

July 28, 2005

Mr. Stephen Paglia
Policy Manager
CCIR Secretariat
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Re: Industry Practices Review Committee Consultation Paper on Relationships between Insurers and Intermediaries

State Farm appreciates the opportunity to comment on the June 3, 2005 Consultation Paper issued by the Industry Practices Review Committee of the Canadian Council of Insurance Regulators (CCIR) and the Canadian Insurance Services Regulatory Organization (CISRO).

As an initial matter, we emphasize that, as a member of the Insurance Bureau of Canada (IBC), we fully support IBC's commentary on the Consultation Paper. We urge CCIR to give serious consideration to IBC's recommendations and observations as they represent the collective thinking of a substantial portion of the insurance industry. However, there are certain matters that involve the unique relationship that State Farm and other similar insurers have with our exclusive agents that could not be adequately addressed in IBC's comments which are on behalf of a more diverse group of insurers. In order that CCIR is fully informed as to State Farm's business model we write separately and in addition to the IBC.

We applaud CCIR's efforts in taking a thorough and fact-based approach in investigating the relationships between insurers and their sales intermediaries. As set forth in the Consultation Paper, it appears that no violations of law have occurred in Canada in this area. State Farm wishes to emphasize, though, that even in the U.S., where Attorney General Spitzer and other investigators did uncover some apparent violations, those instances involved arrangements where brokers represented more than one insurer and where a particular customer's business may have been placed in conflict with the customer's best interests.

Recognizing this particular set of circumstances, legislators and regulators in the U.S. addressed the situation by proposing rules that distinguished between intermediaries that represent multiple insurers in the same product line and intermediaries like State Farm agents who only represent a

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single insurer in a product line. In fact, the current proposals do not apply to agents that work with a single insurer.

Throughout its history of more than eighty years, State Farm's insurance and financial service products have been sold only through its exclusive agency force and those agents sell only State Farm products or, in some select cases where there is no State Farm product available, products from other vendors which are secured through State Farm. State Farm's agreements with its agents establish the exclusive relationship with State Farm and do not permit State Farm agents to act as brokers for the sale of products from other organizations.

We believe that in the relationship between State Farm and its agents there is no element of customer confusion as to what products they are purchasing or any belief that there may be products available from other insurers. What's more, there is no opportunity for the sort of conflict of interest that may have been an issue in the U.S. investigations. There can be no steering of business among different insurance organizations and any element of compensation or ownership cannot influence the placement of business because all risks must go to State Farm or its select partners.

We recognize that some may argue that the mere fact of compensation, whether monetary or nonmonetary, of an intermediary in connection with the sale of a product of service raises a conflict of interest because it influences the intermediary to push for a sale. We note that in this context the Ontario regulation on agent licensing has not been interpreted to include ordinary compensation as a conflict of interest. And even if a commissioned or incentivized sale carries the possibility of a conflict between the interests of the client and the salesperson, State Farm believes that the most appropriate method of dealing with the situation is to disclose relevant information to the client.

State Farm has supported balanced disclosure regimes and has voluntarily participated in the Ontario program that incorporates point-of-sale release of a statement of consumer rights and responsibilities along with information about State Farm's compensation practices.

But while we support a program of relevant disclosure, we believe it is inappropriate to prescribe or limit how an organization may compensate its sales intermediaries. State Farm does choose to use a package of monetary and nonmonetary compensation for its agents – this is a matter which is governed by the private contracts that State Farm has with its agents. Regardless of the elements of compensation involved in any particular transaction, however, the price that State Farm customers pay does not change.

Should competitive pressures warrant, State Farm has and will continue to shape and refine its agent compensation program but we believe that this is a matter that should be left to the private arrangements between insurers and their sales intermediaries and should not be an object of regulation or legislation.

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The bottom line for State Farm is what works in the competitive marketplace. The greatest check on compensation for our agents is the price at which we can sell our product vis-à-vis our competitors. Naturally, we try to beat any competitor's package of service and price but if a competitor gains a temporary edge on us we respond by seeking efficiency, reinventing processes or redesigning compensation. The net result is that we aim to offer the best product at the best price to any consumer in the markets we serve in Canada. Rigid rules will only serve to undermine responsiveness to consumer needs and a rapidly changing marketplace. We urge CCIR to let the competitive marketplace continue to work.

State Farm hopes to continue to work with CCIR and CISRO to develop an insurance marketplace that serves consumers' needs in as efficient and effective a way as possible and we thank you for the opportunity to participate in the consultative process.

Sincerely,

A handwritten signature in black ink that reads "Bob Cooke". The signature is written in a cursive, slightly slanted style.

Robert J. Cooke
Senior Vice-President
State Farm Insurance Companies