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CCIR Update

Regulatory and supervisory initiatives require understanding of expectations, requirements and proper methodology. You must keep abreast of new and changing developments.

To the CLHIA Compliance and Complaints Annual Conference

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First I would like to thank you for inviting me to speak today. As both Chair of the Canadian Council of Insurance Regulators (CCIR) and as Quebec's Superintendent of Solvency, it is an honor to be with you.

I have just completed my third year as Chair of the CCIR and, more and more I value my meetings with the industry. I value these wonderful opportunities to share what is on our minds as regulators and to learn what is on your minds. But especially, I value the opportunity to spread awareness of the CCIR and the work we are doing to improve insurance regulation in Canada.

Today:

- I'll give you an overview of the trends in insurance regulation with particular emphasis on how CCIR is evolving, and
- I'll look at some specific issues CCIR is working on now,
- and finally, I'll speculate a bit on what lies ahead for us, and how we propose to get there.

For any of you who may still not know, CCIR is where the insurance regulators from all 13 provinces and territories, as well as OSFI, come together to keep regulation harmonized where possible and to deal with common issues.

- When CCIR researches, consults with stakeholders, drafts, proposes, recommends, and reviews issues of common interest;
- When we assist provincial regulators in their enforcement activities and in forming the advice they take to their governments;

- When we keep provincial regulators, in big and small jurisdictions alike, informed on international trends and emerging issues;
- when we act as a central clearinghouse for information and questions;

we improve the efficiency of the regulatory process across Canada. Common issues are dealt with **once** rather than 13 times, and the chances of differing regulatory opinions and actions are minimized.

This is an exciting time to be an insurance regulator. The insurance industry has changed. The days of limited risk and limited choice, where being in life insurance was considered boring - the good old days, where unchanging rules worked year after year and all we regulators had to do was make sure they were being followed - those days are **gone**.

Instead, regulators now need to be nimble to respond to rapid changes in the industry and the economic environment. CCIR is responding to this dynamic environment by:

- refocusing our organizational mission and goals, and
- by becoming **more** active and **more** consultative
as we attempt to stay on top of the risks that these changes may bring.

All our work at CCIR is focused on our fundamental goals as regulators: that is to protect consumers and enhance confidence in the Canadian insurance marketplace.

That's why I particularly like the theme of this conference "It's your reputation – Manage the risks," because the good reputation of industry participants is the very thing that inspires confidence in the Canadian insurance marketplace. And, since your reputations are founded in the way you treat your customers, we are all going in the same direction here. It is in everyone's best interest that consumers are well treated and satisfied with their relationships with their insurers and intermediaries.

I know, having been one that, all this changes and regulatory refocusing make it an exciting time to be a Compliance Officer. Complying with statutory, and legal obligations, while necessary, just isn't enough anymore. You, too, must be nimble. Welcome to the club.

TRENDS IN INSURANCE REGULATION

I believe CCIR did very well when we adopted our Approach to Risk-based Market Conduct Regulation, way back in 2008. It put us in the forefront of the movement to change regulatory focus from rules to goals and outcomes, well in advance of most countries. Now that the expectations of governments and international standard setters are raising the stakes in market conduct regulation by emphasizing the fair treatment of customers by insurers and advisors alike, we continue to be ahead of the curve.

Our first significant inroad into fair treatment of customers, though we didn't call it that at the time, came out of a project CCIR took on in 2004: The review of the relationships between intermediaries and insurers to see if there were conflicts of interest in the system that could potentially hurt consumers. Coincidentally, this was also our first significant move from rules to goals and outcomes.

At that time, people were pretty much expecting regulators to come up with new rules to outlaw sales promotion practices and to limit ownership and debt relationships between insurers and intermediaries.

We looked at possible rules – we really thought about it, because there are things we allow that securities regulators don't - but, in the end, we determined that anything we came up with, would be certain to spur some people to search for loopholes and that was definitely **not** the outcome we were looking for. Instead, what CCIR did was to consider the outcomes we **were** looking for.

We developed three principles to manage potential conflicts of interest and then, asked the industry to imbed these principles in their codes of conduct, guidelines and contracts.

You may recall them:

- Priority of the client's interest:

An intermediary must place the interests of policyholders and prospective purchasers of insurance ahead of his or her own interests.

- Disclosure of conflict or potential conflict of interest:

Consumers must receive disclosure of any actual or potential conflict of interest that is associated with a transaction or recommendation.

- Product suitability:

The recommended product must be suitable for the needs of the consumer.

The effect of this was that regulators started treating the industry like grown-ups. We didn't tell you that you couldn't do things, we put the on us on you to ensure that consumers were not hurt by the things you did.

Unsurprisingly perhaps, as we have gained experience in applying this approach, we have found that the outcomes we develop for one issue can often be applied when we look at other issues. There's been a continual growth, not just in Canada but in international forums as well, not so much in our understanding of the goals of regulation, but in the ways we refer to the outcomes and how we group them together.

For instance, as I noted, today we would consider the three conflict of interest principles to be part of the larger outcome of Fair Treatment of Customers.

I'll be talking about this later as I talk about the IAIS Insurance Core Principles, but for now, I just wanted to mention that we have heard that some industry members are concerned that

the focus on Fair Treatment of Customers could lead to increased rules and interference by regulators. I suppose it could, if legislators and regulators were so inclined, but that inclination is not yet in evidence in Canada.

Instead we see this, as a formalization of the concern for their clients that most insurers and intermediaries have always shown and a reminder not to abandon that concern in stressful times. It puts the onus for good, ethical behavior squarely with insurers and intermediaries.

For Canada, this is nothing new. As we've seen, we have been moving this way for almost a decade. But it's good to have Fair Treatment of Customers as an overarching principle because it helps us all to focus on the essentials and to make good decisions no matter how stressful the times.

For regulators, this means, we can respond more quickly to emerging issues because we have a framework to analyse them. We just have to ask:

- What fair outcomes for consumers are we looking for,
- What are the potential risks to consumers, and,
- How can those risks be minimized?

For you, this means that you can anticipate where regulators will be coming from, whatever the issue. Our preference is always to have industry do the right thing without additional laws and regulations, if at all possible.

Knowing that we expect fair treatment, knowing that we expect companies to build cultures where fair treatment is a core value, should, in the end, make your lives easier because our reactions to issues will never surprise you.

The new sets of Core principles developed by the International Association of Insurance Supervisors include two revised ones that deal with Fair treatment of customers, or FTC

ICP 18 deals with intermediaries, while ICP 19 focuses on Conduct of Business. It is in the latter that the FTC concept is embedded in this new set of requirements that will have to be implemented by regulators.

As Julien Reid, mentioned earlier this morning, this new and revised principle sets expectations for insurers to embed in their corporate culture, the fair treatment of customers. Not only at the manufacturing stage of the insurance product, but through its whole life, including when handling the consumer's claims or complaints. The culture of FTC must transpire through all the layers of the insurers. Staff must meet high standards of ethics and integrity. The culture of sound governance must take into consideration FTC.

And since FTC deals with reputation, insurers should make sure that decisions having an impact on customers should be subject to special scrutiny. From top to bottom, from bottom to top, across and diagonally! This is how you'll be able to establish in your organisation an FTC culture.

The implementation of the new IAIS ICPs will represent a great challenge, not only for regulators, but for insurers alike. Close collaboration with the industry will therefore be necessary.

CCIR STRATEGIC INITIATIVES

CCIR, as usual, has a number of strategic initiatives underway. Some of them have to do with assessing risks to consumers around emerging issues, but others are focused on changing how regulators do business.

ICPiC

The biggest initiative of the latter kind is our IAIS ICP Implementation Committee.

CCIR is currently working to ensure that all the Insurance Core Principles are being applied in Canada. For CCIR this means paying particular attention to the market conduct ICPs 18 and 19.

In a number of ways, this project is like trying to study for an exam where you already know 80% of the material really, really, well and you're trying to sort through all your notes to find the few things you don't know in amongst all that – finding and learning that last little bit that will earn you an “A.”

It's a hard project because we do so many of these core things quite well already in Canada, but not necessarily every one in every jurisdiction.

So our ICP Implementation Committee has its work cut out for it.

Disciplinary Information

Upon occasion, one or another provincial regulator takes disciplinary action against a licensed intermediary. When they do, most regulators will publish some information about the disciplinary action they've taken. These tend not to be long lists, but they do contain information that might be useful to insurers and MGAs who are considering contracting an intermediary, or to a consumer who is considering trusting one.

CCIR members have acknowledged that it would serve both the industry and consumers well if there were an online capacity to search out disciplinary information wherever the action may have been taken. There are a number of issues we have to work through to make this happen, but we are committed to seeing it happen.

In the meantime, in case you ever need to look up this kind of information, the CCIR website now has a page called Searchable Licensing Links that has the full list of provincial and territorial sites where this information currently resides.

Issues and Position Papers

We have a number of emerging-issues-type Strategic Initiatives on the go that affect life insurance. I'll just focus on two of them. One is at the initial Issues Paper stage, while the other has reached the Position Paper Stage.

Perhaps I should talk a bit about Issues Papers and Position Papers in general as they are integral parts of CCIRs modus operandi.

When the CCIR adopted the *Approach to Risk-Based Market Conduct Regulation* in 2008, regulators committed themselves to directing regulatory efforts to the most significant issues that either have the greatest potential for consumer harm or that could weaken public confidence if left unchecked. That paper described several principles regulators could follow to achieve this end including proactive identification to prevent issues from turning into problems rather than merely fixing problems after they happen.

This new focus led to new kinds of CCIR projects focused on understanding potential issues rather than on problem solving. These new projects led to new kinds of consultation papers being needed: the Issues Paper and the Position Paper.

Roughly analogous to a government green paper, an Issues Paper is published as the first piece of output from a CCIR committee. Its purpose is to stimulate debate and launch a process of consultation as well as to educate and to build a common understanding of a topic in both regulators and stakeholders. The Issues Paper seeks to articulate the views of the various stakeholders, even when contradictory, and present a well-rounded picture of the topic and issues.

When, after the consultation on the issues paper, the CCIR agrees that the issue is significant, a Position Paper, roughly analogous to a government white paper, will be published to lay out policy, or proposed actions, on the issue of concern. Although a Position Paper will also be released for consultation, it does signify a clear intention on the part of

regulators to go forward with an issue by one or several of the policy options available to regulators.

So, on to our first issue...

Electronic Commerce

You may have seen, or even submitted a reply to, our recently published issues paper on Electronic Commerce in the insurance industry. Like all Issues Papers, it was intended to map out the context and situation as, we believe it currently exists and, to stimulate debate about the issues and, launch a process of consultation as well as to educate and to build a common understanding of the topic for both regulators and stakeholders.

When CCIR looks into an issue, we follow a pretty consistent methodology:

- First we do research to better understand
- Then we consider the facts we've gathered against the first parts of our framework: what outcomes for consumers are we looking for, what are the potential risks to consumers
- Then we go to stakeholders with an Issues Paper to ask whether we have our facts straight.

On past issues papers we've listed potential risks to consumers and asked for input on whether we've identified them all and if the risks we've identified are significant. The Electronic Commerce paper was a little different in this respect because of the broad nature of the topic.

Electronic media can be used for product distribution, or for advertising, or for disseminating information. It can be used by insurers, licensed intermediaries, unlicensed service

providers, by consumers themselves – both as users of the other information and as information providers - and even by regulators.

All kinds of things that we were used to dealing with and controlling through paper flow are now possible to do without paper. And growing numbers of consumers WANT to do their insurance business online or on the phone. So, some very basic regulatory assumptions needed re-examination.

So, instead of possible risks, we listed possible consumer protection goals and asked for input on how best to achieve those goals in the electronic commerce context.

We are still sifting through the responses we've received on this paper, including one from CLHIA, so I cannot speak about the results of this consultation, but the possible goals are worth looking at anyway:

- 1) **Consumers have access to additional information/advice from a licensed intermediary;**
For the last century, the licensing of intermediaries has been the basic way that regulators have assured themselves that consumers would have a good chance of getting decent information and advice. Where does that assurance come from in an electronic world? Are the solutions of the last century still valid for this one? Consumers cannot afford to make a mistake on this.
- 2) **Consumers know they are dealing with a regulated entity;**
This problem isn't confined to the electronic world, but it is certainly exacerbated in it. How **do** we keep scam artists at bay?
- 3) **Consumers have and understand the necessary information about the products;**
- 4) **Consumers have the opportunity to review the accuracy of the information they provide;**

5) Consumers are aware of the terms and conditions;

All of these goals go back to our issue about consumers getting decent information and advice, and the answers aren't obvious to us. Do you ask the consumer to pass an online quiz before you sell to him? Who do we hold responsible if things go wrong for the consumer?

6) Consumers can rely on the transaction;

There has to be a method of positive feedback so consumers can be sure they actually have insurance at the end of a transaction. This is where we begin to miss all the paper we used to have.

7) The consumer's personal information is secure.

In addition to these possible goals, the Electronic Commerce paper also sought stakeholders' comments on whether consumers are better protected if the designation of beneficiaries and the termination of an insurance policy continue to be paper transactions. Paper has been a legal and regulatory security blanket for a long time. It may be time to let it go.

MGAs

Of particular interest to this gathering may be the principles put forth in our very recently published-for-consultation **Position Paper** on *The Managing General Agencies Distribution Channel in the Life Insurance Industry*.

Not an Issues Paper this time – we had one of those on this topic last year. This is the paper that comes out at the end of the process. We have already considered outcomes and have agreed on the significant potential risks to consumers, now we just have to deal with how those risks can be minimized.

Last year's MGA Issues paper succeeded in its goals. It mapped out the history of the growth of the MGA channel and our understanding of how the channel operates – we were pleased to have confirmation in the 20-odd responses we received that we got all that right.

And that volume of responses makes it pretty obvious that we were also successful in our goal of stimulating debate about the issues.

But, you may ask yourself: “Do these consultations really matter? Do they really pay attention to the responses they get, or are they just going through the motions with their minds made up already?”

I can assure you, when CCIR holds a consultation, it is a real consultation: we DO pay attention and what we hear DOES count.

The issues paper asked 26 questions regarding 6 areas of potential risk to consumers. The new Position Paper has only 4 recommendations, and two of those are recommendations to regulators about what WE are doing.

How much more proof could you need that we take your feedback seriously?

So, what are these recommendations?

Recommendation 1: Insurers must have in place effective systems and controls whenever they use the services of an MGA

This is probably a pretty familiar sounding recommendation by now, but I want to point out, that the foundation of this recommendation is based on good corporate governance and the CCIR’s position that insurers are accountable to regulators for their relationships with MGAs.

We are pleased to note the voluntary initiatives that the industry is already taking in this direction with the development by the CLHIA of its standardized MGA Compliance Review Survey and by CAILBA of its Compliance Toolbox.

Life insurers enter into MGA arrangements to meet marketplace challenges such as economies of scale, cost control and heightened competition. Insurers should have the flexibility to configure their distribution operations in the way most suited to achieve their corporate objectives. However, these arrangements can increase an insurer's dependence on the MGA which may increase its risk profile if the arrangement is not properly managed or controlled.

Effective governance and risk management of MGAs is an essential element in the safe and sound functioning of life insurance companies. Strong board and senior management oversight of MGAs help protect policyholders and allow regulators to rely on the insurers' internal processes, thereby reducing the amount of supervisory resources needed to ensure proper conduct within an insurer's distribution channel.

As we see it, effective systems and controls would incorporate four core principles:

- **Principle One – A Clear Strategy**

An insurer has a clear strategy for selecting, appointing and managing MGA arrangements as part of its overall distribution plan.

- **Principle Two – Thorough Due Diligence**

An insurer carries out thorough due diligence of each MGA prior entering into the arrangement to provide services.

- **Principle Three – Well Defined Roles and Responsibilities**

An insurer has a written agreement in place with each MGA which clearly defines the conditions, scope and limits of contracted services

- **Principle Four – Active Oversight**

An insurer proactively manages MGA contracts once in place to ensure compliance with contract conditions.

Recommendation 2: Insurers should incorporate the principles in CLHIA Guideline G8 - Screening Agents for Suitability and Reporting Unsuitable Agents into all of their business across Canada, including any contracts involving the outsourcing of these functions to an MGA.

This recommendation flows from the fundamental principle that the insurer has a “duty of care” obligation to ensure that agents selling its products are suitable, and to report misconduct to regulators. This “duty of care” obligation is already recognized by law in some, but not all, jurisdictions. Duty of care obligations are also contained in CLHIA Guideline G8. By incorporating the G8 principles in MGA contracts, MGAs will also be contractually required to follow these standards.

Recommendation 3: Regular market conduct reviews should be undertaken by regulators to determine if insurers and their agents are providing consumers with adequate information to make informed decisions, and suitable product recommendations.

While not something we asked about, and not directly linked to the MGA distribution channel, product suitability kept coming up in the stakeholder responses to the issues paper so we felt it needed to be acknowledged here.

An initiative is already underway by the Joint Forum of Financial Market regulators, which CCIR is a member of, which involves reviewing the processes in place at insurance companies when designing and developing new products and their marketing materials. The Financial Services Commission of Ontario has announced that they will be undertaking a review of product suitability as part of their strategic priorities for 2012 other provincial regulators are expected to join FSCO in this review which will undoubtedly inform the Joint Forum’s work. The objective here will be to understand and assess the processes agents use in making recommendations to consumers, and making sure these are effective taking into consideration the increasingly complex products in today’s insurance marketplace.

Recommendation 4: Regulators will develop options and an action plan to make sure that adequate information on life agents and MGAs is obtained in a timely manner.

Regulators must have a clear understanding of who are those individuals or companies currently licensed as insurance agents in their jurisdiction; what is their business model and role in the distribution of life insurance products (MGA, AGA, career agent, independent agent with or without contractual relationships with MGAs). CCIR will work with CISRO in developing options to make sure regulators are gathering the market intelligence required to assess risks in the marketplace.

You'll note that we are in the consultation phase on this Position Paper. Nothing is cast in stone yet.

At the end of the consultation period, the CCIR committee responsible for this paper – the Agencies Regulation Committee - will review the comments from stakeholders to this position paper, and will finalize its recommendations. They will then present their final recommendations to the full CCIR for adoption. Once adopted, each jurisdiction will consider the recommendations and evaluate the circumstances in its own jurisdictions to determine what changes, if any, are necessary to implement them.

WHAT LIES AHEAD

In addition to the work CCIR committees do on specific issues, CCIR members spend a considerable amount of time when we meet discussing things that worry us and what we might do about them.

We worry about the risks arising from the increasing interconnectedness of the financial system. We don't have financial pillars anymore, we have webs. We may be insurance regulators, but we have to pay attention to what's happening in the other financial sectors, because the consequences of actions in one sector spread to other sectors.

We worry that knee jerk reactions to the crisis of 2008 may result in unnecessary increases in regulation, or, alternatively, that not enough of the right lessons from that crisis will be learned and acted upon.

We worry about ballooning housing prices and the effect a correction may have on the capital ratios and even the survival of some companies.

We worry about floods and earthquakes. Not just because of the devastation wreaked when they occur but because of the long term effects such a catastrophe can have on the wealth and economic future of region and the nation. As Vancouver goes, so goes the Canada??

We worry about the aging population and what the retirement of so many in a short period of time will mean to the corporate memories of our institutions, including the CCIR, whose members are no bunch of spring chickens.

So, where will CCIR be going from here? What can the industry expect from regulators?

It should be pretty clear by now that CCIR will be proactively researching and considering trends, risks, and issues as they arise and consulting with industry and other stakeholders to check our understanding. No one knows the specific topics, my crystal ball works no better than yours, but the specific topics hardly matter.

What matters is that, as the industry changes (puts out new products, moves to new distribution channels, or whatever), as economic, demographic and technical forces move, we will be working **with you** to assess those trends, risks and issues and act to meet our regulatory goals: consumer protection and confidence.

CONCLUSION

We will keep expecting you to be fair to your customers, to apply good corporate governance practices and build ethical cultures, to live up to the best traditions of the life insurance industry –

Because,
That's what's best for your customers,
For your reputations,
And for the future of us all.

Thank you so much for your time and have a good remainder of the conference.