



2010 Annual Adjustment Review

Alberta Automobile Insurance Rate Board

Alberta Motor Association Insurance Company Submission

May 28, 2010

Alberta Motor Association Insurance Company
Presentation to Alberta Automobile Insurance Rate Board
June 2010

AMA Insurance is a wholly owned subsidiary of the Alberta Motor Association, an organization with 900,000 members, which has provided a variety of products, services and benefits to members and customers for over 80 years.

AMA Insurance is the largest Alberta based insurance company and is regulated by the Alberta Superintendent of Insurance. Whatever changes are implemented as a result of the Automobile Insurance Rate Board (AIRB) annual review will have a significant impact on AMA as over 95% of our business is written in Alberta and Alberta is the only province where we write automobile insurance.

Introduction

With the introduction of auto reform in late 2004, consumers in Alberta have benefitted from a number of industry-wide rate reductions as well as increased coverage provided by Accident Benefits (AB). With the 5% rate decrease required in the 2009 Rate Board decision, current rates are 17% below 2004 levels. To bring rates back to pre-reform levels, ignoring inflation, an increase of 20.5% would be required.

Approach to Rate Making

We consider this to be a very competitive market. There are over 60 insurance companies operating in Alberta and no two of them have exactly the same rates. Insurance is by no means a commodity type product where we all pay the same price and buy the same product. Conceptually it is very difficult to apply an across the board percent change when we all have different starting points, value propositions and business models.

Rate making is very much a prospective exercise. This involves not looking back but looking ahead, the premiums that we set now will be charged 6 to 18 months from now and will be earned by the insurance companies 6 to 30 months in the future. To set adequate rates, we need to look forward at what the costs will be rather than back at what the costs were. Because we are setting rates for 6 – 18 months in the future the rate change required is the difference between the current premium and what the industry's costs will be in 2011 / 2012. The only relevance of the current costs is to provide a starting point to estimate future costs.

It would be an error in principle and in logic to base rate changes for future years to account for the current year's profit or loss. The current year results reflect market and investment conditions, legislative changes, weather patterns and

other intangible factors which may or may not exist in the future. As well, the current year's profit or loss is reflective only of the current calendar year which is impacted by changes from multiple accident years. Reserve releases in the 2009 calendar year relating the MIR constitutional decision actually reflect changes to the loss costs from accident years 2004-2009. To look at any single calendar year in isolation is an oversimplification.

We also note that companies providing insurance and people obtain insurance in 2011/12 may be different than those providing and obtained insurance in 2008/09. This is particularly evident in the past few years in Alberta as we experienced an influence of workers during the economic boom. Basing rates on prior years profits would unintentionally making rates more, rather than less, volatile. If rates are set too low due to past profitability the industry will fail to attract new entrants thereby making the industry less competitive and requiring even greater future rate increases. Likewise, increasing rates to compensate for past losses would make the industry overly attractive and will lead to increased competition resulting in future rate decreases.

Consequently, we would reiterate the principled position that rate making must be a prospective process in which the objective is to estimate as closely as is reasonably possible the losses in those future years and the premiums required to protect against those losses as a reasonable profit.

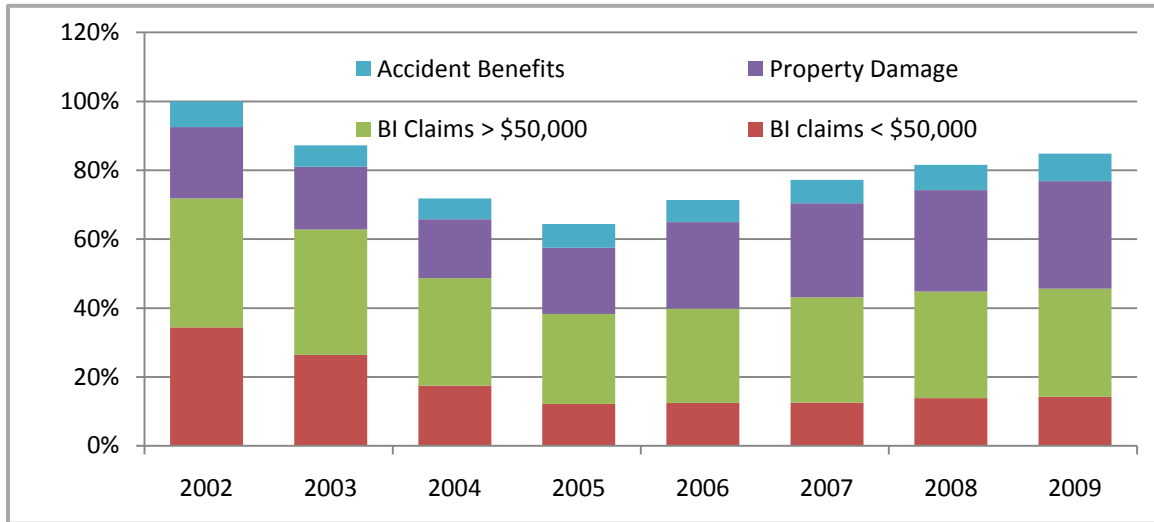
Loss Trends

All statistical information is supplied on an accident year basis using all policies written by AMA Insurance, whether or not it has been ceded to the Risk Sharing Pool. For comparison purposes, 2002 has been selected as the baseline data.

Composition of Loss Costs

Included in the compulsory automobile product are three or four different loss components; the Accident Benefit Costs, the Property Damage Liability Costs (PD) and Bodily Injury Liability Costs (BI). For the purpose of this discussion, we have separated the BI costs into large and small losses with large losses considered as total loss cost (Pecuniary and Non Pecuniary) greater than \$50,000. While not perfectly correlated to capped or non-capped losses there is a high degree of correlation and allows for a more objective determination as to which category the claim falls into.

In assessing the composition of the loss costs, the impact of the significant increase in PD frequency and severity should not be understated. As the following chart illustrates, PD loss costs have grown from roughly 22% of the loss costs in 2004 to 37% in 2009. For determining the required rate increase the most significant assumption relates to the future changes to the PD component of the loss cost.

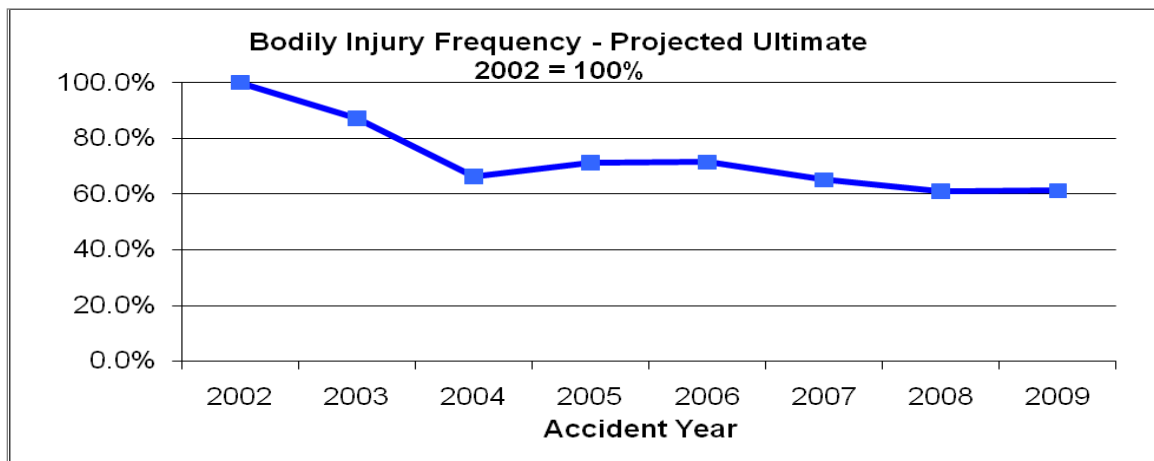


The PD loss costs have not been impacted by auto reform but have increased steadily and substantially over the last five years.

Accident benefit loss costs remain at roughly the same proportionate share as 2004. Accordingly we are focused primarily on the BI and PD loss costs and have not provided analysis of AB loss costs

Bodily Injury Trends – Frequency and Severity

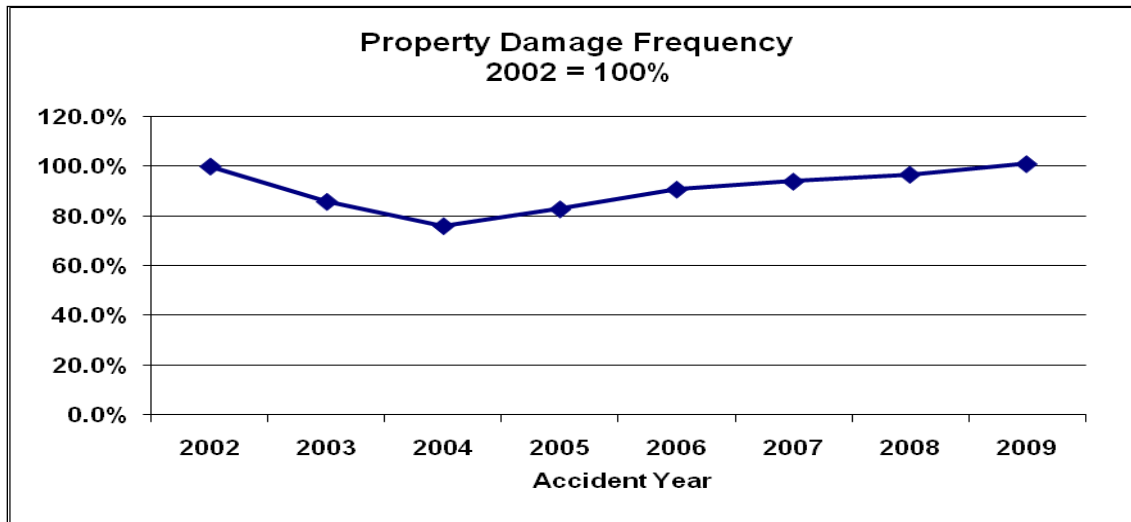
The composition of the loss costs attributable to smaller BI claims has dropped from 34% in 2002 to 14% in 2008 / 2009. A portion of this is undoubtedly due to the minor injury cap but a large portion is also due to a reduction in frequency which occurred between 2002 and 2004. Since 2004 there is no strong evidence of decreasing frequency and the impact of indexing the minor injury cap for inflation has increased the loss cost of small BI claims marginally over this period.



As well, the costs of large BI claims dropped noticeably between 2002 and 2004 but have remained steady since 2004.

Third Party Property Damage Trends – Frequency and Severity

Since 2004, the Property Damage (PD) portion of the costs has increased substantially due to both increased frequency and severity. Until recently, the increased costs of AB coverage and the increased costs of PD liability claims had been largely offset by reduced cost of Bodily Injury (BI) claims. However, this is no longer the case. Current premiums need to reflect not only the reasonably steady costs of BI claims, but the significantly increase in PD costs.



PD severity is now 60% higher than in 2002 and 45% higher than in 2004 pre-tort reform. Combined with increases in frequency, the loss costs associated with this coverage have increased from 20% to 37% of loss costs. These are completely unrelated to tort reform and the MIR constitutional decision.



Conclusion

Based on the data presented, it is clear that loss costs on an accident year basis bottomed out in 2005 and have been growing steadily ever since. This is primarily driven by increases in both frequency and severity for the PD portion of the loss costs.

It is also important to note that while rates have decreased 17% since 2004, the overall loss costs are now approaching 2003 levels with a distinct upward trend.

AMA Insurance submits that our data represents a roughly a 6% market share of the Alberta auto market and is therefore a reasonable reflection of the industry trends. Based on this data, it is clear that industry loss costs will continue to grow in the upcoming accident years and, as a result, rate increases may be required.

With respect to the industry wide rate adjustment, AMA Insurance submits that rate adequacy is particular to each individual company and, consequently, does not believe it appropriate to comment on the magnitude of any adjustment on an industry wide basis.