Saskatchewan Rate Review Panel

Report to the Minister Responsible for Crown Investments Corporation of Saskatchewan

regarding the

SGI’s Auto Fund Rate Application Effective date August 4, 2012

Report submitted May 31, 2012

Executive Summary

The SGI Saskatchewan Auto Fund (SAF) submitted its Application (the Application) for a rate change to the Saskatchewan Rate Review Panel (the Panel) on February 3, 2012. The Application requested a 3.7% overall average increase in rates, with rate rebalancing affecting most vehicle classes. The major portion of this proposed rate increase revolved around the introduction of a proposed 3.5% Contingency Margin. The Application is attached as Appendix B.

An Order from the Minister for Crown Investments Corporation (the Minister) instructed the Panel to review SGI's Saskatchewan Auto Fund Rate Application and submit its recommendations by May 29, 2012. The Panel contracted the services of Eckler Ltd. and Kostelnyk Holdings Corp. (jointly, the Consultants) to serve as technical consultants to assist in reviewing the Application and supporting documentation. The Consultants' report is attached as Appendix C.

The Panel undertook a public consultation process that included public meetings in Saskatoon and Regina. Key stakeholders made presentations to the Panel and provided written submissions. The public was encouraged though advertisements to make submissions by mail, email, and telephone, and to attend the public meetings. SGI's website included a rate calculator, which further enhanced public dialogue.

The Panel's mandate is to evaluate each rate change Application and give the government an opinion on the reasonableness and fairness of the request, taking into account the interests of the customer, the Crown corporation and the public. After completing its evaluation, the Panel agreed with the analysis provided by its Consultants that there were substantial grounds for reducing the rate from that requested by the SAF, while still permitting the SAF to operate on a self-sustaining basis, and at the same time, ensuring stability and fairness in vehicle insurance rating.

The Panel agrees with its Consultants that the reasons given for including a Contingency Margin are not persuasive, since the SAF has a stated objective that rates should be set to break even over time, and the proposed Contingency Margin makes provision for additional revenue above best estimate expected costs. As well, the proposed Contingency Margin duplicates in part the current stated purpose of the Rate Stabilization Reserve (RSR).

The Panel further concurs with its Consultants that the natural growth in the provision for adverse deviations is a proper cost that should be recognized on a best estimate basis using past experience trend assumptions in setting indicated rates, and that the addition of an additional expense provision (perhaps called a "Break Even Margin"), based on SAF's estimate of the portion of the proposed Contingency Margin intended to account for the natural growth in the provision for adverse deviations, is reasonable.

The Panel shares its Consultants' concerns about residual conservatism (cautious assumptions about future costs, resulting in setting rates above what experience alone would otherwise suggest), particularly that they were unable to quantify the amount of conservatism through their Information Requests. The Panel agrees that the SAF should focus on preparing best estimate rate indications, and accepted the advice of its Consultants to consider the possibility of residual conservatism in SAF's rate indication when making its recommendation.

The Panel also shares the Consultants' concerns about the health of the Rate Stabilization Reserve (RSR), which is intended to protect SAF's customers from large rate changes following years with higher than expected claims costs and/or adverse financial events. The Panel believes it is crucial for the SAF to take action now to begin replenishing the RSR, but with a small loading, to avoid the rate shock the RSR serves to mitigate.

The Panel supports SAF's objective to achieve greater fairness through the rate rebalancing provisions in this Application, while further noting that 3 consecutive years of similar applications would be required for the SAF to achieve a satisfactory level of fairness across all customer classes. The Panel's recommendation on rate rebalancing is a first step toward ensuring that all customer classes pay the appropriate rate, and that cross-subsidization across customer classes is minimized.

The Panel also notes and congratulates the SAF for completing the Auto Fund Redevelopment Project, essentially on budget and on time. The Panel applauds the foresight of the SAF in recognizing that its existing systems would soon no longer be supportable, and would result in compromised service to the public. The new system has and will continue to result in reduced costs and efficiencies.

After reviewing the Application and supplementary information provided by SAF, input from the public, and technical analysis provided by its Consultants, the Panel makes the following recommendations (full commentary on each recommendation is located in Section 5 of this Report):

Recommendation #1: That the Saskatchewan Auto Fund implement an overall average increase of 0.6%, effective August 4, 2012, calculated as follows:

- 1.1% for the inclusion of an additional expense provision of 1.25% of premium on an undiscounted basis, perhaps called a Break Even Margin, to allow for the natural growth in the provision for adverse deviations;
- a judgmental reduction of 0.5% to account for residual conservatism in Saskatchewan Auto Fund's rate indication.

Recommendation #2: That the Saskatchewan Auto Fund implement an overall average rate surcharge of 1.0%, effective August 4, 2012, to replenish the Rate Stabilization Reserve, to be charged annually over a fixed two-year period, and to be identified separately on customer billings and in Saskatchewan Auto Fund's internal accounting.

Recommendation #3: That in future applications, the Saskatchewan Auto Fund focus on development of best estimate rate indications, and enhance the level of support and documentation for judgmental overrides of experience-driven assumptions.

Recommendation #4: That the capping levels proposed by the Saskatchewan Auto Fund be accepted, and that, to achieve fairness through Rate Rebalancing, the Saskatchewan Auto Fund be required to submit applications annually for each of the next two years following the period covered by this Application, regardless of whether an overall average rate change is indicated, and that the Saskatchewan Auto Fund file a fully developed implementation plan with yearly transition milestones/targets for clear-rated vehicles and conventionally-rated vehicles, together with the detailed financial impacts for each class, at the next rate application.

Recommendation #5: That the Saskatchewan Auto Fund augment its Capital Management Policy by including an officially defined and stated purpose for the Rate Stabilization Reserve, and that such purpose specifically exclude use of the Rate Stabilization Reserve to fund capital projects, and that the Capital Management Policy be included in the Panel's Terms of Reference for future applications.

Recommendation #6: That the Saskatchewan Auto Fund provide the Panel with an assessment from its external auditor with respect to the Saskatchewan Auto Fund assuming responsibility for the Driver Education program from the Province, confirming the consequences, if any, under International Financial Reporting Standards to the Rate Stabilization Reserve, for the next rate application.

Recommendation #7: That the Saskatchewan Auto Fund review the Future Minimum Filing Requirements proposed by the Consultants and provide the Panel with its comments in a timely manner.

Recommendation #8: That the Saskatchewan Auto Fund, in its upcoming Stakeholder Insurance Product Offering Review, consider the following topics, which were raised during the Panel's public consultations:

- motorcycle safety and driver training
- physical damage deductible levels
- premiums for seasonal use vehicles, including short duration permitting options
- proper use for vehicles licenced as farm vehicles
- the Safe Driver Recognition and Business Recognition programs
- review of risk classifications for all vehicles, in particular, urban and rural taxis.

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1.0 Role of the Saskatchewan Rate Review Panel

1.1 Authority

Through an Order-in-Council dated January 1, 2010, the Minister Responsible for Crown Investments Corporation (the Minister) received continued authority to reappoint the Saskatchewan Rate Review Panel (the Panel) as a Ministerial Advisory Committee. The Panel's mandate states that it shall:

(a) *conduct a review and provide an opinion of the fairness and reasonableness of proposed Crown corporation rate changes, referred to the Panel by the Minister of Crown Investments Corporation; and*

(b) *incorporate as part of its mandate specific terms of reference for particular Crown corporation rate change reviews that may be attached by further Minister's Order.*

Whether in the original Order-in-Council establishing the Panel (437/2000 dated July 27, 2000), or in the Terms of Reference for particular reviews, the Panel has always been instructed to consider: "…the interests of the customer, the Crown corporation, and the public."

The mandate of the Panel extends to three Crown corporations in Saskatchewan – SaskEnergy, SaskPower and SGI's Saskatchewan Auto Fund. Serving as an advisory body to the Minister Responsible for Crown Investments Corporation, the Panel provides independent advice on rate proposals from the above-noted corporations. The final decision about these proposals continues to rest with the Saskatchewan government.

1.2 Members of the Panel

Through the January 1, 2010 Minister's Order, the following members were appointed to serve on the Saskatchewan Rate Review Panel:

Chair	Kathy Weber	Saskatoon
Vice-Chair	Bill Barzeele	Little Bear Lake
Members	Steve Kemp	Regina
	Delaine Barber	Weyburn
	Lyle Walsh	Yorkton
	Daryl Hasein	Biggar
	Burl Adams	Kelvington

1.3 Panel's Terms of Reference

The Saskatchewan Rate Review Panel is requested to conduct a review of the SAF's request for an overall average rate increase of 3.7%, with rate rebalancing, to be implemented August 4, 2012.

Cabinet may implement any rate change adjustment on an interim basis, pending receipt of the Panel's recommendation(s).

The Panel shall function within its mandate and operational terms of reference as specified in the Minister's Order dated January 1, 2010. The Panel shall provide an opinion on the fairness and reasonableness of the SAF's proposed rate changes, having consideration for the following:

- The interests of the Crown Corporation, its customers and the public;
- Consistency with the Crown Corporation's mandate, objectives and methodologies;
- Relevant industry practices and principles; and
- The effects of the proposed rate change on the competitiveness of the Crown Corporation related to other jurisdictions.

In conducting the review of the proposed rate changes the Panel will consider the reasonableness of the proposed changes to SAF rates in the context of:

a) the Saskatchewan Auto Fund's mandate to operate on a self-sustaining basis over time;
b) the objective to maintain adequate capital within a Rate Stabilization Reserve to serve as a cushion to protect customers from large rate increases;
c) the impact of rising claims costs; and
d) the objective of ensuring stability and fairness in vehicle insurance rating such that each vehicle class pays sufficient premiums to cover its anticipated claim costs to minimize cross subsidization.

The Panel shall consider the following parameters as given:

a) the compulsory insurance coverage provided by the Saskatchewan Auto Fund through its legislative mandate;
b) the Saskatchewan Auto Fund is a public account for motorists with no profit component required in pricing the product;
c) the Saskatchewan Auto Fund Capital Management Policy, which requires a Minimum Capital Test ratio of between 75% and 150%;
d) the existing program parameters of the Safe Driver Recognition Program and the Business Recognition Program;
e) the vehicle risk groups used by the Saskatchewan Auto Fund; and,
f) the operating policies and procedures used by the Saskatchewan Auto Fund.

The Minister's Order for this review called for the Panel to complete its work no later than May 29, 2012.

2.0 Saskatchewan Auto Fund Rationale for the Application

The Panel received the Saskatchewan Auto Fund's proposal for rate adjustment (the "Application") on February 3, 2012.

The Saskatchewan Auto Fund is administered by SGI, and provides basic vehicle insurance to all residents of Saskatchewan, with no profit component in pricing coverage. Saskatchewan Auto Fund basic coverage includes Personal Injury coverage, Third Party Liability protection and Physical Damage coverage.

As part of its basic service, the SAF also provides:

- licencing for drivers
- registration for vehicles and trailers
- driver examinations and education
- driver and vehicle fitness programs
- carrier and safety audit programs
- funding for accident prevention and traffic safety initiatives.

According to the Saskatchewan Auto Fund there are 3 main trends driving its Application for a 3.7% overall average rate increase. These trends include:

- Higher income replacement benefits for vehicle collision victims, caused by rising wage levels in the province;
- Higher collision repair costs for both parts and labour; and
- Lower anticipated investment income from declining bond yields.

The major portion of the 3.7% rate request revolves around the introduction of a proposed Contingency Margin of 3.5%. This Application also includes rate rebalancing (a process designed to ensure each class of vehicles is paying sufficient premium to cover its claim costs), which takes into account collision frequency and severity, including damage, injury and liability costs for each class of vehicle. Rate rebalancing means that individual customers' rates may change by more or less than the average increase requested.

The SAF has requested that the proposed rate adjustment take effect August 4, 2012.

3.0 Review Process for the Saskatchewan Auto Fund Application

3.1 Consultants

Eckler Ltd. and Kostelnyck Holdings Corp. were engaged by the Panel as independent technical advisors to review the fairness and reasonableness of the SAF's proposed rate change with rate rebalancing, and to provide recommendations regarding the proposed rate changes, the SAF's Capital Management Policy and its Minimum Capital Test, consistent with the Terms of Reference for the Panel's review of the Application.

Myron Kostelnyk of Kostelnyk Holdings Corp. has served as technical consultant for the Panel on SAF applications since 2005, as well as several SaskEnergy commodity and delivery rate applications, and 3 SaskPower reviews. He has also advised the Manitoba Public Utilities Board on reviews of Manitoba Public Insurance for the past 15 years.

Brian Pelly of Eckler Ltd. has worked with the Panel on three previous SAF reviews, and has been the actuarial advisor to the Manitoba Public Utilities Review Board for its review of annual applications from Manitoba Public Insurance since 1998. Brian is a Fellow of the Canadian Institute of Actuaries and a Fellow of the Casualty Actuarial Society.

As part of the review process, the Consultants, on behalf of the Panel, filed two rounds of Information Requests with the SAF, and had discussions with SAF representatives seeking clarification regarding the Application and supplementary information. The Panel also engaged the services of a technical writer to assist in preparing this report.

3.2 Public Consultations

The Panel invited public comments as part of its review of the Saskatchewan Auto Fund's rate Application. The public consultation process included:

- Public meetings
- Submissions received by mail;
- Online messages received through the Panel's website;
- Messages received directly through the Panel's email address; and
- Messages received through the Panel's toll-free voice mailbox.

The Auto Fund rate Application received news coverage immediately after the original Application was announced. All methods for public input were advertised in daily and select weekly newspapers, on Shaw Cable and Access Communications, and on select radio stations. The Panel developed posters that were placed in SGI offices, brokerage offices and select businesses throughout the province. Public meetings regarding the Application were held in Saskatoon on March 28 and Regina on April 2.

Copies of the Application were available at SGI's offices and on the Panel's website. SGI also provided a rate calculator at its website showing the effect of the proposed rate changes on each vehicle class, which created extra dialogue among the public and assisted in the review process.

The Panel is encouraged by the 76 communications received from organizations and individuals during the review process, a significant increase over previous reviews. Where possible, every submission and comment received a response, and in the case of emails, for the first time in this Panel's memory, some individuals responded again, indicating the beginning of a dialogue. In their report, the Consultants note that the Panel has made significant strides since the last Application in encouraging public input to the review process. These communications have helped to inform the recommendations and observations in this report. The following table summarizes public participation in this review:

Saskatchewan Auto Fund Public Contact	
Messages through email/website	28
Letters received by mail	1
Letters and presentations on behalf of organizations	6
Toll-free voice mailbox	5
Attendance at public meetings (including 2 formal presentations from individuals)	36
Total number of communications with the Panel	76

Organizations such as the Consumers Association of Saskatchewan, Greater Saskatoon Chamber of Commerce, taxi companies in Regina and Saskatoon, a motorsport dealers association, a motorcycle industry council and individual motorcyclists all made submissions at the public meetings (a complete listing is found below). A few key themes emerged from the submissions made by motorcyclists, including the importance of encouraging the use of protective gear, promoting safe and defensive driver training and exploring other alternatives to simply increasing rates. One motorcyclist, for example, suggested that before rates for this class of transportation are raised, *"… more study is required into the nature of motorcycle accidents and (the) non-motorcycle driver. How many (accidents) are caused by evasive action on the part of the motorcyclist? How many of them are caused by inattentive drivers who are only looking for two headlights (i.e. a car, truck, van) on the road?*

Another motorcyclist questioned how many drivers there are who have multiple accidents, yet continue to drive and get insurance. *"Start insuring the driver and not the vehicle,"* he suggested. Another submission observed that, *"SGI's dramatic rate increases do not target unsafe motorcycle drivers, or reduce single or multiple-vehicle accidents that may involve motorcycles. Instead, they will simply collect more to pay out for accidents, or take some motorcycles off the road (regardless of the skill or safety of the operator.)*

Due to the quantity of input from the Public regarding the proposed rate hikes for motorcycles, particularly in the Sport category, the Panel requested that the SAF provide a comparison of SAF rates (both current and proposed) with those of Manitoba and

British Columbia. The SAF's complete response is posted on the Panel's website, however, the section with respect to Sport bikes follows:

Year	Make	Model	Declared Value	SGI – Current	SGI – Proposed	Average MPI Current	Average ICBC Current
2008	HONDA	CBR125R	$2,250	$287	$367	$1,242	$768
2004	YAMAHA	YZF R6	$4,900	$1,029	$1,337	$1,978	$1,371
2007	HONDA	CBR600RR	$7,175	$1,090	$1,416	$1,978	$1,535
2008	SUZUKI	GSX-R750	$8,350	$1,149	$1,493	$2,119	$1,613
2004	YAMAHA	YZF R1	$6,200	$1,110	$1,443	$1,978	$1,641
2007	SUZUKI	GSX-R1000	$8,850	$1,176	$1,529	$2,119	$1,786

In its recommendation #8, the Panel suggests that the Saskatchewan Auto Fund include the issues around motorcycle rates for discussion during its upcoming review of Insurance Product Offerings. The Panel also welcomes the graduated licence program for motorcyclists that the SAF has already initiated, and looks forward to learning more about the effects of this program as meaningful data becomes available.

During the public meetings, representatives of taxi companies addressed what they regard as weaknesses in the Business Recognition program. For example, businesses that are required to participate in the program suffer the consequences when there are accidents, but the driver does not. One taxi operator suggested the program should to take into consideration a longer time period before imposing surcharges for at-fault accidents.

One individual raised a concern over truck operators licencing their vehicles as farm trucks, while operating them as commercial trucks, giving them an unfair advantage and creating potential safety hazards. This concern was echoed in detail in a submission from the Saskatchewan Trucking Association.

During the review, several individuals approached members of the Panel to discuss the possible impact on rates by raising the deductible from the current $700 level. As a result of this feedback, the Consultants asked for the impact on rates of raising the deductible from $700 to $900 in an Information Request. SAF's response, in Second Round IR #48, indicated this change would reduce the rate from the requested 3.7% down to 1.2%.

The Panel expresses its appreciation to the organizations and individuals who took the time to comment on the Application. These submissions and comments are posted on the Panel's website, and include:

- A.M.I.R. Taxi
- Regina Cabs/Premier Taxi
- United Group of Companies
- Radio Cabs
- Greater Saskatoon Chamber of Commerce
- Consumers Association of Saskatchewan
- Motorcycle and Moped Industry Council
- Saskatchewan Powersport Dealer Association

- Saskatchewan Trucking Association
- Individual and group submissions from motorcyclists

The Panel also received 5 phone calls, two of which commented on motorcycle insurance rates. The third dealt with SAF's policy on payment for personal injuries to truckers and the other callers were generally opposed to a rate increase, wanted to see greater efficiency in SAF's operations, and requested information on the date and location of public meetings.

The Panel thanks the SAF for making a presentation on its Application at each of the public meetings and for responding to questions at the meetings. The Panel also thanks the SAF for responding to specific inquiries when requested to do so by the Panel during the review process.

4.0 Summary of the Consultants' Report

Eckler Ltd. and Kostelnyk Holdings Corp. served as the technical consultants for the review process. After a detailed review that included an examination of the SAF Application, two rounds of Information Requests, individual discussions with SAF to clarify specific points, a review of public comments to the Panel, including attending the public meeting in Regina and reviewing the transcript of the public meeting in Saskatoon, and several meetings and conference calls with the Panel during the review process, the Consultants submitted their final report to the Panel on May 23, 2012. It is attached as Appendix C.

A summary of the Consultants' technical assessment of the Application includes the following:

4.1 Contingency Margin

The 2012 Application is the first to include a Contingency Margin. The SAF indicated that the purpose of its proposed Contingency Margin is to generate additional revenue to offset the loss from any increase in the provision for adverse deviations, and to protect against the possibility that one or more of the rating assumptions are incorrect, leading to inadequate rates.

The Consultants describe the proposed Contingency Margin as being in conflict with the break even objective in setting Auto Fund rates, and a departure from the standard actuarial practice in the context of best estimates. The Consultants state that they do not accept including a Contingency Margin that would provide additional revenue above best estimates of expected costs, particularly since one of the objectives of the SAF is to break even over time. In their words:

"We are not persuaded that a contingency margin is needed to protect against the adverse potential consequences arising from the uncertainty in setting assumptions, but rather that is exactly one of the proper purposes of the Rate Stabilization Reserve."(page 68)

The Consultants accept that for the SAF in its current state, recognizing the natural growth in costs related to the provision for adverse potential deviations is a proper cost that should be recognized on a best estimate basis, to be consistent with the Saskatchewan Auto Fund's break even objective. They recommend including an additional expense provision, perhaps called a Break Even Margin, which they estimate would be 1.25% of premium on an undiscounted basis, based on SAF responses to Second Round Information Request #13a. The Consultants further estimate this change would reduce the overall change in average rate level from an increase of 3.7% down to about an increase of 1.1%. (First Round Information Request #48.)

4.2 Capital Management Policy

In its 2009 review, the Panel recommended the SAF establish and implement a Capital Management Policy (CMP) to address situations where the Minimum Capital Test (MCT) for the Rate Stabilization Reserve (RSR) falls significantly below or above the target level of the range set out in the policy. The Minimum Capital Test is an industry regulatory solvency test prescribed by the Office of the Superintendent of Financial Institutions Canada (OSFI), with alteration as prescribed by the SAF Board of Directors, to determine the appropriate level of funds in the RSR.

The SAF policy states that if the MCT is below 75% when calculated on a 12-month rolling average, a proposal is presented to the SAF Board of Directors on replenishing the RSR. The policy also states that if the MCT is above 150% when calculated on a 12-month rolling average, the Directors will receive a proposal for a customer rebate. The policy has set the target level for the RSR at 112.5%, the mid-point within the target range.

The Consultants note there is a risk that the Saskatchewan Auto Fund's Capital Management Policy will fall out of step with the MCT it uses to measure the adequacy of capital it has in its RSR each time the OSFI changes the MCT calculation. They note OSFI has changed the MCT calculation in 2012, and will continue to do so in the future.

"On each occasion that the MCT calculation is changed it calls into question whether or not the change represents an improvement in the relative measurement of capital adequacy for SAF, in the context of the Capital Management Policy. If it does represent such an improvement, then possibly the MCT target range needs to be reassessed in the light of the new information the test result provides. If it does not represent such an improvement, then possibly the target MCT range needs to be reassessed to correct for the distortion caused by the test change, or alternatively, the test change is rejected and the former MCT calculation is carried forward." (page 69)

The Consultants recommend that the SAF provide explicit documentation showing how the CMP would be affected by any actual or known planned changes to the MCT, as a regular part of its rate applications. (page 69)

The Consultants further recommend that an officially defined and stated purpose for the RSR be added to the Capital Management Policy. They do not expect funding for projects such as the Auto Fund Redevelopment Project to be an intended purpose of the RSR. Further, they recommend bringing review of the CMP within the Panel's Terms of Reference in future applications. (page 69)

4.3 Proposed Change in Average Rate Level

The Consultants state their concern over what they call "*possible residual conservatism"* built into the proposed overall average 3.7% rate increase. In this context, "conservatism" refers to making cautious assumptions about future costs, setting rates above what experience alone would otherwise suggest. The Consultants point out that the evidence provided for the selection of future trend assumptions were mostly judgmental overrides of corresponding past trend assumptions. (page 69)

The Consultants make two recommendations to the Panel (page 70) regarding possible residual conservatism in setting the rate level:

- that the Panel, in making its recommendation, consider the possibility of conservatism in SAF's rate request; and
- that the SAF focus on the development of best estimate rate indications, and enhance the level of support and documentation for judgmental overrides of experience-driven assumptions in future rate proposals.

4.4 Rate Stabilization Reserve

The Rate Stabilization Reserve (RSR) exists to ensure rate stability and consistency, so that customers are not subject to ongoing price fluctuations or immediate large rate increases, based on one or more significant adverse insurance events. The RSR is used when hail storms, severe winter conditions and adverse financial events abnormally affect claims costs.

The Consultants observe that while the current state of the RSR does not call for action under SAF's Capital Management Policy, *"The evidence is strong that it will be only a short amount of time before that policy will be triggered by a 12-month rolling average MCT ratio below 75%."* (page 70)

Given the typical frequency with which SAF rate applications are brought forward, the Consultants recommend, *"…some modest level of RSR replenishment loading for a fixed one or two year period, which if expressed as a % of premium seems to fairly make each individual's contribution to rebuilding the RSR commensurate with the risk they bring to the insurance process. The size of the loading ought to be small, to avoid causing exactly what the RSR is intended to mitigate, i,e., rate shock."* (page 70)

With respect to any RSR replenishment loading, the Consultants further recommend, *"…that SAF be instructed to segregate the loading in its accounting and its communications with policyholders, to enhance transparency."* (page 70)

4.5 Rate Rebalancing

Rate rebalancing is the process of setting proposed rates to minimize cross-subsidization across vehicle classes so that rates reasonably reflect the claims experience of each class of vehicles, while also avoiding undue rate shock. In this Application, SAF proposes to cap rate adjustments at plus/minus 15% for customers with an annual premium above $1,000. For annual premiums less than $1,000, SAF recommends dollar caps ranging from $25 to $150. Of the slightly more than one million insured vehicles, almost 220,000 will either receive a dollar or percentage cap under this Application.

The Consultants state that the rate capping philosophy in the Application is fairly applied, and recommend that the Panel accept it, while noting that the exception is for sport motorcycles, where higher capping levels are selected. They observe that sport motorcycles continue to show a *"...very large rate need, and in the absence of any exception to the capping rule, concerns over unfair cross subsidization may otherwise arise."* (page 70)

To support the rate rebalancing process, the Consultants recommend (pages 70-71):

- *"…the Panel to urge the Minister to encourage or even require the SAF to bring forward rate proposals with rate rebalancing on an annual basis to improve the pace by which the SAF is seeking to bring each vehicle's rate within a small tolerance of its rate indication*, and

- *"…in the interest of fairness in rating under the Safe Driver Recognition and Business Recognition programs, …to bring review of these programs within the Panel's Terms of Reference in reviewing future applications."*

4.6 Technical Improvements

The Consultants applaud the progress made since the last application in introducing technical improvements that assisted in the analysis of the Application. They offer suggestions for future consideration in three areas:

- The methodology for selecting the discount rate of interest curve;
- The possibility of developing distinct rate levels for tort and no-fault coverage; and
- The possibility of extending the use of credibility and large loss procedures to enhance the stability of the classification ratemaking procedures.

4.7 Auto Fund Redevelopment Project

In 2005, SAF began developing a new customer information system called the Auto Fund Redevelopment Project (AFRP). The system gives customers online access to more information and the ability to complete some transactions online, while also reducing SAF staffing, maintenance and other operational costs. The project was implemented in phases, with the final phase launched in June 2010. SAF now offers its customers a single point of access for services, and an improved platform for launching future products.

The Consultants state that the final $36 million cost of the AFRP is reasonable, given the period of time since the project cost was estimated, and the complexity of information technology projects. They consider that the project was completed in a prudent and expeditious manner, and that the benefits achieved will match or exceed the initial estimates. They add that the Panel, *"…will expect the SAF to track and quantify the nature of all benefits flowing from the AFRP, and to the extent practical track them apart from any other efficiencies resulting from normal operational overviews."* (page 72)

The Consultants note the SAF's contention that its revenue stream has improved dramatically as a result of the AFRP, and that other jurisdictions are expressing interest in using it. The Consultants recommend that the SAF be required to inform the Panel of any developments in this regard, including any resulting revenues and their impact on rate requirements. (page 72)

4.8 Traffic Safety

The SAF delivers a range of traffic safety programs, focusing on a combination of education, engineering and enforcement to reduce the amount of vehicle accidents. The SAF is currently in a five-year traffic safety program that runs until 2015, with a focus on seven main areas:

- Impaired driving;
- Vehicle collisions involving wildlife;
- Distracted driving;
- Seatbelt education, use and enforcement;
- Speed management;
- Intersection safety; and
- New driver accidents.

The SAF covers the entire cost of its traffic safety programs, which amount to between 2% and 3% of its premium income, including $21 million budgeted for 2012. The Consultants recommend the Panel require the SAF to provide specific details of actual cost savings, as well as a statistical analysis of each program's effectiveness, as part of the minimum filing requirements in all future applications.

The Consultants note that the SAF assumed responsibility for Driver Education from the Province in 2011, with annual costs increasing by $4.9 million in 2012, but with no commensurate revenue contribution from the Province. The Consultants' view is that, *"…unlike traffic safety initiatives specifically geared towards insured motorists, driver education benefits all Saskatchewan citizens, and this funding change moves all costs for this program to the drivers insured by SGI."* (page 74)

The Consultants state that, *"Depending on the basis under which the SAF assumed this responsibility, it could represent an onerous contract under International Financial Reporting Standards, the consequence of which could be very significant to the level of the RSR. We recommend that the Panel request SAF to provide the assessment of its external auditor in this regard, with the next rate Application."* (pages 73-74)

4.9 Cost Allocation

The Consultants are satisfied that SGI's allocation of costs to SAF activities is satisfactory, generally complying with industry cost allocation methodologies, and that the SAF does not unduly subsidize SGI's non-regulated companies.

4.10 OM&A Expenses

Operating, Maintenance and Administrative (OM&A) expenses include salaries, infrastructure costs and support system costs, which account for 6.2% of total SAF costs. Loss Adjusting Expenses, Administrative Expenses and Traffic Safety expenses are included. The Consultants note that OM&A is one area where the SAF has control over its costs.

The total OM&A costs for 2011 increased by $13.7 million (11.3%) to an estimated $137.8 million in 2012. Of this increase, $5.3 million is attributable to Traffic Safety and primarily to the assumption of the Driver Education program.

Regarding salaries, wages and benefits, the Consultants state that the budgeted addition for 2012 of 7.32 full time equivalent employees, plus a 2.20% increase in wages and salaries, and a 2.58% increase in pension expenses are reasonable. They also accept a budgeted increase of $2.7 million for traffic safety programs as worthwhile.

The Consultants note that, *"While we are unable to assess the reasonableness of the remaining $0.9 million budgeted for systems, human resources and marketing, our view is that some allowance for such items is prudent, but the amount may be debatable.*" (page 76) Additionally, they state, *"We were unable to assess the necessity of the approximate $300,000 remaining in other expenditures."* (page 77)

The Consultants note that SAF commissioned a study by the Ward Group, which shows SAF to be above comparable industry results in most measures. The Ward Report indicates that Claims Service and Human Resources are two areas that appear to require improvement, the Consultants note, and that SAF has investigated to understand the matter and identify opportunities for improvement.

In other assessments under OM&A, the Consultants:

- found projected capital and building rehabilitation costs to be reasonable;
- noted that the 2012 decrease in data processing costs was consistent with the original expectations of the Auto Fund Redevelopment Project;
- observed that the increase of $1.8 million in issuer bank charges is linked to customers' greater use of credit cards for online registrations.

The Consultants made two additional recommendations to the Panel, that it require the SAF:

- to identify in more detail all surpluses and deficiencies flowing to the RSR; and
- in preparing its budgets, to include a discrete internal efficiency/productivity factor of 0.5%, which would be a percentage of total OM&A costs, to offset costs attributed to inflationary pressures, in line with the practice of the other Crowns which the Panel reviews.

The Consultants found that the SAF's Investment Policy is being properly administered, employing an independent advisor who manages the investment portfolio and applies the policy on a day-to-day basis.

4.11 Future Minimum Filing Requirements

The Consultants identify 23 recommended Minimum Filing Requirements for the next Application, to provide more guidance to the SAF and to identify specific areas where additional information is needed.

4.12 SAF Stakeholder Insurance Product Offering Review

The Consultants welcome the Saskatchewan Auto Fund's initiative to hold a product review in 2012 involving all stakeholders. Based on the information in the rate Application and feedback from the public during the review, the Consultants recommend the product review include at least six specific subject areas for discussion:

- Motorcycle safety and driver training
- Physical damage deductible levels
- Premiums for seasonal use vehicles, including short duration permitting options
- Proper use classification of Farm vehicles
- Safe Driver Recognition and Business Recognition programs
- Review of risk classification for all vehicles, in particular urban and rural taxis.

The Consultants note that the Panel will be a stakeholder in this product review.

5.0 Panel Recommendations and Analysis

The Saskatchewan Rate Review Panel, in completing its review and analysis, conferring with its consultants, and considering public input regarding the Application, is satisfied that the following recommendations take into account the interests of the customer, the Crown corporation and the public.

5.1 Rate Change Recommendation

Recommendation #1: That the Saskatchewan Auto Fund implement an overall average increase of 0.6%, effective August 4, 2012, calculated as follows:

- **1.1% for the inclusion of an additional expense provision of 1.25% of premium on an undiscounted basis, perhaps called a Break Even Margin, to allow for the natural growth in the provision for adverse deviations; and**
- **a judgmental reduction of 0.5% to account for residual conservatism in Saskatchewan Auto Fund's rate indication.**

Recommendation #2: That the Saskatchewan Auto Fund implement an overall average rate surcharge of 1%, effective August 4, 2012, to replenish the Rate Stabilization Reserve, to be charged annually over a two-year period, and to be identified separately on customer billings and in Saskatchewan Auto Fund's internal accounting.

Recommendation #3: That in future applications, the Saskatchewan Auto Fund focus on development of best estimate rate indications, and enhance the level of support and documentation for judgmental overrides of experience-driven assumptions.

Contingency Margin

The Application requested a 3.7% overall average increase in rates, with rate rebalancing affecting most vehicle classes. The major portion of this proposed rate increase revolved around the introduction of a proposed 3.5% Contingency Margin.

SAF stated that it selected the 3.5% level for its proposed Contingency Margin based on the level of risk as measured by the provisions for adverse deviation (PfAD), an actuarial term referring to a risk management tool used by the insurance industry. The SAF also indicated that the purpose of the proposed Contingency Margin is to generate additional revenue to offset the loss from any growth in PfAD, and to protect against the possibility that one or more of the rating assumptions in the Application are incorrect, resulting in inadequate rates. (First Round IR, #38)

The Consultants state on page 68 of their report that standard actuarial practice is to develop rates based on best estimates, and anything other than a zero PfAD in an indicated rate is a departure from a best estimate. The Consultants further state that one of the stated objectives of the SAF in determining premium rates is that they should be set to break even. Therefore, the Consultants add, "*…we do not accept the inclusion of a contingency margin that makes provision for additional revenue above best estimated costs. We are not persuaded that a contingency margin is needed to protect against the adverse potential consequences arising from the uncertainty in setting assumptions, but rather that this is exactly one of the proper purposes of the Rate Stabilization Reserve.*" (page 68)

The Panel agrees with its Consultants that the reasons given for including a Contingency Margin are not persuasive.

The Panel further concurs with its Consultants that the natural growth in the PfAD for the SAF, in its current state of evolution, is a proper cost that should be recognized on a best estimate basis in setting indicated rates, to be consistent with the objective of setting break even rates. Therefore, the Panel also agrees with the Consultants' recommendation to include a "Break Even Margin", based on SAF's estimate (2nd Round IR, #33a) of 1.25% of premium on an undiscounted basis as the portion of the proposed Contingency Margin intended to account for the natural growth in the PfAD. Accordingly, the Consultants recommended, and the Panel concurred with, a reduction in the average rate level from 3.7% to 1.1%. (page 68)

Replenishing the RSR

The SAF's Capital Management Policy (CMP) uses a common industry tool, the Minimum Capital Test (MCT), to monitor the financial health of its Rate Stabilization Reserve (RSR). The SAF's Capital Management Policy has adopted a target range of from 75% to 150%, with a mid-point target of 112.5%.

The Panel shares the Consultants' concerns about the health of the RSR, which is intended to protect SAF's customers from large rate changes following years with higher than expected claims costs and/or adverse financial events. Currently, the RSR is at or near the low end of the MCT target range set out in SAF's CMP, and the evidence is strong that in the very near future, the 12-month rolling average MCT ratio will fall below 75%.

The Panel believes it is crucial for the SAF to take action now to begin replenishing the RSR, but with a small loading, to avoid the rate shock that the RSR serves to mitigate. The Panel held in depth discussions with its Consultants regarding the appropriate level for this replenishment charge, within a range of 1% to 1.5%, before recommending this RSR replenishment loading be set at 1% of premium in each of the next two years.

Conservatism in Rate Setting

The Panel shares its Consultants' concern about possible residual conservatism that is built into the overall 3.7% change in rate level. In this context, "conservatism" refers to cautious assumptions about future expenses, above what experience alone would otherwise suggest. The Consultants were unable to obtain sufficient information from

SAF through Information Requests to quantify the extent of any such conservatism, noting that, *"The available documentation shows that the selection of future frequency and severity assumptions are dominated by mostly judgmental overrides of corresponding trend assumptions, which are in turn mostly based on an analysis of experience. The evidence provided in support of these future trend selections was mostly judgmental, with limited statistical evidence provided. The overall indicated change in average rate level is quite sensitive to these assumptions, as evidenced by the restatement to use past trends as future trends for three significant coverages for the CLEAR-rated and Heavy classes of vehicles, which was estimated to reduce the overall indicated change in average rate level from +3.7% down to about +1.6%."* (page 69)

The Consultants add that this conservatism could also arise in the forecasted levels of certain non-claims related expenses. They recommended the Panel consider the possibility of residual conservatism in the Saskatchewan Auto Fund's rate indication when making its recommendation, and the Panel agrees. The Panel also agrees that the SAF should in the future focus on preparing best estimate rate indications.

After extensive discussions involving members of the Panel and its Consultants, the Panel established 0.5% as a reasonable best estimate for the amount of conservatism built into the rate request. Factoring this into the rate recommendation reduced the overall average rate level from 1.1% down to 0.6%.

5.2 Rate Rebalancing

Recommendation # 4: That the capping levels proposed by the Saskatchewan Auto Fund be accepted, and that to achieve fairness through Rate Rebalancing, the Saskatchewan Auto Fund be required to submit applications annually for each of the next two years following the period covered by this Application, regardless of whether an overall average rate change is indicated, and that the Saskatchewan Auto Fund file a fully developed implementation plan with yearly transition milestones/targets for clear-rated vehicles and conventionally-rated vehicles, together with the detailed financial impacts for each class, at the next rate application.

The SAF states that the objectives of the rate rebalancing provisions in this Application are to achieve greater fairness in the rates charged to customers, and the Panel agrees. One of the Terms of Reference for this review specifically directs the Panel to consider, *"…the objective of ensuring stability and fairness in vehicle insurance rating such that each vehicle class pays sufficient premiums to cover its anticipated claim costs to minimize cross subsidization."*

The following table from page 4 of the Consultants' report outlines the rate capping proposal.

Dislocation Capping	
Current Annual Rate Range	**Maximum Cap**
$1-50	$25
$51-100	$50
$101-250	$75
$251-500	$100
$501-750	$125
$751-1,000	$150
$1,000 or greater	15%*
• Exception to above caps is the cap proposed for the sport motorcycle classification which is at 30% versus the 15% maximum for other classifications	

Of the slightly more than one million insured vehicles, almost 220,000 either received a dollar or percentage cap under this rate capping proposal.

The Panel supports SAF's objective to achieve greater fairness through the rate rebalancing provisions in this Application, while further noting (1st Round IRs #6 and #9) that three consecutive years of similar applications with rebalancing provisions would be needed for the SAF to bring 95% of vehicles to within 5% of their appropriate rate, which it considers necessary to achieve a satisfactory level of fairness across all customer classes.

The Panel agrees with the SAF that it would be prudent to rebalance rates every year to ensure fairness in vehicle rating. The panel does not, however, agree with the SAF that other priorities or availability of resources should interfere with the rebalancing proceeding on an annual basis, since this issue is of critical importance to fairness for Saskatchewan vehicle insurers.

The Panel's recommendation on rate rebalancing over the next 2 years is a first step toward ensuring that all customer classes pay the appropriate rate, and that cross-subsidization across customer classes is minimized. The Panel also recommends the SAF file a fully developed implementation plan with yearly transition milestones/targets for clear-rated vehicles and conventionally-rated vehicles, together with the detailed financial impacts for each class at the next rate application.

The obvious exception to the uniform application of the proposed capping is for sport motorcycles, which continue to show a very large rate need. The Panel received several submissions from motorcycle industry associations and individual motorcyclists regarding the proposed cap of 30%, or $45 per month. Even with this proposed increase, the SAF indicates that the motorcycle class would still be paying less than the indicated rate. These items are addressed further in Section 3.2, Public Consultations. The Panel welcomes future discussions between SAF and representatives of motorcycle industry associations and individuals to investigate possible alternative solutions to this issue, and have included motorcycle safety and driver training as potential items for discussion in the SAF's review of its insurance product offerings, in Recommendation #8.

5.3 Purpose of the Rate Stabilization Reserve

Recommendation #5: That the Saskatchewan Auto Fund augment the Capital Management Policy by including an officially defined and stated purpose for the Rate Stabilization Reserve, and that such purpose specifically exclude use of the Rate Stabilization Reserve to fund capital projects, and that the Capital Management Policy be included in the Panel's Terms of Reference for future applications.

As stated previously, the purpose of the Rate Stabilization Reserve is to protect Saskatchewan Auto Fund customers from large rate changes caused by severe weather conditions and/or adverse financial events. The Panel also agrees with its Consultant that it is important to formalize the purpose of the RSR in the CMP.

In its response to 1st Round Information Request #43, the SAF indicated that one of the purposes of the RSR is to fund system upgrades such as the recent Auto Fund Redevelopment Project. While the project has resulted in benefits for customers and contributed savings to the SAF, the Panel considers the AFRP as a one-time opportunity to invest in efficiencies and productivity improvements at a time when the RSR was in a surplus position. The Panel does not regard the RSR as a regular source of funding for such projects. A surplus in the RSR would normally indicate that customers are being overcharged, and that a rebate is in order.

5.4 Driver Education Program Impact on the RSR

Recommendation #6: That the Saskatchewan Auto Fund provide the Panel with an assessment from its external auditor with respect to the Saskatchewan Auto Fund assuming responsibility for the Driver Education program from the Province, confirming the consequences, if any, under International Financial Reporting Standards to the Rate Stabilization Reserve, for the next rate application.

In 2011, the SAF assumed responsibility for Driver Education from the Province, resulting in a significant increase in expenses, but with no corresponding revenue contribution from the Province. The Consultants state that, *"Depending on the basis under which the SAF assumed this responsibility, it could represent an onerous contract under International Financial Reporting Standards, the consequence of which could be very significant to the level of the RSR."* The Panel, on the advice of its Consultants, recommends requesting an external auditor's assessment of the consequences of this change, if any, under International Financial Reporting Standards to the RSR, for the next application.

5.5 Minimum Filing Requirements

Recommendation #7: That the Saskatchewan Auto Fund review the Future Minimum Filing Requirements proposed by the Consultants and provide the Panel with its comments in a timely manner.

The Panel supports augmenting the Minimum Filing Requirements to enhance the quality and amount of information filed with the Application, so that fewer Interrogatories are necessary during the review process. This makes the review process more efficient, less complex and less time-consuming for all parties, including the SAF.

5.6 Stakeholder Insurance Product Offering Review

Recommendation # 8: That the Saskatchewan Auto Fund, in its upcoming Stakeholder Insurance Product Offering Review, include consideration of at least the following topics for review:

- **motorcycle safety and driver training**
- **physical damage deductible levels**
- **premiums for seasonal use vehicles, including short duration permitting options**
- **proper use for vehicles licenced as farm vehicles**
- **the Safe Driver Recognition and Business Recognition programs**
- **review of risk classifications for all vehicles, in particular, urban and rural taxis.**

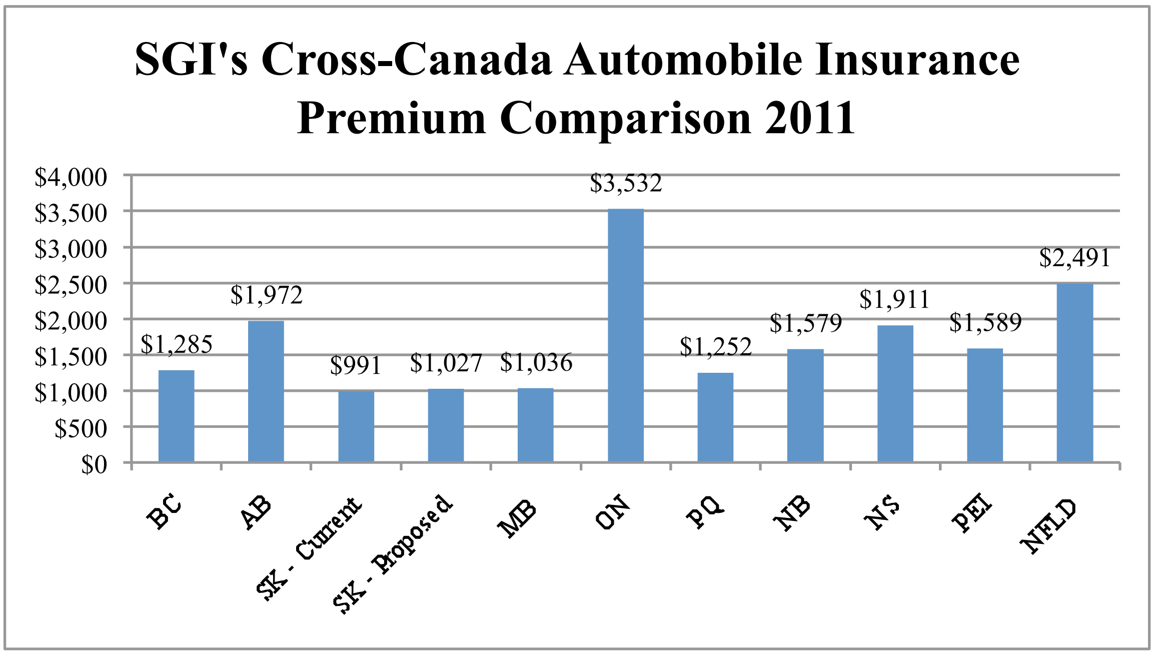
The Panel appreciates the SAF including the Panel as a stakeholder and welcomes its role as an interested party in the SAF's upcoming product review process. The submissions and comments made by the public during the review of this Application identified these as significant issues to be addressed.

6.0 Panel Observations

6.1 Competitiveness with other Jurisdictions

The Minister's Order for this review directed in the Terms of Reference that the Panel consider the effect of the proposed rate change on competitiveness with other jurisdictions. The SAF conducts an annual cross-Canada rate comparison to determine how much a driver would pay for auto insurance, given their vehicle, driving record and claims history. Based on this survey, Saskatchewan has had the lowest average personal auto insurance rates since 2005.

The SAF provided a comparison table in Section 2.3 of their application, as shown below. The Consultants caution that such comparisons are open to question, given the differences that exist between jurisdictions, such as coverages, weather, population and traffic density, road infrastructure, crime levels and vehicle mix.



6.2 Auto Fund Redevelopment Project

This Application contains information about the successful completion of the multi-year Auto Fund Redevelopment Project, which provides SAF customers with access to enhanced information and online services, while also reducing staffing costs by $625,000 and producing other operational savings for the SAF. The SAF states that the annual savings from efficiencies with the AFRP total $1.74 million. This total includes more efficient PST collections, resulting in an additional $637,000 in PST revenues to the Province. The SAF will focus on future efficiencies and cost reductions that it anticipates will yield further cost savings of $326,000. The Panel commends the SAF for its careful management of this project and for its foresight in developing a system that enhances customer service and produces cost savings for the SAF. It is uncommon for information technology projects of this scale and complexity to be completed essentially on budget, and on time.

The SAF indicated that other insurers have expressed interest in the system developed during the redevelopment project, and there may be opportunities for SAF to licence or sell the system to other companies. The Panel asks to be informed of any developments in this regard that might contribute revenues that would affect rate requirements.

6.3 Other Productivity Initiatives

The Panel also notes that the SAF has created a corporate plan to focus on efficiencies through to 2015, and has established a group of staff members to promote efficiency and productivity, and to streamline processes by introducing LEAN methodology across the organization. Initiatives already targeted include further use of technology to improve service to customers and insurance brokers representing the SAF, as well as streamlining internal processes. For example, LEAN initiatives have resulted in an increase of approximately 20% in Highway Traffic Board hearings, while printing costs dropped by 80%. The Panel applauds the work that has been done and encourages the SAF to pursue these and other efficiencies.

6.4 Traffic Safety

The SAF budgets between 2% and 3% of premiums written annually for Traffic Safety programming. The Panel agrees with its Consultants that the costs for these programs projected to 2016 are reasonable. The Panel also supports the Consultants' recommendation that the SAF, to the extent possible, provide specific details of actual cost savings flowing from each program, along with a statistical analysis showing their effectiveness. This has been suggested for inclusion in the minimum filing requirements for future applications.

6.5 OM&A Expenses

The Panel, as noted by its Consultants, sees a need for more detailed information on items within Operations, Maintenance and Administrative Expenses (OM&A). For example, the Panel supports its Consultants' contention that costs for items such as Rentals and Bad Debts be treated as separate line items, rather than being included in the Other category. In the area of External Services, the Consultants note they were unable to assess the reasonableness of $0.9 million budgeted for system improvements, human resources, claims and marketing. (page 76) Similarly, they were not able to assess the need for approximately $300,000 remaining in Other expenditures. (page 77)

The following table identifies OM&A costs by category as provided by the SAF in the second round Information Requests:

OM&A Expenses						
Description	**2009**	**2010**	**2011**	**Budget 2012**	**Variance 2011-12**	
					$	**%**
Wages & Salaries	65,922,897	67,144,231	66,843,104	68,316,777	1,473,673	2.20%
Benefits	11,708,515	11,853,492	11,735,001	12,557,290	822,289	7.01%
Pensions	3,683,284	3,759,353	3,669,686	3,764,254	594,568	2.58%
External Services	3,035,640	5,208,513	3,790,369	6,468,194	2,677,825	70.65%
Driver Education	-	-	2,495,022	7,375,000	4,879,978	195.59%
Material & Supplies	757,751	800,456	707,277	757,749	50,472	7.14%
Travel (incl. Vehicle Costs)	1,826,946	1,892,373	1,969,159	1,879,063	-90,096	-4.58%
Insurance	398,740	411,799	404,965	406,248	1,283	0.32%
Tools & Equipment	151,551	180,939	164,547	169,859	5,312	3.23%
Building Rehabilitation	1,896,591	1,730,934	2,005,364	2,717,223	711,859	35.50%
Amortization Costs	1,142,352	1,293,034	2,265,714	2,420,669	154,955	6.84%
Data Processing	8,115,143	10,113,172	12,398,531	11,650,663	-747,868	-6.03%
Safety Awareness	3,283,937	3,077,511	3,411,208	3,096,304	-314,904	-9.23%
Issuer Bank Charges	3,020,495	3,634,893	4,009,517	5,785,574	1,776,057	44.30%
Drinking & Driving	2,518,176	2,634,797	2,654,809	2,668,624	13,815	0.52%
Awareness	1,807,494	2,002,142	2,684,147	2,880,577	196,430	7.32%
Postage	932,678	1,230,261	832,712	766,349	-66,363	-7.97%
License Plates	159,631	302,031	158,092	582,142	424,050	268.23%
Advertising	1,742,702	1,568,260	1,570,799	1,841,827	271,028	17.25%
Employee Training	234,884	306,400	346,826	1,717,737	1,370,911	395.27%
Other Expenses						
Total	112,339,407	119,144,591	124,116,849	137,822,123	13,705,274	11.04%

These expense items may appear small when factored into calculating the overall rate request, but OM&A is an area where the SAF has control over its costs, and where productivity improvements and efficiencies can be tracked and measured.
The Panel, as recommended by its Consultants, suggests that the SAF, when it is preparing budgets, include an annual efficiency/productivity factor as a % of total OM&A costs in future reviews. The Panel encourages the SAF to consider a factor of between 0.5% and 1.0% of the total OM&A costs in future reviews.

6.6 Capital Management Policy

As part of its last review the Panel recommended the SAF develop a Capital Management Policy to monitor the health of the RSR. The SAF's Capital Management Policy (CMP) uses a standard industry tool, the Minimum Capital Test (MCT) to monitor the financial health of its Rate Stabilization Reserve.

The current CMP involves application of the MCT as defined by the Office of the Superintendent of Financial Institutions (OFSI) in 2011. The MCT was changed by OFSI in 2012, and future changes, which are not yet finalized, are expected in coming years. These changes, which are outside the control of the SAF, may affect the upper and lower thresholds set out in the current SGI Board approved CMP.

The Consultants question whether each change to the MCT calculation represents an improvement in the relative measurement of the capital adequacy of the RSR, in the context of the SAF's CMP. The Consultants suggest that,

"If it does not represent an improvement, then possibly the target MCT range needs to be reassessed in light of the new information the test result provides. If it does not represent such an improvement, then possibly the target MCT range needs to be reassessed to correct for the distortion caused by the test change, or alternatively, the test change is rejected and the former MCT calculation is carried forward." (page 69)

The Consultants recommended that, because of the risk for the CMP to fall out of step with MCT as it evolves, that the SAF, *"... provide explicit documentation of the monitoring of the Capital Management Policy as it is affected by any actual or known planned changes to the MCT, as a regular part of its rate Applications." (page 69)* The Panel looks forward to the SAF providing this type of documentation in future reviews.

6.7 Process, Productivity and Technical Improvements

The Panel agrees with its Consultants that the following suggestions will make future reviews more efficient and less time consuming for all parties:

1. Given the Saskatchewan Auto Fund's mandate to break even over time, and the important role the RSR plays in mitigating rate shock, the Panel supports the recommendation that more detailed reporting of surpluses and costs flowing to the RSR be adopted as part of the minimum filing requirements in all future rate applications.

2. The SAF estimates OM&A items in preparing its budget, as evidenced on page 34 of the Consultants' report, and the Panel requests this information be provided in similar detail in future applications.

3. Both the Safe Driver Recognition and Business Recognition programs can have a significant effect on rates. The Panel suggests it is appropriate to include them in the Panel's Terms of Reference for future reviews.

4. The Panel notes that its Consultants welcome the many technical improvements introduced in this Application, and the Panel encourages the SAF to consider its Consultant's suggestions for further improvements in future applications.

7.0 Impacts

7.1 Impact on the Customer

The recommended overall average 0.6% rate increase, will allow the Saskatchewan Auto Fund to fulfill its mandate, which is to operate on a break-even basis over time. The 1.0% Rate Stabilization Reserve replenishment surcharge, by being expressed as a percentage of premiums, attempts to ensure each individual makes a fair contribution to rebuilding the Rate Stabilization Reserve, commensurate with the risk they bring to the insurance process. The small size of the surcharge recommended is intended to avoid rate shock, while beginning the process of strengthening the Rate Stabilization Reserve.

The recommended rate rebalancing provisions within the Application will ensure more vehicles are paying the appropriate rate and reduce cross subsidization across customer classes; the rates for some customer classes will decrease, while others will increase, all in the interest of achieving greater rating fairness. To reduce the impact of rate shock, the Saskatchewan Auto Fund proposed rate caps.

The current status of rate rebalancing is of critical importance to the fair treatment of Saskatchewan Auto Fund Customers and emphasizes the importance of the SAF filing regular annual applications, since a minimum of two additional applications with rate rebalancing provisions would be required to bring the rates charged to levels that the Saskatchewan Auto Fund would consider it an improvement as it would bring them closer to their goal of bringing 95% of vehicles to within 5% of their appropriate rate. The Panel recommended that the Saskatchewan Auto Fund file regular annual rate applications in its last 2 reports, and reiterates its concern in this report.

7.2 Impact on the Crown Corporation – SGI Saskatchewan Auto Fund

The Saskatchewan Auto Fund delivers basic compulsory vehicle insurance to all residents of the province, with the mandate to operate on a break-even basis over time, neither receiving money from, nor paying dividends to, the Government of Saskatchewan. There is no profit component in the rates the Saskatchewan Auto Fund charges its customers. The recommended rate increase will allow the Auto Fund to break even, while the recommended surcharge will begin the process of improving the financial health of the Saskatchewan Auto Fund's Rate Stabilization Reserve.

7.3 Impact on the Public

The Public, as the shareholder for the Saskatchewan Auto Fund, may be satisfied that the proposed overall rate increase will help the SAF fulfill its mandate to be self-sustaining over time, and provide fair and affordable vehicle insurance to drivers in the Province. Since the mandate of the Saskatchewan Auto Fund is to be self-sustaining – with revenues and costs balancing out over time – the rate increase has no effect on shareholder profits or dividends.

8.0 In Appreciation

The Panel wishes to express its appreciation to the SGI Saskatchewan Auto Fund for the assistance provided during this Application review, and in particular, to those staff members who worked closely with and responded to all the queries of the Panel and its Consultants, thank you for your attentiveness and courtesies offered throughout. The co-operation the Panel received was extremely beneficial to the review process.

The Panel thanks Eckler Ltd. and Kostelnyk Holdings Corp. for their thorough and prompt analysis of the Application.

The Panel thanks technical writer Bill Armstrong for his assistance in preparing this Report.

Finally, the Panel thanks the public who expressed their views about the proposed rate increase and rate rebalancing through public meetings and other communications channels provided.

Appendix A
Minister's Order

Appendix B

SGI’s Saskatchewan Auto Fund Rate Application

to be effective August 4, 2012

Appendix C
Consultant’s Report

Independent Review of
Proposal for a Rate Application

Effective May 23, 2012

provided by:

Eckler Ltd. and Kostelnyk Holdings Corp.