

Rate Stabilization Reserve Capital Management Plan

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2022 General Rate Application



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Agenda

1. Rate Stabilization Reserve (RSR)

- Purpose
- Use of 100% Minimum Capital Test (MCT) Target

2. Capital Management Plan (CMP)

- GRA History
- Changes to Components
- COVID-19 Impacts
- Future Rebate Methodology



Rate Stabilization Reserve



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Rate Stabilization Reserve (1/2)

Purpose of the RSR

“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”

- **CMP is a simple methodology designed to:**
 - Achieve aims of RSR
 - Adjust it annually toward 100% MCT in predictable and orderly manner
- **CMP manages rate volatility by:**
 - taking predetermined steps to move RSR towards its 100% MCT target in each application
 - capping rate surcharges at 5.0%



Rate Stabilization Reserve (2/2)

Reserves Regulation (76/2019)

- **Defines manner in which MPI must determine amount it must retain in its reserves**
 - 100% MCT for RSR
- **Restricts use of surplus funds in RSR**
 - Funds can only be used to reduce rate indication required for Basic in subsequent year
- **In Order 176/19, PUB held the Reserves Regulation to be *ultra vires* and not binding on PUB**
 - MPI still bound to comply with Reserves Regulation despite holding
 - MCT industry best practice, 100% target absolute minimum for P&C insurer in Canada
 - Use of 100% MCT target does not result in excessive accumulation of capital





Capital Management Plan



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Capital Management Plan (1/7)

- **2019 GRA**
 - ▶ **CMP developed, Capital Maintenance Provision introduced**
 - ▶ Impact on Rates: +2.1%
 - ▶ MCT % at start of rating period (March 1, 2019) = **51.5%**
- **2020 GRA**
 - ▶ **Capital Build/Release Provisions introduced, Capital Maintenance Provision eliminated**
 - ▶ **Approved for two year trial period**
 - ▶ Impact on Rates: -2.1% (elimination of Capital Maintenance Provision)
 - ▶ MCT % at start of rating period (April 1, 2020) = **105.8%**
- **2021 GRA**
 - ▶ **Completed year 1 of trial**
 - ▶ Impact on Rates: -5.0% (addition of Capital Release Provision)
 - ▶ MCT % at start of rating period (April 1, 2021) = **~137.0%**
- **2022 GRA**
 - ▶ **Year 2 of trial period – MPI seeks suspension of capital release, extend CMP trial period**
 - ▶ Impact on Rates: 5.0% (removal of Capital Release Provision)
 - ▶ MCT % at start of rating period (April 1, 2022) = **100.0%**



Capital Management Plan (2/7)

Components of CMP

- ▶ **Accepted Actuarial Practice (AAP) Ratemaking**
 - No changes proposed

- ▶ **Capital Targets by Line of Business**
 - Targets set by *Reserves Regulation*

- ▶ **Capital Transfer Rules**
 - Automatic transfer from Extension to Basic where excess capital is available
 - Based on Extension MCT values relative to target at each fiscal year end

 - Reduce or eliminate requirement for capital build provision (to the extent possible)

 - No transfers from Extension to Basic in 2020/21 and 2021/22
 - Excess capital transferred before FYE to DVA
 - MPI expects transfers from Extension to Basic to resume in 2022/23



Capital Management Plan (3/7)

Capital Transfer Rules and the DVA

- ▶ \$60M was transferred from Extension to DVA in March, 2021 with a further \$53M projected in March, 2022
- ▶ MPI is statutorily mandated to administer the DVA; however, there is no corresponding statutory source of funding for these operations
- ▶ MPI is not prohibited from transferring profits from Extension to lines of business other than Basic
 - Transfers of this nature have been occurring for nearly two decades
 - Extension offers optional products with an intent to earn a profit; these profits are for utilization at the discretion of MPI
- ▶ MPI continues to be in dialogue with Government with the aim to obtain funding in order to make the DVA line of business self-sufficient
- ▶ MPI Management and its Board are responsible for the operations and financial health of the overall corporation which includes all of its lines of business



Capital Management Plan (4/7)

Components of CMP (cont'd)

▶ Capital Build or Release Provisions

- Get to 100% MCT in appropriate timeframe (Build = 5 years, Release = 3 years)
 - ▶ Step 1: Determine the Basic MCT at the beginning of the rating period (i.e. April 1, 2022)
 - ▶ Step 2: Calculate the Capital Build or Release Ratio
 - ▶ Step 3: Calculate the Target MCT at the end of the rating period (i.e. March 31, 2024)
 - ▶ Step 4: Compare the forecasted MCT to the Target MCT at the end of the rating period and apply Capital Build or Release Provision if necessary
- MPI seeks suspension of use of Capital Release Provision for 1 year
- Releasing capital via rebate more appropriate than release in current climate
- Removal of capital release provision offset by the rebate application
 - Effectively “resets” RSR at the beginning of rating period by releasing excess capital to 100% MCT



Capital Management Plan (5/7)

Impacts of COVID-19 on CMP

1. RSR is rapidly accumulating significant excess capital due to historic reduction in claims frequency
2. Following 2 rebates totalling \$180M in 2020/21, Basic MCT ratio continues to surpass 100% target more quickly and by higher amount than anticipated
3. COVID-19 tested capital release provision and identified weaknesses
 - Release provision designed to gradually release excess capital
 - More appropriate when excess capital in RSR is not significantly higher than target MCT ratio
 - Could take years to reduce RSR to 100% MCT using capital release provision
4. MPI requires an additional tool to expeditiously release excess capital



Capital Management Plan (6/7)

Why Remove the 5% Capital Release?

Separating Accepted Actuarial Practices (AAP) Rate Indication from Capital Requirements

Stop mixing the **prospective** ratemaking with the capital build/release provisions that result from the **prior** period experience.

1. Strong development of capital due to COVID and need to expedite the return of excess premiums to customers
2. Capital release is a temporary relief, affecting rate stability
 - Timing the removal of the capital release with a rebate is advantageous for customers
3. Rebate requested and overall impact on customers



Capital Management Plan (7/7)

Rebate Methodology

- MPI will fully consider rebate methodology and present same to PUB in 2023 GRA
- Mechanism used in CMP to release larger amounts from RSR while maintaining rate stability
- Rebate “triggered” when the Basic MCT meets a certain threshold
- Rebate calculated at the beginning of a rating year (i.e. March 31, 2022 for the 2022 rating year) and contingent on MCT ratio at that time
- Rebate would be maximum possible to maintain Basic MCT ratio above the 100% MCT over 2 year rating period (i.e. for 2022/23 rates the rating period is fiscal 2022/23 and 2023/24)
- Methodology should address pandemic-like situation wherein the RSR accumulates large amounts of excess capital within a short period of time

