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Overview

MPI should use the investment income on total equity in the calculation of the rate indication

Standards

Section 2620.01 of the Standards of Practice of the Canadian Institute of Actuaries states:

"The best estimate present value of cash flows relating to the revenue at the indicated rate should equal the best estimate present value of cash flows relating to the corresponding claim costs and expense costs, plus the present value of a provision for profit, over a specified period of time."

Standards

Normal, **best practice** to include the investment income on the surplus backing the book that you are pricing for as it is a revenue cash flow to that book.

In a private organization there are several different regions and products that you have to price for. There is a certain amount of capital that is held to support the book being priced for. The investment income on that capital would be taken into account when pricing that book.

There is no impact on the RSR from including Investment income from Total Equity in the Rate Indication

Using the return on total equity in the calculation of the indicated rate requirement does not take money out of the RSR.

It means that more is not added to it from investment income.

Transfers from Basic

The fact that capital has been transferred from Extension and/or SRE is not relevant to whether investment income on the RSR should be included in the rate indication

* Extension and SRE would not exist without Basic
* The profits from these lines should benefit the customers of MPI
* There is an intergenerational equity issue regardless if the money is from Basic, Extension or SRE

Recommendation

Profit Provision as % of Premium = {ROE / [1 – Tx] – IR} / PSR

Where ROE is the target after-tax return on equity

Tx is the expected income tax rate

IR is the expected before-tax investment return rate on assets supporting Total Equity

PSR is the expected (i.e., normal) premium-to-surplus ratio

This would result in a "profit" provision of –IR/PSR consistent with the Corporation's break-even objective for Basic ($0 Profit)