

State Farm Mutual Automobile Insurance Company



Steve Harr, FCAS, MAAA, FCIA
Actuary and Assistant Secretary-Treasurer

One State Farm Plaza, D4
Bloomington, Illinois 61710
Phone: 309.766.3568
Fax: 309.766.0225
E-mail: Steve.Harr.BB5B@STATEFARM.com

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Automobile Insurance Rate Board
200 Terrace Building
9515 – 107 Street
Edmonton, AB T5K 2C3

STATEMENT OF STATE FARM MUTUAL AUTOMOBILE INSURANCE COMPANY

I appreciate the opportunity to provide comments to the Board regarding the annual review of auto insurance premiums for basic coverage in Alberta.

The State Farm Mutual Automobile Insurance Company is the largest insurer of automobiles in North America. State Farm commenced writing auto insurance in Canada in June of 1938.

State Farm is a multiple line insurance organization insuring over 1 million automobiles in Canada, of which 110,000 are in Alberta. In addition, we have over 900,000 Property and Casualty (P&C) policies other than automobile insurance and over 250,000 Life Insurance policies in Canada. State Farm's Canadian Headquarters is in Aurora, Ontario. There are 48 exclusive State Farm insurance agents in Alberta, in addition to a variety of different employees residing and working in Alberta to support their efforts.

It is worth noting that the automobile insurance marketplace in Alberta is very competitive. State Farm is one of a number of insurance companies writing automobile insurance in Alberta. However, since the introduction of the Risk Sharing Pool (RSP), the RSP has become one of the larger insurers in Alberta. This creates significant concerns for a properly functioning competitive marketplace and was not the intent of the RSP. The grid rate level needs to be established at a high enough ceiling that it performs its intended function and also allows the competitive marketplace to operate underneath it. The maximum premium grid should not restrict rates for the lowest cost customers. Increasing the maximum premium will promote competition and reduce the size of the RSP, thereby reducing the grid subsidy.

It is important that the Board not disrupt the competitive market by adopting a rigid and uniform method that might deny insurers a fair and reasonable profit. A competitive marketplace is the best regulator of rates. A more open, competitive market will provide the insurance-buying public availability and reasonable stability of prices. The annual rate adjustment should only apply in establishing the maximum premium and not apply to the rates for individual insurers.

The purpose of my written submission is to provide suggestions to the Alberta Insurance Rate Board regarding the automobile insurance issues set for Hearing in June 2011.

Loss Trends

It is important to recognize that ratemaking is prospective. The auto insurance product is priced before the ultimate costs are known. The rates for the 2011 annual adjustment will affect the premiums for policies effective November 1, 2011 through those policies beginning November 1, 2012; thus over two years from now.

We caution the use of overly optimistic assumptions in the ratemaking process for the maximum premium. We suggest that the maximum premium be established toward the upper threshold of what is an actuarially justified rate. In addition, the premium grid places a ceiling on the premiums but no such limit exists on the losses.

Following decreases in bodily injury claim frequency in 2009, which may have resulted from injured drivers who refrained from making a claim during the MIR challenge process, bodily injury claim frequency has increased considerably during 2010 and early 2011. The average paid claim for bodily injury has remained relatively level during the last year.

For property damage coverage, the average paid claim has increased moderately in recent quarters. Claim frequency decreased in 2010 due in part to light winter weather but has begun to increase in early 2011. Despite the decrease in 2010, property damage claim frequency remains above pre-2009 levels.

For accident benefits coverage, claim frequency dropped following the 2004 reforms but has been relatively flat recently. However, the average paid claim for accident benefits coverage has increased substantially following the increase in the limit to \$50,000 with the reforms in 2004. In addition, the changes being considered to increase coverage for catastrophic accident benefit claims would add additional pressure to the average paid claim.

Impact of Economic Climate on Claim Costs

Several influences affect claim costs. It is difficult to identify one source. However, the slowed economy appears to have impacted the claim costs to some degree. Prior to the economic downturn, claim severity was increasing significantly as the cost of goods and services rose. That pace has slowed some with the economy; however, claim severity continues to increase. In a down economy, claim costs are not subject to the same inflationary pressures as might be experienced during a more robust economy. The kilometres driven usually are reduced during an unfavourable economic cycle; thus less exposure is typically present, affecting claim frequency.

As the economy improves, we expect inflation and kilometres driven will increase, adding pressure to claim severity and frequency, respectively.

It is also worth noting that investment yields have decreased, and we expect that to continue, resulting in less investment income to support the insurance operation. Hence, everything else being equal, the insurers need more from underwriting income to achieve the same return on equity investment.

The main purpose of the annual rate review is to establish the maximum premium. The fact that industry data, including data for those below the maximum premium, is used should be considered when reviewing the change to the maximum premium. One would expect the claim cost and claim frequency levels to be higher for those insureds capped by the grid rate level.

We should allow the competitive marketplace to deal with these marketing strategies and not through a regulatory process that implies one size fits all. Consumers are best served by a competitive marketplace which is responsive to their specific and individual needs. The most successful companies will be those who can satisfy individual customer needs by offering the best combination of value – quality products, excellent service, and competitive prices.

In conclusion, we have significant concerns with the current maximum premium and the grid structure. State Farm is having a larger percentage of our new business capped by the grid compared to our renewal book. Over time, this would have a negative impact on the size of the Risk Sharing Pool. In addition, the percentage of new business capped by the grid is even larger for Edmonton. The subsidy for Edmonton is against cost-based pricing and disrupts the natural functioning of the marketplace.

Again, I appreciate the opportunity to provide comments to the Board regarding Auto Insurance in Alberta. State Farm is committed to working with AIRB in providing a healthy auto insurance environment that is responsive, stable, affordable, and sustainable at meeting the needs of Albertans.


All questions concerning this written submission should be directed to:

Steve Harr
Marty Wietfeldt

(309) 766-3568
(309) 763-4063

steve.harr.bb5b@statefarm.com
marty.wietfeldt.no5q@statefarm.com

Sincerely,

A handwritten signature in black ink that reads "Steve Harr". The signature is written in a cursive style with a large, stylized "S" and "H".

Steve Harr
Actuary

Cc: Barbara Bellissimo