MANITOBA PUBLIC UTILITIES BOARD

Re: MANITOBA PUBLIC INSURANCE CORPORATION (MPI)

2018/2019 GENERAL RATE APPLICATION

HEARING

Before Board Panel:

Robert Gabor, Q.C. - Board Chairperson

Michael Watson - Board Member

Carol Hainsworth - Board Member

Allan Morin - Board Member

Robert Vandewater - Board Member

HELD AT:

Public Utilities Board

400, 330 Portage Avenue

Winnipeg, Manitoba

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APPEARANCES

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Robert Watchman	)Board Counsel
Roger Cathcart	)Consultant
Alex McQuarrie	)Consultant
Steve Scarfone	)Manitoba Public
Matthew Ghikas	)Insurance
Byron Williams (np)	)CAC (Manitoba)
Katrine Dilay	)
Raymond Oakes	)CMMG
Erika Miller	) CAA Manitoba
Christian Monnin	) Bike Winnipeg

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--- Upon commencing at 9:06 a.m.

THE CHAIRPERSON: Good morning, everyone. I understand that there's going to be an exhibit entered by MPI. Mr. Scarfone...?

MR. STEVE SCARFONE: I believe it's actually by Ms. Dilay.

THE CHAIRPERSON: Oh, Ms. Dilay, you're -- okay.

MS. KATRINE DILAY: Good morning.

THE CHAIRPERSON: Good morning.

MS. KATRINE DILAY: As you'll recall, there was an undertaken -- undertaking taken on Monday by Andrea Sherry and so we've just filed the response as CAC Exhibit 24.

THE CHAIRPERSON: Okay.

--- EXHIBIT NO. CAC-24: Response to Undertaking Number 34 by CAC

MR. STEVE SCARFONE: I can advise, Mr. Chairman, there is a con -- a response to a confidential undertaking that we're still just putting the finishing touches on to make sure that that can be addressed as well and we can deal with that at the break.

And the quarterly financial report --

THE CHAIRPERSON: Well, that's what I was referring to is the quarterly --

MR. STEVE SCARFONE: Yeah, we'll -- we'll handle that at the break.

THE CHAIRPERSON: At the break, okay.

MS. KATHLEEN MCCANDLESS: So the Exhibit 55 isn't being entered right now?

THE CHAIRPERSON: I'm just wondering if it shouldn't be entered before we go -- move into submissions.

MR. STEVE SCARFONE: Okay, we can do that then, it's Exhibit 55, as I understand it. Thank you.

THE CHAIRPERSON: Right.

--- EXHIBIT NO. MPI-55: MPI quarterly financial report

(BRIEF PAUSE)

THE CHAIRPERSON: Okay. Ms. McCandless, did you want to start?

MS. KATHLEEN MCCANDLESS: Yes, thank

you.

CLOSING REMARKS BY MS. KATHLEEN MCCANDLESS:

MS. KATHLEEN MCCANDLESS: We have now completed the evidentiary part of this public hearing with respect to the 2018 General Rate Application, or GRA, filed by Manitoba Public Insurance. The Board will soon deliberate on the application for base rates and premiums charged for compulsory vehicle and driver insurance to take effect on March 1st, 2018.

As counsel for the Board, I do not take any position on the merits of any part of the application or the positions taken by any of the parties. My role is to summarize the matters that are before the Board and outline issues that it may wish to consider making its decisions.

In its application, the Corporation has requested a 2.7 percent overall increase in Basic premium revenue, along with changes to the driver safety rating system, equivalent to a further 1.8 percent increase in Basic premium revenue, or $17.5 million.

With respect to the requested changes to the driver premiums through -- through the driver safety rating system, the proposed driver premium increases only impact drivers on the demerit side of the scale and are structured such that no demerit driver will face an increase in their 2018/19 premium relative -- relative to what they paid in 2017/18, if they qualified to move up the scale with an incident free year of driving in 2017/18.

MPI seeks no changes to vehicle premium discounts, and does not propose any changes to service or transaction fees, permit and certificate fees, fleet rebates or surcharges, or the discount for after market and manufacturer or dealer installed anti-theft devices.

The average rate adjustment proposed by MPI for each major vehicle class is as follows:

For private passenger, an overall increase of 2.6 percent.

For the commercial class, an overall increase of 1.4 percent.

For the public class, an overall increase of 1.1 percent.

For motorcycles, an overall increase of 2.8 percent.

For trailers, an overall increase of 16.8 percent;

And for off-road vehicles, an overall

decrease of 43.9 percent.

After consideration of insurance use and territory, and capping and balancing for experience rate adjustments, the results were modelled by the Corporation to assess the impact of various rate and classification changes. In total, the vehicle population for the year of the application is 1,130,267 vehicles, including 69,687 off-road vehicles to which the proposed rate would be applied as follows:

724,523 vehicles or 65 percent of the overall fleet would receive a rate increase. The majority of which would be $99 or less.

286,330 vehicles or 25 percent of the overall fleet would receive a rate decrease.

And 115,238 vehicles or 10 percent would re -- receive no change in rates.

The basis for the 2.7 percent rate requirement changed in the current application. Prior to this application, the Corporation's estimate of its overall rate requirement was based on achieving an approximate breakeven accounting result as measured by net income over the year of the application and the year following.

As directed in Board Order 162/16,

following the 2017 General Rate Application, the Corporation's rate requirement now reflects its interpretation of the requirements of accepted actuarial practice in Canada.

The Corporation's estimate of its overall rate requirement is sensitive to the methods and assumptions used in its derivation. In this hearing, considerable attention was paid to certain assumption areas, including the basis for interest rate forecasting, the choice of the cash flow discount rate, and the consideration of the expected return on investment assets supporting Basic total equity.

With respect to interest rate forecasting, the Corporation has indicated that as a rule of thumb, every 10 basis point increase in the cash flow discount rate used for rate setting will reduce the rate indication by .2 percent.

In this application, the Corporation has adopted a naive interest rate forecast, which assumes no change in market interest rates from current levels. To mitigate the risk of mis-estimation due to interest rate forecasting, in its application the Corporation has proposed a compliance filing process whereby its rate indication would be updated to reflect actual market interest rates in late November 2017, using a naive interest rate forecast thereafter to pre -- to provide a possible foundation for the Board's Order in this application.

The Corporation has filed estimates of the impact of instead forecasting interest rates based on a consensus bank forecast, which is the standard interest rate forecast. And, alternatively, interest rates based on an average of the naive forecast and the standard interest rate forecast, also known as the 50/50 forecast.

Based on market rates as of September 30, 2017, the Corporation estimates that its overall rate requirement would fall to 1.8 percent, with the standard interest rate forecast, and 1.9 percent, with the 50/50 forecast.

Accepted actuarial practice in Canada expects the use of a cashflow discount rate consistent with the investment income to be earned on assets that might be acquired with the net cashflows resulting from the revenue at the indicated rate. So, in other words, the use of an expected new money rate over the proposed rating year.

In its application, the Corporation has assumed this new money rate can be approximated by the claims discount rate used for valuation purposes. The

Corporation has provided an estimate of a true new money yield on its bond portfolio of 3.42 percent, consistent with the application's financial forecast as compared to the application's assumed cashflow discount rate of 3.79 percent, a difference of 37 basis points.

The Corporation has taken the position that the expected return on investment assets supporting Basic total equity should not be recognized for rate-setting purposes. Instead, the Corporation has indicated its intention to allow the return on investments to be a source of natural growth for Basic total equity.

The Corporation has provided an estimate of the impact of including a breakeven profit provision that would include this source of revenue, indicating that the rate indication would decrease from 2.7 percent overall down to a range of 1.1 percent to 1.6 percent, depending on the assumed target capital level. All other things being equal.

The Corporation has also filed estimates of the impact of combining recognition of this source of revenue with interest rate forecasts based on market rates as of September 30, 2017, which indicate that it's overall rate requirement would decrease to a range from 1 -- 0.1 percent to 0.6 percent, depending on the assumed target capital level and the choice of the standard interest rate forecast or the 50/50 forecast.

The Corporation has stressed that rate setting without recognizing the expected growth of Basic's risk profile due to the natural growth of its actuarial liabilities and its investment portfolio will necessarily lead to an expected depletion of Basic total equity.

In the Information Request and public hearing process, the concept of including a capital maint -- maintenance provision in rate setting as is done by the Saskatchewan Auto Fund was discussed.

With respect to financial results, the Corporation has provided to the Board its actual financial results with respect to the seven -- 2016/17 year, as well as for the first six (6) months of the current year 2017/18. For the 2016/17 year, fiscal year, Basic incurred a net loss of $123.1 million compared with a forecasted net loss of $13.4 million in last year's GRA. So, a negative change of $109.7 million.

This negative variance was attributed by the Corporation to an increase of $178.3 million in net claims incurred cost, due primarily to higher than forecasted com -- comprehensive claims at $32 million; higher PIPP claims from actuarial adjustments at $55.5 million; lower than forecasted interest rates at $60.9 million; and $33.6 million in other actuarial rate adjustments.

Overall, there was a variance of $175.7 million in und -- underwriting results from that presented last year. Offsetting this, the positive variances were attributed, in part, to investment income of $82.9 million; $66.1 million higher than the 16.7 million forecast last year.

The higher level of income was attributable primarily due to lower -- lower than forecast, changes in interest rates, accounting for $45.9 million of the difference.

With respect to the current year 2017/18, the subject of last year's GRA, MPI -- MPI forecast for Basic a net loss of $10.7 million for rating purposes which was revised to a net income of $57.5 million in this GRA. This positive change is primarily due to higher forecast growth in interest rates due to the assumed purchase of corporate bonds, which resulted in a forecast $75.6 million reduction in the claims liabilities, $42 million higher than forecast last year.

This positive variance was offset by increases in the collision and property damage forecasts as a result of higher claims frequency of $15 million; an assumed higher write-down of premium deficiency of $22.3 million; an increase in unallocated loss adjustment expense forecast of $0.9 million; and other impacts of $0.3 million.

This morning, MPI filed with the Board its second quarter report for the first six (6) months of 2017/18 ending August 31, 2017. The Corporation reported a net income of $42.3 million, an improvement of $69.2 million from last year for the same period.

Of the $42.3 million re -- in reported net income, MPI reports $9.2 million related to Basic, compared to a net loss of $51 million for the same period last year, an improvement of $59.3 million for the six (6) month period.

MPI also reports that claim's costs decreased by $63.6 million, or 10.5 percent compared to last year, due primarily to a decrease of $28.5 million, or 16.2 percent in bodily injury -- injury claims incurred and a decrease of $40.7 million, or 14.1 percent in physical damage claims incurred.

The $28.5 million decrease in bodily

injury claims was impacted by a decrease of $45.1 million due to the interest rate adjustment on unpaid claims.

In establishing Basic rates, the Board has stated in the past that it looks to the overall financial wellness of the Corporation. MPI has expressed disagreement with this approach and has asked the Board look at Basic's retained earnings only as it is a mandatory line of business that has to stand on its own financially. Though MPI acknowledges that the Basic compulsory program comprises the vast majority of the Corporation's operations. MPI's extension line of business represents 99 -- or 95 percent of the market inn Manitoba.

Over the last three (3) years, MPI has transferred $176 million in retained earnings from Extension to Basic. In 2016/17, $27.8 million. In 2015/16, $75.5 million. And in 2014/15, $72.7 million.

The Corporation had, as of year-end 2016/17, $261.5 million in retained earnings, including $99.2 million in Basic, $94.9 million in Extension, and $70.8 million in special risk Extension. Driver and vehicle licensing operations incurred a $3.3 million loss in 2016/17, reducing non

Basic retained earnings to $162.3 million.

Overall corporate equity as at February 28, 2016, including acc -- accumulated other comprehensive income was $357.2 million, of which 181 million relates to Basic operations; $98.5 million to Extension and 77.7 million to special risk Extension.

With respect to the rate stabilization reserve, the purpose of the RSR is to protect motorists from rate increases made necessary by variances from forecasted results and by unexpected events or losses arising from nonrecurring events or factors.

With respect to the dynamic capital adequacy testing, the DCAT report on Basic's financial condition was prepared internally by MPI's Mr. Luke Johnston, in accordance with the standards of practice of the Canadian Institute of Actuaries, and accepted actuarial practice in Canada.

The Corporation's Basic financial condition would be satisfactory if throughout the forecast period it is able to meet all its future obligations under the base scenario and all plau -- plausible adverse scenarios and that it meets the minimum regulatory capital requirement under the base scenario.

Based on this definition, Mr. Johnston concluded that Basic's fut -- financial condition is not satisfactory because forecasted Basic total equity, in the base scenario, falls below the Corporation's proposed $201 million lower threshold for the Basic total equity target capital range, which it adopted as the minimum regulatory capital requirement.

The dyn -- dynamic capital adequacy test base scenario is substantially identical to the application's financial forecast, and therefore, now adopts the naive interest rate forecast rather than the more optimistic 50/50 forecast used in the prior DCAT.

In its application, the Corporation proposed a Basic total equity target capital range of $201 million to $438 million, as compared to a range of $181 million to $411 million proposed last year.

The Corporation's proposed lower threshold of $201 million was based on scenario testing, adapted from the Basic DCAT to be sufficient to protect against Basic total equity falling below zero dollars at a 1:40 year or 97.5th percentile probability level under the combined scenario over a two (2) year time horizon -- horizon, including routine management regulatory actions.

The Corporation's proposed upper threshold of $438 million is based on a minimum capital test, or MCT ratio of 100 percent arising from the Basic DCAT. The Corporation supports the use of the MCT and the selection of the 100 percent target ratio as an ac -- accepted and objective industry standard. Also used for Basic auto target capital purposes in Saskatchewan and British Columbia.

The Corporation also provided alternative scenario testing based on an iterative modelling approach, which has evolved from work required by Board Order 135/14. This alternative scenario testing indicated a lower threshold for Basic total equity target capital range of $161 million to be sufficient to protect against Basic total equity falling below zero dollars at a 1:40 year or 97.5th percentile probability level under the combined scenario over a two (2) year time horizon, and including routine management regulatory actions.

This alternative scenario testing also indicated a number of different upper thresholds for the Basic total equity target capital range based on testing to maintain Basic total equity above the little level of the $161 million indicated lower threshold and varying depending on the probability level selected, and whether or not routine management or regulatory actions were se -- included.

For example, the indicated upper threshold at the 1:40 year or 97.5th percentile probability level over a two (2) year time horizon ranged from $315 million before routine management or regulatory actions down to 295 million, including routine management and regulatory actions.

With respect to investment income in the investment portfolio, the funds available for investment are primarily unearned premium reserves and unpaid claims reserves. The investment portfolio supports both the payment of accident claims, as well as the pension obligations of the Corporation. The size of the -- of the corporate investment portfolio for the year of the application is projected to be $2.77 billion for 2017/18 to grow to $3.24 billion for 2020/21.

The investment portfolio is currently comprised of 46.5 percent in Canadian fixed income, 23.1 percent in MUSH, 10.3 percent in Canadian equities, 5 percent in US equities, 10.5 percent in real estate, and 3.6 in infrastructure and venture capital.

Historically, the Corporation's investment income has been a major component of its income and has offset its annual underwriting losses. For 2016/17, MPI had an investment income for Basic of $82.9 million against an underwriting loss of $206 million and a total net loss of $123.1 million for Basic.

In the current forecast using a naive interest rate forecast, the corporate investment income was projected to be $119.7 million for 2017/18 of which Basic's share is $101.8 million or 85 percent. Based on the September 30th naive interest rate forecast of 2.1 percent, reflecting an increase of 46 basis points from 1.64 percent used in the GRA filing, the Corporation is now projecting investment income of $34.9 mill -- for Basic to offset a revised underwriting income now forecasted $22.9 million. Net income is now forecasted to be $57.9 million for 2017/18.

In Order 162.16, the Board directed MPI to file an asset liability management study to be filed in this application. The Corporation did not file the asset liability management study but in this hearing indicated that it issued a request for proposals for the study on September 12, 2017 and has engaged a consultant to deliver the study by November 30, 2017.

The Corporation has put in place an accelerated process to have a study produced in that timeframe. The indicated rate applied for by MPI is predicated on an assumed change in its investment strategy to increase the allocation of corporate bonds to a target weight of 18 percent of the total investment portfolio. This has been approved in principle by the investment committee of the MPI board of directors, subject necessary due diligence.

MPI has assumed the corporate bond portfolio would match the composition of the investment grade long-term Canadian corporate bond market, which is approximately 60 percent 'A' rated bonds and 40 percent BBB rated bonds.

MPI has forecasted that approximately $435 million in corporate bonds will be purchased by the end of 2017/18, funded by the sale of government bonds, bringing the total holdings to approximately $500 million.

According to MPI approval in principle of the increased allocation to corporate bonds is also contingent on certain conditions:

1) MPI having a sufficient capital

reserve as requested by MPI being a minimum RSR of $201 million and an upper limit of $438 million, based on a 100 percent minimum capital test ratio.

2) The approval of actuarially indicated rates without offset by investment income generated from the RSR; and

3) The use of the naive interest rate forecast in establishing actuar -- actuarially indicated rates.

MPI indicated that in addition to these three (3) conditions it is awaiting the outcome of the asset liability management study to ensure the proper investment portfolio.

The current proposed investment plan to increase the allocation of corporate bonds to 18 percent is also awaiting approval by the Minister of Finance.

MPI has an investment committee working group which includes members of MPI and the Department of Finance which discusses aspects of the Corporation's investment portfolio, including investment policy, investment income, re-balancing and the monitoring of ex -- external investment managers.

Mr. Garry Steski, the Assistant Deputy Minister of the Department of Finance, Treasury

Division, appeared as a witness subpoenaed by the Board, and provided testimony on the management of MPI's investment portfolio.

Mr. Steski is the co-chair of the investment committee working group. Mr. Scott -- Steski testified that a decision by MPI to invest in corporate bonds below an 'A' rating would require an Order in Council as a class of bonds is not permitted by the provisions of the Financial Administration Act.

With respect to operating expenses, total Basic expenses were $211.2 million in 2016/17, up from $207 million in 2015/16, and are forecast to be $224.1 million in 2017/18. Thereafter, Basic expenses are -- are expected or forecasted to grow to $230 million in the year of the application.

Salaries and benefits are a major component of the operating expenses of Basic, representing over 57 percent of the total operating expenses in the year of the application. Since 2013/14, the Corporation has experienced a compound annual growth of salaries and benefits of 2.7 percent, with compensation that has grown from $113 million in 2013/14 to $121.9 million in 2016/17. Salaries and benefits are forecast to be $128.8 million in the current year and are forecasted to be $130.1 million in 2018/19.

MPI -- MPI is now forecasting an increase in compensation expenses net of vacancy allowance of .88 percent in 2017/18, and an increase of 2.42 percent in 2018/19, which forecasts are in excess of inflation at 2 percent.

The collective agreement between MPI and the Manitoba Government and General Employees Union, which covers 90 percent of MPI's workforce, includes a 1.5 percent increase for year one (1) at a 2.0 percent increase for two -- years two (2) to four (4). The five (5) year contract is in effect for the period from September 18, 2017 to September 26, 2020.

As directed by the Board in Order 162.16, the Corporation prepared a zero-based budget of staffing levels. Staffing for 2016/17 was 1,920.1 full-time equivalents overall, with the projected staffing level of 1,926.9 full-time equivalents for 2017/18, an increase of 6.8 FTEs.

Normal operations staffing levels were one thousand eight hundred and ninety-eight point one (1,898.1) full-time equivalents in 2016 and '17, and were forecast to grow by twelve point two (12.2) FTEs to one thousand nine hundred and eleven (1,911). Initiative staffing levels declined by five point nine

(5.9) full-time equivalents, from twenty-one point two (21.2) to fifteen point nine (15.9).

In this application, MPI has identified nineteen (19) full-time equivalent management reductions in 2017/'18 for a savings of $1.9 million, and thirteen (13) full-time equivalent management reductions in 2018/'19 for an annualized savings of $1.3 million. The annualized savings to Basic in the rating years 2018/'19 and 2019/'20 is forecast to be $1.2 million in each year. MPI also forecasts additional full-time equivalent savings of five hundred and ninety-six thousand dollars ($596,000) in 2018/'19 and $2.85 million in 2019/'20. Details of the full-time equivalent changes were not provided, as they were deemed confidential.

In addition, MPI's 2017/'18 budgeted staff complement includes three hundred and forty point two (340.2) full-time equivalents to support its infrastructure, its IT infrastructure and projects, of which two hundred and forty-eight point two (248.2) full-time equivalents are internal staff, and ninety-two (92) full-time equivalents are external IT contractors.

MPI has indicated that it plans to internalize twenty-seven (27) IT positions over three

(3) years, including twelve (12) reductions in 2016/'17 to achieve $2.4 million in annual savings by 2019/'20. MPI has projected that Basic capital expenditures are $26.4 million for 2017/'18, 37 -- $31.7 million for 2018/'19, and $33.4 million for 2019/'20, amounting to over $91 million in the next three (3) years.

The majority of the capital spending is on IT-related projects. MPI has indicated that it has over $167.1 million in ongoing and future IT projects, including the multiyear Physical Damage Re-engineering Program commenced in 2010/'11 with an original budget of $65 million. One (1) future IT project relates to the replacement of the AOL CARS system at a budgeted cost of $62 million. The forecasted spend on this initiative is a financial funding envelope to ensure future corporate financials have the appropriate anticipated expenditures allocated. No spending on this project is planned for 2017/'18.

Mr. Martin Geffen of Gartner consulting appeared as a witness for the Corporation to speak to the Gartner IT CIO scorecard and inf -- infrastructure benchmark, and the Gartner-prepared evaluation of the Physical Damage Re-engineering Program. According to Mr. Geffen, the original the PDR program included twenty (20) projects, which included the replacement of the CARS system. The replacement of CARS has been removed from the PDR program budget.

Mr. Geffen reported that eight (8) of the PDR projects were completed, and seven (7) were cancelled, as MPI determined that they are not strategic and do not add to the business case. MPI has indicated that the $11.3 million in costs originally budgeted for the seven (7) cancelled projects has been reallocated to remaining projects. Gartner further indicated that there are five (5) projects yet to be completed.

Gartner found that the overall total budget of the Physical Damage Re-engineering Project has not changed, but costs have been reallocated among various components of the project. Approximately $43.4 million has been spent to date, with $18.1 million remaining to complete the program. The PDR program is currently projected to be complete by the end of fiscal year 2019/'20 for a total projected spending of $61.5 million.

With respect to the savings and benefits of the PDR prog -- program, Gartner determined a net present value benefit overall has been reduced from $18 million in last year's evaluation to $13.7 million. The internal rate of return of the project has declined from 8 percent to 7 percent. The cost-benefit analysis excluded maintenance cost, which Gartner estimated based on industry standards to be 18 percent to 20 percent per annum.

Gartner's CIO scorecard report reported that MPI spends 63 percent of its IT budget on personnel, as compared to -- compared to its peers at 44 percent. Gartner also reported that 34 percent of MPI's IT staff is made up of contractors as compared to its peers at 17 percent. Mr. Geffen commented that while MPI's oversta -- overall staffing remains higher than its peers, MPI is transitioning from the use of third party contractors to staff.

The Gartner CIO scorecard and infrastructure benchmark report also indicated that the business process management maturity for MPI remains generally low at 1.6 percent as compared to 1.78 percent for peers, which appears to be an opportunity for improvement.

With respect to road safety spending, MPI is forecasting to spend $13.1 million in Basic road safety and loss prevention programs in 2018/'19. The largest component is spent on driver education, including the High School Driver Education Program, at approximately $3.7 million, or 28 percent of the overall budget. Impaired driving prevention strategies are the second largest expenditure, at $1.9 million, or 15 percent of the overall budget. The balance of the road safety programs are advertising and sponsorships, road safety programming and road watch, which is increased enforcement.

This concludes my closing comments. I have attempted to comment on the main issues that arose this year. I would like to thank both MPI and the Intervenors for their cooperation extended throughout the hearing, and thank you to the panel as well.

THE CHAIRPERSON: Thank you, Ms. McCandless. I see that we have certain guests here. I'm just wondering if you'd like to introduce them into the record. I don't know who's taking the lead, if it's Mr. Ghikas or Mr. Scarfone.

MR. MATTHEW GHIKAS: I'll be starting off this morning --

THE CHAIRPERSON: Okay. Thank you.

MR. MATTHEW GHIKAS: -- Mr. Chairman, and perhaps I will do the introductions. So with us this morning, then, is MPI's chair Brent VanKoughnet on the left, and, you know Mr. Guimond here from past years, Dan Guimond, the president and CEO, and a new face for you as well is Mark Giesbrecht. He is the newly-minted vice-president of finance and chief financial officer, and I suspect you'll see him more in the future.

THE CHAIRPERSON: Thank you. We welcome all of you. At this point, before you start your submission, Mr. Ghikas, I'd like to make a few comments on behalf of the Board in relation to Mr. Guimond who will be retiring from MPI. And I'm -- I don't know, Mr. Guimond, if you feel more comfortable sitting there or sitting here. It doesn't matter to me.

Sure. It might be easier for me to look forward and... I just thought we'd take this opportunity prior to the -- prior to MPI's submission for us to say a few words. I have a letter which will be going to Mr. Guimond today, but I would like to read it into the record.

"Dear Mr. Guimond: We understand that you will be retiring as president and CEO of the Manitoba Public Insurance Corporation, effective March 1, 2018. On behalf of the Board, staff, and advisors of the Public Utilities Board of Manitoba, I would like to -- to both offer our congratulations on your retirement and acknowledge your significant contribution to MPI and to the people of Manitoba.

Since joining MPI as a business -- business analyst in 1990, you have risen through the ranks through a combination of intellect, talent and dedication. You've held a number of positions within MPI, becoming the vice-president in 2005, vice-president of strategy and innovation in 2009, chief information officer in July 2010, and finally, as president and CEO in February 2014.

The world has changed greatly since you joined the Corporation some twenty-seven (27) years ago. I would suggest that when you first joined MPI, it was an insurance company which used technology to some degree, and now it has become primarily a technology company that sells insurance and provides a myriad of services to its customers, and you drove much of that change. This is the last time you will appear before the PUB for a General Rate Application. I suspect that that in itself is reason to celebrate. At the same time, I question whether the public fully understands the role of a Crown corporation and what is required to run it. A focus on best practices while adhering to oversight by an independent adjudicative body.

We have not always agreed on issues. To expect a regulating entity and a regulator to always agree would be naive, as we have different mandates. But on those occasions where we disagreed, we never once doubted your integrity, nor your commitment to the Corporation, the government of Manitoba, or the ratepayers whom you ultimately served.

I understand you will be moving to your dream house in Canmore, Alberta, an incredibly beautiful part of this great country. I am uncertain what you intend to do in the future, but I trust you will continue to be active and use the time to transition to face new challenges. The great American financier, philanthropist, and statesman Bernard Baruch said, 'Age is only a number, a cipher for the records. A man can't retire his experience, he must use it.'

I have a suggestion for about your future endeavors. I was a technology lawyer and worked with many startup companies before I left private practice to become the Chair of the PUB. Startup companies need mentors who want to share their knowledge and experience with passionate young people who dream about changing the world. From what

I have seen, you would be a great mentor.
Again, on behalf of the Public Utilities Board of Manitoba, I congratulate you on your retirement and I wish you and your family health, happiness, and prosperity in the future. Best regards."

Thank you.

MR. DAN GUIMOND: I -- I'd -- I'd like to be able to say a -- a sincere thank you for -- for doing this this morning. I really appreciate it. It's been an interesting career, a rewarding career, and I'm very proud of what MPI does for Manitobans.

And I -- I think -- I think this company MPI is great in the sense of them staying true to its mandate, to its mission statement, and be able to do the things we do for Manitobans when they're involved in -- in automobile accidents, and the kind of coverage we provide, I think it's -- it's top-notch. It's -- nobody can beat us anywhere in the world, and I really feel proud of what we stand for and what we do.

And I appreciate the work that we've done together over the years. I think it's served

Manitobans very well and having the balance that we have in terms of how the laws are written. I think it's positive. Like you said, we don't always agree, but I think at the end, it's good for Manitobans to have these bodies in place, and how we interact, so at the end of the day, it always makes it better for Manitobans.

So thank you very much for doing this this morning.

THE CHAIRPERSON: Thank you, Mr. Guimond. Thank you for your comments.

Mr. Ghikas...?

MR. MATTHEW GHIKAS: The big anti-climax.

THE CHAIRPERSON: I was going to say, now into more mundane matters.

FINAL SUBMISSIONS BY MPI:

MR. MATTHEW GHIKAS: Yes. Yes.

So just in terms of the logistics here this morning, so what we've done. Mr. Scarfone and I are going to divvy things up today, and what we've done is there's been a -- a great collective effort to try to pull together a -- a more comprehensive document that, closing submission, in writing, it's a

-- a document of considerable heft and we prepared it at risk of burdening you with further paper in this proceeding, but I -- I think ultimately, our hope is that that will assist you when you take it away.

We're not going to read that to you today, but what the idea of that is is really, we've done a lot of the legwork to try to make sure we pulled together from the various areas of the application, the various pieces of information and put them in one (1) place for you so that hopefully that will assist your task when you deal with specific issues.

That document would be -- it's been filed and -- for -- for ease of reference, it's been given an exhibit number Exhibit 57, a little out of order here. But the other thing we've done is we've prepared a -- a slide deck, and that is really the basis of what we're going to speak to today. And that -- that has been given an exhibit number for reference as Exhibit 56.

--- EXHIBIT NO. MPI-56: 2018 GRA closing submission PowerPoint (Ghikas and Scarfone)

--- EXHIBIT NO. MPI-57: MPI Closing submission

MR. MATTHEW GHIKAS: And so what -- what we'll do this morning is I will kick it off, and then Mr. Scarfone will take over for a while, and then I will close things off again. And the without -- unless there's questions, I will dive right in.

There is a theme to this application, Mr. Chairman and members of the Board, that should be well understood at this point, and we've set it out on the first slide 3. And it is that Manitobans win when Basic is fiscally sound and self-sustaining. And the theme has come to play in this General Rate Application because the evidence that will -- that you have heard, and the evidence that we will take you back to today is that there is some work that needs to be done in terms of putting Basic on a path that will lead to term rate stability for Manitobans.

And that work does need to be done, in my submission, because it is important to Manitobans that they be able to rely on a product that delivers stable and predictable pricing over time. And I say on slide 3 that the requested orders in this application will put us on that path to the long term rate stability.

The rate increase, which I've restated is 1.95 percent, bec -- as updated to the September 30th interest rate, reflecting the costs of providing the product. Approval of upper and level -- our upper and lower RSR levels provide the capital cushion and the bandwidth to accommodate the volatility that is inherent in the industry. And the use of the total equity -- income on total equity will help provide a mechanism to replenish the RSR where there is no other mechanism to do so, and I will spend a bit of time on that. And the proposed driver safety rating revisions provide a -- both a means of making dra -- making the rating scale more reflective of risk, but also as you heard from Mr. Keith, it provides an important incentive function that ultimately influences claims costs in a way that is favourable to Manitobans overall.

So turning to the next slide of the agenda, the key speaking points, this really is set out as the key points that we're going to address. I am going to address these four (4) points before handing it over.

And they -- first of all, dealing with the Minister's mandate letter, because I believe, and -- and submit that it is a touchstone, certainly for

MPI, and something that the Board should also give consideration to in its deliberations.

I will spend the bulk of my time this morning dealing with points 2 and 3, and that is with respect to the capitalization. And the point being that MPI is thinly capitalized, and maintaining capital based on the proposed RSR levels will promote rate stability.

And the third point being that retaining income on total equity is both consistent with accepted actuarial practice and makes good business sense.

And the fourth point, which is dealt with in considerable detail in the written document, and so I will spend relatively brief amount of time dealing with it is that MPI has taken significant steps to contain operating and claims costs.

I will then hand things over to Mr. Scarfone, and he will deal with -- and there's a point missing, here, actually. The -- the next point that he will deal with is the driver safety rating changes.

And then 5, MPI is exploring ways to increase investment returns, but integral to that is to address the capitalization and the ability to replenish capital when assuming greater risk --

investment risk.

The sixth point, which Mr. Scarfone will deal with, again, is dealing with the IT projects, and the point being that the vast majority of these projects are being delivered on budget, that MPI is benchmarking favourably in important areas, and that value management process is and has been enhanced, and is being consistently applied to all projects.

And the final point that Mr. Scarfone will deal with is with respect to the road safety and loss prevention, and the framework that that is managed through and how that is working in a positive way for MPI and stakeholders. And then finally, I will turn with -- to a few concluding remarks.

So the first point, starting on page -- on -- on slide 7, and this is for those of us following along at home is paragraph 20 of the written submission. We've heard a lot about prudent fiscal management, and that is one (1) of the touchstones in the Minister -- the Minister's mandate letter. The other one that has received less emphasis in the proceeding, but I think -- and in my submission is -- is also important is that of transparency, and I will touch on transparency as well. And it is a priority of -- of MPI's Board of Directors, and I want to deal with at the conclusion of this some of the ways in which the cooperation that, Mr. Chairman, you referred to in the context of speaking to Mr. Guimond, that ways that we can improve the process going forward, both on MPI's part and the process generally. So I will touch on that in my closing.

And I was careful in quoting the mandate letter. When I put the ellipses in, I did smile to myself, but I double checked that. So I think I'm fine.

The prudent fiscal management on slide 8. So that theme arises in this general rate application, Mr. Chairman, because in simple terms, the current state is unacceptable and needs to be addressed, in my submission. And the Basic rates have been deficient. Basic is thinly capitalized, and systemic cross-subsidization is neither desirable nor sustainable.

And it is this process, this GRA process where the complementary roles of MPI and the PUB come together, and it is in this process where we can deal with, together, the issues of adequate capital reserves, appropriate premiums, and efficient and effective operations, which are the -- the foundation for prudent fiscal management to deliver on that mandate letter.

The second priority being transparency, which, again, I will come back to, but I -- but the -- the point being that MPI has made steps, and there has been a -- a significant increase under Mr. Guimond of additional collaboration with stakeholders and with the PUB, and a push, which MPI's hope is that it -- it was noticed by the participants, a push to add information to the materials filed and to do more in terms of -- of providing additional information. And it's -- it's hoped that that is -- that that is noticed and -- going forward. That's the intent to continue to work better on those points.

The -- having said that, there are areas where MPI recognizes it can improve, and I will touch on those later. And as I indicated, there are areas where, in my submission, the process can help with that.

So turning to the capital -- the issue of capital reserves. And this starts on paragraph 19 of the -- of the written submission. And I've included on this slide, slide 11, a quote from the -- section 18 of the MPIC Act because, for obvious reasons, this is an important consideration for the --

for MPI's board of directors. And they -- the -- MPI's board of directors and executive have to measure themselves against that standard ultimately.

And the concern on the part of -- of MPI is that in the current framework, things need to be done to make sure that going forward, the spirit of that provision is -- is adhered to and -- and respected. And so I pose the question at the bottom of slide 11, How do we measure up? And the answer is on the next slide.

Without a doubt, Mr. Chairman, Basic is the most thinly capitalized P&C business in Canada. It -- its Basic capital levels measured in minimum capital test are at 29 percent, and that is the lowest among any of the insurers that were discussed in this proceeding The objective evidence is clear on that point. And the next slide we'll turn to in a moment demonstrates that graphically.

And the evidence of Ms. Sherry and Dr. Simpson was clear that they were not aware of any out -- anyone lower either. And an important point, Mr. Chairman, is that not only is the current MCT lower, but the minimum level of RSR at 1:40 is the lowest level of capital accepted by any regulator in Canada as well.

And Basic has experienced the very type of 1:40 event in the last three (3) years that the RSR is designed to protect against, with Basic having lost $163 million over two (2) years due to interest rates alone. And as My Friend Ms. McCandless referenced, MPI's chief actuary has determined that Basic is in an unsatisfactory financial condition.

Here's the graphic that I alluded to, and it clearly shows where MPI sits relative to the other industry players. Now that thin level of capitalization is compounded in the current circumstances, Mr. Chairman, because Basic is also the least equipped among the Canadian insurers to rebuild or even maintain its capital levels. And I say that because Basic, as it currently stands, has no natural means of maintaining or building capital other than income that it earns on total equity.

Unlike private insurers, MPI's rate indication doesn't build in an underwriting profit. Private insurers have the ability to set that profit. Management will set that profit to make sure that it not only covers off its obligations with its regulator in terms of its MCT to account for natural growth in the business, but also to provide a return for its shareholders.

And unlike other Crown insurers, MPI has no capital maintenance provision to prevent the MCT level from falling as the business grows. And unlike other Crown insurers, MPI has no capital build provision to allow capital to not just be maintained at the current MCT level but to be built back towards whatever target is set as being appropriate by the regulator in those circumstances.

Now, you'll recall, Mr. Chairman, that on Monday, I took Ms. Sherry through the basics of -- of MCT and how it's calculated. And it was undoubtedly a little bit painful to go through that. But I think the exercise is one that's important.

And the key point in taking -- taking Ms. -- Ms. Sherry through that is, is that MCT is a measure of the adequacy of capitalization in the context of the size of the business. And as the business grows, the denominator -- the ratio of capital available to capital required -- the -- the capital required goes up as the business gets bigger. And if no provision is there to make sure that the numerator, the capital available, keeps pace with the denominator, the MCT level is going to drop.

Now, this -- the important point is that this isn't just a trick of math. The reason it's going down is because it's signifying that the adequacy of the capitalization is losing ground based on the size of the business and what the business demands. As the business grows, its exposure to risks increases and more capital has to be there when something unforeseen happens. And capital is eroded due to the natural volatility of the business.

We saw SGI. I took Ms. Sherry to SGI's framework. They -- they not only have a maintenance provision, the maintenance provision is simply one (1) that keeps the numerator in pace with the denominator and keeps the MCT at exactly the same level as when you started the year. They not only have that, they have a provision for capital build, which takes their target of 100 percent MCT and incorporates into the rate indication a positive profit provision that moves them one-fifth (1/5) of the way towards that target each year. One-fifth (1/5) -- one-fifth (1/5) closes the gap one-fifth (1/5) progressively each year.

Both of those provisions are a positive profit provision in the rate indication. They don't call them profit, but in actuarial terms it is a positive profit provision. And MPI has a zero profit provision, meaning that holding all other things being equal, each year as the business grows MCT is going to lose ground and capitalization is not going to keep pace with growth in the business. So each year, we're going to see, all other things being equal, the MCT dropping year after year from a position that is already the lowest of any insurer in Canada.

And on the last bullet on that slide, Mr. Yien spoke to the current available excess retained earnings in Extension $30 million. And the point is that even if the Board of Directors determined that a number -- another transfer from Extension is appropriate, the well is not infinite. And it is important to have Basic self funding itself and not consistently reliant on systemic cross subsidies.

So the solution, in my submission, Mr. Chairman is clear. It's that the lower RSR should be reconfirmed at 1:40. The upper RSR threshold should be set at 438 million, which flows from a hundred percent MCT, but is also supported by DCAT analysis -- and I'll take you there -- and that Basic needs a means of naturally replenishing its capital. And MPI has proposed simply applying the total income -- or the income on the total equity to -- to allow it to do that. That is less than what a maintenance provision would be. So even with that, there's the potential that we would lose ground, barring any -- any variances in the business that would require -- that would result in the MCT changing otherwise.

So on the next slide I've borrowed from the opening presentation of Mr. Yien and Mr. Johnston. And what this encapsulates really is that the -- in the RSR framework the tests that we look at, the question that we asked to test whether the -- the lower and the upper levels are appropriate are different. For the lower level, what we look at is how much capital do we need to withstand a plausible adverse scenario without exhausting total equity. So, you know, do we have enough to make sure that we don't have to go to taxpayers if something happens that brings the total equity to zero.

The test for the upper has to align with what the purpose of the upper level of the RSR is. It really needs to be wide enough to ensure that you're not balancing -- you're not -- you're looking at what level of capital is necessary to make sure that you don't fall below the lower level, necessitating a rebuilding fee.

So when you test the lower level, you're looking at including management actions, what the regulator would do, what MPI would do in terms of increasing rates that would help resist reaching zero. But when you're examining the upper-level the key point is that if you were to look at those factors it would be -- you'd be in a circular analysis, because what you're really trying to do is avoid a scenario where your capital is depleting to the point where you need a rebuilding fee.

So if you're counting rebuilding -- if you're counting rate increases as a means of avoiding a rebuilding fee, you're into a circularity there. So you need to be looking at testing that range, the upper-level adequacy, by -- by not including actions like rebuilding fees. And the just for reference in the transcript, this topic is discussed starting at paragraph 45 of the final submission.

So this touches on the same point, Mr. Chairman, which is that it is the width that is important, the width between those two levels that is important and that allows the protection against natural volatility driving rate increases. And what we want to avoid is a scenario where you're rebating one (1) year and then something happens unforeseen and you're rebuilding the following year. So you need enough width there to -- to account for -- account for those types of volatility, and we have seen significant volatility.

(BRIEF PAUSE)

MR. MATTHEW GHIKAS: And the point that was made by the witnesses is that if your purpose is to avoid volatility where you're bouncing from rebate to rebuild, you have to be doing more than operating right on the minimum, because when you're op -- when you're sitting -- when you're systemically right at the lower levels of that range, you're -- you're not really giving yourself the flexibility to avoid rebuilding fees and absorbing natural volatility. The odds are simply too high that you're going to drop below the level. So the witnesses characterized there being an optimal range and it's -- it's sort of in the upper area of that range between the two (2) levels.

And Mr. Johnston, and there's a quote in -- and I'll just read it, but there's a quote in paragraph 61 of the closing for Mr. Johnston, where he says:

"You know, we're always going to be on the cusp of unsatisfactory financial condition if we don't have

a range -- an RSR range, if we're
just sitting on the very edge all
the time. We prefer to have -- it
would make sense to have a range
where you could handle a normal
amount of financial variability and
the model used in this report is
just that there is existing DCAT
scenarios."

So he's getting at that point where hovering around the minimum is -- where we sit today is not -- not where we need to be in the long term to avoid volatility.

On the next slide I make the point, Mr. Chairman, that this is not a theoretical risk, that we are experiencing the types of circumstances that would lead to this bouncing between -- you know, that would lead to the -- the need for rebuilding fees. And these -- there's actually a good summary of these at paragraph 62 of the closing submission, and if you have it handy you can, you know, take a look at that.

But they -- they -- there's the 163 million loss due to the interest rate forecasts. There is 179 million in 2008/2009 from the stock market crash. Hail caused 49 million and 39 million losses, respectively in 2015 and 2016. And the list goes on from there.

But the cumulative impact of those issues that were identified -- and I'm at paragraph 63 -- the cumulative impact of those is $550 million. So over half a billion dollars of adverse events over a relatively short period of time with the largest negative impact single event is 179 million. And that is an astonishing amount to lose in a short period of time. And it's particularly difficult to handle when you're the most thinly capitalized insurer in the country, and you have no natural means of rebuilding your capital.

So the next slide deals with the minimum. And the point, which should be obvious from the heading, is that the lower RSR is really the lowest that it should go. In paragraph 64 of the argument there's a quote there from Mr. Johnston and he characterized it as the absolute minimum. And he said that the absolute minimum is not a desirable place to be. I think that is -- is an understatement, Mr. Chairman. And the -- the minimum translates to 37 percent MCT. And as I mentioned that this is -- this would be the lowest of any of the ranges permitted by regulators in the country by a country mile.

And this -- this level flows from the collaborative DCAT process, and it's one (1) that MPI is willing to -- to accept and Mr. Johnston is willing to sign off on. But for those of us who were here last year, we heard Mr. Johnston's reticence about having diluted the DCAT to the point at which we're down to 1:40, scenario and the assumptions that are baked into it.

(BRIEF PAUSE)

MR. MATTHEW GHIKAS: In paragraph 72 of the written submission, there is a quote from Mr. Johnston, and I would wager that Mr. Johnston is getting -- is about -- about in this quote -- about as indignant as an actuary is capable of getting, where he -- he's referring to one (1) of the Intervenors making a comment this morning that it's never going to happen and that I've never seen this happen, a 1:40 event. And he says that that's just totally false. It's happening right now. And he's right. It is happening.

Mr. Johnston will not put his professional name on anything lower. And for Dr. Simpson to dismiss the issues associated with adequate capitalization on the basis that this is a Crown corporation and can't go insolvent is, in my submission, missing the point; is that Manitobans expect that -- that Crown corporations be managed as a going concern, and not to turn to taxpayers to fund its operations because it's been managed at a level of capital that can't handle would be seen as a reasonably foreseeable event based on recent experiences.

The next slide deals with the upper target, and this number four-thirty-eight (438) comes from the hundred percent MCT. The DCAT analysis, which will touch on briefly in a moment produces a number that is slightly higher than that but with within the same sort of range. This slide really -- the first point on this slide sums up a lot.

And really the point -- I want to spend a moment on this because I think in prior years the nature of what the MCT test actually is was not particularly well explored. And that's probably a shortcoming on MPI's part more than anything, to explain what this test is, what it does, and why it works for a company like MPI Basic, notwithstanding the fact that it's a Crown Corporation. Because there has been in the past a lot of figurative arm waving about well, M -- this is developed for the private sector and it shouldn't be used for a -- for a Crown corporation.

And in my submission, the evidence that -- that is on the record in this proceeding demonstrates unequivocally that this test is a test that is developed based on risks that affect a wide variety of insurers, including Crown insurers, and that the fact that it's a monopoly fits in the other factors line of the -- of the test. And I -- I do want to spend a moment on this.

So if we could, Diana, if it's possible to pull up two (2) things. The first one (1) is the OSFI guidelines, Exhibit 53. And maybe we can do a split screen on these, if it's possible. So MPI Exhibit 53. And it's a few pages over. It's the list that I took Ms. Sherry to. A little further. There we go.

And then on the other page it would be GRA Volume 2, RSR-5, DCAT Appendix 1D, page 4. Do you need that again? No, you don't because you're the best person at this I've ever seen in my life. I hope you know how good you have it, Mr. Christle. Okay. Thank you, Diana.

So I took Ms. Sherry through these

factors. And the point that I was making in my cross-examination was that every one (1) of the factors on this list could apply to any insurer, Crown or --or private. And for some insurers, some of these lines will play a role. For others, they won't. For MPI, some of them don't merit a value because we, you know, there isn't a -- there isn't an issue with -- associated with this. But, really, what this test is doing is looking at an individual's balance -- an individual insurer's balance sheet.

And why I've put this up side by side, is because you can see this sheet on the right-hand side is MPI's snapshot summary page that corresponds with this list and the OSFI guidelines. And you'll see that some of the lines have zeros were they don't make sense for MPI. And you'll see that others have values in them because they continue to be exposed to interest rate risk, or foreign-exchange risk, or equity risk, or real estate risk.

And it's -- it's in capi -- (ii) e., capital required for other market risk exposures where competition comes into play. So it -- there's no line item that says competitive. You don't need to do that for a when -- when it's developed by OSFI. But -- but that's where that fits in, and that gets reflected in the results of the MCT for Basic.

So if you have two (2) insurers -- two (2) different insurers sitting at a hundred percent MCT, the amount of capital that each one (1) of those is holding is different in dollars. All that a hundred percent MCT is doing is saying, For that insurer, with that balance sheet, and exposed to those risks, is your capital available equal to the capital that you require. That's all it's saying.

And so an insurer that doesn't get exposed to competitive risk is going to end up with, other things being equal, a lower dollar amount produced by a figure of a hundred percent MCT than one (1) that's exposed to market risk. So this is a legitimate test. It's founded in a specific identified probability scenario over 1:100 and its results are based on MPI's own experience.

Ms. Sherry -- on the slide, again, back at slide 20. Thank you, Diana. Ms. Sherry, last year, was quite content to use the MCT test. She changed her views this year. But in my submission, fundamentally, there's nothing wrong with the test, and that her evidence last year should be preferred to the evidence this year.

Now, the next slide deals with the DCAT

scenarios, and the -- the figure on the right-hand side is -- is taken from the opening presentation of Mr. Johnston. But really, it shows that the odds of falling below the lower level when at various levels of capitalization. And you'll see that even in the third line there at 250 million, your odds are 1:2.1. So basically a 50/50 chance of dropping below the lower level and facing a rebuild. And at the proposed amount we're only at a 1:20 chance still. And we've been experiencing events over the last few years that are 1:40 events, which underscores the reasonableness of the proposal that's being made in the current context.

Now, the next slide is underscoring that MPI's proposal would still put MPI below every other insurer in Canada, even with the hundred percent MCT proposal as -- as its upper. The proposed upper RSR of a hundred percent MCT is equal to the regulatory minimum of ICBC, and well below its target of a hundred and forty-five (145), and its rebate level of a hundred and sixty (160).

And I can advise the Chair, just to make sure there's no uncertainty on this, but the regulatory minimum of a hundred percent at ICBC is in a regulation called "Special Direction IC2," issued under the Utilities Commission Act. The level of 145 percent and the rebate of 160 percent is determined by the Regulator. And the proposed upper level of a hundred percent MCT for MPI's Basic Autopac is equal to SGI's target. So MPI's upper is equal to the target of SGI and it's half of what the average of private PNC sure -- insurers hold.

And in my submission, framing these in MCT provides a valuable perspective to Manitobans. Because as we do in very other -- in various other areas, we hold out MPI and compare it against other benchmarks, other insurers, to see how -- to allow Manitobans to see how is your insurer performing relative to others.

And in my submission, when you -- when you tell people who are asking, Why it is Manitoba Public Insurance holding my -- my money that I've paid in premiums? Why -- why are -- why are we holding capital? It's a valuable point for them to know that, Yes, you need to hold capital. All insurers hold capital, because there needs to be money there to pay your claim when something bad happens. There needs to be money there to manage volatility so we're not having your rates bounce around.

But please know, Manitobans, that MPI

holds significantly less capital than every other insurer in the country. And in my submission, that's -- that's something valuable for Manitobans to know, and it's -- it's a value that using MCT provides and only using MCT provides, right? That's -- only the MCT can provide that benchmark comparison. Accounting for the relative size of the businesses of the various insurers using the dollar amounts doesn't cut it because it doesn't account for the difference in the risk profiles and sizes of the business. MCT does that that's valuable.

This slide, I won't belabour this. But I think when the Ernst and Young report is read in its full contact -- context, it's clear that what Ernst and Young is recommending is that ICBC's target be considered, that -- that the government consider reducing ICBC's target to a hundred percent MCT, to be in line with Manitoba Public Insurance and SGI. And so Ernst and Young is -- is actually assuming that MPI's capital target is a hundred percent, which -- well, that's what it's assuming when it gives its report.

I wanted to touch on the point about moral hazard, which was identified in last year's order. And as -- as MPI understood it there was --

the -- the concern was that if MP -- if MPI's capital levels are too significant that there is -- I'm inferring in this -- but that there is a less incentive to manage the business rigorously.

And in my submission, while that theory may warrant consideration, in practice it's just simply unjustified. And I make the point here that it is -- it is clear that you have a Minister who is mandating a focus on prudence fiscal -- prudent fiscal management and a Board of Directors that is fully engaged and committed to delivering on that. But there is evidence on the record, ample evidence, a significant amount of evidence regarding the cost containment processes that have been undertaken.

And in my submission, regulatory oversight, not changing capital levels, is the appropriate mechanism to guard against this concern that I'm inferring underlies that comment in the order. And, frankly, in my submission, it's difficult to see how even if one accepted that was a concept that needed to be considered, how having an RSR range that's lower than any other insurer in the country could incent irresponsible management.

So if we turn now to the upshot. Ratepayers are at risk of ongoing volatility as things sit. And MPI's proposals will reduce that risk. So I want to turn now to --

THE CHAIRPERSON: Mr. -- Mr. Ghikas --

MR. MATTHEW GHIKAS: Yes.

THE CHAIRPERSON: -- I'm just wondering if this is the appropriate point to take the morning break?

MR. MATTHEW GHIKAS: Absolutely. Thank you. Yeah.

THE CHAIRPERSON: Okay. So we'll -- we'll take fifteen (15) minutes. Thank you.

--- Upon recessing at 10:36 a.m.
--- Upon resuming at 10:54 a.m.

THE CHAIRPERSON: Mr. Ghikas...?

MR. MATTHEW GHIKAS: Thank you, Mr. Chairman.

CONTINUED BY MR. MATTHEW GHIKAS:

MR. MATTHEW GHIKAS: Now that everybody's fueled up on coffee, we're good to go. The next topic that I'd like to touch on is appropriate accepted actuarial practice-based premiums with a zero profit provision.

And this really is the framework for discussing the treatment of income on total equity. In this slide at the bottom of the slide, this really -- well, the slide is really a -- just to take us back to the 101s of accepted actuarial practice. And if I can step back for a moment and put this into terms that a simple lawyer like me -- how it was explained to me how this works.

The -- the key thing about accepted actuarial practice is that it focuses on the policies that you're writing in the policy year. So, in our case we're writing policies for the policy year 2018/2019. And what accepted actuarial practice does is it looks at those policies; it looks at the premiums that you're going to take in on those policies; and it looks at the costs of writing those policies; and it looks at the claims' costs that will ultimately be associated with those policies. And it tries to match those things with a provision for profit.

And this is a departure from the way things have been done, which was to look really more of a financial statement kind of view. And what the difference -- the key difference is, is that when you look at a financial view of things rather than an actuarial view, within your time period you have costs and revenues for that matter, but particularly, the claims' costs associated with policies that may have been written five (5), six (6), seven (7) years ago and they happen to be incurring claims' costs during that period.

So it's a fundamental shift. And in MPI's view, it's a -- it's a good shift and they, you know, they welcomed the -- the PUB's direction in pushing that way. It's a good change, and it -- it, you know, promotes rate stability, ultimately.

But in the context of this discussion, it's really important to zero in on that fundamental nature of looking at the policies being written and the cashflows associated with those. And if you look at the quotation from the Standards of Practice, you will see that you're looking at cashflows relating to in - and it's those words that are key - relating to the revenues at the indicated rate.

So that's saying, the cashflows you're looking at are related to what you're charging for the policies that you haven't yet written, okay. So those are the premiums you're bringing for 2018/2019 policies. They should equal the best estimate of the present value of cashflows, again, relating to the corresponding claims and expense costs. So, the costs associated with the policies that you have yet to write. And when you forecast those cashflows out, they should equal, plus a present value of a provision for profit.

And what is critical to understand in the discussion of crediting of -- of the treatment of the income on total equity is that we are talking about a provision for profit; that's what this discussion relates to because the income that is sitting -- the -- the total equity in the business is unrelated to the policies that are going to be written next year.

MPI already holds that cash. And the income that you earn on that has no financial relationship to the policies you are going to be writing next year. It's related to cash you're already holding. So, this isn't a contentious point. This -- this is actually the fundamentals, and you'll see if you look at -- if we flip over.

Well, actually before we do that, this isn't a contentious point. When -- if you look at Ms. Sherry's evidence all of her discussion is related to determining a profit provision. And I will turn you to that, but that's -- there is agreement on this that this is an issue relating to the provision for profit and it's a provision that management sets. So if you're a private insurer, management determines how much profit you want to make and then you include that in your rate indication a provision for profit to make sure that when you're pricing, you're pricing for a profit.

And Crowns don't have a need for a profit for a shareholder per se, but when you look at a maintenance provision, that is a provision for profit. It is a positive profit provision that you are including in your rate indication to make sure that you're bringing in enough cash to maintain the MCT level where it is.

And its capital build provision that SGI has, for example, that is a positive profit provision that they are including specifically in their rate indication to make sure that they're not only maintaining their MCT, but that they're building as well. So they're not -- they're not just recovering their costs, they're not just maintaining their MCT, they're building it and all of that requires a positive underwriting profit provision in the rate indication.

And I will turn, in a moment, to what

MPI's proposal is, is to have a zero profit provision in the rates; that's what -- that's what crediting the net -- the income on -- income on total equity does. It is a zero profit provision in the rate.

And what Ms. Sherry's proposal is, is to include a negative profit provision in the rates or an underwriting loss. So she is pricing the policies for next year at a loss by crediting cashflows associated with something completely unrelated with those policies to reduce the rate indication, that is --and I'll take you to where she does it but that is an underwriting loss priced into these policies. She calls it breakeven, but it's an underwriting loss that she's putting in and I'll take you -- take you there in a moment.

So, focusing in on accepted actuarial practice. This slide is the costs related to the policies written next year. This is effectively the revenue requirement. This is where all the expenses come through that get factored into the rate indication and you'll see where all those pieces fall in and you'll see that the majority of those expenses are claims costs, vast majority are. There's some operating costs in there. There's premium taxes, commissions, and then we have IT projects and IT expenses are down there at 2 percent and 2 percent, respectively. So that is the amortization expense associated with capital projects and IT related expenses. So, I'm going to come back to this -- this pie chart at the conclusion of -- the conclusion of -- of the -- my speaking today when we're talking about going forward.

But really, it's interesting to overlay this pie chart with the areas of focus in the proceeding, and you'll see that we spend a lot of time talking about pieces of that pie that are relatively small re -- relating to the whole -- the whole pie. So, I'll come back to that, but for my purposes right now, that's really just to say, these are the costs relating to -- so, the forecast costs and expenses relating to the policies being written next year.

Next slide. The revenues relating to the policies next year. So MPI collects the premiums for the policies it's going to write next year, and it invests those. And it invests those policies -- those are called the new money and you heard My Friend Ms. McCandless refer to the new money coming in the door.

The new premiums get invested and they earn a return, hopefully. The forecasted income on those new premiums is credited in the rate indication because it's a cashflow relating to those policies.

So I make the point, again, in the last bullet here that the income on total equity is different because this cashflow -- it's still a cash flow to the Corporation, still a cashflow to Basic, but it's not relating to the policies written, and that's provision for profit.

And you will see -- maybe Diana, is it possible to pull up transcript 1722 please, and this is line 16 to 21. Okay. So -- so maybe just a little bit higher on the screen, please.

Okay, and this is the section where we're talking about -- where we're talking about the profit provision, right. And so here's Ms. Sherry's agreeing that -- that is -- that what she's doing is putting in place a profit provision. And she talks about that in her written evidence as well.

And you can see we're talking about it -- her proposal being a negative profit provision. And then if you go down a little bit further, you'll see we're talking about management having the ability to set the profit provision. And this is important because the debate around, can we do this, is it appropriate to do this or not appropriate? Well, the reality is accepted actuarial practice doesn't determine what you do with your profit provision. It takes what management tells you -- management says to the actuary, this is what our profit provision is going to be, please include that in the rate indication and then the actuary calculates the rate based on that profit provision.

So, this isn't an issue about can we do it? Does the actuary -- is the actuary allowed to do this under Standards of Practice one way or the other. The only thing that's affected here is what management or, in this case, the commission is telling management to put in there for a profit provision. Both interpretations, Ms. Sherry's and MPI's, are allowed under actuarial standards. This is a profit provision issue, not an issue relating to cashflows associated with policies.

So, the provision-for-profit slide might actually be helpful to take up Ms. -- Ms. Sherry's evidence, and that's CAC Exhibit 4, page 4, please.

(BRIEF PAUSE)

MR. MATTHEW GHIKAS: And you will see -- actually, let's start on page 2, rates, okay. So the last paragraph on your screen you'll see Ms. Sherry is talking about this being proper.

"So although the proposed rate indication of MPI methodology has improved, it has a significant flaw in the calculation. The calculation includes a 0 percent profit provision which, in effect, allows the expected return on the investment assets supporting the total equity to be available to grow the RSR."

Okay. So she's saying the flaw in MPI's determination of its rates -- its rate indication is that there's a 0 percent profit. And then she goes over to the last page. Let's go to 4 and she says -- go on, right down to recommendation at the bottom there, right.

So she says,

"Investment income on total equity should be included in the calculation of the Corporation's rate indication calculation. This should be done using a methodology discussed or the collaborative process at last year's GRA review process. This methodology is to determine a profit provision adapted to Basic's breakeven objective estimated as IR over PSR..." and so on.

And I put to her that when you do her calculation, you end up with a negative number and she agreed. And so what she's doing -- and -- and she said, yes, it's an underwriting loss. When I asked her.

So, she is pricing in an underwriting loss into the policies going forward in order to facilitate what she's proposing. And she says "it's adapted to Basic's breakeven objective" which -- which I found interesting.

What -- what she's saying is, you know, to be fair, what she's saying is that by doing what she's suggesting, it's causing the total equity in Basic to have the same dollar amount as last year. So, she's saying it's breakeven. She's defining "breakeven" not based on how we're pricing policies properly under accepted actuarial practice, but rather going back to, what's our total income and is it the same this year as it was last year; that's breakeven.

That's what she's saying. And in order to get to the same number as last year, she's having the price next year's policies at a loss.

And I make the point in the last bullet there, and this is a really important point, is that after being so strong and critical of MPI about not moving towards accepted actuarial practice, what Ms. Sherry is doing is a throwback to the old model. She's looking at a balance sheet view, financial statement view of breakeven that has no place in accepted actuarial practice. None.

If we are pricing on accepted actuarial practice, we should be pricing on accepted actuarial practice and looking at the policies that we're writing next year, not trying to end up with the same net income that we had last year by -- by putting in an underwriting loss; that makes no sense, in my submission, and we should not be going back there.

So the next diagram really just -- it takes us back to Mr. Johnston's opening presentation where he -- he spelled this out. And so if we -- if we just look -- it's an intra -- it's -- it's a helpful diagram. I find it helpful anyway, but it sure the -- the elements that I was just walking through where you have the blue at the top, that's the pie chart that we looked at. And then we have -- we have the investment income in the green on the right. That's the new money coming in, the investment income on the new money.

So you're getting the credit of that. It's netting out against it and you end up with the orange, after you've taken into account the forecast income on the new money. So, you've got the orange and then you say, okay, well, what premiums do we need to write in the yellow to match the orange?

And then if you look down it's what Ms. Sherry's doing which is to say, well, actually we're going to put in another loss provision on there, equal to the red so that -- that what we're actually collecting is the light red for policies that we're writing next year.

So, accepted actuarial practice allows either interpretation. And the question then becomes: What makes good business sense? And in my respectful submission, what makes good business sense in the context of Basic is to allow income on total equity to replenish the RSR.

Basic is thinly capitalized. This is its only means of replenishing total equity, other than forecast variances. Other insurers, both private and public, include a positive profit provision in their rate indication to maintain capital and to build capital which MPI doesn't have.

And the next point is an interesting one, because it provides an interesting perspective because what MPI is asking for is actually less than putting a maintenance provision in. So even with this proposal, all other things being equal, the MCT is going to go down, right. So this is not even going to make up the difference based on the forecasted investment income on this. It's not -- it's not making up the difference.

If you -- if you do what Ms. Sherry is saying, and you put in a negative profit provision to allow this to be credited to the rates next year and, then you said, okay, well, now we need a maintenance provision. You're actually going to cancel out that, so you -- and our maintenance provision now has to make up all that, and add more to bring you back up for the growth in the business.

So, what MPI is proposing is a very reasonable proposal and it's less than what you would be doing if you were SGI, even leaving aside their billed provision.

So, when you're -- if you don't have a

means of replenishing capital and you're at the bottom of your RSR range, you really are setting up a circumstance where you're -- you're going to be looking at an RSR rebuilding fee. The odds are very high that you're going to be looking at that and in -- in my respectful submission, that -- that is something that we should be avoiding and this is a way of trying to mitigate against that in a very reasonable fashion, in my submission.

So if we go to the next slide you'll see. I like this quote from Mr. Johnston. I thought he summed it up nicely. Here it is:

> "If you don't do this and you don't have a billed provision, you're relying on luck essentially and luck is not a strategy."

And I like that. I made notes when he said that during the hearing and I wanted to make sure I put that in here because I thought, yep, that pretty much sums it up. And so, in my submission, we should be relying on what is really a strategy and not luck.

Now, one (1) of the arguments that Ms. Sherry put forward for not -- or for -- for pricing the policies next year with an underwriting loss is that it reflects normal best practice. Those were her words "normal best practice." And you'll see there her quote there. She bolded the "best practice."

And the point that I'm making on this slide is that her appeal to best practice and her appeal to normal practice is highly selective because normal practice -- normal best practice in BC would have MPI with a capital target of at least 100 percent MCT, not 37. And if we were to really apply normal best practice, we would be up in the hundred and forty-five (145) degree range of ICBC, or perhaps the 200 range of the private insurers.

And she is advocating last year and Mr. -- Dr. Simpson mentions it again this year, a 1:10 DCAT to set the range around the lower. One in ten, a 1:10 chance of zeroing out your capital after management action. So, after you've had rate increases you're still going to zero out 1:10 chance; that's what she sees as a good idea. Notwithstanding her advocacy of normal best practice.

That is so far off normal best practice that she can't even, as a professional actuary, sign off on that. And that's what she's recommending for MPI.

Normal best practice would be for an insurer to have a means of maintaining its MCT in --

in response to growth in the business. Normal best practice would have a means of growing, building your capital, not just maintaining it. And normal best practice, as she describes it, would avoid systemic cross subsidies.

And I found this -- this point really interesting. She was -- her -- her argument was that -- oh, this is actually on the next slide. I'm stealing my own thunder here. Let's go over to the next slide.

She -- another one (1) of her arguments was one where she said, this is fair. It's fair to, you know, to -- to credit -- credit this income and -- and include an underwriting loss because it avoids intergenerational equity. And her argument in her evidence was, the money held in Basic total equity was built up from policyholders over time. Well, in the rebuttal evidence, MPI pointed out, well, actually a hundred and seventy-six (176) of the hundred and eighty-one (181) million of that isn't actually from Basic policyholders at all, it was a transfer from optional.

And so her response to that was in her PowerPoint that it doesn't matter. They're all the same people anyway and -- and Basic should have access to all the funds in Extension. Of course, that's not an actuarial opinion. She's here to be a professional actuary. She's advocating for a position, but it's -- it's not an actuarial principle that she's citing and she admitted that, in fairness.

But what is interesting is that her actuarial opinion actually speaks exactly the opposite of that outcome. She says:

"Normal best practice to include the investment income on the surplus backing the book that you are pricing, for it is revenue cashflow to that book."

Now, she's saying that because she wants the cashflow sitting in Basic total equity, the income on that, to be associated with the Basic book of the business.

But the logical extension of that is that the optional capital should be there for the optional book, not the Basic book. And so her -- her -- her call to normal best practice completely undercuts her argument there. And frankly, it undercuts the position of some of the Intervenors that this should be a systemic cross subsidy when pricing Basic insurance.

And if we're moving to accepted actuarial practice and we take Ms. Sherry's word for it, we should be treating the Basic book as a standalone.

And this was another one (1) of my favourite quotes from the proceeding, which I wanted to make sure we were in here. Mr. Simpson is simply expressing that he sure hopes that we would be leaving the income on the total equity to rebuild the RSR.

"I sure hope that's what they would do with the money, yes."

Well, we hope you'll do that too.

Very briefly on cost containment. This is, of course, the third pillar of the prudent fiscal management, Mr. Chairman. It's well set out, and the evidence was --was well canvassed at the hearing, so I'll spend less time on it, but really the key message on it -- I'll flip through these relatively quickly.

But the key message is that there is -- there's been a lot done in terms of cost containment. You have a board of directors that is very hawkish on cost containment, and you've seen that play out over -- over the last couple of years, and certainly and recently.

And you -- you'll see these are just

some quotes about, really, we're past the point of low hanging fruit and putting stretch targets and the like that are a real challenge and will continue to be a real challenge for the Corporation.

Just the highlights, really, is that the initiatives focus not only on operating expenses but also on claims expense and if you remember the pie, obviously, the claims expense is the biggest of those two (2) and there will be -- due to the relative size of those pots of money, a limit on the amount that you can reduce rates by cutting operating expenses; still important to focus on it, but obviously, you know, there's a limit on what you can do when the majority of your costs are claims expenses.

So MPI has been looking at both pots and has done a lot in terms of the operating expense budget. We've got decreases in the operating costs and no contribution to the rate indication at all. And then you've got the rodent claim strategy and the physical damage stretch targets, which are -- which are on the claims' costs.

And of course, we shouldn't forget also that you have road safety and loss prevention because, ultimately, those are initiatives aimed at lose -- at reducing claims costs overall and -- and MPI has done a lot in that regard and Mr. Scarfone will deal with that separately.

The successes are reflected in the benchmarking. Those are summarized in the written submission, but they collectively, in my submission, tell a compelling story in terms of cost containment.

And the next slide shows the role that the cost containment has played and you'll see the rodent strategy is -- you'll recall Mr. Johnston saying that originally he was at a 7.7 percent rate increase, and that -- that just wasn't acceptable. So, this is the contribution that got -- got it down to 2.7. And now that 2.7, of course, is 1.95 based on the interest rate update.

But you'll see the rodent strategy is 1 percent reduction and the indication .9 percent for the physical damage stretch targets and .5 for the expense reduction. So, a considerable contribution and the other two (2) items on there are ones that My Learned Co-counsel Mr. Scarfone is going to deal with now.

So, I will turn things over to him, driver safety rating.

MR. STEVE SCARFONE: Thank you, Mr.

Ghikas. Good morning, Mr. Chairperson, panel members.

I do, indeed, intend to begin with the driver safety rating and the proposed changes that are being proposed by MPIC in this rate application. I'll also touch upon information technology, investments, and then, lastly, the loss prevention road safety issue that was spoken to by Mr. Keith.

I do expect, Mr. Chair, that I'll probably be longer than a half-hour, but my -- I'm in your hands. But I expect that I'll get through road safety, at least, and probably information technology depending on when the Board wants to break.

THE CHAIRPERSON: Why don't we just see where we're at, Mr. Scarfone --

MR. STEVE SCARFONE: Yes.

THE CHAIRPERSON: -- and -- and if we can finish shortly after 12:00, we'll just keep going, otherwise, we'll -- we'll determine it at some -- at some natural break in your presentation.

MR. STEVE SCARFONE: Yes.

THE CHAIRPERSON: I don't want to interrupt your presentation at some, you know, at some spot simply because it's noon.

MR. STEVE SCARFONE: Very well. Thank you.

THE CHAIRPERSON: Okay.

FINAL SUBMISSIONS BY MR. STEVE SCARFONE:

MR. STEVE SCARFONE: A big part of this year's General Rate Application are the proposed changes to the driver safety rating system, which system has been in place since 2010 with no changes since its inception. And the Corporation of -- is of the view that now is the appropriate time to make some changes.

The Corporation is of the view that these changes are unique and a creative solution for the -- for the Board to consider. Firstly, it serves to reduce the initial rate indication by 1.8 percent. Perhaps, as importantly, it incents good driving behaviour. And, as -- as indicated throughout the proceeding, it applies only to those drivers on the demerit side of the scale.

I probably should begin with the legislative authority that governed the driver safety rating program. It's found in the regulation under the Manitoba Public Insurance Corporation Act and the purpose of it is set out there, but it's really just to rate a person based on in -- input factors that are recorded on one's driver's license.

And these input factors over time determine the premium that the person must pay for a -- a driver's certificate. So the input factors determine where you fall on that scale. And the input factors are traffic convictions and at-fault claims. Those are the two (2) things that move you down the scale.

On the merit side of the scale or what we've called the good drivers, and on the demerit side of the scale the bad drivers or the riskier drivers as Mr. Keith called them. And one (1) full year of accident free/conviction free driving brings you up the scale and at -- any at-fault claims and convictions bring you down the scale.

So at its core, the proposed changes to the driver safety rating system will employ a user pays pricing approach. Now that is, if a driver engages in poor driving behaviour, the proposal is that -- well -- and as it exists now, they pay more. If a driver does not engage in poor driving behaviour under the proposed changes, they will not pay more, and will likely pay less.

The changes, as Mr. Johnston testified to, will increase road safety. We saw that from the inception of the driver safety rating program. The traffic accidents decreased, as did at-fault claims and convictions.

The proposed changes will increase revenue and will decrease, as I've indicated, the overall rate indication and -- and not to put too fine a point on it, Mr. Chair, but if all demerit drivers went accident free for one (1) year, which we're not suggesting is likely to happen, MPI would not collect one (1) penny of its projected $17.5 million in additional revenue.

But the Corporation would, I expect, publicly celebrate the reduction in claims, both personal injury and property damage.

There's two (2) excerpts there that I'd like to bring your attention to. During the testimony of Mr. Johnston, and again from Mr. Yien. Mr. Johnston said that:

> "We believe that rather than just applying across-the-board increases, particularly to the merit side, that is, to the good drivers that we'd be better served by focusing on the highest risk drivers now going 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 results
in our claims forecast."

So there's a dual benefit to this proposal. And Mr. Yien had to say that there are two (2) factors that are extremely important. And this is from 508, the transcript.

"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."

Mr. Yien said, "it's an amazing result."

And so that is the dual-purpose that we think is served by adoption of the proposed changes by this panel. An increase in road safety and an increase in revenue and a decrease in the overall rate indication.

No driver on the demerit side with a clean driving experience will pay more than he or she did in the previous year; that's an important point. But the proposed changes make driver premiums more reflective of the risk that drivers are imposing on the system, to all Basic policyholders. And the best result is one where drivers change their high-risk driving behaviour and stop imposing those additional costs on everyone else.

There was some evidence put to Mr. Johnston during his cross-examination that convictions aren't directly related to claim costs but it's important to remit remember, Mr. Chair and panel members, what -- those input factors are legislated and have been since 2010. And Mr. Johnston indicated in his evidence that drivers with more traffic convictions are riskier drivers and they cause more accidents.

He said, There is not a direct connection, as a collision obviously doesn't have that direct cost. And those were in the questions -- questions put to him by My Friend Mr. Watchman. But going back again to the DSR application, he said, The conviction experience was seen to be just as strong a predictor of future at-fault claims as accidents were.

And he said, Since the DSR was implemented, what we're hoping for, again, is this time around, after eight (8) years, with increases to the bottom, is that customers will get the message that these types of behaviours have financial consequences, and hopefully they'll do as they did in the first iteration of the RSR and have less accidents.

The conviction behaviour has improved dramatically since the DSR was implemented, and the at-fault claims experienced at the bottom of the scale has also improved dramatically. And so we might expect those same results with the implementation of even higher premiums for the riskier drivers.

The proposed changes, MPI says, is fair and equitable, and will serve as an effective deterrent. And if, Mr. Chair, if you -- if you're not convinced that the DSR is an effective deterrent, you only have to look at the court registry and the number of small claims that are filed by our customers, because when our adjusters find a driver at fault, they have a mechanism available to them to appeal the adjuster's decision, because they know that that at-fault decision, if you will, results in five (5) demerits on the scale.

And so we get served with hundreds of

small claims every year are drivers are up against the other driver trying to have that liability decision overturned. So it is an effective deterrent. People care. They don't want those -- those five (5) demerits added to their -- to their driver's licence.

Under cross-examination, it was suggested to Mr. Johnston that -- again, by My Friend Mr. Watchman -- that the DSR is not statistically driven. And at page 527 of the transcript. Mr. Watchman asked Mr. Johnston"

> "The point being, sir, that is not actuarially sound and in a number of instances, it's not statistically driven?"

Mr. Johnston responded by saying, "I would, looking at this graph" -- and that was the graph that showed the premiums and the costs.

> "I would, looking at this graph, say it's very statistically driven."

So I'm struggling. If your point is just that 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 -- driver premium rates to have demerit drivers pay more of their fair share to the green. And that -- and that to the -- the goal of the proposed changes, to have the demerit drivers pay their fair share.

Important here as well is that Manitobans support the proposed changes. Manitobans want the riskier drivers to pay more for the driver premium, and this was the subject of an undertaking that Mr. Keith provided to Board counsel, the annual surveys that showed Manitobans, at least 50 percent, and more in previous years, are of the view that poor drivers pay too little. This past year was 50 percent, but you'll see back in 2014 and 2015, it was high as 57 percent, never falling below half of Manitobans. So more than half of Manitobans believe that these riskier drivers should pay more.

Everyone has a shared interest in reducing the social and economic costs associated with collisions, and risky driving is a significant contributing factor in collision frequency. We know that. Mr. -- Mr. Keith is said as much. The DSR incensed safer driving, and this Board, from Mr. Ghikas's jurisdiction, the bonus-malus system works.

The benefits of the proposed changes to road safety and loss prevention cannot be overstated. And during his cross examination, Mr. Keith was asked by counsel for the CAC, Mr. Williams, My Friend, to learn -- to explain from a high-level perspective the impact of the DSR on collision frequency.

And I was going to thank Mr. Williams if he was here today, because he effectively threw Mr. -- Mr. Keith a -- a softball, in my view. He asked him an open-ended question on cross-examination. And when you ask a witness like Mr. Keith, an executive who is obviously passionate about his job, an experienced, knowledgeable, and intelligent witness, this is the answer you get to an open-ended question on the high-level benefits of the Driver Safety Rating Program.

Mr. Keith said,

> "With respect to the broader issue of driver safety rating, there can be criticism about not doing enough to protect vulnerable road users, motorcyclists, all road users, for that matter. And 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 discuss. [But he said]

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 being very clear that the people who exhibit this driving behaviour will pay more, and that these drivers are not going to be subsidized by other insurance ratepayers. And by the way, if you're a high-risk driver, you have the power not to ever have to pay these additional premiums."

And he ends by saying:

"So I think we have a real opportunity here at a higher level to 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 a message that if you continue to exercise these types of driving behaviours, you will pay more."

And that is the -- is at the heart of the proposed changes here before you today.

The DSR changes, as I've said, are fair and equitable. The scale provides for financial motivation and allows the drivers on their own to move up and down. The Corporation says the PUB should embrace this opportunity to strengthen the DSR incentives and resist placing too much weight on any misalignment there may be between costs and premiums at one (1) or perhaps two (2) DSR demerit levels.

The proposed changes are the right thing to do. They lower the rate indication and they make our road safer. And the stats maintained by MPI show that claims can be expected to decrease, perhaps dramatically, as they did when it was first implemented eight (8) years ago. And finally, the proposed changes achieve the policy objectives of the regulation.

Now, I'll move on to information technology. And it's important, I think, Mr. Chair, panel members, to -- to bear in mind the -- the relative costs as shown in the costs pie that -- that Mr. Ghikas had before you, and that is that IT projects constitute 2 percent of MPI's overall costs, and IT expenses, an additional 2 percent. So information technology in totality represents 4 percent of the Corporation's total costs.

IT investments reduce risk and they deliver benefits to our ratepayers. And the IT strategic plan will be driven as we heard by the corporate business strategy. These are the areas I'll canvass. MPI's value management process. We heard it's evolving, becoming more formalized. And lastly, I'll touch upon Gartner's IT assessment, which was favourable, in our view.

Information technology investments are driven by four (4) distinct drivers: Strategic planning, external events, things that, as you heard, were -- are outside the control of MPIC, legislative changes, for example. Other drivers include societal changes, and of course, the technical requirements of the Corporation.

MPI will continue to operate under the existing IT strategic plan pending MPIC's board of directors, completing their assessment and establishing a new business direction. The IT strategic plan is in support of the corporate strategic direction. And Mr. Yien indicated that the

IT strategy and business strategy will be filed in the 2019 General Rate Application. In fact, that str -- strategic plan is -- is due to be completed in the fourth quarter, so by March 1st of next year.

Currently, the Corporation is operating under the 2016 IT strategy, which remains MPI's tactical plan for its investments, and includes those three (3) bullet points. The basis for the IT strategy, key drivers for change, and the corporate roadmap of strategic IT initiatives.

MPIC has appropriate governance in place, oversight, and mechanisms in place, and accountability for its value management process. And the value management process as described by Mr. Yien is to ensure benefits and projected costs are achieved. And there's four (4) components to that: There's business case development, business case approval, and BTO project delivery, the business transformation office, and post-implementation reviews as part of the business case component.

There was some discussion in cross-examination on business cases during this proceeding. Mr. Yie -- Mr. Yien fielded most of those questions. He spoke about the value management process, and how it's more than just business cases, in his view.

I want to take you to another excerpt...

(BRIEF PAUSE)

MR. STEVE SCARFONE: At page 405 of the -- of the transcript, Diana, please.

(BRIEF PAUSE)

MR. STEVE SCARFONE: Board counsel was asking Mr. Yien about what, in practical terms, the value management process that was in place at MPIC involved, and his response, I think, is worth repeating.

He said,

> "The value management process is about keeping accountable for projects 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 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, are we ready for this?

And if that's the case, there's some sort of writeup on it. It may not look like a 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 associated costs? And we have to bounce that off others that may have done it before.

And I said yesterday, sometimes we share it with our colleagues, our comparative organizations, like SGI and others. So after those discussions happen, we start to refine, and we start to frame what that benefit looks like.

The cost is little more difficult, particularly if it's something new. And so we get through the process of building it. And then he goes on to say:

> "I just want to differentiate the difference between the past and now. The future means that all that information that he just made

reference to will get captured in
one (1) document, and that's what we
call a business case."

And when I said earlier that we follow value management process, that was a little bit different. It's all those things that are being done, including all the way down to when we approve a business case, and then 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 executive meeting.

So that was his response to what value management is. And so it's important to keep that in mind in the context of business cases, because a business case is just one (1) small part of the value management process. And before an information technology project is undertaken, all of this collaboration internally happens. Discussion committee meetings, emails.

It's important to note as well that on a go-forward basis, all of that in Mr. Yien's testimony will be part of one (1) document called the business case, and that will apply for every project that exceeds a five hundred thousand dollar ($500,000) threshold.

The Gartner IT assessment we say is favourable. The benchmark and scorecard summary shows that MPI's IT spend as a percentage of operating expenses has gone up, indicating successful IT investment. It also shows that the catch-up spending has stabilized; that is, trying to catch up on what they call technical debt. Information technology, employee and incult -- consulting counts are steadily decreasing, and -- and Mr. Geffen confirmed that, that there's lit -- there's less reliance on external consultants for information technology projects. And lastly, the -- the Gartner assessment found that MPI continues to improve its maturity, driving effectiveness of the IT program.

BI3, the business improvement initiative. I -- I'm sorry. I should know that, but BI3 was not touched upon other than a report that was prepared by Ernst and Young. They conducted a post-implementation review of the project and concluded that the BI3 had met its business objectives. EY confirmed that the BI3 is the best in class document in claims management system and it showed productivity savings of $9 1/2 million. And perhaps more importantly, it's increased the duration of closed claims, that is, closed claims are now reduced, resulting in additional savings of $35 million. So the number of days that a claim is open has been reduced as a direct result of the BI3 project.

There was more evidence in this proceeding heard about the Physical Damage Re-engineering Program. We heard from Martin Geffen that the Physical Damage Re-engineering Program is on track, and that the PDR is transforming the way MPIC does business.

I don't know if any of you were up late -- late last night, but the -- the PDR was in the news, the late news on CTV. The direct repair component of it, which is a -- a big part of -- of the PDR, was a feature. It unfortunately started with the anchor Renee Rodgers saying that accidents happen all the time in Manitoba, but then she quickly went on to the main part of her story, which was a customer who was part of the direct repair experience, and speaking with a -- a repair shop owner. And they were all raving about the benefits that it's going to -- to provide to Manitobans.

THE CHAIRPERSON: I'm -- I'm sorry to interrupt, Mr. Scarfone, but --

MR. STEVE SCARFONE: Yes.

THE CHAIRPERSON: -- this comment, plus the small claims comment, you realize we can't --

MR. STEVE SCARFONE: Oh, I understand.

THE CHAIRPERSON: -- it's not -- it's not in evidence.

MR. STEVE SCARFONE: Not in evidence, yes.

THE CHAIRPERSON: So -- so --

MR. STEVE SCARFONE: Yes.

THE CHAIRPERSON: -- you know, while they -- they are positive statements, we can't consider it as part of our deliberation.

CONTINUED BY MR. STEVE SCARFONE:

MR. STEVE SCARFONE: Oh, I absolutely understand, Mr. Chair, yes. Yes.

The evolution of the Physical Damage Re-engineering Program has preserved the original objectives. That was the evidence of Mr. Geffen. Gartner found significant strides in its completion. Gartner found streamlining the projects had occurred, and Mr. Geffen testified that changes in scope were purposeful, and that in the end, at the end of the day, $13.6 million in annual benefits would be realized in perpetuity.

Overall program costs were consistent despite revisioning. And Mr. Yien indicated that in his experience, and Mr. Geffen as well, that budgetary reshuffling as seen under PDR is not uncommon. Most importantly, the PDR program is on target to be completed under budget, $4 million under budget.

(BRIEF PAUSE)

MR. STEVE SCARFONE: In his evidence on the -- on the budgetary reshuffling as -- as I've called it, Mr. Yien said, when I put that to him, he confirmed that he had been exposed in his career to at least twenty (20) projects of this size. And he indicated in his evidence, for a project, this kind of shuffling would not be -- for one (1) project, this kind of shuffling would not be common.

However, PDR, he said, is an aggregate of projects with varying levels of complexity. And for a project of this level of complexity, it would be highly unusual for an organization to plan ahead of time and know exactly what they need. The resources, the timing, the constraints, the budgets, and come back even a couple years later and say, That's exactly how we planned. We got it all perfect. So to answer your question, he said, I would find it highly odd and unusual if the budget did not change.

And we know that it did over the course of seven (7) years. And that trans -- that passage is from page 1,546 of the transcript, Mr. Chair.

(BRIEF PAUSE)

MR. STEVE SCARFONE: And now I'd like to move on to the investment part of the presentation. And the big part of investments in this year's General Rate Application is, of course, the corporate bond strategy. And that strategy is, first and foremost, about optimizing the investment to match existing claims liabilities. And a secondary benefit, of course, is the increased yield and the lower premiums.

It serves to reduce the initial rate indication by .8 percent, but comes with a number of what I've called conditions precedent before full imp -- implementation of the corporate bond strategy can -- can move ahead.

One (1), as we've heard, is ministerial approval. Second is the completion of an asset liability matching study. Third are the targets that Mr. Ghikas spoke to, the rate stabilization reserve targets.

And lastly, that there be no offset of actuarially accepted practice rates with the RSR investment income. And I'll touch upon, at the end of my investments submission, interest rate forecasting risk, and the compliance filing that's been proposed as part of this rate application.

The first condition precedent is Minister approval. The proposal of -- the corporate bond strategy proposes that the bond allocation increase from its current 3 percent to 18 percent by March 1st, 2018, and then also proposes the purchase of triple 'B' bonds, which we heard from Mr. Steski are not a permis -- permitted class of investments under the financial administer -- the -- the financial...

(BRIEF PAUSE)

THE CHAIRPERSON: I believe it's the Financial Administration Act.

MR. STEVE SCARFONE: Administra -- and that -- the -- so I've the acronym wrong. That's why it threw me, yes. The Financial Administration Act. Thank you, Mr. Chair.

It's not a permitted class of investments under that legislation. And so Minister approval would be required if the Corporation is to purchase its triple 'B' bonds as part of the allocation, the new allocation.

Now, on that point, we heard evidence from Mr. Steski that other non-permitted vet -- investments have been allowed in the past. Investments in infrastructure, and investments in real estate were allowed by the Minister's office. And we also heard evidence from Mr. Steski that the Minister of Finance supports the corporate bond strategy, and that the Assistant Deputy Minister Mr. Steski has full confidence in MPIC, and can -- and has some influence over the Minister's decision in that regard.

Mr. Steski testified on that last point at page 1,408 of the transcript, Diana, if you could bring that up for me, please.

At 1,408, at line 10, question was put to Mr. Steski:

"And so, sir, based on your earlier comments about the qualifications 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?"

His response to that question was, "Absolutely."

And the point here being, Mr. Chair, that we do expect Ministerial approval to be forthcoming, the first of the condition precedents for the -- for the corporate bond strategy.

The second condition precedent to the bond strategy is the completion of the asset liability management study. We heard evidence that compliance with PUB Order 162/'16 proved difficult, but that the Order was given. We need priority to allow completion of the ALM for the bond strategy and for the release of the Board Order expected in December of this year.

The evidence was that Mercer Canada was the successful vendor, and that Mercer is aware that MPIC is seeking an upper RSR target of $438 million. The evidence of Mr. Yien was that the ALM will be completed by November 30, 2017. Mr. Yien also indicated in his evidence that he would find it very unlikely if Mercer did not recommend the bond strategy go ahead.

The third condition precedent are the upper and lower targets that Mr. Ghikas spoke to for the reserve -- for the rate stabilization reserve. Before proceeding with the corporate bond strategy MPI requires sufficient capital due to the greater risk.

Mr. Steski acknowledged in his evidence that the purchase of these corporate bonds represents a greater risk to the Corporation in its current portfolio. In this regard MPIC, of course, requires the assistance of the Public Utilities Board. The targets are required to proceed with the bond strategy and allow Basic to achieve long-term financial strength.

And I want to bring you to one (1) further excerpt from the transcript at page 1339. It's a question asked of Mr. Yien on redirect about the conditions that are required to be in place for the corporate bond -- for the corporate bond strategy to proceed. And rather than make use of the three (3) pillars or the three (3) tenets of the prudent fiscal management presentation in the overview of the rate application, Mr. Yien instead chose to make an analogy to a tricycle in his own unique way. But equally as effective in my view.

The question to Mr. Yien was:

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

And you -- his response was, "Absolutely." At line 15:

"Going back to my opening remarks, the Board would like to run MPI as a leading insurance company. And, if I can use the analogy of a tricycle, there are three (3) components to build a strong, sound insurance company. The first is the appropriate rate stabilization range that it can operate under."

And he re-emphasized the word "range" because at any time when we have a target it generates rate shock in his view, because 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 guarantee what he called the shock. And so having that right range is appropriate.

The second component of his tricycle analogy is the investment income:

"There's been discussions already about the investment income itself as 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 the third is using the right, proper interest rates. Actuarial best estimates using the AAP, the actuarial accepted principles. In his view, those are the three (3) wheels, if you will, of a tricycle that the Board really believes in, the MPIC Board of Directors really believes in, in terms of having those conditions be there. So those are the conditions that the Corporation says are needed in order to proceed with the corporate bond strategy.

The final condition precedent, as made reference to in the passage just reviewed from Mr. Yien, has been no offset of AAP rates with the RSR investment income:

"Growing and replenishing total equity is essential to the strategy. And if RSR investment income is used to reduce rates, the RSR simply will grow. In fact, if the investment income from the RSR is used to reduce rates, we can expect the continued depletion of the rate stabilization reserve."

And the Board has seen that evidence in this proceeding in the answer to the undertaking that showed that $560 million been removed from the RSR in the past nine (9) years. That is a depletion of capital reserve. The chronic drawdown of the rate stabilization reserve does not provide the Board of Directors with the comfort it requires to go ahead with the bond strategy.

Riskier investments introduced greater volatility to capital reserves, meaning a greater bandwidth is required. And the evidence from the -- from the witness that was presented under subpoena by Board counsel was that the greater bandwidth is preferred over the narrow one (1) that he was suggesting. It means less likelihood of rebuilding fees, and it's less likely to -- that there will be rebates occurring a year or two (2) after a potential rebuilding fee. The shielded rate stabilization reserve investment income renders the bad years, if you will, more manageable and again reduces the risk of rebuilding fees.

We heard evidence from Mr. Steski about who bears responsibility for the investment portfolio of Manitoba Public Insurance. We say that MPIC and the Department of Finance jointly advise the Minister of Finance in that regard. But ultimately the Minister of Finance is responsible for the MPIC portfolio.

The evidence was, you'll recall, that while MPIC may be driving the bus, the government or Crown owns the bus and ultimately they own the investments that MPIC holds. So in that respect, we see the PUB has somewhat limited jurisdiction concerning the management of MPIC and its investment portfolio. Section 14 of the MPIC Act makes it clear that all MPI property, including money, investment money, is deemed to belong the Crown. And again, Mr. Steski's evidence confirm that.

On interest rate forecasting MPIC, of course, is proposing that it make use of the naive forecast for this year, and that -- that naive strategy or naive forecast involves a strategy or a model whereby interest rates today remain the same throughout the forecast period. The proposal is that MPI would update the Board with respect to the actual interest rate on or about November 30, 2017, and that from the ten (10) year Government of Canada rate, as published by Bloomberg.

With that compliance filing, MPIC proposes that it concurrently provide an explanation concerning how the updated interest rate might affect the overall indicated premium rate. This compliance filing, or as Mr. Ghikas called it, simply an undertaking to provide more information, allows the Board without question the most up-to-date information available for setting the premium rates and the overall rate indication.

It removes any uncertainty in interest rate fluctuation between now and November 30th. It serves to reduce any variability in those three (3) months and it's being provided in conjunction with AAP rate setting, which will minimize interest rate forecasting risk to the greatest extent possible.

Use of the naive forecast, MPIC says is preferred over the standard interest rate forecast for obvious reasons. SIRF performance has -- has been poor over the past several years, to the detriment of MPIC and its policyholders. And it's preferred over the SIRF as well because, under AAP rate-making there's a shorter outlook period. While forecast for breakeven rate making extended over two (2) years, if the compliance filing is accepted by this -- by this Board, it's limited to three (3) months. The Corporation says the naive forecast is the best estimate for rate setting purposes under AAP.

(BRIEF PAUSE)

MR. STEVE SCARFONE: These are the reasons that the Corporation is saying the bond strategy should be implemented. The assumption of the greater risk that the corporate bonds present is reasonable in all the circumstances. Approval by the Minister of Finance, we've heard, is expected. He supports the strategy. The strategy will assist in building sufficient capital reserves, the fundamental to application here this year.

The asset liability management study ensures that due diligence is in place before proceeding with the bond strategy, that the bond strategy requires the RSR lower and upper targets identified. It also requires that there be no offset of RSR investment income.

So that will be my submission before I move into loss prevention and road safety. Do we want, Mr. Chair, to take a five (5) minute break or do you want to plow through?

(BRIEF PAUSE)

THE CHAIRPERSON: Oh, I -- I think that everyone may -- may want to just proceed conclusion.

MR. STEVE SCARFONE: Very well. Thank you.

(BRIEF PAUSE)

MR. STEVE SCARFONE: Moving on to loss prevention and road safety. I see My Friend Mr. Oakes has joined us and Mr. Monnin. MPI is of the view that it's one (1) player in a much larger construct when it comes to road safety in Manitoba. But all stakeholders are working together toward a common vision of zero fatal -- zero fatalities and serious injuries using a safe systems approach. The provincial road safety committee, of which MPIC is a co-chair, will work to achieve these objectives. And the Corporation has formalized its loss prevention strategy and framework that guides all of its loss prevention efforts.

We heard evidence that MPI remains focused to address the IBM observations, particularly in the last year. MPI has developed the data dashboard for each of the programs in the loss prevention portfolio, which allow for base lining against the effectiveness of the programs and how they're measured. The dashboard data provides new insight for program managers into how existing programs can be adjusted and new programs developed. And the dashboards are expected to be completed this year. An overall scorecard to measure return on investment will be developed thereafter.

We heard evidence from Mr. Keith that MPIC has formalized its loss prevention and road safety activities into a three (3) year operational plan, and the second iteration of that was filed with the Board this year. It includes formal frameworks for priority setting, research, program development, and program evaluation. And these frameworks, the road safety committee, the loss prevention strategy, the dashboard, and the operational plan should, in our view, provide the PUB, the PUB, with assurance that the investments made by MPIC in road safety are appropriate, evidence-based, and in keeping with best practices.

MPIC intends to leverage these frameworks to identify road safety priorities, programs, and initiatives it should be pursuing. And funding for these programs, we've heard, will be subject to the rigours of MPI's internal value management process, thereby assuring the value of the money spent on these programs, even where not possible to draw direct correlations between investment and reductions in claims and costs.

And that -- that, in my view, is an important point because it's difficult to measure the investments made in road safety and loss prevention. The -- the Board has heard that, as I understand it, in the past. Mr. Keith, under cross-examination, somewhat of an easy target, not in any way because he's not informed and a knowledgeable witness, but rather given the subject matter of -- of his area. And that is, it's difficult to quantify the benefits that these programs provide. So that's something that the Corporation intends to try and address by subjecting these programs to the value management process.

And on that loss prevention road safety issue, it's -- a number of questions were put to Mr. Keith about the effectiveness of the messaging. Again, it's difficult for the Corporation to measure these. People will continue to get into accidents. The messaging, we hope, is -- is being heard to reduce these collisions, but they happen nonetheless, and form part of a large part of what the legal department does in terms of answering defence claims in bringing subrogated actions for -- for negligence actions. Accidents are essentially negligence actions.

The loss prevention road safety program involves input from other road safety stakeholders through the external stakeholder committee on loss prevention. The committee meets regularly and include representation from all stakeholders that have been part of this proceeding. The Corporation encourages continued stakeholder participation, and the objective is for MPI to continue its regular and ongoing discussion outside of the rate approval process.

Road safety, in MPI's view, is a year-round issue and MPIC is open to considering new initiatives that are cost-effective and fall within the Corporation's mandate. All such suggestions will be considered through established road safety frameworks identified earlier.

(BRIEF PAUSE)

MR. STEVE SCARFONE: And those are my comments with respect to those four (4) areas, Mr. Chair. Mr. Ghikas has a few closing, concluding remarks, subject any questions that the panel has.

THE CHAIRPERSON: Mr. Ghikas.

MR. MATTHEW GHIKAS: Thank you, Mr. Chairman. I've been tasked with wrapping things up, and I want to take us back to the thought that I started with, which was the mandate letter and the two (2) driving themes of that mandate letter which were prudent fiscal management and transparency.

And this slide deals with the former. And really, it is the key point, being that the prudent fiscal management is served by what MPI is seeking in this application and the 1.95 percent rate increase, based on the September 30th interest rates reflects the expected costs of policies written in 2018 and 2019, the focus being on accepted actuarial practice with a zero profit provision.

The upper and lower RSR levels should, in my submission, be approved as reflecting a reasonable level of capitalization and sufficient bandwidth to promote rate stability. They are reasonable in the context of MPI, and also reasonable in the context of a comparison to other insurers in Canada.

The third point being that retaining income on total equity will help offset the natural declines in the MCT due to business growth. And by that I mean it will replenish -- it will provide a natural means of replenishing some of the capital in -- in Basic and provide a mechanism where one (1) would not otherwise exist; that the DSR is a logical step to promoting safe driving. That also happens to have a significant benefit in terms of the rate indication and helping make -- make premiums more reflective of risks that -- that drivers are opposing on the system.

And the final bullet that updating the interest rate forecast using the naive interest rate forecast, first of all, which I -- I did want to note that MPI's appointed actuary, Joe Cheng, has endorsed in the DCAT report. And that's in evidence, and it's referred to and discussed in the written submissions, but that approach has -- has been endorsed by the appointed actuary as well as the chief actuary, Mr. Johnston.

Using the naive forecast and updating it as of November 30th is -- is a fair approach, and it will reduce interest rate risks. And on that point, Mr. Chairman, just mechanically my proposal would be to reserve a -- an exhibit number for that filing which the commi -- or the -- the Board can then determine in its final order whether or not it wants to have regard to it or not, based on its consideration of what the most appropriate approach is. I can let you think about that and I can deal with that tomorrow if need be, further, but that -- that would be my proposal.

THE CHAIRPERSON: I may have some questions about that after you finish, Mr. Ghikas.

MR. MATTHEW GHIKAS: Thank you. The next slide, looking towards the next GRA, really touches on the -- on the issue of, you know, transparency and the role of -- of this process in driving that forward. You've -- you've heard me say that there are complementary roles for the -- MPI's Board of Directors and this Public Utilities Board. And in my submission, that is very true.

And I -- I have been instructed by the Board of Directors to convey that they do see these roles as complementary. They do value the input of the Public Utilities Board in driving continuous improvement at MPI. And there's tangible examples of that, and I mention the drive towards accepted actuarial practice. That is something that the Board has been pushing for and is a good change and one (1) of the things that will make the -- the company better.

There are areas where MPI realizes that it can do better. And one (1) of the issues -- I put the example in there because I think -- I think it actually brings home the point that -- of my submission, and this is the issue of IT projects. With -- with IT projects, MPI recognizes there's been a lot of good work in the IT, and Mr. Scarfone took you through it about the approved value management process, a lot of the improved documentation and the value of documenting it formally and the transparency that that brings.

But MPI recognizes it hasn't done a good enough job conveying that in these proceedings. And one (1) of the issues that would become apparent last week is that there were areas where, when a deep dive was done in particular projects that there were times when the witness in the front row had to consult with -- with support in the back row on these things. And that's something that, you know, MPI wants to give more thought and discussion to with -- with the stakeholders involved in this proceeding.

One (1) thing that, coming from the outside and coming in, that I've noticed is that traditionally the model in these proceedings is one (1) that very much looks like some -- something akin to in estimates type -- what you'd see where there's an executive answering questions with the back row providing support. And that has been the model here in the past, and it is one (1) of the things that MPI wants to -- to talk about, is whether there's going to be opportunities to bring more of the people in the back row forward.

And in the current -- in the case of the IT projects this year the difficulty that we had is that MPI looks at that pie chart and sets out its plans for the proceeding based on that pie chart. And when something like IT comes along, and you see the -- it's an important -- I'm not trying to belittle it. It's important that you put focus on it and you go through these things.

But part of the -- the issue is that when you look at the pie chart from MPI's perspective that, you know, sitting a number of witnesses on IT up here wasn't -- wasn't what MPI was envisaging would be a focus of the proceeding. And -- and by the time it came to discussing bringing forward that it became apparent to MPI that there would be a deep dive on some of these projects. It was -- it was relatively late in the day.

And so what -- what MPI would like to do, and involve everyone in, is to have -- to give some consideration as to whether or not the, you know, there's room if there's going to be deeper dives in certain areas that those be articulated in advance so that the people can -- that we can make sure we have the right people forward to deal with those particular things early in advance.

And, of course, there's a flip side to that as well, which is, you know, we already have hearings that are much longer than any other utility that I've worked for and that I've experienced in any of the jurisdictions I work in. And having an annual hearing, if it's already three (3) weeks long, is -- is long. And there's a value to that and I'm not trying to take away from that.

But to the extent that you're going to be bringing more people forward for deeper dives in particular areas, you're setting yourself up for a very long hearing unless you are able to refine the scope of the hearing. And so my -- my submission and MPI's submission would be that the two (2) considerations have to go hand-in-hand, and -- and some informal discussion early next year would be useful in that regard to try to brainstorm ideas.

And I know MPI has submitted a letter in the past, I believe it was in June, to discuss issues like this to Mr. -- to the Board Secretary, Mr. Crystal and -- and the other parties. And some of those ideas are laid out there. But having those discussions early in the process and -- and having some real direction and scoping orders relating to the proceeding sufficiently in advance would -- would be of assistance.

And -- and you -- you get that type of thing in other jurisdictions where the -- the Board itself is opining on what it wants to hear and see, not necessarily at the outset of the process, but certainly -- certainly, you know, a couple of months beforehand or -- or so, so that, you know, there's a real focus of the parties on particular areas and you don't necessarily focus at the same depth on every issue, every year.

So with that said, it's really just to emphasize the Board of Directors' commitment to work to a better process in these things and -- and express that there -- that MPI recognizes the value of this. But also, you know, really wants to make sure that it's -- that these issues are considered within a framework that recognizes that, you know, in being involved in a process like this for one (1) month every year is a significant investment in terms of corporate resources as well institutional resources. I mean, rather than dollars, but it's a significant investment as well. And it's best to focus those attentions as -- as carefully as possible.

So those are my submissions in that regard. And subject to the questions you indicated you had, I'm happy to take questions. And I know Mr. Scarfone is too.

THE CHAIRPERSON: Sure. Any questions from the panel? Okay. So let's go through this -- the proposal for the filing, the -- the compliance filing. When does -- when does MPI need the rate to put into their computer?

(BRIEF PAUSE)

MR. MATTHEW GHIKAS: I'm advised mid-December.

THE CHAIRPERSON: Okay. We've always gone on the basis -- my understanding from last year was it was December 1st. So the day before you need a rate we're going to get a compliance filing from you and have to issue a decision. Here's the concern I have and it is a purely legal decision.

Our statutory authority and mandate is to set rates. If we're setting out a process effectively in an order based -- waiting for your compliance filing, do we not face an argument that, de facto, you're setting the rate rather than the Board setting the rate?

MR. MATTHEW GHIKAS: I -- I mean, in my submission, I -- no is my -- my answer to that. I understand why -- why you're -- you're asking the question. I -- I think, first of all, dealing with the date. My -- my instructions are that -- that MPI can make it work if -- if by mid-December we have an Order.

The -- the -- in terms of the -- in terms of the fairness argument, the -- the input that's being updated is, as I -- as I indicated before, is -- is no different than the one (1) that has already been updated, right? And it's -- it's the simple -- it flows through what has already been examined by the PUB. It's a number, an input in the number, and it has implications in terms of spitting out a different number. But it is a member and a process that -- that parties have -- have canvassed here.

THE CHAIRPERSON: I guess, Mr. Ghikas, if -- if they answer of MPI is that they only need a rate by mid-December, that's different than what I had understood. So my question was going based on my previous understanding that they needed a number the next day.

MR. MATTHEW GHIKAS: That wouldn't be workable.

THE CHAIRPERSON: That -- that's right.

MR. MATTHEW GHIKAS: I agree with you there.

THE CHAIRPERSON: Secondly, if -- and I would just indicate to everybody, I mean, the panel has not -- has not met to look at a decision and will not move into decision making mode until all the submissions are completed and the hearing is concluded.

So I'm not suggesting we're going this way, but I just want to test it. If you're -- if you are doing this compliance filing as an exhibit do the Intervenors get the compliance filing as well and have an opportunity to at least provide a submission prior to the Board accepting that in evidence as part of its decision-making process?

Because as I understand it what you're saying is it's a simple document. It's a number. We're just going to give it -- we'll give it to the Board, the Board will make a decision based on it. And I'm trying to understand how, after going through -- which I agree is a lengthy hearing, where the Intervenors have received everything and have a position, that seems to be one (1) part that's not involved in the process.

MR. MATTHEW GHIKAS: Well, they -- what I would say in response to that, Mr. Chairman, is that the sensitivities with respect to the impact of interest rates are filed already. So we do know what the mathematical implications of a changing interest rate forecast are. And the number, you know, you can go on to Bloomberg on any given day and see what that number is for that day. And what MPI would effectively be doing is taking the number on November 30th and re-running the numbers and giving you what the results are.

The -- the difficulty I have with the argument that we need a -- that Intervenors would need an opportunity to comment on it, is that -- that would suggest that their submissions would be different depending on whether the number went up or down. And my submission to you is that we should be looking at the mechanic -- is this forecasting methodology an appropriate one (1)? We've all had an opportunity, a fair opportunity, to comment on whether the methodology is correct.

If -- if My Friends would be arguing that they now don't like a methodology because the number doesn't get them to the place where they wanted, my submission would be that that's not a legitimate submission to be making; that if you're content to deal with the -- that the methodology -- you accept the methodology and the results flow from the methodology that's reasonable. Once everybody's commented on whether the methodology is reasonable, the mathematical output of that doesn't require submissions depending on whether the number went up or down. That's my submission to you.

THE CHAIRPERSON: Okay. Thank you for that. The second question, I guess -- no, I'll just let you finish if you --

MR. MATTHEW GHIKAS: All right. Thanks. Yeah.

(BRIEF PAUSE)

MR. MATTHEW GHIKAS: My -- Mr. Crozier was -- was saying to me that the two (2) -- the reason he -- that he wanted to make sure that you understood that the reason we had said December 1st in the past was that December 1st is the day that MPI likes to have it done because getting it later than that does put some institutional pressures on to get it out. So the -- so wanted to want to make that clear. But they -- they are prepared to live with December 15th to make this work.

But the other point that Mr. Crozier was making to me is that, you know, MPI picked November 30th as a date to try to maxim -- minimize the interest rate risk. But there's no magic to the 30th. And so you it would really --

THE CHAIRPERSON: Yes, I understand

that you can pull a --

MR. MATTHEW GHIKAS: Yes. Yeah.

THE CHAIRPERSON: -- you can pull -- pull it any hour of any day.

MR. MATTHEW GHIKAS: Exactly.

THE CHAIRPERSON: Yeah.

MR. MATTHEW GHIKAS: Exactly.

THE CHAIRPERSON: Okay.

MR. MATTHEW GHIKAS: Yeah.

THE CHAIRPERSON: The second question, Mr. Ghikas, if -- if MPI receives an order -- and again, this is purely hypothetical, but receives an Order that provides the -- the DCAT at the low end as requested in the MCT, and all of the things you've requested, so that you become self-sufficient on Basic and you don't have to draw on Extension at any point, what happens with the Extension reserve?

Because I would assume that it would just keep going up year after year. What happens to the -- what happens to the fund? What -- what are the funds used in the extension reserve -- what are they used for?

(BRIEF PAUSE)

MR. MATTHEW GHIKAS: So the -- so, Mr. Chairman, the -- the funds in the optional reserves are the -- are owned by the government, and they're -- I'll have to get -- if you -- if we break for a few minutes, I can get you the answer or I can provide you an answer tomorrow.

But the -- they are owned by the government and the government has the ability to determine what to do with those funds. But the -- the just -- just like any private insurer, the pricing of the product takes into account all sorts of things. So it -- I don't know whether it's necessarily the case that it's going to go up ad infinitum. And that would be within the Board's mandate. And --

THE CHAIRPERSON: Okay. If you could get the answer tomorrow would be just fine.

MR. MATTHEW GHIKAS: Thank you.

THE CHAIRPERSON: And if you do, could you ask whomever you're going to ask if the government has ever pulled money out of MPI's reserve funds.

MR. MATTHEW GHIKAS: I will do that.

THE CHAIRPERSON: Thank you.

MR. MATTHEW GHIKAS: Thank you.

THE CHAIRPERSON: Those are my questions. I guess I have a question for counsel for tomorrow. What order are we going in tomorrow?

MS. KATHLEEN MCCANDLESS: I believe we're starting with Mr. Oakes and then Mr. Williams, followed by Mr. Monnin.

THE CHAIRPERSON: Okay. I'm just -- and with that discussion with coun -- I -- I was just wondering if Mr. Williams was going second or third tomorrow.

MS. KATHLEEN MCCANDLESS: I believe that Mr. Oakes and Mr. Williams had a discussion off-line about having Mr. Oakes go first.

THE CHAIRPERSON: I have no prob -- I understand strokes going first. I guess my question is whether Mr. Monnin should be going second and Mr. Williams third. I -- I mean, unless -- I -- I'm just wondering, Mr. Monnin is going to be sitting here for -- I -- I assume that Mr. Monnin's submission won't be as long as Mr. Williams.

MR. MATTHEW GHIKAS: You aren't suggesting Mr. Williams is long-winded, are you?

MS. KATHLEEN MCCANDLESS: Mr. Monnin was here and he --

THE CHAIRPERSON: We can con -- we can compare --

MR. MATTHEW GHIKAS: That's the pot

calling the kettle black.

THE CHAIRPERSON: -- the number of screens of -- of them to -- to MPI's, but certainly his -- his -- the scope of his inquiry was -- is longer than...

MS. KATHLEEN MCCANDLESS: I can raise that with counsel for the Intervenors.

THE CHAIRPERSON: Yeah, that's -- that's fine either way. And then I guess we will see tomorrow weather we're having reply after -- after the hearing.

MR. MATTHEW GHIKAS: Yeah. I -- I can assure you in -- in that regard. And Mr. Scarfone and I recognize the proper purpose of reply.

THE CHAIRPERSON: Yes.

MR. MATTHEW GHIKAS: We're anticipating that we -- and we're proceeding on the assumption that we will be able to address things tomorrow. We would very much like to do that for everyone's benefit. And -- and I believe that we will be able to do that. If something comes up where we should -- we need more time, we're hoping that the more time we need is measured in -- in an hour rather than a day. So our intention is to get everybody out of here.

THE CHAIRPERSON: That would be most appreciate. Thank you. So we'll adjourn until nine o'clock tomorrow morning. Thank you.

--- Upon adjourning at 12:46 p.m.

Certified Correct,

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Cheryl Lavigne, Ms.