



August 3, 2005

Stephen Paglia  
Policy Manager (A)  
CCIR Secretariat  
5160 Yonge Street, Box 85  
17<sup>th</sup> Floor  
Toronto, Ontario M2N 6L9

Dear Mr. Paglia:

**RE: CCIR/CISRO Consultation on Relationships  
Between Insurers and Sales Intermediaries**

I am writing on behalf of the Canadian Association of Direct Response Insurers (CADRI) in response to the consultation document recently released by the joint CCIR/CISRO Industry Practices Review Committee (IPRC) on the relationships between insurers and sales intermediaries.

Before turning to the specific questions posed in the consultation document, CADRI would like to make some comments of a general nature. The efforts of the IPRC in reviewing current industry practices have provided all stakeholders with important information on how the Canadian insurance market actually functions. The results of the surveys, both IPRC's and the RIBO survey of brokers, document the nature and extent of certain practices regarding insurer/intermediary relationships. Potential regulatory concerns are examined and various policy options for addressing them are discussed.

The IPRC set laudable goals for this exercise: to determine whether issues similar to those in the United States could arise in Canada, and to identify opportunities to enhance public confidence in the Canadian insurance marketplace. CADRI believes that these goals have already been largely achieved, in that the U.S. issues were found not to be a factor in the Canadian marketplace, and no evidence of illegal activity was found. While there may be some outstanding issues relating to perceived or actual conflicts of interest, these are limited and manageable. The RIBO survey of Ontario brokers similarly concluded that there was no evidence of undue "steering" of business because of financial relationships with insurers. These findings indicate strongly that provincial and territorial regulatory regimes governing intermediaries are working as intended. The necessary controls already in place through laws, regulations and voluntary undertakings are having an effect in the market.

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Publication of the survey results also helps to raise awareness of potential conflict of interest issues that could arise during an insurance transaction.

Given that there is no evidence of illegal activity in the marketplace, CADRI does not believe that it is necessary or advisable to initiate a range of new regulatory responses, which will entail compliance and enforcement costs that do not seem justified in terms of benefits to consumers. The practices identified as possibly contributing to a “perception of or actual conflicts of interest in the marketplace” have not been shown to affect consumers in any demonstrable way. While the report states that these practices “may have a negative impact on consumer confidence”, consumers have not been surveyed about this. Moreover, some of the practices, such as non-monetary sales incentives, are not used widely in the P&C industry.

A risk-based regulatory approach was taken in developing the market conduct assessment questionnaire, and it would seem that risk-based regulatory principles should apply to the outcome, i.e., that more prescriptive, interventionist regulation should be directed at the areas of highest risk in the insurance system. The CCIR/CISRO findings show that the financial relationships between insurers and sales intermediaries is, in fact, an area of lower risk. Most insurers have policies and procedures in place to mitigate potential conflicts of interest, and standard contracts are used with brokers selling their products. While the use of contingent commissions is widespread, they are too diffuse and paid after long time lags to expect them to influence particular transactions.

As there was no clear problem identified, there is no justification for the range of regulatory solutions identified in the consultation document. In some cases (e.g. disclosure to consumers), voluntary measures have been adopted since the survey was taken; these address the concerns raised in the paper, but are new. The consultation document mentions building on these requirements, but CADRI believes they should be in operation for at least a year and then assessed before further requirements are layered on top of them.

If it is determined by the IPRC that new policy responses as proposed in the consultation document are necessary, then CADRI submits that it should be recognized that most of the issues simply do not apply to direct writers of P&C insurance. There is no conflict of interest when an intermediary represents a single insurer. The intermediary’s remuneration will not vary based on the particular product sold. Nor is there need for special disclosures to inform consumers of something inapplicable to the transaction at hand.

Following are CADRI’s responses to the questions on pp. 15-17 of the consultation document.

## Policy Options

1. *How do the policy options affect you (insurers)? Do the policy options alter current intermediary relationships with insurers and consumers/clients respectively and if so, how?*

The policy options would have a variable effect on insurers. With respect to codifying the priority of the consumer's interests, there would be no clear-cut effect. This principle already underpins insurance sales through several mechanisms, including intermediary codes of conduct, voluntary industry codes, and the Joint Forum's Principles and Practices for the Sale of Products and Services in the Financial Sector.

Disclosure options would likely have the biggest effect on insurers, but the impact would depend on the content to be disclosed, who would make the disclosure, and how. However, we do not believe any of the options fundamentally alters the intermediary's relationship with either insurers or consumers.

2. *How would the policy options affect the existing methods of insurance distribution?*

CADRI's concern is with a particular form of distribution: direct response, which involves call centers, direct mail and the Internet. The call center environment requires scripts to be used and also places a premium on brevity; callers simply will not stay on the phone to listen to paragraph after paragraph of information not geared to their immediate concerns. Thus, it is of paramount importance to direct response insurers not to lengthen disclosures or include information that may serve to confuse consumers rather than enlighten them. It would also be troubling to have to make disclosures that do not have any bearing on direct response distribution; e.g., regarding financial relationships, compensation of intermediaries who are usually employees of the insurers, and similar issues.

3. *Are the policy options the best means of accomplishing the objectives identified in the consultation paper?*

No, CADRI believes that the policy options presented are duplicative to some extent with currently existing measures and/or are not commensurate with the problems/risks identified. Given that no clear problem was identified, it would be appropriate to continue monitoring the marketplace for evidence that confidence in the insurance system is actually being jeopardized before intervening.

4. *Have the policy options overlooked any other approaches or considerations?*

Yes. There are other possible approaches to enhancing public confidence, such as: surveying consumers, undertaking consumer education initiatives, and publicizing information on regulator and company web sites rather than making it part of every transaction. It would likely be worthwhile to survey brokers in other jurisdictions (replicating the RIBO survey) before implementing new disclosure rules that do not appear, from the Ontario findings, to be necessary. With respect to the findings in the Quebec market, we understand that another consultation will be held in September to consider issues there.

5. *As a consumer/client, do you feel your interests will be better protected by some or all of the policy options . . . ?*

N/A to CADRI.

6. *Are there any regional issues or considerations such as different distribution channels that have not been adequately considered?*

See question #2 with respect to distribution channels.

### **Scope and Applicability**

7. *This consultation paper proposes two potential approaches for determining the scope and applicability of the policy options. Do you have a suggested approach re scope and applicability?*

It makes sense to apply the policy options only to intermediaries who hold themselves out to be independent, since they are the ones making a claim that the public relies on. However, it would be administratively cleaner to apply any policy options to all intermediaries, across all types of insurance and channels, avoiding the issue of “who is independent”. CADRI would support this broader application as long as specific provisions allowed for the unique circumstances of direct response—e.g., disclosures would not have to be made if an issue could not arise in the direct response sales environment.

8. *Should some or all of the policy options apply only to intermediaries that hold themselves out as independent, or should they apply to all intermediaries?*

See the answer to #7; CADRI has a particular concern about the disclosure requirements that may be adopted.

9. *Do you have any suggestions for describing or interpreting independence?*

It will not be simple to identify which intermediaries are “independent”, particularly in light of market trends in recent years, when some brokers found themselves losing markets. In making this determination, CADRI believes that it would be useful to remove all direct employees and career agents who represent only one insurer from the

“independent” category. While having more than one market may or may not be enough to consider an intermediary to be independent, it might be useful to include anyone using the broker association logo, which has been heavily promoted as a mark of independence and way to differentiate brokers in the marketplace.

*10. Some intermediaries provide additional services to insurers or to consumers on behalf of insurers. Are there any services . . . that may create conflicts of interest or potential conflicts of interest?*

CADRI does not believe that additional service arrangements, such as claims or policy service, pose any problems regarding conflicts of interest.

### **Performance-Linked Benefits Provided by Insurers to Intermediaries**

*11. Is the concept of performance-linked benefits sufficiently clear?*

Yes.

*12. Should performance-linked benefits be regulated and if so, how?*

CADRI does not believe it is necessary to intervene in the workplace incentive programs currently in use. In the direct-response model, most compensation paid to agents is salary; there are typically some small cash bonuses available for meeting sales volume targets. We also undertake extensive training and ensure that employees understand their obligations to assess client needs and provide sound advice. As direct writers, there is no possibility of a conflict of interest with respect to recommending one insurer’s product over another because of varying compensation.

*13. Should the restrictions on performance-linked benefits be absolute or limited by introducing appropriate controls and qualifications?*

CADRI does not have comments on this.

*14. In determining what constitutes a performance-linked benefit, should the relevant rules be principle-based or compliance-based?*

CADRI strongly favours principle-based regulation. Compliance-based regulation will likely lead to the need for repeated revisions as some players may seek to introduce new benefits to get around existing rules. It is more straightforward and cost-effective for everyone if the rules are based on principles that can be applied to facts. That also minimizes the risk of regulatory variation across jurisdictions.

*15. Some insurers offer services or assistance to intermediaries (e.g., office space). While these services/assistance may not be linked to a specific performance target, some may argue that they create a potential conflict of*

*interest. Do you agree that regulatory measures need to be introduced to address this potential conflict of interest?*

CADRI does not have a view on these other forms of assistance. These issues do not arise in the direct response environment.

## **Disclosure**

*16. The disclosure option provides for differing levels of detail, timing and methods of disclosure. As an intermediary or insurer, do you anticipate any difficulties in complying with this option?*

Yes, we would anticipate several difficulties, including the length and complexity of new disclosures; the requirement that some disclosures be in writing when our methods are based on verbal/electronic interactions with customers, and the fact that some of the information identified would be difficult to keep current. For example, financial relationships change over time and may fluctuate as market valuations of companies do. Similarly, lists of intermediaries with whom an insurance company works would be changing constantly.

*17. Is the scope of the disclosure option broad enough to provide consumers/clients with sufficient information to make informed purchase decisions? If not, what else should be included? Do you have any suggestions as to how this disclosure option could be structured so that it would be easier to understand?*

The scope of the disclosure option is arguably too broad. Given that there is no evidence that loans, ownership or other financial relationships have led to brokers “steering” business in the RIBO survey, and the fact that this information is both complex and changing, CADRI does not believe it serves consumers well to require such disclosures.

With respect to the two options for enhancing transparency, CADRI would support the second one, Industry-led Best Practices for Disclosure. However, rather than immediately undertaking “an expansion” of the cooperative disclosure initiatives adopted by the P&C insurance industry at the beginning of 2005, CADRI believes that those new practices should be in place for at least a year and then assessed before further requirements are added. It should be noted that some companies have already implemented the new disclosures nationally, rather than in Ontario only.

*18. As an intermediary or insurer, do you anticipate any difficulties disclosing the **quantum** of any commissions and service fees associated with the specific transaction, excluding any contingent commissions, expressed in dollars and as a percentage of the premium?*

CADRI does not have any problems with commission and fee disclosure; it should be noted, however, that our members do not generally use this form of compensation.

*19. Do consumers need to understand how an intermediary is paid for his/her services (e.g., contingent commissions and bonuses) and how much in financial terms the intermediary earns from the sale of a policy to a consumer? Is it relevant information for the consumer?*

It is important for consumers to understand how intermediaries are compensated (method of remuneration). However, CADRI does not believe it is necessary for absolute amounts to be disclosed. Consumers are able to comparison shop based on quotes for certain insurance coverage. The total cost and value proposition are what is important, not how much of the cost is paid to the intermediary.

*20. Are there any innovative methods of satisfying disclosure requirements that you can provide that have not been considered in this consultation paper?*

CCIR/CISRO could develop a standard statement that informs consumers of the issues involved in financial relationships, or support a consumer group in creating their own communications focusing on “myths in insurance”, i.e., taking on areas that are commonly misunderstood by consumers. Insurers and intermediaries could make this and other information available on web sites, for consumers to access if they wish.

*21. Are there any alternatives to disclosure that regulators should consider?*

Consumer education initiatives, continued monitoring of market developments in the areas identified.

### **L&H Insurance**

*22. pertains to L&H insurance*

N/A to CADRI

### **Regulatory Compliance**

*23. Are the policy options cost-effective and enforceable?*

The answer to this question depends entirely on the choices made under each option—e.g., whether to focus on industry-led best practices for disclosure or develop new disclosure regulations; whether to ban or limit some or all performance-linked benefits, etc. Most would be enforceable, but we would question the cost-effectiveness, given the modest benefits for consumers in the absence of a clearly defined problem.

In closing, I would like to thank you for giving CADRI the opportunity to meet with representatives of the IPRC last week. We hope that both the informal discussion and

these written comments will assist the IPRC in making its recommendations to CCIR and CISRO on the best course of action now with respect to intermediary/insurer relationships. CADRI commends the IPRC for publishing the survey results; this has provided a valuable service to the marketplace by shining a light on current market practices and highlighting issues that all stakeholders should be aware of as potential concerns. Please do not hesitate to contact me if you would like to discuss this matter further.

Sincerely,

Richard Evans  
President