



Insurance Brokers Association of Ontario



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Submission from the Insurance Brokers Association of Ontario (IBAO) in response to the CCIR Paper entitled "An Approach to Risk-Based Market Conduct Regulation."

Thank you for the opportunity to respond to and be involved in this process.

The Insurance Brokers Association of Ontario (IBAO) represents in excess of 10,180 professional, independent insurance brokers plus support staff operating over 1,176 offices located throughout the province servicing the needs of the Ontario consumer. The Association represents the interests of our independent member brokers in a variety of ways:

- Advocates and works with governments on behalf of our members promoting free enterprise, in a fair, open and competitive marketplace.
- Advocates on behalf of their clients when proposed legislative changes affect the policies or insurance contracts available to the consuming public.
- IBAO also lobbies Insurance companies to ensure the voice of the independent broker is heard during their business planning and decision making processes in an effort to keep distribution costs as low as possible.
- IBAO will lobby insurers whenever we feel that their actions negatively impact consumers or consumer confidence.
- We provide ongoing continuing education and training opportunities to our members and strive to provide them high quality continuing education material in order to help maintain a higher level of professionalism than any other intermediaries that not only meets but exceeds the continuing education requirements of the Registered Insurance Brokers of Ontario to hold an insurance broker's license in the Province of Ontario.
- We also run licensing courses to introduce and educate new entrants into the insurance field with the basic knowledge requirements for an entry level license examination. We also provide continuing education to assist brokers in obtaining their RIBO Level II (unrestricted) License.

We continually ensure that our members are kept up-to-date with any industry issues throughout various communication channels. We promote the professionalism and integrity of the Independent Insurance Broker and many other support initiatives on behalf of our members.

IBAO'S MISSION STATEMENT

"To preserve and enhance the value and integrity of the
Independent Broker Insurance Distribution System and
to be recognized as an invaluable resource to and by member brokers"

THE ROLE OF THE INDEPENDENT INSURANCE BROKER

Our member insurance brokers act on behalf of their clients, the insurance buying consumers of Ontario. More importantly, unlike other insurance intermediaries, insurance brokers are independent and essentially employed by the consumers they represent, and not the insurers with whom they negotiate. Ideally, Insurance Brokers purchase insurance protection from a variety of insurance providers to best match the consumers' needs.

When a consumer suffers a loss, the insurance broker is often the first point of contact. Although the claim is settled by the insurer, to help alleviate some of the stresses that can often arise in an unfamiliar claim process, brokers act as trusted confidants to their clients until such time the claim is settled.

In addition to placing coverage and assisting with claims, brokers take the time to help their clients better understand the exposures they face and how the insurance products they recommend address, or more importantly do not address them. For more complex accounts, brokers will often provide additional risk management services. Regardless of the type of coverage, purchasing insurance is often a complex decision-making process. There are literally several hundred insurance companies to choose from, each offering their own advantages. Insurance brokers live and work in every community in Ontario, and their primary role is to make the best possible recommendation in order for their client to make an informed decision on the insurance protection they purchase.

Our member brokers live and work in every community in the Province of Ontario and also act as consumer advocates with both Provincial and Federal governments as well as insurance companies.

IBAO's RESPONSE TO THE CCIR PAPER ENTITLED "AN APPROACH TO RISK-BASED MARKET CONDUCT REGULATION"

This consultation draft outlines the potential benefits of Canadian insurance regulatory practices moving towards more of a risk-based approach, rather than a rules-based approach. The document outlines the desired outcomes as well as outlines seven potential benefits of the risk-based approach. We would like to address this paper by first outlining some general thoughts followed by comments relating to the proposed benefits and conclude with some additional thoughts about this proposal and the next steps.

From our perspective, the goal and direction of a risk-based regulatory framework appears to be a global trend for regulating insurance practices, and we commend the Canadian Council of Insurance Regulators (CCIR) for researching the possibility of a similar movement in Canada.

Initial Thoughts

The Canadian Council of Insurance Regulators has charged themselves with the task of harmonizing regulatory frameworks across Canada, and the rationale for taking this approach is clear.

The discussion document quite accurately points out that significant aspects of the regulatory structure surrounding automobile insurance provisions and rate reviews do not lend themselves to a risk-based regulatory approach. In Ontario, we believe this is a very accurate statement and our main basis of concern with this direction.

In addition to the latter, we believe in Ontario this point is magnified through the existence of an all comers rule and other provisions aimed at making insurance available to those who are obligated by law to carry it. In view of the fact that a large majority of Ontario's Insurance Act is focused on the servicing of Automobile Insurance, we caution CCIR about adopting a risk-based approach holistically.

We do, however, believe that despite the aforementioned points, several elements of a risk-based approach could be very effectively woven into the existing rules-based framework. One such example would be the self-assessment questionnaires and complaint reporting systems, some of which have been used in Ontario. We believe these tools will prove an effective way to prioritize those risks that require the greatest degree of focus by the regulatory body. Such tools may not only help establish guidelines to prevent the existence of future risk, but also provide a reference of industry practices when considering the degree of enforcement required in a specific situation where these guidelines are broken. IBAO believes these types of proactive approaches could easily be implemented as part of the existing rules-based structure, and it is in these cases that we are fully supportive of such implementation.

In the early sections of the paper, three challenges to implement the risk-based protocol are outlined.

The first challenge outlined describes encompassing insurance intermediaries and the different insurance distribution channels within the regulation. We agree there will be challenges exercising this type of regulatory structure over intermediaries.

For the risk-based protocols to move forward, one of the key components or requirements within the insurance industry are the actions of the individual board and senior management members within insurance companies. These individuals will be creating individual practices and procedures to meet regulatory requirements for consumer protection and product availability.

The implementation of risk-based protocols could work quite effectively at this level with the co-operation of the insurers because of the requirements related to the establishment of an insurance company that are included in the Insurance Act and the Insurance Companies Act.

- All insurers must have a minimum amount of capital liquidated in order to establish an insurance company.
- By virtue of this sizable requirement of capital, the insurance companies are all incorporated, and all have appropriate governance structures that require a board of directors to steer policy and make corporate decisions on behalf of the corporation.

Implementing a risk-based approach to regulation with intermediaries, specifically brokers, will prove far more challenging. By design, the broker distribution channel currently provides a layer of protection for the consumer who is party to an insurance contract with the insurer. The advocacy and independent advice of the broker prioritizes the interest of the consumer above the insurer. If a risk-based approach was implemented, this priority may be lost. The recent brokerage acquisitions by insurance companies certainly do not seem to place the consumers' interest first.

Market conduct regulations are provincially based, provincial economies differ greatly, and regulators need to reflect these differences as well as protecting the very different needs of consumers from one region to the next. In order to best serve the consumer, we strongly believe provincial based regulation in this area be maintained.

The second challenge outlined in the paper makes note of the fact that the regulation of solvency requires a fairly small number of well-defined risks to be addressed. Market conduct risks tend to be much more difficult to define and quantify. The members of CCIR have reached this conclusion in their own deliberations.

When reviewing a previous CCIR paper regarding Privilege and Whistleblower Protection, one of the immediate responses we received amongst our Board of Directors and membership in general, was the difficulty in being able to quantify what is actually required from a regulatory point of view to monitor market conduct. While risk-based protocols are being used around the globe and adoption of such protocols is becoming more and more common for regulation of financial institutions, it is our position that there is quite a large difference between the role of an actuary within a bank as compared to an actuary within an insurance company. While banks offer financial products, insurance companies offer property and casualty products or risk-based products. Because of the large number of variables, individuals and risks present, the number of ways in which the consumer may be impacted or prejudiced is exponentially increased.

Wealth management and risk management are two very distinctive industries with differing goals. For example, loss of capital gains would be treated with different cautionary and protective regimes than the loss of one's home or business. It may be that implementing changes in wealth management may serve the consumer well but similar changes in the risk management industry may not be in the consumers' best interest.

The third point listed as a challenge described the regulation of automobile insurance and the current prescriptive doctrines for rate reviews and filings that do not lend themselves well to a risk-based regulatory approach. We do not see any instance where a risk-based approach to automobile insurance could work successfully in the Province of Ontario, as the rules-based regulatory approach is required in an all comers environment. If Ontario's regulators were to move forward and apply a risk-based approach, we are concerned that the next step will be pressure from certain facets of the industry to review and inevitably eliminate the all comers environment. Careful consideration should be given to any movement in this direction. Removing the all comers rule from the Ontario marketplace, we believe, could lead to pricing volatility and product availability issues that would have a profoundly detrimental impact on consumers.

Implementation Notes

With the CCIR being a national body, we understand that adoption of any recommendations will be on a province-by-province basis. It is apparent that not all provinces agree that there is a need to move forward or examine this regulatory methodology. Traditional methods of regulation would be our preference at the intermediary level

An Approach to a Risk-Based Market Conduct Regulation

Defining Market Conduct Regulation

In response to your note to stakeholders on page 5 of your document, we have difficulty envisioning how a risk-based approach would work or unfold "equally" for intermediaries in Ontario.

As brokers, our comments are based on the potential consumer harm caused by any changes to the current regulatory environment. As described earlier in our submission, we see no benefit, but rather some potential harm to consumers should intermediaries be regulated under a risk-based approach.

Defining Risk-Based Market Conduct Regulation

Your third paragraph explains that most regulatory agencies have adopted risk-based techniques. They judge these methods to be the best way to meet their mandate to supervise financial markets in the way that accomplishes the goals of legislation and regulation. We understand this statement as it relates to financial markets, i.e. banks and credit unions, however, for insurance companies, specifically in the property/casualty marketplace, we would need more evidence of existing systems in place where this is the case. Our hesitancy lies in the additional and numerous ways in which consumers could be prejudiced because of the variety of factors examined in a placement of a property casualty insurance policy.

The fourth paragraph also provides an example of the regulator spending more time focusing energy where indicators suggest there is a high risk of non-compliance, rather than auditing all insurers equally. Once again, in the current rules-based regulatory framework, we would be surprised to discover that these types of activities were not already taking place, and regulators across the country were not, in fact, already spending the majority of their time investigating or providing clearer guidance to those parties that are evidently more inclined to act outside of the regulator's wishes. As mentioned earlier, we believe that use of some risk-based tool, such as self assessment questionnaires, would be a vital source of market intelligence and integrate well into a rules-based environment.

Marketplace Outcomes That Market Conduct Regulation Seeks To Achieve

This section of the document outlines micro-level outcomes as well as systemic level outcomes that the switch to a risk-based approach would hope to achieve. The goals and objectives outlined here are admirable. If we examine the goals listed within the micro-level outcomes, we feel that each of these could very easily be addressed under the existing rules-based system.

Following are comments made addressing each of the purported advantages to move towards a risk-based approach to regulating. The title for each of the following sections match those found within page 7 of the CCIR paper.

Clarity and transparency of regulation

"Because the identification and prioritization of risks requires an ongoing dialogue between regulators, consumers and industry, a risk-based approach would contribute to the clarity and transparency of the regulatory process."

Understanding the sentiment of the above statement, we are somewhat concerned that previous discussion papers supporting the adoption of risk-based regulatory structures has outlined a process whereby documents used in the self-assessment or audit process by insurance companies, as well as documents compiled by the insurance regulator itself would be privileged, and therefore not disclosed or viewable by the general public. If this is the case, then the criteria or basis upon which a regulator deems a specific insurance body to be high risk would not be transparent to the general public or the insurance industry-at-large.

Better understanding of risks

This continuing dialogue will also assist the market participants, over time, to a better understanding of actions that constitute risks to the achievement of the marketplace outcomes regulators are trying to achieve.

The document implies that a risk-based approach to regulation would improve understanding of the types of risks that the regulator is generally concerned with that would, therefore lead to insurance companies spending more time self-auditing their processes to achieve the outcomes the regulators are trying to achieve. Although this may be true, an alternate position is that a risk-based approach leads to more interpretation therefore, does not achieve understanding, especially not the black and white understanding that a rules-based approach already affords.

It seems that history has shown that the risk-based approach does not lead to the desired outcome described in this paper, but rather has the opposite outcome. We do not see how a risk-based approach would bring more clarity than a rules-based approach when outlining allowable and unacceptable practices. What we have seen is dialogue that has resulted in intervention by regulators to achieve the desired result and in some cases, expand on the existing rules.

Alignment with corporate governance

As this dialogue is centered on risks to marketplace outcomes, it is better aligned with enterprise risk management within the insurance industry. This alignment underscores the importance of corporate governance in modern regulation. If members of the industry understand the marketplace outcomes regulators are trying to achieve and how regulators assess risk to those outcomes, they can more readily assess the risk implications of their actions and see the areas where their internal policies and procedures need to be improved to keep risks in check.

The adoption of a governance-based approach is encouraging, especially when these practices equip boards and senior management with better guidelines on practices and procedures. However, in order to achieve the regulators' objectives, it is critical that both insurers and government interpret these objectives in the same manner.

Proactive Approach to Preventing or Solving Problems

The statements made within the supporting paragraph at this point outlined that problems with a potential market impact for a large number of individual consumers, or that affect a large number of market participants, would be addressed by regulators first. Surely, the same would be true of a rules-based regulatory approach, whereby those risks that pose the largest potential damage to the consuming public, in general, would surely take priority over those that pose a lesser amount of damage to the consumers. We are not sure this point provides any additional support for the overall goal or improves what should be in place today.

Whether rules-based or risk-based, one would assume that in both cases, areas of the greatest concern would take priority. Perhaps, the difference is in the manner in which a regulator gains its market intelligence. As previously mentioned, in addition to the review of complaint data, Ontario has also recently looked to the industry through a variety of self-assessment questionnaires aimed at identifying potential risks that may exist within the industry. We commend this new approach; however, believe these assessment tools can be equally effective in either a rules-based or risk-based regime. The accuracy of these self-assessments is crucial in order for them to be effective, and further consultation with all stakeholders to review the results may be warranted, and is a direction we would support.

Systemic Focus on Marketplace and Consumers

This point suggests that the rules-based regulatory structure is reactive in nature, designed to catch and punish. We do not disagree with the statement. The overall tone of the risk-based approach appears to be to allow the regulator more time to audit those corporations it feels present the highest level of risk. Why could this not be achieved with a rules-based regulative structure? We do not feel you can create any more clarity of what actions are allowable or unacceptable through a risk-based process than you could with a rules-based process. The current structure outlines the rules clearly, and there should be no question as to what activities are deemed to be admissible or not. What is in question is the willingness, in some circumstances, to comply. Corporations found to be in breach of the rules would learn very quickly which ones they should be paying greater attention to by virtue of those areas of the operation that are most frequently being audited to ensure compliance with the rules-based structure.

Increased regulatory efficiency

A regulator's key role is to enforce laws put in place to protect consumers. Risk-based approaches provide a more efficient way of doing that by dealing with problems that may affect many consumers at one time, rather than dealing with them solely on a case-by-case basis.

We have difficulty understanding the real difference in the approach between risk-based versus rules-based. It is not clear why regulators feel they can address issues on a more global basis using a risk-based as compared to a rules-based approach. It appears that the rules-based case-by-case approach allows the regulator to group together complaints against like companies, or types of complaints to understand which marketplace participants either pose the greatest risk of contravening current rules, or what kind of scenarios are commonly created that are detrimental to the consumer. Regardless of the regulatory approach, the key is the regulator's ability to enforce laws to protect consumers. This alone, should be the focus of concern, as our current rules-based regulatory structure appears to be somewhat forgiving when it comes to penalizing those found to be in breach. The enforcement of laws is crucial and should not be taken lightly. Without consequences breaches will continue, regulators will become less effective, and the consumers' best interest will not be served.

In Closing

In Ontario, as well as across Canada, regulators are currently working diligently to get a better overall understanding of the current regulatory marketplace. CCIR has recently been active with the release of a questionnaire on Insurer Practices for Managing Conflicts of Interests and the Consultation Paper on Privilege and Whistleblower Protection. This would suggest that concerns exist within the industry today, and we understand that tabulating and reviewing the results of these surveys will take some time. We would suggest that a complete review and consultation with all stakeholders take place before CCIR implements any changes to the current structure. The work that is currently under way will give all stakeholders a better understanding of the obstacles present today that need attention. In order to move to a principle-based or risk-based regulatory environment, there needs to be a desire to change and from our perspective, the lack of desire of some outweighs moving forward.

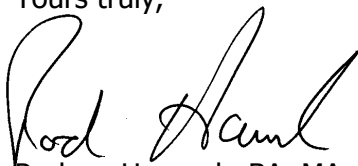
Brokers are principle-based and the one guiding principle that serves as the backbone of our beliefs is that the priority or interest of the client is foremost and takes precedence over our own interest. Today, we are seeing insurers who are willing to ignore that principle in return for their own internal gains. Fortunately at this time, there are very few insurers taking this position, but nevertheless it is a fact in our industry today. As stated earlier on in this document, principles need to apply equally and until there is willingness by all parties, implementing any change would be risky at best. We have to be mindful of where we are and not lose sight that our business is cyclical. Currently, we are in one of the softest markets we have seen in the history of our industry. It is a time when willingness to use capacity, availability and flexibility are exhibited by nearly all insurers and it appears almost any change is possible. The inevitable next hard market will result in a change of appetite; therefore, we need to tread lightly.

Lastly, the comments within the White Paper entitled "The Road Ahead," seem to indicate that the proposed risk-based approach will be the recommendation, and regulators will begin to move in this direction following the consultative process. The tone is quite decisive. If stakeholder responses to the White Paper demonstrate that further investigation is required into the potential difficulties and problems that may occur through implementation of a risk-based approach, we are quite confident that CCIR's recommendation to its regulatory membership will be to stay implementation pending the necessary investigation.

For us, the paper raises many more questions than answers, and we would like to take advantage of the offer extended within the paper to meet in person with the Council to discuss the issues around Risk-Based regulation. The Executive Committee of the IBAO Board of Directors would greatly welcome such a meeting. To arrange a meeting, please contact Randy Carroll, Chief Executive Officer at 416-488-7422.

Once again, thank you for providing us the opportunity to read and respond to the consultation paper.

Yours truly,

A handwritten signature in black ink, appearing to read "Rodney Hancock". The signature is fluid and cursive, with the first name "Rodney" and last name "Hancock" clearly distinguishable.

Rodney Hancock, BA, MA, Ph.D, CCIB
President