

EXAM 6 – CANADA, FALL 2012

4. (1.75 points)

Various forms of automobile rate regulation exist in Canada.

a. (0.75 point)

Briefly describe each of the following forms of rate regulation:

- i. File and use
- ii. Use and file
- iii. Prior approval

b. (1 point)

A province is considering changing from a prior approval system to a use and file system. Briefly describe four ways in which this change could benefit the province's policyholders.

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Question 3

Answer key:

- a) Briefly describe two uses of credit-based insurance scores.
- Determine whether an insured qualifies to be written by the company
 - Segment risks into different groups with similar expected costs for the purpose of rating, risk classification, risk tiering
 - Risk Sharing Pool or Residual Market assignation
- b)
- Since much of an insurer's business is likely to be renewal business, even if the economic crisis caused a dramatic distributional shift in credit scores the overall impact would have been minor since capping and other factors would have mitigated the impact since credit scores are just one variable in rating.
 - An insurer which uses credit-based insurance scores might see a decline in overall scores leading to an increase in average rates. However assuming that the overall rates are actuarially sound, this increase should be adjusted through off-balancing therefore not increasing total premiums collected.

**** Similar answers were accepted*

Actual candidate answer for full marks:

- a) → to segment the risk e.g. risk classification factor or tier factor
→ to determine whether the risk is good to be underwrote by the company
- b) → In economic crisis, every policyholder would be affected the same way, the relative between different group might not be affected.
→ Credit score is used to determine rate relativity but not overall rate level, so in the economic crisis, the overall rate level will not be affected.
→ If there is shifted in credit score, it seems to be a common practice to insurance company by self correcting using rate differentials.

Examiner's report:

Part A was answered much better than part B. On part B participants sometimes answered on credit scoring in general and did not mention in terms of the economic crisis.

Question 4

Answer key:

- a)
- i. File & Use: Insurers file rates with the regulatory authority and after some defined period of time, rates are "deemed" to be approved
 - ii. **Use & File**: Insurers file rate structures with the regulatory authority but may begin using the new rates immediately.
 - iii. Prior Approval: Strict form of rate price regulation where regulatory authority must approve rates before they can be used.

b)

- i. Use & file rate regulation decreases volatility in insurance premiums compared to a prior approval system
- ii. Use & file systems have less regulatory costs thereby decreasing insurance premiums compared to a prior approval system
- iii. Lack of regulatory lag compared to prior approval system reduces the magnitude and frequency of price swings thereby causing less uncertainty for consumers.
- iv. Use & file systems have smaller residual markets than prior approval states
- v. Will likely lead to a larger number of insurers therefore providing more choice to consumers.
- vi. More refined classification or rating algorithm or innovation
- vii. Regulators have more time to focus on solvency or market conduct

Actual candidate answer for full marks:

- a) i) File-and-use: rate level and risk classification must be filed with regulator a certain period of time before being used
- ii) Use-and-file: rate level and risk classification may be used as soon as possible and must be filed within a stated period of time
- iii) Prior approval: rate level and risk classification system must be filed and approved before being used
- b) –Rates would be more adequate as an insurer can adapt to changing conditions more rapidly.
- Rates would be lower as insurer would incur lower cost for rate filing process.
- This increased competition environment would increase availability of automobile insurance
- This competitive environment would stimulate innovation and policyholders would have improved choice of coverage

Examiner's report:

Overall parts A and B were well answered. However, on part B candidates sometimes gave nearly identical responses for the four ways. Furthermore, candidates also thought that Use and File would lower costs vs. Prior Approval insurance without giving valid details on why.

Question 5

Answer key:

- a) 2 of the following
 - i. the CIA to give precedence to service in the public interest over self-interest of the member
 - ii. the CIA to increase its support of research and development for P&C insurance, develop standards of practice for this area, and increase its contribution to basic and continuing education for its students and members on these topics (any one of the listed)
 - iii. the CIA to improve and expand its contribution to the development and direction of public policy issues in Canada
- b) 2 of the following
 - i. surplus test provisions were strengthened by providing for minimums based on written premiums and incurred claims and existing margins on reserves