COMMENTARY **ICBC**

ICBC REPORT PRESENTS DISTORTED PICTURE OF THE FINANCIAL IMPACT OF COVID-19

On 14 May 2020, minister responsible David Eby announced that ICBC's poor financial condition did not permit a premium rebate to reflect a dramatic decline in claims costs resulting from efforts to contain the COVID-19 virus. The poor state of the public auto insurer finances ("no financial buffer") and the uncertainty of the financial markets convinced the government that it was too soon agree to a rebate.[1]

A report prepared by ICBC on the financial impacts of the COVID-19 pandemic was released to bolster the decision to not provide a rebate.[2] Unfortunately, the report presented a distorted picture and appeared to show the worst-case scenario. The report used selective and unverifiable information to muddy the waters, resulting in enhanced confusion rather than clarity.

Key Points

ICBC's report used actual claims and premium revenue for the period from March 15 to May 2, 2020. ICBC said that during these seven weeks (49 days) the number of new claims dropped by 46% compared to the same period last year, with a reduction in claims cost of approximately $158 million.[3]

In the same period ICBC provided various policy sales statistics and asserted that premium revenue had declined by a surprising $283 million.[4]

The corporation also referenced a significant decline in its equity investments as of 31 March 2020, which was the end of its fiscal year. It noted that if the financial markets do not recover the loss could affect ICBC's current year position by more than $1.0 billion. The decline in the discount rate, which increased the cost of the unpaid claim liability, was also mentioned as a possible cost pressure for the current year.[5]

All in all, the report presents a case that ICBC cannot afford a rebate.

[1] No reference was made to the BC Utilities Commission, which has the statutory authority over Basic insurance, in the government's media statement; https://news.gov.bc.ca/releases/2020AG0035-000880
[2] https://www.icbc.com/about-icbc/newsroom/Documents/COVID19-impacts-report-May2020.pdf
[3] Ibid. p. 5.
[4] Ibid. p. 4.
[5] Ibid. p. 6.

But a closer examination results in many questions. Unfortunately, this report conforms to ICBC's normal practice of providing selective information without proper analysis or explanation to justify a position.

ISSUES

No Separation by Fiscal Year

By using data from March 15 to May 2 as the reporting period ICBC mixed the expenditure saving and revenue loss between two fiscal years. The books for last year closed on 31 March 2020, therefore any gains or losses to the bottom line resulting from the response to the pandemic for the 17 days in March affect the prior year. Any possible premium rebate should be calculated on the revenue and expenditures forecast for the current year.

ICBC states that the 2019/20 year-end capital reserve equity was substantially reduced due to the drop in the market value of its investment portfolio. The report did not give a specific value to the loss, nor did it note that a significant amount of the loss in the value of the equity portfolio has been regained in April.

No Forecast Provided

ICBC has a track record of not providing detailed financial forecasts, and when it does (such as the annual service plan) it is often wrong. The current report is no exception. A proper analysis would have been based on the actual results for April and a forecast for the first quarter.[6] A longer term forecast would probably have presented a different picture, where claims savings would be much higher and premium losses would only be slightly higher.

It is logical that policyholders who chose to cancel their insurance (or switch from business to the less expensive pleasure use) will do so early in the period, while the savings from fewer claims will occur over a longer timeframe (probably to a lessening degree in future weeks or months).

We do not know how many of the increase in policy cancellations or downgrades occurred in 2019/20 compared to the current year. Nor do we have the benefit of ICBC's forecast of the future monthly claim savings to present a more complete picture.

[6] See for example my paper of May 7,2020; http://www.bcpolicyperspectives.com/media/attachments/view/doc/commentary_covid_19_and_icbc_savings_7_may_2020_2/pdf/commentary_covid_19_and_icbc_savings_7_may_2020_2.pdf

Claims Savings Appear Understated

ICBC says that new injury and vehicle damage claims for the seven weeks presented were down by 46 % compared to the same period last year. It said that the average number per week was down by 7,200, or about 50,400 in total, with a reduction of $158 million in claims costs.

A simple division shows that the average cost per claim not incurred was $3,135. Yet this is far less that the average for 2017/18 (2018/19 not available) of approximately $16,000 per Basic claim. From information provided during the BC Utilities Commission's review of the 2019 Basic rate request, ICBC reported that the average cost to settle Basic injury claim was $41,810, while the average cost of a vehicle damage claim was $4,015.[7] The apparent drop in the average claim cost between mid-March and May 2nd is not credible.

An additional test of the veracity of the reported savings involves the 18 February 2020, service plan financial forecast for 2020/21. If the 46% reduction in claims was applied to seven weeks of ICBC's current year claims cost forecast the savings would total approximately $340 million, not the $158 million claimed by ICBC.[8]

Either the 46% reduction in claims is too high, or the average claim cost saving is too low. Yet the percentage reduction seems reasonable because the Manitoba public insurer reported a 48% reduction in collisions as of mid-April.[9] If a conservative average claim cost of $12,000 was used the total savings would have been about $600 million

The Reported Premium Revenue Loss Is the Worst Case

In addition to the apparent understating the savings in the cost of claims, the report appears to overstate the loss of premium revenue. ICBC stated that premium revenue had declined by $283 million "compared to what would normally be received" during the seven-week period.[10]

The $283 million loss equates to about $40 million/week for the seven weeks reviewed in the report. The 2020/21 budget forecast net premiums earned of $6.66 billion, or about $128 million/week. The declared loss of $40 million/week is 31% of the budget; did premium revenue really drop by 31%?

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7 http://www.bcpolicyperspectives.com/media/attachments/view/doc/occasional_paper_no_68_icbc_stats_18_june_2019_2/pdf/occasional_paper_no_68_icbc_stats_18_june_2019_2.pdf Table 3.5.

8 The 2020/21 forecast was $5.4 billion, or $104 million/week X 7 weeks X.46 = $334.9 million.

9 https://steinbachonline.com/local/mpi-to-issue-rebate-cheques-help-offset-covid-19-impact The Manitoba public insurer is providing a significant rebate.

10 https://www.icbc.com/about-icbc/newsroom/Documents/COVID19-impacts-report-May2020.pdf p. 4.

ICBC did not provide any detail to explain its estimate. One must infer the reasons from a series of statistics provided for the seven-week period.

ICBC says that there were 103,712 cancellations in the period, some 53% (or 36,700 more in the same period in 2019).[11] Using an average premium of $2,000 per policy[12] the additional loss from cancellations would be $73.4 million. But his must be reduced to reflect the fact that few, if any, of the cancelled policies would be for the 12-month coverage period. Assuming an average of half of the 12-month coverage remained when the policy was cancelled, the savings would be $36.7 million. ICBC did not provide a specific amount for the lost revenue due to cancellations.

ICBC then stated that there were about 31,200 changes from business to pleasure use, although the marginal change number was not provided. Assuming an average $400 savings per policy, this results in a loss of 12.4 million. Again, assuming 50% of the coverage period remained when the change occurred, the savings would have been $6.2 million.

ICBC also stated that policy renewals in the period were 12% less, or 78,600 non-renewals (576,108 X .88 X 100 – 576,108 = 78,600) than for the same period last year.[13] The apparent loss for non-renewals is approximately $157 million (78,600 X $2,000), if ICBC had not budgeted for some or all of this loss for 2020/21. We do not know because ICBC did not provide an actual to budget comparison.

If true, the 12% drop in renewals for the seven weeks should be cause for serious concern to senior management and the government. As usual, ICBC did not provide any analysis or explanation for this major decline in renewals.

The total revenue loss for the three examples in this analysis is approximately $202 million. The $283 million revenue loss claimed by ICBC cannot be verified from the information provided. It appears to be a worst-case scenario because ICBC did not forecast how many of the cancelled or modified policies will be reinstated in the next weeks or month as the restrictions on movement and gatherings are loosened. This is a glaring fault with the report and results in a distorted picture of the COVID-19 impact on ICBC's finances.

Did the Pandemic Push ICBC into Insolvency?

The report stated that:

> As a result of the unprecedented downturn in equity markets, the market values of ICBC's equity investments significantly declined at the March 31, 2020 year-

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[11] ICBC did not explain why 67,000 policies were cancelled in the same period in 2019; this seems to be a significant number of cancellations.

[12] ICBC does not report on its average combined Basic and Optional premium, but in the background material released on 6 February 2019 to support the new enhanced care (no-fault) liability scheme the $2,000 figure was used.

[13] ICBC said there were 576,108 policy renewals in the period, therefore a 12% increase would be

> end which will negatively impact the company's fiscal 2019/20 financial results. The pandemic uncertainty also presents an evolving risk to fiscal 2020/21 if the market value of ICBC's equity investments do not recover. This negative impact on ICBC's results could exceed $1 billion in fiscal 2020/21 depending on the length and scope of the global market downturn.[14]

A $1.0 billion loss ("negative impact") is a scary number. Is a loss of this magnitude possible, or likely? Unfortunately, ICBC did not provide any detail about its investment portfolio, or its forecast 2019/20 year-end equity position.

By 31 December 2019, ICBC reported practically no equity.[15] It is likely that the drop in interest rates, and the March meltdown in the equity markets, caused by the response to the pandemic resulted in ICBC's year-end liabilities exceeding its assets. The ICBC report should have discussed this in more detail, as the poor financial condition of our public insurer was the primary reason advanced for not providing a premium rebate.

The report did note that the lower interest rates reduced the discount rate on the unpaid claims, which increased the claim liabilities in 2019/20. No amount was presented. In its latest service plan ICBC stated that a 1% decline in the discount rate adds about $400 million to the unpaid claims liability.[16] The report did not mention that this additional claim liability cost is offset by an increase in the market value of the fixed income (bond) assets. The equity assets, however, suffered a major drop in value in March, which may have reduced the value of these investments by about $1.0 billion by 31 March 2020. But again, the report is silent about the rebound in the equity markets in April.

The report also mentions that the planned amendments to the Evidence Act were not enacted by the end of the last fiscal year. As a result, the planned savings of approximately $400 million to the unpaid claims liability were not realized, which further exacerbated ICBC's insolvent position as of 31 March 2020.[17]

Enhancing Trust in ICBC?

Transparency is the basis of trust. Recently, Premier John Horgan and Attorney General David Eby admitted that the public lacks trust in ICBC.[18]

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[14] https://www.icbc.com/about-icbc/newsroom/Documents/COVID19-impacts-report-May2020.pdf p. 5.

[15] The equity was only $168 million; https://www.icbc.com/about-icbc/newsroom/Documents/Q3-stmt-of-ops.pdf

[16] ICBC 2020/21 to 2022/23 service plan; https://www.icbc.com/about-icbc/company-info/Documents/service-plan-2020-2023.pdf p. 19.

[17] For background see; http://www.bcpolicyperspectives.com/media/attachments/view/doc/commentary_icbc_400_million_27_october_2019/pdf/commentary_icbc_400_million_27_october_2019.pdf

[18] http://www.bcpolicyperspectives.com/media/attachments/view/doc/commentary_public_trust_30_jan_2020_3/pdf/commentary_public_trust_30_jan_2020_3.pdf p. 1.

It is unfortunate that the attorney general allowed the COVID-19 document to be released in an effort to justify the decision to not provide policyholders with a premium rebate. It would have been sufficient to provide a summary of the 2019/20 capital reserve (or negative equity) to justify the no rebate decision. Instead, by releasing what appears to be a distorted worst-case financial report the public's trust in the corporation has been further eroded.

 http://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 has been an intervener in the BC Utilities Commission's recent reviews of both ICBC's and BC Hydro's rate requests.