Mr. Nicolas Jimenez March 19, 2018

Interim President and CEO,
Insurance Corporation of British Columbia

Dear Mr. Jimenez,

Thank you for you email of 15 March 2018 in which you clarify some of the assumptions respecting ICBC's most recent three-year forecast in the February 2018 service plan. Your email did assist my understanding on a few of the questions posed in my Occasional Paper No. 53.[1]

I am a firm supporter of public auto insurance and believe that the ICBC organizational model is fundamentally sound. However, I believe that for a Crown corporation with the size and impact of ICBC there is significant improvement required in the quantity and quality of its public disclosure and accountability.

ICBC operates two different insurance programs. Because the Basic program is compulsory there is an obligation on the part of ICBC to significantly enhance its public reporting. While the Optional program competes with private insurers for sales, ICBC is a near monopoly as it has enjoyed a market share of some 90% for many years.

The three-year service plan (as well as the annual report and the quarterly reports) should be disaggregated to the program level. The reports should also include some standardized information service information, such as the number of policies earned, and claims filed. This would provide the media and the public with a much better understanding of the operations and challenges faced by the corporation.

The decision to provide only the 15-month 2016/17 results in the annual report and the recent service plan is regrettable, as it obfuscates comparisons with past and future fiscal years. I urge you to add the April to March results for 2015/16 and 2016/17, provided in response to my 2017 Information Request RM 1-4, Attachment A (as part of the BC Utilities Commission review of the 2017 Basic rate request) as an addendum to ICBC's annual report posted on your website. The three-year service plan should also be amended to add the 12-month 2016/17 fiscal year comparative.

Given the major changes to the Basic coverage, both for the no-fault accident benefits and the cap on pain and suffering for minor injuries, I would think that it is in the interests of ICBC and the government for the public to have a better understanding of the operations and financial outlook of the two insurance programs.

It is in this light that I reviewed the 2018/19 to 2020/21 financial forecasts.

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[1] http://www.bcpolicyperspectives.com/media/attachments/view/doc/occasional_paper_no_53_26_feb_2018/pdf/occasional_paper_no_53_26_feb_2018.pdf

The Capital Reserve Targets

BC was an early adopter of the OSFI minimum capital test (MCT) formula for determining appropriate capital reserves targets for the monopoly Basic program, and the competitive Optional program. The government set the MCT ratios at 100% and 200% respectively, and the BC Utilities Commission later raised the Basic management target to 145%.

You state that there is no longer a regulatory minimum for the Optional program, but we do know from the Ernst Young report that as of July 2017 the management target was 250%.[2] This was slightly lower than the 260% board-approved management target reported in the government's 2012 review of ICBC.[3]

What is the current board-approved management target for the Optional program?

You mention that the Optional insurance operates in a competitive environment. The major private insurers must maintain a large capital buffer, yet we know that ICBC's Optional program ended 2016/17 with an Optional capital ratio of about 130% -- well below the OSFI supervisory target for the private sector insurers.

Because ICBC does not separate the Basic and Optional programs on its three-year service plan forecast the public has no insight as to the apportionment of the projected 2017/18 and 2018/19 cumulative $2.0 billion capital reserve loss between the Basic and Optional programs.

When minister Eby announced the suspension of the 100% minimum regulatory requirement for the Basic program he stated that it would take several years for ICBC to restore a healthy capital reserve levels. " 'The first goal is to make sure ICBC stops hemorrhaging money,' the minister said. He expects it will take several years for the corporation to return to a healthy capital reserve."[4]

Not only does ICBC's latest service plan not separate the Basic and Optional capital reserves, it shows little or no rebuilding of the combined reserves by 31 March 2021. You note that ICBC still has sufficient assets to cover its claim liabilities, yet the margin of risk of a taxpayer bail-out is now very high.

It would seem to me that the public should be provided with more explanation as to the risks involved with operating with such low reserves. Also, I wonder how long the private insurers will be content to have ICBC operate the Optional program with (if one can make inferences from the three-year financial forecast) minimal capital reserves when their pricing reflects the OSFI requirement.

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[2] http://www.icbc.com/about-icbc/company-info/Documents/Affordable-and-Effective-AutoInsurance-Report.pdf p. 88.

[3] https://www2.gov.bc.ca/assets/gov/british-columbians-our-governments/services-policies-for-government/internal-corporate-services/internal-audits/icbc-review.pdf p. 19.

[4] https://www.theglobeandmail.com/news/british-columbia/bc-suspends-icbcs-capital-reserve-minimum-raising-prospect-of-bailout/article38142639/

The Financial Forecast

You are correct to note that I attributed all the savings from the Basic product changes to the incurred claims costs. This seemed the most logical approach given the lack of any separation of the savings provided by ICBC, and that the vast majority of the savings will result from the cap on pain and suffering on minor injury claims. I would be happy to revise my paper if you will provide me the apportionment for the three years.

You may also wish to include an explanation was to how $392 million is forecast to be saved through product changes in 2018/19 when the cap on pain and suffering does not take effect until 1 April 2019.

I appreciate your explanation of the 2018/19 increase in the current year claims forecast but, given the increase in the actual claims costs during the last two or three years, I continue to be incredulous about the approximate 27% increase over the 2017/18 forecast prior to the $392 million in forecast savings from the Basic product changes.

You suggest that since 2018/19 is the last year of the full tort system "it is prudent to provide for additional cost pressures that may accumulate on claims incurred prior to the announced reforms." Is one to infer from this statement that ICBC is anticipating a surge in claims during the coming year that would be for amounts higher than ICBC has experienced in the past for similar types of injuries?

For 2020/21, one would expect that the cap on pain and suffering for most injury claims would have resulted in a much more moderate forecast growth in claims costs compared to the approximate 10% increase (after product changes) that is reflected in the service plan. I am assuming that the announced increases to the accident benefits monetary limits will not result in a significant net increase in costs, as claimants are currently recovering most of these costs through the claims litigation process.

Provision for Prior Years

Re-estimation of the claim liability occurs every year; it is the size of the previous underestimation of claims costs that is of concern. From the explanation provided in the government's three-year fiscal plan (not in ICBC's service plan) one would conclude that the great majority of the $591 million for 2017/18 will be apportioned to the Optional program (injury claims over $200,000).[5] This is on top of the $302 million recorded for adjustments to prior year Optional claims recorded in 2016/17.

An initial mis-estimation of this magnitude (approximately $800-$900 million) over two years should require more explanation than that provided in the government's three-year plan or ICBC's service plan.

[5] Assuming that the difference in the dollar amount per claim in the new estimate compared to the previous estimate only impacts the Optional forecast.

Deferred Premium Acquisition Cost (DPAC)

Apparently, the accounting rules state that deferred premium acquisition costs must be unwound if the policy becomes unprofitable. The large reduction in the estimate for 2018/19 is based, as I understand your explanation, on the expectation that policies sold in 2018/19 will be profitable; yet a combined operating loss of $684 million is forecast for that year.

Clearly, most of the policies will carry-over to 2019/20, and a smaller number to 2020/21. As ICBC forecasts operating losses for 2018/19 and 2019/20, the favourable impact for 2018/19 seems overstated. This gets into areas of actuarial discretion, which is best left to the professionals.

However, the service plan provides no explanation or rationale for the 2018/19 dip in expenditures in this category. It should have as the positive change is so large.

Summary

In summary, I believe that the three-year service plan forecasts give rise to many questions which are not discussed in the assumptions section (which reads more as a summary of qualifications and disclaimers).

I believe that ICBC must do a better job in explaining its operations and the challenges it faces in the coming years was it moves to restore a satisfactory financial condition. Public support for the proposed changes in coverage is vital, and the public should expect better accountability from our public auto insurer. This comment applies to both the compulsory and the Optional products.

Thank you again for writing and your offer of a continuing dialogue.

Sincerely,

Richard McCandless