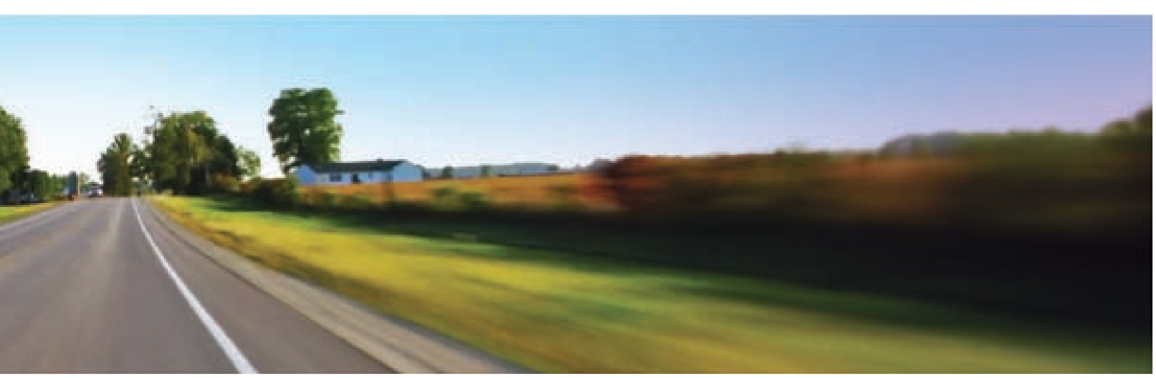
# Review of Insurance Corporation of British Columbia

August 2012



BRITISH COLUMBIA

# Review of Insurance Corporation of British Columbia

Internal Audit & Advisory Services
Ministry of Finance

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## Abbreviations

| | |
|---|---|
| BC | British Columbia |
| BCUC | British Columbia Utilities Commission |
| BI | Bodily Injury |
| CEO | Chief Executive Officer |
| CIO | Chief Information Officer |
| CPI | Consumer Price Index |
| CRS | Claims Rated Scale |
| DL | Driver Licensing |
| DR | Disaster Recovery |
| EDL | Enhanced Driver License |
| EIC | Enhanced Identification Card |
| EOI | Expressions of Interest |
| FTE | Full Time Equivalent |
| HR | Human Resources |
| IAAS | Internal Audit & Advisory Services |
| ICBC | Insurance Corporation of British Columbia |
| ISC | Intersection Safety Camera |
| ISD | Information Services Division |
| IT | Information Technology |
| MB | Manitoba |
| MCT | Minimum Capital Test |
| MD | Material Damage |
| NB | New Brunswick |

| | |
|---|---|
| OSFI | Office of the Superintendent of Financial Institutions |
| OSMV | Office of the Superintendent of Motor Vehicles |
| P&C | Property and Casualty |
| QC | Quebec |
| SK | Saskatchewan |
| TP | Transformation Program |
| VP | Vice President |
| the province | The Province of British Columbia |

## Executive Summary

The Insurance Corporation of British Columbia (ICBC) is one of Canada's largest property and casualty insurers, with over 5,000 employees, and has premiums revenue of $3.7B plus $440M in investment income. ICBC is the sole provider of Basic Autoplan, which is the mandatory auto insurance in British Columbia, regulated by the British Columbia Utilities Commission. In addition, vehicle owners may purchase from a variety of Optional insurance products, from either ICBC or other private sector insurance companies, to increase their protection. A network of over 900 independent brokers offer Basic and Optional insurance from ICBC and Optional insurance from other companies in a competitive marketplace. ICBC also provides driver licensing, vehicle registration and violation ticket administration on behalf of government.

For the past 10 years, ICBC has kept overall rate increases to an annual average of 0.8%, with Basic insurance increasing by 1.6% and Optional decreasing by 0.3%. In 2012, higher claims costs, primarily arising from bodily injury claims, coupled with declining investment income have led ICBC to request an 11.2% Basic insurance rate increase, partially offset by a decrease in Optional rates of 6%.

As part of the government's commitment to review all crown corporations, Internal Audit & Advisory Services (IAAS) conducted a review of ICBC to ensure it is being well managed and adhering to its public sector mandate. Working with a Deputy Ministers' Committee, IAAS evaluated the governance, operating costs, compensation, claims management, forecasting, investments, and Information Technology (IT).

ICBC has been able to keep the average premium increase low despite rising bodily injury claim costs. These increasing costs are the main challenge for ICBC and they need to develop and implement an overarching strategy to manage bodily injury claims.

ICBC uses sound practice in managing its investments and has achieved better than average returns over the majority of the last ten years, which has helped to offset premium increases.

There are areas where ICBC is not aligned with government's priority of cost containment, including growth in management, compensation and operating costs, despite the economic downturn in 2008. The board should set clear direction to institute a culture of cost consciousness and financial discipline across the organization.

### Governance and Organizational Structure

ICBC's Board of Directors is appointed by and accountable to the Province of British Columbia. The Board guides the strategic direction of the corporation and ensures it fulfills its mandate, as defined in the Government's Letter of Expectations. The Board has appropriate policies, processes and structures to carry out its roles and responsibilities.

There is a large senior management team comprised of the President, 10 Senior Vice Presidents and 13 Vice Presidents (or equivalents). The corporation is organized into ten divisions, each led by a senior executive.

ICBC is not fully aligned with government priorities, in particular for cost containment. This would be enhanced by developing a closer and more consistent relationship between government and the Board.

### Insurance

Two types of insurance exist in the British Columbia auto insurance market: the mandatory insurance referred to as Basic insurance, and Optional insurance which is purchased at the discretion of the vehicle owner. Basic insurance is the compulsory requirement for all vehicles registered in British Columbia and must be purchased through ICBC. Basic insurance predominantly covers the at-fault driver for damages to third parties, both property and bodily injury. Optional insurance can be purchased from ICBC or a private insurance company and is predominantly for material damage caused to the at-fault party's vehicle.

### Claims Costs

Claims account for 75% of ICBC's total costs and have experienced significant growth as a result of higher bodily injury claims. While the cost-per-bodily injury claim has been increasing at an average of 6% annually for a number of years, until recently this was offset by a decline in the number of claims made by vehicle owners. However, in 2010, the number of bodily injury claims also began to rise, which has led to the significant growth in total claims costs.

Rising bodily injury claims predominantly affect Basic insurance rates as the majority of bodily injury claims are settled within the $200,000 threshold covered under Basic insurance. Although many factors affecting Basic bodily injury costs are beyond their control and some initiatives have been undertaken, ICBC should develop and implement an overall strategy to manage bodily injury claims to address these costs.

Legal costs are another factor in the increasing cost of claims. The rate to which plaintiffs seek representation has increased from 31% in 2000 to 40% in 2011. Legal costs paid by ICBC in this period increased from $134M to $279M. ICBC also uses internal counsel for 20% of legal work related to claims. Given these increasing costs, ICBC should review the utilization of internal versus external counsel for potential efficiencies.

In setting the premiums for a given year it is necessary to forecast the amount of claims that will be paid out for accidents in that year. These estimates are a significant part in determining the premiums, and ICBC has been within 5% of the actual results over the last 10 years, which is reasonable for this type of forecasting.

## Insurance Premiums

The main factors in setting insurance premium rates are costs of claims, operations, investment income, and the requirement to keep sufficient capital levels to maintain the financial health of the company. ICBC has an appropriate methodology for allocating basic and optional costs and revenues separately to ensure that one line of business does not subsidise the other.

Basic premiums are only intended to cover costs while Optional premiums are meant to be competitive and generate a profit. Optional insurance has generated profits each year, which were retained to build ICBC's equity, from $314M in 2002 to $3.8B in 2010, at which point dividends were paid to the Province of British Columbia.

## Investments

Investment income is a substantial part of ICBC's revenue and helps reduce the premiums that would have to be paid by policy holders. ICBC has $11.4B in investment assets which generated an income of $441M in 2011 ($530M in 2010). However, investment income has declined in recent years mainly due to low interest rates and volatile equities markets.

ICBC uses sound practice in managing its investments. Proper governance structure and practices are in place and the investment department has generally achieved above average results.

## Insurance Brokers

Independent brokers sell Basic and Optional insurance from ICBC and also offer Optional insurance from other companies. ICBC has not appointed new brokers since 1992 as ICBC believes the current complement can handle the volumes without additional costs.

On average, 8.9% of premiums go to broker commissions (about 3% for Basic and 14% for Optional). ICBC paid $325M in commissions in 2011 ($311M in 2010). In recent years, ICBC has implemented two award programs to encourage increased performance and customer service.

### Staffing and Compensation

From 2007 to 2011 ICBC experienced a 32% increase in management positions across the organization, while union positions declined by 1%. The total compensation cost for the management and confidential employees increased 50% during the last five years, compared to a 9% increase for the bargaining unit for the same period.

Bonuses paid to management have been generous with easily met criteria resulting in almost all staff receiving them. In addition to ICBC management being among the highest paid within the British Columbia public sector, benefits and perquisites provided to senior management have generally exceeded the rest of the sector.

These increases in both staffing and compensation levels continued even after the economic downturn in 2008 when government implemented stricter cost controls. ICBC should endeavour to return to levels that are more consistent with 2008 as part of a general move to control and reduce costs.

### Operating Expenses

A culture of cost-containment and financial discipline has been lacking in recent years. ICBC's expense policies are generous when compared to the BC Public Service with exceptions approved by senior management.

The corporate budgeting process is decentralized and the incremental approach to budgeting is not sufficiently challenging the organization to reduce costs. Over the last five years, operating cost increases have outpaced inflation. ICBC should regularly conduct detailed budget reviews to ensure costs are contained and aligned with government direction.

### Procurement

ICBC spends approximately $300M annually to procure goods and services for operations. In many cases, for public procurement of higher value contracts, cost ends up being a secondary consideration as ICBC typically selects the best product or service. This process does not always demonstrate clearly that value for money has been received.

### Information Systems

Overall, the IT function within ICBC is effectively governed and supported by a comprehensive IT strategic planning process that ensures business and IT alignment over the long-term. ICBC's main business applications are aging custom built systems, dating back to the 1970's. A key driver for their Transformation Program (TP) has been the replacement of these systems.

The new IT infrastructure and systems to be delivered through TP require a more robust IT security function than currently exists as well as new disaster recovery plans.

**Transformation Program**

In 2010, ICBC began the TP to modernize its claims and insurance processes and systems. The TP is expected to be completed in 2017 at a total cost of $400M and is funded through profits generated by Optional insurance premiums.

Overall, the TP has adequate processes in place to support ongoing project management. However, initial planning was not sufficiently detailed, which has led to impacts on project budget estimates, project benefits and schedule. In addition, the Program is not clearly separated into phases which would enhance the communication and reporting to Government and facilitate managing the scope against the budget.

**Road Safety and Driver Licensing**

In addition to the insurance business, ICBC invests in road safety and loss management programs to reduce traffic-related injuries, accidents, auto crime and fraud. ICBC also provides non-insurance services for the government, such as driver licensing, vehicle licensing and registration, and violation ticket administration and fines collection.

Many of the driver licensing systems are nearing the end of their useful life and lack the flexibility to accommodate new business requirements. While no timelines have been established for the replacement of these legacy systems, this should be a priority given their importance to many stakeholders.

* * *

We would like to thank the management and staff of ICBC and other stakeholders who participated and contributed to this review for their cooperation and assistance.

CDBrown

Chris D. Brown, CA
Assistant Deputy Minister
Internal Audit & Advisory Services
Ministry of Finance

## Introduction

ICBC is the sole provider of Basic auto insurance and sells Optional auto insurance products in a competitive marketplace.

Governed under the *Insurance Corporation Act,* it was established as a provincial Crown corporation in 1973 as the sole provider of auto insurance in British Columbia (BC). In 1976, legislation was amended to allow other insurance companies to sell Optional auto insurance products.

Prior to 2004, ICBC received direction on rates from the Province of British Columbia (the province). Subsequently, the British Columbia Utilities Commission (BCUC) was appointed as the regulator for Basic insurance rates.

ICBC employs over 5,000 staff with 38 claim centres and 21 driver licensing (DL) locations around BC and headquarters in North Vancouver. ICBC is one of Canada's largest property and casualty (P&C) insurers generating over $3.7B in revenue from Basic and Optional premiums along with $440M of investment income in 2011. Insurance products and services are available through a province-wide network of approximately 900 independent brokers, government agents and appointed agents. ICBC processes approximately 900,000 claims each year over the telephone and through claims centres and facilities.

ICBC invests in road safety and loss management programs to reduce traffic-related injuries, accidents, auto crime and fraud. In addition, ICBC provides the following non-insurance services:

- DL;
- vehicle licensing and registration; and
- violation ticket administration and fines collection on behalf of the provincial government.

For the 10 years ending in 2011, ICBC has kept overall rate increases to an average of 0.8% per year, with Basic rates increasing by 1.6% and Optional rates decreasing by 0.3%, on average, per year.

**ICBC Rate Changes for all Vehicles 2001 - 2012**

| Year | Basic | Optional | Overall |
|---|---|---|---|
| 2001 | 0.0% | 0.0% | 0.0% |
| 2002 | 6.6% | 8.7% | 7.4% |
| 2003 | 2.0% | 8.9% | 4.8% |
| 2004 | 0.4% | 0.4% | 0.4% |
| 2005 | 0.0% | -7.6% | -3.4% |
| 2006 | 6.5% | 0.0% | 3.7% |
| 2007 | 3.3% | -3.8% | 0.2% |
| 2008 | 0.0% | -3.0% | -1.2% |
| 2009 | 0.0% | -3.3% | -1.4% |
| 2010 | -2.4% | -3.0% | -2.7% |
| 2011 | 0.0% | 0.0% | 0.0% |
| **10 yr average** | **1.6%** | **-0.3%** | **0.8%** |
| 2012* | 11.20% | -6.00% | 3.60% |

**2012 Basic rate change is not yet approved.*

Despite sound investment management, ICBC's investment income has been declining since 2007. Declining investment income combined with increasing claim costs prompted ICBC to apply for an 11.2% Basic insurance rate increase which BCUC approved on an interim basis pending the outcome of the filing.

In 2010, ICBC began to modernize its claims and insurance processes and systems through the initiation of what ICBC has termed the TP. TP is expected to complete in 2017 at a total cost of $400M funded through Optional insurance premiums.

## Purpose & Objectives

In the 2011 Throne speech, the provincial government made a commitment to review all crown corporations to provide assurance they are being well managed and adhering to their public sector mandates. In keeping with this commitment, IAAS undertook a review of ICBC, commencing February 2012.

This review evaluated, and as appropriate, made recommendations with respect to the following:

- Governance framework and organizational structure.
- Reliability of forecasts including actuarial analysis used in rate setting.
- Operating costs including employee compensation.

- Primary cost drivers and their impact on rates and rate setting, including bodily injury (BI) claims.
- Investment portfolio management and related revenue.
- Progress and expenditures on TP.

## Approach

IAAS conducted a broad review of ICBC, working with a Deputy Ministers' Committee who were regularly provided with detailed information and areas of concern identified by IAAS during the project. The approach included:

- conducting interviews with key management and staff across ICBC and related stakeholders;
- reviewing and analyzing legislation and policies;
- research for comparable information from other relevant organizations and other jurisdictions;
- reviewing and analyzing financial reports and variance reports; and
- reviewing and analyzing key operations and processes.

## Overall Conclusion

For the past 10 years, ICBC was able to keep the average annual rate increase to 0.8% despite rising BI claim costs. These increasing costs are the main challenge for ICBC and although many factors affecting BI are beyond their control (weather, judicial decisions, number and severity of accidents), ICBC needs to develop and implement an overarching strategy to manage BI claims.

Insurance premiums are invested to provide a return and managed so that claims can be paid as they arise. Like any insurance company, investment income is a substantial part of ICBC's revenue. ICBC uses sound practice in managing its investments and has achieved better than average returns over the majority of the last ten years.

There are areas where ICBC is not aligned with government's priority of cost containment including growth in operating costs and in particular, staffing and compensation. In the last five years, ICBC increased the number of management positions by 32% and total management compensation cost by 50%, despite the economic downturn in 2008. The board should set clear direction to institute a culture of cost consciousness and financial discipline.

In 2010, ICBC began to modernize its claims and insurance processes and systems through the TP. Overall, TP has adequate processes in place to support ongoing project management. However, planning was not sufficiently detailed for a $400M project, which has led to impacts on budget estimates, project benefits and schedule.

# 1.0 Governance and Organizational Structure

## 1.1 Governance

ICBC's Board of Directors is appointed by and accountable to the province. The ministry and the Board work closely with the Board Resourcing and Development Office in selecting qualified individuals for the board.

Overall, the Board has provided adequate guidance and oversight in the majority of ICBC's operations; however, there are areas where ICBC is not aligned with government's priority of cost containment including full time equivalent (FTE) growth, compensation, operating costs and procurement. The Board's oversight of these areas could be stronger with clearer direction to the management team.

Board Operations

The Board has proper policies, processes and structures in place to carry out its roles and responsibilities. The Board currently has eleven members which have the appropriate combination of skills and industry experience to guide ICBC. The Board Chair and four members were appointed this year.

The Board of Directors guides the company's strategic direction and ensures it fulfills its mandate, as defined in the Government's Letter of Expectations. To assist with carrying out its responsibilities, the Board has five committees – Audit, Human Resources (HR) and Compensation, Transformation Program, Governance, and Investment.

ICBC's management reports to the Board on a regular basis. They provide reports, updates, advice and recommendations on major issues and the Board approves all major strategies and policies. In addition, management informs the Board of key corporate risks and the Board monitors and reviews these risks through its committees.

The Board had concerns with the term limits of its members as this impacts continuity. In response, the Board has been expanded from eight to its current eleven members to assist in ensuring the Board remains adequate in size and accommodate turnover. At the time of this review, the Board was developing a succession plan to advise the Government of a timetable for renewing board membership.

## Recommendations:

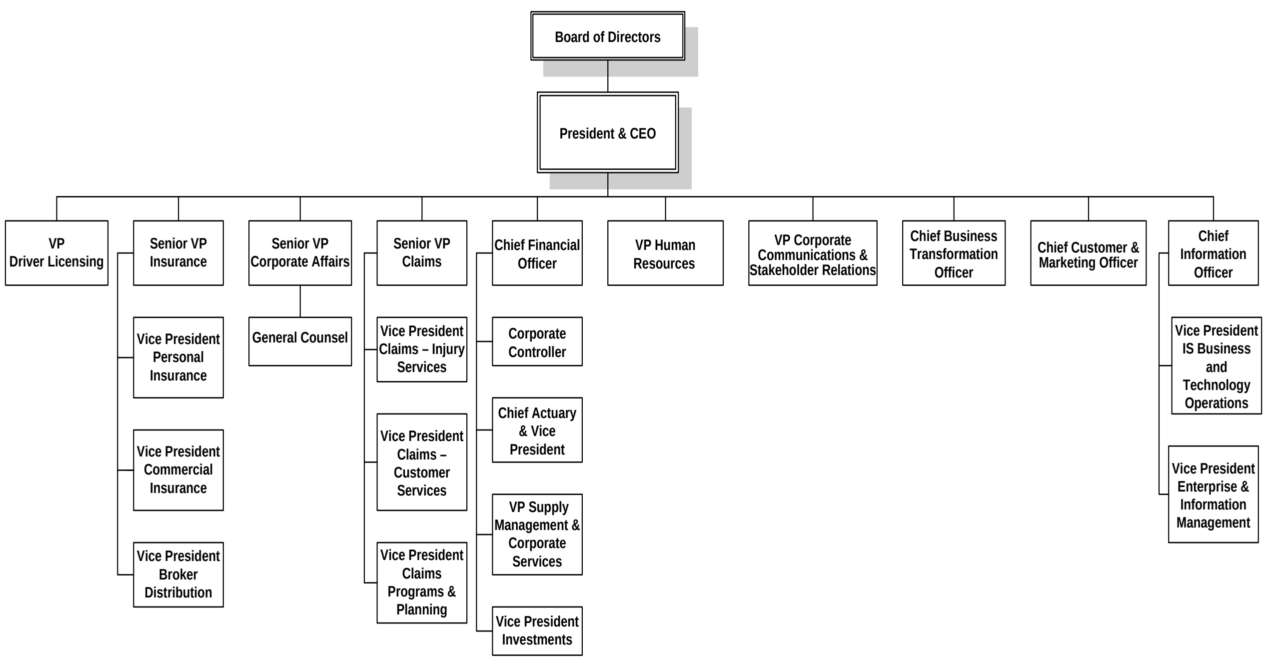
**(1) ICBC and the Province of British Columbia should develop a closer and more consistent relationship to improve oversight of ICBC and ensure alignment of priorities.**

**(2) ICBC's Board should develop clear expectations on cost containment.**

### 1.2 Organizational Structure

ICBC's large senior management team is comprised of an executive committee (consisting of the President and 10 senior executives) and 13 additional Vice Presidents (VPs) (or equivalents). ICBC is organized into ten divisions. Each division is led by one of the senior executives who reports directly to the President & Chief Executive Officer (CEO) as shown in Figure 1. ICBC's major lines of business are Claims, Insurance, and DL, and approximately half of ICBC employees work in Claims, making it the largest division.

Figure 1: ICBC Organizational Structure



## 2.0 Insurance

Two types of insurance exist in the BC auto insurance market: the mandatory insurance referred to as Basic insurance, and Optional insurance which is purchased at the discretion of the vehicle owner. They provide protection for policyholders against damages to property as well as injury to third parties arising from a motor vehicle accident.

Basic insurance is the compulsory requirement for all vehicles registered in BC and must be purchased through ICBC. Its benefits are legislated in the *Insurance (Vehicle) Act and Regulations* and include coverage for third party liability up to $200,000, accident benefits (medical expense and rehabilitation up to $150,000, and some wage loss), as well as uninsured or underinsured motorist protection. Basic insurance predominantly covers the at-fault driver for damages to third parties, both property and BI.

Optional insurance can be purchased from ICBC or a private insurance company and includes extended third party liability coverage beyond $200,000, comprehensive, and collision coverage. Optional insurance is predominantly for Material Damage (MD) caused to the at-fault party's automobile.

### 2.1 Claims

Claim costs account for approximately 75% of ICBC's total costs. These costs are comprised of payments to injured parties, payments for services related to claims, and expenses incurred for investigation and defence.

ICBC is responsible to record, investigate, assess, negotiate and settle each claim on behalf of the party at-fault (defendant). While the party bringing the action may carry insurance with ICBC, the damage is being charged against the policy of the person at-fault, whom ICBC represents.

ICBC is obligated to meet the interests of both the insured and the injured by minimizing its exposure and avoiding rate increases while fairly settling the claim for the injured party.

In September 2011, the Claims Division restructured to a functional model to better align its resources and responsibilities. Previously, the model was based on geographic location, creating inconsistencies in the handling of claims. By focusing staff on functional areas, ICBC expects consistencies and efficiencies to develop, contributing to the foundation for the new claims system within TP.

Claims are categorized into two lines: MD (non-injury) and Injury Claims which are handled by risk and complexity.

### 2.1.1 Material Damage

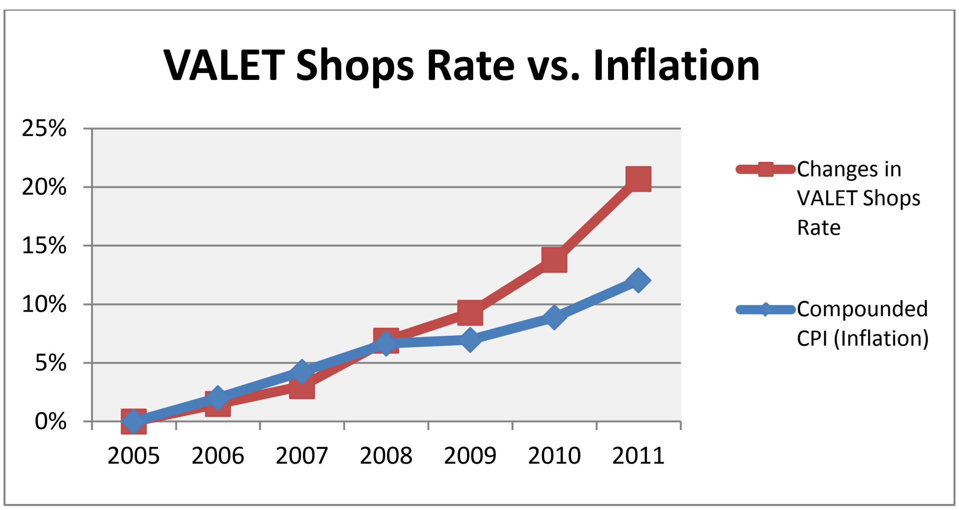
MD claims, also referred to as non-injury claims, represent approximately 40% of the total claim costs. The claims are vehicle related and are covered through two means:

- damage caused to one's own vehicle such as collision, comprehensive, and glass – which is covered under Optional insurance; and
- damage done to the property of other's – which is covered under the Third Party Liability (Basic insurance) and Extended Third Party Liability (Optional insurance).

The average MD claim has increased from $2,407 to $2,735 (an increase of 13.6%) during the years 2007-2011, but the number of claims per year has decreased. The combined effect has been a slight decrease in MD claims, from $1.1B in 2007 to $1.04B in 2011.

The most significant portion of MD claims costs is auto repair. Auto body shops constitute 46% of ICBC's MD claims, of which 93% are performed at VALET car shops. The VALET shops are accredited auto body shops that must maintain prescribed performance levels.

The rate paid to VALET shops grew from $58 in 2005 to $70 in 2011 and was negotiated through the Collision Repair Industry Agreement. The following graph shows how the growth in rates paid to VALET shops exceeded the growth in the Consumer Price Index (CPI).

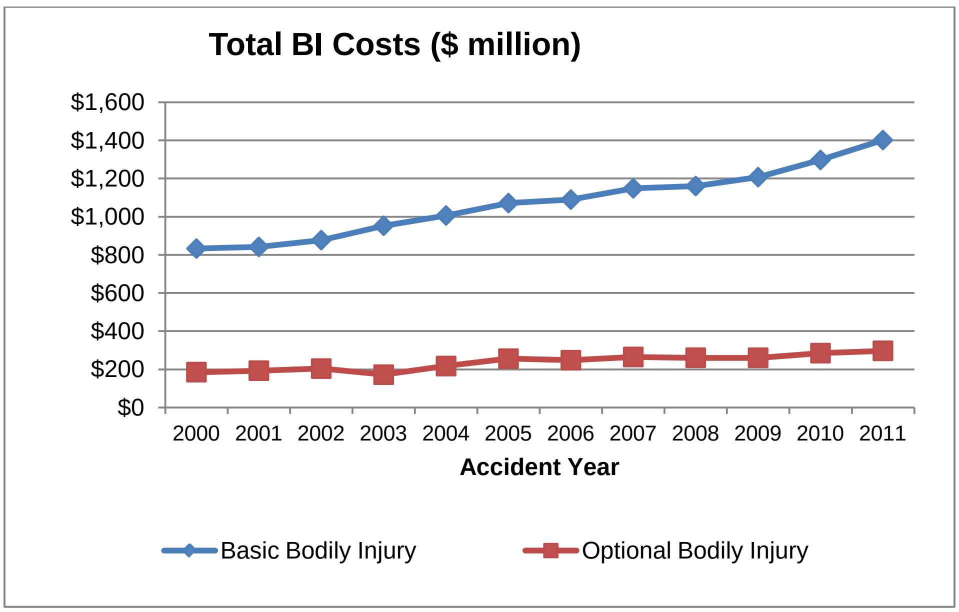


Monitoring of MD claims is conducted through performance measures that include average loss (cost/claim) and cycle time (duration in which to complete the activity). The metrics were implemented in 2009, and while there has been some improvement throughout the province, the metrics continue to evolve.

### 2.1.2 Bodily Injury

Injury claims represent 60% of total claim costs and are primarily related to BI.

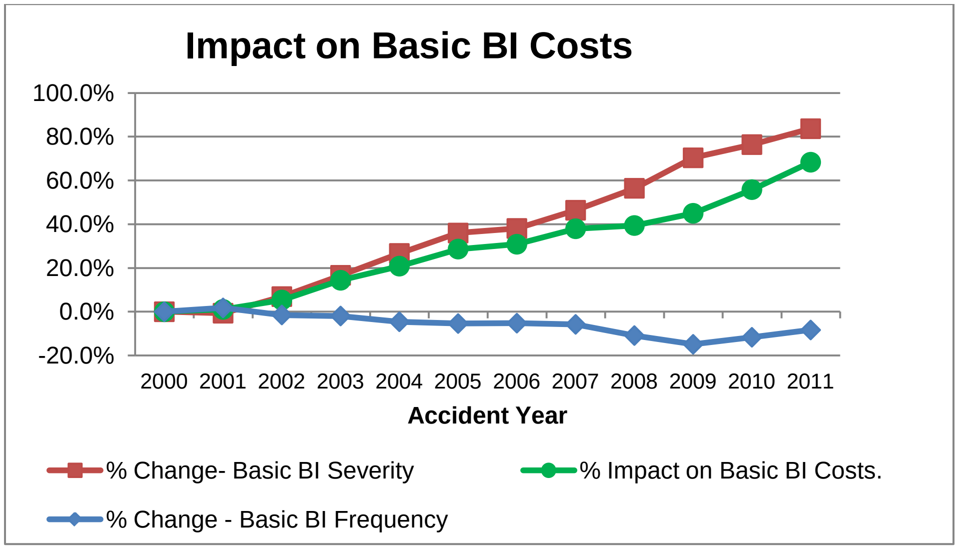
Rising BI claims predominately affect Basic insurance rates as the majority of BI claims are settled within the $200,000 threshold covered under Basic insurance. Since 2000, Basic insurance BI costs increased by $569M (68.3%) to $1.4B, while Optional BI increased by $112M (60.5%), to $300M.




BI claims costs are a function of two key factors: average cost per claim (severity) and number of claims (frequency).

The severity for BI claims has had average annual increases of 6% over the last decade, far exceeding inflation. The frequency of BI claims experienced a downward trend until 2009. This trend partially mitigated the effects of the increased cost per claim. Since 2010, the number of claims has increased, adding to the significant growth in total claim costs.

The graph below shows the cumulative effect of increasing severity and changing frequency on Basic BI costs.




Historically, BI costs have not been consistently well managed. While ICBC has recently developed and implemented a number of initiatives to address the magnitude of Basic BI claims costs, there has not been an overall strategy. Many of these initiatives were refined or re-enforced recently including:

- Making fair and firm offers.
- Segmented BI claim management by risk.
- Greater management oversight.
- Quality assurance reviews.
- Staff training.

Although many factors affecting Basic BI costs are beyond ICBC's control (weather, judicial decisions, number and severity of accidents), the management and control of BI claims costs have only recently been a priority focus.

## Recommendation:

(3) **ICBC should develop and implement an overall strategy to more effectively manage bodily injury claims.**

### 2.1.3 Legal

Legal representation has contributed to the growing costs in both settlements and legal fees while impacting the justice system. In BC, the courts determine compensation to victims for their injuries which include: lost wages (past and future), care, and amounts for "pain and suffering" (general damages).

ICBC does not involve counsel in any claim until the injured party retains representation. The rate to which plaintiffs seek representation has increased from 31% in 2000 to 40% in 2011 and in cases where the settlement is expected to be greater than $20,000, 85% of BI claimants are represented by counsel.

From 2000 to 2011, legal costs paid by ICBC increased from $134M to $279M, not including contingency fees (estimated by ICBC at approximately 30%) paid by claimants to their lawyers. The increased representation rate directly impacts ICBC's legal costs and has contributed to increasing claim costs.

In addition, ICBC has internal counsel which support approximately 20% of legal work related to claims. External counsel are hired in locations where internal counsel are not available or when specialized expertise is required for complicated claims. Claims have become more complex due to factors including:

- previous court decisions;
- increased demand for medical treatments; and
- increased need for medical experts and documentation for investigative purposes.

ICBC focus internal counsel on the claims that would provide the greatest savings compared with retaining external counsel. There has not been an overall review evaluating the appropriate allocation of internal versus external counsel in recent years, although smaller reviews for specific locations have been conducted.

## Recommendation:

**(4) ICBC should review the utilization of internal and external legal resources to maximize cost effectiveness.**

## 2.2 Actuarial Experience

In calculating the premium to be charged for insurance, ICBC must estimate the amount of claims that will have to be paid out for the accidents occurring in the year. These estimates play a significant part in determining the premiums. ICBC is in conformance with accepted actuarial practice, and the external actuary and external financial auditors consider the estimates to be reasonable.

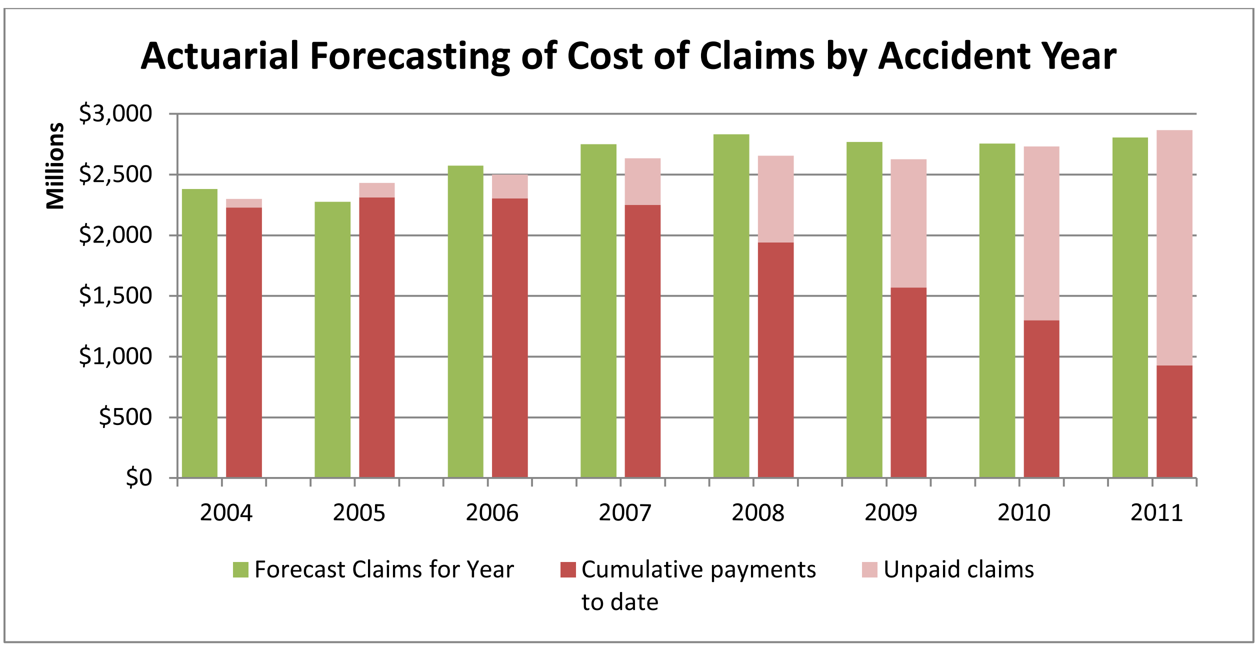
**Forecasting the Cost of Claims**

The actuarial group uses available information, including past history, current demographics and inflation, to forecast future data, such as number and types of accidents expected to occur in a certain year and the cost of claims resulting from these accidents. This forecast is used to calculate premiums needed for the upcoming year.

BI claims form the largest component of the unpaid claims liability, with the longest residual payment period. BI amounted to 54% of 2011 payments and 87% of 2011 estimated unpaid claims.

**Accuracy of Forecasting**

Actual results have been within 5% of the forecast over the last 10 years, which is considered reasonable. The graph below shows the initial forecast for claims costs by accident year, compared with today's estimate of those costs – i.e., what has been paid, plus what is still expected to be paid. The estimated value of total unpaid claims from all accident years is currently $6.4B, with payments expected to continue through to 2038 (with most being paid within five years).



Independent Evaluation

ICBC retains an external actuary to work with its internal actuarial group. Having an external actuary adds an outside perspective and strengthens the objectivity of the actuarial forecasts.

For a full independent assurance of conformance with accepted actuarial practice, external auditors include actuaries in their audit team to perform an evaluation of ICBC calculations on unpaid claims.

## 2.3 Insurance Premiums

Premiums for Basic insurance are regulated by BCUC and requests for changes go through a public process. Basic insurance premiums only cover costs, while ICBC sets the premiums for Optional insurance to be competitive with private companies and generate a profit.

Premiums have remained steady in recent years, with rate increases averaging 0.8% over the last 10 years. For 2012, a rate increase of 11.2% was requested for Basic while Optional decreased by an average of 6%.

### 2.3.1 Rate Setting

For both Basic and Optional insurance, major factors in premium rate setting are costs of claims and operations, investment income, and the requirement to keep sufficient capital levels.

Allocation Methodology

Basic and Optional costs and revenues are accounted for separately in ICBC to ensure that one line of business does not subsidise the other.

ICBC has an appropriate methodology for allocating costs and revenue to Basic or Optional insurance. Approximately 90% of costs and revenues are directly attributed to either Basic or Optional. The remaining 10% is allocated based on a methodology that is verified by independent auditors and approved by BCUC.

Minimum Capital Test

The Federal regulator, Office of the Superintendent of Financial Institutions (OSFI), oversees insurance companies in Canada and sets the Minimum Capital Test (MCT). MCT calculates the minimum level of capital necessary for an insurance company to cover unexpected events. As a crown corporation, ICBC is not subject to OSFI regulation, but is mandated by the province to follow the OSFI rules for MCT.

Provided the minimum MCT is met, insurers will set their own targets to reflect the characteristics of their individual businesses. The ICBC Board approves targets each year, currently set at 130% for Basic insurance and 260% for Optional insurance. The MCT target for Basic is also subject to BCUC approval, and both targets are subject to direction from the province.

In 2005, ICBC was directed to transfer $530M from Optional insurance to Basic insurance to help meet the Basic MCT target. Then, in 2007, an additional $100M was transfered for the same purpose.

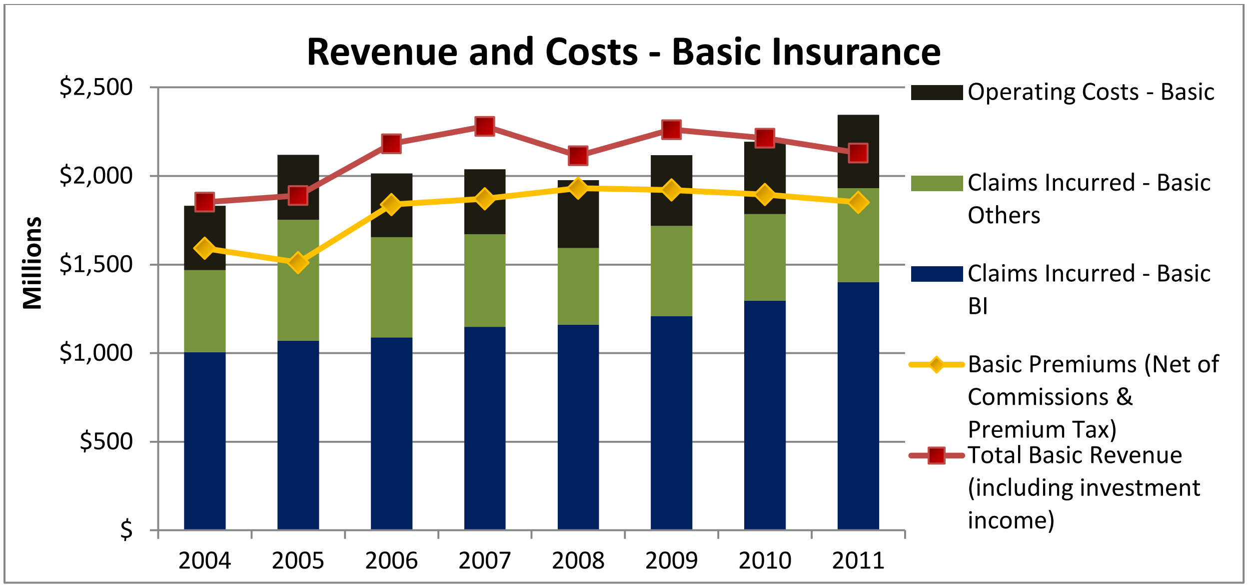
## Basic Insurance

Approval by BCUC is required for changing Basic insurance rates as well as for changing the rate design (e.g., making adjustments between territories).

ICBC estimates future claims costs, operating costs and potential MCT shortfalls to arrive at the revenue required. The revenue requirements are offset by expected investment income, and the balance is collected as premiums. If premiums at current rates are expected to be insufficient, a rate increase application is submitted to BCUC (or a rate reduction in case of surplus, as happened in 2010).

The premium rate for Basic insurance increased in 2007 and was reduced in 2010 (no rate changes in 2008 or 2009), with the result that 2011 premiums were almost the same as five years ago.

As shown in the following graph, total revenues, including investment income, covered the costs from 2006 – 2010. In 2011 revenues for Basic insurance were less than costs, primarily because increasing BI costs and decreasing investment returns were worse than forecast. As a result, for 2012 ICBC requested a rate increase of 11.2%, and has received an interim approval by BCUC.




In an effort to minimize Basic rate increases, the province has recently directed that the Basic MCT be allowed to fall to 100% through January 2015. Without this intervention, the MCT target of 130% would apply, and the 2012 increase would have been higher.

## Optional Insurance

Optional insurance rates are not regulated; ICBC sets the rates, aiming to be competitive with the private insurers who sell optional coverage in BC. ICBC has been able to maintain optional premiums at a level that are competitive and sufficient to generate a profit.

Total premiums and fees increased from $1,555M in 2007 to $1,642M in 2011 as a result of increased number of policies sold. Average premiums per optional policy have decreased over the last five years, including 2012.

Rates are designed to cover costs and maintain a Board-approved MCT level, currently at 260%. Amounts of capital above this level are paid to the province as dividends. Optional insurance has generated profits each year, which were retained to build up ICBC's equity, from $314M in 2002 to $3.8 billion in 2010, at which point dividends were paid to the province ($576M in 2010 and $101M in 2011).

Private insurers have not gained a significant share of the BC market but they have the advantage of choosing to only insure lower risk drivers and geographical locations, which allows them to select the more profitable parts of the market. ICBC responds to this competition by using steeper discounts and more sub-territories for Optional rate setting, but no customers are denied insurance and drivers are not charged more based on age.

Individual Rates

Individual rates are based on the claims history of the vehicle owner (discounts are given for history of no claims) and territory (urban centres have a higher rate of accidents).  Legislation directs that for Basic insurance there is to be no discrimination based on age, sex, marital status, etc., and ICBC applies this same policy for Optional insurance.  A seniors discount applies to both Basic and Optional.

For each year without a chargeable claim, an insured person moves down a level in the Claims Rated Scale (CRS) discount table.  There are 20 discount levels which offer premium discounts and/or other benefits; however the Basic discount rate is 43% for all the levels from 9 to 20, which means that customers at these levels have the same discount.  Under the current system, someone who has earned the maximum discount can cause three accidents and still continue to receive the same 43% reduction.

BC is the only North American jurisdiction that still bases its premiums on the vehicle owner rather than driver.  The current CRS model is scheduled to be replaced by a Driver Risk Model as part of the TP.  ICBC conducted a public consultation on this topic in May and June of 2012, with the results due to be released in August.

### 2.3.2 Other Canadian Jurisdictions

Provinces have different auto insurance systems with different coverage and rules.  In addition, data on premiums is not readily available, making it difficult to compare rates across jurisdictions.

Provinces with public insurance providers [BC, Manitoba (MB), Saskatchewan (SK), Quebec (QC)] have less variation between premiums charged to new drivers and experienced ones.  As a matter of public policy, there is no discrimination based on age, gender or marital status.

MB, SK and QC predominately use a no-fault system where accident victims receive a defined level of benefits, regardless of who is responsible for the collision.

In jurisdictions with competitive markets, insurance companies use as much data as possible to fully price the risk of insuring a person, which leads to wider variations, with higher premiums for young drivers and lower premiums for drivers belonging to statistically safer demographics.

Several provinces have experienced premium increases, prompting government action through legislative changes to contain claims costs.  Ontario and Newfoundland instituted deductibles, which had an effect for a limited time only, before premiums started to increase again.  Alberta, Nova Scotia, and New Brunswick (NB) had more long term success with caps on minor injuries.  NB also created a regulatory agency with the power to approve rate increases by insurance companies.

## 3.0 Investment Management

ICBC uses sound practice in managing its investments. Proper governance structure and practices are in place and the investment department has generally achieved above average results.

Insurance premiums are invested to provide a return and managed so that claims can be paid as they arise. Like any insurance company, investment income is a substantial part of ICBC's revenue.

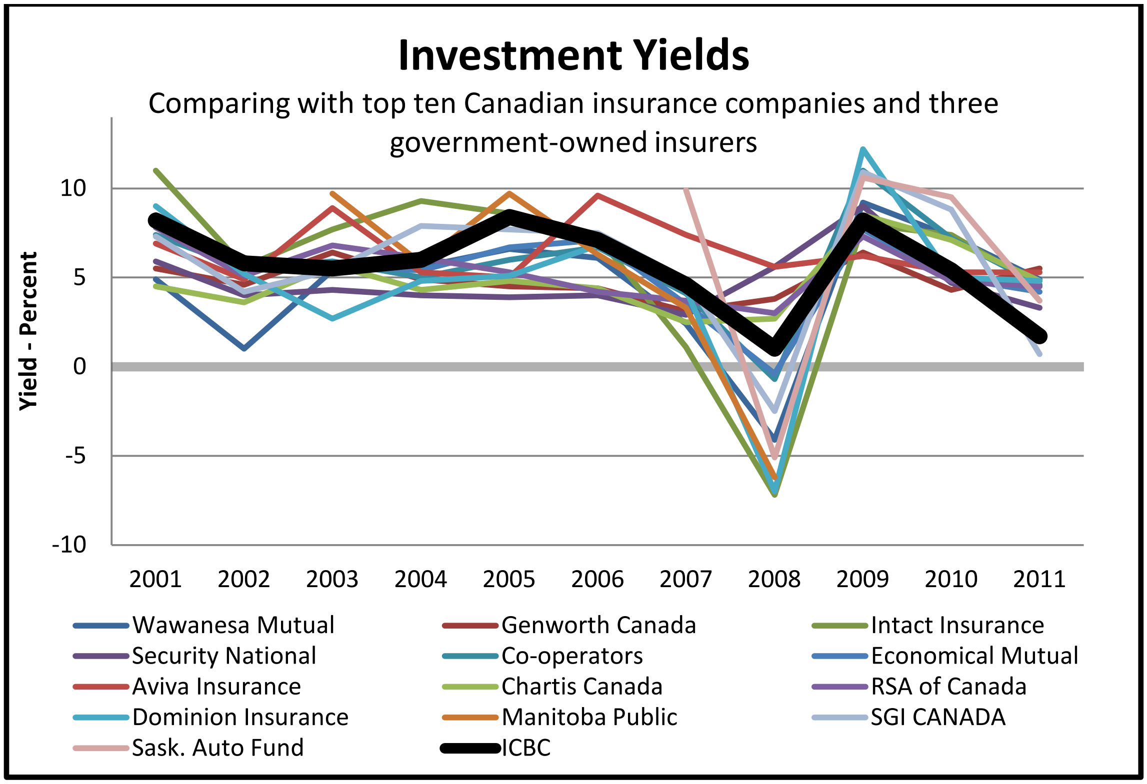
Performance of Investment Assets

ICBC had $11.4B in investment assets in 2011, comprising of:

| | |
|---|---|
| Bonds and Money Market | $7.5B |
| Equities | 2.4B |
| Mortgages | 1.0B |
| Real Estate Properties | 0.5B |
| Total: | $11.4B |

These assets generated an income of $441M in 2011 ($530M in 2010). Investment income helps reduce the premiums that would have to be paid by policy holders. Recent years have seen a period of global economic uncertainty with declining interest rates and volatile equities markets, resulting in reduced investment income.

Overall portfolio performance reflects the conservative investment approach taken by the department. The chart below shows performance against the ten largest Canadian P&C insurers and three government owned insurers. ICBC, represented by the prominent black line, has achieved better than average returns over the majority of the last ten years. Their decline in 2011 was in large part due to an unrealized loss on equities, while other companies reduced their equity allocation after the economic downturn of 2008.




*Source: MSA Research Inc., MSA Report 2012, 2011 and 2006.*

Governance and Management

ICBC manages the bond/money market, mortgage, and real estate portfolios internally, while equities are managed externally. The portfolio has usually generated an excess value-added[1] return well above investment department management costs.

Although not regulated like other insurers, ICBC follows sound practice, such as the OSFI guidelines. Policy is approved by ICBC's Board, on recommendation of the Investment Committee, and is revisited regularly to ensure appropriate portfolio mixes.

Due diligence is performed when hiring equity investment managers and there is appropriate oversight by the investments department. Total fees paid to managers and internal staff compare favourably to industry averages.

[1] Portfolio value-added is a function of identifying trading opportunities for "relative value" – actively managing the portfolio to obtain higher returns than would be obtained from a passive "buy and hold" approach.

## 4.0 Insurance Brokers

ICBC sells its product through independent brokers, also known as Autoplan agents, who sell Basic insurance for ICBC. At the same time, they act as independent brokers for the Optional insurance, where they offer a choice of ICBC or private insurance products.

Almost all ICBC insurance is sold through the 906 Autoplan brokers. In addition, ICBC runs an in-house Autoplan Sales Centre at their headquarters in North Vancouver where the product is made available directly to customers. When necessary, in very small remote communities, government agents are appointed to sell insurance.

Legislation allows ICBC to appoint brokers as needed, but since 1992, ICBC's policy has been to not issue new licences. ICBC feels there has been no demonstrated need and supporting a larger network is likely to be more costly.

An Autoplan agency license is valuable given the limited number. It can only be obtained from an existing broker and cannot be terminated unilaterally by ICBC. The requirement to purchase Basic insurance from an Autoplan agent guarantees business. Brokers are allowed to change location, as long as the provincial network continues to serve each community.

Some larger brokers have purchased multiple licences. There are only 250 distinct brokers in the market and 57% of total premiums are sold by the top 20 broker-groups.

### 4.1 Commissions

Brokers are paid commissions of varying size by the insurance companies. ICBC paid over $325M in commissions in 2011 ($311M in 2010). On average, 8.9% of premiums go to broker commissions (about 3% for Basic and 14% for Optional).

Basic Autoplan commission is a flat fee-per-transaction. A set amount is paid for each transaction. ICBC sets these rates after consulting with the broker community while taking into account inflation, labour costs, lease rates, etc. Optional insurance commissions are percentage-based and are intended to be competitive with private insurers

Other Costs

In addition to the regular commissions for Basic and Optional premiums, ICBC has recently implemented two award programs, based on specific performance criteria including: customer service, complex transactions, and compliance with procedures.

The Broker Performance Award commenced in 2010 and has an annual budget of $1.8M. 624 brokers qualified in 2011, achieving the seven key targets of the program.

The Customer Service Award was launched in 2011, and totalled $3.5M for the partial year. The top ten award earners received between $10,508 and $17,993, while the bottom ten award earners received between $64 and $408. Almost all (901 of 906) brokers qualified for at least a portion of the award, which is primarily based on a customer survey by a research firm. The program has a budget of $7.4M for 2012.

Brokers also receive compensation for other services provided, such as debt and tax collection for the province. For 2011, these fees, together with payment plan fees and miscellaneous transactions, totalled $30.7M.

ICBC's broker support system has 104 employees, such as broker account reps, managers, and call centre operators who answer questions on more complicated transactions. The annual operating cost for the support system is $9M.

### 4.2 Broker Network

ICBC considers Autoplan brokers key business partners and the relationship with them vital to maintaining their Optional market share and revenues, and as such cultivates the relationship between the larger brokers and ICBC executives.

The independent broker network is necessary for maintaining a market-based Optional insurance in BC as it allows private insurers an access to car insurance customers. Although independent brokers are paid commissions, they do not represent insurance companies. A broker's primary duty is to the customer and the customer should be offered the best policy for their needs.

Since ICBC feels the current model serves the needs of the corporation and their customers as well as allowing for a competitive market on Optional insurance, no alternative distribution model has been considered, such as direct selling online or through their own offices.

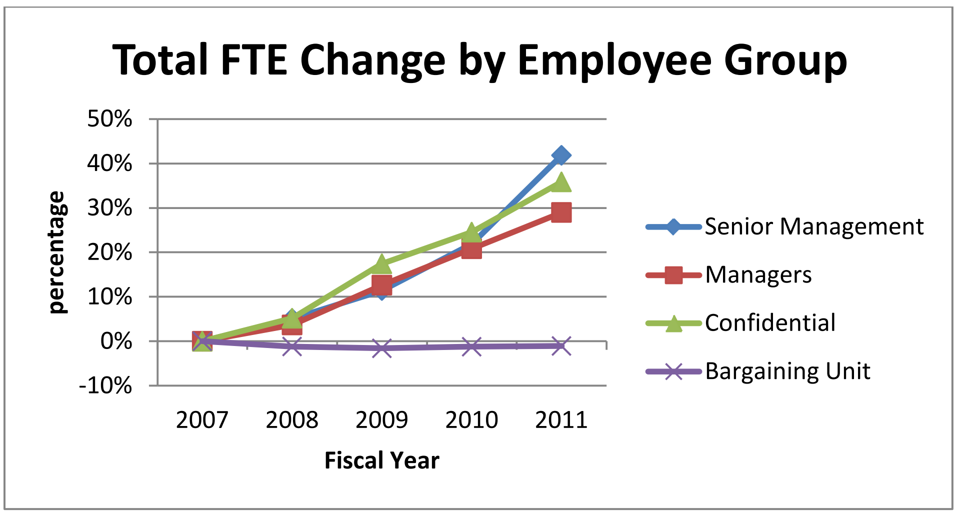
## 5.0 Operations

### 5.1 Staffing

ICBC's FTE positions increased from 4,947 in 2007 to 5,176 in 2011, and includes those assigned to TP. Despite the economic downturn and cost containment strategies implemented by the province since 2008, ICBC continued to grow, adding 272 management positions across the organization representing an increase of 32% in non-union positions.

The chart below illustrates the trends of FTE growth by employee group from 2007 to 2011:

- Senior Management (Directors and above) increased from 49 to 69 (40.8%);
- Managers increased from 537 to 692 (28.9%);
- Confidential employees (non-union technical and administrative positions) increased from 269 to 366 (36.1%); and
- Bargaining Unit FTEs decreased from 4,092 to 4,049 (-1%).




All divisions saw an increase in Management and Confidential employees during this period.

ICBC anticipates there will be 364 staff reductions upon completion of TP in 2017. These reductions will be in the Claims division and expected to be achieved primarily through attrition.

As a result of the growth in management and slight decline in the bargaining unit, the span of control (management to bargaining unit employees) declined from 1:7 in 2007 to 1:5 in 2011.

Both ICBC's Human Capital Plan and Organizational Design Policy include the goals of maximizing span of control and reducing management layers, although deadlines have not yet been established.

## Recommendations:

(5) **ICBC should reduce total management and confidential staffing to a level more consistent with 2008.**

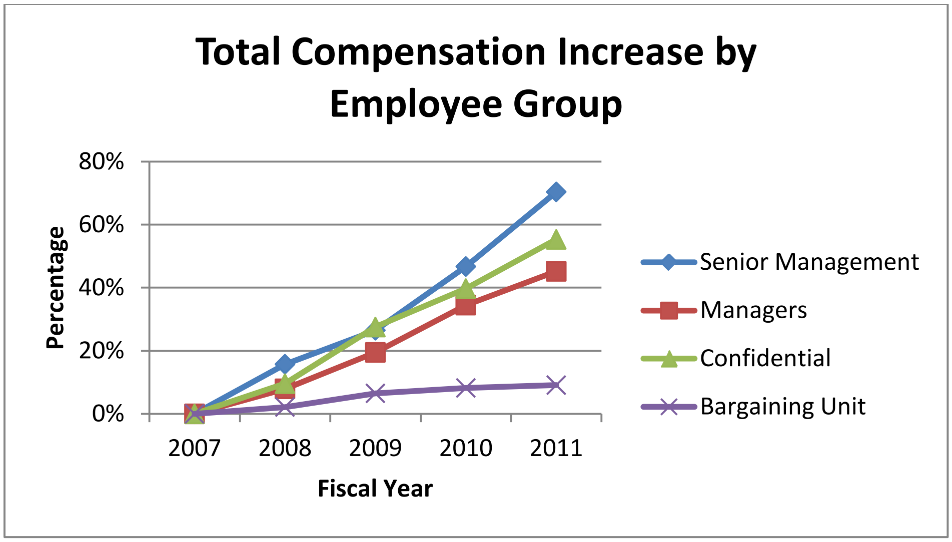
(6) **ICBC should develop action plans, with timelines, for maximizing span of control and reducing management layers across the organization.**

### 5.2 Compensation

As a result of the economic downturn in 2008, the BC government limited salary increases to deal with fiscal pressures. However, in the last five years, total management compensation cost at ICBC has increased 50% ($52.5M) due to new hires and salary increases.

From 2007 to 2011, the compensation for:

- Senior Management (CEO, Senior VP's, VP's and Directors) increased by 70%, from $12.3M to $20.9M;
- Managers increased by 45%, from $67.2M to $97.6M;
- Confidential increased by 55%, from $24.3M to $37.7M; and
- Bargaining Unit increased by 9%, from $265.6M to $289.8M.




Between 2007 and 2011, senior management's salaries increased an average of 20% ($51,000), compared to an average increase of 10% ($6,700) for the Bargaining Unit employees.

The table below shows the number of employees earning between $75,000 and $200,000 increased by 52% and those earning over $200,000 increased by 315% in the last five years.

| Employees earning | 2007 | | 2008 | | 2009 | | 2010 | | 2011 | |
|---|---|---|---|---|---|---|---|---|---|---|
| | # | % | # | % | # | % | # | % | # | % |
| $75K - $200K | 848 | 17.1% | 981 | 19.9% | 1,182 | 23.6% | 1,285 | 25.3% | 1,291 | 24.9% |
| > $200K | 13 | 0.3% | 24 | 0.5% | 32 | 0.6% | 53 | 1.0% | 54 | 1.0% |

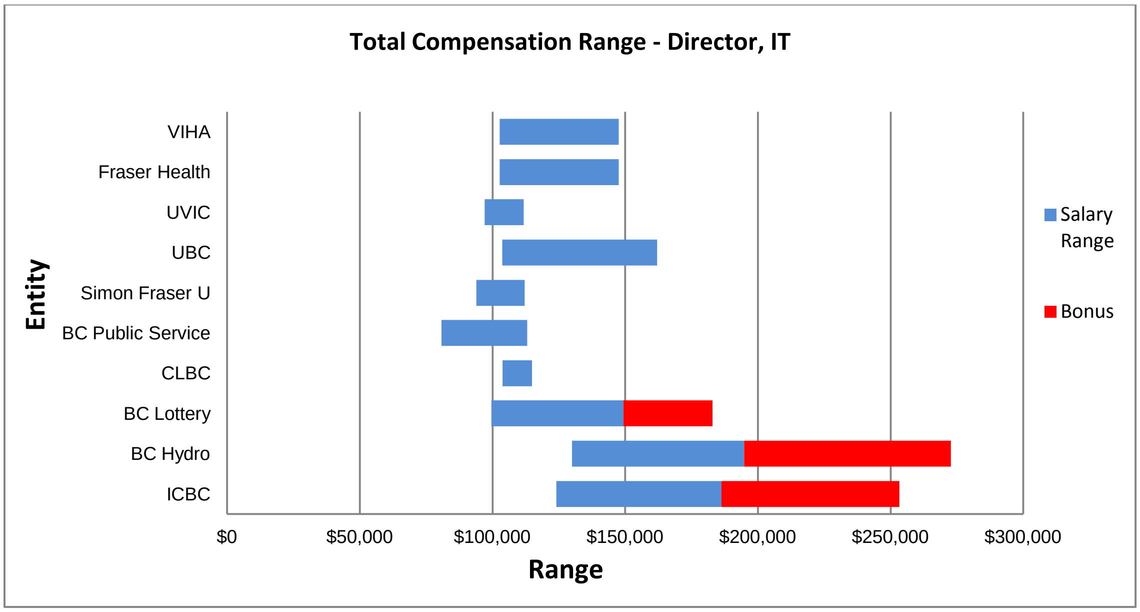
## Management Compensation

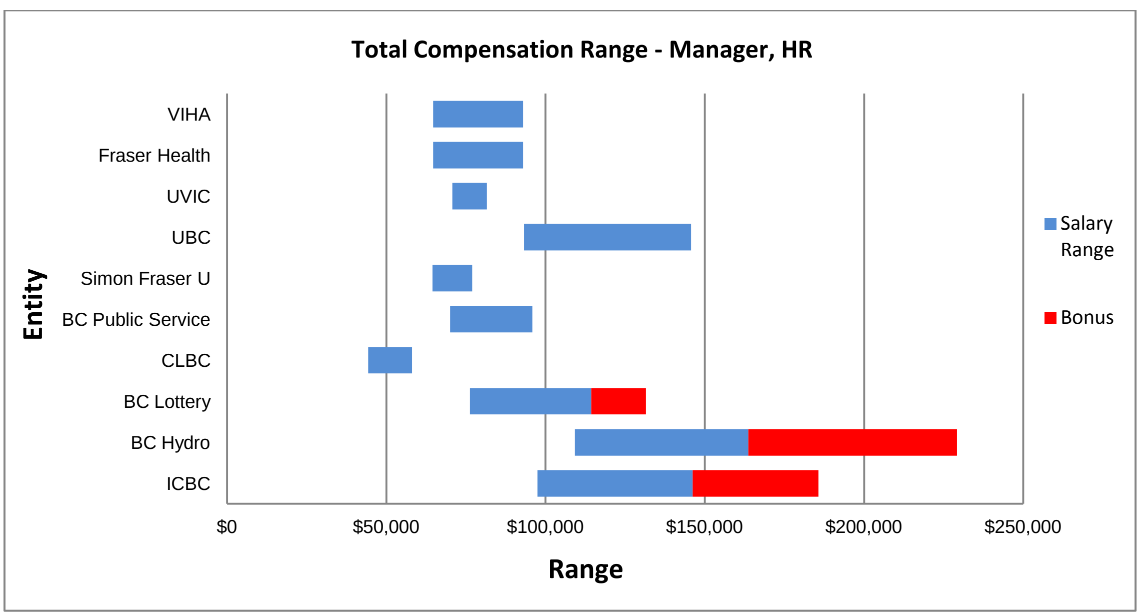
ICBC has a management compensation framework that it considers to be market competitive for its executive, senior management, managers, and other excluded staff.

Compensation consultants are commissioned on a regular basis to monitor salaries in general industry, insurance companies, and the public sector, to ensure ICBC's compensation is competitive. Among the public sector entities selected are Canada Mortgage and Housing Corporation, Federal Government of Canada, and the Government of Alberta. The province, despite being the shareholder of ICBC, was not included as a comparator.

The framework is reviewed and approved by the Board annually, and allows ICBC to align their salary structures with the comparators. Individual merit-based increases are awarded based on performance. In the last five years, these increases have resulted in ICBC's management being among the highest paid within the BC public sector.

Based on data provided by Public Sector Employers' Council and ICBC, management salaries are consistently in the top two among BC public sector organizations. A comparison of compensation for other public sector organizations is shown in the following graphs. Overall, salary ranges of directors and managers of Finance, HR and IT appear to be consistently amongst the highest paid. It is important to emphasize that a full compensation analysis was not completed; these comparisons did not assess the level of responsibility, position complexity, and labour market between these comparators.



Special Salary Adjustments

ICBC also provides for special adjustments that increase the employee's base salary. These are provided to management where ICBC believes that market adjustments are required or there is risk that the employee might resign. Some management employees have received adjustments more than once within a five year period (two employees received special adjustments in four out of the last five years).

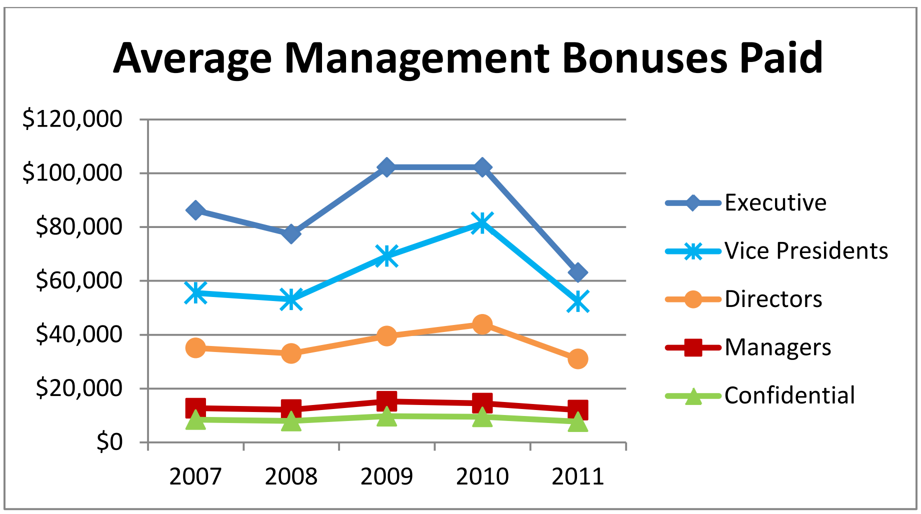
When the compensation framework was introduced in 2007 a number of adjustments were made to address perceived market inequities. The highest salary adjustment made in 2007 was $66,455 (34.2% of base salary) for an employee considered to have valuable skills and be at risk of leaving. More recently, the number and dollar value of special adjustments has declined and in 2011 the highest adjustment was $17,000 (7.2% of base salary).

Bonus

ICBC has a bonus plan for both management and bargaining unit staff, the total bonus paid out in 2011 being $18.1M. Prior to 2011, bargaining unit employees received approximately $2,100 per year. In 2011, this decreased to under $1,000 each.

Management employees received bonuses based on three components: corporate, divisional and individual performance.

Once targets are established, payments are determined by mapping the performance levels onto a scale ranging from 0% to 150%. Over the last five years, over 95% of the management employees received a bonus.




Prior to 2011, at least 90% of management received 100% or more (from the 150% available) of the eligible bonus. For 2011, ICBC adjusted their bonus structure, but still saw over 85% receive at least 75% of their eligible bonus.

Although ICBC introduced a financial trigger for the bonus plan commencing in 2011, the target is unreasonably low. The trigger requires ICBC to first achieve a corporate net income of $35 million before allowing any bonus payments; ICBC has not had a net income below $140M in any of the last five years.

### Pension

Management employees are members of the ICBC Pension Plan, which is funded through contributions made by ICBC (2/3) and the employees (1/3); normal practice in the public sector is closer to 1:1. In addition to the pension plan, ICBC has established a Supplementary Employee Retirement Plan which is funded entirely by ICBC for management employees earning over $149K. Since 2010, bonus payments have been included in pensionable earnings; management has 15% of their bonus pay included while senior executives have 100% included.

### Signing Bonuses and Relocation Plans

Signing bonuses are paid to management employees and since 2007 approximately $365,000 has been paid, with the highest individual amount being $40,000.

ICBC has three relocation plans for new hires (management, directors, and Executives) that provide considerable flexibility in reimbursing relocation expenses. Further, senior management can approve expenses in excess of the plan as they are only considered to be guidelines.

Relocation expenses for two of the new hires reviewed included reimbursements of:

- $188,000 - including $88,000 for the loss on the sale of the employee’s house.
- $131,000 – including temporary accommodation of approximately $4,500/month (exceeding the policy of $2,500/month).

### Other Benefits

Senior management receives perquisite allowances ranging from $15,500 to $18,500 annually to cover items such as vehicle allowances, etc., paid bi-weekly as a cash allowance.

Management and bargaining unit groups have vacation entitlements and benefits that are broadly comparable to BC Public Sector. More generous areas include overtime for bargaining unit employees, and short-term sick leave packages.

Termination of Employment

In the last five years, ICBC has spent over $25M in severance and salary continuance payments. In addition, senior management is eligible for perquisites and bonus payments after being terminated as they are regarded as having met the corporate and divisional performance objectives.

Instances included payments of $17,000 for perquisites and $57,000 for bonus payments, as well as a $110,000 non-competition payment.

## Recommendations:

(7) **ICBC should reduce total management and confidential compensation to a level more consistent with 2008.**

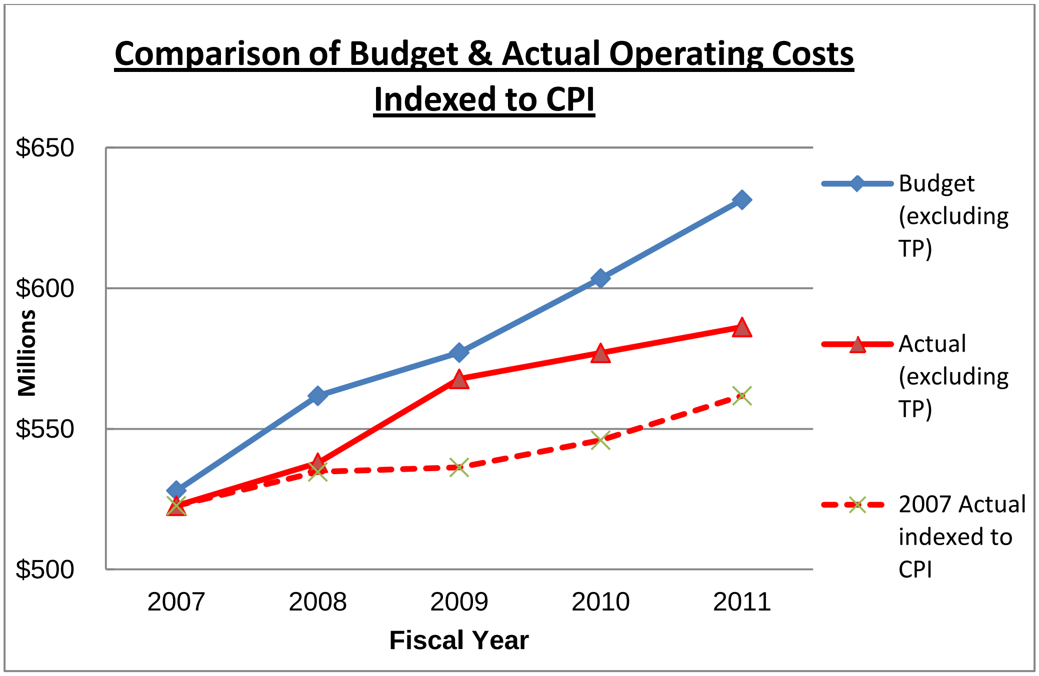
(8) **ICBC should bring their compensation framework more in line with the greater public sector and ensure more consistent compliance with policies.**

### 5.3 Other Expenses

The corporate budgeting process is decentralized leading to inconsistent practices across the organization. ICBC's use of an incremental approach to budgeting is not challenging the organization to reduce costs and, as a result, inflated budgets continue, allowing divisions to easily achieve favourable results.

Corporate budget guidelines and assumptions are provided to the divisions which assist with planning and monitoring. A variance report, comparing budget and actual, is prepared monthly to further assist with monitoring.

Over the last five years, the operating cost budget, excluding costs associated with TP and the profit and loss on disposal of assets, has increased by 19% ($100M) and has always exceeded actual results. This is illustrated in the following graph, which takes 2007 actual results and increases them at the rate of the CPI to demonstrate how much operating costs have outpaced inflation.




Setting budgets that are too easily met does not sufficiently challenge ICBC, at an organizational level, to find savings. Introducing the rigor of a zero-based budget would help detect inflated budgets and assist with finding cost-effective ways to deliver operations.

### Operating Expenses

Operating expenses, excluding compensation, totalled $185M in 2011 and included building expenses, staff relations, IT, training, and corporate promotions.

ICBC's expense policies are generous when compared to the BC Public Service and are deemed to be guidelines with exceptions approved by senior management. A culture of cost-containment and financial discipline has been lacking in recent years. In 2011, ICBC spent approximately $1.8M on staff relations including Christmas parties and staff lunches. Further instances of a lack of fiscal restraint were identified within operational expenditures such as out-of-province training, travel, retreats with golf and wine tours, etc.

### Functional Review

In November 2011, ICBC began a functional review of its corporate services to identify areas which can be streamlined across the organization. These services include budgeting, procurement and purchasing. The review was temporarily suspended in February 2012 as ICBC resources were redeployed to assist with the government review and the BCUC application. ICBC intends to resume this review.

ICBC indicated that corporate services represent 16% of total FTEs.  Previously, ICBC had conducted a similar review for their information management function which saw the realignment of information management resources under the Information Services Division (ISD).

## Recommendations:

(9) **ICBC should regularly conduct detailed reviews of the budget to ensure costs are contained and aligned with the Province of British Columbia's priorities.**

(10) **ICBC should strengthen their oversight of the corporation's expenses to instil a culture of cost containment and financial discipline.**

### 5.4 Procurement

ICBC spends approximately $1.5B annually to procure goods and services.  The majority of these expenditures relate to suppliers for claims ($855M) followed by commissions paid to insurance brokers ($329M).  The remaining $300M per year is spent on operations.

Key Business Partners

To deliver its services, ICBC works with a series of key business partners including: independent insurance brokers who provide auto insurance products and services to the public, an extensive network of suppliers in the automotive industry, medical services providers, and legal services providers.

**Breakdown of Procurement by Key Business Partners**

| Partners | 2011 in millions |
|---|---|
| Collision Repair Shops | $500 |
| External Lawyers | $135 |
| Medical Services | $ 70 |
| Glass Shops | $ 35 |
| Other (rental vehicles, private investigators, towing and heavy equipment) | $115 |
| **Claims Total** | **$855** |
| **Insurance Brokers** | **$325** |
| **Total** | **$1,180** |

Prior to the March 2010 amendments to the *Federal Competition Act*, ICBC would negotiate rates with industry associations of insurance brokers and auto body shops. The *Act* introduced significant amendments which caused concerns that setting prices with groups of suppliers may be a contravention of the *Act*. As a result, ICBC has assumed a new model where it establishes rates unilaterally, using industry data collected through third party surveys and other relevant data.

Operations

ICBC spends approximately $300M on operations using a combination of competitive and non-competitive processes. For public procurement of higher value contracts, ICBC designed an Expressions of Interest (EOI) process to select the best product or service that places the primary emphasis on the best technical solution.

In many cases, this results in cost being a secondary consideration and the selection process not clearly demonstrating value for money. More than 65% of the 283 competitive bids conducted by ICBC over the last five years were carried out through EOI.

ICBC has direct award (non-competitive procurement) thresholds of over $25,000 for goods and $100,000 for services in keeping with provincial trade agreements. Since 2010 ICBC has direct awarded a significant number of contracts (more than 50%), which includes contract extensions, and requires the reasons to be documented and approved. A high percentage of direct awards reviewed did not have an appropriate justification, yet were still approved by management.

Acquisitions made under these direct award thresholds are referred to as direct payments by ICBC and are required to have at least three quotes.  Of the direct payments sampled, 56% did not have quotes and 44% only had two quotes.

Procurement Management

At ICBC, the procurement function is decentralized; each department procures the specific goods and services necessary to operate with support from Supply Management, which is responsible for overseeing all activities related to the acquisition of goods and services within ICBC.

Although ICBC has a Corporate Acquisition Policy with the objective of maximizing value for money, the lack of an effective reporting system does not allow for appropriate monitoring of key performance indicators that would ensure this objective is being met.  This policy is a framework for all types of procurement and applies to all departments, setting the expectation that ICBC will procure goods and services in an open, ethical and transparent manner.

ICBC has established performance indicators to evaluate some of its key business partners, but infrequently conducts post-contract evaluations.

ICBC has comprehensive conflict of interest policies and procedures in their Code of Ethics, which applies to all Board members, employees, and contractors.

Best practices in procurement require a vendor complaint and dispute resolution mechanism that provides suppliers with an opportunity to raise concerns related to supply management processes and to request a review of those processes deemed inappropriate.  ICBC is developing a new Corporate Acquisition Policy and plans to include such a mechanism.  This would enhance the relationship with key business partners by formalizing the channel for concerns to be heard and addressed.

Some of the solicitation documents selected for the review could not be examined as the documentation had been destroyed, despite the contract still being in effect.  This was in accordance with ICBC's records retention policy.

## Recommendations:

(11) **ICBC should more clearly demonstrate value for money in procurement, using competitive processes whenever possible.**

**(12) ICBC should develop relevant key performance indicators to ensure it can appropriately monitor its procurement process and performance.**

**(13) ICBC should strengthen the procurement process through the implementation of a vendor complaint and dispute resolution mechanism, and a post-contract evaluation process.**

**(14) ICBC should amend their records retention policy to prevent the destruction of documentation for ongoing contracts.**

## 5.5 Information Technology

Overall, the IT function within ICBC is effectively governed and supported by a comprehensive IT strategic planning process that ensures business and IT alignment over the long-term.

The IT function at ICBC is represented by the ISD. As of December 2011, ISD had about 570 FTEs and 70 contractors managing over 450 applications supporting the Claims, Insurance, and DL businesses.

ISD is led by a Chief Information Officer (CIO) who has a direct reporting relationship to ICBC's CEO. The CIO has the appropriate authority, responsibility, accountability, and reporting lines to effectively lead the IT function.

Although processes required to effectively run the IT function are established, some are not properly documented (e.g., portfolio management, system backups, IT trend analysis, etc.). Documenting these procedures would help with consistent operations and minimize over-reliance on key personnel.

Information Systems

ICBC's main business applications are aging custom built systems, dating back to the 1970's. A key driver for their TP has been the replacement of these systems.

Despite their age, ICBC's core systems are reliable, in part due to the current performance and capacity planning processes for the mainframe systems. However, ICBC acknowledges that these processes are not suitable to manage the future requirements of the post TP environment.

As a result, ICBC commissioned a study to determine the changes required to ensure proper oversight of the future IT environment. The review concluded in 2011 with several recommendations that ICBC has begun to action.

Disaster Recovery

Disaster Recovery (DR) Planning is an IT function that ensures controls and processes are in place to recover the IT capacity of an organization in the event of a disruption (e.g., fire, earthquake, flood, power outage, data breach, etc.). ICBC has plans in place that are tested annually to recover their current systems after a disruption in service. However, as new systems are being implemented through TP, new DR plans are required to ensure the timely recovery of these new applications.

IT Security

The new IT infrastructure and systems to be delivered through TP require a more robust information security function than currently exists. While progress is being made towards remediating the information security risks, attention is required to address the following issues:

- The IT security function does not have the appropriate authority or reporting relationship to effectively govern security.
- Several IT security related recommendations of the ICBC's 2011 Technology Alignment Strategy review are still in progress or outstanding which may put the new IT environment at risk if not completed in a timely manner.

## Recommendations:

(15) **ICBC should ensure that IT processes are appropriately documented.**

(16) **ICBC should ensure that new disaster recovery plans are developed and tested before the new Transformation Program systems are implemented.**

(17) **ICBC should ensure the IT security function has the appropriate reporting relationship and authority in the organization.**

(18) **ICBC should prioritize and implement the remaining security initiatives stated in the Technology Alignment Strategy, given the significant risk and impact to the Transformation Program and new IT environment.**

# 6.0 Transformation Program

ICBC is undergoing a multi-year project, called Transformation Program, aimed at updating its business processes and aging technology infrastructure that supports ICBC's services.

TP is a series of projects which include the modernization of claims and insurance processes and systems, building and managing customer relationships, and making rates more reflective of driver risk. TP commenced in 2010 and is expected to be fully implemented by the end of 2017. The cost of TP is limited to $400M and is funded from Optional insurance.

Overall, TP has the key processes in place to support program execution and monitoring, and appears to be adequately documented and resourced. However, planning was not sufficiently detailed, which has led to impacts on project budget estimates, project benefits and timeframe.

## 6.1 Project Management Practices

Although key planning steps were carried out for TP, more detailed planning should have been applied in particular on scope, budget and benefits. Project initiation and planning are the initial stages in the project lifecycle and require a detailed analysis. The following examples illustrate a lack of comprehensive planning:

- December 2011 estimates projected cost for Claims portfolio increased by 51% from December 2010. This increase is to reflect more realistic costs and higher-than-anticipated complexity integration requirements with other ICBC Systems.
- The breakeven point for TP has been moved from 2019 to 2022 due to adjustments in timing of benefits realization, along with high level planning and early project assumptions.
- The financial benefits have not been fully identified across ICBC as discussed later in this section. This was in part due to the lack of a framework for defining and measuring benefits, which was not a priority at the planning phase of TP.

In addition, the Program is not clearly separated into phases which would enhance the communication and reporting to Government and facilitate managing the scope against the budget.

As ICBC implements individual TP projects, they use sound project management practices to oversee the execution and monitoring. For example:

- A centralized program management approach.
- Advice and guidance for the execution of TP is provided by independent risk and business advisors, and a systems integrator.
- The governance model includes a TP Committee, which is a committee of ICBC's Board of Directors established to assist the Board in its oversight of the Program.

## Recommendations:

**(19) ICBC should provide interim progress reports to the Province of British Columbia on the costs, scope, benefits, and schedule of each Transformation Program phase, along with any variance explanation.**

**(20) ICBC should formally involve the Province of British Columbia with significant IT projects to leverage public sector experience and lessons learned from other large scale initiatives.**

### 6.2 Other TP Areas

TP Risk Assessment

A formal project risk management process has been established for TP, with periodic reviews performed to provide an assessment of project management practices, deliverables and activities. In addition, quarterly risk assessments are conducted by a third-party risk advisor. The advisor includes a review and validation of ICBC's internal risk assessment for the Program. The identified risks and related recommendations are communicated within the program governance structure, including the Transformation Program Committee.

According to recent risk assessment reports, progress is being made towards mitigating the major risks identified. However, key risk areas such as data migration, legacy system decommissioning, as well as the ability of the IT function to support and sustain TP still require greater focus and priority from ICBC given the complexity and impact of these areas to the Program.

Timelines and Scope Changes

The expected completion of TP has shifted from late 2016 to late 2017 to reflect scope refinements and more detailed requirements. Projects within TP are at varying stages.

The result of the quarterly risk assessment conducted by the third party risk advisor indicates that scope management processes for TP appear to be operationally effective. While there have been scope changes and refinements to reflect increased clarity of project requirements, no significant scope reductions had occurred at the time of our review that would impact the strategic objectives of the Program.

Considering the complexity and inter-dependencies of TP projects, managing scope against the established budget for the Program may become more challenging as individual projects advance. A continued focus on scope management is required to ensure that capabilities are not removed from scope to address budget and/or deadline constraints.

TP Budget

Overall the TP remains within budget. As at December 31, 2011, the total cost of the Program (expense and capital) was $114.7M. The cumulative total budget for this period was $152M. ICBC is in year three of TP with $124.2M (31%) spent as of February 2012. This is consistent with the overall progress of the Program, which was estimated to be 35% complete at the time of this review.

The Program's total projected costs remain at $400M. ICBC estimates that increases in project portfolio costs are expected to be offset by equivalent decreases of other TP costs such as program management, IT parallel processing and contingency.

TP Benefits

While TP is expected to allow ICBC to meet increasing customer expectations, ensure the future reliability and adaptability of the systems, and improve services and options to both Basic and Optional insurance policyholders, financial benefits have not been fully quantified across the corporation.

The full annual financial benefits of TP are currently estimated at $93.4M and are expected to be fully realized as of 2018. However, they are derived almost exclusively from one single division (Claims). The implementation of a framework for defining and measuring benefits was not a priority at the planning phase of TP, which contributed to the above issue. As a result, the estimated annual benefit is expected to be higher in the future as ICBC better accounts for the benefits.

## Recommendations:

(21) **ICBC should ensure that key areas identified in Transformation Program risk assessments are promptly addressed.**

(22) **ICBC should quantify the additional financial benefits to be realized from the Transformation Program.**

## 7.0 OTHER ITEMS

Under the *Motor Vehicle Act,* Office of the Superintendent of Motor Vehicles (OSMV) is the lead agency responsible for road safety in BC and has delegated certain programs to ICBC. On behalf of OSMV, ICBC provides services for vehicle registration, driver training and licensing, and administers the Vehicle Impoundment Program, Driver Improvement Program and Driver Fitness Program.

### 7.1 Road Safety

In 1981, ICBC began developing and implementing programs for road safety. ICBC's Road Safety unit has programs for drivers, vehicles and roads, which contribute to the objectives of preventing crashes and reducing severity of injuries to help control claims costs. Road Safety has sound planning and evaluation processes to ensure programs meet their objectives.

Budgeting and Funding

From 2007 to 2011, the average annual operating cost was approximately $42M. All programs, with the exception of the auto crime program, are fully funded by Basic insurance premiums. Auto crime program's costs are allocated between Basic and Optional insurance premiums based on a BCUC approved methodology.

Planning and Evaluation

Each program consists of a number of initiatives, for example, speed awareness campaigns, which contribute to the achievement of the overall objectives.

ICBC tracks the progress of programs through post-implementation reviews to determine if objectives and targets are being met. In addition, regular comprehensive program evaluations are conducted for the Intersection Safety Camera (ISC) and Road Improvement (partnerships with BC road authorities for projects ranging from road signage to road widening).

Outcomes and Benefits

Road Improvement and ISC are two programs with crash reduction benefits that have been quantified through relevant crash data. The results of the 2009 Road Improvement evaluation indicated an 11.9% reduction in property damage resulting in no injury, and a 19.6% reduction in incidents resulting in BI and death.

A 2009 study on ISC found the program contributed to a 4.9% reduction in total crashes, and a 4.3% reduction in crashes resulting in BI and death.

Quantifying the direct benefit of other road safety programs, like speeding and impaired driving, is more challenging. Nevertheless, ICBC monitors programs by tracking outputs and driver survey results which show changes in driver perceptions and attitudes.

## 7.2 Driver Licensing

ICBC's DL core services delivered across the province include issuing of driver licenses and administering knowledge and road tests.

### 7.2.1 Driver Licensing Operations

ICBC collects DL fees on behalf of the government, but only retains a small portion of those fees. In 2011, DL collected approximately $80M and retained $6.5M. DL operating costs are funded through Basic Insurance and were $54M in 2011.

DL is involved in two major government initiatives - Enhanced Driver License (EDL) and Enhanced Identification Card (EIC), and BC Services Card. In May 2009, ICBC began issuing BC residents EDL and EIC cards which are approved documents for travel to the U.S. by land or water. ICBC is also working with the Ministry of Health to produce BC Services Cards which will replace the BC Care Card.

### 7.2.2 Driver Licensing Systems

ICBC manages about 40 DL systems with the majority of the core systems being custom built mainframe applications. DL systems perform a variety of functions which are mostly related to data processing and storage in support of services provided by ICBC.

Application Security Controls

Overall, controls and procedures are in place to ensure secure access to the DL systems and related data. ICBC conducted internal assessments to evaluate the effectiveness of the processes to grant and remove access to the DL systems, and implemented additional controls to strengthen these processes.

Although ICBC has performed some access control reviews, comprehensive audits have not been performed recently to assess the design and effectiveness of other key internal controls over these applications. For example, data entry and output verification, audit trails, system authentication and interfaces, system documentation. This may impact the proactive identification and mitigation of system governance and security issues.

System Upgrade & Replacement Plans

Since the mid-1990s, ICBC has been responsible for managing and providing support to the DL systems. They have maintained and modified these systems to accommodate new business, security and technical requirements.

Despite a number of modifications undertaken by ICBC, many of the DL systems are nearing the end of their useful life and are in need of replacement. These systems lack the flexibility to accommodate new business requirements, place increasing reliance on key individuals due to a shortage of mainframe expertise, and have progressively higher upgrade costs.

No timelines have been established for the replacement of these legacy systems; however it is not expected to commence before completion of TP in 2017.

## Recommendations:

(23) **ICBC should ensure that comprehensive audits of the Driver Licensing systems are performed regularly, given the sensitivity of the information within the Driver Licensing systems.**

(24) **ICBC should place a higher priority on replacing the legacy Driver Licensing systems.**

## Appendix A

### SUMMARY OF RECOMMENDATIONS

| | |
|---|---|
| **1** | ICBC and the Province of British Columbia should develop a closer and more consistent relationship to improve oversight of ICBC and ensure alignment of priorities. |
| **2** | ICBC's Board should develop clear expectations on cost containment. |
| **3** | ICBC should develop and implement an overall strategy to more effectively manage bodily injury claims. |
| **4** | ICBC should review the utilization of internal and external legal resources to maximize cost effectiveness. |
| **5** | ICBC should reduce total management and confidential staffing to a level more consistent with 2008. |
| **6** | ICBC should develop action plans, with timelines, for maximizing span of control and reducing management layers across the organization. |
| **7** | ICBC should reduce total management and confidential compensation to a level more consistent with 2008. |
| **8** | ICBC should bring their compensation framework more in line with the greater public sector and ensure more consistent compliance with policies. |
| **9** | ICBC should regularly conduct detailed reviews of the budget to ensure costs are contained and aligned with the Province of British Columbia's priorities. |
| **10** | ICBC should strengthen their oversight of the corporation's expenses to instil a culture of cost containment and financial discipline. |
| **11** | ICBC should more clearly demonstrate value for money in procurement, using competitive processes whenever possible. |
| **12** | ICBC should develop relevant key performance indicators to ensure it can appropriately monitor its procurement process and performance. |
| **13** | ICBC should strengthen the procurement process through the implementation of a vendor complaint and dispute resolution mechanism, and a post-contract evaluation process. |
| **14** | ICBC should amend their records retention policy to prevent the destruction of documentation for ongoing contracts. |

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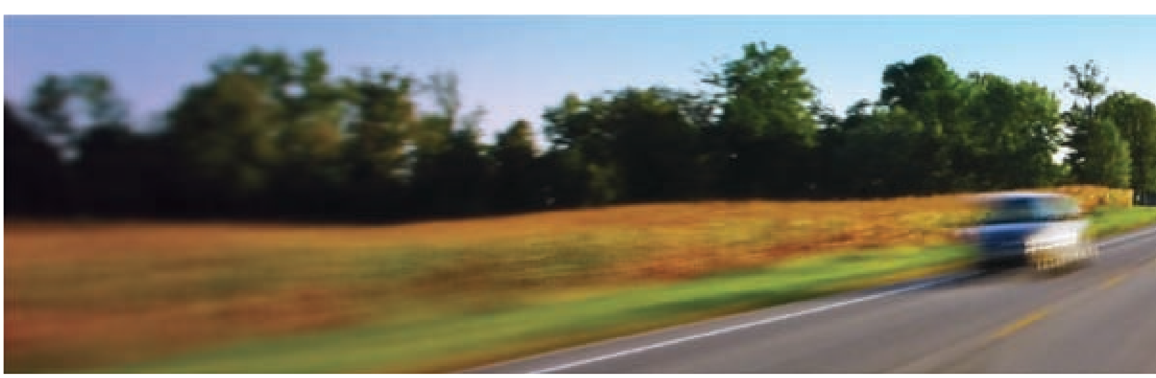
|---|---|
| **15** | ICBC should ensure that IT policy and procedures are appropriately documented. |
| **16** | ICBC should ensure that new disaster recovery plans are developed and tested before the new Transformation Program systems are implemented. |
| **17** | ICBC should ensure the IT security function has the appropriate reporting relationship and authority in the organization. |
| **18** | ICBC should prioritize and implement the remaining security initiatives stated in the Technology Alignment Strategy, given the significant risk and impact to the Transformation Program and the new IT environment. |
| **19** | ICBC should provide interim progress reports to the Province of British Columbia on the costs, scope, benefits, and schedule of each Transformation Program phase, along with any variance explanation. |
| **20** | ICBC should formally involve the Province of British Columbia with significant IT projects to leverage public sector experience and lessons learned from other large scale initiatives. |
| **21** | ICBC should ensure that key areas identified in the Transformation Program risk assessments are promptly addressed. |
| **22** | ICBC should quantify the additional financial benefits to be realized from the Transformation Program. |
| **23** | ICBC should ensure that comprehensive audits of the Driver Licensing systems are performed regularly, given the sensitivity of the information within the Driver Licensing systems. |
| **24** | ICBC should place a higher priority on replacing the legacy Driver Licensing systems. |



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