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Market Conduct Regulation for General Insurers - What you need to know

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Introduction

Good afternoon everyone. I'm pleased to be here, to have this next hour to spend with you to talk about Market Conduct Regulation.

I have two objectives today that I hope to achieve in the next hour.

The first is to update you on what CCIR is doing in the area of market conduct regulation, and equally important, why we are doing it.

The second is to try to alleviate what I know is some apprehension, some concern….dare I say dread, that what this all means is an entirely new layer of regulation and burden on insurers.

I can't guarantee I will relieve you of all your apprehension, but I do hope I can convince you that what is coming is not entirely new, nor simply an added regulatory burden.

What is Market Conduct Regulation?

So, what exactly do we mean by market conduct regulation? I sometimes think that "Market Conduct" sounds like one of those industry or regulator euphemisms we use when we don't want to say what we really mean.

Fundamentally market conduct is about treating consumers fairly. Consider it like the "golden rule" of regulation – "treat consumers the way you want to be treated".

If only it were that simple.

Why the increased focus?

The increased focus on market conduct by financial regulators around the globe followed the last financial crisis. Much has been written about this crisis and its causes and some still dispute what the real causes were.

But there is little dispute that among the many break-downs there were clear examples of breaches of the most basic market conduct principles. Consumers were not treated fairly.

We had poorly designed products being mis-sold to consumers. Those products were then repackaged and resold, again without attention to their suitability to the customers purchasing them.

And then new products, insurance products, were created to attach to these products, and they too were mis-sold.

All of this was fed by lack of disclosure, poorly designed incentives and a culture in some firms that can only be described as greed.

So, arguably, the greatest financial crisis of a generation began as a market conduct problem left undetected.

What followed was a solvency crisis that threatened not only the financial sector, but the economy itself. In many ways the industry and its regulators are still recovering from the fall out.

The initial focus of regulators coming out of this, as you all well know, was on prudential standards. Boosting capital and liquidity requirements, increasing risk management and governance, changes to accounting standards. Those requirements are still working their way through.

But addressing prudential standards alone will not address all that we know went wrong, and that is where an increased focus on market conduct regulation comes in.

Market Conduct Risk and Canada's Insurance Sector

Market conduct is about a company's interaction with its customers. It's about ensuring that you keep the fair treatment of those customers in mind in everything from building your products, designing your sales and marketing strategies, overseeing the distribution of your products and of course in managing claims.

And there are some unique features of the insurance business in Canada that present some increased market conduct risks.

Independent distribution

The most significant is that your products are distributed primarily through independent, third parties.

This is increasingly the case for other products in the financial sector like mortgages for example, but in the insurance industry the separation of distribution and manufacturing has been in place for years.

So why does this present added risk? Because insurers are forced to compete not only for the ultimate consumer but also for their share of the distribution channel.

And what does the distribution channel generally want?

They want products that are easy to sell and compensate them well. They want compelling marketing, friendly sales tools, and they want a piece of the action if they sell a lot of your product.

Sometimes - not always, but sometimes - what they want is not in the interest of the consumer.

Thorough needs assessment, education and careful explanation of exclusions, clear disclosure, product comparisons….those things are complicated, they take time and they can be uncomfortable to discuss.

Compensation and incentives that are designed to reward volume versus quality advice – these are things can compromise what is in the best interest of the consumer.

But if you make the product too difficult to sell or you don't have the best broker incentive promotion out there, you may lose distribution volume to your competitor.

As an insurer, it can be difficult to remember who the customer is. Is it the consumer who is buying your product or is it the agent that is selling it?

Mandatory Purchase

What is also unique about your business is that consumers often but your product because they have to; not because they want to. They need house insurance to get a mortgage; they need car insurance to drive.

This can drive commoditization and competition on price and this can make suitability - ensuring consumers take the time to understand what they need and what they are buying - a big challenge.

It might be easier for you and your distribution channel to simply make the product simple and cheap and hope consumers read the fine print but if they don't, sort it out as best you can at the claims end.

It's about the Consumer.

So, my point is that the very structure of your industry creates the need for added vigilance by companies and their regulators on market conduct; on ensuring we keep the consumer's interest in mind.

That's a little bit about the why – why we need to up our game on market conduct regulation.

As regulators we also like to point you in the direction of international standards; the IAIS and their Insurance Core Principles as the reason we are doing things. CCIR and its member regulators aspire to meet these best standards for regulators. We think that reflects well on us as regulators and in turn, on you as an industry.

But I also know you're tired of being told "we're doing this because everyone else is".

So let me give you another answer. We're doing this because it's the right thing to do. It's the right thing for the consumer and doing the right thing for the consumer is always going to be the right thing for your business, and for ours.

So, enough about the why. Let's talk about the what.

What, precisely, is CCIR doing? What can you look forward to?

What is CCIR doing?

First let me say CCIR works hard at harmonization wherever possible. We know this is a priority for you and we share that priority.

As regulators we are ultimately creatures of our provincial statues, and those are statues are not uniform. But, wherever practical we aim to align our supervisory activities.

Memorandum of Understanding

So, as a first step in improving our oversight of Market Conduct we created an MOU – an agreement among participating jurisdictions that we would share information and align our activities wherever possible.

The MOU provides the basis for more effective communication, information sharing and cooperative supervisory activities.

The aim is to:

- limit regulatory duplication – so the results of one supervisor's actions can be shared, rather than each regulator having to conduct the work themselves; and,

- to enable sharing of data and analysis, resulting in a better and more comprehensive understanding of market practices and more effective, early identification of risks.

Ten provinces and territories have signed the MOU to date; the remaining three are expected to sign in the near future

Cooperative Framework

Next, in November of last year, CCIR published is Cooperative Market Conduct Framework.

This framework builds upon the MOU by detailing how CCIR members will work together

It identifies the types of information CCIR members will share and the types of activities we will undertake together, including:

- conducting cooperative reviews or examinations at the industry and entity level;
- systemic market analysis through an Annual Statement on Market Conduct
- sharing consumer complaint statistics;
- reviews of new products and major changes.

We are very pleased with this Framework and the wide participation by CCIR member jurisdictions. We believe this represents a significant, historical shift in the regulation of the country's insurance market

CCIR members will begin working together, "on the ground", in supervising the insurance marketplace: wherever two or more members have identified a common concern or risk they intend to respond to, they will develop a plan to work together to address it. This includes sharing responsibilities and resources across provincial and territorial borders

This level of coordination will limit the duplication and extend the reach of supervisory activities and the information obtained from any reviews or cooperative supervisory activities will be shared with the other MOU signatories.

So what's next?

CCIR is working with industry to develop a harmonized annual information return for insurers. The information collected will provide us with the information needed to put more rigour around our monitoring of market conduct risks and controls.

Having a harmonized form will prevent duplication in information requests as insurers will need to complete one form for their operations in Canada. Implementation of the annual return is targeted for January 2017.

And last week, at our spring meeting in Montreal, CCIR members began building their first cooperative supervisory plan. This involved each jurisdiction sharing its supervisory priorities for the year ahead. Next, we identify where those priorities are shared or overlap and determine how we can combine, rather than duplicate our efforts and resources. This will, in turn allow you to combine rather than duplicate your efforts and resources.

Not entirely new concept

The last thing I want to do before we move to questions is take minute to convince you that all of this is not another layer of entirely new requirements.

Rather it's an extension of what you already do, what you already know and what you are already working on.

Solvency regulation is something we all know and understand…and dare I say accept as necessary and appropriate.

And in Canada the regulators all apply fundamentally the same solvency framework. In British Columbia we adopt, both in regulation and supervisory practice, OSFI's framework and guidelines.

That framework and the supporting guidelines come down to some basic questions:

- Are the insurers measuring, monitoring and managing their financial risks prudently?

- Do they have enough capital, that is to say, enough capacity to absorb severe but plausible losses and still meet obligations to policyholders?

- Do they have enough reinsurance and liquidity – that is to say, cash, and assets that are easily converted into cash – to pay their liabilities as they come due, even under stress?

These questions are not entirely different from the questions we are asking as market conduct regulators:

- Are the institutions measuring, monitoring managing their market conduct risks, appropriately?

- Do they have appropriate safeguards to ensure they are treating their customers fairly and delivering appropriate consumer outcomes?

- Do they have tools needed to proactively identify and rapidly respond to customer problems, threats to their reputation and poor consumer outcomes?

Solvency regulation – whether by OSFI, FICOM, Alberta or AMF - includes requirements related to capital, accounting and financial risks but also requirements for sound business practices.

Guidelines such as Corporate Governance, Regulatory Compliance Management and Operational Risk Management already ask insurers to have in place appropriate structures, policies and controls to ensure that they are operating ethically with a duty of care and managing their reputational risk. They also require that insurers be able to evidence the effectiveness of such safeguards.

More recently there is an increased focus on board defined Risk Appetite frameworks and the role of culture is managing risk.

Regulators want to see regular reporting to the board on any ineffectiveness or significant breaches of the institution's code of conduct.

We want board-level attention paid to compensation policy and practices for dealing with conflicts of interest and standards of ethical business conduct and we want appropriate "tone at the top".

Then there is ORSA, or Own Risk and Solvency Assessment. This is something I know you are all actively working on.

The ORSA Guideline asks insurers to:

> *Define and assess the materiality of all known, reasonably foreseeable, emerging and other relevant risks that may have an impact on an insurer's ability to continue operations, in both normal and stressed situations. An insurer's identified risks are expected to evolve as its business activities and environment evolves.*
>
> *The assessment should include all material risks, whether these are explicitly captured in the regulatory capital framework or not, as well as risks that are not easily quantifiable.*

What that says to me is that a properly completed ORSA will encompass and insurers market conduct risks.

So I will suggest to you that if you are meeting all of our expectations as solvency regulators you are already going a long way to meeting our expectations as market conduct regulators.

What is likely to feel different to you as we move ahead is the degree of rigor and proactivity that we apply as regulators. That will be a learning process and an adjustment for us all.

But as I said at the beginning this is about the consumer and I am confident that if we all keep that in mind then the process and the outcomes will strengthen the industry.

I am happy to take your questions.