Research & Development

The Effects of the September 1, 2013 Private Passenger Auto Rate Filing

April 2014

Introduction

As part of the R&D mission, we seek to provide you with information and analysis to measure portfolio performance and identify opportunities. This report provides an update on the shared Automobile portfolio (Company 789).

Good operating protocol for all rate activity includes evaluating the impact of changes as soon as practical. We now have six months' worth of data to assess the results of the September segmentation rate filing.

History

The September 1, 2013 Private Passenger Auto (PPA) rate filing was completed as part of the regular review process conducted on behalf of the Auto Rate Filing Committee (ARFC).

An external scan of competitors showed the shared auto portfolio was outperforming the industry in both loss ratio and growth. However, after a period of growth over several years, exposure and premium had peaked around the middle of 2012.

An internal scan identified a very seasoned book, with a significant proportion of middle aged drivers with many years licensed. A portfolio diagnostic using predictive analytics scoring methods was performed by Eagle Eye Analytics. Their analysis supported the conclusion that better performing drivers were those with many years licensed. The existing highest driving record E was made up of the largest number of exposures, presenting an opportunity to more finely segment. Feedback from member companies collected in the last survey (March 2012) provided the direction for the segmentation strategies, including addressing concerns over declining volume of underage drivers.

The rate filing was originally submitted in the Spring of 2013. At that time, the provincial government announced intention to mandate a 15% reduction in auto insurance rates. We were able to negotiate the final filing with an effective date of September 1, 2013 to fall within the government's time line.

The objectives of the rate filing were:

1. Identify segments that have better performance to improve loss ratio,
2. Improve competitive positioning to increase growth,
3. Contribute to the mandate to take -8% rate in the first year.

We were in the enviable position to be one of the first to implement a decrease in rates with the filing projected to have a -6% impact on annual premiums. The rate filing introduced:

- New higher driving records 10, 20, and 30 (with driving record E merging into the new 30), based on number of years licensed as primary qualifications

- The 10% genNow! discount for underage classes available only to the children of a Mutual policyholders who now have their own policy

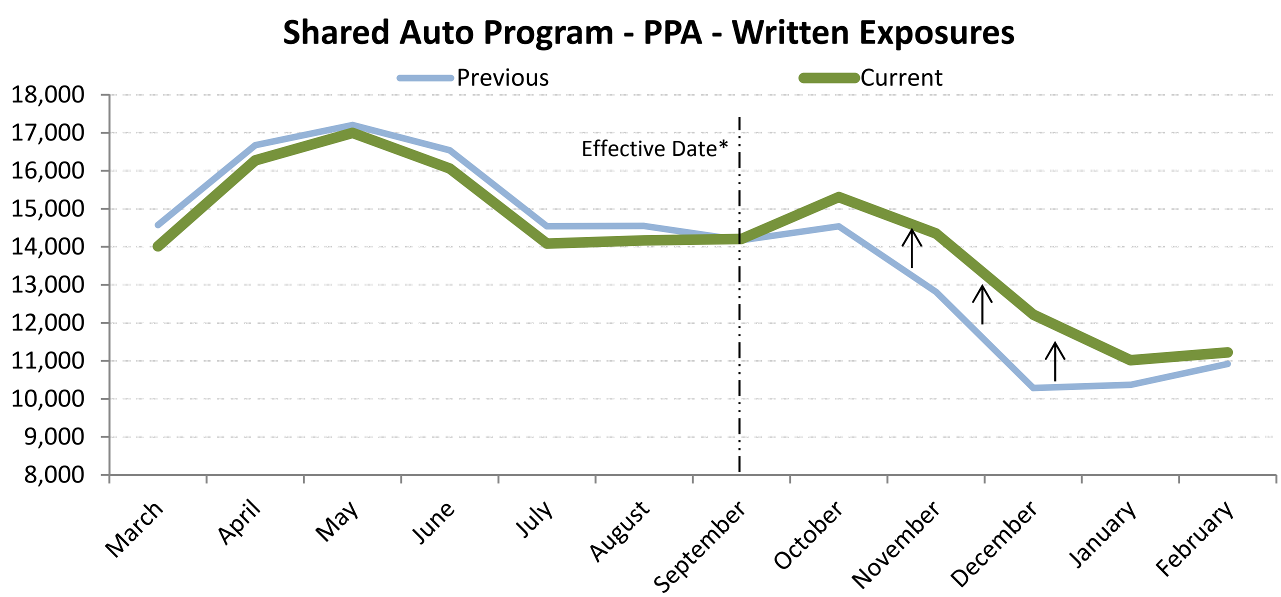
Impact of Rate Filing

The rate decreases in this filing would reduce premium volume for the Mutuals, putting further pressure on expense ratios. In order to offset the decline in premium, significant growth in written exposures is required. R&D held a workshop at the automobile underwriters' roundtable in October, which demonstrated how the rate filing would affect total premium volume and the exposure growth required to recoup lost premium.

Since the filing went into effect, Member Companies in the shared auto program have been successful in generating new business growth.

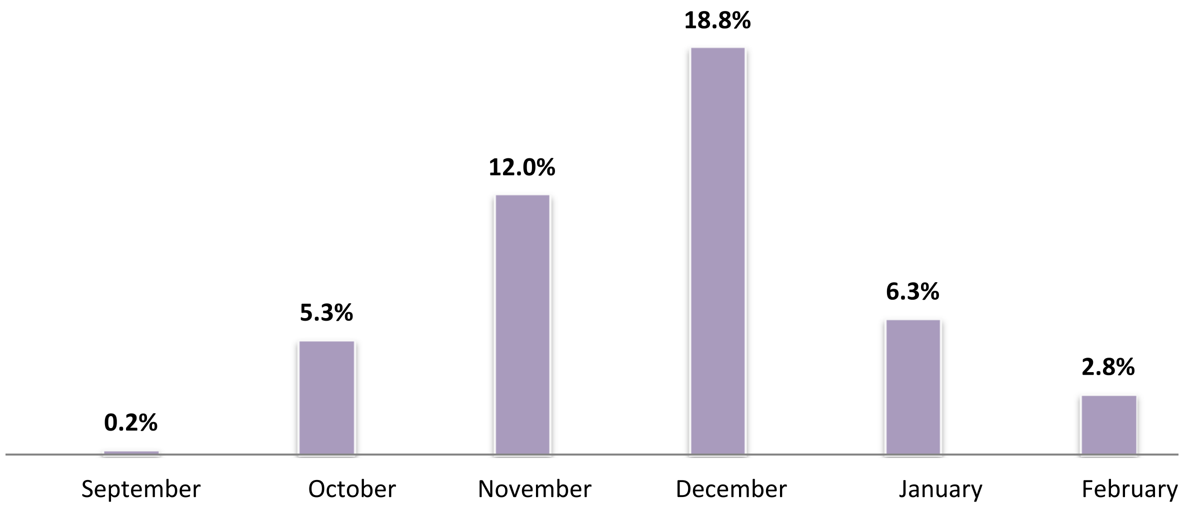
The filed impact of -6% is offset by a forecasted 10% growth in annual exposures. Based on the data for 2013 Q4, the total effect of the September 1 rate filing will only be a -3.5% impact on annual written premium.

The new growth in exposures can be seen in the following graph. Note the significant lift in written exposures for the previous 6 months since the September 1 rate filing went into effect (Sept 1, 2013 – February 28, 2014), and the same 6 month period in the previous year (Sept 1, 2012 – February 28, 2013). This occurs after a period when written exposure counts had trailed behind in every month. Also note that the gap appears be narrowing in January and February 2014. This could be the result of competitors implementing rate decreases, following the industry requirement to file in December 2013. It appears the Shared Auto Program enjoyed several months of competitive advantage as a result of being the first organization to implement a required rate decrease.



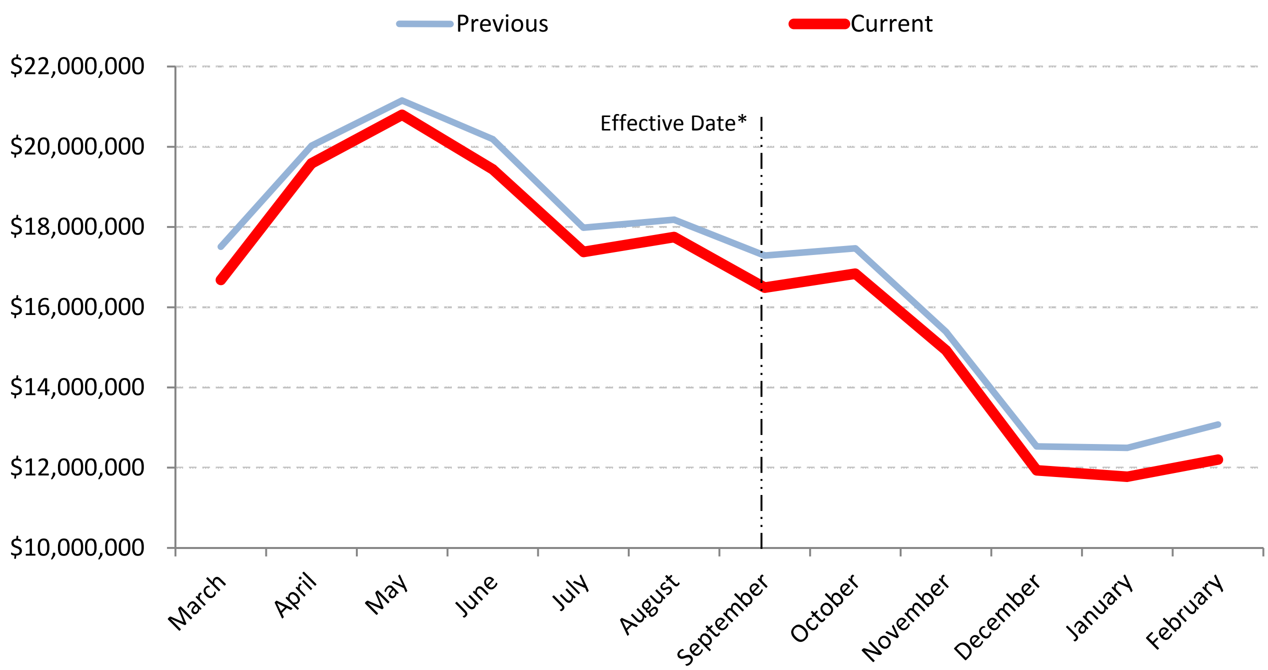
This exposure growth can be shown in another manner. The chart below shows the year over year written exposure percentage growth for each month since the rate filing was implemented. For example, October 2013 saw 5.3% more written PPA exposures than October 2012. The month of December 2013 saw largest growth compared to the same both a year before at 18.8%.

Shared Auto Program - PPA - Written Exposure Growth

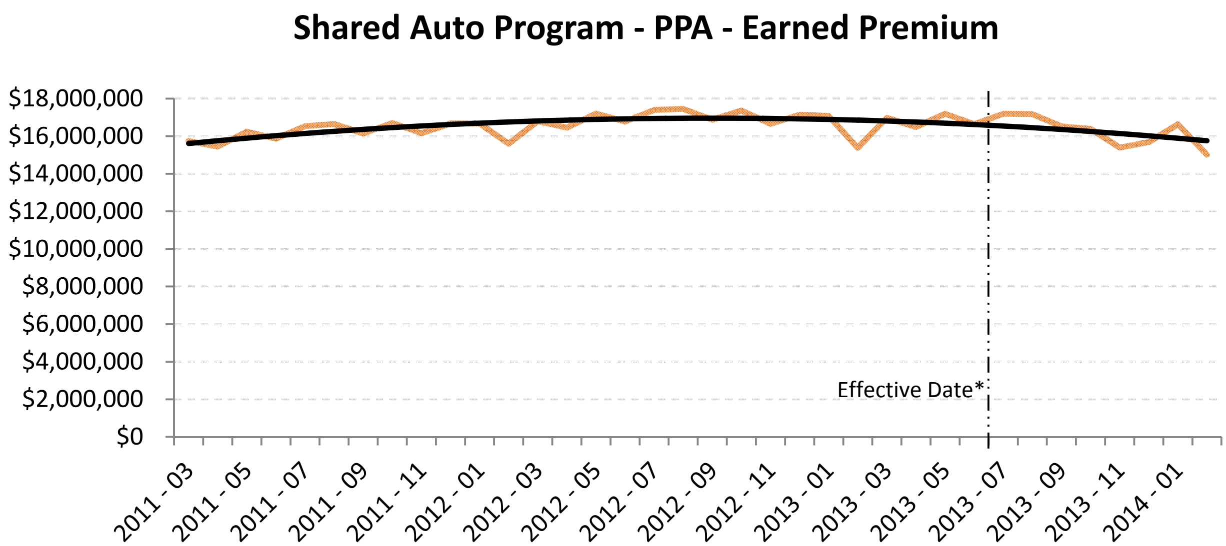


The growth has not been enough to completely offset the decline in premium volume. As you will note in the graph below, written premium volume in the last 12 months trails the previous rolling 12 month period in every month. However, it appears the gap in written premium volume narrowed for the months of October, November, and December, but appears to have widened significantly in 2014.

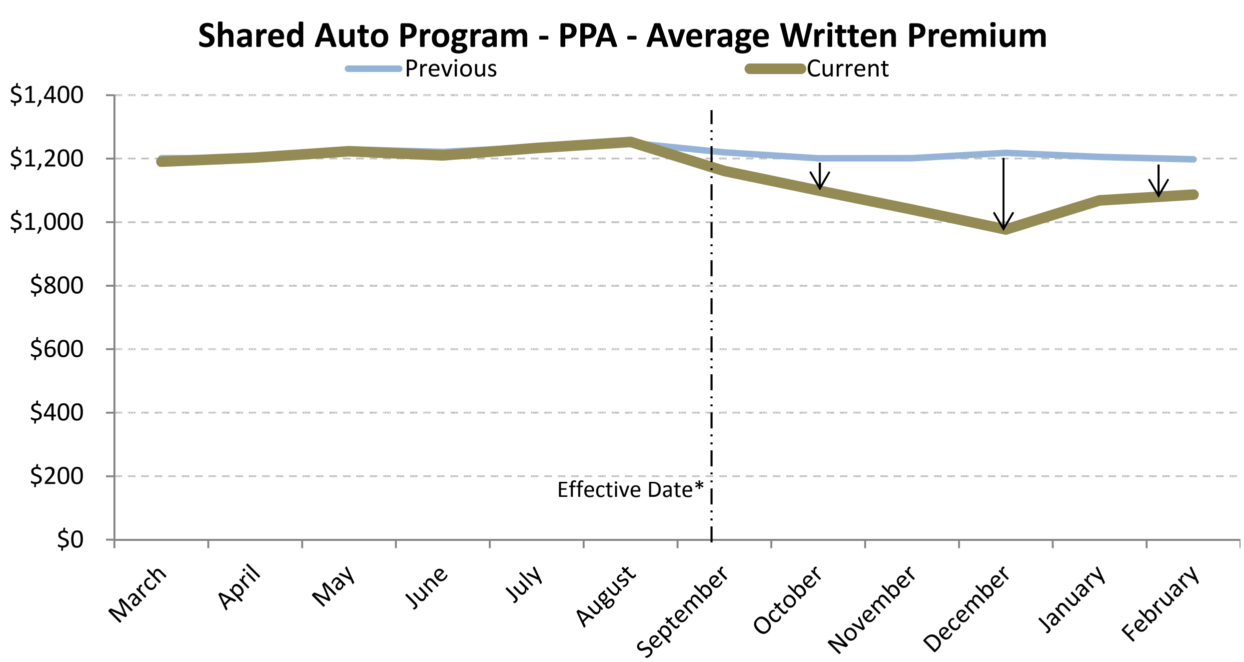
Shared Auto Program - PPA - Written Premium



As such, there is a continued trend of declining earned premium volume, which peaked in the middle of 2012. The following graph shows Earned Premium for the last 3 years, with a smoothing trend line added in black.

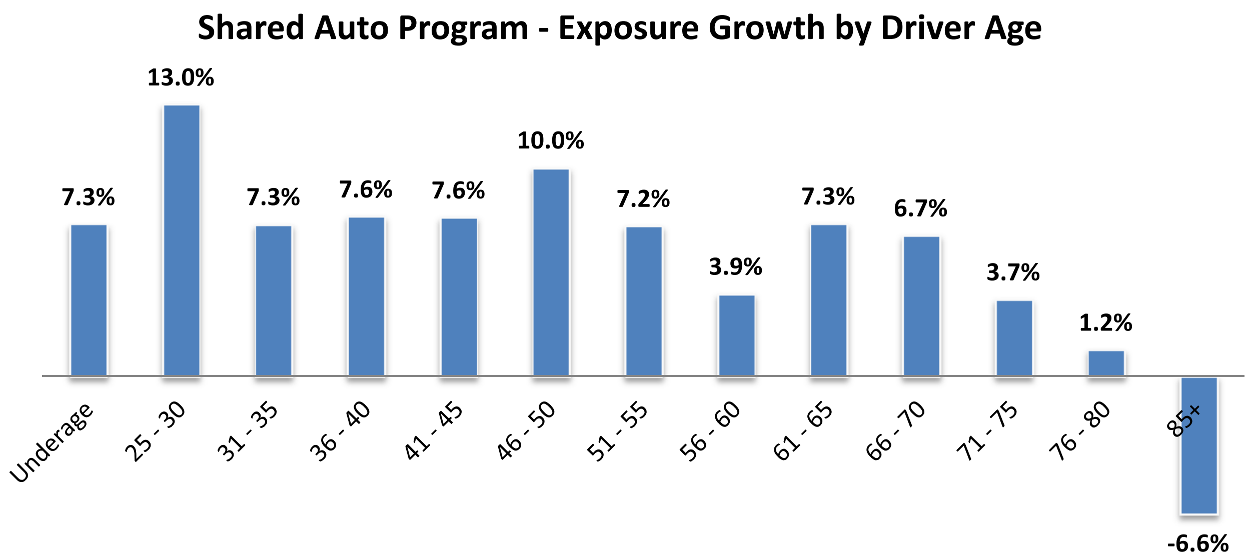


The reason why the increased exposure growth did not fully recoup the premium volume is due to the effects of the rate filing on the average premium charged to policyholders, which has been more significant than the overall filing impact of -6%. Before the September rate filing the average written premium in each month for 2013 was identical to 2012 because there had been no significant rate change activity. Since the rate filing, the average written premium in December 2013 was 20% lower than one year ago in December 2012.



This would indicate significant growth in areas where large rate decreases were made. Recall the goal of the rate filing was to improve driver segmentation with targeted lower rates, and in this regard the filing was a success. Another reason for the lower average premium is the natural aging of drivers within the auto portfolio which would see more drivers moving into the higher driving record categories and be eligible for the retiree discount. We have noted these trends and others which impact premium volumes previously in R&D's November 2013 report entitled *The Reduction in Auto Premium Volume for the Shared Auto Portfolio.*

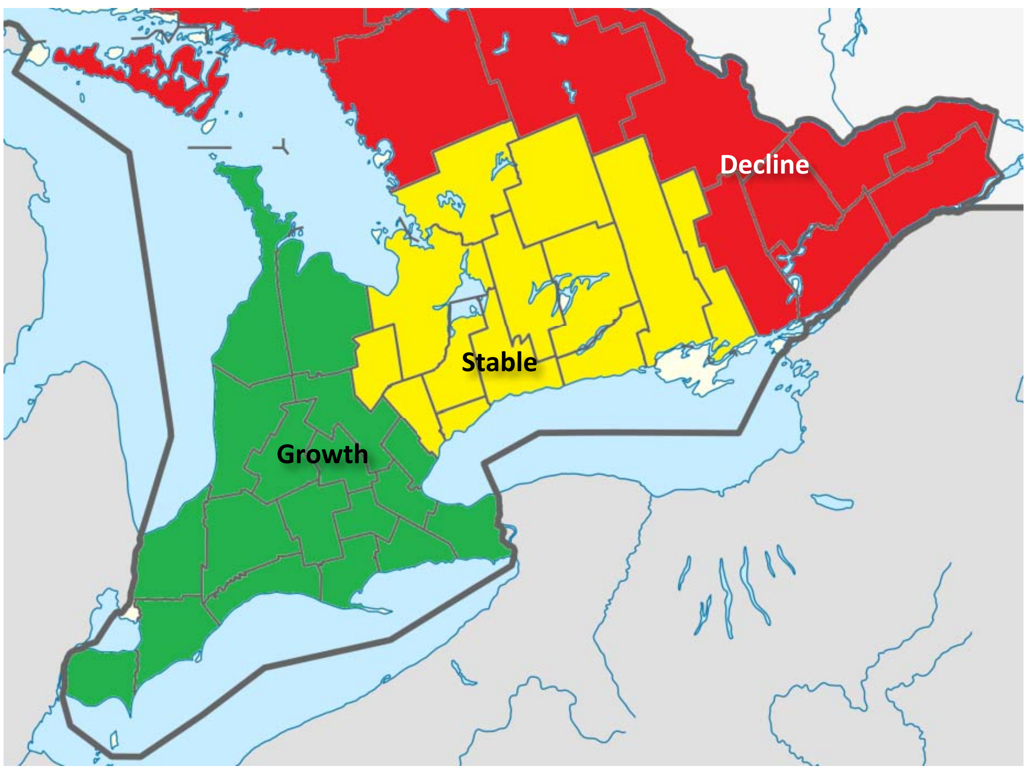
The implementation of the September 1 rate filing has resulted in exposure growth for nearly all age groups, as can be seen below.



There has been **<u>high exposure growth in the new 10, 20, and 30 driving records</u>**. Note that the highest growth rates above are for drivers aged 25 – 30 at +13%, most of whom would be eligible for the new driving record 10, as well as drivers aged 46 – 50 at +10%, who would benefit from the low rates of the driving record 30. The factors influencing this growth are improved rates, and the natural aging of drivers in our portfolio. As the composition of the Shared Auto portfolio includes more experienced drivers our overall performance is expected to improve over time. Comparing the 6-month experience of Sept 2013 – February 2014 versus the same 6 month period in 2012 – 2013, **<u>there has been an improvement in the Shared Auto Program PPA loss ratio of 1.3 points</u>**, from 43.7% to 42.4%. With large reductions expected in premium volume, it is imperative rate filings segment better performing risks to preserve a superior loss ratio. Reducing expenses will also help member companies maintain profitability.

The rate filing also introduced the genNow! discount to provide an additional discount for underage drivers insured with the Mutuals. As can be seen above, there has been **<u>growth in exposures for underage classes.</u>** This reverses a multi-year trend of declining numbers of young drivers. Unfortunately, the genNow! discount has not been as successful as was originally intended. During the filing process, FSCO required additional criteria for the discount to apply only to registered owners of vehicles. There has been some membership feedback suggesting it has not been successful in retaining family business with underage classes. This is because OSAP eligibility for post-secondary education precludes a student from owning a vehicle. Thus, parents maintain vehicle ownership and the insurance costs cannot be offset with the genNow! discount. We have continued to explain our rationale and concerns with FSCO, however their position is that without the requirement it would be too similar to the existing multi-vehicle discount, which isn't permissible.

Geographically, the exposure growth has been concentrated in southwest Ontario: Lake Huron, Lake Erie, Niagara Falls, London, Windsor, and Hamilton areas. Exposure growth rates have been as high as +10% to +15% in these areas. There has been little to no change in the central region of lower Ontario: Toronto, Oshawa, Orangeville, Barrie, Lake Simcoe, and Kawartha Lakes. And there has been a decline in exposures in Northern Ontario, and the rural areas surrounding Ottawa.



Data Submission Error affecting Driving Records in OMIA Database

The purpose of the September 1 rate filing was to target experienced drivers with the new 10, 20, and 30 driving records. Initial investigation has determined that the growth in exposures has exclusively come in under these higher driving records. Unfortunately, a mapping discrepancy on the EDI files for one vendor system has caused some 10, 20, and 30 driving records to come into the OMIA database as 1, 2, and 3s, as only the first digit was being sent through instead of converting properly to OMIA's higher driving record codes. This discrepancy has affected data submissions for the months of September, October, and November, before being corrected by the conversion to the XML database format in December. As such, it is currently not possible to show growth rates by driving record which includes this 3 month time period. Any data report based on OMIA's database involving driving record will be skewed by these incorrect submissions. ***Any users of the OMIA Auto QlikView application should be warned that any exhibits involving driving record will not be accurate.***

Upcoming Auto Rate Filing

Member Companies should be aware of the current political environment surrounding automobile premiums. We were required to submit a territorial rate filing by December 13, 2013 to further contribute to the government's requirement of -8.1% by August 1, 2014.

Our original submission was filed as -4% overall, through moving to postal codes and creating several new territories. Unfortunately, FSCO rejected our submission on the basis of their analysis concluded an actuarial indication -10.3%.

We proposed introducing a Mature Citizen's discount to further segment better performing customer characteristics. The Auto Rate Filing Committee approved this and provided direction to negotiate further with FSCO meet half way. We were able to persuade FSCO that we are committed to working with them to achieve the mandate, while protecting the viability of all of our member companies.

The next PPV rate filing will be effective July 1, 2014 to introduce postal code rating and Mature Citizen's discount for an overall rate reduction of -8.1%

Member Companies are encouraged to determine appropriate strategies to meet their business needs. Increasing exposure volume to recoup the premium decline will help manage your expense ratio, but it is imperative to maintain rigorous risk selection methodology to attract and maintain better performing customer segments.