FSRA
Financial Services Regulatory Authority of Ontario

FINANCIAL SERVICES REGULATORY AUTHORITY OF ONTARIO

2023 REPORT OF THE CHIEF EXECUTIVE OFFICER ON THE FACILITY ASSOCIATION

14 November 2023 Prepared under delegated authority.

REPORT INDEX

A. INTRODUCTION: FSRA and Facility Association (FA) relationship

The Facility Association (FA) is an unincorporated non-profit association of insurers operating across Canada. Its purpose is to be the "insurer of last resort" to consumers who cannot find insurance in the regular market. Section 11.1 of the *Compulsory Automobile Insurance Act* (the *Act*) requires FSRA[1] to make an annual report to the Minister of Finance on the affairs of the FA[2] that the Minister tables before the Legislative Assembly.[3]

In Ontario the Compulsory Automobile Insurance Act (CAIA) requires the FA to establish a Plan of Operation, approved by FSRA, "for providing a contract of automobile insurance to owners, lessees and licensed drivers of motor vehicles who, but for the Plan, would be unable to obtain such insurance." This is referred to as the residual market. Every insurer writing auto in Ontario is a member of FA and must comply with the Plan of Operation.

FSRA undertakes an annual examination and financial and risk analyses of the FA to determine if the FA is meeting their objective and functioning in accordance with the *Act* and the Plan. FSRA is reporting on:

- Market share and availability as of June 30, 2023
- RSP volumes and trends as of June 30, 2023
- Financial results for the fiscal year ended October 31, 2022
- Findings of the 2023 examination
- Risk management practices and mitigation
- Rate, rule, and operational changes approved by FSRA since the last report.

[1] Both the CEO of FSRA and FSRA may exercise regulatory authority under the *Act*. However, for the purposes of this report, reference will only be made to FSRA as the CEO may delegate his/her regulatory authority to FSRA staff, as permitted by s. 10(2.3) of the Financial Services Regulatory Authority of Ontario Act.

[2] *Compulsory Automobile Insurance Act*, R.S.O. 1990, c. C.25, s 11.1 The Chief Executive Officer shall make an annual report to the Minister of Finance on the affairs of the Association and the Minister shall then lay the report before the Assembly if it is in session or, if not, at the next session. 1993, c. 10, s. 52 (8); 1997, c. 28, s. 29; 2018, c. 8, Sched. 4, s. 3.

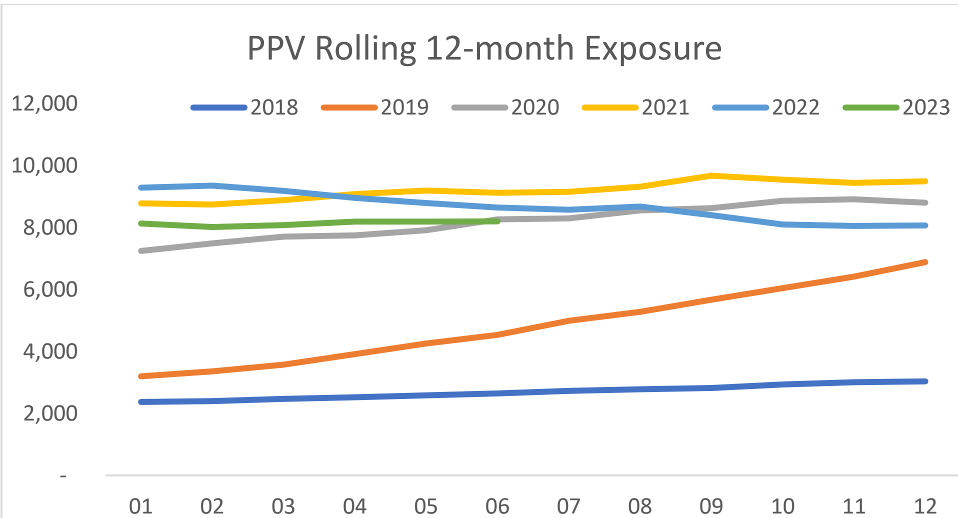
[3] The 2019, 2020, 2021 and 2022 reports have not been tabled.

B. MARKET SHARE AND AVAILABILITY (ONTARIO RESIDUAL MARKET)

Private Passenger Vehicle (PPV)

As of June 30, 2023, there were 8,205 Private Passenger Vehicle (PPV's) in the residual market. This is a decrease of 5% in comparison to the previous year and is a positive trend. More PPV consumers are finding insurance in the regular market. [4]

The PPV residual market currently accounts for 0.1% of the total written exposures in Ontario. This is below the 2003 market share peak of 3.9% of 225,000 vehicles.



The FA received approval for a 13.1% rate increase effective April 1, 2023. This increase was necessary to ensure that rates reasonably covered the claim risk. The increase ensures that FA PPV rates are not competitive when compared to insurers in the voluntary market that write similar business.

Non-PPV Categories

Some categories of non-PPV have seen growth in residual market share over the past few years. In the past year some categories have improved (e.g., motorcycles) but others continue to see challenges. The FA confirms the Commercial, Interurban, Taxi, and Buses categories face a higher "market share and availability" risk (as noted in FA's Enterprise Risk Management discussed later in this report).

Motorcycle

As of June 30, 2023, there were 613 motorcycles in the residual market, a 50% decrease from last year and a meaningful change from the growth in 2021. The motorcycle residual market is 0.5% of the total written exposures in Ontario.

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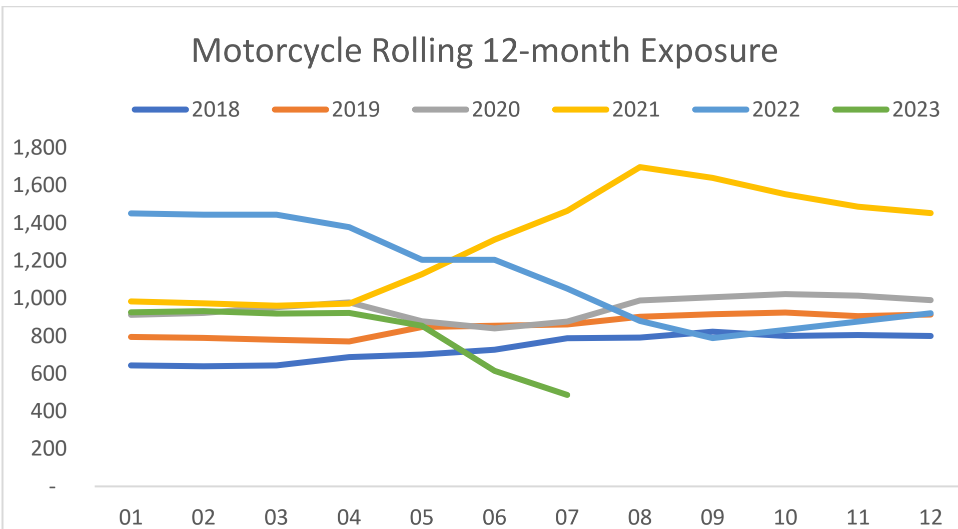
[4] This trend, as well as the stability of the Risk Share Pool discussed later in this report, is an early indication that insurers are complying with FSRA's Take All Comers enforcement action. FSRA will continue to monitor activity in this area.

FA filled a need when Motorcycle sales to newly licensed motorcycle drivers in Ontario increased[5] sharply in 2021. This led to a significant increase in motorcycles insured through the residual market. As drivers gained experience, they were able to return to having their insurance needs met in the voluntary market.

The Motorcycle category includes mopeds (engine under 50cc), scooters (engine under 250cc), and medical (mobility) scooters. It does not include e-bikes unless the pedals have been removed. However, compulsory auto insurance for scooters and e-bikes is a grey area (many are not plated, although they may meet the definition of "motor vehicle") and it is unclear if these are serviced in the standard insurance market. Home insurance may provide some legal protection depending on the product sold.



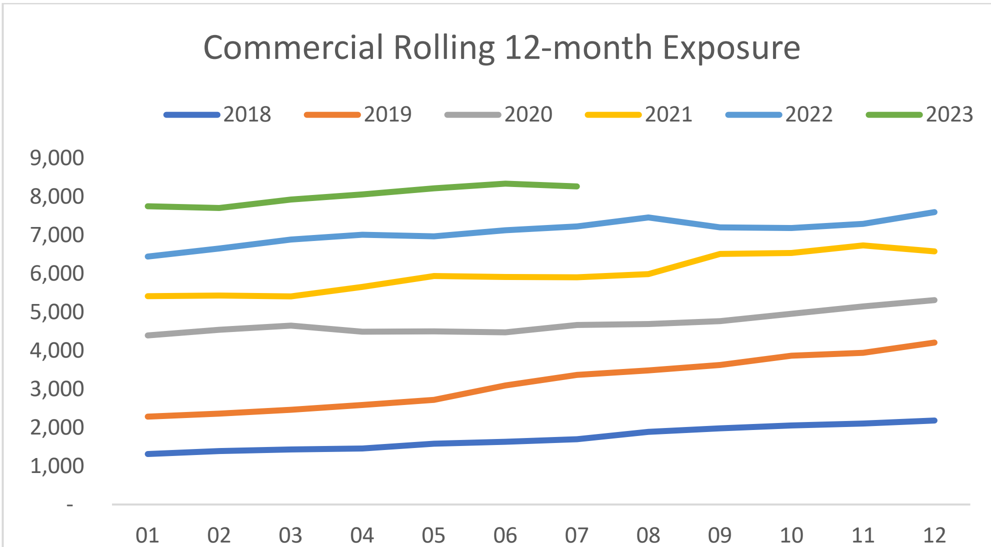
To further mitigate the risk, the FA implemented a 6.5% rate increase for motorcycles which allows the FA to earn a reasonable underwriting profit. Rate increases in FA also ensure that the FA's motorcycle rates are not lower or more attractive to consumers when compared to insurers in the voluntary market. The FA expects the voluntary market will continue to absorb this business over time.

Commercial Vehicles

The number of individually rated commercial vehicles in the residual market continues to increase. As of June 30, 2023, there were 8,337 individually rated commercial vehicles in the residual market, a 15% increase over the same period last year. The increase in delivery vehicles drove most of the growth, including the influx of vehicles used for meal deliveries and courier services because of the COVID-19 pandemic. The individually rated commercial vehicle residual market currently accounts for 2.4% of the total written exposures in Ontario.

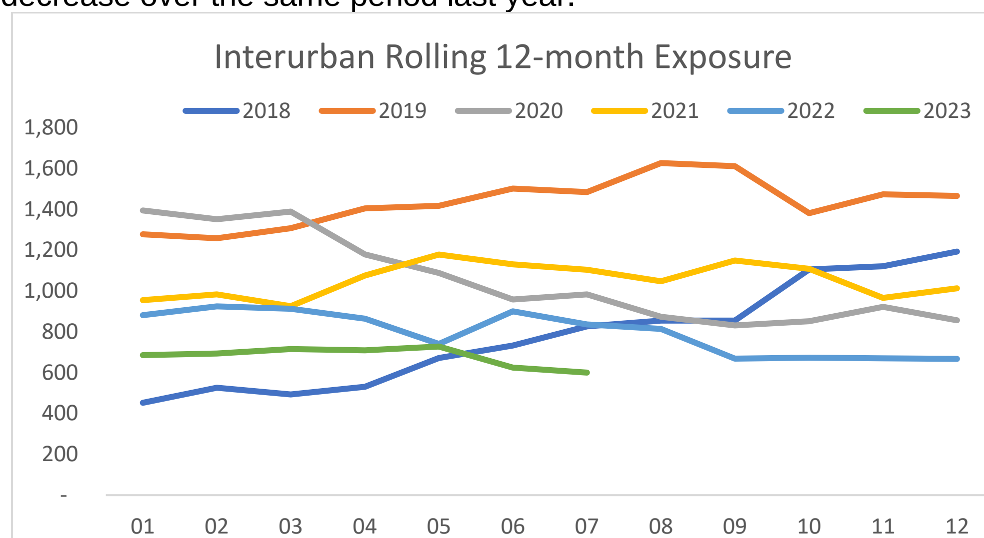
[5] For 2021, the Motorcycle & Moped Industry Council reported 17,521 motorcycle sales in Ontario. This is an increase of 12.6% compared to 2020 and 23.2% compared to 2019.

This category remains a concern, and FSRA and the FA will continue to monitor the voluntary market's underwriting appetite.



Interurban Vehicles

As of June 30, 2023, there were 625 interurban vehicles in the residual market, a 31% decrease over the same period last year.



Decreases in the Ontario interurban exposure counts over the past few years have been linked to increases in other parts of the country. There is a concern that some Ontario operators may be using jurisdictions outside of Ontario as their home base to gain access to lower insurance rates. Since insurers share loss costs for the residual market by area, this activity results in lower risk provinces and drivers paying higher premiums to cover the losses of those drivers operating in a higher cost area.

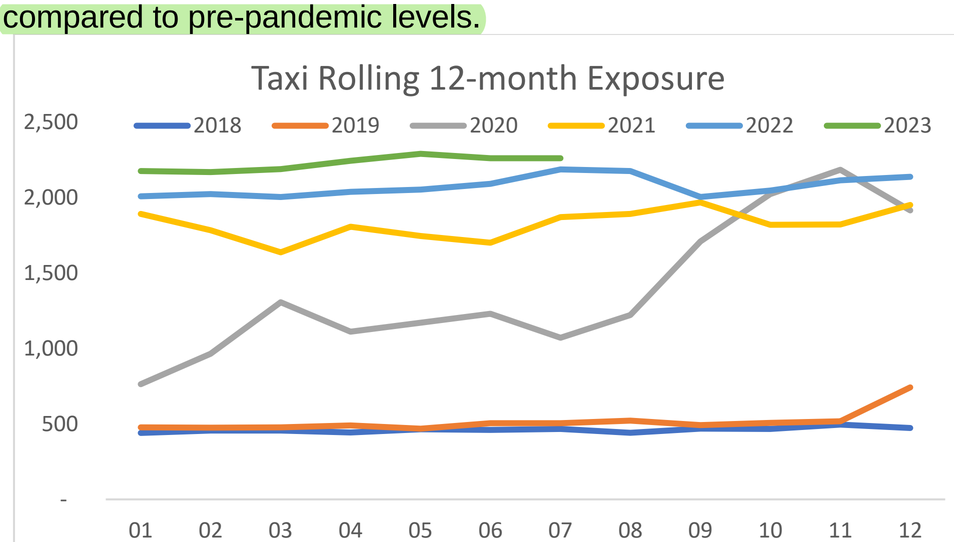
In 2020, the FA made changes to clarify and strengthen the rating and underwriting rules to allow for more thorough underwriting of commercial vehicle risks. In 2022, the FA developed and received approval for a Canadian rating matrix that reflects the rates in the province or territory where the vehicle is driven, rather than where it is registered. FSRA expects these changes to lead to an increase in the number of interurban vehicles in the Ontario residual market as the pricing advantage of registering vehicles in other areas will be negated.

Taxis

Taxis continue to be a challenging line of business for the FA. This category includes individually rated taxis, limousines, airport limousines, as well as fleets. It does not include ride-sharing services, which are currently insured in the regular market. [6]

In 2022, The Ontario FA market share for all types of taxis in this category is about 18% on a written premium basis. For individually rated taxis, the FA is the top writer in Ontario with a market share of 88% written premium and 77% of written exposures. Insurers in the voluntary market are choosing to restrict the amount of taxi business they accept or have exited the market entirely. As of 2023, there are only three insurers in the voluntary market writing individually rated taxis.

There was a slight increase of 4% in written exposures in the first half of 2023, compared with the 23% increase in written exposures in the first half of 2022. This is on top of the 38% increase in 2021 and 144% increase in 2020. The FA expected an increase as many of the taxis that were idle during the COVID-19 pandemic returned to service. However, the increase is higher than expected. As of June 30, 2023, there are 2,261 individually rated in the residual market, an amount almost double when compared to pre-pandemic levels.

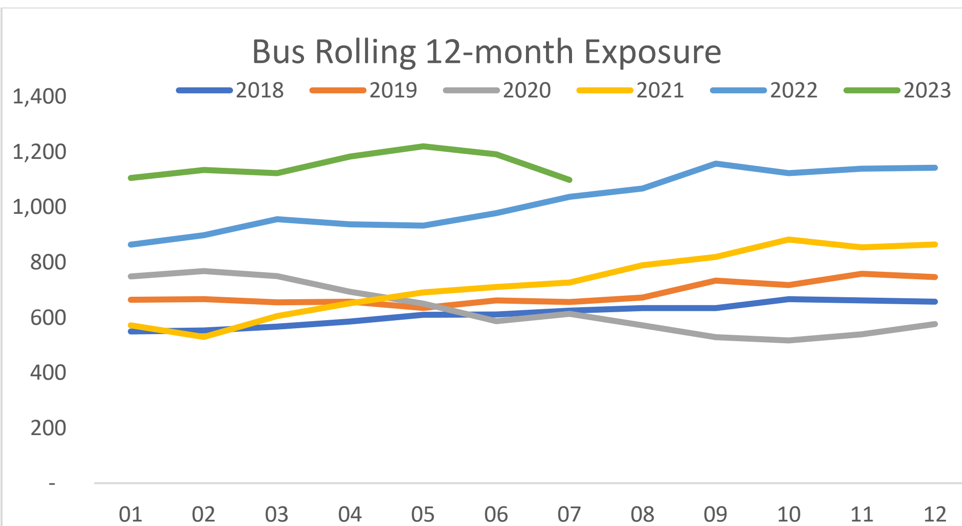


[6] FSRA publishes the ride-sharing programs it approves on its website: https://www.fsrao.ca/consumers/auto-insurance/ridesharing-carsharing-and-auto-insurance-ontario-protect-yourself

To help reverse this trend, the FA introduced an optional, enrollment-based Video Telematics program. This program provides taxi operators with a discount of either 3% or 8%, depending on the services purchased. The FA introduced the program in 2022. It was not designed to improve policy retention or price, but to help taxi operators return to the voluntary market. In other provinces, FA has become the sole insurer of individually rated taxis. The FA expects that taxi operators with proven and documented improvements in driving behavior and loss experience will find insurance in the voluntary market. It will take more than a year to evaluate the success of the program as operators will need time to prove they are good risks before moving to the voluntary market. FSRA will work with the FA to monitor the results of the program.

Buses (Public and Private)

The number of buses in the residual market increased significantly through 2021 and into 2023. As of June 30, 2023, there were 1,191 buses in the residual market which is a 22% increase over the same period last year. The recent growth is a return to pre-pandemic volumes. FSRA will continue to monitor this line of business.



C. RSP VOLUMES AND TRENDS (ONTARIO)

FA also operates a Risk Share Pool (RSP) under authority of s7 (6) CAIA. The RSP operates in Ontario and some other provinces. Insurers can cede risks to the RSP it must accept under its underwriting rules. The process is opaque to consumers (they do not know that they have been placed in the RSP). The insurer issues the policy and handles any claims, but the insurer cedes all of the premium to the RSP and the RSP repays the insurer most of any claim payout. Insurers can use the RSP to immediately handle underpriced or risky business without filing rates or rules with FSRA, or without losing valuable customers whose riskiness may be temporary (e.g., high theft auto). Consumers benefit from a tool that provides alternatives to knee-jerk rate increase or restrictive decline rules. However, there are limits to what insurers can place in the RSP and it is used inconsistently (some insurers use it up to the limit while others do not use it at all).

Cessions to the RSP have been stable over the last five years and have remained close to 50% of the maximum allowable cession limit of 5%.

As of January 1, 2022, Ontario insurers no longer retain 15% of the risk (premium and claims) and risks ceded to the RSP are transferred at 100%. The FA made this change as part of a nationwide RSP harmonization initiative. RSP usage is tied to the members' ceding rules, not the retention limit. Although there has been an increase in the number of exposures ceded to the RSP since January 2022, it is not due to the change in the retention rule. Rather, the increase in cessions is more likely a result of the removal of COVID-19 restrictions which has led to an increase in traffic volumes and the expectation of lower underwriting profits across the industry.

See Appendix A for additional background information on the RSP and the residual market operations. In future, a deeper dive into the RSP and how it can be used to benefit consumers may be warranted.

D. FINANCIAL RESULTS

The *Act* defines the FA as an unincorporated non-profit association of insurers. This means that while there may be profits or losses in any given year, the FA is not operating for the financial gain of its members. Any losses are covered by the industry which is very well capitalized and therefore positioned to backstop any losses. FSRA relied on the work of the external auditor appointed by FA to assess the quality of FA's financial statements.

The auditor presented an unqualified audit opinion for both the residual market and the Ontario RSP audited financial statements for the year ended October 31, 2022, and reported that it did not identify any material weaknesses in internal controls.

The FA published audited financial statements for residual markets (including the Uninsured Automobile Funds) across Canada, as well as the Ontario RSP. The FA has decided for early adoption IFRS (International Financial Reporting Standards) 17 together with IFRS 9, as permitted by IFRS 17. In the auditor's opinion, the financial statements present fairly, in all material respects, the financial position of the FA as of October 31, 2022, and its financial performance and cash flows for the year then ended in accordance with International Financial Reporting Standards ("IFRS").

See enclosure for the audited financial statements.

E. MARKET CONDUCT EXAMINATION

Market Conduct completed their annual examination of the FA. For this year's examination, Market Conduct focused on Ontario operations with the following areas selected for review:

a. General
b. Internal Audit
c. Protection of Personal Information
d. Sole Servicing Carrier (SC) with a focus on claims transition

The Market Conduct Examination did not reveal any serious deficiencies in the FA's procedures or practices and noted improvements since last year's examination. Three aspects of the FA's operations were noted in last year's report Service Standards, PPV renewals, and Servicing Carrier. Two of those (service standards, PPV renewals) are now resolved or progress made as noted in the examination report. The remaining issue is the fact FA is serviced by a sole Servicing Carrier. The FA continues to take steps to reduce barriers for potential new Servicing Carriers. While a sole Servicing carrier has pros (greater quality control and consistency) and cons (risk if sole carrier exits), FSRA will continue to monitor and follow up on the situation.

See enclosures for the full Market Conduct Examination report.

F. RISK MANAGEMENT

FSRA expects all insurers, including the FA, to have a well-defined Operational Risk Management (ORM) Framework in place.[7] The term "ORM Framework" refers to the policies, procedures and any related documents that outline how the insurer manages the operational risk in its auto insurance rating and underwriting activities. Managing operational risk in an insurer's processes under an ORM Framework follows a consistent cycle and includes risk identification; risk assessment; risk prioritization and mitigation; and risk monitoring and reporting.

The FA has developed an Enterprise Risk Management (ERM) program. As part of the ERM program, the FA's management team prepares an ERM Status Report and provides it to the audit and risk committee at each of its quarterly meetings. Once approved by the committee, the Board of Directors reviews and approves the ERM Status Report.

[7] FSRA operational risk management framework in rating and underwriting of automobile insurance guidance

The ERM Status Report provides the audit and risk committee and the Board of Directors with commentary on how the FA is meeting its strategic objectives as well as information on the status of the individual risks. The ERM Status Report identifies and prioritizes the top risks to the FA and this prioritized list of risks forms the basis of risk assessment, mitigation, monitoring, and reporting. The FA meets with FSRA semi-annually to review the ERM Status Report and discuss any additional operational matters related to the findings.

The FA continues to develop and refine its ERM program to be more dynamic and to align with the organization's objectives. The most recently approved ERM Status Report includes the FA's Risk Appetite Statement with five key pillars:

1. Market share and availability
2. People
3. Financial performance and management
4. Stakeholder satisfaction and reputation
5. Operational

The FA assesses each of the five pillars against a pre-defined tolerance level of minor, moderate, major, severe, or catastrophic. As of October 15, 2022, the only pillar that remains elevated above tolerance is "Market share and availability". The FA rated this pillar as "severe" against a tolerance level of "major." The FA defines this risk as the inability to maintain a minimal residual market share.

Non-PPV risks, specifically Commercial, Interurban, Taxi, and Buses, continue to drive the elevated risk in "Market share and availability." The Board of Directors reviewed and approved the FA's mitigation plan for these categories.[8] The FA will monitor and adjust the plan as required to ensure it remains effective.

FA also identified an increased risk related to Data Governance, due to potential risks associated with General Insurance Statistical Agency (GISA)[9]. GISA is transitioning to a new statistical service provider, delivery infrastructure and data operations, a plan GISA is executing on nine insurance regulatory authorities and more than 140 P&C insurers across Canada. GISA has addressed these risks by extending the transition plan timelines and establishing an Industry Advisory Committee (IAC) to provide strategic advice. As a result, FA's Chief Risk Officer expects this risk to be substantially mitigated or reduced when next evaluated in the spring of 2024. FA and FSRA will continue to monitor.

[8] The "Market Share and Availability (Ontario Residual Market)" section of this report includes the mitigation plan for each category.

[9] GISA is the statistical agent for FSRA and eight other participating insurance regulatory authorities across Canada

G. APPROVED RATE AND RULE CHANGES

FSRA must approve all non-fleet residual market rates that are written on Ontario Automobile Policy 1 or Ontario Policy Form 2. The FA has received approval for the following rate filings since the last report:

Category	Overall Rate Change	Renewal Effective Date	Notable Changes
Motorcycles	+6.5%	April 1, 2023	Base rate change uniform by territory
Private Passenger Vehicle	+13.1%	April 1, 2023	Base rate change uniform by territory but varies by coverage
Commercial (Interurban)	0%	September 1, 2023	Introduction of a rating matrix that reflects the rates in the province or territory where the vehicle is driven, rather than where it is registered.
Public Vehicle (Taxis and Limousines)	-3.1%	Dec 1, 2022	Introduction of a Video Telematics Discount with a discount of 3% (monitoring only) or 8% (monitoring plus coaching).

The FA reviews actuarial indications for Ontario auto annually in the fall. On April 12, 2022, at its Annual General Meeting, the FA Board approved full delegation of rate filing authority to its President & Chief Executive Officer. Previously, all rate filings required Board approval before submission to the regulation. This change means rates reflecting risk can be implemented in a timelier manner. FA presents any potential rate and rule changes for 2024 to the Rates and Rules Advisory Committee before submission to FSRA for review and approval decisions.

H. PLAN OF OPERATION AND PROCEDURE MANUAL CHANGES

FSRA approved FA's Accounting and Statistical Manual on June 12, 2023. Most of the changes were related to editorial and rule changes supporting the implementation of IFRS17. FSRA indicated in the approval email that FSRA will no longer require FA to send requests for approval on changes in FA's procedure manuals. This will facilitate FA's implementation of changes and will align with other areas' practices.

I. CONCLUSION

FSRA is satisfied that the FA is conducting its affairs in accordance with the *Act* and the FA Plan of Operation, including making automobile insurance available to those who would otherwise be unable to obtain such insurance in Ontario. Although FSRA did not identify any serious operational or procedural deficiencies, there are some follow-up items for 2023-2024:

- Review commercial availability with a focus on delivery vehicles
- Review interurban trucking volume changes resulting from introduction of rating matrix
- Monitor and report on results of the taxi UBI (Usage Based Insurance) program
- Monitor and follow up on the reliance on a Sole Servicing Carrier.
- Follow up on the Data Governance risk status due to the revised GISA transition plan.

J. ENCLOSURES

1. Market Conduct Examination Report
2. Audited Financial Statements of Facility Association Residual Market Segment and Uninsured Automobile Funds - October 31, 2022
3. Audited Financial Statements of Facility Association Ontario Risk Sharing Pool - October 31, 2022

APPENDIX A – BACKGROUND

The FA commenced operations in Ontario in 1979 as an insurance industry organization with legal status under the *Act.* All insurance companies that are licensed to underwrite automobile insurance in Ontario are compelled by statute to be members of the FA.

The FA's purpose is to guarantee that automobile insurance will be available to individuals who might otherwise be unable to obtain insurance in the voluntary market. This is referred to as the residual market. Insurers that are designated Servicing Carriers issue automobile insurance policies to individuals. The Servicing Carriers have contracted with the FA to collect premiums, administer policies, and pay claims on its behalf. The residual market operates in the following provinces and territories: Ontario, Alberta, Nova Scotia, Prince Edward Island, New Brunswick, Newfoundland and Labrador, Yukon, Northwest Territories, and Nunavut.

The FA also administers the Risk Sharing Pool (RSP). The RSP is an optional mechanism for individual insurers to transfer higher risk private passenger vehicles that do not qualify for the residual market. Insurers use the RSP to manage private passenger vehicles that are underpriced relative to the risk borne by the insurer. The Ontario RSP started in 1993 followed by Alberta (2004), New Brunswick (2005), Nova Scotia (2007), and Newfoundland and Labrador (2020).

An insurer's use of the RSP is invisible to the consumer as the insurer issuing the policy also manages the claims. Each insurer group may cede up to 5% of the vehicles it insures based on its own risk tolerance and ceding rules. Individual insurer's use of the RSP varies, even within the same insurer group. Since the 5% limit is on a group level, individual insurers may have ceding percentages that exceed 5%. Insurers share the loss experience of the RSP based on their Ontario private passenger vehicle market share and the insurer's usage of the RSP, each weighted at 50%. Insurers are compelled to assume losses based on the market share component of the sharing formula, even if an insurer does not utilize the RSP.