

Address by

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Commercial Practices (market conduct) revised Guideline

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First of all, I wish to thank the CLHIA for this opportunity to present the AMF's revised Commercial Practices Guideline. I would like to especially thank Mr. Bernier for inviting me to attend this Annual Conference, which continues to garner great interest within the industry.

Increasingly, prudential regulation worldwide has shifted the spotlight from matters of solvency and the ability of institutions to meet their financial obligations to consumers, particularly during a crisis or corporate wind-up.

Therefore, it is a definite challenge for me to be here today and speak to you about the AMF's aim and commitment to provide institutions operating in its jurisdiction with a framework that sets out what is expected in terms of sound commercial practices.

Quite a challenge indeed; however, as AMF Superintendent of Solvency, it is a stimulating one that ties in with the insurers' conduct towards customers and the risk — to name just one — to their reputation in the event of misconduct.

Such conduct could ultimately give rise to major solvency issues. This is precisely what concerns me.

On reading the agenda for this Annual Conference, I couldn't help but notice that several topics deal with the key issue of fair treatment of consumers.

Organizational culture, ethical culture, consumer complaints, e-commerce, enterprise risk management, compensation practices, point-of-sale disclosure, and compliance —these are all clearly focused on consumers and the fair treatment they should receive.

This focus is a consequence of the recent financial scandals that have rattled the business world and have highlighted the importance of consumer protection measures.

Regulatory bodies, governments and the public alike, are now more keenly interested in an institution's commercial practices, ethical conduct and integrity.

In addition, many international organizations, including the International Association of Insurance Supervisors (IAIS), the Joint Forum and even the Organisation for Economic Co-operation and Development (OECD), are revising or planning to revise or develop key principles that, foster sound commercial practices and protect consumers' interests.

Today's consumers are faced with an array of increasingly complex and sophisticated financial products. This is why:

- they must have access to suitable information that allows them to make informed decisions when purchasing financial products or services;
- information given to consumers must not be deliberately misleading or contain misrepresentations;
- products must be sold objectively, with no constraints or influence that would result in a consumer being offered an unsuitable product.

The issues concerning the fair treatment of consumers are many and interrelated. They come into play not only at the time of sale, but also throughout the life cycle of the product and the period during which the consumer holds the product.

Therefore, ensuring that consumers are treated fairly means that institutions must put in place an equitable complaint examination system and consumers must be assured that private information will be handled confidentially.

These are some of the aspects covered in the AMF's proposed commercial practices framework.

Ensuring adequate consumer protection and information builds confidence in the industry, which in turn leads to greater market discipline and effectiveness.

In the proposed guideline, the fair treatment of consumers is approached from the perspective of the need for institutions to manage reputational risk.

A spotless reputation gives an institution a major strategic edge. On the other hand, a sullied reputation could be an institution's downfall.

Poor commercial practices can swiftly damage an institution's reputation. Given the prevalence of social networks today and the speed at which information circulates, a corporate name or logo can fall from its pedestal in no time!!

COMMERCIAL PRACTICES GUIDELINE

To maintain public confidence in the financial services industry and safeguard consumers' interests, the AMF expects fair treatment of consumers to be a core component of an institution's corporate culture.

Achieving this goal requires tone at the top from both the board and senior management in order to:

- build a corporate culture centred on the fair treatment of consumers;
- orient commercial practices to ensure the fair treatment of consumers;
- apply sound - and even best - practices; and
- manage the institution's risks by treating reputational risk, admittedly difficult to quantify, as a major issue.

Board and management resolve and commitment are essential, as staff attitudes and behaviour at all levels of the organization will have a bearing on the fair treatment of consumers.

Boards and senior management must ensure that all employees fully understand the reputational risks inherent in their sector of activity so they can identify and manage those risks.

A corporate culture must permeate departments and functions at all levels of an institution, although tempered differently depending on the input of an institution's decision-making staff. All members of the organization must be aware of the silent yet insidious presence of reputational risk and its potentially devastating effects.

DRAFT GUIDELINE ON COMMERCIAL PRACTICES: FIRST CONSULTATION

Mindful of the importance and innovative nature of the measures it published, the AMF sought to consult the industry on its initial proposed commercial practices guideline. This consultation was held from November 6, 2009 to March 31, 2010.

The guideline was drafted using an innovative, intersectoral approach so that the AMF's expectations could extend to insurers and deposit-taking institutions alike.

We also sought to take a further step and ensure optimal tie-in between specific Québec legal requirements under *An Act respecting the distribution of financial products and services* (the "Distribution Act") and the benchmarks set out in the guideline.

As a result, the initial draft guideline focused on the following five areas:

- The roles and responsibilities of the board of directors and senior management;
- The design, selection, promotion and distribution of financial products and services;
- Advice;
- Complaint examination and dispute settlement;
- Protection of personal information.

As advocated by core international principles, the initial draft guideline was intended primarily to ensure that institutions adopted a holistic approach to their risk exposure – reputational risk being an integral part of this approach – with such an approach transcending the legal framework and going beyond a mere compliance-based approach.

This was our intention: to impress upon institutions the importance of remaining attentive to consumer advisory services, as they could significantly impact reputational risk management.

As the AMF is the first Canadian regulator to set out its commercial practices expectations, this initiative has generated great interest from industry participants.

For the sake of transparency, all comments were posted on the AMF website, unless the commenter requested otherwise.

FIRST CONSULTATION: COMMENTS

Among the feedback received during the first consultation, several comments by the CLHIA attracted our attention, including some general observations:

- The guideline imposes supervision of independent distributors over which insurers have no control;
- The guideline should focus on the insurer as a manufacturer, not as a distributor;
- The AMF should work with the CCIR to prevent jurisdictional conflict regarding commercial practices and to promote harmonization.

Based on these comments and the reactions to the guideline, the AMF identified the major irritants, but also possible misunderstandings or misconceptions.

As an integrated regulator, the AMF cannot allow itself to create interference within the various sectors under its responsibility or deliver contradictory interventions depending on whether it is fulfilling its solvency or distribution mandates, for example.

Therefore, this first draft appears to have been too forward-looking.

We did not intend to impose additional obligations by issuing our expectations via the guideline, but rather to raise insurers' awareness of the fact that reputational risk is embedded in their business conduct and processes.

For example, insurers were not asked to supervise independent distribution networks; instead, they were urged to be better informed about their networks regardless of the sales method used.

An insurer's name, logos and branding are in the public domain and are what consumers identify with. When a consumer is ill advised, the insurer's name and brand image are at risk.

SECOND CONSULTATION: MAJOR CHANGES

Based on the feedback from the first round of consultation and some strong reactions from commenters, we decided to review our initial draft in a new light.

A second draft guideline was therefore issued for industry consultation from March 11 to April 22, 2011.

The main changes are in Part A of the guideline, which outlines general expectations applicable to all institutions.

Further to the decision to withdraw the distribution of insurance products from Part A of the guideline, since it was covered under the Distribution Act, the table of contents in the revised guideline is as follows:

First consultation	Second consultation
Roles and responsibilities of the board of directors and senior management	Roles and responsibilities of the board of directors and senior management
	Incentives management framework
Design, selection, promotion and distribution of financial products and services	Product design and marketing
	Information for consumers
	Product advertising
Advice	
Complaint examination and dispute settlement	Complaint examination and dispute settlement
Protection of personal information	Protection of personal information

The second version of the guideline responded to changes in core principles and the sound commercial practices orientations of international bodies.

In fact, since the first consultation, core international principles were amended to ensure that the fair treatment of consumers would be embedded in each institution's corporate culture.

As a result, it became necessary to review the principle governing the roles and responsibilities of the board of directors and senior management.

The AMF's keenness to make directors and officers accountable is apparent in all the frameworks presented in the form of guidelines issued to date.

The Commercial Practices Guideline is no different.

The guideline no longer covers insurer's distribution activities per se (for example, advice), since the very act of advising customers is reserved for representatives, as set out in the Distribution Act.

To avoid confusion, and further to comments by the CLHIA on the juxtaposition of the current legal frameworks, the revised version of the guideline focuses on the responsibilities of insurers in their capacity as manufacturer, not distributor.

Despite the fact that the AMF considers that the commercial practices framework should extend beyond the confines of a financial institution and not overlook the intervention of individuals in the provision of customer service, the framework is now rid of what some commenters clearly believed to be potential irritants.

However, insurers are not relieved of their responsibilities. They must monitor the risks associated with the distribution of their products, particularly as such monitoring is part of reputational risk management.

As an integrated regulator, the AMF needs to ensure that its commercial practices expectations with respect to insurers are aligned with the legal and regulatory obligations of representatives and firms governed under the Distribution Act.

Lastly, the AMF set out its expectations regarding information for consumers and product advertising, and added its expectations about the management of overall compensation strategy incentives.

DRAFT COMMERCIAL PRACTICES GUIDELINE: SEEKING CONSISTENCY

The Commercial Practices Guideline applies to all financial institutions operating in Québec (other than banks).

Although the AMF is the first Canadian regulator to set out commercial practices expectations, this guideline was developed to be consistent:

- with international guidance, to foster harmonization with other jurisdictions;
- with current pan-Canadian regulation, to avoid overlapping, administrative burden or arbitrage. To this end, the AMF took into account the orientations and initiatives of the CCIR, of which I currently serve as Chair;
- with best practices across Canada. In particular, we took under consideration CLHIA's guidelines on disclosure of product information and direct marketing. The most striking example of this initiative and these harmonization efforts is still the AMF's Guideline on Individual Variable Insurance Contracts Relating to Segregated Funds, which, based on successful exchanges between the AMF and CLHIA, is fully harmonized with regulation Canada-wide;
- between the deposit and insurance sectors, by setting out core principles rather than specific rules in order to facilitate, insofar as possible, implementation of these principles by institutions based on the nature, size and complexity of their activities.

PART A - GENERAL EXPECTATIONS

As mentioned, Part A of the guideline sets out general expectations applicable to all institutions.

In fact, although the financial characteristics of certain products may be similar, the rules governing their design and marketing may often differ, simply because the institution manufacturing the product is different.

In the AMF's opinion, a lack of consistency in products with similar characteristics (such as segregated funds (life and health insurance) and principal-protected notes (deposit-taking institution)) could undermine consumer protection.

This could ultimately lead to situations of arbitrage, even competitive inequities.

From this perspective, the AMF's expectations for this first part apply to both insurers and deposit-taking institutions and were expressed in seven key principles covering:

- The roles and responsibilities of the board of directors and senior management;
- Incentives management framework;
- Product design and marketing;
- Information for consumers;
- Product advertising;
- Complaint examination and dispute settlement;
- Protection of personal information.

Part B sets out specific expectations for a given product or activity according to the sector or type of institution.

Since each sector (deposit and insurance) has a different legal framework (distribution of products as the best example) and different clientele, it is expected that many additional subjects will be added, as necessary, in the future.

It is especially true when we will need to harmonise our expectations to insurers on topics already covered by the Distribution Act and the legal obligations the intermediaries have. A right balance will always be needed between the two frameworks: principles-based for insurers and rules-based for distributors.

Our guideline provides specific expectations for both life and health insurers with regard to claims examination and settlement;

As for life insurers, it makes a link to the Guideline on individual variable insurance contracts relating to segregated funds.

These provisions (which are presented in a separate guideline) are an integral part, by reference, of the Commercial Practices Guideline.

I will address a little bit later the expectations that AMF has on both of these topics.

ROLES AND RESPONSIBILITIES OF THE BOARD OF DIRECTORS AND SENIOR MANAGEMENT

The AMF expects the institution's board of directors and senior management to establish, document and implement strategies, policies and procedures that make the fair treatment of consumers a core component of the institution's corporate culture.

Some of the comments received during the first consultation on the guideline referred to the fact that the roles and responsibilities of the board of directors and senior management were already covered in the Governance Guideline.

It was proposed therefore that the Commercial Practices Guideline be limited to requiring a commitment from the board and senior management to include the commercial practices guideline in their governance plan.

All of the AMF's similar frameworks highlight the roles and responsibilities of directors and officers precisely to illustrate the importance of these functions, but also to confirm the AMF's intention to make directors and officers accountable.

We believe it is far more effective to include these roles and responsibilities in our Commercial Practices Guideline, since the expectations would then be more specific and focused.

Merely requiring a commitment from the board and senior management to build this guideline into their governance plans does not provide the AMF with the assurance that effective measures will be put in place.

To make the fair treatment of consumers a core component of an institution's corporate culture, the board and senior management must:

- set the tone through their active participation;
- make a strong personal commitment;
- be attentive to:
 - events within their institution and to departures from internal policies that compromise the institution's reputation or that threaten the fair treatment of consumers;
 - high standards of ethics and integrity;
 - potential conflicts of interest and the way they are managed; and
 - personal information protection issues.

The AMF expects the financial institution to establish overall compensation strategies to ensure that a benefit offered by the institution to its managers and sales force, as well as to any individual or entity that could be part of the institution-client relationship do not prejudice the fair treatment of consumers.

Although the revised guideline no longer covers the distribution of financial products and services by insurers, and in particular, advisory services, the AMF nevertheless sought to express its expectations with regard to incentives, given the importance of this issue from the perspective of reputational risk management and potential conflict of interest.

Therefore, the payment of incentives by insurers to intermediaries may interfere with the responsibilities of intermediaries to act in the best interests of consumers.

The AMF also considers that the payment of incentives should be accompanied by a minimum of transparency for consumers.

Certain stakeholders proposed ensuring transparency by fully disclosing potential conflicts of interest and obtaining a signed document to that effect from the customer. The AMF however recommends that incentives be disclosed on insurers' websites.

The AMF is mindful that incentive compensation is part of the way insurers do business and helps boost sales to a certain extent.

Without prohibiting such incentives, which include commissions, bonuses, variable compensation, non-cash awards, contests and promotions, the AMF expects institutions to implement an incentive management framework that clearly shows their commitment to ensuring that these practices will not prejudice the fair treatment of consumers.

Therefore, institutions are now responsible for demonstrating to the AMF that their incentive management frameworks were created with the aim of protecting consumers' interests.

PRODUCT DESIGN AND MARKETING

The AMF expects the financial institution to develop and market its products commensurate with target consumers' interest.

Some of the CLHIA's comments about product design and marketing submitted during the first consultation highlighted the following:

- the AMF should expect manufacturers to ensure that their products are aligned with consumers' needs;

- insurers that are not firms should, for example:
 - draft appropriate disclosure documents to help consumers make better decisions;
 - produce documents that enable representatives to fully understand the products;
and
 - disclose conflicts of interests;

- Financial institutions are already required to:
 - define viable products and services;
 - tailor products and services to target consumers;
 - comply with the Distribution Act when distributing products;
 - provide disclosure documents that help distributors and consumers examine a product;
 - make this information readily available on paper or electronically; and
 - update the information and ensure that it is relevant and easy to understand.

These comments prompted the AMF to adjust its expectations regarding the design and marketing of products so as to limit the responsibilities of institutions to their role as manufacturers.

In addition, certain other commenters asked that we specify the type of information consumers should receive.

These comments seemed relevant. Therefore, separate parts were created in the guideline to cover information for consumers and product advertising.

I should also point out that, further to the comments received, this principle excludes group contracts. Furthermore, it relates to new products only.

Therefore, when we ask institutions to carefully assess their products prior to marketing, they are not required to review existing products and services that meet consumers' needs. However, if that is not the case, a re-examination is of course essential!

INFORMATION FOR CONSUMERS

<p>The AMF expects the financial institution to draft appropriate disclosure documents on its products to enable consumers to make informed decisions.</p>
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Products may have the same basic features but also significant differences, which must be contemplated by the institution's disclosure regime to ensure that consumers receive the appropriate information on the products they intend to purchase.

Consumer information should, for example:

- be drafted in clear simple language, be limited to the essential elements and be presented in a format that is easy to read and understand;

- enable the consumer to understand a product and its main features, as well as its advantages and risks;
- focus on the potential advantages, while accurately and clearly identifying the potential related risks;
- list terms, exclusions, restrictions and limitations applicable to the product, any fees and expenses to be borne by consumers, the consumer's rights and obligations and any tax consequences;

As an integrated regulator, the AMF also has the mandate to provide assistance to consumers of financial products and services. We therefore value consumer education and we believe that an informed consumer is a better consumer.

Giving consumers an insurance policy in plain language gives them a better understanding of the product they are buying. This should, in our view, raise their confidence in the financial institution they are dealing with. And, we all know that financial institutions rely on the trust and confidence of consumers.

Within the same expectation:

The AMF expects the financial institution to disclose to its clients any change affecting the institution that is of concern to them, all periodic product information and any change to the products they hold or in respect of which they have rights or obligations.

For example, where a product's terms are changed, the institution should provide information that will help clients to understand the changes, inform them of their rights and obligations and, if necessary, obtain their consent.

This expectation reflects the comments I just made on consumer trust and confidence.

PRODUCT ADVERTISING

The AMF expects the financial institution to ensure that the information in advertising material is accurate, clear and not misleading.

The institution should ensure that advertising material is reviewed independently of the individual or organization that prepared or designed it for the institution.

This review should enable the institution to ensure, for example, that:

- when the advertising mentions a specific advantage, it also fairly discloses, in close proximity and in the same manner, any restrictions, exceptions, limitations or risks that could affect the advantage;
- the source of the statistics used is identified;
- testimonials used in advertising are authentic.

Drawing on the comments received to date, we will review these expectations with the legal obligations contained in the Regulation under the Act respecting insurance. Some minor changes in wording might therefore be necessary.

COMPLAINT EXAMINATION AND DISPUTE SETTLEMENT

The financial institution must provide equitable resolution of complaints filed with it.

Pursuant to the legislative provisions in the laws administered by the AMF, institutions have certain complaint examination obligations. Hence the word “must” rather than “should” as is used in the other expectations in the guideline.

Because these obligations are so important when speaking about incorporating the fair treatment of consumers into an institution’s corporate culture, it was necessary to mention these obligations in the guideline. Essentially, these obligations are:

- adopt a complaint examination and dispute settlement policy;
- receive complaints from any interested party and examine them in an impartial manner;
- send the complainant an acknowledgement of receipt and a written notice informing him/her that if not satisfied with how the complaint was handled or the settlement, he/she may request that the file be transferred to the AMF;
- send the complaint file to the AMF at the complainant’s request;
- prepare and submit complaint reports to the AMF.

However, since institutions’ complaint examination obligations are covered by an existing regime, the principle proposes that institutions refer to the AMF website, as suggested by the CLHIA.

Despite the existing legal obligation, it is nonetheless very important that insurer's set up processes and procedures to enable them to effectively manage consumer complaints and disputes.

PROTECTION OF PERSONAL INFORMATION

The AMF expects the financial institution to have a policy and procedures that protect the confidentiality of the personal information obtained from consumers.

Despite the comments submitted by the CLHIA during the first round of consultations, the protection of personal information, like complaints examination and dispute settlement, were to be covered in the Commercial Practices Guideline for the following reasons:

- The protection of consumer information is crucial to an institution's reputation, for the protection of consumers' interests and for maintaining public confidence in the financial services industry;
- A breach in information confidentiality could have a major impact on the institution's risk profile and, ultimately, its solvency;
- An institution must adopt policies and procedures regarding the collection, retention, use of personal information and disclosure to third parties in the course of its business.

This principle complements the legal obligations of institutions under existing legislation by specifying the aspects that are not covered or are relevant for demonstrating their ability to prevent inappropriate use or disclosure of the personal information they hold.

These expectations seem pertinent, even though *An Act respecting the protection of information in the private sector* and the provisions of the *Civil Code of Québec* already provide a complete regime governing the obligations of individuals and entities that hold and use personal information.

In fact, the intended purpose of these legal obligations is in no way contradictory; rather, they complement our expectations.

PART B - CLAIMS EXAMINATION AND SETTLEMENT

The AMF expects an insurer to examine and settle claims filed with it in an equitable manner using a procedure that is simple and accessible for claimants.

The examination and settlement of claims help determine whether dealings with consumers are fair. Insurers should inform consumers about their claims examination and settlement services and how they can access the services in point of sale information and on their websites.

Insurers should designate an officer or employee to examine and settle claims. They should also implement policies, procedures and controls that, for example:

- resolve claims in a manner that is effective, equitable and transparent for the claimant;
- inform the claimant of his/her rights and obligations prior to the examination of the complaint;
- do not settle for a lower amount than the claimant is entitled to receive, in particular through compensation incentives for claims employees;
- use reasonable methods for evaluating claims and losses, where applicable;

- review decisions resulting in a total or partial rejection of a claim according to the appropriate levels of delegation;
- inform the claimant about the procedure for filing a complaint with the insurer if he/she is dissatisfied with the examination or proposed settlement of the claim.

INDIVIDUAL VARIABLE INSURANCE CONTRACTS RELATING TO SEGREGATED FUNDS

For the time being, the individual variable insurance contracts relating to segregated funds guideline is separate from the Commercial Practices Guideline, since it had to be published and updated concurrently with the guideline developed for similar products, namely, mutual funds.

This guideline is available in French and English on the AMF website at www.lautorite.qc.ca under “Insurance and Financial Planning,” “Guidelines.”

This guideline came into effect on January 1, 2011.

And, as mentioned before, this guideline is harmonized with the CLHIA G2 Guideline.

WHAT TO EXPECT FROM THE AMF

Similar to the manner in which it was done for all AMF guidelines published to date (other than the capital adequacy guidelines, of course), a transition period will be granted after the guideline comes into effect.

This transition period is intended to enable institutions to adopt the expectations set out in the guideline and, in doing so, develop the strategies, policies and procedures necessary to enable them to adequately address the AMF’s expectations to ensure full implementation of the guideline.

However, it should be noted that the complaint examination and dispute settlement provisions will be effective as of the final publication of the guideline.

Because these provisions are drawn essentially from legal requirements, they are understandably mandatory.

During the transition period, namely, two years after the guideline comes into effect, AMF Supervision of Insurers will oversee the main implementation steps.

At this point, we expect to require that insurers designate a contact person whom the AMF can reach as needed and whose role and responsibilities will clearly involve the implementation of the guideline and subsequent follow-up.

The insurer must map out an action plan and timeframe for implementation and develop the requisite documentation for full implementation consisting of strategies, policies and procedures.

Experience with the implementation of other guidelines (Governance, Integrated Risk Management, and Compliance) has shown that we need to insist that insurers inform us of their implementation status on a regular basis. The frequency has not yet been determined.

Past experience has also taught us that institutions respond well to the AMF's requests for information. These requests are relatively unrestrictive because there is no prescribed format. For example, reports prepared for the board of directors may be filed with the AMF.

Once the review of all comments received is finalised, and a final version is published, the AMF will make public its expectations regarding the full implementation of our expectations by the insurers.

CONCLUSION

In conclusion, I wish to highlight that all AMF expectations set out in the guideline were reviewed based on the changes in international commercial practices guidance.

The AMF's approach to the commercial practices framework is based on best national and international practices. The AMF supports this approach, which consists in making insurers accountable for managing their reputational risk.

It is often said that risk management is mainly about transforming these risks into opportunities and thereby creating value.

It is precisely this school of thought that underlies the principles of the guideline. Sound and prudent management of reputational risk by an institution can only bring near and long-term benefits.

The life and health insurance industry operates over a long timeframe; therefore, it is in insurers' interest to treat their customers well.

This approach is advantageous for both the consumer – who then places his trust in the institution and readily purchases its other products and services or recommends the institution to family and friends – and for the insurer, who benefits, for example, in this specific case, from a broader client base and greater client loyalty.

Finally, I want to thank the CLHIA and individual insurers for the comments they have provided and the support they have shown (especially our friend JP Bernier with his numerous emails!!) throughout this challenging and innovative process.

At the end of the day, consumers in Québec will come out as better consumers.