20 YEARS

AIRB AUTOMOBILE INSURANCE RATE BOARD

2024 EXCESS PROFIT REVIEW RESULTS

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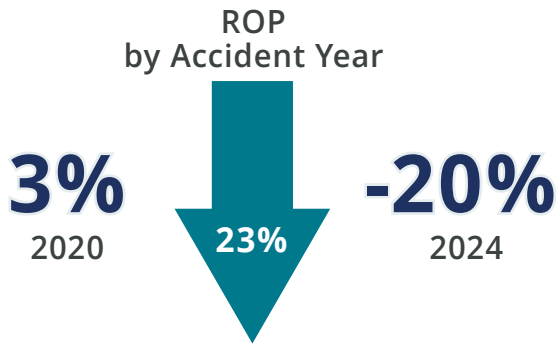
Executive Summary

The Automobile Insurance Rate Board (AIRB) has implemented a policy to measure excess profit in accordance with section 9.1, Returning Excess Premiums, of the Automobile Insurance Premiums Regulation. Insurer profits were spotlighted during the pandemic when for the first time in several years the industry was profitable. There are several organizations reporting on insurer profits, but one common feature is they are all on a financial year basis. The AIRB developed and implemented its policy to measure excess profit, in relation to our target profitability, which is on an accident year basis.

Financial year reporting is generally on a return on equity or ROE basis, reflecting the return made for shareholders. ROE is determined on a financial year reporting basis. The AIRB establishes a return on premium or ROP, which reflects the provision for profits an insurer is permitted to include in their rating program, investment income is not considered. The AIRB assesses excess premiums on an accident year basis, consistent with how premiums are established in insurer rating programs. "Accident year" refers to the year in which a loss actually occurred, regardless of when the claim was paid. This approach leads to more accurate profitability reporting. An insurer rating program is a complex algorithm used to establish an individual policyholder's premium. Rating programs consider results on an accident year basis to predict expected costs in future accident year periods. The AIRB regulates return on premium as it protects Albertans from excess premiums.

For the first-year reporting, due May 1, 2025, all insurers who wrote more than 15,000 PPV exposures in 2024 were required to submit the profit and loss (P&L) report. In total 25 insurers representing 98.67% of the market[1] submitted their P&L report, and 16 insurers who did not meet the 15,000 vehicle threshold, representing the remaining 1.33% of the market, requested and were granted an exemption for 2024 reporting.

Overall, the industry weighted average return on premium (ROP) was -19.96% for the 2024 accident year, down from -2.80% in 2023. Industry profits peaked in 2021 at 9.18% return on premium and have decreased steadily since. While we collected data on the prior five accident years (2020 through 2024), we are only able to assess the return premiums for accident years 2024 and onwards, as section 9.1 of the Automobile Insurance Premiums Regulation is not applied retroactively to accident years in which it was not in force.



The results on return of premium for 2024 were not unexpected. Not only did 2024 have significant catastrophic events increasing insurer claims costs, but insurers also had their premiums limited under the Good Driver Rate Cap. The 2024 accident year reflects premiums collected under the rate pause which was in effect from January 25 to December 31, 2023, and the Good Driver Rate Cap which was effective on changes to rating programs implemented after January 1, 2024. Several insurers did not implement the rate cap until July 1, 2024, meaning for half of the 2024 accident year premium increases were paused, and for the latter six months, drivers meeting the definition of Good Driver were capped at +3.7%.

Recognizing volatility in one accident year may not be a predictor of future results, we allowed insurers to achieve profits 3% greater than our ROP prior to requiring return of excess profits. In 2024, there were no excess profits to return. As a sensitivity test, we estimated the level of premium increase insurers would need to have earned a 6% ROP in 2024. We found the premium level would have needed to increase by approximately 36% to achieve the 6% ROP on an industry wide basis.

[1] Some insurers with less than 15,000 vehicles submitted the P&L report as they were part of a larger insurer group. While they had the option to request an exemption, many insurers submitted P&L reports anyway.

Policy

Background

Following amendments to the Automobile Insurance Premiums Regulation in 2023, specifically the addition of section 9.1 – Returning Excess Premiums, the AIRB was required to develop a policy to measure excess profit, **in relation to our target profitability**, which is a 6% return on premium (ROP) as of October 2023.

In November 2024, the AIRB approved Policy P07 – Return of Excess Premiums, outlining the authority and procedures for the submission of data in the profit and loss (P&L) report, exemptions, how the threshold would be determined, and reporting timelines.

Profit & Loss Report

The data we require to evaluate profit on a return on premium basis by accident year is not currently available through other sources or regulatory reporting. Historically, our only window into an insurer's profitability was through General Insurance Statistical Agency (GISA) financial exhibits, or Office of the Superintendent of Financial Institutions (OSFI) financial data.

Therefore, we needed to collect new data to evaluate an insurer's profitability in compliance with the regulation and the AIRB's policy. Whether the data comes from GISA or OSFI, ultimately it is based on an insurer submissions. Therefore, we required each insurer to submit their P&L report to provide the required data.

Each year during the Annual Review process, the AIRB determines the ROP for industry for the period commencing October 1. The ROP had been steady at 7% for many years, until the AIRB lowered it to 6% in 2023 (effective January 1, 2024) based on the construction of a capital asset pricing model which supported lowering the overall profit level. The same approach was used in Ontario to justify their decrease to a 5% ROP many years ago. The needed ROP to justify insurers risk was higher in Alberta than Ontario primarily due to volatility in profitability due to the increased number and severity of catastrophic events in Alberta compared to Ontario.

The P&L report contains six sections:

1. Loss Ratio
   - In this section, insurers submit their premiums and losses related to paying out for accidents. Insurers submit their incurred losses, which must be factored to ultimate values. It also includes unallocated loss adjustment expenses[2] (ULAE) and the Alberta health levy[3]. Insurers also submit their prior year estimate of each accident years ultimate losses[4].
2. Claim Discounting
   - Insurers submit the average time it takes them to settle and pay a claim. This is important because the longer a claim takes to close, the longer the insurer is likely to be earning investment income on the losses it will eventually pay and therefore increases their profit level.

[2] ULAE is all costs related to handling losses but cannot be attributed to a *single* claim. For instance, many insurers use independent loss adjusters in rural areas. These adjusters may be paid a flat rate instead of a rate per claim handled.
[3] The Alberta health levy is legislated under the *Crown's Right of Recovery Act*. The health levy recovers from automobile insurers the Governments cost of health services provided to victims of automobile accidents.
[4] See Loss Development Factoring section in the Appendix.

3. **Premium Delay**
   - For policyholders who do not pay annually, the insurer faces some delay in receiving the premium. This is time when the insurer is not able to invest the premium and therefore lowers their profit level.
4. **Expenses**
   - Settling claims is not an insurer's only cost. They must also pay brokers or agents commissions to write their policies to Albertans, they must pay rent on buildings, pay for office supplies and technology and a variety of other factors. All the non-loss related expenses are collected here.
5. **Results**
   - This section compiles all the results in sections one through four and calculate the relevant profit levels so the insurer understands where they stand.
6. **Certification**
   - We require each P&L report be attested by a licensed actuary[5], who is ultimately responsible to ensure the information submitted is complete and accurate. The person must be licensed in good standing and cannot be an executive of the insurer. Actuaries who submit false information can face significant sanctions such as having their credentials revoked.

Ensuring Insurers Are Not Excessively Profitable

Our policy requires we mandate insurers to return premiums from the most recent accident year. As we show in the Loss Development Factoring section in the Appendix, this year, being the first year of reporting for the 2024 accident year is the most volatile year. Insurers have only received a handful of the total number of claims they will, let alone paid these claims out. It is not unexpected for ultimate losses to differ from between -10% and +10% from the first valuation.

Therefore, we do not want to encounter the scenario where an insurer is deemed excessively profitable, only for their losses to end up being higher than expected which with this new data, we would deem them not excessively profitable.

To ensure this does not happen, we have two mechanisms within the P&L report to provide a buffer.

1. We define Excessive profit as an amount, to be specified each year, above the profit threshold. In the 2024 P&L report, we define this amount as 3% above the threshold. This means insurers would have to return premiums if their ROP was 9% or greater.
2. We consider prior adverse development. If losses are adversely developing over years (a new claim pattern is emerging different from historical data, which may be caused by reforms, data changes or any number of reasons), then insurers may receive an additional buffering mechanism.
3. Insurers must also be above the profit benchmark over the past five years. This ensures the profitable year was not an anomaly.

Therefore, for an insurer to be mandated to rebate profit in 2024, they must meet the following criteria:

1. They must have an ROP, after considering prior adverse development patterns, above the profit threshold of 6%, plus an additional buffer of 3%, for a total of 9%.
2. Their five year weighted ROP exceeds the profit threshold without including any buffers, which is approximately 6.77%.

[5] An actuary is a professional who manages and assesses financial risks for an insurer.

How Are They Still in Business?

While these results may not make sense to Albertans, it's important to remember insurers typically operate multiple lines of business. Anyone who has been to Costco may be familiar with a "loss leader," the idea they take a loss on a certain item to gain customers for items with higher returns. For instance, insurers often encourage bundling your home and auto insurance. Home insurance premiums are not regulated, and therefore may be more profitable than auto. While they may lose 20% on auto, they may be earning enough on their property lines to offset these losses.

Without the auto insurance line, by far the most common type of insurance bought, consumers may not be aware of the insurer and not purchase their home insurance through them. Additionally, they earn investment income on premiums (see Return on Premium Versus Return on Equity (ROE) section in the Appendix) which will also offset these losses.

Are They Not Just Self Reporting?

While we understand some readers may be hesitant to evaluate an insurers profit based on their own submission, we have several protections to ensure what an insurer submits is accurate.

For instance, some of the most important variables in the P&L report are premiums and incurred losses by accident year. We have access to extremely granular data from GISA and can verify most of the insurer's P&L report submission against their GISA data. While GISA data is also submitted by the insurer, it is a vital resource to the insurance industry and any data manipulation would hurt the insurer and industry itself significantly, as they rely on the data for setting prices.

In general, we have a comparison for nearly every value an insurer submitted to the AIRB, and we vet any discrepancies. If we believe an insurer is misleading us, we can require the insurers correct their submission if we deem it necessary. Additionally, the certification section ensures one employee, who is not an executive, signs off on the data, recognizing any false information could lead to significant sanctions.

More details on our comparison data are found in the next section.

Why Doesn't the AIRB Calculate it?

While we have reference points, it would be inappropriate for us to set values on behalf of insurers, as they know their business best. For instance, an insurer might change their policy on how much money they set aside when a claim comes in (reserving). Changes in reserving can cause distortions in the data which must be accounted for to ensure the data year over year remains comparable. If we were to try to determine their loss development factors ourselves, we may not appropriately handle this as we are not aware of changes to their reserving practices.

Exemptions

The threshold for exemptions was set at the same level as the AIRB's filing guidelines for exemption of a full filing for consistency. This level also recognizes insurers with less than 15,000 PPV exposures are likely to have extremely volatile earnings, where they oscillate between extremely profitable and extremely unprofitable years which equal out to acceptable profit levels over a very long time horizon. To promote market entry and encourage competition, we grant exceptions to these small insurers, so we don't limit the profitable years they need to stay in business.

Key Results

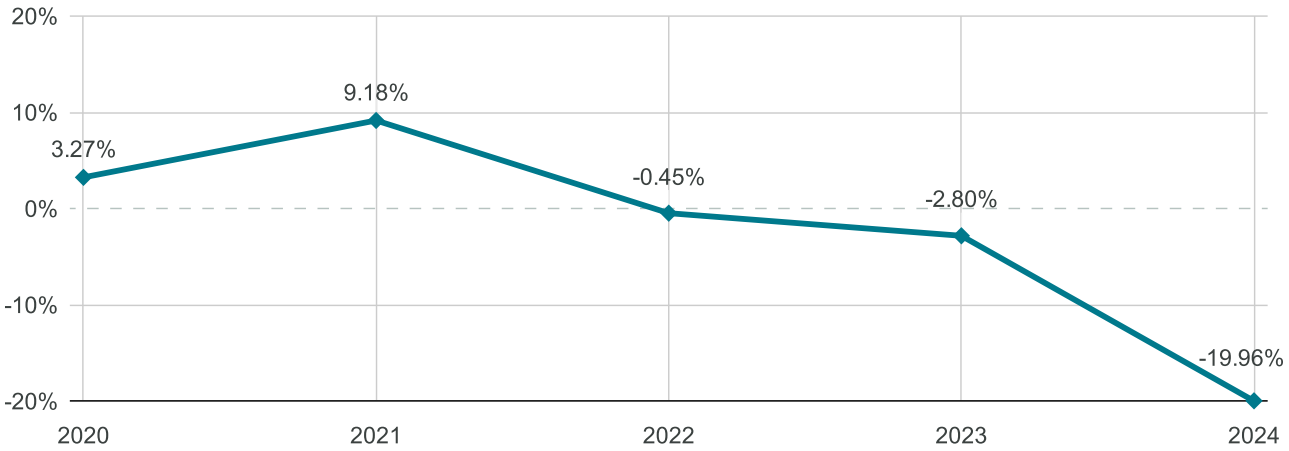
Summary

All insurers who wrote more than 15,000 PPV exposures in 2024 were required to submit the P&L report. The 15,000 vehicle threshold was chosen to align with our rate filing guidelines, in which insurers below the threshold are not required to submit a full filing. A full filing requires large and robust data which insurers below the threshold would not have. Credible data is required to conduct the required actuarial analysis. Due to the volatility of their business, their profits are also volatile, and this is discussed in greater detail in the report.

In total 25 insurers representing 98.67% of the market[6] submitted their P&L report, and 16 insurers who did not meet the 15,000 vehicle threshold, representing the remaining 1.33% of the market, requested and were granted an exemption for 2024 reporting. Of those 25 submissions, 13 required a revision which changed their profit level.

Overall, the industry weighted average ROP was -19.96% for the 2024 accident year, down from -2.80% in 2023. Industry profits peaked in 2021 at 9.18% return on premium and have decreased steadily since. While we collected data on the prior five accident years (2020 through 2024), we are only able to assess the return premiums for accident years 2024 and onwards, as section 9.1 of the Automobile Insurance Premiums Regulation is not applied retroactively to accident years in which it was not in force.

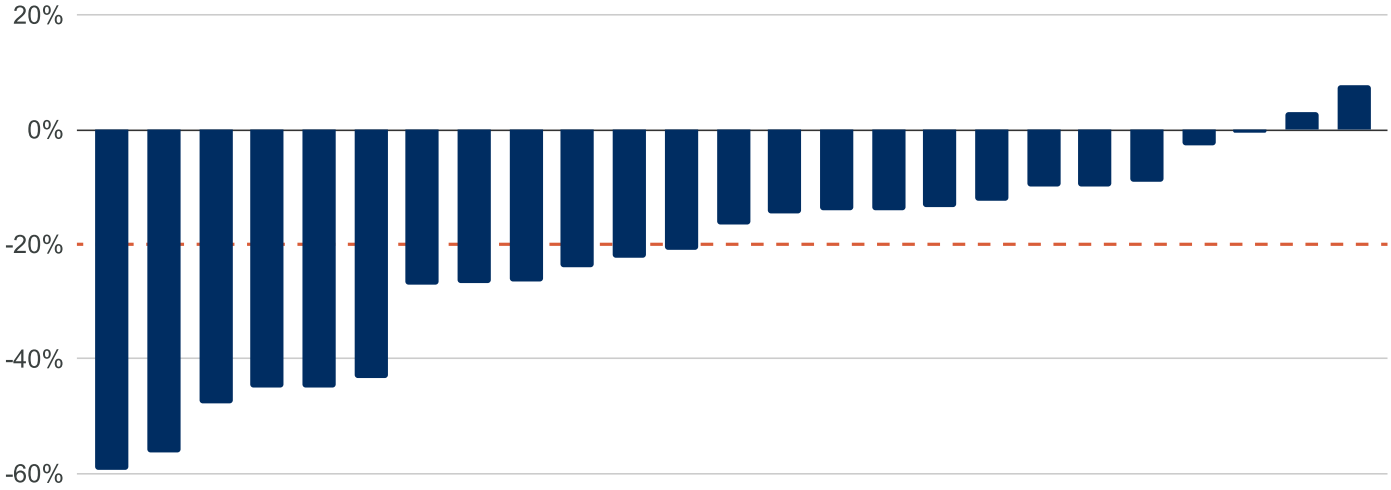
Industry ROP by Accident Year



Alberta has a competitive marketplace, with each insurer targeting different segments of consumers or areas of the province. In addition, not all insurers were adequately priced following the pandemic when driving mobility started to increase and claims started to increase back to the pre pandemic levels. With the rate pause in 2023 followed by a rate cap in 2024, it was expected the results would vary by insurer, and overall the industry would not be profitable when looking at the 2024 accident year for Alberta private passenger vehicles only.

[6] Some insurers with less than 15,000 vehicles submitted the P&L report as they were part of a larger insurer group. While they had the option to request an exemption, many insurers submitted P&L reports anyway.

ROP by Company



Changes to ROP After Submission Consideration

After initial review, all submissions required additional follow up with the submitter. Following their responses, 13 insurers were either required or volunteered to submit a revision. A majority of these revisions were to ensure insurers were all submitting their data on the same basis.

For instance, some insurers interpreted our definition of claim duration differently than the rest, resulting in much lower loss ratios when compared to their peers if submitted on the same basis. Other changes were small but included adjustments to the methodology used to allocate expenses to Alberta PPV, altering of the class of vehicles submitted, and other changes.

The graph below demonstrates the impact on submitted P&L report realized profit levels after insurer revisions. Unless indicated, all figures and references to data are based on the final submissions.

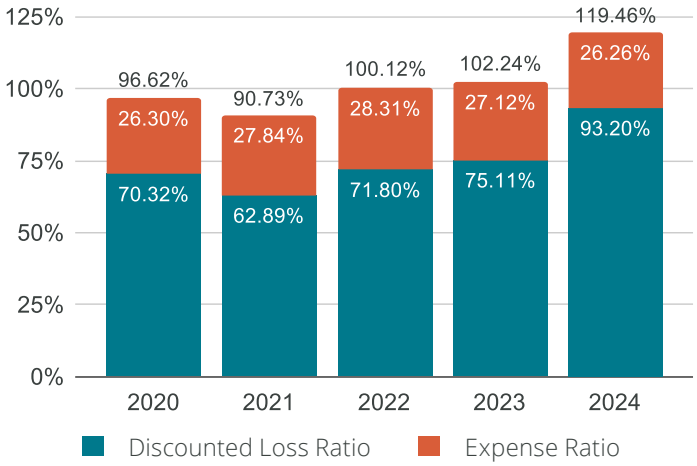
Difference Between Final & Initial ROP by Company

Loss & Expense Ratios

An insurer's costs can be broken down into losses and expenses. Losses are the costs of settling and paying claims, and expenses are the cost of day to day operations like staffing, buildings, and other items. The graph shows the loss[7] and expense ratios for the industry.

In 2024, a significant increase in losses was seen, particularly but not entirely, due to the severe hailstorm in Calgary in August of 2024. Each year as we've emerged from the pandemic and activity returns to normal, we have seen the loss ratio continue upwards.

Loss & Expense Ratios

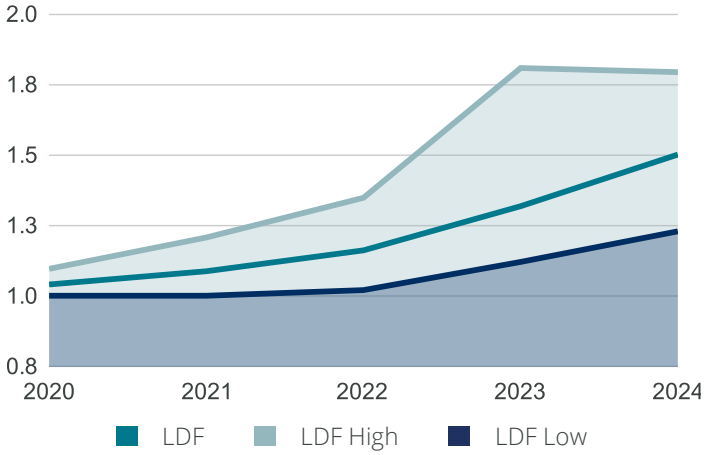


Loss Development

As we have discussed, not all claims are in and settled for each accident year. The process to estimate the difference from current losses (incurred) to final losses (ultimate) is touched on briefly in the loss development factoring section in Appendix. On a technical level, there are many ways to calculate these factors, and each insurer will have their own view on what is a reasonable formulation.

To give a broad sense, the graph shows the Loss Development Factors (LDFs) for each accident year, including a shaded region corresponding to a 95th percentile for the industry. As we can see, the LDFs are highest in 2024, as expected, at around 1.50, but most values were within 1.23 and 1.79. With the Calgary hailstorm, some insurers saw their 2024 LDFs lower than their 2023 LDFs due to the fact weather claims became a much higher portion of their losses, and they settle much faster than other claim types. We were able to confirm with GISA data this was accurate.

Industry Loss Development Factors (LDFs)



Differences to Other Data Sources

A variety of organizations report on insurer profits, but one common feature is they are all on a **financial year** basis. As shown in Accident Year Versus Financial Year section in the Appendix, losses paid out in a financial year cannot be attributed to their respective accident year which can cause issues. For instance, when we lowered the ROP from 7% to 6% for the 2024 accident year, financial losses from 2024 are paying a mixture of primarily 2023 claims, but also some from 2024 and some from before 2023. In this case, it's unclear whether we should apply a 6% or 7% threshold.

As stated in Return on Premium Versus Return on Equity (ROE) section in the Appendix, financial reporting is on an ROE basis, which our profitability metric does not apply to. We regulate return on **premium** as it protects Albertans.

[7] Losses including the Health Levy and all ULAE costs.

Superintendents Report

The Superintendent of Insurance publishes an annual report using data collected by the Office of the Superintendent of Financial Institutions, which is an independent agency of the Government of Canada, and data collected directly from provincially incorporated insurers. Generally, this data is primarily for all lines of business Canada wide, but they do have some limited data for Alberta auto class of insurance, which the Superintendent's office uses in their report.

General Insurance Statistical Agency (GISA)

Similar to the Superintendent's report, GISA's financial information is a financial year-based source of data. However, it provides a picture of profitability at the Alberta PPV level.

Earning Calls

There is a disconnect for consumers when they hear about earnings calls in the news. When they hear their insurer earned a healthy profit, they default to their interaction with the insurer, their auto insurance. However, earnings are often presented on a company-wide business, incorporating many lines of business in many provinces, and in some cases even many countries. The profit an insurer earns across these lines and geographies can vary significantly.

Comparison Data

Data Sources

For the loss ratio tab, we can extensively vet any information provided by insurers with GISA data from our Point in Time (PIT) database. This is a very granular data stream we receive directly from GISA and has all the required premium, vehicle and loss information.

Additionally, we review the companies GISA financial information submissions, whose format is used for the expenses section.

Premium & Losses

For premiums and incurred losses[8], we use our PIT data. This forms the bedrock of the P&L report, as there are no adjustments made to this data from GISA. We expect each insurer's submission should match data from our PIT query, and any deviations are investigated.

Loss Development Factors

Perhaps the most significant data point and the most unique to each company in the P&L report are the LDFs, as we have discussed earlier. This can increase the size of losses from anywhere between 1.1 and 2.0 times, depending on the insurer. Theoretically, an overestimation of the LDFs could be used to hide excess profit.

Knowing this, we construct loss triangles[9] with our PIT data for each insurer. Selecting LDFs is an "art," but with this data we can tell if an insurer is consistent with the data. For instance, depending on the insurer's method of selection[10], we may find an acceptable range for a years LDF to be between 1.30 and 1.60, and then we can compare to their submission.

[8] Incurred losses are all losses which have either been paid or set aside.
[9] Loss triangles are a way to track estimated losses over time for each accident period and are used to calculate the loss development factors we have mentioned.
[10] An insurer may consider all accident periods, or maybe just a few recent ones, or even only accident periods in the same part of the year. These methods are all valid.

Appendix

Definitions

Accident Year Versus Financial Year

An **accident year** is the calendar year in which an accident occurs. For instance, a claim which occurs in 2019 and is paid in 2021 has all payments attributed to claim attributable to the 2019 year and is available in the 2021 release of data. This compares to a **financial year**, which attributes losses to the year in which they are paid. Consider a simple example of a claim which ultimately costs $50,000 is paid out in 2021.

The claim occurs in 2019, and the insurer initially sets aside $10,000 in 2019, also known as a reserve. The following year, the claim is still open, and the injuries are not recovering as initially estimated, so the insurer increases the reserve to $30,000. The following year, the claim closes and the insurer pays the full $50,000. The tables below presents how this is reported in accident year basis, compared to a financial year basis:

Accident Year	2019 Calendar Year	2020 Calendar Year	2021 Calendar Year
2019	$10,000	$20,000	$20,000
2020	$0	$0	$0
2021	$0	$0	$0

Financial Year	2019 Calendar Year	2020 Calendar Year	2021 Calendar Year
2019	$10,000	$0	$0
2020	$0	$20,000	$0
2021	$0	$0	$20,000

From the data, we know it takes about one to two years to settle most claims. Therefore, in a given financial year, most losses paid out are for losses occurring one to two years ago, including long lengthy claims from more than two years ago, and short speedy claims less than one year ago.

Loss Development Factoring

As losses are reported on an accident year and it may take several years for the claims to settle, insurers must apply a LDF to take the incurred losses to the final (ultimate) value. In the simple example from above where the ultimate value is known, the insurer would have an LDF of 5.00 in 2019, 1.67 in 2020, and 1.00 in 2021. When multiplying the incurred losses by these factors, you would have the ultimate value.

The more recent the accident period, the less time it has had to mature and settle the claims, and therefore these results are quite volatile. You can see this in the LDFs as they are very high at the start indicating a majority of claims have not been settled, and approach one over time, the LDF when every claim is settled and paid.

Insurers **do not know** what the final values of claims will be but are able to estimate what is statistically likely based on historical data patterns. When the predicted values are lower than the actual values, we refer to this as **adverse development**, and when the predicted values are too high, we call this **favorable development**.

Return on Premium Versus Return on Equity

Our profitability metric is ROP. It is the amount of profit an insurer makes from the premium you pay. For instance, if their average premium is $1,500 and all their costs total to $1,450, then they earn a return on premium of 3.45%.

In financial reporting, the profitability metric is often ROE. There are two differences between these metrics:

1. ROP calculates profit relative to premium, while ROE calculates profit relative to equity.
    - Insurers assign a certain amount of equity, or capital to support Alberta PPV, such as in paying for claims and other expenses. This is akin to an investor buying shares in a company.
2. ROE considers investment income made by the insurer.
    - Insurers invest the premiums they are paid. Imagine the insurer invests in a low risk asset and earns 3% returns. Then with the $1,500 premium which was paid, they will earn $1,545. This increases their profit from 3.45% to 6.55%.

In this way, it becomes clear the two ways an insurer makes money is the premium they charge and the investment income they earn. In a hypothetical world, insurers could charge higher premiums or earn a higher investment return.

Premium Required for 6% ROP Calculation

We can write many variables in the return on premium profit formula as a ratio of premiums or losses.

We assume ultimate losses[11] remained the same as they did in 2024, as did the loss discount factor. The ULAE ratio is related to losses and not premiums, so it would remain constant. Finally, the health levy ratio is chosen so the Government of Alberta recovers all the expenses to treat auto accidents, since the losses are the same, we would expect the health levy to stay the same[12]. This means only expenses should scale with premiums.

ROP =
*Earned Premium * (Premium Delay Factor) - Ultimate Losses * (Loss Discount Factor) - Health Levy Ratio * Earned Premium - ULAE Ratio * Ultimate Losses - Expense Ratio * (Earned Premium)*

Therefore, to calculate the premium required for insurers to hit 6% ROP, we solve the following equation:

$$0.06\text{p} = 0.9825\text{p} - \$4{,}264{,}071 - \$384{,}332 - 0.2640\text{p}$$

Where **p** is premiums, 0.9825 is the industry weighted average premium delay factor, $4,264,071 is discounted losses in thousands, $384,332 is the health levy and ULAE expenses in thousands, and 0.2640 is the industry weighted average expense ratio.

Solving for **p**, we get:

$$\$4{,}648{,}403 = 0.6585\text{p}$$

or

The required premiums are $7.06 billion

When only considering the acquisition portion of expenses (20.53%) and keeping the general expense portion (5.72%) the same, as they are fixed cost which should not change with premiums, unlike acquisition expenses which are variable, as they are typically a proportion of premiums. When we solve the following equation:

$$0.06\text{p} = 0.9825\text{p} - \$4{,}264{,}071 - \$384{,}332 - 0.2053\text{p} - \$306{,}007$$

Solving for **p**, we get:

$$\$4{,}954{,}410 = 0.7172\text{p}$$

or

Required premiums would be approximately $6.91 billion (approximately 36% increase)

[11] For more information on what ultimate losses are, see Loss Development Factoring section.
[12] Technically, if premiums were to increase, the health levy ratio would decrease and result in overall the same charge to industry.

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