REPORT

INSURANCE INDUSTY

BY

Financial Services Consumer Alliance

# Canadian Insurance Industry in a Regulatory Crisis: Commercial Practices – Norms of the Industry – Laws and Regulations: Are the Gaps too Large to Overcome?

*Service is the accessory to the sale. If there is no more service, there are no more sales. (from a judge of the Superior Court of Quebec)*

## Executive Summary

The regulatory environment surrounding the sale of insurance in Canada could be considered one of the great mysteries for a neophyte. Perhaps it is a consolation for this neophyte to know that this environment represents a greater mystery for a professional like me with more than 20 years of experience in the financial industry. While regulations in the insurance industry remained frozen in time, the regulations for securities, investments, general insurance and mortgages continue to change in order to remain relevant with the objective of increasing the protection of the public.

This created a gap or distortion in the financial industry where the insurance industry can for example sell the same investments using some of the practices prohibited for the sale of mutual funds or by distributing insurance according to practices prohibited in the general insurance industry. This was the subject of a letter to the "Canadian Securities Administrators" in relation with new regulations regarding mutual funds whereas the same investment in insurance is absolutely not regulated. http://911insurance.wordpress.com/2013/03/07/the-financial-regulatory-apartheid/

Whether it is the Insurance Act of each province, the Law on the distribution of financial products and services specific to Quebec or the Federal Income Tax Act in regards to the taxation of life insurance, these laws have not evolved or changed in the last 40 years (note: the exception is Quebec with the Law on the distribution of financial products and services introduced in 1998). While the commercial practices of the life insurers were evolving rapidly because of technological and social changes and the globalisation of the economy, legislators and regulators have maintained a regulatory status quo. A perfect example of this situation is with the demutualisation which accelerated the privatization of the distribution of insurance by the transformation of the career agencies into independent distributors. This was the subject of a discussion in "**Record volume 26 NO3 Session 130PD US and Canadian Demutualization - Postmortem, Barry Shemin:**

"*In our career agency system, we eliminated a branch system and merged it into our general agency system where the general agent owns the agency. Now that we have a separate distribution company we are increasing our use of bottom line distribution financial measures. This is happening gradually, but, over time, the separate company will become more separate and will be expected to stand on its own feet. And we reduced the hiring of inexperienced agents for economic reasons and are focusing more on programs to attract experienced agents."*

However the Insurance Act in each of the provinces with the exception of Quebec still addresses distribution through the agent model which takes its source from the career agency. For these provinces, it is still necessary for an insurance representative to be sponsored as an agent by an insurer in order to provide advice or sell life insurance. This is in contradiction with this separation now existing between insurers and representatives with the introduction of new intermediaries named Managing General Agent (MGA). This separation has evolved to such an extent that the agents are representing themselves in the marketplace as being independent

brokers whereas in terms of most regulations this is not the case. This sponsorship also became a barrier to the entry of new recruits into the insurance industry. Under the sponsoring model, the recruitment of new representatives without experience is facing serious challenges because most companies have little motivation to sponsor such representatives. Again Quebec alone tried to address this problem moving away from this system of sponsorship with the introduction of the Law on the distribution of financial products and services.

The declaration of Shemin also showed a major problem. Without the recruiting of inexperienced agents, the pool of experienced agents becomes ever more smaller and the competition more intense between the insurance companies. To attract the advisors, these companies have to offer sales incentives that are in opposition with this strategy of separation and independence jeopardizing the objectivity of representatives who are representing themselves as being independent. This type of commercial practices and conflict of interest was denounced by the **Regroupement Indépendant des Conseillers Financiers du Québec in a letter to the regulator, the AMF:**

*"Thus this put in question the "moral legality" of some of the commercial practices which, by their nature, place the advisor in a situation of conflict or appearance of conflict of interest, necessarily to the detriment of the interest of the consumer. »*

This demutualization had another effect even more pernicious as it is described by **Robert Willson on the demutualization of Sunlife in the same document and discussion in Chicago:**

"*We've also put in an early retirement package in Canada and Great Britain. In Canada, 250 people out of around 3,000 took the opportunity to retire. In Britain, about 60 people retired, but it's a much smaller operation. This has resulted in a very significant loss in corporate memory which has interesting ramifications since we have new management who don't really know how the company has worked. They know how the public world works, but they don't know the company itself."*

This declaration of Wilson illustrates a phenomenon that is not well understood by the regulators. This loss of corporate memory is one of the most important elements which explain why many of the commercial practices of the insurers violate insurance laws. This demutualisation of the profits associated with this loss of corporate memory created a gap between practices, norms and laws. Ethical conduct was the first casualty of this environment. The best example of this situation is, as we shall see in more details later, the existence of orphan policies. These orphan polices which by law cannot even exist are extremely common in the insurance industry and are the result of the demutualization and privatization of the distribution leading to the disappearance of the career agencies with some companies conveniently forgetting to address the existence of the in force blocks of businesses that were under the responsibility of their career agencies or branches. Our first case study on Manulife will demonstrate this phenomenon in all of its ambivalence.

Our analysis Post Mortem of the demutualization will illustrate how this demutualization allowed the injection of the capital necessary for the buyout of insurance companies in financial

difficulties not at a discounted price but at prices that were grossly exaggerated which compounded the problem of the existence of the toxic insurance products sold by these companies as described by Julie Dickson, Superintendant OSFI:

*"I have attended this conference on several occasions in the past and one that I remember particularly well was in November 2005. There was a session on the history of toxic products in Canada. A reinsurer provided all the gory details. He said that the first major Canadian insurance industry toxic product was "Term to 100", offered in the 1980s. This product was a great idea at the time, but the problem was that early years' premiums far exceeded expected claims, and later years premiums were far less than claims. The industry had assumed that lapses would be the same as with other products, and they were not – the educated guesses turned out to be horribly wrong and the consumer response was more sophisticated than expected."*

As for the taxation associated with life insurance, the situation is even direr and the commercial practices of the insurers even more abusive. It is now about 40 years since the insurance industry has waited for the Federal Department of Finance to propose changes and updates to the Income Tax Act to the Minister of Finance in order to clarify and improve the taxation of life insurance. The contradictions in the interpretations of the Income Tax Act by different insurers have created a lot of problems for the industry. This problem has degenerated into a crisis. Insurers have used these contradictions in their interpretations of the Income Tax Act as a marketing and sales strategy to increase sales of life insurance. The best example is with Maritime Life giving itself a competitive edge in the sale of segregated funds by interpreting the Income Tax Act liberally in regards to the taxation of these funds by treating distributions as capital gains while other companies such as Transamerica treated the same distributions as income. The same thing happened with the introduction of the 10/8 leveraging strategy where again companies abused the Income Tax Act by making very aggressive interpretations of the Income Tax Act in regards to the deduction of interest from policy loans taken to earn income. This also demonstrate the lack of willingness and ability of the insurers to police themselves by acting responsibly through consensus achieved through their own association CHLIA (Canadian Life and Health Association) which truly failed to promote corporate ethics and responsibilities within its members. In the end, it is the taxpayers who have picked up the tab to cover the cost of the abuses of the insurance companies.

There is an enormous problem of ethics within the insurance companies at the level of the executives. Each time the regulators prohibit a commercial practice by introducing or modifying a law because the results of this commercial practice are considered improper, executives of insurance companies use all of their resources and knowledge at their disposition to go around this law in order to institute a new commercial practice which will deliver the same results that were considered as being improper. This corporate culture of « executives/cheaters » is hurting the industry and has even stalled the introduction of new legislations. Regulators know they cannot count on these executives/cheaters to be responsible and to show restraint. These regulators are trying to come up with the perfect laws and regulations that cannot be bypassed. In view of the complexity of the insurance industry, such laws and regulations do not exist and

as a result the insurance industry is in a position of perpetual legal stalemate where regulators are afraid to make things worse by updating the laws. A good example of this situation is the management of the single premium insurance problem and how it was prohibited by the regulators and how some insurance companies were able to go around the law in order to produce the same results. The solution of the regulators at the time was to prohibit the sale of the single premium life insurance with the introduction of the MTAR and ETP regulations which have been abused by the insurers which has now prompted the Department of Finance to propose new legislation for the introduction of a “Tax Avoidance Policy”.

Only Quebec offered a flicker of hope when it introduced the Law on the distribution of financial products and services. This law was revolutionary. However as we will see, this law was a success but also a great failure. This law was a great success because for the first time the question of the independence and autonomy of the insurance agent was addressed. In fact for the first time, this law recognized that the public had an interest in regulating the distribution of financial products which so far had been mostly under the domain of the insurers’ competencies and responsibilities. This law forced the immigration of the distribution from its corporate domain of responsibilities to the public domain of responsibilities. As a result, all insurance representatives have to conduct themselves professionally and were obligated to join a professional association which is « La Chambre Financiere » and were forced to adhere to a code of ethics and professional conduct which is still a choice in many other provinces.

This law was a great failure because it did not change the way insurers did business in Quebec. Their commercial practices remained the same. This is because the Quebec Regulator, the AMF, refused to apply the Law on the distribution of financial products and services allowing insurers to operate outside of this law. This position of the AMF is clearly stated in a very strange letter written by its past president St-Gelais in response to complaints made in regards to these commercial practices by the Association for independent advisors in **Quebec named the Regroupement Indépendant des Conseillers Financiers. This letter of St-Gelais stated:**

*« We have to inform you that we will be unable to follow up on your request to take a position in regards to the commercial practices listed in your correspondence. Indeed the role of the AMF is not to validate the legality of the commercial practices taking place in the industry at the request of interested parties.»*

This strange letter of the previous president of the AMF represented a refusal by the AMF to apply the law to the insurers and to exercise the powers and responsibilities as conferred to this organization by the National Assembly of Quebec. Even worst, the AMF established a system of regulations which excluded the insurance companies but strictly applied to the insurance advisors. The infractions of the insurers in relation to these illegal commercial practices were going to be addressed solely by taking selective action against the insurance advisor. By going after the advisor through penal and administrative proceedings, the AMF hoped to influence the insurance companies in willingly changing their illegal practices. As I have said before in giving this example, it is like the police deciding to fight prostitution by arresting the prostitutes while

ignoring the actions and the existence of their Pimps. The AMF pushed this folly to such an extent that it decided to keep secret the views of advisors regarding the commercial practices of the insurers by refusing to publish a survey made on these practices; even denying the existence of such survey under a request to have access to the survey's results made under the Freedom of  Information Access Act.

http://www.conseiller.ca/nouvelles/pratiques-commerciales-en-assurance-de-personnes-lamf-ne-publiera-pas-de-rapport-15239

This created an environment where 100% of the insurance advisors in Quebec are committing infractions and are in violation of the Law for the distribution of financial products and services or their code of ethics when the advisor accepts to conduct their operations on the basis of the commercial practices of the insurers. The extent of the gap between commercial practices, norms and the laws is so large that this situation has criminalized the environment in which the advisor operates. This is viewed as a positive by the AMF and the syndic of la Chambre Financiere because this creates a pool of infractions from which they can easily work and earn convictions while justifying the need for more resources and regulations while at the same time receiving financial incentives from fines earned against advisors found guilty of having followed the commercial practices of insurers.

This explains why in 1 month only, in Quebec, there are 500% more advisors that are found guilty of an infraction than for the whole of Canada for one complete year.

http://contrelamf.wordpress.com/2013/02/20/la-corruption-une-maladie-des-quebecois/

Suddenly in 2013, there have been more changes in 3 months than in the last 40 years. These commercial practices through my relentless work have attracted the attention of the legislators. The Federal Minister of Finance has addressed the abuses of the insurers in relation to the strategy 10/8 by prohibiting such leveraging strategies. Le Quebec Minister of Finance will also revise the Law on the distribution in this province.

As a result, there is an opportunity to change the industry for the better on the basis of the interest and protection of the public. Still, there are a lot of doubts about whether this will happen and there is some fear that the changes will favor particular interest groups. This has been stated in this article: « **Pratiques Commerciales, les besoins des clients relégués au deuxième rang »** http://www.conseiller.ca/nouvelles/ppratiques-commerciales-les-besoins-des-clients-relegues-au-second-rang-39222

The objective of this report is to ensure that the interest and the needs of the public are first considered by educating the legislators on what is actually happening within the insurance industry. Changes will not come from those who have cheated the law. Is it too late? Is the gap between commercial practices, norms and the laws too enormous to be overcome? The answer is hard to find. It is however clear that the introduction of different class actions against various insurers in the last year was not an accident. This represents a symptom of this regulatory gap

which transforms clients into victims of these fraudulent regulated commercial practices. Sadly this is only the beginning. The number of class actions will only increase in the future to such an extent that it will put into peril the solvency of the insurance industry at a point of time when this industry is facing serious challenges such as the low interest environment in which it cannot operate profitably. I predict in fact that in order to protect and save this industry the government will have to intervene directly or indirectly to provide support or immunity to the insurance companies in regards to their past commercial practices. Do not be surprised? This has already happened when the Minister of Finance Flaherty secretly modified the Income Tax Act without any challenge from the opposition to save the insurance companies and advisors involved in selling the 10/8 strategies from being sued by very powerful and wealthy clients. The public and the taxpayer have yet to know the cost of this bailout that it will have to pay.

## Author's notes

I would like to dedicate this report to the Quebec regulator known as the AMF (Autorite des marches financiers). Without all of the energies and actions deployed by the AMF to keep me from publishing this report, I would never have had as much determination in publishing it. Sadly this report will contain little information on the point of views and preoccupations of the financial advisors. This is because I was hoping to learn about such preoccupations through a survey conducted by the AMF many years ago. I therefore did a request under the Access to Information Act to have the results of this survey. Sadly the AMF denied the existence of this survey despite the fact that I had in my possession a letter from the previous president of the AMF, St-Gelais, confirming its existence. I was thoroughly disappointed by this lie of Me Benoit Longtin who is an officer of the AMF and also member of the Barreau of Quebec. I expect better respect of the laws from employees of the AMF and from lawyers. I was also informed that even if the AMF would acknowledge the existence of this survey, the AMF would not share its results with me on the basis they were considering such survey as being a new form of fraud investigation and therefore by law such investigations are strictly confidential. Imagine if police were investigating crimes trough surveys. Anyone with a brain can reach the conclusion that a survey cannot be deemed an official investigation of an infraction. Again I can only note the poor judgement of Benoit Longtin and his poor respect of the law.

It is ironical to state that in publishing this report, I am in fact breaking the law because the AMF through its chief of investigation, Helene Barabe, informed me that all the subjects covered by this report were under investigation and therefore I did not have the right to talk about the deficiencies I have found in the law. In publishing this report, I am committing an infraction but I believe that the Charter of rights and freedoms is the greater power and I will never surrender my rights and freedoms to the AMF. As I stated to a judge recently, laws and their deficiencies cannot be investigated. Laws and their deficiencies can be studied and analysed and they cannot be made confidential. Laws belongs to us the public and we have the right to discuss and criticize laws.

Whether you are a legislator, a regulator, a journalist or simply a consumer, I strongly advise that you read this report. It is a unique report and none has ever been written or will be ever

written to discuss the real problems facing the financial industry objectively from an insider and outsider perspective. I will analyze rigorously the deficiencies in the law through the commercial practices and norms of the industry. I will not only explain those simply in a language that can be understood, I will also be referencing materials written across the world in trying to determine if these problems have occurred in other countries and what were the solutions that were implemented. I will also be reviewing and discussing hundred of legal judgments to see how our judicial system has interpreted and addressed these deficiencies. You will be surprised how judges have different point of views to such an extent that we even have opposing decisions.

Finally when all of this information is analysed, I will used real and practical cases based on my 20+ years of financial industry experience to illustrate how these deficiencies have applied and how they are addressed in the real world.

In its response to the CCIR (Canadian Council of Insurance Regulators) in regards to all of the problems associated with the MGA Life Insurance distribution model with regulations not having been updated in the last 40 years, CHLIA representing the insurers stated:

*"Despite the absence of a clear and consistent description of how the channel operates, there is no evidence of systemic problems in the channel." CHLIA June 2010.*

It is clear that for insurers business as usual is very profitable. But tell this to the countless number of orphan policy owners who have lost their insurance and other benefits because of a model that discourages and even prevents policy owners from receiving service they pay for from licensed advisors. Claude Distasio representing CHLIA in response to questions regarding orphan policies demonstrates the bias of the insurers towards maintaining the status quo at any price, even at the price of the protection of the public.

*« As stated by Mne Di Stasio, insurers have demonstrated that they offer a service to customers where generally the client will never find himself between two chairs. Source : Conseiller.ca »*

This is the real problem which we are facing in the industry and which explains why insurance regulations are out of date by more than 40 years. Regulators believe every statement made by CHLIA and they simply refuse to hear the consumers.

## Distribution List

The goal is to publish this report with the greatest circulation possible. This report will be published in French and in English.

One of my objective through the use of the information contained in this report was to force the AMF to admit publicly that the insurers were violating the law. This has been done and the AMF because of my incessant work was forced to publish a Notice stating that in the case of orphan clients, the insurers were in violation of the Insurance Act.

http://www.lautorite.qc.ca/files//pdf/reglementation/distribution/avis/2013mai23-avis-clients-orphelins-fr.pdf

I am now in contact with all of the other provincial regulators and I intend to get the same results. For me this is important. This report is worth nothing; any actions or new regulations are worth nothing if insurers can ignore the laws like they have done in the past because regulators simply look the other way.

In disseminating this report, I will not have the help of journalists. For example in Quebec, news media's have too much to lose in terms of advertising money to confront the AMF or the insurers. After the behavior of Conseiller.ca, of its editor Yves Bonneau and journalist Sophie Stival, it is quite clear I cannot rely on the objectivity and integrity of the press. I had provided in an interview to Stival information and proofs showing that Sylvain Theberge of the AMF and Claude Distasio were misrepresenting the facts in regards to orphan policies even providing evidence of fraud in regards to Manulife strategy of increasing illegally lapse rate on orphan policies. Conseiller.ca censored that information.

This report will therefore be sent to the following list of people to break down the wall of secrecy:

1. All regulators in Canada
2. All Ministers of finance and justice for each province and federal government.
3. All elected representatives for each province and Parliament of Canada.
4. Different consumer protection groups
5. More than 1000 journalists in Canada
6. To all advisors in Canada and lawyers in Canada.

# INTRODUCTION

## Historic of the Insurance Industry

*To know where you are going, you ought to know where you've started and where you've been… (Richard Proteau)*

I always had a great pride in working in the insurance industry because I knew of its rich history and of its contributions to society. Insurance is the ultimate application of the principle of cooperation which created an enormous social capital until the time we as members were seduced by the siren' song of the speculators and allowed this social capital to be securitized through the demutualization of our insurance companies. Above all, the history of the insurance has shown us an important lesson. There is great profit to be made by cooperating. It is not always about competition. It is not always about me or you; it is not about this individual greed that we have mistaken with capitalism. Insurance has demonstrated what capitalism can accomplish by taking care of us, of our communities and of our societies. Finally insurance has proven that a collective approach to the question of risk and returns could promote the spirit of entrepreneurship while contributing to the dynamism and stability of the economy. It is not only a history worth remembering; it is a future worth fighting for.

The idea of insurance is an idea passed down as a torch from generations to generations; from societies to other societies. It is difficult to say where the concept of insurance started whether it be in ancient China or Babylonia. What we know is that the Babylonians codified the rules regarding insurance in the code of Hammurabi to facilitate commerce through the Mediterranean. Merchants were allowed to borrow money to finance the purchase of merchandises while paying an additional premium to the lenders. These lenders guaranteed that the amount borrowed would be cancelled if the merchandise was either stolen or destroyed.

It was the Greeks and the Romans who introduced life insurance in 600 AC. This insurance was offered through guilds and charitable societies. Members of these guilds or societies contributed to a general fund which was used to help members during time of extreme emergencies.

It was only in the 17th century that we see the emergence of insurance companies when a famous coffee shop was opened by Edward Lloyd in London becoming the place for merchants, ship-owners and underwriters to meet and discuss their marine insurance needs.

In Canada, our insurance industry dates from 1804 when the insurance company Phoenix opened an office in Montreal. Five years later a group of business man in Halifax created the Halifax Fire Insurance Association while the Quebec Fire insurance Company was established in 1819. The fire peril was the principal preoccupation of Canadians and there were more than 40 companies which were insuring that risk in 1905. Profits were excellent with total premiums taken of $14 million while only $6 million were paid in claims.

In 1865, Matthew Gault received a charter to create the Sun Insurance Company of Montreal which was followed by the creation of London Life in 1874 and Manufacturer Life Insurance Company in 1887.

In today's society and economy, the insurance business is divided along the line of the general insurance and life insurance which includes group and health insurance. The principal function of insurance is to transfer risk. The client who takes insurance pays a premium in exchange for the promise to be indemnified against an unlikely and uncertain event. By reducing uncertainty and volatility, insurance companies soften economic cycles and reduce the impact of crisis as much at the level of the individual than at the level of the aggregate of these individuals which is the society. Insurance is now a part of all financial transactions which take place in our economy and society whether it is for the buying and selling of merchandise, assets or services and for sectors such as transport and lending of capital.

**As mentioned by Haiss and Sümegi** *« Given the growing importance of the insurance sector and the increasing number of interlinks to other financial sectors, the evolving role of insurance companies vis-à-vis economic growth and stability should be of growing relevance for policy makers and supervisors. With regard to emerging and transition economies, the sequencing of reforms and the role of the insurance sector should also be a major concern in efforts towards catching up in economic growth and systemic stability »* **(The relationship of insurance and economic growth – A theorical and empirical analysis, Peter Haiss / Kjell Sümegi)**

While it is widely accepted that insurance increases productivity, an analysis made by Butler and Gardner (1998) demonstrated there may be an hidden cost associated with insurance resulting in a negative impact on productivity by proving that productivity is reduced for workers

who are insured because of a greater number of accidents for insured workers than uninsured workers. – A theorical and empirical analysis, Peter Haiss / Kjell Sümegi, **Paper for presentation at the 2006 EcoMod Conference, Hongkong, June 28-30, 2006)**

Until 1990, the model of organization of insurance companies across the world was under the form of mutual companies as we can see below with the number within parenthesis showing when the company demutualized.

| Rank | Company | Status |
|---|---|---|
| **U.S.** | | |
| 1 | Metropolitan | Mutual (98) * |
| 2 | Prudential | Mutual (98) * |
| 3 | Connecticut General | Stock |
| 4 | Principal Mutual | Mut. holding (98)** |
| 5 | Nationwide Life | Stock |
| 6 | New York Life | Mutual |
| 7 | Equitable Life | Stock (92) ** |
| 8 | Hartford Life | Stock |
| 9 | John Hancock | Mutual (98) * |
| 10 | Northwestern Mutual | Mutual |
| **Canada** | | |
| 1 | Sun Life | Mutual (98) * |
| 2 | Manulife Financial | Mutual (98) * |
| 3 | Laurentian | Stock (90) ** |
| 4 | Great West Life | Stock |
| 5 | Canada Life | Mutual (98) * |
| 6 | London Life | Stock |
| 7 | Mutual Life | Mutual (97) * |
| **U.K.** | | |
| 1 | Prudential | Stock |
| 2 | Standard Life | Mutual |
| 2 | National Mutual | Stock (95) |
| 4 | Norwich Union | Stock (97) ** |
| 5 | Legal & General | Stock |
| **Germany** | | |
| 1 | Allianz Leben | Stock |
| 2 | Hamburg Mannheimer | Stock |
| 3 | R+V Leben | Stock (89) ** |
| **Australia** | | |
| 1 | AMP | Stock (98) |
| 2 | National | Mutual Stock (95) |

Note: Source for this table is the Reorganization **of Financial Services and Life Insurance Demutualization — The View from Abroad** by Hironobu Murakami

**Historic: The Demutualisation**

*Was the demutualization the result of the expropriation of the capital by senior managers for their own benefits? Having lived through different demutualization, I have observed no proof or evidence of this. This expropriation came in fact much later, after demutualization, demonstrating that greed is like a seed. When it was watered by demutualization it was only a question of time before human nature followed its course. (Richard Proteau 2013)*

In the month of March 1999, the parliament of Canada adopted a piece of legislation referred to as Bill C-59 which allowed the big mutual life insurance companies to demutualize. This process allowed a company where the ownership resided with policyholders to become a company where the ownership resided with shareholders. While this is the accepted definition of a demutualization, there is a different point of view:

A partially different view is **taken by Griffiths (2004) who claims that** "*the origin of demutualization is when the cooperative has lost its cooperative identity and what distinguishes it from investor-oriented companies."* In other words he identified two stages of demutualization: a first-one in which cooperatives lose their values and the second one, characterized by the formal conversion into investor oriented enterprises. This view was shared also by the **ICA president of that time, Ivano Barberini, a former manager of the Italian consumer cooperation, who in 2007 claimed**: "*The economic value of cooperation is the result of the implementation of its social values for the benefit of members and of the community in which the cooperatives operate. Nevertheless, on occasion this has not been the case, and changes have taken a direction that is anything but the right one. In diverse parts of the world, certain major cooperative groups have favored the logic of pure financial gain and market dynamics, to the detriment of the characteristic identity of cooperation. In certain situations, decisions of this kind have led to the complete "demutualization" of cooperative enterprises.*"To sum up we can say that at least three kinds of definitions of demutualization has been used by scholars and practitioners: the first one focusing on ownership structure (Chaddad 2004 and Birchall 1998), the second taking into consideration the deviation from traditional cooperatives (Zvi Galor 2007) and the third one based on the coop values (Griffith 2004 and Barberini 2007). Source: **Demutualization and its Problems** Patrizia Battilani Harm G. Schröter »

If we believe in the definition of demutualization from Griffiths and Barberini, we can therefore say that the Caisses Populaires Desjardins have accomplished their first phase of demutualization by losing their cooperative values in favor of pure financial gains. By expanding geographically across Canada, the cooperative movement Desjardins has also demutualized geographically by diluting the implementation of the social values that has created this movement originating from the social values of the communities located across Quebec.

What are the motives which push the need for demutualization? The social factors are the neo liberalism, globalization and securitization of the economy. We have to add that the demutualization started in the United States under the guidance of the school of economists of Chicago who were able to install their agenda of privatization and deregulation in this country which then became the norm in the majority of countries across the world. Therefore when we speak of globalization we should instead be talking about Americanization.

What pushes an insurance company to demutualize? Many theories exist about this subject such as the organizational isomorphism, cultural changes, expropriation by senior managers and inefficiencies and lack of growth perspectives.

What I remember of my personal experiences since I have lived through demutualisation is that the motive was the size of the company and only the size was important. Bigger is better and the only option to protect Canadian insurance companies in this new global world and this is what was disseminated to the public. Size was measured principally through the share of the market controlled by the company. Since senior managers did not have the patience to organically grow the company, there was a need to consolidate the entire industry and the only way for the insurance companies to access the capital needed to increase their size through consolidation was to demutualize. Was this good for shareholders? We are starting to learn this was not the case because this consolidation became a war of egos with the best example of this being the war between the CEO of Maritime Life Bill Black and the CEO of Manulife, D'Alessandro.

What I can state is that the demutualization in Canada injected the capital necessary for the consolidation of the insurance industry permitting the newly demutualized companies to buy insurance companies in financial difficulties such as NN, Aetna, Colonia, Crown… at ridiculous prices. I called the unofficial first bailout in the Canadian insurance industry was paid by policy owners or the mutual companies. A question still unresolved is whether if this bailout was influenced by the Vanishing Premium class actions that were putting in peril the financial stability of these mutual companies.

As it was said by Julie Dickson OSFI, these companies in financial difficulties bought by the newly demutualized companies had one thing in common and this was a portfolio of insurance toxic products:

*« I have attended this conference on several occasions in the past and one that I remember particularly well was in November 2005. There was a session on the history of toxic products in Canada. A reinsurer provided all the gory details. He said that the first major Canadian insurance industry toxic product was "Term to 100", offered in the 1980s. This product was a great idea at the time, but the problem was that early years' premiums far exceeded expected claims, and later years premiums were far less than claims. The industry had assumed that lapses would be the same as with other products, and they were not – the educated guesses turned out to be horribly wrong and the consumer response was more sophisticated than expected. »* **Source : Julie Dickson Challenges in the Life Insurance Industry Remarks by Superintendent Julie Dickson Office of the Superintendent of Financial Institutions Canada (OSFI)to the 2010 Life Insurance Invitational Forum**

**As stated by the president Kathy Bardswick and CEO of the insurance company the Cooperators in 2006**: « "Mutuals grow to meet the need; stock companies need to grow to survive. »

Is this survival dependant in maintaining a state of perpetual regulatory status quo in the insurance industry which permits these demutualized companies to operate using commercial practices which should be considered fraudulent and which are considered fraudulent in other sectors of the financial industry? Is the ability of insurers to break the law while being protected by regulators linked to the existence of the toxic portfolio of products now under the management of these demutualized companies; principally to increase lapse rates? These are questions which we will attempt to answer in analysing the commercial practices of insurers and

the norms existing in the insurance industry to see how they conform to the various laws or Acts such as the Insurance Act of the various provinces and the Act pertaining the distribution of financial products and services in Quebec.

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**Case Study no.1**
**Bureau de décision et révision Case File 2012-048 Proteau v. Manuvie**

We were in February 2013 in the conference room of the Bureau de Décision et Revision; the administrative tribunal for the financial industry in Quebec. This was an audition pro-forma where we were supposed to establish the calendar regarding this trial against Manulife. However, the lawyer for Manulife had introduced a motion in inadmissibility arguing that I did not have the judicial interest to proceed with my complaint and that the Bureau, as an administrative tribunal, did not have the competency to judge in this matter.

I was requesting a series of orders against the Direct Channel of Manulife under article 115 of the Act respecting the distribution of financial products and services. Article 115 had been added recently in November 2012. My request and this trial were going to create important jurisprudence in the use of this article of the law.

*115. If it is brought to the knowledge of the Bureau de décision et de révision that a firm, any of its directors or officers, or a representative has, by an act or omission, contravened or aided in the contravention of a provision of this Act or the regulations, or that it is necessary in order to protect the public, the Bureau may, once the facts have been established, cancel, revoke or suspend the firm's or the representative's registration or certificate or subject it to restrictions or conditions. The Bureau may also, in all cases, impose an administrative penalty not exceeding $2,000,000 for each contravention.*

*For the purposes of the first paragraph, before making a request to the Bureau, an interested person within the meaning of section 93 of the Act respecting the Autorité des marchés financiers (chapter A-33.2) must notify the Authority and obtain confirmation from the Authority that it does not itself intend to make such a request. The Authority must inform the interested person in writing of its decision within 10 days after being notified.*

Reading carefully this article of the law we see it only applies to a firm or representative. The legislators have specifically excluded the insurance companies under the present article of this law in reference to the protection of the public. Why do insurers benefit of such protection? This is a mystery. Therefore if an insurer commits a fraudulent action against a customer or the public while distributing one of its products, the Bureau de décision et révision does not have the competency and the power to intervene even if the protection of the public is threatened. It can't stop an insurer from continuing with his fraudulent practice.

It seems therefore that my request and procedure presented to the Bureau could only fail to the pleasure of the lawyers representing Manulife. However this is not as simple. We first have to define the status of the Independent Channel of Manulife. Should we consider it a firm or is it simply an operation and department of Manulife like their client services department? Whether the Direct Channel of Manulife is a firm, should it be determined by whether it is registered as such with the AMF or be determined by the operations of the Direct Channel and by what it is doing? In other words, if the Direct Channel does exactly the same things as a firm and compete against other firms, should it not be considered a firm even if it is not registered? The fact that it is not registered is just another infraction committed by the Direct Channel. The

answer is positive. The Direct Channel is a firm and therefore Manulife as its owner is subject to the article 115 of the Act pertaining to the distribution of financial products and services.

**In other words, if it acts like a firm, do what a firm does and compete with other firms, then it is a firm.**

This was my defense and this is what I presented to the Bureau against the motion to dismiss from Manulife. It had quite an impact on the lawyers of Manulife. Also I had the distinct impression the judges of the Bureau thought the question of competency was going to be a simple one allowing them to dismiss my request very quickly. It seems I disappointed them.

This question surrounding the nature of the Direct Channel of Manulife forced me to re-evaluate my 5 years working in this channel as a Director of Sales and then as a Vice President and leader of this channel in Quebec.

We have seen the commentary of Barry Shemin in « Record volume 26 no 3 Session 130PD **US and Canadian demutualization – Postmortem ,** where he was saying they had eliminated their career branches by privatizing these branches or by merging them with other agencies. In other words we are talking about the privatization of a distribution channel. What is extremely interesting and what is not known by regulators is this privatization did not happen when Manulife decided to eliminate its branches. Manulife did not privatize its career branches deciding instead to eliminate them like they never existed. Manulife substituted to these career branches a Direct Channel whereby the career agent who was now considered an Independent agent was offered the choice of placing his business directly with Manulife through the Direct Channel. If the career agent did not select this option then he had to choose to deal through an intermediary; MGA (Managing General Agency). Truly instead of privatizing its career branches Manulife had decided to privatize its advisors. This created a lot of confusion and a lot of problems since there was no coordinated strategy or rules created within Manulife to deal with existing block of business and their service; blocks which were owned by branches and which had ceased to exist.

For example, what was supposed to happen for blocks of business existing with a branch and service by this branch because the advisor was deceased, retired or simply gone? This dead advisor could not sign a contract with the Direct Channel or transfer its block of business to a MGA. We now understand how orphan policies with a permanent status were created. These orphan policies were transferred unilaterally in the Direct Channel when this was illegal because the Direct Channel is not registered as a firm and cannot be responsible or owner of blocks of business.

The second problem was the greed of Manulife and its needs for profits at the expense of the clients. This is directly attributable to the demutualization. This is a greed which I have fought against for the 5 years I have worked at Manulife. Manulife was always stating the Direct Channel was not profitable and as a result critical staff positions needed to be cut. I always stated the opposite. The Direct Channel, which I considered by mistake as a firm, owned and was responsible for an enormous block of inforce business. Usually firms receive a yearly compensation of 3% of the amount of yearly premiums paid associated with their inforce block

of business for providing service. The Direct Channel did not receive anything. How could I be responsible for this block of business without any revenue; revenue needed to pay for the necessary human resources to ensure compliance on this inforce block of business? I could not be profitable and compliant. It was therefore not surprising that my audit of the Direct Channel revealed numerous infractions through illegal commercial practices.

This greed of Manulife had an impact on everyone. If an advisor decided not to deal with the Direct Channel, he had to transfer to the MGA channel. His block of inforce policies should have followed him by being transferred there. This was not happening. The MGA was refusing the transfer of this block because Manulife refused to pay the yearly compensation of 3% for servicing this block. The MGAs were right. Why would they take responsibility for these blocks of policies if there was no revenue associated with the blocks considering it would cost them money to service these blocks of business? Imagine how this was a great deal for Manulife. They were getting rid of their responsibilities for these blocks of business but kept the 3% revenue; taking it all as profit. The MGA were not stupid and their answers were simply: « No Way! We are not going to take your responsibilities and liabilities for free! »

This created therefore an enormous amount of blocks of business that were literally floating between channels with no one responsible to ensure compliance and service for these blocks of business. Continuity of service was irrevocably broken. It was only a matter of time before these floating blocks of business were forgotten to increase the number of permanent orphan policies.

Now imagine this whole process repeated each time Manulife was buying a company which had career branches and each time these branches were eliminated with all the blocks of business dumped in the Direct Channel. This strategy could only lead to a disaster. The inforce blocks of business, to ensure continuity of service, legally had to be transferred to another branch and the Direct Channel was not registered as a firm/branch. This disaster became a known fact following the lawsuit of an advisor against Manulife. **This advisor named Mr. Cormier of Drummondville launched a lawsuit against Manulife 500-17-058610-109 and started a process which ultimately forced the AMF to publish a Notice declaring the existence of orphan policies as being illegal.**

Manulife was successful in hiding its problems with orphan clients for a time because the Direct Channel and the only branch left named Services Financiers Manuvie Inc. was under the direction of the same individual who was Guy Couture. While all the other branches were eliminated and despite the fact the blocks of business were not transferred to Services Financiers Manuvie, since Guy Couture was both the leader of the branch and Direct Channel, you had the impression the orphan policies were in fact under Services Financiers Manuvie instead of the Direct Channel which was illegal.

But all bad things have an end when the truth comes out. This took place when the direction of the Direct Channel was taken over by Richard Clayman who came from the career side of the business and who believed the Direct Channel was the consolidated firm or super branch of all

Manulife business placed through the previous career distribution channel. He believed he was the guardian of the rich history of the career distribution of Manulife. The Direct Channel was for him the ultimate evolution of this channel. Therefore he believed he had the responsibility to supervise the advisors and their blocks of business. This change of leadership was repeated across Canada which was strange since the individuals concerned such as Richard Clayman did not believe in the wholesaler model proposed by Manulife where no one is responsible for anything except pushing sales up no matter the cost. It is not surprising that a few months later all the VPs such as Richard Clayman across Canada were fired as they were consider dinosaurs creating a tremendous loss of corporate memory. Sometimes such a loss is necessary when you want to cheat.

This is how Richard Clayman recruited me and this explains why I believe the Direct Channel was a firm which is not true as it is not registered while however doing and engaging in the activities of a firm.

A big problem for Manulife was that the only remaining firm was still under the name of Guy Couture when Richard Clayman took the leadership of the Direct Channel. It was now evident the Direct Channel was acting like a firm and this was the state of the channel I was faced with when I took over. I did not believe in the wholesaler model and for me the Direct Channel was a firm and therefore I was responsible to ensure all of the operations of the Direct Channel were compliant with the Act pertaining to the distribution of financial products and service like any other firms. I therefore proceeded in tackling the orphan problems to ensure that for once and for all this illegal practice was resolved while at the same time exposing the fact there was something even more sinister behind the problem of orphan policies. **I discovered that Manulife had removed the name of advisors from policies artificially creating orphan policies. I discovered this on lapse notices found in the garbage because there was no agent assigned to these policies because their names had been removed.**

This case study generates a lot of question which we will try to understand and answer as we analyse the laws and how they are applied.

1. Why is the Act pertaining to the distribution of financial products and services exclude the insurers when these insurers are actively and directly involved in the distribution of financial products and services? This does not protect the public and results in illegal commercial practices by insurers such as the orphan policies. We will also see the implications in terms of compliance since this exclusion allows insurers not to report infractions committed by advisors if this looks bad for the insurance company. This is instead dealt internally without being reported to the regulator.
2. Should advisors have the right to sign contracts directly with the insurer without having to pass through a firm to distribute financial products and services? Who will be supervising the advisors? The insurers have demonstrated they are not interested in supervising advisors. To answer this question we should look at what is done in another sector of the financial industry. In the mutual fund industry, the investment advisor is not able to contract directly with the mutual fund company. The investment advisor must go

through a dealer and only one dealer. The law forces the dealer to be responsible for the supervision of his representatives. If a mutual company or insurance company wants to actively and directly be involved in the distribution of its products, it must create a dealer which Manulife has done with Manulife Investments which is a company separate from Manulife with its own CEO. What holds true for this industry should hold true for the insurance industry.

3. Finally it is interesting to note that the greatest frauds have been committed in Canada when the line separating the manufacturer from the distributor has become blurred. This is what happened with Norbourg. There is no advantage for the public to permit insurance companies to contract directly Independent Advisors to distribute their products. These advisors are independent and they should be dealing at arms length with the insurance company and therefore through a MGA. If an insurance company wants to deal directly with advisors it should create its own MGA or start a career agency. Companies such as Manulife have been allowed to be directly involved in the distribution while being able to operate outside the Act pertaining to the distribution because they are excluded from this Act. This directly contributed to the creation of the permanent status for orphan policies. Policy owners who were orphaned have lost benefits and insurance coverage as a result of this. This has to be stopped.

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# Section 1 – Insurance Intermediaries

## Section 1.0 Agent, Broker, Advisor, Representative…

The agent, broker or advisor regardless of how you want to call him is the brick while licensing is the mortar use to build the foundation of the financial industry. How this brick and mortar are put together will ultimately be dependent on the type of distribution that will be used to bring a financial product to the market. To understand distribution we must therefore have a look at the brick and mortar of the financial industry.

As a starting point to this study, we will use a paper published by the **Canadian Council of Insurance Regulators (CCIR), entitled "MGA Life Insurance Distribution Model".** This document was produced because those responsible for the insurance industry have finally realized that without updates to insurance laws and regulations for 40 years, we are now facing some serious problems. CCIR in its introduction begins with:

*« The move in the life insurance industry from a Career Agency distribution model to a Managing General Agency distribution model may have created a number of risks to consumers and gaps in regulatory regimes. »*

It is important to understand that at the very beginning of the insurance industry, the distribution of insurance was done solely through agents who worked for one insurer and from branches operated by that insurer. It was therefore clear that all the actions of the agent were the actions of the insurer even if the agent acted outside of the scope of his authority. This takes its source from Common Law which includes Agency Law, Tort Law and Statute Law.

Agency law governs the agency relationship between an insurer and an insurance representative, regardless of the fact that the insurance representative may act on behalf of

more than one insurer, through one or various MGAs. Agency is a relationship in which one person is authorized to represent and act for another person. In the field of insurance, the "principal" is usually the insurance company and the "agent" is the representative. There are a number of court decisions under agency law that clearly set out the circumstances when an insurer is responsible to the policyholder. Similarly, there have also been court decisions under common law that clearly set out the circumstances when a representative is responsible to the policyholder (e.g. advice giving, recommendation of a product).

Tort law deals with legal liability issues usually involving damages for negligence. Under tort law, there are a number of court decisions which clearly set out the circumstances when an insurance company has been found negligent in fulfilling its contractual obligations to the policyholder (e.g. unfair denial of a claim). Similarly, there are a number of court decisions which clearly set out the circumstances when a representative may be found negligent in its responsibilities to his/her client (e.g. providing unsuitable advice, putting their interest ahead of the client's interest).

Finally, there is statute law which varies in jurisdictions across Canada and focuses on regulating the market conduct of insurance representatives and insurers. Under statute law, insurance representatives must meet certain criteria before they are issued a license to sell insurance.

As we have stated, these agents worked from insurance branches operated by the insurer. The roles of these branches and its employees were to recruit and form new agents and manage/supervise existing agents. For a long time, these agents were considered to be employees of the insurer and therefore represented themselves to prospective and existing clients under the name of the insurer. This changed when legislation was introduced allowing agents to act as independent entrepreneurs. This did not change the existing agency relationship contrary to what was stated by insurers. It only provided financial independence to the agent. This change affected branches allowing existing agents to work outside of their branch by running and paying for their own operations while claiming the cost involved with this. The agent still operated under the name of the insurer and the ownership of the block of business still belonged to the insurer. As we shall see, this identity of an independent entrepreneur would come into conflict with the definition of the concept of an independent advisor/contractor because insurers promoted the use of the word independent to convince the public they were offering independent advice through these newly independent entrepreneurs which was far from the truth.

The term « career/exclusive agent » started to appear when certain insurers started to give agents their autonomy beyond simple financial independence and this is what started the privatization of the distribution of insurance and the emergence of the MGA as the independent intermediary between the now independent advisor and insurer (becoming a manufacturer of products only) The career/exclusive agents are those who kept the right to operate under the name of the insurer. But the law had not changed and still has not changed. Under the law all these advisors/representatives were and are still agents of the insurers with various degrees of independence; **an independence which was therefore not a right but a privilege conferred by the sponsoring insurer to the advisor to operate and sell financial products under his name and sell products of other insurers. As for any privileges, it is not freely given and it certainly can be easily taken away…** Again it is important to repeat that aside from Quebec, this privatization was not recognized in the legislation which did not change. The origin of this privatization is summarized by CAILBA : (please note the wrong choice of word. "Life Insurance

brokerage" should be replaced with "Life insurance independent agencies activity". We will see why later.)

« *The origins of Life Insurance brokerage activity in Canada go back to the early 1970's with both Maritime Life and Aetna Life. The actual emergence of the MGA Life brokerage distribution system began approximately 30 years ago but has gained far more prominence since the latter part of the 1990's. Prior to that evolution, the distribution of Life Insurance and related products had been dominated by the 'career' system, wherein Insurers each had their own captive sales organizations.In the late 1990's many of the major Insurers (Canada Life, Sun Life, Standard Life, Manulife, Aetna, and Prudential (among others) began to dismantle these expensive career branch systems in favor of contractual arrangements with Life Brokerage firms, which became known as Managing General Agencies or MGA's. The advantages of product distribution utilizing MGA's were (1) far less capital intense, (2) allowed Carriers to eliminate a number of fixed costs (premises, staff etc) and replace those costs with a variable cost structure more closely tied to production and (3) the opportunity to expand product distribution through a broader range of Life sales organizations, leaving today companies like London Life, Great West Life, Sun Life (acquired Clarica) maintaining their career branch systems.*
*These processes were slow to evolve. In many cases the career Branch Managers, who were managers for the career Insurers, became the entrepreneurs who created MGA's to provide a 'home' for the Advisors who had become disenfranchised by their respective companies.* »

While the insurers were moving forward, the regulators maintained the regulatory status quo by not modifying the laws to reflect these changes. In legal terms, the term « independent » « broker » and « MGA » were often not defined. Legally the advisors remained an agent of the insurer despite their independence. If the advisors were allowed to transact with other insurers this was not the result of a legal right. This was truly a privilege conferred and sponsored by an insurer. **Contrary to what is stated by CAILBA, this privatization was not a change to a brokerage activity. It was a change from tied agents to multi-tied agents.**

***Note: As we shall see in common law provinces, the right to deal with other insurers is a contractual granted right and therefore an acquired right. In Quebec, it is the reverse. The right of dealing with many insurers is a "natural and statutory right" which can be limited contractually.***

This regulatory situation is quite bizarre and it is therefore not surprising that the public is confused by this situation and relationship. Using an analogy, it is like slavery had not been abolished by an act of law but instead, it is the owners of the slaves that have decided to give their slaves the privilege of freedom. However under the law they would still be slaves. I am certain that for these slaves this would not be enough. Freedom is a right and not a privilege. This is exactly how it is perceived by advisors who have decided to become independent. They believe it is their right and not their privilege and this is how they represent themselves to the public as being fully independent. Legally however this is not the case. What is however surprising is there is still little opposition to the insurer sponsorship requirement by advisors who consider themselves to be independent.

Only Quebec separated itself from insurer sponsorship of agents by introducing the Law pertaining to the distribution of products and financial services. Under this law which is rooted in the Civil Code of Quebec, the agent in insurance does not exist. There are only representatives and these representatives can either be attached to a firm and therefore acting for this firm or they are independent as we see here:

*3. A representative in insurance of persons is a natural person who offers individual insurance products in insurance of persons or individual annuities from one or more insurers directly to the public, to a firm, to an independent representative or to an independent partnership.*

*A representative in insurance of persons acts as an advisor in the field of individual insurance of persons and is authorized to secure the adhesion of a person in respect of a group insurance or group annuity contract.*

*14. No representative may pursue activities as a representative unless the representative is acting for a firm, is registered as an independent representative or is a partner in or employee of only one independent partnership.*

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**Case Study no 2: Can an agent become independent?**
**Pierre Latreille against Industrielle Alliance 200-06-000001-977**

I was sitting with other Manulife executives in what we could name the sitting version of the O.K. Corral. The hostilities were opened and I was the only one who was opposing changes that Manulife wanted to introduce in the Direct Channel resulting in the laying off of most of my staff. In the defense of my staff, I stated that I needed all of them in order to meet our legal responsibility associated with the servicing of our inforce block of business. One executive looked at me dismissing my claim: “In the Direct Channel we are not responsible for the service given to the clients by our advisors. They are independent advisors and this is their responsibility and not ours…”

“Not entirely true,” I answered with a weak smile. “Independent (multi-tied) business only makes maybe 30% to 40% of our total inforce block of business. The rest falls under a tied agency relationship where we are responsible ultimately for the delivery of service because when the policies were sold our advisors were captive and therefore full agents and even employees of Manulife or of the companies we bought.”

Everyone laughed at the table assuming I had missed something so obvious. “All of these past agents have signed new contracts a long time ago which make them independent advisors” said one of the executive.

“True but did we notify the clients of this change in the contracting of our advisor? Have they been informed?” There was silence around the table. “Well, then it means that from the point of view of these clients, the advisors still have the apparent authority to act as agents and since they are apparent agents, then we apparently have the responsibility for the service they are providing.”

This time there was no laughter. “This happened a long time ago anyway. No worries… Prescription would apply.”

“This is not my opinion,” I stated. “In fact, prescription has not even started because still today clients are unaware of this change and what it means.” Can you hear the sound of a fly buzzing in a room? Well on that day you could. Was I right or wrong in my assessment?

The Latreille case provides us with a reference as to the contractual difference between a representative/employee and an agent while defining the term « service » in relation to sales. At

first Latreille was an employed representative of Industrial Alliance and his powers and responsibilities were defined by his employment contract:

**2 – Powers and Responsibilities of the representative**
**The company authorizes the representative to solicit and obtain applications and requests for the kind of contract and financial services offered directly by the Company or through another company with which the Company has signed a distribution agreement. The representative commits to give to the insured and clients the service to which they are entitled to. The representative commits to work exclusively for the Company and to this end , will transmit to the Company any applications for insurance or annuity obtained by him and also any other requests for any other contracts for financial services offered by the Company or through another company with which the Company has signed a distribution agreement. The representative is attached to a branch in the exercises of his function.**

As stated by the judge, Pierre Latreille is an employed representative of Industrial Alliance with his salary paid through commissions. The Industrielle contract is conformed to the law as there are not agents in Quebec – only representatives.

In 1993, he signs a new contract which gives his financial independence of an independent entrepreneur.

**2. Powers and responsibilities of the agent**
**a) The company authorizes the agent to solicit or to obtain applications or request for other different contracts and financial services that the Company offers or through another company with which the Company signed a distribution agreement. The agent will engage to provide to the insured and clients a service with quality in conformity with the rules of ethic for his profession.**

I would have to state that the contract is not clear. The contract is not conformed to the law. An agent does not exist in Quebec. So what is Latreille? The contract gives Latreille his financial autonomy but the attachment provision has disappeared. If Latreille is not attached then he would have to be an independent representative. However knowing about the distribution of Industrielle, I know this is not the case, since representatives of Industrielle represent themselves under the name Industrielle. Therefore they would be attached to Industrielle.

Latreille is not happy with his agent contract because he wants to offer other products from other insurers while owning his clients. He decides to leave Industrielle to become a broker which is not defined under Quebec law. What he wanted really was to be an unrestricted independent representative. With the confusion with the use of different terms, it is difficult to ascertain this.

As we can see here, even for the experts the terms representative, brokers, advisor, agent mean different things; meanings that often changes depending of the legal context such as contractual law or statute law. It varies by provinces. It has therefore become very difficult for consumers to understand and determine the authority that a representative has in relation to the regulatory and contractual relationship with the insurer

Finally it is important to note that when Latreille stopped servicing his clients, Industrielle assigned the block to another agent. Judge Lacroix stated clearly that service is the accessory to the sale. If there is no service, there is no sale. As a result, Industrielle had the obligation to

take over the service in designing a new agent or by doing the service itself through an employee such as a Sales Director. This raises the question whether such employees should be licensed. Some provinces such as Nova Scotia permit employees to act as agent of the insurer without a license:

*(3) A member or representative of an insurer licensed pursuant to Section 6 to carry on the business of insurance in the Province, who does not receive a commission and who acts only in the name of and on behalf of the insurer may, without a license, act as an agent for the insurer*

**Based on this information, I was right in stating to Manulife that the service of the inforce block of business under their Direct Channel was inseparable from the sale of the product…We were responsible for the service.**

**Question:**

**(1) Insurers use agent/representative contract that are the same across all of Canada. However provincial legislations vary greatly. Should regulators require insurers to provide agent/representative a contract that is compliant with the legislation and legal terms used where the contract is signed?**

**(2) Should all marketing materials, reports and others be also compliant?**

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## Section 1.1 Agent and Broker Under Common Law

Again as a starting point to define what is an agent under common law we will refer to the paper published by the Canadian Council of Insurance Regulators (CCIR), entitled "MGA Life Insurance Distribution Model despite the fact that part of the definition is false ::

*« Although the definitions of "agent" and "broker" differ somewhat from province to province, generally speaking, a life insurance agent is a licensed individual who has a contract to place insurance with at least one insurer. In common law jurisdictions, life insurance representatives care considered "agents" of the insurer, whereby the insurer is obligated to uphold the agreements made by the agent with a third party. In life insurance, a broker is an agent with contracts with a number of insurers. Generally they consider themselves independent of the insurers, but, for life insurance, the agency relationship still holds in common law »*

In fact I do not agree with the last part of this statement. Most common law jurisdictions exclude the use of the term broker in the life insurance industry as we see here when we look at the Insurance Act for Nova Scotia. Also this statement conflicts with the definition of a broker for commercial insurance and conflicts with the definition of a broker accepted around the world. Using the expression multi-tied agents would be more accurate preserving the strength of the agency relationship that exists between insurers and agents even if they have contracts with many insurers. Using the term broker dilutes the strength of this agency relationship; a concept not accepted by the Courts.

***Nova Scotia Insurance Act***
*(5) A license for any class of insurance other than life insurance entitles the agent to act as a broker.*

So it is pretty clear that for life insurance, an agent cannot act as a broker in some provinces. There are only insurance agents. In fact, in Nova Scotia, if you are a life insurance agent and

representing yourself as a broker you would be breaking the law as you cannot and are not licensed to act as a broker. Any life insurance company that make its agents sign a broker contract would be considered as inciting someone to break the law. How can the agent represent multiple companies? It is the sponsoring insurer that allows the agent to place business with another company.

In Quebec, a broker does not exist and you only have representatives in insurance that are attached or independent. All representatives have the statutory right to represent many insurers unless they sign a contract with an insurer which would limit this right. Under the Civil Code, the representative act under mandate of an insurer.

**Question: Should there be two types of licenses in Quebec. One restricted license for representatives who have accepted to be limited in their right to represent many insurers and a license for regular representatives?**

In Ontario the regulatory situation is quite puzzling. Under the law, an agent is anyone who solicits insurance and who is not a member of the Registered Insurance Brokers of Ontario.

***Ontario Insurance Act***
*"agent" means a person who, for compensation, commission or any other thing of value,*
*(a) solicits insurance on behalf of an insurer who has appointed the person to act as the agent of such insurer or on behalf of the Facility Association under the Compulsory Automobile Insurance Act, or*
*(b) solicits insurance on behalf of an insurer or transmits, for a person other than himself, herself or itself, an application for, or a policy of insurance to or from such insurer, or offers or assumes to act in the negotiation of such insurance or in negotiating its continuance or renewal with such insurer,*
*and who is not a member of the Registered Insurance Brokers of Ontario; ("agent")*

The Ontario Insurance Act gives you the impression that a life agent can be a broker in this province which is not the case when we consult the Registered Insurance Brokers Act.
The term broker is defined under the meaning of the Registered Insurance Brokers Act. Under the Registered Insurance Brokers Act we find that a broker is:

**Registered Insurance Brokers Act**
*"insurance broker" means any person who for any compensation, commission or other thing of value, with respect to persons or property in Ontario, deals directly with the public and,*
*(a) acts or aids in any manner in soliciting, negotiating or procuring the making of any contract of insurance or reinsurance whether or not the person has agreements with insurers allowing the person to bind coverage and countersign insurance documents on behalf of insurers,*
*(b) provides risk management services including claims assistance where required,*
*(c) provides consulting or advisory services with respect to insurance or reinsurance, or*
*(d) holds himself, herself or itself out as an insurance consultant or examines, appraises, reviews or evaluates any insurance policy, plan or program or makes recommendations or gives advice with regard to any of the above; ("courtier d'assurances")*

Again for someone that is not attentive, the definition of insurance broker in this Act let you believe that a life insurance agent can be an insurance broker. However this perception changes when you look at the definition of « insurance » in the term « insurance broker ».

**Registered Insurance Brokers Act**

*"insurance" has the same meaning as in the Insurance Act, but does not include life insurance as defined under that Act; ("assurance")*

As a result an insurance broker does not include life insurance. However in Ontario it is amazing the number of agents in life insurance that hold themselves as insurance broker and firms that advertise using insurance brokers for life insurance.

## Case Study 3: Bravia Life – When market practices have evolved beyond statute laws…

Here we are using the example of Bravia Life for no particular reasons – just because it comes on the first page of a google search on life insurance brokers. Here is what their web site states:

***ABOUT BRAVIA LIFE***

*At Bravia Life, we're committed to helping Ontario families prepare for the future. Our trustworthy Ontario life insurance specialists can help you achieve financial protection with reliable, secure, and affordable insurance planning and policy structuring that works for you.*

*Bravia Life specializes in Ontario life insurance, disability and critical illness policies from $10,000 to $25,000,000. As a reputable insurance broker for over 15 of Canada's largest insurance companies, we have direct access to Certified Management Accountants (CMA), Chartered Life Underwriters (CLU) Certified Financial Planners (CFP) and Registered Trust and Estate Practitioners (TEP) for professional tax and estate planning, as well as setting up reliable personal, business and corporate owned policies.*

The site specifically states like many other sites that they are an insurance broker for life companies. How can this be when the statute says you can? Is it therefore surprising to see that the consumer cannot make head or tail of who is dealing with?

**Registered Insurance Brokers Act**
*3. (1) No person shall hold himself, herself or itself out as an insurance broker or as the holder of a certificate under this Act unless the person is the holder of a certificate under this Act.*

One possible reason is that the Act is very badly written. Basically a life insurance agent cannot be an insurance broker. However since life insurance is excluded from the term insurance, he can basically hold himself as an insurance broker without committing an infraction despite the fact he can't be an insurance broker. This can give a real head ache...

This is the answer provided by FSCO:

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Dear Mrs McNamara-Mucha,

Usually I don't give second chances.I will be nice this time and remind you that the report I am working on will be circulated accross Canada. It will be personally delivered to every MP of every provincial legislature, federal MP, senators...

Do you truly want to proceed with this answer. I will help you out. There are no two distributions systems. There are 2 Acts enacted by Ontario legislature. One Act is the Insurance Act and the other is the Registered Insurance Brokers Act. Also, the web site of Bravia does not use broker in its corporate name.

It says it is an insurance brokers and therefore using a term defined and protected under the Brokers Act. So if I try to understand your logic, you mean i could use the term insurance broker in Ontario and hold myself as an insurance broker because because i don't work in the property and casualty insurance since your are saying the Brokers Act only apply to those who work in property and casualty...or

the correct legal wording that Bravia shoud have employed is: as a reputable agent representing *over 15 of Canada's largest insurance companies'*

Under the law Bravia is an agent and not a broker and therefore is making a misrepresentation and breaking the law.

Again is that truly the answer you want to provide? And finally I find it ironic that you refer me to a paper written by regulators on MGAs which basically states that the notion or the existence of MGAs have not been recognized under the law of most common law provinces and 40 years later regulators are trying to address this regulatory gap. I am well aware to this paper...

The public don't know who they are dealing with. Insurer contract don't match the law. Marketing materials don't match the law and now it seems the regulators don't know the law; i hope not.No wonder why the consumer is lost...

Regards

Richard Proteau
----- Original Message -----
**From:** Karen McNamara-Mucha
**To:** 'rproteau@consumerights.ca'
**Sent:** Tuesday, September 09, 2014 12:17 PM
**Subject:** question regarding regulations

Dear Mr. Proteau:

Your email below has been referred to the Market Risk Assessment Unit for a response.

Please note that there is nothing prohibiting life insurance agencies from using the term "broker" in their corporate name. Essentially, there are two distribution systems, one for property and casualty (RIBO brokers regulated under the RIBO Act), and the other for life and accident & sickness.

As information, I am attaching a copy of the May 2012 position paper from the Canadian Council of Insurance Regulators entitled "The Managing General Agencies (MGA's) Distribution Channel in the Life Insurance Industry", which you may find useful.

Regards,

Karen McNamara-Mucha
Compliance Officer

**From:** Richard Proteau [mailto:rproteau@consumerights.ca]
**Sent:** September-07-14 2:04 PM
**To:** Contact Centre
**Subject:** question regarding regulations

The Financial Services Consumer Alliance, an alliance of consumers working to improve consumer protection in the financial industy is working on a report regarding the commercial practices currently existing in the insurance industry.

We are currently reseaching and analysing current legislation and statutes of each individual provinces.

It is our interpretation that under the Register Broker Act, no one can hold himself to be an insurance broker and a life insurance agent cannot be an insurance broker. However we see that in Ontario a lot of life agents holding themselves as insurance broker.

Is our interpretation wrong?

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Under the Alberta Insurance Act, the plot thickens. The term agent is defined with the term broker and independent contractor. Basically anyone licensed acts as an agent but can enter into an agency relationship as an employee or under his own name as an independent contractor. The agent can represent himself also as a broker if he is has multiple agency contracts. **It is interesting to note that Alberta in recognizing that a life insurance agent can act as a broker, it has introduced a provision against the presumption of agency where the agent cannot be considered the agent of the insured to his detriment.**

As a result, the insurer would not be able to argue in Court that coverage be denied because the broker was the agent of the insured when he relayed inaccurate information to the insurer.

**Alberta Insurance Act**
*(c) "agency contract" means a contract between an insurance agent and an insurer in which the insurance agent agrees to act as an insurance agent in respect of insurance issued by the insurer, but does not include …*
*(bb) "insurance agent" means a person who, for compensation, (i) solicits insurance on behalf of an insurer, insured or potential insured, (ii) transmits an application for insurance from an insured or potential insured to an insurer, (iii) transmits a policy of insurance from an insurer to an insured, (iv) negotiates or offers to negotiate insurance on behalf of an insurer, insured or potential insured or the continuance or renewal of insurance on behalf of an insurer or insured, or (v) enrolls individuals in prescribed contracts of group insurance,*
*(e) "independent contractor" means an individual who enters into a contract in the individual's own name to provide services as an independent contractor;*
*(2) Every individual that holds an insurance agent's certificate of authority for life insurance must (a) be an employee or an independent contractor of a business that holds an insurance agent's certificate of authority for life insurance and be recommended by the licensed life company that recommended the business receive its certificate of authority, or (b) be an employee of a licensed life company and be recommended by the company.*
*Insurance broker*

*488 No insurance agent may purport to be an insurance broker unless (a) the insurance agent is a party to 2 or more subsisting agency contracts with different insurers, and (b) none of the agency contracts requires the insurance agent to deal only with insurance offered by one insurer.*

Truly, it seems that the concept of uniformity behind the Uniform Insurance Act fell between the cracks at one point in time and this means we are faced with a lot of term conflicts between provincial laws, insurance contracts and commercial practices actually existing in the insurance industry. Also provincial laws are in opposition with laws and definitions used around the world which is not every effective since we operate in an integrated global economy. Provinces also ignore the rich history of how brokers emerged in the marketplace and how the definition of a broker is not linked to multiple contracts but is instead linked to independence and acting for the client.

Since there are so many variations of these terms, it is impossible for consumers to understand who they are dealing with and what is the authority of the agent or representative he is dealing with. Sadly this situation becomes even more complex when we link licensing and contracting with the insurer as we shall see in the case study below.

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## Case Study no 4: What authority and responsibility an agent and its principal have?

### Lafreniere against Transamerica 500-05-065871-012
### Mignault against GWL CI 06-01-48403

In Mignault versus GWL, the judge Keyser refers to the following excerpt to define what is an agent and the agency relationship that exists in this affair. It is far from being this simple. There are many things wrong with the definition and terms employed here.

*Principal and Agent*
*65 The relationship of principal and agent exists where a person or entity (the principal) empowers another (the agent) to act on its behalf in such a way as to affect its legal relationship with third parties. Agency relationships generally, but not always, arise out of a contract. Agents can be either employees or independent contractors. The general rule is that, regardless of whether the agent is an employee or an independent contractor (Fridman, The Law of Agency)*

The problem is that contractually there are enormous contractual differences in any existing agency relationships. I like to categorize agency relationship in two separate groupings.

There are agents who operate under the name of their principal usually an insurer (London Life,Clarica...). These agents can be employees or independent entrepreneurs. As a result, since the agent operates under the name of the principal, he represents the principal in all contractual things. This agent is exclusive to the principal and can only offers products of the principal or products of other companies contracted through the principal. As a result, most often these agents are also multi-tied agents (brokers in Canada) because they can offer the products of other insurers if their principal has signed an agreement permitting this. **They are not however Independent Brokers and they should refrain from using this term.** Finally the clients are owned by the principal. Usually the contract signed by these agents will include non-compete clauses and buy-out clauses.

The other type of agent operates under his own name and therefore the agency relationship is limited to the scope of his contractual authority such as taking an application. The advice he provides is not the responsibility of the primary principal (insurer). He is independent in that regards. He is not exclusive to anyone and can contract with as many different insurers as he wishes and in any legal ways he wishes. This type of agent is never an employee. He is always an independent entrepreneur owning his own business. As an independent entrepreneur, he can operate his business under sole ownership (under his own name) or he can incorporate a business as a separate entity. If he incorporates, the corporation will become the firm and he will attach himself to this firm where usually he will be both the agent and principal of this firm. So the advisor in this case will become a full agent of his firm (placing business under the name of the firm) with the firm becoming the independent contractor having signed a contract with the insurer. The advisor is contracted by adding him to the contract signed between the firm and insurer by annexing the contract (Annex A) and adding his name to this Annex A. It is important to state that through this Annex, the corporation can add to the contract other advisors who will become agents of the corporation. If this is the case, the corporation will have to sign a contract with the insurer that specifies the title or ownership of the business/clients submitted by the agents attach in Annex A (corp and title contract or corp and non title contract). As we can see this becomes very complicated and very much impossible for the consumer to know who is responsible for him. Luckily unless it has changed, insurers do not allow corporations to be annexed to these contracts (corp. on corp. contract).

For independent contractors or representatives, the ownership of the clients is often not clear and very ambiguous depending on the contract signed. Who owns and who is responsible for what is difficult to define and certainly impossible for the consumer. The service is shared by the principal/agent and even by any other intermediaries used such as a MGA. What I can state is that defining who owns what and who is responsible can become a legal nightmare. This will be further discussed in a different case study…

At the core of Mignault versus GWL was the determination about whether Palmer was fully an agent of GWL or was a representative with limited agent authority as stated here

***[8] The position of the plaintiffs is that at all times Palmer was acting as an agent for GWL and that they are, therefore, responsible for his actions. The position of the GWL is that Palmer was an independent contractor for them and was the agent for the Mignaults in all of their dealings with them. They say that if they are wrong in that position, that Palmer was, in any event, acting outside any actual or apparent authority.***

What is apparent and actual authority?

*Principal and Agent*
*65 …principals are vicariously liable for the wrongful acts of their agents committed within the scope of their actual or apparent authority. When deciding if vicarious liability has arisen, then, the relevant consideration is whether the agent had "actual" or "apparent" authority to undertake the wrongful act. The Law of Torts, 3d ed., Irwin Law 2007, Philip Osborne at 344 and 352.*

*Actual Authority*
*There are two types of actual authority - express or implied. Express actual authority arises where an agent has been expressly authorized to act on behalf of a principal. This type of authority is often conferred in a formal document. Implied actual authority, on the other hand, covers the reasonable and necessary activities undertaken by the agent in pursuit of his or her*

*express actual authority (Peter Birks, ed., English Private Law, vol. II (New York: Oxford University Press, 2000) at pp. 182 - 186).*
*Apparent Authority*

*Apparent authority (also called ostensible authority) exists where the words or conduct of the principal would lead a reasonable person to believe that the agent was authorized to act, notwithstanding the fact that the principal and ostensible agent had never discussed such authority. The doctrine applies regardless of whether the agent is acting in fraud of the principal, but is negated where the third party is aware of this fraud (Birks, supra at p. 185; Atiyah, supra, at pp. 234-235). Professor Atiyah, describes apparent authority "as a form of estoppel by representation" with the essential ingredient "that the servant is known by the third party to be such, and to be acting or purporting to act on behalf of his master"*

What arguments did Judge Keyser use to define the authority of Palmer and the responsibility of GWL? The judge use the fact that:

(1) The clients Mignault were never informed of the form and substance of the contract signed by Palmer with GWL

***Note: The nature of the contracts signed between agent and insurer is believed to be an internal matter in the industry and therefore not included in the disclosure to the client. Clearly the judge believes the industry is wrong in its assumption.***

(2) In all of its outgoing communications to Mignault, GWL used the term agent while the term independent contractor was used in the contract between Palmer and GWL
(3) From 1991 to 1996, Palmer had signed an agent contract with GWL which stated that he was an agent but acted as an independent ***contractor "1. DUTIES. You shall solicit as an independent contractor, applications for life and disability income insurance and annuities."***
(4) He was housed at GWL between 1991 and 1996.
(5) This agent/independent contract was cancelled in 1996, and then he signed a broker contract stating that he was an independent contractor with GWL. So what is the change in the contractual authority of Palmer? There are no changes. It is the same authority. The only thing under provincial law that a broker contract could change is to clearly establish that by this contract Palmer is not restricted in his solicitation to represent GWL but he can represent other companies. Clearly GWL thought by using the term broker it made Palmer independent from GWL which went against provincial legislation. GWL tried to use the term broker to change the nature of an agent authority when under the law; the term broker only applies to the number of companies an agent can sell. This created a lot of confusion and the judge had to interpret the contract outside of its terms as defined by the law.

As we can see there are a lot of conflicts with the contractual terms used by GWL with statute law. It is therefore not surprising that the Mignault were confused about the authority of Palmer believing he was acting on behalf of GWL. The judge therefore had to interpret the authority of Palmer based on the narrow view that the Mignault possessed of the status and authority of Palmer with GWL.

Coming back to Manulife and its Direct Channel, this proves my position was correct. First as per the Mignault case, it is the responsibility of the insurer to inform the client of the authority of their agents and to inform them of any changes to this authority. If this is not done, then this authority would be interpreted from the viewpoint of the clients. As a result, even if the agents of

Manulife became independent, they still had their original apparent authority which meant that Manulife was vicariously liable for their actions in regards to the service provided on the inforce blocks of business.

In Lafreniere versus Transamerica, the judge framed this responsibility of the insurer for those who act at the same time as agent and independent representative/contractors. In this case, Lafreniere sought to have his policies paid up on the basis of the representations that were made to him by his advisor. Transamerica denied its responsibility on the basis that the agent was not a representative of the company and therefore his representations to the client were not authorized.

Again we notice the use of the wrong terms. Transamerica was wrong to say this because in Quebec all of those selling insurance are representatives. Under the Civil Code what is important to define is the mandate of the representative and the responsibilities flowing from this mandate.

The judge made a decision to the benefit of the client stating that Transamerica was responsible for its representative on the basis that the responsibility of the insurer is not ceded behind the responsibility of the intermediary. To the contrary, the insurer must take all the means possible to ensure that the advice that the client has the right to receive is correctly given because it is the products of the insurers that need explanations and not the product of the intermediaries. Therefore the intermediary that executes his duty of giving advice remains within the mandate given by the insurer. Since Transamerica did not provide good training to the representative; did not provide good information; Transamerica became responsible for the advice provided by its representative even if he was independent.

**When we link this decision to Latreille decision we see that the same reasoning would apply to the service of inforce policies. Service is inseparable from the sale. Therefore the insurer is responsible to ensure that all its agents or independent contractors provide service and that they have the means to do it. Clients are entitled to receive service and if this is not done insurers are required to act to correct the situation by taking over the service or assigning a new agent or contractor. It is important to note that this goes against the commercial practice of not offering a service contract to a contracted representative whose contract has been cancelled to end the right of solicitation of the representative for this insurer. This will be discussed further in the section regarding the orphan policies.**

**As a result, again I was right in stating that the Direct Channel of Manulife had a responsibility for the service of its inforce block and that I needed the staff to do it. Lafreniere also provides an interesting interpretation of the prescription date. The judge decided that prescription did not start when the client found the misrepresentation or the fault but that the prescription started only when the contract would actually lapse which represented the actual time when the client would lose his right to the insurance coverage**

## Section 1.2 Independent Representative and the Civil Code

It was in 1998 that the Law pertaining to the distribution of financial products and services was enacted in Quebec permitting “Caisses Populaires” and other banks to sell life insurance and insurance companies to sell bank products. However these truly only applied to the Caisses

Populaires since banks under the Federal Charter were still prohibited from selling insurance in their branches because of federal legislation.

This new law created eight financial disciplines under the supervision of one regulatory body Autorite Marche Financiers (AMF) primarily responsible for the licensing of insurers, representatives and for the investigations of any penal and administrative infractions while two professional bodies « Chambre Financiere » et « Chambre de Dommages » were responsible for the protection of the public by investigating complaints of violations of the code of ethics adopted by each of these two bodies.

Through the licensing, this new law made advice and solicitation a professional reserved act which can only be done by a physical person who is licensed. This person under the law is called a representative. Under this law, the concept of a broker/courtier does not exist. All representatives may represent many insurers.

*3. A representative in insurance of persons is a natural person who offers individual insurance products in insurance of persons or individual annuities from one or more insurers directly to the public, to a firm, to an independent representative or to an independent partnership.*

*A representative in insurance of persons acts as an advisor in the field of individual insurance of persons and is authorized to secure the adhesion of a person in respect of a group insurance or group annuity contract.*

*14. No representative may pursue activities as a representative unless the representative is acting for a firm, is registered as an independent representative or is a partner in or employee of only one independent partnership.*

This is a major difference with the other provinces. In Quebec, the representative has the legal right to represent many insurers and it is the insurer contract which will restrict this right of doing business with other insurers. In many other provinces, the agent represents legally one insurer and is given the contractual right to represent other insurers. We could say that for most common law provinces, anyone licensed is created as an agent and slave to one insurer while in Quebec; anyone licensed is created as a representative free to deal with any insurers while being free to choose to contractually limit this right.

Finally the representative can act for a firm and therefore becomes mandated by that firm or he can act for himself and under his own name by becoming an independent representative.

## Section 1.3 Today's Agent/Independent Contractor/Independent Representative and the MGA

*Note: for the purposes of efficiency we will use the term representative to mean an agent that is not attached, an independent contractor or an independent representative.*

Representatives can contract with an insurer in two different ways. The representative can contract directly with the insurer and this means the contract is formed between the representative and the insurer. There are no intermediaries. The second way for the representative is to contract through an intermediary who holds the contract with the insurer. The agency contract is being formed between the intermediary and the insurer. The representative is an Annex to this contract. This intermediary is called the Managing General

Agent (MGA). Because the MGA has many representatives on its Annex, it is able to pool the production of these representatives in order to sign contracts with multiple insurers since each insurer will impose sales requirement for their contract. The more representatives an MGA has, with these representatives being good producing agents, the greater the ability of the MGA to sign many contracts with different insurers. By transferring their production/sales to an MGA, the representative also share in this pooling by being able to get the same amount of bonusing for each insurer independently of his production with each insurer. He will get the same bonus for each insurer because his bonus will be based on his total production with the MGA. This however only holds true if the MGA achieve all his sales requirements with each insurer. For example, if a representative does not place any business with Manulife, the MGA's ability to offer the same bonus to this representative will be dependent on other representatives doing business with Manulife or the MGA will lose its contract with this insurer. Finally, an independent representative can contract with multiple MGAs to get access to the insurers he wants. An MGA can also contract with another MGA to access an insurer (usually because this MGA's sales volume is too low and would not meet the sales requirements of the insurer) becoming an Associate General Agent. In the distribution section of this report, we will discuss in further details the implications of using one MGA, multiple MGAs or contracting directly with the insurer.

The Canadian Council of Insurance Regulators (CCIR), in its report entitled "MGA Life Insurance Distribution Model" defines the MGA as:

"*Unlike the Career Agency model, where there was a one-on-one relationship between an insurer and a representative, in today's marketplace, most representatives are now independent and often deal with more than one MGA in order to obtain the coverage that is most appropriate for the consumer, or, at times, in order to maximize their compensation.. an MGA is an individual, partnership or corporation that holds at least one direct brokerage contract with a life insurance company registered to do business in Canada. Within the industry, the entities referred to as MGAs vary greatly in their structure, the services they provide and the contractual obligations they have to both insurers and representatives. In performing these services the MGA is not normally dealing directly with the public, though the information about a client that the representative has gathered will be seen by the MGA.*

*An MGA is a conduit that facilitates business between the representatives, their clients, and insurers by providing some or all of the following services:*
*• Supporting and assisting a representative in obtaining contracts with insurers, which can include granting authority to a representative to act on behalf of an insurer,*
*• Processing and tracking representatives' business submitted by a representative,*
*• Providing representatives with direct sales support,*
*• Facilitating the two way flow of information between the insurer and the representative,*
*• Pooling of commission payments for the representative from various insurers,*
*• Facilitating the submission of completed contracting requirements between a representative and an insurer,*
*• Training representatives,*
*• Providing market conduct compliance support to insurers, and, in some cases,*
*• Developing products and/or assisting in the adjusting of claims on behalf of an insurer."*

The problem that regulators currently faced in regards with the existence of the MGAs is their inability to recognize that MGAs are independent entities separate from the insurers whereby the insurers have delegated their distribution duties such as supervision and training of the representative to the MGA. Regulators consider this a regulatory risk which is quite apparent and stated in the Draft of the Financial Institutions Commission of British Columbia (FICOM):

*"A regulated financial institution is responsible to have adequate controls and oversight of its business functions to ensure that undue risk or harm to the public does not occur. This includes prudent and effective controls over any business function outsourced to, or provided by, a third party. 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 most appropriate way to achieve their corporate objectives. However, insurers need to be aware that these arrangements can increase their dependence on the MGA, which may increase their risk profile if the arrangement is not properly managed or controlled. While insurers establish oversight and control processes for outsourced functions they consider to be material, research conducted by CCIR for the MGA Paper suggests insurers may not be implementing such processes for functions outsourced to MGAs."*

This thinking of the regulators represents quite a departure from current market practices while truly ignoring what the consumer wants. The consumer was not represented in the research conducted by CCIR. Our research conducted by the Financial Services Consumer Alliance indicates that the consumer want to have the choice of dealing with Independent Representatives who are able to offer independent advice. Therefore defining the term independence is extremely important and protecting the use of this term is also equally important. FICOM position on MGA would prohibit MGA and any independent representatives from giving true independent advice because of a conflict of interest where the manufacturer (insurer) controls and has oversight of the intermediary. We believe that in order to foster and protect independent advice this oversight of the MGA cannot be delegated from the regulators to the insurers. When we consider the existence of orphan policies, we can only conclude that insurers have failed dramatically in their own oversight and oversight of their branches or Direct Channel. In view of this tremendous failure on the parts of insurers, we cannot support the delegation of even more authority to the insurers.

Monitoring procedures as stated on principle #4 of the draft written by FICOM should be conducted by the regulators and not the insurers. MGAs should not become a simple doorway to an insurer. MGAs should provide an additional regulatory space which can be used to increase consumer protection.

FICOM has to recognize that the MGA is an agent, independent contractor and an agency which forms agency relationship with agents/sub agents of the insurer.

(1) The MGA has an agency relationship with the insurer arising from the agency contract between MGA and Insurer where the insurer delegated its authority to the MGA. This authority is the responsibility of the insurer and the insurer must ensure it is properly used.

(2) The MGA is an independent business and contractor. This side of the MGA business cannot be put under the oversight of the insurer as this would represent a conflict of interest. Oversight of the independent contractor activities should be under the oversight of the regulator.

(3) The MGA has an agency relationship with its agents arising from the contract signed between MGA and agent. The nature of this agency relationship and delegated authority has still not been defined under current laws and regulations.

(4) The Insurer has an agency relationship with its sub agents which are agents of the MGA. This agency relationship is formed only when the agent is put on annex of the contract between

MGA and insurer, which only usually happens when the agent submits his first application for this company.

The FICOM and CCIR papers also failed to consider the consolidation of MGAs and the emergence of national MGAs which have signed national contracts with insurer; the same national contracts originally offered to the financial services subsidiaries of banks such as Wood Gundy, Merryl Lynch… It is quite clear that the emergence of these national accounts will require greater uniformity in any regulations applying to MGAs and certainly a cohesive approach to regulating these entities; approach that cannot be delegated to the insurers.

FICOM and CCIR also fail to consider the supervisory conflict with MGAs its position would create with multiple insurers having to supervise the same MGA. They also fail to recognize that some MGA are owned by an insurer for example; an exclusive insurer wanting to give access to its tied agents to other insurers creates an exclusive MGA to make its agents multi tied i.e. insurer Industrielle with the MGA Solicour. Also some so called independent MGA are wholly or partly owned by insurers, i.e insurer Transamerica ownership of MGA Groupe Cloutier (current) or AXA with Groupe Gadoua (past)

Finally, we believe strongly that regulators and current legislation should recognize the wish and the need of Canadians to receive independent advice. We therefore believe that the term independent should be defined under the law and be reserved to only those who can offer independent advice. In 2005, a survey was conducted CCIR with industry player regarding the need of defining independence. Here are the results of this survey:

*2. Should independence be defined?*

*Insurance products are sold through a variety of means including direct writers, agents and brokers. Some intermediaries hold themselves out as being independent and consumers have expectations about the objectivity, role and obligations of these intermediaries in sales transactions. Others work for one or a few specific insurers. A number of respondents provided comment on whether or not there needed to be a clear definition of "independent" agents or brokers in order to avoid potential conflicts of interest.*
*Comments Received:*
*The thirty-two responses (ten insurers, four intermediary associations, two self-regulatory organization, four insurer associations, six consumer associations, four brokers and two individuals) to this issue are very diverse. For example:*
*• One insurer suggested that independence should be a synonym for objectivity;*
*• One individual suggested that eliminating the use of "independent" will eliminate much of the consumer perception that the entity or person is truly independent. The word "broker" should be used for those having agency contracts with more than one insurer. Perhaps "Exclusive Agent" should be used for those having an agency contract with only one insurer;*
*• One intermediary association suggested that all insurance intermediaries, by the very nature of the service they render, are assumed to have some degree of independence by the public;*
*• One intermediary association suggested that all intermediaries should be considered independent, unless they hold themselves out as representing one insurer;*
*• One insurer suggested that independence is not something that can or should be codified;*
*• One insurer suggested that a reasonable approach would be to create a definition of independence which clearly states that capital share, ownership, or financial ties must be less than 50 percent in order to enhance transparency and improve customer confidence;*
*• One insurer believed strongly that a good broker must be truly independent, which means that he/she will always act in the customer's best interest;*

*• One individual suggested that criteria should include number of markets (at least 4 for L&H and personal lines, more for commercial), corporate ownership and level of license / training;*
*• One self-regulatory organization suggested that with the implementation of the Registered Insurance Brokers Act in Ontario in 1981, all "independent" agents thereafter became known as "brokers", while captives retain the "agent" designation. There are no "independent" agents in the property and casualty insurance marketplace in Ontario; and*
*• One intermediary association suggested that the law of agency and B.C.'s disclosure regulations address the issue of independence adequately. A related issue identified in the consultations was whether or not policy options identified in the paper should apply to all intermediaries or only to those that hold themselves out to be independent. Seventeen respondents provided comments:*
*• Three insurers noted that (exclusive / captive) agents and direct channels generally have no conflict of interest concerns when making recommendations.*
*• Four respondents (two intermediary associations, one insurer association and one insurer) suggested that an intermediary who represents only one company should be required to disclose to consumers their captive status.*
*• Eleven respondents (one insurer association, three insurers, two consumer associations, two intermediary associations, one self-regulatory organization, one intermediary and one industry respondent) stated that the policy options should apply to all intermediaries:*
*• The industry respondents put forth the need for a level playing field; and*
*• One consumer association stated that most consumers do not distinguish between brokers and agents or know of the different classes of licences.*
*• Four respondents did not agree that policy options should be applied to all agents and brokers:*
*• One consumer association and one individual suggested that the policy options should be applied to independent brokers;*
*• One industry association suggested that the distinction between single and multi company representation probably warrants a different type or level of detail in disclosure to consumers;*
*• One industry association suggested that all policy options, except establishing the priority of the client's interest in legislation or regulation, should apply to the brokerage distribution channel only. The requirement that the client's interests be placed above those of the intermediary or any third party is appropriate for both agents and brokers.*
*IPRC Analysis:*
*The duties of agents and brokers toward their clients have been interpreted by the Courts to be essentially the same. Both agents and brokers owe a high standard of care to understand their client's needs and to provide a product recommendation to meet their needs. The expected standard of brokers and agents includes the duty to advise if the coverage does not meet all of the client's needs. Similarly, the duty to give the relevant information to the client so that he or she can decide what action to take is equally applicable to both agents and brokers.*
*It is clear from the responses received that there is no common agreement or understanding about what "independence" means. In addition, it would be very difficult to define "independence" in law even if there was agreement. If all intermediaries are held to the same ethical standards, then it may not be necessary to define "independence" as a rule to distinguish roles between different intermediaries. However, the number of markets intermediaries represent differs, and consumers need to be aware of this.*

The impact of the lack of definition of the term independent is quite apparent in view of the following case study.

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**Case Study 5: Investors Group; Are they independent?**

What should the word independent mean? For the consumer, the word independent is someone who has the ability to offer advice independently of any influence from any third party. There cannot be any conflict of interest. Sadly the word independent is used quite liberally by the industry often confusing the fiscal status of a representative with the type of authority he has. As a rule, the less authority a representative has in being able to act for the insurer; the greater the independence he has. Let's look at the advisors of Investors Group. Are they independent? How are they portraying themselves to the public?

Below is an add posted in the newspaper by Investors group :

- *Starting date : As soon as possible*
- *Hourly/yearly wage : To be discussed*

*Canada's Financial Planning Services Leader*

*With over 80 years experience helping Canadians and our team of over 4,600 Consultants, Investors Group is dedicated to building lasting client relationships. Today, we serve one million clients through our dedicated Consultant Network - one of the largest in Canada - and their local support staff teams. Consultants are independent but are supported by our solid infrastructure and support.*

First thing wrong is with the term consultant. It is certainly not defined or recognize in any legislation of any provinces. Does a consultant need to be licensed? Does a consultant have the right to offer financial advice or sell financial products? Companies should try to use legal terms in all of their communications to the public. It is the only way for the public to understand the licensing structure; a licensing structure which is portrayed by the regulators as the first line of defense in the protection of the consumer.

Let's describe what a representative of Investors Group is. All of the Investors Group representatives are first mutual funds licensed and primarily offer investment and financial planning advice. Most of them are also insurance licensed and can offer life insurance. Representatives of Investors Group represents themselves under the name of Investors Group. Therefore they are a captive sales force. They usually work out a branch of Investors Group. Any client a representative has is the property of Investors group and not the property of the representative. If the representative quits Investors Group to change firm for example, he does not take his block of clients with him to the new firm. The clients stay with Investors Group and are assigned to new representatives. In the Investors Group contract, there is a non-compete clause preventing the representative from contacting his clients. Finally for the insurance, Investors Group representatives can only sell the products offered by Investors Group or offer products of other insurers who have signed a contract with Investors. The representative cannot enter into an agreement with other firms such as MGAs to access insurers not offered by Investors. It is for this reason that Investors Group representatives are not considered independent. In the real following case, you will see the actual results of not being independent.

At the time, I was working for Berkshire Insurance as the Director of Insurance for the Maritimes. We had recruited a new representative in Prince Edward Island. This representative had previously been with Investors Group. While he could not contact his previous clients, his clients were however free to contact him and he could then transfer them to Berkshire. One of his clients contacted him because he had some questions about the Universal Life he had sold

him. Usually Investors Group representative are not very knowledgeable about insurance even if they are licensed. This is why they have an in house insurance specialist. Since I was also the insurance specialist at Berkshire, he asked me to review the Universal Life in question.

The first thing I noticed was that the client was rated a smoker for smoking cigars. In fact all of the 5 insurance companies offered by Investors considered cigar smokers like cigarette smokers. With Berkshire, the representative now had access to all of the insurance companies and it just happened that Standard Life considered cigar smokers as non-smoker. When I ran a new non-smoker illustration, the premium went down by more than $7,000 if the client took a new Universal Life with Standard Life. This was the good news he could tell his client. The bad news was that he was going to have to explain to his client why he had been unable to offer him this deal and why he paid $7,000 too much when he was with Investors Group; not an easy task.

This is why he asked me to come at the meeting to help him out with the client. I had to sit with the client and explain to him the difference between a representative who is independent and a representative who is not independent. I supposed I did a great job because the client took the new Standard Life policy and he did not sue Investors Group. I considered this a job well done until I received a call a few days later…

The person calling me was none other than the Superintendent of Insurance for the province of Prince Edward Island. My first reaction was to wonder why such an great personage was calling me. I guessed that I had not done such a great job after all and the client had made a complaint against Investors Group and this was so serious than the Superintendent himself was involved in the matter. Rapidly I learned that I was wrong because the Superintendent was accusing me of having done an infraction in his province.

It seems that Investors Group had a direct line to the Superintendent and had called him accusing me of selling insurance in this province without a license. This superintendant was therefore calling me to tell me that this replacement was illegal and that if I did not stop this replacement I was going to be prosecuted for having committed an infraction.

I have this reflex when I am threatened; I get angry fast and I push back. I am not a guy you can threaten without facing some serious consequences. The flow of the conversation changed suddenly when I told him that I would welcome such prosecution and that as Director of Insurance I had a duty to manage my agents and this meant sometimes accompanying them in client meetings as a specialist in insurance. To do this, there were no requirements for licensing. Finally God himself would not be able to tell me to act against the best interests of a client and as a result he was out of luck. The Superintendent hung up and I never heard from him again or Investors Group

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## Section 1.4: The insurer

Aside from duty of good faith and fair dealing with the insured, provincial regulations require insurers to establish and maintain a system that is reasonably designed to ensure its agents complies with the Act, the regulations and the terms of the agent's license. This still holds true for insurers that use agent "captive agent". However with the introduction of the MGA, who now act as an intermediary, this duty of the insurer has been delegated to the MGA. Could the insurer do this? This question will be answered when the regulators recognize in the law the existence of the MGA.

Independent representatives can also sign direct contracts with insurers without the use of an intermediary. Because the representative is not exclusive to the insurer, the insurer holds that this representative is not an agent of the insurer. In this case, we could state based on the insurer's representations that the representative is responsible for himself. Is this the case? It is impossible to know because while regulators have just recognized the existence of the MGA, direct distribution is not even on their radars.

Most common law provinces require an insurer to sponsor an agent for the regulator to provide a license to the agent. In some provinces (such as Ontario) do not require insurers to sponsor the advisor once certain experience requirement levels are met (2 years) whereas other provinces (such as New Brunswick) require an insurer to sponsor the agent for an indefinite period of time. Other provinces (such as British Columbia) require the insurer to provide a certification in respect of the agent but do not require any exclusivity. It is the insurer's responsibility to meet its sponsorship obligations**.**

**The nature of this sponsorship obligation and associated responsibilities are now undetermined. For example for 5 years I held an insurance license in Nova Scotia sponsored by Canada Life after moving to Quebec to work as an employee for Manulife. Originally my sponsorship was obtained by my MGA when I was working as an insurance agent in Nova Scotia but during that time, I never met someone from Canada Life in regards to my sponsorship. This demonstrates that the sponsorship system is antiquated and offer no benefices or protection to the industry or the consumer.**

## Section 1.5 Industry Associations

There are numerous industry associations which represent interest of the insurers, the distributors and of the representatives. Since regulators conduct regulatory review through industry survey, it is clear that the voice of the consumer is outnumbered, unheard and sometimes even not represented. Here are the associations which have the ear of the regulators:

**1. CHLIA**
Established in 1894, CLHIA is a voluntary non-profit association with member companies accounting for 99 per cent of Canada's life and health insurance business.

The mission of the CLHIA is to serve its members in areas of common interest, need or concern. In carrying out this mission, the Association shall ensure that the views and interests of its diverse membership and of the public are equitably addressed.

Based on its mission and operating philosophy, the strategic objectives of the Association are:
1. To build consensus among members on issues and concerns of importance to the industry.
2. To promote a legislative and regulatory environment favourable to the business of its members.
3. To foster sound and equitable principles in the conduct of the business of its members.
4. To inform and educate members about domestic developments and, where warranted, international developments of importance to them.
5. To preserve and advance the industry's reputation.
6. To promote, on behalf of its members, public policies that contribute to the betterment of the Canadian economy and society.

7. To deliver maximum value for money to its member

**2. CAILBA**

ABOUT CAILBA

MISSION STATEMENT

The Canadian Association of Independent Life Brokerage Agencies (CAILBA) will include, as its members, a majority of the country's life and health insurance brokerage agencies. Its mandate will be to lobby provincial and federal legislative issues affecting the industry, and establish uniform standards within the industry for efficient information processing. It will also provide an effective forum for networking and relationship building among members, insurance companies and industry vendors.

PURPOSE

The Canadian Association of Independent Life Brokerage Agencies (CAILBA) has been organized by agencies who understand that some things which must be done to protect and improve the place of life brokerage agencies in the socio-economic system, must be done collectively. CAILBA's purposes are:

To foster and expand the responsible and effective distribution of life and health insurance and related financial services for the benefit of the brokers, agents, companies and consumers that are serviced by agencies;
To increase the knowledge of members regarding the lawful, efficient and profitable applications of technology and systems for agency management;
To promote practices, regulations, and legislation in the best interest of life brokerage agencies, producing agents and to better serve consumers;
To provide a legally constituted medium through which members may deal with common concerns and co-ordinate their collective efforts;
To work with other organizations in the interest of the insurance industry.

**3. Advocis**

On June 4, 1906, the members of the Life Underwriters Associations of Montreal, Quebec City, Prince Edward Island and Toronto met and founded the Life Underwriters Association of Canada (LUAC) to act in the interest of life insurance agents and represent their views to government and the public.

Then as now, professionalism and advocacy drive the Association's mandate.

Today, Advocis, The Financial Advisors Association of Canada, is the oldest and largest voluntary professional membership association of financial advisors and planners in Canada. We are the home and the voice of Canada's financial advisors. Through its predecessor associations Advocis proudly continues a century of uninterrupted history of serving Canadian financial advisors, their clients, and the nation.

With more than 11,000 members organized in 40 Chapters across Canada, Advocis members serve the financial interests of millions of Canadians.

As a voluntary organization, Advocis is committed to professionalism among financial advisors. Our members are professional financial advisors who adhere to an established professional Code of Conduct, uphold standards of best practice, participate in ongoing continuing education programs, and maintain appropriate levels of professional liability insurance and are committed to putting their client interests first.

Our members are experts who can provide a full range of financial services including estate and retirement planning, wealth management, risk management and tax planning.

**4. Independent Financial Brokers**

Who
Independent Financial Brokers (IFB) is a not-for-profit Association representing independent insurance, mutual fund and other financial service professionals.
Just like the name says - IFB members are 'independent'. That means that they do not work exclusively for one company, and are able to sell the products and services of two or more companies

What
As an Association, our role is to enhance and protect the businesses of our members and to support consumer choice. We do this by maintaining an active dialogue with the federal and provincial governments, the industry regulators, and the decision-makers. In addition, we provide our members with a variety of benefits, including high-quality Continuing Education opportunities so that they can remain on top of changes and developments within the industry.

Why
If you are independent financial services professional, you should be a member of Independent Financial Brokers. With an over twenty-year history of successfully fighting for the rights of the independent, IFB is the only Association dedicated to the needs and concerns of the independent broker.

**5. OLHI**

Who is OLHI?

The OmbudService for Life & Health Insurance (OLHI) is a national independent complaint resolution and information service for consumers of Canadian life and health insurance products and services, including life, disability, employee health benefits, travel, and insurance investment products such as annuities and segregated funds.

We were established in 2002 as a Not for Profit corporation and operated under the name “Canadian Life and Health Insurance OmbudService” until August 17, 2009. OLHI is a member of the Financial Services OmbudsNetwork (FSON), a Canada wide dispute resolution service supported by Canada’s financial services regulators and financial services firms.

**6. CSF**

Mission
The mission of the Chambre de la sécurité financière is to protect consumers by maintaining discipline and overseeing the training and ethics of nearly 32,000 members who work in five

sectors and registration category, that is, group savings plan brokerage, financial planning*, insurance of persons, group insurance of persons and scholarship plan brokerage.
The Chambre carries out its mission by stringently monitoring the practices and continuously upgrading the knowledge of these professionals.

**7. APCSF (the translation of French to English done by APCSF of their web site requires some improvements…)**

The mission: defend our rights and our reputation
To preserve the perpetuity of independent financial council by the promotion and defense of its members' common professional interests and by grouping together these people under the banner of a strong voice to represent them.

We take action!
Our objective: form once for quite the Independent Regroupment of Advisors of the Quebec Financial Industry services from which the mandate will be to defend our professional interests with the diverse bodies of frame, to exploit our rights and our interests and promote our reputation with the public.

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## Case Study 6: CAILBA; Are they independent?

CAILBA as we see by the use of independent in its corporate name portrays itself as being independent to the public. We therefore find this communication very interesting where Daniel Kahan, an advocate for life settlement in Canada, want to discuss this issue legal in many provinces of Canada to understand CAILBA's position. CAILBA refused stating that the views of CAILBA are simply those of the insurers and that they would never adopt a stance that is different than what the insurers want. Is this the idea of independence… No wonder the insurers do not want the word independence to be defined in the legislation

Richard, how is your Policyholders Association progressing?

Did you see the Insurance Journal articles on Viaticals ?

---------- Forwarded message ----------
From: Info <info@cailba.com>
Date: Thu, May 8, 2014 at 3:50 PM
Subject: RE: CAILBA Member Communication - Life Settlement (Viatical) Schemes in Canada
To: Daniel Kahan <dekahan@gmail.com>, georgepolzer@islsp.org
Cc: Allan Bulloch <abulloch@ppisolutions.ca>, Arnold Scheerder <arnolds@rgpafin.com>, Bob Ferguson <bobferg2000@yahoo.com>, Casey Brandreth <casey@daystar-financial.com>, David Stewart <david.stewart@financialhorizons.com>, info@cailba.com, Marc Lantaigne <Marc.Lantaigne@financialhorizons.com>, Michael Williams <mwilliams@bfgon.com>, Natalie Ho <natalie.ho@logiq3.com>, Nick Simone <nsimone@qfscanada.com>, Paul Brown <PBrown@idcwin.ca>, Terri DiFlorio <terri.diflorio@hubfinancial.com>

Dear Daniel,

Thank you for your query.  CAILBA members act as intermediaries for insurance companies and as such, will adopt no stance different from that of insurers.  It is not our intention to weigh

in on this topic.  Rather, our bulletin to members was intended to alert them to the potential for fraud.

Best regards,

Michael Williams

Michael Williams | CAILBA | President | 105 King Street East, Toronto, ON, M5C 1G6
416-548-4223 | www.CAILBA.com | info@CAILBA.com

From: Daniel Kahan [mailto:dekahan@gmail.com]
Sent: Thursday, May 08, 2014 1:26 PM
To: info@cailba.com
Cc: georgepolzer@islsp.org
Subject: Fwd: CAILBA Member Communication - Life Settlement (Viatical) Schemes in Canada

Arnold,  one of your members just forwarded this to me for my attention.

As the new (volunteer) Executive Director of ISLSP ( see www.islsp.org ) we are also concerned about such STOLI schemes being created on both sides of the border but I think it would behoove CAILBA to differentiate between STOLIs where there is a potential lack of insurable interest from the outset and those LS companies (primarily in Quebec where there are NO trafficking restrictions) who offer Canadian seniors (who have owned their policies for years) the opportunity to sell their Term to 100 life policies if they no longer need them or (worse) can't afford to continue making the premium payments or make the policies paid-up.

You are probably aware of the 1993 OIC Guidelines on Living Benefits which most life insurers do not adhere to and the introduction in 2000 by the late Jim Flaherty when he was Ontario Finance Minister of Schedule G of the Red Tape Reduction to repeal sec. 115 of the Ontario Insurance Act subject to the promulgation by FSCO of Life Settlement Regulations.

I would be very interested to know where CAILBA stands on legitimate Life Settlements, especially in the 4 Provinces which never implemented the insurance trafficking restrictions back in the 1930s.

Daniel Kahan ASA, Executive Director, ISLSP  416-782 8766

PS I would be delighted to come and discuss this matter with you and your Board of Directors in more detail to see if we can find some common ground and act on behalf of your members when their insurers prohibit them to act in the best interests of the policyholder and will punish them with the loss of their licence.

From: Info [mailto:info@cailba.com]
Sent: Thursday, May 08, 2014 8:01 AM
To: ' CAILBA Info'
Subject: CAILBA Member Communication - Life Settlement (Viatical) Schemes in Canada
Importance: High

Dear CAILBA member:

We wanted to bring it to your attention that a potential Life Settlement (Viatical) scheme is currently being promoted here in Canada, involving a so-called “Pension Company” that provides a non-recourse loan for $25,000 or $50,000. The borrowers are required to purchase a $500,000 or $1million dollar Life Insurance policy. A joint bank account is opened with the borrower and pension company. The pension company pays the premiums for the life insurance policy, which is assigned to the pension company.

The so-called non-recourse loan has an unreasonably high interest rate of 12%. On death, all the premiums paid by the pension company plus the loan of $25,000 or $50,000 plus 12% interest (capitalized) is deducted from the Death Benefit. If the Loan and premiums paid exceed the Death Benefit, the beneficiaries get nothing and the loan, being non-recourse, is not called. We do not know where the funding for the so-called pension company is coming from. We also wonder whether there are money laundering implications.

We understand that this has been happening for a few years. For one company, relatively high face amount ($500,000 - $1 million) term insurance purchases were made online through the company’s direct insurance channel. The term plans were then converted to Term 100 plan.

We have been told that the person behind the marketing scheme may be a former life insurance agent whose license was revoked.

If you identify any such concerns, please notify the insurance company involved. I would also appreciate being informed.

Sincerely,

Arnold Scheerder

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## Section 1.6 P&C versus Life Insurance; the Quebec and Ontario Example

*The Supreme Court of Canada in Fletcher v. Manitoba Public Insurance Co. said : “Selling insurance is not . . . like selling groceries, and the law should not treat them alike.” The broker is a professional who is held to a commensurately higher duty of care.*

In Quebec, as we have seen, all of those who are licensed to advise and sell insurance are licensed as representatives whether they sell insurance or property and casualty insurance. Representatives are independent or not. If they are not independent, they must act for a firm. This represents clear legislation about licensing with a good definition of what is a representative that is applied across all financial services minimizing consumer confusion. Since the representative is mandated by the insurer in its actions with the consumer, the only determination to be made is about the nature of this mandate and the responsibility of insurer and representative in regards to this mandate which has been done through court cases as we have seen in our case studies.

However the responsibilities of the representative versus an independent representatives towards the consumers is not addressed clearly since both type of representatives share the same code of ethics. For example, the code of ethics states that:

*A representative must, in the practice of his profession, always remain independent and avoid any conflict of interest.*

How can the representative remain independent when under statute law he is not independent because he acts for a firm or he is the employee of an insurer? It is clear that to improve consumer protection in Quebec, there should be two code of ethics; one for all representatives with an annex for independent representatives.

In the common law provinces, this does not hold true. First there are tremendous variations across the provinces. We will take as an example the province of Ontario. In the property and casualty insurance, the definition of a broker is well defined which result in clarity of the definition of a broker linking this definition to independence and the ability to represent many insurers. This has allowed these brokers to regulate their independence. In fact they have their own Act or statutes to regulate their activities with their own organization for self governance.

*Who is RIBO?*

*RIBO stands for the Registered Insurance Brokers of Ontario. It is a self-governing, self-supporting organization of general insurance brokers in Ontario. RIBO was established by the Ontario government in 1981 to protect the public during insurance transactions with brokers, through self-governance.*

*RIBO regulates the licensing, professional competence, ethical conduct and insurance related financial obligations of all independent general insurance brokers in the province of Ontario.*

*What is a Registered Insurance Broker?*

*A registered insurance broker is an independent insurance professional in Ontario governed by the Registered Insurance Brokers Act. Brokers sell general insurance including coverage of your home, business, automobile, boat etc. They offer product choice from a variety of companies and offer independent advice. Brokers represent their client's best interest when negotiating a contract between the client and the insurer.*

*Every registered insurance broker must be properly licensed.*
*Every registered insurance broker is subject to a code of conduct.*
*Every registered insurance broker must meet certain qualification standards and continuing education requirements, established by the Qualification & Registration Committee.*
*Every registered insurance broker must be bonded and covered under an Errors & Omissions policy.*
*How is the Public Interest Represented?*

*At least one member of the public, appointed by the Lieutenant Governor in Council, sits on every RIBO Committee to represent the interest of insurance consumers and the public in general.*

*RIBO also has a Complaints and Investigation Department to assist consumers with any enquiry or complaint regarding a broker. When a complaint is received, it is RIBO's responsibility to ensure that both sides of the enquiry are investigated promptly and fairly.*

*RIBO's Consumer Complaints Officer resolves the majority of complaints from the public within 24 hours. Complaints indicating that professional misconduct has occurred are referred to the Complaints Committee.*

*To Whom is RIBO Accountable?*

*On a yearly basis, RIBO must provide the Minister of Finance, the Superintendent of Financial Institutions and every RIBO registrant with a copy of the Annual Report. Included in this report is a statistical summary of registration numbers and discipline proceedings, committee reports and the audited financial statements.*

*The Annual Report and a report of a yearly examination by the Financial Services Commission are subsequently tabled in the Ontario legislature for review by its members.*

The question therefore is: Why has life insurance regulations not evolved at the same pace and fashion than the Property and Casualty insurance in Ontario? This should have been natural and if the life industry has not changed, this is because it is unnatural; this unnatural state the result of powerful lobbies that are able to promote their interests above those of the consumers.

Referring to the CCIR survey, here are the answers regarding the Life insurance industry adopting the same standards than the P&C industry. We do not agree with these results.

*Nine respondents (four intermediary associations, two insurer associations, two intermediaries and one insurer) were of the view that different regulatory responses were required for the P&C and L&H sectors:*
*• One insurer association suggested that consistency across the financial sector can be best achieved in principle rather than in detail;*
*• One intermediary association suggested that it is critical that any new requirements recognize that P&C products and L&H products are essentially different; and • One insurer stated that there is a distinction between L&H and P&C products in that L&H products are sold, not bought.*

## Section 1.7 Brokers and agents in the mortgage industry

Again we in an industry we have a significant difference with the meaning of broker and agent. If we refer to the Mortgage Act of Ontario we see that basically an agent and broker substantially the same. The difference in not in their independence or who they represent. The difference is measured terms of experience and supervision. To become a broker you must first be an agent for a certain length of time working under the supervision of a broker.

This regulatory perspective of the agent versus broker is quite significantly different from the perception of the public. Why is it perceived or accepted that there is no agency relationship between a broker and a bank contrary to the insurance industry.

If we accept the fact that an agency relationship arises from the formation of a contract between a principal and an intermediary, such contract in fact does not exist between the broker and the bank contrary to an insurer and life insurance representative. Let's consider 2 examples based on my previous experience where I was licensed both as a mortgage broker and insurance agent in Nova Scotia. I was a mortgage broker with a brokerage house named Invis. Now in submitting mortgage applications though Invis, my suitability was never reviewed by any lenders. I did not sign any contracts with any of the lenders.

As an insurance agent, I submitted my insurance applications through an MGA. With the submission of the first application with an insurer, the insurer reviewed my suitability. If this suitability was accepted, then I signed a contract with the insurer as an Annex to the MGA contract. While as an Annex, I signed a very simple contract since most of the contractual provisions were found in the contract between the MGA and insurer, there was still a contract between me and the insurer. Finally, to have a licence as a mortgage broker I did not need to be sponsored by a bank while I needed to be sponsored by an insurer to be a licensed agent.

## Section 1.8 Canada versus the World

It this report we will strive to compare each section with what has happened in Canada versus what has happened around the world. At the beginning of the life insurance industry, intermediaries in insurance were very much the same in Canada, United States, Europe, India and Europe. Since then significant changes have occurred and Europe seems to represent the most mature regulatory environment with many European countries having with various degrees of success integrated the concept of multi-representation, independence and broker in their laws and regulations. As a result we will start our comparison with Europe:

**Europe**

We will use the definition of intermediaries used by CEA. The CEA is the European insurance and reinsurance federation. Through its 33 member bodies — the national insurance associations — the CEA represents all types of insurance and reinsurance undertakings, eg pan- European companies, monoliners, mutuals and SMEs. The CEA represents undertakings that account for approximately 94% of total European premium income. In its March 2010 report on Insurance distribution channels in Europe, CEA use the following definition of intermediaries to allocate market share to each distribution channel:

Intermediaries are (1) Agents; Intermediaries who represent the interests of the insurer, (2) Tied agent; Intermediary acting as an agent of the insurer and under exclusive agreement to refer business to one Insurer, (3) Multi-tied agent; Intermediary acting as an agent for several insurers and with multiple insurer agency agreements and (4) Brokers; Intermediaries who represent the interest of the client.

The term "Insurance Broker" was defined in Article 2(1)(a) of the EEC Directive on insurance agents and brokers in December 1976.

"Persons who, acting with complete freedom as to their choice of undertaking, bring together, with a view to the insurance or reinsurance of risks, persons seeking insurance or reinsurance and insurance and reinsurance undertakings, carry out work preparatory to the conclusion of

contracts of insurance, or reinsurance, and, where appropriate, assist in the administration and performance of such contracts, in particular in the event of a claim".

The European Union passed a directive on insurance intermediation in 2002 (Directive 2002/92/EC) that led to new legislation in all EU states, Norway and Switzerland. As explained by Helena Rempler in relation to Swedish legislation: “Directive 2002/92/EC on insurance mediation (IMD) was implemented in Sweden in 2005 by the Swedish Insurance Mediation Act (SFS 2005:405). Under this Act, an insurance intermediary (a private individual or a legal entity) may conduct business as an independent or a tied intermediary. The definition of “tied insurance intermediary” set out in the IMD (“any person who carries on the activity of insurance mediation for and on behalf of one or more insurance undertakings in the case of insurance products which are not in competition but does not collect premiums or amounts intended for the customer and who acts under the full responsibility of those insurance undertakings for the products which concern them respectively”) has been implemented in the Swedish Insurance Mediation Act. It is understood that this is how the IMD has been implemented in all jurisdictions within the EU/EEA. Independent intermediaries (often referred to as brokers) must apply to the SFSA for a licence and, when a licence is obtained, register the intermediary business at the Swedish Companies Registration Office. A tied intermediary on the other hand, is not required to conduct business through a licence. Instead, a tied intermediary acts under the liability of the insurer to which it is tied, but must nonetheless be registered at the Registration Office.”

Despite this directive, the intermediation of insurance in Europe is not as homogenous as we would first think and therefore is still a work in progress with the legal status of insurance intermediaries varying throughout the European insurance market leading to the same problem existing in Canada which is the difficulty in determining whether an intermediary is legally an agent or broker.  Contrary to Canada where there are no progress on this issue; continued liberalization and homogenization is expected in Europe. The implementation of the Third Generation of Insurance Directives will enabled all European Union-based insurers to establish their own representatives throughout the Single Insurance Market [SIM] and to offer their services in cross-border trade under the freedom of services.

It is clear that Europe has progressed much further than Canada on mediation of insurance. In fact aside from Quebec and Alberta, the majority of the provincial legislation does not even recognize or deal with the reality of multi-tied agents. As for the term broker, if recognized in any Canadian provinces, it is used to define an agent who sells multiple insurers instead of someone who is acting independently under a mandate of a client. Some provinces are better at recognizing who is exclusive and who is an independent contractor. Therefore if we bring the best of both worlds to define an agent as an intermediary, we have (1) Tied-agent who are contractually exclusive (under principal name) or act as independent contractor (under own name) and (2) Multi-tied agent who are contractually exclusive (under principal name) or act as independent contractor (under own name).

When the Multi-tied agent is exclusive there are two types of agency relationship. There is one primary agency relationship with the exclusive/sponsoring insurer. A primary agency relationship exists with the sponsoring insurer under which name the agent operates. There are multiple secondary agency relationships which are very limited in their nature with secondary insurers who have formed a distribution contract with the primary insurer. We state that the agency relationship is very limited between the agent and secondary insurers because it is clear that the acts of the agent would always be interpreted under the primary agency relationship even when the agent is representing the secondary insurers.

When the Multi-tied agent is not exclusive and acts as an independent contractor under is own name, there are various agency relationship which are formed. There is a legacy agency relationship with the insurer sponsoring the licence. We are calling this a legacy agency relationship as there are no obligations on the insurer to monitor the suitability of the agent it is sponsoring nor are they any sales requirements. A primary agency relationship will exist between the agent and the MGA or MGAs he contracts with. Through the MGA contract, he will be able to contract with the insurer as a "sub agent" and therefore will have a secondary agency relationship with the insurer. It is at this level where regulators have a different point of view about the MGA. They consider that the duties and obligations of the insurers cannot be delegated to the MGA and therefore the agency relationship between insurer and agent in this instance cannot be secondary but is instead a primary agency relationship in its nature.

To show the evolution of the regulation of intermediaries in Europe, we have selected a sample of countries for review:

## Belgium

In 2007, this was the picture of the intermediaries existing in Belgium:

**1. Insurance broker:** the intermediary who put the policyholders in contact with the insurance companies without being bound to the choice of a particular company.
**2. Insurance agent:** the intermediary charged by virtue of one or more contracts or powers of attorney to present, to propose and to prepare or to conclude insurance contracts or to help in their management or in their performance, especially in the event of a claim, in the name of and on behalf of one or more insurance companies.
**3. Insurance sub-agent**: the intermediary who is not an insurance broker or an insurance agent but act on behalf of an insurance broker or an insurance agent.
**Concept of "tied insurance intermediary" as defined in IMD :** no

It's clear therefore that in 2007, Belgium did not conform to IMD but as we can in less than 7 years, this country was able to modernize its legislation to the standards of MiFID which introduced harmonized conduct of business rules across the European Economic Area for investment service providers. **Why is Canada absolutely unable to do the same?**

PWC in its 2011 report *"Study on the impact of the revision of the Insurance Mediation Directive (ETD/2007/IM/B2/51) Final Report*" summarized the Belgium market as followed:

"Belgium implemented the IMD on 15 March 2006. Prior to the transposition of the IMD into Belgian legislation, insurance intermediaries (including direct writers, brokers, agents and sub-agents) were subject to statutory regulation by the law of 27 March 1995. Furthermore, while the original intention of the 1995 legislation was to capture intermediaries, the Belgian state (at the request of the Belgian insurers association) decided to extend the conditions across the market in order to prevent any loopholes. The impact of the IMD in 2006 was therefore expected to be small as the IMD was prepared during the Presidency of Belgium and was therefore largely inspired by the existing Belgian legislation. For the distribution of insurance products, the Belgian regulator (CBFA) differentiates between the Responsables de la Distribution (those responsible for distribution) and Personnes en contact avec le public (those dealing with the public). Those who are Responsables de la Distribution fall under the requirements of the IMD and are required to register with the CBFA. There are around 22,000 Responsables de la Distribution in Belgium. Responsables de la Distribution can be agents,

brokers or direct writers. In addition to formal registration with the CBFA, they must prove that they are of good character and that they have a Master‘s degree and specific knowledge of the insurance market. They must also have a minimum level of training in subject matter approved by the CBFA over a three year period, and this can be checked by the CBFA. Due to market fragmentation, the controls for brokers are more complicated than for direct writers. The ongoing costs of training and registration within this supervisory regime are considered high. New and simplified mechanisms are expected to be applied in the future with regards to the registration procedures of Responsables de la Distribution. Of relevance to the impact analysis for Belgium is the existing structure of the market. Brokers are highly important to the distribution of insurance products in the country, accounting for over 40% of overall premium totals (one third of life and two-thirds of non-life products respectively). Furthermore, the majority of brokerages in Belgium are estimated to have between three to five staff, making them vulnerable to changes which may cause significant administrative impact. Against this, the brokerage industry benefits from an advanced IT infrastructure that captures and communicates data in a highly streamlined fashion between brokers and insurers. Therefore, any further data transfer requirement that could be incorporated into this platform would be of low impact. It should also be noted that Belgium does not have a lengthy chain of intermediaries between the insurer and the end customer by comparison to some other member states, a point of significance regarding disclosure of remuneration regimes.”

As per the report produced by Baker & McKenzie, Belgium continued its regulatory progress “*MiFID for the insurance industry as from 30 April 2014*”

“Acknowledging the importance of a level-playing field between the insurance industry and the investment services industry resulting from the similarity between certain financial instruments and insurances, new Belgian legislation4 (granting power to the King to expand the scope of the existing MiFID rules to insurance undertakings and insurance intermediaries) has been adopted. Under MiFID, insurance undertakings and insurance intermediaries will be subject to detailed organisational requirements relating, for example, to matters such as the management of conflicts of interest and the structuring of compliance, internal audit and risk management functions. In addition to this, MiFID will introduce detailed conduct of business rules for insurance undertakings and insurance intermediaries covering aspects of the sales process, including provisions covering marketing communications, suitability and appropriateness requirements. Introducing new definitions:

"**Service providers**" means: “(i) insurance undertakings, including their tied agents and the insurance subagents acting under the responsibility of these tied insurance agents (together defined as "insurance undertakings sensu lato"); and (ii) all the insurance intermediaries other than tied insurance agents.”

"**Tied insurance agent**" means "the insurance agent:
- who may only exercise insurance mediation activities in the name and for the account of:
o one single insurance undertaking; or several insurance undertakings to the extent that the insurance agreements of these undertakings are not mutually competing agreements;
- by means of one or more agreements or mandates; and
- who act under the full responsibility of (these) insurance undertaking(s) regarding the relevant insurance agreement(s).”

"**Mutually competing insurance agreements**" are each of the following:
- The insurance agreements, which form part of the group of activities "life," and qualify as investment insurance products or insured savings10;

- The insurance agreements, which form part of the group of activities "life," and do not qualify as investment insurance products or insured savings;
- The insurance agreements, which form part of the group of activities "non-life," belonging to the same branch of activity11.

"**Insurance intermediary, other than tied insurance agent**" means:
- "the insurance intermediary, who, by means of multiple agreements or mandates, may exercise insurance mediation activities in the name and for the account of several insurance undertakings without being tied to such insurance undertakings, and the insurance subagents acting under such insurance intermediary's responsibility; and
- the insurance broker and the insurance subagents acting under such insurance broker's responsibility."

**Specific liability regime for insurance (sub)agents**
Where a tied insurance agent is appointed, insurance undertakings must remain "fully and unconditionally" responsible for any action or omission in relation to the Insurance MiFID Rules on the part of their tied insurance agent when acting on behalf of the insurance undertaking, notwithstanding possible liability of the tied insurance agent in case of an obvious shortcoming. Where a sub-agent is appointed, insurance agents and brokers must remain "fully and unconditionally" responsible for any action or omission on the part of their subagent when acting on behalf of the insurance agent or broker. This liability regime will require the responsible service providers to establish internal measures to ensure compliance with the Insurance MiFID Rules.

## Denmark

Insurance brokers obtain a license as either a life- or a non-life insurance broker or both. Insurance brokers refer to a natural or legal person who pursues insurance mediation on the basis of an agreement concluded with a customer. The insurance broker must be independent of any insurance company. The insurance agents are registered according to the insurance company they have agreements with, but there is no information about which products they sell. Insurance agent corresponds to the concept of "tied insurance intermediary" as defined in the IMD. They act on the basis of an agreement with one or more insurance companies.
3. The subagents are registered by the Danish FSA and the registration shows to which insurance company they are linked. They work on the basis of an agreement with an insurance agent under the full responsibility of the insurance agent.
Concept of "tied-insurance intermediary" as defined in the IMD: We do not use the term tied IIM, but our concept of agents and subagents in many way corresponds to the concept of ties agents in the IMD.

In 2011, Denmark FSA wrote a response to the European Commission highlighting that there was still regulatory and term conflicts across Member States advocating and recommending that the Commission keep the IMD as a minimum harmonization directive with the possibility for Member States to introduce stricter national requirements. To illustrate this Denmark used the regulations of brokers in this country:

"In the interest of general good, the Danish Act on Insurance Mediation therefore contains a prohibition on receiving commission or other remuneration from insurance companies when pursuing activity as an insurance broker in Denmark. The prohibition has been in place since 2006…insurance brokers are obliged to provide an objective advice to his or her customers. In that sense, insurance brokers are bound to be independent of any insurance companies…The

Danish FSA could also accept a general commission prohibition in Europe in regard to insurance brokers. However, the Danish FSA acknowledges that this will not be obtainable due to the differences in the European markets of insurance mediation".

## Germany

1. "Makler" (broker), § 34d (1) and (2) Gewerbeordnung
2. "Vertreter" (agent), § 34d (1) and (2) Gewerbeordnung
3. "gebundener Vermittler" ("tied insurance intermediary" as defined in the IMD), § 34d (4) Gewerbeordnung
4. "produktakzessorischer Vermittler" (intermediary whose principal professional activity is other than insurance mediation and the insurance is complementary to the product or service supplied), § 34d (3) Gewerbeordnung
5. "Versicherungsberater" (insurance advisor, giving advice in insurance matters without receiving any commission from an insurance company), § 34e Gewerbeordnung
Concept of "tied-insurance intermediary" as defined in the IMD: yes

PWC in its 2011 "Study on the impact of the revision of the Insurance Mediation Directive (ETD/2007/IM/B2/51) Final Report" summarized the German market as followed:

The German insurance market is a mature and regulated market with a high penetration of insurance products among the population38. Insurance undertakings in Germany rely heavily on intermediaries with more than 90% of business being executed via this channel. Direct writers, therefore, represent a minor share of the market. There are 260,196 registered intermediaries in Germany. The majority of these intermediaries are rather small structures with an average of four to five employees. Whereas the insurance undertakings are under the supervision of the federal financial supervisor Bundesamt für Finanzdienstleistungen' (BaFin), intermediaries have to register with the Chambers of Industry and Commerce (IHK).The transposition of IMD in Germany took effect on 22 May 2007 and represented a major change in Germany as insurance intermediaries (including brokers, agents, and sub-agents) were neither subject to authorisation nor to any other registration requirements at that time. Although no cost benefit analysis was undertaken in Germany a majority of market participants estimate that the adaptation to the new law was expensive and time consuming. Prior to transposition of IMD into German law over 400,000 insurance intermediaries were estimated to be active in the market (Including part time intermediaries), a figure which has now dropped by over one third. Despite this drop, a number of the previous intermediaries are now active as _Tippgeber', or referral agents, which are only allowed to refer prospects to intermediaries and do not have the right to advise customers. The laws implementing the Directive 2002/92/EC on Insurance Mediation are the _Gesetz zur Neuregelung des Versicherungsvermittlerrechts" and the _Verordnung über die Versicherungsvermittlung und -beratung' (VersVermV).

## Italy

Insurance and reinsurance intermediaries are classified into five categories corresponding to the five sections into which the register is subdivided:
1. insurance agents, in their capacity as intermediaries acting in the name or on behalf of one or more insurance or reinsurance undertakings (Section A);
2. insurance and reinsurance brokers in their capacity as intermediaries acting on behalf of their client without the power to represent insurance or reinsurance undertakings (Section B);

3. direct canvassers who, also as subsidiary activity to the main business, pursue insurance mediation in life business and in accident and sickness insurance on behalf of and under the full responsibility of an insurance undertaking and work
without fixed working hours or without obligations as to the result to be achieved exclusively for said undertaking (Section C);
4. banks, financial intermediaries, authorized stock brokerage companies, the company Poste Italiane (Italian Mail) (Section D);
5. any other persons dealing with mediation, such as employees, collaborators, canvassers and the other subjects charged by the intermediaries registered under the Sections A, B and D, for mediation outside the premises where the intermediary conducts business (Section E).
Concept of “tied-insurance intermediary” as defined in the IMD: A concept of "tied insurance intermediary" as defined in the IMD does not fall in any of the above categories of intermediaries.

## India

Intermediation of insurance in India is not as differentiated as in Europe. In fact a lot of the definitions of the intermediaries are similar to those employed in Canada. India has however one distinct advantage in regards to consumer protection. It only has one regulatory regime that applies to the whole of India while in Canada the regulatory regimes vary substantially with each province. India has the uniformity that was promoted by the concept of the Uniform Life Insurance Act in Canada whose progress stalled for various reasons which we will explore further.

Note: The concept of a Uniform Life Insurance Act (“the Act”) does not actually exist as a single statute, either federally or provincially. The title refers to a series of provincial statutes dealing with contracts of life insurance issued within the jurisdiction of each province and territory, with the exception of the province of Quebec. The statutes are generally uniform (hence the name) and can, for the most part, be considered as if they were one, homogeneous law.

Insurance intermediation is regulated in India by the Insurance Regulatory and Development Authority (IRDA). The Insurance Regulatory and Development Authority (IRDA) as constituted to regulate and develop insurance business in India. As a key part of its role, it is responsible to protect the rights of policyholders. It differentiates intermediaries based on an Insurance Intermediary which means individual agents, corporate agents including banks and brokers – they intermediate between the customer and the insurance company. Insurance Intermediary also includes Surveyors and Third Party Administrators but these intermediaries are not involved in procurement of business. Surveyors assess losses on behalf of the insurance companies. Third Party Administrators provide services related to health insurance for insurance companies. An agent is a person who is licensed by the Authority to solicit and procure insurance business including business relating to continuance, renewal or revival of policies of insurance. An agent could be an Individual Agent or a Corporate Agent. An Individual Agent, as the name suggests is an individual who in an intermediary representing an insurance company while a corporate agent is an intermediary other than an individual, representing an insurance company. A Designated Person means an officer normally in charge of marketing operations, as specified by an insurer, and authorized by the Authority to issue or renew licences under the applicable regulations. . A Composite Insurance Agent means an insurance agent who holds a licence to act as an insurance agent for a life insurer and a general insurer. An Insurance Broker means a person licensed by Insurance Regulatory and Development Authority who arranges insurance contracts with insurance companies on behalf of his clients.

An Insurance Broker may represent more than one insurance company. While an Agent represents only one insurance company ( one general, one life or both if he is a composite agent, apart from a health insurance company), a Broker may dealt with more than one life or general or both.

## U.S.

U.S. like Canada is in a regulatory rut unable to reconcile State interests with Federal interests the same way Canada is unable to reconcile provinces with other provincial interests. The difference between Canada and U.S. is that there is at least a perception of the need to reform U.S. state regulations under a federal regulatory system. That perception is inexistent in Canada with the Canadian Federal Government taking absolutely no leadership presence in trying to influence provinces to harmonize their insurance regulations to the detriment of consumer protection.

In Linkslater Insurance Update January 2007:

“Reform and modernisation of the U.S. state insurance regulatory system is being actively debated. If the proposed reforms are eventually adopted, some of them may affect foreign as well as home grown insurers. Insurance agents and insurance companies cite a range of problems in the state-based system of insurance regulation. These include inefficient licensing systems for both agents and companies and needlessly expensive and duplicative financial and marketing requirements and audits. A variety of reform proposals have been tabled in recent years. These generally involve the creation of a federal insurance regulatory system (including an optional federal charter for insurance companies and agencies) or the establishment of uniform standards in selected areas of state insurance regulation. Last year Senator John Sununu introduced the National Insurance Act of 2006 (the “NIA”), a bill which, if it had been enacted by Congress would have allowed life and property/casualty insurers, including foreign insurers, to choose federal rather than state regulation under an “optional federal charter” regulatory system. The NIA proposed a parallel, federal system of regulation and supervision for insurers and insurance producers (agents and brokers). Insurers and producers would be free to elect federal or state regulation. All aspects of regulation would have been subject to federal standards: organization, licensing, financial, product and market regulation, reinsurance, corporate transactions, producers and holding company regulation. An insolvent “National Insurer” would be subject to “receivership” under federal law, a procedure which may lead either to rehabilitation or to liquidation. Subject to limited exceptions, a National Insurer would not be subject to the application of state laws, including state insurance laws. The bill lapsed when it was not passed before the end of the congressional term, but many people consider that such reforms are long overdue and similar proposals may follow in the new Congress. These are not the only measures which have been proposed or adopted to reform the insurance market. The proposed Non-admitted and Reinsurance Reform Act of 2006 (HR 5637) was introduced in the House of Representatives in June 2006. The bill seeks to impose uniform state rules for non-admitted (surplus lines) insurance and reinsurance. It also applies single state regulation and uniform standards to the non-admitted insurance and reinsurance market place. As with the LIA this bill has also lapsed. It was passed by the House of Representatives but not the Senate. Finally, the Interstate Insurance Product Regulation Commission has been set up. Its purpose is to establish uniform standards for the regulation of individual and group annuity, life insurance, disability income and long-term care insurance products. The Commission operates within the state-based regulation of insurance, the standards, however, promulgated by the Commission only apply to the 29 states which have to date joined the Interstate Compact.”

## Case Study 7: Canadian Case Law versus European Case Law

Case law in Europe varies greatly from case law of the various provinces of Canada. This is expected since case law results from the interpretation of the law by judges. As a result, case law in Europe has tackled and is still tackling the issue of the legal status of intermediaries in trying to determine whether an intermediary is acting as the agent of the insured or agent of the insurer. This was the subject of a review by The English and Scottish Law Commissions of insurance contract law:

"THE STATUS OF AN INTERMEDIARY - WHOSE AGENT?
2.7 The issue of whether an intermediary is acting for an insurer or insured is complex. Under the general law of agency, the court would normally start by looking at any express agreement between the insurer and the intermediary: in particular, did the insurer give the intermediary actual authority to act as their agent for the purposes of receiving information or explaining the questions asked? In the absence of any express authority, the court may look for implied authority, by asking what was normal in that particular market. Finally, even if an agent was acting outside the terms of their actual authority, the insurer may still be held liable for their actions if the insurer held them out as having apparent authority to do what they did. These general principles have been interpreted and applied to different sorts of insurance intermediaries…It is possible that the category into which the intermediary falls affects the issue of whether a firm acts as an insurer's agent for purposes of receiving information and explaining questions. As we saw above, an intermediary will normally be considered to be the insured's agent if it analyses the whole market, but the position of a tied agent is less certain. However, the matters required in the initial disclosure document are not necessarily decisive on this point. Intermediaries are not required to declare whether they are acting for the insured or the insurer in explaining the documentation, filling in forms or passing on information."

An example of this difficulty associated with the duality of intermediaries is seen in Winter v Irish Life Assurance where the policyholders bought life insurance through a large firm of independent insurance brokers. The brokers knew that both policyholders suffered from cystic fibrosis, but this information was not disclosed to the insurer. The case was heard in the High Court before Sir Peter Webster, who held that the brokers acted for the policyholders, not the insurers. The relationship between the brokers and the insurers was insufficient to establish an agency. It was not sufficient that the insurers paid the brokers commission, or gave them publicity material over-printed with the brokers' name, or provided guidance and training about how the forms should be filled in. The judge laid particular stress on the fact that the policyholders approached the brokers to find them insurance. He said that the position might have been different if the insurer had provided the broker with the names of various leads and asked them to approach clients to sell the insurer's products.

As we can see, European Case Law is much different than in Canada reflecting the complex intermediation existing in Europe. In the common law provinces of Canada, the intermediary is the agent for the insurer and if legislation such as in Alberta is enacted to recognize the ability of an intermediary to represent many companies as a broker, there is a provision in the Act against the presumption of agency with the insured to his detriment. In Quebec, case law is more in line with European case law because of more modern regulations. Case law in Quebec has recognized the existence of the duality of the intermediary as we can see in Madill c. Importations Leroy inc., 1990 2662 (QC CA):

“It is well established that because of its particular nature the broker’s mandate is of necessity double. Whether, at any given time, he is acting on behalf of his client or on behalf of the insurer with whom he transacts, is very much dependent upon the facts of each particular case. It is certainly not my intention to embark upon an analysis of the various acts which a broker is called upon to perform in the day-to-day exercise of his practice or to attempt to pigeon-hole them. Savard, an independent insurance broker, consulted as he was by his client with a view to obtaining a particular type of coverage, is, first of all, reputed to be cognizant of the types of coverage available which respond to the needs of his particular clients. In addition to being mandated to obtain insurance, as Savard was, he had an obligation to counsel his client and explain to him the scope of the coverage available and the ramifications of any changes which may, from time to time, be brought about through changes in underwriting requirements.
In accomplishing these duties he is acting solely on behalf of his client. He is then both an agent and a counsellor and, in the circumstances of the present case, these two functions are inseparable.”

## Section 1.9 Recommendations: On the modernization of the Regulations of the intermediaries in Canada

1. Consumers in Canada are confused about who they are dealing with when buying insurance. As shown in this section, there is a greater need for uniformity of provincial legislation and regulations. The concept of the Uniform Insurance Act must be rekindled with the federal government providing the necessary leadership to the provinces.

2. Legislation and regulations must be updates to recognize the terms tied agent and multi-tied agents. We support the position of Alberta and Ontario in regards to the presumption of agency for multi-tied agents. All legislation must differentiate who is exclusive and who is an independent contractor.

3. Sponsoring of agents by one insurer for a license to be issued should be abolished as it contributes absolutely nothing to the determination of agent suitability.

4. The term broker should be a reserved term across all financial services with the same definition. Should brokerage be allowed in the life industry? At this juncture, we do not believe that introducing broker in life insurance would be reasonable considering the amplitude of the changes required to update legislation.

5. Recognition of the existence of MGA allowing the delegation of authority from the insurer to the MGA under an agency relationship. The insurer would be only responsible for ensuring that the authority transferred to the MGA while the regulator is responsible for suitability and compliance of the MGA. The MGA in turn would be responsible for the agent it contracts.