AUTORITÉ DES MARCHÉS FINANCIERS

Address by

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As Chair of the Canadian Council of Insurance Regulators (CCIR) and as Superintendent of Solvency with l'Autorité des marches financiers, it is an honour to be invited to speak to you today and to give you an update on projects and undertakings by both the CCIR and the AMF.

Since early this year, CCIR has been working to develop a new strategic plan. One of the first steps we took was to ask industry stakeholders for their input. A number of stakeholders expressed various levels frustration toward CCIR and the perception that we, CCIR, did not "deliver" according to expectations – especially expectations that CCIR can deliver harmonized solutions to issues that all jurisdictions will follow.

Since receiving that input, we have been taking a hard look at who we are, what we CAN do; CANNOT do, and what we SHOULD do.

It is important to note that CCIR is comprised of officials, not ministers. What does that mean? We, the superintendents, we the CEOs, in our provinces or territories, we do not make the laws. We manage and enforce a body of laws that our respective legislative bodies have voted for. So, it is unrealistic to think that CCIR can impose anything – much less a single solution that must be followed.

Even when CCIR members agree on a common response to an issue, this does not necessarily translate into common behaviour. Each jurisdiction has its own legal and regulatory environment that may lead to differences in how policies and regulations are implemented.

Is harmony out of the question then? By no means. Is CCIR powerless? Not at all.

Governments across the country look to their regulatory bodies – the CCIR members – as their primary advisors on insurance issues. The work that CCIR does, to research, consult, draft, propose, recommend, and review issues of common interest, assists regulators in forming the advice they take to their governments. We might not make

rules, but we can take strong positions and make recommendations that are taken seriously by regulators and governments. In most cases, this results in regulation that is less discordant and more harmonious than might otherwise be the case.

It may be imperfect at times; however, any amount of harmonization is bound to pay off in decreased costs of compliance for the industry. We hope to have a draft Strategic Plan ready in the next few months. As it is likely to be quite a different kind of plan, we were planning to send the draft to the industry for comment before finalizing it. This has not been our practice to date, but we hope that this will help bridge the gaps that exist between industry expectations and what CCIR can deliver.

Now, let me reflect on some of the main issues that preoccupy us these days, beginning with a topic that is near and dear to you and in which you were actively involved this past year; the use of **credit ratings** by insurers.

I would like to take this opportunity to tell you that we appreciate your interest. Whether it was your presentation in September 2009 or your comments made at the start of this year about the IBC Code of Conduct, your input has helped us to understand the importance of this issue for your industry.

Despite the growing use of credit scoring, you have your work cut out, as you have yet to convince a good number of consumers and regulators that it is not discriminatory. Many believe that the use of credit scores is at best, a substitute for consumers' lifestyle variables such as, level of income and financial stability.

More recently, blunders by insurers, combined with consumer complaints, have thrown the media spotlight on this topic, which has generated considerable political interest in a number of Canadian jurisdictions and with our neighbours south of the border.

As well, consumers see that credit scoring is not allowed for automobile rate criteria in several jurisdictions; that New Brunswick and Newfoundland, and possibly even Ontario

are moving toward a wider prohibition, and wonder why it is allowed for any other product.

The recent change in government in New Brunswick has showed down the process begun by the tabling of Bill 43, which introduced a new ban on the use of rate-setting factors such as credit scoring and other financial information for private passenger automobile insurance and residential property insurance. The government has now received the input requested from insurers on their position about other lines of insurance and the timelines for introducing any changes.

In Ontario, Bill 130 – The Homeowners Insurance Credit Scoring Ban Act, has just passed first reading. This bill will prohibit the use of credit scoring in personal property insurance. Enforcement details have not been determined at this stage. The use of credit scoring in auto insurance has been banned in Ontario since 2005.

The findings of a survey conducted in the spring of 2009 by the Ontario Financial Services Commission on behalf of several other provinces, showed that 16 insurers, accounting for nearly 49% of the market, were using credit scoring for home insurance. The survey also demonstrates that there were wide gaps between the impact of credit scoring on the availability and cost of insurance and its disclosure to consumers.

Although we in Québec, did not take part in this exercise, we know that the use of credit scoring is even more widespread. In automobile insurance, the analysis of rate manuals and the results of our annual questionnaire on rate-setting, showed that 28 out of the 80 insurers who underwrote private passenger vehicles in 2009 used credit scoring.

That's 86% of the market. Assuming that these same insurers use credit scoring for home insurance, 84% of this market is affected, according to our calculations.

This greater use in Québec is certainly not unusual. The nature of the market, the heavier concentration of direct insurers than anywhere else in Canada, as if you didn't

already know!, the regulatory model, leaves more freedom for the use of classification criteria. However, I would also like to remind you that we are able to evaluate the merits of these practices and, if necessary, intervene to improve them. I would like here, to praise the initiative by IBC-Québec, which, in the spring of 2009, took the lead in Canada by proposing to its members, the first guide to using credit information.

The AMF saw a huge rise in 2009 in various forms of feedback from the public about credit ratings: requests for information, dissatisfaction or formal complaints. Regardless of the form, we expect Québec insurers to take the necessary measures to reduce and, ultimately, eliminate complaints related to practices that do not meet the highest standards. We feel that even one justified complaint about a misdeed, is one too many.

At the Canadian level, the CCIR has been working on the review of the use of credit scoring in insurance for some times. It had hoped to finish it by now but there have been some delays. The Credit Scoring Working Group is now hoping to have an issues paper ready for consultation in the spring of 2011.

This paper, will outline the results of our research and will include an overview of the actions taken to date, by regulators both in Canada and in other countries. Given the legislative action in some provinces, the CCIR does not intend to take a position on this issue, since harmonization is not possible.

The issues paper to be prepared by the Credit Scoring Working Group will not be proposing regulatory action. Rather, its purpose will be to stimulate debate and launch a process of consultation as well as to, educate and build a common understanding of the topic in both regulators and stakeholders.

A second area of interest to both CADRI and CCIR is the expanded Complaint Reporting System.

We just recently began to run reports from the expanded system. As usual with a new system, there have been some bugs in the reporting module that are being corrected. However, once that is done and we develop a history with the data, we fully expect that the information gathered will assist regulators in focusing their market conduct reviews on areas where risks were flagged.

Also, once we have more experience with the system, we should be initiating a project to revisit the data points and definitions intrinsic to the system. No precise timing has been set for this review, but the industry will be fully informed and involved when the review eventually takes place.

CADRI members may also be interested in knowing that our Electronic Commerce Committee, with its new chair Eric Stevenson of the AMF, is actively working on a paper dealing with some thorny issues affecting consumers, issues such as electronic beneficiary designations and electronic delivery of proof of automobile insurance cards. It is also working on a comprehensive review of the capacity of the current regulatory framework to adequately protect consumers obtaining insurance products online. Among other thing, the Committee will be looking at confidentiality, identity verification and record maintenance.

On November 1, at its annual Rendez-vous, an event where the AMF meets with the industry, my colleague, the Superintendent of Distribution Mario Albert, gave a most interesting presentation on alternative distribution channels for insurance products, which of course included web-based offerings.
Given that in Québec alone, on-line purchases of insurance jumped 102% between January 2009 and January 2010, we can see why we need to take a good hard look at the impact this distribution method can have on consumers.

Insurance offerings through individuals or firms not licensed in Québec, the lack of appropriate advice and the glut of information, make it impossible for consumers to

discriminate among products. Information security and transaction reliability are the vulnerable risk areas intrinsic to this method of distribution.

The AMF is carefully examining this distribution method and is planning several controls to ensure better public safeguards. The AMF's initiatives will therefore support the work of the CCIR's Electronic Commerce Committee.
Now, let's talk about surveys! We know how much our surveys are appreciated by the industry! As you have told us many times, there has recently been a proliferation of regulatory surveys on a variety of topics.

And before you groan too loudly, I want to point out that, in a way, the increase in the number of surveys is a good thing… It means we care!

But mostly, it is evidence that CCIR's approach to Risk-Based Market Conduct Regulation is taking hold.

Beyond any sarcasm, let me tell you how useful surveys really are for regulators. Surveys are one way regulators can quickly gain an overview of what is happening in the industry on a specific issue.

However, we definitely have heard the pleas for help from compliance officers, who seem to be buried under multiple survey requests. You have told us that these survey requests from regulators – not just CCIR but the regulators themselves - overlap as to subject, overlap as to completion date, use different formats and in some cases are pretty unclear as to what the point of the exercise is.

CCIR is working to resolve this issue. We have drafted some Survey Standards, that is, best practices for regulators to follow when considering a survey. These are currently being translated and will be published for industry comment later this fall.

At our fall meeting a few weeks ago, CCIR agreed to move forward with an initiative to create a facility – perhaps a data-base, perhaps some kind of internet search solution – to that would be a Central Source on Disciplinary Actions. While individual CCIR and CISRO members publish information on disciplinary decisions, there is no centralized source of this information. Having some form of central source would assist regulators, insurers, MGAs and consumers to research the suitability of an intermediary without having to go through a number of sources.

The AMF is chairing this committee, and we hope to make significant progress over the next year.

So, I have talked to you about what CCIR is and what we are not and I have discussed some of the issues we are working on. I hope it brought a better understanding of what CCIR is and what we can do.

Now, I'd like to talk about some ongoing works at l'Autorité des marchés financiers, works that are important for the members of your organization.

Let's start first with a status on our **commercial practices guideline**. First published in November 2009 for public consultation, the guideline was the object of numerous comments from industry including yours. We did listen and the guideline will be amended to reflect some of the comments received. Once reviewed, it will be republished for a second consultation; probably sometimes in the first quarter of 2011.

In our defense, the Commercial Practices Guideline is the first Canadian initiative on this particular issue. And as no benchmarks existed, I must admit it was challenging for us internally. It was challenging to bring under one guideline the requirements of the Act respecting insurance and the "Act respecting the distribution of financial products and services".

Basically, with our guideline, we are aiming at fostering a “treat the customer fairly culture (TCF) throughout the industry.

As a member of the International Association of Insurance Supervisors (IAIS) Market Conduct Subcommittee, we are actively participating in the development of a Standard and Guidance Paper on “Conduct of Business”. And in the near future, the OECD will also publish a paper on the protection of consumer of financial products and services.

These two papers will be a valuable source of information for us and will be used to update our own guideline.

Now let’s move on to the topic **distribution without a representative**. Prescribed by the Act respecting the distribution of financial products and services, it is as you know, an exceptional regime for the distribution of financial products and services.

Under this regime, an insurer can offer insurance products or secure a client’s adhesion through a distributor, provided that:

- the distributor’s business is not in the field of insurance;

- the insurance product offered is incidental to the good that is being sold and,

- the insurer has prepared, submitted a distribution guide.

Some of the areas where we are finding issues associated with the distribution without a representative regime are:

- Disclosure of information to consumers
- Cancellation of the contract
- Supervision of distributors

- Disclosure of distributors' remuneration
- Financed single premiums
- Use of telemarketing

When it comes to the **disclosure of information** to consumers, we find that in many instances, the guides in their current form do not achieve the disclosure objectives that are desirable to properly protect consumers.

Another area of concerns is the Cancellation of the contract. In the context of Distribution Without Representative, Québec legislation allows for a period of 10 days during which the consumer may request cancellation of the insurance coverage. We find that consumers are generally not aware of the existing cancellation process, or the duration of the cancellation period.

Another issue is that distributors are the second main source of disclosure of information to the consumer but, we find that they do not always play a complementary role to the guide with respect to the disclosure of relevant information to consumers.
The Act respecting the distribution of financial products and services requires distributors to disclose their remuneration to consumers if it is over 30%. Moreover, a distributor that offers more than one insurance product for the same goods must inform the consumer of its remuneration for the sale of each of those products.

However, the Act is silent as to the form that the remuneration and the disclosure should take. The data gathered in many instances, leads us to believe that disclosure measures are not well understood, are often not applied and that they are sometimes even bypassed by the industry. If the fulfillment of this obligation is not clear, or not controlled, the tendency will be to omit to disclose…

In the case of insurance products with financed single premiums, it appears that it is difficult for consumers to evaluate the real cost of the premium, because the interest is added to it. We also find that consumers are unfamiliar with the methods used to

calculate the reimbursement of such premiums in the event, that the insurance contract is being cancelled. And thirdly, the reimbursement does not correspond to the premium paid, less the number of months that have elapsed. In conclusion, it appears that these methods of calculating the reimbursement of premiums in the event of a cancellation can compromise the process and render the consumer captive.

In telemarketing situation, it is impossible to give the consumer a copy of the guide prior to the purchase of the product and the application of the cancellation period can also be problematic. In these circumstances, we are facing the fact that the guide does not fulfill its disclosure role, bringing us to conclude that the distribution without a representative regime is ill suited for telemarketing.

A third topic I would like to bring to your attention, is compliance with Quebec's regulatory regime. The Act respecting insurance requires that insurer adheres to sound and prudent management practices. The same act also empowers the AMF to issue guidelines pertaining to management practices. As such, our Compliance Guideline is based on principles, and exposes our expectations in terms of sound management practices. It promotes the establishment of a compliance culture within financial institutions doing business in Québec.
In that sense, compliance is an approach that goes beyond the "classic" concept of compliance to laws and regulations; it includes compliance to the regulator's guidelines, to its notices and also, compliance to internal code of conduct, policies, and procedures.

The main principle underlying our supervisory approach is "accountability". The institution is responsible and accountable for the implementation of management and control functions among which, the compliance function.
The institution must implement strategies, policies and procedures to manage its compliance.

Supervisory activities linked to compliance are done both off and on site:

During the time of implementation, our off site supervision is mainly the review and analysis of the biannual report filed the insurer. The report outlines a status on the institution's implementation of strategies, policies and procedures in order to be ready to achieve compliance with the guideline's principles in April 2011.

On site, in evaluating the quality of the compliance management function we look for:

- formal and, by formal we mean documented, approved framework of compliance management, including strategies, policies and procedures;
- the independence of the compliance function;
- "Powership" of the function;
- Staff competence;
- Communication and follow up processes.

It is to be noted that in instances where the assessment is unsatisfactory, the supervisory report will include recommendations. The institution will then have to provide a corrective action plan including a timetable to achieve compliance.

We do follow up and if necessary, some progressive actions may be taken as provided for by the Act respecting insurance.

What are we having in our guidelines pipeline?

We are active member of the IAIS Governance and Compliance Subcommittee. We have lead the drafting team charged to rewrite the IAIS Core Principle, Standards and Guidance on Suitability of persons (fit and proper requirements). The final version of the Core Principle pertaining to Suitability of persons was approved at the IAIS annual meeting at the end of October. The work done as part of the drafting team, as you can imagine, will serve as input in the development of our guideline on Fit and proper.

The planned guideline will be an integral part of the “foundation stones” already developed– Governance –Risk Management – Compliance (GRC). Together, they contain our expectations with regard to the sound and prudent management practices for financial institutions doing business in Québec.
The planned guideline on the other hand, will outline our expectations on fit and proper requirements for board members and senior management of insurance and deposit taking institutions.

We are planning on publishing the draft for consultation in the first quarter of 2011.

In May 2009, the Basel Committee on Banking Supervision (BCBS) issued Principles for sound stress testing practices and supervision. Stress testing as you all know, is a critical tool used by banks as part of their internal risk management and capital planning. The guidance sets out comprehensive principles for the sound governance, design and implementation of stress testing programs for banks. Stress testing also, is a key component of the supervisory assessment process that assists supervisors in identifying vulnerabilities and evaluating banks' capital adequacy.
Last year, OSFI issued for comments a draft version of its Guideline E-18 – Stress Testing. Last December, the final form was published. It describes their expectations with respect to the use of stress testing by all federally regulated financial institutions.

Our expectations on sound practices in the use of stress testing are currently spread throughout small sections of various guidelines. Therefore, in order to clearly outline our expectations on sound and prudent management practices while using stress tests, we will be publishing a new guideline sometimes in 2011.

Our new guideline on Individual Variable Insurance Contracts relating to Segregated Funds, differs from any of our other published guidelines. It stresses the execution rather than the interpretation of the legal requirement, with the purpose of ensuring harmonization of the rules developed by the industry and rules recognized by CCIR.

In order to provide consistent framework to life insurers, it is largely harmonized with the G2 guideline of CLHIA on Segregated Funds. In addition to the information to be disclosed prior to sale, the Guideline covers different aspects, including continuous disclosure, disclosure in advertising and contractholder rights. It also discusses certain specific expectations, such as administration of funds, investments, accounting and audit requirements.

It is also, closely linked to a “Regulation to amend the Regulation respecting information to be provided to consumers” published for consultation at the same time. The consultation ended at the end of october. After It has been presented to the Minister of Finance for consultation in order to be effective January 1st, 2011.

From our big pipeline, we also recently published an update of the Outsourcing Risk Guideline. We did update our requirements to introduce a new appendix outlining: “Example of centralized list of material outsourcing arrangements”. The draft updated guideline was published on our Website for consultation. As no comments were received, the draft guideline will be presented to the Minister of Finance for consultation to be effective January 1st, 2011.

The AMF recently completed a major reform of replacement insurance; the “replacement guarantee” that car dealerships in Québec were selling to protect buyers against depreciation if their vehicle was a total loss.

Since 2000, several insurance companies have left the market of contractual responsibility with the result that many companies that were issuing these replacement guarantees, no longer had an insurer to assume the financial risk if the contract was not honoured. In the event of default, consumers risked being left by the side of the road and not receiving any compensation for a claim.

Also, the fact that consumers were not purchasing this product directly from regulated insurers only increased the risk that they would not receive reimbursement and, that any commitments towards them would not be honoured.

The AMF therefore, held two public consultations intended mainly to decide on what measures were needed to enhance consumer protection. Having determined that the industry was generally in favour of transforming replacement guarantees into insurance products offered exclusively by insurers, the AMF introduced a new framework for this type of product.

As a result, replacement guarantees are now issued by insurers and are part of a standardized form – Q.P.F. No. 5 – which must be approved by the AMF, as stipulated in section 422 of *An Act respecting insurance*.

The aim of this new framework is to help consumers better understand the product and, reduce the financial risk associated with the insolvency or bankruptcy of an issuer, car dealership or other company.
This risk is virtually eliminated since, it is protected by the financial system framework governing insurance products, including compensation bodies in the event of insurer bankruptcy.

As this product is now sold exclusively by certified insurers, consumers are better protected.

However, new automobile insurance policy Q.P.F. No 5, which came into effect on October 1st, includes a specific feature in that, it can be distributed without a representative. In fact, in Québec, all insurance products must be offered and distributed to consumers in accordance with *An Act respecting the distribution of financial products and services*. This Act recognizes two distribution methods for insurance products: distribution with a representative and distribution other than through a representative.

The AMF views replacement insurance as a basic, complementary product and, as such, can be distributed without a representative via a distribution guide prepared in accordance with the Act.

Another initiative that I feel strongly about and which we have begun in the past months in co-operation with the *Groupement des assureurs automobiles*, le GAA, is the review of all automobile insurance policy forms. The goal is to make them easier for consumers to understand.

This became necessary in light of the numerous studies showing a low level of understanding of current forms drafted in legal language. If you consider that less than 15% of the public is able to understand the contracts they are required to purchase, it's high time we acted.

We also believe that the industry will benefit from the re-drafting of automobile insurance policy forms into plain language. Armed with contracts they can understand, consumers may have a more positive view of the industry. This change is therefore an opportunity for the industry to reshape public perception and, in the process, earn the public's deeper trust.

This work will be done over several months and will help us improve our understanding of consumers, not only their rights, but their obligations as well.

I would like to speak a bit about one of our most recent initiatives. No other regulator in Canada has taken a formal interest in taking the pulse of P&C insurers about the impact of climate change.

The core mission of Canada's regulators is to protect consumers. Faced with emerging threats that pose a risk to them and threaten their physical integrity and their material and financial wealth, we believe that it is our duty to evaluate the extent to which this

threat is real and its potential impact on the business, financial health and, ultimately clients of the financial institutions tasked with protecting them.

Even though the causes and consequences of climate change may raise questions and doubts by a minority, I should point out, there's no denying global warming. Just think about it. 13 of the past 14 years have been the hottest on record in the past 150 years.

The issue that interests us in particular at the AMF, is obviously the increasingly frequent and severe effects of climate change and their consequences for insurers. This is why, we made climate change a top agenda item at the AMF's 2009 Rendez-vous. At a public round table, insurers, reinsurers and experts all agreed that P&C insurers were at the heart of this issue and, at the same time, among the players most able to help society adapt and to be a catalyst for the actions that can counter the most sudden and devastating effects of climate change. This observation was confirmed by the Insurance Bureau of Canada, which stated in its most recent annual report that adaptation to climate change tops the list of strategic issues for the industry.

In short, we decided to walk the talk by developing a survey that will determine the extent to which each insurer:

- is up to date and concerned about climate change;
- has identified climate change risks;
- is taking steps to assess the related impacts; and
- is taking concrete measures to prevent them and adapt.

We deliberately chose to make this consultation exercise voluntary so as to seek quality over quantity in the responses. Despite the absence of several players, including some major ones, we believe that we can draw important lessons from this exercise. We are now collating and analyzing the responses, and expect to formulate the main conclusions by December, after which we will outline the next steps.

As you can see, we are always attentive to the concerns of consumers and the industry in an effort to maintain an effective regulatory framework that keeps pace with developments. This survey is another way of doing that. As I said earlier, it means we care!

I am particularly proud of the place the AMF has earned through its national and international representations. The Solvency team works diligently to identify, understand, present and often defend the needs of its regulated entities. As for CCIR, it is important that we keep our channels of communication open. As chair of CCIR, I do also work very hard at finding the proper way for your voices to be heard. We are currently trying to use the web to increase the frequency, the quality of our meetings with the industry.

As Superintendent, I invite you to participate in the meetings and roads shows held by the AMF Supervision and Standards units. Your comments are important to us. Do not hesitate to contact us. Mario Albert the Superintendent of Distribution and his team are as eager as we are in Solvency to make sure that we give the industry the regulator it deserves.

Thank you!