prevention
8 model, which, if the PUB accepts this model, then next
9 year we can move forward on a lot of those items in
10 this loss prevention framework.
11 We are, of course, administrators of the
12 plan on behalf of the Government of Manitoba, and we
13 believe that we can satisfy some, not all, of PUB's
14 demands in this loss prevention framework. And it
15 gives us more leeway and more latitude. And we will,
16 of course, always ensure that we stick within our
17 jurisdiction and -- but we believe that a lot of the
18 things can be placed in this new construct of the loss
19 prevention framework for next year.
20 MS. ANITA NEVILLE: Thank you.
21 THE CHAIRPERSON: Well, this concludes
22 the 2015 Manitoba Public Insurance Corporation general
23 rate application hearing. On behalf of the Board
24 panel, I'd like to thank everyone for their cooperation
25 throughout this hearing. This includes the front row

1 of MPI, Mr. Guimond, Ms. Reichert, Mr. Johnston, and
2 Mrs. Kalinowsky. And, of course, the MPI staff behind
3 the scenes there as well.
4 Our Intervenors, CAC, CMMG, CAA, ARM,
5 Bike Winnipeg, and IBAM. All the presenters who came,
6 the associate and acting secretary of the Board, Ms.
7 Jennifer Dubois, and our document manager Ms. Diana
8 Villegas. Our court reporter, Ms. Cheryl Lavigne. Our
9 counsel Ms. Grammond, and our -- of course, our
10 advisors Mr. Cathcart and Mr. Pelly.
11 I would also like to thank Mr. Guimond
12 for appearing throughout the hearing process. Your
13 presence and input has been very much appreciated.
14 The -- the Board also appreciates the
15 member of the -- members of the public who took time to
16 sit in on the hearing during the course of the
17 hearings. And the panel -- just to let you know, the
18 panel will be meeting in the very near future to
19 deliberate and make our final determinations on the
20 matters before us.
21 However, before we depart, I'd like to
22 extend my best wishes to everyone for the upcoming --
23 coming holiday season.
24 So that's concludes our hearing, and
25 enjoy your trips and holidays and whatever.

1 MS. ANITA NEVILLE: Travel safety.

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3 --- Upon adjourning at 4:07 p.m.

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5 Certified correct,

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10 Cheryl Lavigne, Ms.

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