ICBC SUFFERS WORST EVER FINANCIAL YEAR

Background

On 28 August 2018 the government released ICBC's 2017/18 annual report.[1] The report generally confirms the 20 February 2018 forecast of a combined $1.3 billion operating loss, and a drop in the combined capital reserve (equity) of $1.46 billion.

In keeping with ICBC's minimalist approach to public reporting,[2] the corporation did not report on key units of service, such as the number of policies sold, or the number of injury and material damage claims. The management discussion section summarizes the change in certain revenue and expenditure categories at the corporate level, but no analysis was provided to explain the changes.

Unfortunately, ICBC did not provide comparable 12-month year-over-year comparisons in its financial statements. Instead it compared the 12-month 2017/18 fiscal year (April -March) to the 15-month 2016/17 fiscal year (January-March) bridge year. This makes simple comparisons in terms of year-over-year changes difficult, but the management discussion section of the annual report did use comparable 12-month periods for comparison – a marked improvement from last year's report.

THE PROGRAM VIEW

ICBC does not report its finances results at the program level, which is a significant gap in its accountability. Because Basic insurance is compulsory, one would expect a significant amount of financial and key performance measure reporting for this form or insurance. Instead, the annual reports include a single page financial summary that separates the Basic and Optional financial results – where again the comparison to the prior year is not clean as 12-months are being compared to 15-months.

To assist those who prefer a proper "apples to apples" comparison, Table 1 shows the 12-month April to March fiscal year results for the Basic and Optional programs (see page 22 of the annual report). The April 2016 to March 2017 results were provided by ICBC in response to my request during the BC Utilities Commission's review of the 2017 Basic rate request.

[1] https://www.icbc.com/about-icbc/company-info/Documents/ar-18.pdf

[2] http://www.bcpolicyperspectives.com/media/attachments/view/doc/occasional_paper_no_57_25_june_2018/pdf/occasional_paper_no_57_25_june_2018.pdf

TABLE 1 – FY2017/18 COMPARED TO FY 2016/17 (12-MONTH) ($=million)

	----- BASIC -----		--- OPTIONAL ---		--- COMBINED ---	
	2017/18	2016/17	2017/18	2016/17	2017/18	2016/17
REVENUE						
Net Prem Earned	3,149,312	2,925,681	2,179,626	1,988,019	5,328,938	4,913,700
Fees and Other	69,046	65,077	44,252	41,212	113,236	106,289
Total Earn Revenue	3,218,358	2,990,758	2,223,878	2,029,231	5,442,236	5,019,989
Investment Income	324,642	421,566	137,561	202,478	462,203	624,044
EXPENDITURE						
Claims Costs						
Current Year	3,451,207	3,149,091	1,633,027	1,462,491	5,084,234	4,611,582
Est. for Prior Year	218,191	(78,352)	344,766	280,975	562,957	202,623
Total Claims	3,669,398	3,070,739	1,977,793	1,743,466	5,647,191	4,814,205
Claim Serv & Safety	273,807	244,188	128,687	120,196	402,494	364,384
Operating Costs	121,887	121,722	138,701	141,898	260,588	263,620
Prem Tax & Comm.	451,395	178,478	341,288	509,137	792,683	687,615
Total Expend.	4,516,487	3,615,127	2,586,469	2,514,697	7,102,956	6,129,824
Non-Insur. Loss	(126,645)	(126,291)	--	--	(126,645)	(126,291)
Net (Loss) Income	(1,100,132)	(329,094)	(225,030)	(282,988)	(1,325,162)	(612,082)
Optional Transfer	99,000	201,000	(99,000)	(201,000)	--	--
Post Transfer Loss	(1,001,132)	(128,094)	(324,030)	(483,988)	(1,325,162)	(612,082)
EQUITY						
Retain. Earn Begin	1,459,879	1,415,881	988,601	1,654,544	2,458,480	3,070,425
Net (loss) Income	(1,001,132)	(128,000)	(324,030)	(483,943)	(1,325,162)	(611,945)
Opt. Capital Transf.	470,000	172,000	(470,000)	(172,000)	--	--
Retain. Earn. End	928,522	1,459,879	204,476	998,601	1,132,998	2,458,480
OCE Begin Year	(17,552)	(148,360)	(5,940)	(78,242)	(31,865)	(226,602)
Net Change Assets	(185,232)	78,904	(78,489)	37,071	(262,721)	115,975
Pension Change	90,348	51,904	43,898	26,858	134,246	78,762
OCE End of Year	(112,436)	(17,552)	(48,904)	(14,313)	(161,340)	(31,865)
Non-Control Change	(3,042)	(10,496)	(1,024)	(5,940)	15,505	(16,436)
Total Equity	826,459	1,455,742	160,704	990,444	987,163	2,446,186
Liabilities						
Unearned Prem.	1,549,552	1,430,000	1,080,192	984,503	2,629,744	2,414,503
Unpaid Claims	8,607,916	7,851,433	3,287,780	2,666,538	11,895,696	10,517,971

	MCT	e46	103	e18	132	31	112

Source: ICBC annual report 2017/18 and 2016/17 from BCUC, ICBC 2017 rate request, IR 1, RM 1-4 Attachment A; http://www.bcuc.com/Documents/Proceedings/2017/DOC_50367_B-2_ICBC-Responses-to-IR-1.pdf PDF p. 1172.

Key Points

A comparison of the operating results is also hampered by the transfer of Optional operating and capital funding during these two years. For 2016/17 (12-month) a total of $373 million was transferred, and a further $569 million in operating ($99 million) and capital ($470 million) was transferred in 2017/18.

1 Gap Between Actual and Target Capital Reserves Widens

For about 12 years the BC Utilities Commission has required a Marginal Capital Test (MCT) management target of 145% for the Basic program. For 2017/18 the target would have required approximately $2.6 billion, while the actual was $826 million, resulting in a shortfall of approximately 1.8 billion.

For many years the government required a minimum 100% MCT ratio, but this requirement was suspended by cabinet order on 26 February 2018[3] as the government was unwilling to approve a massive increase in Basic premiums to sustain the minimum level of capital reserve.

The ICBC board of directors had required an Optional management target of 250% (see EY), but this was ignored as the Liberal and NDP governments ordered most of the Optional capital reserve dissipated to subsidize the Basic rates. By 31 March 2018 I estimate that the Optional funding shortfall at approximately $2.1 billion.[4]

TABLE 2—GAP BETWEEN ACTUAL AND REQUIRED CAPITAL ($=million)

	2012	2013	2014	2015/16	2016/17	2017/18
BASIC -- ACTUAL	1,427	1,716	1,633	1,290	1,455	826
TARGET@145%	1,508	1,668	1,740	1,890	2,045	2,610
SURPLUS/(DEF)	(81)	48	(107)	(600)	(580)	(1,784)
OPTIONAL--ACTUAL	1,820	1,927	1,983	1,590	990	161
TARGET@250%	1,450	1,575	1,663	1,750	1,800	2,250
SURPLUS/(DEF)	370	352	320	(160)	(810)	(2,089)

[3] OIC 67/18.

[4] Assuming that 1% MCT is $9 million; 250% is $2.25 billion while the actual was $160.7 million.

COMBINED	289	400	213	(760)	(1,390)	(3,873)

Source: see Table 1.

Table 3 shows the effect of the capital shortfall gap of reducing the Basic management target to 80%, and reducing the Optional management target to 150%, as discussed in my Occasional paper No. 56.[5] The combined 2017/18 shortfall drops from approximately $3.9 billion to $1.8 billion.

TABLE 3—GAP BETWEEN ACTUAL AND REDUCED REQUIRED CAPITAL ($=million)

	2012	2013	2014	2015/16	2016/17	2017/18
BASIC -- ACTUAL	1,427	1,716	1,633	1,291	1,455	826
TARGET@80%	830	920	960	1,050	1,130	1,440
SURPLUS/(DEF)	597	796	673	241	325	(614)
OPTIONAL--ACTUAL	1,820	1,927	1,983	1,588	990	161
TARGET@150%	870	950	1,000	1,050	1,250	1,350
SURPLUS/(DEF)	950	977	983	538	(160)	(1,189)
COMBINED	1,547	1,773	1,656	779	165	(1,803)

Source: Derived from ICBC annual reports.

2. Current Year Claims Costs

The growth in the estimate of current year claims costs for the Basic program moderated compared to the two previous years, while the growth in the Optional claims was somewhat less that in the prior 12-month period.

TABLE 4 – Per Cent Change in Current Year Claims Costs

	2012	2013	2014	2015/16	2016/17	2017/18
BASIC	6.7	5.0	5.6	20.2	14.0	9.6
OPTIONAL	1.2	4.4	9.0	14.7	17.9	11.7

Source: see Table 1.

The Basic provision for prior years claims costs grew dramatically eliminating most of the reduction in the prior year. ICBC appears to have adopted a conservative approach to providing for these claims costs.

TABLE 5 – Change in Provision for Prior Years Claims Costs ($=million)

	2012	2013	2014	2015/16	2016/17	2017/18
BASIC	(13.7)	12.4	108.5	205.3	(380.9)	296.5
OPTIONAL	(41.5)	2.4	127.3	(41.6)	238.4	63.8

5 http://www.bcpolicyperspectives.com/media/attachments/view/doc/occasional_paper_no_56_19_april_2018/pdf/occasional_paper_no_56_19_april_2018.pdf

Source: see Table 1.

Major fluctuations makes one question….With a 14% increase in current year Basic claims costs for 2016/17, ICBC actuaries reduce provision for prior year Basic claims by 78.4 million (a swing of $381 million from 2015/16). Adds volatility to total provision for claims costs, see Table xx below.

The per cent change in the combined current and prior year claims costs shown in Table shows a high degree of volatility in the Basic program, which needs to be explained.

TABLE 6 – Per Cent Change in Current and Prior Years Claims Costs

	2012	2013	2014	2015/16	2016/17	2017/18
BASIC	6.1	5.6	1.7	39.3	0.2	19.5
OPTIONAL	(3.2)	4.9	5.1	28.7	47.2	13.4

Source: see Table 1.

Most insurance companies try to restrain the growth in the unpaid claim liability (UPL)because any increase in liabilities unmatched by asset growth will reduce equity. ICBC has seen its Basic UPL grow at an annual average of 10%, while the Optional UPL increased rapidly in the last two years. This is an important explanation for the drop in Basic and Optional equity experienced in the least three years.

In 2017 ICBC hired many more claims adjudicators to process more claims and reduce the UCL.

TABLE 7 – Per Cent Change in the Value of Unpaid Claims Liability

	2012	2013	2014	2015/16	2016/17	2017/18
BASIC	9.7	8.1	9.1	11.2	13.0	9.6
OPTIONAL	2.5	4.7	9.4	9.5	24.3	23.4

Source: ICBC annual reports.

Additional reports will be issued in the near future.

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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.