CLOSING SUBMISSIONS OF

THE COALITION OF MANITOBA MOTORCYCLE GROUPS

2022 General Rate Application

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INVESTMENTS

Coalition of Manitoba Motorcycle Groups appreciates the opportunity to provide the board with submission in this years General Rate Application. This Application has canvassed a wide range of incredibly complex issues, which are often overlapping and interrelated.

Motorcycle claims costs have been on a downward trend for several years[1], yet each year MPI comes to the Board seeking an increase in premiums for motorcyclists. Despite improved driving behaviour and reductions in claims costs, motorcyclists are being required to pay higher premiums, primarily as a result of interest rate changes.

MPI's Investment Strategy has been a sticking point for CMMG for several years now. The last ALM study provided for an investment portfolio for Basic Claims that is comprised entirely of fixed income assets[2]. This investment decision has had a disproportionate impact on the motorcycle major class in particular, as their basic premium has a very high composition of Personal Injury Protection Plan claims when compared to other classes. While the composition of the motorcycle basic policy may be relative to the type of risk posed, CMMG submits that the sensitivity to long term interest rate volatility is a disproportionate and unfair factor that requires addressing. It is the position of CMMG that this issue can be addressed through small improvements to the Corporation's investment strategy.

The Shadow Portfolio 2 includes a mix of fixed income assets, public equities and alternatives. Notably the Shadow Portfolio 2 includes 5% private equities, 13% Canadian equities and 16% Real Return Bonds[3]. Over the period from July 2020 to July 2021, Shadow Portfolio 2 substantially outperformed the Basic Policy Portfolio, with Shadow Portfolio 2 providing returns of 5.01% and the Basic Policy Portfolio providing returns of -3.61% (a difference of 8.62%)[4].

The Shadow Portfolio 2 raises the question, "Why is MPI not shifting towards an investment portfolio with a similar mix given the better performance of Shadow Portfolio 2?". The refrain repeated by MPI is 'it is too risky", or "it is too volatile". MPI has even said equities or growth assets are prohibited from inclusion in the Basic claims portfolio[5]. MPI relies on the very low risk appetite of its Board of Directors to validate its portfolio makeup.

A review of Modern Portfolio Theory provides some insight into whether MPI's investment strategy is obtaining optimal risk/reward balance. The Efficient Frontier was discussed during cross examination with Mr. Bunston and shows the relationship between portfolio returns and risk[6]. Constraints on a portfolio, for example where certain asset classes are excluded, may have the effect of shifting the efficient frontier

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[1] CMMG (MPI) 1-9 Appendix 1
[2] Transcript Pg 1697 Line 9-15
[3] CMMG (MPI) 1-10 Pg 3
[4] CMMG (MPI) 2-14 Pg 7
[5] Transcript Pg 1659 Line 16-24
[6] Transcript Pg 1670 Line 4-8

down[7]. The cost of this shift will result in either lower returns for the same level of risk or higher risk for the same level of return, or a combination of the two[8].

MPIs Board of Directors determines the risk appetite of the Corporation. When examining the efficient frontier, it is necessary to determine risk appetite first, and then seek to maximize the return for that level of risk[9]. It is important as well to remember, which was acknowledged by Mr. Bunston, that a portfolio's location on the efficient frontier is determined at the total portfolio level[10]. Asset classes therefor should not be independently evaluated for their risk/return nature. Instead, it is necessary to look at the makeup of a portfolio as a whole to determine what ideal weighting of asset classes can be added to achieve the desired risk of the portfolio while also achieving maximum returns.

CAC Manitoba and CMMG questioned MPI on the issue of surplus volatility. Surplus volatility refers for the difference in value of the assets and liabilities in a portfolio[11]. Mr. Bunston agreed that surplus volatility is the most important measure of risk for asset backing claims liabilities[12]. Further Mr. Bunston agreed that where portfolio A has lower surplus volatility than portfolio B, portfolio A would then have higher realized risk adjusted returns[13].

The results from the Shadow 2 Portfolio raise 3 questions:

1. **How do the realized returns for Shadow Portfolio 2 compare to the policy portfolio?**
2. **How does the realized surplus volatility for Shadow Portfolio 2 compare to the policy portfolio? And**
3. **Were the realized risk-adjusted returns for Shadow Portfolio 2, since inception better or worse than the policy portfolio?**

To Answer these questions, I'd like to look at MPI Exhibit #121 which is response to Undertaking 40. Now I'd like to take a little bit of time to just look at this document for the Boards benefit as this was not reviewed during the evidentiary portion of the hearing.

We can see along the top of the document, that the information is provided on a monthly basis since March 2019, so the inception of the Shadow Portfolios, to the most recent data in September 2021.

On the left side of the document, the first heading is "Assets- Basic Claims Portfolio". This provides the Assets for the Actual and Policy portfolios, and then the Shadow Portfolios 1 and 2. Unfortunately the totals have not been provided, but where the asset returns are calculated and compounded over the year, the data demonstrates that the Shadow Portfolio 2 out performed the basic policy portfolio. As was also identified by counsel for CAC Manitoba, the returns for the policy portfolio and the Basic Portfolio 1 were approximately on par.

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[7] Transcript Pg 1680 Line 6-13
[8] Transcript Pg 1681
[9]Transcript Pg 1672 Line 17-21
[10] Transcript Pg 1673 Line 10-13
[11] Transcript Pg 1593 Line 6-9
[12]Transcript Pg 1593 Line 11-16
[13] Transcript Pg 1620 Line 17-24

This answers the first question – realized returns for Shadow Portfolio 2 exceeded those of the basic policy portfolio.

The next subheading on this Appendix provides the liabilities. And the two headings below that are Surplus and Surplus volatility. Now the surplus of the portfolio is simply the difference between Assets and liabilities. You'll see that MPI has provided a calculation of Surplus using the nominal liabilities, and using the real liabilities. The same has been done for Surplus Volatility. Ms. Dilay touched on the difference between nominal and real during her closing submissions. A nominal benchmark does not recognize inflation risk. Conversely real benchmark recognizes the nature of the true liabilities. It is CMMG's position that, as a result, the nominal benchmark is an unreliable portrayal of liabilities and the nominal results in this undertaking should be ignored.

On the bottom left of Exhibit #121 Appendix A is the calculation of Surplus Volatility for the respective portfolios. The second column provides Surplus Volatility over a 31-month period from March 2019 to September 2021. The realized surplus volatility for Shadow Portfolio 2 measured in real terms was 3.27% which is essentially the same volatility as the policy portfolio at 3.24%.

> **This answers our second question – surplus volatility for Shadow Portfolio 2 is equal to that of the basic policy portfolio selected by MPI.**

Finally, then when we examine the relationship between the realized returns of both portfolios, and the surplus volatility of both portfolios, it demonstrates to us both portfolios had similar surplus volatility while the Shadow Portfolio 2 had higher returns.

> **This answers our third question – Shadow Portfolio 2 has higher risk-adjusted returns than the basic policy portfolio.**

How can this information then be used to examine MPI's investment strategies?

What we can see now is that excluding asset classes from a portfolio due to the nature of that asset class alone, has a cost. In this case the realized returns in the policy portfolio were lower with the same level of surplus risk. Shadow Portfolio 2 provides a concrete example, with data, of the costs that constraints on the basic policy portfolio have had. CMMG agrees that equities, alone, may have higher asset volatility than alternatives like bonds. BUT from a total portfolio perspective, the inclusion of these more volatile assets can have the desired effect of increasing returns while maintaining MPI's low appetite for surplus risk.

As a result, CMMG submits that MPIs rationale that their Board's low risk tolerance justifies the exclusion of equities from the basic portfolio is unsubstantiated.

MPI has proposed a new Asset Liability Management study be completed and is working to issue an Request For Proposal to conduct the study. CMMG understands it is MPIs position that the ALM study will take approximately 6 months to complete, which does not include the timeframe for the RFP process. While MPI has indicated they are hopeful and working towards having the study completed for the next GRA[14] MPI has provided no guarantee. CMMG is concerned that based on this timeline, the ALM study

[14] Transcript Pg 1687 Line 25-Pg 1688 Line 1-6

may not be completed in a timeframe which will allow review prior to the commencement of the 2023 GRA hearing. The effect will be that Interveners will not have the opportunity to review the ALM study during the Information Request process, severely limiting the opportunity to properly examine the issue. As acknowledged by MPI the previous study was completed on an expedited basis of 3-4 months[15]. CMMG submits that the proposed ALM study also be expedited to ensure full examination of the study can be completed at next years GRA, for the benefit of the public and the Public Utilities Board panel members.

CMMG proposes that this study should provide the Board some insight as to MPIs risk appetite, and its ability to incorporate growth assets into the basic portfolio while still maintaining the desired risk exposure. As a result CMMG provide the following recommendations to the Board:

Recommendations:

1. **That the new ALM study be completed on an expedited basis the results of which should be filed with the 2023 Application;**
2. **That the new ALM study provide an objective opinion regarding the prudence of including or excluding various assets in the basic claims portfolio. (i.e., equities or other non-fixed income assets). This opinion should consider the following:**
    a. **Whether the inclusion of growth assets is prudent while maintaining the surplus volatility (the relevant risk) at levels that are consistent with the risk appetite of the corporation;**
    b. **If so, what weighting of equities and other non-fixed income assets may be included to achieve the best possible expected risk-adjusted return?**

DRIVER SAFETY RATING SYSTEM

The Driver Safety Rating System has been a topic of considerable interest for this Board for several years now. MPI has come before the Board this year taking the position that the DSR system should remain in place for at least 5 years, and MPI has proposed some changes for this year with more changes to come in future General Rate Applications.

History of DSR

The Board has been seeking a thorough review of the DSR model and a pricing examination of both the primary driver model and the registered owner model for years

[15] Transcript Pg 1689 Line 19-21

- 2018 GRA: Board Ordered that a Technical Conference take place regarding availability and practicality of other analytical tools and ratemaking methodologies to better determine DSR rates and discounts based on principal driver rating rather than simply registered driver rating[16]
- 2019 GRA Board Ordered MPI to report on public consultation in the following year, and on decision to collect data for alternative rating models[17]
- 2020 GRA Board Ordered that MPI confirm which model it would proceed with, a pricing examination of the primary driver and registered owner models. It is notable that although seeking a variation of parts of this Order pertaining to DSR, MPI didn't seek variation requiring a pricing examination of the primary driver model to indicate that they did not have sufficient data to provide a pricing examination.[18]
- 2021 GRA Board Ordered MPI to propose driver rates and discounts that are more actuarially sound, and also shall bring a plan including timelines, major milestones and implementation date for changes to the DSR system[19]

The History of the examination of the DSR system, demonstrates the Boards attempts over the last several years to obtain a fulsome review of the current DSR model, including pricing, as well as a review of alternative models and the potential pricing of those models. As the Board is aware, we are here today still without a pricing examination of the primary driver model. In fact MPI still has not collected data on this model, despite the Board's clear interest in the primary driver model since 2018.

MPI has carried out some of the directives above. A Technical conference was held, a pricing review of the registered owner model was provided, a public consultation process was conducted and reported, and this year some adjustments to the registered owner DSR system have been proposed, with a promise that further adjustments will be proposed in future GRAs.

Of concern to the CMMG, is MPIs proposition in their closing argument that for next GRA, that MPI will "undertake a thorough review of its pricing and incentive models" including a "work plan setting out the scope and duration of the review".

This proposal is simply starting from square one again. This perspective of 'starting over' was also referenced by Mr. Prystupa[20]. Mr. Prystupa was asked whether MPIs position continued to be that only two models, the primary driver and registered owner, were worth considering. Mr. Prystupa indicated that MPIs position is that we should look at it with a "*fresh set of eyes where no – no model or combination of models is off the table at this point, and – and everything really needs to be – needs to be recon -- reconsidered at this time*"

It is CMMG's position that the proposal to start again is completely unreasonable. A pricing analysis of the registered owner model has been completed. We know the registered owner model is not accurately pricing risk. We know that the primary driver model would be more actuarially sound. The Board has already demonstrated their interest in the primary driver model as the most reasonable alternative to the

[16] Board Order 130/17
[17] Board Order 159/18
[18] Board Order 176/19
[19] Board Order 1/21
[20] Transcript Pg 1736-1737

current system. For MPI now to be implying that we are going to start this painstaking process from the beginning again is frankly absurd.

Current DSR model

The current registered owner model is not actuarially sound. This is undisputed by MPI[21]. The pricing analysis completed by MPI demonstrates cross subsidization with better drivers subsidizing poorer drivers[22]. Mr. Luke Johnston, MPIs former head actuary, acknowledged that the current model is not actuarially sound[23]. Mr. Phoa, MPI's actuarial analysist who provided evidence in this years GRA confirmed the current model does not accurately price risk.

MPI has therefor proposed improvements to the current model. MPI is proposing a gradual transition towards adding additional DSR levels at the top end of the range to be implemented over the next 5 years. MPI is further proposing that the discount percentages offered at DSR levels 10 + gradually increase, to move towards more actuarially indicated rates[24]. While CMMG is supportive of this shift in the interim, it is CMMG's position that the ultimate goal of achieving accurate pricing based on risk is unattainable within the current model.

The current registered owner model does not prohibit the registration of a vehicle by an individual who does not primarily drive that vehicle[25]. No matter how the model is altered or improved it will continue to accommodate this risk misalignment. There has been considerable reference throughout this years Application of customers 'gamming the system'. This phrase implies that the system or model is being inappropriately used, which is simply not the case. No customer is gaming a system by operating within the permitted rules of the system. If anything, the current registered owner model encourages registration of vehicles under an individual with the best or better DSR rating. Further it is important that registration of vehicles is not limited to a household. It is very likely that children no longer living at home continue to register their vehicles with their parents who have a more favourable rating.

MPI has supported is stance in favour of the registered owner model over the primary driver model by arguing that customers do not want a change. This was again referenced by Mr. Scarfone during his closing submissions[26]. As the Board is well aware, MPI conducted a customer survey of the DSR system in 2019. The report provided responses from customers who were in favour of the registered owner model. Customers in support the current model made references qualities of the model focusing on

- it being 'fair',
- that it is accurate and works,
- that MPI should not change was isn't broken[27]

[21] 2022 GRA Part VI DSR Pg 7 Line 16-18
[22] 2022 GRA Part VI DSR Pg 12 Line 6-8
[23] 2021 Transcript Pg 1588 Line 8-13
[24] 2022 GRA Part VI DSR Pg 9-14
[25] Transcript Pg 1915 - 1915
[26] MPI Exhibit #122 Pg 47
[27] CMMG (MPI) 2-13 Appendix 1 Pg 47

CMMG submits that the customer survey failed to adequately inform customers of the details of the models they were providing feedback on. Customers were not provided with MPIs position that the registered owner model is not fair, is not accurate and is not working[28].

Despite these concerns, the customer feedback indicates that the primary driver and registered owner models are the most favoured models by customers[29]. The survey also demonstrated that almost half of respondents prefer a different model from the registered owner model[30]. It is CMMGs position that had customers been properly informed of the issues presented by the registered owner, as well as the fact that changes to the current system would be required in any event, the responses to the survey would have likely been different, and perhaps more in favour of a primary driver model.

Throughout the hearing MPI raised concerns about the primary driver model. The principal concern raised is that a primary driver model will not solve the current problems that exist with the registered owner model. Witnesses for MPI repeatedly indicated that customers could lie as to who is the primary driver[31]. Mr. Scarfone in closing also touched upon this, saying 'People lie'[32]. CMMG does acknowledge that it is conceptually possible for customers to be untruthful in their registration of insurance. However, the proposition that people today who register their vehicle with another individual to reap the benefit of a better DSR level, as is permitted by the current system, that those people will chose to lie or misrepresent the primary driver of their vehicle in a different model is an assertion unsupported by any evidence. CMMG submits that MPIs position that the primary driver model then will suffer the same risk inaccuracies is illogical and wrong.

MPI witnesses commented that the primary driver model would create a burden for customers who may have to report changes in primary driver to MPI throughout the course of the year[33]. On cross examination Mr. Prystupa acknowledged that the intention of project NOVA, which is in process now, is to allow customers to renew or purchase plans online[34]. These technology improvements will help to alleviate any burden MPI customers may experience where they need to register a change in the primary driver of their vehicle.

MPI voiced concerns with administration of claims in the primary driver model[35]. MPI seems to be implying that where someone other than the primary driver is driving the vehicle during the collision that this will impede the claims administration process. CMMG submits the claims administration process under the current registered owner model where the driver at a collision is not the registered owner would be unchanged.

Finally, we come to the challenges posed by project NOVA. MPI has in previous years and in this GRA said, that implementing the Primary Driver model during NOVA is 'not feasible'. MPIs evidence on this point has been inconsistent. Mr. Mitra starting at Page 2372 of the transcript confirmed that Duck Creek will have the functionality or configuration to implement a change in the DSR system. As he outlined, the

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[28] Transcript Pg 2016 Line 20 – Pg 2016 Line 4
[29] Transcript Pg 1709 Line 24 – Pg 1708 Line 10
[30] Transcript Pg 1906 Line 21 Pg 1907 Line 14
[31] Transcript Pg 1711 Line 23
[32] Transcript Pg 2614 Line 14-18
[33] Transcript Pg 1714 Line 7-11
[34] Transcript 1916 Line 5-12
[35] Transcript Pg 1714 Line 12-17

ability to more easily make changes is part of the reason that project NOVA is happening in the first place – to move away from the legacy systems, and towards off the shelf solutions. Mr. Mitra confirmed that where a change is not made before the 3A release, that does not prevent the Corporation from configuring Duck Creek in the future. Other factors such as customer communication, determining the detail of the model itself, legislative changes etc.. are the items that will require some time and resources. CMMG acknowledges that there will be some cost to these changes, but submits, that whether those changes happen now or in 5 years, the cost to customers will be the same. The challenges and cost to the Corporation must be balanced with the cost to customers of maintaining the current model. Even with the proposed changes to the DSR system, good drivers continue to subsidize poor drivers. This cross subsidization will continue to occur during the period that MPI proposes to very slowly shift to a more actuarially sound system. Every year that the primary driver model is not implemented, is another year of compounding costs to good drivers.

MPI provided evidence in last years GRA, which was then reaffirmed on cross examination by Mr. Watchman, that where the Public Utilities Board makes a recommendation on a change to the DSR model MPI will initiate the process to have the Lieutenant Governor in Counsel consider changing the model[36]. While MPI is free to take their own position with regard to a change in the DSR system, MPI must acknowledge the evidence presented in this hearing.

CMMG submits that the various reasons presented by MPI for maintaining the registered owner model do not hold up upon review. The primary driver model provides a more accurate system based on risk. It would be more fair, and just as simple as the current registered owner model. It can be implemented within the project NOVA timeline and will quickly and efficiently terminate cross subsidization occurring in the current model. The DSR system is key in reducing collisions frequencies[37]. Further, improvements to the actuarial soundness of the DSR system will lead to further improvements in collisions claims thereby reducing costs and reducing required premiums[38]. MPIs suggestion that they need to provide a business case, is simply another stalling tactic. MPI was ordered by the Board in Order 1/21 at Pg 67 that MPI bring forward a plan, including timelines, milestone and implementation date for any changes to the DSR model. MPI instead has not provided this information and indicated it will not move forward with a change. Where MPI wanted to provide a business case to the Board they have had more than ample opportunity to do so.

CMMG's recommendations on the DSR issue are as follows

Recommendations:

1. **That MPI be Ordered to immediately commence collection of primary driver data from insureds**
2. **In the 2023 GRA filing that MPI provide an analysis of the partial primary driver data collected to date, including but not limited to**
    - **% of drivers who have a different declared primary driver from registered owner;**

[36] Transcript Pg 1795
[37] Transcript Pg 1892 Line 21-24
[38] Transcript Pg 1894 Line 13-19

- **DSR differentials between registered owner and declared primary driver of vehicles; AND**
- **An examination of the impact on insurance premiums a change to the primary driver model would have on those registered owners who have declared different primary drivers for their vehicles;**

3. **In the 2023 GRA filing that MPI provide a pricing analysis of the primary driver model using the partial data collected, extrapolated for all MPI customers;**
4. **In the 2023 GRA filing MPI provide a discussion of business rules the Corporation would recommend for a primary driver model;**

Ratemaking

In the 2021 GRA MPI was Ordered to file an alternate rate indication by major use class with the use of points on a yield curve. CMMG disagrees with MPIs interpretation of the directive, and cross-examined Mr. Phoa on this issue. While MPI acknowledged CMMGs differing interpretation of the directive, they were unable to provide an undertaking using the interpretation advanced by CMMG in time for this hearing. As a result the Board directed CMMG, the Taxi Coalition and MPI to discuss the matter and provide wording which will provide an Alternate Rate Indication for next years GRA. As MPI noted in their oral evidence, we have collaborated and reached agreement.

CMMG therefore recommends the following:

Recommendation:

1. **That MPI be Ordered to provide in the 2023 GRA an Alternate Rate Indication on an Overall basis and by Major Class using the yield that corresponds to each Major Class's average duration. The average duration by Major Class is to be calculated using only the claims for a particular Class.**

CMP

The Capital Management Plan has been a challenging topic in this years GRA. When the Capital Management Plan was first proposed by MPI it did not receive a favourable response from the CMMG. As some may recall, Mr. Oakes affectionately referred to it as the "Collect More Pesos" Program. It appeared to our client as a slush fund – a way for MPI to line their reserves to ensure any missteps made by the Corporation can be adequately covered for. Mr. Oakes compared the CMP program to the Cow Brand Baking Soda company, where a company which sells baking products, wants more, and creatively comes up with an advertising campaign which encourages people to buy their baking soda and immediately pour it into the garbage to make it smell better[39].

Despite these analogies the CMP was approved by the Board in Order 176/19 for a two year trial period. Unfortunately, that trial period has been mostly subsumed by the current and ongoing pandemic. As a result, MPI has requested from the Board an extension of the trail period.

CMMG acknowledges the limitations that have been identified in the CMP over the course of this pandemic. My client is not opposed in principle to MPI's proposal that the trial period of the CMP be extended for one year. It would be beneficial to the Board to have the CMP operational over a more 'normal' year.

Unfortunately, we don't whether the next year even be normal. Manitoba is experiencing is 4th wave and the pandemic looks like it will continue going forward. As MPI has indicated it is impossible to predict how the pandemic will continue to play out. It is likely that further rebates will be required in the future.

With that in mind it is CMMG position that the CMP does require modifications, to provide a system for returning excess revenues collected quickly to rate payers. CMMG understands from MPIs closing submissions and questioning from the panel that the capital release provisions will be maintained in the future and that MPI is seeking to remove the 5% release for this year only[40].

CMMG therefore is supportive of MPIs proposal for an additional year of the Capital Management Plan and looks forward to further proposals from MPI as to how the CMP can be modified to better accommodate for excess retained revenues.

REBATE, TRANSFERS TO DVA

The Transfers from Extension to the DVA line of business has been a major topic in this years General Rate Application. Our friends at CAC Manitoba have canvassed in detail and with great skill the legislative issues with MPIs decision to transfer Extension revenues to Baisc.

CMMG supports CAC Manitoba's position and recommendations to the Board that the Board should find the transfer to DVA from extension to be unlawful and that as a result the Rebate amount as proposed by MPI should be increased to include the total of $113 Million dollars.

I would like to thank the Corporation and its witnesses for their presentations during the hearing and candid answers during examination. Further I want to thank the other Interveners in this application for their collaboration and finally thank for the board for their consideration of the intervention of CMMG in this year's Application.

[39] 2019 GRA Transcript October 30, 2018 Pg 1754 - 1755
[40] Transcript Pg 2654 Line 9 – Pg 2656 Line 1