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 5, 2014
Pages 1424 to 1781

1 APPEARANCES

2 Candace Grammond)Board Counsel

3

4 Kathy Kalinowsky)Manitoba Public

5 Michael Triggs)Insurance

6

7 Byron Williams)CAC (Manitoba)

8 Meghan Menzies)

9 Landon Hermary)

10

11 Raymond Oakes)CMMG

12

13 Angele Young)CAA (Manitoba)

14 Mike Mager (np)

15

16 Irvin Frost (np))ARM

17

18 Christian Monnin)Bike Winnipeg

19 Jason Carter)

20 Charles Feaver (np))

21

22 Dave Schioler (np))IBAM

23

24

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EXHIBITS

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1 --- Upon commencing at 9:04 a.m.

2

3 THE CHAIRPERSON: Well, welcome back,
4 everyone. And we're glad to see you're feeling better,
5 Ms. Kalinowsky, or a little bit anyway. We're going to
6 start this morning with the continuing cross-
7 examination by Mr. Williams from CAC. And that will
8 begin our day. So, Mr. Williams?
9 MR. BYRON WILLIAMS: Thank you, and
10 good morning, members of the panel. With your
11 permission, I should note that Ms. Desorcy was here all
12 day yesterday, and -- and I neglected to -- to
13 acknowledge that. And she has asked me -- just we know
14 Mr. Singh is retiring, so with your permission I just
15 have a very brief comment on behalf of CAC.
16 We just want to acknowledge Mr. Singh's
17 outstanding career as a public servant, both in
18 Manitoba and internationally. And if our memory serves
19 us right, I think it dates back to pre-Ms. Schreyer
20 when he first joined the -- the public service. And he
21 certainly had many important milestones in his career.
22 In the 1970s he was at the forefront of
23 the first rent regulation in Manitoba. In many ways,
24 he capped his career with an outstanding contribution
25 to the NFAT hearing, as well. And his intellectual and

1 academic abilities are -- are well known, but our
2 client recalls him best for the human face that he gave
3 to the Public Utilities Board, the fact that he cared
4 as much about someone facing a disconnection as he did
5 a critical matter of public policy.
6 So CAC (Manitoba) certainly wishes Mr.
7 Singh well, and we hope that he'll come back to visit
8 from -- from time to time. So thank you for that
9 opportunity.
10 THE CHAIRPERSON: Thank you, Mr.
11 Williams. I'm sure Mr. Singh will appreciate those
12 words.
13
14 MPI PANEL 2 CONTINUED:
15 DAN GUIMOND, Previously Sworn
16 LUKE JOHNSTON, Previously Sworn
17 HEATHER REICHERT, Previously Sworn
18
19 CONTINUED CROSS-EXAMINATION BY MR. BYRON WILLIAMS:
20 MR. BYRON WILLIAMS: Mr. Johnston, a
21 couple of actuarial short snappers. Honest. You'll
22 recall yesterday we -- I was -- I was attempting to ask
23 you a question about the data warehouse, Mr. Johnston.
24 MR. LUKE JOHNSTON: Yes.
25 MR. BYRON WILLIAMS: And I struggled to

1 find the reference, but I wonder if Diana could pull up
2 CAC 2-34. And, Mr. Johnston, you see the question
3 posed by CAC (Manitoba) is why the simple all year
4 linear trend was used to foca -- forecast claims counts
5 incurred.
6 You see that question?
7 MR. LUKE JOHNSTON: Yes, I do.
8 MR. BYRON WILLIAMS: And MPI provides a
9 response, and -- and it's -- starting at line 3 you
10 note that claims count incurred figures for years prior
11 to 2001 are difficult to compile, and this is related
12 to an internal issue with the data warehouse.
13 Is that correct, sir?
14 MR. LUKE JOHNSTON: Yes, that's the --
15 that's what it says there, yes.
16 MR. BYRON WILLIAMS: Yeah. And
17 certainly we're asking by way of undertaking if you can
18 -- or -- or maybe you've already answered the question
19 -- if you can provide an explanation of the challenges
20 with the data warehouse, in -- in terms of data prior
21 to 2001, whether they -- and -- and whether they still
22 continue, sir?
23
24 (BRIEF PAUSE)
25

1 MR. LUKE JOHNSTON: I'm going to get a
2 complete answer from -- from our business analytics
3 area. But I believe it has to do with the imple --
4 implementation of the CAR system and -- and better data
5 collection capabilities, but I'll use the words of the
6 experts on the analytic side. And I'll take that as an
7 undertaking.
8 MR. BYRON WILLIAMS: Okay.
9
10 --- UNDERTAKING NO. 48: MPI to provide an
11 explanation of the
12 challenges with the data
13 warehouse, in terms of data
14 prior to 2001, and whether
15 they still continue
16
17 CONTINUED BY MR. BYRON WILLIAMS:
18 MR. BYRON WILLIAMS: And just we'll
19 very quickly turn to PUB 1-40(d). And, Mr. Johnston,
20 you'll recall that we had some discussion in terms of
21 the -- the increases in weekly indemnity reported
22 represented in the table on page 3 of this information
23 response.
24 Do you recall that, sir?
25 MR. LUKE JOHNSTON: Yes, I do.

1 MR. BYRON WILLIAMS: And I won't turn
2 here, but, Mr. Johnston, you'll accept, subject to
3 check, that if we were to compare the tabular reserves
4 at valuation with zero percent discounting for the
5 actuarial reports of October 31st, 2013, versus October
6 31st, 2012, we'd find a difference of less than a
7 million dollars.
8 Would you accept that, subject to check?
9 MR. LUKE JOHNSTON: Subject to check,
10 that difference, I believe, occurs between the two (2)
11 October reports.
12 MR. BYRON WILLIAMS: And so what we're
13 trying to understand for our client, sir, is how one
14 gets a $11.3 million increase in reported when the case
15 reserves based on tabular reserving went down, you
16 know, between nine hundred thousand (900,000) and a
17 million dollars?
18 MR. LUKE JOHNSTON: So I will -- I am
19 going to have somebody look at the details of this in a
20 bit more detail. My comments yesterday were that
21 beyond the ten (10) year mark the actuarial department
22 essentially reserves these on a what's called tabular
23 reserving basis in our analysis. The -- per my
24 comments yesterday, the case managers still modify
25 reserves however they see fit per reserving guidelines.

1 It's just that we -- not that we ignore, but we do our
2 own kind of actuarial work on -- on those older claims.
3 But I see your point here and why would
4 that difference be so small when so much case reserves
5 are added. And we'll get you the answer on that.
6 MR. BYRON WILLIAMS: Okay, thank you.
7 And the undertaking, Mr. Johnston -- and thank you,
8 court reporter -- is to provide an explanation of -- or
9 reconciliation between an $11.3 million increase in
10 reported for the years 1994 through 2003 for weekly
11 indemnity when the year-over-year ultimates went down
12 by around nine hundred thousand dollars ($900,000).
13 Is that a satisfactory undertaking, Mr.
14 Johnston?
15 MR. LUKE JOHNSTON: It is.
16
17 --- UNDERTAKING NO. 49: MPI to provide a
18 reconciliation between an
19 $11.3 million increase in
20 reported for the years 1994
21 through 2003 for weekly
22 indemnity when the year-
23 over-year ultimates went
24 down by around nine hundred
25 thousand dollars ($900,000)

1 CONTINUED BY MR. BYRON WILLIAMS:
2 MR. BYRON WILLIAMS: And given that I
3 didn't acknowledge my client yesterday, I'll just note
4 she's here today. A couple more short snappers based
5 upon exhibits filed yesterday. And I wonder if we
6 could turn to MPI Exhibit 18.
7
8 (BRIEF PAUSE)
9
10 MR. BYRON WILLIAMS: And I'm not sure
11 if this is you, Ms. Reichert, or -- or not, but it was
12 a response of -- fro -- of the Corporation being asked
13 to provide some form of analysis with respect to the
14 calculation of the anticipated additional 30 million in
15 -- in costs.
16 Does MPI recall that -- that
17 undertaking?
18 MS. HEATHER REICHERT: Yes, we do.
19 MR. BYRON WILLIAMS: And just in terms
20 of by high-level summary, would it be accurate to say
21 that this preliminary analysis is based on a sample of
22 three (3) vehicles, being a 2014 Lexus, an 2013
23 Equinox, and a 2014 Ford Edge?
24 MS. HEATHER REICHERT: Yes, I believe
25 that's true.

1 MR. BYRON WILLIAMS: And -- and MPI has
2 been careful in pre -- presenting this analysis to say
3 that it is not a forecast, agreed?
4 MS. HEATHER REICHERT: Agreed.
5 MR. BYRON WILLIAMS: It's indicating
6 that the projections here are simply indicative of a
7 trend that should be monitored.
8 Would that be fair?
9 MS. HEATHER REICHERT: Yes, that would
10 be fair.
11 MR. BYRON WILLIAMS: And the
12 Corporation's current expectation based upon this
13 limited sample is that, in quotation marks:
14 "This new normal will be a
15 significant part of the repair mix in
16 the 2020 to 2021 time frame."
17 Would that be accurate?
18 MS. HEATHER REICHERT: I believe the --
19 the comment that Mr. Guimond has made with respect to
20 this particular information is that we expect to see
21 this increasing complexity increasing the cost of
22 repairing vehicles, and that that's going to occur over
23 the next years, really -- what's the word I'm looking
24 for -- really showing itself in and around the 2020.
25 So there may be some before that and then continuing

after that.

MR. BYRON WILLIAMS: And it would be fair to say, and accurate to say, that the cost impacts have not been incorporated into the current forecast as it's -- as this mechanism will take some time to develop.

Would that be fair?

MS. HEATHER REICHERT: Yes, that -- that would be fair.

MR. BYRON WILLIAMS: If we can turn to MPI Exhibit 31.

(BRIEF PAUSE)

MR. BYRON WILLIAMS: Okay. And, Ms. Reichert, this is some context for the RSR rebuilding fee, coincidentally my first appearance, I think, before the Public Utilities Board and an extremely unsuccessful one (1), I might add.

Ms. Reichert, just at a high level when we look at this response, MPI was successful in the 1996 year in getting rate changes of roughly 6 percent, comprised of a 4.1 percent overall rate increase and a 2 percent RSR rebuilding fee.

Would that be correct?

1 MS. HEATHER REICHERT: Yes, that would.
2 MR. BYRON WILLIAMS: And as we move to
3 the 1997 year, again, not one (1) of my more successful
4 adventures.
5 The Corporation was successful in
6 getting an additional 2 percent overall rate increase,
7 a continuation of the 2 percent RSR rebuilding fee,
8 plus an additional 2 percent RSR rebuilding fee or
9 surcharge added?
10 MS. HEATHER REICHERT: Yes, that's
11 correct.
12 MR. BYRON WILLIAMS: So, in essence, in
13 that year they got a continuation of the RSR surcharge
14 that was already in place and then an additional 4
15 percent, comprised of 2 percent of a rate increase plus
16 an additional surcharge, agreed?
17 MS. HEATHER REICHERT: Agreed.
18 MR. BYRON WILLIAMS: And finally, in
19 1998, it received an additional 1 percent increase, as
20 well as an additional 1 percent surcharge on -- on the
21 RSR -- or as -- as part of the RSR surcharge, agreed?
22 MS. HEATHER REICHERT: Yes. As I read
23 this, MPI applied for a 2 percent additional surcharge,
24 but -- but was re -- awarded or ordered only a 1
25 percent additional.

1 MR. BYRON WILLIAMS: Okay. Thank you.
2 MS. HEATHER REICHERT: You must have
3 done better that year, Mr. Williams.
4 MR. BYRON WILLIAMS: I didn't really
5 hit my stride till the next decade, Ms. Reichert. I'm
6 just amazed Ms. Desorcy kept me around. MPI-37, if we
7 could turn there. And to the second -- second -- well,
8 the first -- first page including the "Committee
9 Purpose" subheading.
10
11 (BRIEF PAUSE)
12
13 MR. BYRON WILLIAMS: Yes, to the next
14 page, please, and under the subheading "Committee
15 Purpose," the third paragraph. And keep scrolling
16 down. Perfect. And I don't know if this goes to Ms.
17 Reichert or to Mr. Johnston, but you'll see there's a
18 discussion in this paragraph -- just by -- by way of
19 context.
20 This is the terms of reference for the
21 innovation and cost containment committee, agreed?
22 MS. HEATHER REICHERT: Yes, it is.
23 MR. BYRON WILLIAMS: You can see in the
24 middle of this paragraph there's a reference to new --
25 newer vehicles being more expensive to repair.

1 Do you see that reference?
2 MS. HEATHER REICHERT: Yes, I do.
3 MR. BYRON WILLIAMS: But a couple
4 sentences farther down you'll -- you'll also see a
5 reference to as these -- suggesting that as these safer
6 vehicles make up a larger percentage of the vehicle
7 fleet, it will ultimately lead to a reduction in claims
8 and claims costs.
9 Do you see that reference?
10 MS. HEATHER REICHERT: Yes, I do. And
11 that actually is in reference to the safer vehicles
12 being autonomous cars that basically drive themselves,
13 and what the industry is showing, that the only
14 instance I guess where an autonomous car has been
15 involved in a -- in a collision was when the driver
16 actually took over and overrode the autonomy of the
17 car, if you will.
18 MR. BYRON WILLIAMS: And has the
19 Corporation -- is its assertion of the impact of the
20 safer veter -- vehicles ultimately leading to a
21 reduction in claims and claims costs, is that based
22 upon general information, or has the Corporation
23 undertaken any analysis to -- to explore its
24 implications for the longer term?
25 MS. HEATHER REICHERT: That would be

1 general observation and general -- general research, if
2 you will.
3 MR. BYRON WILLIAMS: Would it be fair
4 to say then when we look at the population of vehicles
5 that Manitoba Public Insurance anticipates insuring
6 into the future, that we on -- on the one (1) hand we
7 have the pressures on the collision side with
8 anticipated increase collision costs.
9 You'll accept that as one (1) -- one (1)
10 part of the dialogue?
11 MS. HEATHER REICHERT: Yes. Excuse me.
12 MR. BYRON WILLIAMS: And as another
13 part of the future that Manitoba Public Insurance
14 anticipates is safer vehicles ultimately leading to a
15 redic -- reduction in claims and claims costs.
16 MS. HEATHER REICHERT: That's correct.
17 I believe what we are anticipating though is that the
18 increased costs of the more complex materials that are
19 in cars is going to happen sooner than what we're going
20 to see in any great extent in Manitoba in the way of
21 autonomous vehicles.
22 So hence the -- the need for us to be
23 very conscious of everything that we can do to
24 streamline the costs of -- of repairing vehicles in the
25 near term to prepare and ensure, as Mr. Guimond has

said, ensure that we can maintain rate stability, not having to increase rates significantly because of those increasing costs. That we can offset that by becoming more efficient and -- and streamlining processes.

MR. BYRON WILLIAMS: Go ahead, Mr. Johnston. I see you're reaching for the pen -- the button.

MR. LUKE JOHNSTON: No, what you're -- yeah, what -- what you're saying is -- is true, and to an extent the forecast already incorporates some of this. You've probably seen that we've increased our collision severity assumptions this year. Some of the recent years have been very poor; 10 percent last year.

But if you look at the -- on the injury side, we actually are forecasting no growth, or something close to zero growth in injury counts. So on a per-vehicle basis we're actually forecasting declining frequency, and that is based on experience. That's not based on, you know, just a guess or some kind of insight we have. The last seven (7) or eight (8) years we've seen flat injury growth.

Also, our severity trend on the PIPP side, I think on the longer term coverages I -- I believe -- I believe they're something around inflation or less. So we actually already have fairly optimistic

1 assumptions in our forecast for -- for injury, but
2 that's -- that's tied to -- to our actual experience.
3 So we're not -- if it gets better, great. But in the
4 short term, I -- I wouldn't expect something
5 drastically different from our forecasts.
6 MR. BYRON WILLIAMS: And -- and that's
7 helpful, Mr. Johnston. I -- I just want to make sure I
8 understand the dynamics. So you've -- you've flagged
9 on the PIPP side both the relatively flat collision
10 frequency, as well as some relatively positive
11 experience with the more serious claims?
12 MR. LUKE JOHNSTON: Flat -- actually,
13 it's -- depending on how you calculate frequency, on an
14 absolute count -- injury count basis, we're assuming
15 the counts are just going to stay the same, despite
16 growing vehicle counts. On a injury per vehicle basis,
17 we're actually forecasting declines. And the severity
18 side on PIPP, I believe we're at or below inflationary
19 growth. So very optimistic assumptions, but tied to
20 the actual historical results. So we believe there's a
21 valid basis for that.
22 MR. BYRON WILLIAMS: And then the
23 additional dialogue that's been flagged in the terms of
24 reference is some future opportunities associated with
25 -- and Ms. Reichert, I can't remember the term you

1 used, whether it's Byron-less cars or driverless cars.
2 But that's -- that's something that is
3 not built into the forecast, but is an opportunity
4 farther down the line that MPI anticipates?
5 MS. HEATHER REICHERT: Yes. My
6 comments are with respect to physical damage and
7 collision. Mr. Johnston was speaking about safer cars
8 from the perspective of bodily injury. Autonomous
9 cars, actually, are preventing physical damage, because
10 they are avoiding collisions altogether. So it is with
11 respect to impact on physical damage repair costs that
12 I was referring, contrary -- not contrary, but whereas
13 Mr. Johnston was referring to bodily injury, which we
14 are already seeing.
15 MR. BYRON WILLIAMS: And -- and thank
16 you for that. That's most helpful.
17 Mr. Johnston, probably over to you. And
18 Diana, in a few moments, we'll be turning to the DCAT.
19 And we don't need to pull it up next, but I think the
20 next -- the next page coming is page 20, but we don't
21 need it right now.
22 Mr. Johnston, you probably have the
23 purpose of the RSR memorized, but would it be fair to
24 characterize it as being intended to protect motorists
25 from rate increases made necessary by unexpected events

1 and losses arising from non-recurring events or
2 factors?
3 MR. LUKE JOHNSTON: I think you might
4 have said, "rate decreases," but rate increases, yeah.
5 MR. BYRON WILLIAMS: Just -- we -- we --
6 MR. LUKE JOHNSTON: We'll -- we'll give
7 them all the decreases they -- they love -- they want,
8 yes.
9 MR. BYRON WILLIAMS: That's wishful
10 thinking, yet again.
11 MR. LUKE JOHNSTON: Yeah. That is put
12 increases in there, and yes.
13 MR. BYRON WILLIAMS: I really should
14 get some sleep. And by its very definition, Mr.
15 Johnston, you'll agree that the RSR is not there to
16 insulate ratepayers of the Corporation's executive from
17 legitimate rate pressures that reflect inflationary
18 trends?
19 MR. LUKE JOHNSTON: That's fair. I
20 don't know how long it's been, but we've been coming
21 here, always asking for break-even rates, and sometimes
22 that reflects increasing pressures on -- on our --
23 whatever collision or injury side. And we expect to
24 continue to do that, and that -- yes. That wouldn't be
25 considered, like, one of these abnormal events that

shock our financial results.

MR. BYRON WILLIAMS: And indeed, it's your view that, all other things being equal, if there is a credible, significant increase in projected claims costs, management should be prepared to increase rates as quickly as possible to respond to that?

MR. LUKE JOHNSTON: Agreed.

MR. BYRON WILLIAMS: And again, presuming all other things being equal, and assuming a significant increase in projected claims' costs, you would recommend, no doubt, that the level of rate increase be commensurate with the commensurate level of the projected significant increase in projected claims costs?

MR. LUKE JOHNSTON: We will, of course, continue to apply for break-even rates is -- is our intent. So, in general, I believe that would be true. Of course, when we're faced with seeing different cost pressures, we're going to do whatever we can to try to mitigate those. But as a general statement, I agree.

MR. BYRON WILLIAMS: Okay. And that's consistent with the general concept of principle, that today's ratepayers should pay for the -- today's costs, agreed?

MR. LUKE JOHNSTON: Agreed.

1 MR. BYRON WILLIAMS: And certainly MPI
2 would not recommend drawing down the RSR to insulate or
3 partially insulate ratepayers from a credible
4 significant increase in projected claims costs, agreed?
5 MR. LUKE JOHNSTON: I believe that
6 would imply that we would need a rate increase to break
7 even -- even and we wouldn't ask for it, and by doing
8 that essentially deflect it to future policyholders. I
9 don't believe the Corporation would propose something
10 like that.
11 MR. BYRON WILLIAMS: Would it be also
12 fair to say that if there was a credible forecast
13 decline in interest rates leading to a decline in
14 projected net income, that all other things being
15 equal, management should be prepared to seek a rate
16 increase?
17 MR. LUKE JOHNSTON: Can you just repeat
18 that for me?
19 MR. BYRON WILLIAMS: Yes. I took some
20 care with that one, Mr. Johnston. Let's... All other
21 things being equal, if there was a credible forecast
22 decline in interest rate -- rates leading to a credible
23 forecast decline in projected net income, all other
24 things being equal, management would be prepared --
25 should be prepared to increase rates?

1 MR. LUKE JOHNSTON: Similar to the
2 forecast you see today, our intent is always to put
3 forward a best estimate. If the best estimate, in our
4 opinion, is that interest rates are going to decline
5 and that's going to cause pressure to net income in the
6 rating period, I would assume that we'd apply for that
7 rate increase.
8 What we're -- on this interest rate
9 front, what we're debating here is how credible -- or
10 how much of a best estimate this interest rate forecast
11 is that we have right now, right. I don't -- I
12 personally don't have a lot of comfort with it, even
13 though it is coming from the banks. But that's
14 currently what we're using in our forecast.
15 Because of the current level of interest
16 rates, whenever you're predicting really big swings,
17 you're -- you're looking at potential risks in the
18 rates that you put forward.
19 MR. REGIS GOSSELIN: I got to follow up
20 that question because -- that answer because, you know,
21 seeking a rate change because of a drop in interest
22 rates is one (1) thing, but it's within your control to
23 address duration matching without coming to this Board.
24 It's within your control to address duration matching
25 right now without coming to this Board.

1 And, I guess, is that an option that's
2 being considered in the face of -- in the face of a --
3 of a experience -- we're already experiencing a rate
4 decline relative to your forecast?
5 MR. LUKE JOHNSTON: Absolutely. Per my
6 earlier comments, when -- when faced with situations
7 like this where we have larger risks, we're -- we're
8 always looking to mitigate in the cost-benefit of that
9 mitigation. So in this particular GRA, there are
10 significant benefits to be had if the rates do rise.
11 Another option is to attempt to immunize
12 our self as much as possible against those rate increa
13 -- or those interest rate increase or decreases. But
14 there's costs to that, as well. If -- if you look at
15 our increasing interest rate forecast, one (1) of the
16 reasons the rate increase isn't higher is because we're
17 expecting to get all these benefits.
18 If you take those expected benefits
19 away, well, the rate -- the overall rate's going to
20 have to compensate for not getting that, as well,
21 right. So we're -- it's a -- it's a difficult decision
22 point for us, right. So that's kind of that -- that
23 cost-benefit spectrum, that risk tolerance.
24 And it's really no different with
25 something like equities. If we want to be really low

1 risk in terms of net income variability, we could just
2 go completely out of equities and go into something
3 more stable. But we know there's an investment income
4 benefit to ratepayers, and I believe it's worth a
5 couple percent on rate, that we get by taking that
6 risk. So it's all -- there's always a tradeoff. And
7 what we're right now on the ALM is essentially trying
8 to assess that tradeoff and -- and proceed in the best
9 interests of ratepayers.
10 MR. REGIS GOSSELIN: Now, and I want to
11 take that duration issue a little bit -- I'm sorry, Mr.
12 Williams, but I just want to take that duration
13 matching issue a little bit... Looking at it from the
14 equity perspective. I'm talking shares now.
15 My understanding was that, for example,
16 in the case of SGI the shorter-term durations are lined
17 up with the bond liabil -- or the bond assets, fixed
18 income assets. That they're lined up together for the
19 shorter duration.
20 As far as the longer-duration
21 liabilities, they are lined up with the investments in
22 the stock market. So even though they may be faced
23 with higher volatility in the stock market, you've got
24 lots of time to recover because you're really trying to
25 cover the long-term liabilities.

1 So my question is, have you considered
2 that as a means of addressing your exposure, and at the
3 same time minimizing the short-term impacts of
4 fluctuations in the stock market?
5 MR. LUKE JOHNSTON: Yes, that's --
6 that's essentially what we're doing with the ALM study.
7 As Ms. Reichert discussed, we -- we -- as a short-term
8 measure we lowered the duration gap, but we'll wait for
9 the results from the study. And -- and if you -- as
10 you've seen in some of the undertakings, you can see
11 our -- the -- some of the issues we've faced.
12 Like, so if -- if complete cashflow
13 matching, for example, gave us a result similar to our
14 flat interest rate forecast, like that's a really
15 significant rate increase, right? Like, I'm not saying
16 it is, but if it -- something more than two point four
17 (2.4). So we're -- we're faced with that dilemma. But
18 I would totally agree with you that it's something that
19 we want to look at and -- and put something optimal.
20 Yeah.
21
22 CONTINUED BY MR. BYRON WILLIAMS:
23 MR. BYRON WILLIAMS: There, of course,
24 out of that discussion there's about three (3)
25 different questions to -- to follow up on.

1 And -- and just -- just so I understand,
2 Mr. Johnston, you're not suggesting that the
3 Corporation has to go out of equities to achieve more
4 protection, or in terms of mitigating interest rate
5 risks.
6 That's -- that wasn't any part of your
7 suggestion?
8 MR. LUKE JOHNSTON: No, the point there
9 was just that there's risk-reward to different
10 investment decisions. And similar with -- with
11 interest rates. If you take a lower risk approach, you
12 won't propose as much -- high as a DCAT target.
13 Similar would be with equities. If you got out of
14 equities, you wouldn't need as big of a risk buffer to
15 absorb shocks. So that -- that was just the general
16 risk-reward concept.
17 MR. BYRON WILLIAMS: Okay. Thank you.
18 And -- and you'd no doubt also point out that there's
19 an opportunity cost if -- if one doesn't take -- engage
20 in equities, in the sense that you would be arguably
21 foregoing, over the longer term, higher income
22 opportunities.
23 MR. LUKE JOHNSTON: Yes, we would.
24 MR. BYRON WILLIAMS: Now, Mr. Johnston,
25 when I asked my kind of question a -- a little bit ago,

1 you indicated that you didn't have a lot of confidence
2 in terms of the bank forecasts that you relied on in
3 making the original rate application.
4 Fair enough?
5 MR. LUKE JOHNSTON: Fair enough. It's
6 -- in light of the history, it's a very risky forecast
7 in -- in my opinion. But I recognize where it comes
8 from, from the banks themselves. And from that basis,
9 it's obviously considered reasonable for someone like
10 myself in a DCAT report -- or it wouldn't be seen as
11 unreasonable to rely on a -- the bank forecast. So
12 that's -- that's what we used in our proposal and
13 that's also what I believe was ordered by the PUB at
14 the last -- the last GRA.
15 MR. BYRON WILLIAMS: And just to -- in
16 terms of comfort level, would it be fair to say that
17 you are more comfortable with the -- the bank forecasts
18 as of September or October 2014 than you were with the
19 more dated April forecast?
20 MR. LUKE JOHNSTON: I don't know if
21 there's any change in comfort level for me. All that's
22 happening with those forecasts is they're just assuming
23 that interest rates are in revert historical long-term
24 averages, and that's the -- the magnitude and speed at
25 which that happens is a little difficult to digest

1 based -- especially based on recent history.
2 So what my concern is, is that we're not
3 talking so much about interest rate risk in general;
4 we're talking now about forecasting risk. We're now
5 saying, We think it's going to be 5 percent a few years
6 from now even though it's only, you know, two (2)
7 something percent or whatever now.
8 It's that bet, right. We know that
9 interest rates are going to fluctuate around their
10 current levels, but based on history the -- a massive
11 increase like this doesn't seem very probable. But
12 this is a completely unique environment, so it -- it's
13 very difficult to put a probability on that.
14 MR. BYRON WILLIAMS: Mr. Johnston, for
15 rate-setting purposes, it's fair to say that MPI would
16 prefer to rely upon the forecasts of September or
17 October as compared to the forecast from April from the
18 major banks and Global, agreed?
19
20 (BRIEF PAUSE)
21
22 MR. LUKE JOHNSTON: If you can, can you
23 repeat that just to make sure I answer your question?
24 I -- I -- or I can kind of paraphrase and see if I got
25 it right.

1 MR. BYRON WILLIAMS: Let's -- let's see
2 if -- if we're on -- on all fours.
3 MR. LUKE JOHNSTON: Do -- do I believe
4 it's more reasonable to use the more recent banks'
5 forecasts than the one (1) that was in the GRA as -- as
6 filed?
7 MR. BYRON WILLIAMS: Yes. For rate-
8 setting purposes.
9 MR. LUKE JOHNSTON: Rate-setting
10 purposes. So I -- it's hard for me to say that a more
11 recent forecast is not better information. It is,
12 right. Like we have -- we have updated information
13 providing the Board the latest information, which
14 obviously changes our -- our rate indication as shown
15 in -- I can't remember the undertaking. I bel -- or I
16 think it's Pre-Ask 5.
17 So from an interest rate perspective
18 only, I do believe that that's a more relevant forecast
19 for the Board's consideration. Of course, all
20 forecasts updated six (6), seven (7), eight (8) months
21 in the future are going to probably be a little bit
22 more reasonable than the ones we made eight (8) months
23 ago.
24 But this one in particular does have a
25 very, very big impact when it changes, so it's

1 important for the Board to understand that.
2 MR. BYRON WILLIAMS: And leaving aside
3 issues related to the, in quotation marks, "the risk-
4 adverse scenario," presented by MPI last year, would
5 MPI be in general agreement with the concept that if
6 there is a material change from a forecast that was
7 used for the rate application to a more updated
8 forecast, that that should be an important factor in
9 the Board's deliberations for the purposes of rate
10 setting?
11
12 (BRIEF PAUSE)
13
14 MR. LUKE JOHNSTON: Yeah, I agree with
15 that. And similar issues occurred last year when
16 interest rates were going in the other direction. They
17 were -- they were rising, I believe, at the time of the
18 hearings. And that was also something we presented
19 scenarios and -- and discussed at that time.
20 MR. BYRON WILLIAMS: And just for the
21 clarity of my client, leaving aside the RSR surcharge
22 proposal, is MPI still recommending a 2.4 percent rate
23 increase?
24 (BRIEF PAUSE)
25

1 MS. HEATHER REICHERT: I can respond
2 directly to that. So in week 3 of the GRA hearing, the
3 -- MPI is not, at this point, amending its rate
4 application, so I'll -- I'll leave it at that.
5 MR. REGIS GOSSELIN: That response has
6 got me a bit perplexed. I thought I heard very clearly
7 from Mr. Guimond that MPI was not changing its rate
8 application but was -- preferred to have a 3.4 rate
9 increase rather than have two point four (2.4) plus a 1
10 percent rate rider?
11 MS. HEATHER REICHERT: As I understand
12 it, yes, Mr. Guimond did make a suggestion when he was
13 doing his testimony but my understanding, technically,
14 that suggestion was not a technical or formal amendment
15 of our rate application. So I think that that was the
16 -- the gist of the question that Mr. Williams was
17 asking.
18 So the correct answer to that question
19 is we're not amending the rate application, but, yes,
20 Mr. Guimond definitely made a suggestion in his opening
21 testimony that a 3.4 percent rate increase looked to be
22 appropriate, especially when we did the Pre-Ask 5 that
23 indicated intere -- interest rates, you know, at their
24 current levels and current forecasts would indicate a
25 higher than a 2.4 percent rate increase.

1 CONTINUED BY MR. BYRON WILLIAMS:
2 MR. BYRON WILLIAMS: And recognizing
3 that your -- that MPI is not seeking to vary its
4 application, if my client were to ask MPI's advice on
5 the rate increase, am I correct in inferring that MPI
6 would advice CAC that a 3.4 percent rate increase was
7 desirable?
8 MS. HEATHER REICHERT: Yes.
9 MR. BYRON WILLIAMS: Mr. Johnston, if -
10 - if we could turn to the DCAT. And, Diana, please,
11 page 20. And if we could scroll down to the -- oh, the
12 -- thank you, Diana. Right there is perfect.
13 Mr. Johnston, this is a table setting
14 out the recent and current financial position of the
15 Corporation for the years '09/'10 through 2013/'14,
16 agreed?
17 MR. LUKE JOHNSTON: Agreed.
18 MR. BYRON WILLIAMS: And as we cast our
19 eyes down the first column to the fifth lit -- fifth
20 last entry, Mr. Johnston, you'll see a reference to the
21 IT optimization fund, and a withdrawal of $65 million
22 associated with it in the 2010/'11 year.
23 Do you see that, sir?
24 MR. LUKE JOHNSTON: I do.
25 MR. BYRON WILLIAMS: And then in the --

1 the next year we see whatever the opposite of a -- a
2 deposit of -- of 65 million?
3 MR. LUKE JOHNSTON: That's right.
4 MR. BYRON WILLIAMS: And if we -- we
5 look at the history of the 2010/'11 year, and you'll
6 correct me if my terminology is -- is wrong, Mr.
7 Johnston, but in that year, we saw a significant
8 reduction in claims costs as compared to the previous
9 year associated with a large release from the incurred
10 but not reported.
11 Is that correct, sir?
12 MR. LUKE JOHNSTON: That's correct, a
13 large release in the actu -- in the actuarial claim
14 liabilities, yes.
15 MR. BYRON WILLIAMS: And if we seek to
16 understand the history of this entry for the IT
17 optimization fund, in essence, when MPI became -- as it
18 became to understand the nature of the release that was
19 coming it made its -- a decision to segregate a certain
20 fund in retained earnings as a placemark for funds that
21 might be required over time with respect to the
22 information technology optimization.
23 Is that your recollection, sir?
24
25 (BRIEF PAUSE)

1 MR. BYRON WILLIAMS: And -- and Mr.
2 Johnston, if you need a -- oops -- a history or
3 reminder, Order 162/11, page 59 has a...
4 Do you have that here? We probably...
5
6 (BRIEF PAUSE)
7
8 MR. REGIS GOSSELIN: Mr. Williams,
9 would you mind repeating the question?
10
11 CONTINUED BY MR. BYRON WILLIAMS:
12 MR. BYRON WILLIAMS: Oh, dear. My --
13 what I was trying to -- to suggest was, as MPI became
14 aware of the magnitude of the -- the potential release,
15 it made a decision -- I'm not offering any judgment on
16 it -- to segregate a certain sum in retain earnings to
17 placemark funds that might be required over time with
18 respect to information technology.
19 MS. HEATHER REICHERT: I -- I think
20 that Mr. Williams is trying to -- and potentially infer
21 that there was some link between the release of the
22 claim liability reserve and the establishment of the IT
23 optimization fund. There was absolutely no link.
24 MR. BYRON WILLIAMS: Fair -- fair
25 enough. And then let's -- let me just scratch that

1 part of the question, and let's get to the facts. And
2 I apologize if that was -- I didn't mean to misdirect
3 your answer.
4 MS. HEATHER REICHERT: So our
5 understanding -- and this was before my time, but
6 according to the -- the Board Order, which was Order
7 Number 162/11, number 3:
8 "For rate-setting purposes, the IT
9 optimization project shall not be
10 funded from Basic retained earnings."
11 So the -- the Corporation had suggested
12 establishing a separate fund to -- to fund the IT
13 optimization project that it knew was going to, you
14 know, take considerable dollars. The PUB order, that's
15 not to fund that through the Basic program in this
16 manner, and that's why you see the following year a
17 reinstatement of those dollars into the general
18 retained earnings, if you will, of the Basic line of
19 business.
20 MR. BYRON WILLIAMS: Thank you, Ms.
21 Reichert, and thanks for assisting me in following that
22 up.
23 If we can go to -- back to the DCAT
24 report at page 66. And Mr. Johnston, we won't probably
25 -- yeah, leave it right there, Diana. Mr. Johnston,

we'll come probably to this reference in just a couple moments, but it's got nice colours. I thought I'd leave it up there.

Mr. Johnston, when we use words like 'a probability distribution', would it be fair to describe that as a table or a equation that links -- links each outcome of historical experience or a statistical experiment with its probability of occurring -- occ -- occurrence?

MR. LUKE JOHNSTON: That's fair.

MR. BYRON WILLIAMS: And probability distribution fitting is the fitting of a distribution to a series of data concerning the repeated measurement of a variable phenomena.

Is that a definition we could use?

MR. LUKE JOHNSTON: Yes. I'll accept that.

MR. BYRON WILLIAMS: And the aim of distribution fitting is to predict the probability, or forecast the frequency of occurrence of a phenomena in -- in a certain interval?

MR. LUKE JOHNSTON: Yes. This -- I don't want to get ahead of your questions, but this table that you're seeing on page 66 is essentially doing that. There's inputs, actual values, and we're

1 attempting to build a model that fits very well to that
2 historical experience.
3 And so when we're doing something like
4 simulating claims, we get something as realistic as
5 possible to -- to the history. And having that, this
6 curve that you see here, allows us to generate kind of
7 random events on that -- that spectrum. And it can
8 also be shifted forward for inflation and other things
9 like that. So it allows us the -- the flexibility to
10 do our modelling.
11 MR. BYRON WILLIAMS: Thank you. And
12 that's very helpful, the answer. And never apologize
13 for getting ahead of me on something like this.
14 It'd be fair to say that there are many
15 probability distributions, and generally you could say
16 that some, depending on the data, can be fitted more
17 closely to the observed frequency of the data than
18 others?
19 MR. LUKE JOHNSTON: Yes, that's true,
20 especially in -- there's certain ranges of data where
21 there's a lot of information, and there's other areas
22 where it's -- there's less. And that's often the --
23 the most difficult part of fitting distributions is --
24 is the so called tail of the distribution where there's
25 less credible information.

1 MR. BYRON WILLIAMS: And, Mr. Johnston,
2 will -- we're -- I -- I don't want to move too much
3 into that discussion yet, but if we look at the --
4 shall we call it a table, or shall we call it a
5 graphic? What shall we call it, Mr. Johnston? The
6 distribution in front of us.
7 MR. LUKE JOHNSTON: Graph's fine.
8 Sure.
9 MR. BYRON WILLIAMS: When we look at
10 the graph in front of us, when you use the term 'tail',
11 you're speaking about the -- as we move past 10 -- 10
12 million in claim severity to the right-hand side of
13 that distribution?
14 MR. LUKE JOHNSTON: Right. Except that
15 we're talking thousands here, ten (10) -- ten thousand
16 (10,000), but --
17 MR. BYRON WILLIAMS: Excuse me.
18 MR. LUKE JOHNSTON: -- but this is --
19 no, this is a good example because it's clear to
20 everybody that there is a fairly firm upper bound on --
21 on vehicle damage. Our maximum mature value is fifty
22 thousand (50,000), so you wouldn't expect hail damage
23 to produce a lot of thirty thousand dollar ($30,000)
24 claims.
25 If you were to look at the PIPP graph,

1 now claims can go out to be, like, 6, $7 million. So
2 it becomes very scattered and a really long tail. So
3 while this distribution kind of peaks around -- a
4 little be -- below five thousand (5,000), probably
5 around three thousand dollars ($3,000) or so, and tail
6 -- and the tail kind of ends at fifteen thousand
7 (15,000), the -- something like income replacement
8 would kind of, again, peak at a few thousand but end at
9 several million.
10 MR. BYRON WILLIAMS: Okay. Thank you.
11 And when we think of distributions, Mr. Johnston, and
12 we'll come back to this one in a moment, but we often
13 think of them as a -- in the form of a bell curve or
14 normal distribution where the data tends to fall
15 symmetrically around a central value.
16 Would that be fair?
17 MR. LUKE JOHNSTON: That's the most
18 common distribution that people would -- would know,
19 like a -- like a regular person. Not necessarily
20 what's most common in -- in insurance, but I -- I
21 understand your comment, yes.
22 MR. BYRON WILLIAMS: And what you're
23 telling us here is that this is clearly not a normal
24 distribution. We've got a -- a -- the peak or mode to
25 -- at the -- towards the left at around three thousand

1 dollars ($3,000), and with the tail trickling off to
2 the -- to the right.
3 Would that be fair, sir?
4 MR. LUKE JOHNSTON: That's fair.
5 MR. BYRON WILLIAMS: And if we look up
6 to the top of the graph, the fit that MPI -- through
7 at-risk has designated as the one (1) that -- that
8 works best here is risk W-E-I-B-U-L (sic). That's the
9 distribution that -- that it's -- feels is the best fit
10 for this analysis?
11 MR. LUKE JOHNSTON: Yes, gone are the -
12 - gone are the days where actuaries sit down and try to
13 do this stuff by hand. We -- we run it through
14 software and it tests hundreds of different
15 distributions and -- and tells us what the best fitting
16 one is. And then we can graph it like this and say,
17 Well, you know, that -- I agree, that looks pretty
18 good. Yeah.
19 MR. BYRON WILLIAMS: And it's -- it's
20 important as one moves into analysis, in particular
21 stochastic analysis, that care is taken in -- in
22 selecting the distributions because a better fit is
23 anticipated to lead to better predictions, agreed?
24 MR. LUKE JOHNSTON: Agreed.
25 MR. BYRON WILLIAMS: Now, Mr. Johnston,

you had a bit of a conversation with My Learned Friend Ms. Grammond last week on stochastic modelling, so -- but I just want to spend a couple moments on it.

A stochastic model is a model that estimates the probability distribution for a given outcome by allowing certain inputs to be random variables rather than fixed estimates, agreed?

MR. LUKE JOHNSTON: Agreed.

MR. BYRON WILLIAMS: And linking us back to distributions, a random variable is allowed to take on a range of value based on the assumed distribution of that variable, agreed?

MR. LUKE JOHNSTON: Agreed.

MR. BYRON WILLIAMS: And from that, the stochastic model creates a distra -- distribution of outcomes by running a large number of simulations using the random inputs, correct?

MR. LUKE JOHNSTON: Correct.

MR. BYRON WILLIAMS: And the simulation relies on the process of explicitly representing uncertainties by specifying inputs as probability distributions, agreed?

MR. LUKE JOHNSTON: Agreed.

MR. BYRON WILLIAMS: And ultimately the outcome that flows from that exercise is a large number

of separate and independent results, each representing a possible future for the system, agreed?

MR. LUKE JOHNSTON: Agreed.

MR. BYRON WILLIAMS: And again, as we've said previously, they are then assembled into an output in -- in the form of a probability distribution.

MR. LUKE JOHNSTON: That's right.

MR. BYRON WILLIAMS: You're a good man, Mr. Johnston. Thank you for that.

Going to interest rate risk, in preparing your DCAT analysis relating to interest rate risk, would MPI have reviewed the Bank of Canada's monetary policy report dated April 2009, and in particular the annex titled "Framework for Conducting Monetary Policy at Low Interest Rates"?

MR. LUKE JOHNSTON: I don't personally recall reading that document. I'd have to ask our -- our investment department if -- if that was reviewed by them. But it was -- I don't recall reading that.

MR. BYRON WILLIAMS: And, Mr. Johnston, you -- it's not an undertaking. If it -- if it was memorized or if it's part of the Bible for the team, you'll -- you'll let me know?

MR. LUKE JOHNSTON: I will.

MR. BYRON WILLIAMS: But that's not an

1 undertaking. And again in preparing the DCAT analysis,
2 would -- would you have reviewed -- from the Bank of
3 Canada review the summer of 2010 "Monetary Policy and a
4 Zero Bound of Nominal Interest Rates"?
5 MR. LUKE JOHNSTON: I don't recall
6 reading that. The same comment as the previous answer.
7 MR. BYRON WILLIAMS: Thank -- thank
8 you. I had noted both of those on the best sellers
9 list at Chapters, Mr. Johnston, so I was just
10 wondering.
11 MR. LUKE JOHNSTON: Or in the romance
12 section.
13
14 (BRIEF PAUSE)
15
16 MR. BYRON WILLIAMS: You've risen
17 incredibly in my estimation, sir. We can agree that
18 since 1991 the Government of Canada and the -- the Bank
19 of Canada have had an expressed policy objective of
20 keeping inflation low, stable, and predictable?
21 MR. LUKE JOHNSTON: Agreed.
22 MR. BYRON WILLIAMS: And the current
23 inflation target as measured by the total consumer
24 price index remains at the midpoint of the control
25 range of 1 to 3 percent?

1 MR. LUKE JOHNSTON: That's my
2 understanding.
3 MR. BYRON WILLIAMS: And it's also fair
4 -- it's also your understanding that the Bank of Canada
5 carries out monetary policy through changes in its
6 target overnight range of interest, agreed?
7 MR. LUKE JOHNSTON: Yes.
8 MR. BYRON WILLIAMS: And turning, if --
9 if we might, to page 57 of the D-C-A-T report, DCAT.
10 Scrolling down to the bottom, if you would, Diana. And
11 actually, is this -- just one (1) second, please.
12
13 (BRIEF PAUSE)
14
15 MR. BYRON WILLIAMS: Page 56. I
16 apologize. At the bottom of page 56, the table under,
17 "Inflation risk." Mr. Johnston, in preparing your DCAT
18 and assessing inflation risk, you reviewed the all
19 items Consumer Price Index for two (2) distinct
20 historical periods, one (1) being from 1914 to 1991 and
21 the second being from 1992 to 2013, agreed?
22 MR. LUKE JOHNSTON: Agreed.
23 MR. BYRON WILLIAMS: The significance
24 of the second period, being the 1992 to 2013 period, is
25 that coincides with the Bank of Canada inflation

1 targeting area, correct?
2 MR. LUKE JOHNSTON: Correct.
3 MR. BYRON WILLIAMS: And the purpose of
4 your analysis was to examine whether or not within the
5 data you could associate a structural break in the data
6 associated with the Bank of Canada inflation targeting
7 era, agreed?
8 MR. LUKE JOHNSTON: Agreed.
9 MR. BYRON WILLIAMS: And if we look at
10 the data, sir, for the period between 1915 and 1991, we
11 can see that the average for that time period was
12 interest rates as measured by the all Canada -- all
13 items Consumer Price Index of about 3.6 percent.
14 Is that correct?
15 MR. LUKE JOHNSTON: Correct.
16 MR. BYRON WILLIAMS: And we can also
17 see a substantial standard deviation of 5.4 percent?
18 MR. LUKE JOHNSTON: Yes.
19 MR. BYRON WILLIAMS: And by standard
20 deviation simplistically, would that suggest variance
21 around the -- around the mean or average, sir?
22 MR. LUKE JOHNSTON: Yes, going back to
23 your bell curve, as you can see here, it's probably not
24 possible that the standard deviation's going to be
25 negative 5.4 percent of that mean. But as a general

statement, it's -- it's the variability around the -- the mean. This is likely skewed to one (1) -- to one (1) end, yeah. Not likely; is.

MR. BYRON WILLIAMS: And if we look at the post -- or the current inflation targeting area, we see, as compared to the earlier area, a lower average interest rate of -- in the range of 1.8 percent.

Is that correct, sir?

MR. LUKE JOHNSTON: Correct.

MR. BYRON WILLIAMS: We also see a much more modest variation around the mean in terms of 0.7 percent or standard deviation?

MR. LUKE JOHNSTON: Yes.

MR. BYRON WILLIAMS: And based on this analysis for the purposes of the DCAT modelling of interest rate risk, you chose to base your assessment of inflation risk focussing on data from the recent period, 1992 to present.

Is that correct?

MR. LUKE JOHNSTON: Correct.

(BRIEF PAUSE)

MR. BYRON WILLIAMS: Just for purposes of definition, Mr. Johnston, assuming for a moment that

1 inflation is running at 2 percent and the interest rate
2 was 4 percent, would I be correct in saying in -- based
3 upon that example, that the nominal interest rate was 4
4 percent and the real interest rate was 2 percent, being
5 the difference between four (4) and two (2)?
6 MR. LUKE JOHNSTON: Yes.
7 MR. BYRON WILLIAMS: And I take it you
8 are familiar with the concept of zero lower bonds,
9 suggesting that nominal interest rates cannot fall
10 below zero?
11 MR. LUKE JOHNSTON: Familiar with that,
12 yes.
13 MR. BYRON WILLIAMS: And we work under
14 that presumption that nominal interest rates cannot
15 fall below zero given the understanding that rational
16 agents would not purchase an asset yielding a negative
17 return when they could hold currency at a zero rate of
18 return, agreed?
19 MR. LUKE JOHNSTON: Agreed.
20 MR. BYRON WILLIAMS: In essence, at --
21 with nominal interest rates below zero, cash would
22 become a more attractive option, agreed?
23 MR. LUKE JOHNSTON: Agreed.
24 MR. BYRON WILLIAMS: And MPI is aware,
25 or would accept, subject to check, that the Bank of

Canada has clearly stated that it considers twenty-five (25) basis points to be the effective lower bound for its overnight target rate?

You'll accept that, subject to check?

MR. LUKE JOHNSTON: I'll accept that.

(BRIEF PAUSE)

MR. LUKE JOHNSTON: Thank you.

MR. BYRON WILLIAMS: And, Mr. Johnston, I want to move from the concept of zero lower bound to the concept of negative yield.

You're familiar with that concept?

MR. LUKE JOHNSTON: Generally, yes.

MR. BYRON WILLIAMS: Let's assume for discussion purposes, a market year -- yield on a Government of Canada ten (10) year bond was 1.7 percent as of a certain date.

Are you prepared to accept that?

MR. LUKE JOHNSTON: I am.

MR. BYRON WILLIAMS: And assume as well that if inflation was expected to be 2 percent during the next ten (10) years.

You'll -- you'll take that assumption with me, Mr. Johnston?

1 MR. LUKE JOHNSTON: I will. That's not
2 a lot different than the current situation, actually.
3 We're around 2 percent, and ten (10) year bond, and the
4 inflation forecasts that we get continue to be around
5 two (2).
6 MR. BYRON WILLIAMS: Okay. Then a ten
7 (10) year bond purchased on this date and yielding 1.7
8 percent would have a negative yield of 0.3 percent on
9 an annual basis over this period, all other things
10 being equal?
11 MR. LUKE JOHNSTON: Yes.
12 MR. BYRON WILLIAMS: And you would
13 agree interest rates are this low relative to expected
14 inflation? It would be reasonable to assume the
15 probability of interest rates increasing is much higher
16 than the probability of interest rates falling?
17 MR. LUKE JOHNSTON: I don't know that.
18 I know that the probability of interest rates falling
19 by two hundred (200) basis points is zero, probably,
20 but historically, what we've shown is the probability
21 of increases or decreases in the short term has been
22 relatively equal, and this is -- yeah. This is clearly
23 an area of difficulty in a -- in the -- in modelling
24 right now.
25 And in last year's DCAT, what I -- what

1 I did was essentially assume that -- what you've just
2 stated, that I didn't think interest rates could
3 decline any further. And -- but we had difficulty
4 assessing the likelihood that they would increase or --
5 or stay the same. So we modelled our adverse scenario
6 on the flat -- flat interest rates.
7 That particular methodology was clearly
8 judgmental. Like it -- a -- I stated that in the
9 report. There is a need for -- from all parties, I
10 think, for a little bit more of a historical basis to
11 that, and that was the -- that was a rationale in --
12 for this year's modelling, to look at the actual
13 changes in the current rate that historically have
14 occurred, so you could tie it to some kind of real data
15 for today and for some future period when we actually
16 have 5 percent interest rates again. So the modelling
17 stays consistent.
18 MR. BYRON WILLIAMS: Thank you, Mr.
19 Johnston. And I appreciate that answer.
20 I jus -- I just want to be clear for the
21 record, in circumstances of negative yield, would you
22 agree with the proposition that it would be reasonable
23 to assume the probability of interest rates increasing,
24 is much higher than the probability of interest rates
25 falling?

1 MR. LUKE JOHNSTON: I don't know that.
2 And the last five (5), six (6) years has shown that
3 maybe that's not a good assumption. But, like I said,
4 I -- I know it can't fall forever and it can't fall
5 below zero. Like, there's lower bounds to that. But
6 I'm not in a position to confidently state that I think
7 the probability that it's going to go up tomorrow is
8 higher than the probability it's going to stay the same
9 or -- or go down tomorrow.
10 MR. BYRON WILLIAMS: Mr. Johnston, who
11 wrote the duration matching discussion paper for the
12 Corporation?
13
14 (BRIEF PAUSE)
15
16 MR. BYRON WILLIAMS: And -- and, Mr.
17 Johnston, I don't need to know the name. I just --
18 were -- were you involved in that document?
19 MR. LUKE JOHNSTON: I was. I -- I --
20 did you have a reference?
21 MR. BYRON WILLIAMS: Yes. I'm -- I'm
22 going to suggest to you, in Section 3.2 of the duration
23 discussion paper, that Manitoba Public Insurance
24 suggested that when interest rates are this low
25 relative to expected inflation it is reasonable to

1 assume the probability of interest rates increasing is
2 much higher than the probability of interest rates
3 falling.
4
5 (BRIEF PAUSE)
6
7 MR. LUKE JOHNSTON: I don't have
8 trouble with that statement. My comments are that they
9 can't -- they can't fall much -- much farther. So I --
10 there's no probability that they're going to fall
11 seventy (70) basis points, like -- or whatever the
12 case, in my opinion. I don't -- the lowest of all
13 time, I believe, is one-point-six-eight (1.68). I
14 don't see it being one (1). So from that perspective,
15 there -- of course there's higher probability of a
16 seventy (70) basis point increase than there is of a
17 decrease.
18 But in terms of just changing from the
19 current level, I -- I see your point that there's a lot
20 -- a lot of territory that interest rates could go on
21 the upside and not so much on the downside. I get
22 that. What I'm saying is in the short-term, and in the
23 last five (5) years, I don't have a confident position
24 that I know that as a factual statement that they're
25 guaranteed to go up with much higher probability.

1 MR. BYRON WILLIAMS: Let's just go back
2 to -- to my premise though, Mr. Johnston. You don't
3 have a problem with the premise that in a negative
4 yield environment it would be reasonable to assume the
5 probability of interest rates increasing is much higher
6 than a probability of them falling, agreed?
7
8 (BRIEF PAUSE)
9
10 MR. LUKE JOHNSTON: Sorry. I feel like
11 I already answered that question several times.
12 MR. BYRON WILLIAMS: Okay. So that's
13 your answer. That's fine.
14 I'm moving to a new topic, Madam Chair.
15 I can indicate for the panel, I still have some work to
16 do but it's not an overwhelming amount. So if I'm not
17 done this morning, which is some -- a -- a modest
18 possibility, it will be early in the afternoon, just
19 for others in the room.
20 I'm sorry. I'm moving to a new and -- a
21 topic area that would probably take half an hour. So
22 I'd suggest a break, subject to the Board's guidance.
23 THE CHAIRPERSON: Yeah, I -- we will
24 take a break now and we'll come back a little after
25 10:30. Thank you.

1 --- Upon recessing at 10:18 a.m.
2 --- Upon resuming at 10:36 a.m.
3
4 THE CHAIRPERSON: Welcome back from
5 your break, and we're ready to begin again with Mr.
6 Williams and his cross-examination.
7
8 CONTINUED BY MR. BYRON WILLIAMS:
9 MR. BYRON WILLIAMS: Thank you, Madam
10 Chair. If -- if we can open up Information Response
11 PUB Manitoba Public Insurance 1-74(c), the attachment,
12 that would be great. Thank you.
13
14 (BRIEF PAUSE)
15
16 MR. BYRON WILLIAMS: Ms. Reichert,
17 you'll agree that this table presents information
18 technology costs on a corporate basis, the actuals for
19 the years 2009/'10 through '13/'14, as well as the
20 forecast and projections from '14/'15 onto '18/'19,
21 agreed?
22 MS. HEATHER REICHERT: Yes, agreed. I
23 do want to point out though that this is a table that
24 has both expenditures -- operating expenses, if you
25 will, as well as capital expenditures that would be

1 actually reflected on the balance sheet in the year
2 that they're incurred.
3 MR. BYRON WILLIAMS: And -- and that's
4 fair enough. And I really, Ms. Reichert, want to focus
5 on operating expenses.
6 And you'll agree with me that that is
7 segregated on this table being the first -- the first
8 line, correct?
9 MS. HEATHER REICHERT: Yes.
10 MR. BYRON WILLIAMS: And just before we
11 walk through this, Ms. Reichert, you'll recall that --
12 and we do not need to go here, Diana -- but in MPI
13 Exhibit 38, Manitoba Public Insurance itemized an
14 additional 5.3 million in -- in costs related to the
15 PDR?
16 MS. HEATHER REICHERT: That sounds
17 right. I'm just going to get that reference.
18 MR. BYRON WILLIAMS: Exhibit 38.
19
20 (BRIEF PAUSE)
21
22 MS. HEATHER REICHERT: Sorry, I'm --
23 I'm not sure how you referred to this but, yes, on --
24 on Exhibit 38, this 5.3 million was what Mr. Guimond
25 had referenced that would be eventually additional

1 operating costs relative to the PDR project. So
2 currently and once absolutely completely implemented,
3 it's anticipated that ongoing operating costs of about
4 5.3 million will offset the 13.3 million in savings.
5 MR. BYRON WILLIAMS: And, Ms. Reichert,
6 just for my information, would that additional 5.3
7 million be recognized in -- in the Corporation's
8 estimation of operating expenses in -- in its response
9 to PUB 1-74(c), or -- or would that be new to this --
10 to this analysis?
11 MS. HEATHER REICHERT: Two point six
12 million of this five point three (5.3) is with respect
13 to the software licensing costs, the Mitchell software
14 licensing costs, that we are contributing on behalf of
15 the -- the body shops. So that's starting to be
16 incurred.
17 Where that gets reflected in our
18 forecast is within the claims' forecasting section.
19 I'll ask Mr. Johnston to -- to clarify what -- what Z-
20 files are, but it's an offsetting -- not offsetting --
21 it's an expense that is part of claims -- overall
22 claims liabilities and claims' expenses.
23 So you won't see it on the line that
24 we're referring to right here. It is in another part
25 of our forecast. But 2.6 million of the five point

1 three (5.3) is currently included in -- in our
2 forecast.
3
4 (BRIEF PAUSE)
5
6 MR. BYRON WILLIAMS: So just so I
7 understand, Mr. Reichert, in the Corporation's
8 forecast, the expenditures associated with the Mitchell
9 software -- ware licensing would not appear in the
10 information response addressing information technology
11 costs on a corporate basis, but your evidence is that
12 it appears in the -- the Cor -- Corporation's
13 application under Z-files?
14 MS. HEATHER REICHERT: Yes. And Mr.
15 Johnston just corrected me that Z-files is an internal
16 terminology. So Z-files, for the panel, refers to
17 unallocated loss adjustment expenses. And I can give
18 you the reference of where we specifically refer to the
19 2.6 million if that would be helpful. It is in Claims
20 Incurred section, which is in Volume II; 8.2 is the
21 specific section. And it's on the -- the bottom of
22 that page. I -- I think we referred to this last week
23 when we were talking about the software.
24 I think, Diana, if you can, pull it up.
25 It might just be helpful for the panel to see what I'm

1 referring to. Awesome.
2 So just -- so again, at the top of this
3 it said, "Unallocated Loss Adjustment Expenses," is the
4 category. And if you scroll right down to this last
5 paragraph, the '15/'16 forecast increased by 2.6
6 million over last year's forecast, and that was the
7 collaborative estimating. That's the software licences
8 with respect to the body shops.
9 So why it's included in here is it --
10 it's a cost of handling processing physical damage
11 claims with the repair industry. So it's not an
12 internal, if you will, IT operating expense for
13 maintaining our in-house systems. That's why the
14 differentiation.
15 MR. BYRON WILLIAMS: And thank you for
16 that. And just so I understand, apart from the
17 software -- the operating costs associated with
18 software, such as Mitchell, are there other corporate
19 IT costs that I wouldn't find in the response to PUB 1-
20 74(c)?
21 MS. HEATHER REICHERT: There's nothing
22 that immediately comes to mind, that -- that, as it
23 relates, because it's an IT cost specifically related
24 to the repairing of vehicles with our partners in the
25 body shops. That's why it is where it is. I'm not

1 aware of any other significant IT cost that -- that are
2 of that same nature.
3 MR. BYRON WILLIAMS: And just going
4 completely off script, no doubt, for example, the
5 technology in the brokers' offices wouldn't be
6 captured.
7 Where would it be captured?
8 MS. HEATHER REICHERT: The -- the
9 technology in the brokers' offices, which is computers,
10 would be data processing equipment. And so that would
11 -- that would be reflected through that line
12 expenditure.
13 MR. BYRON WILLIAMS: And by 'line
14 expenditure', you're referring to PUB 1-74(c)?
15 MS. HEATHER REICHERT: Yes, I believe
16 that's where it should be, is in the data processing
17 expenses.
18 MR. BYRON WILLIAMS: Okay. And I'm not
19 asking for an undertaking. But, Ms. Reichert, if your
20 memory's refreshed and there's other items that -- that
21 aren't in corporate IT as presented in PUB 1-74(c)
22 analogous to the Mitchell, you'll -- you'll advise us
23 of that?
24 MS. HEATHER REICHERT: Yes, I will.
25 MR. BYRON WILLIAMS: And we'll pull up

1 -- Ms. Reichert, you -- you use the figure for Mitchell
2 of 2.65 million.
3 Is -- is that correct?
4 MS. HEATHER REICHERT: As it related to
5 the software licences? Yes, I did.
6 MR. BYRON WILLIAMS: And when we look
7 at MPI Exhibit 38, being Undertaking 25, we see a
8 figure of 3.5 million for -- for Mitchell licensing, so
9 a difference -- I'm too tired to do the -- the math.
10 But there's a difference between the two
11 (2) figures you gave, Ms. Reichert?
12 MS. HEATHER REICHERT: So the 2.65 is
13 embodied within the 3.5. Not all of the increased
14 software expenditures have yet been incurred. So -- so
15 the -- the difference will be future -- future
16 expenditures of that same -- same nature.
17 MR. BYRON WILLIAMS: So the difference
18 being roughly eight hundred and fifty thousand
19 (850,000) in operating expenses annually?
20 MS. HEATHER REICHERT: I'm sorry. I
21 was distracted there. Can you repeat your question,
22 please?
23 MR. BYRON WILLIAMS: I hope it wasn't
24 like Mr. Johnston looking at my face yesterday. When
25 you spoke of the difference, presumably, you meant the

1 difference between the two point six (2.6) -- two
2 million, six hundred and fifty thousand (2,650,000)
3 that you referenced, which is previously, and the 3.5
4 million that is set out in the Corporation's response
5 to -- or Exhibit 38, agreed?
6 MS. HEATHER REICHERT: Yes.
7 MR. BYRON WILLIAMS: And my
8 understanding is that that difference is roughly eight
9 hundred and fifty thousand (850,000) in annual
10 operating expenses?
11 MS. HEATHER REICHERT: That would be
12 the math, yes.
13 MR. BYRON WILLIAMS: And your evidence
14 is that that eight hundred and fifty thousand (850,000)
15 is for future expenditures that are -- have not -- that
16 -- expenditures that are yet to come?
17 MS. HEATHER REICHERT: Yes. That is my
18 understanding.
19 MR. BYRON WILLIAMS: And, Ms. Reichert,
20 just so I understand, is that eight hundred and fifty
21 thousand (850,000) for -- related to Mitchell for
22 expenditures yet to come, is that currently in the
23 Corporation's IT cost projections?
24 MS. HEATHER REICHERT: Not in the
25 schedule that you referenced, which was whatever...

MR. BYRON WILLIAMS: PUB 1-74(c).

MS. HEATHER REICHERT: Thank you very much. To my knowledge, no, that is not included in those lines.

MR. BYRON WILLIAMS: And in terms of where the 2.65 million is referenced, my question is: Is that eight hundred and fifty thousand (850,000) referenced there?

(BRIEF PAUSE)

MR. BYRON WILLIAMS: And, Ms. Reichert, if it's -- I don't mean to unduly delay matters, so if you want to take that as an undertaking, being an undertaking to indicate whether the -- that eight hundred and fifty thousand (850,000) in annual operating expenses related to Mitchell software is -- is currently represented in the Corporation's costs or not, I would accept that as an undertaking if you're prepared to.

MS. HEATHER REICHERT: Sure. I will take that as an undertaking, just to confirm.

MR. BYRON WILLIAMS: Thank you for that.

--- UNDERTAKING NO. 50: MPI to indicate whether the eight hundred and fifty thousand (850,000) in annual operating expenses related to Mitchell software is currently represented in the Corporation's costs or not

CONTINUED BY MR. BYRON WILLIAMS:

MR. BYRON WILLIAMS: And, Ms. Reichert, leaving aside the Mitchell software licensing, there's -- but still focussing on Exhibit 38 of Manitoba Public Insurance, there is an additional one million, eight hundred thousand (1,800,000) in expense categories either to be determined, or in incremental technical support staffing, agreed?

MS. HEATHER REICHERT: Correct.

MR. BYRON WILLIAMS: And going back to PUB 1-74(c), the attachment thereto, Ms. Reichert, my -- my question to you is would -- is that 1.8 million currently represented in the total IT operating expenses along the top line?

MS. HEATHER REICHERT: If my recollection serves me well, we are projecting to be

1 completed -- the PDR project, to be completed in the
2 fiscal year '17/'18. So the ongoing operating expenses
3 that you're referring to, i.e. the one point 3 (1.3) to
4 be classified, and the five hundred thousand (500,000)
5 of technical support would start to be reflected in the
6 2018/'19 projected number there.
7 I know we had talked previously about
8 the -- the jump in 2018/'19 projected ongoing operating
9 expenses being a large part to do with the amortization
10 of or the starting of the amortization of the physical
11 damage project. And so additional operating costs of
12 this nature would also start to be reflected in
13 '18/'19.
14 MR. BYRON WILLIAMS: Ms. Reichert, just
15 looking at this -- this table, it would be accurate to
16 say that if we compare total IT operating expenses in
17 2009/'10, the actuals versus the actuals in 2013/'14,
18 we see roughly a $27 million difference, rising from
19 29.16 million in '09/'10 to 56.27 million in '13/'14.
20 Fair enough?
21 MS. HEATHER REICHERT: Yes, that --
22 that is fair enough. And a large part of that, again,
23 you need to recall that MPI was undertaking very
24 significant IT projects in that time frame, some of
25 which would start to be amortized during that time

1 frame. So those increases are -- are the result of
2 both implementation expenses, things that we don't
3 capitalize when projects are going on, and then the
4 starting to capitalize very significant deferred --
5 deferred expenditures during that time period. So that
6 -- that is why a great deal of that expense is
7 increasing during that time period.
8 MR. BYRON WILLIAMS: Thank you for
9 that. And -- and the Corporation has calculated that
10 the compound annual growth for that period was 17.9
11 percent?
12 MS. HEATHER REICHERT: Yes. And,
13 again, to note '13/'14 to '18/'19 compound annual
14 growth is considerably less, as I've commented
15 previously, because our view is other than the physical
16 damage re-engineering project, which is very
17 significant and it is a -- a large expenditure, we feel
18 that we have come to that point where all of the
19 significant systems are now -- have been refreshed or
20 upgraded. And so that we should be able to now move
21 into a more stable IT span going forward. Hence, the -
22 - the significant reduction in the compound annual
23 growth rate.
24 MR. BYRON WILLIAMS: You're talking a -
25 - a growth in -- in anticipated annual operating

1 expenses for the Corporation of -- in excess of $23
2 million annually between 2014/'15 and projected
3 '18/'19, agreed?
4 MS. HEATHER REICHERT: Again, yes.
5 Again, mostly contributed to by the amortization of
6 significant capital expenditures that have occurred.
7 MR. BYRON WILLIAMS: And a 7 percent
8 compound annual growth rate increase?
9 MS. HEATHER REICHERT: Yes.
10 MR. BYRON WILLIAMS: Agreed?
11 MS. HEATHER REICHERT: As -- as I --
12 yes. I agree, and as I -- as I've mentioned,
13 significantly less because our -- our annual capital
14 expenditures in IT are starting to stabilize. Hence,
15 the -- the reduction. But you are still going to see,
16 during that time frame, increases in the IT
17 expenditures because of the amortizations of things
18 that have occurred in -- in -- and have occurred and
19 are being completed within the last five (5) to ten
20 (10) years.
21 MR. BYRON WILLIAMS: And as we've
22 agreed, growth of some $23 million over that four (4)
23 year period, in annual IT operating expenses for the
24 Corporation, correct?
25 MS. HEATHER REICHERT: As a result of

1 significant capital expenditures that have occurred in
2 the previous years --
3 MR. BYRON WILLIAMS: Okay.
4 MS. HEATHER REICHERT: -- that have
5 been brought forward to this -- to this hearing and --
6 and in those years.
7 MR. BYRON WILLIAMS: Now, Ms. Reichert
8 -- and, Diana, if we could please turn to CAC
9 Information Request 3-11(b). And Table 4 on that
10 attachment, please.
11 Ms. Reichert, you see here on Table 4 a
12 look at MPI Basic operating expenses, actual and
13 projected, from 2009/'10 through 2018/'19, as compared
14 to operating expense growing -- if it was growing at
15 the pace of the change in the consumer price index.
16 That's what this table attempts to -- to
17 calculate, agreed?
18 MS. HEATHER REICHERT: Yes. And do you
19 mind just giving me the reference for this again,
20 please?
21 MR. BYRON WILLIAMS: Absolutely. And
22 CAC 3-11, Ms. Reichert. And if you're looking -- we'll
23 just -- Ms. Kalinowsky, we can just hand the...
24 And, Ms. Reichert, we'll just give you -
25 - as you orientate yourself to this table, you'll see

1 that the -- the fifth column is calculating by MPI --
2 calculating by MPI the -- what the growth and operating
3 expense would look like if it tracked the Consumer
4 Price Index, agreed?
5 MS. HEATHER REICHERT: Yes. And I'm
6 recall --
7 MR. BYRON WILLIAMS: Do you need a
8 moment?
9 MS. HEATHER REICHERT: Yes, I -- I will
10 in a moment, but I just -- I am now recalling that this
11 three dash eleven (3-11) was an update, I think, of the
12 CAC 1-62 --
13 MR. BYRON WILLIAMS: CAC 1-62.
14 MS. HEATHER REICHERT: -- which is one
15 of your favourite all-time schedules in the Hearing, as
16 I recall you commenting.
17 MR. BYRON WILLIAMS: It -- it is. And
18 I believe this one is -- is slightly -- I'll happily
19 share both with you, but I -- I believe that this is a
20 little more modest compared to one dash sixty-two (1-
21 62), Ms. Reichert.
22 MS. HEATHER REICHERT: Yeah, if I may.
23 I just need to consult with counsel.
24 MR. BYRON WILLIAMS: Okay.
25

(BRIEF PAUSE)

MS. HEATHER REICHERT: Okay. So I -- I was anticipating that this particular schedule was going to become the topic of -- of some questions, and I -- in anticipation of that I actually have an exhibit. If I can enter that, and we could get that up on the screen and look at that, and I can speak to that, and -- and probably in the process answer the questions that Mr. Williams has on the -- the impact of CPI versus our actual cost.

MR. BYRON WILLIAMS: As long as I'm provided a paper copy, I don't mind.

(BRIEF PAUSE)

MR. BYRON WILLIAMS: Presumably MPI-46.

(BRIEF PAUSE)

MS. HEATHER REICHERT: So if it's -- if it's okay with Mr. Williams, if I can maybe just explain what is in front of us relative to the -- the IR that you were referring to?

MR. BYRON WILLIAMS: Ms. -- Ms.

1 Reichert, I'm -- I'm happy to get any information on
2 the record. We'll come back to the IR in a couple
3 moments.
4 MS. HEATHER REICHERT: Okay. So
5 knowing that this was Mr. -- one of Mr. Williams's
6 favourite schedules, and I have been asked questions on
7 it in prior hearing -- in prior hearings, I've often
8 responded that my concern with trying to answer
9 questions about a CPI increasing expenditure within
10 MPI, when the base number that we're looking at
11 includes significant one (1) time implementation
12 expenses and applying CPI to those one (1) time
13 expenditures isn't, from my perspective, a good
14 analysis or -- or it doesn't paint the right picture to
15 help the Board understand what's happening with our
16 normal operating expenses.
17 So what this schedule this year is
18 doing, and I've submitted as this exhibit, is focussing
19 on the normal operating expenses of the Basic program.
20 Now, unfortunately, the Corporation was not
21 segregating, as we are today, normal operating expenses
22 from implementation expenses prior to 2010/'11. So
23 that's why this schedule starts at 2010/'11 whereas the
24 IR which was focussing on total costs started at
25 2009/'10. So that's just one (1) thing I wanted to

1 draw to the -- to the panel's attention.
2 So if we -- if we can, this -- this
3 first -- the first page takes the Basic claims expenses
4 for -- the Basic claims expenses, and does calculate an
5 average expense per unit based on what our current
6 expenditures are. And then the second table takes
7 Basic operating expenses. So you've got claims
8 expenses on the top and operating expenses in the
9 second table.
10 And just to remind the panel, when we
11 were talking earlier, last week or the week before,
12 these are the categories that are shown on our pro
13 forma statements that I believe Ms. Grammond was asking
14 me questions about a couple weeks ago. So they are an
15 allocation of an allocation within Basic.
16 So we allocate all of our expenses
17 between our lines of business. And then within Basic
18 we do a further allocation to categorize them between
19 claims expenses and operating expenses, but they're all
20 normal, from what I under -- you know, from my
21 categorization, they're normal operating expenses.
22 It's just that for purposes of the pro forma we do need
23 to further allocate them on the basis of claims
24 incurred and other allocators between what shows as
25 claims expense on our pro forma and shows as operating

1 expense.

2 So that's the -- these two (2) tables,

3 and it calculates an average expense per unit.

4 And if we can scroll down to the next

5 page. Just down a little bit. Or sorry -- I'm sorry,

6 up a little bit, sorry. So what table...

7

8 (BRIEF PAUSE)

9

10 MS. HEATHER REICHERT: Okay. So Table

11 3 and Table 4, again, with the proviso that these are

12 normal operations only, does not include implementation

13 expenses in the -- in the years noted. And still,

14 Table 3 is claims expenses, Table 4 is operating

15 expenses. What this table is doing is saying, if MPI's

16 expenditures increase at the rate of inflation what

17 would that expense be? And that's shown in column 5.

18 It say -- column 5, "CPI Claims

19 Expense." You'll see it starts at ninety-four thousand

20 (94,000). It goes to one thirty-eight (138). And then

21 it compares it to what MPI claims expense was shown on

22 -- on our pro formas, either actual or forecasted, and

23 then shows an increase or decrease.

24 Similarly, the next table does that for

25 Basic operating expenses and shows what would it be if

1 -- if at that base year it -- it just increased each
2 year by inflation and how does that compare to what
3 we're actually reflecting.
4 If you can please scroll down to the
5 last table. This table takes the two (2) previous
6 tables and adds them together. As I just mentioned,
7 these are total Basic operating expenses that are then
8 allocated to claims expense or the subcategory of
9 operating expense.
10 So this totals the two (2) previous
11 tables, Table 3 and Table 4. So you can see that on
12 the -- the CPI increasing basis total operating
13 expense, claims and operating expense, went from a
14 hundred and forty-five (145) in '10/'11 up to two
15 hundred and thirteen (213) and change in '18/'19.
16 Comparing that to what MPI actually incurred in those
17 years and is forecasting to have occur in '15/'16 and
18 on, you see the increase/decrease columns to the -- to
19 -- column, pardon me, to the far right.
20 So while, yes, in the early years there
21 were increases in -- there were increases in MPI
22 operating expenses in total relative to had they only
23 grow by CPI. So you can see 7 million in '11/'12, five
24 million six (5,600,000) in '14 -- well, that's
25 forecasted for '14/'15. The important thing to -- to

1 appreciate is that when you get into what we are
2 currently forecasting for '15/'16, '16/'17, which is
3 what is impacting on our rate requests, our rate
4 indication, we are actually forecasting to be less than
5 what the costs would have been, had we just increased
6 by inflation.
7 So we are more than -- more than beating
8 inflation, if you will. And if you look further to the
9 -- to the additional forecasted years, you can see that
10 -- that we're 11 million under what it would be if we
11 increased by inflation, and 15 million under what it
12 would be if we had increased by inflation.
13 There are legitimate reasons why, in
14 '11/'12, we were higher than inflation. That happened
15 to be a year of the -- of the salary negotiated
16 contract, where -- negotiated, as per the mandate by
17 the -- the Province of Manitoba's Compensation
18 Committee. There were four (4) years of two point nine
19 (2.9), which, as you can see, if you look back to
20 '11/'12, '12/'13, and '10/'11 in particular, that was
21 at -- at a rate that was higher than inflation in -- in
22 most of those years. Three (3) percent in '11/'12 was
23 very close to the two point nine (2.9), but
24 nonetheless, the other years were significantly less
25 than two point nine (2.9). However, that was the

1 negotiated contract done within the mandate and
2 obviously contributes to -- to us being different than
3 inflation in those years.
4 Similarly, there were higher than
5 inflationary increases in benefit-costs, such as the
6 pension. Pension plan increases were more significant
7 in those years than inflation. So legitimate reasons
8 why we would be higher than an inflationary increase in
9 those years.
10 So thank you for -- for letting me just
11 put this information in front of you. I think it --
12 it, from my perspective, puts forward the -- the
13 picture that we are doing what we can to contain costs
14 that we're forecasting in the future, to beat the
15 inflationary increases, and we're -- we're -- we're
16 getting past that -- that period when operating
17 expenses were going up because of all of the activity
18 that was happening. Not the -- these do not include
19 implementation expenses, but there are offshoots of
20 normal operating expenses when you do increase your IT
21 footprint, as we were increasing it during those times.
22 So it's now -- we're past that hump, and
23 we are forecasting to very much control and work within
24 inflationary -- or less than inflationary increases.
25 MR. BYRON WILLIAMS: Thank you. Just -

1 - let's stay on this page for a moment. If we look at
2 the 2018/'19 year, MPI, of course, is not projecting
3 that consumers will pay 77.8 million in Basic operating
4 expenses, agreed?
5 Ms. Reichert, your -- your best estimate
6 would be that consumers will be paying roughly 87.3
7 million in operating expenses for Basic in that
8 particular year?
9 MS. HEATHER REICHERT: Can you give me
10 the reference? I'm sorry.
11 MR. BYRON WILLIAMS: You've essentially
12 taken out $9.5 million, agreed?
13 MS. HEATHER REICHERT: Correct. The
14 nine point five dollars ($9.5) (sic), representing what
15 would have been implementation expense is forecasted
16 for '18/'19.
17 MR. BYRON WILLIAMS: Yes, but Ms.
18 Reichert, you're not telling my client that they'll
19 only be paying 77.8 million in Basic operating expenses
20 in that year, agreed?
21 MS. HEATHER REICHERT: I am saying that
22 they'll be paying Basic operating expenses, estimated
23 forecasted at this time, of seventy-seven point eight
24 (77.8) as it relates to normal operations of MPI as
25 currently forecasted.

1 MR. BYRON WILLIAMS: So just focussing
2 on that number, coming out of consumers' pockets, all
3 other things being equal in operating expenses, in that
4 particular year for Basic will be about 87.3 million,
5 agreed?
6
7 (BRIEF PAUSE)
8
9 MS. HEATHER REICHERT: Correct.
10 Eighty-seven million, two hundred and ninety-eight
11 (87,298,000) forecasted as operating expenses including
12 implementation in 2018/'19. And in addition, one
13 hundred and thirty-eight, three hundred and nineteen
14 (138,319) for claims expenses forecasted in '18/'19.
15 MR. BYRON WILLIAMS: Okay. Now, if we
16 can go back to CAC 3-11 for a moment please. I think
17 it's being proposed as MPI-46.
18 MS. HEATHER REICHERT: Yes.
19 THE COURT REPORTER: Are we going to be
20 marking this as an exhibit?
21 MS. HEATHER REICHERT: Yes.
22 THE COURT REPORTER: Thank you.
23
24 --- EXHIBIT NO. MPI-46: Tables of Basic claims
25 expenses and operating

1 expenses

2

3 CONTINUED BY MR. BYRON WILLIAMS:

4 MR. BYRON WILLIAMS: So when we look at

5 this table, Ms. Reichert, this is what Manitoba

6 consumers will be asked to pay in terms of MPI Basic

7 operating expenses based upon the Corporation's current

8 best forecast?

9 MS. HEATHER REICHERT: Column 6, yes.

10 That -- that represents what's actually been incurred

11 and what is currently in our forecast for Basic

12 operating expenses, including implementation and normal

13 operations. Yes.

14 MR. BYRON WILLIAMS: And if we look,

15 just for example, at the '18/'19 year, what that's

16 telling us is that there's a -- if -- if what consumers

17 are paying was tracking at the rate of inflation from

18 the '09/'10 base, they'd be paying about $18 million

19 annually, in that particular year, less, agreed?

20 MS. HEATHER REICHERT: On the

21 assumption everything within the very first base year

22 that inflation -- or, pardon me, that CPI is then added

23 to. So from 2009/'10, on the assumption that all of

24 the costs, the -- in that base year of '09/'10, are

25 legitimately subject to inflationary increases, then

1 that would say that our operating expense would be
2 being projected to be the sixty-nine, three fifty-seven
3 (69,357).
4 My point is that there are many costs
5 within our overall operating expenses for MPI that we
6 know were one (1) time in nature, because they relate
7 to implementation of significant IT projects,
8 especially in those early years. So to assume that
9 those will increase, subject to this inflation, the CPI
10 is not an -- is not a -- a reasonable assumption to
11 make in trying to do this kind of a comparison which is
12 why I removed those from the -- the exhibit that I've
13 prepared.
14 MR. BYRON WILLIAMS: And -- and I've
15 certainly let you have your conversation on that.
16 If we look at the -- the year that we're
17 currently in, Manitoba consumers will be expected to
18 pay about 73.6 million in operating expenses relate to
19 Basic, agreed?
20 MS. HEATHER REICHERT: Relating to
21 Basic normal operating and implementation expenses,
22 that is the amount that's currently being forecast in
23 our pro forma.
24 MR. BYRON WILLIAMS: Okay. And, Ms.
25 Reichert, let's -- let's -- even if we were to look

simply at the increase in normal operations for the '14/'15 year that would be about five (5) point -- 5.3 percent, agreed? Leaving aside the money that consumers have to pay, if we're just looking at the increase in normal, that's about a -- in 2014/'15, that was about a 5.3 percent increase, agreed?

(BRIEF PAUSE)

MS. HEATHER REICHERT: Sorry, I'm not sure where the reference is. So subject to check, I'll -- I'll take your -- your math of the 5.3 percent increase. Again, I need to remind the panel that when you just look at Basic operating expenses as -- exclusive of the claims expense, then what you have happening is allocation changes that can change the amount that's allocated to operating versus to claims on the basis of the allocator, such as the amount of claims incurred or the -- the staff complement, or the weighted average call centre contact ratio. There's different allocators.

So in order to avoid having a comparison done that -- that just compares 2013/'14 operating expenses -- normal operating expenses to 2014/'15 normal operating expenses, you can get noise in there

1 from changes in allocators. And I think I had spoken
2 to that a couple of weeks ago, that there was about a
3 $4 million increase in what was being allocated to
4 Basic because of the increasing claims experience, or
5 claims counts numbers, that we've been -- we've been
6 seeing.
7 So based on our allocation methodology
8 approved by the -- the PUB, there were some increases
9 that were occurring in the forecast because of that.
10 So when you've got an overall $4 million increase as a
11 result of allocation -- allocation -- allocators,
12 sorry, allocators, then on top of that you've got
13 allocations between claims and operating.
14 So the schedule that's up here on Table
15 4 is showing, yes, operating expenses are looking to be
16 higher than inflationary increases in those years. If
17 you roll up to Table 4 -- or 3, pardon me, of the same
18 schedule, and again if you look at this from the
19 perspective of just normal -- so I guess I should be
20 saying Exhibit -- the 46 that was up there. You'll
21 actually see that -- that on my Exhibit 46 the
22 difference in the claims section were less than the
23 inflationary increases, which is why I -- I said it's
24 important to look at the two (2) in total to get a real
25 picture of what was happening in those respective

1 years.

2 MR. BYRON WILLIAMS: And just before we

3 finish here, Ms. Reichert, when you talk about noise,

4 that would be $4 million of noise, but that comes out

5 of ratepayers' pockets, agreed?

6 MS. HEATHER REICHERT: It is an

7 allocation, yes, that does increase the amount that

8 needs to be funded through premium rates. Yes -- yes,

9 it does.

10 MR. BYRON WILLIAMS: Okay. Now, Ms.

11 Reichert, you can accept this subject to check or I can

12 give you a reference.

13 But would it be fair to say that for the

14 '13/'14 year, the IT staff is -- is represented in

15 full-time equivalents for the Corporation is expected -

16 - was -- was three hundred and thirty-two (332)?

17 MS. HEATHER REICHERT: No, that -- that

18 would not be a fair -- a fair statement.

19 MR. BYRON WILLIAMS: Internal and

20 external, Ms. Reichert.

21 MS. HEATHER REICHERT: Okay. So to

22 clarify the three thirty-two (332), if I -- if I'm

23 aware of the reference, I think that's coming from the

24 Gartner review -- report that they do on an annual

25 basis. That Gartner report includes consultants and

1 equates them to full-time equivalent staff. So as it
2 relates to actual employees on -- receiving a salary
3 from MPI, the number is something significantly less
4 than that. And I won't guess, but it is definitely
5 significantly less than the three hundred (300).
6 MR. BYRON WILLIAMS: Yes. And if my
7 question was imprecise, which I'm not sure it was, all
8 in, including internal and external staff, the full-
9 time equivalents associated with information technology
10 is a bit over three hundred and thirty (330) persons as
11 measured in FTEs, agreed?
12 MS. HEATHER REICHERT: As it relates
13 to, again, IT operations, as well as IT projects. So
14 remembering that there were still significant projects,
15 i.e., the one we've talked about a fair bit, the
16 Physical Damage Re-engineering Project, where there
17 will be consultants that are working on that project
18 that will be included within that three hundred and
19 thirty-two (332).
20 So -- so, yes, as a -- as an overall FTE
21 equivalent. But as normal operating IT staff to
22 support the systems that we have which have increased
23 significantly over the -- the past many years, the
24 number of actual staff in the organization is
25 substantially less that three hundred (300) and

whatever the number was.

MR. BYRON WILLIAMS: And we'll come to that in just a second. So you've noted that the systems have increased substantially. And in terms of the internal staff, it's about two hundred and ten (210), two twelve (212), as measured in FTE equivalence?

MS. HEATHER REICHERT: I would really like to --

MR. BYRON WILLIAMS: Okay.

MS. HEATHER REICHERT: -- know the reference so that I can --

MR. BYRON WILLIAMS: You need a reference. That's three sixteen (3-16). I thought you'd have this memorized, Mr. Reichert.

MS. HEATHER REICHERT: I just res --

MR. BYRON WILLIAMS: PUB 3-16.

MS. HEATHER REICHERT: PUB 3-16, okay. So subject to check, yes, two hundred (200).

MR. BYRON WILLIAMS: And two hundred and twelve (212), Ms. Reichert?

MS. HEATHER REICHERT: Subject to check, two hundred and twelve (212).

MR. BYRON WILLIAMS: And in terms of the equivalent external folks as measured in FTEs,

1 we're talking about one hundred and twenty (120),
2 agreed?
3 MS. HEATHER REICHERT: Agreed. Oh,
4 yes, okay.
5 MR. BYRON WILLIAMS: Now, Ms. Reichert,
6 the Gartner Group -- and we can turn if you'd like to
7 AI.12, Appendix 4 -- it compares Manitoba Public
8 Insurance to its peers in terms of the percentage of
9 company employees who are IT employees, agreed?
10 MS. HEATHER REICHERT: Sorry, was there
11 a specific page reference?
12 MR. BYRON WILLIAMS: Oh, page 15.
13 MS. HEATHER REICHERT: Thank you.
14
15 (BRIEF PAUSE)
16
17 MR. BYRON WILLIAMS: And, Ms. Reichert,
18 if you've forgotten my question, it wasn't that good of
19 a question anyways, but you'll agree that Manitoba
20 Public Insurance -- or the Gartner Group on behalf of
21 Manitoba Public In -- Public Insurance compares the
22 percentage of MPI employees in IT as part of the -- as
23 a percentage of the Corporation versus their peers,
24 agreed?
25 MS. HEATHER REICHERT: Correct. And on

1 -- if I'm not mistaken, this particular measure would
2 be FTEs, including internal and external. I -- I think
3 that --
4 MR. BYRON WILLIAMS: I think you're per
5 -- mistaken.
6 MS. HEATHER REICHERT: Oh, am I
7 mistaken on this one? Well, you know, I know that you
8 will correct me if I am.
9 MR. BYRON WILLIAMS: We're going to
10 come to that in -- in just a second, Ms. Reichert.
11 Well, I'm going to suggest to you, and
12 you'll correct me if I'm wrong, that this represents
13 the internal staff as a percentage of the Corporation
14 as compared to the total number of employees?
15
16 (BRIEF PAUSE)
17
18 MR. BYRON WILLIAMS: And, Ms. Reichert,
19 if you're looking for the in-house versus contractors,
20 that's on page 17.
21
22 (BRIEF PAUSE)
23
24 MS. HEATHER REICHERT: Sorry, I am
25 looking on -- on page 15. And I'm just doing some --

1 some math. So -- so based on the percentages on -- on
2 page 15, our total number of company employees is in
3 and around nineteen hundred (1,900) to two thousand
4 (2,000), but just roughly. So that's why I was fairly
5 certain --
6 MR. BYRON WILLIAMS: Okay.
7 MS. HEATHER REICHERT: -- that the
8 number that they were calculating here, like, MPI 2013
9 being seventeen point two (17.2), was taking the -- the
10 Gartner number of FTEs that includes --
11 MR. BYRON WILLIAMS: Got --
12 MS. HEATHER REICHERT: -- consultants
13 to arrive at seventeen point two (17.2), which is like
14 three hundred (300) and something divided by
15 approximately nineteen hundred (1,900) to two thousand
16 (2,000). So that - that's why I -- I thought they were
17 using the external and internal number.
18 MR. BYRON WILLIAMS: That's fair
19 enough. And that's helpful. And I appreciate that
20 clarification. What that's suggesting is that the --
21 accepting that this is a combination of external and
22 internal, that the peer average was about 11 percent as
23 compared to the MPI average in 2013 of about 17
24 percent?
25 MS. HEATHER REICHERT: Correct. And my

1 understanding of why -- and -- and I -- my
2 understanding of why we are still higher than what that
3 peer average is, is that MPI is still on the basis of
4 2013, which is the '12/'13 fiscal year, still in that
5 heavy IT enhancement period, so there's a lot of
6 activity. We're not in the stable, like, Let's just
7 maintain what we have phase
8 So my understanding from my discussions
9 with colleagues is that is still why we will show
10 higher than an overall industry average. But -- but,
11 yes, I take that we're at seventeen point two (17.2)
12 versus a peer average of eleven (11).
13 MR. BYRON WILLIAMS: And, Ms. Reichert,
14 just to follow up on your very thoughtful point, when
15 we looked at the number of external contractors
16 anticipated by the Corporation going forward, it's
17 still looking at maintaining that level out a number of
18 years, agreed?
19 I had that conversation with Mr. Guimond
20 the first week of the hearing.
21 MS. HEATHER REICHERT: Generally
22 speaking, yes, because we -- we still are doing, as
23 we've talked about, the Physical Damage Re-engineering
24 Project.
25 MR. BYRON WILLIAMS: And if we turn to

1 page 17, what we have there is a comparison between the
2 relative ratio of consultants to in -- in-house staff,
3 comparing MPI to its peers.
4 Is that fair?
5 MS. HEATHER REICHERT: Yes. That's
6 true. And this definitely shows that MPI has a higher
7 proportion of external consultants in our overall FTE
8 complement, as calculated by -- by Gartner. And the
9 difficulty that we have in Manitoba is attracting the
10 right skill set, the -- the IT architecture resources,
11 et cetera; extremely difficult to be able to attract
12 those at the appropriate salary, because IT -- IT
13 salaries are still very -- very competitive. Hard to
14 find, first, the skill set. And then if you find the
15 skill set, hard to be able to attract them to become a
16 actual employee. So that's resulting in us having to
17 rely more on consultants than on actual employees or
18 staff.
19 It is an area that we see we are off
20 side with what the industry norm is. It is an area
21 that I know that the VP and CIO is looking to try to
22 bring us closer to that. It will take time. The --
23 there's no question. But it is something that we are
24 overall looking to -- to get closer to that norm.
25 MR. BYRON WILLIAMS: Ms. Reichert,

1 you're telling me that instead of going to law school,
2 I should have gone into computer sciences?
3 MS. HEATHER REICHERT: We all should
4 have gone into computer science.
5 MR. BYRON WILLIAMS: Then we couldn't
6 have this fun, though. If we could turn to -- and
7 thank you for that. If we can turn to -- and thank you
8 for that. If we can turn to CAC 1-60, attachment (a),
9 and page 6 specifically. And Ms. Reichert, this is
10 just one (1) expenditure out of your road safety and
11 advertising that my client wished to ask you about.
12 And -- and if -- if it's one that's unfamiliar with
13 you, you can certainly assist my client by way of an
14 undertaking.
15 If we go to page 6, under "Safety
16 advertising sponsorships." Thank you, Diana. Right
17 there's perfect. Ms. Reichert, one (1) that caught my
18 client's attention is the fourth entry from the bottom
19 of the page, related to Wind City Productions. And
20 I'll ask you to confirm that in this particular year,
21 MPI committed in the range of one hundred thousand
22 dollars ($100,000) to -- under safety advertising
23 sponsorships, to the Wind City Productions, a branded
24 web series.
25 Is that your understanding?

1 MS. HEATHER REICHERT: Yes, it is. And
2 I will take as an undertaking. I have general
3 familiarity of -- with -- with what that related to,
4 but rather than misspeak in any way, I will take as an
5 undertaking to describe more clearly what that
6 expenditure related to.
7
8 --- UNDERTAKING NO. 51: MPI to describe what
9 specifically the one
10 hundred thousand dollars
11 ($100,000) that MPI
12 committed to Wind City
13 Productions related to
14
15 CONTINUED BY MR. BYRON WILLIAMS:
16 MR. BYRON WILLIAMS: Okay. And -- and
17 Ms. Reichert, have you, like Ms. Menzies and myself,
18 viewed that web series?
19 MS. HEATHER REICHERT: I know I did
20 attempt to view it at one (1) time on -- on the system
21 at work and wasn't able to and didn't get back to it.
22 But -- but, yes, I am aware that it was viewed by many.
23 MR. BYRON WILLIAMS: I wonder if you
24 can, by way of undertaking provide the evaluation
25 report analyzing the effect of Wind City sponsorship in

1 -- in reducing the costs -- the social and economic
2 costs of automobile accidents in the province?
3 You do evaluation reports for these
4 sponsorships, agreed?
5 MS. HEATHER REICHERT: We do many
6 evaluation reports. I cannot say unequivocally that we
7 did an evaluation report of this specific project. And
8 as the -- the panel likely is -- is aware, often it is
9 very difficult to show causality from a advertising
10 program and subsequent reductions in claims. It's very
11 difficult to -- to draw that direct line.
12 So your question about -- and I will, as
13 an undertaking, determine whether or not we did do an
14 evaluation of this specific expenditure; and if we did,
15 endeavour to provide that to the Board. I won't go so
16 far as to say that it will show if we've done one (1)
17 direct cau -- direct impact to claims as a result of
18 this particular program and advertising.
19 MR. BYRON WILLIAMS: I appreciate your
20 cau -- caution, Ms. Reichert, and that's certainly --
21 the undertaking, as I understand it, is to investigate
22 whether there was an evaluation in terms of this
23 particular expenditure, and if so to provide it for the
24 Board's information, agreed? Related to the one
25 hundred and four thousand (104,000) in safety

1 advertising sponsorships associated with Wind City
2 Productions.
3
4 --- UNDERTAKING NO. 52: MPI to investigate whether
5 there was an evaluation
6 related to the one hundred
7 and four thousand (104,000)
8 in Safety Advertising
9 Sponsorships associated
10 with Wind City Productions
11 and the number of persons
12 who viewed the branded web
13 series; and if so to
14 provide it for the Board's
15 information
16
17 CONTINUED BY MR. BYRON WILLIAMS:
18 MR. BYRON WILLIAMS: And, Ms. Reichert,
19 in -- in so doing, would you investigate the number of
20 persons who -- who viewed the -- the branded web series
21 as well for my client?
22 MS. HEATHER REICHERT: Yes, I will.
23 THE COURT REPORTER: Is that part of
24 the same undertaking?
25 MS. HEATHER REICHERT: Yes, it is.

(BRIEF PAUSE)

CONTINUED BY MR. BYRON WILLIAMS:

MR. BYRON WILLIAMS: I'm -- just one (1) second. If I could consult with the Board secretary for one (1) moment?

(BRIEF PAUSE)

CONTINUED BY MR. BYRON WILLIAMS:

MR. BYRON WILLIAMS: Ms. Reichert and the MPI panel, I'm going to be asking you to direct your attention to an excerpt from the AAA Foundation for Traffic Safety "Evaluation of Beginner Driver Education Programs." And -- and while CAC distributed this excerpt, I believe, for marking purposes, MPI actually provided the link, and that is MPI-17. So my understanding is that this is part of Exhibit MPI-17, subject to confirmation from My Learned Friend Ms. Kalinowsky. But I -- she's nodding her head, so that's where we -- where we are.

And, Ms. Reichert, is that you or Mr. Johnston?

MS. HEATHER REICHERT: I'll ask you to ask your question, and then we'll -- we'll figure that

1 out.

2 MR. BYRON WILLIAMS: Are you familiar

3 with this report?

4 MS. HEATHER REICHERT: Only

5 peripherally.

6 MR. BYRON WILLIAMS: Do you feel able,

7 Ms. Reichert, to at least discuss some of the

8 observations from the executive summary? I'll be

9 gentle.

10 MS. HEATHER REICHERT: Yeah. If -- if

11 you --

12 MR. BYRON WILLIAMS: As always.

13 MS. HEATHER REICHERT: -- promise -- if

14 you promise to be gentle. Start, and then I will

15 definitely respond only to what I feel comfortable in

16 responding to. MR. BYRON WILLIAMS: Fair enough. And

17 I -- I think that's -- I appreciate your cooperation.

18 I think that's an appropriate way to proceed.

19 Directing your attention to page 4 of

20 the executive summary, the second full paragraph, Ms. -

21 - Ms. Reichert, I'll just ask you to con -- confirm

22 that this is -- the second full paragraph is basically

23 just referring to the fact that, to-date, evaluations

24 have not necessarily demonstrated that driver education

25 programming to-date is producing safer driving --

1 drivers.
2 Would that be fair?
3 MS. HEATHER REICHERT: I think you've
4 somewhat paraphrased that, but -- but generally, yes.
5 MR. BYRON WILLIAMS: Okay. And when we
6 look at this survey conducted by AAA, you'll agree with
7 me that it examined results both in Manitoba and
8 Oregon?
9 Would that be fair? Related to high
10 school driver education programming -- driver education
11 program, excuse me?
12 MS. HEATHER REICHERT: Yes, that is my
13 understanding.
14 MR. BYRON WILLIAMS: And if you need a
15 reference, I can provide it. But would you agree that
16 in -- in terms of the Oregon program, an -- an analysis
17 was done in terms of their driver education programming
18 in terms of performance on the license tests, and in --
19 and in terms of collisions, convictions, and
20 suspensions? That's on page 8 under "Safety
21 Effectiveness," if you need the reference, Ms.
22 Reichert.
23 MS. HEATHER REICHERT: Yes, I see that
24 there.
25 MR. BYRON WILLIAMS: So that's for

1 Oregon. In terms of the safety effectiveness of the
2 Manitoba high school driver education program, it would
3 be fair to say that the program was assessed in terms
4 of performance on licence tests, agreed? Again that's
5 from page 8 under "Safety Effectiveness."
6 MS. HEATHER REICHERT: Yes.
7 MR. BYRON WILLIAMS: So unlike the
8 analysis conducted in Oregon, the MPI high school
9 driver education program was not assessed in terms of
10 its performance in terms of collisions, convictions,
11 and suspensions, agreed?
12 MS. HEATHER REICHERT: Yes.
13 MR. BYRON WILLIAMS: And, Ms. Reichert,
14 if you're unable to answer this question I'll
15 understand why. You'll just explain that to me.
16 But in terms of the decision not to
17 examine the Manitoba Public Insurance high school
18 driver education program in terms of its performance in
19 terms of collisions, convictions, and suspensions, was
20 that at the advice of Manitoba Public Insurance, or are
21 you aware?
22 MS. HEATHER REICHERT: I can't respond
23 to that question. I -- I can take it as an
24 undertaking, if you would like.
25 MR. BYRON WILLIAMS: Yes, and I

1 certainly don't mean to be unfair. So if you can
2 inquire as whether the decision not to evaluate the
3 performance of the MPI high school driver education
4 program in terms of collisions, convictions, and
5 suspensions was done at the request of MPI, that would
6 be helpful.
7 MS. HEATHER REICHERT: Yes, I will.
8
9 --- UNDERTAKING NO. 53: MPI to inquire as to
10 whether the decision not to
11 evaluate the performance of
12 the MPI high school driver
13 education program in terms
14 of collisions, convictions,
15 and suspensions was done at
16 the request of MPI
17
18 CONTINUED BY MR. BYRON WILLIAMS:
19 MR. BYRON WILLIAMS: Now, just -- I
20 know both you and I love talking methodology. Just at
21 page 6, at a very high level -- right there, Diana, is
22 perfect.
23 Ms. Reichert, I'm not going to get into
24 the details but you'll agree with me, regardless of the
25 waves and cross-sectional components employed, there

1 was a comparison of -- of a group of -- of students in
2 high schools across the province comparing students who
3 indicated they were going to take driver education
4 versus those who indicated they were not planning to
5 take it.
6 So that's the comparison, those planning
7 to take it and those not taking it, agreed?
8 MS. HEATHER REICHERT: Are you
9 referring to the last bullet there? The first, I'm
10 sorry.
11 MR. BYRON WILLIAMS: Yeah, well, either
12 bullet's fine, Ms. Reichert. In essence, what you were
13 -- we were doing -- what AAA was doing was comparing
14 the scores on Manitoba driver licence road tests among
15 those who graduated from the high school driver
16 education program versus those who had not, agreed?
17 MS. HEATHER REICHERT: Agreed.
18 MR. BYRON WILLIAMS: And in doing so,
19 it was not just assessing -- it was getting insight
20 into both groups, presumably. We'll scratch that
21 question. I'll do it more elegantly, I hope, a little
22 later on.
23 In turning your attention to page 7
24 under, "Changes in Student Outcomes," the first bullet,
25 you'll agree with me that one (1) positive outcome in

1 terms of exposure to the MPI high school drive
2 education program was that it was associated with
3 greater self-reported driving skills and less risk-
4 taking behaviours after controlling for age and gender.
5 Would that be fair?
6 MS. HEATHER REICHERT: Yes.
7 MR. BYRON WILLIAMS: If we go to --
8 under the bullet, "Knowledge Gains," would you agree
9 that the survey reported significant increases in
10 knowledge, both in terms of the graduated driver's
11 licensing program and safe driving issues among teens
12 in the Oregon-approved driver education program, but
13 not for those in the MPI program with the possible
14 exception of higher knowledge scores?
15 Would that be fair? And if we can
16 scroll to the next page, that would assist Ms.
17 Reichert.
18 MS. HEATHER REICHERT: I agree that is
19 what it says in that bullet.
20 MR. BYRON WILLIAMS: And the bullet
21 which follows suggests that there was -- with -- in
22 both cases, still a relatively low level of knowledge
23 among teen drivers completing these programs in both
24 Manitoba and Oregon?
25 MS. HEATHER REICHERT: Correct.

1 MR. BYRON WILLIAMS: Turning your
2 attention to, "Licence Test Performance," scrolling
3 down page 8, the first bullet.
4 In terms of the Manitoba drive licence
5 road test -- I'll divide this into two (2) parts --
6 there was no significant difference, you'll agree with
7 me, in the past rates for the -- the Manitoba students
8 who took high school driver's ed. versus the non-
9 driver's ed. group? Stopping there.
10 Fair enough?
11 MS. HEATHER REICHERT: Fair enough.
12 MR. BYRON WILLIAMS: Although the MPI
13 group that did have better test scores both among those
14 who failed and those who passed, correct?
15 MS. HEATHER REICHERT: Correct.
16 MR. BYRON WILLIAMS: In terms of
17 licence test performance under the second bullet,
18 anyone who knows teenagers won't be surprised by this
19 one, you'll see that the Manitoba driver's ed. students
20 with an intermediate licence still showed a
21 significantly higher rating of their self-reported
22 driving skills which might, the authors conclude,
23 suggest they overestimate their actual skill levels?
24 MS. HEATHER REICHERT: It sounds pretty
25 typical teenage behaviour.

1 MR. BYRON WILLIAMS: And at the risk of
2 testifying, it -- based upon my observations of men in
3 their young 20s, I think its pretty typical of them, as
4 -- as well.
5 I won't -- Ms. Reichert, we won't go
6 through it except for to note on pages 9 and 10 that
7 there is a discussion of the results in Oregon in terms
8 of whether taking driver's ed. was associated with
9 reductions in collisions. Just -- we'll just note that
10 for the panel.
11 You'll -- you'll nod your head and agree
12 with me verbally on that?
13 MS. HEATHER REICHERT: Yes.
14 MR. BYRON WILLIAMS: At page 10 under,
15 "Driving Skills," which is towards the bottom of the
16 document, you'll see in -- in essence a mixed blessing
17 with students exposed to the driver education program
18 in Manitoba demonstrating both a significant -- well,
19 dem -- demonstrating a significant increase in self-
20 rated skills as compared to non-driver's ed. -- ed.
21 group.
22 Do you see that?
23 MS. HEATHER REICHERT: Yes.
24 MR. BYRON WILLIAMS: And you'll agree
25 with me, looking to the rest of the -- the paragraph,

1 that the authors note that this can be both a potential
2 safety benefit to the extent that self-rated skills
3 reflect actual skills, but may have the potential to
4 generate an optimism -- optimism bias of an unrealistic
5 skill level.
6 Would that be fair?
7 MS. HEATHER REICHERT: Yes.
8 MR. BYRON WILLIAMS: On page 11, the
9 second bullet -- or it -- excuse me, I apologize, the
10 second paragraph -- there is a suggestion that more
11 focus should be placed specifically on -- in training
12 in hazard anticipation skills for the -- the Manitoba
13 high school program.
14 Do you see that, Ms. Reichert?
15 MS. HEATHER REICHERT: Yes, I do.
16 MR. BYRON WILLIAMS: And just by way of
17 undertaking, and I think this will make Mr. Guimond
18 happy, if you can -- if you're prepared to, Ms.
19 Reichert, undertake to indicate whether MPI in terms of
20 placing additional training in hazard anticipation
21 skills, what if any plans they have with regard to
22 their -- their program, that would be helpful.
23 MS. HEATHER REICHERT: Yes, I will take
24 that undertaking.
25

--- UNDERTAKING NO. 54: MPI to indicate if it plans to place additional training in hazard anticipation skills into the Manitoba high school program

CONTINUED BY MR. BYRON WILLIAMS:

MR. BYRON WILLIAMS: And going down two (2) bar -- two (2) paragraphs, Ms. Reichert, you'll see a -- a suggestion that the authors are recommending a detailed review of the road test and curriculum content to determine the sources of test unreliability, the extent to which covers driving errors -- errors that are critical, and which errors could be addressed in the driver education program.

Do you see that reference?

MS. HEATHER REICHERT: Yes, I do.

MR. BYRON WILLIAMS: And, Ms. Reichert, again realizing that you're being generous with your time here, if -- if by way of undertaking you could agree to two (2) elements. One (1) is to clarify what is meant by "test unreliability." And, secondly, to indicate whether MPI is considering a detailed review of the road test and curriculum content.

1 MS. HEATHER REICHERT: Sure. I'll take
2 that undertaking.
3
4 --- UNDERTAKING NO. 55: MPI to clarify what is
5 meant by "test
6 unreliability" and indicate
7 whether MPI is considering
8 a detailed review of the
9 road test and curriculum
10 content
11
12 CONTINUED BY MR. BYRON WILLIAMS:
13 MR. BYRON WILLIAMS: And turning to
14 page 13 in terms of -- under the heading "Conclusions
15 For Driver's Education." And I'll give you a second
16 just to review that, Ms. Reichert, if you'd like.
17
18 (BRIEF PAUSE)
19
20 MR. BYRON WILLIAMS: One (1) of the
21 conclusions of the authors is that the investigation
22 provide some evidence in support of the benefits of
23 driver education in terms of the intermediate measures
24 such as improved knowledge and driving skills and
25 safety, agreed?

1 MS. HEATHER REICHERT: Agreed.
2 MR. BYRON WILLIAMS: The authors do
3 caution though that positive effects of the MPI program
4 have been modest, or in relation to some factors
5 absent, and caution must be taken regarding their
6 potential to reduce collisions.
7 Did I paraphrase that fairly, Ms.
8 Reichert, in your view?
9 MS. HEATHER REICHERT: Yes, I think you
10 did. MR. BYRON WILLIAMS: Ms. Reichert, just
11 one (1) last question. In preparing this report --
12 just one (1) second. Excuse me.
13
14 (BRIEF PAUSE)
15
16 MR. BYRON WILLIAMS: Ms. Reichert, MPI
17 was one (1) of -- you'll agree with -- you'll agree
18 that MPI was one (1) of the financial supporters of
19 this study, along with the Centre for Disease Control
20 and Prevention, the National Highway Traffic Safety
21 Administration.
22 Would those be the three (3), going to
23 the acknowledgments on the -- the inside page?
24 MS. HEATHER REICHERT: That sounds
25 reasonable.

1 MR. BYRON WILLIAMS: And are you...
2
3 (BRIEF PAUSE)
4
5 MR. BYRON WILLIAMS: And if you're not
6 able to answer this, don't -- don't worry about it.
7 Are you aware why MPI was the -- chosen, or asked, to
8 participate in this particular study?
9 Was -- and if not, that's fine, Ms.
10 Reichert.
11 MS. HEATHER REICHERT: No, I -- I can't
12 comment.
13 MR. BYRON WILLIAMS: Madam Chair, I
14 have one (1) relatively small area I -- I hope that I -
15 - I think I might be able to cover. And then subject
16 to a review of my notes, I think I would be -- well, a
17 review of my note and a review of my client's
18 instructions, I would be probably done. I'm not sure
19 if it will take five (5) minutes or ten (10), but I
20 don't expect it to be particularly long.
21 If I could ask MPI to turn to the
22 response to PUB/MPI Pre-Ask 5, and I believe it was --
23 I'm not sure if that's under MPI Exhibit 10-5 or not,
24 but it's the -- it's the table -- yeah, the attachment
25 to the Pre-Ask 5(a).

(BRIEF PAUSE)

MR. BYRON WILLIAMS: And these are just a few cleanup questions to make sure that we understand this table. Looking at the 2014 calendar year, the second-last column is the -- a characterization of the -- the MPI standard forecast that was used in the General Rate Application, agreed?

MS. HEATHER REICHERT: Agreed.

MR. BYRON WILLIAMS: And the figure, focussing on the first quarter, would be... The 2.62 percent used for that figure would be based upon the forecasts, I'll ask you to accept subject to check, of RBC for the March end, Scotia for the March end, TD for the March end, BMO for the average of the first quarter, and CIBC for the March end.

Would you accept that subject to check?

MS. HEATHER REICHERT: Yes, I -- I think you're just reading in what the data source dates are there --

MR. BYRON WILLIAMS: Well --

MS. HEATHER REICHERT: -- or -- or the --

MR. BYRON WILLIAMS: -- the -- the --

MS. HEATHER REICHERT: -- average of

period, average of period. So, anyways, yes, I agree.

MR. BYRON WILLIAMS: Well, we'll come to one (1) of those points. But the data source you'll see there are for October and September. I'm focussing, Ms. Reichert, on the two point six-two (2.62) employed for the first quarter of 2014.

And I'm asking you to accept those -- those data sources subject to check.

MS. HEATHER REICHERT: I accept.

(BRIEF PAUSE)

MR. BYRON WILLIAMS: And for the second quarter, again for the March 2014 standard, that would represent the forecasts of the banks and -- and Global for the -- in the case of RBC, the June end; in the case of Scotia, the June end; in the case of TD, the June end; in the case of BMO, the average second quarter; and in the case of CIBC, the June end, agree -- you'll agree, subject to check?

MS. HEATHER REICHERT: Yes.

MR. BYRON WILLIAMS: Okay. So, in essence, for the first quarter we've got the March end dates for all but BMO, for -- for which you use the average for that quarter, agreed?

1 MS. HEATHER REICHERT: Yes.
2 MR. BYRON WILLIAMS: And for the second
3 quarter we've got the June end, with the exception
4 again of BMO, which uses the average for that period,
5 agreed?
6 MS. HEATHER REICHERT: Agreed.
7 MR. BYRON WILLIAMS: And again, a small
8 point, but when -- if one (1) -- moving to the column
9 one (1) more to the left, the 2.25 percent, for the --
10 for the -- do you see that heading, "October 2014
11 standard average," Ms. Reichert?
12 MS. HEATHER REICHERT: Yes, I do.
13 MR. BYRON WILLIAMS: And you'll see
14 there's a suggestion, moving a couple columns over,
15 that this is applied to the fis -- MPI fiscal quarter,
16 Ms. Reichert.
17 Do you see that?
18 MS. HEATHER REICHERT: Yes.
19 MR. BYRON WILLIAMS: And am I correct
20 in suggesting to you that the MPI fiscal quarter, the
21 first quarter of 2014/'15, would run from March through
22 May?
23 MS. HEATHER REICHERT: Correct, March
24 1st to May 30th.
25 MR. BYRON WILLIAMS: And so if one

1 tried to back out that 2.25 percent number, Ms.
2 Reichert, I'll suggest to you that that's based upon a
3 end-of-May calculation?
4 MS. HEATHER REICHERT: Yes.
5 MR. BYRON WILLIAMS: Similarly -- and
6 so just to understand what you're doing in that first
7 quarter, you're comparing the forecasters mostly using
8 March end dates versus your first quarter and your --
9 the calculation using the May end date, agreed?
10
11 (BRIEF PAUSE)
12
13 MS. HEATHER REICHERT: So just to be
14 clear, the yellow highlighted, those would have been
15 the actuals as at -- the two point two-five (2.25)
16 would have been the actual as at the end of May based
17 on Bloomberg data. So we're taking an actual as at the
18 end of May and taking the difference from what we used
19 in our forecast for that same period.
20 MR. BYRON WILLIAMS: I understand that
21 point. What I -- I just want to make sure everyone in
22 the room understands is you're comparing the actual for
23 the end of May versus the bank forecast for March?
24 MS. HEATHER REICHERT: Yes, which was
25 used as our forecast for the end of may.

1 MR. BYRON WILLIAMS: And similarly, Ms.
2 Reichert, if we look at the -- in the fourth column,
3 under the results for the second quarter, those would
4 be calculated using Bloomberg data for the period
5 ending August 2014, agreed?
6 MS. HEATHER REICHERT: Yes.
7 MR. BYRON WILLIAMS: And a very small
8 point, Ms. Reichert, under "Data source dates." You
9 can just either accept this subject to check, or you
10 can -- we don't need an undertaking. But in term --
11 for CIBC -- actually, I'll scratch that.
12 For CIBC, Ms. Reichert, I guess the
13 question we're asking is our understanding is that CIBC
14 uses end dates, not averages. And -- and so I guess
15 the question we're posing to you is when you call that
16 a CIBC average of the period, is it as of -- is it just
17 the -- is it the average, or is it the end date?
18
19 (BRIEF PAUSE)
20
21 MS. HEATHER REICHERT: We can -- we can
22 check that, if -- if you would like. I -- I can take
23 it as an undertaking if you want?
24 MR. BYRON WILLIAMS: Yeah. It's --
25 it's a small point, but just for clarification, be --

our understand -- so what I'm seeking clarification on is -- is whether CIBC uses end dates or averages, and what that data source Sep -- dated September 17th, 2014, for CIBC represents.

Is that satisfactory?

MS. HEATHER REICHERT: Yes.

--- UNDERTAKING NO. 56: MPI to provide whether CIBC uses end date or averages and what the September 17th, 2014, data source represents for CIBC

MR. BYRON WILLIAMS: And, Madam Chair, subject to a review of my notes and client instructions, I may have one (1) or two (2) questions afterwards, but I expect that concludes our cross-examination.

THE CHAIRPERSON: Thank -- thank you very much, Mr. Williams. One (1) question from Mr. Gosselin.

MR. REGIS GOSSELIN: I have a coup -- couple of questions, I guess. The first one is related to normal operating expenses. And you identified -- attempted to show that those normal operating expenses

1 were tracking CPI or close to CPI.
2 I guess the question I have is: What
3 was excluded from the total expenditures to arrive at
4 normal expenditures?
5 MS. HEATHER REICHERT: What would have
6 been removed would have been implementation expenses
7 from total expenses. So when we talk about
8 implementation expenses on the capital, when we're
9 talking about capital, and there is deferred
10 expenditures, there is capital expenditures, and then
11 there is implementation expenses. That's what would
12 have been removed to arrive at the -- the normal
13 operating.
14 MR. REGIS GOSSELIN: So implementation
15 expenses, could you define that a bit more finely for
16 me?
17 MS. HEATHER REICHERT: So
18 implementation expenses would typically be when we have
19 staff. The -- the large part of that would be staff
20 that are working on a specific project that they would
21 be allocated to that project, charged to that project.
22 But we still expense those costs as opposed to
23 capitalizing them as part of the project. That's a --
24 an internal policy that MPI has followed for -- for
25 some time.

1 So that's the majority of the kinds of
2 expenditures that would be in there. There might be
3 other types of small expenditures that, again, are not
4 capitializable in nature but are relating to a specific
5 implementation, but the majority would be the staff
6 costs.
7 MR. REGIS GOSSELIN: One (1) of the
8 issues we face when -- when we sit as a -- a Board to
9 consider rate applications is we're often called upon
10 to make decisions based on information collected some
11 months prior and submitted to us in an application
12 form. And we faced that issue with -- with the major
13 utilities in the province, whether it's Centra or MPI,
14 or it's Hydro.
15 So -- so the case of Hydro, it may be,
16 you know, it may be water conditions are different and
17 so on, and export sales are better. So what we see
18 before us is an application, and what actually is
19 happening at the time that we are asked to make a
20 decision are two (2) different things. And I guess
21 we're seeing some of this now because MPI has based its
22 application on a certain set of scenarios, the most
23 important one of which is probably interest rate
24 forecasts. At least that's what I heard.
25 So -- so what we attempt to do with

1 Hydro and the other utilities is we attempt to try to
2 get them to give us a picture of what's actually
3 happening at the moment, so that we're not caught in a
4 situation as happened with this -- with this Board
5 before where -- where we're being told one (1) story
6 and a couple of days -- lit -- literally a couple of
7 days later the story is different after the -- the
8 Board has announced its rate application. And I -- we
9 have to find a way that we get some recent information
10 that provides us guidance with making a rate decision.
11 And -- and at -- at the moment, I -- I don't feel I
12 have enough information as a Board member to be able to
13 say -- to quantify in dollar terms what the impact is
14 of the rate changes that you have actually occurred.
15 So, you know, if it's the intention of -
16 - I would, frankly, would like to make a decision as a
17 -- as a Board member with the recent information about
18 the impact of the impact of the fluctuation in interest
19 rates.
20 So we -- we -- I think we have had
21 numbers, but could you -- I'd like to be able to look
22 at what the significance is in actual dollar terms over
23 the time frame that we're being asked to consider.
24 MS. HEATHER REICHERT: I believe we
25 have provided that to the Board. Pre-Ask -- PUB Pre-

1 Ask number 5 is using rates forecasted as at October of
2 2014. So that, I would propose, is the most recent
3 information as it relates to current forecasts of
4 interest rates and the impact that it -- that interest
5 rates alone would have on MPI.
6 And Mr. Johnston has just reminded me
7 there was Undertaking number 23, where the -- the Board
8 asked, or someone asked us to do the same forecast
9 assuming interest rates did not increase, but stayed
10 flat as they seem to have been doing in the last little
11 while. And that is un -- in Undertaking number 23,
12 which I am not sure what exhibit that is, but -- but
13 it's in -- in what we submitted yesterday I believe.
14 MR. REGIS GOSSELIN: There was an
15 article this week in the in the Globe and Mail, or at
16 least it might not have been -- it might not have been
17 this week. I'm looking at it right now. But it -- it
18 talks to the -- the yield curve for Canada, and no --
19 and basically indicating that the yield curve is
20 showing a very flat profile going out from the time at
21 which the yield curve was -- was calculated.
22 And I guess I'm -- I'm asking the
23 question now. I hate to spring this on you but I mean,
24 is a yield curve, the Canadian yield curve, one (1) of
25 the tools that might be considered in establishing our

interest rate forecast?

(BRIEF PAUSE)

MS. HEATHER REICHERT: Maybe if we can, we'll -- we'll chat over lunch, and then first thing when we come back from lunch, because there are aspects within our forecast where we are considering the yield curve. But I just want to be very clear and -- and precise in -- in responding to your -- to your question.

THE CHAIRPERSON: We'll accept that. And we'll break for lunch now, and we'll come back around ten (10) after 1:00. Okay. Thank you.

--- Upon recessing at 12:11 p.m.
--- Upon resuming at 1:15 p.m.

THE CHAIRPERSON: Welcome back. We're going to begin with Ms. Grammond. She has a few announcements to make.

MS. CANDACE GRAMMOND: Thank you, Madam Chair. Just a couple of housekeeping matters. First of all, today, obviously, we're sitting late, past the time that we normally sit. So we're advised that the

1 building will have a security person on the main floor
2 between 6:00 and 6:45, the idea being that would be
3 kind of the window when we would take a break, like, a
4 dinner break.
5 So if anyone wants to leave the
6 building, they need to go out through the front door
7 and come back in the same. The elevators on the second
8 floor will be closed off and so forth. So that's one
9 (1) item.
10 The other item is, over the course of
11 the hearing, and even in advance of the hearing
12 starting but after the application being filed, the
13 Board has received a series of emails from members of
14 the public. There are seven (7) of them that I would
15 say are in lieu of presentations, people that have just
16 sent short emails in to the PUB office.
17 So rather than reading those in, I'm
18 just going to circulate them to all the parties. So
19 the panel's got them. They're not evidence.
20 Obviously, they are just in the vein of a presentation,
21 but I'll circulate them to MPI and to all of the
22 Intervenors for information.
23 THE CHAIRPERSON: Thank you, Ms.
24 Grammond. I believe Ms. Reichert has comments to make
25 in regard to tho -- a question just before lunchtime.

1 MS. HEATHER REICHERT: Yes, I have a
2 couple of also housekeeping things, if I can. I just
3 wanted to -- to get back to Mr. Williams. He asked a
4 question on the PUB Pre-Ask 5, the interest rate table.
5 He asked specifically if the CIBC as of September 17th,
6 2014, it was known as a data source, if that was end of
7 period or average. And, in fact, it was a typo. It
8 should be end of period. And Global Insight right
9 below that is an average. So I just wanted to clarify
10 that and avoid formal response by an inder --
11 undertaking.
12 Right before lunch, Mr. Gosselin asked
13 about using the yield curve for forecasting interest
14 rates. So I just wanted to clarify that we use the
15 Government of Canada ten (10) year bond rate throughout
16 our forecast period. It's a point. It's one (1) point
17 on the -- on the yield curve. And then we apply to
18 that a spread that takes into account the duration of
19 the marketable bonds.
20 So we do -- we do forecast duration and
21 we use the Government of Canada bond, which is only one
22 (1) point, on the -- the ten (10) year bond, which is
23 only one (1) point on that yield curve, and then adjust
24 that to reflect the duration of different bonds along
25 the yield curve. So we in fact use as appropriate the

1 yield curve in our forecasting of interest rates. So I
2 just wanted to clarify that.
3 And Mr. Gosselin also had asked
4 specifically about recent information and the impact on
5 our rate indication. And I had referenced that we did
6 provide in -- in Pre-Ask number 5 -- PUB Pre-Ask number
7 5, as well as Undertaking number 23, some information
8 as -- as to different scenarios relating to interest
9 rates. And if -- if possible, Diana -- and I'm sorry I
10 didn't give you a head's up. But if possible if you
11 could go to PUB Exhibit number 42, which is Undertaking
12 number 23. I thought it might be helpful for the --
13 the panel if I just highlighted some of the information
14 contained in that -- in that exhibit.
15 Exhibit number 42, Undertaking number
16 23, yes. If you can go to the very first page, please,
17 Diana. Oh, I'm sorry, it's a document as opposed to
18 the attachment. Did I -- okay. Okay. So to the table
19 at the bottom of that page. So -- so this
20 particular table is summarized in the information that
21 was in Pre-Ask number 5, where we show a 3.4 percent
22 rate increase and the October standard interest rate
23 forecast.
24 So the line that I wanted to highlight
25 for the -- the panel is the third from the bottom, "Net

1 income," where in 2014/'15, based on the October
2 standard interest rate forecast, we would be projecting
3 an $82 million loss in '14/'15. And then you can see
4 the other numbers across there, as part of that
5 forecast.
6 The next line, "Retained Earnings,"
7 shows what retained earnings would be forecasted to be
8 with those respective net incomes having -- you know,
9 if they were to occur that way. So the underlying
10 assumption here is the October standard interest rate
11 forecast. So that's the five (5) major banks and
12 Global Insight.
13 So if we can go to the next page. This
14 is a similar table. And at the top table is with the
15 3.4 percent rate increase, which is our GRA, our -- our
16 submitted rate -- rate increase and the 2 percent flat
17 Government of Canada ten (10) year bond yield. So that
18 was a request that was made. Well, what would that
19 impact be? And again, I would draw your attention to
20 that net income line.
21 So at a flat interest rate the impact
22 obviously is much more significant to MPI. And you see
23 a hundred and three (103) loss of potential in '14/'15
24 and forty-five (45) loss, thirty-eight (38), thirty-one
25 (31), thirty-nine (39). And you can see on -- in that

1 scenario retained earnings actually goes into a
2 negative position and remains in a negative position
3 throughout that forecast period.
4 If we can flip back to the very
5 beginning to the -- to the paragraph above these
6 tables, I'll just highlight there. So -- so the first
7 table shows three point four (3.4) October standard
8 interest rate forecast, which I'll remind you does show
9 an increasing interest rate forecast. So the impact
10 there is essentially -- it's -- it's 3.4 percent. Just
11 reading from that top paragraph:
12 "The assumption of a flat 2 percent
13 interest rate reduces net income by a
14 cumulative 240 million over the
15 forecast period, while the impact
16 during the rating period is an
17 average reduction in net income of 40
18 million per year."
19 The total implied '15/'16 required rate
20 increase in that regard is in excess of 8 percent which
21 includes the 3.4 percent rate increase in -- that we've
22 submitted in our application. So I just wanted to walk
23 you through and -- and draw your attention to,
24 specifically, Mr. Gosselin's question before the lunch
25 hour.

1 MR. REGIS GOSSELIN: Thank you for that
2 more detailed explanation. I'm sorry, I have a
3 question. I -- I lost you on the yield curve issue.
4 Could you -- could you -- what I -- what I was trying
5 to get at is when you calculate the standard rate based
6 on the bank rates, bank estimations, and the Global
7 estimation you get an average.
8 I was suggesting perhaps you should
9 encompass what the yield curve is projecting as rates
10 going forward as part of that calculation to arrive at
11 a -- at an average value. So -- so in addition to
12 using the -- the values of the banks, from the bank
13 estimates and Global's, you would encompass the
14 estimation derived from the yield curve to arrive at --
15 at est -- at a -- at a rate forecast.
16 MS. HEATHER REICHERT: I'm going to let
17 Mr. Johnston take a stab at answering it, because
18 sometimes his words are a little bit better presented
19 than mine.
20 MR. LUKE JOHNSTON: That would be the
21 first time I've ever heard someone say that. So we
22 might -- I think we're talking about the same thing,
23 but we're talking about the yield curve. We're talk --
24 the -- the way I'm seeing -- understanding it is you're
25 looking at the yields for different maturities, you

1 know, at different maturity levels.
2 And so longer maturities generally will
3 have a higher -- I think people demand a higher yield.
4 So we're really forecasting just the ten (10) year bond
5 points on that yield curve. So, like, short maturities
6 will have lower yields and the -- you know, they'll
7 increase.
8 If there's a general increase in
9 interest rates, you'll generally see some sort of a
10 shift. Often, we'll refer to it as a 'parallel shift',
11 where every point on that curve will increase.
12 That's -- it doesn't always happen that
13 way, but the way Ms. Reichert was describing it is our
14 model does take into account the changes in the yield
15 curve based on how we invest our money. But we -- we
16 weren't understanding how -- how we could use the yield
17 curve in its totality to make the forecast, since we're
18 really looking at kind of one (1) point on that yield
19 curve.
20 Is -- does that make sense? Does that
21 help? Yeah? Okay.
22 THE CHAIRPERSON: Mr. Williams...?
23 MR. BYRON WILLIAMS: I don't have any
24 more questions, but certainly, if the panel has more
25 interest in that particular issue -- if not, that's

1 fine, but if you wanted to articulate in writing kind
2 of what exactly the panel's thinking of, we'd -- we'd
3 certainly be happy to get advice from Mr. McCormick in
4 terms of -- of that. So I -- I would just make that --
5 that offer.
6 THE CHAIRPERSON: Yeah. Thank you, Mr.
7 Williams.
8 Now we're ready to have the cross-
9 examination by Mr. Oakes of CMMG. Mr. Oakes...?
10 MR. RAYMOND OAKES: Thank you, Madam
11 Chair. I have a couple of preliminary matters. The
12 first would be a new exhibit. I believe it would CMMG
13 Exhibit number 4. It's the document which is the
14 Canadian Institute of -- of Actuarial Standards of
15 Practice. There's excerpts from that document, and
16 I'll be seeking to make that the next exhibit. That's
17 number 4. Thank you.
18
19 --- EXHIBIT NO. CMMG-4: Excerpts from the Canadian
20 Institute of Actuarial
21 Standards of Practice
22
23 MR. RAYMOND OAKES: And just by way of
24 general comments and advice to the Board, I hope that
25 you're not wondering about the length and whether the

1 chair has adequate padding all over the chair because
2 I'm examining in the area of actuarial practice and
3 rate-making methodology. So you'll just be using the
4 front of your seat as -- just the edge.
5 And also by way of general comments, I
6 do want to commend both Mr. Johnston and Ms. Reichert
7 with respect to their testimony so far. We have two
8 (2) extremely competent, skilful witnesses in their
9 chosen areas.
10 And even better than that, their
11 responses in the course of this hearing have been very
12 responsive to the question, accurate, and shows the
13 integrity that they bring to their positions. And I'm
14 hopeful that I'll make those same comments in my final
15 argument, and I certainly expect that I will.
16
17 CROSS-EXAMINATION BY MR. RAYMOND OAKES:
18 MR. RAYMOND OAKES: At this time, I'd
19 ask Diana if she could, to put up CMMG 1-5 up on the
20 monitors. Thank you.
21 And, Mr. Johnston, I'm asking you to
22 look at the increases sought by the Corporation in the
23 first three (3) years of those tables, and I'll just
24 highlight what they are. Of course, you can see them.
25 2004/'05, the Corporation sought 19.93 percent.

1 2005/'06, they sought 15.01 percent. 2006/'07, they
2 sought 12.7 percent.
3 Do you see that, sir?
4 MR. LUKE JOHNSTON: Yes, I do.
5 MR. RAYMOND OAKES: All right. And
6 then we've -- we see, looking at that table, we've had
7 quite a different situation commencing after 2011 where
8 every year to date has -- the Corporation has sought a
9 decrease. In fact, every year including 2011, the
10 Board has pre -- approved a decrease in the motorcycle
11 rates.
12 Do you see that, sir?
13 MR. LUKE JOHNSTON: Yes.
14 MR. RAYMOND OAKES: Okay. Now, going
15 back to what I would term the bad old days, 2004, '05,
16 '06, inclusive, the first three (3) indicated there,
17 you'll recall the contention of the CMMG during those
18 years was that these were massive rate increases that
19 were unwarranted, and causing rate shock and financial
20 hardship to the motorcyclist province.
21 Do you recall that, sir?
22 MR. LUKE JOHNSTON: Something to that
23 effect, yes.
24 MR. RAYMOND OAKES: And the contention
25 of the CMMG at that time was that these were knee-jerk

1 reactions, and the Corporation should have a smoother
2 curve of increases to avoid rate volatility.
3 Do you recall that, sir?
4 MR. LUKE JOHNSTON: I'm not sure if --
5 if I recall those exact words, but I would agree that
6 the CMMG would have preferred something less than some
7 of the large increases they were receiving over that
8 period.
9 MR. RAYMOND OAKES: You'll agree that
10 was the thrust of our intervention, those specific
11 words?
12 MR. LUKE JOHNSTON: Yeah, that's fair.
13 MR. RAYMOND OAKES: Okay. I wonder if
14 we could put up at this time MPI Exhibit number 3. And
15 this is the article from the Free Press dated October
16 22nd, 2014. And we don't need to have it up on the
17 screen but the reference to the transcript is page 468.
18 And your president is quoted as saying
19 that a 4.4 percent increase would be too steep an
20 increase for vehicle owners.
21 Do you see that or recall that evidence,
22 sir?
23 MR. LUKE JOHNSTON: Yes, I see that
24 there. It's about the third column of text in the
25 middle.

1 MR. RAYMOND OAKES: Thank you. And on
2 cross-examination, your president said that in his
3 opinion anything above 2 percent more than inflation
4 would be a problem.
5 Do you agree with -- do you recall that,
6 sir?
7
8 (BRIEF PAUSE)
9
10 MR. LUKE JOHNSTON: Yes, I believe
11 those were the comments, and --- and it was in regard -
12 - in regards to the -- the entire fleet, what -- what's
13 appropriate for an overall increase to the fleet.
14 MR. RAYMOND OAKES: And if we can just
15 switch back to the previous representation, CMMG 1-5,
16 you'll see in the three (3) years at the top of that
17 table the Corporation didn't have any of those same
18 considerations about protecting motorcyclists and that
19 increases of 4.4 percent would be too steep.
20 Do you agree, sir?
21 MR. LUKE JOHNSTON: The -- our rate
22 changes have always had dispersion among the different
23 classes, depending on the rate requirements of the
24 particular class. So we heard a little bit earlier
25 that taxis, for example, were getting a fairly

1 substantial increase because of their experience.
2 So every time we submit a rate
3 application, we do have classifications that are on
4 kind of the outer bounds of our -- of our caps that we
5 use. So we have a 15 percent plus or minus experience
6 cap, and then a firm 20 percent cap on everyone's rates
7 in a particular year.
8 It's definitely not the Corporation's
9 preference to have rate changes like that. We would
10 prefer that everybody's rates are as stable as we've
11 seen in -- for the overall indicator. But at the same
12 time, we've committed here to setting rates on an
13 actuarially sound basis, and we have a methodology for
14 determining rate requirements that -- that we utilize.
15 And as of today and recent history, we
16 have those -- vehicles can go up plus or minus 15
17 percent if that's what their hist -- historical results
18 show is required.
19 MR. RAYMOND OAKES: Thank you for that,
20 Mr. Johnston. And we're going to get into the nuts and
21 bolts of your actuarial methodology. Before I do that
22 though, you'll recall early in the hearing your
23 president used the term 'immunizing Manitobans from
24 rate volatility'.
25 Do you recall that, sir?

1 MR. LUKE JOHNSTON: Something to that
2 effect, that's fair, yeah.
3 MR. RAYMOND OAKES: And when you look
4 at CMMG 1-5 on your screen there, do you see that the
5 Corporation certainly failed to immunize the Manitobans
6 that are motorcyclists from any rate volatility?
7 MR. LUKE JOHNSTON: I'll answer your
8 question, then I just -- I'd like to expand a little
9 bit on this. So to your question, clearly it -- it was
10 not a desirable results for motorcyclists or not the
11 Corporation's preference to have significant rate
12 increases on motorcycles. Nobody wants that. But
13 again, talking about our -- the methodology we use here
14 where there's no cross-subsidization, at the time of
15 the application these were the increases required.
16 And a few -- you talk about in here, Mr.
17 Oakes, about we kind of had a bad period where we had a
18 lot of big rate increases, and lately it's been more
19 favourable. A lot of things have changed with -- with
20 motorcycle claims experience over the years. The first
21 big step was moving motorcycles to the PIPP program.
22 And their cro -- their cost profile changed
23 significantly relative to what their current rates
24 were.
25 So we went through a difficult period

1 for motorcyclists where we were trying to get them to
2 their required rate. And this isn't a perfect
3 comparison, but -- and if you look at mopeds when they
4 were paying, like, a hundred dollars and, you know, the
5 -- they started getting more experience, well, 25
6 percent -- 25 per -- like, it -- it takes a while to
7 catch them on.
8 So that's one (1) piece. But in terms
9 of the more recent experience, we've seen -- we've seen
10 a few things. We had the loss transfer hearings and we
11 put in PIPP cost allocation. So that was a benefit for
12 motorcyclists in terms of, in the past, motorcyclists
13 were often more injured and PIPP -- or and claims in
14 general, and they were having to absorb all their PIPP
15 costs. Well, we -- at these hearings, we -- we changed
16 that rule, so it would be split between the two (2)
17 parties, and that brought motorcycle costs down
18 considerably.
19 The other piece is that motorcycle
20 experience has been better in the last -- in -- in
21 recent years. We did some work a while back to start
22 splitting data by body style, charging more equitable
23 rates to, you know, sport bikes versus, you know, more
24 standard bikes. And that seemed to help the
25 experience, as well, so that's another piece.

1 And I'm sure Mr. Oakes is going to
2 discuss this, but the significant adjustment to our
3 PIPP forecast that was made in 2010 also lowered the
4 motorcycle rate indication because motorcycles, 80 --
5 85 percent of their losses are PIPP. So whenever we
6 make a big adjustment to PIPP like that, motorcycles
7 feel it more than any other class.
8 So that's some of the explanation of --
9 as to why the recent experience is better and why the
10 old experience was maybe not so good.
11 MR. RAYMOND OAKES: Thank you for that,
12 Mr. Johnston. I appreciate you are attempting to
13 educate the Board in this area, and we appreciate your
14 comments.
15 Just by ware -- way of clarification
16 though, in the table that you have in front of you,
17 CMMG 1-5, this is all post-no-fault experience, isn't
18 it?
19 MR. LUKE JOHNSTON: Like, this is all
20 experience in the -- the PIPP program. Is that the --
21 MR. RAYMOND OAKES: Yes.
22 MR. LUKE JOHNSTON: Yes.
23 MR. RAYMOND OAKES: Okay. So your
24 first explanation about catch-up doesn't relate to this
25 at all when you have a required rate of one thousand,

1 twelve dollars and nine-six ($1,012.96) cents in
2 2004/'05 and you asked for a 15 percent increase,
3 followed by the increases you see there. That's got
4 nothing to do with catch-up.
5 You're in fact asking for a rate
6 requirement that is much higher than the rate
7 requirement today?
8 MR. LUKE JOHNSTON: That -- that's
9 fair. At that point in time, I wouldn't call that
10 catch-up anymore. It was trying to put motorcycle
11 rates in -- in the historical context, particularly the
12 years -- the decade following PIPP there was definitely
13 a catch-up period that had to occur.
14 At that particular point in time, not
15 having all of the evidence in front of me, but my
16 expectation would be that this would be more driven by
17 the experience that we had in front of us and our
18 expectations at that time.
19 MR. RAYMOND OAKES: Well, Mr. Johnston,
20 you're still saying there's a catch-up period in the
21 decade following 2004/'05, and I'm suggesting --
22 MR. LUKE JOHNSTON: Well before, sorry,
23 bef -- before that. Yeah, '94 to 2003. Like that --
24 maybe not exactly those years, but I'd have to look
25 back to see what indications we had in the early days

of PIPP, and they were likely very uncertain for -- for motorcyclists.

(BRIEF PAUSE)

MR. RAYMOND OAKES: Now, since we're speaking somewhat in a historical perspective, you will recall that the Corporation used to use five (5) years of experience in calculating the motorcycle rates.

Is that correct, sir?

MR. LUKE JOHNSTON: I -- I can't remember how far back this goes, but we've always used ten (10) years in my -- in my time here -- here, twelve (12) years. We've always used ten (10) years of experience for serious losses, and that's for all classes. What we did for motorcyclists or -- the motorcycle class in recent years is to average their PIPP experience, all of it, over ten (10) years with the intent to stabilize the variability in the rates.

And now that it appears we're at a more steady state, if not declining, doing that, I think, would eve -- even more important going forward in terms of, you know, keeping as -- as to your point, keeping the rate changes in a more manageable range, like, let's -- you know, these are longer. It is a variable

1 class, and it's -- it's 85 percent PIPP. And often,
2 we're talking about a few large claims, you know, here
3 or there that can really swing the results. So we
4 thought going ten (10) years would give this group the
5 most rate stability going forward.
6 MR. RAYMOND OAKES: Is it possible, Mr.
7 Johnston -- I've been at this twenty-two (22) years.
8 You've indicated you've been doing actuarial work with
9 the Corporation twelve (12) years, and I think you took
10 over from Mr. Palmer and became a witness in these
11 proceedings about three (3) or four (4) years ago.
12 Is that correct, sir?
13 MR. LUKE JOHNSTON: This is my third
14 year in the front row. Likely, six (6) to eight (8)
15 years in the back row.
16 MR. RAYMOND OAKES: And is it possible
17 that the Corporation used to use five (5) years bef --
18 in the years before these tables?
19 MR. LUKE JOHNSTON: I apologize. Maybe
20 I -- I missed that part of -- in my answer. So serious
21 losses were always ten (10) years. All of the other
22 PIPP experience had previously been five (5).
23 MR. RAYMOND OAKES: Thank you. Now,
24 one (1) of the references in the standard of practice
25 is 2620-'02. It's probably the second page into your

1 materials. And I have a question concerning that. And
2 if you could just scroll down just a little? Thanks.
3 That's great.
4 MR. LUKE JOHNSTON: Sorry, what was the
5 reference there again?
6 MR. RAYMOND OAKES: 2620, and it would
7 be '05, "Change in Circumstances."
8 MR. LUKE JOHNSTON: I have that.
9 MR. RAYMOND OAKES: Okay. Now, when
10 you gave your -- your long explanation previously about
11 all the parts of the puzzle that add up to the
12 motorcycle experience, you talked about how the
13 environment had changed. There was the -- you spoke of
14 the loss attribution rules. And I'd suggest to you
15 that originated in Board Order 97/'05.
16 Do you recall that, sir?
17 MR. LUKE JOHNSTON: I do.
18 MR. RAYMOND OAKES: Okay. And then
19 more recently in 2010, there was Board Order 122/'10.
20 At page 57 of that Board order, the -- the Board at
21 that time enhanced those loss attribution rules to
22 extend it to pedestrians and wildlife.
23 Do you recall that, sir?
24 MR. LUKE JOHNSTON: Yes, I do.
25 MR. RAYMOND OAKES: Okay. And what I'd

1 suggest to you, Mr. Johnston, is that where there's
2 been a significant change in circumstances or
3 environment, would it be proper actuarial practice, and
4 further, make sense, to give more weight to data after
5 that change?
6 MR. LUKE JOHNSTON: In the case of --
7 in the case of the -- let's call it loss transfer or
8 PIPP -- call it -- PIPP cost allocation is what -- how
9 we refer to it internally, all the history was also
10 adjusted to reflect how the new procedure, for lack of
11 a better word, would -- would take effect.
12 So -- so we did actually go back and
13 adjust all the history to reflect the -- the Board
14 order. So in that case, the data is all on the same
15 basis that we're using for -- for rating.
16 MR. RAYMOND OAKES: If we can go back
17 to CMMG 1-5, there's two (2) years of -- I'm going to
18 term it anomalies or outliers that MPI continues to use
19 that costs -- result in the costs for motorcyclists
20 being higher than we say they should be. And I'm
21 referring of course to 2006/'07, 2010/'11. And when we
22 -- it's instructive to look at the loss ratios in that
23 respect.
24 Do you see, sir, in 2006/'07, that the
25 loss ratio is shown as 148.78 percent?

1 MR. LUKE JOHNSTON: Yes, I do.
2 MR. RAYMOND OAKES: Okay. And that's
3 approximately eight (8) years ago.
4 MR. LUKE JOHNSTON: Approximately, yes.
5 MR. RAYMOND OAKES: And then also in
6 2010/'11, we see the loss ratio reached over 100
7 percent, at 105.84 percent.
8 MR. LUKE JOHNSTON: Yes.
9 MR. RAYMOND OAKES: When we look at the
10 experience since 2011, we have some very negligible
11 loss ratios; a low of 40 percent to a high of 62.6
12 percent.
13 Do you see that, sir?
14 MR. LUKE JOHNSTON: Yes, I do.
15 MR. RAYMOND OAKES: Would you agree
16 with me that, looking at the experience that's in front
17 of us right now, that -- that 148.78 percent is an
18 outlier, is an anomaly with respect to that decade?
19 MR. LUKE JOHNSTON: Well, you're --
20 you're essentially getting back to the -- the rationale
21 for using longer-term averages on serious losses. We
22 do this for all classes because we don't -- we want to
23 control the -- the rate shock which you're referencing
24 -- or the outliers, pardon me, that you're -- you're
25 referencing.

1 If you think about -- say we started
2 using three (3) or five (5) years of data as a basis
3 for rating and, by bad luck, motorcycle class happened
4 to have a few major losses in the last year and the
5 loss ratio was 150 percent.
6 I don't think that would be appropriate
7 for us to use three (3) years of data and -- and
8 suddenly say that the motor -- motorcyclists need a --
9 a massive rate increase. Nor do I think I would want
10 to rely on a couple, admittedly very good, years to
11 completely change the motorcycle rate indication and
12 rely exclusively on those two (2) numbers.
13 So we're -- we're -- we have the
14 procedures in place to create rate stability. And at
15 the same time you see that, by some of the rate
16 decreases that are coming in, that the experience is
17 being recognized. If -- if those numbers were 100
18 percent, I don't think we'd be applying for as big of a
19 rate decrease, if any rate decrease at all. So we are
20 gradually recognizing the experience.
21 I agree, at some point in our history
22 that 148 percent loss ratio is going to fall off of the
23 -- out of the data. And I -- I really hope for the
24 motorcycle class that they continue to have that
25 experience and that -- and that number falls out.

1 But essentially, we're getting -- that -
2 - that year is getting one-tenth (1/10) of the weight
3 in the -- the analysis. So nothing else to add, I
4 guess.
5 MR. RAYMOND OAKES: Okay. One (1) of
6 the things you did add is you said the Corporation has
7 procedures in place to create rate stability.
8 Looking at CMMG 1-5, did you not have
9 them previously, or did you just not employ them
10 previously?
11 MR. LUKE JOHNSTON: No, they've been
12 there. It's -- we put the -- these rules in place to
13 try to create stable rate requirements. But if the
14 reality of the experience is indicating a 20 or 30
15 percent rate increase, we also have procedures in place
16 to charge actuarially sound rates with caps in effect,
17 so at the time those rate apps were -- were filed, that
18 was the indicated experience.
19 And like -- and as you mentioned, and --
20 and I mentioned, some things have changed in recent
21 years that make the motorcycle loss ratio more -- more
22 favourable, and those are starting to flow through into
23 rates.
24 MR. RAYMOND OAKES: Part of the
25 discussion earlier, you spoke about unusually large

1 losses. And so if I could direct you to the actuarial
2 Standards of Practice, twenty-six (26) dash -- or
3 twenty-six two zero point zero-nine (2620.09) and it's
4 headed, "Unusual events." Thank you, Diana.
5 It states that an actuary should
6 consider that loss experience may be -- have been
7 subject to catastrophes, large losses, or other unusual
8 events. Large loss capping is a popular procedure in
9 ratemaking, and its purpose is to limit the fluctuation
10 of the indicated rates. However, that's not a
11 procedure that MPI currently uses in their rate-making
12 process.
13 Could a large loss capping procedure
14 have mitigated the year-to-year rate changes,
15 especially given the high loss ratio in the '06/'07
16 accident year?
17 MR. LUKE JOHNSTON: With -- well,
18 whether we cap losses or not, we still have to collect
19 enough revenue to cover the expected loss cost of the
20 entire fleet. Our methodology for -- for dealing with
21 large losses is to smooth them out over a decade.
22 So if -- if a classification, say, had
23 one (1) serious loss worth $1 million in -- over the
24 last decade, that class would essentially be allocated
25 a hundred thousand dollars ($100,000) of losses as the

1 expectation for -- for a single rating year. We think
2 that's appropriate methodology for essentially
3 smoothing those bumps out.
4 If we don't -- if we were to put a
5 capping methodology in place, what would happen is we
6 would calculate rates with the caps in effect, and then
7 obviously we'd have a significant shortfall, because we
8 haven't included all the losses in -- in our rate
9 calculation. We have all these -- these capped amounts
10 that were excluded. You'd then have to find a way to
11 offset somehow to collect all that money from your
12 other ratepayers.
13 So the most global way to do it would be
14 to cap all the losses, and then tell everybody they
15 need to pay some kind of additional amount in their
16 rate to cover, you know, large losses. Rather than do
17 that, we -- we think it's more appropriate just to put
18 it in the rates for each class themself, and smooth it
19 out over a decade. That's -- that's how we choose to
20 do it. And -- and that's also the PUB approved
21 methodology for as long as I can remember.
22 MR. RAYMOND OAKES: If we can just put
23 one dash five (1-5) up on the screen again? And in
24 considering your answer, looking at the increases from
25 19.93 percent one year to the decreases that we

1 presently see the Corporation applying for, you're
2 telling me this the smoothing out over the decade?
3 MR. LUKE JOHNSTON: Again, it's -- I'm
4 not saying it's good that -- or desired that
5 motorcycles got a 15 percent rate increase, and it's --
6 I definitely don't want to show up to CMMG meetings and
7 tell them that that's the case, but this is how we do
8 our -- our methodology.
9 The -- I see the increases sought in
10 this table, but in terms of the rate requirement that
11 you see in the second column next to the years, really,
12 between '04 and '11/'12, that rate requirement was
13 basically around eleven hundred dollars ($1,100).
14 Maybe the first year, sorry, is one thousand dollars
15 ($1,000) but between '05 and '11/'12, it -- basically
16 eleven hundred dollars ($1,100) the whole time.
17 And my thinking is that the significant
18 adjustment to PIPP in 2010 that was made was likely the
19 main driver to drop that -- that rate down to nine
20 hundred and seventeen (917). And the favourable
21 experience in recent years is helping that rate fall
22 even farther.
23 MR. RAYMOND OAKES: So what I'm hearing
24 in the last part of that answer was that the reason
25 that those rates were inflated to eleven hundred

1 dollars ($1,100) instead of the eight seventeen (817)
2 rate requirement today is because the Corporation used
3 the wrong tail factor for all those years and
4 artificially inflated the rate?
5 MR. LUKE JOHNSTON: So, as you know,
6 there -- there was a large release in 2010/'11. It was
7 definitely not the Corporation's intent to collect more
8 money on PIPP than -- than was required. But clearly,
9 when we released $250 million, that -- that was the end
10 result. But remember, we have a undertaking on this,
11 but it's taken us a lot of years to -- to build up
12 experience for the PIPP program.
13 And we -- what led to the $250 million
14 release was essentially us restating our expectations
15 on how long accident victims live in -- in car
16 accidents. And it took us a lot of years to get a
17 stable result for that. We felt we had credibility to
18 do that in -- in 2010/'11, and we did so.
19 And -- one (1) second, please.
20
21 (BRIEF PAUSE)
22
23 MR. LUKE JOHNSTON: I can't recall the
24 exhibit, but...
25

1 (BRIEF PAUSE)

2

3 MR. LUKE JOHNSTON: I'm finding the
4 reference. But we do have an exhibit showing that the
5 -- we collected essentially the equivalent of twelve
6 dollars ($12) a policy more than what ended up being
7 the PIPP costs from 1994 to 2010.
8 MR. RAYMOND OAKES: I recall the
9 exhibit because it was offered as an undertaking even
10 though none was sought. But the twelve (12) bucks is
11 for overall vehicle populations.
12 Isn't that correct?
13 MR. LUKE JOHNSTON: Correct. To be
14 fair, it would -- it would be larger for motorcycles.
15 MR. RAYMOND OAKES: And you're telling
16 me that the Corporation used the wrong tail factor for
17 seventeen (17) years based on that exhibit?
18 MR. LUKE JOHNSTON: It takes a
19 significant amount of time to understand the life
20 expectancies of seriously injured claimants. It's not
21 something you're going to figure out five (5) years
22 into the PIPP program. It's also a very significant
23 adjustment that you better be very sure that you got
24 this right because once you -- you make that change, if
25 it -- if the claimants start living longer or you're

1 wrong, you're going to pay a very significant price
2 when the claims aren't closing as fast as you're
3 anticipating them to.
4 So that's -- at that point in time,
5 that's where we felt that we had enough experience
6 beyond the five (5) to ten (10) year range where we
7 felt our tables that we were using were appropriate.
8 MR. RAYMOND OAKES: And I -- I don't
9 want to fault you personally. It certainly predates
10 your involvement. And, in fact, you were the actuary
11 who blew the whistle on the whole issue. In -- in an
12 email to the external actuary you indicated that you
13 could no longer support that tail factor.
14 Isn't that correct?
15 MR. LUKE JOHNSTON: There were
16 discussions that we -- our experience is becoming more
17 and more credible that it was pretty -- it was to the
18 point where we could no longer rationalize the old life
19 expectancy assumptions that we had. So that -- it was
20 at that point that we decided to make that change.
21 MR. RAYMOND OAKES: And just to
22 reiterate, the use of the incorrect tail factor and
23 enhanced reserves costs motorcyclists much more than
24 private passenger?
25 MR. LUKE JOHNSTON: Without getting too

1 technical, if -- if private passenger vehicles have
2 about 30 percent of their costs on PIPP and motorcycles
3 have 85 percent proportionately, I would -- on an
4 approximate basis, of course, the effect is likely the
5 same in terms of the twelve dollars ($12). It would be
6 -- maybe two and a half (2 1/2) to three (3) times
7 more, if that's -- if that's fair for -- for this
8 forum.
9 MR. RAYMOND OAKES: I appreciate the
10 answer. When there was the $250 million release --
11 when -- that's fine. When there was the $250 million
12 release though, motorcyclists only got the same amount
13 back as private passenger.
14 There -- that was -- that two (2) to
15 three (3) times wasn't taken into account by the
16 Corporation, was it?
17 MR. LUKE JOHNSTON: Everyone got the
18 same rebate, that's true. Motorcyclists got the
19 biggest effect on their rate requirement. So all the
20 historical motorcycle experience would have been
21 adjusted to the new assumptions. And as you can see in
22 the table that you have, it almost immediately resulted
23 in a -- a 10 percent rate decrease which would have
24 taken effect in -- in that year. There -- there was a
25 little bit of a timing lag between when the results are

1 changed and the GRA is filed.
2 MR. RAYMOND OAKES: I want to speak
3 about weighting of years. And we're almost done with
4 CMMG 1-5. But with respect to the recent experience --
5 and I'm looking at everything since 2011/'12 as the
6 recent experience. Actuarial Practice number 1730.11
7 that we've supplied to you states that the pertinent
8 past experience data relates to the recent past rather
9 than the distant past.
10 So the question based on that standard
11 of practice is: Would it not be more appropriate to
12 give greater weight to the three (3) most recent
13 insurance years, particularly given the lower loss
14 ratio in those years?
15 MR. LUKE JOHNSTON: I don't think so.
16 That -- I think that right now that is in the best
17 interest of CMMG, I guess, in terms of getting the
18 lowest rate possible for motorcyclists. But in terms
19 of the long-term stability of -- of motorcycle rates, I
20 don't think it's in our best interest to start using
21 the three (3) year average because the serious losses
22 are going to happen.
23 Like, it's -- it's not that it's -- that
24 it's just going to stop. And that is great news that
25 those last three (3) years have been lower, and that

1 tells me that as a group motorcyclists have generally
2 avoided the serious claim. And we hope that continues.
3 But from a rate stability perspective and a data
4 credibility perspective, we continue to think a long-
5 term average is appropriate. And ten (10) years is
6 what we use right now.
7 MR. RAYMOND OAKES: Mr. Johnston, we're
8 going to ask Diana to put up CMMG Interrogatory 1-12.
9
10 (BRIEF PAUSE)
11
12 MR. RAYMOND OAKES: And it'd be the --
13 it'd be the attached table following that response.
14 And I ask you to look at the actual loss ratios,
15 including the pool loss to the right. You have an
16 average of 74.38 percent for a private passenger.
17 Do you see that, sir?
18 MR. LUKE JOHNSTON: Yes, I do.
19 MR. RAYMOND OAKES: And then looking at
20 the years since 2011, you have 70.25 percent, 77.87
21 percent, 8 -- 84.2 percent.
22 Do you see those, sir, for the last
23 three (3) years?
24 MR. LUKE JOHNSTON: Yes, I do.
25 MR. RAYMOND OAKES: And if we can just

1 go back to CMMG 1-5 and compare the loss experience in
2 those three (3) years for motorcycles. Thank you,
3 Diana. And we see -- starting in 2011, we see 54.98
4 percent; we see 40 percent the following year; we see
5 62.6 percent.
6 We don't see any of the roughly 77
7 percent loss ratios that you have for private passenger
8 the last three (3) years, do we?
9 MR. LUKE JOHNSTON: Yeah. No, you're -
10 - you're correct that loss ratios are different. But
11 the -- as you know, the loss ratio has not -- has gone
12 up in the last couple of years for passenger vehicles
13 as a result of -- largely as a result of collision
14 experience.
15 And we're applying for about a two (2) -
16 - I believe it's two point seven (2.7) for passenger
17 vehicles, and motorcycles are getting negative 6
18 percent, approximately. So in terms of the trend of
19 those two (2) numbers, I think the -- the rate
20 indications are moving in the right direction.
21 MR. RAYMOND OAKES: Well, certainly the
22 Corporation would think that the rate indications are
23 good, especially in 2012/'13, when it has a loss ratio
24 of 40 percent for motorcyclists. And the presumably
25 the -- the rest of it, or a good portion of it, is

gravy to the Corporation.

Is the Corporation still indicating that it's supposed to be providing insurance to motorcyclists on a break-even basis?

MR. LUKE JOHNSTON: Yes, we are. And again, that's -- I think I've explained the rationale for why we -- we believe that longer-term average is in the best interests of the motorcycle pool on a go-forward basis.

MR. RAYMOND OAKES: Okay. Let's talk about a going-forward basis. The rate indication for motorcyclists for 2015/'16, according to the Corporation, would be a 7.3 percent decrease, would it not, sir?

MR. LUKE JOHNSTON: That sounds correct, subject to check.

MR. RAYMOND OAKES: Okay. But that's not what the Corporation is seeking, is it?

(BRIEF PAUSE)

MR. LUKE JOHNSTON: No, and it's not what we're seeking, and that's basically because of the capping rules we have for individual rates in terms of no rate increase can have experienced adjustment more

1 than minus or plus fifteen (15). That -- that was a
2 net result from running a -- the indicated rates
3 through the rate model.
4 MR. RAYMOND OAKES: So we have capping
5 when motorcyclists should be getting a bigger decrease
6 on an individual basis. We don't have any capping when
7 there's an anomaly of a year like '06/'07 on -- on
8 large losses.
9 Can you explain to me how we -- we
10 sustained increases of 15 percent and had the
11 Corporation applying for 19.93 percent, but somehow
12 you're capping the difference between 6.55 percent and
13 7.3 percent when it comes to a decrease in rates?
14 MR. LUKE JOHNSTON: The capping applies
15 in both directions and historically, so I -- I'm going
16 to speculate here. But I believe that the reason that
17 the actual increase approved in -- in your chart here,
18 in some cases the 14 percent relative to nineteen (19)
19 is likely because the same capping rules took effect,
20 except on the opposite direction, in terms of
21 increases.
22 MR. RAYMOND OAKES: Well,
23 directionality would be one (1) thing, but explain to
24 me how the Corporation's okay with motorcyclists
25 getting hammered for a 15 percent increase, but somehow

1 they're not okay when we're entitled to another few
2 points of a percent in a decrease?
3 MR. LUKE JOHNSTON: The capping would
4 just apply to classifications where the decrease is 15
5 percent or more, and again, that's another form of rate
6 stability that we use just to prevent really
7 significant swings in rates in a particular year.
8 Currently, the thresholds for that are
9 the plus or minus 15 percent changes due to experience,
10 so that's not -- that's not some kind of MPI judgment.
11 That is the data indicates that fifteen (15) -- you
12 know, plus or minus more than 15 percent is -- is
13 required, and we're capping at -- at that per our
14 Board-approved methodology.
15 MR. RAYMOND OAKES: Now -- now, Mr.
16 Johnston, I complimented you on that you're a very
17 responsive witness, and I -- I don't want to recant it
18 all. I -- I'm sitting here still puzzled. I can
19 understand if motorcyclists were entitled to a fifteen
20 (15) per -- or a 20 percent rate decrease, and you
21 said, You know what, we don't like to see rates go up
22 and down. We like to see them smooth, to which is the
23 opposite of what I'm looking at here.
24 But in that case, I could understand if
25 you came and say, The required rate is a 20 percent

1 decrease. We're -- we can only give you fifteen (15),
2 because we're trying to smooth the decreases. But here
3 we've got an indicated rate of 7.3 percent decrease,
4 and yet you come forward before this Board for only a
5 6.55 percent.
6 Can you explain that, please?
7 MR. LUKE JOHNSTON: I -- I think I
8 already have. As I discussed, the -- there's
9 procedures in place. Rates are calculated based on
10 historical experience to charge what is required based
11 on that historical experience, and then there's
12 experience-based caps put in place to ensure that rates
13 don't swing by more than plus or minus 15 percent.
14 Those types of swings are -- are rare for the
15 classifications in general.
16 Motorcyclists happen to be a very high
17 volatility class, because you're -- you're -- you might
18 be talking about a hundred injury claims in a year, and
19 if -- if we have a good year, there'll be no serious
20 losses and you'll get a very nice loss ratio, and
21 that's great news. If we don't have a good year and
22 there's one (1) or two (2) serious losses, then you
23 have a higher loss ratio, sometimes over 100 percent.
24 So when you have very unstable data like
25 that, you don't want to give too much weight to a

1 couple data points. You want to try to smooth it out,
2 and get a little bit of stability in your projections.
3 And that's -- that's what we've done. I -- I don't
4 know how else I can describe it than -- than that.
5 MR. REGIS GOSSELIN: Mr. Oakes, I
6 wonder if I -- I don't want to interrupt your line of
7 questioning, but where did you get the seven point
8 three-three (7.33)?
9 MR. RAYMOND OAKES: The witness has
10 already admitted that that's contained in the required
11 rate calculations by the Corporation in the
12 application. I don't have the reference offhand.
13 MR. LUKE JOHNSTON: In -- the easiest
14 place is probably the overview, page 35. So we -- the
15 -- the first step is always to calculate the indicated
16 rate change before any capping or any -- anything
17 occurs in -- in terms of the capping rules that we
18 have, just to show what, you know, what -- what it is.
19 And so on this table, it's -- negative
20 seven point three (7.3) is -- was indicated by
21 actuarial rate setting. Plug it into our rate model,
22 which applies all the -- the rules that we have.
23 Again, this is Board-approved methodology.
24 In this case, it appears that some
25 classifications had indicated decreases in excess of

1 negative fifteen (15), and they were essentially capped
2 at that amount. The -- the capping does occur on other
3 classes as well, but it is very rare to have
4 classifications change by that amount.
5 Again, motorcycles have had some recent
6 changes to their data in terms of some of the changes
7 that have been made, like -- like loss transfer, for
8 example, that have caused some bigger swings recently.
9 But the methodology we have, we -- in -- in our view,
10 is the best for stability going forward.
11 MR. REGIS GOSSELIN: Could you point me
12 to the location where I can see the calculations that
13 were done to get from seven point three-three (7.33)
14 down to six (6) point -- 6 odd percent?
15 MR. LUKE JOHNSTON: I can try to -- to
16 summarize something. And -- and the reason I say,
17 "try," because we would be looking at every single
18 motorcycle, like -- so, like, you know, this rate
19 group, this body style, this territory, and there would
20 be indicated changes. And then it would show how we
21 capped them, and then got less or more revenue than --
22 than required.
23 So I will try to produce an exhibit that
24 shows -- I think, really, all you need to see is which
25 motorcycles got -- got capped at that negative fifteen

1 (15). And then you can see why it's less than the
2 seven point three (7.3). Is that helpful?
3 MR. REGIS GOSSELIN: Yes, it would be.
4 Yes.
5 MR. LUKE JOHNSTON: We could -- so we
6 can do that if that's a formal undertaking, yeah. Do
7 you need me to describe that better?
8 THE COURT REPORTER: Yes, please.
9 MR. LUKE JOHNSTON: Per the table on
10 page 35 of the overview section, MPI will provide a
11 reconciliation of how we -- motorcycles go from an
12 indicated negative seven point three (7.3) to an
13 experience-based change of negative six point six
14 (6.6).
15 Is that okay, Mr. Oakes?
16 MR. RAYMOND OAKES: Yes, Mr. Johnston.
17 Thank you for that. I'm a little relieved, actually,
18 because I thought the answer to Mr. Gosselin's
19 questions was going to be, I can't tell you that
20 without you knowing the secret actuaries handshake, but
21 I'm relieved that that's not the case.
22
23 --- UNDERTAKING NO. 57: MPI to provide a
24 reconciliation of how
25 motorcycles go from an

1 indicated negative seven
2 point three (7.3) to an
3 experience-based change of
4 negative six point six
5 (6.6)
6
7 CONTINUED BY MR. RAYMOND OAKES:
8 MR. RAYMOND OAKES: I'm going to move.
9 I think we've beaten CMMG 1-5 to an early demise. I
10 want to talk about the extra point that you want to
11 take off the motorcyclists to lessen our decrease even
12 further, and that's with respect to the RSR rebuilding.
13 Now, you'll recall when your president
14 testified that we reviewed his quotes in Exhibit 3, the
15 Free Press article, and it pointed to two (2) main
16 contributions to the stress on the RSR, being the
17 severe winters the last couple of years, and then the
18 technological advances and the cost of repair
19 presumably in cars.
20 Do you...?
21 MR. LUKE JOHNSTON: I think the
22 question is: Do I remember that conversation? Yes, I
23 do.
24 MR. RAYMOND OAKES: Okay. And in
25 previous years, yourself and your predecessor, Mr.

1 Palmer, have conceded that hail isn't a big exposure
2 for motorcyclists?
3 MR. LUKE JOHNSTON: Given that that's
4 not covered under the Basic program, I would agree that
5 --
6 MR. RAYMOND OAKES: Okay.
7 MR. LUKE JOHNSTON: -- it doesn't
8 affect the rates very much.
9 MR. RAYMOND OAKES: And, similarly, the
10 severe winters that your president pointed to, that's
11 not a consideration for motorcyclists?
12 MR. LUKE JOHNSTON: Agreed.
13 MR. RAYMOND OAKES: Okay. The cost of
14 repair, we haven't seen riderless technology in
15 motorcycles, not likely to. It kind of -- kind of
16 defeats the purpose of transportation, doesn't it? So
17 again, that's not a consideration?
18
19 (BRIEF PAUSE)
20
21 MR. LUKE JOHNSTON: Can you repeat the
22 last question? I'm pretty sure I agree with you, but -
23 - maybe it's not repeatable.
24 MS. HEATHER REICHERT: Riderless.
25 MR. LUKE JOHNSTON: With autonomous

1 motorcycles and -- and things like that --
2 MR. RAYMOND OAKES: That the -- the
3 cost of repair of the vehicles. There isn't some trend
4 in motorcycles that's contributing to that?
5
6 (BRIEF PAUSE)
7
8 MR. LUKE JOHNSTON: I'm being told that
9 there is -- there are some issues in terms of the
10 complexity of motorcycle repairs, as well. But again,
11 85 percent of motorcycle rates are for PIPP, so it --
12 it's a -- it's a smaller component of the rate. I -- I
13 agree with that. MR. RAYMOND OAKES: And the benefits
14 payable on your PIPP, when they get to -- largers are
15 covered by layers of reinsurance, aren't they, sir?
16 MR. LUKE JOHNSTON: Is the question are
17 more motorcycle -- of motorcycle losses covered by
18 reinsurance?
19 MR. RAYMOND OAKES: Yes. That large
20 losses are covered by layers of reinsurance.
21 MR. LUKE JOHNSTON: Not often -- we --
22 now. We have -- I'd have to check, but we've had a --
23 a $5 million retention for a little while now. So
24 there's only a few -- a few claims historically that
25 have actually gone above that. And in recent years, I

1 -- I don't believe they were motorcycle claims, but I -
2 - I can't -- I can't confirm. We have very minimal
3 number of claims actually go through that 5 million
4 threshold. It's more to protect us from that mega-
5 claim that -- you know, like a bus full of people or
6 something that we're worried about.
7 MR. RAYMOND OAKES: What I'm going to
8 suggest to you, Mr. Johnston, that based on all of
9 those answers the lack of hail exposure in the Basic
10 program, the inapplicability of winter experience, and
11 subject to some general comments you made,
12 technological advances in motorcycles, there's no
13 exposure on those issues to the RSR from the motorcycle
14 experience.
15
16 (BRIEF PAUSE)
17
18 MR. LUKE JOHNSTON: Our -- our policy
19 historically and -- and going forward is to apply
20 rebates and rebuilding fees equally to all classes.
21 Motorcyclists also received all the rebates that we had
22 in -- in the past ten (10) years proportionately to
23 their premium as well. So RSR rebuilding fees can --
24 can be generated from -- for -- for a lot of reasons.
25 In our overview, we talked about collision being over

1 budget by some, I believe close to 30 million.
2 However, there's other factors. Of
3 course, the interest rate decline. Motorcyclists are
4 also the most sensitive to interest rate changes
5 because they're almost all PIPP. So to the extent that
6 we forecast a particular require -- PIPP rate
7 requirement based on a higher interest rate and that
8 doesn't materialize, our -- our motorcycle PIPP
9 projections would be higher or lower than -- than we
10 expected.
11 So I agree with you, Mr. Oakes, that
12 motorcycles did not cause a $30 million in additional
13 winter claims, but there's a lot of other sources of
14 RSR declines that motorcycles are definitely a -- a
15 part of. And we -- we don't know -- or not we don't
16 know. We don't want to change our methodology to start
17 hand-picking who gets RSR fees and who doesn't, and who
18 gets rebates and who doesn't. We believe that the --
19 the more equitable kind of a crossover -- over approach
20 is more publicly acceptable.
21 MR. RAYMOND OAKES: Just chopping that
22 long answer up a little bit, you spoke about the
23 rebates. And I though we previously established that
24 motorcyclists should have been entitled to
25 approximately 2.5 to 3 percent times the amount of

1 rebate per dollar of premium that private passenger
2 received because 80 percent of their premium is PIPP
3 benefits and that's not the case for the private
4 passenger.
5
6 (BRIEF PAUSE)
7
8 MR. LUKE JOHNSTON: I don't recall
9 saying two (2) to three (3) times the rebate, but my
10 comment was around the twelve dollars ($12) per policy
11 overstatement, for lack of a better word. Motorcycles
12 would be a larger percentage of that, so if there was a
13 -- an overstatement it -- it would affect them
14 disproportionately to the two (2) to three (3) times
15 level, as you quoted.
16 MR. RAYMOND OAKES: And that two (2) to
17 three (3) times overstatement of the tail factor then
18 would -- should result in them receiving two (2) or
19 three (3) times -- or a rebate that's a factor of two
20 (2) to three (3) times the dollar-per-dollar rebate
21 given a private passenger?
22 MR. LUKE JOHNSTON: I don't agree with
23 that. There's -- we had the PIPP rebate, we had other
24 rebates related to other gains that we had, such as on
25 equities or favourable results in general. And nothing

else to add on that really.

MR. RAYMOND OAKES: Well, we can leave that alone. I don't think we're in the happy circumstance of receiving any large rebates any time soon.

We ruled out a number of areas where motorcycles don't contribute to stress on the RSR. But you were -- you only identified one (1) circumstance is which there was exposure to the RSR by motorcycles and that was interest rates.

Is that correct?

MR. LUKE JOHNSTON: No, there's -- there's others as well. Anything that's a more general impact, like -- so the performance of our asset portfolio would always be considered a -- you know, on a more general basis overall.

My reference to interest rates is that, clearly when we're talking about all these interest rate impacts on claims, these are impacts on our PIPP costing because it's all on a present-value basis. So that's -- that was the -- the meaning for my comments on that.

Any other impacts, whether it's expenses or other types of things, we'd attribute to the -- to the overall fleet.

1 MR. RAYMOND OAKES: And to be clear,
2 for the 2015 year, the Corporation really doesn't know
3 whether there's any interest rate variability that's
4 going to cause any stress to the RSR?
5 MR. LUKE JOHNSTON: I do know there's
6 going to be interest rate var -- variability. It's
7 just we don't -- yeah, we don't know how our forecasted
8 interest rates will -- will compare to actual. We --
9 we don't -- like, we're using the -- the interest rate
10 methodology that -- that the Board approved, standard
11 methodology.
12 We know we'll get variability from that
13 number. It's not going to work out exactly as
14 forecasted. We're just trying to quantify that
15 information for ourselves and the Board just so we
16 understand kind of the range of outcomes that we could
17 -- could see from that variability.
18 MR. RAYMOND OAKES: Now, I wonder if
19 Diana can find MPI Exhibit 31, which was Undertaking
20 32. I just want to talk about the level of the RSR for
21 a little while. This was used by Mr. Williams earlier
22 this morning.
23 And when we look at the amounts for the
24 RSR, I think we'll have to scroll down a little bit.
25 But I'll just recap the information that's contained in

1 this response. And it indicated in 1996 the RSR was
2 approximately $5 million.
3 Is that correct, sir?
4 MR. LUKE JOHNSTON: Correct.
5 MR. RAYMOND OAKES: In '97, it was in
6 the hole by about 50 million.
7 MR. LUKE JOHNSTON: Correct.
8 MR. RAYMOND OAKES: And in the
9 following year, it started out being 25 million in the
10 hole, twenty-four four one five (24.415), to be exact,
11 and wound up being fourteen million, one hundred and
12 thirty-seven dollars ($14,000,137).
13 Is that correct, sir?
14 MR. LUKE JOHNSTON: Yes.
15 MR. RAYMOND OAKES: In each of those
16 years, MPI functioned as an insurer in Manitoba and
17 provided insurance to the Manitobans that qualified for
18 it.
19 Is that correct, sir?
20 MR. LUKE JOHNSTON: Well, we definitely
21 -- we functioned. We're still -- we're -- we're still
22 here today. But I wouldn't describe this period as
23 desirable in any way. A lot of significant rate
24 increases flowing through here at this time, and this
25 is not something that we want to repeat if that's -- I

1 -- I mean, functioning.
2 Like, we're always going to -- you know,
3 we're going to function with whatever circumstances are
4 put -- you know, that we're dealing with, but this is
5 not preventing -- you know, for the -- for the purposes
6 of the RSR, I don't see this as desirable at all.
7 MR. RAYMOND OAKES: Well, sir, I didn't
8 ask you whether it was desirable. I think you started
9 to -- made the comment that we'll -- MPI will always
10 function. Did I hear you, sir?
11 MR. LUKE JOHNSTON: Faced with any kind
12 of adverse event, we still, of course, have to attempt
13 to function to the best of our abilities. We'll --
14 we'll do whatever we can to mitigate events and deal
15 with them, but functioning is -- is -- it's...
16 MR. RAYMOND OAKES: If you like, I can
17 ask it a different way. In these three (3) years that
18 we just looked at, did the Corporation carry out its
19 mandate?
20
21 (BRIEF PAUSE)
22
23 MR. DAN GUIMOND: Maybe I'll answer
24 that one. In terms of -- our mandate is to provide
25 rate predictability and stability to Manitobans, which

1 means that a person who's on monthly payment who keeps
2 the car, that next year's rate will be approximately
3 the same.
4 MR. RAYMOND OAKES: Well, Mr. Guimond,
5 welcome back, and thank you for entering the fray. I
6 appreciate that. And I wish we would have had those
7 assurances in the years we looked at in CMMG 1-5 when
8 the motorcyclists were getting rates sought by the
9 Corporation with increases of nineteen (19) and change
10 percent.
11 With respect to the -- the years that
12 we're just examining in this particular exhibit, can
13 you tell me what the Public Utility Board's target RSR
14 would have been at -- in 1998, or in that period?
15
16 (BRIEF PAUSE)
17
18 MR. LUKE JOHNSTON: Sorry. The -- per
19 the -- the bullets, the target was 15 percent of
20 written premiums. I'd have to check what the -- the
21 premiums were at that time. They'd be a lot lower than
22 they are today, but that -- that was the target. That
23 -- that's similar to the -- the -- not similar, very --
24 essentially, we're --
25 MS. HEATHER REICHERT: Midpoint.

1 MR. LUKE JOHNSTON: -- yeah, the
2 midpoint of the percentage of premium method that we're
3 using today.
4 MR. RAYMOND OAKES: I wonder if you
5 could, whether you could provide a table, and there may
6 be a table that is similar, but a table that shows the
7 Board's target for the RSR, MPI's target for the RSR,
8 and the actual amount of the RSR for the last ten (10)
9 years?
10 MR. LUKE JOHNSTON: We can do that. I
11 suspect we actually have it somewhere in the
12 application, but we'll -- we'll find it.
13 MR. RAYMOND OAKES: Thank you, sir.
14 MR. LUKE JOHNSTON: And if not, we'll
15 undertake to do it.
16
17 --- UNDERTAKING NO. 58: MPI to provide a table that
18 shows the Board's target
19 for the RSR, MPI's target
20 for the RSR, and the actual
21 amount of the RSR for the
22 last ten (10) years
23
24 CONTINUED BY MR. RAYMOND OAKES:
25 MR. RAYMOND OAKES: And I'm going to be

1 moving topics. I think that the cross-examination will
2 use most of the time before the arrival of Dr. Simpson,
3 and I'm heartened by Mr. Guimond's return to the fray.
4 I'm -- want to speak about the issue of road safety.
5 And it may be me, but I didn't
6 understand your comments, Mr. Guimond, about the -- why
7 anything changes when road safety changes name -- the -
8 - its name to loss avoidance, and becomes part of that
9 part of the Corporation's program delivery. Can you
10 explain that to me?
11 MR. DAN GUIMOND: To the -- the best of
12 my understanding, the regulator is trying to find out
13 if the road safety budget is optimized, and we have not
14 been able to demonstrate that to the regulator. A lot
15 of the things that we do under road safety is -- has to
16 do with intangibles in the -- in the sense that you
17 can't really prove that advertising on texting and
18 driving or buckle up or things of that nature, that you
19 can really relate it to frequency -- reduction in
20 frequency and severity.
21 But I think if we were to -- what I'm
22 proposing -- what the Corporation is proposing is, if
23 we were to put -- report on -- on the Basic loss
24 prevention as a portfolio, a portfolio of different
25 budgets that does different things, and then you can

1 correlate the advertising maybe that you make towards
2 certain projects.
3 For example, if we target the high
4 school driver ed program, for example, and we were to
5 do a -- an effort on collision avoidance, telematics
6 and so on, and then also provide advertising under road
7 safety or advertising campaign, combine that with text
8 and driving and so on, and at the end of the day you
9 can show, Well, I've spent so much money and for that
10 funding envelope, I can demonstrate a return on
11 investment, then at least the regulator would be able
12 to say, Okay, at least at the portfolio level, I know
13 that -- that you're getting a -- a return on investment
14 and you're -- you can defend the expenditure, even
15 though maybe -- maybe at a particular line item on
16 advertising you can't really for sure say, I've saved
17 money.
18 It's a little bit like when we buy the -
19 - the flashing lights for the kids on -- for Halloween.
20 Did we prevent two (2) kids from dying that night?
21 We'll never be able to prove that. We -- we don't
22 know. It's an intangible.
23 But when you start to look at it at the
24 portfolio level and how you link everything together,
25 at least you know that, for that amount of money in its

1 entirety, we have a return on investment that's
2 satisfactory.
3 MR. RAYMOND OAKES: Thank you for that,
4 sir. I want to go from that general statement -- and I
5 appreciate that answer. And these questions may be
6 directed at someone who has the more line-specific
7 program knowledge that you alluded to, and it's CMMG 1-
8 9. I want to ask about the hot mapping of -- of
9 accident areas.
10 We were a little surprised when the
11 Corporation wasn't utilizing this hot mapping. And we
12 brought it to the Board's attention, asked questions
13 about it. Now I guess we're a little disappointed that
14 there hasn't been any use of this tool, or that the use
15 of it didn't demonstrate any discernible patterns that
16 would help the Corporation.
17 Can someone speak to how much effort was
18 put into utilizing the hot mapping results that were
19 provided?
20
21 (BRIEF PAUSE)
22
23 MR. LUKE JOHNSTON: I can speak to it
24 in terms of a forecasting rating perspective.
25 Motorcycles are a lower frequency, high severity type

1 classification. We've likely given evidence in this
2 hearing before that the actual motorcycle crash rate is
3 lower than passenger vehicles, but the accidents are
4 more severe.
5 So often, we're talking about just a
6 handful of bad motorcycle claims contributing to a lot
7 of the losses. And then, I believe, we're maybe two
8 hundred and fifty (250), three hundred (300) motorcycle
9 collisions in a year, right? And so we can -- you can
10 imagine how sparse those counts would be spread out
11 over the whole Province of Manitoba. It's not like the
12 hundred thousand (100,000) plus we might get on the
13 passenger vehicle side.
14 So that's -- in terms of hot mapping,
15 that would be -- that would be my main issue with using
16 that for motorcycles, that the credibility of the data
17 would be extremely low for making road safety
18 decisions.
19 MR. RAYMOND OAKES: Now, Mr. Johnston,
20 I appreciate you answering the question, but I think
21 you answered it more from the actuarial standpoint. Is
22 there someone in the room today who's responsible for
23 road safety and has intimate knowledge of the workings
24 of that department?
25 MR. DAN GUIMOND: I just -- I just want

1 to clarify your question in terms of road safety. I --
2 I guess you're asking are there things that we are
3 aware that maybe would help motorcyclists to maybe keep
4 the loss -- positive loss ratios that we're seeing in
5 the last three (3) years and maybe even reduce those
6 loss ratios.
7 Is that what you're getting at from a
8 program perspective?
9 MR. RAYMOND OAKES: No. Specifically,
10 I'm looking each year for new initiatives of MPI, use
11 of existing initiatives, things like the hot mapping,
12 the number of specific questions about the
13 Corporation's use of it. There would be other
14 questions about the people in -- in that department
15 that do research, if they do any, with respect to
16 motorcycle safety initiatives. There'd be questions
17 about the initiatives developed for wildlife collision
18 reduction.
19 I'm asking whether there's somebody with
20 intimate program knowledge with respect to the
21 Corporation's efforts in those areas.
22 MR. DAN GUIMOND: We do have somebody
23 that works in road safety. And I -- I can tell you
24 that, for example, we're sharing information with SGI
25 on the telematics on the motorcycles that they did

1 recently. Because they -- they too have to resolve an
2 -- an issue regarding the motorcycle rates and -- and
3 the rate lines and so on. So we are sharing that
4 information.
5 We have also had a meeting a few years
6 ago which I found very interesting in terms of if -- if
7 we want to get serious about maybe lowering the loss
8 ratio on motorcycles. There are things, for example,
9 when people get their driver licence for their
10 motorcycle, should there be a limit on the size of the
11 bike in terms of what should they be driving for the
12 first few years based on -- on the -- even the size of
13 the individual.
14 A lot of issues is to be able to keep
15 control of the bike. Not -- not to -- even the
16 telematics that SGI did, a lot of it has to do with
17 just being able to control the bike in different
18 curves, for example, when they -- they go around and so
19 on.
20 So we are looking at these things.
21 There is a fine line, though, when as a corporation you
22 know maybe what you could do to help people out not to
23 get into trouble, but at the same time, there's --
24 there's the rights of the people.
25 Like, if they get their licence, then

they want to get themselves a -- a bike that's very, very powerful, should -- should people say, No, you can't -- you're not allowed to buy a bigger bike. I mean, for -- for the experience you have you shouldn't go over so many CCs. And then, of course, if they start with a small bike, then after they have the experience they'd have to sell the bike and buy another one. And so now they're incurring expenses and so on.

So I think we're going to be working with the CMMG and really going over those discussions that we had a few years and -- and look at what we can really do to help with managing the -- the loss ratio, just in the same way that I talked about taxis a little bit.

MR. RAYMOND OAKES: I appreciate your comments again, Mr. Guimond. And I suggest to you that they're at a high level and what I'm hearing is there isn't somebody here today from road safety that can tell us about the work that's being done in wildlife collision reduction or specific programs like.

Is that correct?

MR. DAN GUIMOND: Not here, but they will -- we will be sending somebody at the annual general meeting of the CMMG.

MR. RAYMOND OAKES: Oh, okay. But not

1 -- not in the context of the Public Utility Board's
2 inquiry?
3 MR. DAN GUIMOND: No.
4 MR. RAYMOND OAKES: That being the
5 case, I'm not going to ask the road safety questions.
6 I want to -- this will be the last area of inquiry, and
7 then perhaps the Board can have a break before Dr.
8 Simpson arrives. But you recall at the commencement of
9 the hearings that Mr. Doug Houghton, who is present in
10 the room today, had provided a presentation.
11 Do you recall that presentation, Mr.
12 Johnston?
13 MR. LUKE JOHNSTON: I -- I was not here
14 at that time, so I don't recall it. But I'm familiar
15 with what was discussed.
16 MR. RAYMOND OAKES: Okay. And some of
17 the points that Mr. Houghton looked at was comparing
18 rates between different vehicles and -- and escalating
19 premiums in PIPP insurance.
20 Would you agree with that, sir?
21 MR. LUKE JOHNSTON: Yes.
22 MR. RAYMOND OAKES: And Mr. Houghton
23 puts forward some other methodologies for assigning
24 PIPP costs, including a flat rate for PIPP.
25 Do you recall that, sir?

1 MR. LUKE JOHNSTON: I do.
2 MR. RAYMOND OAKES: Okay. And is it
3 fair to characterize Mr. Houghton's work that was
4 contained in his presentation as reasonable and an
5 accurate -- accurate presentation of facts?
6 MR. LUKE JOHNSTON: Sorry, I was
7 talking there. Was the question whether I thought Mr.
8 Houghton's presentation was reasonable and factual?
9 MR. RAYMOND OAKES: Yes.
10 MR. LUKE JOHNSTON: Yeah. No, I have -
11 - I've worked -- not worked, but I've -- I've met with
12 Mr. Houghton and CMMG for a number of years now. And
13 over the years, we've both educated ourselves quite a
14 bit in terms of my understanding of motorcycles and Mr.
15 Houghton's understanding of how MPI sets rates.
16 So, yes, I definitely have a lot of
17 respect for Mr. Houghton, and he -- he definitely
18 understands how rates are set at MPI and some of the
19 things that he could do to perhaps improve the rates
20 for motorcycles. So I -- while I may not agree with
21 everything that he proposes, I -- I agree that it's
22 reasonable from their perspective.
23 MR. RAYMOND OAKES: So in terms of your
24 disagreement, would you agree with me that I'd
25 characterize those as philosophical differences with

1 respect to the appropriateness of some of these program
2 changes?
3 MR. LUKE JOHNSTON: Philosophical is
4 probably okay. There's -- some of them are bigger
5 policy decisions when you talk about putting PIPP on a
6 driver's licence or something like that. The rating
7 impacts alone would be very significant, and it would
8 be a complete shift in how rates are set in -- in the
9 province.
10 So while I understand the -- the idea --
11 I don't have an issue with that -- moving to such an
12 approach would be a significant change and involve a
13 lot of other decisions. And the Corporation's not
14 proposing doing anything like that right now.
15 MR. RAYMOND OAKES: And I think you
16 understand, Mr. Johnston, that his proposals are coming
17 from equity or fairness basis because of the 33.7
18 percent of drivers that don't have a vehicle registered
19 in their name, which equates to some two hundred and
20 eighty-one thousand, two hundred and nine-three
21 (281,293) drivers.
22 Can you generally, subject to check,
23 confirm that?
24 MR. LUKE JOHNSTON: There might have
25 been two (2) questions in there. I can confirm the --

1 the driver counts, not -- we have I believe an
2 undertaking on that. About a third of the drivers
3 don't insure a vehicle.
4 I did talk a little bit about that, that
5 there's -- there's kind of this household concept as
6 well that occurs where it's -- there's really no need
7 for each person to insure their own vehicle if one (1)
8 person insures all of them.
9 But -- I don't know if I -- maybe you
10 can repeat the first part of your question. I don't
11 think I answered it.
12 MR. RAYMOND OAKES: That his approach
13 was based on equity and fairness in that 33.7 percent
14 of drivers, which is two hundred and eighty-one
15 thousand two ninety-three (281,293) drivers, don't have
16 a vehicle in their name and therefore don't pay
17 insurance premiums.
18 MR. LUKE JOHNSTON: Yeah, I understand
19 the concept. Again, it's -- you have to look at the
20 household as well as -- as saying that one (1) spouse
21 doesn't pay insurance because the other person happens
22 to ensure all the vehicles. I don't know if that's
23 accurate.
24 And then we do -- we do collect some
25 premium from drivers, particularly from demerit

drivers, when their experience is very poor. We collect up to twenty-five hundred dollars ($2,500) additional for higher-risk drivers.

MR. RAYMOND OAKES: Right. In addition to those drivers that don't pay insurance by virtue of having a vehicle in their name, there's also heavy trucks that don't contribute to PIPP that are available to receive those benefits.

Is that correct, sir?

MR. LUKE JOHNSTON: Correct.

MR. RAYMOND OAKES: And then also he points to other issues of fairness, such as the fact that he might have a motorcycle insured but likely also a second or a third vehicle, and only be driving one (1) at one (1) time.

Do you understand that issue as well, sir?

MR. LUKE JOHNSTON: Yes, I do. And I think just as a general philosophy I believe Mr. Houghton's position is that -- just to move PIPP to a licence-based charge as opposed to the way -- as opposed to tracking it on a vehicle basis like we do today. That's -- if that's fair. That's -- that's my understanding.

MR. RAYMOND OAKES: Madam Chairperson,

that concludes the cross-examination I have at this time. Thank you.

THE CHAIRPERSON: Thank you very much, Mr. Oakes. We can take I guess a break until Mr. -- Mr. Simpson, I was going to say something else, anyway, yes, until Mr. Simpson arrives. Thank you.

--- Upon recessing at 2:50 p.m.

--- Upon resuming at 3:18 p.m.

THE CHAIRPERSON: All right. Welcome back. Now I'd like to call upon Mr. Williams of CAC to induce -- introduce his witness, Dr. Wayne Simpson, and then begin your direct.

MR. BYRON WILLIAMS: Yes, Madam Chair, I'd -- I'd ask that the Board secretary have Mr. -- excuse me, Dr. Simpson sworn, please.

CAC (MANITOBA) PANEL:

WAYNE SIMPSON, Sworn

EXAMINATION-IN-CHIEF BY MR. BYRON WILLIAMS (Qual.):

MR. BYRON WILLIAMS: Good afternoon, Dr. Simpson.

DR. WAYNE SIMPSON: Good afternoon.

1 MR. BYRON WILLIAMS: And before we
2 start with your qualifications, I wonder if you can
3 define for me first of all what you mean by the term
4 'applied microeconomics.'
5 DR. WAYNE SIMPSON: Well, applied eco -
6 - microeconomics is -- is actually a steadily growing
7 field within economics which applies to the study of --
8 of individual -- what we call economic agents. That is
9 to say, firms, and households, and other people who
10 participate in the market; governments and so on, and
11 so forth. And applies it to the analysis of data, and
12 the development of policy prescriptions and proposals.
13 MR. BYRON WILLIAMS: And what, if any,
14 ramifications does applied econo -- econometrics have
15 for subject matters such as risk management and -- and
16 investment strategies?
17 DR. WAYNE SIMPSON: Well, applied
18 econometrics involves the analysis of -- of economic
19 data, and the behaviour of agents involves behaviour
20 under risk. And therefore the analysis of individual
21 behaviour involves the behave -- the study of models
22 which use that risk to predict behaviour in tests to
23 see whether in fact those predictions hold. And that
24 uses applied econometrics.
25 MR. BYRON WILLIAMS: Okay. Thank you.

1 Dr. Simpson, you have a PhD from the London School of
2 Economics?
3 DR. WAYNE SIMPSON: Right.
4 MR. BYRON WILLIAMS: And you've been a
5 full professor at the Department of Economics at the
6 University of Manitoba, where you've taught since 1979.
7 Is -- is that correct, sir?
8 DR. WAYNE SIMPSON: Yes.
9 MR. BYRON WILLIAMS: And would it be
10 accurate to characterize your area of academic
11 expertise as including labour economics, applied
12 econometrics, applied microeconomics, and economic and
13 social policy analysis?
14 DR. WAYNE SIMPSON: Yes. That's what I
15 usually characterize as my principle areas of interest,
16 in terms of research and teaching.
17 MR. BYRON WILLIAMS: And, Dr. Simpson,
18 you have either authored or coauthored three (3) books
19 and more than fifty (50) peer-reviewed articles on
20 these and related topics?
21 DR. WAYNE SIMPSON: Yes.
22 MR. BYRON WILLIAMS: And you have done
23 at least a couple of papers on the impact of risk on
24 the behaviour of -- of the firm?
25 DR. WAYNE SIMPSON: Yes, I have.

1 MR. BYRON WILLIAMS: And, sir,
2 currently you serve in the editorial board of Canadian
3 Public Policy.
4 Is that correct?
5 DR. WAYNE SIMPSON: That's correct.
6 MR. BYRON WILLIAMS: And would it be
7 fair to describe that organization as Canada's foremost
8 peer-reviewed academic journal for economic and social
9 policy?
10 DR. WAYNE SIMPSON: Yes, correct.
11 MR. BYRON WILLIAMS: And you serve on
12 the econo -- the executive council of the Canadian
13 Economics Association?
14 DR. WAYNE SIMPSON: Yes, that's true,
15 too.
16 MR. BYRON WILLIAMS: And perhaps you
17 can just tell us a little bit about the McCracken award
18 that you were a co-winner of in 2014?
19 DR. WAYNE SIMPSON: Yes, this was
20 awarded -- this is awarded annually for -- in
21 recognition of contributions for the development and
22 analysis of economic statistics. And Derek Hum and I
23 and Professor Forger, at the Health Sciences Campus,
24 were awarded this for work essentially related to the
25 Manitoba Basic annual income experiment and the

1 development of longitudinal data for that, and the
2 analysis of that data.
3 MR. BYRON WILLIAMS: And who presents
4 the McCracken award?
5 DR. WAYNE SIMPSON: That's presented by
6 the Canadian Economics Association.
7 MR. BYRON WILLIAMS: Dr. Simpson, in
8 addition to your academic career, would it be correct
9 to suggest you have worked at the Bank of Canada, the
10 Federal Department of Labour, and the Economic Council
11 of Canada?
12 DR. WAYNE SIMPSON: Yes. And, in fact,
13 I worked at the Economic Council of Canada during the
14 period when they instituted wage and price controls and
15 monitoring in the late '70s.
16 MR. BYRON WILLIAMS: And your work
17 there was at the Centre for the Study of Inflation and
18 Productivity. Is that right?
19 DR. WAYNE SIMPSON: That's correct,
20 yes.
21 MR. BYRON WILLIAMS: And would it also
22 be accurate to say that you have also served as a
23 consultant in the private sector and to government pri
24 -- primarily in the area of labour, economics, and
25 policy evaluation?

1 DR. WAYNE SIMPSON: I have, yes.
2 MR. BYRON WILLIAMS: And in recent
3 years, Dr. Simpson, amongst your non-academic
4 assignments, you have served as an expert advisor to
5 Prairie Research Associates, Human Resources and
6 Skilled Development Canada, as well as to CAC
7 (Manitoba) through the Public Interest Law Centre?
8 DR. WAYNE SIMPSON: Yes.
9 MR. BYRON WILLIAMS: And in terms of
10 your evidence before the Public Utilities Board, Dr.
11 Simpson, you testified on statistical issues relating
12 to the payday lending industry in 2007.
13 Is that correct?
14 DR. WAYNE SIMPSON: I did.
15 MR. BYRON WILLIAMS: And you provided
16 to the Public Utilities Board on payday lending issues
17 indeed last year, in 2013?
18 DR. WAYNE SIMPSON: That's right, at
19 the review time.
20 MR. BYRON WILLIAMS: And you have
21 appeared with regard to Manitoba Public Insurance as an
22 expert witness during the 2007, 2010, and 2013 hearings
23 on the subject of the Rate Stabilization Reserve and in
24 -- and as well as on subjects such as investment
25 strategy?

1 DR. WAYNE SIMPSON: Yes.
2 MR. BYRON WILLIAMS: And you appeared
3 in the 2014 Need For And Alternatives To review of
4 Manitoba Hydro's Preferred Development Plan?
5 DR. WAYNE SIMPSON: Yes.
6 MR. BYRON WILLIAMS: And in the MPI
7 proceedings and in the Hydro NFAT, were you qualified
8 as an expert in applied microeconomics and applied
9 econometrics?
10 DR. WAYNE SIMPSON: Yes.
11 MR. BYRON WILLIAMS: And, sir, you also
12 played a role during the 2011/'12 Manitoba Hydro
13 general rate application when the risk analysis of Drs.
14 Kabursi and Magee was presented, is that correct, as an
15 advisor?
16 DR. WAYNE SIMPSON: Yes, I did.
17 MR. BYRON WILLIAMS: And for the pur --
18 as it relates to this hearing, sir, how would you des -
19 - would you describe your professional expertise -- how
20 would you describe your professional expertise as it
21 relates to this hearing?
22 DR. WAYNE SIMPSON: I come at this from
23 the perspective of a person who does applied
24 microeconomics and applied econometrics and who has
25 studied questions related to risk and investment

1 strategy and had some practical experience in previous
2 MPI rate applications.
3
4 SUBMISSIONS BY MR. BYRON WILLIAMS (Qual.)
5 MR. BYRON WILLIAMS: Thank you, Dr.
6 Simpson. I'd ask that Dr. Simpson be qualified as an
7 expert in applied microeconomics and in applied
8 econometrics. And obviously, it's open to others to
9 comment, but that's certainly the qualifications we'd
10 seek to have him qualified for.
11 MS. CANDACE GRAMMOND: I have no
12 comments on behalf of the advisors. MPI may have some
13 comments though.
14 MS. KATHY KALINOWSKY: We have no
15 concerns with him being qualified as an expert in those
16 two (2) areas of economics.
17 MR. BYRON WILLIAMS: And, Madam Chair,
18 just for a couple of housekeeping matters, an updated
19 curriculum vitae of Dr. Simpson has been distributed,
20 and we'd suggest it be marked as CAC Exhibit 17.
21
22 --- EXHIBIT NO. CAC-17: Curriculum vitae of Dr.
23 Wayne Simpson
24
25 MR. BYRON WILLIAMS: And a -- he -- Dr.

1 Simpson will be presenting a PowerPoint this afternoon,
2 which we've distributed and -- and would ask that it be
3 marked as CAC Exhibit 18.
4
5 --- EXHIBIT NO. CAC-18: PowerPoint presentation of
6 Dr. Wayne Simpson
7
8 MR. BYRON WILLIAMS: And I note that --
9 my understanding is that Dr. Simpson discovered a
10 couple of typographical eras -- errors, so the
11 PowerPoint that appears is -- is consistent in
12 substance, but there may be a -- hopefully two (2) less
13 typographical errors than might have been in the
14 original version that was distributed.
15
16 RULING (Qual.):
17 THE CHAIRPERSON: Thank you, Mr.
18 Williams.
19 MR. BYRON WILLIAMS: Dr. Simpson, would
20 you like to take us through your PowerPoint? I -- I
21 may interrupt from time to time.
22
23 EXAMINATION-IN-CHIEF BY MR. BYRON WILLIAMS:
24 DR. WAYNE SIMPSON: Thank you. So this
25 is based on the report, and it doesn't deviate a great

1 deal from the report. It elaborates at certain points
2 and -- and adds a few different pieces to the -- to the
3 same -- in the same vein. I start with the notion that
4 the purpose of the Rate Stabilization Reserve is not in
5 dispute. That is to say, based on the most recent
6 Board order, and this is cited in the DCAT:
7 "The stated purpose is to protect
8 motorists from rate increases made
9 necessary by unexpected events and
10 losses arising from non-recurring
11 events or factors."
12 The question, really, is how we
13 establish and maintain a Rate Stabilization Reserve
14 that will actually achieve this objective. And I start
15 by looking at where we are, which is the -- using the
16 percentage of premium, the POP, as I call it. You've
17 seen that somewhere in the references. Or the Kopstein
18 approach from 1989, which advocated and has been used
19 since, a range for the RSR, and I've highlighted the
20 word 'range' because I'm going to come back to that, of
21 10 to 20 percent of annual premiums, which indexes the
22 'R' -- the Rate Stabilization Reserve to business
23 growth.
24 And this is valuable, because a lot of
25 things we do, we set numbers and we don't index them to

1 things that they -- they should be indexed to. So one
2 (1) advantage of using annual premiums is that as the
3 business grows, the RSR range grows commensurably.
4 And, therefore, the volatility that grows with it is
5 also taken care of. That said, it does not connect the
6 RSR directly to the risks that are facing MPI.
7 It is, however, what I call a simple,
8 transparent, and stable method that has survived a
9 series of alternatives which I've become familiar with
10 through my previous testimony before the Public
11 Utilities Board on the MPI rate applications, the
12 RA/VaR, the MCT, and the DCAT at five (5) year
13 intervals. And we get to this year, 2015, the rate
14 application where we have the percentage of premium
15 range projected to be 83 million to 166 million. And
16 through the DCAT report of 2014, MPI are proposing an
17 RSR target of 194 million based on that report.
18 Oops. So in terms of issues, I have two
19 (2). One (1) is the -- the question of the target as
20 opposed to a range. The target that appears in the
21 DCAT as opposed to a range that is the percentage of
22 premiums approach that is currently used. And then
23 secondly, the manner in which the DCAT scenarios are
24 constructed.
25 And here I divide this up into three (3)

1 parts. One (1), the base scenario. Secondly, the less
2 adverse scenarios, the equity decline and high loss
3 ratio scenarios. Less adverse in the sense that they
4 don't lead the DCAT report to conclude that there are -
5 - is a need to rebuild the RSR given existing resources
6 and the existing range. And then the more adverse
7 scenarios, the interest rate decline, and combined
8 scenarios where they reach the conclusion that the RSR
9 is inadequate.
10 And I -- I guess my comments on the base
11 scenario and the less adverse scenarios will be
12 relatively brief in the sense that I don't think these
13 are the most serious concerns, and I'll have a little
14 more to say about the more -- the more adverse
15 scenarios.
16 So issue 1, the RSR target versus the
17 range. And as I said, the percentage of premiums
18 approach specifies a range based on annual premiums
19 estimated to be 83 to 166 million, a minimum of 83
20 million, a maximum of 166 million, with the idea that
21 the Rate Stabilization Reserves should be allowed to
22 fluctuate within this range, and that in fact there
23 shouldn't be any sort of alarm in terms of rebates
24 unless we get above 166 million and surcharges to -- if
25 we get below 83 million to rebuild the RSR.

1 The DCAT report, on the other hand,
2 recommends a target, or what is at least once in the
3 report referred to as a target minimum, of 194 million.
4 And as an addendum, I should add that there is the
5 accompanying report, very brief, which recommends an
6 RSR -- 'upper level' is the term used, maximum -- of
7 325 million based on 100 percent Minimum Capital Test,
8 MCT.
9 And this range is about double the
10 range, a little more than double at the minimum, a
11 little less than double at the maximum, of the range
12 proposed by the percentage of premiums approach.
13 So first what I want to do is make a
14 fairly -- what seems like a fairly straightforward
15 argument that, in terms of rate stabilization, what we
16 want to think of is -- is a range rather than a target.
17 I don't want to belabour this point, but the simple
18 examples I took in my report were to say, Let's
19 consider an RSR target of 200 million. The numbers are
20 strictly illustrative, but the 200 million kind of
21 rounds off the 194 million in the DCAT report.
22 And for that RSR target, rates were
23 adjusted to achieve the target each year. So that was
24 what you might call a -- a hard target. If you're off
25 it, you're concerned and you -- you adjust your -- your

1 actions.

2 Then the second one is an RSR target of

3 zero with rates adjusted to offset any losses or rebate

4 any gains each year. So these two (2) RSR targets have

5 the same sorts of hard objectives. One is 200 million

6 and the other is zero.

7 And then, third, a range which I've

8 taken to be 100 million on either side of the 200

9 million, a range of 100 to 300 million, with rates only

10 adjusted to keep the RSR within this range.

11 So which of the RSR strategies achieves

12 the most rate stabilization? Well, I don't think it's

13 surprising to say that that is going to be the -- the

14 third. The first two (2) strategies essentially lead

15 to the same type of response to losses or gains that

16 arise from these non-occurring events or factors.

17 That is to say, rebates to motorists

18 when favourable events read to -- lead to retained

19 earnings above the RSR target, and then rate increases

20 or surcharges or rate rebuilding fees, whatever you

21 want to call, RSR rebuilding fees, when unfavourable

22 events lead to earnings below the target.

23 So there's really no more stability from

24 a $200 million RSR target than there is from an RSR

25 target of zero and no RSR at all. This is intended to

1 starkly make the point that the intention of the RSR is
2 rate stabilization. And to do that, it needs to have
3 some -- some parameters to it that allow that to occur.
4 The difference, of course, is that, in
5 the case of the $200 million RSR, the money is with MPI
6 instead of with motorists who therefore can't use this
7 to execute their consumption and investment plans in
8 the province.
9 Well, that leads us to the third
10 strategy. The third strategy is this RSR range from
11 100 to 300 million, and this leads us to some rate
12 stabilization. That is to say, if the range is at the
13 lower end, 100 to 200 million, there are no increases
14 or surcharges in that range. There's no rebuilding of
15 the RSR. And from 200 to 300 million, there are no
16 date -- rate decreases or rebates in that range. So we
17 have a region of -- of stability where no actions are
18 deemed necessary.
19 Now, that said, of course, there is not
20 a strict advocacy that there has to be an immediate
21 response to rebuild the RSR. And in fact, in the DCAT
22 report, there's a discussion of an RSR rebuilding fee
23 of 1 percent over the course of four (4) years. But I
24 think this is really on a question of degree.
25 That is to say, whether you said, Let's

1 -- let's introduce 4 percent rebuilding fee now to get
2 the RSR back to where it should be -- a target -- or
3 whether we say, Let's do it over a series of four (4)
4 years, it still stands to be somewhat destabilizing by
5 prescribing immediate reaction to the target rather
6 than allowing the RSR to fluctuate as it would in a
7 range and allow rates to stabilize.
8 So if we look at the current
9 circumstances then, in 2013/'14 we had what everyone
10 has agreed who lived through it, is it was a very harsh
11 winter. It has -- in one (1) of my questions, my IRs
12 to MPI, they characterize this as a one (1) in twenty
13 (20) year event based on their analysis of their own
14 claims data. And it leaves us with retained earnings
15 at $100 million.
16 Now, in the current percentage of
17 premiums range of 81 to 162 million, that's within the
18 range so there's no prescribed action. If we took, for
19 example, the midpoint of that range, in other words the
20 average of eighty (80) -- eighty-one (81) and a hundred
21 and sixty-two (162), which is 122 million, that would
22 imply that we're at a shortfall of $22 million, which
23 potentially if you call the hundred mill -- the 100
24 million versus 122 million, the 122 million a target, a
25 hard target, a shortfall of 22 million motivating an

1 RSR rebuilding premium. So this is the point based on
2 the current circumstances of the difference between a
3 target and a range.
4
5 (BRIEF PAUSE)
6
7 DR. WAYNE SIMPSON: The other point is
8 this accompanying brief, essentially a paragraph, which
9 says that if we think about the RSR as a range, then
10 why not use the Minimum Capital Test, MCT, at 100
11 percent as the maximum? I would argue against this
12 approach not on the basis of the particular number
13 realized, the 325 million.
14 In fact, it struck me in looking at this
15 that when you do the DCAT and generate an MCT, you
16 might generate a number that's greater than 100
17 percent, so you'd have the perverse effect that you
18 would have a minimum generated from the DCAT that was
19 more than the maximum generated from 100 percent MCT.
20 Maybe not likely, but possible.
21 But it illustrates the point that this -
22 - using the MCT at 100 percent as your point of the
23 maximum is inconsistent with the whole DCAT process.
24 And there's a -- there's a direct -- lacking direct
25 link between the criterion for the minimum, which is

1 based on the risk to the -- to MPI, and the maximum
2 based on the MCT.
3 It's also arbitrary. I don't know how
4 this would be substantiated by evidence or clear
5 argument. And as I've said before, I think there's a
6 question about whether this 100 percent MCT, which
7 might be used in the private sector for insurers who
8 face risk of insolvency, is appropriate for a monopoly
9 Crown corporation that has neither competitive
10 pressers, nor the insolvency risk.
11 So that's about the target versus the
12 range. That's all I have to say about that.
13 And then the second issue is the
14 question of the scenarios, and I said I'd broken this
15 up into three (3) parts: the base scenario, the less-
16 adverse scenarios, and then the more-adverse scenarios.
17 The -- the base scenario then, this is
18 the -- in the DCAT the realistic assumptions that
19 forecast financial position on the basis for comparison
20 about with how the risky scenarios inter -- affect it
21 is consistent with the insurer's business plan.
22 In the base scenario, earnings fall from
23 100 million to 71 million in 2014/2015. Now, I don't
24 find that surprising. If you take a benchmark, as
25 economists do, with -- of the rate of inflation, rate

1 of inflation has something to do certainly with MPI's
2 costs. It's labour costs in particular, but probably
3 it's other costs, as well. There -- any particular
4 firm in any particular industry, there won't be a
5 direct link to inflation. This is the overall
6 inflation in the economy, but there certainly is going
7 to be some links.
8 And that's sort of a benchmark. So with
9 an inflation rate that has been forecast at 1.5 to 1.7
10 percent, the premium increase of .9 percent lies
11 somewhat below that, about, what, .6 to .8 percent
12 below. And so it's not surprising that that would --
13 might have some effect on -- on the earnings of MPI.
14 That said, it is a bit surprising to me
15 that with a proposed increase of 3.4 percent in
16 2015/2016, which is 2.4 percent plus the rebuilding fee
17 of 1 percent, which is well above the inflation
18 forecast at 2 percent, so it's a real increase of 1.4
19 percent in the -- in 2015/2016, earnings only rise to
20 $85 million. They don't even completely recover to 100
21 million that we started from, from 2013, 2014.
22 So I wondered about that. And I looked
23 a little bit at the base scenario. One (1) thing that
24 I noticed -- and there may be many other factors
25 involved in this. I don't, you know, have access to

1 the model to look and see what other assumptions might
2 -- might be employed that might be generating this.
3 And I -- I -- there may well have be -- be discussion
4 about this at the PUB. But one (1) thing is this five
5 (5) year average methodology to forecast claims growth.
6 Because while that might seem like --
7 you know, kind of smooths out claims, claims fluctuate
8 quite a bit. And what has happened there is that a
9 really good year for claims has dropped off, and a not
10 nearly so good year has come on in the five (5) year
11 average. And that's allowed claims growth forecasts to
12 jump from .16 percent annually to 1.81 percent. That's
13 a pretty big jump.
14 It strikes me, for example, that if we
15 adopted it -- a methodology, took advantage of all the
16 data, didn't arbitrarily assume, say, a five (5) year
17 moving average, if we estimated, say, a linear trend to
18 the data, we simply took the claims data from, say,
19 2001 and we estimated a linear trend, we wouldn't get -
20 - as we added observations on this end, in this year
21 adding '13/'14, for example, we wouldn't get nearly as
22 much volatility. That wouldn't jump around nearly as
23 much as it is in this instance. So I think that's
24 something that MPI should be looking at to try to get a
25 more stable claims growth forecast.

1 And I think, to some extent, that has
2 something to do with the fact that earnings do not
3 rebound in the base scenario despite a fairly
4 substantial increase above inflation of the proposed
5 rates.
6 Okay, so looking at the -- the base
7 scenario. This is right out of the DCAT report. I
8 have combined the rate increases and the rebuilding fee
9 of 1 percent. The proposal is for 2.4 percent rate
10 increase in '15/'16 and 1 percent RSR rebuilding fees
11 in '15/'16, '16/'17, '17/'18, and '18/'19. The effect
12 of that is a 6.4 percent increase over four (4) years,
13 which is front loaded to 2015/2016.
14 Now, given that scenario or proposal,
15 the base scenario generates earnings that do recover to
16 154 million by 2018/2019. So what I suggest in the
17 report, first of all, is that I don't understand why 1
18 percent of the proposed increase is described as an RSR
19 rebuilding fee. It certainly may -- this may reflect
20 the difference between the notion of a target and a
21 range, but I don't think that's necessarily --
22 particularly in the context of inflation, running it
23 around -- by the forecasts, around 2 percent.
24 Everybody seems to more or less agree
25 that that's the consensus forecast, because that's the

1 Bank of Canada's target range, and that's the Bank of
2 Canada's forecast. With that kind of stable growth in
3 costs, you would think that much of this would not be a
4 rebuilding fee but would simply be part of their
5 attempt to -- to keep up with -- with growing costs of
6 doing business.
7 And then the second question is why the
8 rate increase that's front loaded at 3.4 percent in
9 2015/2016 isn't spread out over the four (4) years.
10 That is to say, that 6.4 percent increase could be 1.6
11 percent increase in each of the '15/'16, '16/'17,
12 '17/'18, and '18/'19. That leads us to roughly the
13 same point. Some minor differences in terms of the
14 timing of the increases, no doubt, but the 6.4 percent
15 overall increase should get the base scenario back to
16 something like the same level in '18/'19 as it is
17 there, which is more than adequate from the standpoint
18 of the current RSR range based on percent of premiums.
19 So that's the base scenario. Then less
20 adverse scenarios, the equity decline and high loss
21 ratio scenarios, both of which the DCAT report
22 concludes do not warrant a change in the RSR range. I
23 would note that the -- in the equity decline scenario,
24 which was the more adverse scenario, the most adverse
25 scenario in previous reports, certainly the report that

1 I looked at the last time I testified.
2 Part of that adversity related to the
3 pre-1955 data which used the evidence from the Great
4 Depression. And what happened was that when you looked
5 back and dated, essentially, the equity declines and
6 where they came from, the most adverse ones in the --
7 in that previous report, they all occurred during that
8 Great Depression of the 1930s, which was a very bad
9 period. And I also argued a period that we weren't
10 likely to repeat.
11 And, in fact, we had fairly fresh
12 evidence from 2008/2009 at that time that monetary
13 policy reaction in the 21st Century was considerably
14 different than it was during the Great Depression of
15 the 1930s, where essentially, not necessarily
16 intentionally, but essentially they allowed the
17 monetary system to collapse, and that the collapse of
18 monetary policy and monetary supp -- money supply led
19 to a contraction in output and a sharp decline in -- in
20 the stock market. Not only a crash, but a lingering
21 malaise in the stock market, and that that wouldn't
22 happen again.
23 Now, that said, and I want to come back
24 to that because I draw a parallel with the interest
25 rate decline scenario this time, there are questions --

1 other questions about the scenario that now uses the
2 1956 data and on. So in some sense I feel that they've
3 accepted the argument and -- perhaps reluctantly, I
4 don't know -- but are now using only the data from the
5 post-war period, which doesn't include the Great
6 Depression.
7 The -- one (1) -- one (1) thing that's
8 changed from the previous report on the equity decline
9 scenario is the four (4) year horizon was used
10 previously. So the equity declines which were mostly
11 from the Great Depression were four (4) year declines.
12 That's now been replaced by declines of one (1) and two
13 (2) years, which I would argue ignores the evidence
14 that's there in the report that there's a rebound in
15 the third and fourth years that is understated when you
16 simply use the base scenario assumptions for those
17 third and fourth years.
18 Looking at their evidence, I suggest the
19 recovery as much as 9 percent in year 3, and 21 percent
20 in year 4. In other words, stock markets decline and
21 sometimes they decline sharply, but those are followed
22 by -- by reversals, or what we call a rebound effect,
23 and that that has not been captured in the -- in the
24 treatment of the equity decline scenario.
25 In terms of the high-loss scenario,

1 which is the claims data, the -- and we're -- one (1)
2 of my questions to them was: Well, how bad was last
3 year? Because I -- I initially thought it might -- I
4 think it's the worst winter in a hundred years, right?
5 So I thought, Well, this might be a one (1) in one
6 hundred (100) event.
7 But, in fact, looking at their own
8 claims data, they situated it at about the 5 percent
9 tail of -- of claims costs. So it was high, but it was
10 only -- they would characterize as a one (1) in twenty
11 (20) year event. And I think that illustrates that
12 they do have a lot of rich data. They have it monthly
13 or even more frequently than that.
14 And they use that data to estimate
15 claims outcomes, to identify adverse outcomes at
16 specified risk tolerances; a 5 percent tail, one (1) in
17 twenty (20), 2.5 percent tail, one (1) in forty (40)
18 and so on. They have limited that data analysis to
19 annual data since 2001, which really only gives them
20 thirteen (13) data points -- thirteen (13) data points
21 to try to fit the distribution to, which is a little
22 bit thin by statistical standards.
23 They do have monthly data. They do have
24 data before 2001. I -- I gather there are some
25 inconsistencies or some -- I think it's been referred

1 to as data warehouse problems with that. But it seems
2 to me that there is more that can be made of that
3 evidence either in terms of more of the data on an
4 annual basis, or more frequent data on a monthly and/or
5 annual basis to fit the distributions.
6 I -- I think this would be useful
7 because in all the DCAT reports that I've seen, the
8 claims data, the high-loss ratio scenarios always
9 appeared as one (1) of the top three (3) individual
10 risks that the Corporation faces. So it seems to me
11 that if there is something that can be done to improve
12 the quality of that analysis, that probably should be
13 done.
14 Okay. Turning to the adverse scenarios.
15 These are the interest rate decline scenario and the
16 combined scenario that combines the interest rate
17 decline scenario with the equity decline and high-loss
18 ratio scenarios. And it concludes that the percentage
19 of premiums RSR range is not sufficient to withstand
20 these adverse events and form -- is the foundation for
21 the recommended RSR target, or target minimum, of $194
22 million from the DCAT report.
23 The interest rates -- it seems curious
24 that we're talking about interest rate declines,
25 because we're in a period where interest rates are

1 historically low. And I'll show an interest rate --
2 the interest rate series in a minute, but they haven't
3 been this low in a very, very long time. We may have
4 to -- we'd have to go back to the 1930s to see anything
5 like this.
6 And they're partly low because as we've
7 come out of the recession, the economy has remained in
8 -- "persistent slack" is the character --
9 characterization the Bank of Canada has used. So
10 unemployment rates are higher than they would like to
11 see, and the economy is operating with -- below what
12 they would call full capacity.
13 They keep expecting it to return to full
14 capacity, and they keep projecting that that will
15 occur. I think the current projections are it'll occur
16 in 2015/2016, but it hasn't gotten there yet.
17 So we're in a situation where interest
18 rates are low. And one (1) observation we'd want to
19 make is that there is a lower bound on interest rates,
20 essentially a -- a lower bound of zero, if you want to
21 be -- or slightly more than zero.
22 That is reflected by the fact that, as
23 an asset, cash has a return of zero, and that if
24 interest rates were, in fact, at zero, everybody'd hold
25 cash and nobody would buy bonds and nobody would issue

1 bonds, which would lead to both monetary policy
2 ineffectiveness and essentially a collapse of the
3 financial system as we know it.
4 So there is some lower bound on how low
5 interest rates can go. And I think, in most -- most
6 people's minds, that -- that has been achieved.
7 So the consensus forecast, then, that's
8 in the DCAT report not surprisingly suggests rising
9 interest rates to 2018/2019. Now, this may partly
10 reflect the idea that interest rates have nowhere to
11 go. If they can't decline, they're going to eventually
12 rise.
13 I think it partly also reflects the
14 continued reports from the Bank of Canada that the
15 economy will slowly return to full capacity. And, of
16 course, once it does, interest rates will begin to rise
17 to prevent the economy from overheating and generating
18 inflation.
19 And this is part of the Bank of Canada's
20 inflation targeting parl -- policy which says that,
21 when they anticipate inflation starting to rise, they
22 tend to -- to react. And that's something that's
23 relatively new to this century, but which they now
24 operate under.
25 So what -- the -- the question, here,

1 then, that's posed in the DCAT report is, Well, what if
2 interest rates don't rise? What if, in fact, they
3 fall? And the question there is the question of how we
4 go about developing this -- this scenario.
5 So what does the DCAT do? The DCAT
6 analyzes long-term bond yields from 1956 to 2014 over
7 one (1) to four (4) year horizons. It finds interest
8 rate declines, 2.3 percent in one (1) year, 3.2 over
9 two (2) years, two (2) -- three point seven (3.7) over
10 three (3) years, and four point two (4.2) over four (4)
11 years at a one (1) in forty (40) probability, the 2.5
12 percent tail of the interest rate declines over the
13 period.
14 Based on the forecast rate in 2014/'15
15 fourth quarter of 3.1 percent for the ten (10) year
16 Government of Canada bond, this implies negative
17 interest rates in years 2 to 4. Well, we know that
18 doesn't make any sense, because there will be no bonds
19 at that point. People will hold cash. If cash gets
20 you zero, you're not going to take minus 1 percent to
21 hold bonds.
22 So what happens here -- and this, to me,
23 suggests that the interest rate declines are
24 problematic in terms of describing what might happen
25 today -- is that they apply a lower bound. They

1 prevent interest rates from going lower than the lowest
2 monthly Government of Canada ten (10) year bond yield
3 since 1989.
4 This lower bound essentially means that
5 interest rates can only fall 1.4 percent. They can
6 fall from 3.1 to 1.7 and remain there. And that means
7 that they will essentially just do that. The interest
8 rate scenarios, whatever you pick as that lower bound,
9 given these interest rate declines, it will go straight
10 there in year 1 and stay there for four (4) years.
11 So I think, to me, that int --
12 illustrates a big problem. The big problem is that all
13 of the interest rate declines that are found in the
14 DCAT report looking at the period from '56 to today are
15 adverse scenarios that occurred during one (1) period
16 of very high interest rates between '76 and '85.
17 Now, I didn't play around too much with
18 the data. I simply said, Okay, we started in '56, so
19 let's look at '56 to '65, '66 to '75, '76 to '85, but
20 as I did that, and remembering what my first mortgage
21 was, which was in 1978 and then again in 1979 when I
22 came to Winnipeg, I said, Well, something pretty
23 significant was happening then that doesn't have
24 anything to do with what's happening today, and that
25 was what is known as the great stagflation.

1 The great stagflation, imagine, was an
2 average interest rate from 1976 to 1985, an entire
3 decade of 11 1/2 percent. Now, a lot of young people
4 today have no memory of that, except for their parents
5 and grandparents griping about it. Because, you know,
6 this -- this is unprecedented in -- in modern times.
7 And I argue that much like the equity
8 declines taken from the great depression, which were in
9 the 1930s, I question how valid it is to base the
10 interest rate declines on the -- for today's low
11 inflation -- low interest rate environment on the high
12 inflation, high unemployment, high interest rate
13 environment of the great stagflation.
14 You can contrast the decade interest
15 rates of 11.5 percent between '76 and '85 with the 3.6
16 percent interest rate since 2006. We haven't quite got
17 ten (10) years since 2006, but I doubt -- doubt anyone
18 forecasted that that's going to change much upward or
19 downward in the -- in the remaining two (2) years.
20 And also again, to repeat this point
21 about monetary policy, I think monetary policy much
22 like it is improved to avoid the collapses associated
23 with the Great Depression, and we've seen some evidence
24 of that in the treatment of the recession in '08/'09,
25 it's also improved to avoid the mistakes associated

1 with the great stagflation.
2 That is to say, it has adopted inflation
3 targeting procedures which causes the Bank of Canada to
4 lean against the wind of inflation once it gets near
5 the top of that band of 3 percent. And that was not
6 the case earlier, and I think monetary policy has
7 learned from that period, because that was a worldwide
8 phenomenon and a worldwide lesson, that if it's a
9 choice between high inflation and low inflation, you're
10 not going to get very much out of that in terms of
11 improved economic performance, and so you're better off
12 to adopt a low inflation strategy.
13 So this is just a -- a plot of those
14 interest rates from the DCAT report, the same series,
15 which I went and got from CANSIM. And you can see here
16 that this -- you know, this series has a pretty regular
17 pattern. That is, it starts fairly low in 1956, the
18 start of the series.
19 Interest rates are not quite as low as
20 they are today, but they're fairly low. And there's a
21 runup of interest rates over time, fairly slow at
22 first, but steady growth. I think there are some
23 particular points in the early '70s associated with
24 dramatic increases in oil prices, the end of the
25 Vietnam war and the way the US government financed the

1 Vietnam war, and a whole host of other things that are
2 cited in basic economics textbooks that suggests that
3 there was a series of cost push and demand pull factors
4 that pulled inflation higher, and with it, higher
5 interest rates because these are nominal interest
6 rates.
7 So in order to get investors to accept
8 these bonds, and in order for people to find investors
9 who will accept these bonds when they issue them, they
10 need to reflect the -- the cost of living. So as
11 inflation rates went up, nominal interest rates went
12 up. What also happened during this period was,
13 however, that unemployment rates also went up. So
14 there was persistent slack.
15 So then we have the area that's been
16 circled, the red oval, that roughly circles the --
17 ovals -- the period of the great stagflation, and this
18 is the period where interest rates peaked at almost 18
19 percent, and then began the decline. And I think the
20 point to make here is that the decline was pretty
21 precipitous once it occurred.
22 Now, the reason for that is because a
23 number of extraordinary measures were eventually taken
24 to -- to pull back inflation, and one (1) of those I
25 was involved with was the wage and price controls of

1978/1979. I was at the economic council when those controls were instituted, and -- and that monitoring process was introduced. A number of other countries did similar things. And eventually, inflation began to slow down. Well, once inflation began to slow down, the fact that there was a lot of slack in the economy, unemployment rates were high and there was a need to restimulate the economy, meant that interest rates followed it down.

That is to say the Bank of Canada and other centra banks adopted a fairly expansionary fisc -- monitory policy, and that expansionary monitory policy was to lower interest rates. And so interest rates came down quite sharply. And the interest rate declines that we see in that data are in fact the declines that you see on the right-hand side of that peak that is in the -- the red oval.

And interest rates continued to decline, we see, all the way to where we are today. It's not a steady process, but this smooth path has gotten us down to -- to where we are today, which reflects two (2) things. One (1) is low inflation, which is the consequence, I think, of -- of modern inflation, targeting a monitory policy, and, two (2), the -- the recovery -- the slow recovery from the recession of

1 2008/2009.

2 Now, what I do -- I did then I think in

3 response to an IR from the -- from the PUB is I loo --

4 I said, Well, what if we take out this period of the

5 great stagflation, the period in the -- period in the

6 red oval.

7 And then, secondly, what if we take out

8 the other two (2) decades, one (1) on each side of it,

9 which, also, if you look at it, have fairly high

10 inflation rates and in -- high interest rates, and look

11 only at the two (2) periods that are most comparable,

12 which is the first decade, '56 to '65, and then the

13 period from 2006 to 2014.

14 So in response to PUB/CAC 1-4, I did

15 that. And you can see that the interest rate declines

16 are fairly substantial. And this is just a way of

17 saying that I think the reliance on the great

18 stagflation exaggerates the kinds of interest rate

19 declines that we might -- might see. I'm not sure that

20 these are even typical of what we might see at this

21 point, given how low we've gone. They still imply that

22 you would get to the floor because a 1.4 percent drop

23 gets you to the floor, right. You'd get to the floor

24 by year 3, and you'd stay there in years 3 and 4.

25 So the other question I asked was about

1 the -- the floor because, essentially, what the DCAT
2 report does is it plucks a single monthly Government of
3 Canada ten (10) year bond yield, the smallest one in
4 the series, which I think is July 2012. I used the
5 series, the closest thing I could find, and found a
6 minimum of 1.6 percent. But I also looked at what it
7 was for -- for that year, it was 1.85 percent, and what
8 it was for four (4) years. It was 2.53 percent.
9 Now, if you said, What is the minimum
10 floor that you would get to over a four (4) year
11 horizon, because in these DCAT scenarios you're getting
12 to the floor immediately and it's staying there for
13 four (4) years, it seems to me you'd be more
14 appropriate to use a four (4) year floor than a -- than
15 a one (1) month floor and projecting it out over four
16 (4) years.
17 So I think that also, in a sense,
18 overstates the -- the risk facing the Corporation from
19 an interest rate decline in addition to the inclusion
20 of the data from the great stagflation and -- and other
21 high interest rate periods.
22 So then, looking at the combined
23 scenario, this is a joint impact of the interest
24 decline scenario, which is the most adverse of the
25 individual scenarios, the equity decline scenario, and

1 the high loss ratio scenario. And what it does is it
2 combines these scenarios to determine the adverse
3 financial impacts based on one thousand (1,000)
4 simulations for each return period.
5 Now, it strikes me that this is an
6 interesting way to proceed because once you have these
7 financial impacts you have a way of thinking about how
8 you might construct an RSR range. And I could -- I
9 could talk a little bit about that, although I didn't
10 in the -- in the report.
11 But from that they then take the 2.5
12 percent lower tail of financial impacts, the most
13 adverse impacts, and they identify that with a
14 particular combination of interest rate declines,
15 equity declines, and high loss ratio. And using the
16 interest rate floor methodology, which is the
17 methodology used in the interest rate decline scenario,
18 they determine the level and pattern of retained
19 earnings from 2015/'16 to 2018/'19, and find that it's
20 pretty similar to the interest rate decline scenario.
21 And also that the recommended RSR bet -- of the
22 combined scenario is about $4 million, I think, more
23 than the recommendation for the interest rate decline
24 scenario.
25 So I don't think this is surprising in

1 the sense that if the interest rate decline scenario is
2 the most adverse, then it probably fairly dramatically
3 influences the combined scenario and is most certainly
4 the main driver of the results for that scenario. And
5 so I -- I find this problematic in the same sense that
6 I find the interest rate decline scenario problematic
7 in the sense that they rest on interest rate declines
8 from the great stagflation that I don't think has any
9 relevance to the current circumstances.
10 They raised on a floor, which I think is
11 -- is also questionable as a -- as a basis for thinking
12 about where interest rates might, in the worst of all
13 possible worlds, go and stay. Maybe it's not the worst
14 of all possible worlds for all. Certainly for -- for
15 debtors it's not the worst of all possible worlds, but
16 it's -- it -- it's not a good world to be in for -- for
17 financial stability and for -- for MPI.
18 The -- so then I come to the
19 recommendations. I have five (5). I've tried to
20 shorten these a bit and combined a couple of the
21 recommendations from the report. The first one (1)
22 being this point that the RSR should be a range and --
23 as it is in the percentage of premiums calculations
24 now, and not a target as it is in the DCAT report.
25 The rate increases, rather than being

1 front loaded to 2015/2016 and labelling some of them as
2 RSR rebuilding fees, should simply be stable rate
3 increases of 1.6 percent, which gets you to 6.4 percent
4 over four (4) years and are more consistent with the
5 train of inflation and the reflection of how that'll
6 affect costs, since inflation is expected to be fairly
7 stable at 2 percent over the next four (4) years. So
8 this is, you know, roughly compensating for inflation.
9 Thirdly, that the interest rate decline
10 and combined scenarios should be discounted since they
11 rely on evidence from the great stagflation that does
12 not apply to the current situation, and exaggerate the
13 kind of interest rate declines that might in fact
14 occur.
15 And then in terms of what should be
16 done, I think the Kopstein percentage of premiums
17 approach should continue to be used to establish the
18 RSR target range. Range, not target. These are --
19 this range is adequate for the equity loss and high-
20 loss ratio scenarios as they're conceived in the DCAT
21 report. And I don't think the interest rate decline
22 and combined scenarios are credible as they stand and
23 exaggerate the risk of interest rate declines and,
24 therefore, risk to the Corporation.
25 Finally, I think that because the

1 Kopstein method does not address the risk facing the
2 Corporation the DCAT continues to be a useful exercise
3 to assess risks. That some of the scenarios have some
4 problems with them that I've described, and I think
5 should be addressed or considered. That MC -- MPI
6 should consider how the DCAT can be used to establish a
7 range rather than a target, because I think that's what
8 you need for the RSR to be a Rate Stabilization
9 Reserve. And that in determination of a maximum, that
10 the hundred percent MCT is not justified as an RSR
11 range for a monopoly Crown corporation. Thank you.
12 MR. BYRON WILLIAMS: Dr. Simpson -- or
13 actually, Madam Chair. Dr. Simpson is ready for cross-
14 examination. Just given the time if I might recommend,
15 like, a -- a two (2) minute beauty break? Not that he
16 needs it, but perhaps I do. And -- and then we'll be
17 certainly -- we're at your -- your beck and call. But
18 if we could just have a quick break that would be
19 appreciated.
20 THE CHAIRPERSON: Sure. We'll have a
21 quick break and then we'll resume and I believe cross-
22 examination by Ms. Kalinowsky will follow.
23
24 --- Upon recessing at 4:12 p.m.
25 --- Upon resuming at 4:21 p.m.

1 THE CHAIRPERSON: Okay. Welcome back.
2 We'll begin with the cro -- cross-examination of Dr.
3 Simpson by Ms. Kalinowsky from MPI.
4
5 CROSS-EXAMINATION BY MS. KATHY KALINOWSKY:
6 MS. KATHY KALINOWSKY: Good afternoon,
7 Professor Simpson.
8 DR. WAYNE SIMPSON: Good afternoon.
9 MS. KATHY KALINOWSKY: I think all of
10 us would have wished that we had a professor such as
11 yourself that was very clear, and we could have taken
12 amazing notes when we were going through university.
13 So thank you very much for your attendance today.
14 DR. WAYNE SIMPSON: Thank you.
15 MS. KATHY KALINOWSKY: I'd like to
16 start asking you just some basic questions here. But
17 would you agree that a Crown corporation that has a
18 monopoly on an entire line of business such as Basic in
19 this province should have a capital reserve indeed to
20 protect consumers from rate increases caused by
21 unexpected events and losses?
22 DR. WAYNE SIMPSON: I think so in the
23 sense that, you know, there's a lot of evidence that
24 consumers are risk averse, and they -- they don't want
25 sudden jumps in rates. And therefore, rate

1 stabilization is something that they would value.
2 MS. KATHY KALINOWSKY: And then
3 further, is it your opinion that the capital reserve
4 should be kept to the smallest amount possible?
5 DR. WAYNE SIMPSON: The -- okay. Sure.
6 I'm not sure what you mean by "the smallest amount
7 possible." There -- there are opportunity costs to
8 everything, and those opportunity costs should be taken
9 into consideration, yes.
10 MS. KATHY KALINOWSKY: Well, would you
11 agree with me that there must be some kind of
12 rationalization to justify the smallest amount
13 possible?
14 DR. WAYNE SIMPSON: Yes.
15 MS. KATHY KALINOWSKY: You can't
16 randomly just pick out some number --
17 DR. WAYNE SIMPSON: Exactly.
18 MS. KATHY KALINOWSKY: -- of course.
19 DR. WAYNE SIMPSON: Yes.
20 MS. KATHY KALINOWSKY: And in your
21 written evidence, you recommend that the amended
22 percentage of premiums, or this Kopstein approach,
23 continued to be used to establish the RSR target range,
24 right?
25 DR. WAYNE SIMPSON: Yes, I do.

1 MS. KATHY KALINOWSKY: And in fact, the
2 amended percentage of premiums, or the Kopstein
3 methodology, produces an RSR target range of 83 to 166
4 million, which is indeed lower than the methodology
5 recommended by MPI, which is 194 to 325 million,
6 correct?
7 DR. WAYNE SIMPSON: Yes.
8 MS. KATHY KALINOWSKY: In your 2012
9 report to the Board -- and of course I believe this is
10 your fourth appearance to the Board -- you recommended
11 that the amended percentage of premiums, or this
12 Kopstein approach -- method would continue to be used
13 to establish the RSR range, right?
14 DR. WAYNE SIMPSON: I did.
15 MS. KATHY KALINOWSKY: And at that GRA,
16 the amended percentage of premiums, or the Kopstein
17 methodology, would produce a smaller RSR indeed than
18 the methodology that was then recommended by MPI,
19 right?
20 DR. WAYNE SIMPSON: I -- I'm pretty
21 sure that is correct, yes.
22 MS. KATHY KALINOWSKY: And back in
23 2009, you and Professor Hum, who you co-testified with,
24 also prepared a -- evidence for the -- on the RSR for
25 the Public Utilities Board, correct?

1 DR. WAYNE SIMPSON: We did, yes. I
2 believe our -- our report was a little broader than
3 that, but we certainly talked about that as well, yes.
4 MS. KATHY KALINOWSKY: And one (1) of
5 the things in that 2009 report that you recommended
6 indeed to the Public Utilities Board is at that time to
7 use the risk analysis/value at risk approach for
8 determining the size of the RSR, right?
9 DR. WAYNE SIMPSON: We did, yes. It
10 has some features of -- of stability and transparency
11 and so on that are -- are akin to the percentage of
12 premiums approach. And at that time, we -- we thought
13 that might be useful.
14 MS. KATHY KALINOWSKY: And would it be
15 your recollection that in 2009, the two (2) -- the risk
16 analysis/value at risk approach produced a smaller RSR
17 than the methodology at that time recommended by
18 Manitoba Public Insurance?
19 DR. WAYNE SIMPSON: You're testing my
20 memory, but I -- I will take it that you have read the
21 report and have reported it correctly.
22 MS. KATHY KALINOWSKY: Well, just
23 subject to check then, the numbers would be -- for the
24 risk analysis/value at risk would be 102 million to 255
25 million, and the DCAT at that time was 185 million?

1 DR. WAYNE SIMPSON: Yes. I think we
2 raised some questions about the way in which the RA/VaR
3 had been calculated. So I'd have to go back to the
4 report to see if those were reflected in our
5 recommendations.
6 MS. KATHY KALINOWSKY: So would it be
7 fair if I could summarize, then, that your history of
8 recommendations to the Public Utilities Board does
9 indeed result in a methodology that produces a reserve
10 consistently smaller than what MPI has recommended?
11 DR. WAYNE SIMPSON: Certainly the last
12 couple of reports, yes.
13
14 (BRIEF PAUSE)
15
16 MS. KATHY KALINOWSKY: I do have a
17 piece of the transcript that I'd like to have read into
18 the record or looked at. If -- if we pass it to Diana,
19 it could perhaps go on the overhead. It's from 2012,
20 and it's your testimony, Dr. Simpson, from pages 1,498
21 to 1,500 of the application.
22 MR. BYRON WILLIAMS: We -- we have no
23 problems with that. We certainly would ask that Dr.
24 Simpson be given a paper copy as well, if you wouldn't
25 -- wouldn't mind?

(BRIEF PAUSE)

CONTINUED BY MS. KATHY KALINOWSKY:

MS. KATHY KALINOWSKY: So I'll just let everybody read that for a moment right now first.

(BRIEF PAUSE)

DR. WAYNE SIMPSON: Yeah, I vaguely remember -- remember this exchange, yes.

MS. KATHY KALINOWSKY: And, Diana, can you go down a little bit, please?

(BRIEF PAUSE)

MS. KATHY KALINOWSKY: And there's two (2) things that I want to point out on here, but the third-last line there says,

"Until there is consensus on how to resolve the suspicion that the scenario chan -- choice is driven by the size of the RSR that you want, the DCAT remains problematic."

I want to focus on consensus there. You remember saying that, correct?

1 DR. WAYNE SIMPSON: I'm trying to find
2 the word 'consensus'. Where is that?
3 MS. KATHY KALINOWSKY: Third -- third-
4 last line, where the cursor is --
5 DR. WAYNE SIMPSON: Oh, down here,
6 okay.
7
8 (BRIEF PAUSE)
9
10 DR. WAYNE SIMPSON: Yes, okay. Sure,
11 m-hm.
12 MS. KATHY KALINOWSKY: And if, Diana,
13 you could move it up further towards the top there, the
14 second response of Professor Simpson.
15 "I don't think we yet have an answer
16 to that until we, as I said before,
17 have full confidence in the DCAT and
18 in the form of a consensual basis for
19 the way in which it's operated, the
20 way in which the scenarios are
21 determined."
22 You also agree that you said that,
23 "consensual basis"?
24 DR. WAYNE SIMPSON: Yeah, I don't think
25 I have any problem with -- with what I've said there,

1 no.

2 MS. KATHY KALINOWSKY: Sure. And in

3 fact I think you mentioned earlier on in your testimony

4 today that MPI has dropped the Depression-era equity

5 returns.

6 Is that correct?

7 DR. WAYNE SIMPSON: Right.

8 MS. KATHY KALINOWSKY: And that could

9 perhaps be seen as consensus from MPI reaching with --

10 out to CAC, and your recommendations perhaps over a

11 number of years?

12 DR. WAYNE SIMPSON: I think that's an

13 example of where the -- the process -- the DCAT process

14 can benefit from transparency and oversight, yeah.

15 MS. KATHY KALINOWSKY: And did you

16 participate in the DCAT technical conference this year

17 that MPI and the PUB both participated in for the

18 purposes of building consensus on the DCAT?

19 DR. WAYNE SIMPSON: I don't -- I don't

20 believe I did. I -- I received transcripts, but I

21 didn't actually appear at the con -- at -- at the --

22 MR. BYRON WILLIAMS: He might have been

23 -- Dr. Simpson might have been busy with another PUB

24 proceeding.

25 DR. WAYNE SIMPSON: Exactly. Or I

1 might have been doing my day job. I'm not real -- I
2 can't remember now.
3
4 CONTINUED BY MS. KATHY KALINOWSKY:
5 MS. KATHY KALINOWSKY: And another
6 point that I would like to...
7
8 (BRIEF PAUSE)
9
10 MS. KATHY KALINOWSKY: Excuse me. I've
11 been sick and obviously my voice is getting the better
12 of me now. Another point that I would like to
13 establish with this testimony that's here in front of
14 the screen, towards the bottom you said that:
15 "With the DCAT approach, I think the
16 suspicion, until it is eliminated, is
17 that you start out with a number you
18 want to get for the RSR, and then you
19 find scenarios to justify that."
20 Do you remember saying that?
21 DR. WAYNE SIMPSON: It's in the
22 transcript.
23 MS. KATHY KALINOWSKY: Okay. Thank
24 you.
25 DR. WAYNE SIMPSON: I have full face --

1 faith in the transcriber.
2 MS. KATHY KALINOWSKY: Okay. Do you
3 still believe that to be true?
4 DR. WAYNE SIMPSON: That may be a bit
5 blunt. I would say that I -- I don't know that there -
6 - it's necess -- I think this is only a suspicion, and
7 I'm not sure that it would be founded in -- in any way.
8 I don't know exactly what discussions go on at MPI in
9 terms of what they hope to get out of the DCAT before,
10 in fact, it's -- it's developed for any given year.
11 MS. KATHY KALINOWSKY: Thank you for
12 that. In your testimony, you've -- you've stated that,
13 although progress has been made, there's still problems
14 with the DCAT analysis and the implications for the
15 proposed RSR. And you focus on two (2) issues, the
16 issue of the target RSR as opposed to the range and the
17 issue of the DCAT scenarios and how they're
18 constructed.
19 You spoke about that at length earlier
20 on today, correct?
21 DR. WAYNE SIMPSON: That's correct. I
22 mean, tho -- those are areas where I feel I have the
23 expertise to speak. There may be other areas where
24 other people could have concerns. I -- I'm not
25 limiting the concerns to those two (2) areas. I'm only

1 saying that those are the areas where I would have -- I
2 feel I have something to say.
3 MS. KATHY KALINOWSKY: And, Diana,
4 could you please pull up page 3 of the application of
5 Manitoba Public Insurance?
6
7 (BRIEF PAUSE)
8
9 MS. KATHY KALINOWSKY: I'm just letting
10 you read that. Have you read that before, Dr. Simpson?
11 DR. WAYNE SIMPSON: I imagine I have,
12 yes.
13 MS. KATHY KALINOWSKY: And maybe I'll
14 be blunt here, but do you not understand that -- the
15 third bullet to mean that MPI wishes to establish an
16 RSR range within the minimum DCAT amount being the
17 bottom end of the range and the hundred percent MCT
18 value being the upper end of the range in the sense of
19 194 million to 323 million?
20 DR. WAYNE SIMPSON: That's what that
21 says, yes. That's not what the DCAT report says.
22 MS. KATHY KALINOWSKY: Would you agree
23 that MPI is applying for a range for the RSR?
24 DR. WAYNE SIMPSON: That statement in
25 the application does imply that, yes.

1 MS. KATHY KALINOWSKY: I think we've
2 already covered some of this, but back in 2009, you
3 recommended that the PUB use the risk analysis/value at
4 risk approach for determining the size of the RSR. Do
5 you recall that?
6 DR. WAYNE SIMPSON: Yes.
7
8 (BRIEF PAUSE)
9
10 MS. KATHY KALINOWSKY: Sorry, I just
11 had to find a source. I'm going to ask Diana if she
12 could pull up page 4 of your report. It's your written
13 report, not your slide presentation.
14
15 (BRIEF PAUSE)
16
17 MS. KATHY KALINOWSKY: And if you move
18 to the bottom of that page, there's another large quote
19 there. And the second sent --
20 DR. WAYNE SIMPSON: This is the one
21 from my previous report, yes.
22 MS. KATHY KALINOWSKY: Yes.
23 DR. WAYNE SIMPSON: Okay.
24 MS. KATHY KALINOWSKY: And so the
25 second line in that large block quotation reads:

"The report does not find a compelling case to alter the current practice of using the percentage of premium Kopstein risk analysis value at risk and the DCAT MCT calculations to inform the Board on the target RSR and does not recommend a change in practice."

Was this your opinion in 2012?

DR. WAYNE SIMPSON: I've just found it, sorry.

(BRIEF PAUSE)

DR. WAYNE SIMPSON: I guess that was it in 2012, yeah. The RA/VaR has kind of fallen by the wayside, but, sure, yeah.

MS. KATHY KALINOWSKY: So I just want to confirm my understanding, then, of a changing position of yours. In 2009, it's use the risk analysis and value at risk. And in 2012, it's use the combination of Kopstein percentage of premiums, the risk analysis, value at risk, the DCAT, and the MCT to determine an RSR target.

DR. WAYNE SIMPSON: I believe in that

1 report that I said that the -- the incumbent was the
2 percentage of premiums approach and should be retained,
3 but that the others would be useful to inform the Board
4 on the risks facing the Corporation and therefore
5 useful to inform the Board about whether the percentage
6 of premiums approach was failing in fut -- to capture
7 future risk. That -- that would be my characterization
8 of what I intended there.
9 MS. KATHY KALINOWSKY: Okay. So is it
10 my understanding, then, that your position is today,
11 RSR is not a target. It's a range. The MCT is not
12 justified, so it can't be used. And you should only
13 use the Kopstein approach to determine the size of the
14 RSR.
15 So my question, if that understanding is
16 correct, is that considering you've issued three (3)
17 different reports in five (5) different years with
18 three (3) different opinions, how can the PUB consider
19 you to be consistent today in your advice to the Public
20 Utilities Board?
21 DR. WAYNE SIMPSON: Well, if you read
22 the next sentence:
23 "While the percentage of premium
24 Kopstein methodology is unrelated to
25 the risk faced by MPI

1 I said again this time] it has the
2 advantage of being the incumbent
3 method of calculating the target RSR
4 that is easily understood by the
5 public."
6 Stable, transparent, which is what I
7 said in this report.
8 "While the RA/VaR and -- and DCAT/MCT
9 methodologies address the risks faced
10 by MCI and offer alternative useful
11 tools to assess the size of the RSR,
12 particularly when important new risks
13 emerge."
14 The only thing that would change there
15 is that given the current emphasis on the DCAT and the
16 slow decline, if you will, of the -- any reference to
17 the RA/VaR, I -- I've dropped the RA/VaR from my
18 discussion as well. But I -- that -- that sta --
19 statement, I think, is consistent with exactly what
20 I've said this time around.
21 MS. KATHY KALINOWSKY: Earlier today in
22 your testimony you acknowledged that the percentage of
23 premiums approach is indeed unrelated to the risks
24 faced by Manitoba Public Insurance?
25 DR. WAYNE SIMPSON: It doesn't address

1 the risk, but I also pointed out that it has the virtue
2 of being indexed to the growth in the size of the
3 business operation, which is related to the size of the
4 volatility in the sense that that reflects risk. So
5 the size of the risk has something -- is captured in
6 some sense by the Kopstein approach. But in terms of
7 evaluating risks that emerge and that are different
8 over time, then obviously something like the DCAT is
9 far more relevant to that exercise.
10 MS. KATHY KALINOWSKY: And looking at
11 that second sentence -- or third sentence, I guess,
12 that you read in there, we talked about the percentage
13 of premiums, Kopstein methodology indeed having the
14 advantage of being the incumbent.
15 You would still agree with that?
16 DR. WAYNE SIMPSON: Sure. It survived
17 discussions about whether they -- we should use the
18 RA/VaR in 2000, the MCT in 2005, the DCAT in 2010, and
19 it remains -- we've remained with it because it -- the
20 PUB has chosen to remain with it because I think they
21 believe that it has some advantages that -- that the
22 others do not offer. And, therefore, it has the
23 advantage of incumbency. It is the method that's been
24 used for a long period of time.
25 MS. KATHY KALINOWSKY: So are you aware

1 that the original percentage of premiums approach as
2 designed by Mr. Justice Kopstein, that methodology that
3 was used by the Board from 1990 to 2001, set a target
4 for the RSR based upon 15 percent of the percentage of
5 premiums written?
6 DR. WAYNE SIMPSON: I was not aware of
7 that. That was a bad idea. Well, that was a bad idea
8 only in the sense that if that target was interpreted
9 in the fashion that I've described the response to
10 deviations from the target. I suspect that wasn't the
11 case.
12 MS. KATHY KALINOWSKY: And then were
13 you aware that that methodology of percentage of
14 premiums was replaced by the PUB for a period of eight
15 (8) years with the risk analysis/value at risk
16 approach?
17 DR. WAYNE SIMPSON: Yes. Some portion
18 of that, yes.
19 MS. KATHY KALINOWSKY: So it's really
20 just since 2009, then, that the PUB has indeed used a
21 methodology that drops the lowest end of the RSR range
22 to 10 percent of premiums written, correct?
23 DR. WAYNE SIMPSON: Yes. Well,
24 following the Kopstein report, yes.
25 MS. KATHY KALINOWSKY: Well, the

1 Kopstein report said 15 percent as a target. What I'm
2 trying to get at now is that the Public Utilities Board
3 altered that and dropped the lower level down to 10
4 percent.
5 Would you agree with that?
6 MR. BYRON WILLIAMS: I'm going to
7 interrupt for just one (1) second, Ms. Kalinowsky, and
8 to the -- to the panel. I'm quite happy to -- if you
9 wanted to share the excerpt from the appendix of
10 Kopstein report, certainly my recollection is a bit
11 different from yours in that there is a range, but also
12 that they suggest the 15 percent.
13 So just for context, I think it would be
14 helpful for Dr. Simpson to have that. I -- I don't
15 want to interrupt your conversation, but -- you can
16 proceed, but I just think it might be useful for him to
17 have that, the actual excerpt from the Kopstein report.
18 MS. KATHY KALINOWSKY: What we were
19 relying upon was one (1) of the Board orders rather
20 than the actual Kopstein report, and the Board order
21 quoted Kopstein. I can produce that in just a couple
22 of moments.
23 MR. BYRON WILLIAMS: And -- that's
24 okay. But I -- I guess my point is simply this:
25 Kopstein was much more nuanced than -- than I think

1 it's been presented. And I don't want to interfere
2 with your cross-examination, so I'll just -- continue.
3 We'll -- we'll accept your characterization for -- at -
4 - for this -- for the purposes of the discussion.
5
6 CONTINUED BY MS. KATHY KALINOWSKY:
7 MS. KATHY KALINOWSKY: Went through a
8 number of numbers previously in my cross-examination,
9 Professor Simpson.
10 But would you agree that 10 percent of
11 premiums written is indeed the smallest methodology
12 that the Public Utilities Board has ever used for
13 determining the size of the RSR?
14 DR. WAYNE SIMPSON: I don't have enough
15 information to make that claim, no, to -- to agree or
16 disagree with that assessment.
17 MS. KATHY KALINOWSKY: Fair enough.
18 Thank you.
19 DR. WAYNE SIMPSON: I suspect it'll
20 come up at some other point in the hearings.
21 MS. KATHY KALINOWSKY: When we talk
22 about the monies in the RSR, as I move to a different
23 area away from history and into the current milieu, are
24 you aware that MPI invests the monies accumulated in
25 the RSR so as to generate income to be used to reduce

1 the amount of money that ratepayers have to pay?
2 DR. WAYNE SIMPSON: Yes.
3 MS. KATHY KALINOWSKY: So if MPI has an
4 RSR of $200 million and it was able to achieve a return
5 of 8 percent, which is what its investment return was
6 last year, that would mean that MPI -- the RS -- the
7 monies in the RSR would produce $16 million annually?
8 DR. WAYNE SIMPSON: Sounds about right.
9 MS. KATHY KALINOWSKY: So if MPI earns
10 income of $16 million annually through its investments,
11 that indeed is $16 million then that it does not have
12 to ask ratepayers to pay for by way of increased
13 premiums, correct?
14 DR. WAYNE SIMPSON: That's right.
15 MS. KATHY KALINOWSKY: I believe in
16 2009, in your evidence -- although it might have been
17 your evidence and Professor Hum's evidence -- you said
18 that high RSR balances were both publicly and socially
19 wasteful.
20 Do you recall that?
21 DR. WAYNE SIMPSON: No.
22
23 (BRIEF PAUSE)
24
25 MS. KATHY KALINOWSKY: Just one (1)

1 moment, please, and I'll find the reference for that.
2 MR. BYRON WILLIAMS: And he could
3 probably accept it subject to check. But -- but if you
4 want to put the reference in front of him, that would
5 be --
6 DR. WAYNE SIMPSON: Sure. I'm not --
7 I'm not saying it -- it isn't in the report. You've
8 read it. I just don't recall it.
9 MR. BYRON WILLIAMS: So, Ms.
10 Kalinowsky, if you -- he can certainly accept it
11 subject to check.
12 DR. WAYNE SIMPSON: Yeah. That's fine,
13 yeah. I can call Dr. Hum. He has a photographic
14 memory. No, not quite, but close.
15
16 CONTINUED BY MS. KATHY KALINOWSKY:
17 MS. KATHY KALINOWSKY: Board Order
18 161/'09 states on page 34 of 84:
19 "Drs. Hum and Simpson opined that the
20 setting aside of excess reserves, RSR
21 balances higher than required..."
22 Look at that. She's amazing. Thank
23 you, Diana.
24 "...for events very unlikely to
25 happen is both publicly and socially

1 wasteful."

2 DR. WAYNE SIMPSON: Well, that sounds

3 like my colleague's phrasing, but I -- I think what

4 he's getting at here is that there's a notion that if

5 that $200 million were available to motorists, to

6 ratepayers, then they would make the decisions about

7 how that money was spent. If they decided to invest

8 that money, and earned a comparable rate of return,

9 let's suppose they put it into pension funds and earned

10 a comparable rate of return, then it would be

11 equivalent. That is to say, they wouldn't have the

12 reduction in -- in rates for -- Autopac rates, but

13 they'd have the returns on the investment, which would

14 be equivalent.

15 On the other hand, they might choose not

16 to do that. That is to say they might choose to spend

17 that money in other ways. They might decide that they

18 needed it for -- they're a young family now, and they

19 need to think about saving money later. And in that

20 case, rather than simply having lower Autopac rates,

21 they'd have more money available to spend on things

22 that they thought were the -- of most value to them.

23 And then that's how I would interpret that idea that

24 there would be some waste publically and socially in an

25 excess reserves in the RSR.

1 MS. KATHY KALINOWSKY: Is that kind of
2 like the analogy as a bird in the hand is worth two (2)
3 in the bush?
4 DR. WAYNE SIMPSON: No, the analogy is
5 that I know better how to spend my money than somebody
6 else.
7 MS. KATHY KALINOWSKY: Okay. Well,
8 let's run this out, then, for a -- a few years, then.
9 So if MPI did not experience any unexpected losses that
10 required it to draw down it's RSR, and the RSR was
11 always at the $200 million level for a period of five
12 (5) years, then in each of those years, it was able to
13 earn $16 million on the interest, that would mean that
14 all things being equal and not compounding the amount
15 of money, then, that Manitoba ratepayers would have
16 saved be -- be -- would have been saved from paying $80
17 million, then?
18 DR. WAYNE SIMPSON: That's correct.
19 And if they -- $200 million was in the hands of
20 motorists as investors, they might well generate $80
21 million in income which they may or may not have to pay
22 taxes on.
23 MS. KATHY KALINOWSKY: But eventually,
24 they'd have to pay for that in insurance at much higher
25 rates --

1 DR. WAYNE SIMPSON: That's right.
2 MS. KATHY KALINOWSKY: -- in the
3 future.
4 DR. WAYNE SIMPSON: So it would be a
5 wash.
6 MS. KATHY KALINOWSKY: Assuming that
7 they didn't spend it but instead they saved it, for the
8 consumers?
9 DR. WAYNE SIMPSON: They chose to spend
10 it. Presumably that was the preferred way the -- that
11 -- that was their preference, and therefore they are
12 better off.
13 MS. KATHY KALINOWSKY: Okay. Thank you
14 for that. In your report, you have a recommendation
15 that:
16 "The use of 100 percent MCT to
17 establish a maximum for the RSR is
18 not appropriate in the context of a
19 monopoly Crown corporation."
20 Is that correct?
21 DR. WAYNE SIMPSON: I -- I don't think
22 that number, if it's applied to the private sector, has
23 any application to the -- to a monopoly Crown corp,
24 because I think they're different types of
25 organizations facing different sorts of risk,

1 particularly risks of insolvency.
2 MS. KATHY KALINOWSKY: Well, let's talk
3 about that. And that's indeed the maximum for the RSR,
4 is the 100 percent. Is that correct, of what you were
5 saying?
6 DR. WAYNE SIMPSON: That -- that was in
7 -- in the accompaniment to the DCAT report, and in the
8 application, which you've now pointed out.
9 MS. KATHY KALINOWSKY: And you're, of
10 course, aware that SGI uses an MCT of 100 percent to
11 calculate its minimum rate stabilization reserve?
12 DR. WAYNE SIMPSON: That has been
13 pointed out to me, yes.
14 MS. KATHY KALINOWSKY: And ICBC uses an
15 MCT of 130 percent to calculate its minimum RSR?
16 DR. WAYNE SIMPSON: Yes. I have a
17 couple of questions about that, which I -- I don't
18 think I have an answer to so far. One is, why does BC
19 chose a hundred and thirty (130) and Saskatchewan a
20 hundred? And then secondly, Is that a target of the
21 sort that doesn't stabilize rates, or is that a range?
22 Is there a range around that?
23 I -- I don't know the answer to these.
24 I haven't seen any documents that explained what they
25 are, and haven't seen any documents that would explain

1 how they reached those decisions based on any sort of
2 assessment of -- of the risk to the corporations and
3 the off -- offsetting opportunity costs.
4 MR. BYRON WILLIAMS: Ms. -- Madam
5 Chair, if I could just -- there is an exhibit filed
6 yesterday, MPI 25, that I think would assist both Ms.
7 Kalinowsky and -- and Dr. Simpson because it -- it just
8 seems to me that it's got a different characterization
9 of the MCT. And -- and with the panel's permission,
10 I'll approach Dr. Simpson and just share that with him.
11 And I would ask -- and that just may assist his
12 discussion with Mr. Kalinowsky.
13
14 (BRIEF PAUSE)
15
16 DR. WAYNE SIMPSON: Oh, yes, yes, yes,
17 I do remember seeing this. Yeah.
18
19 (BRIEF PAUSE)
20
21 MR. BYRON WILLIAMS: And, Ms.
22 Kalinowsky, I apologize for interrupting, but I just
23 thought it would assist the discussion.
24
25 (BRIEF PAUSE)

1 DR. WAYNE SIMPSON: Okay. Oh, that's
2 up here now. Okay, good.
3 So, in fact, for SGI, my home province,
4 the -- the range is 75 to 150 percent of the MCT, so a
5 hundred doesn't even appear anywhere there, nor is it
6 even the midpoint. I don't know. That
7 characterization is mystifying.
8 The average MCT, however, is well below
9 that, fifty-eight (58). Now it's at 64 percent, which
10 I guess triggers the rebuilding fee. But again, why
11 seventy-five (75)? Why one-fifty (150)? They seemed
12 to be plucked out of the air. I -- I'm sure they have
13 some basis in the private sector, but I don't see the
14 transference to the public sector monopoly.
15 ICBC, wow, 145 percent. That's a big
16 number. And if it's below a hundred percent they must
17 file a plan within sixty (60) days for restoration
18 above the hundred percent minimum. So a hundred
19 percent in their case is a minimum. I don't even see
20 130 percent in there -- theirs. I don't know what
21 these characterizations mean. I don't see a maximum
22 for theirs, but their minimum is a hundred percent MCT,
23 which is your proposed maximum.
24
25 CONTINUED BY MS. KATHY KALINOWSKY:

1 MS. KATHY KALINOWSKY: M-hm. So is it
2 your concern then that MPI is suggesting using a
3 hundred percent MCT for its maximum RSR while the other
4 -- our -- what we call our sister Crowns, sister
5 insurers, use it to establish their minimum RSR?
6 DR. WAYNE SIMPSON: Well, concern of --
7 I -- on the face of it, based on what I know about the
8 Manitoba situation, I'd have a concern that ICBC's
9 holding an awful lot of money -- motorists' money that
10 probably doesn't reflect, unless there's something I'm
11 missing about the British Columbia economy and its
12 effect on insurance rates, that doesn't reflect the
13 risk that's facing that corporation.
14 'Cause that would be the point, wouldn't
15 it? You'd be holding this money as a rate
16 stabilization reserve in case there were unforeseen
17 risks, the -- such as Winnipeg's harsh winter. Of
18 course, they don't have harsh winters in Vancouver, or
19 they don't have those kinds of harsh winters. So right
20 off the bat, the climate issue is -- is -- earthquakes
21 or something.
22 I just don't see where those numbers
23 would -- would have -- bear any relationship to the
24 kinds of risks they would face, but I -- I don't know.
25 I have no knowledge of their deliberations or their

filings.

MS. KATHY KALINOWSKY: So just based upon this response here then, would I be able to conclude from what you've said then that for the past seven (7) years for SGI and ICBC for about the past num -- it doesn't say how long there, but their regulators have indeed been wrong to use the MCT to establish their minimum RSRs?

DR. WAYNE SIMPSON: Well, wrong is a -- is a -- I wouldn't use the word 'wrong'. I think in the balance between protecting against risks and making sure that motorists are not paying more into the fund than is necessary to satisfy their needs for rate stabilization, that these numbers look high.

MS. KATHY KALINOWSKY: But you'd --

DR. WAYNE SIMPSON: It's from the Manitoba experience as I know it.

MS. KATHY KALINOWSKY: But you would agree with me that two (2) out of three (3) regulators say that minimum MCT should be at those levels, as in this response to the undertaking?

DR. WAYNE SIMPSON: I take the information for what it says, yes.

(BRIEF PAUSE)

1 MS. KATHY KALINOWSKY: You have a
2 slide, it's slide number 17 of 26. And I didn't check
3 whether it's the same in this one, in the presentation
4 today or not. And those pages aren't numbered, so I'm
5 flailing here on this.
6 DR. WAYNE SIMPSON: Is it that one?
7 It's up now.
8 MS. KATHY KALINOWSKY: Yes, the final
9 bullet point there. It states:
10 "What is the risk to MPI if rising
11 interest rates do not materialize and
12 interest rates fall."
13 You see that bullet point, right?
14 DR. WAYNE SIMPSON: Sure.
15 MS. KATHY KALINOWSKY: And wouldn't it
16 perhaps be better to say, What is the risk to
17 ratepayers if rising interest rates do not materialize
18 and interest rates fall? Because it's really the
19 ratepayers at the end of the day.
20 DR. WAYNE SIMPSON: Yes, that's what I
21 meant.
22 MS. KATHY KALINOWSKY: And, of course,
23 you would understand that the amount of money that MPI
24 is forecasting to earn through its investments is
25 indeed dependent upon what the forecasted interest

rates are?

DR. WAYNE SIMPSON: Yes, because that affects the bond market, the bond yield.

MS. KATHY KALINOWSKY: And, of course, you would understand that if interest rates do not increase as per the forecasted incres -- increased rate, then MPI will not have the revenues and the monies it forecasted it would off its investments?

DR. WAYNE SIMPSON: That's the risk.

MS. KATHY KALINOWSKY: And, of course, you understand that the rates the PUB sets are based upon the assumption that MPI will be receiving the forecasted money as per its application?

DR. WAYNE SIMPSON: Right. They're built into the base scenario. I think that's what you're getting at.

Is that right? Yeah.

MS. KATHY KALINOWSKY: Yes. And you understand that MPI's application for rates this year is based upon following the major banks and Global Insight, their forecasts, correct?

DR. WAYNE SIMPSON: That's right.

MS. KATHY KALINOWSKY: And the -- I have here in my notes here that the forecasts of the banks have been wrong for the past five (5) years.

1 Don't know about your using the word 'wrong', but
2 haven't -- haven't been realized.
3 DR. WAYNE SIMPSON: Have not been
4 realized. That's right. The -- I think everyone
5 agrees that the recovery from the recession has been
6 slower than anticipated, and that is reflected in
7 interest rates staying lower than they would have
8 expected, yeah.
9 MS. KATHY KALINOWSKY: And, of course,
10 that's a risk that is transferred on to the ratepayers
11 of Manitoba Public Insurance, right?
12 DR. WAYNE SIMPSON: Yes. And that's
13 what this is attempting to capture. This scenario.
14 MS. KATHY KALINOWSKY: And so, of
15 course, you would understand then there if -- if there
16 is a shortfall in revenue that occurs, then -- that the
17 ratepayers will have to pay higher rates in the future?
18 DR. WAYNE SIMPSON: If -- if the rate
19 stabilization reserve doesn't cover it, that's correct.
20 MS. KATHY KALINOWSKY: And I think also
21 somewhere in your evidence previously you've also said
22 that MPI could -- and perhaps go to the government to
23 recover this shortfall?
24 DR. WAYNE SIMPSON: Well, I think that
25 was in the context of the application of the MCT and

1 the question of -- of a monopoly Crown corp compared to
2 a private insurer where the risk of insolvency is quite
3 different. I -- I actually think that pro -- the
4 Corporation would likely not go to the government.
5 They would, perhaps, find other ways to -- to finance a
6 shortfall in the short-term, and then we'd be talking
7 about a different situation in terms of their
8 application to the PUB.
9 MS. KATHY KALINOWSKY: So your position
10 has changed from previous years when you indicated,
11 indeed, that MPI could go to the government?
12 DR. WAYNE SIMPSON: Well, no, I think
13 the context in which I made those comments was not what
14 you've characterized. It was different. And I'm not
15 sure that would be the only avenue open to MPI. Or --
16 or even the preferred avenue.
17
18 (BRIEF PAUSE)
19
20 MS. KATHY KALINOWSKY: You provided
21 some information earlier on today about the period of
22 great stagflation, and how -- and you stated that there
23 were indeed concerns or problems with how the DCAT
24 scenarios were constructed with regards.
25 And that was with respect to at least

1 the great stagna -- great stagflation issue, right?
2 DR. WAYNE SIMPSON: That was my concern
3 with the interest rate decline scenario, or one (1) of
4 my concerns, yes.
5 MS. KATHY KALINOWSKY: So when you
6 identified this as a concern, did you perhaps run the
7 change in the scenario to determine if there were
8 indeed any material impact upon the final DCAT result
9 by excluding that great stagflation period?
10 DR. WAYNE SIMPSON: Yes. I have a -- a
11 version of your model sitting on my computer, and I did
12 run it. No, I didn't.
13
14 (BRIEF PAUSE)
15
16 MR. BYRON WILLIAMS: Are you looking
17 for Exhibits 41 or 42?
18
19 (BRIEF PAUSE)
20
21 CONTINUED BY MS. KATHY KALINOWSKY:
22 MS. KATHY KALINOWSKY: Diana, could I
23 get you to put up -- sorry, MPI Exhibit number 41,
24 please?
25

1 (BRIEF PAUSE)

2

3 MS. KATHY KALINOWSKY: Sorry about

4 that. I apologize. I didn't want to get into some

5 technical economics and actuarial science here, but I

6 think I'm getting into that in any event.

7 But MPI Exhibit number 41, the second

8 table down, the change in Government of Canada ten (10)

9 year bond yield over one (1) to four (4) year periods,

10 that's a comparison, excluding the stagflation period,

11 from 1976 to 1985. And you can compare that to above,

12 which includes just 1957.

13 You see that, Professor Simpson, of

14 course?

15 DR. WAYNE SIMPSON: Yeah. This is my

16 point, that the major declines that were identified,

17 the largest declines, were predominantly in the period

18 of the great stagflation, that's right.

19 MS. KATHY KALINOWSKY: And you can see

20 the note at the bottom of the second table says that:

21 "The Government of Canada ten (10)

22 year bond rate was 2.06 percent as of

23 October 31st, 2014. The DCAT model

24 applies a floor to the Government of

25 Canada ten (10) year bond at 1.68

1 percent, or thirty-seven (37) basis
2 points below the current rate."
3 DR. WAYNE SIMPSON: Yes. So these are
4 -- these are the Government of Canada ten (10) year
5 bond rates. This -- so this is a different series from
6 the one used in the -- in the DCAT report, correct? I
7 shouldn't be asking you that. Sorry. I -- it is a
8 different series.
9 MS. KATHY KALINOWSKY: Sure. And just
10 continuing to read on in that note there, the final
11 line then states:
12 "The financial impact to the
13 Corporation would be approximately
14 equal in all scenarios where the
15 floor is reached."
16 DR. WAYNE SIMPSON: Depending on how
17 the floor is defined, which is a question I also had
18 about the -- about the scenario because it chooses,
19 remember, the minimum monthly figure and says that the
20 interest rates will stay at that level for four (4)
21 years. I have trouble believing that is credible.
22 And of course this -- this is a
23 different series from the one in the DCAT report. But
24 I accept the premise that if you get large declines and
25 get to that floor fast, that's going to have pretty

1 dramatic impact. What I really question is how
2 credible that scenario is.
3
4 (BRIEF PAUSE)
5
6 MS. KATHY KALINOWSKY: I apologize.
7 I've got it here. And it's -- it's your presentation
8 from today. And it's called, "Interest Rate Decline
9 Scenario." And I don't have a page number for it, I'm
10 sorry. And it's the second...
11 DR. WAYNE SIMPSON: Seventeen (17),
12 eighteen (18), nineteen (19), twenty-one (21)?
13 MS. KATHY KALINOWSKY: It's -- it's two
14 (2) pages after the chart, like, the bell curve chart.
15 DR. WAYNE SIMPSON: Twenty-two (22).
16 MS. KATHY KALINOWSKY: Twenty-two (22).
17 So at the bottom there, the four (4) year minimum is
18 2.53 percent for 2010 to '13.
19 So you're recommending that's about
20 fifty (50) basis points higher than what exists right
21 now?
22 DR. WAYNE SIMPSON: As a four (4) year
23 minimum, yeah, it makes more sense than -- than the
24 monthly minimum of the entire series. Remember, this
25 is a situation which -- which is going to endure for a

long period of time.

(BRIEF PAUSE)

MS. KATHY KALINOWSKY: So just trying to figure out then, how would you use a floor that's 50 percent -- or, sorry, fifty (50) basis points higher than what the current interest rate is for that period -- or for the current --

DR. WAYNE SIMPSON: The context here was the use of the long bond rate. And I think the forecast for the fourth quarter of '14/'15, if I'm not mistaken, was 3.14 percent, which was -- is above two point five-three (2.53). Is that correct? Yes, the for -- the forecast rate was 3.1 percent. That was the starting point for the DCAT rate interest rate decline scenario, not two point o-six (2.06); two point one-four (2.14), I think, actually, to two (2) decimal places.

MS. KATHY KALINOWSKY: And you've talked earlier today about the equity decline scenario, and particularly the adoption of the one (1) year and two (2) year equity declines rather than the four (4) year decline used earlier.

And you stated today that that indeed

1 ignores the rebound in the equity values which is
2 captured quite often in the third and fourth year after
3 the -- there's a reversal in the stock market?
4 DR. WAYNE SIMPSON: Right.
5 MS. KATHY KALINOWSKY: Are you aware
6 that this issue is specifically addressed and explains
7 how this is not an issue in our filing?
8 DR. WAYNE SIMPSON: No.
9 MS. KATHY KALINOWSKY: So you have not
10 looked at the Information Requests CAC-64 or PUB 2-43?
11 DR. WAYNE SIMPSON: I believe -- well,
12 I'd have -- I'd have to see them to remember if those
13 particular numbers I have consulted.
14 MR. BYRON WILLIAMS: You're more than
15 welcome to share those with him.
16
17 (BRIEF PAUSE)
18
19 MR. BYRON WILLIAMS: Just to move
20 things alo -- around, does MPI have the -- a paper
21 version of these? We've -- these have been shared with
22 -- with Dr. Simpson.
23
24 (BRIEF PAUSE)
25

1 CONTINUED BY MS. KATHY KALINOWSKY:
2 MS. KATHY KALINOWSKY: And then the
3 other Information Request was PUB 2-43?
4 DR. WAYNE SIMPSON: Well, let's --
5 let's not go to there yet. So you're claiming that
6 this -- I guess the answer to 'B', which says:
7 "The purpose of modelling separate
8 distributions for one (1), two (2),
9 three (3), and four (4) year of
10 cumulative returns specifically
11 address the issue that year-to-year
12 equity returns are not independent."
13 That's true. But I was specifically
14 referring to the periods of sharp equity declines. I'm
15 not sure that this is even applying to that -- that
16 question, except that those might be elements in the --
17 in whatever is -- is being referred to here. Those
18 might -- that my -- data points, but they wouldn't be
19 the only data points.
20 MS. KATHY KALINOWSKY: A few questions
21 here, Professor Simpson on another note.
22 But are you aware that the Board of
23 Directors of Manitoba Public Insurance is willing to
24 transfer very significants (sic) of money -- amounts of
25 money from excess retained earnings in special risk --

1 risk extension, and also extension lines of business,
2 maybe in the amounts of approximately $100 million to
3 the Basic RSR?
4 DR. WAYNE SIMPSON: I do now.
5 MR. REGIS GOSSELIN: Could you repeat
6 the question?
7 DR. WAYNE SIMPSON: I -- I may have
8 heard that before.
9 MR. REGIS GOSSELIN: Could you repeat
10 the question? The first part of it?
11
12 CONTINUED BY MS. KATHY KALINOWSKY:
13 MS. KATHY KALINOWSKY: All right. I'll
14 -- I'll try. Are -- are you aware that the Board of
15 Directors of Manitoba Public Insurance is willing to
16 transfer very significant amounts of money from excess
17 retained earnings of special risk extension and
18 extension to the Basic RSR, perhaps in the amount of a
19 hundred or more million dollars?
20 MR. BYRON WILLIAMS: And just out of
21 fairness to the Witness, it -- it seems to me, based on
22 my vague recollection, that there were some
23 stipulations associated with that transfer. And so, in
24 fairness to the witness, if you want to attach the
25 stipulations that were presented by your Chief

1 Executive Officer, that might be of some assistance to
2 him.
3
4 CONTINUED BY MS. KATHY KALINOWSKY:
5 MS. KATHY KALINOWSKY: Ah, no, I'll
6 just proceed. But, yes, I agree, there are some
7 stipulations and they're written out, of course, in his
8 written testimony.
9 Are you aware, Professor Simpson, that
10 Basic sustained a $70 million loss this year?
11 DR. WAYNE SIMPSON: Yes, because that
12 leads to the rundown in -- in retained earnings, yes.
13 MS. KATHY KALINOWSKY: And are you
14 aware that Basic sustained a $70 million loss also in
15 2012/'13?
16 DR. WAYNE SIMPSON: Yes, that's
17 correct.
18 MR. BYRON WILLIAMS: And just -- I -- I
19 hate to do this, but I think it's -- the revised figure
20 was 63 million.
21 DR. WAYNE SIMPSON: Certainly the one
22 last year is -- is partly explained by the harsh winter
23 and the claims' loss which is precisely the type of
24 scenario that you're looking at in the risk -- the risk
25 scenarios for the DCAT. The previous year, I think

it's probably a series of other things.

CONTINUED BY MS. KATHY KALINOWSKY:

MS. KATHY KALINOWSKY: Sure. Are you aware that the current RSR balance -- are you aware of what the current RSR balance is?

DR. WAYNE SIMPSON: Today?

MS. KATHY KALINOWSKY: As at -- or what it's forecast for the end of February 28th, 2015?

DR. WAYNE SIMPSON: 2015. So that is subject to checking the report and my notes, I -- it is 85 million.

MS. KATHY KALINOWSKY: It's -- actually it's $61 million.

DR. WAYNE SIMPSON: Sixty-one (61)?

MS. KATHY KALINOWSKY: Yes.

DR. WAYNE SIMPSON: That's a revision, right? In the DCAT report?

MS. KATHY KALINOWSKY: I'm looking at the pro forma financial statements.

DR. WAYNE SIMPSON: Okay. That's fine. Okay. I'm wrong.

MS. KATHY KALINOWSKY: And are you aware that the Corporation has indeed forecast an RSR of minus $3 million in 2014/'15, and minus $49 million

1 in 2015/'16, based upon an infor -- based upon an
2 undertaking asked by the Public Utilities Board as to
3 what will happen to the RSR if the current interest
4 rates stay flat at the current level?
5 DR. WAYNE SIMPSON: Not aware, but you
6 stated it. Yeah. That -- that's a calculation that
7 you've made based on the assumptions in the -- in the
8 base scenario, and then constructing a -- an
9 alternative scenario.
10 Is that correct?
11
12 (BRIEF PAUSE)
13
14 MS. KATHY KALINOWSKY: With that I'd
15 like to thank Professor Simpson very much for his
16 answers today, and for being indulgent in me as I tried
17 to look up some fairly complicated actuarial and
18 interest rate information. Thank you very much.
19 DR. WAYNE SIMPSON: Thank you.
20 MR. BYRON WILLIAMS: Madam Chair, just
21 if -- if, again, if the Witness could be excused for
22 five (5) minutes with your permission. I think we're
23 doing okay for schedule. Obviously, we're --
24 THE CHAIRPERSON: Yes, that would be
25 just fine. We'll -- we'll take a five (5) minute

1 break.

2

3 --- Upon recessing at 5:17 p.m.

4 --- Upon resuming at 5:25 p.m.

5

6 THE CHAIRPERSON: We'll begin again.

7 And Ms. Grammond, Board counsel, to begin your cross-

8 examination.

9

10 CROSS-EXAMINATION BY MS. CANDACE GRAMMOND:

11 MS. CANDACE GRAMMOND: Thank you, Madam

12 Chair.

13 So, Dr. Simpson, we have a series of

14 questions for you on a variety of different areas in

15 the material that you've provided. And so for

16 reference purposes I'll mostly be referring to your

17 report as opposed to your PowerPoint.

18 DR. WAYNE SIMPSON: Okay.

19 MS. CANDACE GRAMMOND: Diana, so maybe

20 we'll start on page 16 of the report. And, Dr.

21 Simpson, this is on the issue of a target range versus

22 a target point.

23 DR. WAYNE SIMPSON: Okay.

24 MS. CANDACE GRAMMOND: We see here --

25 DR. WAYNE SIMPSON: Sorry -- sorry,

1 what was the page?
2 MS. CANDACE GRAMMOND: Sure. Sixteen
3 (16), so it's just up on the screen.
4 DR. WAYNE SIMPSON: Oh, with the
5 recommendations. Okay, sure.
6 MS. CANDACE GRAMMOND: Yeah.
7 DR. WAYNE SIMPSON: Yeah.
8 MS. CANDACE GRAMMOND: So it's in that
9 first paragraph numbered 1. The last sentence there
10 reads:
11 "An annual RSR target may be no
12 better than no RSR in terms of rate
13 stabilization."
14 Can you explain what you meant by that
15 sentence?
16 DR. WAYNE SIMPSON: Well, I -- I
17 compared two (2) scenarios, one (1) in which there was
18 an RSR target of 200 million, the other which was an
19 RSR target of zero which is no RSR at all, to
20 illustrate that if you responded the same to deviations
21 from those targets, you got the same amount of rate
22 volatility.
23 And, therefore, if the goal was to
24 stabilize rates because that's what motorists would
25 prefer because they're averse to sudden changes in

1 their rates, then -- then you're not achieving that
2 with the 200 million any better than you are with the
3 zero or no -- no RSR.
4 MS. CANDACE GRAMMOND: Okay.
5 DR. WAYNE SIMPSON: And I guess I chose
6 zero just to emphasize that point, not -- not to
7 advocate for no RSR because, as I said, the -- you
8 know, I accept that motorists do consider rate
9 stabilization to be valuable.
10 MS. CANDACE GRAMMOND: Thank you. Now,
11 we know that you favour a target range over a target
12 point.
13 Can you tell us what in your view is the
14 root cause of the instability in using a target as
15 opposed to a range?
16 DR. WAYNE SIMPSON: The instability
17 involves what the rules are when you're off the target
18 because you're almost never going to hit the target,
19 right? I mean, one (1) number. So if you set that one
20 (1) number and then you say, Well, if it's below I need
21 a rebuilding fee and if it's above I have to rebate;
22 then most of the time you're going to either be
23 rebuilding or rebating. If you have a range that's not
24 going to happen because you're going to have a series
25 of numbers between the midpoint and the bottom where

1 you don't have a rebuild and between the mid-point and
2 the top where you don't have a rebate.
3 So that was the -- what I was trying to
4 get at there --
5 MS. CANDACE GRAMMOND: Okay.
6 DR. WAYNE SIMPSON: -- in those
7 examples.
8 MS. CANDACE GRAMMOND: Okay. So how
9 important to this conclusion is your assumption that
10 rates are adjusted to achieve the RSR target each year?
11 DR. WAYNE SIMPSON: Well, as I
12 indicated that was the way I set it out to -- to
13 magnify the point. But I think the point is only one
14 (1) of degree.
15 If, for example, you said, Well, instead
16 of doing it all at once, let's do it over two (2) years
17 or three (3) years, or in this case four (4) years.
18 Let's divide up what we need to achieve and -- and
19 divide it up over four (4) years. Of course, that will
20 change over time because the next year you probably
21 won't end up where you thought you were going and
22 you'll have to adjust it further. But all of that is
23 destabilizing. So any target is destabilizing,
24 provided you respond to the target, whether you respond
25 ann -- annually or you respond over a longer period of

time.

MS. CANDACE GRAMMOND: Thank you. Diana, if we can go to page 6 of the report. And I just need to locate the reference on the screen. If you could just scroll down a little bit.

(BRIEF PAUSE)

MS. CANDACE GRAMMOND: Okay. So the first full paragraph that we see on the screen that begins with, "the key qualifier here is" --

DR. WAYNE SIMPSON: Right. This -- this is what I've just mentioned, yeah.

MS. CANDACE GRAMMOND: Yeah. So if we look just towards the end of that first full paragraph, we see reference -- and I'm just starting on the third last line:

> "Generating instability in rates of the sort the RSR is designed to avoid."

This is a concern that you've raised.

DR. WAYNE SIMPSON: M-hm.

MS. CANDACE GRAMMOND: And would it not be true, though, that this con -- this concern could arise even if a range for capital is used, that there

1 can still be instability in the rates?
2 DR. WAYNE SIMPSON: Could you restate
3 that?
4 MS. CANDACE GRAMMOND: Sure. So if we
5 understand what you're saying here in this particular
6 paragraph correctly, you've raised a concern about
7 instability in rates --
8 DR. WAYNE SIMPSON: Right.
9 MS. CANDACE GRAMMOND: -- the very
10 thing that the RSR is designed to avoid.
11 But isn't it true that stability -- or
12 instability can still arise even where there's a range
13 in place as opposed to a target point?
14 DR. WAYNE SIMPSON: Right. Instability
15 can arise if the -- if circumstances are so adverse or
16 favourable that you get outside that bounds -- those
17 bounds, sure, because at some point you probably are
18 going to want to take corrective action. I won't
19 qualify that.
20 MS. CANDACE GRAMMOND: Okay. And you
21 talked about -- when I asked you about the target
22 point, that it -- you're never going to hit it so
23 you're always going to end up with replenishment or a
24 rebate.
25 Do you have any recommendations on how

1 either replenishing or rebating should be designed in
2 terms of process to mitigate that concern?
3 DR. WAYNE SIMPSON: A range. You mean
4 as opposed to a target. If you have a range, you
5 reduce the amount. The wider the range, the -- the
6 less you -- the less action is prescribed. There is
7 some risk in -- in widening a range because, if that
8 minimum is too small, you run the risk of a series of
9 adverse events being, you know, reducing the retained
10 earnings to a -- an unsustainable point.
11 But, you know, these are independent
12 events, and you'd expect that the adverse events are,
13 on average, followed by corresponding favourable
14 events. And we see some of that in the replenishment
15 of the earnings associated with the base scenario, I
16 think.
17 MS. CANDACE GRAMMOND: So even where
18 there's a range in place, should replenishment be
19 spread over multiple years, in your view?
20 DR. WAYNE SIMPSON: Yes, in the sense
21 that I think overreacting to the particular level of
22 the RSR is -- is as destabilizing as -- as
23 underreacting to it, yeah.
24 MS. CANDACE GRAMMOND: Okay. Now, do
25 you believe that the DCAT approach could be used as a

1 basis for setting both a lower and an upper target
2 capital level or a -- a range?
3 DR. WAYNE SIMPSON: I think it could be
4 used for that purpose, but it wouldn't be the way a
5 DCAT is currently used. I don't think, as -- I think,
6 as I understand the DCAT report, it follows industry
7 practice. And the industry practice is to take
8 particular events and run them through a non-stochastic
9 financial model.
10 That said, the combined scenario takes -
11 - combines three (3) events, runs them through the
12 model, does a thousand (1,000) simulations, and
13 generates a distribution of financial impacts.
14 It seems to me that that, including more
15 than probably three (3) risks, would generate a summary
16 of the risks facing the Corporation that might be used
17 to develop a DCAT. But it would have to be done in
18 that framework -- that is to say, what I would
19 characterize as a -- as a Monte Carlo exercise of some
20 kind, yeah.
21 MS. CANDACE GRAMMOND: Okay. Just one
22 (1) follow-up question on my earlier question to you
23 about whether replenishment should be spread over a
24 period of years. Let's talk about rebating for a
25 minute.

1 In your view, would there be any reason
2 to spread a rebate over multiple years, especially
3 considering the costs of issuing a rebate?
4 DR. WAYNE SIMPSON: Well, I -- I think,
5 with an appropriate range, the -- the argument is
6 equivalent on both sides. That is to say, just as you
7 wouldn't want to overreact to rebuilding, you would
8 also not want to overreact to rebating. That's how you
9 get stability in the system.
10 MS. CANDACE GRAMMOND: Thank you. Now,
11 coming back to what MPI is proposing, are you
12 comfortable with the selection of a one (1) in forty
13 (40) year probability level as a basis for setting the
14 lower Basic target capital level?
15 DR. WAYNE SIMPSON: I -- I think -- I
16 could -- subject to verification, I guess is the term,
17 I believe that Dr. Hum and I talked about this in a
18 previous report. And our view was that this seemed to
19 be a bit excessive in terms of the kind of risk
20 tolerance we would conceive for an operation of the
21 sort of MPI. And I think we are good for a one (1) in
22 twenty (20) risk tolerance.
23 MS. CANDACE GRAMMOND: And you would
24 maintain that view now?
25 DR. WAYNE SIMPSON: In terms of the

1 minimum, I -- I think that one (1) in twenty (20) would
2 be more appropriate than one (1) in forty (40) as for
3 the range. I think you'd want to think about what the
4 minimum and maximum meant. The one (1) in forty (40)
5 would be more like the midpoint rather than -- of the
6 range rather than the -- than the minimum.
7 MS. CANDACE GRAMMOND: And my next
8 question was going to be: What would you suggest for a
9 probability level at the high end, at the max?
10 DR. WAYNE SIMPSON: Well, something
11 more than -- or less than one (1) in forty (40),
12 whatever that would be, one (1) in a hundred. You
13 know, the benchmark, I think, because it's what we have
14 and -- and have understood for a while, is -- is the
15 Kopstein approach. And those numbers in conjunction
16 with what the DCAT -- well, not the DCAT, the Monte
17 Carlo simulations are telling us would probably give us
18 some idea of what -- what we want to discuss in terms
19 of risk tolerance.
20 So without going through that exercise
21 it's hard to say, just pluck numbers out of the air,
22 but maybe the one (1) in one hundred (100) would be a
23 maximum.
24 MS. CANDACE GRAMMOND: Okay.
25

1 (BRIEF PAUSE)

2

3 DR. WAYNE SIMPSON: It's hard to --
4 just to add to that. It -- it's hard to think about
5 what kind of risks motorists are interested in
6 tolerating because, ultimately, they are the people who
7 would pay the -- the price, if you will, of -- of
8 instability, or get the benefit, I guess, instabil --
9 it's hard to know what -- what kinds of risk you -- you
10 might want to do focus groups and try to establish it
11 in that fashion. That's sometimes done, qualitative
12 research. Try to find out what motorists think,
13 proposing different risk scenarios, what kinds of
14 things they think are -- are risks worth taking.
15 It seems to me, and I think we made this
16 point in an earlier report, Dr. Hum and I, that, you
17 know, you have to look at what the consequences are of
18 -- of a catastrophe of the sort MPI might face, a
19 really adverse scenario. It clearly isn't -- isn't
20 likely to be like the one (1) in seven hundred (700)
21 flood which would cause billions of dollars' damage to
22 the -- the city and is protected against by the new
23 floodway, but it would probably be, you know, certainly
24 something. It wouldn't be one (1) in seven hundred
25 (700); it would be less than that.

1 MS. CANDACE GRAMMOND: Okay. So
2 subject to your comment about consulting with
3 motorists, would it be fair to say that your view would
4 be minimum of one (1) in twenty (20) and a maximum of
5 one (1) in one hundred (100)?
6 DR. WAYNE SIMPSON: Well, that view
7 would be pretty uninformed in terms of what motorists
8 are interested in in term -- or willing to tolerate in
9 terms of risk, but those are the numbers that have been
10 discussed in -- in previous -- the -- the adverse
11 scenarios have been discussed around the issues one (1)
12 in twenty-one (21) and forty-one (41) and one hundred
13 (100), but those are numbers, I think, taken from the -
14 - from the DCAT industry, not -- not -- they aren't
15 numbers that I have -- I've chosen.
16 MS. CANDACE GRAMMOND: And --
17 DR. WAYNE SIMPSON: So I'm not sure I
18 want to be wedded to those numbers.
19 MS. CANDACE GRAMMOND: Okay. That's
20 fine. With respect to consulting with motorists, how
21 would the risk tolerance of motorists be in that
22 context?
23 DR. WAYNE SIMPSON: Well, my halftime
24 colleague, Greg Mason, at Prairie Research Associates,
25 would probably have a better answer to this than I

1 would because they do this kind of thing. But you'd
2 need to pose a set of questions. And I -- I claim no
3 expertise in this area. You need to pose a set of
4 questions to try to get at estimating what other risks
5 that motorists think are worth insuring against.
6 And they would have to be scenarios
7 that, you know, if this happens, this is going to cost
8 you. How -- would you like to avoid this by paying
9 this amount of insurance, essentially, because that's
10 what it is. It's insurance, rate -- rate stabilization
11 insurance.
12 So I imagine that there is a literature
13 that does these kinds of things. And I'd imagine that
14 insurers take some advantage -- private insurers
15 certainly take some advantage of this kind of
16 literature to -- to formulate their products and so on.
17 MS. CANDACE GRAMMOND: Now, have you
18 formed an opinion on whether the target range that
19 we're discussing should be expressed in terms of the
20 RSR or in terms of total equity of the Corporation?
21 DR. WAYNE SIMPSON: No, not really.
22 MS. CANDACE GRAMMOND: Sorry. And I
23 should clarify, it's total equity for Basic, not for
24 the Corporation. But I assume that doesn't change your
25 answer.

1 DR. WAYNE SIMPSON: No. No.
2 MS. CANDACE GRAMMOND: Okay.
3 MS. CANDACE GRAMMOND: Ms. Grammond, as
4 you're aware, Dr. Simpson does have the benefit of a --
5 a team supporting him with some dialogue. It's totally
6 up the Board, if you'd like him to consider that as an
7 undertaking, it may be -- we're certainly prepared to
8 do that. But I -- I leave that totally to you.
9 MS. CANDACE GRAMMOND: I think I'll --
10 I'll take you up on that because I think it is
11 something that the Corporation's put forward as an
12 issue, and the Board needs to decide it.
13 So, you know, whether we're going to
14 hear from you in final argument or whether you -- if
15 you want to put evidence on the record from him, then
16 I'm -- I'm not going to say no to that if it could
17 assist the Board in its deliberations.
18 MR. BYRON WILLIAMS: If I could have
19 one (1) moment.
20
21 (BRIEF PAUSE)
22
23 MR. BYRON WILLIAMS: Ms. Grammond, just
24 -- we're -- I was just discussing with Dr. Simpson his
25 expertise on that particular issue versus Mr. Dyck and

1 -- and Ms. Sherry. We could do it one (1) of two (2) -
2 - two (2) ways. He could certainly consult and -- and
3 then provide some information, or CAC could present a
4 position in closing.
5 But if you would -- would like the
6 benefit of -- of his advice, recognizing it's probably
7 stretching a bit beyond his core expertise, I'd --
8 we're -- we're prepared to -- to offer that. And I
9 leave it to you.
10 MS. CANDACE GRAMMOND: I guess my
11 comment would be if it's going to come from him in
12 terms of an answer to undertaking, there needs to be
13 the opportunity for follow-up cross. So, I mean, he's
14 your witness. CAC's put him forward. If you didn't
15 elicit that evidence, I'm not trying to force you to do
16 that if -- but since you made the offer, we're having
17 the discussion.
18 As I say, if -- if you feel that for him
19 to possibly have to answer follow-up questions is going
20 to be difficult for any practical reason and you're
21 comfortable with your client just putting forward a
22 position in argument, that's fine.
23 MR. BYRON WILLIAMS: I think we could
24 present some pros and cons of -- of the -- undertake to
25 present some pros and cons of the two (2) options.

Whether there's an ultimate opinion presented there, we could certainly present kind of a -- a learned dialogue on that.

MS. CANDACE GRAMMOND: Okay. So CAC undertakes to provide some dialogue with respect to the question of total equity for Basic versus RSR.

MR. BYRON WILLIAMS: Yes. Thank you.

--- UNDERTAKING NO. 59: CAC to provide some dialogue with respect to the question of total equity for Basic versus RSR

MS. CANDACE GRAMMOND: Just one (1) moment, Madam Chair.

(BRIEF PAUSE)

CONTINUED BY MS. CANDACE GRAMMOND:

MS. CANDACE GRAMMOND: Okay. Thank you. I'll leave that area for the moment. And, Dr. Simpson, I have some questions for you with respect to the alternative RSR rebuilding plan.

So this is from page 10 of your report, and also referenced in your PowerPoint at slide 11.

1 But let's stay with page 10 here up on the screen.
2 So you've given evidence that an
3 alternate rate increase of 1.6 percent annually over
4 the next four (4) years would be preferable to a 2.4
5 percent increase in rates and a 1 percent RSR load.
6 And you reference -- and it's -- I think we just need
7 to go down a bit, Diana.
8 You reference in the middle of the page
9 the notion of front loading the rate increase to the
10 2015 -- '15/'16 fiscal year, which you think seems
11 unnecessary. You're with me on that part of your
12 evidence? You're nodding, so I'll take that as a yes.
13 DR. WAYNE SIMPSON: Yes, sorry.
14 MS. CANDACE GRAMMOND: That's okay.
15 Now, would you agree that your proposed alternative
16 approach spreads the requested rate increase in
17 combination with the RSR rebuilding load evenly over a
18 four (4) year period?
19 DR. WAYNE SIMPSON: Yes.
20 THE COURT REPORTER: Your mic, sir?
21 DR. WAYNE SIMPSON: Is it on?
22 MS. CANDACE GRAMMOND: No.
23 THE COURT REPORTER: No.
24 DR. WAYNE SIMPSON: Sorry. Yes, that's
25 the intent.

1 MS. CANDACE GRAMMOND: And so are you
2 suggesting, then, that a 1 percent -- a 1.6 percent
3 rate increase be granted this year, and then that any
4 subsequent rate increases be subject to a further
5 review at future GRAs?
6 DR. WAYNE SIMPSON: Yes.
7 MS. CANDACE GRAMMOND: So you would
8 anticipate, then, that MPI would come back to the
9 Board. Its expenditures would be examined in the same
10 manner that they typically are in this proceeding, and
11 -- including necessity and prudency of costs and so
12 forth?
13 DR. WAYNE SIMPSON: Yes. It would be
14 the usual GRA, yeah.
15 MS. CANDACE GRAMMOND: And can you tell
16 us what your view is about the distinction between a --
17 a rate increase versus the RSR rebuilding load in terms
18 of value or advantage, either to the ratepayers or to
19 MPI as -- from one (1) approach to the other?
20 DR. WAYNE SIMPSON: Yes. I see no
21 advantage.
22 MS. CANDACE GRAMMOND: No advantage to
23 --
24 DR. WAYNE SIMPSON: Either.
25 MS. CANDACE GRAMMOND: -- either side?

1 DR. WAYNE SIMPSON: Either party in the
2 classification. The money -- as far as the motorists
3 are concerned, they don't care if -- if it's a two
4 point four (2.4) plus 1 percent rebuilding. They might
5 -- maybe they're more willing to accept the 1 percent
6 premium, you know, given the harsh winter last year or
7 something like that. There may be a perception. But
8 in terms of their actual payments, 3.4 percent is 3.4
9 percent, and -- and that goes into MPI's revenue stream
10 in the same way as if -- whether it's a -- 1 percent is
11 a rebuilding fee or not.
12 MS. CANDACE GRAMMOND: Okay. I have
13 some questions for you then about the DCAT base
14 scenario, and this is referenced in a few different
15 places; in the response to PUB/MPI 1-55, if we can go
16 there, and in particular, 1-55(c).
17 So this is, in essence, the trend
18 analysis that MPI provides. You're familiar with this,
19 right? Generally?
20 DR. WAYNE SIMPSON: M-hm. Yes.
21 MS. CANDACE GRAMMOND: And in your
22 report -- so we can leave this up on the screen. I'll
23 -- I'll read to you something from your report, and if
24 we need to go there, we can, but I -- I assume you'll
25 recognize it. This is page 9 of your report. You say:

1 "It is unclear why a five (5) year
2 moving average has been used, which
3 leads to the instability in the
4 claims forecast for the base
5 scenario, and contributes to the
6 disappointing retained earnings
7 forecast in the base scenario."
8 You're familiar with that statement in
9 your report?
10 DR. WAYNE SIMPSON: Yes. That was my
11 understanding of what -- what the -- the -- what had
12 happened, yes.
13 MS. CANDACE GRAMMOND: And the context
14 for that statement relates to the forecast of the
15 number of claims shown in the trend analysis before us.
16
17 Is that right? That would be at line --
18 DR. WAYNE SIMPSON: Yeah. Yes.
19 MS. CANDACE GRAMMOND: -- 13.
20 DR. WAYNE SIMPSON: Yes.
21 MS. CANDACE GRAMMOND: Yeah.
22 DR. WAYNE SIMPSON: Let's -- let's take
23 a 'yes' on that. I -- I'm just looking at everything,
24 but I -- yeah, I think you're right. Yeah.
25 MS. CANDACE GRAMMOND: Okay. Now, you

can confirm that the claims forecast for the base scenario in the DCAT is built up coverage by coverage, as documented in the Claims Incurred, or Volume II, section of the GRA?

DR. WAYNE SIMPSON: Yes.

MS. CANDACE GRAMMOND: And can you explain how, in your view, the trend analysis that we have in front of us relates to the claims forecast for the base scenario?

DR. WAYNE SIMPSON: The growth in claims is based on a five (5) year moving average, which would be 2010 to '14, I guess. Is that correct? You -- you -- I'd have to go back and look what -- what exact years, but you -- you're basing it on a five (5) year moving average, right?

MS. CANDACE GRAMMOND: Yeah. I think in the top right-hand --

DR. WAYNE SIMPSON: So -- so --

MS. CANDACE GRAMMOND: -- part of the screen we see that.

DR. WAYNE SIMPSON: Yeah.

(BRIEF PAUSE)

DR. WAYNE SIMPSON: I'm not sure what

1 question you're asking me there.
2 MS. CANDACE GRAMMOND: Okay. So if --
3 if I understand your report correctly, you say in your
4 report it's unclear to you why a five (5) year moving
5 average has been used which leads to instability in the
6 claims forecast for the base scenario and contributes
7 to the disappointing retained earnings forecast in the
8 base scenario.
9 DR. WAYNE SIMPSON: Right.
10 MS. CANDACE GRAMMOND: So what I'm
11 asking is: Can you explain how the trend analysis that
12 we have in front of us relates to the claims forecast
13 for the base scenario in the DCAT?
14
15 (BRIEF PAUSE)
16
17 DR. WAYNE SIMPSON: A five (5) year
18 moving average, you're going to take the previous five
19 (5) years. Is that correct? And -- and as you move
20 along each year, you're going to drop off one (1) year
21 and add the new year's data. And that's how you're
22 going to get your -- your claims growth forecast into
23 the future, which is part of the base scenario, which
24 goes forward to 2019.
25 What I -- my -- and that's -- that is

1 what is described in the DCAT, and they also describe
2 the fact that what they've dropped off in that process
3 is a very good claims year where claims dropped quite
4 considerably. And therefore the -- the -- there's a
5 dramatic change in the claims growth.
6 What -- what my point was is that none
7 of that captures the trend as it has evolved, say, from
8 2001. So it would back-cast the data to -- to use more
9 of that data and provide, as you added additional new
10 data, more stability to that -- that trend growth.
11 That was my point, but I'm basing my
12 description of what they did on what they say they did
13 --
14 MS. CANDACE GRAMMOND: Okay.
15 DR. WAYNE SIMPSON: -- in the DCAT
16 report.
17 MS. CANDACE GRAMMOND: Would you agree
18 that the trend analysis that we see would be improved
19 if it was linked to the claims forecasting process?
20 DR. WAYNE SIMPSON: Yes.
21 MS. CANDACE GRAMMOND: Now, are you
22 recommending the use of standard time series techniques
23 to improve the trend analysis or the claims forecast
24 for the base scenario, or both?
25 DR. WAYNE SIMPSON: I would think both.

I don't see any reason why that wouldn't be a useful procedure. Now, when I say, "standard time series techniques," I -- I'm really just talking about basic regression here of -- of claims on -- on time.

MS. CANDACE GRAMMOND: And can you tell us a little bit about the advantages of using standard time series techniques for that purpose?

DR. WAYNE SIMPSON: It captures more of the trend as it evolved in the data, and would be less -- would be more stable in the sense that it would not drop off favourable years, as -- as happened, I guess, in 2009, and added in unfavourable years like 2013/'14.

In other words, when you have -- when you have the situation we had last year where you have a particularly harsh winter, which was characterized as a one (1) in twenty (20) event, that's going to have a much larger impact on claims growth in a five (5) year average, being added to a five (5) year average, in particular in that case as you dropped off a rather favourable claims year at the -- at the other end, than it will in a long-term view of what the growth has been in claims over a long period -- longer period of time.

MS. CANDACE GRAMMOND: Okay. So how would you expect use of the standard time series techniques to affect the current DCAT base scenario if

1 these were in use now?
2 DR. WAYNE SIMPSON: Well, I would think
3 that claims growth, just as it was understated by the
4 five (5) year average when the favourable year was in
5 and then dropped this year, it's overstated now with
6 the harsh year of last year, one (1) of the five (5)
7 observations, and that what you get is something in
8 between those two (2) as your -- as your estimate of
9 the -- of the claims growth over -- well, you don't
10 need to start at 2001. You could start at any
11 reasonable point. I don't -- picked 2001 because that
12 is the available claims data that doesn't have data
13 warehousing problems, or whatever the term is.
14 MS. CANDACE GRAMMOND: Thank you. Now,
15 have you formed an opinion on the appropriateness of
16 the basis of forecasting interest rate movern --
17 movements for the GRA forecast?
18 DR. WAYNE SIMPSON: Well, they use a
19 consensus forecast of -- of people who forecast
20 interest rates, all right? And that seems to be a
21 reasonable way to proceed.
22 The problem I have is not with that in
23 its use of the base forecast. It's with how you then
24 think about the interest rate risk. And the question I
25 -- I asked myself several times, but, you know, I

1 haven't expressed until now, but I will now, was if you
2 ask the interest rate forecasters what they thought was
3 the possibility, you know, in probabilistic terms of
4 interest rates falling to 1.68 percent and staying
5 there for four (4) years, I think most of them would
6 say it was virtually impossible. In other words, a lot
7 less than 2.5 percent.
8 MS. CANDACE GRAMMOND: So do you have
9 any recommendations on how the interest rate forecast
10 might be strengthened?
11 DR. WAYNE SIMPSON: Not the forecast
12 itself, no. The consensus forecast, I think -- I think
13 there's a fair amount of agreement at the moment among
14 forecasters, you know. It isn't like there's a lot of
15 disagreement, because we have a relatively stable
16 environment. We have low inflation at low interest
17 rates with virtually nowhere to go but up, but the
18 question of how long that's going to take is not clear.
19 So I -- I don't think there's -- there's
20 a problem with the consensus forecast of the sort that
21 you might have gotten during the great stagflation.
22 The great stagflation, if you'd posed questions at that
23 point, nobody knew where the economy was going in those
24 days.
25 MS. CANDACE GRAMMOND: So do you have

any comment with respect to the number of forecasts that MPI is using at present? Namely, the five (5) banks and --

DR. WAYNE SIMPSON: Five (5).

MS. CANDACE GRAMMOND: -- Global Insight?

DR. WAYNE SIMPSON: I think it's immaterial at the moment. I -- I don't really have an opinion. It -- it's not a -- no. I don't have an opinion.

MS. CANDACE GRAMMOND: Thank you. Madam Chair, I'm going to go into some questions about some of the specific scenarios. I know it's 6:00, so I just have one (1) follow-up question on some of the earlier evidence, and then we can take the break.

So, Dr. Simpson, I had asked you a few minutes ago about the -- the minimum probability -- or the probability level tied in with the minimum and of the range. And you had said you thought -- and you referenced some evidence from a few years ago that one (1) in forty (40) was too conservative, and you've -- favour one (1) in twenty (20).

Can you give us a little bit more of the -- the why for that, other than that one (1) in forty (40) is too conservative?

1 DR. WAYNE SIMPSON: I'm trying to rec -
2 - I don't want to speak against what Professor Hum and
3 I discussed at that time, but I think the question here
4 is around -- it's not around the DCAT so much, right,
5 and -- and what the industry standard might be there
6 and -- and insolvency and so on. It's a question of
7 what motorists want to be insured against, and I don't
8 think they want to be excessively insured against rates
9 -- against rising or falling rates. So I think they
10 want a degree of rate stability. The only question is
11 how much that degree is.
12 And at the time, I think we questioned
13 whether one (1) in forty (40) captured that, or whether
14 it was probably better to use something like one (1) in
15 twenty (20). In other words, they're risk averse, but
16 they're not that risk averse. And some of them may not
17 be risk averse at all. I mean, some people -- some
18 people gamble. That's not risk averse.
19 MS. CANDACE GRAMMOND: So would it be
20 your view that consultation with motorists should be
21 done for both the minimum and the maximum end of the
22 range?
23 DR. WAYNE SIMPSON: Oh, yeah. If that
24 -- if that were the route you went, you would want to
25 do it for both ends, yeah. You know, how much

1 insurance do you want? What's kind of a minimum?
2 What's kind of a maximum? would be the kinds of
3 questions you'd want to try to get at.
4 MS. CANDACE GRAMMOND: Thank you. So,
5 Madam Chair, I think we can take the -- the dinner
6 break. I can indicate that I'm more than a third but
7 not quite halfway through, so I'll probably have about
8 -- I'm going to ballpark -- forty-five (45) minutes
9 when we resume.
10 So I don't know if we want to break for
11 half an hour or break for forty-five (45) minutes, but
12 I'm in the Board's hands either way.
13 THE CHAIRPERSON: What does the group -
14 - yes, Kathy -- Ms. Kalinowsky, pardon me.
15 MS. KATHY KALINOWSKY: It's been a long
16 day, so we're all getting rather chummy with each other
17 here. But we'd be prepared to continue going if --
18 without a break even if that's a possibility.
19 THE CHAIRPERSON: We could -- how about
20 half an hour, and then we'll come back and resume. Is
21 that okay? Security guard is here from 6:00 to 6:45,
22 but we'll come back at 6:30.
23
24 --- Upon recessing at 6:01 p.m.
25 --- Upon resuming at 6:34 p.m.

1 THE CHAIRPERSON: Well, we're going to
2 begin again with cross-examination by Ms. Grammond.
3 MS. CANDACE GRAMMOND: Thank you, Madam
4 Chair.
5
6 CONTINUED BY MS. CANDACE GRAMMOND:
7 MS. CANDACE GRAMMOND: So, Dr. Simpson,
8 I have a few questions for you about the equity decline
9 scenario. So this is what I think is slide 13 of your
10 PowerPoint. I just put my own little handwritten
11 numbers on it. Okay. So it must be -- it's not this
12 slide. It's the next slide, so it must be slide 14 in
13 the electronic version.
14 DR. WAYNE SIMPSON: The rebound?
15 MS. CANDACE GRAMMOND: Pardon me?
16 DR. WAYNE SIMPSON: The rebound effect,
17 or rebound?
18 MS. CANDACE GRAMMOND: No, no. This is
19 the one. The one that's up on the screen --
20 DR. WAYNE SIMPSON: Okay.
21 MS. CANDACE GRAMMOND: -- is the one,
22 yeah. Okay. So as you've stated here in this slide,
23 the previous DCAT put forward by MPI used a four (4)
24 year equity decline scenario. That's been replaced in
25 the current DCAT with a one (1) and two (2) year equity

1 decline scenario that ignores the recovery in markets,
2 in -- in essence.
3 Is that right?
4 DR. WAYNE SIMPSON: The third and
5 fourth year returns, yeah.
6 MS. CANDACE GRAMMOND: Okay. Do you
7 consider the two (2) year equity decline scenario to be
8 plausible?
9 DR. WAYNE SIMPSON: Well, I'm not
10 exactly sure what you're asking there. The two (2)
11 year equity decline is -- is plausible for a two (2)
12 year horizon, that is.
13 But you're looking at a four (4) year
14 horizon, which means you have to take account of the
15 fact that if -- if equities decline over the first two
16 (2) years, what happens to them in the next two (2)?
17 So the four (4) year reflects the horizon --
18 MS. CANDACE GRAMMOND: So --
19 DR. WAYNE SIMPSON: -- of the -- of the
20 scenario to 2018/'19.
21 MS. CANDACE GRAMMOND: So would it be
22 fair to say that, in your view, the two (2) year equity
23 decline scenario as presented overstates the adverse
24 impact?
25 DR. WAYNE SIMPSON: Yes.

1 MS. CANDACE GRAMMOND: And do you
2 recommend that the equity decline scenario should
3 incorporate the rebound effect after a major market
4 decline based on how markets would typically react?
5 DR. WAYNE SIMPSON: That's right, based
6 on the evidence, yes.
7 MS. CANDACE GRAMMOND: Okay. Those are
8 my questions on the equity decline scenario. Next is
9 the high-loss ratio risk scenario, which I think is the
10 next slide. And so I'm not going to take you to
11 something specific on the screen. It's just there for
12 reference.
13 In your report -- and if we need to go
14 there, you say so -- you question the use of Basic
15 claims experience since 2001. And you say that that's
16 because it is based on only thirteen (13) annual
17 observations.
18 Do you recall that from your report?
19 DR. WAYNE SIMPSON: Right.
20 MS. CANDACE GRAMMOND: Would you agree
21 that each of those annual observations is actually
22 comprised of thousands of individual claims, each of
23 which contributes to the estimation of the underlying
24 probability distributions for simulation purposes?
25 DR. WAYNE SIMPSON: Yes.

1 MS. CANDACE GRAMMOND: And how many
2 years of Basic claims experience would you consider to
3 be sufficient and appropriate for this purpose?
4 DR. WAYNE SIMPSON: I think I'm going
5 to backtrack on the previous answer because maybe I
6 didn't understand what you were getting at. You've got
7 a lot of information, but the -- the evidence that
8 you're using is the -- the claims outcomes costs for --
9 annually, right?
10 And that allows you, for example, to
11 situate the 2013/2014 claims number on a distribution.
12 So those are annual data. So you've only got thirteen
13 (13) observations that you're actually using to fit the
14 distribution of claims costs outcomes on an annual
15 basis, as -- as I understand what's happening here.
16 So it is true that underlying that are
17 thousands and thousands of claims, but you're not
18 analyzing the individual claims. You're analyzing the
19 annual costs --
20 MS. CANDACE GRAMMOND: But --
21 DR. WAYNE SIMPSON: -- of those claims
22 and putting it in -- them into a distribution.
23 MS. CANDACE GRAMMOND: But you would
24 agree that each of those individual claims contributes
25 to the estimation of the underlying probability

1 distributions?

2 DR. WAYNE SIMPSON: Sure. Yes, yes.

3 And you could model in that fashion, you know, the

4 outcome, yes, exactly. I -- I thought, well, you could

5 do it monthly, but in fact you could do it as every

6 claim comes in.

7 You could -- you could place that claim

8 on a distribution, and then the number of years doesn't

9 matter. You'd have -- you'd have an awful lot of

10 information that you'd be using. You'd -- you'd have

11 to then convert that distribution of claims into an

12 annual claims cost, which I presume could be done.

13 MS. CANDACE GRAMMOND: So do you have a

14 view on how many years of claims experience should be

15 used?

16 DR. WAYNE SIMPSON: If the data is

17 relevant, more than -- more is -- is better in the

18 sense that thirteen (13) is not very many points to try

19 to get an accurate picture of what a distribution looks

20 like.

21 If you think about it, you're talking

22 about things like a one (1) in forty (40) event. Well,

23 it's hard to think of a one (1) in forty (40) event

24 when only -- you only have thirteen (13) observations

25 to -- to do it. So if you're thinking of a one (1) in

1 forty (40) event, you'd probably want more than forty
2 (40) observations.
3 You could, for example, do it on a
4 monthly basis. You'd have two hundred and sixty (260)
5 observations. And then you'd have to worry about the
6 monthly seasonality issues arising from that.
7 This is the easy way to do it, and I
8 think there's some statistical questions about whether
9 it gives you the kind of reliability you'd want to have
10 to -- to fit a -- a distribution on a one (1) in twenty
11 (20) or one (1) in forty (40) probability.
12 MS. CANDACE GRAMMOND: Just a moment.
13 DR. WAYNE SIMPSON: I don't know if
14 that answers your question. Sorry.
15 MS. CANDACE GRAMMOND: I'm getting a
16 message here that this computer needs to be plugged in.
17 I don't want to lose Mr. Pelly, so we need to just plug
18 this computer in. I'll -- I'll keep going. Okay. So
19 I -- and he says he doesn't want to be lost.
20 MR. BYRON WILLIAMS: Ms. Grammond --
21 Ms. Grammond, can you actually see him?
22 MS. CANDACE GRAMMOND: No, I can't see
23 him. He can hear everything that we're saying, and
24 then he can type back.
25 MR. ROGER CATHCART: We've turned the

video off.

MS. CANDACE GRAMMOND: Yeah. The video was on. There was -- earlier we had the video on and we had the computer turned so he could see the screen.

MR. BYRON WILLIAMS: If you can put him just up on the screen for a couple of seconds, that'd be awesome, in his pajamas or something.

MS. CANDACE GRAMMOND: I don't know. I'm sure he's laughing, but he's not typing anything, so I don't know.

UNIDENTIFIED SPEAKER: No ha-ha.

MS. CANDACE GRAMMOND: Yeah. No. Oh, I think maybe he's going to say, "LOL." Wait. What does that stand for?

MR. ROGER CATHCART: ROFL?

MS. CANDACE GRAMMOND: I don't know. Oh, ROFL, rolling on the floor laughing. Okay. Back to work. Back to work.

CONTINUED BY MS. CANDACE GRAMMOND:

MS. CANDACE GRAMMOND: The -- the interest rate decline scenario, Dr. Simpson, which I think is two (2) slides ahead from where we are, you are recommending that the stagflation period be excluded from consideration.

1 That's right?
2 DR. WAYNE SIMPSON: Yes. Not only
3 that, but that in particular.
4 MS. CANDACE GRAMMOND: Sorry. He -- I
5 have to just say this. So he says, "ROFL." Then he
6 says what it is, "Roll on floor laughing." And then he
7 says, "duh." He can hear that we don't know what it
8 means. Okay. Sorry.
9 So, Dr. Simpson, back to work. You --
10 you recommend that the stagflation period be excluded
11 from consideration in the interest rate decline
12 scenario.
13 DR. WAYNE SIMPSON: Well, it seems the
14 most inappropriate to base interest rate declines on,
15 yes.
16 MS. CANDACE GRAMMOND: And do you have
17 a view of the extent to which the inclusion of that
18 period is impacting the target and by how much?
19 DR. WAYNE SIMPSON: No.
20 MS. CANDACE GRAMMOND: Can you give us
21 an indication directionally of how you believe the
22 inclusion of the stagflation period is affecting the
23 target?
24 DR. WAYNE SIMPSON: Well, it -- it's
25 not -- excluding that -- that piece will not increase

1 the target; whether it decreases the target just
2 depends on how quickly the floor that they set bites.
3 And that bites pretty quickly the way that it is set up
4 now, so it may not have any effect. So then I would
5 have questions about whether that -- that whole
6 construction scenario makes much sense.
7 But you would expect that the RSR would
8 be less -- the proposed RSR would be less than 194
9 million if you -- if the floor did not bite and you
10 took out the high inflation, high interest rate periods
11 -- the high interest rate periods, I'm sorry.
12 MS. CANDACE GRAMMOND: And are there
13 any other time periods that you are suggesting be
14 excluded from the analysis?
15 DR. WAYNE SIMPSON: Well, in -- in
16 response to the PUB(CAC) 1-4, I think it was, I also
17 asked deleted the decades before and after the great
18 stagflation just because interest rates, they are also
19 in the order of 7 or 8 percent over the whole decade,
20 and therefore quite a bit higher than -- than the
21 period we have dealt with recently. And that would
22 just really include only the first decade of the data,
23 and of the last eight (8) years are the only two (2)
24 really low interest rate periods.
25 And so I -- one (1) of the things I did

1 was calculate what that would be. And that does make
2 quite a difference. I think I said the floor, even
3 such as it's constructed in this scenario, doesn't bite
4 then until the third year. So, certainly, the
5 implications are that the proposed -- the RSR would be
6 smaller, the target RSR would be smaller in that
7 circumstance.
8
9 (BRIEF PAUSE)
10
11 MS. CANDACE GRAMMOND: Okay. Can you
12 comment on the removal of the specific time frames from
13 the analysis and whether that has any effect on the
14 statistical validity of the analysis? Like if you
15 remove too much, doesn't it compromise the integrity at
16 some point?
17 DR. WAYNE SIMPSON: Well, this -- this
18 -- this whole scenario is problematic just because we
19 haven't been here before; certainly in this data set
20 from '56 on, we simply have never really been here
21 before.
22 I have trouble with the whole scenario.
23 So if you said to me at that point you might as, Well,
24 give up and think about some other way of introducing
25 the scenario or think about an alternative scenario and

1 just say we don't know here, we'd have to go about it
2 some different way, I would disagree.
3 I have trouble -- I have trouble
4 thinking that even with the con -- concerns I have
5 about the data -- in other words, dropping the three
6 (3) middle decades and then talking about the floor --
7 that you are getting anything approaching a
8 representation of what the really -- the one (1) in
9 forty (40) risk, it really is in terms of the interest
10 rate decline.
11 MS. CANDACE GRAMMOND: So what would
12 you say about using just the period of time after the
13 stagflation period?
14 Would that be enough data?
15 DR. WAYNE SIMPSON: Well, that includes
16 of that period from '86 to '95 -- is that right, '86 to
17 '95, which -- where interest rates remained a
18 relatively high and in some periods dropped fairly
19 dramatically. So whether that's appropriate to
20 today's, as I say, I don't know that any other period
21 that we faced in recent times. Maybe the most -- the
22 closest thing we have come to this was the Great
23 Depression, but that really isn't relevant either
24 because I think that was a different world, different
25 monetary policies and everything else. I think we are

in uncharted territory in terms of constructing a scenario of this type.

(BRIEF PAUSE)

MS. CANDACE GRAMMOND: So are you suggesting that if we are in new territory, that there is simply no historical basis upon which to do the analysis?

DR. WAYNE SIMPSON: No. There's -- there really is, no -- you know, the appeal to evidence doesn't always work. And in this case, it probably is as close to not working.

But I think the whole exercise of trying to make it work has shown why it doesn't work and generated a discussion about how relevant this particular scenario should be and consideration taken of it.

MS. CANDACE GRAMMOND: And if we used just the last twenty (20) years, that would be twenty (20) times twelve (12) data points, right? Twelve (12) months per year.

DR. WAYNE SIMPSON: Yeah.

MS. CANDACE GRAMMOND: Is that enough to be reliable for modelling, in your view?

1 DR. WAYNE SIMPSON: It's reliable, but
2 as I say, that decade before 2006, those interest
3 rates, if I remember correctly, are -- it's a new --
4 much higher interest rate era, much higher inflation
5 era -- some of it, anyway, late '90s -- than -- than we
6 face today. But it's better than including the great
7 stagflation and -- and the periods around it, sure.
8 MS. CANDACE GRAMMOND: Now, do you
9 believe that in the current interest rate environment,
10 it is reasonable to assume an interest decline scenario
11 from current levels for a sustained multi-year period?
12 DR. WAYNE SIMPSON: Well, as I said, I
13 -- I think if you asked consensus forecasters on that,
14 they would -- they would think that is imp -- more
15 improbable than one (1) -- one (1) in forty (40), and I
16 would agree with that.
17 I guess my agreeing with it is putting
18 words in their mouth too, so they haven't said that.
19 But if they did, I would agree with it.
20 MS. CANDACE GRAMMOND: Okay. Now, in
21 one (1) of the IRs that the Board asked of you after
22 receiving your report -- it's number 4, so PUB(CAC) 4,
23 and I'm sure if -- yeah. There we go. You say in the
24 response to (c) -- so if we can just go down a bit?
25 Yeah.

1 Just near the bottom of the screen,
2 you'll see a sentence that begins, "My unease about
3 this scenario"?
4 DR. WAYNE SIMPSON: M-hm.
5 MS. CANDACE GRAMMOND: You're with me?
6 DR. WAYNE SIMPSON: Oh, okay. Yeah.
7 MS. CANDACE GRAMMOND: Yeah.
8 DR. WAYNE SIMPSON: The -- this -- I --
9 I -- so I did, in fact, express this here. I said I
10 had never expressed this, but in fact, I have expressed
11 this, yes.
12 MS. CANDACE GRAMMOND: Okay. So you
13 say:
14 "My unease about this scenario might
15 be summarized as follows. Would the
16 consensus forecasters of interest
17 rates believe in the current economic
18 environment that there was a one (1)
19 in forty (40) chance that interest
20 rates would fall to 1.68 percent and
21 stay there for a period of one (1) to
22 four (4) years? I think the
23 consensus answers to this question
24 would be, No."
25 DR. WAYNE SIMPSON: Yeah.

1 MS. CANDACE GRAMMOND: Okay.
2 DR. WAYNE SIMPSON: That's a good
3 summary of what I -- what I --
4 MS. CANDACE GRAMMOND: Okay.
5 DR. WAYNE SIMPSON: -- tried to say.
6 MS. CANDACE GRAMMOND: So from your
7 response there and the evidence that you've given
8 today, are you suggesting that the interest rate
9 decline scenario as constructed and presented by MPI is
10 not plausible?
11 DR. WAYNE SIMPSON: Yes. That's my
12 point.
13 MS. CANDACE GRAMMOND: And can you just
14 confirm why you hold that view?
15 DR. WAYNE SIMPSON: It -- it's based on
16 an analysis of data that I don't think is credible,
17 because a lot of it comes from high interest rate
18 periods, so the interest rate declines are exaggerated.
19 It's based on the adoption of a floor which is, I
20 think, questionable in terms of its use of monthly data
21 to forecast a four (4) year floor. And to elaborate on
22 that, we're in a territory where we haven't been
23 before, where interest rate declines are less
24 predictable than they would be if we'd experienced this
25 in the past.

1 MS. CANDACE GRAMMOND: So coming back
2 to what we were speaking about a few minutes ago, if
3 the stagflation period was removed from the analysis,
4 do you believe that your concerns would be alleviated
5 about this --
6 DR. WAYNE SIMPSON: No.
7 MS. CANDACE GRAMMOND: -- particular
8 scenario?
9 DR. WAYNE SIMPSON: No. That was the
10 first thing that jumped out at me, and I -- I have
11 perhaps overemphasized that. But that alone -- it was
12 simply the most obvious and quickest thing to identify,
13 since -- since I lived through that.
14 MS. CANDACE GRAMMOND: But not the only
15 issue in your view?
16 DR. WAYNE SIMPSON: Not the only thing,
17 because the numbers you get still are -- are, to me,
18 not plausible.
19 MR. REGIS GOSSELIN: Is that because of
20 the Canadian situation? You know, while you were --
21 while you were talking about your early testimony, I
22 had pulled up interest rates in Germany, and Sweden,
23 and Switzerland, where they have, in fact, negative
24 retail rates for interest, so.
25 DR. WAYNE SIMPSON: Negative nominal?

1 MR. REGIS GOSSELIN: Yes.
2 DR. WAYNE SIMPSON: How is that
3 possible?
4 MR. REGIS GOSSELIN: That's what exists
5 in Germany, and Sweden, and Switzerland. So look at it
6 from our perspective. Clearly, there's a business risk
7 that rates will remain low. So you are suggesting that
8 because we don't have evidence, given uncharted waters,
9 we should just ignore it. We should just use Kopstein
10 or the business risk.
11 And yet it's a very real risk because if
12 interest rates do not materialize as expected, there's
13 going to be a loss on the balance sheet. There's going
14 to be a loss on the income statement.
15 DR. WAYNE SIMPSON: M-hm.
16 MR. REGIS GOSSELIN: So I think, as a
17 panel, I'm having difficulty trying to reconcile the
18 notion that we should ignore interest rates, because it
19 has an impact both on -- on income, but it also has an
20 impact on reserve levels. And so...
21 DR. WAYNE SIMPSON: Well, we do have --
22 we do have some experience with what has happened to
23 the consensus forecast. I think the comment was made
24 that the consensus forecast has been wrong five (5)
25 years in a row. We have some idea of where that has

1 gone, and there's a distribution of outcomes on that
2 forecast. That presumably provides us with some
3 information.
4 The forecasts were primarily wrong on
5 interest rates rising, not on interest rates falling.
6 Whether that can be used to tease out a reasonable
7 scenario about what might happen if they're wrong again
8 and -- and the interest rates rise, which everybody
9 sees as inevitable, is deferred.
10 You know, what's the probability of --
11 of that happening? I suspect the probability of that
12 happening is not -- is not that low. It's probably
13 some reasonable probability, but it's not 50 percent
14 because it's not the consensus forecast.
15 MS. SUSAN PROVEN: I wanted to ask you
16 a little bit about what you think when it comes to
17 consumer debt ratios, which we know are high, 160
18 percent, and then the government debts. And there's
19 lots of governments with debt.
20 And I wonder about how that links to the
21 interest rate. Is there a link? Because I'm sure
22 governments aren't keen to raise or see a rise in the
23 interest rates because they know this is going to be
24 problematic for a lot of people.
25 DR. WAYNE SIMPSON: M-hm.

1 MS. SUSAN PROVEN: So I -- I just
2 wonder, given that situation, what do you think? How
3 long would this go on? And is it sustainable? Because
4 --
5 DR. WAYNE SIMPSON: Well, I mean, debt
6 makes the market, right? Because --
7 MS. SUSAN PROVEN: Right.
8 DR. WAYNE SIMPSON: -- for -- for
9 debtors, there's lenders, and that's what makes the
10 market.
11 MS. SUSAN PROVEN: And it keeps the --
12 our economic -- our commercial, what, free enterprise
13 system going. So, I mean, we're not going to have
14 people working unless people are buying. And people
15 are buying with money they don't have.
16 So I'm just saying that, you know, as
17 long as you can keep this going, everything's fine.
18 And I -- and we heard a lot of frustration from the
19 Corporation about the fact that the five (5) major
20 banks that they rely on for the interest rate forecasts
21 have been promising an increase. But that increase
22 hasn't materialized.
23 And given that -- and I think we all
24 know that -- I just wonder, you know, how long -- like,
25 can this go on forever? You're the economist. That's

1 why I'm asking the question.
2 DR. WAYNE SIMPSON: Can this go on
3 forever? Well, not very likely because that has never
4 happened. A situation doesn't stay stable and things
5 do change.
6 You asked about the -- the debt. I'm
7 not sure that -- that consumers are being as irrational
8 as some people suggest because what they're responding
9 to is -- is the -- is the very fact that interest rates
10 are low. In other words, debt is cheap.
11 MS. SUSAN PROVEN: M-hm.
12 DR. WAYNE SIMPSON: And governments
13 don't necessarily react in quite the same way. But
14 remember also that the government is not in control of
15 monetary policy. It -- there's monetary policy
16 independence. And I think what's being pursued, the
17 low interest rate policy, is really the Bank of Canada
18 doing what it can to provide sufficient stimulus to the
19 economy in keeping with its inflation target. So
20 that's -- that's one (1) part of it.
21 But the other part of it is, from the
22 standpoint of -- of borrowers, they're -- they're
23 borrowing like crazy because debt is cheap. And the --
24 the -- what they've tried to do to choke some of that
25 off in -- in certain housing markets, of course, is

1 tried to increase the requirements for down payments,
2 which is just about the only thing you can do because
3 you can't convince people they shouldn't borrow if debt
4 is cheap and they think they should. And that's what
5 they're doing.
6 MR. BYRON WILLIAMS: Madam Chair, just
7 because Chairperson Gosselin had asked some interesting
8 questions, I wonder -- I've just -- I grabbed from the
9 monetary policy report what they're saying about German
10 and -- and other bonds. And so I guess I have two (2)
11 things -- well, I'll -- with your permission, I'll --
12 I'll provide -- provide that to Dr. Simpson and he can
13 either offer some commentary about it now. Or if you'd
14 like to respond to the Chairperson's question, which
15 our client agrees is a very important question, we
16 could also offer some more thought by an undertaking.
17 So I was just grabbing, with your
18 permission, I -- I knew I had read it very recently
19 and, with your permission, I'll sure that with him
20 anyways.
21 If we could just have a couple of
22 minutes.
23 THE CHAIRPERSON: That will be fine.
24
25 (BRIEF PAUSE)

1 MR. BYRON WILLIAMS: And just for the
2 Board's information, I was bringing to Dr. Simpson's
3 attention something he'd brought to my attention. It
4 is the Bank of Canada October monthly reports. And I
5 think pages 3 and 4 have a bit of a discussion on that.
6
7 (BRIEF PAUSE)
8
9 DR. WAYNE SIMPSON: Yeah, you can put
10 this up, page... Page 4.
11 Now what is -- am I on? Yeah, what it
12 says just before that on page 3, essentially, is that
13 the US has announced that it is going to end what has
14 been referred to as a quantitative easing, which means
15 it's going to stop buying bonds. And that's going to
16 put up some -- some pressure on interest rates. And
17 that's why when you look at the interest rate forecasts
18 that are associated with charts like 5 and 6, you can
19 see that the -- the trends are upward. I mean, that's
20 the kind of scenarios that people envisage.
21 Now, that is a little bit different from
22 the scenarios that have been discussed before because
23 this is the first time the US has actually made an
24 announcement that they are going to end the
25 quantitative easing, which has been going on since the

-- since the recession.

And as US interest rates go up, Canadian interest rates, I would expect, are likely to follow. But this is -- this is a gentle rise over time.

If you look at Chart 6, for example, the next one. So you can see that -- that for the US it goes from all the way up to 2 percent from under a 1/2 percent and they see Canada responding -- being overtaken by the US. But our interest rate's rising -- the -- the policy rate rising from -- from 1 percent to about 1.6 percent. And so other rates will follow in concert to this.

This is -- this is the best forecast of what is -- is likely to happen, but it's backed by this specific announced intention of the US to reduce the stimulation in its monetary policy by limiting the monetary -- the quantity of easing.

MR. REGIS GOSSELIN: What I was getting at -- okay. There's two (2) effects, here. One (1) -- one (1) is using interest rate forecast to establish the appropriate Rate Stabilization Reserve, and there's the interest rate forecast that goes into determining how much income they're going to earn for the investments. Hence, it's critical to the setting of rates. So pretty clear from the evidence that's before

1 us that the rate level's that's being requested, namely
2 3.4 percent, is -- is not going to address the -- the
3 outcome that's being projected, which is getting the
4 ship back on even keel, because they're not generating
5 enough revenue to cover the -- the costs that they're
6 incurring on a go -- on a immediate basis.
7 So setting aside the issue around the
8 Rate Stabilization Reserve and the -- whether or not
9 the -- the interest rate scenarios are plausible, let's
10 say you leave that one aside for -- for the time being.
11 The -- what you're proposing is to feather in the rate
12 increases in the face of evidence that's before this
13 panel that -- that the rates being requested are
14 justified by revenue levels that are inadequate.
15 And so I'll -- I'll -- let me -- let's
16 leave aside the issue around the Rate Stabilization
17 Reserve. Let's talk about interest rate forecasts as
18 it relates to the setting of rates on a -- on a two (2)
19 year basis.
20 DR. WAYNE SIMPSON: When we're talking
21 --
22 THE COURT REPORTER: Your mic, sir.
23 DR. WAYNE SIMPSON: Okay. We're --
24 we're talking about the base scenario in terms of the -
25 - the three point four-one-one-one (3.4111) versus one

1 point six (1.6), one point six (1.6), one point six
2 (1.6), one point six (1.6), not -- not the adverse
3 scenarios, right?
4 So there, the simple point was why don't
5 we plan for rate stabilization in the -- in the base
6 scenario, and then from there look at alt -- the alt --
7 adverse -- the alternative scenarios, the adverse
8 scenarios from that perspective?
9 MR. REGIS GOSSELIN: I'm not sure we're
10 talking about the same thing. You -- you went from an
11 argument around establishing what would be an
12 appropriate Rate Stabilization Reserve level, which is
13 one (1) thing.
14 But interest rate forecasts are also
15 used by the MPI to establish what they will generate as
16 far as income from their investments. And clearly, the
17 basis on which they are setting rates uses a forecast
18 which is not going to be achieved probably during the
19 rate -- during the -- the period that's before us.
20 So your suggestion to vary the rate
21 increase staggered over four (4) years, in the face of
22 evidence that we've seen to date, would mean that next
23 year there'll be a loss, which will, in fact, reduce
24 the reserve levels that they currently have.
25 So what we'd be doing, in effect, is

1 punting the problem to a later group of policyholders,
2 and that's why I have trouble with what you're
3 suggesting as far as a recommendation to feather in the
4 rate increases.
5 MR. BYRON WILLIAMS: Mr. Chair (sic),
6 before Dr. Simpson answers, just -- I think there's a -
7 - a miscommunication here. He'll -- in the sense that
8 his commentary is in that section that was referred to
9 him by Ms. Grammond is about -- it's not about rates --
10 the rate setting or the rate forecasts for the GRA.
11 It's not opining on that. It's opining on the base
12 scenario in the model.
13 And so that -- so -- so I -- I -- he --
14 he may so -- if you go to that section, he's talking
15 about the base scenario within the model, as -- it's
16 not an opinion. He has not been reviewing the evidence
17 in this hearing. He's talking about in terms of the
18 base scenario that goes into the model, the analysis
19 that -- that should go -- go into it. And I think
20 that's the miscommunication, and --
21 MR. REGIS GOSSELIN: I guess what I'm
22 looking at is the second -- the second to last page of
23 his recommendations where he's clearly saying 1.6
24 percent over the next four (4) years.
25 DR. WAYNE SIMPSON: If you look at

1 slide 12 of my presentation, this is -- this is -- the
2 table's from the DCAT report. As I look at this, I see
3 earnings rebuilt to 154 million.
4 Now, I think your point here is that, if
5 you dropped '15/'16 to 1.6 percent from 3.4 percent,
6 you're not going to make $85 million. You're going to
7 make, well, considerably less than that. I'm not sure
8 where that number takes you because we haven't -- we
9 haven't looked at that scenario.
10 But my point was that we're going to get
11 somewhere close to the 154 million by '18/'19 unless
12 there's new information in the base scenario that's
13 been presented since the DCAT report.
14
15 (BRIEF PAUSE)
16
17 CONTINUED BY MS. CANDACE GRAMMOND:
18 MS. CANDACE GRAMMOND: Okay. So, Dr.
19 Simpson, my last set of questions to you were with
20 respect to the interest rate decline scenario
21 specifically. And in your report -- so not in your
22 PowerPoint, but in your written report -- you made the
23 comment that that particular scenario, interest rate
24 decline scenario, was not credible. And one (1) of the
25 reasons you gave was that interest rates have nowhere

1 to decline in the current economic situation of
2 historically low interest rates.
3 You recall that from your report?
4 DR. WAYNE SIMPSON: Yeah. I think
5 that's a common view and kind of expresses the view of
6 -- of forecasters, that -- that interest rates will go
7 up eventually because they won't go down.
8 MS. CANDACE GRAMMOND: So your reason
9 for making that statement that interest rates have
10 nowhere to decline is based on what you're learning
11 from forecasters?
12 Is that fair to say?
13 DR. WAYNE SIMPSON: Right. That's my
14 sense of -- of what I've read, yes.
15 MS. CANDACE GRAMMOND: Now, do you have
16 an issue with the time frame of four (4) years that's
17 being utilized in this scenario?
18 DR. WAYNE SIMPSON: No. No, I don't
19 think I -- that's been the standard for quite a long
20 time, and the DCAT reports use a four (4) year -- four
21 (4) year horizon. The further you look out, the less
22 accurate you're going to be anyway, so it doesn't make
23 sense to look too far ahead. This seems like a
24 reasonable horizon to me.
25 MS. CANDACE GRAMMOND: Okay. So you

1 don't have an issue with the time frame. We've talked
2 about the removal of the stagflation period as
3 something you've identified as a necessary change.
4 Are there any other changes that you
5 would suggest to fix this scenario for you?
6 DR. WAYNE SIMPSON: Well, I mean, I
7 think -- I think the floor is -- is too low. The -- I
8 think -- I -- I produced numbers from the same series
9 that suggest two point five-three (2.53) instead of one
10 point six (1.6).
11 I mean, that's illustrative that -- I
12 just think a sustained floor of -- of one point six
13 (1.6) is -- is not credible based on the evidence
14 available, because you're looking at a monthly minimum
15 of the entire series and assuming that it can be
16 sustained for forty-eight (48) months, when the
17 evidence is that the lowest forty-eight (48) month rate
18 is considerably higher than that.
19 MS. CANDACE GRAMMOND: So you're saying
20 to use the average -- or the -- sorry, the -- the low
21 from the four (4) year average as opposed to the
22 monthly low?
23 DR. WAYNE SIMPSON: The lowest four (4)
24 year average.
25 MS. CANDACE GRAMMOND: The lowest four

1 (4) year average.

2 DR. WAYNE SIMPSON: It's also the case,

3 the way they construct these series, that they base it

4 on the close on a particular Wednesday of the month.

5 And, you know -- so -- so essentially, that minimum,

6 that monthly minimum, is -- is possibly a one (1) day

7 minimum, not a monthly minimum. I don't know. What

8 happened the rest of the month?

9 Interest rates don't usually move too,

10 too much too quickly, down or up, with the exception of

11 times like the great stagflation, of course.

12 MS. CANDACE GRAMMOND: Now, we've been

13 speaking about your concerns with respect to the

14 interest rate decline scenario.

15 Do you have the same concerns with

16 respect to the combined scenario because of the

17 dominant adverse circumstance within that scenario

18 arising from interest rate decline?

19 DR. WAYNE SIMPSON: The interest rate

20 decline is a part of that scenario. It is the most

21 adverse scenario. The results of the interest rate

22 decline and the combined scenarios are virtually

23 identical. And so my conclusion, unless I see evidence

24 to the contrary, is that that is what is driving that

25 scenario, yes.

1 MS. CANDACE GRAMMOND: So do you have
2 suggestion as to how the combined scenario should be
3 constructed in a way that is different from what we
4 have?
5 DR. WAYNE SIMPSON: Well, the changes
6 to the interest rate decline scenarios would -- would
7 affect that.
8 MS. CANDACE GRAMMOND: So if you fix
9 that, you'll fix both?
10 DR. WAYNE SIMPSON: Both the floor and
11 the exclusion of the great stagflation and other high
12 interest rate periods.
13
14 (BRIEF PAUSE)
15
16 DR. WAYNE SIMPSON: It struck me when I
17 was looking at that combined scenario that the kind of
18 simulations that are done there could be done for all
19 of the risk factors included, and you'll get a
20 distribution of financial outcomes which would form the
21 basis for thinking about a plausible range for the rate
22 stabilization reserve, rather than restricting it to
23 those -- those three (3) outcomes.
24 MS. CANDACE GRAMMOND: Thank you. I'm
25 going to move then to some questions about the MCT

1 ratio. So, Dr. Simpson, I know you gave a little bit
2 of evidence earlier with respect to the role of MPI and
3 its status.
4 Can you give us a little bit of
5 elaboration on the characteristic differences between a
6 Crown corp, such as MPI, and a private-sector insurer
7 regarding the applicability of MCT?
8 DR. WAYNE SIMPSON: Private-sector
9 insurer has to worry about the rates that others
10 competitors are setting. And if they set a rate that
11 is too high, they will lose business; if they set of
12 rate that is too low, they'll get probably more
13 business then they can handle and at rates that
14 probably lead to losses. So they have to worry about
15 what others are doing.
16 And so that differs from MPI because MPI
17 can appeal to this Board for -- for rates and justify
18 it on the basis of their -- of their business, and they
19 don't have to worry about competitors taking their
20 business if they set a rate that is too high.
21 In terms of solvency, a private insurer
22 is subject to the bankruptcy laws of the reg --
23 jurisdiction, whereas I don't think of those apply to -
24 - to MPI. I don't think anyone contemplates that MPI
25 is going to be insolvent. There's going to be measures

1 taken by MPI or by its backer, which is, essentially,
2 the Government of Manitoba and the Province of
3 Manitoba, to make sure that doesn't happen.
4 MS. CANDACE GRAMMOND: And I appreciate
5 your comments on solvency with respect to that.
6 In terms of the applicability of the MCT
7 though, are rates and competition really a factor, or
8 were you just giving me a main difference between MPI
9 and a private-sector insurer?
10 DR. WAYNE SIMPSON: Well, that drives
11 the question of capital adequacy, because capital
12 adequacy is around the question of -- of avoiding
13 bankruptcy and not having to take drastic measures
14 which would cost you business.
15 MS. CANDACE GRAMMOND: Thank you. Now,
16 in one (1) of your earlier reports provided to the
17 Board -- and it's cited on page 7 of your current
18 report -- you made the statement that:
19 "It was, therefore, questionable
20 whether the test, the MCT, was
21 applicable to a public Crown
22 corporation with monopoly over basic
23 insurance."
24 Maybe -- we just need to go down a bit,
25 yeah. So within the quote from your earlier report,

1 it's in the -- roughly in the middle of that first
2 complete paragraph of the quote, what I just read in.
3 So my question is:
4 Is your concern about applicability
5 really about the minimum capital test itself, or is it
6 about the interpretation of the calculated MCT ratios?
7 DR. WAYNE SIMPSON: I'm not sure what
8 you are asking here. What I'm -- I guess -- the point
9 was, should you apply the kinds of MCT targets, say 100
10 percent, that might apply in the private sector to --
11 to MPI? And I was drawing a distinction based on the
12 nature of their business and their ability to raise
13 rates and not lose market share.
14 They're obviously not going to lose
15 market share based on their rates, as a -- as a -- a
16 private insurer would or could.
17 MS. CANDACE GRAMMOND: I -- I guess
18 what I was trying to distinguish between was the
19 applicability of the test as opposed to the selection
20 of the ratio.
21 DR. WAYNE SIMPSON: The test falls out
22 of the DCAT. So in a sense, I don't necessarily
23 distinguish the two (2). In fact, I think earlier
24 today there was a reference to the fact that I'd put
25 DCAT/MCT. I mean, the MCT is a quick calculation from

1 -- from the -- from the DCAT, right? So the two (2)
2 aren't -- can be linked.
3 So I wasn't -- I wasn't -- you know, I
4 wasn't drawing a distinction to that -- to that
5 process. I -- that -- that's -- they're one (1) and
6 the same.
7 MS. CANDACE GRAMMOND: Okay.
8 MR. REGIS GOSSELIN: You just said
9 something that -- I -- I understood the DCAT at the
10 upper level to be based on the plausible scenarios, one
11 (1) in a hundred (100).
12 MCT is based on a different set of
13 calculations, isn't it?
14 DR. WAYNE SIMPSON: If -- if you used a
15 one (1) in one hundred (100) risk tolerance to generate
16 a -- an upper minimum, then it would be associated with
17 some -- you'd cal -- you'd be able to calculate what
18 the implied MCT level was for that. It might be a
19 hundred, it might be something quite different from
20 that. But --
21 MR. REGIS GOSSELIN: But in a context
22 to what we've been discussing, MCT, in relation to the
23 industry --
24 DR. WAYNE SIMPSON: Yeah.
25 MR. REGIS GOSSELIN: -- other than MPI,

1 that calculation is based on a framework that has
2 nothing to do with plausible scenarios. It -- it
3 discounts asset values and so on, though --
4 DR. WAYNE SIMPSON: No, but any -- any
5 outcome of the financial model, which is what the --
6 the DCAT consists of the base scenario and then the
7 adverse scenarios, which are run through this financial
8 model. And one (1) -- and an outcome of the financial
9 model would then be the -- would be the implied MCT,
10 right? So that's how you'd get your -- your maximum
11 and your minimum if you applied the DCAT and applied
12 different risk tolerances. I think that's right, isn't
13 it?
14 The -- the reference I was making in the
15 combined scenario was a little -- sorry -- was a little
16 bit different because there, if you -- if you use the
17 different risk factors and use the at-risk methodology
18 to generate the simulations, then you'd have the
19 financial outcomes.
20 But in -- in picking off, say, the --
21 the one (1) in twenty (20) and the one (1) in one
22 hundred (100) values, just to take numbers for the
23 minimum and the maximum, then associated with those in
24 the -- in the financial model, I think you would have a
25 -- an MCT level -- target, minimum and maximum again.

1 But they would fall out of the
2 assessment of risks. They wouldn't be plucked out of
3 the air like 100 percent was some gold standard or 50
4 percent or 75 percent was a gold standard.
5
6 CONTINUED BY MS. CANDACE GRAMMOND:
7 MS. CANDACE GRAMMOND: So, Dr. Simpson,
8 are you recommending anything with respect to an
9 appropriate target level for a Basic MCT ratio?
10 DR. WAYNE SIMPSON: No. I don't feel
11 confident in -- in that -- in doing that, no.
12 MS. CANDACE GRAMMOND: And is it your
13 view that there is no value in using the MCT as a
14 yardstick for assessing Basic capital adequacy?
15 DR. WAYNE SIMPSON: Well, I guess one
16 (1) thing I am saying is that, if the pri -- private
17 insurers have a yardstick, then -- then the yardstick
18 for MPI and other public insurers should be lower. How
19 much lower, I -- I think is -- would just be
20 impressionistic on my part.
21 MS. CANDACE GRAMMOND: Okay. So on
22 that, you say in your report that any target for the
23 MCT, whether 100 percent or 50 percent or some other
24 number, remains arbitrary.
25 DR. WAYNE SIMPSON: M-hm.

1 MS. CANDACE GRAMMOND: If a
2 relationship could be established between a Basic MCT
3 ratio and a Basic capital target level, would that
4 arbitrariness be addressed, in your mind?
5 DR. WAYNE SIMPSON: Well, it -- it
6 would be if, in fact, the -- you're saying linking the
7 -- let's say, the RSR minimum and maximum arrived out
8 of a DCAT to MTC levels, then --
9 MS. CANDACE GRAMMOND: To the ratio --
10 DR. WAYNE SIMPSON: -- then I think
11 that is a useful additional piece of information you
12 get out of the -- out of the DCAT, but it wouldn't be
13 the fundamental piece. You wouldn't want to fixate on
14 those numbers. I wouldn't think you'd want to fixate
15 on the -- on this -- on the way in which the DCAT is
16 being done to generate the -- to express the risks that
17 the Corporation faces.
18 MS. CANDACE GRAMMOND: Okay. But if
19 you were able to utilize the outcome of the DCAT, or
20 the Basic capital target level if that is what you were
21 using, to establish the MCT ratio, then it would no
22 longer be arbitrary, right?
23 DR. WAYNE SIMPSON: No, it would be a -
24 - a figure that would be the result of a risk
25 assessment, that's right, yes.

1 MS. CANDACE GRAMMOND: Okay.
2 DR. WAYNE SIMPSON: I just meant that
3 picking some number before the -- for the fact, like
4 100 percent, was arbitrary. I didn't mean that
5 whatever came out of a risk assessment was arbitrary,
6 no. It is what it is. It is part of the -- it's --
7 it's -- it's an output of the risk assessment, just
8 like the -- the other aspects of the balance sheet.
9 MS. CANDACE GRAMMOND: Thank you. I'll
10 move then to a few questions about the continued use of
11 the current approach, the POP or the Kopstein approach
12 that we've been speaking about.
13 You say in your report that it's more
14 difficult to argue that this mechanical approach
15 captures the risks facing MPI. For that reason, you
16 say it's reasonable to argue that an alternative
17 approach to establish the RSR might be superior.
18 You recall that from your report?
19 DR. WAYNE SIMPSON: M-hm.
20 MS. CANDACE GRAMMOND: You're nodding,
21 so that's a 'yes'?
22 DR. WAYNE SIMPSON: Yes. Sorry, yes.
23 MS. CANDACE GRAMMOND: That's okay. Is
24 it your view that the PUB's current RSR target range
25 remains relevant because it is indexed to the growth

1 and annual premium of the Corporation, or of Basic?
2 DR. WAYNE SIMPSON: Well, I -- as I
3 said, I think that is a virtue of the system in that --
4 as I said, it is indexed to the volume of business.
5 And -- also as the volume of business grows, I think
6 the size -- the volatility of the business, which is
7 some sort of measure of -- of risk, which actually is
8 the measure that was -- the basis for the RA/VaR
9 approach, is also indexed to that.
10 So those two (2) elements are indexed.
11 On the other hand, it isn't -- if -- if -- if risk
12 change, and we've talked a lot about the risk changing
13 in terms of, for example, interest rates, maybe the
14 interest rate risk really has changed, then you want to
15 try to evaluate that. And there is nothing in the
16 Kopstein approach that would accomplish that.
17 MS. CANDACE GRAMMOND: Now, do you
18 believe that the current target approach provides
19 enough capital to withstand a plausible event of one
20 (1) in forty (40) years?
21 DR. WAYNE SIMPSON: The Kopstein
22 approach?
23 MS. CANDACE GRAMMOND: The current
24 target, yeah.
25 DR. WAYNE SIMPSON: Yes, for the equity

1 decline and for the high claims loss -- high -- high
2 loss ratio scenarios.
3 I have difficulty thinking about the
4 interest rate decline scenario, just because I don't
5 think it is credible.
6 MS. CANDACE GRAMMOND: Would you say
7 the same for each of the risk areas tested in the DCAT?
8 DR. WAYNE SIMPSON: By "the risk
9 areas," you mean the equity decline? Yeah, the --
10 MS. CANDACE GRAMMOND: Different
11 scenarios.
12 DR. WAYNE SIMPSON: Yeah, the -- yeah -
13 - for two (2) -- for two (2) the RSR -- of the Kopstein
14 RSR is adequate, and for two (2) it isn't. And so the
15 two (2) it isn't are just the two (2) that I think it's
16 very difficult to construct using the existing
17 evidence, a reasonable scenario for decline for
18 interest rate movements, negative interest rate
19 movements.
20 MS. CANDACE GRAMMOND: Would you agree
21 that the investment assets and the actuarial
22 liabilities of MPI are the main source of risk to Basic
23 capital levels?
24 DR. WAYNE SIMPSON: Yes.
25 MS. CANDACE GRAMMOND: And if the

1 investment assets and the actuarial liabilities are
2 growing faster than premium overall, do you believe
3 that the current RSR range is keeping up with the
4 growth of Basic?
5 DR. WAYNE SIMPSON: Not in -- not in
6 that scenario, no.
7 MS. CANDACE GRAMMOND: Okay, just a few
8 final questions. You've seen the, I assume, the draft
9 undertaking request that the Board circulated to the
10 parties, including MPI?
11 DR. WAYNE SIMPSON: What's the number?
12 MS. CANDACE GRAMMOND: It's not -- it
13 doesn't have a number.
14 DR. WAYNE SIMPSON: I think I have --
15 yes, I have -- yes, I have.
16 MR. BYRON WILLIAMS: And I'll present
17 it to Dr. Simpson to refresh his memory, but I'm -- I'm
18 quite confident his memory will be refreshed.
19 MS. CANDACE GRAMMOND: Sure.
20
21 (BRIEF PAUSE)
22
23 MR. BYRON WILLIAMS: You can proceed
24 with your -- your questions, yeah.
25 MS. CANDACE GRAMMOND: Perfect.

1

2 CONTINUED BY MS. CANDACE GRAMMOND:

3 DR. WAYNE SIMPSON: I -- I think I have

4 it, yeah. This is the Phase 1 DCAT scenarios --

5 MS. CANDACE GRAMMOND: Yeah.

6 DR. WAYNE SIMPSON: -- et cetera?

7 Yeah, yeah.

8 MS. CANDACE GRAMMOND: Yeah. That's

9 the one.

10 DR. WAYNE SIMPSON: Okay.

11 MS. CANDACE GRAMMOND: So included

12 within that draft document, there's a -- is a request

13 with respect to the modelling of the interest rate

14 decline risk, which is a -- an ask to change the

15 modelling approach from using percentage point

16 difference to using percentage differences based on a

17 shortened history of Government of Canada ten (10) year

18 bond rates to exclude the stagflation period. You're

19 familiar with that --

20 DR. WAYNE SIMPSON: Yes.

21 MS. CANDACE GRAMMOND: -- piece of --

22 DR. WAYNE SIMPSON: Yes. I read that.

23 Yeah.

24 MS. CANDACE GRAMMOND: Okay. Would the

25 approach reflected there address some or all of your

1 concerns with respect to the setting of assumptions for
2 the interest rate decline scenario in the DCAT?
3 DR. WAYNE SIMPSON: It would address
4 some. But as we discussed, and I think about this
5 scenario, less and less of it.
6 MS. CANDACE GRAMMOND: Okay. So you're
7 saying it would address some, but the more you think
8 about it, the 'some' is diminishing?
9 DR. WAYNE SIMPSON: Yeah. The portion
10 is diminishing.
11 MS. CANDACE GRAMMOND: Okay.
12 DR. WAYNE SIMPSON: Exactly.
13 MS. CANDACE GRAMMOND: Okay. And why
14 is that?
15 DR. WAYNE SIMPSON: Well, as I said, as
16 I thought the -- further about the floor, I think that
17 is a problem. And as I think generally about the
18 question of how -- of -- of what people would think of
19 this scenario who are consensus -- are the consensus
20 interest rate forecasters, the less I think that they
21 would find this plausible, even at one (1) in forty
22 (40).
23 But I'm not an interest rate forecaster,
24 so I'm -- I'm conjecturing. I just feel very
25 uncomfortable with this scenario, because the evidence

we have just doesn't help.

MS. CANDACE GRAMMOND: Okay. One of the other requests in that document is with respect to modelling of the equity decline risk. And that was a request to change the modelling to include a historically based post-decline recovery effect based on a shortened history of the S&P -- that's "S" and "P" -- composite total return index comparable to that currently used in the DCAT.

You recall reviewing that aspect of the document?

DR. WAYNE SIMPSON: Yes.

MS. CANDACE GRAMMOND: Would that approach address some or all of your concerns with respect to the setting of assumptions for the equity decline scenario?

DR. WAYNE SIMPSON: What -- what -- I don't know what a 'shortened history' means.

MS. CANDACE GRAMMOND: I -- a -- a shorter time frame. Shorter historical time frame.

DR. WAYNE SIMPSON: The specific question here, you're not going to get at this question by simply looking at, you know, correlations over time of int -- you're going to have to look at the specific equity declines that are sharp and that were -- so the

1 dis -- amount of the recovery is going to depend on the
2 amount of the decline. This is really the point.
3 And the adverse events, the -- the way
4 the DCAT is constructed to look for these adverse
5 events over one (1) and two (2) years, suggests that
6 there's sharp declines. And my point is that in those
7 circumstances, you're going to get sharp recoveries.
8 I'm not sure how you're going to capture
9 that, other than by looking at those periods in the
10 fashion that I have, or in more detail in the fashion
11 that I have.
12 MS. CANDACE GRAMMOND: Well, what if
13 the time frame used with that which is currently used
14 in the DCAT?
15 DR. WAYNE SIMPSON: One (1) in two (2)
16 years, or four (4) years?
17 MS. CANDACE GRAMMOND: Hang on. Oh,
18 okay. So the -- the time frame that excludes the pre-
19 1956 data.
20 DR. WAYNE SIMPSON: Oh. Okay. Well, I
21 --
22 MS. CANDACE GRAMMOND: Sorry.
23 DR. WAYNE SIMPSON: -- I -- yeah.
24 MS. CANDACE GRAMMOND: That's what I
25 thought it meant, but then your question threw me off.

1 DR. WAYNE SIMPSON: Yeah. That isn't -
2 - that isn't -- I mean, that's -- that's helpful
3 because you get smaller declines, which are more
4 representative of the modern era. But in terms of
5 estimating the recovery from those declines, you need
6 to have a -- a statistical process or simple
7 calculations that actually do that. And the four (4)
8 year -- the four (4) year horizon did that. Because,
9 of course, the four (4) ori -- horizon captured both
10 the declines and the recovery, at least roughly.
11 I don't know that the exact decline and
12 recovery is a four (4) year period, but at least it
13 reflected the horizon we're looking at, and it did show
14 that in fact that, over the four (4) years, the extent
15 of the annual decline was smaller than it would be over
16 one (1) or two (2) years, so you get some -- you -- in
17 other words, reflecting recovery.
18 MS. CANDACE GRAMMOND: Okay. Fair
19 enough.
20 DR. WAYNE SIMPSON: So I would say the
21 best way then to go would be to simply use the four (4)
22 year decline -- four (4) year horizon.
23 MS. CANDACE GRAMMOND: Okay. But with
24 such a statistical process to model the recovery, would
25 your concerns be addressed?

1 DR. WAYNE SIMPSON: It would. It
2 probably would amount to something like the same thing,
3 though, as using the four (4) years.
4 MS. CANDACE GRAMMOND: Okay. Just one
5 (1) last question with respect to the document that you
6 have in front of you. And I know you reviewed it prior
7 to today.
8 Do you have any recommendations to
9 improve what's contained within that document in terms
10 of requests for changes?
11 DR. WAYNE SIMPSON: I didn't make any,
12 but that was partly because of lack of time to really
13 go beyond where I had gone today.
14 MS. CANDACE GRAMMOND: Is that
15 something that CAC's going to provide?
16 MR. BYRON WILLIAMS: CAC would be
17 pleased to offer some advice about any additions to
18 this --
19 MS. CANDACE GRAMMOND: And, sir --
20 MR. BYRON WILLIAMS: -- by way of
21 undertaking. We'll seek the advice of Dr. Simpson.
22 MS. CANDACE GRAMMOND: Yeah. And --
23 and certainly it's not restricted to just Dr. Simpson's
24 input because I appreciate there are others that you
25 would consult with.

1 Okay. I think, Madam Chair, that that
2 concludes my cross-examination of Dr. Simpson. Mr.
3 Williams may have some re-examination before we close
4 for the day.
5 THE CHAIRPERSON: Mr. Williams, do you
6 have some re-direct?
7 MR. BYRON WILLIAMS: A few questions
8 just I hope to clarify a -- a bit of confusion that I
9 no doubt contributed to.
10
11 RE-DIRECT EXAMINATION BY MR. BYRON WILLIAMS:
12 MR. BYRON WILLIAMS: First of all, Dr.
13 Simpson, recalling that you were asked about the
14 plausibility of the one point six eight four (1.684) by
15 PUB counsel, assuming a 2 percent in -- inflation rate
16 target by the Bank of Canada, and taking into the --
17 into account the concept of negative yields, can you
18 offer any commentary about the plausibility of
19 sustained bond yields at less than the targeted
20 inflation rate?
21 DR. WAYNE SIMPSON: Well, you know,
22 inflation is a benchmark, and just as there's a lower
23 bound (sic) on nominal yields, there's some degree of
24 boundaries on negative real interest yields -- that is,
25 interest rate yields that are lower than the rate of

1 inflation, not at the policy end, you know, the
2 overnight bank lending rates, but certainly in the case
3 of -- of lenders and borrowers.
4 You take, for example, mortgage rates.
5 You say, What's the lower limit on mortgage rates?
6 Well, if -- if they are below the rate of inflation,
7 then the mortgage lenders are not doing as well as
8 presumably -- they're not even keeping up with
9 increases in their costs.
10 And what is likely to happen then is --
11 is they're either going to find alternative investment
12 instruments, alternative equities, bonds, and so on
13 that would offer them a better return is -- is their
14 likely response.
15 So it's hard to conceive -- I mean, you
16 know, the Fisher rule is that the average return on
17 investment is something like 3 percent over inflation,
18 probably less for secure bonds. But it's certainly
19 going to be something in addition to inflation, and --
20 and negative real returns on investment are like -- not
21 likely to be sustained over a long period of time.
22 MR. BYRON WILLIAMS: Number 2 and just
23 following up on questions from Chairperson Gosselin, in
24 preparing your report determining the Manitoba Public
25 Insurance Rate Stabilization Reserve, were you opining

1 or offering an opinion on the modelling and assumptions
2 going into the DCAT and the Rate Stabilization Reserve,
3 or did you consider your mandate to be broader to offer
4 an opinion on the merits of the General Rate
5 Application?
6 DR. WAYNE SIMPSON: Well, I think the
7 two (2) are related, and I didn't -- I focussed on the
8 former, but didn't exclude the latter.
9 MR. BYRON WILLIAMS: Okay. In terms of
10 the interest rate scenario and following up on
11 questions both by Ms. Grammond and -- and the panel,
12 are you saying don't test for interest rate risk, or
13 are you saying that more care should be exercised in
14 developing that analysis?
15 DR. WAYNE SIMPSON: Well, I -- you
16 know, I think the benchmark here is the high-loss ratio
17 that keeps -- it keeps coming up as -- as the third --
18 kind of the third risk in the -- but it is -- it is
19 based on the sense that claims are going to bounce up
20 and down.
21 And you're going to have some good years
22 and you're going to have some bad years, and a lot of
23 that's related to weather, a lot of it's related to
24 other things. That is -- some of these other
25 scenarios, I think there's a -- I guess what -- for

1 better -- want of a better term I'd use the sniff test.
2 And when I see them, I just say, like
3 the equity decline scenario last time, and I said,
4 Where are these numbers coming from? This time I said,
5 These interest rate declines are huge compared to where
6 we're at in terms of interest rates. And the fir --
7 next thing I say is, Where are they coming from? And
8 once I start looking, the whole thing smells.
9 MR. BYRON WILLIAMS: Fair enough, but -
10 - fair enough, but... Would you concede the legitimacy
11 in preparing a DCAT, and indeed the importance of
12 testing for interest rate risk?
13 DR. WAYNE SIMPSON: Yes. I -- I don't
14 have a definitive answer as to how it would be best to
15 do that within the confines of appealing to the
16 evidence that is -- that we've looked at.
17 MR. BYRON WILLIAMS: And, sir, in the
18 course of the undertaking, you would be prepared to
19 offer any additional thoughts you have?
20 DR. WAYNE SIMPSON: I'd try to think
21 about it, but I -- I'm not particularly optimistic.
22 But I -- I'll certainly try.
23 MR. BYRON WILLIAMS: Madam Chair, we
24 certainly appreciate the courtesy of everyone and the -
25 - the thoughtful questions by the panel, by MPI, and --

1 and Board counsel. And we have no further re-direct.
2 And we appreciate the Board's patience in hanging
3 around this late at night.
4 THE CHAIRPERSON: Thank you very much,
5 Mr. Williams. And on behalf of the panel, I'd like to
6 thank Dr. Simpson for joining us today as an expert
7 witness. And I know your testimony has given us a lot
8 to consider in our deliberations, so thank you.
9 DR. WAYNE SIMPSON: Thank you.
10
11 (WITNESS STANDS DOWN)
12
13 MS. CANDACE GRAMMOND: Just before --
14 THE CHAIRPERSON: Ms. Grammond...?
15 MS. CANDACE GRAMMOND: Yeah. Just --
16 just before we leave, and I'll send an email around
17 tomorrow for those that are not here, but here's the --
18 the plan, I think, for the next number of scheduled
19 days.
20 So Wednesday, the 12th of November, we
21 have IBAM coming at 9:00 a.m. with their witness.
22 Thereafter, we'll have cross-examination by Mr. Monnin
23 on behalf of Bike Winnipeg. We will then have a
24 presentation by ARM. I've told them to come for 1:00
25 p.m., plus or minus, I guess. We'll see how the day

1 goes.

2 Thereafter, we'll have any further

3 cross-examination for MPI in terms of follow-up on

4 answers to undertakings or -- and that may be by me or

5 by Intervenors. And then, if time permits on Wednesday

6 the 12th, I will do my closing comments. I'll have

7 them ready and, if -- if possible, I will.

8 Other than that, I think there's no

9 purpose for us to convene tomorrow or Thur -- or Friday

10 of this week. So with the panel's permission, and

11 subject to any other comments, I think we'll next get

12 together Wednesday, the 12th, at 9:00, go through the

13 order of proceedings as I've described them, and we'll

14 see about timing for Mr. Williams's close and the

15 comments -- closing comments of the other Intervenors

16 as well.

17 MR. BYRON WILLIAMS: And --

18 THE CHAIRPERSON: Mr. Williams, go

19 ahead.

20 MR. BYRON WILLIAMS: -- and I

21 appreciate this. We had had some discussions with My

22 Learned Friend, Ms. Kalinowsky, because our client is

23 mindful of -- of two (2) things: One is, how much time

24 it takes for them to prepare their argument, but also

25 the opportunity for MPI to fully canvass and -- and

1 provide full response.
2 For a variety of personal reasons, I
3 will not have quite as much time as I'd normally would
4 this weekend to prepare. I would have liked to be in a
5 position to give a closing argument on the 12th.
6 I'm hoping I can give some comfort to
7 Ms. Kalinowsky and MPI that we will do our very best to
8 have a detailed list of recommendations for the 12th
9 that we would share, at least, so you can -- I think
10 that's the most that I could offer, and I -- I'd hope
11 that would assist at least in some -- some way to
12 assist in preparation.
13 So just given the personal
14 circumstances, I am not sure we can do much better than
15 that.
16 MS. CANDACE GRAMMOND: So for
17 scheduling purposes then we'll likely have Mr. Williams
18 closing and the closing of other Intervenors on
19 Thursday the 13th. That may or may not take the whole
20 day. And then perhaps the MPI closing will commence at
21 noon on the Friday, but that's subject to Ms.
22 Kalinowsky's comments at that time and we'll see. It's
23 just a possibility.
24 MS. KATHY KALINOWSKY: Sure, that's --
25 we'll -- we'll see how things unfold. Would appreciate

1 getting anything earlier obviously from the CAC
2 counsel.
3 I would also say that on Wednesday we
4 might want to exercise our right for re-direct
5 examination, of course, as provided per the outline of
6 procedures.
7 MS. CANDACE GRAMMOND: Just one (1)
8 other thing. In terms of the outstanding undertakings,
9 I know I'm -- that they are all being worked on. To
10 the extent that they can be made available tomorrow,
11 Friday, Monday, that would be helpful just so that we
12 can review and then have any follow-up cross questions
13 on the Wednesday.
14 MS. KATHY KALINOWSKY: Yes, we'll try
15 and we'll submit them by email in the next few days.
16 MS. CANDACE GRAMMOND: Perfect.
17 THE CHAIRPERSON: Well, that ends our
18 proceedings for this evening. Thank you very much
19 everyone again. And I guess we will have a recess
20 until next Wednesday. So we'll see you there at 9:00
21 a.m. Thank you again.
22
23 --- Upon adjourning at 7:45 p.m.
24
25

1 Certified Correct,

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5 _____

6 Cheryl Lavigne, Ms.

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