COMMENTARY **ICBC**

A CLOSER LOOK AT ICBC'S FORECAST LOSS FOR 2022/23

Recently ICBC released its financial forecast for the current fiscal year ending 31 March 2023, together with the actual results for the first nine months to 31 December 2022.[1] The service plan shows a significant increase in forecast claims costs, and a sharp reduction in investment income compared to the budget. The forecasted operating loss of $298 million compares to a budgeted income of $327 million, while the equity is forecast at $3.28 billion, a decrease of some $ 854 million from the prior year adjusted budget. The Minimum Capital Test (MCT) ratio is expected to decrease to approximately 90% compared to the 110% achieved in the prior year.

Unfortunately, ICBC does not provide separate forecasts for the Basic and Optional insurance programs in its service plan document, nor the MCT measure of financial health. The third quarter (Q3) report does separate the Basic and Optional programs, as does the year-end annual report to some degree.

HIGHLIGHTS

A significant decrease in investment income and higher claims costs are the key reasons for the operating loss forecast for the current year. Rising interest rates and poor equity performance significantly lowered investment income and triggered an impairment loss.

For the 23-month period from May 2021 to March 2023, ICBC retained the equivalent of 11.5% of the combined premium to rebuild its capital reserve (as measured by the MCT ratio), but the increase in the forecasted claims costs and the steep decline in investment income negated the capital build.

Net Premiums Earned

As shown in Table 1, the forecast for net premiums earned is only $25 million (0.5%) higher than the budget. There was no general premium increase for the current year, and ICBC did not provide data on the planned and actual policies sold nor explain the increase in revenue.

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[1] The year-end forecast is included in the three-year service plan, see https://www.icbc.com/about-icbc/company-info/Documents/service-plan-2023-2026.pdf For the Q3 summary see https://www.icbc.com/about-icbc/company-info/Documents/StmtofOperations-Dec22.pdf

TABLE 1—NET PREMIUMS EARNED ($=million)

	A2021/22	B2022/23	F2022/23	Change	%
Premiums Earned	5,180	5,253	5,278	25	0.5
Basic Capital Rebate	396	--	--	--	
Net Premiums Earned	4,784	5,253	--	--	

Source: Service plans 2022/23 and 2023/24, and the 2021/22 annual report p. 18.

The forecast for the 12-month fiscal year appears reasonable when compared to the actual results for the third quarter.

Cost of Claims

ICBC forecasts that the cost of current year claims will be $449 million lower than the budget, while a surprising increase of $531 million in the forecast of prior years claims to the budget resulted in a net increase in claims costs. The forecast of total claims costs is $1.6 billion higher than the total for last year.

ICBC did not explain the higher forecast, nor provide any data on the number of claims filed or the average cost per claim.

TABLE 2—CLAIMS COSTS ($=million)

	A2021/22	B2022/23	F2022/23	Change	%
Current Year	2,922	4,129	3,680	(449)	(10.9)
Prior Years Adjust.	(430)	(107)	424	531	
Total	2,492	4,022	4,104	82	2.0

Source: Service plans 2022/23 and 2023/24, and the 2021/22 annual report p. 18.

The current year forecast for the 12-month fiscal year appears reasonable in light of the actuals for the first nine months. The large increase in the adjustment for prior years claims does not appear reasonable given the large decreases recorded during the last two years,[2] and the minor reduction reported for the first nine months of the year. The Q3 report shows the combined adjustment of prior years claims at negative $34 million, while the year-end forecast suggests a $460 million swing in only three months.

In light of the significant increase in interest rates during the current year, which result in an increase in the discount rate, one would expect to see a reduction in the provision for unpaid claims. In its 2021/22 annual report ICBC stated; "Overall, 2021/22 net claims-incurred costs of $2,492 million were $849 million lower than the claims costs incurred in 2020/21. The major contributing factors were **the increase in discount rate** [my emphasis] and a reduction in the amount reserved for future claims handling

[2] In 2020/22 there was a negative $367 million negative adjustment, while for 2021/22 the negative adjustment was $430 million.

costs…Prior years' claims adjustments were better than budgeted mainly due to **a higher discount rate** [my emphasis] and lower-than-expected bodily injury claims severities."[3]

Investment Income

ICBC forecasts that the net investment income will be $645 less than the budget. The service plan did not provide any analysis or discussion to explain the significant impairment loss for 2022/23. ICBC did note that "the 2022/23 investment income outlook is lower than originally planned primarily due to expected impairments from the bond and equity funds, realized losses on bonds, and lower than planned equity distributions."[4]

TABLE 3—INVESTMENT INCOME ($=million)

	A2021/22	B2022/23	F2021/22	Change	%
Investment Income	1,418	623	409	(214)	(34.3)
Impairment Loss	(6)	0	(431)	(431)	
Net Invest. Income	1,412	623	(22)	(645)	

Source: Service plans 2022/23 and 2023/24, and the 2021/22 annual report.

Is the impairment loss a realistic estimate? Certainly, the investment portfolio of bonds and equities has lost value compared to the prior year, but the Q3 report showed an impairment loss of only $62 million as of 31 December 2022, compared to the $431 forecast for 31 March 2023. Is ICBC forecasting a severe decline in financial markets?

Net Income and Equity

The forecast net income of ($298) million shows a $625 million swing from the budget level. This is due to a reduction of $645 million in investment income and a $424 million increase in the adjustment of prior years claims costs. These negative adjustments were partly offset by a $449 decline in current year claims costs compared to the budget.

TABLE 4—NET INCOME AND EQUITY ($=million)

	A2021/22	B2022/23	F2022/23	Change	%
Net Income	2,217	327	(298)	(625)	
Equity*	3,715	4,528	3,278	(1,250)	(20.7)
Estimated MCT %	99	e120	e90	e(30)	(18.1)

[3] https://www.icbc.com/about-icbc/company-info/Documents/ar-22.pdf p. 21.
[4] https://www.icbc.com/about-icbc/company-info/Documents/service-plan-2023-2026.pdf p. 27.

Note * The 2022/23 service plan equity has been lowered by $396 million to reflect the capital rebate that was announced after the forecast was published.

Source: Service plans 2022/23 and 2023/24 and the 2021/22 annual report.

ICBC states that the MCT ratio is an important industry measurement used to assess required capital levels.[5] Unfortunately, it no longer reports the MCT ratio in its annual service plan.

A PROGRAM PERSPECTIVE

As noted earlier, ICBC does not provide its year-end financial forecasts by program. The purchase of Basic automobile insurance from ICBC is compulsory, while the purchase of additional coverage through the Optional program is not. This distinction should be sufficient justification to require ICBC to separate its service plan forecasts, as it does in the quarterly and annual reports.

A reviewer can develop some general understanding of the program forecasts by analyzing ICBC's minimalist third quarter financial report.[6] As of 31 December 2022, ICBC reported net income of only $189 million, a decrease over the same period of the prior year. Basic net income was $279 million, while Optional program reported a net loss of $90 million.

In terms of the capital reserve, the Basic MCT ratio declined to 90% from 92%, while the Optional dropped from 115% to 96%.

It would be useful to explore these changes in claims costs to measure performance of our Crown auto insurer, but ICBC does not provide any service measures (number of policies sold or claims filed) or performance measures (frequency of severity of claims) in its service plan, or in its annual reports.

 https://www.bcpolicyperspectives.com/

The writer is a retired senior BC government public servant whose paper describing the BC government's manipulation of the finances of BC Hydro from 2008 to 2014 was published by *BC Studies* in November 2016. *BC Studies* published his paper on the 40-year financial history of ICBC in 2013. He is an intervener in the BC Utilities Commission's reviews of ICBC's and BC Hydro's rate requests.

[5] See the Q3 report https://www.icbc.com/about-icbc/newsroom/Documents/StmtofOps-Dec2021.pdf
[6] ICBC provides a high level discussion, a one page operating summary and a one page financial position. BC Hydro provides far more detailed quarterly reports, as does the Manitoba Crown auto insurer.