

Risk Based Market Conduct Survey

Alberta Finance and Enterprise

Superintendent of Insurance

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Executive summary

Within the Financial Sector Regulation and Policy division of Alberta Finance and Enterprise, the Superintendent of Insurance is responsible for the regulation and supervision of Alberta provincial insurance companies and regulates the market conduct of all licensed insurance companies operating in Alberta. The Superintendent is also responsible to develop sound public policy on insurance matters to ensure Albertans have necessary and adequate insurance available to them.

On April 22, 2008 a Risk Based Market Conduct Survey was sent to all licensed insurance companies operating in Alberta. This inaugural survey was conducted to gather information regarding insurance companies' compliance with various sections of the *Insurance Act* (Act) related to their interaction with insurance agents including restricted agents and insurance adjusters.

The survey results indicate that many insurance companies use more than one type of intermediary for marketing and distribution of insurance. The majority of respondents indicated they use either independent or company intermediaries.

The survey asked insurance companies licensed in Alberta if they have policies and procedures in place to ensure they were in compliance with the Act. The survey results indicate the majority of companies have policies and procedures in place to assist them with compliance with the Act. The results also confirm that insurance companies have mechanisms in place to regularly review their policies and procedures. The majority of the companies indicated that senior level staff reviews these policies and procedures on an annual basis.

In general the overall results of the survey indicate a low risk of non compliance by insurance companies with respect to the surveyed sections of the Act.

Background

Under the *Insurance Act* (Act) appointed examiners review insurance companies' compliance with market conduct sections of the Act and its Regulations. In an effort to prioritize regulatory activities, improve market conduct compliance supervision and readily identify potential risks in the insurance market place the Office of the Superintendent of Insurance is moving towards a risk based approach to assess the market conduct activities of insurance companies licensed in Alberta.

On April 22, 2008 a Risk Based Market Conduct Survey was sent to all insurance companies licensed in Alberta. This inaugural risk based survey was used to gather information regarding the different distribution models used by insurance companies and their risk management control functions with respect to the regulatory requirements under the following sections of the Act:

Sec 452 (4) and (5)	Business with authorized insurance agents
Sec 460 (4)	Business with authorized insurance adjusters
Sec 485 (1)	Establish and use of insurance agent screening procedure
Sec 486	Establish and use of screening procedure to ensure restricted insurance agent personnel marketing insurance are knowledgeable about the insurance being marketed
Sec 499	Payment of compensation to unauthorized insurance agents

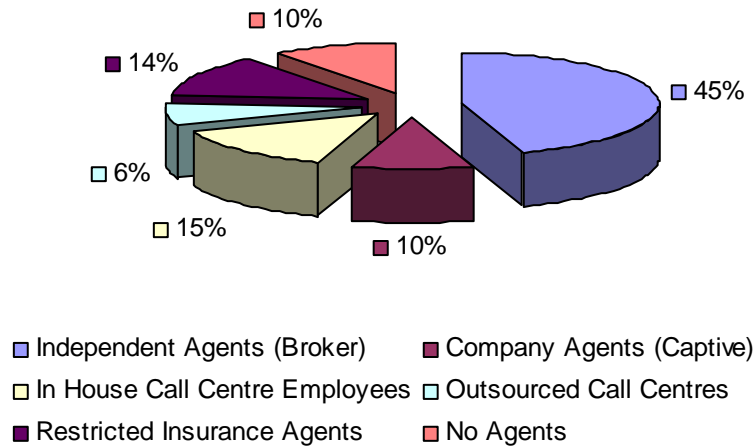
When the survey was mailed to insurance companies it generated a number of questions from property and casualty companies. As a result, a backgrounder paper was subsequently issued to assist companies with the questions in the survey. The surveys were to be completed and submitted by July 31, 2008.

Summary of Findings from Responses to the Survey

The risk based market conduct survey was sent to all insurance companies licensed in Alberta in April 2008. A total of 215 responses were received to the survey. The aggregate results for all companies who responded are presented below in the same order as the questions referenced in the survey.

Intermediaries

The survey's findings indicate that many insurance companies use more than one type of intermediary to market and distribute insurance, including internal and external sources. The following graph shows the breakdown of the different methods insurance companies employ to market their insurance products in Alberta:



We found that 55% of respondents use either independent or company agents to market and distribute insurance, 21% use a call centre, 14% use a restricted insurance agent and the remaining 10% indicated that they do not use an insurance agent because their book of business is in runoff or the company markets the insurance without the need for an insurance agent.

Procedures to ensure companies are use only authorized insurance agents

Under sections 452 (4) and (5) of the Act, no insurance company may employ an individual to act as an insurance agent or allow a business (agency) to act as an insurance agent on their behalf unless the individual or business holds a valid and subsisting insurance agents certificate of authority. The survey asked insurance companies if they had policies and procedures in place to ensure compliance with these subsections of the Act.

The survey results indicate that 93% of insurance companies who responded have policies and procedures in place to ensure they only do business with an insurance agent who holds a valid certificate of authority. 7% of insurance companies responded indicating they do not have

policies and procedures. We will be following up with these companies to determine what action they will take to establish policies and procedures.

Procedures to ensure companies are only doing business with authorized insurance adjusters

Under Section 460(4) of the Act, no insurance company may enter into a contract with an independent contractor or business to act as an insurance adjuster for the company unless the independent contractor or business holds a valid and subsisting insurance adjusters certificate of authority.

The survey results indicate that 55% of insurance companies who responded have policies and procedures to ensure they only do business with insurance adjusters who hold valid certificates of authority. 34% of the companies indicate that the policies and procedures were not applicable to their organization because as a life and health company they do not utilize insurance adjusters. 11% of the insurance companies indicated they do not have policies and procedure. We will be following up with these companies to determine what action they will take to establish policies and procedures.

Establishment and use of screening procedures

The designated representative of an insurance agency is required to recommend the application for employees' insurance agent certificate of authority. However, the designated representative's application for a certificate of authority must be recommended by an insurance company who has a contract with the agency employing the designated representative. Where an insurance company recommends a designated representative's insurance agent certificate of authority, section 485 (1) of the Act requires the insurance company to establish reasonable screening procedures to determine whether the designated representative is suitable to act as an insurance agent and to use those procedures to screen that individual before making their recommendation.

The survey results indicate that 77% of insurance companies who responded have established and use screening procedures to determine the suitability of an individual to be recommended as the designated representative of an agency and as an insurance agent. 13% of companies stated the procedures were not applicable to their organization, and 10% indicated they do not have policies and procedures. We will be following up with these companies to determine what action will be taken to establish policies and procedures.

Procedures to ensure employees of restricted certificate holders are knowledgeable about the insurance they market

Section 486 of the Act requires every insurer, on behalf of which a restricted insurance agent is marketing insurance, to establish reasonable procedures to ensure that personnel marketing insurance for the holder of the restricted insurance agent's certificate of authority is knowledgeable about the insurance being marketed.

The survey results indicate that 30% of insurance companies who responded have and use policies and procedures to ensure that restricted certificate holder employees are knowledgeable about the insurance being marketed. 56% of respondents indicated that the procedures were not applicable to their organization because they do not have any restricted insurance agents marketing insurance on their behalf. 7% of insurance companies responded indicating that they do not have policies and procedures in place. We will be following up with these insurance companies to determine what action will be taken to establish policies and procedures.

Compensation to unauthorized insurance agents

Section 499 of the Act prohibits insurance companies from paying any commission or other compensation to any person acting or offering to act as an insurance agent in Alberta unless that person is authorized to act as an insurance agent under the Act. In most cases insurance companies pay commission to the agency which also holds an insurance agent certificate of authority and not to the individual in the agency who sells the insurance to the agency's clients.

The survey results indicate that 85% of insurance companies have policies and procedures in place to ensure they only pay compensation to authorized insurance agents. 7% of respondents indicated that the policies and procedures were not applicable to their organization and the remaining 8% of respondents indicated they do not have policies and procedures in place. We will be following up with these companies to determine what action will be taken to establish policies and procedures.

Procedures incorporated into and maintained in relevant business operations

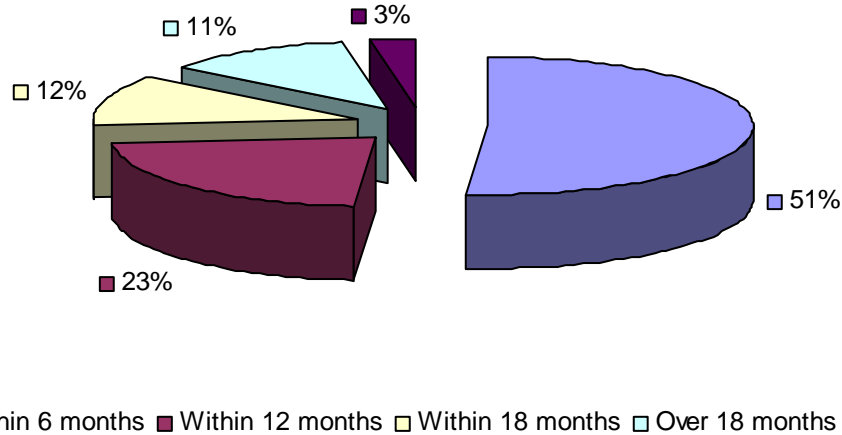
The survey results indicated that 92% of insurance companies responded that they have all the previously mentioned procedures incorporated into and maintained in their relevant business operations. 5% of respondents indicated that the policies and procedures were not applicable to their organization.

Assessment of Methodology for ensuring the requirements of the Act are met

The survey results indicated that 94% of companies responded that the methodology for identifying, assessing, communicating, and maintaining knowledge of the requirements set out in section's 452 (4) and (5), 460 (4), 485 (1), 486 and 499 of the Act ensure that appropriate individuals have the information they need to effectively comply. 5% of respondents indicated that the requirements under these sections of the Act were not applicable to their organization.

Frequency for Updating Procedures

Each Company surveyed has set timelines for updating procedures to address changes in products, activities, and corporate structure and these timelines differ between organizations. The survey results indicated that 74% of respondents had updated their policies within the last twelve months. The following graph shows the frequency of updates and the percent of reporting companies in each time period.



The survey asked companies about the interval in which their procedures are reviewed. The results indicated that 81% of the companies reviewed their procedures on a regular or scheduled interval and 19% responded that their procedures are only reviewed when there are changes to legislation.

Protocol for Reporting Non Compliance

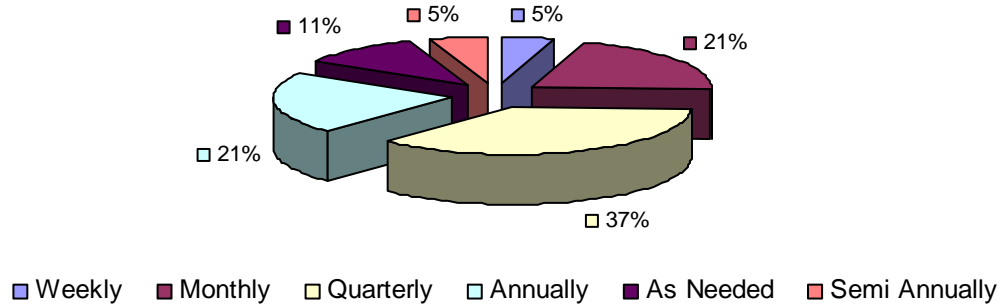
The survey also sought to gain a better understanding of the protocols in place for reporting non compliance with the policies and procedures. The survey results indicate that 83% of the insurance companies have established a documented protocol that requires the reporting of instances of non-compliance with the procedures and related remedial action plans. 17% of respondents do not have a documented protocol for reporting non-compliance.

Risk Management Control Functions

Risk management controls systems are one way to ensure that the procedures contain all the necessary controls to ensure compliance. The results of the survey show that 93% of the insurance companies responding indicated that their risk management control functions do ensure that all relevant procedures are sufficiently robust to control compliance with the Act and Regulations and, where significant issues arise, they are escalated to senior management and the Board of Directors as appropriate. 7% of respondents indicated that their risk management control functions do not ensure that the procedures are sufficient. We will follow up with these companies for further clarification.

Frequency of Normal Course Reports to Senior Management

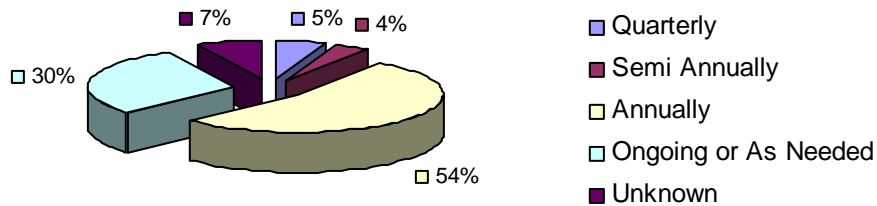
Each Company has set timelines for reporting normal course reports to senior management. The survey results indicated that 37% of respondents provide reports to senior management on a quarterly basis, 21% provide reports monthly and 21% report once a year. The following graph shows the breakdown of timelines for reports to senior management.



Frequency for Assessing the Effectiveness of the Reporting Procedures

Insurance companies have different timelines for assessing the effectiveness of reporting procedures they have in place. More than half of the respondent indicated that they review the effectiveness of reporting procedures on an annual basis, while 30% of the companies review the effectiveness on an ongoing or as needed basis.

The following graph shows the frequency of assessing reporting procedures.



Conclusion

The implementation of this Risk Based Market Conduct Survey was a success and has proven to be an effective tool that can be used to maximize the resources available and deploy regulatory efforts to the areas that present the highest potential risk to the insurance market place in Alberta.

This first risk based market conduct survey enabled the Office of the Superintendent of Insurance to evaluate insurance company compliance with the five sections of the Act and evaluate the risk of non compliance. The results are not a guarantee that all companies are in compliance with these sections of the Act at all times, however, the survey is a useful tool to allow the Superintendent's office to obtain confidence that most of the companies licensed in Alberta were at a low risk for non compliance with the legislative sections.

The success of the survey has demonstrated the effectiveness of a risk based approach to the regulation of the insurance industry in Alberta. We will now look at the potential to use this approach as a method to review industry market conduct in other areas.

Appendix #1 – Excerpts from the Insurance Act

Insurance agent's certificate

452

(4) No insurer may employ an individual to act as an insurance agent unless the individual holds a valid and subsisting insurance agent's certificate of authority.

(5) No insurer may allow a business to act as an insurance agent on its behalf unless the business holds a valid and subsisting insurance agent's certificate of authority.

1999 cI-5.1 s452

Adjuster's certificate

460

(4) No insurer may enter into a contract with

- (a) an individual as an independent contractor, or
- (b) a business

to act as an adjuster unless the individual or business holds a valid and subsisting adjuster's certificate of authority or meets the requirements of subsection (1)(b) or (2)(b).

RSA 2000 cI-3 s460;2001 c9 s3

Screening procedures

485(1) Every insurer that recommends an individual or sole proprietor to be issued an insurance agent's certificate of authority must

- (a) establish reasonable screening procedures to determine whether the individual is suitable to act as an insurance agent, and
- (b) use those procedures to screen an individual or sole proprietor before making a recommendation.
- (a) establish reasonable screening procedures to determine whether the individual is suitable to act as an adjuster, and
- (b) use those procedures to screen an individual before making a recommendation.

RSA 2000 cI-3 s485;2001 c9 s10

Knowledgeable personnel

486 Every holder of a restricted insurance agent's certificate of authority and every insurer on behalf of which the holder is marketing insurance must

- (a) establish reasonable procedures to ensure that personnel marketing insurance for the holder are knowledgeable about the insurance being marketed, and
- (b) use those procedures.

1999 cI-5.1 s486

Dealing with unauthorized insurance agents

499(1) No insurer, no officer, employee or agent of an insurer and no insurance agent may, directly or indirectly, pay or allow, or offer or agree to pay or allow, any commission or other compensation or anything of value to any person acting or offering to act as an insurance agent in Alberta, unless that person is authorized to act as an insurance agent under this Act.

(2) Subsection (1) does not apply to the payment

- (a) by an insurance agent of part of the agent's commission to insurance agents outside Alberta, or
- (b) of renewal commissions under the terms of an agency contract.

1999 cI-5.1 s499

Appendix #2 – Risk Based Market Conduct Questionnaire



SUPERINTENDENT OF INSURANCE

**Risk Based Market Conduct Questionnaire
Regarding Sections 452, 460, 485, 486 and 499 of the Insurance Act**

Name of Company: _____

Name of Contact Person: _____

Position/Title: _____

Telephone: _____

E-mail: _____

Survey Questions

1) Which of the following intermediaries does your company make use of in the marketing and distribution of insurance?

Independent Agents (Broker)	<input type="checkbox"/>
Company Agents (Captive)	<input type="checkbox"/>
In-House Call Centre Employees	<input type="checkbox"/>
Outsourced Call Centres	<input type="checkbox"/>
Restricted Insurance Agents	<input type="checkbox"/>

2a) Does your company have appropriate procedures for complying with the requirements set out in section 452 regarding a person acting as an insurance agent without a valid certificate of authority?

Yes (Please provide documentation)

No (Please advise when you will provide us with documentation)

2b) Does your company have appropriate procedures for complying with the requirements set out in section 460(4) regarding a person acting as an adjuster without a valid certificate of authority?

Yes <input type="checkbox"/> (Please provide documentation)
No <input type="checkbox"/> (Please advise when you will provide us with documentation)

2c) Has your company established and used screening procedures pursuant to section 485(1) to determine the suitability of an individual to be recommended to act as an agent ?
Yes <input type="checkbox"/> (Please provide documentation)
No <input type="checkbox"/> (Please advise when you will provide us with documentation)

2d) Has your company established and used reasonable procedures pursuant to section 486 to ensure that personnel marketing insurance for the holders of a restricted insurance agents certificate of authority are knowledgeable about the insurance being marketed?
Yes <input type="checkbox"/> (Please provide documentation)
No <input type="checkbox"/> (Please advise when you will provide us with documentation)

2e) Does your company have appropriate procedures for complying with section 499 with respect to compensation in any form not being paid to a person for transacting insurance without a valid certificate of authority for the class of business transacted.
Yes <input type="checkbox"/> (Please provide documentation)
No <input type="checkbox"/> (Please advise when you will provide us with documentation)

3a) Have all of the procedures mentioned in question 2 been incorporated into and maintained in relevant business operations?
Comment:

3b) Does the methodology for identifying, assessing, communicating and maintaining knowledge of the requirements set out in sections 452, 460, 485, 486 and 499 ensure that appropriate individuals have the information they need to effectively comply?

Comment:

4a) Please identify the title and position of the individual(s) responsible for day-to-day compliance and oversight controls that include monitoring and reporting procedures through which significant problems are identified, escalated and resolved.

Comment:

4b) Please identify the title and position of the most senior officer responsible for approving the content and frequency of normal course reports pertaining to the procedures mention in question 2.

Comment:

5) When were the company's procedures mentioned in question 2 last updated to address changes in products, activities or corporate structure?

Date:

6a) Are the procedures reviewed on a regular or scheduled interval?

Yes (Please provide documentation)

No (Please advise when you will provide us with documentation)

6b) Has your company established a documented protocol that requires the reporting of instances of non-compliance with the procedures and related remedial action plans?

Yes (Please provide documentation)

No (Please advise when you will provide us with documentation)

7) Does your company's risk management control functions ensure that all relevant procedures are sufficiently robust to control compliance with the Insurance Act and Regulations and, where significant issues arise, that they are escalated to senior management and the Board if Directors as appropriate?

Yes (Please provide documentation)

No (Please advise when you will provide us with documentation)

8) What is the frequency of normal course reports to senior management?

Comment:

8a) What is the frequency for assessing the effectiveness of the reporting procedures?

Comment:

CERTIFICATION

I have knowledge of the information provided in this questionnaire. The information fairly represents the policies and procedures followed by the company as of the date this questionnaire is being signed.

Signature of
Chief Executive Officer or Chief Agent:

Date:

Name (Please Print)

“The personal information that you provide on this form will be used for the purpose of administering the *Insurance Act*. It is collected under the authority of section 33(c) of the *Freedom of Information and Protection of Privacy Act* and is protected by the privacy provisions of the Act. If you have any questions about the collection of this information, please contact Peter Blandy, Compliance Manager at (780) 415-8556.

MAIL COMPLETED QUESTIONNAIRE TO:

**Alberta Finance and Enterprise
Superintendent of Insurance
Room 402, Terrace Building
9515 – 107 Street
Edmonton, Alberta T5K 2C3**