CLOSING SUBMISSIONS

2018 GENERAL RATE APPLICATION

October 18, 2017

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1 INTRODUCTION

1 Over the past fifteen years, Manitoba Public Insurance's ("MPI" or the "Corporation") rates have consistently been among the lowest in the country for comparable coverage and service.1 This is only the fifth time during that fifteen year period that the Corporation has applied for an increase in Basic Autopac rates. Simply put, Basic rates have exhibited a level of rate stability that would be the envy of any other Canadian jurisdiction.

2 As Messrs. Yien and Johnston both emphasized in their opening presentation, the favourable track record of low and stable rates in Manitoba is currently at risk. In recent years, the premiums set by the Public Utilities Board ("PUB" or "Board") have proven insufficient to cover the actual costs of providing Basic insurance. MPI has suffered losses totaling $163 million due to interest forecasts not materializing, during the last three years. The successive rate deficiencies have eroded Basic capital to such an extent that MPI's Chief Actuary is unable to sign-off on Basic as being in a satisfactory financial condition -- despite the transfer of $176 million from the competitive lines of business.[2]

3 In the absence of these transfers, Basic policyholders would have faced approximately 18% in Rate Stabilization Reserve ("RSR") rebuilding fees[3]. Currently, almost all of the RSR capital balance was derived from transfers. Even after these transfers, Basic's capital level is the lowest among any public or private insurer in Canada.

[1] MPI Exhibit 1, Overview, page 20
[2] In the past three years, MPI has transferred $176 million just to meet the minimum RSR:
$27.8 million in fiscal 2016/17
$75.5 million in fiscal 2015/16
$72.7 million in fiscal 2014/15
[3] PUB (MPI) 2 - 10

4 MPI has a long-term vision for Basic insurance - one that involves rate stability, with inflationary costs being largely offset by natural premium growth. Getting to that position requires the type of cost control that MPI has demonstrated in this Application. It also requires setting sufficient premium rates based on Accepted Actuarial Practice to reflect best estimates of the costs and cash flows associated with policies written in the 2018 policy year. It further requires a settled methodology for determining an RSR range that is sufficiently "wide" to withstand reasonable unforeseen losses without triggering rebuilding fees.

5 Interveners in this proceeding, by contrast, push for the bare minimum capitalization, and the narrowest possible RSR range. At the same time, they want investment income earned on the RSR – presently capital transferred from competitive lines to return Basic to satisfactory financial condition – to be used to set premium rates below what is necessary to match the costs associated with the policies written in the 2018/19 policy year. These conditions create the proverbial "vicious cycle". The probability is high in such circumstances that Basic will frequently be in an unsatisfactory financial position (i.e., below the lower RSR), and crediting income earned on the RSR capital to offset premium rates removes the only option for rebuilding depleted capital within the Basic business apart from luck (i.e., favourable forecast variances). As Mr. Johnston noted on the first day of the Hearing[4]:

> "So in the absence of those other methods, the only way the rate stabilization can grow…is through its investment income, and luck. Really, the only other way is luck, and that's not a strategy."

6 Well run businesses also consider the long-term health of the company. Subsidization by the competitive lines is not a sustainable solution either – particularly when Extension currently has only $30 million left after depletion by successive transfers.[5]

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[4] T: 110, 23 – 111, 2
[5] T: 616, 16 - 25

7 MPI's evidence demonstrates that approving the proposed rates and other requested relief[6] will promote rate stability and support the longer-term financial health of the Corporation. It will position MPI well going forward.

8 The Board's rate setting mandate means that the Board has significant influence over fundamental elements of the Basic Autopac business, including: (i) how much revenue MPI collects (the rate), and (ii) how much of that revenue MPI can retain for mitigating risks, absorbing rate volatility, and investment (the RSR). The certainty MPI requires at present to operate the business and make investment decisions will come from:

a) Establishing an adequate upper RSR target, that provides sufficient bandwidth to absorb fluctuations and avoid rebuilding fees, using 100% MCT or an equivalent DCAT based approach

b) Establishing premium rates that cover the costs of the policies issues, and are not offset by investment income on the RSR

c) Using the best estimate naïve forecast as at November 30th, and confirming the final rate approval through a compliance filing, and

d) confirming a DCAT-based RSR lower limit

9 MPI's Board of Directors believe that the Board and MPI each have specific and complimentary roles. The Board of Directors values the observations and insight that result from the rate setting process, and carefully consider its outcomes when they determine how to operate the business. The Board of Directors believe that ongoing efforts in the regulatory process have and will continue to benefit the Corporation and the Manitobans we serve.

[6] MPI Exhibit 1: Overview, page 16

1.1 Prudent Fiscal Management Will Promote Low and Stable Premium Rates

10 MPI's Board of Directors have been delivered a mandate to restore prudent fiscal management[7]. The Board of Directors have determined that prudent fiscal management relies on three pillars:

- Adequate Capital Reserves
- Appropriate Premiums
- Efficient and Effective Operations

11 Basic requires an RSR range that is sufficiently wide to absorb financial volatility, avoid RSR rebuilding fees, and maintain stable and predictable rates. Basic Autopac is among the most thinly capitalized insurance plans in Canada, and operates at a capital levels that are significantly below other public and private insurance companies.

12 Basic also requires that premium rates be set to cover the costs of a policies issued. Premium rates cannot be systematically deficient, if Basic is to provide long term rates stability. It makes good business sense in the circumstances presently facing Basic, to allow RSR investment income to replenish the RSR.

13 This application demonstrates that MPI is operating in an efficient and effective manner. The record shows that controllable costs are being reduced, with forecast expenses down by 1.9% over last year's GRA. This success continues to be demonstrated in the MPI's benchmarking results.

14 Prudent Fiscal Management also means recognizing the impacts on ratepayers. In the past three years, Basic has received $176 million transfers to ensure the

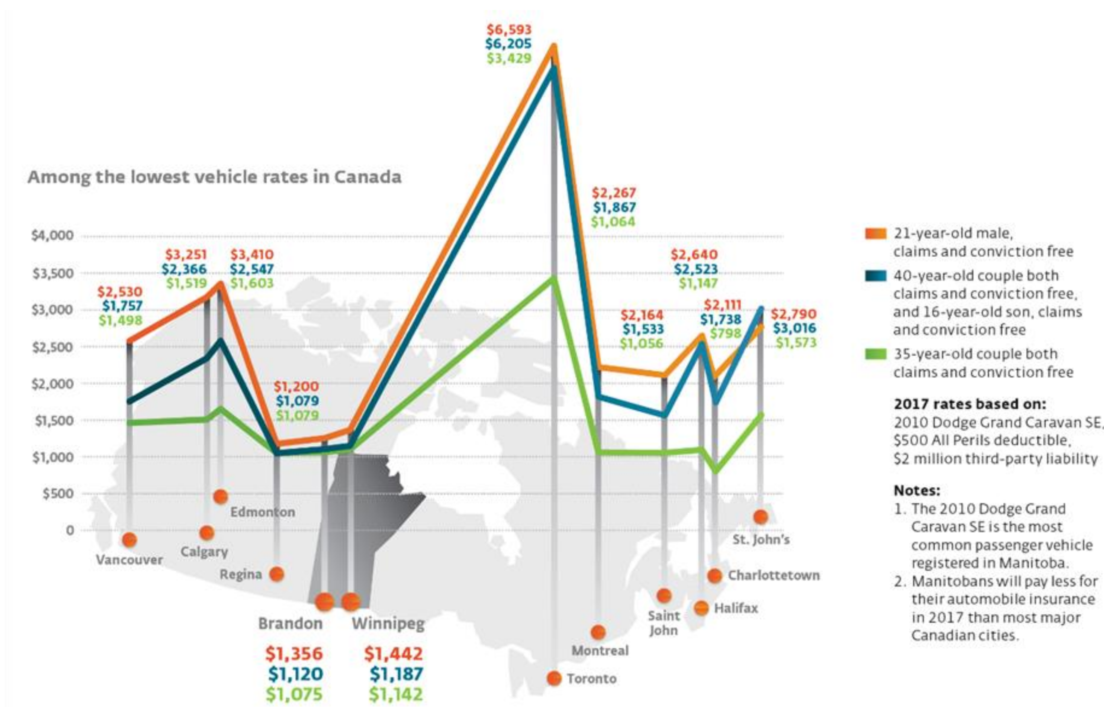
[7] MPI Exhibit 1: Overview Appendix 1

satisfactory financial condition of Basic. It was prudent at the time to make these transfers, and offset approximately 18% in RSR rebuilding fees, but this action cannot be relied on in the future. Basic insurance must by design, stand on its own, and cannot rely on subsidies.

1.2 Affordable Comprehensive Insurance at Stable Premium Rates

Manitoba Public Insurance delivers universal access to comprehensive auto insurance to all Manitobans at affordable and stable premium rates.[8] MPI rates for comparable coverage are among the lowest in the country, year after year. (See Figure 1 below). They will continue to retain this relative position with the proposed rate increase.[9]

Figure 1: National Auto Insurance Rates Comparison

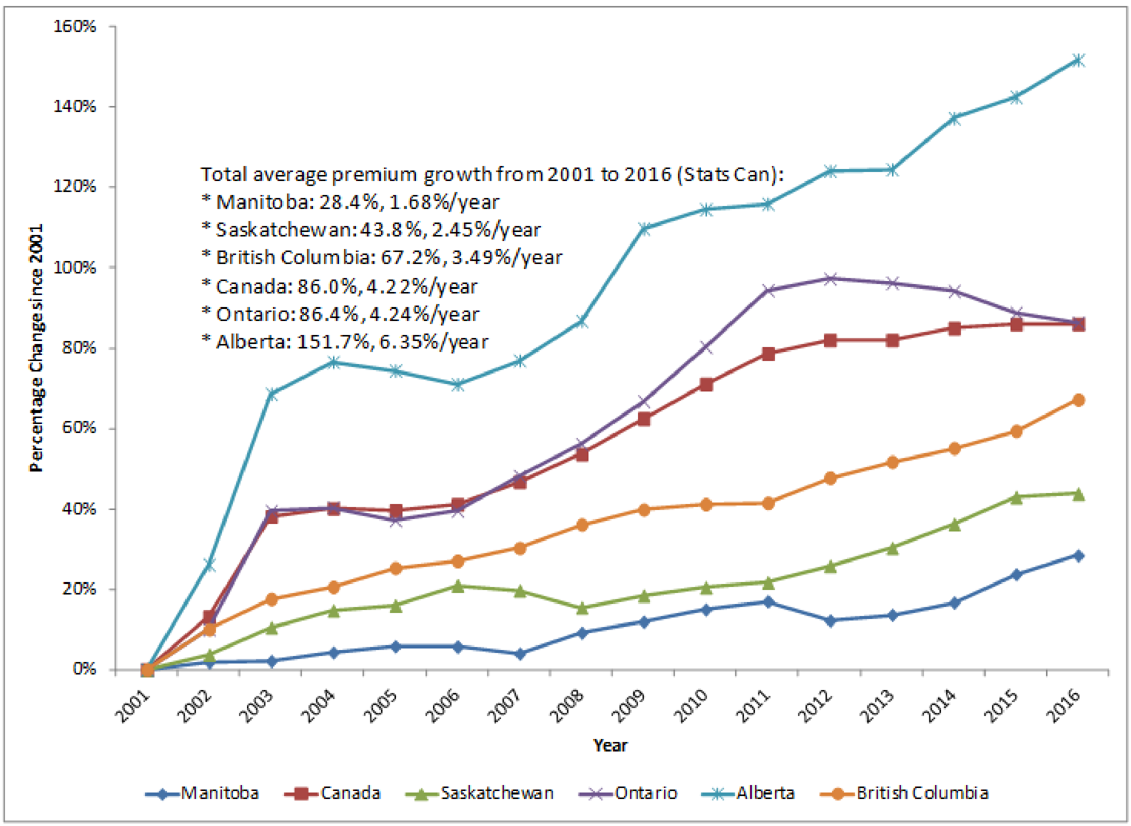


[8] MPI Exhibit 11: CFO & Chief Actuary Presentation, Slide 5
[9] Exhibit 1: 2018 GRA, BMK.4.3

16 MPI has maintained for many years, that Manitobans value knowing that the cost to insure the same vehicle should stay about the same from year to year. In the 2015 GRA, MPI presented a consumer survey analysis[10] that demonstrates Manitobans value stable and predictable rates, and this fact remains true today. It is on this basis that MPI, a provider of an essential insurance product, places such an emphasis on premium rate stability.

17 Figure 2 shows that MPI's premium growth rates are the lowest surveyed by Statistics Canada[11], and is evidence that MPI takes seriously its commitment to stable and predictable premium rates.

Figure 2: Average Auto Insurance Premium Growth by Province



18 Based on MPI's past research, there is a legitimate concern that premium rate volatility would damage the public's confidence in MPI, and the public auto

[10] 2015 GRA: Exhibit 11, Rebuttal Evidence, page 12
[11] MPI Exhibit 1: 2018 GRA, BMK.4.3.3, Figure BMK-9

insurance model more generally. MPI recognizes that many Manitobans, and many Canadians more generally are facing pressure[12] to make ends meet. Significant auto insurance cost escalations, such as the approximately 18% in RSR rebuilding fees (that were avoided by transfers from extension over the past three years) could lead to public outcry, and have negative impacts with real financial consequences for ratepayers, and especially vulnerable consumers.

19 MPI will elaborate in greater detail below, but the essential point is that significant rebuilding fees, resulting from adverse financial results with limited capitalization, would cause a greater hardship to more people, and MPI's rate ask is designed to limit that possibility.

1.3 Maintaining Affordable and Stable Rates Depends on Prudent Fiscal Management

20 The theme of MPI's 2018 General Rate Application is one of prudent fiscal management, and flows from the Minister's mandate letter to MPI's Board of Directors, which states[13]:

> *Manitobans have elected a government that is committed to improving the province of Manitoba. Our priorities include restoring prudent fiscal management, creating jobs, improving health care and education, improving our partnerships and relationships with business and communities, and increasing openness and transparency of our government. We are focused on achieving results on behalf of Manitobans.*

21 The following sections elaborate on the MPI Board of Directors' views prudent fiscal management and how the three essential elements are being addressed.

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[12] T: 95, 4 - 15
[13] MPI Exhibit 1: Overview, Attachment A

1.3.1 MPI Has Demonstrated Efficient and Effective Operations

22 Evidence of MPI's efforts to operate efficiently and effectively pervades the record in this proceeding. This closing submission highlights a number of areas where MPI has taken steps to contain costs and improve its effectiveness in the areas of operating costs, IT capital, and initiatives targeting claims cost reductions. For instance:

a) A 1.9% decrease in average rating year expenses between the 2017 and 2018 GRA[14] (See Section 4 – Cost Containment of this Closing Submission)

b) A flat budget for 2017/18 achieved through a stretch target, such that operating expenses are not contributing to the indicated rate increase. (See Section 4 – Cost Containment of this Closing Submission)

c) MPI compares favorably to industry on a variety of efficiency metrics, including Gross expense per policy in force at 27.89%, compared to the Canadian Benchmark of 37.57.[15] (See Section 4 – Cost Containment of this Closing Submission)

d) While the drivers of claims costs are in many respects beyond the Corporation's control, MPI has targeted areas where it can make a difference – Rodent Claims Strategy, and Road Safety and Loss Prevention. (See Section 4 – Cost Containment of this Closing Submission)

e) The External Labour Strategy is delivering cost savings ahead of schedule. (See Section 7 Information Technology of this Closing Submission)

f) MPI is consistently applying a more refined form of value management to all IT projects going forwards. (See Section 7 Information Technology of this Closing Submission)

[14] MPI Exhibit 1:Expenses, Figure 1
[15] MPI Exhibit 1: Benchmarking, BMK.4.1.2

g) Gartner's CIO Scorecard, highlights that IT spend as a percentage of operational expenses is improving (See Section 7 Information Technology of this Closing Submission)

23 MPI's Board of Directors and Executive team remain hawkish on the matter of cost containment. MPI's Board of Directors are both skilled and appropriately engaged on this matter.

1.3.2 An RSR With Sufficient "Bandwidth" Enables Rate Stability

24 Long-term rate stability is tied to adequate capitalization. An appropriate RSR range, meaning one that has a lower target high enough to provide the absolute minimum level of capital, and an upper target that establishes a range wide enough to absorb the variability in operating results, and prevent the need for significant rebuilding fees.

25 MPI's proposed Lower RSR target of $201 million reflects the approach determined through collaboration (1-in-40 year scenario), and is the minimum necessary to ensure positive total equity for Basic, in the event of unexpected variances from forecasted results, and losses arising from non-recurring events. To put the Minimum RSR in perspective:

a) At that level of capital Basic should expect to deplete total equity once every 40 years, even after rate increases intended to put the company back on track.

b) It equates to approximately 37% MCT.[16] OSFI would intervene if the capital of a federally regulated insurer fell below 150% MCT. The publicly

[16] MPI Exhibit 1: RSR.5, DCAT page 4

owned Basic insurance providers in BC and Saskatchewan use 100% MCT as a regulatory minimum and target respectively, not a maximum.

c) In the past three years, MPI has experienced the type of scenario upon which the RSR minimum was based, requiring transfers of $476 million to adequately capitalize Basic during that period.[17]

26 In section 2 of these Closing Submissions, MPI explains why its proposed Maximum RSR target is an appropriate level of capital to protect Manitobans from undue rate volatility. This submission will review in much greater detail the reasons why a 100% MCT upper RSR target is the best choice, but an alternative to this approach is to establish a range, based on a 1-in-40 probability, three year combined scenario DCAT without management action. This methodology produces a very similar result ($442 million), to the 100% MCT based target of $438 million.

27 Whether framed in terms of MCT or as a DCAT probability, the fundamental issue is whether it is desirable to trigger a rebate if the resulting capital reduction will compromise MPI's ongoing ability to absorb unforeseen losses without a subsequent rebuilding fee. MPI submits that it is most consistent with stable and predictable ratemaking to maintain a sufficient RSR "band" such that the likelihood of a 'rebates followed by surcharges' scenario is kept to a minimum.

28 Once the upper RSR Target is established with certainty, the process of rebuilding the capital reserves can begin. The Board of Directors will explore options to replenish Basic's RSR without placing an ask on ratepayers, once there is certainty that funds below a reasonable upper RSR target will not be rebated.

[17] T: 160, 13-17

1.3.3 Rates Should Be Sufficient to Maintain and Replenish Deficient Capital, Not Be Set to Lose Money

29 Sufficient premium rates are essential to maintain long-term rate stability. Systematic rate deficiencies erode capital and necessitate action to replenish it. In recent years, Extension has subsidized Basic, but that is neither desirable nor sustainable. MPI is seeking approval of sufficient rates, consistent with Accepted Actuarial Practice in Canada.

30 For a private insurer, sufficient rates based on Accepted Actuarial Practice means that premiums are forecasted to cover not only the forecast costs associated with the policies written in the policy year, but also a provision for profit. The profit serves the function of ensuring the business is capitalized. For the other non-profit crown insurers like ICBC and SGI, the "profit provision" contemplated in Accepted Actuarial Practice is re-cast as a "capital provision", the intent of which is to ensure that capital not only keeps pace with growth in the business (capital maintenance provision) but also systematically replenishes when it is too low (capital build provision). Universal compulsory automobile insurance rates in BC and Saskatchewan are only considered adequate when the rate indication covers the costs of the policies written plus the capital provisions.

31 MPI has no capital maintenance provision, no capital build provision, and no provision for profit. The only other means of replenishing the RSR capital balance is through the investment income generated on the RSR capital, and through favorable variances from forecast, or stated simply, through luck.[18]

32 The CAC's witness Dr. Simpson confirms that using RSR investment income to grow the RSR balance is a reasonable approach[19]:

[18] T: 113, 8 -21
[19] T: 1591, 24 – 1592, 4

MR. STEVE SCARFONE: And you're also aware, sir, that the Corporation would like to grow the rate stabilization reserve use -- using investment income from the reserve itself; correct?

DR. WAYNE SIMPSON: I hope that that's what they would do with the money, yes.

33 Deducting the income on total equity from the premium rates for policies written in policy year 2018 is, expressed in actuarial terms, including a "negative profit" provision in the rate indication.[20] Stated in simple terms: the policies MPI will be selling would be priced to lose money. The effect of that result is that (other things equal) MPI's RSR will become progressively more undercapitalized relative to growth in the business (i.e., the MCT will decline). Unforeseen losses will compound the issue. For the reasons described next, Basic policyholders should expect to be faced with a large rebuilding fee at some point in the future.

1.3.4 Future Transfers Will Backstop Severe Losses, Not Substitute for Proper Capitalization and Adequate Rates

34 MPI has in the past three years, transferred a total of $176 million from the competitive lines of business to the Rate Stabilization Reserve[21] to meet the minimum RSR threshold and maintain satisfactory financial condition of Basic Autopac. These significant transfers negated the need for approximately 18% in RSR rebuilding fees[22] over three years, but also significantly depleted extension reserves. It is reasonable to ask "how favorably would the public view MPI, and public auto insurance more generally, if those RSR rebuilding fees had been placed on ratepayers?". The answer is most likely, not very favorably at all. Therefore, MPI's concern about the maintaining Manitoban's confidence in the public auto insurance model.

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[20] As discussed later, this is evident from the calculations requested by the PUB's consulting actuary and the calculation included in Ms. Sherry's evidence. The "P=" number in those calculations – signifying profit - is negative.
[21] T: 98, 22 - 99, 3
[22] PUB (MPI) 2- 10

35 The Board of Directors has been willing to transfer funds and subsidize Basic's total equity in the face of past adverse results, but this should not, and cannot be relied on in the future; for the following reasons:

a) First, it is not prudent to operate Basic on the expectation that transfers from competitive lines can continue to maintain Basic's total equity position at a satisfactory level. Long term sustainability depends on premium rates funding the cost of insurance, including the total equity reserve.[23]

b) Second, significant transfers from extension have occurred in the past three years, which has significantly reduced the total equity position of the extension line of business. There are limited funds remaining to draw on, and a capital transfer similar to those made two and three years ago (approximately $75 million in each instance) would just not be possible.

c) Third, Accepted Actuarial Practice requires premium rates to reflect the costs associated with those policies written in the policy year. Following that methodology should reduce the need transfers of this nature.

36 MPI's Board of Directors will consider future transfers of excess capital from the competitive lines to backstop unanticipated losses, or to replenish the total equity balance above the minimum, but not to address systemic deficiencies in Basic Autopac rates. Continuing to transfer funds to backstop rates that are set with a negative profit provision to deliberately price policy premiums at a loss is not a sustainable course of action.

37 The CAC's actuarial expert, Ms. Sherry has made the point that normal practice is for income associated with the book to support the book[24]. While she made this statement in the context of arguing that Basic should havea negative profit provision, the same logic suggests that subsidization by other lines of business should be avoided

[23] T: 100, 17 -20
[24] T: 1675,23 – 1676,1

2 RATE STABLIZATION RESERVE

38 Having a sufficient capital reserve is foundational to any insurance company, whether it is private or public. Capital reserves are an insurer's commitment to pay claims liabilities, and it must be understood that existing claimants are the first in line to benefit from those funds. The capital reserve is there to ensure that the insurance company can withstand unforeseen losses, preferably with minimal rate volatility.

39 MPI is very thinly capitalized, subsisting at the bare minimum, and this cannot continue.[25] MPI must be permitted to maintain capital within an optimal range between the upper and lower RSR targets will promote rate stability.

40 MPI elaborates on the following points in this section:

a) The existing RSR Framework, propertly applied, promotes rate stability, and reduces the ask on ratepayers;

b) Maintaining total equity at the lower RSR target defeats the purpose of the RSR, and increases risks of rebuilding fees;

c) The RSR range must have enough bandwidth to absorb variability and adverse financial results, which is achieved under MPI's proposed upper RSR target based on 100% Minimum Capital Test (MCT);

d) MPI's alternative DCAT based approach to establishing the upper RSR target is comparable, and therefore acceptable

[25] T: 552, 5 -20

2.1 The Existing RSR Framework Supports Rate Stability

41 The existing RSR Framework, properly applied, is appropriate to both the stated purpose of the RSR and the Basic's objective to deliver predictable and stable rates.

42 The RSR's stated purpose is[26]:

> *To protect motorists from rate increases that would otherwise have been necessary due to unexpected variances from forecasted results and due to events and losses arising from non-recurring events or factors*

43 The essential point is that the RSR exists to protect ratepayers from the financial implications of adverse results, whether stemming from unexpected variances from forecast, or unforeseen events. The RSR promotes rate stability, and avoids rate shock, by limiting the need for RSR rebuilding fees when Basic experience adverse financial results.

2.2 The Range is Central to the Existing RSR Framework

44 The existing RSR framework is built around the concept of a "range", that is defined by a lower and upper RSR target (or threshold). The specifics of the upper and lower targets are explored in detail below, but the key point is that the two targets serve different purposes, have different tests to establish the target level, and in combination define the appropriate range required for the Basic RSR to fulfill its purpose.

45 The Lower RSR Target establishes the absolute minimum level of capital required to achieve satisfactory financial condition. The target is based on the Dynamic Capital Adequacy Test (DCAT), and establishes a level of total equity required under the base scenario and all plausible adverse scenarios, for MPI's assets to be greater

[26] MPI Exhibit 1: RSR.3

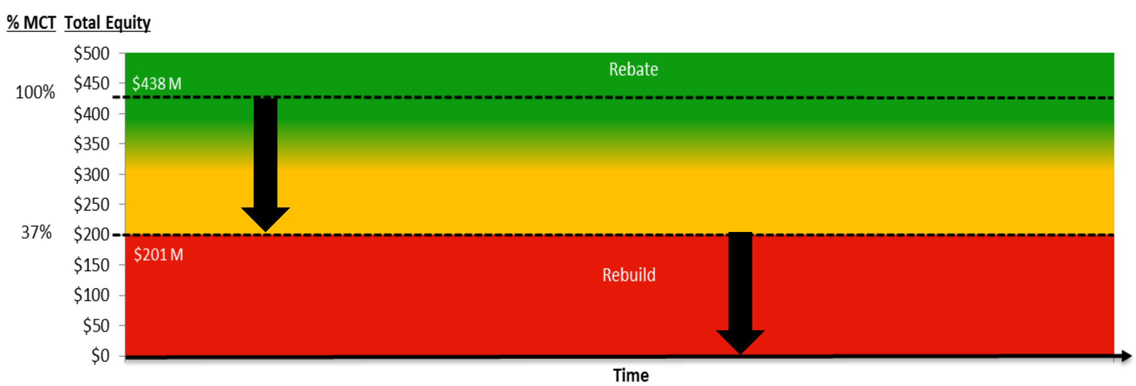
than the statement value of liabilities.[27] Said differently, the test for the Lower RSR target is depleting total equity to zero.

46 The Upper RSR Target is used to establish the range above the lower target, that is sufficiently wide to absorb the variability in the operating results, and reduce the risk that ratepayers will be faced with rebuilding fees, when Basic experiences adverse financial results. Mr. Johnston explained[28]:

> *The upper target, and -- and the range itself, the -- the range is supposed to be a place where you can handle most financial variability without triggering rebuild fees or having rebates all the time. Most, not all. Sometimes you fall below or -- or sometimes you'll have a few good years in a row and you might need a rebate but that's all we really see is the purpose of the RSR. So something above that absolute minimum.*

47 MPI has prepared two estimates for an upper RSR target, that use different methods, but deliver approximately the same result. Using either approach is acceptable to MPI, so long as an appropriate range is established based on a reasonable test, appropriate to the methodology. MPI elaborates on the methodologies and tests below, but Figure 3 offers a high level presentation of the tests.

Figure 3: RSR Targets and Tests



[27] MPI Exhibit 1: RSR.5 DCAT 1.1 p. 6
[28] T: 611

48 The lower RSR Target establishes the minimum amount of the total Equity required by Basic, and is tested against the zero total equity threshold. The Upper RSR Target establishes the range, and is tested against the lower target.

49 Despite this, the CAC's witness Dr. Simpson continues to focus on the probability of the total equity depleting from the upper RSR threshold to zero[29]:

> *And there's an argument -- some argument for a wider range, since there -- an issue has been made of this that the range is too narrow by greater risk tolerance levels. Not 1:2,000, but maybe 1:500.*

50 MPI explained at some length the error in this reasoning in response to PUB (MPI) 2-26. Dr. Simpson, appears to disregard the purpose of the RSR. He continues to apply the incorrect test to the upper RSR target, and instead alludes to flood probabilities, which have no obvious relevance to an insurance company's capital reserve.

2.3 Width of RSR Range Influences Rate Stability and Investment Strategy

51 Having certainty in the RSR parameters and a sufficiently wide range between the lower and upper targets promotes rate stability, and affords Management the clarity and certainty around how much total equity might be available which is important for setting investment policies. This latter point is further explained in the Section 6 on Investments.

52 When the Corporation has a narrow RSR range, it risks rate volatility. The situation MPI is trying to avoid is one where funds are rebated in one year, and an RSR rebuilding fee is required in subsequent years because of unforeseen events occurring. This type of volatility is undesirable, and it is avoidable with an adequately wide RSR range.

[29] T: 1572, 10-14

53 An adequately wide RSR range provides stable and predictable rates, because when the total equity balance is between the upper and lower RSR targets, there is no 'ask' of ratepayers. This means that ratepayers are only charged the appropriate actuarially indicated rate, with no additional RSR rebuilding fees, which could lead to rate shock.

54 Mr. Johnston and Mr. Yien elaborated on this concept in response to questioning from PUB counsel on the merits of an RSR range, versus an single RSR target[30]

> *MR. ROBERT WATCHMAN: Thank you. Now, in response to Information Request 168-B, the Information Request was to discuss the merits of using a Basic target capital range versus using a single Basic target capital level. And in your response you state: "A range is preferable to a single target capital level because it identifies when rebuilding fees and rebates should be considered." And you also note: "A single target capital level would normally require rebates sur -- surcharges each year to balance to the target, which does not promote rate stability preferred by ratepayers."*
>
> *But would you agree that the balancing to target required for a single target capital level necessarily identifies when rebuilding fees and rebates should be considered?*
>
> *MR. LUKE JOHNSTON: I think all we're talking about here is if we have a range we can stay in that range and not have any kind of constant rebuild fee or rebate fee, or whatever you want to call it. Whereas, if we have a target capital -- let's say, for example, the target's $200 million, and wherever we are relative to $200 million we're going to move towards that amount and have a rebuilding fee equal to one-fifth (1/5) of the amount that we need. Notice, SGI has something like that. Whether they use it or not all time, I don't --I don't know. But that would mean we always have a fee. Like, we're either building or rebating some kind of fee in theory, if you're always going to move to the target, like, unless you're right at it. That would seem to add another level of instability to the rate calculation. Our preference would be to have a range that we operate*

[30] T: 618

in where no fee at all is required, only in extreme circumstances when you fall out of that -- that range.

MR. PETER YIEN: Maybe if I can add this as well. When we do have a target, we are guaranteeing fluctuations again. And again, it's a philosophical discussion to say, Is it okay if we end up having a situation?

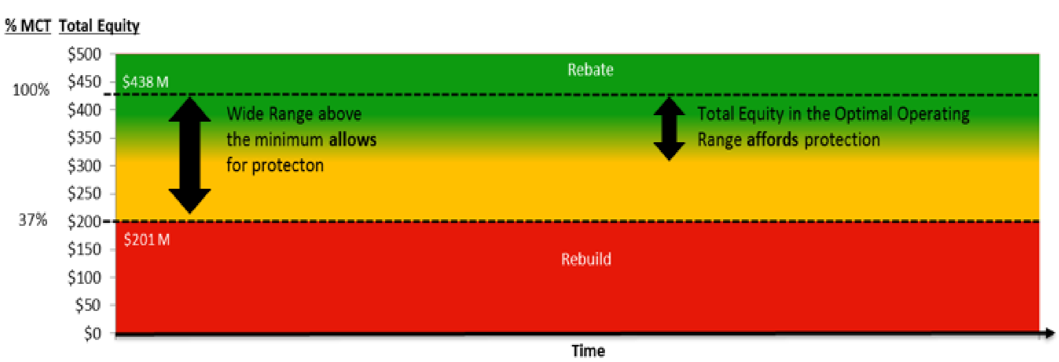
55 The existing RSR framework, predicated on a range defined by an upper and lower RSR target (or threshold) provides the best means of shielding ratepayers from the increased rate volatility and potential rate shock that can occur when rebuilding fees are required. Below, MPI explores the implications of alternative RSR frameworks, such as that used by SGI, but in MPI's submission such alternatives are sub-optimal to achieve the purpose of the RSR.

2.4 Maintaining Capital at the Lower RSR Target Defeats Purpose and Increases the Risk of Rebuilding Fees

56 An adequate range for the RSR must also be accompanied by a total equity balance that offers meaningful protection, i.e. that is not perpetually at the minimum level.

57 This concept was articulated by Mr. Yien in his opening statements, when he referred to an 'optimal range'[31], which is stylistically depicted in Figure 4 below.

Figure 4: RSR Balance in the Optimal Range



[31] T: 108

58 The figure depicts colored zones highlighting the 'optimal range' of the RSR balance. Total equity below the lower RSR Target (red) is an insufficient level of capital to provide for the satisfactory financial condition of Basic. The lower half of the RSR Range (yellow) provides for satisfactory financial condition but does not provide ratepayers with as much protection from adverse events as is afforded with the RSR balance near the top of the range. A total equity balance in the green zone within the RSR range is the 'optimal' range that affords protection to ratepayers from adverse results.

Mr. Yien described this 'optimal range' for total equity as follows[32]:

> *Just to summarize, at the minimum level of total equity, meaning the lower rate stabilization reserve target, Basic can withstand the model as adverse scenarios after management action. Operating above the RSR rate stabilization reserve minimum promotes this rate stability I talked about. The rate stabilization reserve range needs to be sufficiently wide, not narrow, so that it can absorb these unforeseen events.*
>
> *So it should be well above the minimum to reflect the variability in the financial results, within reasonable limits. The total equity is in the optimal range. When it is, it provides our ratepayers the best protection from rebuilding fees.*

59 MPI does not propose a specific value, or a specific 'optimal range', within the RSR range, but notes that with more total equity more protection is afforded to ratepayers. Accordingly the optimal range is thought of as being in the top half of the RSR range, with the upper RSR target being the 'reasonable limit'.

60 When the RSR total equity balance is at the lower RSR target, as it has been for the last three years, ratepayers are not provided protection against adverse financial results. Even the smallest of negative result will drive Basic below the lower RSR target, necessitating some form of capital rebuild action.

[32] T: 108

61 Mr. Johnston explained as follows[33]:

> *We -- we're always going to be on the -- the cusp of unsatisfactory financial condition if we don't have an RSR range. If we're just sitting on the very edge all the time. So we prefer to have – it would make sense to have a -- a range where you could handle a normal amount of financial variability and the model used in this report is just, that there's existing DCAT scenarios.*

62 Adverse financial results are not just possible, but are a reality in MPI's operating environment. MPI explained in its Application that over the past three years, it has lost $163 million due to interest rate forecasts that have not materialized. In Undertaking 28, MPI provided further details of adverse events since 2007/08 that have drawn down the RSR:

- Stock Market Crash: In the 2008/09 fiscal year, the Corporation's equity portfolio declined by 39.7%, or $179 million. If the same percentage decline occurred based on the forecasted balance in equities as of March 1, 2018, the impact would be a $172 million reduction in the RSR in fiscal 2018/19.

- Hail: In 2015/16 and 2016/17 Basic experienced net hail claims costs of $49 million and $39 million respectively, which were more than double the previous 10 year average annual net hail costs (after adjusting historical hail claims to current exposure and cost levels).

- Collision: In 2010/11 through 2013/14 poor winter driving conditions resulted in Basic experiencing three of its four worst-ever accident years for collision frequency. In 2010/11, 2011/12, and 2013/14 collision frequency averaged 138.3 claims per 100 vehicles, which is approximately 9% higher than the collision frequency forecasted in the 2018 GRA. If such an event occurred beginning in 2018/19, the Collision forecast would be approximately 10,500 additional collision claims and $40 million over budget per year.

[33] T: 588

- PIPP: Beginning approximately in accident year 2010/11, there was an unexpected increase in the number of lifetime injury claimants. In fiscal 2015/16 and 2016/17 the claims liabilities for Weekly Indemnity were increased by $54 million and $36 million respectively to account for this change in experience.

63 The cumulative impact of these events is in excess of $550 million, and the single largest event negatively impacted the Total Equity by $179 million. In this kind of operating environment Basic's RSR is not providing protection if the total equity balance is at the minimum.

64 Mr. Johnston summarizes this issue as follows[34]:

> *MR. ROBERT WATCHMAN: Can you explain why the upper threshold scenario testing was before routine management and regulatory action while the lower is after?*
>
> *MR. LUKE JOHNSTON: Definitely. So we understand that as this process has evolved, the DCAT is measuring the absolute -- sorry, first – first off, the DCAT is just giving my opinion about whether MPI's Basic satisfactory condition, a side kind of calculation, and in our DCAT, which is definitely unique, is to say, What's the absolute minimum amount you could have to -- to have satisfactory financial condition?*
>
> ***The absolute minimum is not a desirable place to be, but it's a -- it -- it's a good number for our -- our Board and MPI's board to have as a -- as a -- a point where you need to take action, the action likely being a rebuilding fee. So it is necessary. And so that -- that is that calculation. The upper target, and -- and the range itself, the -- the range is supposed to be a place where you can handle most financial variability without triggering rebuild fees or having rebates all the time. Most, not all. Sometimes you fall below or - or sometimes you'll have a few good years in a row and you might need a rebate***

[34] T:611

> ***but that's all we really see is the purpose of the RSR. So something above that absolute minimum.***
>
> *[Emphasis added]*

2.5 MPI's Applied For Capital Targets are Consistent with the Purpose of the RSR Framework

65 The following sections outline MPI's proposed RSR targets, and explain how these are consistent with the purpose of the RSR, and in the public interest.

2.6 The Lower RSR Target is the Absolute Minimum Total Equity

66 MPIs is applying for a 2018/19 lower RSR Target of $201 million, which equates to a MCT ratio of 37%.There have been no material changes to the methodology to establish the lower RSR Target.[35]

67 MPI submits that the Public Utilities Board should reaffirm the applied for approach for determining the lower RSR target going forward. After many years of discussion and collaboration, this methodology is established and appropriate to the purpose of the RSR framework. The actuary can sign off on the sound financial condition of Basic at the level of capital given the base scenario, assumptions around the adverse scenarios, and the selected probability level.[36]

68 The lower end RSR target is intended to reflect the absolute minimum amount of reserves necessary to ensure a satisfactory financial condition. Stated another way – it identifies the minimum amount of the RSR at the start of the rating period such that the reserve would stay above zero dollars for the 1-in-40-year scenarios modeled. Falling below zero means that the chief actuary cannot sign off on the satisfactory financial position of Basic. The DCAT 1-in-40-year scenarios have been exhaustively tested in a transparent and collaborative process. The result of the

[35] MPI Exhibit 1: RSR.5 DCAT.1.7.2
[36] MPI Exhibit 1: RSR.5 DCAT p.5

DCAT analysis is that the lower end of the RSR target is $201 million for this rating period.[37]

69 MPI accepts this approach for establishing the minimum level of capital, recognizing that to have a higher level of minimum capital could potentially mean asking ratepayers to fund additional rebuilding fees to secure the satisfactory financial condition of Basic.

70 While MPI accepts a $201 million lower threshold this year it should be recognized that the amount is very low – equal to 37% MCT[38], and would be the lowest by far of any insurer in Canada.

71 A 1-in-40 year scenario falls well short of capturing all plausible adverse events, and there is a real prospect that Basic Autopac could lose more than $201 million in a short period of time. This is underscored by the fact that MPI has just had experience very similar to a 1-in-40 year scenario.

72 In his opening presentation Mr. Johnston laid to rest any uncertainty about the potential for 1-in-40 adverse scenario to occur[39]:

> *And then we used the PUB's current 1:40 risk tolerance for the -- for the lower level, so the range represents what's the normal variability you'd have in a three-year period at a 1:40 year confidence. The DCAT lower target is 201 million. And it's -- we have not changed our methodology for that calculation.* ***One of the Intervenors made a comment this morning that this is never going to happen, and I've never seen this happen. That's totally false. It's happening right now. In the last five (5) years alone, we've lost over $300 million on Basic. In the last two (2) years, we've lost more than $170 million. So the recent experience is actually worse than we're even modelling in the DCAT right now.*** *The lower RSR target effectively means if you had $201 million in the bank right now, once every forty (40) years, including management action, that being a rate increase or rebuilding fees, you would exhaust that entire amount one (1) every forty (40) years.*

[37] MPI Exhibit 1: RSR.5 DCAT p.4
[38] MPI Exhibit 1: RSR.5 DCAT p.4
[39] T:148

> *Given that we're setting rates with no profit, we'd expect about a 50/50 chance of falling of the -- of the RSR falling, or -- or versus going up, if we're using best estimates. So falling to zero is obviously very bad, but there is a -- a lot of combinations where the, you know, we're falling to 100 million, or falling to 50 million that would trigger RSR rebuilding fees.*
>
> *[emphasis added]*

73 Recent experience has been more severe than the adverse scenarios modeled in the DCAT, to establish the lower RSR target. Two hundred and one million is the absolute lowest level of capital required for Basic to achieve satisfactory financial condition, and even at that level, Basic remains thinly capitalized and vulnerable.

2.7 Transfers from Extension Should Be the Exception, Not the Expectation

74 The fundamental premise underpinning this GRA is that Basic compulsory insurance must fund itself. It must cover its own costs and replenish its own reserves. It is imprudent to operate Basic Insurance with any expectation of subsidies from other lines of business or Government.

75 Long term sustainability of Basic Insurance requires that rates fund the cost of insurance. Rates cannot be set to systematically under collect the cost of polices. This can result in losses drawdown the Basic's capital reserve (expressed as % of MCT), threatening the financial condition of Basic, and the rate stability that Manitobans demand.

76 Basic's financial results in the past 5 years have been poor. Four of the last five years have had negative net income of $50 million or more (the exception year having only $2 million in positive net income).[40] This has resulted in the need to transfer $176 million from the Extension line of business, in the last three years, just to achieve the absolute minimum level of capital and maintain satisfactory

[40] UT 27, Appendix 1

financial condition. As discussed above, operating at the minimum level of capital defeats the purpose of the RSR.

77 Basic's losses, and the subsequent transfers from Extension have been so significant, that the RSR is now almost entirely comprised of subsidies from other lines of business.

78 These transfers from extension were necessary, prudent and in the best interests of Ratepayers, as they offset approximately 18% in RSR rebuilding fees[41], that would otherwise have been levied against ratepayers. However, this pattern cannot be allowed to persist.

79 Surplus funds in extension should not be relied upon, and the competitive market product should not be treated as a funding mechanism for the regulated product. As Mr. Yien explained[42], there is presently $30 million in excess retained earnings in extension, and the ability to transfer funds is not guaranteed.

80 Further the Board of Directors are responsible to the Corporation as a whole, and must weigh the risks of reducing the capital levels of the Extension line of business, to subsidize the Basic line of business. It is not prudent fiscal management to rely on further transfers going forward.

81 Indeed the recent experience of ICBC is instructive, where the optional line of business was deliberately used to offset losses on the Basic product. This approach is no longer sustainable in the face of significant losses to the extension line.[43]

82 The CAC witness Dr. Simpson casually dismisses the very serious implications of Basic depleting its total equity[44]:

> *And whereas a sole private insurer would face bankruptcy in the event of insufficient capital, leaving policyholders and claimants at*

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[41] PUB (MPI) 2-10
[42] T: 616, 16 - 25
[43] PUB (CAC) 1-1, Attachment A, page 21
[44] T: 1569, 19-25

risk of not being fully indemnified for their losses, a government insurer is implicitly backed by the government, meaning this risk is minimal. In other words, the risk of -- of bankruptcy is minimal.

83 Notwithstanding that MPI is crown corporation, Manitoba taxpayers have every right to expect that the company will be managed prudently.

2.8 Proposed Upper RSR Target is Appropriate

84 In requesting an upper RSR target of 100% MCT, MPI recognizes that the PUB rescinded its notional approval of this approach to establishing the upper RSR Target in the 2017 GRA Order. MPI is aware of the PUB's stated reasons for decision, and respectfully requests that it reconsider, given the full breadth of evidence before it in this proceeding. The following sections will outline this evidence, and make the following points about the appropriateness of the MCT test for setting the upper RSR Target:

1. MCT test is appropriate because it is an industry standard capital adequacy test that considers actual risks facing Basic. Most of these risks exists by virtue of the fact that Basic is a Property and Casualty (P&C) insurer, and are in no way mitigated by the fact that Basic is a regulated monopoly. Because it is an industry standard, the MCT test allows for comparison to other P&C insurers, both public and private.

2. It is an objective assessment, relying the breadth of information, and depth of experience possessed by the Office of the Superintendent of Financial Institutions.

3. MCT is a test based on Basic's balance sheet, which is different than the DCAT scenario testing, and a diversity in approaches to setting the RSR targets is preferable.

85 Further, the following sections will explain that 100% is the appropriate target level for the MCT test for the following reasons:

1. At 100% MCT, capital available is equal to capital required, which is a meaningful and deliberate target that is appropriate to the circumstances of Basic, and the consistent with the RSR framework.

2. MPI's request for 100% MCT upper threshold is appropriate, and supported by the DCAT based analysis that achieves similar capitalization under reasonable assumptions.

3. The PUB's concerns with respect to moral hazard at capital levels approaching 100% MCT is misplaced, and that constraining capital levels is too blunt an instrument to address moral hazard concerns and has considerable collateral impacts.

86 MPI submits that approving an upper limit is a key component of the long term sustainability of Basic, as well as a key component of the corporate bond strategy (discussed in detail in Section 6 on Investments).

2.8.1 MCT is an Industry Standard Test that Measures the Risk Facing Basic

87 The MCT is a standardized test that is used by the Property and Casualty insurance industry and its regulator. The MCT was developed to assess the key risks faced by the industry and to harmonize capital requirements across jurisdictions in Canada. It is a risk-based approach that reflects the riskiness of individual Property and Casualty insurers. The risks being measured by the MCT are indeed relevant to MPI, and other monopoly crown insurers, such as SGI and ICBC.

88 The 2016 MCT guideline outlines the five risk categories that underpin the Minimum Capital Test[45]:

45 RSR.4.5.2.2

1. **Insurance Risk**: the risk arising from the potential for claims or payouts to be made to policyholders. Uncertainties exist around the ultimate amount of net cash flows, and the timing of these cash flows.

2. **Market Risk**: the risk that arises from changing rates or prices in various markets such as interest rates, foreign exchange and real estate. Trading, investing and related business activities create exposure to these risks.

3. **Credit Risk**: the risk of loss arising from counterparty's inability or unwillingness to fully meet a contractual obligation due to an insurer. OSFI describes this risk materializing any time funds are extended through contractual agreements.

4. **Operational Risk**: the risk of loss resulting from inadequate or failed internal processes, people, and system, or from external events. An insurer is exposed to operational risk through day-to-day operations, or specific external events.

5. **(Less) Diversification Credit**: to account for the fact that not all risks are perfectly correlated, and that an insurer is unlikely to incur the maximum possible loss from each risk type simultaneously.

89 Under cross examination the CAC's actuarial expert concurred that Basic Autopac faces these risks[46]:

> *MR. MATTHEW GHIKAS: Okay. So let's go through some of the items. First of all, 1(a) capital required for unpaid claims and premium liabilities. Do you see that?*
>
> *MS. ANDREA SHERRY: M-hm. Yes, I do.*
>
> *MR. MATTHEW GHIKAS: Okay. You'd agree with me that Basic Autopac has unpaid claims and premium liabilities?*

[46] T:1692,7 – 1695,9

MS. ANDREA SHERRY: I would agree.

MR. MATTHEW GHIKAS: And you'd agree with me that Basic Autopac has risks associated with the potential for catastrophes?

MS. ANDREA SHERRY: I would have to look into that one, to be honest with you because I'm not sure if that's thr -- anything related to earthquake.

MR. MATTHEW GHIKAS: Okay. But depending on the catastrophe and depending on what they're writing, they can conceivably have that, correct?

MS. ANDREA SHERRY: Correct.

MR. MATTHEW GHIKAS: Right. And to the extent that they have less than another insurer, that's going to be picked up in the -- in the balance sheet, correct?

MS. ANDREA SHERRY: Yep.

MR. MATTHEW GHIKAS: Okay. And the next one "margin required for reinsurance seated to unregistered reinsurers." MPI doesn't include anything for that.

MS. ANDREA SHERRY: M-hm.

MR. MATTHEW GHIKAS: But -- so we'll - we'll leave that one. But you'll agree with me that MPI has exposure to interest rate risk?

MS. ANDREA SHERRY: Yes.

MR. MATTHEW GHIKAS: And that, for example, would be reflected in the fact that there is -- there is -- had to be $163 million transferred from optional to the Basic side of the business to deal with interest rate variances?

MS. ANDREA SHERRY: I would agree that MPI has interest rate risk, yes.

MR. MATTHEW GHIKAS: Right. And you'd agree with me that MPI has foreign-exchange risk on investments that are US denominated or US infrastructure investments?

MS. ANDREA SHERRY: Yep.

MR. MATTHEW GHIKAS: And you'd agree with me that MPI, to the extent that it is holding equity in its portfolio, has equity risk?

MS. ANDREA SHERRY: Yes.

MR. MATTHEW GHIKAS: And you would agree with me that if there is real estate in MPI's portfolio - which I understand there is - MPI would also face real estate risk?

MS. ANDREA SHERRY: Yes.

MR. MATTHEW GHIKAS: And you'd agree with me -- let's skip over the next one. You'd agree with me that there is the potential for counter-party default risk for MPI?

MS. ANDREA SHERRY: Yes.

MR. MATTHEW GHIKAS: Okay. And the next two they are no values for MPI, so I'll skip over those. And there is the potential for operational risk, just like any other insurer; correct?

MS. ANDREA SHERRY: Correct.

MR. MATTHEW GHIKAS: Okay. Now, I take it that the fact that MPI is not subject to competition, the only place for that to fit is under 2(e) capital required for other market risk exposures?

MS. ANDREA SHERRY: Yes, I believe you're correct in the MCT.

MR. MATTHEW GHIKAS: Okay. And so for Basic then what MPI would simply do is put a zero value in for that, on their P&C-1 form. Right?

MS. ANDREA SHERRY: Is that a question?

MR. MATTHEW GHIKAS: It is.

MS. ANDREA SHERRY: I don't know what MPI would do.

MR. MATTHEW GHIKAS: Okay. So if -- if there is no market risk exposure from competition, you would expect that simply -- the insurer would simply fill -- fill out that line item reflecting the fact that they have no competitive risk; correct?

MS. ANDREA SHERRY: Okay.

90 Ms. Sherry concurs that nearly all of these risks captured in the MCT test are in fact risks that Basic is exposed to, and risks that Basic is not exposed to will not be reflected in the MCT calculations. MPI quantifies these risks in *Volume II, RSR.5 DCAT Appendix 1D*.

91 MPI's status as a crown corporation and its monopoly over the compulsory insurance do not mitigate these risks. This fact has not been refuted in the evidence of any party to this proceeding, and to the contrary is fully supported by the fact that MPI can, and does, measure these risks in accordance with the OSFI guidelines.

92 Further, other monopoly crown insurers, namely ICBC and SGI, employ the MCT as the appropriate test of Capital Adequacy for their regulated compulsory insurance business. For our purposes, the importance of an "apples to apples" comparison with other insurers is that Manitobans can see objectively that MPI is retaining less policyholder premiums than any other insurer in the country, public or private. A test that is good enough for every other insurer in Canada should be good enough for MPI.

2.8.2 MCT Test has Informational Advantages Not Available to MPI

93 Further to the point that MCT is an objective test, OSFI developed the MCT risk factors based on research and consultation with the P&C industry, and applies this

capital adequacy test to all federally regulated P&C insurers. OSFI described the process of developing the risk factors as follows[47]:

> *To develop the new insurance risk factors , OSFI conducted a variability analysis based on incurred and paid data to assess the insurance premiums and claims risks. The review of the insurance risk margins was done in collaboration with the Canadian Institute of Actuaries (CIA) and the Autorité des marchés financiers (AMF). The CIA's role was primarily to provide independent advice, and actuarial expertise and data validation during the study. OSFI provided a high level summary of the methodology used to develop the proposed insurance risk factors in its May 2013 discussion paper.*

94 The MCT test has been developed based on the breadth of information available to OSFI, leveraging through collaboration the deep expertise of the CIA and AMF. The MCT test is evidence based.

95 Mr. Johnston articulated the informational advantage of OSFI as follows[48]:

> *It considers our risk, similar to, you know, how other insurance companies are measured. A big advantage of this test is they – is -- is the office of the superintendent of financial institutions has a lot more information than MPI on these risks. Sometimes, I'm sure I might be accused of operating on bit of an island and only looking at MPI data. This would be a good reason to, you know, somewhere else to look in terms of how they assess some of these risks that MPI maybe can't quantify to the same extent. And then, of course, by using the standard measure, you can compare to other jurisdictions.*

2.8.3 A Capital Adequacy Test Based on the Balance Sheet Compliments the DCAT Based Lower RSR Target

96 MPI's desire to leverage the MCT test for setting the upper RSR target is also based on the benefit that a diversity in approaches brings. The MCT test is objective, and

[47] CAC (MPI) 1-4(a)
[48] T: 150

based on the balance sheet, which provides an additional, objective perspective to establishing the RSR Range.

97 The preoccupation with the type of risk-based test used to express the dollar threshold is really a side issue to the more fundamental point that MPI needs to know that Basic will be able to accumulate sufficient capital to manage rate volatility and have flexibility in its investment strategy. However, MPI submits that MCT is an appropriate test for two main reasons.

2.8.4 At 100% MCT Capital Available is Equal to Capital Required

98 The MCT test is a ratio of capital available to capital required, and is expressed as a percentage. At 100%, the ratio of capital available to capital required is 1, meaning that capital available equals capital required. This level is not arbitrary, and is not based on judgement.

1. 100% MCT is appropriate for setting the upper RSR target, for two reasons: it establishes a reasonable range for the RSR, which as discussed in the sections above, allows the RSR provide protection to ratepayers, and enhance rate stability; and

2. When MCT is above 100%, the capital available is in excess of capital required (by definition). This fact is conceptually aligned with the RSR framework which contemplates that funds in excess of the upper RSR target are available for refund to ratepayers. Funds in excess of 100% MCT are surplus to the "capital required" under the MCT test, and it makes good sense that those funds would be excess to the purpose of the RSR.

2.8.5 The DCAT Based Estimate of the Upper RSR Target Supports the 100% MCT Based Target

99 In compliance with Board Order 162/16, and based on feedback from stakeholders to the DCAT technical conference, MPI adapted the DCAT analysis to estimate the upper RSR target, based on the following criteria:

a) **The analysis is also evidence based**: Stakeholders would prefer a target that is generated from the collaboratively developed DCAT analysis; one that can be supported through the modeling of DCAT-based scenarios.

b) **The analysis excludes management action**: The appropriate RSR range would exclude management action so it reflects expected variability in financial results before any assumed management actions at the selected risk tolerance. Management actions could then be utilized to remain in the acceptable RSR range.

c) **Has a higher or equal risk tolerance than the lower capital target**: It is reasonable that the RSR 'operational' range would have a higher (e.g. 1-in-20) or equal (1-in-40) risk tolerance than the lower RSR target.

d) **Has a reasonable time horizon for which variability can be managed**: The RSR range should reflect a reasonable timeline for which financial results could fluctuate within an acceptable range of results without generating frequency rebuilding fees or rebates.

100 MPI's recommended upper target, based on a three year combined scenario, before management action, at the 1-in-40 probability level is $442 million. This amount is slightly more than the applied for 100% MCT Upper RSR Target of $438 million. This range appropriately reflects the variability in operating results and further supports MPI's request for 100% MCT based upper RSR target as just reasonable and in the public interest.

101 MPI also cautions against the PUB's adoption of methods that have been only lightly explored in this process through information requests and undertakings. The iterative modelling that MPI was asked to produce in response to third round information request[49] is one such example. This modelling is based on an unreasonable assumption, and the results cannot be relied upon. In this particular example, the modelled scenario requires an assumption that $305 million in capital would be transferred to Basic, which has no basis in reality, given that level of capital does not exist in other lines of business.

2.8.5.1 The CAC's Actuarial Expert is Uncertain if MCT is the Appropriate Test

102 Under cross examination, Ms. Sherry's own past testimony was put to her, regarding the suitability of the MCT test for determining the upper RSR target:

> *MR. MATTHEW GHIKAS: Okay. So let me -- let me ask you this again. I'm not sure if I understood whether you are objecting to the use of the test itself, or whether you're objecting to the use of 100 percent.*
>
> *MS. ANDREA SHERRY: I'm objecting to the use of the MCT as -- in setting the RSR range.*
>
> *MR. MATTHEW GHIKAS: Okay.*
>
> *MS. ANDREA SHERRY: You can calculate the MCT and see where you're at, but it's -- I – I don't think it should be used to set the RSR range.*
>
> *MR. MATTHEW GHIKAS: Okay. Can we go, Diana, if you can pull up last year's transcript, please. And to page 2,059. And you can -- if you go down to line 15, please. Okay. Now, last year, Ms. Sherry, you -- I cross-examined you last year, right?*

49 MPI Exhibit 40: PUB (MPI) Pre-Ask 5

MS. ANDREA SHERRY: I recall.

MR. MATTHEW GHIKAS: And if -- starting at line 15 of this transcript, I asked you: "And I've seen your transcripts, Ms. Sherry, where you had indicated that you didn't believe MCT was the appropriate -- was appropriate for use for MPI. Is that correct?" Answer: "I wouldn't say that it's not appropriate to use for MPI. The MCT is really just an output of a set of financial statements. My opinion is that it shouldn't serve as the – a hundred percent MCT shouldn't serve as the upper target for the RSR." Now, do you recall being asked those questions?

MS. ANDREA SHERRY: Vaguely.

MR. MATTHEW GHIKAS: Okay. And do you recall giving those answers?

MS. ANDREA SHERRY: Yes.

MR. MATTHEW GHIKAS: And were they true?

MS. ANDREA SHERRY: Yes.

2.8.6 Constrained Capitalization is Not the Appropriate Means to Address Moral Hazard

103 PUB Order 162/16 stated:

> *The Board is concerned that the degree of conservatism implied by the Corporation's proposal may be excessive based on the Corporation's scenario testing at the more extreme percentile levels of possible outcomes, potentially giving rise to a risk of moral hazard.*

104 Generally, moral hazard is considered to be the lack of incentive to guard against risk, where on is protected from its consequences. Notwithstanding that guarding against risk is the central theme in MPI's application for an upper RSR target based on 100% MCT, MPI understands the PUB's concerns around the potential for risk of moral hazard to be that, with a higher level of capital MPI may become less diligent in cost containment, or initiative spending.

105 MPI respectfully requests the PUB re-evaluate its stated position in this matter. First, MPI has a number of measures in place to demonstrate that MPI is operating prudently and efficiently, including benchmarking, the value management process, and success in cost containment. Each of these controls hold MPI accountable to achieving stated goals, delivering results, and to operating efficiently and effectively

106 Second, and in any event, constraining Basic's capital is too blunt an instrument for mitigating the potential risk of moral hazard. A significant portion of this GRA process has been devoted to exploring the serious risks associated with Basic's thinly capitalized state, and constraining Basic's capital on the grounds of a potential risk of moral hazard is inappropriate because the collateral risks are so serious.

2.9 An Upper RSR Target Equivalent to 100% MCT is also Appropriate

107 In Order 162/16 the PUB stated that the following question remains unanswered[50]:

> *beyond what percentile level is it no longer reasonable and appropriate for the Corporation to hold funds against possible adverse circumstances, instead of rebating these excess funds back to the ratepayers?*

108 MPI respectfully submits that its applied for Upper RSR Target of $438 million, based on 100% MCT is the appropriate level beyond which funds may be rebated to ratepayers. A significant body of evidence has been presented on the record of this GRA, upon which the PUB may make this finding.

109 In the alternative to this approach, MPI submits that its DCAT based upper RSR Target of $442 million is also appropriate, and in the current circumstance very

[50] Order 162/16 p.61

closely aligns with the applied for MCT based target. In this regard, MPI considers the DCAT based approach to be acceptable.

110 Should the PUB choose an upper RSR Target lower than 100% MCT, MPI's Board of Directors believes it is appropriate for the Minister of Finance to acknowledge the risk associated with setting such a target.

2.10 Adjustments to the RSR Framework Must be Given Due Consideration in Future Proceedings

111 Alternative approaches to establishing RSR targets have been lightly canvassed through Information Requests and undertakings to this proceeding. Further, the PUB has sought information from MPI on completely new mechanisms for the RSR Framework, such as capital maintenance provisions, and capital rebuild provisions.

112 MPI has made its best effort to comply with these information requests, under the tight timelines of GRA process, but MPI is not confident that it has fully considered the implications of these alternative approaches. Similarly, MPI's Executive and Board of Directors have not approved any of the various approaches canvassed through the GRA process.

113 If the PUB wishes to review alternative approaches to the RSR framework, that it direct MPI to bring such a proposal in the next GRA. This would allow MPI's Board of Directors adequate opportunity to consider and develop proposals that fully consider the myriad of implications that would result from significant changes to the RSR framework. As well, the PUB and interveners would be afforded an opportunity to fully consider the range of implications of any new proposal, through the full GRA process.

2.11 Closing Remarks on the RSR

114 An adequately wide and well-funded RSR is essential for the long term sustainability of Basic Autopac. The RSR is a very important tool for delivering predictable and stable rates demanded by ratepayers.

115 MPI's proposed upper and lower RSR targets are reasonable, considered, and appropriate to the circumstances of Basic. If approved MPI's capital targets will remain considerably lower than any other insurance company, public or private, in Canada.[51] This fact was highlighted in cross examination of the CAC's actuarial expert Ms. Sherry[52]:

> *MR. MATTHEW GHIKAS: Okay. All right. Are you aware, Ms. Sherry, that MPI's current capital level is 29 percent MCT?*
>
> *MS. ANDREA SHERRY: I believe I read that throughout the hearing process, yes.*
>
> *MR. MATTHEW GHIKAS: Okay. And you -- you seem to have a lot of experience in Canada. Are you aware of any P&C insurer anywhere in Canada, Crown or private, where the applicable regulator has determined that such a capital level is sufficient?*
>
> *MS. ANDREA SHERRY: I am not aware of that, no.*
>
> *MR. MATTHEW GHIKAS: Okay. And in terms of the lower RSR level coming out of the collaborative process, that's based on a 1:40 DCAT scenario, Ms. Sherry?*
>
> *MS. ANDREA SHERRY: That is what is being proposed, yes.*
>
> *MR. MATTHEW GHIKAS: And you're aware that that currently translates to $201 million for basic Autopac?*

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[51] There is no evidence on the record of any insurer having less capital than MPI, and no evidence that any regulator has approved a lower minimum capital target.

[52] T:1698,22 – 1701,12

MS. ANDREA SHERRY: I'm just checking the number. You are correct, yes.

MR. MATTHEW GHIKAS: Okay. And that that translates to 37 percent MCT?

MS. ANDREA SHERRY: Yes.

MR. MATTHEW GHIKAS: Okay. Are you aware of any other P&C insurer anywhere in Canada, public or private, where the applicable regulator has determined that an acceptable minimum level of capital is the amount generated by a 1:40 DCAT scenario?

MS. ANDREA SHERRY: No, I am not aware.

MR. MATTHEW GHIKAS: Okay. Are you aware of any P&C insurer anywhere in Canada, public or private, where the applicable regulator has determined that 37 percent MCT is an acceptable minimum level of capital?

MS. ANDREA SHERRY: No, I am not aware.

116 An also confirmed by the CAC's economist Dr. Simpson[53]:

MR. STEVE SCARFONE: And Dr. Simpson, you're aware that MPIC is currently operating at approximately 30 percent MCT?

DR. WAYNE SIMPSON: Right.

MR. STEVE SCARFONE: Are you aware of any private insurer that operates at 30 percent MCT?

DR. WAYNE SIMPSON: No.

117 MPI submits that certainty is important when it comes to the RSR purpose and parameters. The amount of capital held is fundamental to corporate decision making, and it is particularly important for an insurance company that is exposed

[53] T: 1613, 1-7

to significant uncertainties. MPI is respectfully looking to the Board to bring closure to the remaining issues around the RSR.

3 PREMIUM RATES SHOULD ALLOW FOR INCOME ON THE RSR TO MAINTAIN AND REPLENISH BASIC'S CAPITAL

118 Investment income on the RSR capital balance must be allowed to remain in the RSR to maintain and replenish the capital reserves above the absolute minimum level for satisfactory financial condition. Without another means to maintain or drive the capital balance up into an optimal range, the RSR balance will not keep pace with the growth of the business. This will erode the MCT ratio and jeopardize the ability of the RSR to meet its stated purpose to protect ratepayers from rebuilding fees. In this section we make the following points:

a) MPI's proposal is consistent with Accepted Actuarial Practice;

b) Applying investment income on total equity funded by extension and prior year policy premiums to reduce the premiums of policies written this year, prices Basic policies at a loss.

c) Faced with two options under Accepted Actuarial Practice, MPI's proposal makes the most sense in the context of Basic being thinly capitalized with no other mechanism to either maintain or build capital.[54]

d) The reason other insurers can apply income on total equity to offset premium rates (i.e., what is, in actuarial terms, a negative profit provision) is because their rate indications also include a positive profit provision (private insurers) or a capital maintenance and capital build provision (SGI and ICBC) that more than offsets the impact.

e) The RSR balance is not "ratepayer's money"[55], as CAC and its experts suggest, in either law or fact.

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54 T: 552, 5 - 20
[55] CAC (MPI) 1-1

3.1 MPI's Proposal is Consistent with Actuarial Standards of Practice

119 MPI's proposal is consistent with Accepted Actuarial Practice (AAP). AAP standards of practice do not require that the profit provision be calculated on a total return basis, or that investment income from total equity otherwise be deducted from AAP rates.[56]

120 The Actuarial Standards of Practice, section 2620.01, provides the following with respect to setting rates[57]:

> *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.*

121 The costs in question are those specifically related to policies written in the 2018 policy year. Similarly, the cash flows "relating to" the policies are the premiums collected from customers associated with policies written in the 2018 policy year. It also includes any investment income earned on those new policy premiums.

122 The total equity in the RSR is not related to the policies written in policy year 2018. Leaving aside the capital transfers for a moment, the total equity would normally be associated with variances from forecast of policies written in all prior years. The same would be true with income earned on that total equity. In reality, the link to Basic policies written in the policy year at issue is even more tenuous given that the funds in the RSR are almost exclusively from Extension transfers. Mr. Johnston and Mr. Yien both made this point at the hearing.[58]

123 In actuarial terms, the use of income on total equity to offset costs associated with writing policies in the 2018 policy year is actually tied to the profit provision in the

[56] CAC (MPI) 1 - 1
[57] MPI Exhibit 11: Slide 19

[58] T: 551, 7 -17

Actuarial Standards of Practice. Mr. Johnston was clear that actuarial standards of practice allow this treatment.[59]

124 As discussed in a moment, the application of investment income on total equity to offset the premium rates this year yields a negative profit provision. In other words, rates are not being set to break even.

125 AAP standards of practices are broad, and allow the actuary to apply judgement, and are simply not determinative of this matter. MPI contends that what should be determinative, is if the proposed approach is appropriate to the circumstances of Basic, and makes good business sense.

3.2 Applying RSR Investment Income to Reduce Premium Rates Prices Policies at a Loss

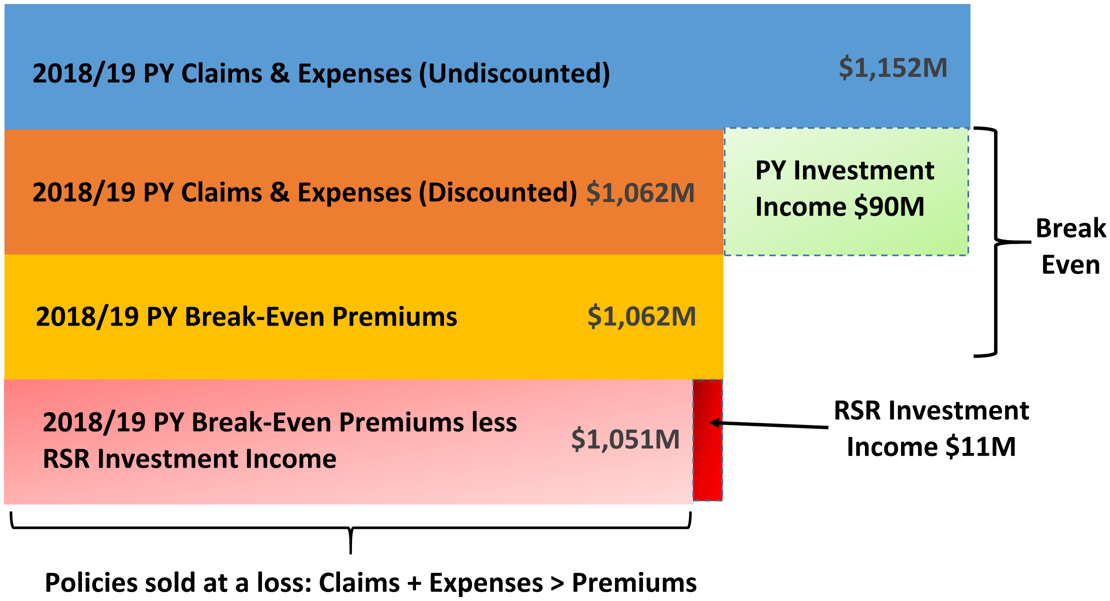
126 Rebating RSR income through policy premiums prices policies at a loss.[60]

127 Today's RSR balance in unrelated to the policies being priced to be sold in the future, and so is the investment income earned on the capital in the RSR. Deducting the RSR investment income from the break-even premium drops the price of the policy below the cost (or discounted claims and expense costs), and prices the policy to sell at a loss.

128 The following graphic illustrates to scale, the impact of reducing break-even premiums by RSR Investment income (narrow red bar), and the impact of the policy year investment income that is already accounted for in premium rates (light green bar).

[59] T: 549, 16 -21
[60] T: 113, 14 -21

1 **Figure 5: Break Even Rate Calculation for 2018/19 Policy Year (PY)**



2 AAP ratemaking is an appropriate departure from the previous 'net-income' ratemaking approach, as it removes the financial impact of past policies from the determination of rates for newly issued policies (particularly through the influence of interest rate forecasts)[61]. The suggested treatment of investment income on total equity re-establishes that link to past policies.

3 MPI's RSR at any given point in time, is a function of variances from forecast of past polices and/or transfers from other lines of business, and is unrelated to new polices yet to be issued. Any reduction of new policy premiums with yet to be earned investment income from total equity is, in effect, a rebate of total equity to new policy holders. A rebate of funds from another source, be it investment income or otherwise, creates a premium deficiency for those new policies on a stand-alone basis.

4 The fact that applying income on total equity to the policies written in this policy year yields a negative profit provision is evident from the calculations and scenarios

[61] MPI Exhibit 1: Investments INV.2.3

that MPI was asked by the PUB to undertake and the formula in Ms. Sherry's evidence. Both of these calculations yield a negative number for the profit provision.

5 Mr. Johnston elaborates on this approach, and how it prices policies at a loss[62]:

> *All – we're saying here, take the claims costs and expenses, take the present value with considering investment income, and charge a rate to break-even. And now we're talking about taking the present value of a profit which would make – basically sell these policies at a - - — at a loss.*

6 MPI's position is that it is appropriate to prospectively set rates in accordance with AAP based on MPI's best estimate expectation of the cost to provide those policies, including a zero profit expectation. This results in a "cost pass-through" approach for each new policy written.

3.3 MPI's Proposal Makes Good Business Sense in the Current Circumstances of Basic

7 MPI's desire to improve its capitalization stems from a legitimate concern around adequate capitalization, and a desire to avoid rate instability that would result from requiring large rebuilding fees from ratepayers.[63]

8 Reducing AAP rates by forecasted investment income on total equity creates a premium deficiency and also inhibits sustaining and rebuilding the RSR.

a) A deficiency in the rates associated with a negative profit provision would (other things equal) result in Basic capitalization losing ground relative to the growth of the business. The MCT ratio – which is the ratio of capital

[62] T: 550, 15- 20
[63] T: 166, 8 -16

available to capital required, expressed as a percentage – would actually decline simply by virtue of the growth of the business (the denominator).[64]

b) With no profit provision or capital build provision in the rate indication, and no retention of investment income on total equity, the only means for the total equity balance to grow is through luck[65]. If the total equity balance remains consistently low, there is an increased risk of needing rebuilding fees to maintain satisfactory financial condition for Basic.

9 Continuing to transfer funds to backstop rates that are set with a negative profit provision and deliberately pricing policy premiums at a loss is not a sustainable course of action. It is not a scenario in which the Board of Directors would envision making further transfers to Basic.

10 Therefore, the issue of rebating investment income is fundamentally tied to the adequacy of the total equity balance, relative to the upper and lower rate stabilization reserve target framework.

11 Within the reasonable limits defined by the RSR framework, MPI prefers to carry more protection than less, hence the notion of an 'optimal range' for the RSR balance. In the optimal range ratepayers are better served by having more protection from adverse results.[66]

12 The CMMG claims that 'one time events' and drawdowns of the RSR have been non-existent.[67] The evidence to the contrary is unequivocal, given $176 million has been transferred into the Basic Reserve[68], and the Board must not also overlook this undesirable trend.

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[64] T: 1710, 24 – 1713, 18
[65] T: 110, 23 – 111, 2
[66] In response to CAC (MPI) 1-113 of the 2017 GRA, MPI explained that 2013/14, 2014/15 and 2015/16 resembled a three year adverse scenario, which resulted in a total equity decline of $143.1 million, notwithstanding a record low collision frequency. MPI's need to improve its capitalization stems from a legitimate concern around adequate capitalization.
[67] T: 63, 3 -7
[68] MPI Exhibit 1: Overview, OV.1.1

3.4 Other Insurers Have Provisions in the Rate Indication to Maintain and Build Capital

13 The total return treatment may be a valid concept for private sector P&C insurers and SGI and ICBC but this is only so because of other considerations that exist for them that do not exist for MPI.

14 Private sector property and casualty insurers earn a positive return on equity. They also carry significant reserves. For example, private sector P&C insurers build a positive profit provision into their rates, and have 150% MCT supervisory capital target, with many choosing to carry reserves in excess of 200% MCT.[69]

15 The capital management plans of SGI and ICBC have maintenance and build provisions in the rate indication. SGI's describes their capital maintenance and build provision in their Capital Management Policy document[70]:

> ***Capital Build and Release Provision***
>
> *The capital build and release provisions are intended to build or release capital through rates in a measured way by reducing rate volatility that would arise if the full amount of any shortfall or excess were accounted for in the rates in a single rate change. The capital build provision requires that SAF recover 1/5 of the deficiency in capital below 100% MCT every year in the base insurance rate. Similarly, for the capital release provision, SAF would release 1/5 of the surplus above 100% MCT into the basic insurance rate every year. SAF will include a capital build or release provision as part of the ongoing rate indication.*
>
> ***Capital Maintenance Provision***
>
> *As SAF's business volume grows through inflationary pressures and vehicle population, an additional amount of capital is required in order to maintain the MCT at its current level. Specifically, the denominator in the MCT calculation (capital required) is increased by*

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[69] PUB Exhibit 11: Attachment to PUB (CAC) 1 – 1, ICBC: Affordable and effective auto insurance – A new road forward for British Columbia, Report Page 179
[70] PUB (MPI)2 -38, Attachment A

> *factors such as higher claim costs and growth in investments. Correspondingly the numerator (capital available) must grow by the same percentage as the denominator in order to maintain the same MCT ratio. Put another way, even if SAF were able to break even on rates every year, MCT would erode over time as the growth in capital required outpaced the growth in capital available. To address this, a Capital Maintenance Provision will be added to the base rate, designed to offset the decline in MCT arising from the overall growth in SAF's business.*

16 MPI does not target a positive profit / capital provision, and in recent years has carried reserves which, but for transfers of excess equity from competitive lines, have been below the lower RSR threshold. These reserves are a fraction of those held by private sector insurers and other crown insurers in Canada.

17 Just as having an RSR reserve in excess of 200% MCT is not appropriate in MPI's operational environment applying the total return approach under the current RSR framework is not appropriate.

3.5 MPI's Approach is Most Consistent With the Current Rate Stabilization Reserve Framework

18 The current RSR framework establishes that customers will not be asked to directly fund the rate stabilization reserve unless total equity falls below the lower threshold, while total equity that exceeds the upper threshold would be eligible for a rebate.

19 MPI's proposal means that it is unnecessary to include a capital maintenance and capital build provision in the rate indication, and that capital will be maintained and replenished organically. The contrary proposal to apply income earned on total equity to price policies below cost means that there is a systemic erosion of the MCT.

3.6 The CAC's Experts are Incorrectly Framing the Issues

20 The RSR balance is not "ratepayer's money"[71], as CAC and its experts suggest, in either law or fact.

21 Section 14(1) of the MPIC act is unequivocal in establishing that MPI an agent for Her Majesty the Queen in Right of Manitoba and all the funds are deemed to be property of Her Majesty the Queen in Right of Manitoba.[72] While the legislative provisions are clear, there is further precedence in the SCC Stores Block decision which finds as principal ground for that decision, that "ratepayers enjoy no property right in the assets used to provide them with service".[73]

22 From a business perspective, insurance premiums flow from the insured policyholders to the insurer who is at risk. As with most any commercial transaction, the ratepayer has purchased a product, relinquishing legal tender in exchange for the good or service. There is simply no credible basis in legislation, regulatory law, or business practice to support the notion that Basic's total equity balance is 'in fact' ratepayer money.

3.7 Concluding Remarks on Pricing Policies at a Loss

23 MPI's essential point is that it is not prudent fiscal management to set premiums below the cost of the policies. This amounts to a rebate of total equity in premium rates, and will exacerbate MPI's thin capitalization, given no other means (exist to counteract the effects), such as a capital maintenance or rebuild provision.

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[71] CAC (MPI) 1-1
[72] CAC (MPI) 2-15
[73] http://www.energyregulationquarterly.ca/case-comments/alberta-utility-asset-disposition-uad-court-of-appeal-upholds-commission-utilities-seek-leave-from-the-supreme-court#sthash.fnSClK9O.E8xDPrra.dpbs

4 COST CONTAINMENT: OPERATING COSTS ARE NOT DRIVING RATE INCREASE

24 MPI's premium rate is based on claims costs and operating costs. Only claims costs are driving the rate increase request. If claims costs stayed flat, Management action on operating costs would have resulted in a rate decrease. Despite business growth, Management has found ways to reduce costs without reducing services.

25 MPI's proposed rate increase already reflects significant efforts by MPI to reduce controllable costs, which are detailed primarily in the "Cost Containment" section of the Application. MPI's ongoing cost containment efforts have allowed the Corporation to absorb inflationary pressures. Operating expenses have decreased by 1.9% and are not contributing to the proposed rate increase.[74]

26 In the following sections of the Closing Submission, MPI highlights the evidence demonstrating the following points:

- First, MPI's Innovation and Cost Containment Committee (ICCC) has a clear mandate to identify opportunities to contain costs and implemented PUB Orders on cost containment.

- Second, MPI has had significant success in recent years reducing costs despite, (a) significant portions of Operating Expenses being fixed through contract or otherwise outside of MPI's direct control, and (b) increasing claims volumes and policies in force.

- Third, in identifying opportunities for operating cost containment, MPI is mindful of maintaining service levels and avoiding unintended increases in claims costs.

74 MPI Exhibit 1: Volume II, EXP , page 9

- Fourth, MPI's efforts in cost containment are reflected in the results of key efficiency benchmarks.

4.1 MPI Has Established a Committee With a Clear Mandate to Contain Costs

27 MPI's ICCC, which is comprised of a cross functional senior leadership team, is responsible for identifying and implementing cost saving opportunities.[75] The ICCC has successfully implemented the PUB's three key orders on cost containment, relating to zero based budgeting, reporting on past savings and identifying additional savings.

4.2 MPI Implemented Zero Based Budgeting

28 PUB Order 162/16, Item 10.4, provided:

> *"In the 2018 GRA, MPI provide a zero-based budget for staffing using actual staffing levels as a starting point for forecasting purposes and demonstrate on that basis, the targeted staffing level reductions identified by the Corporation."*

29 MPI implemented a zero based budgeting approach for staffing using actual FTE with a vacancy allowance. The application of a vacancy allowance ensures that required positions that happen to go unfilled throughout the year are not charged to ratepayers. This approach has resulted in reductions to budgeted and forecasted FTE counts for the years 2017/18 through to 2019/20.[76]

30 As noted by Mr. Yien[77]:

> *Secondly, zero-base budgeting. What does that mean? We're enhancing that process. Zero-base budgeting means to look at our expenses for areas that we don't understand and ask ourselves, Can*

75 MPI Exhibit 1: Volume II, EXP.3.2, page 12
76 MPI Exhibit 1: Volume II, EXP.3.2, page 13
77 T: 103, 6-14

we do better? Can we do with less without sacrificing those things that I talked about earlier? Not only that, what are the areas that we need to challenge ourselves and stretch a little bit,14 as hard as it seems?

4.3 MPI Has Reported on Targeted Savings

31 PUB Order 162/16, Item 10.5, provided:

In the 2018 GRA, MPI report on specific targeted savings forecast in the Application and compare with actual results.

32 In last year's GRA, the ICCC reviewed and identified areas where efficiencies could be realized. Based on this review, MPI committed to a reduction of 15 FTE's. As can be seen in the figure below, these reductions have been achieved.[78]

Figure EXP- 5: 3.2 FTE Reduction in Fiscal Year 2017/18 [79]

Line No.	Classification	2017 GRA	2018 GRA
1	**Clerical**	4	2
2	**Technical/Professional**	9	11
3	**Supervisor**	0	0
4	**Management**	2	2
5	**Corporate Total**	**15**	**15**

[78] MPI Exhibit 1: Volume II, EXP.3.2, page 13
[79] MPI Exhibit 1: Volume II, EXP.3.2, page 14

33 Figure EXP-7 provides an update on savings presented in the 2017 GRA:

Figure EXP- 7: 3.2 Cost Saving Listing - Innovation & Cost Containment Committee - Basic (Estimated)[80]

Line No.	Category of Cost Containment	2017/18FB 2017 GRA	2017/18FB 2018 GRA	2017/18FB Diff	2018/19F 2017 GRA	2018/19F 2018 GRA	2018/19F Diff	2-Year Total 2017 GRA	2-Year Total 2018 GRA	2-Year Total Diff
1	*(C$000s, except where noted)*									
2	**Cost Savings:**									
3	Pembina Service Center, staff reductions (80%)	-	340	340	260	350	90	260	690	430
4	Postage (70%)	560	260	(300)	560	328	(232)	1,120	588	(532)
5	IBM Data Center Operations, operational spend (80%)	1,296	1,262	(34)	1,253	2,213	960	2,549	3,475	926
6	Physical Damage Re-engineering, staff reductions (90%)		-	-	2,250	784	(1,466)	2,250	784	(1,466)
7	**Staffing Strategy:**									
8	Reduction of 15 FTE (80%)	900	1,156	256	900	1,190	290	1,800	2,346	546
9	**Total**	**2,756**	**3,018**	**262**	**5,223**	**4,865**	**(358)**	**7,719**	**7,883**	**(96)**

34 **Pembina Service Centre 5 FTE reductions:** Estimated reduction amounts of $260,000 were expected to occur in 2018/19 based on the 2017 GRA. In this year's filing, not only has the estimated reduction amount increased, but the savings will be realized one year earlier in 2017/18.[81]

35 **Postage:** Reductions of $560,000 per annum were anticipated in last year's GRA. As the Postage initiative did not commence as originally expected, a lower amount of savings has been realized. MPI is still looking at ways in which it can reduce the number of mailings sent out by registered or certified mail.[82]

36 **IBM Data Centre:** The estimates for 2017/18 provided in the 2017 GRA are expected to be approximately $34,000 less than expected in the 2018 GRA. This is

80 MPI Exhibit 1: Volume II, EXP.3.2, page 14
81 MPI Exhibit 1: Volume II, EXP.3.2, page 15
82 MPI Exhibit 1: Volume II, EXP.3.2, page 15

anticipated to be favorably offset for 2018/19 as MPI expects to achieve approximately $960,000 higher in savings than planned during the 2017 GRA.[83]

37 **Physical Damage Re-engineering staff reductions:** In last year's GRA, 25 FTE reductions were expected to occur in 2018/19 for an estimated savings amount of $2.25 million. Based on the timing of these reductions, MPI still expects these reductions to fully materialize but the majority of the reductions will now take place in 2019/20. This is reflected in the $1.4 million variation above.[84]

4.4 MPI Has Targeted Additional Staffing and Compensation Savings

38 PUB Order 162/16, Item 10.6, provided:

> *MPI continue its efforts to find further savings beyond the $9 million identified in 2017/18 and 2018/19 and in the 2018 GRA, file an update with respect to additional cost containment efforts relative to staffing levels and compensation expenses.*

39 MPI has identified the following savings related to staffing and compensation in this Application, which form part of MPI's broader initiative to contain costs:

- MPI committed to a significant FTE reduction of 6.9% or approximately 133 FTE from 2017/18 through to 2019/20 as compared to the 2016/17 budgeted levels.

- MPI has also taken steps to mitigate increases in salary levels, including a zero per cent general wage increase for management personnel in 2017, and a zero merit increase for management personnel in 2017.[85]

[83] MPI Exhibit 1: Volume II, EXP.3.2, page 15-16
[84] MPI Exhibit 1: Volume II, EXP.3.2, page 16
[85] MPI Exhibit 1: Volume I, OV.1.3, page 6

4.5 MPI Identified Additional Savings From Many Sources, Despite Fixed Costs and Growing Business

40 Total Basic expenses represent approximately 19.4% of total Basic costs of the rating years[86]. When compared to the prior year's forecast of the rating years, the current year forecast has decreased by 1.9% in total Basic expenses.[87] These savings were identified from many sources, and despite significant fixed costs and growth in claims volumes and policies in force.[88]

4.5.1 Savings Came from Many Sources

41 MPI identified savings from many sources, underscoring the work the Corporation undertook to contain costs. MPI is well past the stage of "easy wins" in terms of operating costs. As noted by Mr. Yien[89]:

> *"We tried everything we could in terms of limiting the increase…"*

42 These budget reductions reflect careful, sustained attention by MPI to control costs.

43 The sources of these savings include[90]:

- Reducing FTE counts by 6.9% (133 FTE) by fiscal year end 2019/20 compared to the 2016/17 budgeted amount

- Implementing a Management controlled stretch target of $2.6 million in 2017/18 to achieve a flat budget and continuing the stretch target throughout the forecast

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[86] MPI Exhibit 1: Expenses, Exp.3
[87] MPI Exhibit 1: Volume II, EXP.1, page 3
[88] MPI Exhibit 1: Overview, OV.1.3
[89] T: 319, 17-18
[90] MPI Exhibit 1, Volume II, EXP.1, page 2

- Continuance and evolution of the ICCC to monitor and control expenses
- Zero percent general growth increase in the 2017/18 operational budget
- Zero percent growth (no CPI) built into the forecast for 2018/19 and 2019/20
- Reducing Special Service expenses by approximately $1 million in 2017/18 (with these savings continuing throughout the forecast)
- Reduction of overall building expenses throughout the forecast through identification of efficiencies/synergies and subsequent building closures
- Reduction of various initiative related project expenses

44 Figure EXP-1[91] below provides a comparison of the prior year and current year forecasted Basic expenses over the rating years. The Figure shows the composition of the 2.9% reduction in corporate operating expenses, before premium taxes and commissions.

[91] MPI Exhibit 1: Volume II, EXP.1, page 3

Figure EXP- 1: 1.0 Expense Comparison – 2018 vs. 2017 GRA Rating Years

Line No		2018 GRA Avg. of Rating Yrs	2017 GRA Avg. of Rating Yrs	Change (2018-2017)	Change (Percent)
1	*(C$000s, except where noted)*				
2	Basic Allocated Corporate Expenses:				
3	Claims Expense	138,863	137,290	1,573	1.1%
4	Road Safety/Loss Prevention	13,019	14,140	(1,121)	(7.9%)
5	Operating	75,195	83,146	(7,951)	(9.6%)
6	Regulatory/Appeal	4,175	3,604	571	15.8%
7	Total Basic Allocated Corporate Expenses	**231,252**	**238,180**	**(6,928)**	**(2.9%)**
8	Basic Direct Expenses:				
9	Commissions	41,658	41,017	641	1.6%
10	Premium Taxes	32,595	32,353	242	0.7%
11	Total Basic Direct Expenses	**74,253**	**73,370**	**883**	**1.2%**
12	Total Basic Expenses	**305,505**	**311,550**	**(6,045)**	**(1.9%)**

4.5.2 MPI Achieved These Savings Despite Operating Requirements and Growth

45 MPI's ability to realize these significant savings is all the more notable given the extent to which MPI's costs are fixed and business is growing.

46 Normal Operating expenses, including expenses incurred to manage the day-to-day operations of MPI are generally fixed or non-discretionary in nature.[92] Significant costs that fall into this category are compensation expenses, which are 58% of MPI's overall Corporate expenses for 2016/17.[93] Compensation expenses bring with them general wage increases tied to existing collective agreements. Mr. Yien stated[94]:

> *But we're also tied to the existing collective agreements in which there is the gross wage increase, GWI, that's already included. That's not something we can do.*

[92] MPI Exhibit 1: Volume II: EX.3, page 10
[93] MPI Exhibit 1: Volume II: EXP.4, page 19
[94] T: 319, 20 – 320, 1

So those elements are things that are beyond our control that are contributing mainly for that increase.

47 Further, claims volumes and policies in force are expected to rise in the rating years, which could reasonably be expected to increase MPI's operating costs. In addition to projected growth in claims resulting from growth in vehicle volume[95], the 2018/19 total Basic ultimate incurred forecast is $23.5 million or 3.1% higher than last year's forecast.

48 Despite these increases, MPI committed to and achieved a $2.6 million operating stretch target. Mr. Yien characterized the claims stretch target as follows[96]:

Yeah. The -- this -- this was a -- a real stretch. The reason why we call a stretch target is when we put it in as part of regional budget, we really didn't know where we were going to get it from. The goal was really just to keep our budget flat. We knew it was a challenge. The way we came at it was we had a certain -- some number of ideas, and those ideas have gone through what I call prioritization to ensure that it doesn't affect customer service. It doesn't impact projects that are ongoing, driving either an increase cost, or perhaps delaying the cost of that project or completion of that project.

49 Mr. Yien cited the example of being "a little bit more vigilant" on janitorial expenses to highlight how MPI targeted savings anywhere that it could.[97]

50 This type of sustained effort is paying dividends for Basic policyholders.

4.6 MPI is Mindful of Maintaining Service Levels and Avoiding Claims Cost Increases

51 Operating expenses represent a small component of MPI's overall revenue requirement relative to claims costs, meaning that there are limits on the ability of

[95] MPI Exhibit 1: Volume II: RSF.3.1.1, Claims Forecast, page 7
[96] T: 324, 22 – 325, 9
[97] T: 322, 20 – 323, 2

MPI to reduce rates by cutting operating costs. In pursuing cost containment opportunities, MPI must be, and is, cognizant of two factors:

a) First, as noted by Mr. Johnston, there is an inflection point where cutting operating expenses too deep can result in higher claims costs[98]:

> *There's a -- there's kind of an inflection point where not having enough staff can start causing trouble with claims costs. So if you just approve every claim automatically you could have almost no staff. So I want to be careful on that one (1). But per your comment that is true that we are -- appear to be doing more with certain number of claims staff.*

b) Second, MPI's service model needs to be sustained. Mr. Yien stated, for instance[99]:

> *So, you know, cost-cutting is -- is great, but if we are cost-cutting at the detriment of our claimants and our ratepayers that would not be so great. So in some of those areas there are limits in terms of where we can go, I know the Board is cognizant of that as well.*

52 The efficiency benchmarks, discussed next, demonstrate that MPI has struck the right balance.

4.7 MPI's Work to Contain Costs Is Reflected in Efficiency Benchmarks

53 MPI's efforts in cost containment are reflected in the results of key efficiency benchmarks. The results of key 2015/16 benchmark indicators are summarized in the figure below.[100]

[98] T: 376, 22 – 377, 3
[99] T: 371, 13 – 372, 8
[100] MPI Exhibit 1: Volume I, BMK.4.1, page 12

Figure BMK- 1: 4.1 Corporate Performance Results

Line No.	Metric	Corporate Perfromance Measures	MPI 2011/12	MPI 2012/13	MPI 2013/14	MPI 2014/15	MPI 2015/16	Canadian Personal Auto Group 2015/16	Canadian Benchmark Group 2015/16	US Personal Auto Group 2015/16
1	4.1.1	Total Gross Expenses as a % of Gross Premiums Written (GPW)	31.17%	32.01%	30.41%	29.88%	27.89%	35.03%	37.57%	36.86%
2	4.1.2	Total Gross Expenses per Policy In Force	$295	$288	$282	$286	$280	$433	$530	$433
3	4.1.3	FTEs per $100 million of GPW	150.63	153.25	148.33	140.39	130.98	104.57	107.6	103.17
4	4.1.4	Ratio of Staff to Management	7.44	6.83	7.52	7.04	6.64	5.83	6.02	5.76
5	4.1.5	Total Personnel expense per FTE	$ 79,209	$ 79,058	$ 76,872	$ 78,342	$ 81,473	$ 90,735	$ 93,338	$ 105,692
6	4.1.6	Loss Ratio	73.89%	77.75%	88.42%	82.99%	70.90%	66.26%	63.14%	59.96%
7	4.1.7	Net Investment Yield	4.01%	5.88%	7.10%	9.13%	-1.44%	4.00%	3.40%	2.30%

54 Some pertinent observations:

a) MPI's ratio of Total Gross Expenses as a % of Gross Premium Written continues to be considerably lower than the benchmark group[101]

b) MPI continued to have significantly lower gross expenses per policy than the benchmark group[102]

c) MPI's FTEs per $100 million of Gross Premium Written continues to decrease[103]

d) MPI has a "flatter" organizational structure with lower overall personnel and management expenses per FTE[104]

e) Personnel expenses continue to be much lower than the benchmark group[105]

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[101] MPI Exhibit 1: Volume I, BMK.4.1.1, page 13
[102] MPI Exhibit 1: Volume I, BMK.4.1.2, page 13
[103] MPI Exhibit 1: Volume I, BMK.4.1.3, page 14
[104] MPI Exhibit 1: Volume I, BMK.4.1.4, page 15
[105] MPI Exhibit 1: Volume I, BMK.4.1.5, page 15

f) MPI consistently returned more premiums to Manitobans in claims costs than the benchmark groups[106]

g) MPI's claims expenses are significantly lower than the benchmark group[107]

h) MPI's claims expense per reported claim are consistently lower than benchmark groups despite a high claims frequency[108]

i) MPI's reported claims per claims FTE is consistently higher than the benchmark groups[109]

j) MPI's reported claims per 1,000 policies in force is consistently high due to a business model that permits a high claims frequency[110]

k) MPI's FTEs per 100,000 reported claims is consistently lower than benchmark groups, demonstrating effectiveness in managing a high reported claims volume[111]

l) MPI's staff per 100,000 reported claims is lower than benchmark groups reflecting lower staffing levels relative to reported claims[112]

m) MPI's total gross expenses per reported claim is consistently lower than benchmark groups due to effective management of reported claims[113]

55 Mr. Yien observed that the results should be considered in the context of MPI's overall service model, and cautioned against over-focusing on one statistic.[114] However, these benchmarks cumulatively tell a compelling success story.

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[106] MPI Exhibit 1: Volume I, BMK.4.1.6, page 16
[107] MPI Exhibit 1: Volume I, BMK.4.2.1, page 18
[108] MPI Exhibit 1: Volume I, BMK.4.2.2, page 18
[109] MPI Exhibit 1: Volume I, BMK.4.2.3, page 19
[110] MPI Exhibit 1: Volume I, BMK.4.2.4, page 19
[111] MPI Exhibit 1: Volume I, BMK.4.2.6, page 21
[112] MPI Exhibit 1: Volume I, BMK.4.2.8, page 22
[113] MPI Exhibit 1: Volume I, BMK.4.2.9, page 23
[114] T: 371, 13 – 372, 8

4.8 MPI is Also Taking Steps Within its Control to Address Claims Costs

56 MPI is taking action to control claims cost escalation where such action will be effective, while balancing the interests of claimants and ratepayers. Notable steps include the rodent strategy and a collision severity stretch target.

4.8.1 Rodent Strategy Has Brought Material Savings

57 On March 1, 2017, MPI successfully implemented the Rodent Claims Strategy involving a simplified repair process to address lengthy claims durations while ensuring the continued safety and health of our customers. The new process is in-line with common auto insurance practice and in accordance with recent changes in Health Canada guidelines. Since implementation, there has been an average reduction in cost per claim of approximately $2,400. As noted by Mr. Johnston[115]:

> *And in claims incurred, page 15, after two (2) months we had seen an average reduction in these claims of approximately twenty-four hundred dollars ($2,400) per claim. And this allowed us to make a pretty good estimate about -- on terms of what this would -- would save us without, you know, just we're not making something up here. We had two (2) 20 months of data that said twenty-four hundred (2,400), and it seemed reasonable to project that forward.*

58 Taking the 2016 annual rodent claim count of 3,775, this would equate a projected annual savings of approximately $9 million in 2017/18. MPI is also anticipating a decline in frequency, resulting in an additional projected savings of $1 million in 2017/18. For GRA forecasting purposes, a projected annual reduction in claims costs of $10 million per year from the current baseline rodent claims forecast. These assumed savings are incorporated into the Comprehensive claims forecast.[116]

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[115] T: 995, 13-21
[116] MPI Exhibit 1: Volume II, CI.2.9, page 14-15

59 MPI was asked why it hadn't implemented the rodent claim control strategy sooner. Mr. Yien replied[117]:

> *So simple elegant solutions don't simply happen. It involves a collaboration of understanding what the process is, perhaps maybe even the nature of what things are being fixed, including the entire process. So we do have to go through that process to discuss and finally agree that the net impact to both the claimant, the repair, as well as to the Corporation from a liability and future potential liability needs to be. So it's essentially a very balanced approach and does take some time.*

4.8.2 MPI Has Taken Initiatives to Address Collision Severity

60 Vehicles continue to become more expensive to repair as a result of advanced technology embedded in vehicle parts prove to collision damage; and as more technically advanced repair techniques become mandatory. In an effort to control physical damage claims severity growth going forward, MPI[118]:

- trained all claims staff on estimating standards;
- created an internal group to decide on controversial estimates;
- rolled out shop-specific key performance indicators emphasizing the importance of estimate accuracy;
- offered courses to body shops on estimating standards; and
- had Shop Relationship Advisors work with shops to improve shop standards.

61 There is evidence of a reduction in collision severity starting in December 2016 and MPI believes that this favourable experience is at least partially caused by the

[117] T: 998, 11 – 999, 2
[118] MPI Exhibit 1: Volume II, CI.2.9, page 15

Management actions described above. MPI anticipates additional savings going forward, but there was only 3 months of data, so MPI was unable to provide a detailed breakdown of the Management action impacts. However, based on the observed evidence to-date, Management has targeted to reduce physical damage claims cost by approximately $9 million over the base case forecast in the 2018/19 accident year. For GRA forecasting purposes, the stretch target was built into the forecast by (i) reducing the total loss severity growth rate by 0.50% for all physical damage forecasts and (ii) assuming a lower Collision repair frequency trend than the original forecast.[119]

62 Mr. Johnston expressed confidence in the initiatives based on early results[120]:

> *…at least to date as of about the end of August, we are seeing favourable progress on these [Key Performance Indicator] targets. So I can say from a actuarial rate setting perspective that I continue to have confidence that the management actions in the previous slide related to claims are -- are on target.*

4.9 Concluding Remarks on Cost Containment

63 MPI's efforts to control operating and claims costs have made a difference, as evidenced by the fact that operating costs are not contributing to the proposed rate increase, and management action on claims costs has reduced the requested rate increase. As Mr. Yien highlighted in his opening presentation, MPI will continue to investigate, identify and implement operating cost reduction initiatives:

> *We will continue to look for areas where we can have cost reductions. In fact, moving forward, we'll be building a dashboard to ensure that we are continuously identifying opportunities to drive savings without sacrificing service, without sacrificing the deliverables that we have committed to, and it's evidenced by actions to reduce operating costs in the budget.*[121]

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[119] MPI Exhibit 1: Volume II, CI.2.9, page 17
[120] T: 118, 2-7
[121] T: 102, 21-103, 3

5 THE DRIVER SAFETY RATING SYSTEM

64 One of the unique and arguably most creative actions taken by management to reduce the 7.7% rate indication (as initially presented to MPI by its Chief Actuary, Luke Johnston) was to increase revenue by $17.5 million through changes to the Driver Safety Rating (DSR) system. If the changes are approved by the Public Utilities Board, the overall insurance premium rate paid by all drivers will be reduced by 1.8%.

65 In this section MPI elaborates on the following points:

a) The DSR system incents good driving behavior, and MPI’s proposal in this GRA will be effective both for drivers who respond to the incentives, and those who don’t;

b) The changes to the DSR proposal are a statistically driven policy decision, designed to ensure that incentives for good driving are preserved through the transition year; and

c) Manitobans support the idea that riskier drivers should pay more.

5.1 The DSR System is Intended to Incentivize Good Driving Behaviours

66 The DSR Program has been in place now for 7 years, first implemented by the Corporation in 2010. The purpose of the DSR Program is set out in subsection 2(2) of the *Driver Safety Rating System Regulation* 13/2009:

> ***2(2)*** *”The purposes of the driver safety rating system are to rate a person based on the input factors recorded in his or her driver record, or on the absence of input factors in the record over time, for the purpose of determining the premium that the person must pay for a driver's certificate.”*

67 The "input factors" specified in the regulation relate primarily to *Criminal Code* and *The Highway Traffic Act*, and *Driver Licensing Regulation* offences. The "input factors" are intended to discourage poor driving behavior. As is evident from the Traffic Collision Statistics Report 2016 poor driving behavior is the cause of most collisions.

68 The DSR Program devised a scale upon which drivers are positioned depending on their driving experience – assigning demerits for at fault accidents and traffic convictions. Put simply, the "good drivers" reside on the merit side of the scale and pay less in driver premiums and the "bad drivers" reside on the demerit side of the scale and pay more in driver premiums. Driving one full year without an accident and conviction free moves a driver up the scale while at-fault accidents and convictions result in movement down the scale.[122]

69 To date, since inception, there have been no changes to the premiums charged to drivers under the DSR Program. The corporation is proposing changes to the demerit side of the scale that is projected to produce an additional $17.5 million in revenue to offset an otherwise required 1.8% increase for all rate payers.

70 At its core, the DSR and the proposed changes employ a "user pays" pricing approach. If a driver engages in the poor driving behavior they will have to pay a higher driver premium. If they do not engage in this poor driving behavior they will not pay more.

71 If the incentives to drive safer are effective, the corporation, in turn, will not realize its increased revenue projections. By way of an extreme example, if each and every driver on the demerit side of the scale were to avoid accidents and convictions by driving safer for one full year, the corporation would not collect any of the projected $17.5 million. While that scenario is obviously highly unlikely, it would be an outcome the corporation would publicly celebrate due to the decrease

[122] MPI Exhibit #7, PUB (MPI) Pre-Ask 6, Appendix 1

in claims, both personal injury and property damage, which MPI, expects would exceed the loss in revenue.

72 Mr. Johnston explained[123]:

> *"And we believe that rather than just acri -- applying across-the-board increase, particularly to the merit side, that we'd be better served by focusing on the highest risk drivers, not only to provide a better match to claims costs and premiums but also to potentially and incent – improve driving behaviour, which could give us some, perhaps, additional favourable results in our -- in our claims forecast."*

73 And Mr. Yien elaborated[124]:

> *"When we really read through it, it sounds like, Okay. Well, we're just trying to find a way to increase premiums. But ultimately I think the net positive effect is the driver has control over this. And, in fact, if drivers remain safe we don't even want this premium, because ultimately what is going to happen in our business is if people are driving safer it's going to reduce claims incurred. It's amazing result."*

5.2 This Management Action is Effective with Drivers Who Respond to the Incentive, and Those Who Don't

74 What makes this particular management action so unique is its dual purpose. If the changes do not result in a positive change in driving habits the corporation will receive the $17.5 million from the "bad drivers"; however, if the changes directly incent better driving habits and increase road safety, this will invariably result in less accidents and lower claims costs. All of these objectives and potential outcomes are what makes the proposed changes to the DSR such a creative solution in lowering the initial rate indication.

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[123] T:506, 8-16
[124] T:508, 8-15

75 It is important to note that the proposal will ensure that no driver on the demerit side of the scale who had clean driving experience in the past year will pay more than they did last year. Improved driving behavior will continue to be rewarded through the transition year to the new scale.

76 By doing so, MPI is making driver premiums more reflective of the risk those drivers are imposing on the system – on all Basic policyholders. People who cause more accidents would, under actuarially driven ratemaking, pay premiums reflective of risk. The proposed changes to the DSR achieves this objective within the constraints of the existing DSR framework. The best result is one where drivers change their high risk behavior and stop imposing additional costs on all Basic customers.

77 The proposal is fair because avoiding higher premiums is entirely within every driver's control.

78 The cross-examination by counsel for the Board focused almost exclusively on the extent of statistical alignment at certain DSR levels. The statistics are important, but in MPI's submission, this approach will miss the forest for the trees. Drivers on the demerit side of the scale are there because they have engaged in high risk driving behaviors. Mr. Johnston provided a succinct response during part of his explanation[125]:

> *Q: "So when we look at the -- the right of that -- the far right of that graph, at the minus 10 -- 20 level, it's indicating that the current premium is $3553, which falls short of an average claims cost of $4245 which would indicate a need to increase the driver premium at that level?"*
>
> *A: "There's -- as you go into the demerit levels on to the negative side, there's thankfully less drivers that live on that negative 20 area. And just -- just so everybody understands what it takes to be negative 20 on the scale. It's about two points down the scale for a minor conviction, minus 5 for an at-fault collision. I believe it's minus 10 for a -- a DUI. So it -- you've got to do a lot of things to get down*

[125] T:524

the bottom of that scale. But thank -- thankfully, there's not a lot of drivers down there."

5.3 The Proposed DSR Scale Changes are Statistically Driven

79 In response to a suggestion that the proposed increases across the DSR levels was purely policy driven, and not statistically based, Mr. Johnston clarified that the proposed changes to the DSR are "a policy decision based on statistical information…".[126]

80 It matters not that traffic convictions, which move drivers down the DSR scale, do not result in direct claims costs for the corporation. Movement in this regard is legislated under the *Driver Safety Rating System Regulation* (Regulation 13/2009) and the corporation has no choice but to move drivers down the scale based on "input factors" over their annual rating term. As stated above, the poor driving behavior reflected in the "input factors" are the cause of most collisions. . Moreover, Mr. Johnston testified that statistics now show that drivers with more traffic convictions are riskier drivers and cause more accidents[127]:

Q: "So we have collisions where the drivers are at fault and received demerits. We also have convictions whether they're Highway Traffic Act or possibly criminal and the driver receives demerits."

A: "Correct."

Q: "So -- but in respect of those conviction demerits, there's not necessarily a claims cost associated with the assignment of those demerits."

A: "There is not a direct -- as a collision obviously has a direct cost. But that -- the -- going back again to the DSR application, the conviction experience was seen to be just as strong of a predictor of future at-fault claims as a -- as accidents. And I suspect if you are someone who's speeding or running red lights or not wearing seatbelts, it's only a matter of time 'till you kind of join the at-fault

[126] T:541
[127] T:532

accident club there; right? Like it -- it -- those behaviours are going to lead to accidents. So since DSR has been put in, and what we're hoping for, again, this -- this time around with -- with increases to the bottom, is that customers will get that message, that those types of behaviours have financial consequences and -- and hopefully they'll do as they did in the first iteration of DSR and have less of them. And they've -- the conviction behaviour has improved dramatically since DSR is implemented. And the at-fault claims experienced at the bottom of the scale has also improved dramatically."

81 Again, the proposed changes are fair, and an effective deterrent.

5.4 Manitobans Support the Idea that Riskier Driver Should Pay More

82 The proposed changes also have the support of Manitobans. During cross-examination by Board Counsel, Mr. Ward Keith, VP of Business Development & Communications and CAO, said the majority of Manitobans believe that people who exercise high risk driving behaviors should pay more for insurance.[128]

83 Later in his testimony he was asked to provide the results of annual surveys that supported his assertion that the public thinks higher risk drivers should be paying more in premiums. Undertaking Number 17 was the result, which corroborated Mr. Keith's evidence:

Do poor drivers pay too little, too much or about right for their vehicle insurance?

	2017	2016	2015	2014
Too little	**50%**	**51%**	**57%**	**57%**
About right	42%	42%	38%	39%
Too much	8%	7%	5%	4%

[128] T:679

84 There is clearly a shared interest on the part of MPI, the PUB and all Interveners in reducing the social and claims costs associated with collisions. Mr. Keith spoke about the progress made to date, but also that further work needs to be done. Risky driving is contributing significantly to the frequency of collision.

85 The Driver Safety Rating Program is a rate structure that incents safer driving. From its introduction in 2010, the DSR data shows that this type of rating scale - a bonus/malus system – works quite effectively. The proposed changes to the premiums will be an incentive for those drivers who engage in high risk behavior with unacceptable regularity to be safer drivers.

5.5 The Proposed Changes to the DSR are Statistically Driven

86 Mr. Johnston made the point that one of the issues with examining too closely the difference between costs and driver premiums at the demerit end of the scale is that there are too few drivers at the lower end which means the data has little or no “actuarial credibility”. That is, the discrepancy is always going to vary year to year at the lower demerit levels. While explaining for Board counsel Figure REV – 30 (Projected Premiums and Claims Costs per Driver by DSR Level), Mr. Johnston had the following to say[129]:

> *“Yes, and that really stems to my – my last point. There are less drivers in that section of the curve. And we have to make a selection. We don’t – you can see the line sometimes goes up and down and we’re not going to charge less for minus 13 than we charge for minus 12, for example.”*

87 And;

> *“We’re trying to get our premium ask from the highest risk drivers based on the graph you have here with the -- we believe a well-supported based on the -- green line increased to the demerit side of the scale. There’s no – again, guided by the green line that you see. And it’s a lot more stable on the merit side where there’s a lot of*

[129] T:524

drivers and then it becomes more sporadic at – at the demerit side. There is no attempt here to match perfectly every single level the dollar amount. Next year that line will be up and down, based on the variability of the claims for minus 16 type drivers."[130]

88 When it was suggested to Mr. Johnston under cross-examination that the DSR is not statistically driven, he said the following[131]:

> *"I would – looking at this graph I would say it's very statistically driven. So, I'm struggling – if your point is just the green line doesn't match the red line, then I agree with you, but there is definitely an upward trend in the green line and we're basically directionally moving our driver premium rates to have demerit drivers pay more of their fair share to that green."*

5.6 The Proposed DSR Changes Will Improve Road Safety Including for Vulnerable Road Users

89 Aside from meeting the primary objective of achieving a revenue increase of 1.8% from driver premiums, the benefits on the Road Safety/Loss Prevention cannot be overstated. During his cross-examination, Mr. Keith explained it more eloquently than can be paraphrased herein[132]:

> *Q: "And I'll save most of my questions about driver safety rating and fleet rebates to -- for Mr. Johnston –"*
>
> *A: "M-hm."*
>
> *Q: "-- but at a high level, we can agree that driver safety rating, there's some pretty supportive evidence that it's had a – a positive impact in terms of the mitigating the likelihood of -- of the collisions, agreed, sir?"*
>
> *A: "Yes, and as well as in influencing safer driving behaviour. I do think that's an important point, Mr. Williams….But with respect to the*

[130] T:526
[131] T:527
[132] T:926

broader issue of driver safety rating, you -- you know, there can be criticism about that we're not doing enough to protect vulnerable road users, and motorcyclists, or all road users, for that matter. I know there could be questions about the actuarial science behind how the premium was established for each level of the DSR scale, which I am certainly not an expert to -- to discuss. But -- but I'm the road safety guy, and so when I look at the opportunity here that exists for us to demonstrate some real leadership in terms of taking a stance on high-risk driving behaviour, and -- and being very clear that -- that people who -- who exhibit high-risk driving behaviours on the road, high-risk drivers will pay more for their insurance, and the high-risk driving activities of these drivers are not going to be subsidized by other insurance ratepayers. And by the way, if you are a high-risk driver, you have -- you and you alone have the power not to have to ever pay those additional premiums that are proposed. So you have the power as a high-risk driver not to be one (1) of the individuals to contribute to that $17.5 million. The way to do that is to improve your driving behaviour….So I think we have a real opportunity here to, at a higher level, be able to do much more to protect cyclists, to protect pedestrians, to protect motorcyclists, to protect all road users by getting at the high-risk driving behaviour in a very tangible and very financial way that will send the message that, if you continue to exercise these kind of behaviours, you will pay more."

90 The current rating scale establishes progressive steps for drivers to move up and down depending upon their driving behavior. The PUB should embrace this opportunity to strengthen the DSR incentives and resist placing too much weight on any misalignment between cost and premium at one or perhaps two DSR demerit levels. The evidence of Mr. Johnston was that these will align after just one year.[133]

5.7 Concluding Remarks on the Driver Safety Rating System

91 MPI's proposal is the right thing to do -- it's fair. It lowers the rate indication by 1.8% and agreeably dovetails with road safety objectives and the public perception

[133] T:526

that high risk drivers should pay higher premiums. Statistics maintained by MPI since the DSR was introduced also show that claims can be expected to decrease.

92 Risky drivers have the ability to avoid paying higher premiums by improving their driving behavior, and the reward for good driving is preserved in MPI's proposed changes to the DSR scale.

93 MPI's proposed changes to DSR scale are statistically driven, and achieve the policy objectives of the DSR system as set out in Regulation. MPI's management action to reduce the rate request on all ratepayers, focusing instead on demerit drivers is in the public interest.

6 INVESTMENTS

94 In this section, MPI expands on the following points:

a) The most significant aspect of 'Investments' for this year's GRA is the proposed corporate bond allocation to 18% of the current investment portfolio. The corporate bond strategy relies on the following factors:

- The Asset Liability matching study is now underway as part of the corporate bond strategy
- RSR upper and lower targets
- Approval of Actuarial indicated rates without offset against RSR investment income.
- Approval by the Minister of Finance

b) The Minister of Finance is ultimately responsible for MPI's investment portfolio, and MPI cannot unilaterally direct investment strategy.

c) The adoption of AAP ratemaking has diminished both the impact of, and risk associated with, the interest rate forecast, by shortening the forecast horizon. MPI's proposed "compliance filing" approach to update the interest rate underpinning premium further reduces interest rate forecasting risk.

6.1 Corporate Bond Strategy

95 The advice from the Corporation's Chief Actuary was that MPI would require a 7.7% rate increase in order for Basic to achieve its target of operating on a break-even basis.[134] The MPI Executive and Board of Directors decided an increase of this magnitude was not acceptable and took immediate Management Action to reduce the required rate indication.

[134] MPI Exhibit 1: Ov.2, page 13

96 Part of these actions were to examine the investment portfolio to determine if there was a strategy available to increase the investment return, thereby reducing premium rates. An allocation to corporate bonds was recommended to the Executive on the basis that it was possible to implement; provided a reasonable corporate bond allocation relative to peer comparisons and provided a material reduction to the basic rate indication going forward.[135] By raising the corporate bond allocation to 18%, the rate indication is reduced by 0.8%.[136]

97 The Investment portfolio is primarily intended to raise revenue to pay for future cost of existing claims. The primary purpose is not to reduce future premium payments. As such the Board of Directors are prudently cautious.

98 There are a number of conditions precedent to the strategy, listed below in no particular order:

- Approval by the Minister of Finance (by Order-in-Council)[137]
- Completion of Asset Liability Matching Study[138]
- Rate Stabilization Reserve (RSR) Targets of $201 million (lower) and $438 million (upper)[139]
- Approval of actuarial indicated rates without offset against RSR investment income[140]

99 The corporation intends to sell holdings from the corporation's marketable bond portfolio (Government of Canada and Province of Manitoba bonds) to purchase approximately $427 million[141] in additional corporate bonds. The current corporate bond allocation is approximately 3% of the fixed income portfolio and 2% of the

[135] MPI Exhibit 1: Inv. 2.2.1, page 14
[136] MPI Exhibit 1: OV.2.2, page 14
[137] T: 1410, 6-16
[138] T: 1459, 2-5
[139] T: 1340 - 1341
[140] T: 1341
[141] PUB (MPI) 2-24(a)

total investment portfolio.[142] The proposal would see the corporate bond allocation increase to 18% by March 1, 2018.[143]

100 Of importance here is the corporation's intention to add Triple 'B' rated bonds as an allocation. As explained by PUB witness Garry Stetski, Assistant Deputy Minister for the Department of Finance (Treasury Division), the addition of Triple 'B' rated bonds would require an Order-in-Council, i.e. approval by the Minister of Finance, because Triple 'B' rated bonds are not a permitted class of investment under *The Financial Administration Act*.[144]

101 In addition, the Minister of Finance has the ability to simply reject the investment strategy if he feels it contains something of concern to the Minister's Office. Mr. Stetski testified that if there was something the Minister was uncomfortable with he would tell MPI not to proceed.[145]

102 Having said that, in his direct examination, Mr. Stetski testified that his office would be supportive of MPI's proposed change to the investment portfolio having been fully informed of the strategy by MPI's investment department.[146]

103 For this particular condition precedent, the question becomes whether approval by the Minister of Finance can reasonably be expected? The evidence of Mr. Stetski was that during his tenure as a member of the Investment Committee Working Group (8 years), the Minister had endorsed two categories of investments not permitted under *The Financial Administration Act* – investments in real estate and infrastructure were approved by Order-in-Council.[147] Indeed, the only investment that Mr. Stetski was aware of that did not meet with Minister approval (before Mr. Stetski's time with the Department of Finance Treasury Division), was a proposal by MPI that it be allowed to invest in international equities.[148] Ultimately this proposal was not approved because of its proximity to the financial crisis of 2008. At the

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[142] PUB (MPI) 1-40
[143] T: 26, 5-9
[144] T: 1410
[145] T: 1409
[146] T: 1398-1399
[147] T: 1411-1412
[148] T: 1418

time this made eminent sense. However, Mr. Stetski did confirm during his direct exam that if the corporation was today to make a proposed change to invest in international equities, there would be no concern from the perspective of the Department of Finance.[149]

104 In further answer to the approval question above, consider that corporate bonds -- unlike the investments in infrastructure and real estate (but approved nonetheless) -- are a permitted class of investment under The Financial Administration Act, so long as the bonds are rated 'A' minus or higher.150 The Triple 'B' bonds identified for purchase by the corporation are the main reason the corporate bond strategy requires Ministerial approval.151 Triple 'B' bonds are an essential part of the strategy if the desired result of an increased yield to the fixed income portfolio is to be achieved. Mr. Stetski confirmed for the Chairperson during his testimony that he expected Triple 'B' bonds would yield a higher return than the non-marketable bonds issued by Manitoba municipalities, school divisions and hospitals (MUSH bonds), which bonds now form a large part of the MPI investment portfolio.152 However, Mr. Stetski could not say for certain whether corporate bonds in the 'A' minus category would yield a higher return than MUSH bonds.[153]

105 The other important factor when trying to gauge whether the corporate bond strategy would meet with Minister approval is the confidence held by Mr. Stetski in the MPI Investment Committee and the influence Mr. Stetski has over the Minister's final decision making authority:

> *Q: "And so, sir, based on your earlier comments about the qualifications and -- and the competency of the investment committee members, is it fair to say, sir, that you would have complete confidence in the investment committee's ability to properly and prudently manage and make decisions concerning MPIC's investment strategy?"*

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[149] T: 1389
[150] T: 1385-1386
[151] T: 1385-1386
[152] T: 1433
[153] T: 1434-1435

A: "Absolutely."

Q: "So a short way of saying that, sir, is, in your view, the ratemakers -- or the ratepayers, sorry, of the Corporation are in good hands with the investment committee?"

A: "Yes"[154]

106 And:

Q: "If, given your familiarity with the Investment Committee sitting as an observer at some of the meetings, and your active role in the Working Group, is it fair to say that as it concerns the investment strategies emanating from the Working Group and the Investment Committee, the Minister might seek your input with respect to any particular strategy?"

A: "Yes."

Q: "And has that, in fact, happened in the past?"

A: "Yes.?"

107 The Department of Finance supports MPI's corporate bond strategy:

Q: "Are you able to comment on the views of the Department of Finance with respect to this requested change?"

A: "Well, I guess, generally adding corporate bonds at that level is going to add an element of risk to the portfolio. However, in the context of the -- the information that was provided by the investment department outlining what similar portfolios do with regard to this, it's - it's not out of line. So, we would be supportive." [155]

[154] T: 1408, 10-23
[155] T: 1398, 18-1399, 2

108 Given all of the foregoing, it seems reasonable to expect that Ministerial approval will be forthcoming as it concerns the corporate bond strategy as currently proposed.

6.1.1 Asset Liability Management Study

109 By PUB Order 162/16 the Corporation was to have completed and filed as part of the 2018 General Rate Application an Asset Liability Management (ALM) study. Compliance with this Order proved difficult given the time constraints. However, in order to implement the corporate bond strategy, due diligence required a completed ALM Study. As such, the Investment Committee directed Management to expedite the ALM Study.

110 The Request for Proposal was issued in September 2017[156] and the successful Vendor (Mercer Canada)[157] selected in early October. The asset liability study, all three phases, is expected to be completed by November 30, 2017.[158]

111 MPI is of the view that providing Mercer with an upper threshold for the Rate Stabilization Reserve will result in a more meaningful asset liability study because the authors will know the potential parameters of what may be invested. The ALM study is currently underway and Mercer is aware that MPI is seeking an upper RSR target of $438 million.[159]

112 During his cross-examination by counsel for the Consumers' Association of Canada (Manitoba), Acting VP of Finance and CFO Peter Yien had the following to say about the importance of the ALM study and its completion by November 30, 2017[160]:

Q: "And is there magic, sir, in the date of November 30th, 2017?"

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[156] T: 1443
[157] T: 1444
[158] T: 1445
[159] T: 1456
[160] T: 1045, 21-1047, 5

A: "Maybe you could define "magic". I'm not sure what you mean."

Q: "So does -- to the extent that you're able to share, does Manitoba Public Insurance have a particular reason why it's aiming for November 30th, 2017, sir? Is it part of the planning process? Is it -- where does it fit within the planning process of MPI?"

A: "Sure. That's a -- that's a great question. There's been lots of discussion to date in this hearing talking about our business strategy. Part of our business strategy does involve, where do we invest and how do we invest? And that's -- that's a very -- the ALM study, the asset liability matching study, is a critical input to that. Another critical input would be the PUB order. So the magic, if -- if I could define it, is having all of that come together. So we have enough information for the Board to exercise -- to do governance under decisions. The decision on asset liability matching also hinges on the PUB Order. And I had said this earlier, of having the right rate stabilization lower limit, rate stabilization reserve upper limit, and when we have all of that in front of us, including charging the right rates that I talked about earlier, applying the actually accepted principles that you talked about earlier, as well, then yeah, that's the magic. We have to have all the ingredients at the same time, call it information, in front of the Board [MPIC Board of Directors] to make an informed and prudent decision to drive the fiscally responsible actions that one needs to take."

113 Later in his testimony, Mr. Yien was asked by Board counsel about the results of the ALM and what might happen if Mercer recommended against the proposed corporate bond strategy[161]:

Q: "And if Mercer does not recommend an 18 percent allocation to corporate bonds, what would the corporation do with that information?"

A: "I think the Board would review and -- and, again, go back to some of the assumptions as I said earlier, some of those constraints and assumptions are being informed. And we would -- the board would definitely exercise its due diligence to challenge those assumptions, understand how that compares with our peer group, I mentioned that earlier, that's important as well. And if it's truly

[161] T: 1450, 10-1451, 4

financially not sound, not prudent to buy 18 percent bonds, we – we wouldn't do it. We don't think that's a very likely possibility, but, yeah, in a theoretical question, if -- if -- if it's a different numbers, I don't think the board will override that and -- and effectively abdicate proper governance."

114 In the opinion of Mr. Yien, a witness with a wealth of experience in financial matters, the possibility of the ALM study not matching the proposed increase in corporate bonds is very unlikely. It therefore seems reasonable to expect this condition precedent, the ALM study, to be met.

6.1.2 RSR Upper ($438 million) and Lower ($201 million) Target Range

115 MPIC is willing to take on the additional investment risk in corporate bonds provided there is sufficient capital available to absorb any potential negative return. This reasoning was supported in the cross-examination of Mr. Stetski by counsel for MPI[162]:

Q: "Sir, we've heard evidence in this proceeding from Mr. Yien, the VP of Finance for MPIC, that in order for the corporate bond strategy to proceed, the Corporation would like to have se -- some security that it has adequate reserves in place. Were you aware of that?"

A: "Not really, but..."

Q: "Okay. Did you have an opportunity to review any of the evidence that Mr. Yien gave at this proceeding?"

A: "I've scanned some information related to investments."

Q: "Okay."

A: "But I have not read everything that's been said at the hearings."

[162] T: 1415, 24-1417, 11

Q: "So were you aware, sir, that there is a connection at least, between the corporate bond strategy and capital reserves?"

A: "Yeah, I believe -- yes, there is connection there. Yes."

Q: "And you've indicated, sir, that the move to increase the allocation to include more corporate bonds is a riskier-type investment. Would you agree with that?"

A: "I agree with that."

Q: "More so than it was, or is, for government bonds?"

A: "Yes."

Q: "And the MUSH bonds, as they call them?"

A: "Yes."

Q: "And with – with the higher risk, sir, would it make good prudent financial sense to have a capital buffer in place, if we're going to move into that area of investments?"

A: "I would think that would help mitigate that risk, yes."

116 The RSR range with approved targets of $201 million (lower) and $438 million (upper) would provide a measure of financial security whereby the $237 million range would be protected from total equity rebates. The investment income earned on the money in the RSR, whether it be $205 million or $435 million, would be retained by the RSR to either grow the RSR or replenish it in those years when an unexpected drawdown of capital is required.

117 In order for the PUB to assist MPI implement the corporate bond strategy (and to allow Basic to achieve long-term financial strength), the PUB needs to understand the rationale for the prerequisites. As Mr. Yien testified in redirect[163]:

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[163] 1339, 13-1341, 20

Q: "Thank you. And for -- and for Mr. Yien, Mr. Yien, I believe it was on Friday at the end of your cross-examination by my friend Mr. Williams, you indicated that the Corporation would require from the PUB its upper and lower requested RSR targets, or it wouldn't proceed with the corporate bond strategy. Do you recall that?"

A: "I do."

Q: "And sir, at least from my perception, this, to me, almost sounded – it almost sounded like an -- ultimatum. Is that the message that you wanted to convey to the Board on this -- on this issue?"

A: "Absolutely not. We have a high level of respect for the PUB. As I state -- said in my opening remarks, one (1) of the reasons why I'm here is to represent the voice of the Board, and the Board would like to move forward with continuous collaboration with the PUB. I don't like the word 'ultimatum', because it's disrespectful, and certainly, that's -- that's not the way we want to go, and I hope that no one really perceives it that way."

Q: "So there are legitimate business reasons for not proceeding with the corporate bond strategy in the absence of the upper and lower RSR targets?"

A: "Absolutely. Again, going back to my opening remarks, the Board would like to run MPI Insurance as a leading insurance company irrespectful [sic] of what has been done in the past, or how it was run. And if I can use the analogy of a tricycle, there are three (3) key components to build that, a strong, sound insurance company. The first is the appropriate rate stabilization range that we can operate in. And I re-emphasize the word 'range', because any time when we have a target, it generates rate shock, because if we have a number that we are aspiring to, take any number, once we go above it, it's rebate; once we go below it, it's rebuilding fee. So we -- we guarantee a shock. And so having that right range is appropriate. The second is in the investment income. There's been discussions already about the investment income itself is money set aside to pay for future claims. They specifically relate to our liability, with some level of an uncertainty, and we want to keep that money so that we can pay the claims as they become due and not offset that investment income for reducing rates. They relate to past policies and past claims. And then the third is using the right proper interest rates, actuarial best estimates, using the AAP, the actuarially accepted

> *principles. And those are the three (3) wheels, if you will, of a -- of a tricycle that the Board really believes in in terms of having those conditions to be there."*

118 The corporate bond strategy involves a number of moving parts. The four conditions of its implementation are interdependent. The Investment Committee and Minister of Finance require an Asset Liability Management study in favor of increasing the allocation to corporate bonds. Ideally, the authors of the ALM study would have an upper RSR target to allow them to know what investment amounts are at risk. The RSR must have a wide enough range to absorb volatility, there must be assurances that total equity will not be rebated prematurely, and there must also have a mechanism for growth of total equity (no offset of RSR investment income against actuarial indicated rates). The corporation requires all four before it can proceed with the corporate bond strategy, which will benefit ratepayers by lowering premiums.

6.1.3 Approval of actuarial indicated rates without offset against RSR investment income

119 The strategy to be employed, if approved by the PUB, will include growing (and replenishing) the corporation's total equity by using investment income generated by the RSR. However, if RSR investment income is used to reduce premiums, i.e. to lower rates, the RSR will not grow. Indeed, if RSR investment income is not retained by the RSR, the RSR will eventually be depleted over time due to unexpected and unforeseen events.

120 This does not provide the MPI Board of Directors with the comfort it requires to depart from the portfolio allocation currently in place and proceed with a riskier investment strategy.

121 As acknowledged by MPI in this rate application (and confirmed by Mr. Stetski during his cross-examination), with the increase in corporate bonds comes greater

risk.164 While there is an expectation that the corporate bonds will produce a higher investment return, there is of course the possibility that the projected investment income will not materialize in any given year. If RSR investment income is protected from the rate setting process (ratemaking), the "bad years" become more manageable, and ratepayers are at less risk of being charged an RSR rebuilding fee.

122 This condition precedent falls upon the Public Utilities Board.

6.2 The Minister of Finance is Ultimately Responsible for MPI's Investment Portfolio

123 Although the Corporation and the Department of Finance jointly advise the Minister of Finance on the investments, the Minister of Finance is ultimately responsible for the Corporation's investment portfolio[165]. Neither MPI, nor the PUB, can unilaterally direct investment strategy. The PUB's consideration of MPI's investments must account for the limits on bodies' jurisdiction.

124 Pursuant to section 14(1) of *The Manitoba Public Insurance Corporation Act* all moneys acquired by the Corporation are deemed to be the property of Her Majesty in right of Manitoba. Section 12 of that Act requires the Corporation to pay to the Minister of Finance all the moneys that are in its reserves so that the Minister can invest those moneys. These moneys form part of the government's Consolidated Fund and are to "be invested in accordance with *The Financial Administration Act*."

125 The Minister of Finance is ultimately responsible for investing the moneys of the Corporation[166], and MPI cannot unilaterally direct investment strategy.

[164] T: 1417
[165] T: 1409
[166] T: 1372

6.3 Reducing Interest Rate Forecast Risk with the Compliance Filing outweighs perceived procedural fairness concerns

126 There were questions at the hearing about MPI's proposal to set premium rates using the naïve forecast as of November 30, 2017. MPI referred to this proposal in the Application and in other written materials as a "Compliance Filing" proposal. The choice of wording appears to have given rise to some confusion. The proposal, in essence, is straightforward:

127 MPI will undertake to file on December 1:

1. the interest rate on the 10-year Government of Canada bond rate as published by Bloomberg at market close on November 30, 2017; and

2. an explanation of how that interest rate will affect the overall indicated premium rate, holding all other factors constant;

128 Following this update, the PUB issues its decision in early December, stipulating the approved interest rate, and premium rate that informs the overall rate indication;

129 MPI follows its usual practice of making a Compliance Filing that accounts for all changes flowing from the PUB Order, whether relating to interest rates or otherwise. Through the compliance filing, the PUB will provide final approval of detailed rates, and rates by major class, based on the overall indicated premium rate that is generated based on Bloomberg's published November 30th 10-year Government of Canada bond rate.

130 This proposed approach only differs from the current approach in two respects. First, the proximity of the forecast date is two months later than usual. Generally, the PUB asks MPI for information current to September 30, or sometime proximate to the hearing, and bases its decision (which is usually after November 30 anyway) on that updated information. Second, MPI's proposal is to use a naïve forecast rather than the Standard Interest Rate Forecast.

6.3.1 November 30, 2017 Data is the Most Current Information Practical

131 Using information current to November 30, rather than September 30, has three benefits:

132 It allows the PUB to use the most up to date information practical in setting the premium rates. In a perfect world, rates for the policy year commencing March 1, 2018 would be based on interest rates as at February 28, 2018. This is obviously not practical. Using interest rates current to November 30, 2017 effectively reduces the period over which the forecast can vary to three months.

133 Using the most up to date information in tandem with rate setting based on Accepted Actuarial Practice, minimizes MPI's exposure to interest rate forecast risk, and sets premium rates on a best estimate basis.

134 In the event stakeholders are convinced that interest rates are going to rise, the approach provides an additional two months for that to occur.

6.3.2 Use of the Naïve Forecast

135 The proposal to use the naïve forecast as at November 30, rather than the SIRF makes sense given the proximity of the forecast date to the start of the policy year. Whereas in past years under the "break even approach" the forecast was required to extend over 2 years. However, the period of time in issue is much shorter under Accepted Actuarial Practice.

136 There is a significant body of evidence that the naïve forecast is a best estimate for rate setting purposes under AAP[167]. Further, MPI's Appointed Actuary, Mr. Joe Cheng endorses the naïve forecast for the base scenario in the DCAT.[168]

137 The adoption of AAP ratemaking has diminished both the impact of, and risk associated with, the interest rate forecast, by shortening the forecast horizon. MPI's proposed compliance filing approach to update the interest rate underpinning premium rate reduces interest rate forecasting risk.

6.4 Concluding Remarks on Investments

138 MPI's corporate bond strategy is reasonable and implementable, and with appropriate due diligence and pre-conditions in place MPI believes that the corporate bond strategy can be approved by the Minister of Finance.

139 There are good business reasons for MPI's conditions for the corporate bond strategy, including having adequate capital to support riskier investments, and an ALM study to ensure appropriate due diligence.

140 MPI's proposal for interest rate forecasting reduces interest rate forecasting risk to the extent possible, and uses an objective market based forecast of interest rates. Concerns around procedural fairness are misplaced. The PUB and parties to the this proceeding have had opportunity to test all aspects of MPI's application, and the proposed interest rate forecast is a single variable, outside of MPI's control. MPI has explained the proposed process, and the provided a sensitivity analysis allowing the PUB and parties to approximate the overall rate indication based on the prevailing market interest rates.

[167] MPI Exhibit 1: INV.2.3

[168] PUB (MPI) 2-7 Attachment A

7 INFORMATION TECHNOLOGY

141 Information technology (IT) is essential in any modern business. MPI pursues IT initiatives that ensure security, and system reliability, as well as enhance the customer experience. IT initiatives support the business strategy, and MPI has a demonstrated track record of delivering IT initiatives on time and on budget.

142 MPI has a value management process that is maturing and formalizing elements such as business cases. MPI recognizes there is a level of transparency demanded by the rate setting process, and MPI is intent on both understanding what information is useful and relevant to the PUB's determination of just and reasonable premium rates, and delivering that information.

143 In this section, MPI elaborates on the following points:

a) MPI's IT initiatives deliver value to ratepayers, and reduce risks. IT initiatives have various drivers, and initiatives are often not discretionary.

b) MPI's IT strategic plan must support the corporate business plan, and will be developed once corporate strategic direction is set.

c) MPI's value management process is evolving and becoming more formalized, and will deliver business cases for significant capital expenditures, and post implementation reviews to demonstrate value.

d) Gartner continues to find that MPI's overall IT maturity is improving, and MPI is successfully implementing an external staffing strategy driving savings.

7.1 MPI's IT investments Reduce Risk and Deliver Benefits to Ratepayers

144 MPI pursues IT investments that are targeted at reducing risks related to information systems, from a security, reliability and customer service perspective. MPI's IT systems must be protected from security threats, in order to protect sensitive information. IT systems must operate at high availability, to ensure that customers are served. These kind of investments deliver benefits to ratepayers, in terms of customer experience and peace of mind.

145 MPI's IT investments are driven by one of following four distinct drivers[169]:

- **Strategic Planning**
  Processes where ideas for new projects and products are vetted through senior management to determine if they align with the corporate strategic goals.

- **External Events**
  External forces that cause MPI to act or respond. An example of this would be legislative changes.

- **Societal changes**
  Response to occurring social changes. Examples of this type of change include waiving deductibles for vandalism claims and the immobilizer initiative (which was in response to soaring vehicle theft rates).

- **Technical requirements**
  Response to technology obsolescence or risk mitigation. These series of initiatives ensure that the corporate infrastructure and software platforms remain current and on supported versions.

[169] MPI Exhibit 1: IT Information Technology p.5

146 Some of these drivers are inherently discretionary, while other simply are not. IT investments related to Strategic Planning are at the discretion of the Board of Directors and Management to ensure that MPI meets the mandate established by the Government.

147 By contrast, investments related to technical requirements, or external drivers offer little room for discretion. Prudent operation of MPI's IT assets requires that MPI invest as necessary for the security and reliability of the systems. When vendors release system updates, it is beneficial and often necessary for MPI to remain current with the releases. Falling behind often results in longer, larger, more complex, and more costly projects.[170]

148 Similarly when Government makes legislative changes IT expenses must be incurred in order to reflect those changes. The majority of MPI's ongoing IT investment is driven by external events or technical requirements. These expenses must be incurred in order to fulfill legislative obligations or to keep IT systems operating and secure. These investments are not made in the context of a positive cost/benefit financial metrics because the cost of not doing them is often incalculable.

149 MPI's corporate strategic direction will be developed this year, and during this time of transition, MPI has a limited set of IT investments planned during the rating years. These investments are a continuation/completion of existing projects, or to address a technical requirement that must be completed. Inflight projects are being completed, and MPI's IT budget reflects the prudent investment decisions that are required to ensure systems are secure, and customers are well served.

150 The initiatives planned for rating years that are extensions of existing projects are[171]:

[170] MPI Exhibit 1: IT Information Technology p.6
[171] MPI Exhibit 1: IT page 8

- **Human Resources Management System Phase 3 & 4**
  this project is planned for completion in 2018/19. The project details were provided in the *2013 GRA Volume III AI.18*

- **Customer Claims Reporting System**
  This project is planned for completion in 2019/20[172], and is a key element of PDR. Further details of the PDR program are provided in Gartner's independent review in *Volume I Physical Damage Reengineering*.

- **Customer Self Service**
  This project is in the early planning stages. The Corporation intends to launch an on-line services capability for high volume/low complexity transactions and services which are currently causing customer service delays at MPI Service Centers.

151 The following projects in the rating years are driven by technical requirements[173]:

- **Technology Risk Management**
  This program is a suite of projects will keep existing technology in a stable and supported state and address other technology risk through process and technology improvements. These projects are planned for the current budget year, through the rating years.

- **AOL/CARS Replacement**
  This is a significant project MPI anticipates scoping in 2018/19. In 2018/19, the Corporation will assess and establish a strategy and business case to upgrade or replace the AOL/CARS legacy systems.

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[172] MPI Exhibit 1: PDR Attachment A, PDF page 14
[173] MPI Exhibit 1: Information Technology, page 9

7.2 MPI's IT Strategic Plan Will be Driven by Corporate Business Strategy

152 Since its appointment in mid-2016, MPI's Board of Directors has been deliberate and thorough in assessing the MPI's business, in order to prudently set the Corporate strategic direction. In December of this year, MPI's Board of Directors will establish the business direction for the company to follow under its leadership.

153 Once the business direction is established, MPI will be in a position to develop an IT strategic plan that will support this corporate strategic direction. Information technology exists to support the business, and the IT strategy must therefore support the business strategy. These two strategies are fundamentally linked through an order of precedence.

154 In his testimony, Mr. Yien elaborated on the purpose of an IT strategy, and its subordinate role to the business strategy[174]:

> *MR. PETER YIEN: And our timelines, we fully expect that the -- the strategic plan to be completed in Q4 of this year. So before March 1st, we would have it completed.*
>
> *MS. KATHLEEN MCCANDLESS: Okay, so it would be filed in next year's GRA.*
>
> *MR. PETER YIEN: Absolutely.*
>
> *MS. KATHLEEN MCCANDLESS: Generally, can you comment on what the purpose is in creating an IT strategic plan.*
>
> *MR. PETER YIEN: The purpose of creating an IT strategic plan involves I think really three (3) things: The first one (1) is just ensure that we're inline with the business strategy. That's -- that's critical that's important. A lot of that relates into the more innovative value creation type projects. They -- they -- they're a little bit*

[174] T: 413

> *different. And those –- for those types of projects with not having anything new until we have the new business plan in place.*

155 With Corporate strategic direction pending, MPI has been operating under the framework of the 2016 IT Strategy[175], which is for all intents and purposes remains MPI's the tactical plan for IT investments. This plan includes

- The Basis for the IT strategy, including Architectural Drivers and Principles
- Key Drivers for Change (Business Drivers and Information Technology Drivers)
- The Corporate Roadmap of Strategic IT Initiatives

156 MPI continues to operate according to these principles, and respond to the change drivers as outlined in this strategy.

7.3 MPI's Value Management Process is evolving, and becoming more formalized

157 In last year's GRA, MPI introduced the latest evolution of the value management process, and with this GRA, MPI has continued to elaborate on its approach to formulating initiatives, and monitoring the costs and benefits. MPI has consistently sought to implement new initiatives that will add value to the experience of customers, employees and stakeholders, and value management is integral to delivering these initiatives.

158 MPI's Value Management process formally evaluates initiatives at every step from concept to implementation to ensure that each initiative effectively addresses the business challenges and opportunities that MPI deals with on an ongoing basis.

[175] 2016 GRA: Volume I IT Strategy

159 MPI's Value Management process follows a systematic approach to ensure that results and benefits are accurately captured, and that initiatives reflect and support corporate goals.

7.4 Appropriate Governance Oversight and Accountability: Value Management Process

160 In this section, MPI outlines the evidence demonstrating that it has appropriate governance and oversight mechanisms in place for IT. MPI has clear accountabilities and uses a Value Management Process to define the expected benefits and the expected cost of new investments. The value management process also ensures that the expected benefits and costs are achieved after new investments are implemented.

161 MPI's Value Management Process consists of the following components[176]:

- <u>Business Case Development</u> – The Value Management Process requires that business cases be completed for all initiatives involving investments over $500 thousand.
    - Business Case development follows an iterative approach. The first phase of the process, known as the Thin Business Case, consists of a high-level presentation of the new initiative.
    - If the concept is approved by Senior Leadership, additional time is spent further investigating and documenting the key qualitative and quantitative elements of the proposal.
    - The second phase of the business case development is the Detailed Business Case; in this phase:
        - All sections of the business case template are to be completed in this phase.

[176] VM Value Management p.3

  - The financial analysis business case template is completed to support the financial projections of costs, benefits and cash flow implications based on detailed documented assumptions.

- Business Case Approval – Business cases involving projects defined as capital projects are approved by the Executive Committee and MPI's Board of Directors as part of the corporate capital budgeting process.

- BTO Project Delivery - The mandate of the Business Transformation Office (BTO) is to guide the transformation of business operations throughout MPI. Accordingly, this department represents the project implementation capabilities of MPI and is accountable for the planning and successful execution of strategic corporate initiatives and projects approved and prescribed by MPI's Executive Committee. BTO has an overall management team that oversees the execution of the portfolio of approved projects.

  The BTO Project Delivery Methodology guides projects through 7 phases of project delivery. Project schedules are managed through the use of status reporting and project delivery controls. Project delivery controls are a means to check that specific criteria have been met at periodic phases during a project's lifecycle.

  BTO manages projects to budget through the monthly preparation of a number of internal financial reports. These financial reports are then reviewed by BTO management to confirm that the portfolio is tracking to budget. Next, the project financials are reviewed by the BTO Steering Committee, and where appropriate members of BTO and Finance management teams meet collectively with their Executives to review the project financials. On a regular basis, the Board of Directors is presented a status update on all strategic initiatives. At that time, any variance or risk to budgets or timelines are brought forward as well as the planned corrective actions.

- Post Implementation Reviews - As part of the Business Case component of the Value Management Process, all business cases are tracked to final resolution.

The primary purpose of the Post Implementation Review is to assess and report on:

- Project Deliverables – As outlined in the business case and, where applicable, any additional or revised deliverables as documented in the project plan or charter documents.
- Project Benefits – As outlined in the business case and, where applicable, any additional or revised benefits during project implementation. This will include both quantitative and qualitative benefits.
- Project Financial Summary – Comparing actual costs to project budgets
- Lessons Learned - Focus on what was done well along with improvement opportunities and recommendations that impact the Value Management process.

7.5 The Value Management Process is Evolving, and Becoming More Formalized

162 Under cross examination, Mr. Yien explained how MPI's Value Management process is more than just a 'business case'[177]:

> *MS. KATHLEEN MCCANDLESS: And so when you say that those existing projects for technology modernization are following -- following "the value management process," perhaps you could just fill me in on how they're following the previous value management process.*
>
> *MR. PETER YIEN: Sure. The value management process is about keeping accountable for project that we decide to execute. So it starts with the generation of ideas; are they challenged? They get challenged in the previous value management process through various forms. It could be challenged at the executive level, or one (1) level down before the idea even gets discussed any further. After that, the -- the idea gets refined, gets further discussed. And then ultimately at some point they'll say, Well, are we ready for this? From a technology people/technology process perspective. And with that the case, there is some sort of a write-up on it. It may not look like a*

[177] T: 405

business case but it gets shared. And it gets shared through email or through meetings and then after that point, there's discussions on, How do we calculate the benefits? What are the costs associated? And we have to bounce that off through others that may have done it before. I said yesterday, sometimes we share with our colleagues. Our comparative organizations, like SGI and others, for example. So after those discussions happen, we start to refine and start to frame what that benefit looks like. The cost a little bit more difficult. Particularly, if we're doing something new. And so we through that process of building it. I just want to differentiate the difference between the past and now. The future means that all of that information is captured in one document, which we call a business case. When I said earlier that we follow value management process that was a little bit different, is all those things are being done, including all the way down to when we approve a business case. Management approves the business case through an executive committee meeting.

The Board reviews the benefits of that business case and all that information as part of that meeting. Moving forward though, the business case becomes a very integral part of it. It just means capturing all that information in one spot, for ease of reading, for ease of review. So that is new. So in the past, the projects have gone through that process.

163 Mr. Yien also explained how the Value Management process is being formalized to ensure that the business case document is completed for substantial initiatives[178]:

MS. KATHLEEN MCCANDLESS: So does -- does that mean that the -- if we -- I won't name them all, but they -- the four (4) technology modernization projects that we were just looking. Would they have had business cases?

MR. PETER YIEN: They would not have what we'd characterize as a one-document with the business case, no, that's the refinement.

MR. PETER YIEN: Yeah. Let me clarify that before I answer your next question. I don't want to give the impression that we don't have business cases. What I will say, is we don't consistently have a one-document that describes everything. So we do have business cases

[178] T: 407

for some projects, is the way we envision it currently, moving forward in the future. That's kind of the newer refined standard. We have information that effectively if you mapped it to a business case, you could re – you could redo that, if you will. We could fill in the blanks using the new templates, that just takes time. So we do have that information. So essentially, the refinement is more formal documentation.

164 Mr. Yien further explained that the formal business casing process will be applied to all business cases over $500,000[179]:

MS. KATHLEEN MCCANDLESS: Thank you. So, the Corporation then -- its IT governance process at this time to ensure they manage correctly according to budget, et cetera, that is now the value management process is going forward.

MR. PETER YIEN: Yes. Their managing of budgets again has always been there. I just want to emphasize the -- the key point is really the thresholds in which we decide to build a business case. We've also refined the business case template in itself, so that, you know, everything from ease of reading, to putting a little bit more rigor in what goes and it, essentially.

MS. KATHLEEN MCCANDLESS: So the threshold for what requires a business case, what is the thresholds set at now?

MR. PETER YIEN: Five hundred thousand dollars ($500,000). And just to put in perspective, that's exactly our capitalization policy. So it aligns perfectly. So in the future if our capitalization policy changes then the value management process would be, again, refined or updated to reflect the same capitalization target

165 Finally, Mr. Yien elaborated on the benefit of condensing the value management process into a single business case, and how the formalization of this step is an improvement to MPI's Value Management Process[180]:

MR. PETER YIEN: Yeah, in an ideal world, I would totally agree that we would have business cases for everything. And that -- that --

[179] T: 411
[180] T: 419

that's certainly a best practice. There are some times when the business case itself will evolve and needs to be updated and I also believe that that's important when circumstances change. So I do agree with you that having the business case itself in one (1) document is extremely valuable, but I would also need to think about if a business case was there, but without the proper governance of review, challenge, discussion, generating of that idea whether it is a good idea or not, enhancing that, doesn't happen in a business case. When I refer to a value management process, I'm talking about the entire process of getting to a business case. So having a business case is actually important, but we need to continue our valuement -- process -- our valuement procces -- our value management process which included all of the other thing -- factors that I talked about. So, yes, we do need to be more formal. Although we discuss the value of the benefits and -- and the costs. The documents do exist, but it's in one (1) document, then there's another document, then there's another document. Do we need to put it together in one? Absolutely. And I think moving that would create simplicity of review moving forward. So the risk is, it is possible to answer your question. The risk is it is possible that through that process we might miss something. So having everything at one (1) spot is actually helpful to ensure that we've got everything.

MR. PETER YIEN: The past process was more informal, and we recognize that that's an area that we could improve, and hence the new value management process creates a more formal process.

7.6 Gartner's IT Assessment is Favourable

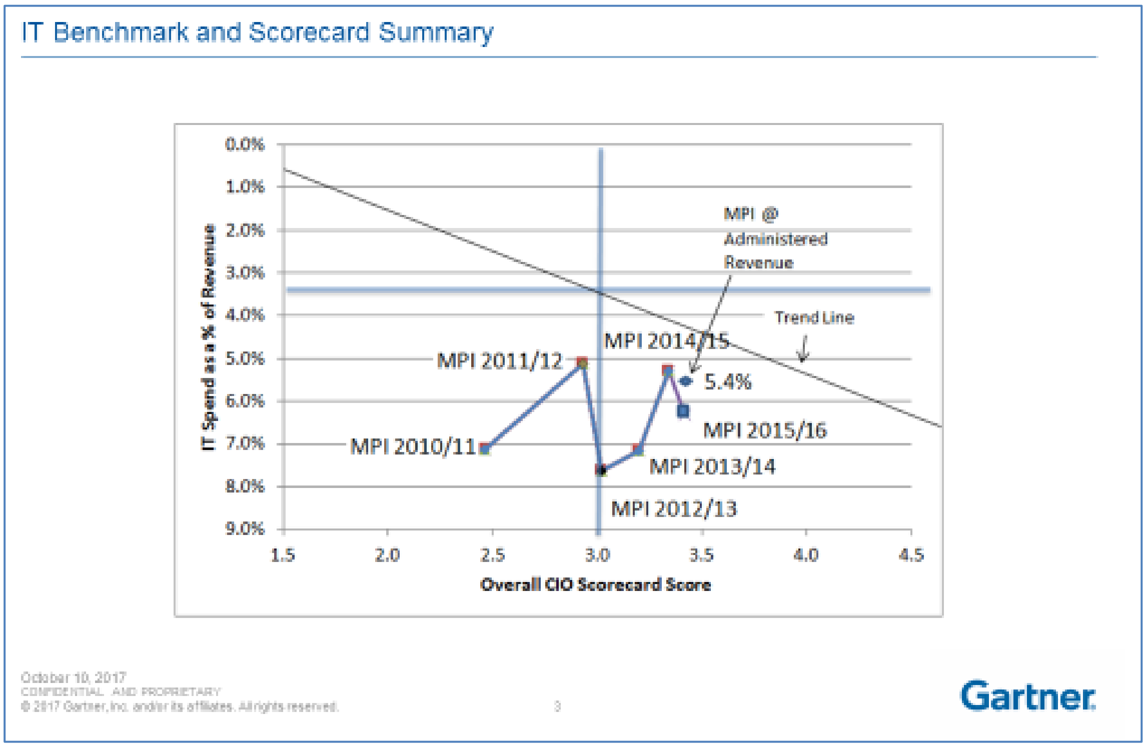
166 MPI engages Gartner Consulting, a leading information technology research and advisory company to conduct IT benchmarking on an annual basis. Mr. Geffen testified[181]:

We – as part of Gartner – part of Gartner's consulting practice, we have a rigourous, pure, structured peer benchmarks that we do. And we've been doing these benchmarks for MPI year over year for a number of years as – as I say, and we really focus on three(3) things

[181] T: 1121, 1-9

> *in – in their IT operating costs, process maturity and readiness for sort of align – IT alignment with the business.*

167 The fact that MPI retains Gartner year after year, demonstrates MPI's commitment to improving IT infrastructure and operations, while increasing accountability and reducing costs. Gartner's reporting shows that MPI has made significant progress and continues to be well positioned when it comes to IT. Below is a graphic representation of MPI's overall CIO Scorecard Score.[182]



168 Mr. Geffen noted that the graph demonstrates a good result. In 2010-2012, MPI undertook technology modernization required after a number of years of low technology investment, which increased IT Maturity. Since implementation of those modernizations, MPI has significantly reduced the cost as part of operating revenue.[183] Mr. Geffen noted that a slight increase in IT spend as a percentage of

[182] MPI Exhibit 17: page 3
[183] T: 1124-1125

revenue was not material, especially considering the business transformations spearheaded by MPI in recent years.[184]

7.6.1 Gartner IT Benchmarking and CIO Scorecard

169 The evaluation instruments that Gartner uses, and the objectives of that review, are as follows[185]:

Three structured evaluation instruments	Provide the following outcomes
▪ IT Spend Analysis ▪ CIO Scorecard ▪ Infrastructure & Operations Scorecard	▪ Evaluate the relative maturity of the IT organization ▪ Assess the IT organization's ability to react to rapidly changing business requirements ▪ Compare relative funding levels of IT at MPI ▪ Compare MPI's infrastructure and operations costs, staffing and service levels with those of similar enterprises

170 Gartner's methodology is described further in the Application.[186] It is important to note that the timing of the Benchmarking exercise does not allow the CIO scorecard to be filed with the PUB in the same year it is completed. The CIO scorecard available to the PUB in a given year only reflects progress up to the previous year.

7.6.2 MPI's IT Spend as a Percentage of Operating Expenses has Gone Up Indicating Successful IT Investment

171 MPI's IT spend as a percentage of revenue has increased 4.7% during the last 5 years, while peers have increased IT spend by 5.1% from 2012/13 to 2015/16. A

[184] T: 1149-1150
[185] MPI Exhibit 1: Volume 1, BMK Attachment A
[186] MPI Exhibit 1: Volume 1, BMK Attachment A

better measure for MPI is IT spend as a percentage of operating expenses since MPI is not focused on increased revenues.[187] MPI's spend as a percentage of operational expenses rose from 5.40% in 2014/15 to 6.10% in 2015/16 due to a reduction in operating expenses which is often an indication of successful IT investment.[188]

7.6.3 "Catch-up" Spending has Stabilized

172 MPI's proportion of IT spend on activities that are focused on running the business (vs. growing and transforming) is in line with the peer group. The proportion of IT spend related to growing the business has steadily exceeded that of the peer group. As "Catch-up" spending has stabilized, running the business has remained relatively stable.[189]

> *"In terms of the -- the allocation of that spending, the catch-up spending is the spending on that 20-year problem has stabilized and the foc -- focus now is on business improvement and so we see MPI spending money more on technology that's looking to transform the business or to -- to grow the business."*[190]

> *"So we see that -- that when we compare to peers, the Run The Business spending is in line with peers and the sum of grow and transform is -- is -- is in line with peers. MPI is spending more on the grow the business than on the transformation which prob -- makes sense for an organization of the type that MPI is."*[191]

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[187] MPI Exhibit 1: Volume I, BMK.5.1.1, p 33; & MPI Exhibit 1: Volume I, BMK Attachment A, PDF p 7
[188] MPI Exhibit 1: Volume I, BMK.5.1.1, p 35
[189] MPI Exhibit 1: Volume I, BMK.5.1.2, p 37
[190] T: 1127, 7-12
[191] T: 1128, 5-11

7.6.4 IT Employee and Consultant Counts are Steadily Decreasing

173 MPI's IT FTEs as a Percentage of Company Employees ratio remains higher than the peer average but this ratio is reflective of the number of IT initiatives that MPI has undertaken. The initiatives underway include the automation of business processes, with one of its goals being to reduce overall staffing requirements of the Corporation. Thus, the higher ratio of IT FTEs is reflective of objectives aimed to increase overall efficiency of the Corporation.[192] Mr. Geffen referred to MPI's IT workload and the fact that some of the workload is regulatory and that MPI does not necessarily have control over those aspects[193]:

> *You know, on one hand, it is more than peers, and so the -- to that degree with -- it is higher than what we would expect. On the other hand, we do know that there's a -- a heavy workload that -- that's since -- sort of -- PDR's, you know, get to completion, and then with insertion of work, I -- MPI doesn't always have control over that level of -- of work that needs to -- needs -- needs to get done.*

174 From 2012/13 to 2014/15 MPI has steadily decreased the proportion of consultants. There has since been a slight increase in the proportion of consultants from 34% in 2014/15 to 35% in 2015/16 which reflects the number of IT initiatives MPI has undertaken.[194]

175 Mr. Geffen noted[195]:

> *MPI has -- has taken -- taken significant efforts to transition significant positions that were filled by third-party contractors or -- into staff -- into staff roles which we -- we see as -- as a really positive step.*

176 Mr. Geffen further testified that contractors could be used to target specific skills and may be a way to deal with a high salary market or for situations where the skill

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[192] MPI Exhibit 1: Volume I, BMK.5.2.1, page 38
[193] T: 1158, 16-23
[194] MPI Exhibit 1: Volume I, BMK.5.2.2, page 39
[195] T: 1127, 16-21

set is only required for a specific period of time.[196] In terms of bringing consultant positions in-house, Mr. Geffen testified that[197]:

> *Do you -- you know, can you afford -- can you meet market -- market rates, can you find the skills yourself, and do you want to make long-term investments? And so it's those kinds of things in terms of -- continue to have a look at that.*

7.6.5 MPI Continues to Improve its Maturity, Driving Effectiveness

177 MPI improved its overall Maturity rating to 3.42 in 2015/16 from 3.34 in 2014/15.[198]

Figure 6: Maturity Rating and IT as a % of OpEx[199]

	Maturity Score	IT as a % of Opex
2010/11	2.46	7.8%
2011/12	2.93	7.2%
2012/13	3.02	7.8%
2013/14	3.2	6.9%
2014/15	3.34	5.4%
2015/16	3.42	6.1%
2015/16 Peer	2.84	5.6%

178 MPI's year-on-year work improving IT maturity will have a positive impact on the quality and cost of IT initiatives. For example, nearly all of MPI's new applications have been delivered on-time and on-budget.[200] Increased maturity should help MPI contain costs providing leverage in new initiatives.[201]

[196] T: 1151-1152
[197] T: 1157, 8-12
[198] MPI Exhibit 1: Volume I, BMK Attachment A, PDF page 5
[199] MPI Exhibit 1: Volume I, BMK Attachment A, PDF page 8
[200] MPI Exhibit 1: Volume I, BMK Attachment A, PDF page 6
[201] MPI Exhibit 1: Volume I, BMK Attachment A, PDF page 7

7.7 BI3 Has Delivered on Business Case Objectives

179 For this year's GRA, MPI commissioned a post implementation review of the Business and Injury Improvement Initiative (BI^3). Ernst and Young (EY) was retained to assess the achievement of the BI3 business case objectives.

180 EY performed a detailed review of the benefits from BI^3 that accrued to the quality service, and PIPP claims administration. EY assessed qualitative and quantitative benefits, and established that BI^3 had met the business case objectives.

181 On the qualitative indicators, EY confirmed that the BI^3 project did resulted in an IT systems renewal that enhanced operational effectiveness.[202] At its core, BI3 was an initiative to digitize PIPP claims administration, with a claims administration system. EY confirmed that BI3 implemented a best in class document management and claims management capabilities, that achieved benefits across nine areas of the organization.

182 EY also reviewed the quantitative benefits of the BI^3 program confirming that productivity improvements resulted in $9.53 million in savings. EY also confirmed that the duration of closed claims was reduced by 4.3 days, exceeding the four day target identified in the business case, resulting in savings of $35.01 million.[203]

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[202] MPI Exhibit 1: BI3 Attachment A , PDF page 4
[203] MPI Exhibit 1: BI3 Attachment A, PDF page 5

8 PHYSICAL DAMAGE RE-ENGINEERING IS ON THE RIGHT TRACK

183 The Physical Damage Re-engineering Project (PDR) will fundamentally change the way that MPI handles physical damage claims.[204]

184 As noted by Mr. Yien[205]:

> *It's a transformative project that will streamline operations and make our customers' cars get fixed easier; directly to the repair shops.*

185 PUB Order 162/16 10.10 directed MPI to obtain and file an independent assessment of the development and roll-out of the PDR project. The PUB asked for information on the progress of the pilots, the timing of implementation, the costs of the project and anticipated savings.[206] MPI retained Gartner, a leading information technology research and advisory company to conduct an independent[207] evaluation of the PDR program. Gartner’s May 26, 2017 report can be found in Volume I of the Application as Attachment A to the PDR section. Gartner’s findings, summarized below, demonstrate that PDR is on the right track.

8.1 The Evolution of PDR Has Preserved the Original Objectives

186 Gartner found that MPI had made significant strides in completing projects and streamlining the remaining projects so that only the projects that add to the business case will be pursued to completion.[208] Mr. Geffen testified[209]:

> *The PDR program has been -- is going through a number of exercises in terms of the -- the - - the scope and the approach as -- as one*

[204] CAC (MPI) 1-63
[205] T: 28, 6-8
[206] MPI Exhibit 1: Volume I, PDR, page 2
[207] CAC (MPI) 1-62(a) Attachment A and (b) Attachment B, PDF page 13
[208] MPI Exhibit 1, Volume I, PDR Attachment A, PDF page 3
[209] T: 1129, 1-23

would expect a large -- a large program -- a large multi-year transformational program to do"

"It has transitioned -- reported last year from a complex initiative that was made up of five (5) different subprograms and twenty (20) projects within those programs. All of that over the past year, as I've said before, the pace has -- has ramped up. MPI has completed eight (8) projects. MPI has cancelled seven (7) projects after determining that they're not strategic and do not add to the business case. So, the PDR team in -- in each of its stage gate, so MPI takes each of its program -- projects through a number of stage gates and at certain stage gates an assessment was -- was completed for those seven (7) projects, and it was determined that given the additional spending, the returns were not as -- as significant as originally projected and the projects were -- were cancelled. Money had been -- has been reallocated from those projects to some of the ongoing projects.

187 Mr. Geffen testified that it was not unusual for the scope to change on such a large project and that MPI has been successful in making sure that scope changes were purposeful and considered[210]:

Well, as -- as I -- as I responded to -- to the Chair, the, you know, in -- in the -- in a -- a large program such as this, it's not unusual to see a change direction in -- in -- over time. It's not unusual to change scope or change right -- right where you actually -- where you're allocating your -- where you're spending the money.

And one (1) of the important things that we've seen for our clients is to assist just a bit beyond that is that where you have a large-scale project -- program such as this, it's important to maintain -- to main -- maintain focus on where you're going, but constantly do kind of a -- a risk assessment, an in -- internal risk assessment is always changing in a purposeful way, and have we made purposeful decisions in terms of the kinds of changes we -- we want to make?

We've -- we see some organizations that'll embark on a pro -- program like this, and it all sort of slowly drift over time. And that, you know, you get called to do a -- a program postmortem, and you

[210] T: 1278, 11 – 1279, 18

kind of wonder, How do you end up over here, when you were aim -- aiming for over here?

And I think that if I were to -- maybe a bit colloquially, I would say if -- if PDR was kind of aiming over here, I think that it has had a lot of focus over time terms of direction, and it's ending up sort of over here, but that the dir – directive change has been purposeful over time, that it -- that every change has been considered, discussed at, you know, at -- at the first -- at the project level, at the management level, before making a -- a change to the project -- the program direction.

188 Gartner determined that MPI had implemented practices and procedures to deal with issues that require close monitoring[211] and that MPI had reduced much of the prior concerns about the potential for additional cost, extended timelines and deferred benefits realization.[212]

Costs continue to be consistent with those projections. Benefits projections continue to be consistent as they were last year, but they will take -- or projected to take a -- a -- a slower ramp up and longer to come to a steady state. And then that the -- the ques -- a new question that was added this year is about maintenance. Again, that is -- at the highest level of maintenance is accounted for in oper -- in operating budgets …[213]

189 Mr. Yien addressed the evolution of PDR as follows[214]:

And program management is really important because we need to look at the overall benefits and whether we can achieve it. And this is a really important point because as these projects are cancelled it would determine that the related benefits are either not with it, meaning that any additional costs that are incurred is not worth doing. Or that the benefit is already met

[211] MPI Exhibit 1, Volume I, PDR Attachment A, PDF page 16-17
[212] MPI Exhibit 1, Volume I, PDR Attachment A, PDF page 17
[213] T: 1122, 18 – 1123, 2
[214] T: 449, 1- 450, 1

by either another solution that was already resolved through a project later or earlier. And these are harder to predict.

But I will tell you that the related benefits that we had originally planned to achieve, other than these ones that we've identified, as we don't want to do it because the incremental values isn't there, that we are meeting the business objectives. And that's kind of demonstrated, if I can refer to, on page 20 of the PDF.

When you kind of look at the net present value of this project there's a sustainable $13.6 million per -- in perpetuity that we are able to achieve. And in addition, the net result of cancelling those projects offen -- effectively saves us $4 million. And that $4 million, when you compare it to any potentially benefits that might be lost, is the cost benefit decision that we have made as an organization, that it was -- it made sense.

8.2 PDR Program Costs have been Consistent Despite Revisioning to Ensure that the Project Objectives are Effectively Achieved

190 Program costs have remained consistent from inception at $65.5 million, with $43.4 million having been spent to date and a remaining $18.1 million expected spend to complete the initiative.[215] Gartner found that MPI had budgeted for maintenance costs associated with PDR such as ongoing software costs, licensing fees and physical asset replacement cycle.[216]

191 Gartner ascertained that the PDR program has reached the point where significant components of the program have been moved into operations and MPI is starting to transform to the Direct Repair model.[217]

[215] MPI Exhibit 1, Volume I, PDR Attachment A, PDF page 4
[216] MPI Exhibit 1, Volume I, PDR Attachment A, PDF page 4
[217] MPI Exhibit 1, Volume I, PDR Attachment A, PDF page 11

192 Gartner found that MPI has demonstrated effective project and program management with focus on completing projects and ensuring that they move into production to start generating benefits as follows[218]:

- Smaller MPI operational footprint achieved through decommissioning and / or repurposing MPI service centers and the decommissioning of the Pembina Highway Service Centre.
- Direction of nearly 15% of estimates to distributed estimating (DE) shops.
- Introduction of collaborative estimating and direct repair have reduced estimate effort and provided efficiencies for MPI and repair shops.
- Delivered value to repair industry partners through improved processes and faster payments.
- Vehicle repairs meet relevant standards as defined and measured by quality of repairs standards and KPI's.
- The new shop relationship management model and KPI's are now operational, and new Accreditation and estimating standards are in place.
- There is a continued health of the overall Repair industry measured by the continued profitability of the Manitoba repair industry.[219]

193 Gartner concluded that PDR is showing an Internal Rate of Return of 7% and a Net Present Value of $13.7 million.[220] In terms of the ongoing return on investment, Mr. Geffen noted[221]:

> *"The -- the benefits do ramp-up to a steady state of -- of about $13.65 million of annual benefits. Those benefits are projected to*

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[218] MPI Exhibit 1, Volume I, PDR Attachment A, PDF page 14
[219] MPI Exhibit 1, Volume I, PDR Attachment A, PDF page 19
[220] MPI Exhibit 1, Volume I, PDR Attachment A, PDF page 21
[221] T: 1138, 13-20

> *continue in perpetuity. The benefits are about reduced -- reduced internal costs, reduced costs in -- of -- and -- and reduced cost of some of the external suppliers like loss-of-use providers and shops, and that -- that kind of thing."*

194 The report of the Gartner Group provides compelling evidence that PDR is progressing well.

9 CLAIMS COST FORECAST REFLECTS BEST ESTIMATE

195 This Section addresses the key drivers of the requested rate increase. MPI makes the following main points:

- First, MPI's requested rate increase reflects the Corporation's current best estimates for all forecasts, consistent with AAP. MPI employs standard forecasting and modeling techniques in deriving best estimates for all of its forecasts.

- Second, the drivers of the requested rate increase are largely outside the control of MPI. These factors were not the focus of the proceeding and are covered in detail in the Application.

196 MPI is taking action to control claims cost escalation, which is detailed in the Cost Containment Section 4 of this closing submission. MPI is addressing external factors where it can, and taking action that will be effective in limiting rate increases.

9.1 MPI Has Transitioned to AAP

197 In the Claims Incurred chapter of the Application, MPI recaps in a general and simplified way how the Corporation prepares forecasts, and how the change between this year's and last year's forecasts impact the rate indication. The methodology accords with accepted actuarial practice. It has been certified by MPI's Chief Actuary (Mr. Johnston). It was also peer reviewed by MPI's Appointed Actuary (Joe Cheng).

198 Mr. Johnston described the significance of the adoption of AAP rate setting this year as follows. He emphasized that the focus is now on the forecast costs and revenues

associated with policies written in the 2018 policy year, not the impact on MPI's financial statements[222]:

> *"And -- and just so the everybody understands what would happen when we switch from the old rate-making methodology which was -- our old rate-making methodo -- methodology would literally just say, Set net income to zero. Find the premium that makes these numbers zero. Our new accepted actuarial practice methodology says, Just look at the policies you're selling next year and make -- and make sure they don't earn any profit, which is different than -- than the fiscal year view."*

> *"So what can happen, for example, is we have almost $2 billion of claim liabilities. If interest rates were assumed to fall over the period, the -- the costs -- or the -- the present value of those liabilities would go up, can -- could create a loss on the [income] statement, but that's completely unrelated to the new policies we're selling today. So it is possible to have positive or negative net income, but still sell the new policies that break even"*

9.2 Major Drivers of the Rate Increase are Largely Beyond MPI's Control

199 Claims costs and claims expenses are about 88 percent of the rate.[223] The 2018/19 net claims incurred forecast has increased by $125.5 million from last year's forecast. The net claims incurred forecast is shown in Figure CI-1.[224] The figure below shows the major drivers of the forecast increase in claims incurred, which are also the drivers of rate increase. The major drivers of the rate increase are largely beyond MPI's control.

[222] T: 205, 16 – 206, 9
[223] T: 115, 1-3
[224] MPI Exhibit 1: Volume II, CI, page 6

Figure CI- 1: Net Claims Incurred[225]

Line No.		2016/17	2017/18	2018/19	2019/20	2020/21	2021/22
1	*(C$ 000s, except where noted)*						
2	**Claims Incurred before Financial Provisions**						
3	Weekly Indemnity	$125,584	$51,643	$89,680	$87,539	$86,985	$87,419
4	ABO - Indexed	$75,621	$55,652	$82,893	$82,112	$82,712	$83,750
5	ABO – Non-Indexed	$32,134	$29,610	$30,535	$30,890	$31,300	$31,718
6	PIPP Enhancements	$8,908	$4,771	$11,095	$10,908	$11,037	$11,270
7	Public Liability - BI	$5,443	$4,362	$4,595	$4,600	$4,629	$4,674
8	Collision	$392,497	$417,031	$444,959	$474,907	$506,936	$541,168
9	Comprehensive	$117,204	$106,810	$113,436	$120,001	$126,907	$134,208
10	Property Damage	$42,769	$44,363	$46,001	$47,675	$49,432	$51,272
11	**Total**	$798,458	$714,241	$823,192	$858,631	$899,938	$945,479
12	Unallocated Loss Adjustment Expenses	$39,869	$42,205	$43,912	$45,901	$47,910	$50,195
13	Change in Internal Loss Adjustment Expense Provision	$10,168	($4,904)	$6,656	$5,853	$5,637	$5,535
14	Change in Reinsurance Ceded Provision	$786	$0	$0	$0	$0	$0
15	Other Financial Adjustments	($2,217)	$0	$0	$0	$0	$0
16	Change in DPAC / Premium Deficiency Provision	$12,971	($12,128)	($9,474)	$2,471	$3,625	$6,251
17	**Total Net Claims Incurred**	$860,035	$739,415	$864,286	$912,856	$957,110	$1,007,461

200 The Claims Incurred chapter of the GRA explores this in detail, and as it was not ultimately the focus of the proceeding it is not covered in these closing submissions.

9.3 Concluding Remarks on Claims Costs Reflect Best Estimates

201 MPI has adopted full AAP rate setting, which has changed the focus to pricing policies, and away from the net income based pricing used in the past. Further, most of the factors driving the rate increase are outside of MPI’s control.

[225] MPI Exhibit 1: Volume II, CI, page 5

10 LOSS PREVENTION IS A PRIORITY FOR MPI

202 Working with Manitobans to reduce risk on the road has been a longstanding mission for MPI. MPI has, for many years, invested heavily in road safety and loss prevention. MPI expects to invest $13.2 million in 2017/18 and $13 million in 2018/19, reflecting MPI's ongoing commitment to improving safety and reducing loss costs.[226] MPI's Road Safety and Loss Prevention framework and initiatives are described in detail in the Application, Volume I Loss Prevention.

203 When it comes to road safety in Manitoba, MPI is one player in a much larger construct. All relevant stakeholders must work together towards a common vision of zero fatalities and serious injuries on Manitoba roads using a "Safe Systems" approach. The Provincial Road Safety Committee, of which MPI is a co-chair, will work to achieve these objectives. Internally, MPI has formalized a Loss Prevention Strategy and Framework that guides all of its loss prevention efforts.

204 Over the past year, MPI has focused efforts to address IBM observations relative to data through the development of data dashboards for each of the programs in the loss prevention portfolio. These data dashboards allow for baselining against which the effectiveness of programs can be measured. The data also provides new insights for program managers into how current programs can be adjusted and new programs developed. The work on data dashboards will be completed in 2017/18 and overall scorecard to measure return on investment developed thereafter.

205 MPI has formalized its activities into a three year operational plan, the second iteration of which was filed with the Public Utilities Board this year. The operational plan includes formal frameworks for priority setting, research, program development, and program evaluation.

206 Taken together, these frameworks provide assurance to the Board that the money MPI invests in road safety programming is appropriate, evidence-based, and based

[226] MPI Exhibit 1: Volume II, PF.1

on proven or promising best practice. Rather than establish an artificial target for road safety funding, the Corporation's approach is to leverage the frameworks to identify the road safety priorities and related programs and initiatives it should be pursuing. Funding to support these programs will then follow, subject to the rigor of our internal value management processes, thereby assuring value for money spent – even if it is not possible to draw direct correlations between investments in road safety programming and reductions in claims and claims costs.

207 Input from other road safety stakeholders is received through formal channels including the External Stakeholder Committee on Loss Prevention. This committee meets regularly and includes representation from all the interveners represented at Public Utilities Board hearings. MPI encourages interveners to continue attending these meetings to share information, stay informed about MPI road safety efforts, and provide input. Our objective is to continue regular and ongoing discussion outside of the rate approval process. Road safety needs to be discussed year round not just during the hearing. MPI remains open to considering new initiatives that are cost effective and fall within the Corporation's mandate. Any suggestions put forward will be considered through the road safety frameworks that have been established.

208 In this section, MPI addresses specific issues raised in the proceeding and makes the following points:

a) MPI Loss Prevention Strategy and Framework is consistent with best practices

b) MPI continues to develop and implement its Loss Prevention Strategy and Framework

c) MPI's strategy is informed by Stakeholder input

d) There is an overall downward trend in road fatalities

e) MPI has chosen its road safety priorities for 2017/18 based on evidence

f) MPI is expanding its driver education programs

g) MPI is proactively addressing drug impaired driving

h) Enhanced Enforcement is used to support awareness campaigns

i) MPI has invested in programs to help protect vulnerable road users

j) MPI is addressing wildlife claims within its mandate and on a cost-effective basis

k) Motorcyclists benefit from general road safety programming as well as targeted programming

l) Auto theft trends are understood and solutions are being developed

10.1 Loss Prevention Strategy and Framework is Consistent with Best Practices

209 MPI's efforts continue to be guided by its legislated mandate, the work is informed by the three year road safety operational plan first introduced in 2014 and updated as part of this submission. The operational plan includes formal operational frameworks for priority setting, program development and program evaluation that together, provide objective and evidence-based approaches to our road safety work. Doing so ultimately ensures that MPI is spending the right amount of funding on programs that have the greatest potential to influence road user behaviour.

210 MPI's Loss Prevention Strategy and Framework ("Strategy"), introduced in 2015, is a formalized framework, consistent with best practices. It allows MPI to apply a coordinated and measured approach to Road Safety.[227] The Strategy is expected to

227 MPI Exhibit 1: Volume I, LP.2, page 7

provide evidentiary support for future investment decisions and be a strong return on investment.

211 The Strategy incorporates prevention programs, legislated vehicle and driver standards and post-collision cost containment.

- Prevention programs seek to reduce the likelihood of accidents and accident severity. Education, driver fitness tests, programs aimed at changing perceptions and behavior and safety incentives all fall under the prevention umbrella.[228]

- Loss-cost programs seek to reduce costs after a collision has occurred and include such things as recovery of incorrect payments, salvage value and negotiation of vendor service costs.[229]

212 This holistic approach is grounded in research and analysis with a focus on evidence based, proven strategies that allow MPI to address a problem on several fronts or over a long period of time. This approach also enables collective tracking and establishes benchmarking used to assess the efficacy of the Corporation's overall program expenditures.[230]

213 MPI is only one piece of the Loss Prevention puzzle which makes it challenging to attribute MPI's role and particular MPI interventions to a specific correlating reduction in collisions, claims and claims costs.

214 Moving forward, MPI will be making greater use of its data to guide programming decisions.[231]

[228] MPI Exhibit 1: Volume I, LP.2, page 7
[229] MPI Exhibit 1: Volume I, LP.2, page 7
[230] MPI Exhibit 1: Volume I, LP.2, page 10
[231] MPI Exhibit 1: Volume I, LP.2, page 7-8

10.1.1 Loss Prevention Strategy Implementation is Progressing

215 Since MPI's last progress report on the Loss Prevention Strategy, (refer to *2017 GRA Volume I Loss Prevention LP.2.1*), the following notable activities and initiatives have been accomplished.

- The Loss Prevention Dashboard project was initiated with the identification of phase one (2016/17) and phase two (2017/18) development priorities.
- Loss prevention programs have been grouped into three areas – Driver Safety Programs, Vehicular Programs, and Loss Cost Reduction Programs.
- Loss Prevention dashboards are designed in Tableau to serve business unit managers and Executive decision makers at MPI. Dashboards illustrate trends and opportunities which can be shared with the PUB and other stakeholders to gain consensus on future direction for MPI's loss prevention programs. Most importantly, the dashboards provide empirical evidence about the effectiveness of programs in achieving desired outputs and outcomes.
- Dashboard analytics are complete for phase one programs. MPI has developed models for reporting individual costs for phase one programs, which had not previously existed.
- The External Stakeholder Committee on Loss Prevention continues to meet quarterly for information sharing and discussion on loss prevention issues and programs.

216 Implementation of MPI's Loss Prevention Dashboard continues.[232]

232 MPI Exhibit 1: Volume I, LP.2.1, pages 8-9

10.2 MPI's Strategy is Informed by Stakeholder Input

217 MPI's Road Safety and Loss Prevention work is informed through Stakeholder engagement. MPI looks for input on opportunities to partner on investment, resources, influence and ideas for mutual benefit.[233] Three main avenues for engagement are as follows:

- Participation on the External Stakeholder Committee on Loss Prevention:

  The Committee is comprised of representatives from the Province of Manitoba (Manitoba Infrastructure), the City of Winnipeg (Public Works), the Manitoba Motor Dealers Association, the Coalition of Manitoba Motorcycle Groups, CAA Manitoba, the Manitoba Trucking Association, the Automotive Trade Association, Safety Services Manitoba, the Consumers Association of Canada (Manitoba), Bike Winnipeg, and the Manitoba Association of Chiefs of Police.[234]

- The Provincial Road Safety Committee:

  The Provincial Road Safety Committee is co-chaired by senior representatives from Manitoba Infrastructure and MPI and is tasked to develop a strategic and holistic approach to road safety and to increase cooperation and collaboration among stakeholders. A main task is to deliver Road Safety Plan for Manitoba.[235]

- Through its participation on The Provincial Road Safety Committee, MPI supports the adoption of a Safe Systems model and Vision Zero (or Toward Zero) approach to road safety which would address the social costs of collisions (health, economic and societal factors) at a jurisdictional level.[236]

233 MPI Exhibit 1: Volume I, LP.3, page 11
234 MPI Exhibit 1: Volume I, LP.3.2.1, page 12
235 MPI Exhibit 1: Volume I, LP.3.2.2, page 13
236 MPI Exhibit 1: Volume I, LP.3.2.2, page 14

- Safe Systems and Vision Zero seek to reduce human toll on Manitoba's roadways and ensure the right Provincial departments, agencies and MPI take the right actions that contribute toward shared goals in accordance with their individual mandates. This enables MPI to be responsive to its ratepayers and its pursuit of low insurance rates and enables all players in the road safety system to take action to reduce human toll and associated social costs of collisions.[237]

- Direct Engagement:

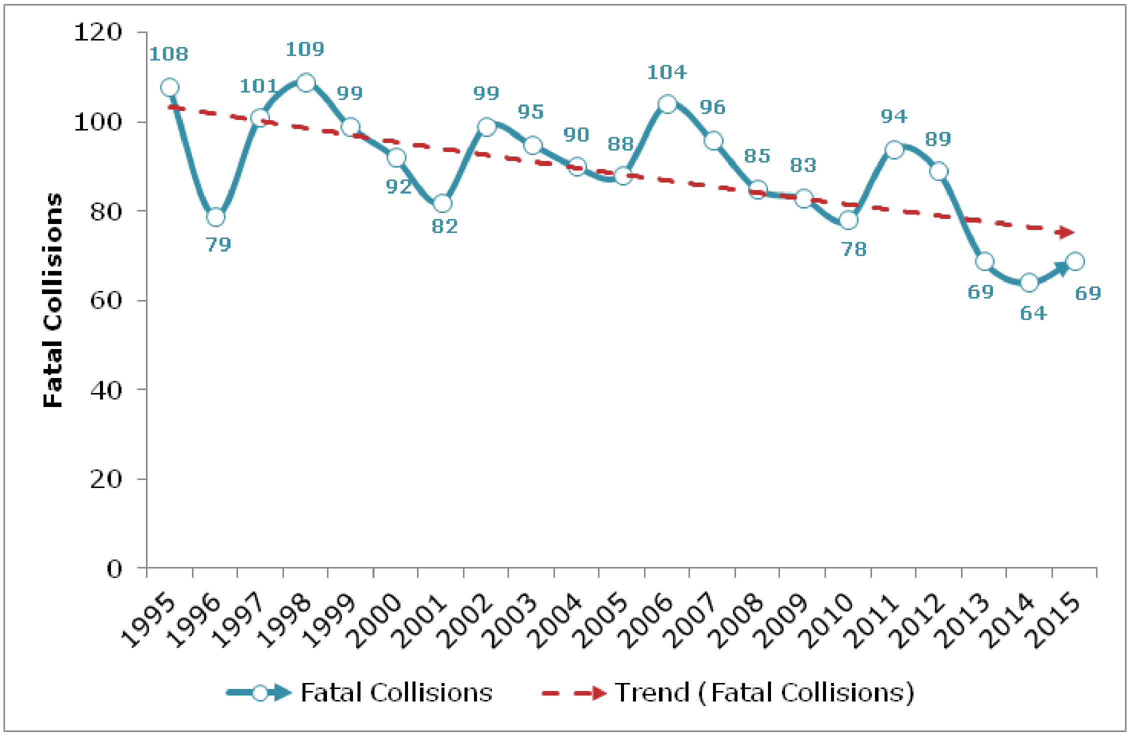
  MPI also engages with small groups to collaborate on loss prevention solutions that are narrower in scope.[238]

10.2.1 Overall Downward Trend in Road Fatalities

218 Although road fatalities increased in 2016, there has been an overall downward trend in actual motor vehicle fatalities and fatal collisions. This has been achieved despite continuous growth in the number of licensed drivers and registered vehicles using Manitoba's roadways.[239]

[237] MPI Exhibit 1: Volume I, LP.4.1, page 22
[238] MPI Exhibit 1: Volume I, LP.3.2.3, page 15
[239] MPI Exhibit 1: Volume I, LP.4.1.1, page 23

219 **Figure LP- 1: 4.1.1 MB Fatal Collisions: Summary of Trends from 1995 to**
220 **2015[240]**



221 As noted by Mr. Keith[241]:

> *But when we see downward trending like this, it does tell us that, collectively with our stakeholders, collectively with vehicle technology improvements, with tougher legislation, with greater enforcement and with greater ability to influence driver behaviour and road user behaviour, we are making progress in this province on an overall basis.*

222 With respect to the sharp increase in fatalities in 2016, Mr. Keith said[242]:

> *Clearly, the results in 2016 reflect the complexity of road safety and how difficult of a nut that is to crack. Based on the interdependencies that play a role in terms of safety on our public roadways and the interdependencies between road-users, vehicles, the roads they drive*

[240] MPI Exhibit 1: Volume I, LP.4.1.1, page 24
[241] T: 652, 21- 653, 3
[242] T: 654, 11 – 655, 5

> *on, the speeds they drive legislation, rules of the road, enforcement and public awareness and -- and trying to change road user behaviour to get to a point where no fatality is acceptable on our public roadways in the future.*
>
> *These results do not indicate, and should not be seen as an indication that road safety efforts by MPI or our stakeholders are ineffective or are failing. This just speaks to the randomness and the concern with respect to being able to track and convincingly create downward trending in terms of the results. And to that end, I am pleased to say that, based on 2017 very preliminary data, we have returned to our previously enjoyed downward-trending in fatal collisions and fatalities.*

10.2.2 MPI Determined 2017/18 Road Safety Priorities Based on Evidence

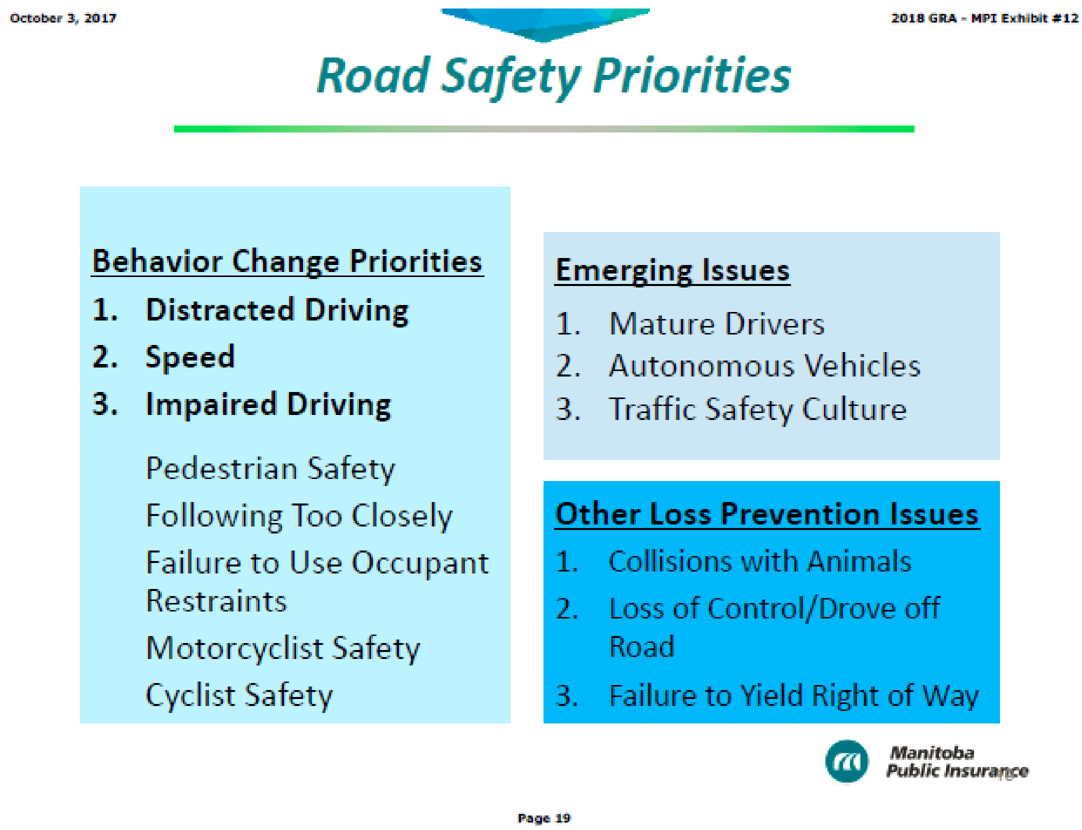
223 MPI analyzed, rated, and ranked road safety priorities using a number of weighted criteria, including: crash severity frequencies from the Traffic Collision Statistics Report (TCSR)/Traffic Accident Report (TAR) and Off Road Vehicle (ORV) datasets over several years, public opinion from MPI polling, national industry priority guidelines, stakeholder expectations and relative cost.[243]

224 As noted by Mr. Keith in his direct presentation[244]:

> *An important component of our work on loss prevention and road safety is being able to measure the cost benefit of programs where that is possible, and ultimately demonstrate value for money in terms of achieving outcomes. We know this is an important piece of information for the Board and it is also important to our ratepayers. Ultimately, they must be satisfied that our efforts with respect to loss prevention and road safety are evidence-based, are data-driven and are based on best practice, and that the dollars we invest are appropriately placed to achieve the best possible outcomes.*

[243] MPI Exhibit 1: Volume I, LP.4.1.3, page 27
[244] T: 645, 1-12

225 MPI identified the following Behaviour Change and Road User Issue priorities based on that assessment:

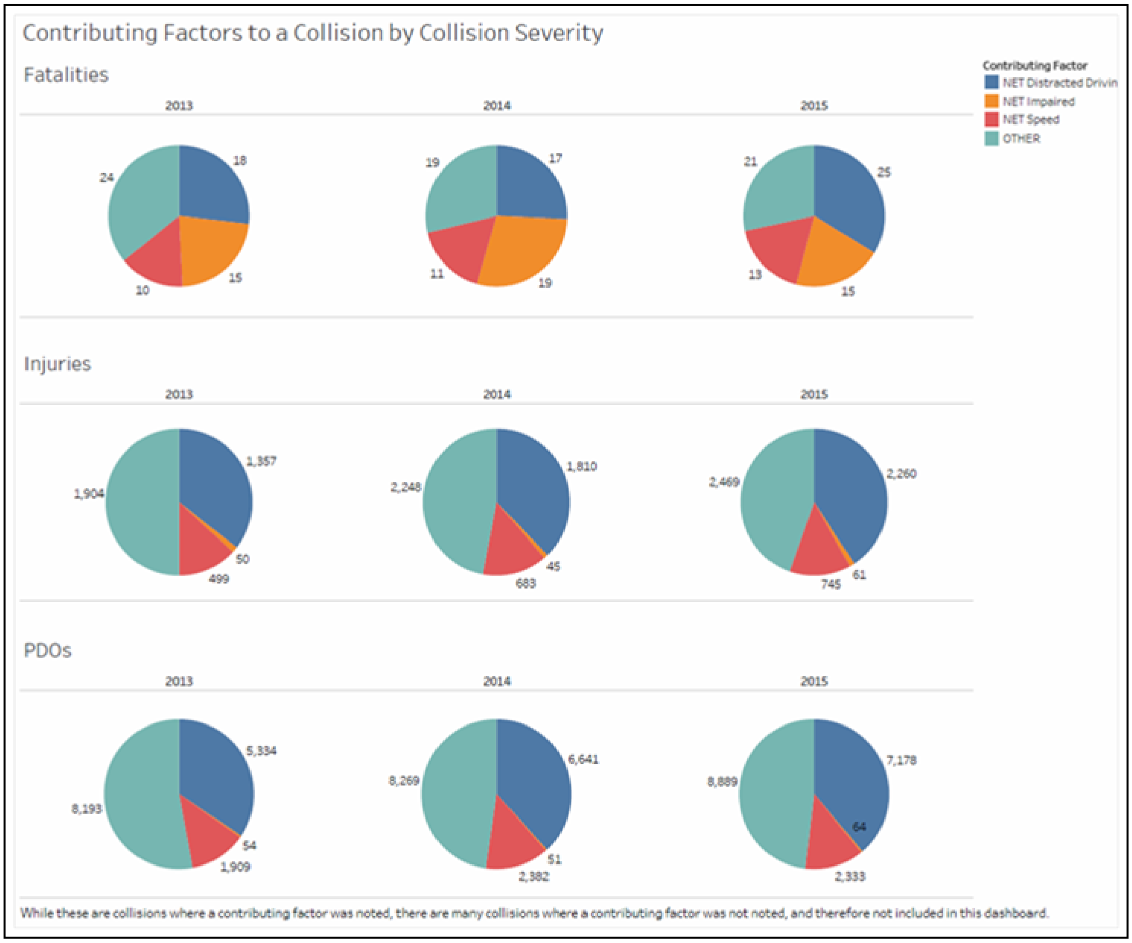


[245]

226 The Driver Behavior dashboard provides a visual comparison for consistent annual data for all major contributing factors to accidents and provides evidence to support MPI's top three priorities.[246]

[245] MPI Exhibit : slide 19
[246] MPI Exhibit 1: Volume I, LP.4.1.3, page 27

Figure 7 - Driver Behavior Dashboard



227 The Driver Behaviour dashboard provides important empirical evidence to support the road safety priorities established and verified by MPI. Distraction, speed, and impairment are driver behaviours behind the majority of claims.

10.2.3 MPI is Expanding its Driver Education Programs

228 MPI is redeveloping the program curriculum on the High School Driver Education program to incorporate a Traffic Safety Culture[247]:

[247] T: 660, 2-10

> *Understanding the rules of the road is important. Understanding the skills necessary to operate a vehicle safely is important, but what's really going to make a difference for new young drivers, in our view, is focusing on the -- the -- the higher-level competencies of judgment, attitude, decision-making, hazard perception and propensity to taper it -- take risk.*

229 MPI is also delivering adult education programming for adults that may not have had access to the high school program such as immigrants and refugees and those who live in remote Northern communities.[248]

10.2.4 MPI is Proactively Addressing Drug Impaired Driving

230 Evidence indicates that drugs are present in Manitoba drivers.[249] MPI is expanding its efforts to address drug impaired driving with a new public awareness strategy/campaign. The campaign will raise awareness about the risks and dangers associated with drug impaired driving, and help shape public behaviour and attitudes on this issue.[250]

231 Mr. Keith spoke about the intent of the program[251]:

> *The intent, quite frankly, is to raise awareness about drugs generally, and about how cannabis, in particular, can impaired driving. So that when cannabis becomes legal in 2018, drivers will be in a position to make informed, safe decisions about whether to drive after consuming cannabis. The campaign includes a four-pronged approach with messaging focused on four (4) distinct audiences: New teen drivers to our high school driver education program, youth in general, the medical community and their patients, and the general public.*

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[248] T: 659
[249] MPI Exhibit 1: Volume I, LP.4.1.4, pages 39-44
[250] MPI Exhibit 1: Volume I, LP.4.1.4, page 44 and LP – Appendix 11
[251] T: 663, 14-24

232 MPI has studied the effects on road safety in jurisdictions where cannabis has been legalized and found that drug-related motor fatalities doubled and there were significant increases in drivers testing positive for cannabis[252]:

> *Taken together, the experience in other jurisdictions, the prevalence of drug use among Manitoba drivers today and clear misconceptions about how drugs can impaired driving, taken together, these things ask -- these things give us a very sific -- significant concern that when cannabis is legalized drug impaired driving collisions, fatalities and serious injuries will increase.*
>
> *This is why we're working so hard with our other stakeholders to get ahead of this issue and to educate drivers about the real consequences of cannabis impaired driving. Also, that when cannabis becomes more accessible in Canada drivers will be able to make informed decisions, right decisions, safe decisions about whether to drive after consuming cannabis.*[253]

10.3 Enhanced Enforcement is Use to Support Awareness Campaigns

233 In conjunction with campaigns aimed at raising awareness and changing behaviors around speeding, distracted driving and impaired driving, MPI funds enhanced enforcement in conjunction with law enforcement to drive home the campaign messaging. Mr. Keith testified[254]:

> *So we -- we have very specific initiatives that we provide enhanced enforcement funding for. So we provide enhanced enforcement funding for impaired driving, and this is specifically during the period May to September or October.*
>
> *And really, it is about ensuring that our -- our public awareness campaigns are supplemented by visible enforcement, particularly on*

[252] T: 665
[253] T: 666 7-23
[254] T: 692, 19 – 694, 5

long weekends and weekends during the summer months when there is a lot of traffic on the highways.

We also provide enhanced enforcement in -- for two (2) months of the year in April and July. Subject to check, I believe it's in April and July to support our awareness campaigns on distracted driving, use of cell phones while driving, and texting while driving, and we also provide enhanced enforcement funding to support back-to-school safety. And so we focus on pedestrian safety when kids are back to school in September, and to -- and -- and that is both within designated school zones and outside of those school zones as well.

More recently, we've also provided some funding to the RCMP for enforcement of impaired driving on winter and ice roads in the northern part of the province, and so that funding is provided specifically to the RCMP.

This funding is not intended to replace traditional police enforcement of the traffic laws on our roadways. Our expectation is that their efforts with respect to enforcement continue. This is very specifically enhanced or elevated enforcement to increase the visibility of law enforcement on the roadways and, therefore, to increase in driver's minds the -- the perceived likelihood of being apprehended should they choose to participate in these illegal and high risk behaviours.

10.4 MPI has invested in Programs to Help Protect Vulnerable Road Users

234 MPI's road safety portfolio includes appropriate initiatives directed at vulnerable road users, including pedestrians and cyclists.

10.4.1 Pedestrians

235 Research has demonstrated that pedestrians are most likely to be involved in a collision during winter. In 2016, MPI began a series of pedestrian safety tactics. For drivers, specific messaging was delivered via billboards, radio, print ads, and on the back panels of buses. For pedestrians, messaging was installed strategically in transit corridors where high risk pedestrian behaviour is common.

10.4.2 Cyclists

236 MPI partnered with Bike Winnipeg and other stakeholders to deliver the Bicycle Education & Skills Training in schools pilot program which provides cycling instruction and on-road experience to students in grades 4-8 with the goal of making them more aware of cyclists' safety needs which prepares them for vehicle driving later in life.[255] Other examples of cycling safety programs administered or sponsored by MPI include[256]:

- Bike It! (downtown commuter training)
- Cycling Champion
- Bike to Work/Bike to School
- The Commuter Challenge
- Bike Rodeos for pre-school aged children
- Ciclovia
- Integration of cycling safety and motorist responsibility content into the High
- School Driver Education program curriculum
- Annual cycling safety awareness campaign

237 Mr. Keith noted:

> *We continue with our cycling -- our other cycling safety programs. Our cycling champion program. Our workplace cycling safety program for commuter cyclists. We've added information about the importance of cycling safety and sharing the road carefully and*

[255] MPI Exhibit1: Volume I, LP.4.1.4, page 47
[256] MPI Exhibit 1: Volume I, LP.4.1.4 , page 50

> *appropriately with cyclists in our provincial Driver Handbook. And have put significant content into our High School Driver Education program.*
>
> *Finally, this year I'm really pleased that we were able to work with Bike Winnipeg on a new public awareness campaign called, "Leave Space to Breathe". This is a new campaign that more than ever before specifically calls out the expectation that drivers leave a metre of space when passing cyclists. Because cyclists need the space to navigate on the road and navigate around obstacles on the road. And they cannot ride safely, knowing that they're going to be brushed up against by a two-thousand (2000) pound vehicle or a five-thousand (5000) pound truck or a fifty-thousand (50,000) pound semitrailer.*
>
> *So our messaging is clearer than ever and we were really pleased to work with Bike Winnipeg and my understanding is Bike Winnipeg was also very pleased that we were able to come out with much clearer direction, in terms of the importance of leaving a metre of space so that cyclists can ride safely.*[257]

10.5 MPI is Pursuing Cost-Effective Measures Within Its Mandate to Address Wildlife Claims

238 CMMG has raised the issue of wildlife collisions in this proceeding. Wildlife collisions have remained relatively constant over the past few years, with periodic declines - notably in 2013 and 2014, possibly attributed to severe winters and a decline in the deer population.[258] MPI is taking additional steps to address this important issue:

- First, MPI expanded its wildlife collision awareness efforts, installing highly visible, seasonal variable message signs along roadways known to have high concentrations of deer-vehicle collisions in Manitoba.[259]

- Second, MPI is actively exploring alternatives to better isolate true 'hot spots' for wildlife collisions. If 'hot spots' can be verified through empirical data, then

[257] T: 670, 1-671, 2
[258] CMMG (MPI) 1-10
[259] MPI Exhibit 1: Volume I, LP.4.1.4, page 50-51

MPI will pursue additional targeted and conventional awareness initiatives in collaboration with the province of Manitoba.[260]

- Third, DRIVR-X, MPI's virtual reality experience which immerses the viewer in various real life scenarios, features a scenario involving the risk of wildlife on the road.[261]

239 These are meaningful steps, and are cost-effective for policyholders.

240 PUB Order 10.35 ordered MPI to further study the use of fencing to prevent wildlife collisions. MPI has already examined this issue extensively. MPI has previously filed four[262] studies, reproduced this year in *Loss Prevention Appendix 15* on wildlife mitigation measures, including wildlife fencing. The studies demonstrate that wildlife fencing is not a cost effective solution.

241 In addition, MPI cannot spend significant financial resources on a pilot project that is essentially a road infrastructure project. The legislative authority in section 6(2)(h) of *The Manitoba Public Insurance Corporation Act* does not enable MPI to do so. Further, the Manitoba government has explicitly directed MPI not to fund road infrastructure. Until such time as MPI receives new instructions from the Province, MPI is unable to undertake such expenditures.[263]

242 MPI has engaged CMMG directly on this issue to provide a detailed explanation of the existing analysis and recommendations. MPI has explained its intention to focus its resources and effort on the wildlife hot spot research that will identify density of

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[260] CMMG (MPI) 1-10
[261] CMMG (MPI) 1-15
[262] 1) AI.9 Wildlife Collision Review, 2011 GRA IR Round 1, PUB (MPI) 1-100, Collisions Involving Motor Vehicles and Large Animals in Canada, Final Report to Transport Canada, L-P Tardif & Associates, March 2003;
2) 2013 GRA IR Round 1 – PUB(MPI) 1-67(a) Attachment, Wildlife Collision Reduction Pilot Intervention 2011 Evaluation Report, Manitoba Public Insurance, 2012;
3) 2013 GRA IR Round 2, CMMG (MPI) 2-4;
4) 2017 GRA Attachment LP-E, Wildlife Collision Mitigation Review and Cost Benefit Analysis, Manitoba Public Insurance, 2016
[263] MPI Exhibit1: Volume I, LP.4.1.4, page 52

collision occurrences, deer population, habitat and other environmental information.[264]

10.6 Motorcyclists Benefit from General Road Safety Programs as Well as Targeted Programming

243 CMMG has argued in this proceeding, as in past proceedings that MPI is spending too little on motorcycle safety. MPI submits that motorcyclists benefit from broader initiatives as well as initiatives focused on motorcyclists. MPI's public awareness campaigns and safety interventions are generally designed to address road user behaviors that contribute to collisions.[265]

244 Programs addressing driver distraction, speed and impairment are equally relevant and targeted to motorcycle and motor vehicle drivers.[266]

245 Programs specifically targeted to motorcyclists, including the rebate program for the extended *Gearing Up* motorcycle training program, comprise 1.8% of total road safety expenditures. On a per-vehicle basis, total spending on road safety programming is forecasted at $11.66/vehicle compared to $15.18/motorcycle on motorcycle specific initiatives.[267]

10.7 Auto Theft Trends Are Understood and Solutions are Being Developed

246 MPI has collaborated with strategic partners to reduce auto theft.[268] The rate of total auto theft in 2016 was 84 percent lower than the height of the auto theft crisis in 2004; however, the rate of total theft claims and claims costs have risen since 2011. In response, MPI undertook detailed analysis to understand the cause of the increase in total theft claims. The Auto Theft Dashboard indicates that auto theft is

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[264] MPI Exhibit1: Volume I, LP.4.1.4, page 51
[265] CMMG (MPI) 1-13
[266] CMMG (MPI) 1-13
[267] CMMG (MPI) 1-13
[268] MPI Exhibit 1: Volume 1, LP.4.3, pages 65-70

a crime of opportunity and loss prevention efforts are more appropriately directed at vehicle owners to protect keys and never leave running vehicles unattended. Specific new interventions are in the proposal and business case stage of development. A return to 2012 total theft levels would result in an incurred cost reduction of approximately $5 million per year.[269]

Figure 8 - Auto Theft Dashboard - Theft Analysis[270]

Reasons of Theft

Reason Category	Theft Reason	2016
Stolen With Keys	Keys stolen by thief	312
	Keys in vehicle (not ignition), vehicle unlocked	234
	Keys missing/lost	195
	Keys in ignition (engine running), vehicle unlocked	158
	Keys stolen by guest/visitor	147
	Keys in vehicle (not ignition), vehicle locked	133
	Keys in ignition (engine not running), vehicle unlocked	102
	Keys in vehicle (not ignition), unsure if vehicle locked or unlocked	69
	Carjacking	34
	Keys in vehicle (not stated where),vehicle unlocked	33
	Voluntary parting - rental/borrowed/test drive	31
	Keys in vehicle (not stated where),unsure if vehicle locked or unloc..	22
	Keys in ignition (engine running), vehicle locked	21
	Keys in vehicle (not stated where),vehicle locked	10
	Keys stolen by resident of house	10
	Keys in ignition (engine running), unsure if vehicle locked or unlock..	7
	Keys in ignition (engine not running), unsure if vehicle locked or unl..	5
	Keys in ignition (engine not running), vehicle locked	3
Stolen Without Keys	Trailer - keys are not required to steal vehicle	225
	Keys are not required to steal vehicle	215
	Vehicle is unprotected - not immobilized	134
	Vehicle not recovered or destroyed	122
	Immobilizer examined and found to be defective	2

[269] MPI Exhibit 1: Volume 1, LP.4.3, page
[270] MPI Exhibit 1: Volume I, LP.4.3, page 69

10.8 Vehicular Programs

10.8.1 Physical Damage Centre of Excellence

247 The Physical Damage Centre of Excellence in Automotive Research and Training (COE) is operational and enables collaboration with original equipment manufacturers to bring new and emerging technology and training to Manitoba, improve collaboration with the Manitoba repair industry and enhance partnerships with educational institutions.[271]

10.8.2 Vehicle Standards and Inspections

248 MPI administers Manitoba's vehicle inspection standards on behalf of the Province which help insure that vehicles are safe and meet the equipment requirements set out in *The Highway Traffic Act*.[272]

10.9 Loss Cost Reduction

10.9.1 Subrogation and Recovery

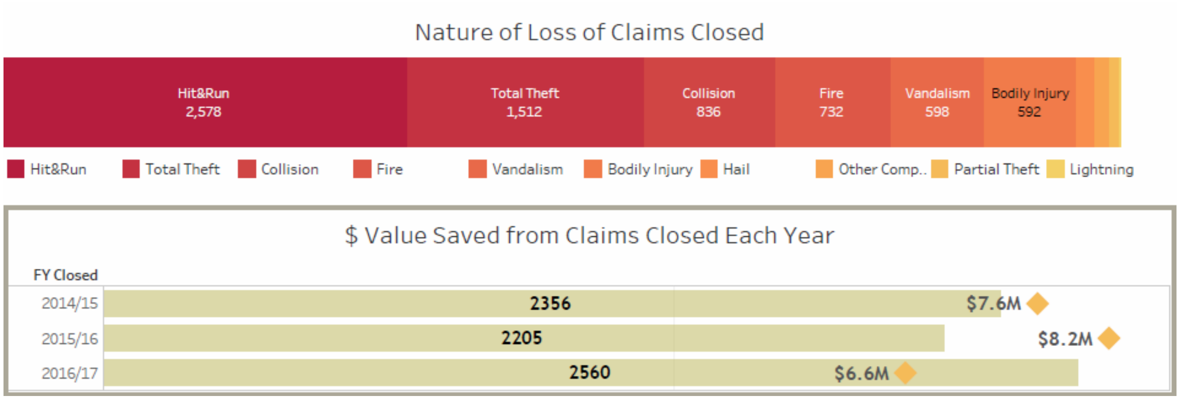
249 The Special Accounts and Subrogation Unit acts to secure, preserve, and enforce MPI's right of recovery through various means including litigation and other collection efforts.[273]

271 MPI Exhibit 1: Volume 1, LP.5.1, page 74
272 MPI Exhibit 1: Volume 1, LP.5.2, page 75
273 MPI Exhibit 1: Volume 1, LP.6.1, page 76

10.9.2 Fraud Prevention

250 The Special Investigations Unit investigates suspicious claims which expose MPI to financial risk and fraud.[274]

Figure 9 - Fraud Dashboard – Types of Fraud & Savings Achieved



10.9.3 Salvage

251 Total loss vehicle are sold as salvage and may qualify to be rebuilt to required provincial standards for road use, or sold for parts. MPI continues to explore opportunities to expand the reach of auctions to access more buyers and increase MPI's revenue.[275]

10.10 Loss Prevention and Road Safety Summary

252 MPI recognizes that influencing road user behaviour is only one component of a more holistic 'safe systems' approach to road safety. For this reason, MPI continues to work with other road safety stakeholders through direct collaboration and as a member of the Provincial Road Safety Committee where all stakeholders that can influence outcomes are represented.

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[274] MPI Exhibit 1: Volume 1, LP.6.2, page 77
[275] MPI Exhibit 1: Volume 1, LP.6.2, page 79

11 CONCLUSION

253 MPI faces significant uncertainty in its day-to-day operations from a variety of factors including claims volatility, capital market conditions, and industry changes. MPI respectfully submits that the regulation of MPI should be a stabilizing force, and not one that adds to uncertainty. The rate setting mandate of the Public Utilities Board confers significant influence over fundamental elements of the business – (i) how much revenue MPI collects, and (ii) how much of that revenue MPI can retain for mitigating risks and investment. The certainty MPI requires to operate the business and make investment decisions will come from consistent application of the break-even rate principle, confirmation of the RSR definition, a realistic risk-based RSR lower limit, and an RSR upper limit set at a level sufficiently above the lower limit that can absorb the volatility associated with adverse events.

ALL OF WHICH IS RESPECTFULLY SUBMITTED.