S&P Capital IQ

CONTENTS



# Intact Financial Corporation TSX:IFC

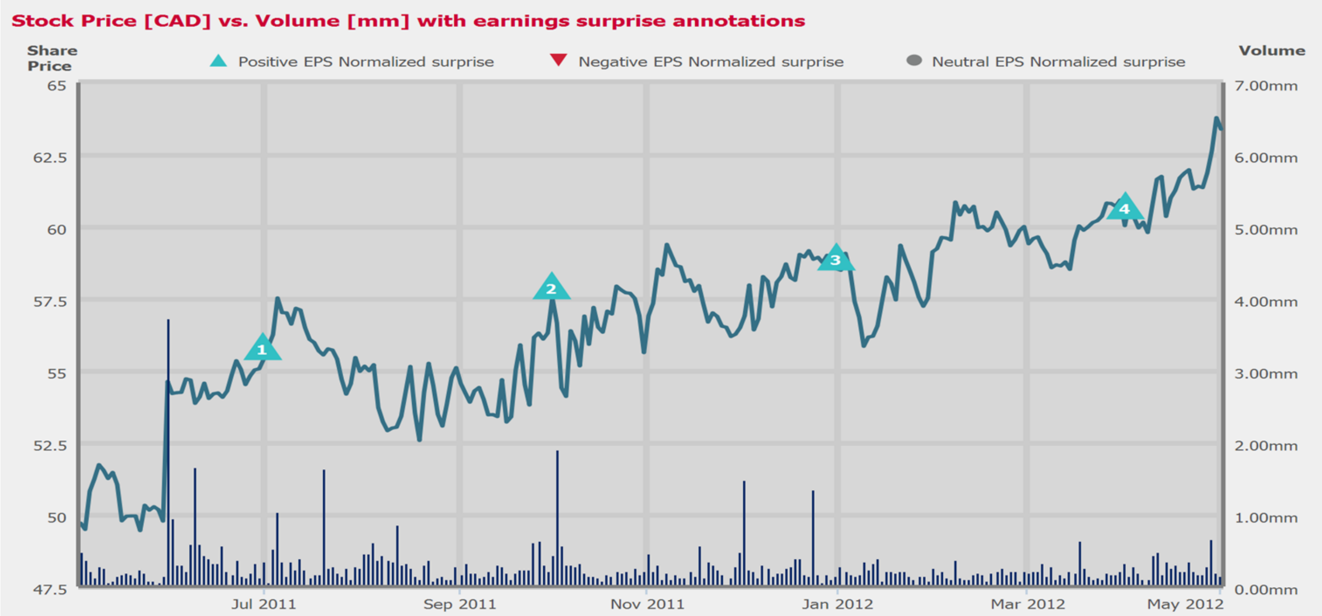
## *FQ2 2012 Earnings Call Transcripts*

Wednesday, August 01, 2012 3:00 PM GMT

## S&P Capital IQ Estimates

| | -FQ2 2012- | | | -FQ3 2012- | -FY 2012- | -FY 2013- |
|---|---|---|---|---|---|---|
| | CONSENSUS | ACTUAL | SURPRISE | CONSENSUS | CONSENSUS | CONSENSUS |
| **EPS Normalized** | 1.41 | 1.35 | ▼(4.26 %) | 1.42 | 5.43 | 6.31 |
| **Revenue (mm)** | 1673.79 | - | ▼(5.07 %) | 1703.90 | 6650.21 | 7188.47 |

Currency: CAD
Consensus as of Jul-26-2012 12:34 PM GMT




**- EPS NORMALIZED -**

| | CONSENSUS | ACTUAL | SURPRISE |
|---|---|---|---|
| **FQ2 2011** | 0.72 | 1.36 | ▲88.89 % |
| **FQ3 2011** | 1.03 | 1.11 | ▲7.77 % |
| **FQ4 2011** | 1.12 | 1.14 | ▲1.79 % |
| **FQ1 2012** | 1.25 | 1.34 | ▲7.20 % |

# Call Participants

## EXECUTIVES

**Alain Lessard**
*Senior Vice President of Commercial Lines*

**Charles Brindamour**
*Chief Executive Officer and Director*

**Dennis Westfall**
*Former Vice President of Investor Relations*

**Mark A. Tullis**
*Vice Chairman*

**Martin Beaulieu**
*Chief Operating Officer of Direct to Consumer Distribution and Senior Vice President*

## ANALYSTS

**Andre-Philippe Hardy**
*RBC Capital Markets, LLC, Research Division*

**Doug Young**
*TD Securities Equity Research*

**Mario Mendonca**
*Canaccord Genuity Limited, Research Division*

**Tom MacKinnon**
*BMO Capital Markets Equity Research*

# Presentation

**Operator**

Good morning. My name is Adam, and I will be your conference operator today. At this time, I would like to welcome everyone to the Intact Financial Corporation's Second Quarter Earnings Results Conference Call. [Operator Instructions] Thank you. Dennis Westfall, Vice President of Investor Relations, you may begin your conference.

**Dennis Westfall**
*Former Vice President of Investor Relations*

Thank you, Adam, and good morning, everyone. A link to our live webcast and background information for the call is posted on our website at www.intactfc.com under the Investor Relations tab. As a reminder, the slide presentation contains a disclaimer on forward-looking statements, which also applies to our discussion on the conference call today.

Here with me today are Charles Brindamour, Chief Executive Officer; Mark Tullis, Chief Financial Officer; Martin Beaulieu, Senior Vice President, Personal Lines; and Alain Lessard, Senior Vice President, Commercial Lines. We will start with formal remarks from Charles and Mark, followed by a Q&A session. Martin and Alain will also be available to answer your questions during the Q&A session.

With that, I will now ask Charles to begin his remarks.

**Charles Brindamour**
*Chief Executive Officer and Director*

Thanks, Dennis. This morning, we announced the second quarter net operating income of $180 million, or $1.35 per share, that's 55% higher than a year ago, continuing our quarterly trend of solid operating results. Our strong broad-based underwriting results were partially offset by the impact of the severe storm system that brought substantial damage to a number of communities in late May. Overall, we reported a 92.3% combined ratio both during the quarter and in the first half of the year.

Our 46% top line growth reflects the strong retention we've maintained on the AXA Canada portfolio. In fact, we've experienced retention in the AXA book comparable to that of the Intact portfolio. I consider this quite an impressive result, particularly in the context of an integration, where dislocation in terms of price and product are present for both brokers and customers. The performance so far is, no doubt, superior to my experience in previous transactions. I indicated on our last quarterly call that we should have more clarity on a sustainable level of retention by today's call. So with that in mind, I'm comfortable saying that we expect the retention of the acquired portfolio to continue at the robust levels experienced to date.

Our underwriting performance and steady investment income resulted in our operating ROE reaching 17.3%, while book value per share was up 13% from a year earlier.

Our outlook for the industry remains unchanged from a top line perspective as recent results have played out largely as we anticipated. The low interest rate environment and reinsurance market conditions should support our outlook and will likely lead to firmer conditions over time.

From an underwriting perspective, the industry ended 2011 with a combined ratio of 100%. So for 2012, we anticipate some improvement in Personal Lines but will likely be offset by a reduction in the level of investment income. The resulting industry ROE is likely to improve from 6% in 2011 to upper single digits, bolstered by the 11% industry ROE reported in Q1, driven in part by mild winter conditions.

Looking specifically at Intact Financial, we strongly believe we'll continue to outperform the industry's ROE by more than 500 basis points in 2012.

Turning to Ontario Auto. We continue to see the benefits of the combination of the reforms and our own actions, but we remain prudent and disciplined in our approach. Although the industry made some headway in reducing its dispute resolution outstanding cases, a meaningful backlog remains. This leaves a level of uncertainty with respect to the interpretation of the regulations that were implemented through the reforms. The government, though, remains firm in its resolve to address the situation and improve conditions for Ontarians.

According to industry results, the loss ratio in Ontario Auto for 2011, excluding Intact Financial, improved by about 19 points from a year earlier. Preliminary results for Q1 showed that the improvement continued into this year. However, the industry loss ratio in that line of business still translates into a combined ratio of approximately 105% for the industry, indicating that the industry still loses money in that jurisdiction.

In Personal Property, benefits from our actions to improve results helped to offset the elevated level of cat loses experienced during the quarter. The resulting 104.5% combined ratio was much improved from last year, which included losses related to the Slave Lake wildfires. It was, however, also a stark reminder of the importance of maintaining our focus on the actions already taken and to monitor and adapt to the increasing level of severe weather occurrences.

Pricing conditions in Commercial Lines remained soft, but we remain focused. From a growth perspective, our results are beginning to reflect our value proposition, which includes a broader product suite and combining the expertise of both companies, as well as a continued focus on small and mid-sized businesses.

Turning to our integration of AXA Canada. Almost 3/4 of policies and customers have already converted. As such, I'm very comfortable saying that our integration is on track. This is due to the hard work of countless individuals from across the organization, who have come together to ensure that our brokers and customers continue to receive top-notch service, as demonstrated by our national broker satisfaction being at an all-time high.

On JEVCO, our message is also unchanged from what we communicated on our last call. We continue to work to obtain the regulatory approvals required in advance of closing, which is targeted for the fall. We followed a similar process to the one we followed last year, and that integration planning started shortly after announcing the JEVCO acquisition. In planning for the integration, a key principle is to ensure that there will be no disruption to the AXA integration, nor to the high level of service we currently provide to brokers and customers, as we prepare a stronger offer for both customers and brokers. Current plans are to begin renewing the JEVCO business on our own platform in early 2013.

In conclusion, the resilience of our operating results was once again illustrated as we recorded a combined ratio of 92.3% despite more than $60 million of cat losses during the quarter. Given the strength of our operational platforms and the flexibility provided by our financial position, we believe that we'll continue to outperform the industry and strengthen our leadership position in the coming months and years.

And with that, I'll now turn the call over to our CFO, Mark Tullis.

**Mark A. Tullis**
*Vice Chairman*

Thank you, Charles. This morning, we announced operating income of $1.35 per share, up from $0.87 in the second quarter of 2011. Adjusted earnings per share of $1.11, excluding acquisition-related items, were slightly below the level from last year. These results reflect strong underwriting results across our lines of business with the exception of Personal Property, which experienced $51 million in losses related to the severe storm system that Charles referenced.

Top line growth continues to be excellent at 46%. As Charles mentioned, AXA retention has been strong, and we now have sufficient comfort that we expect this to continue through the integration period. Retention is impacted in 2 ways: by customer attrition and by broker cancellations. Despite the integration, in total, we have achieved retention similar to what we would expect in a normal year.

Slides 8 and 9 show results by line of business. In Personal Auto, premium growth benefited from organic growth, as well as the AXA business. As AXA had a larger proportion of lower premium Québec business, our unit growth was even stronger than our premium growth. At 89%, our combined ratio was 3.3 points higher than last year's exceptional 85.7, driven by less favorable prior year claims development, primarily due to industry pools.

We reported an underwriting loss of $16 million in Personal Property during Q2 due to severe weather, which more than offset improved underlying results. Excluding the impact of prior year claims development and catastrophes, our loss ratio improved 4 points from Q2 of last year.

AXA's contribution was once again most evident in our Commercial Lines business with premium growth at 71%. Commercial underwriting results were excellent with a total combined ratio of 88.2%. The Commercial Auto was exceptionally strong at 79.6%, and Commercial P&C improved to 91.3%.

On the investment side, net investment income of $95 million in the second quarter was up 25% from a year ago due to the additional investments related to AXA Canada. Declining yields have resulted in lower-than-expected investment income, and we expect this to continue in the coming quarters. Under current accounting rules, common shares are required to be impaired when the market value of the shares drops below book value for a given period of time. Declines in certain sectors of the market, notably energy and materials, thus resulted in $23 million of equity impairments this quarter. If markets remain flat, additional impairment through the end of 2012 would be expected to be around $15 million.

Our financial position remains solid at the end of Q2 with an MCT of 205% and $649 million in excess capital, while our book value per share was up 13% from a year ago.

On the financing side, we successfully raised $200 million of medium-term notes, and we repaid the $150 million remaining on our term credit financing related to the AXA transaction.

Our debt to total capital ratio is now 19.8%, in line with our target of 20%. As Charles mentioned, the integration of AXA Canada continues to be on track. We remain comfortable with our $100 million after-tax synergy target and are on plan with $37 million run rate already secured in 2012 and a $50 million run rate expected by the end of the year as occupancy savings and internalization of claims functions take hold in the second half of this year. We are also on plan with respect to restructuring and integration expenses.

The JEVCO transaction continues on track, and we remain confident of achieving both our financial and our strategic objectives, namely: achieving an estimated IRR above 20% and book value per share accretion of 2.6%; strengthening our offer for brokers and customers while expanding existing product offering into complementary lines; and strengthening our commercial and specialty line capabilities. Closing is still anticipated for this fall.

In summary, we are pleased with the significant progress made to date on the AXA integration and look forward to the integration of the JEVCO business in the months ahead. We believe our solid financial position and disciplined approach to the business provide a strong foundation from which to build.

With that, I'll turn the call back to Dennis.

**Dennis Westfall**
*Former Vice President of Investor Relations*
Thanks, Mark. Adam, we are now ready to take questions.

# Question and Answer

**Operator**

[Operator Instructions] Your first question comes from the line of Andre Hardy from RBC Capital Markets.

**Andre-Philippe Hardy**
*RBC Capital Markets, LLC, Research Division*

My line of questioning is around the $75 million of gross catastrophe costs in the quarter. So first of all, was that all Montréal and Thunder Bay?

**Mark A. Tullis**
*Vice Chairman*

Yes, largely. Yes.

**Andre-Philippe Hardy**
*RBC Capital Markets, LLC, Research Division*

Okay. So when we look at the industry numbers, and I realized you don't come up with the industry numbers, someone else does, but $75 million into $200 million implies 37% market share. So I presume you have lower market share, but correct me if I'm wrong.

**Charles Brindamour**
*Chief Executive Officer and Director*

Yes, you're right that we don't have 37% market share. But it's significantly higher than our national market share.

**Andre-Philippe Hardy**
*RBC Capital Markets, LLC, Research Division*

Okay. So when we look at the implied difference between what you're saying and what the industry estimate is, do you think we'll wake up with a higher estimate for the industry? Or you feel that you're being conservative? And if you can't really answer it the way I phrased the question, perhaps you could help us understand. Of the $75 million, how much of it relates to claims you've already received versus an estimate of claims that you will be receiving?

**Charles Brindamour**
*Chief Executive Officer and Director*

Yes, I think just a couple of points, Andre. The first point is that our view is that our market share in this market is probably greater than our national market share, which is at 17%, and therefore, not yet 37%. And the second point, and we've seen that in the previous cats in the West last year, is that we tend to be quite prompt to reserve for the ultimate of the cat, very soon after the cat. And the patterns we've seen in the past year is that we were a few quarters ahead of the ultimate industry numbers when we compared our numbers in Personal Property with the industry. And in what proportion is those 2 factors driving the difference, I'm not 100% sure because we don't have the industry data on that. But these are the 2 main reasons. Absolutely, no doubt. Mark, maybe you want to comment.

**Mark A. Tullis**
*Vice Chairman*

Well, I think the other thing to your question, how certain are we, obviously, cats continue to evolve through time, but these are May cats. So we have had a couple of months to look at them and feel fairly confident with our estimate at this point.

**Charles Brindamour**
*Chief Executive Officer and Director*

You want to give a sense of how much is unreported versus -- or how much is IBNR versus case reported? You guys have that information or...

**Mark A. Tullis**
*Vice Chairman*

Yes, we'll report to that.

**Charles Brindamour**
*Chief Executive Officer and Director*

Okay. Because I think that was the second part of your question, Andre.

**Andre-Philippe Hardy**
*RBC Capital Markets, LLC, Research Division*

Yes, I'll wait for the answer later.

**Operator**

Your next question comes from the line of Tom MacKinnon from BMO.

**Tom MacKinnon**
*BMO Capital Markets Equity Research*

Specific question kind of really on -- or 2 of them. One, with respect to Page 5 of the supplements. There's a -- and you may have addressed this in some of your remarks, but I just didn't hear the -- I didn't get to the opening of the call. But to this corporate expenses and other, which are, in fact -- these things jump all over the place here on Page 5, but they were negative 16 in the first quarter and then positive 4 in the second. And I really don't have a feeling for what they are or how they should trend going forward.

**Charles Brindamour**
*Chief Executive Officer and Director*

Go ahead with your second quarter -- the second question.

**Tom MacKinnon**
*BMO Capital Markets Equity Research*

Okay. The second question is on the favorable reserve development in the quarter. Just trending a little bit higher than the long-term average of 3% to 4%. I understand the 3% to 4% is a long-term average. How should we look at that over the last little bit you've been able to beat that. How should we be able to -- should we think of that going forward? And it looks the favorable development was across kind of all business lines here. So maybe just -- and how much of that would have been attributable to the AXA book?

**Charles Brindamour**
*Chief Executive Officer and Director*

Yes. So I think that we're not changing our view on the long-term sort of pattern in the 3%-ish range. I think that the level above the long-term range is in part driven by the AXA portfolio. And it is also in part driven by the fact that the environment, the core environment, across the lines of business, but in particular in Ontario, continues to be favorable. And as such, the cautious stance that we've taken is still there, but as the time passes, clearly, favorable development on the cases themselves have been slightly higher than historically they've been. So we'll go back to your first question, Tom.

**Mark A. Tullis**
*Vice Chairman*

I think to get to the chase, I would view Q2 as more representative from a going-forward basis. There were some unusual items in Q1, including the fact that AXA and Intact had different cutoff dates. And so there was some sort of noise that went through in Q1 to make up for the fact that the cutoff date, the cutoff timing, was earlier for AXA. So you could kind of use some of that as a catch-up, true-up sort of thing. So I think for purposes of anticipating going forward, I would view Q2 as more normal.

**Tom MacKinnon**
*BMO Capital Markets Equity Research*

And if -- is that number then going to be modestly positive, kind of? If we got a 4 per quarter, is that kind of what we should be thinking about going forward?

**Mark A. Tullis**
*Vice Chairman*

Well, I think if you look at -- and I'm not only looking at the corporate expenses and others, but sort of that whole chart there. So the distribution revenues, there is an increment because of distribution that we picked up from AXA. So the 23 versus, say, prior years, that's a bona fide increase from AXA.

**Charles Brindamour**
*Chief Executive Officer and Director*

So we've got more distribution.

**Mark A. Tullis**
*Vice Chairman*

Correct. I think if you look at sort of the pattern of what's been going on in the corporate expenses and others in prior years where it sort of bounces around from minus a little bit to plus a little bit, that's the sort of pattern that you will see going forward on the expense line.

**Operator**

Your next question comes from the line of Doug Young from TD Securities.

**Doug Young**
*TD Securities Equity Research*

First question on Ontario Auto. I guess the message in what -- reading what you've said and in your release, more needs to be done to fix it for the industry. And I think you said the industry combined ratio, roughly around 105%. But we're starting to see price increases are basically nonexistent for the industry. We're seeing, I think, more players wanting to write business in Ontario, so maybe getting a little more competitive. I'm just wondering, how much more improvement should we be expecting? Or what other changes might be coming that would provide further improvement for the industry?

**Charles Brindamour**
*Chief Executive Officer and Director*

Well, I think the first point I'd like to make, Doug, is that in 2012, you've got about 4% of rates running through the system coming from rate approvals from 2011, okay? And so that's the impact on the written premium of the industry this year is about 4%. The earned impact will be higher than that because of the rate increases that were taken from the past as well. So I think it's one thing that one should keep in mind. I think you're right to say that if we look at Q1 and Q2, rate changes have been largely nonexistent. Though if you look at the pattern, you see -- by company, you see mild decreases in some areas and increases in other areas. Where could improvements come from? I think that, clearly, providing greater clarity as a result of reducing the backlog is one area. Secondly, the definition of catastrophic injury will be another source of improvement or comfort for the industry. And my own view is that this is likely to come through this fall. And then the anti-fraud task force released a number of recommendations, which in the coming 24 months, I suspect, are likely to have an impact as well. So I think that there's still a number of meaningful elements on the table to improve the cost equation in Ontario. But until those elements are taking hold, it's hard to see our rates could go much the other way in Ontario. So as far as we're concerned, the industry is still running above 100%. Interest rates are putting additional pressure on the industry players. And our view has not really changed, unless additional cost reduction measures are taking effect.

**Doug Young**
*TD Securities Equity Research*

I guess, Charles, maybe just to ask you, and I don't know if you can answer this or not, but is it realistic to think Ontario Auto, from an industry perspective, could get down to 95% considering all of these changes?

**Charles Brindamour**
*Chief Executive Officer and Director*

Well, I don't think that the industry combined ratio has to go down to 95% in Ontario because this is a line of business with a fairly long tail. And as a result, it is a line of a business that has more investment income potential than other lines of business. But it's not unreasonable to think that the combined ratio of the industry should be 100% in that line of business for the market to be healthy and optimal in terms of desire for growth.

**Doug Young**
*TD Securities Equity Research*

Okay. And then just on the mediation backlog, I think you quoted that it's been down for Intact 25% from the peak in 2011, which I think is the same amount that it was down in Q1. Has there been any improvement for Intact sequentially?

**Charles Brindamour**
*Chief Executive Officer and Director*

No, it's about 1/3. And there hasn't been material improvements in the past few months. We keep seeing the good trend, but there -- because new mediations are coming in the system at the same time, so we're about at the same level of reduction. The industry over that period -- the industry backlog over that period stopped increasing and has actually dropped by 2%, which is positive. FSCO has a number of measures from a process point of view, as well as they're bringing third parties to help on the mediation and the arbitration front. And the sort of numbers that I've been hearing about coming from FSCO is that the third-party help that will come on the mediation front could address 2,000 mediations per month. And so when you look at a backlog of about 30,000 mediations, these are more than light measures that the government is considering to take action there.

**Doug Young**
*TD Securities Equity Research*

Fair to say it's still going to take a long time to deal with. Like this is going to be a 2013 event? Is that fair to assume as well?

**Charles Brindamour**
*Chief Executive Officer and Director*

Yes, I think it's fair to say that to get to certainty, you probably have a good 6 to 12 months ahead of us of there. I don't think the backlog will go to 0. It'll reach a run rate that is more reasonable than where we are now.

**Martin Beaulieu**
*Chief Operating Officer of Direct to Consumer Distribution and Senior Vice President*

And we don't need the backlog to go to 0 to maybe eliminate uncertainty. I think we did a volume of decisions coming from these mediations or outcomes.

**Charles Brindamour**
*Chief Executive Officer and Director*

Yes, exactly. And I think, Doug, the dynamic, when you look at the outstanding mediations, part of the issue is that you've got, what is it, I think it's 75%, 80% coming from pre-reform claims.

**Martin Beaulieu**
*Chief Operating Officer of Direct to Consumer Distribution and Senior Vice President*

That's right.

**Charles Brindamour**
*Chief Executive Officer and Director*

So you hear that the backlog is dropping, and you say, "Well, okay, so when do we get parity?" Well, part of the issue is that what is dropping are pre-reform claims, hence the uncertainty around the reform claims, even though the backlog drops is still there. But when I look at the core operation, I mean, the benefits are coming in as anticipated.

**Doug Young**
*TD Securities Equity Research*

I guess one last line. Organic growth and a direct insurance organic growth in Ontario Auto. I mean, you've given the number last few quarters, but didn't see it in your release. Do you have that number handy?

**Charles Brindamour**
*Chief Executive Officer and Director*

Yes. It's north of mid-single digit on the direct side of the house.

**Operator**

[Operator Instructions] Your next question comes from the line of Mario Mendonca from Canaccord Genuity.

**Mario Mendonca**
*Canaccord Genuity Limited, Research Division*

I want to pursue that line a little further, the questioning about the backlog. I understand that as much as 3/4 relate to pre-reform mediation. But if you do go through, if the industry goes through 2,000 a month, you're going to be through 6000 presumably over the next 3 months if, in fact, the third-party service providers get started in the near term. So by the next -- in 3 months from now, when we're having this discussion again, you're going to have a lot of information. What I -- what will be helpful to understand is, does it matter -- does it really matter to Intact what the industry learns if, in fact, Intact's already been through, say, 25% of the peak backlogs? Does it matter to you what the industry actually reports?

**Charles Brindamour**
*Chief Executive Officer and Director*

Yes. I'll let Martin answer that.

**Martin Beaulieu**
*Chief Operating Officer of Direct to Consumer Distribution and Senior Vice President*

It does because we're addressing our own backlog. But the outcomes of those mediations become the interpretation of the product on a go-forward basis, and we would be bound by these decisions. But assuming that these mediations are aligned with what arbitrations or core decisions would be, but that's the assumption we're going.

**Charles Brindamour**
*Chief Executive Officer and Director*

I think arbitrations are binding and become common. Non-mediations, not as much. But there's a backlog in arbitration as well. And yes, definitely, there's an influence in other case settling on our own case, as such, caution on our partner.

**Martin Beaulieu**
*Chief Operating Officer of Direct to Consumer Distribution and Senior Vice President*

Because if we go to mediations, these will be the same outcomes that we will get as the rest of the industry.

**Charles Brindamour**
*Chief Executive Officer and Director*

The second point, Mario, is that one should not assume that the third-party providers are necessarily crunching 2,000 files right now. They have not started. I think that's the intent of the government. They're far down the road. And I'm not exactly sure when it will start. It will be in the coming months. That's why I want to be cautious on that front.

**Mario Mendonca**
*Canaccord Genuity Limited, Research Division*

So if not next quarter, then presumably by the end of this year you're going to have more information?

**Charles Brindamour**
*Chief Executive Officer and Director*

Yes, I think we'll have more information by the end of this year.

**Martin Beaulieu**
*Chief Operating Officer of Direct to Consumer Distribution and Senior Vice President*

The plan was for this to start by the end of the summer.

**Charles Brindamour**
*Chief Executive Officer and Director*

But as every quarter progresses, we'll get more information. I think that our results to date show that the reforms are effective. As you know, we've said we're taking a cautious stance on the files that are in mediation. And if mediation and arbitration pans out as the reform anticipate, then I think that will be positive. There's no doubt about it. But it's too early to tell or reflect that positive outcome because it's not yet an outcome.

**Mario Mendonca**
*Canaccord Genuity Limited, Research Division*

Is there -- can we take anything from the 2% reduction in the backlog? Those mediations that were resolved, the resolutions that came through this quarter, were they favorable? Were they unfavorable? Is there anything you can offer there?

**Charles Brindamour**
*Chief Executive Officer and Director*

No.

**Mario Mendonca**
*Canaccord Genuity Limited, Research Division*

Just not enough information?

**Martin Beaulieu**
*Chief Operating Officer of Direct to Consumer Distribution and Senior Vice President*

That's not enough information because a lot of these mediations that are for the post-reform are around the minor injury guidelines. But no 2 cases are exactly the same. And you need to develop a certain volume to see patterns arising. So what we see as of yet, there's nothing to cause an alarm, but that's not enough to change our status.

**Charles Brindamour**
*Chief Executive Officer and Director*

Yes, exactly. And let's go back to the point that if 3/4 come from pre-reform claims, obviously, the first claims to fall off the backlog are likely to be pre-reform claims. And I think where we express a view on uncertainty is more on the effect of the reforms themselves. Therefore, that will come at the tail end of dealing with the backlog issue.

**Mario Mendonca**
*Canaccord Genuity Limited, Research Division*

I see. And then finally, when you do have information -- and Mark, you made the point, we don't need 100% resolution of the backlog to -- at some point, you're going to have enough information. Assuming the resolution is favorable, what sort of things can we expect? Would we expect a release, a big, positive reserve development in a given quarter or 2? And could we expect the current quarter -- the current year claims ratio to improve if, in fact, the resolution is favorable? I'm just trying to think of how this could manifest itself in your results going forward.

**Charles Brindamour**
*Chief Executive Officer and Director*

Yes. I think that our stance to date has been to say, "All right. This is what we observe as files come in, and let's take a cautious stance in terms of bulk reserving, so to speak." And we've been doing that for now close to 2 years or 18 months, since the reforms. As I don't think certainty will come in a quarter but will likely come over time, if things turn out well, there could be favorable development slightly in excess of the historical pattern but not on a structural basis. It would happen over a number of quarters as the information becomes clearer and more...

**Mario Mendonca**
*Canaccord Genuity Limited, Research Division*

It will be temporary?

**Charles Brindamour**
*Chief Executive Officer and Director*

Yes, I think so. I think we have seen, Mario, the 12 points that I've been talking about since the reforms materialize in the results throughout the latter part of 2011 and this year. And structurally, will there be much more than that? I don't think so.

**Operator**

There are no further questions at this time. I'll turn the call back to the presenters.

**Charles Brindamour**
*Chief Executive Officer and Director*

Well, I think I'd like to come back to Andre's earlier question about the second quarter cat level and your question in relationship with our number versus the industry's number. My point was that we tend to be quick to get to ultimate in terms of reserving. At the end of the quarter, on these cats, Andre, about 1/3 of the amount was IBNR driven. Okay? So that is a reflection of the fact that even though the reporting has largely matured, we're pretty comfortable we're at ultimate on that front, I don't know what the industry is doing. Our experience in the last year is that there has been deterioration from prior cats in subsequent quarters as we compare with industry results. So I would leave that for you to think about. Second point I'd like to make, Andre, is that the $200 million number, it's not clear to me it was measured at the end of the quarter for the industry, while our number is measured at the end of the quarter. So therefore, there's a degree of maturity that might be different as well in the interpretation. So I think we feel pretty good about our number. We don't have great visibility in the industry number. And our track record shows that we've been quicker to get to ultimate in our assessment of cats. I don't hear Andre's reaction because he's not on the line, but I trust that's what you were after. I think that's it.

**Dennis Westfall**
*Former Vice President of Investor Relations*

I think there's one more question on the line. Go ahead.

**Operator**

Your next question comes from the line of Tom MacKinnon from BMO.

**Tom MacKinnon**
*BMO Capital Markets Equity Research*

Charles, with respect to -- you talked about potential improvements in Ontario Auto, and one of them was this definition of cat. Now I assume that has to be the -- does that has to do with the stacking? Where do we stand in terms of stacking? And I know you took a reserve to sort of suggest a -- if the outcome was going to be negative in terms of that interpretation. Are we looking at any change in the rules with respect to the stacking?

**Martin Beaulieu**
*Chief Operating Officer of Direct to Consumer Distribution and Senior Vice President*

Yes, the proposal has a multiple number of recommendations, but one of them is reversing the latest trends in courts, that physiological and psychological damages could be stacked. The new definition would remove that stacking. So that would not change, from a reserving perspective, that would not change the past, but it could change the future.

**Charles Brindamour**
*Chief Executive Officer and Director*

Yes. And in terms of whether the previous decisions, which sort of allowed stacking, whether that's holding or not, Tom, I think part of the issue in cats is you don't get a large number of cats. These are small numbers. They just happen to be the high severity. So I think still same story there.

**Tom MacKinnon**
*BMO Capital Markets Equity Research*

So if -- yes, you said the reverse the trend in the courts. Now, does that mean that if there's -- I mean, you set up a reserve to handle this, which -- in the fourth quarter.

**Charles Brindamour**
*Chief Executive Officer and Director*

On the open claims.

**Tom MacKinnon**
*BMO Capital Markets Equity Research*

Okay. So it doesn't apply retroactively to those open claims then?

**Charles Brindamour**
*Chief Executive Officer and Director*

No.

**Operator**

Your next question comes from the line of Doug Young from TD Securities.

**Doug Young**
*TD Securities Equity Research*

Sir, just on the Commercial side, I believe it was mentioned, and correct me if I'm wrong, that there was some increase in severity on Commercial P&C. And I know last quarter, you had a number of large fire-related losses. Was there again another increase in severity this quarter in Commercial P&C? And if so, can you give us some details around that?

**Charles Brindamour**
*Chief Executive Officer and Director*

I'll ask Alain Lessard, our Senior VP, Commercial Lines, to take this one, Doug.

**Alain Lessard**
*Senior Vice President of Commercial Lines*

Okay. Well, on the severity side, the loss ratio, the current year loss ratio for the quarter, dropped by about 1 point, which was largely due to the catastrophe, the Slave Lake fire last year, which affected us in Commercial Lines. But going back to large losses, last quarter, we reported a surge in large fire. This quarter, we're basically back to normal site level. We're about 8 points lower than the last quarter, in line with our historical average. And we are slightly above last year's, about 1 point higher than last year in numbers or in dollars of large losses. So we don't see any trend or anything emerging in the severity side. It's within the, I would say, reasonable fluctuation from quarter-to-quarter.

**Charles Brindamour**
*Chief Executive Officer and Director*

The bump in severity that we've observed in Q2, Doug, was in part driven by a number of deserving [ph] calls we've made. So nothing to be concerned about in relationship with large losses, and I would say nothing to be concerned about in relationship with the performance of that line.

**Operator**

There are no further questions at this time.

**Dennis Westfall**
*Former Vice President of Investor Relations*

Thank you, everyone, for participating. The webcast will be archived on our website for 1 year. A telephone replay will be available at 2 p.m. today until Wednesday, August 8. The replay number is 1 (855) 859-2056, and the passcode is 95492189. A transcript will also be made available on our website. Please note that our third quarter results for 2012 will be released on November 7. That concludes our conference call. Thank you, and have a good day.

**Operator**
This concludes today's conference call. You may now disconnect.