Executive Summary

On July 5, 2004, ICBC filed an application for approval of the Financial Allocation Methodology and a filing relating to Road Safety, and Collection of Data relating to Age, Sex and Marital Status.

ICBC understood there to be a new regulation to the British Columbia Utilities Commission to be deposited soon after July 5, 2004, and ICBC advised the Commission that the actuarial Basic rate and financial information relating to 2005, requested by the Commission, would likely be impacted by the new regulation. ICBC indicated that it would file this information on July 12, 2004 as ICBC would have calculated the Basic insurance rate indication based on the requirements set out in the new regulation.

The provincial government issued Orders of the Lieutenant Governor in Council (OIC) No. 647 dated June 30, 2004 with the attached Special Direction IC2 to the British Columbia Utilities Commission (Special Direction). OIC 647 was subsequently amended by OIC No. 678 dated July 6, 2004. The provincial government also issued OIC NO. 666, dated June 30, 2004. This OIC gives BCUC the jurisdiction to ensure that costs are properly allocated to the ICBC's Basic insurance business.

The Special Direction requires that changes in Basic insurance rates are made in a relatively stable and predictable manner and are set on the basis of accepted actuarial practice. The Special Direction also requires the Commission to set rates for Basic insurance to allow ICBC to achieve and maintain capital available for Basic insurance equal to at least 100% of the Minimum Capital Test established by the federal Office of the Superintendent of Financial Institutions. The Special Direction also sets out the allocation of ICBC's retained earnings as of December 31, 2003 between Basic and Optional insurance.

This Volume 2 of ICBC's application and filing with the Commission consists of the materials affected by the Special Direction. Specifically, this volume contains: the actuarial rate level indications for Basic insurance in 2005; controllable costs for

Basic insurance for 2005; capital requirements for Basic insurance and additional information on performance measures. This second volume also includes an addendum to the Financial Allocation Methodology (Chapter 1 in Volume 1) that pertains to the allocation of retained earnings that was also impacted by the Special Direction.

ICBC is not applying for a revision to its rates for Basic insurance. The actuarial and other financial information in this filing is provided in response to the Commission's letter of May 20, 2004.

Actuarial Rate Level Indications

ICBC's rate level requirements are calculated in accordance with accepted actuarial practices as required by the Special Direction. The actuarial approach is designed to match the premiums collected and investment income, in connection with policies written during a period, with the anticipated claims costs, operating expenses and desired net income resulting from those policies.

The actuarial rate level indication has been prepared by ICBC's independent appointed actuary, Eckler Partners Ltd. The actuarial analysis takes into account assumptions and a number of factors. Among the considerations are weather, economic indicators, and the expected reduced claims costs resulting from the implementation of the Enhanced Graduated Licensing Program by the provincial government.

The actuarial analysis indicates that a 2.3% increase to Basic insurance rates is required should the anticipated court tariff, used to determine the Party-and-Party costs for indemnification of successful litigants, be increased. This amount was determined using the same methodology used by ICBC in 2003. However, as the Commission denied an increase in 2004 Basic insurance rates for an increase in the tariff given the uncertainty about the amount, timing and nature of the increase, and as there is no new information regarding the anticipated increase in the tariff, the actuarial analysis has also determined the rate indication excluding an increase in the court tariff to be 0.5%. Both amounts also include the required capital discussed below.

Given the anticipated small claims increase, ICBC's maintenance of controllable costs and staffing, and the steady contribution of investment income, ICBC is not applying for an increase in Basic insurance rates. This is consistent with providing smooth and stable rates for policyholders while building the required capital gradually over the next ten years, and such an application would not be cost-effective for this small a rate indication.

Controllable Costs

This filing provides current information on ICBC's controllable costs for Basic insurance. Controllable costs are defined within ICBC as all costs (compensation and operating costs) to run the insurance and non-insurance business with the exception of claims payments, broker commissions and premium taxes. Controllable costs consists of road safety and loss management services, claims services, and insurance and non-insurance operating costs.

ICBC embarked upon aggressive cost cutting measures in 2001 that resulted in a 26% decrease in controllable costs from 2000 to 2002 and ICBC had only minimal increases in costs in 2003. ICBC continues to look for new ways to achieve operational excellence and efficiency. This strategic focus on continual improvement of financial health, and becoming more customer-focused and fiscally responsible, is reflected in ICBC's planning and budgeting process.

2005 costs are expected to increase by $4.9 million over 2004 outlook due to the following cost changes anticipated for 2005:

- Increased funding to support enhanced traffic law enforcement.
- Increased planned program and system changes.
- Inflationary increases of 2% for affected services and operating expenses, other than compensation.
- Contractual salary increases.
- Increased revenue from the premium financing program to offset some cost increases.

ICBC will continue to tightly control costs and operate like a business on behalf of its customers. ICBC will continue to look for more effective and efficient ways of conducting its business to keep premiums as low and as stable as possible while providing the service customers expect.

Capital Requirements

This filing provides a discussion of the ICBC's capital requirements for the purposes of determining 2005 actuarial rate level indications. Insurance companies require capital in order to absorb unexpected losses arising from unusual events and factors, and to protect policyholders. ICBC's need for capital is recognized in Special Direction IC2 which provides that Basic insurance must achieve capital available of at least 100% of the Minimum Capital Test (MCT) by December 31, 2014 and maintain that capital available thereafter.[1]

As required by the Special Direction, ICBC has allocated retained earnings between its Basic and Optional insurance businesses. The resultant deficiency in the required capital available for the Basic insurance business to achieve 100% of MCT, projected at December 31, 2004, is approximately $496.1 million.

ICBC's approach is to distribute the build-up of capital over the next ten years so that Basic insurance policyholders have the benefits of smooth, stable and predictable Basic insurance rates. In keeping with this approach, ICBC has included $25 million in the 2005 Basic insurance rates on account of the capital deficiency. Accordingly, ICBC has requested Eckler Partners Ltd. to incorporate this amount in the actuarial rate level indication included in this filing. The 2005 Basic insurance rate indications of 2.3% (including changes to the court tariff) and 0.5% (excluding changes to the court tariff) incorporate the 2005 contribution of $25 million to address the capital deficiency.

[1] Special Direction IC2 to the British Columbia Utilities Commission, B.C. Reg 647/2004 and 678/2004, Section 3(1)(b)

Performance Measures

This filing provides the 2003 results and anticipated 2004 results and variance explanations for the ICBC Performance Measures adopted as part of the Negotiated Settlement approved by Commission Order G-49-04. Also included are the various new measures added during the negotiated settlement process. These measures include new claims initiation using the 120 second threshold within which a percentage of calls are answered, customer contact service level, injury paid severity, legal representation rate, and number of complaints heard by the Fairness Commissioner.

Conclusion

ICBC looks forward to working with the Commission and intervenors during this application for approval of the recommended financial allocation methodology and filing of actuarial and financial information for 2005.